

## **Economic Development in Post Conflict Society A Cluster-Focused Development Plan**

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### **Introduction: Post Conflict Society and the magnitude of the problem**

In 2003, Kashmir, Chechnya and Colombia were but a few of the 30 significant armed conflicts occurring throughout the world. The results of these conflicts have been catastrophic, and are symbolized by mass gravesites, startling cruelty and a loss of human dignity.<sup>2</sup> The statistics are staggering. More than 4 million people have been killed in violent conflicts since the fall of the Berlin Wall in 1989, with the vast majority of the deaths attributed to intra-state hostilities. During the 1990s, there were 39 major conflicts with at least 1,000 deaths per conflict per year, with nine of ten casualties being non-combatants.<sup>3</sup>

While the causes of conflict are debatable and germane to a specific region, there are underlying similarities in which power and resources are distributed by the state and other relevant players that exacerbate the problem.<sup>4</sup> These focus on the rights of regional, religious, ethnic or other groups and highlight a sense of social and economic inequality that often leads to the conflict. One of the primary causes, if not the primary cause, of this inequity is relative and sometimes comprehensive poverty, and an inability to improve the underlying economic condition. It is then that the disenfranchised may resort to violence or the powerful elite resorts to pre-emptive strikes.

The results are frighteningly predictable. Post-conflict societies are typically rife with corruption, weak or illegitimate political institutions, damaged infrastructures, ineffective economies and a society with no shared vision on how to develop a solution. The resulting conflict goes beyond immediate pain and suffering and can inhibit the country or region's ability to stop the cycle of violence.

As a first phase, the international community responds with peace keeping forces. These activities are typically followed by a second phase that provides support to local partners. This support focuses on creating institutions that provide the stability to develop the economic base. More specifically, this typically involves rule of law, security for citizens, political and other institutional

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<sup>2</sup> Friends Committee on National Legislation (FCNL) website

<sup>3</sup> The World Bank Website; Post Conflict Reconstruction

<sup>4</sup> Goor, L. van de (1996) *Major Findings of the Research Project 'Causes of Conflict in the Third World'*; According to Emil Payin, in *Settlement of ethnic conflicts in post-Soviet society*, All these varieties of ethno-ideological conflicts have one thing in common: a veneration, often bordering on the irrational, of what the parties describe as their sacred "historical rights".

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reform, tax amendments, private property rights, refugee home location, and a stabilized micro-economic environment.

Establishing the laws and reforms that provide this stability can be completed expediently, with the support of international expertise. However, if economic development does not commence at a rapid rate, there is more of an incentive to use corrupt means to “game the system” as opposed to growing the wealth base. This corruption can enforce the sense of inequity within the system, and help to reverse the peace process that was achieved by military or other mechanisms.

While stabilizing activities are essential, there must be a plan to develop the economy by creating regionally and globally competitive firms *at the fastest rate possible*. Therefore, a third phase must create the enabling environment to improve the average citizen’s standard of living. This has been a critical agenda item for a wide variety of powerful organizations worldwide. For example, since 1980, World Bank lending to post conflict societies has increased by 800% and now accounts for almost 25% of the Bank’s \$18.5 billion portfolio. However, the Bank’s post-conflict reconstruction primarily supports only these two goals: first, to address short term challenges that may include humanitarian aid, and second, to build physical and institutional capital.<sup>5</sup>

The question is then, what are the most important imperatives that will improve the standard of living or the prosperity of a region. Professor Paul Krugman, the MIT economist, wrote that, “Growth in a nation’s standard of living equals the growth of the nation’s productivity--period.” Even taking into account all of the forces at play in the rapidly changing world economy, it is still the case that the only way a nation becomes more productive is to become more effective at satisfying the needs of rewarding customers and partners. If true, the imperatives must focus on creating an environment where investments are targeted at improving productivity – especially the productivity of individuals through education and training that focuses on satisfying those needs.

Therefore, after implementing the first two phases of a reconstruction plan, the international community and the leaders within the region must then move to an investment phase. This is where investments in physical infrastructure are combined and overpowered by an investment in more relevant assets – those that focus on developing the skills of the workforce in the region. Only this will address the root causes of the conflict, promote reconciliation, and stop the cycle of violence.

This paper addresses the third phase of rebuilding the Post Conflict Society by improving the prosperity for all citizens in the region. The first section will review how two regions, Rwanda and the Balkans have invested historically, in the context of a proper investment framework, in what we refer to as the Seven Forms of Capital. The second section outlines the Five Imperatives that

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<sup>5</sup> World Bank Post Conflict Aid; Oversight Issues to Congress by Martin A. Weiss; April 19, 2004

constitute the change process in Post Conflict Society, and provide broader success stories that focus on microeconomic activity, with a brief description of cluster theory.

## I. The Investment Framework and Results in Two Regions

### a. Focusing on the right investments

What does it take to rebuild Rwanda, the Balkans and other post conflict regions and enable prosperity? In order to answer this question, the simple and more complex impediments to creating wealth must be understood. The simple explanation is that natural resources, money and technology are the absolute necessities of wealth creation. However, they alone provide no guarantee of success.

The reality is that prosperity is more than natural resources, income or even purchasing power. It is also the enabling environment that provides the basis for a high level of productivity. When prosperity is considered in this broader context, it is useful to consider seven kinds of enabling capital that are intended as Nobel Laureate Amartya Sen suggests, “to give a better idea of a nation’s ability to produce things in the future.”<sup>6</sup> Of these seven forms of capital, the first three represent tangible, physical capital. The last four constitute higher, social forms of capital, and while more difficult to measure, have the greatest effect in creating prosperity. The seven forms are as follows:

1. Natural endowments, such as location, subsoil assets, forests, beaches, climate or the quality of its agricultural products.
2. Financial resources of a nation, such as savings and international reserves.
3. Manmade capital, such as buildings, bridges, roads and telecommunication assets.
4. Institutional capital, such as legal protections of tangible and intangible property, efficient government departments, and firms that create value and train and compensate workers well.
5. Knowledge resources, such as international patents, research centers, or university and think-tank capabilities.
6. Human capital, such as skills, insights and individual capabilities.
7. Cultural capital – more than articulations of culture, such as language, music and ritual, it includes attitudes and values linked to innovation, productivity and prosperity.

The development of these higher forms of capital creates the environment for individual and their firms to succeed. They encourage the innovation required to

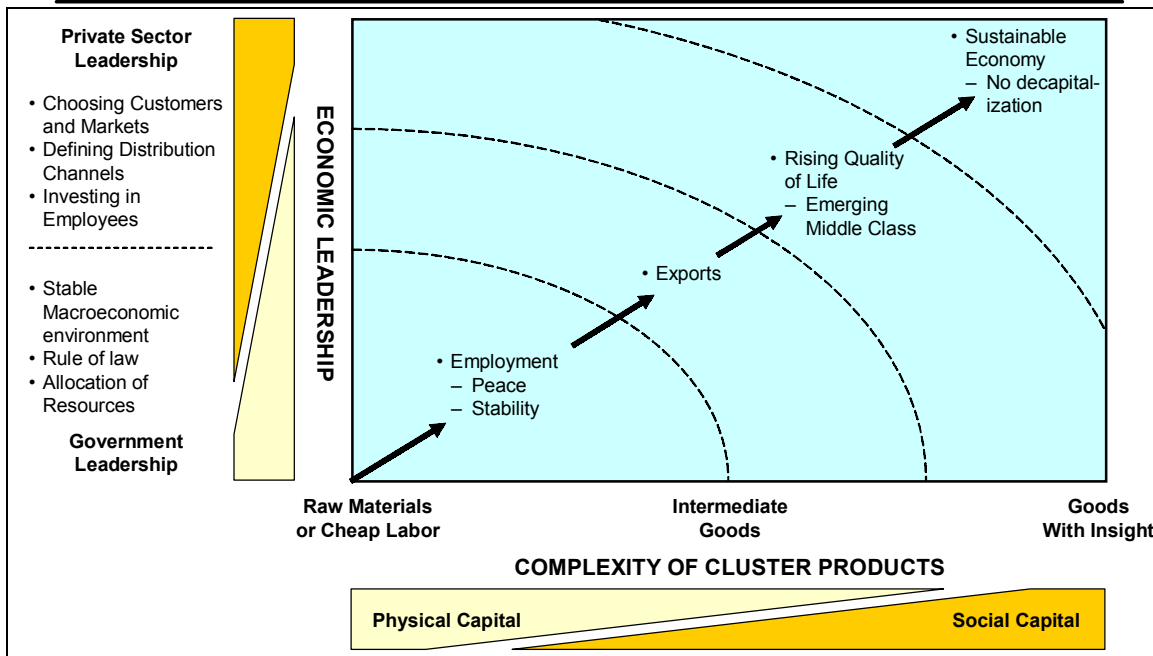
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<sup>6</sup> Fairbanks, Michael, “Changing The Mind of a Nation: Elements in a Process for Creating Prosperity”, Published in Culture Matters: How Values Shape Human Progress, Lawrence Harrison and Samuel Huntington, Basic Books, New York, 2000.

create jobs, higher salaries, and better returns to managers and investors. In such an environment, firms need to focus less on acquiring government favors and protected markets, or access to natural resources. The focus of these microeconomic foundations includes making strategic choices, utilizing best practice operations and services, leveraging effective distribution channels, and implementing effective marketing and learning procedures. Finally, the focus must include maximizing the effectiveness of innovative clusters<sup>7</sup> of related and supporting institutions that include universities, associations and private sector firms that support the development of a regional industry.

When a Post Conflict Society begins to become more prosperous, there is typically a shift from lower or physical forms of capital to higher, social forms. While the government initially plays a commanding role – allocating limited resources to create a stable economic environment, the private sector begins to emerge. Only the market forces of a free and unfettered private sector can direct the investments in creating higher forms of capital for a country. Without this transition, the forces of paternalism and protectionism risk preventing an economy’s ability to move beyond simple exports to the production of complex goods that can sustain and grow an economy

### The OTF Cluster Selection Process Choosing Clusters for Afghanistan’s Current Stage of Development



*Invest Rents from Selling Physical Capital in creating the Higher Forms of Social Capital Required to Sustain to Economy and Society that Afghanistan Seeks*

<sup>7</sup> According to Professor Michael E. Porter of the Harvard Business School, Clusters are geographic proximate firms and organizations with related and supporting industries within a particular field, linked by commonalities and complementarities. Close proximity among cluster firms force innovation among successful firms as they compete for their customer base. For more detail please go to section II of this paper in sub section 1 “Focusing on cluster development to improve productivity”, third and fourth paragraph.

<sup>8</sup> Neal Donahue and Michael Fairbanks, Seminar Entitled “Building The Competitive Advantage of Afghanistan”, Kabul Afghanistan, October 2003.

## b. Understanding the Impact of investments: Rwanda and Serbia

### Rwanda

In July 1994, military forces of the Rwandan Patriotic Front (RPF), led by now President Paul Kagame, entered Kigali and ended a three month genocide that took the lives of between 800,000 and one million Tutsis and moderate Hutus. Millions of displaced people returned to Rwanda and began the effort to rebuild their lives and their country. This ended over four years of bloodshed that culminated in the mass genocide.<sup>9</sup>

An interesting, and perhaps necessary question to ask is what led to former friends and neighbors<sup>10</sup> engaging in a ritual of mass genocide.<sup>11</sup> One view is to examine the assets in place in Rwanda as the mounting tension of conflict increased. Perhaps a more enlightening question is to ask about the assets that were in place when viewed through the filter of seven different types of capital.

In the early 1980s over 60% of Rwanda's population lived in poverty, and life expectancy, at approximately 40 years, was among the lowest in the world. But there was a promise of prosperity, with relatively well developed man-made capital, as compared to its neighbors it had good roads, electricity, water and telephones. It was selling almost \$150 million annually in coffee and tin was the second largest export revenue generator. Other physical assets existed, and although large natural gas deposits were discovered near Lake Kivu, they were not yet developed.

However when the tin market collapsed in 1985, followed by famine in 1987 and a drop in coffee prices by over 50% in 1989, it set the stage for one of the worst atrocities in modern history. With over 300 people per square kilometer, Rwanda was the second most densely populated country in Africa. This was particularly problematic as less than 200,000 jobs were outside of agriculture and 90% of the population lived in rural areas and existed on subsistence farming.

It is important to note that many Rwandans were relying heavily on physical capital, such as tin and basic coffee production – where they had no control of price levels in world-wide markets. Second, Rwandans were not investing in their social capital, as less than 10% of those who graduated from primary school went onto to graduate from secondary school. Knowledge resources were basically non-existent to the majority of Rwandans. Institutional capital was invested to develop mistrust among the two groups - as an ethnic quota system inhibited Tutsis from advancing in the government or the military.

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<sup>9</sup> Donahue, Neal, "How Business Strategy is Transforming Rwanda", Fletcher Forum of World Affairs (Vol 28:2), Summer 2004.

<sup>10</sup> A rumor of the initial distinction between Hutus and Tutsis was that it was made by the Belgians in 1935, based on the number of cows owned by each farm – those with ten or more were classified as Tutsis

<sup>11</sup> In 1963, with the third lowest per capita income in the world and in the early 1970s, hostilities led to discursions where Tutsis were massacred in Rwanda and Hutus were massacred in Burundi. Not surprisingly Tutsis uprisings were met with swift retribution.

Culturally, it is hard to imagine how Rwandans could believe that innovation and productivity had any importance in their individual prosperity, compared to the wealth gained through political legacy. The economic result was that by 1994, the economy shrunk by 50%, inflation surpassed 60%, and property and infrastructure had been destroyed. This set the stage for 3 months in 1994 where professionals had been particularly targeted in the genocide.

### Serbia & Montenegro

Without an extensive history lesson, the conflict in Serbia was the result of a longer problematic environment beginning when the Byzantines consolidated their empire by playing off religious and other interests of Serbians and Croats, in the 1300s.<sup>12</sup> It was further complicated by the advent of the Ottoman Empire in the same century. Ethnic tensions have ebbed and flowed over time but exploded during World War II, where stories such as Croatian massacres of Serbs near the Zagreb airport were among the many atrocities. As Yugoslavia prospered from its inception through the 1980s, many Serbians believed that Tito favored his region in Croatia with a more robust investment strategy. When Yugoslavia disintegrated after the fall of the Soviet Empire, leaders in Serbia and other states wasted little time in re-engaging the conflict.

After a decade of wars, sanctions and unsustainable policies, the Serbian economy was seriously damaged by the year 2000. The \$1,350 per capita GDP in 2001 was half of the 1989<sup>13</sup> level, and less than one-third of Croatia's \$4,614.<sup>14</sup> As a percent of GDP, Serbian export levels for 2001 were 19%, compared to 47% for Croatia, and FDI dropped to below \$27 million. Finally, official salary levels dropped to near \$100 per month and some estimated that the gray economy surpassed 40% of the economy.

For most physical capital, Serbia and Montenegro was found to have reasonably good ratings for natural endowments, such as proximity to markets, or arable land and for man-made assets, such as roads. Although it has an advanced economy compared to many post-conflict societies, in

#### Measured by its physical capital, Serbia is a moderately wealthy nation.

##### Financial

- \$200 monthly salary is at parity with Bulgaria, Romania and Macedonia, but lags Croatia and Slovenia
- Serbia ranks 54<sup>th</sup> of 81 WEF countries for available domestic credit as a % of GDP
- 83% of Serbian surveyed leaders state access to capital is difficult
- The interest rate spread of 13.3 ranks Serbia 73<sup>rd</sup>
- The Serbia investment rate ranks it 78<sup>th</sup> in the WEF
- FDI, at \$165 million, ranked Serbia last in the WEF in 2000; although improvements are underway

##### Man-Made

- Serbia ranks 36<sup>th</sup> in the WEF for paved roads as a percent of roads
- Serbia ranks 45<sup>th</sup> for telephone lines and 54<sup>th</sup> in mobile phones in the WEF
- At 2.3 personal computers per 100 citizens, Serbia ranks 62<sup>nd</sup> in the WEF
- Serbia ranks 54<sup>th</sup> in the WEF for losses in power transmission, as a percent of output
- Serbia only lags Slovenia among measured regional countries for producing machinery as a percent of exports

##### Natural Endowments

- Serbia has close proximity to the European Union market
- There is an abundance of raw material – I.e., 36% arable land level is among the region's highest
- Fruit growers claim that climate, soil and geographic location provide Serbia with excellent fruit varieties
- Waterways have provided cheap and effective transportation to ports along Danube and other locations

<sup>12</sup> Ghosts of the Balkans; Robert Kaplan 1990; provides the pre-1990s context for Serbia

<sup>13</sup> 1989 GDP level referenced from 2002 IMF Country Report, other GDP measures from SIEPA website

<sup>14</sup> World Bank Data Profile

2000, over 55% of its (official) export base were basic raw materials. Serbia also had poor levels of available credit and access to capital.

In terms of social capital, it performs well in human capital, as it ranks in the top quarter globally for secondary school enrollment, and within the top third for R&D.<sup>15</sup> However, these results may not be as positive as they suggest. First, specialized training is a much better predictor of national prosperity than basic education levels.<sup>16</sup> Second, per capita GDP is among the lowest globally, with absolute investment in R&D much lower. Third, the largest area for concern appears to be cultural and institutional capital, as leaders feel trust is among the lowest in the world; are split on if the government should lead or follow; and feel that corruption is one of the largest issues.

**Measured by its social capital, Serbia is a relatively poor nation, but does provide human capital support**

Cultural	Human	Knowledge	Institutional
<ul style="list-style-type: none"> <li>67% of leaders state that trust is among the world's lowest</li> <li>Produce buyers complain that growers often break contracts to sell goods for a higher price</li> <li>Only 23% of surveyed Serbian leaders believe that trust between the government and the private sector is high, relative to the world</li> <li>"The problem is that businesses here do not trust each other – and we are not used to sharing any information." Furniture cluster member</li> </ul>	<ul style="list-style-type: none"> <li>Serbia ranks 26<sup>th</sup> among the WEF for tertiary school enrollment and 16<sup>th</sup> for secondary school</li> <li>Serbia ranks 23<sup>rd</sup> for R&amp;D spending as a percent of GDP, but per capita GDP ranks 77<sup>th</sup></li> <li>Cluster members state that high schools should provide relevant technical training</li> <li>"We need to collaborate with universities to create the latest management and technical curriculum – they are not up to date." Cluster member</li> </ul>	<ul style="list-style-type: none"> <li>The primary request among cluster members is to learn about foreign markets</li> <li>Half of Serbian leaders state that local customers are demanding and do provide opportunities for them to learn about sophisticated customers</li> <li>Serbia ranks 28<sup>th</sup> in the WEF for utility patents per million population</li> <li>We gather market data from trade shows and form our partners, who tell us what designs to produce." Furniture Cluster Member</li> </ul>	<ul style="list-style-type: none"> <li>Two-thirds of surveyed Serbian leaders state that corruption is the main impediment to competitiveness; Corruption is ranked as the 4<sup>th</sup> largest problem in the country.</li> <li>80% of surveyed Serbian leaders state that tax policy discourages R&amp;D</li> <li>Chambers of commerce do not serve us well for networking, information or other benefits. We need to fix these and make them work again."</li> <li>Serbia ranks 67<sup>st</sup> in the WEF for the number of procedures to start a business</li> </ul>

## II. Addressing the change process in Post Conflict Societies

### 1. Focusing on cluster development to improve productivity

How can nations that have recently been ravaged by the turmoil of war focus on sustainable development and work together to achieve prosperity? Given the broad principles that underlie competitive advantage, a Post Conflict Society must create an environment that will support and encourage firms to achieve and sustain advantage. Harvard Business School Professor Michael Porter's research, which was summarized in his book, *The Competitive Advantage of Nations*, has identified four broad determinants that work together as a system and constitute the Competitive Diamond of national advantage.

<sup>15</sup> Based on 2002 World Economic Forum Ratings

<sup>16</sup> Robert Barro, Robert C. Waggoner Professor of Economics at Harvard University, during his presentation to the Serbian National Competitiveness Council in Cambridge, MA, in Cambridge, April 15, 2003.

The four determinants are factor conditions such as transportation, communication, and human resources; demand conditions, where sophisticated local customers typically improve the ability of firms to meet foreign customer needs; context for firm strategy and rivalry, which influence investment policies, protect intellectual property, and foster productivity growth; and related and supporting industries.

In nations with internationally competitive industries, they operate as a system, with each determinant vigorously reinforcing the other leading to constant upgrading and change throughout the system. Because of the interrelated nature of the diamond, nations are rarely home to just one competitive industry; rather, an environment is created which lead to the development of clusters of mutually supportive industries. These clusters are linked together as a system through vertical (buyer – seller) and horizontal (common customers, technology, channels) relationships.

Clusters innovate faster because they draw on local networks that link technology, resources, information, and talent. Strong competitive local pressures increase incentives for a cluster participant to innovate. Clusters build the basis for specialized skills and capabilities and enable competitive advantage in world markets.<sup>17</sup> This flow of services encourages large companies to support the development and growth of small and medium sized enterprises. These small and medium size enterprises will be the biggest source of employment in a Post Conflict Society.

## 2. Addressing Five Imperatives

As donor organizations and consultants re-engage with post conflict societies there is almost a template that is being developed for creating prosperity, which uses cluster theory. This involves working with cluster members, as defined by Professor Porter, to expedite the initial cluster development process from several decades to several years. This focuses on organizing key cluster players and developing a work plan that will use initiatives for cluster members to create platforms of innovation that improve productivity. This model allows *firms* to compete locally and regionally but to also collaborate for regional or global advantage. In addition, it is intended to leverage other members of the cluster as well as the government and NGOs. Projects are structured to enable cluster and public sector leaders to pursue principles of competition, investment in human and knowledge capital, and cooperation in complex decisions. Finally leaders focus on ***informed choice and timely action***.

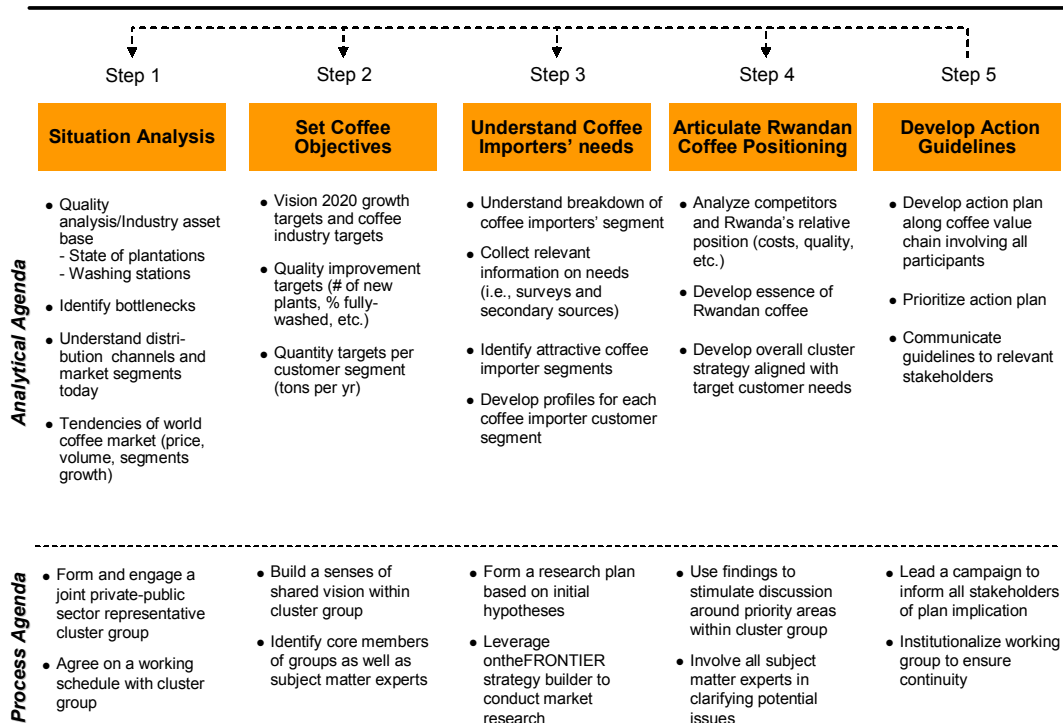
Projects begin with consultants leading the dialogue and developing the work plan, but activity shifts to leaders in the industry over a short time frame, typically from two to four years. The OTF Group uses a five step change process which

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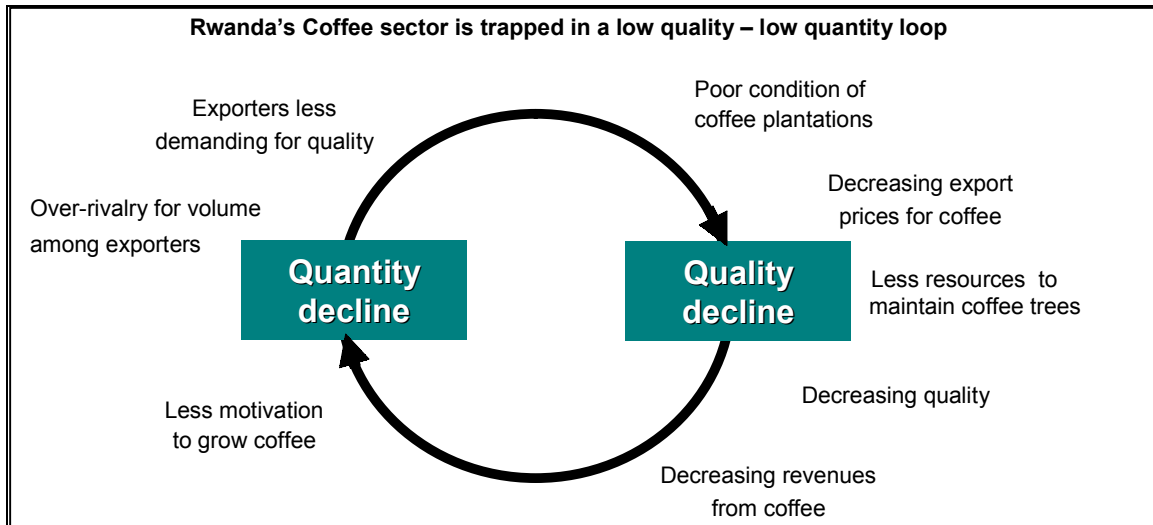
<sup>17</sup> Clusters of Innovation: Regional Foundations of U.S. Competitiveness; Professor Michael E. Porter, Harvard University; Monitor Company; The OTF Group; Council on Competitiveness; 2001 page 7

effectively galvanizes cluster members to learn how to analyze situations through a competitive framework to quickly set goals. Prior to the last step of developing a work plan the third step requires identification and segmentation analysis of customers, followed by an articulation of competitive position.

### Five Step Process - Coffee



For example, in the Rwanda coffee sector, the situation analysis determined that Rwanda's coffee sector had been trapped in a low-quantity / low-quality loop, a vicious cycle in which quality decline triggers quantity decline and vice versa. When farmers received the same price for different quality grades of coffee this reduced motivation to maintain plantations. Without these efforts, the quality declined and the industry was punished by price discounts applied to an already low commodity coffee price. This effect was reinforced by excessive rivalry among the current coffee exporters who compete for coffee quantity in order to cover fixed costs – a nearly impossible task given a local processing overcapacity estimated at 200%. Rwandan exporters were paying growers increasing prices for lower and lower qualities of coffee, even as the global market prices were falling to historic lows. Rwandan coffee exporters attributed the decline in commodity prices to cyclicalities and began buying high and selling low; hoping to outlast their competitors until coffee prices rebounded.



A lack of available long-term financing meant that there were only four coffee washing stations in the entire county compared to more than 2,000 washing stations in Kenya, which contributed to a lack of adequate quality control systems. Further many of the coffee trees were abandoned during and after the genocide, resulting in a lack of care and pruning – and over 25% were at least 30 years old. When attention could be paid to the coffee trees, fertilizer and pesticide costs, and limited extension services minimized the impact of farmers.

Together, these factors led to production yields of only 350 grams of coffee per tree. For comparison, Costa Rica, harvests more than 1.5 kilograms of coffee from the average tree. In addition, Rwanda was producing an average quality grade coffee and the commodity price levels for this grade decreased by half. This was the basis to choose a strategy to upgrade production, combined with market research to understand buyer and consumer needs, choosing a competitive position and beginning the action plan.

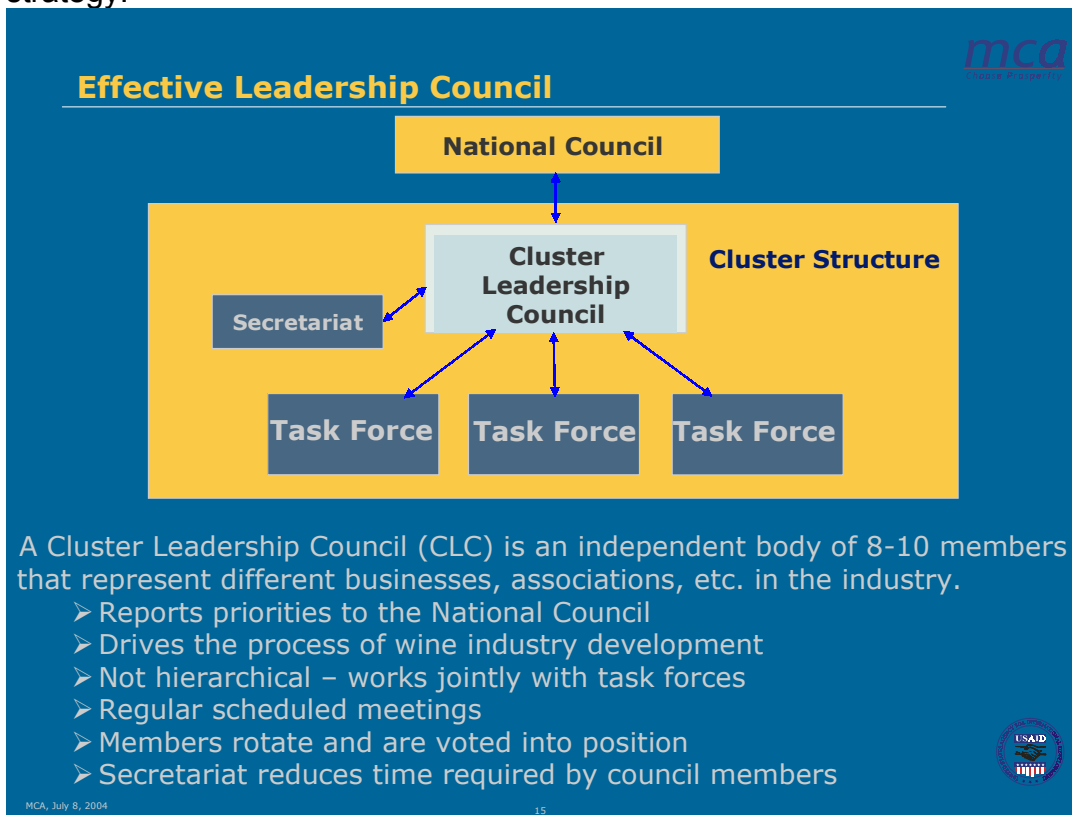
### **The Imperatives**

Although developing a cluster based agenda has challenges – not only in creating an effective work plan and in generating accountability among cluster members to expedite the process – there are subtle imperatives that must be addressed that seem mostly unique to a Post Conflict Society.

1. **Institutionalizing clusters and country leaders will assist in country wide institution building.** As institution building typically occurs simultaneously with cluster and economic development in a Post Conflict Society, there is often not the possibility to wait for institutions to be created. Further, a robust cluster agenda can be informative on the type of institution and activities developed to support a competitiveness project work plan.

In Macedonia for example, a National Competitiveness Council was formed as a plenary group to place competitiveness as a dialog on a national level. This group identifies obstacles to competitiveness and implements change. For instance, it has recently reduced import tariffs on raw materials that are used to create value-added goods. It also holds forums for clusters. Recently, members of the tourism industry obtained expedited Visa processing for tourists, and co-funding for promotion and trade missions. The council may also support cluster building associations and institutes with tax breaks for training, etc.

Finally, the cluster itself is institutionalized with a leadership council that reports to the national council, prioritizes and coordinates task force activity, as the cluster members build their work plans. Task force groups do the work, coordinating with members in the industry and with outside organizations such as NGOs and develop their work plans based on insights and strategy.



2. **There is a need to humanize the environment, in order to attract foreign direct investment.** Often it is easy for foreign investors to remove post conflict societies from their short list of investment regions, due to generalized perceived risks. It is then paramount for local leaders to show that the majority of people are humane and that the region does have real investment opportunities.

After 1994, Rwanda began to develop a plan to revitalize the economy and provide a secure environment for foreign investors. The exchange rate was deregulated in 1995, it joined the WTO in 1996, and a new tax law was implemented in 1997. Privatization began in 1998, combined with tax and other breaks for foreign investors, including tariffs being reduced from 100% to 40%. Bank laws were introduced and banks restructured in 1999. In 2000, the government formed the Rwanda Investment Promotion Agency that offered a one stop shop for investments and create a free trade zone.

However, perhaps an equally important part of this campaign is Rwanda's focus on tourism (<http://www.rwandatourism.com/home.htm>) – which places a face on the people of Rwanda. Rwanda's goal in tourism is to generate \$100MM in tourism receipts in 2010 by focusing on creating high value and low environmental impact experiences for Eco-travelers, Explorers and Individual Business Travelers. One major event that helped in enabling this goal was the Official Launch of Rwanda as a Tourism Destination at ITB in London in November 2003. This not only was helpful in implementing the tourism strategy, but this and word of mouth among travelers is signaling to investors that Rwanda is past its ethnic conflicts and is now an open and friendly environment. The effect of promoting Rwanda as a safe tourist destination also positively impacts the reputation of Rwanda as a safe investment environment.<sup>18</sup>

- 3. When developing clusters and national councils it is critical to have all voices represented in task force and council groups.** It is particularly important that there is a clear understanding that the outside party(ies) is being a fair broker and that no one particular group is benefiting at the expense of other groups. This is true in general, but both sides involved in the conflict should be active participants.

In 2001, Macedonian and Albanian political leaders signed the Ohrid Accord providing for significant constitutional amendments and political reforms that would improve the status of the ethnic Albanian minority. But the signature was delayed five days, while Macedonian government troops and ethnic Albanian rebels engaged in a deadly series of tit-for-tat retaliations. Although there was little trust or even expectation of peace among either ethnic Albanians or Macedonians, peace has held. In 2003, an equal number of Macedonians and Albanians began working together on a Lamb and Cheese Cluster project. They have jointly performed trade missions, trainings and local and regional promotions. While the group is small, with little PR, it sets an excellent example for the larger population as a whole.

- 4. Leveraging and coordinating donor agencies will have the greatest impact earlier in the process.** In earlier years NGO and Donor organizations have the largest teams, typically the most money, but are not

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<sup>18</sup> Rwanda has generated over \$30 million in FDI by 2002, from the UNCTAD FDI/TNC database; UNCTAD.org

usually well coordinated. A single agreed upon agenda (within reason) can greatly increase the chances of robust success:

In Rwanda, donor organizations agreed to work with the coffee cluster to fund \$25 million of a \$69 million plan that focused on upgrading coffee quality and targeting highly discerning and affluent coffee drinkers with a promotion campaign. Donor organizations were organized to support training, planting new trees and washing stations co-funding, and association development. The public sector financed energy supply, road infrastructure, warehouses, irrigation and promotion co-funding with the private sector, including the development of a website. (<http://www.rwandacoffee.com/>) The government also removed export taxes through part of a productive conversation with industry leaders. The private sector budgeted \$23 million primarily on washing stations, new trees and promotion.

In the Balkans and Eastern Europe, regional competitive-based projects meet annually to share best practices, understand how country leaders may collaborate, and how specific similar clusters may cooperate – such as in combining several countries as stops in a tourist destination package. In addition, Serbia’s fruit and fruit juice clusters identified standards and training as critical requirements to selling to regional European markets. The cluster task forces contacted organizations such as Southeast Europe Enterprise Development (World Bank) that performs subsidized management training, Soros funded Open University for organic training, and ACDI/VOCA for phytosanitary and HACCP standard training. Training center co-funding was also being considered by International Relief and Development, America’s Development Foundation and Mercy Corps.

5. **A nation that is migrating from a protracted conflict must completely shift its preconditions for change.** In order to develop an agenda for change, there are five mutually exclusive and comprehensive conditions that must be in place. In a Post Conflict Society, these conditions exist, but are structured to achieve horrific results – therefore, each of these conditions must be addressed in a way to shift the results to a productive agenda:

- Can the **tension** that has existed in a divisive way be altered so that former adversaries will see the need to work together on a common agenda?
- Are people **receptive** to considering new ideas and experimenting with new actions that will focus on economic development and not on an environment of violence?
- Does the society embrace a clear sense of **guiding principles** towards the goal of creating wealth for the average citizen, instead of viewing wealth as finite, which requires a violent approach in a zero-sum game?
- Do leaders have an agenda to gain competitive **insights** necessary to make complex choices?

- Is the ***new leadership*** prepared to act on each of the above four conditions for change *constructively*?

New leaders are emerging in Serbia's wood furniture industry, and are focusing on ways to work together on developing foreign markets. The tension in the industry that resulted from sanctions, as total exports dropped by 80% throughout the 1990s, is now born of decreases in relative productivity and design. The furniture, construction materials and flooring cluster guiding principle is to enable the group to re-engage with markets and increase exports by a conservative \$15 million in five years.

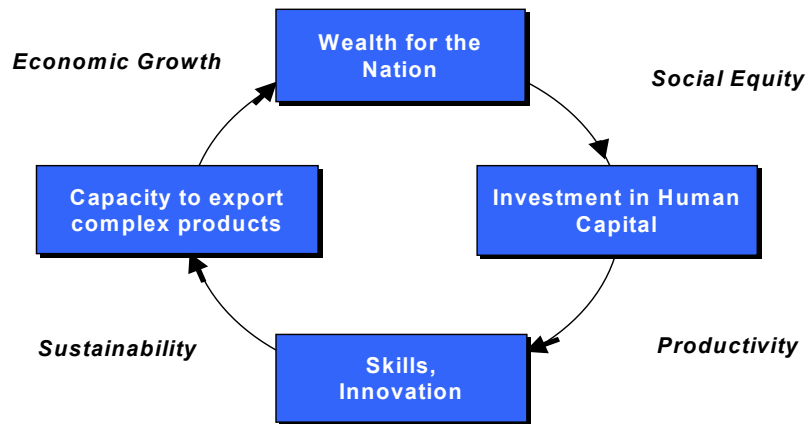
Members that were interested in collaboration gave other members factory tours, shared information, jointly built trade fair booths, and examined ways to upgrade technology. They brought in local university professors for information concerning foreign market trends. Several members have targeted regional markets and have won jointly bided contracts, where individually they would have lost. They have spent time together performing market research to address additional contracts and have begun joint sourcing and procurement.

Based on research, they are now examining longer-term projects such as creating industry standards and developing a regional fashion and furniture design center, in collaboration with the textile industry.

***Summary: Improving the Standard of Living Through Productivity***

The central economic goal for a post conflict region or nation should be to rapidly attain a high and rising standard of living for *all* of its citizens. This is reflected in high per capita income and high paying, satisfying jobs for a large proportion of those who are able to work. A high and rising standard of living is driven by high and rising productivity based on a nation's stock of the seven forms of capital: *cultural, human, knowledge, institutional, financial, man-made and natural endowments*. Increasingly, countries depend heavily on more complex advantages needed for innovation.

## How Does Wealth Actually Get Created?



Countries and companies that export complex products generate profits that they can re-invest in the compensation and training of their workers. Better-trained and motivated workers improve the capacity to export increasingly complex products, which bring sustained increases in wealth for the average citizen. (See diagram above.) For post conflict societies, the challenge to create this “Virtuous Cycle” of investment in human capital and more highly sophisticated exports has emerged as a central development challenge. This challenge must take into account subtle imperatives that could inhibit the change process. Ultimately a program focused on expedient investment in human and social capital in post conflict societies is the only way to address the issues of inequity and to avoid the mistakes of the past.