International companies in fragile states

Denmark must not fail to promote corporate social responsibility in fragile states. International companies remain active in these environments, and often worsen rather than alleviate poor governance. Financial transparency and human rights initiatives offer the first step in ensuring that this detrimental influence is corrected.

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There is no frontier separating fragile states from the global economy. The political instability and physical insecurity of fragile states has not resulted in a lack of interest from international companies. Rather, foreign investment is predominately focused on the exploitation of natural resources amidst the poor governance, protracted poverty and violent conflict that characterize these environments (see Table 1). Foreign investment in the natural resources of fragile states has not only dominated the formal economies of these countries, but also provided the vast majority of their governments' revenues. For instance, oil revenues in Sudan account for over 60% of total government earnings. This combination of foreign investment in malign economic and political environments has resulted in international companies having a resoundingly detrimental influence in fragile states. They act as vehicles producing value out of natural resources through the international market place, often cementing the political power of oppressive governments, exacerbating inequality, or worse, intensifying and prolonging civil wars.

'Governments in fragile states are often dependent on revenue from the natural resources exploited by international companies.'

The negative repercussions of international companies being active in fragile states have been highlighted by non-governmental organizations. For example, calls have been produced seeking an end to West Africa's 'blood diamond' trade, opium production in Afghanistan, and forced labour and oppression in Burma's oil-dependent economy. The United Nations has also underlined the importance of international companies in various 'name and shame' campaigns, most notably concerning illegal mineral extraction in the Democratic Republic of Congo.

POLICY RECOMMENDATIONS

1. The influence of international companies should become a key element in Denmark's policy towards fragile states.
2. Denmark should promote corporate social responsibility initiatives among Danish companies.
3. Denmark should enhance efforts to increase corporate social responsibility initiatives at a multilateral level among donor governments.

The private sector can frustrate peace and development in fragile states in numerous ways. While some interventions, such as diamond-smuggling, are illicit in nature, aiming to profit directly from the instability of war, others are legitimate, for instance corporate activity in Sudan's oil industry, but nonetheless have an adverse influence on conflict. Indeed, in civil wars, both governments and rebel groups have exploited private-sector actors as vehicles with which to earn the revenue they need and establish the required international connections to access military arms and continue fighting. Furthermore, the private sector has provided a source of self-enrichment for ruling elites, which in many cases has magnified the political and social grievances that brought on the conflict in the first place.

International companies in the extractive industries of petroleum, mining and timber represent much of the legitimate side of the private sector prevalent in

TABLE 1: FOREIGN DIRECT INVESTMENT IN FRAGILE STATES

Failed states rank	Country	GDP growth, 2006	FDI stock as percentage of GDP, 2006	Primary commodities as percentage of top five export commodities, 2005
1	Sudan	11,8	30,3	100
2	Iraq	-4,3[b]	3,0	ND
3	Somalia	ND	5,1	ND
4	Zimbabwe	-4,8	25,7	89
5	Chad	1,3	68,5	ND
6	Ivory Coast	4,1	24,0	82
7	DR Congo	5,1	12,7	ND
8	Afghanistan	5,3	0,3	ND
9	Guinea	2,8	20,7	98[c]
10	Central African Republic	3,5	14,2	95
15	Uganda[a]	5,3	25,0	100
16	Bangladesh[a]	6,7	6,3	6[d]
21	Nepal[a]	1,9	1,5	17[d]
31	Kenya[a]	5,7	5,0	100[d]
33	Burkina Faso[a]	5,6	1,7	97[d]
36	Egypt[a]	6,8	36,4	85
	World	4,0	24,8	

Notes: a) Danida partnership country; b) Year 2000; c) Year 2002; d) Year 2003
Sources: Foreign Policy Fragile States Index, UNcomtrade, UNCTAD, World Bank World Development Indicators

conflict-affected countries. These companies, compared to their counterparts in manufacturing or services, more often remain in conflict settings because of the sizeable, fixed and capital-intensive nature of their investments. Manufacturing and service industries have either never functioned in these environments, or else the necessary infrastructure and networks have been destroyed by war. The enormous capital investments, advanced technology, technical expertise and access to international markets of extractive industry corporations are essential in producing value from natural resources in fragile states. However, the economic benefits of this foreign investment often translate into feeding conflict rather than resolving or mitigating it.

CORPORATE SOCIAL RESPONSIBILITY IN FRAGILE STATES: BETWEEN RHETORIC AND REALITY

The activities of international companies do not necessarily have to result in doom and gloom in fragile states. Foreign investment can spur on social development through economic growth, infrastructural development and employment. However, good governance is essential as a conduit for making the connection between foreign investment and social and economic development. International NGOs have spearheaded the development of policy instruments, such as the UN Global Compact, the Extractive Industry's Transparency Initiative and the US/UK Voluntary Principles on Security and Human Rights. These initiatives aim to influence a significant part of the demand-side of the equation – international companies – in order to alter the oppressive and exploitive practices of governments in fragile states, representing much of the supply-side. Corporate Social Responsibility (CSR) is rising on the agenda of many international companies, including those investing in fragile states.

> 'The implementation of international CSR initiatives by international companies can not only improve social development in fragile states, but also enhance firm performance.'

International companies have often lost out in the emerging markets of fragile states through their conduct in face of the challenges presented in these precarious investment climates. The execution of Ken Saro-Wiwa and other campaigners for the Ogoni people of the Niger Delta brought Shell's activities in Nigeria to widespread international attention, damaging the company's reputation. Similarly, BP and Chevron's continual investment in Angola has often been connected with government corruption amidst an utter lack of social service provision for the country's poor. The image of De Beers was forever tarnished by its activities in West Africa, and Levi Strauss and Co. and the Danish companies Carlsberg and DLH were forced to exit Burma due to divestment pressures from international human rights groups.

There is a business case for CSR activities in fragile states. But even those international compa-

TABLE 2: OIL COMPANIES PARTICIPATING IN INTERNATIONAL CSR INITIATIVES, June 2007

Company	Home country	EITI	Global Compact	Voluntary Principles	Global Reporting Initiative
A.P. Møller-Maersk	Denmark				
British Petroleum	United Kingdom	√	√	√	√
Chevron	United States	√		√	
CNOOC	China				
Exxon Mobile	United States	√		√	
Gazprom	Russian Federation				
Norsk Hydro	Norway	√	√	√	
ONGC	India		√		
Petrobras	Brazil	√	√		√
Petronas	Malaysia				
Royal Dutch Shell	United Kingdom / Netherlands	√	√	√	√
Sinopec	China		√		
Statoil	Norway	√	√	√	√
Total	France	√	√		

Source: UNCTAD

nies who are experienced in operations in fragile states are still discovering the benefits of CSR. For example, positive relations with local populations can result in less stoppage time due to a lack of violent responses from communities around operating zones of the sort that have frequently occurred in Nigeria and Sudan. International companies in fragile states continue to struggle with the idea that, despite their apolitical stance, their main activities produce political and social ramifications. They often must navigate political divides in society in their CSR activities, placing the national government at odds with local communities. Altogether, the implementation of international CSR initiatives in fragile states by international companies can not only improve social development, but also enhance firm performance.

Good governance is lacking not only within fragile states, but also at the global level. International CSR initiatives, such as the UN Global Compact or the Extractive Industries Transparency Initiative, contain flaws in monitoring and enforcement, but they remain crucial in advancing international norms and values among companies that are active in fragile states. Thus far, no binding international regulation exists over foreign corporate activities in these countries. Voluntary principles continue to grow on an ad hoc basis between international companies, NGOs, the United Nations and donor governments. However, many western corporations, as well as those emerging in China, India and other parts of Asia, have not been proactive in taking on pro-development and conflict-sensitive practices in their operations in fragile states.

ASIAN INVESTMENT

The investment of Asian companies in fragile states still pales in comparison to that of companies from North America and Europe. Nonetheless, many commentators have promoted the idea that the recent expansion of Asian companies may lead to a loss of western influence, not only in terms of the promotion of human rights and development, but also with regard to access and control over natural resources on the continent. These worries have been most pronounced with regard to oil-producing countries in sub-Saharan Africa. Corporations originating from North American or European countries, where relatively high expectations of corporate responsibility exist, are more compelled to take on human rights-sensitive and financial transparency measures to avoid emerging reputation and legal costs that can be incurred in home markets. On the other hand, the state-owned companies of rising developing economies, such as China, India and Malaysia, have little pressure from their home constituencies concerning the human rights consequences of their activities.

> ‘Asian companies are increasingly engaging in corporate social responsibility activities.’

In recent years, Asian national oil companies operating in fragile states in Africa have shown signs of increased adoption of CSR activities. This involves sponsoring hospitals, schools and other infrastructural projects in their areas of operation. However, thus far they do not present their CSR activities as effec-

TABLE 3: DANIDA'S PUBLIC PRIVATE PARTNERSHIP PROJECT, 2004-2007

	2004		2005		2006		2007	
	Projects	Grant (DKK mn)	Projects	Grant (DKK mn)	Projects	Grant (DKK mn)	Projects	Grant (DKK mn)
PPP in fragile states[a]	3[b]	4.5	1[b]	3	5[b]	6.7	3	4.8
Other PPPs	2	4.9	3	11.6	7	64.7	8	23.2
Total	5	8.4	4	14.6	12	71.4	11	28.0

Notes: a) Includes the following countries: Bangladesh, Egypt, Indonesia, Kenya, Nepal, Pakistan, Sierra Leone, Sri Lanka and Uganda; b): Includes regional projects and hence, also, grants to non-fragile states.

Source: DANIDA

tively as their more experienced western counterparts. Nonetheless, like their western counterparts, these social activities clash with the wider political ramifications of their economic investment, particularly in more 'contentious' environments, such as Sudan and Burma. This makes the task of 'selling' the social benefits they provide more problematic.

POLICY ADVICE FOR DENMARK

Aside from emerging Asian companies in fragile states, western corporations have also failed to live up to standards of corporate social responsibility. There still remain a large number of international companies that have yet to take on international CSR initiatives (see Table 2). For instance, Denmark's flagship company, A.P. Møller-Mærsk, sits awkwardly next to leading Chinese companies in failing to take on international CSR initiatives. The importance of CSR in fragile states is far from universal. There is a need to build a consensus on CSR issues in fragile states among corporations, as well as within and among donor governments. This is not only relevant from a development perspective, but also to ensure the long-term security and progression of foreign investment in fragile states.

Denmark currently supports CSR activities in developing countries through Danida's Public Private Partnership Programme (PPP), which works within the UN Global Compact framework and seeks to enhance CSR activities in order to promote social and economic development. The programme started operating in 2004, and since then Danida has granted DKK 19 million for 12 PPP projects in fragile states (see Table 3). Danish businesses are active in fragile states; the Danish government should do more to ensure they play a positive role in these environments.

> 'Denmark should place a higher priority on ensuring Danish companies that are active in fragile states take on financial transparency and human rights initiatives.'

Closer dialogue must be established between Denmark and Danish companies that are active in fragile states. This task of corporate engagement should be considered of high priority to Denmark and other donor governments. Donor governments have a crucial role to play in bridging the governance gap in fragile states. At both national and international levels, it is critical that Denmark promotes financial transparency and human rights sensitivity among Danish corporations as an integral part of its fragile states policy.

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