



DIRECTIONS IN DEVELOPMENT
Private Sector Development

How Firms Cope with Crime and Violence

Experiences from around the World

Michael Goldberg, Kwang Wook Kim, and Maria Ariano



THE WORLD BANK

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THE WORLD BANK
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Foreword

The World Bank's *World Development Report 2011: Conflict, Security, and Development* identified a significant knowledge gap concerning the impact of crime and violence on the private sector. Although researchers have examined crime and violence thoroughly resulting from some perspectives—such as youth and crime issues or the rule of law—little work has been done on how private businesses cope.

Crime and violence inflict high costs on the private sector—costs that are rising globally, according to the World Bank's Enterprise Surveys, discussions with chambers and associations, and the Bank's Country Partnership Strategies, which reference the losses in terms of gross domestic product (GDP). In Latin America and the Caribbean, for example, losses crime and violence have been estimated at 9 percent of GDP in Honduras, 7.7 percent in El Salvador, and 3.6 percent in Costa Rica. In sectors such as clothing assembly, international purchasers can shift know-how and capital quickly to less violent destinations, while other sectors such as extractive industries are more likely to stay despite rising violence. Behind the statistics are human costs: lost jobs; shifting of businesses' working capital from productive uses to security firms; and an increase in contraband, fraud and corruption, and "rule of law" issues.

In this book, original case studies from Brazil, Colombia, Jamaica, Mexico, Nepal, and Rwanda illustrate the specific challenges to businesses and the coping mechanisms that firms and groups of firms have used successfully against crime and violence. The book's findings have implications for the private sector, governments, and the World Bank's efforts to support both under difficult circumstances.

Janamitra Devan
Vice President, Financial and Private Sector Development
The World Bank Group

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Imagine developing a six-country case study series covering Latin America, South Asia, and Africa and then synthesizing the results for a book on a highly controversial topic. This helps you to begin to imagine the number of people and the level of support and commitment it has taken to reach the finish line with this publication.

The first people to acknowledge are those who helped with the strategic vision, leadership, and financial support. For their support from the beginning, the authors thank Yongmei Zhou, Nabila Assaf, Bertine Kamphuis, and Michael Engman (of the World Bank's Fragile and Conflict-Affected States unit); Lily Chu (manager of the Bank's Financial and Private Sector Development Network for Latin America and the Caribbean); and Klaus Tilmes (director, Financial and Private Sector Development Network). Others who shared their insights included Pierre Guislain (International Finance Corporation, IFC) and Joel Hellman (the World Bank's Fragile and Conflict-Affected States office).

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As this project evolved, the authors turned to senior World Bank and other experts to serve as peer reviewers and would like to express the team's appreciation to World Bank staff members Ivan Rossignol, Rodrigo Serrano, and Flavia Carbonari as well as to Dr. Topher McDougal of the University of California, San Diego, for playing this thoughtful role.

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Abbreviations

| | |
|--------|--|
| C3 | Program on Crisis, Conflict, and Cooperation |
| CAS | country assistance strategy |
| CCSD | Center on Conflict, Security, and Development |
| CEDEZO | <i>Centros de Desarrollo Empresarial Zonal</i> |
| CGAP | Consultative Group to Assist the Poor |
| CPA | Comprehensive Peace Agreement |
| CPS | country partnership strategy |
| CSIS | Center for Strategies and International Studies |
| CSR | corporate social responsibility |
| DIME | Development Impact Evaluation Initiative |
| DPC | Development Policy Credit |
| DPL | development policy loan |
| ECSC | European Coal and Steel Company |
| eHIPC | enhanced Highly Indebted Poor Country |
| ERBF | Eastern Regional Business Forum |
| ESW | economic and sector work |
| FDI | foreign direct investment |
| FNCCI | Federation of Nepalese Chambers of Commerce and Industry |
| FPD | Finance and Private Sector Development |
| GDP | gross domestic product |
| ICAP | International Career Advancement Program |
| ICBSP | Inner Cities Basic Services for the Poor Project |
| IDA | International Development Association |
| IEG | Independent Evaluation Group |
| IFC | International Finance Corporation |
| JAC | Juntas de Acción Comunal |
| JSIF | Jamaica Social Investment Fund |
| LPPP | local public-private partnership |
| M&E | monitoring and evaluation |

| | |
|-------|--|
| MFI | microfinance institution |
| MIGA | Multilateral Investment Guarantee Agency |
| MSME | micro, small, and medium enterprise |
| NBF | Nepal Business Forum |
| NGO | nongovernmental organization |
| OBA | output-based approach |
| ORPTN | Office of Tourism and National Parks |
| P&G | Procter & Gamble |
| PPD | public-private dialogue |
| PPF | public-private forum |
| PPM | public-private mechanism |
| PSD | private sector development |
| PSOJ | Private Sector Organization of Jamaica |
| RIEPA | Rwandan Investment Promotion Agency |
| RNIC | Rwanda National Innovation and Competitiveness |
| SDN | Sustainable Development Network |
| SME | small and medium enterprise |
| StAR | The Stolen Asset Recovery Initiative |
| TAL | Technical Assistance Loan |
| TI | Tijuana Innovadora |
| TWG | Tourism Working Group |
| UNODC | United Nations Office on Drugs and Crime |
| UPP | Unidade de Polícia Pacificadora |
| VDC | Village Development Committee |
| WBG | World Bank Group |

The Nature, Scale, and Scope of Private Sector Responses to Crime and Violence

Introduction

The costs of crime and violence to the private sector amount to significant losses in terms of gross domestic product (GDP), according to World Bank Enterprise Surveys, discussions with private sector chambers and business associations, and dialogues with governments throughout Latin America.¹ Losses caused by high rates of crime and violence have been estimated at 9.0 percent of GDP in Honduras, 7.7 percent in El Salvador, 5.0 percent in Jamaica, and 3.6 percent in Costa Rica (World Bank 2010, 2011a, 2011b, 2011c).

The private sector's response to crime and violence varies by country, size of firm, and sector, among other factors. For example, in an environment with a high concentration of small and medium enterprises such as Jamaica, international buyers have lower switching costs: they can shift work orders, know-how, and capital in a short time to less-violent countries. On the other hand, large firms in extractive industries in Guatemala have millions of dollars in capital investments and are therefore forced to absorb the increased costs incurred in environments with high rates of crime and violence. From a financial perspective, these high rates can lead to increased business costs, such as a shift of scarce working capital from productive uses to security solutions; losses resulting from theft, contraband, fraud, and corruption; and higher insurance costs. At the same time, some firms simply exit the market, while others (such as private security firms) thrive amid high levels of violence, and some become party to the violence. The violence may be part of a strategy by powerful firms to eliminate competition or a way to run a protection scheme. Finally, in some cases, firms can contribute to alleviating the root causes of crime and violence by responding in a way that brings adversaries together and provides a platform for peaceful interaction and alignment of economic interests.

Some governments are increasingly concerned with the social and economic effects of high rates of crime and violence, as the recent cases of Honduras, Guatemala, and Brazil illustrate. In the first two months of 2012 alone, the government of Honduras received a Development Policy Loan (DPL) focused on crime and violence issues (the first such DPL by the World Bank). Guatemalan President Otto Fernando Pérez Molina proclaimed a response to rampant crime and violence as the top priority for his administration's national development strategy (*La Hora* 2012). In Brazil, Rio de Janeiro is increasing its "pacification programs" in the slum areas to prepare for the World Cup (2014) and the Olympic Games (2016).

Although the issue of crime and violence has been examined thoroughly from a number of perspectives—such as youth gangs, money laundering, drug trade, human trafficking, and justice system reform—little systematic work has been done to understand how private businesses cope and try to preserve their competitiveness. (See box 1.1 for a literature review on the role of firms in environments that are prone to violence and conflict.) This volume documents a wide spectrum of coping strategies, from exit to survival, from acting alone to collective security mechanisms, and from operational strategies to predatory strategies (in which firms contribute to crime and violence).

This understanding of business coping strategies is an important input into how the private sector, governments, and the World Bank Group can help the business sector to survive and even grow in environments with high rates of crime and violence. The World Bank Group can support businesses in a range of direct and indirect ways, such as policy dialogues, lending, investment, business environment diagnostics, advisory and convening services, research, benchmarking exercises, and surveys (for example, the Bank's Doing Business and Enterprise Surveys).

Study Scope and Methods

This volume analyzes how firms, private sector associations, and other private sector actors cope with crime and violence—differentiating, when possible, by firm size, sector, and other characteristics that help explain the choice of coping mechanisms and their effectiveness. The analysis includes case studies of recent efforts to tackle crime and violence involving the private sector and describes cases of crime and violence associated with the drug trade, human trafficking, political and ethnic violence, and weak rule of law in some postconflict countries. However, it is not comprehensive. It does not, for example, include cases of violence during ongoing civil wars or from domestic violence. The cases primarily include examples of relatively successful coping mechanisms.

Although the private sector (both the real and the financial sector) can also perpetuate crime and violence, the volume focuses primarily on nonpredatory coping mechanisms. The city studies include Ciudad Juárez, Medellín, Mexico City, Rio de Janeiro, and Tijuana; the country-level studies include Jamaica, Nepal (with a focus on the hydropower sector), and Rwanda (with a

focus on the tourism sector). These case studies were chosen to reflect the diversity of the private sector responses to violence, including such factors as

- Geographical diversity;
- Enterprise size;
- Sectors or industries;
- Sources of crime and violence, including not only cases where crime and violence levels are particularly high, but also cases where rule of law is relatively weak following civil war (Nepal) and genocide (Rwanda);
- Challenge type (how firms are affected by crime and violence); and
- Coping mechanisms.

Box 1.1 Literature Review on the Role of Firms in Environments Affected by Violence and Conflict

The literature review describes the impact of violence on firms (McDougal 2010) and a variety of coping mechanisms, including exit (Hirschman 1994); violence and conflict mitigation through associations and trade (Jha 2007; Santa-Barbara 2007; Varshney 2002); and perpetuation of the violence (McDougal 2010; Pugh, Cooper, and Goodhand 2004).

Hirschman (1994) gives a historical perspective on the power of exit as a way for firms to cope with unfavorable environments, suggesting that the United States was born as a result of businessmen exiting the European market in favor of a new liberal frontier. Business exit is outlined as a positive condition of economic development and an underpinning of free capitalist growth and innovation.

The coffee industry in postconflict Rwanda serves as a platform for former enemies to reconcile and form relationships. Varshney (2002) uncovers similar themes in India: a study of six large cities in India found that the presence of civic associations was the decisive factor in preventing the outbreak of ethnic violence in some cities, while others succumbed to such violence. The key insight from Varshney's work is that the social capital developed through civic associations (business associations, professional associations, unions, and indeed commercial transactions *per se*) brings Hindus and Muslims together around a common set of interests, providing a platform to form "peace committees" that address emerging rumors, tensions, and clashes. Moreover, some businesspeople have a vested interest in violence (and seek to perpetuate it) while others have an interest in preventing it.

Jha (2007) develops a quantitative analysis of the legacy of medieval trading ports in India, finding that a medieval trade legacy had a significant effect on ethnic violence. The 1,000 years leading up to the 17th century saw a relationship develop between Muslim traders and the Hindus in the port cities on the Indian subcontinent. This duration of symbiotic trade relations depended on the complementarity of traded goods that could not be locally replicated or stolen and was facilitated by few barriers to trade, allowing for competition, low prices, and redistribution of surpluses. In other words, Hindus and Muslims were bound together through rational interest and the social connections that were passed down through generations. Today, those cities that were once medieval ports are 20–30 percent

box continues next page

Box 1.1 Literature Review on the Role of Firms in Violent and Conflict-Affected Environments*(continued)*

less likely to experience a religious riot, even as feuding Muslims and Hindus have killed more than 40,000 across India since 1947. From 1850 to 1950, such towns had 80 percent less chance of experiencing religious violence in any year. Because of the heavy silting of river inlets brought by yearly monsoons, many of these medieval harbors are now landlocked, yet the legacy of medieval trade's institutional mechanisms continues to prevent ethnic violence from reaching the levels of the rest of the country. Santa-Barbara (2007) provides further evidence of the immense peacekeeping power of industry, suggesting that the decades of European peace following World War II that brought unprecedented levels of economic growth were partly the result of the European Coal and Steel Company (ECSC), which served as an important step in the formation of the European Union.^a The examples of traders in India and the ECSC show how firms can play a critical role in reducing conflict and promoting lasting peace.

Pugh, Cooper, and Goodhand (2004) outline the combat, shadow, and coping economies that arise from waging war, profiteering from war, and coping with war. The authors use the examples of Afghanistan, Bosnia and Herzegovina, and Sierra Leone to show the resilience of shadow economies, the power of these economies to fuel protracted conflict, and the need for a regional focus in addressing conflict-based impediments to business because violence can so easily spill over national borders. McDougal (2010) looks into the case of Liberia to investigate the sensitivity of firms to the civil war. He notes that often looters preserve the value-added process to have a sustainable source of value to extort. Finally, he also outlines (2010) four central strategies that Liberian firms adopted to cope with increased predation: dispersal, increased throughput, investment in strengthened property rights, and accommodation. To determine their strategy, firms weighted the tendency of predatory groups to loot and the firms' own willingness to expend financial or social capital. McDougal argues that the most successful firms during wartime are those that can rapidly gather and process information at the place of production to adapt their functions spatially and temporally.

a. The European Coal and Steel Company began in 1957 as a Western European economic union creating a joint market for coal and steel. It was dissolved in 2002 and absorbed by the European Community.

Based upon an analysis of the cases, the paper discusses policy implications, including strategic and operational recommendations for the World Bank Group. The research questions include the following:

- How does the private sector respond to crime and violence, and why are some firms and groups of firms more effective than others?
- What are the policy implications for governments as well as for the World Bank Group's support of efforts to eliminate poverty and the conditions that encourage crime and violence?

Note

1. Policy dialogues were recently held during the development of Country Partnership Strategies and Country Assistance Strategies with governments in Latin America.

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Crime, Violence, and the Economy

Factors Contributing to Crime and Violence

Crime and violence compose a multifaceted issue in which several, often inter-related, factors play a role (Serrano and Carbonari 2012):

- *Individual factors*, such as exposure to violence, substance abuse, and behavioral and psychological disorders (for example, early aggressiveness or hyperactivity)
- *Family factors*, such as harsh parenting styles, a history of family violence, substance abuse in the family, lack of supervision, and neglect
- *School or peer-related factors*, such as peers who engage in violence, unhealthy dating relationships, and an unsafe school environment
- *Community factors*, such as concentrated economic disadvantage, inequality, high turnover of residents, high youth unemployment, high density or rapid urbanization, and low social cohesion and trust
- *Societal factors*, which can be divided into *internal* (such as social norms condoning violence, weak institutions, and a legacy of violence) and *external* (such as the availability of weapons and the influence of organized crime or political violence)

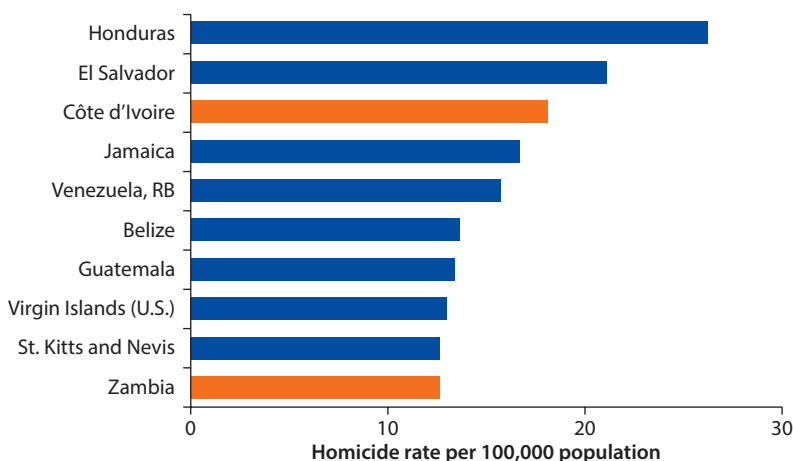
Some factors may even originate outside the state, such as an external economic shock or the infiltration of international drug cartels or foreign fighters (World Bank 2011d, 73). Usually these risk factors are intertwined, and they do not exist in isolation. Their accumulation results in high rates of crime and violence.

Across the Latin American and Caribbean region, the drug trade is a key issue. This takes the form of clashes between criminal networks and security forces, between rival gangs, and between the gang and the local community or city. In Brazil, social inequality is also an important risk factor contributing to violence. In Jamaica, the violence is related to historical patterns of periodic riots and violence dating back to colonial times. In Nepal and Rwanda, political and ethnic conflicts are key sources of violence. Postconflict tension is another source of violence mentioned in the Rwanda case.

Indicators of Crime and Violence

Although homicide rates do not capture the full complexity of crime and violence, they do allow for comparison across countries and over time. In 2010, the United Nations Office on Drugs and Crime (UNODC) estimated that, globally, the total number of annual deaths by homicide was 468,000 (UNODC 2011, 9). The homicide rates in Africa (17 per 100,000) and the Americas (16 per 100,000) were more than double the global average (6.9 per 100,000); the rates in Asia, Europe, and Oceania (3–4 per 100,000) were roughly half the average. Figure 2.1, figure 2.2, and figure 2.3 show, respectively, the countries with the highest homicide rates, the homicide rates in the six country contexts

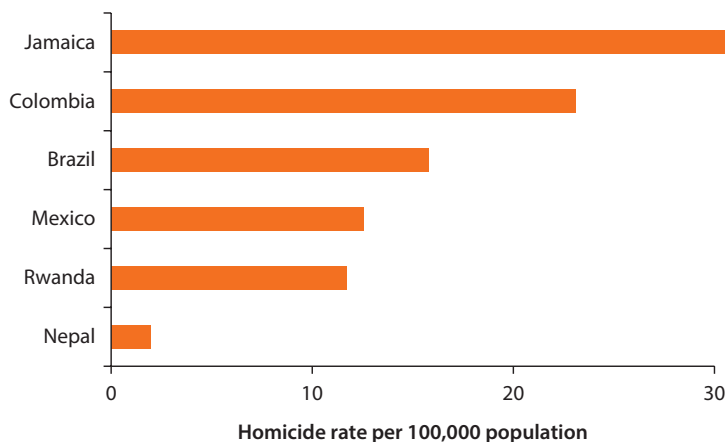
Figure 2.1 Countries with the Highest Homicide Rates



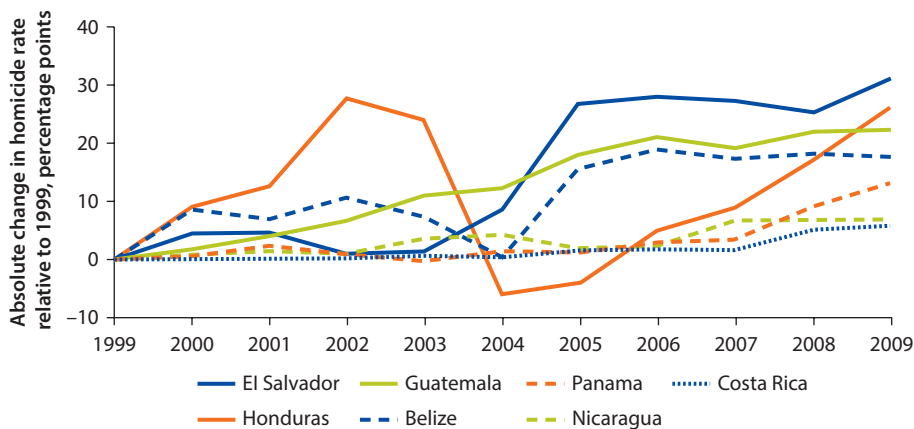
Source: UNODC 2011.

Note: Blue bars represent Latin American and Caribbean countries.

Figure 2.2 Homicide Rates in Case Study Countries



Source: UNODC 2011.

Figure 2.3 Homicide Rate Trends in Central America, Selected Countries, 1999–2009

Sources: World Development Report calculations based on UNODC 2007; UNODC and World Bank 2007; and national sources.

Note: Base year for homicide rate is 1999 = 0.

of the case studies, and trends in Central America. The highest homicide rates were concentrated in the Latin America and Caribbean region, which included 8 of the top 10 countries with the highest homicide rates in the world in 2010, as shown in figure 2.1.

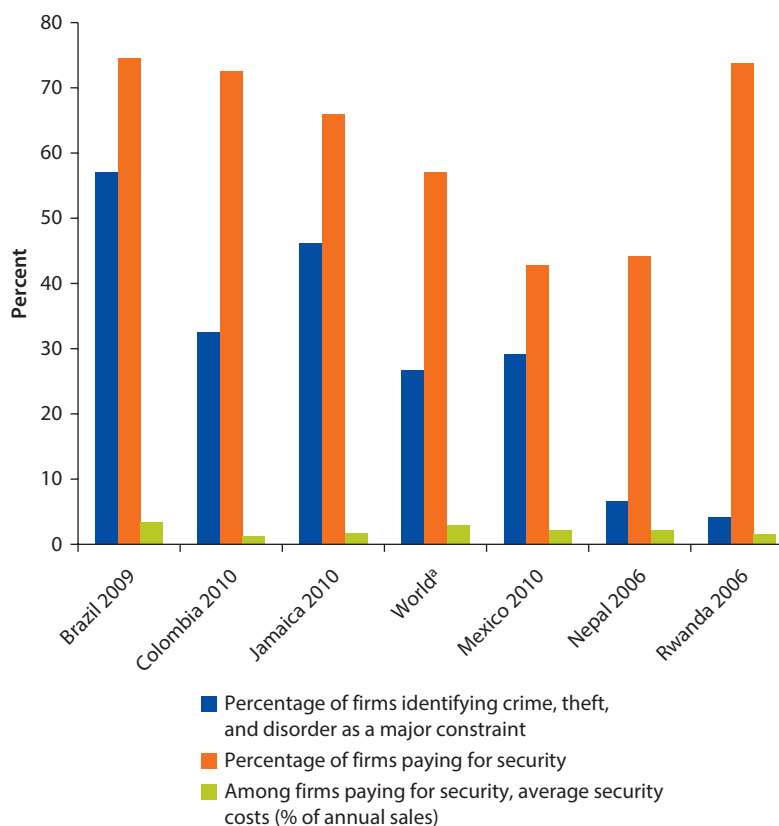
Since 2005, homicide rates in Central America and Mexico have been increasing, with Honduras in particular experiencing rates that more than doubled between 2004 and 2009, as shown in figure 2.3.

What is driving these spikes in crime and violence? The city and country studies for Latin America and the Caribbean corroborate existing Bank and other research that points to at least three drivers of crime and violence in the region: First, Central America is located between the lucrative cocaine consumer market in North America and the main areas of coca cultivation in Bolivia, Colombia, and Peru. Second, the legacies of social unrest and political violence, leading to weak rule of law, have facilitated informal and illicit networks such as cartels. Third, several risk factors for crime and violence have accumulated—such as inequality and social exclusion, as shown by the Rio de Janeiro case.

Comparing the Impacts of Crime and Violence

The economic opportunity costs of crime and violence are high. Figure 2.4 depicts country-level business losses for the city and country cases in this volume, compared with the global average. These losses could have been used to improve basic services (health, education, water, and infrastructure) and lower the poverty rates over time. In Central America, the economic impact can make up nearly a tenth of a country's economy, as in the case of Honduras, at 9.0 percent of gross domestic product (GDP). El Salvador's loss is estimated at 7.7 percent, compared with 5.0 percent in Jamaica and 3.6 percent in Costa Rica

Figure 2.4 Security Constraints and Costs of Doing Business in Case Study Countries Relative to Global Averages



Sources: World Bank 2009, 2010a.

a. World averages come from the most current compilation of World Bank Enterprise Survey data online at <http://www.enterprisesurveys.org/Data/ExploreTopics/crime#World>.

(World Bank 2010b, 2011a, 2011b, 2011c). The costs of protecting the firms from crime and violence elevate these losses even more.

According to the World Bank's Enterprise Surveys in recent years, the global average indicators of business losses due to crime and violence are high, with 57 percent of firms paying for security and 27 percent of firms identifying crime, theft, and disorder as a major constraint (World Bank 2010a).

Among the country contexts described in this paper, Brazil (75 percent), Rwanda (74 percent), and Colombia (73 percent) have the highest percentages of firms paying for security. However, businesses in Colombia and Rwanda also report the lowest costs for security services, as percentages of annual sales. Brazil (75 percent) and Jamaica (46 percent) have the highest percentages of firms identifying crime, theft, and disorder as a major constraint to their ability to conduct business (World Bank 2009, 2010a).

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Coping Mechanisms of Private Firms: Analysis of Global Cases

Overview of Case Studies

The case studies illustrate the diversity of coping mechanisms employed by the private sector, often in cooperation with the public sector and surrounding communities (see table 3.1). The Rio de Janeiro and Medellín cases are significant, for example, because they are frequently cited success stories in fighting urban crime and violence in Latin America. The Rio de Janeiro case exemplifies an approach that uses the police force, jointly with social programs, to counter crime and violence and establish the necessary conditions for private investment. An alternative is the Medellín case, which illustrates a multifaceted and softer approach to violence—pragmatically using both force and inclusive urban development policies—when drug lords are simply too powerful to be confronted primarily by force.

In terms of coping mechanisms, public-private mechanisms (PPMs) are some of the most proactive ways to address high rates of crime and violence. Most of the case studies include examples of PPMs in some form or another. The case studies from Mexico include a “cluster initiative”¹ in Tijuana and public-private forums (PPFs) in Mexico City and Ciudad Juárez. In some cases, the public sector leads such programs (see the Rio de Janeiro pacification programs); in other cases, the private sector takes the lead (see Mexico’s *Tijuana Innovadora*), or the sectors collaborate in a joint public-private program (see Rwanda’s value chain working groups). In sum, firms cope with crime and violence in several ways. Table 3.1 provides an overview of the case studies.

How Crime and Violence Affect Firms

The cases show that crime and violence affect firms in five different ways:

1. *Exclusion from economic activities.* In Colombia and Brazil, criminal gangs used coercion (threats, intimidation) and access to cheap (at times illicit)

Table 3.1 Overview of Case Studies for How Firms Cope with Crime and Violence

| | <i>Colombia (Medellín)</i> | <i>Brazil (Rio de Janeiro)</i> | <i>Jamaica</i> | <i>Mexico (Ciudad Juárez, Mexico City, Tijuana)</i> | <i>Nepal</i> | <i>Rwanda</i> |
|-------------------------------------|---|--|--|---|---|--|
| How crime and violence affect firms | Exclusion, rents, extortion via gang-related business, kidnappings, bombings | Exclusion and extortion through gang-related businesses | Factory shutdowns, loss of business, lower national productivity and investments, brain drain | Extortion fees, kidnappings, theft, assault to logistical providers, blockades | Forced “donations,” extortion, obstructions, strikes | Loss of business and visitors to competitor country (Uganda) |
| Source of violence | Drug trade, political violence (between guerrillas and paramilitaries), breakdown of social order | Drug trade, accumulation of several risk factors such as inequality | Drug trade, legacy of riots dating back to slave trade | Drug trade, accumulation of several risk factors such as inequality | Political (armed conflict, civil unrest, politically motivated disruptions); ethnic (clashes among several ethnic groups); criminal (armed group, mafia violence and extortion) | Postconflict and postgenocide conditions |
| Coping type | PPM, clusters, exit, pay (firm-level security arrangements and extortion fees), joining criminal activities, advocacy | PPM where private sector partly funds public program for security and pacification of violent areas, CSR | PPM to promote a program against crime and violence, pay (security arrangements by individual firms), adaptability of firm-level operations, CSR | PPM in the form of PPFs and cluster initiative (<i>Tijuana Innovadora</i>), arrangements by individual firms, use of social media | <i>Individual firms:</i> exit, relocation, delay of investment, pay (incurring higher protection costs), collusion with violent groups, exploitation of new business opportunities <i>Collective:</i> cost-sharing of security services, lobbying for government action, private sector acting as a mediator, PPD on reforms <i>Hydropower sector:</i> delay in investments, reorientation of the business model, negotiation of protection with local communes | PPM: participatory value chain approaches (working groups) in tourism, coffee, tea, and leather industries |

table continues next page

Table 3.1 Overview of Case Studies for How Firms Cope with Crime and Violence (continued)

| | <i>Colombia (Medellín)</i> | <i>Brazil (Rio de Janeiro)</i> | <i>Jamaica</i> | <i>Mexico (Ciudad Juárez, Mexico City, Tijuana)</i> | <i>Nepal</i> | <i>Rwanda</i> |
|-----------------------|--|---|---|---|--|---|
| Policy implications | Role of participatory approaches, cluster initiatives, lessons from participatory budgeting to procure noncriminal firms | Incentives to attract investments in postviolent areas | Collective actions and cluster initiatives, institutions and implementation issues matter, lessons learned from microfinance programs | Facilitation of cluster initiatives | More systematic data collection on protection arrangements; promotion of economywide, inclusive PPD, bringing together divergent interests | Facilitation of participatory value chain and cluster initiatives |
| World Bank Group role | Facilitation of clustering, implementation arrangements | South-South exchanges (Latin America and the Caribbean, global fragile regions) | n.a. | Facilitation of cluster initiatives, PPDs | Extension of diagnostics to clarify protection arrangements that firms use; facilitation of inclusive, economywide PPD | Facilitation of participatory value chain and cluster initiatives |

Note: CSR = corporate social responsibility; PPD = public-private dialogue; PPF = public-private forum; PPM = public-private mechanism; n.a. = not applicable. *Cluster initiatives* involve geographic concentrations of interconnected companies, specialized suppliers, service providers, and associated institutions in a particular field. The initiatives help identify policy and institutional impediments to competitiveness and can be an effective vehicle for catalyzing reforms.

inputs to become the exclusive provider of services (utilities, cable, and sale of consumer goods) to the local community. This also limits the choices to consumers, forcing them to buy goods and services with less than optimal quality and price.²

2. *Productivity losses.* The cases of Jamaica and Nepal illustrate losses in the form of factory shutdowns (or constraints, such as not operating after dark), which translate into lost outputs and higher costs due to increased security investments and operating costs.
3. *Climate of uncertainty and negative image.* Widespread perceptions of uncertainty and risk created by crime and violence result in an expansion of constraints (less long-term investment), lost revenues to firms (as buyers move away or reduce orders), and less direct investment for the region. For example, during the years immediately following Rwanda's genocidal violence, the country lost significant tourism revenues because most visitors preferred to stay in neighboring Uganda. Tijuana had a similar experience until proactive public-private partnerships reversed the situation.
4. *Supply chain interruptions.* Firms experience lower access to inputs and markets because of blockades and other violent obstructions, affecting the ability of firms to produce, sell, and deliver their products.
5. *Brain drain.* The loss of in-country skill and talent is another negative consequence to firms, and it is particularly critical for a small nation like Jamaica.

Coping Mechanisms

The case studies illustrate different ways in which the private sector copes with situations of crime and violence, including the following Table 3.2 captures a typology of firm coping strategies.

- PPMs
- Participation in the economic system by engaging in the criminal activities
- Additional security spending, factory-hour decreases or shutdowns, and alliances with local communities
- Collective action among firms
- Adaptation of business strategy and operations, including production and markets
- Local corporate social responsibility (corporate social responsibility, or CSR)
- Exit

Colombia: Medellín

The case of Medellín shows that businesses and entrepreneurs coped with the city's persistent crime and violence through a wide range of responses:

- *Exit*, especially by many businesses in violent neighborhoods
- *Perpetration*, with many businesses participating directly in the violence

Table 3.2 Matrix of Firm Strategies to Cope with Crime and Violence

| | <i>Private sector only</i> | <i>Public-private</i> |
|--------------------|--|--|
| Individual firm | <ul style="list-style-type: none"> • Self-defense, including hiring private security firms, installing security systems • Adjustment of business's organization to reduce opportunity for crime, including delay of investment • Relocation | <ul style="list-style-type: none"> • Single firm that gets army protection • Negotiation of protection with local communities |
| Collective (firms) | <ul style="list-style-type: none"> • Advocacy via (a) donations to organizations involved in peacemaking and antiviolence programs, and (b) collective efforts by businesses toward forums and clusters (e.g., Medellín's Chamber of Commerce, Juárez's private sector forum) | <ul style="list-style-type: none"> • Firms that partially fund security and pacification programs (Rio) • Incentives for firms to invest in pacified areas (Rio) • Private sector forum, transformed later into an NGO (Juárez) • Catalyzed value chains |

Note: NGO = nongovernmental organization.

- *Pay*, such as spending to hire private security firms, install security systems, and, in many cases, pay off the criminals
- *Advocacy*, which took two forms: (a) as private donations to peacemaking and antiviolence programs, and (b) as cooperation among some businesses, individual entrepreneurs, and their private foundations to increase the impact of their efforts

To strengthen Medellín's legal economy and to position the city as a national and global economic competitor, business leaders worked with the city government, beginning in the 1990s, to determine the state of the city's economic development, potential competitive advantages, and main challenges, as well as to encourage the use of a "cluster" model. The Medellín Chamber of Commerce played an instrumental role in launching cluster initiatives—in garments, business tourism, information and communication technology, medical and dental services, construction, and power—building a cadre of private sector leadership focused on competitiveness issues. In addition, several chambers of commerce, private sector foundations, and a private university set up a program with the mayor's office to collect and disseminate quality-of-life data in Medellín for planning and assessment purposes.

Medellín's local government played an instrumental role during this period through a multifaceted approach to crime and violence. Mayor Sergio Fajardo adopted an aggressive social outreach program in the neighborhoods where the city government had rarely ventured before. He improved financial transparency to persuade the city's business leaders to pay more taxes, established a participatory budgeting system, and included significant public consultations in the preparation of the city's development plan. The city's participatory policies created a new source of revenue (city contracts) for small businesses in areas experiencing high rates of crime and violence, and gave citizens better access to decisions that affect their lives at the local level (Lamb 2010, 235–36;

Restrepo Mesa 2007). In addition, a network of business support centers (*Centros de Desarrollo Empresarial Zonal*, CEDEZOs) was created throughout the city to provide support and technical advice to microenterprises, and the Banco de las Oportunidades was established to provide low-interest micro-loans. Finally, the increased fiscal collection was used to focus on inclusive social and economic policies.

Brazil: Rio de Janeiro

In Rio de Janeiro, a public-private partnership in the city's shanty towns (*favelas*) focused on win-win solutions in the fight against crime and violence. In 2008, the state government launched the Pacification Police Unit (*Unidade de Polícia Pacificadora*, UPP) program, a law enforcement initiative aimed at reclaiming *favelas* controlled by narco-traffickers and private militias. The UPP program had the political support of federal, state, and municipal governments as well as strong support from the public. The private sector played an important role in financing part of this initiative and, as conditions permitted, in following up with investments that led to job creation, thus contributing to social and economic development in the pacified areas. To encourage investments in former crime-ridden areas of the city, the government provided private sector firms with business incentives (such as tax reductions and cheaper access to land and workers).

Only a few years after the implementation of the UPP program, significant investments have been made in the *favelas*. One of the boldest commitments was from the multinational company Procter & Gamble, which installed a labor-intensive factory in a *favela* after its pacification. The firm received property tax reductions from the municipality. Another successful effort was the *Projeto Comunidade* (Project Community) from Natura, a Brazilian manufacturer and marketer of skin care, cosmetics, perfume, and hair care products. The project was launched in 2011 and is helping to revitalize the local economy in the Complexo do Alemão *favela* after the pacification process. The *Projeto Comunidade* offers noncash credit and skills training to women interested in working as Natura representatives. The credit may be exchanged for Natura products, which then must be sold within 21 days (Koul 2011).

Finally, as part of its CSR efforts, Light S.A., the Brazilian energy company working in the generation, transmission, distribution, and marketing of electricity in Rio de Janeiro, has been running a *favela* cleanup program by encouraging residents to recycle. The company's recycling programs are helping to bring improvements to life in the *favelas* and boosting household wealth by paying for recycled goods.

Jamaica

The case of Jamaica shows that not all industries are affected equally by crime and violence.³ Crime affects security costs the most in tourism, distribution, manufacturing, processing, and entertainment. Firms in challenging environments such as Jamaica respond with a variety of individual and collective coping

responses, including attempts to make the firm less vulnerable to crime, adjusting the organization of business activity to reduce opportunities for crime, and in some cases even striking an accommodation with criminal networks. The most common security measures adopted by individual businesses to protect themselves are protective grills on buildings, special fencing, installed alarm systems, and guards. Small firms tend to install metal grills and to fence the premises; large firms use fences and security guards. Moreover, many firms have adopted adjustments that directly change business activity, such as closing before dark, and that result in the loss of production shifts and reduce the firm's productive capacity.

Among the coping mechanisms by large individual firms, Sandals, one of the largest providers of tourism services in Jamaica, developed a proactive approach based on the concepts of CSR. Sandals created an internship program for groups of at-risk youth, who learn a variety of hospitality industry skills, such as cooking, cleaning, and customer service. This effort is complemented by interventions in one of its neighboring communities, Flankers, such as support for the Flankers Peace & Justice Center, which provides social activities, special programs for women, and mediation services for the community. Sandals also supports literacy and education programs and an animal shelter.

The role of firms in providing information to public security bodies can be illustrated by the Private Sector Organization of Jamaica (PSOJ), a national organization of private sector associations, companies, and individuals. In 1989, the PSOJ established the Crime Stop Partnership, a public-private partnership supporting a network of private firms, communities, the police, and the media. The Partnership enables information sharing and reporting and involves the public in the fight against crime. As of September 2009, the Partnership paid out more than \$185,000 in rewards and had received 18,953 calls leading to 1,942 arrests. The police also recovered property valued at about \$2 million and destroyed narcotics valued at about \$5 million.⁴

Finally, the World Bank–financed Jamaica Inner Cities Basic Services for the Poor Project (ICBSP) focused on the most violent neighborhoods in Kingston and Montego Bay. This experimental public-private microfinance support system targeted high-crime neighborhoods as part of a broader engagement in communities with high levels of violence. The ICBSP was launched in 2006, and its design included an innovative microfinance component to provide access to finance by private microfinance institutions for microbusinesses in the targeted neighborhoods. Unfortunately, the experiment was discontinued at the request of the implementing agency when its board decided that risk credit was not compatible with the mandate of the organization. Although the effects on crime and violence were minimal in this case, the pilot showed that innovative approaches to access to finance for local microbusinesses could be a useful tool in a broader “response toolkit” by the public and private sectors.

Mexico: Ciudad Juárez, Mexico City, Tijuana

In Mexico, cartels competing for the control of a \$35 billion yearly market for cocaine in the United States generated record levels of violence in 2010

(UNODC 2011). The case shows how firms have been adapting to such a context by finding innovative solutions that can be implemented by individual firms, business associations, or entire industry sectors—in partnership with the public sector—by investing in security to protect firms' physical and financial assets and by training employees in crime prevention.

In Tijuana, the private sector responded to a growing wave of crime and violence with cluster initiatives, focusing on the city's key competitive advantages as a way to cope and to drive sustainable growth in the region. Thanks to the entrepreneurial spirit of a local businessman, José Galicot, a widely publicized private sector forum was created (*Tijuana Innovadora, TI*), bringing together global business and media leaders. *TI* evolved later into a dynamic nongovernmental organization (NGO) working on the city's strategic development. More than 700,000 people and 100 international corporations attended a two-week *TI* forum, where local firms showcased their products and attracted investors, talent, and new business opportunities. After such initial gains from the cluster initiative, the government stepped in, helping the forum to evolve into a more permanent public-private organization funded jointly by companies, local business associations, and public authorities at the federal, state, and municipal level.

Other cities in Mexico leveraged PPFs to address crime and violence through private sector participation in information sharing with security forces. In Ciudad Juárez, small and medium enterprises (SMEs) have found web-based social networking to be a tool for coordinating with the federal police, including reporting on criminal activities. In October 2010, local entrepreneur David Alamillo organized the 40 SMEs in a violent Ciudad Juárez neighborhood and partnered with the federal government to cope with the growing wave of crime and violence.

Finally, in Mexico City, the private sector and NGOs have been collaborating to promote greater accountability and voice through PPMs and technology. Local NGOs, SMEs, and large corporations have been developing mobile applications to reduce local police red tape, monitor gangs' operations, and foster accountability to local authorities. As in Ciudad Juárez, developing a direct communication channel with local authorities and following up on crime reports proved to be key elements of success.

Nepal

Nepalese firms have been coping in a variety of ways with political instability, crime, and violence. Individual firm responses include exiting the market, adjusting business practices by incurring higher protection costs, giving in to extortion demands, colluding with violent groups to influence bidding processes, and exploiting new business opportunities. Moreover, firms sometimes cooperate to share the costs of private or public security services or to lobby the government. Business associations have played a mediation role in conflict cases through the network of local chambers of commerce, which continued to operate in areas where the government did not have a presence.⁵

In particular, the hydropower sector has been at the center of much of the conflict, sometimes violent, over access to business opportunities and sharing of

benefits because of the importance of hydropower to Nepalese street-level, inter-party and intraparty, and international politics. Firms have incurred substantial costs because of forced donations, extortion, obstructions, and strikes on a regular basis. Also, construction of hydropower plants was regularly delayed, and operations sometimes had to be stopped. In response to these obstacles to hydropower development, some firms delayed their investment in major infrastructure. Others have reoriented their business model away from the long-term expected returns on electricity generation and toward the ample rent-making opportunities that the major hydropower infrastructure and transportation contracts offer. Still others have tried to establish local protection arrangements with village leaders, especially once substantial investments in the main infrastructure had been made. The success of hydropower firms in establishing workable local arrangements varied across regions, depending on the interests and the wealth opportunities of the local leaders. Also, while the central government proclaimed a hard-line policy against vandals who obstruct much-needed electricity generation, local government authorities actively supported, facilitated, or left room for nonstate arrangements between hydropower companies and local communities.⁶

Rwanda

The case of Rwanda shows how the private sector responded to the looming postconflict violence when the country had just survived violent genocide. Under the leadership of President Paul Kagame, growth was restarted through a shared vision for the future and novel PPMs. The case highlights the role of “value chain working groups,” initially focusing on three key industries: coffee, tea, and tourism. All three industry value chains employed a common approach around a participatory leadership by the private sector with active government involvement. In particular, the Tourism Working Group (TWG) was initially funded by the government but enabled the private sector to take ownership and leadership. The TWG was intended to encourage leadership by the private sector that was inclusive, reflecting the wide range of value chain actors and firms of different sizes. The inclusion of SMEs was particularly important in an environment of impending violence and conflict.

Moreover, the TWG made an explicit decision to focus on high value versus mass tourism. Although quick wins were critical to help build momentum, the TWG worked for months to come up with a comprehensive industry action plan to serve as a shared road map for both the public and private sectors. Strengthening cooperation and institutions was particularly important in post-conflict Rwanda. A major hallmark of the TWG has been its investment of time and effort to institutionalize the value chain working groups to address structural coordination issues and lack of trust.

The government was instrumental in kick-starting the national competitiveness program and the TWG. Government representatives participated in the working groups and provided real-time feedback and actions as discussions took place. One of the most important policy changes has been

institutional: the World Bank's Africa Finance and Private Sector Development (FPD) Department played a critical initial role by strengthening the Tourism Board and the Rwandan Investment Promotion Agency while increasing the responsibility of the private sector. The TWG became the *de facto* mediator between these and other value chain actors. Moreover, the TWG helped all parties to better understand the constraints facing businesses (particularly small ones), helping Rwanda become one of the star cases in the World Bank's Doing Business reforms. The TWG also approved the creation of commercial courts in 2006, the lack of which had been a major source of constraint facing the private sector. Other reforms took place either as inputs from the working groups or in parallel to them. These included improving access to finance for local tour operators and transportation companies by shifting from collateral-based lending to more flexible criteria, including two leasing windows with the support of FPD and the World Bank Group's International Finance Corporation.

Analysis and Lessons Learned

These cases reveal the different forms of PPMs that can be used in response to crime and violence. Although public sector leadership played a decisive role in Colombia and Rwanda, in the other cases the leadership for the initiative came from the private sector. In all countries, the cases highlight the importance of leadership in crime-ridden and violent environments, specifically the capacity of a champion to mobilize different actors toward a common agenda. PPFs were used for this purpose in Rio de Janeiro (Brazil); Medellín (Colombia); and Ciudad Juárez, Mexico City, and Tijuana (Mexico). In Rio de Janeiro, PPFs collaborated with and occasionally helped fund the pacification program. In Mexico, PPFs contributed to a greater inclusion of SMEs in violence-reduction programs involving the government and large companies. In Tijuana, the "innovation clusters" leveraged their geographical competitive advantage—proximity to California's technology-driven corporations such as in Silicon Valley—to dramatically turn around high homicide rates and declining investments. Cluster initiatives in Medellín also employed that city's competitive advantage in a no less significant manner (although the decline of homicide rates is not directly attributable to these efforts, as was the case in Tijuana). Finally, the case of Nepal shows how firms can adapt in violent environments through a wide range of responses, including a PPF (the Nepal Business Forum).

In addition to PPMs, the case studies often cited individual firm responses. The studies illustrate the enormous creativity of firms in coping with difficult circumstances. The first decision is whether to exit the area or the business altogether, or to invest time and resources in one or more coping mechanisms. When firms try to adapt to the circumstances, there is a price to be paid. Their security costs may rise. They may also reorient their business model or delay investments. Large firms can also respond through CSR programs that address local needs while also meeting market and shareholder demand. One example is the program to train and employ local women to sell cosmetic products

in Brazil's slums. More often, CSR programs encourage the private sector to assume some public sector functions, such as funding security (Brazil) or youth employment programs (Jamaica).

Overall, some key lessons emerge from these cases:

- *The transformative impact of collective actions by firms.* The cases show that collective actions by firms can be a powerful response mechanism, whether in the form of PPFs, firm-to-firm actions to pool resources, cluster or value chain initiatives, or information-sharing with security forces. Collective actions benefit not only small firms, which often cannot afford the extra costs, but also bigger firms that benefit from an improved business environment and supply chain efficiencies. That said, the cases point to the importance of supporting SMEs in environments of high crime and violence.
- *The importance of leadership.* Critical leadership comes from both the public and private sectors, as the cases of Mexico (private sector leadership), Colombia (public-private), and Rwanda (mainly by the president) show. All the cases show the presence of a champion that facilitated major responses to situations of crime and violence. The challenge is to identify the champion(s) and provide effective support.
- *The public sector's role in enabling successful private sector responses to crime and violence.* In particular, a multifaceted approach by the public sector proved particularly important in Medellín and Rio de Janeiro, where tax and other incentives as well as promotional campaigns attracted investments in violent or formerly violent areas. Moreover, public sector involvement enables the implementation of longer-lasting solutions—for example, by institutionalizing private initiatives as in the case of TI.
- *The importance of quick wins and building trust.* It is important to have quick wins and concrete examples of the possibility and the efficacy of fighting the effects of crime and violence on firms' activities, as the cases of Mexico and Rwanda show. Early demonstration effects can come from forming and implementing a joint plan, such as for a branding campaign. In addition, the public sector needs to take the time to build the necessary trust in the communities affected by crime and violence. A relationship based on trust encourages communities to adopt and fight for valuable solutions that encourage investments.
- *The importance of communication.* The cases showcased examples of how communications strategies can change how potential visitors and investors perceive a country or a city (Rwanda through familiarization tours, and Tijuana through its TI public relations campaign). They also show how communications campaigns can help build momentum in support of progress and enhance opportunities to build social consensus around the changes.

- *The importance of listening to entrepreneurs.* Their knowledge, ingenuity, urgency, and flexibility show how individual firms adapt their operations and markets in the face of crime and violence, as the case of Jamaica proves. The challenge is to capture this information in the context of its environment and institutions; prioritize “best fit” interventions; and tailor a process that would help strengthen the private sector ecosystem, including connections with the regional and global supply chains, as the cases of Brazil, Colombia, and Mexico have shown.

Policy Implications

Although no single model best supports the private sector in all crime-plagued and violent environments, these cases point to some emerging policy implications.

An Integrated Approach

First, supporting private sector responses should be part of an integrated approach with the public sector to reduce crime and violence. The Medellín case best exemplifies this, where continuous experimentation persisted despite mistakes and fierce responses by the drug lords. When drug lords became too powerful, the public sector employed community participatory budgeting and encouraged the forming of civic associations, which allowed procurement of goods and services outside the criminal network. The private sector—led by the Medellín Chamber of Commerce—was equally persistent, as exemplified by its proactive role through cluster projects. This enabled the participation of SMEs and large firms, attracted investment, and encouraged public-private dialogue on sustaining competitiveness in difficult environments. Brazil also employed an integrated approach, although with a clearer reliance on force than in Colombia. Rio de Janeiro’s pacification units enabled enough stability for private investments to come in (whereas in the Colombia case, violence, competitiveness, and enterprise adaptability coexisted in a more nuanced manner). PPFs were widely employed in Ciudad Juárez, Mexico City, and Tijuana, requiring an integrated mix of security, rule of law, “voice” and accountability mechanisms (including use of social media), and community and private sector development.

Public-Private Forums

Second, some type of PPF was cited in all the cases. Understanding the nuances of PPFs and finding opportunities to support such initiatives in environments with high rates of crime and violence remain an open policy agenda. In particular, participatory value chain approaches (or clusters) remain a promising public-private instrument to be further examined in situations of violence. In Medellín, clusters have helped a considerable number of firms to cope and even thrive, even when violence did not seem to go away. In Tijuana, cluster initiatives (*TI*) were instrumental in transforming a place of high crime and violence into a highly competitive and innovative region. Moving forward, this report finds that it would be important to understand the policy challenges and opportunities of

value chain and cluster initiatives for building PPFs in other environments of high crime and violence by leveraging different regions' unique competitive advantages and endowments.

Small and Medium Enterprises

Third, SMEs remain particularly vulnerable to crime and violence, yet they also represent the most promising gains from policy interventions. In a deteriorating business climate, SMEs remain exposed to such constraints as theft, extortion, productivity losses, expansion constraints, and loss of revenues because of coordination failures, lack of access to finance, and supply chain interruptions. Although violence is costly to all firms, SMEs incur a disproportionately high burden and are less equipped to cope with the impacts of crime and violence. In Jamaica, for example, small firms spend 17.0 percent of revenues on security, compared with 0.7 percent by large firms. As the case of Ciudad Juárez illustrates, SMEs benefit from programs that reduce or eliminate these constraints, so they are eager to participate in public and public-private initiatives—such as PPFs, collective action, value chains or clusters, microfinance, matching grants, participatory value chain initiatives, and infrastructure and energy projects.

The World Bank Group

The cases and secondary research presented in this report point to specific areas of action for the World Bank Group. In addition, the *World Development Report 2011* provides important recommendations for work in fragile, conflict-affected, and violent environments (World Bank 2011b). They include increasing cross-sectoral identification of new investment opportunities, encouraging South-South exchanges, and adapting existing Bank practices to high-crime and violent environments (along with internal operating mandates required to carry them out). The recommendations also include recalibrating tolerance for risk across Bank teams and moving beyond traditional approaches (see chapter 5).

Notes

1. Cluster initiatives center on geographic concentrations of interconnected companies, specialized suppliers, service providers, and associated institutions in a particular field. The initiatives help identify policy and institutional impediments to competitiveness and can be an effective vehicle for catalyzing reforms. Clusters can be organically grown (for example, software in Silicon Valley and the Arizona optics cluster) or induced through a catalytic public sector role (for example, tourism in Rwanda and Sri Lanka) (Shakya *et al.* 2009).
2. Robert D. Lamb of the Center for Strategic and International Studies points to the persistence of economic motivations behind the rebel and gang networks. After eliminating ideology and other factors, the underlying motivation for violence is to gain economic advantages (Lamb 2010).
3. The varying effects were shown, for example, by World Bank focus groups held in April 2010 with small and medium-size firms in the food processing and tourism industries (World Bank 2011a).

4. The original data are in Jamaican dollars. They were converted at the exchange rate of March 28, 2012.
5. Interview with representative of the Federation of Nepalese Chambers of Commerce and Industry, Kathmandu, Nepal, February 25, 2011.
6. Interview with businessman, Kathmandu, Nepal, April 28, 2011.

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World Bank Group Work: From Policies and Research to Operational Initiatives

Growing Focus on Crime and Violence

This chapter provides an overview of the World Bank Group's (WBG) experience on the topic of crime and violence. It is based on (a) a review of recent World Bank country assistance strategies (CASs) and country partnership strategies (CPSs); (b) interviews with key Bank teams on this topic (regional and sectoral);¹ and (c) a review of recent Bank publications.

There has been little systematic research on the potential and actual role of international development agencies in support of firms and public-private mechanisms in environments with high rates of crime and violence. Nevertheless, available recent World Bank CASs and CPSs for countries in Latin America and the Caribbean indicate significant interest in the topic. Table 4.1 lists the latest CASs and CPSs highlighting crime and violence in that region.

Private Sector Development (PSD) Initiatives

Despite this growing interest and the impact of crime and violence on businesses and the economy,² the CASs, CPSs, and other World Bank studies lack a strong private sector perspective. Notable exceptions include studies and projects that address the following:

- *Trade logistics.* This is one of the few active thematic groups within the Bank that has touched on private sector responses to crime and insecurity and their relationship to transport and cargo security. Several analytical activities and discussions linking the impact of crime and violence to transportation, logistics, border and customs, and supply chains include firm responses to crime and violence and environmental regulatory issues. Preliminary results of cargo security studies include analytical pieces on trucks in high-crime corridors

Table 4.1 Recent World Bank CASs and CPSs Addressing Crime and Violence in Latin America and the Caribbean

| <i>Country</i> | <i>CAS or CPS mentions crime and violence as significant</i> | <i>Private sector engagement is emphasized</i> |
|--------------------------------|--|--|
| Colombia CPS FY12–16 | X | |
| Costa Rica CPS FY12–15 | X | |
| Dominican Republic CPS FY10–13 | X | |
| El Salvador CPS FY10–12 | X | |
| Guatemala CPS FY09–12 | X | |
| Haiti CAS ISN FY12 | X | |
| Honduras CPS FY12–14 | X | X |
| Jamaica CPS FY10–13 | X | X |
| Mexico CPS FY08–13 | X | |
| Panama CPS FY11–14 | X | |

Note: CAS = country assistance strategy; CPS = country partnership strategy.

(not well documented in most logistics and trade economic and sector work [ESW]), such as the effectiveness of convoys of trucks relative to individual trucks.³

- *Urban upgrading projects.* These projects often include specific interventions that combine urban renewal with a citizen security focus at the local and community level to prevent crime and violence. Examples of such projects are the Jamaica Inner Cities Basic Services for the Poor Project (ICBSP) and the Barrio-Ciudad Project in Honduras.
- *Local public-private partnerships (LPPPs) for citizen security.* Jointly produced by the International Center for Crime Prevention and the Bogotá Chamber of Commerce, this initiative provides a guide on LPPPs for private sector associations (ICPC, Bogotá Chamber of Commerce, and World Bank 2011). This approach was piloted in Honduras and Brazil and involved associations from both countries. In addition, the Bank has partnered with INCAE Business School in Costa Rica and the Council of Americas to establish national and regional dialogues on public-private partnerships in Central America.
- *Investment climate interventions.* These projects use public-private dialogue (PPD) mechanisms, as discussed in box 4.1, to better tailor reforms needed to generate new investments and jobs to the needs of the client countries.

Non-PSD Initiatives

Among non-PSD initiatives, the Bank has supported and financed the following:

- *Institutional reform.* The First Programmatic Reducing Vulnerabilities for Growth Development Policy Credit (DPC) for Honduras in the amount of \$86 million is an example of this type of initiative. This credit's development

Box 4.1 Public-Private Dialogue in Investment Climate Interventions

Public-private dialogue (PPD) has proven to be an important mechanism in World Bank interventions to improve national and regional investment climates in client countries. In particular, PPD provides a mechanism between the private sector and political parties in government to encourage a national discussion focused on reforms needed to generate new investments and jobs.

The monitoring and evaluation (M&E) review of 30 World Bank Group (WBG)-sponsored PPDs undertaken in 2009 found that PPD has been an effective instrument of choice to prioritize and promote reforms in International Development Association (IDA) and postconflict countries, both top WBG priorities (Herzberg and Toland 2009, 5).

A further review of investment climate programs in 16 countries was undertaken in June 2011 to catalogue and assess alternative approaches to investment climate and private sector development in fragile and conflict-affected states (Harwit 2011, 7–8). The review finds that the interventions succeeded in implementing the WBG's investment climate projects, based on the necessity for "quick wins" and reaching important results established at the project design stage. According to lessons learned and staff interviews, quick wins with regulatory reforms are important both for the client government to restore confidence to country constituents and for the WBG team to establish credibility and win support for follow-on work in the future. Across all country groups, a PPD has worked well as an entry strategy program to discuss regulatory reforms in progress and to create dialogue on additional reforms and has been essential to the reforms' success.

Also, a postcompletion evaluation of the Nepal Business Forum Phase I undertaken by the WBG's Independent Evaluation Group (IEG) further confirms the usefulness of PPD in a conflict-affected state (World Bank 2011b, 4). The IEG found the objective of promoting PPD around private sector reforms to be appropriate in the context of a country struggling to establish democracy, and the PPD objectives under this project have been broadly met. In addition, as of August 2012, during the second phase of this project, more than 41 recommendations out of 120 coming out of the PPD had been implemented, including two reforms that have delivered \$5.67 million in private sector cost savings, notably in an environment of significant political turmoil that formerly had little public-private or even private-private dialogue.

Source: Nepal Investment Climate Reform Program, International Finance Corporation.

objective is to assist the government in strengthening the fiscal management, institutional mechanisms, and programs needed for an integrated violence prevention strategy. The Honduras DPC-supported initiative supports four areas that are central to the reform program: (a) tax administration, focused on improving taxpayer compliance; (b) civil service reform, focused on the rationalization of the public wage bill by delinking teachers' salary adjustments from those reflected in the private sector's minimum wage; (c) pension reform, designed to lessen contingent fiscal vulnerabilities by reducing the public pension institutions' actuarial deficits; and (d) citizen security reform, focused on

strengthening institutional coordination mechanisms and programs needed for an integrated violence prevention strategy.

- *Specific thematic lending.* The overall citizen security agenda of the World Bank (the agenda in Latin America and the Caribbean, in particular) has been growing around a package of services that include lending operations and knowledge and advisory services. For example, the Specific Investment Loan on Citizen Security in Honduras is the first World Bank investment loan entirely focused on citizen security.
- *Mainstreaming crime and violence into sectoral operations.* For example, the Rio de Janeiro Metropolitan Development Policy Loan (DPL) and the Municipal Technical Assistance Loan (TAL) incorporate crime and violence components in their urban upgrading programs. The Sierra Leone Youth Employment Support Program provides interventions for early childhood development and targets the poorest families and at-risk youth.
- *Technical assistance.* These initiatives can include studies, surveys, and observatories to diagnose and analyze the drivers, evolution, and effects of crime and violence over time, as well as prevention approaches (see, for example, World Bank 2011a, 2011c).
- *The Stolen Asset Recovery Initiative (StAR).* A partnership between the WBG and the United Nations Office on Drugs and Crime, StAR supports international efforts to end safe havens for corrupt funds. In particular, StAR prevents the laundering of the proceeds of corruption and facilitates more systematic and timely return of stolen assets. Although StAR is not directly linked to coping mechanisms of firms, it is one of the few analytical initiatives within the Bank that can be helpful in designing future initiatives for this purpose (for example, to address reputational risks in Bank-supported initiatives involving the private sector in the global supply chain).

Notes

1. The community of practice point persons for this topic include Jordan Schwartz (Trade and Logistics Product Lead and Global Team Lead on Trade and Facilitation), Jean Denis Pesme (Stolen Asset Recovery Initiative), Rodrigo Serrano (Latin America and the Caribbean Social Development crime and violence contact point), and Javier Posas (International Finance Corporation Honduras).
2. In Central America, the costs of crime and violence are estimated at close to 8.0 percent of regional gross domestic product (World Bank 2011a).
3. The truck convoy effectiveness analysis is in progress. The study is led by Gwyn Fries (Latin America and the Caribbean Sustainable Development Network). See also the Trucking Industry Survey for most of Central America led by Daniel Saslavsky (Poverty Reduction and Economic Management Network) and Gonzalo Ayala (Latin America and the Caribbean Sustainable Development Network) (World Bank 2012).

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World Bank Group Support for Private Sector Development in Environments of Crime and Violence

Opportunities for Support

This initial research effort confirms the existence of a rich body of case studies from all over the world on the private sector's varied responses to situations of crime and violence. The examples in this study showcase opportunities for policy makers and World Bank teams to facilitate practical support to the private sector in growing crime- and violence-prone environments—support such as investments, exchanges, pilots, and adapting existing Bank practices to these environments. Such opportunities raise the question: “Is the World Bank equipped to deliver innovative and effective private sector development (PSD) responses in countries and sectors facing high crime and violence?” In other words, can Bank teams even start engaging on these topics internally and obtain a sufficient operational mandate to make progress?

The question of whether the Bank should be involved in the gray areas of security and development—in particular, in the frontier topic of PSD—is not a trivial one. The Bank and its counterparts have already made some progress in addressing crime and violence, but, as the 2011 *World Development Report* has pointed out, traditional approaches will not be sufficient to advance the agenda on fragile, conflict-affected, and violent situations (World Bank 2011). For example, tolerance for risk in Bank operations needs to be recalibrated in situations of high crime and violence. The implications for Bank operations from country cases, past Bank operations, regional dimensions, and other questions for further research are discussed below.

The case studies have introduced a wide range of coping mechanisms that could be the basis for a systematic approach by the World Bank Group (WBG) (coordinating the complementary instruments of the Bank, the International

Finance Corporation [IFC], and the Multilateral Investment Guarantee Agency [MIGA]) as well as other interested donors, leading think tanks, the private sector, civil society, and ministries. With so many stakeholders affected and involved, this is not an agenda the Bank can advance in an isolated way.

Moving the Agenda Forward

Six practical suggestions to move this agenda forward can be drawn from the case studies:

1. *Identify new investment opportunities by building on the growing demand from client countries.* This can be advanced through the growing demand, thematic visibility, and interest within client countries and among Bank staff on this topic. For example, country assistance strategy (CAS) and country partnership strategy (CPS) could address crime and violence, not just as context but also as part of both the strategic response and the operations design, incorporating the lessons learned and best practice experiences. Also, according to country priorities and context, investments can be either stand-alone projects or part of a multisector strategy in collaboration with other WBG teams. Consultations for new investments can be facilitated by kick-starting or supporting existing public-private forums (see below) and other local initiatives. Pilot projects to increase the private sector's resilience to crime and violence include lighting of public areas (the IFC is currently examining this); a range of PSD tools within slum upgrading programs such as microfinance, matching grants, and business support services (which could also be integrated with, for example, Bolivia's *Barrios de Verdad* model); and corporate social responsibility initiatives. Investments can also build on the approach of the recent Honduras development policy loan (DPL) and adapting the Bank's Doing Business reform efforts to include crime and violence explicitly.
2. *Adapt existing Bank project-level technical interventions.* The cases point to PSD mechanisms with some established practices within the WBG. For example, much of the work on participatory value chains and clusters in the WBG is being coordinated by the Competitive Industries practice within the Finance and Private Sector Development (FPD) Network. FPD, along with the Center on Conflict, Security, and Development (CCSD) and other Bank teams, can play an important coordinating role in adapting assessment, design, implementation, and monitoring and evaluation tools to high-crime and violent environments. Tools specific to small and medium enterprises, such as microfinance and matching grants, exist in robust forms across FPD. In particular, the Bank should move toward facilitating the implementation of public-private mechanisms and quick wins and solutions that help build trust among the different actors involved. Public-private forums could also benefit from the public-private dialogue (PPD) thematic area currently housed in the World Bank Institute and other public-private initiatives across the Bank Group (see ICPC, Bogotá Chamber of Commerce, and World Bank 2011). Finally, Bank projects

cannot fund security forces but can coordinate with security improvements in government and donor programs and can build capacity.

3. *Strengthen coordination among existing thematic groups.* This includes greater coordination among FPD; the IFC; the Sustainable Development Network (SDN) (such as the Trade Facilitation Thematic Group, SDN's crime and violence urban thematic group); the Financial Market Integrity Group; and IFC Central America, which has a growing interest in both investment and advisory services in this area. CCSD and FPD can help kick-start and start facilitating some of these coordination activities, including through its new knowledge platform.¹ This platform includes common interests across different practices, such as public-private forums. In particular, unit-specific themes and cross-collaboration opportunities involve the following:
 - *IFC investment operations and advisory services.*² A thematic group has been formed that involves IFC investments and advisory services related to the growing crime and violence trends in Central America.
 - *SDN Trade Facilitation Global Expert Team, Crime and Violence Urban Thematic Group.* Concrete examples of joint work include the development of toolkits on private sector responses to crime and violence, to be designed and tested during joint missions with Latin America and the Caribbean SDN and FPD.³
 - *FPD Global Practices (Competitive Industries).* Operational mechanisms emerging from the Mexico and Rwanda case studies can be developed to address the rich variety of coping mechanisms—such as cluster and competitiveness initiatives and PPD mechanisms—in proactively supporting the private sector in responding to situations of crime and violence. Because of the high reputational risk, such an exercise should support internal decisions on when the Bank should not intervene at all.
4. *Contribute to existing initiatives and strengthen coordination with external, new, and nontraditional stakeholders and partners.* In particular, the Bank could support existing initiatives and promote the coordination of its future activities with traditional and nontraditional external stakeholders and partners. The Bank has already undertaken coordination efforts and initiatives in crime-ridden and violent environments but not directly in the PSD area, pointing to new areas and possibilities for future work. Indeed, the experiences of the World Bank and other donors show that the focus of most of the projects and activities against crime and violence have included the private sector only marginally, even as the World Bank Enterprise Surveys describe crime as one of the main constraints to productivity and growth (World Bank 2010). Moreover, there is little secondary research on the roles played by the private sector in crime prevention.⁴ Increased information sharing and exchange, as well as further research within and across countries, would help to better inform discussion and debate in this area.
5. *Coordinate and disseminate knowledge.* The Bank could continue to coordinate the generation of knowledge about private sector responses to crime and violence. One of the most practical implications emerging from the cases is

the value of South-South learning around this topic. The many ideas, lessons, and ongoing challenges outlined in the cases illustrate the potential opportunities in such exchanges. The Bank could not only coordinate and encourage existing regional dialogues (Brazil and Colombia) but also help provide a more robust global perspective. For example, Brazil's pacification units and Colombia's integrated experiences can also be informative for African and South Asian countries facing armed conflict, and all could benefit from greater exchanges on the topic. By serving as a custodian of quality and relevance, the Bank could develop a more systematic approach in facilitating such exchanges. It could commission additional case studies and establish a coordination mechanism to gather, communicate, and establish knowledge links among client countries and the donor community.

6. *Support sources of statistics on crime and violence.* This effort would aim to (a) collect primary data that can provide firm-level information about how crime and violence affects firms and their coping strategies; (b) inform policies, interventions, and programs; and (c) help build momentum by showcasing progress and results of pilot projects and other interventions. The Bank could support and work with existing "violence observatories" to bring in the perspective of the private sector, improve the quality of data collected, and standardize the indicators across countries. In addition, the Bank could strengthen the accountability mechanisms so that academia, civil society, and the private sector can provide oversight of the information generated by the public sector. In particular, the case of Medellín shows how independent statistics on crime and violence replaced politically motivated reporting. The United Nations Office on Drugs and Crime and the World Bank's Enterprise Surveys could contribute to this kind of transparency. The Bank's Development Impact Evaluation Initiative (DIME) team (specializing in monitoring and evaluation) and the Development Economics Vice Presidency could both play a role in this work.

Operational and Research Issues

The case studies described in this report point to a number of areas for future research. As with many research projects, the emerging questions outnumber those initially posed. To begin, further research should seek to identify the key indicators that measure the relationship between crime and violence and the private sector.

At the level of the client country or city, are there other effective coping mechanisms not identified in this report? If so, additional research should seek to identify the best illustrative cases and describe the most effective strategies. The researchers will also need to ask which strategies the WBG can support and which strategies it cannot.

At the level of the local government and local private sector, do some prerequisite social or political circumstances facilitate the private sector coping mechanisms? If so, can a taxonomy of public-private structure and approaches be developed? The answer to these questions may depend, for example, on which

actors are in the lead (large versus small firms, associations versus public-private forums, national versus local authorities) and which element has the greatest weight (legitimacy, force, or perceptions).

At the operational level, how can the WBG best provide its clients with its extraordinary lending, technical assistance, and convening capacity to encourage cooperative exercises of knowledge sharing? The Bank Group's goal should be to marshal these products and capacities to address the needs of the private sector, the public sector, and civil society. In addition, the goal should be to strengthen public-private mechanisms by enhancing trust between the public and private sectors. That said, however, there are internal constraints and policies that limit the Bank's effectiveness in responding quickly to client demands—and these issues should be resolved.

Notes

1. "theHive" is a knowledge-sharing platform designed to connect practitioners, researchers, policy makers, and organizations working on issues of fragility, conflict, and violence around the world. For more information, see http://www1.worldbank.org/operations/hive/WhattheHive_loop_final.html.
2. IFC Honduras is putting together a thematic group on this topic, including public-private dialogue (PPD) and forums, investments in firms providing lighting in urban areas, and security audits advisory services.
3. An economic and sector work budget to develop a toolkit for Central America is under internal review.
4. Many different terms are used throughout the world to describe private sector involvement, such as public-private partnerships, business and nongovernmental organization engagement, social partnering, and corporate social responsibility.

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Case Studies

Case 1: Medellín, Colombia—How the Public and Private Sectors Have Coped with Violence

By Robert D. Lamb

Nestled in a highland valley in Colombia's coffee-growing region, Medellín is a city of 2.3 million people who have dubbed their home the City of Eternal Spring, in reference to the springtime climate they enjoy year-round (with an average temperature of about 22°C). During most of the 20th century, Medellín, capital of the department of Antioquia, was known as a powerhouse in textiles and small industry and as a leader in urban planning. Factories offered middle-class wages and fringe benefits, and the conservative culture of the region emphasized a strong work ethic and loyalty to the factories' owners and other authority figures. Business leaders periodically worked with the government to develop long-term visions for the city's development. One consequence was that, while Colombia's civil war—known simply as *La Violencia* (the violence), fought between Liberals and Conservatives during the 1940s and 1950s—devastated much of the country, Medellín was largely untouched. The city's industrialists consciously kept politics out of the workplace to keep Liberal-Conservative tensions to a minimum. The city's economy continued to thrive as a result.¹

During the 1960s, however, as Asian manufacturers began offering inexpensive textiles and other products on the world market—and in Colombia itself—Medellín's factories suffered a reduction in demand for their products globally and domestically, and, as in most of Colombia, Medellín went through a major period of consolidation in which many small and medium enterprises (SMEs) were acquired or forced out of business by large conglomerates. Meanwhile, between the mid-1950s and the early 1970s, the city's population almost tripled, partly due to migration by coffee farmers facing a global rise in competition and decline in prices. The city's urban planners could not keep up with the population explosion. The manufacturing sector was damaged; the labor glut depressed wages; unemployment skyrocketed; and the poor, unable to afford

housing, built shantytowns on the city's mountainside periphery, where many died in the mudslides that are a common feature of Medellín's geology.

The rest of the history is well known. The breakdown of social order, the explosion of poverty, and the high concentration of so many unemployed people without public services or legal recognition created a population desperate for resources and respect. These were found in smuggling—at first, stolen goods (cars, household electronics, cigarettes), then narcotics. As narcotics smuggling became big business and the demand for illicit enforcement of verbal agreements grew, a new labor category emerged in the city: assassin. (The drive-by assassination, with a driver and a shooter on a moving motorcycle, was invented in Medellín.) By the late 1980s, more than 100 of Medellín's street gangs had gone into the business, joining the more-established organized criminals who killed for money. By some estimates, 3,000 people (with a median age of 16) were employed in this labor category, hired to murder cheating lovers, political opponents, union organizers, business competitors, deal breakers, rival gang leaders, and anyone else targeted by somebody with a grudge and money to spend. Most important, however, they acted as the enforcers for Medellín's major drug smugglers, the most notorious of whom was a former cigarette and marijuana smuggler named Pablo Escobar.

There is no need here to go into the history of Medellín's role in the narcotics trade. It suffices to say that Escobar became so wealthy from creating cocaine smuggling networks and franchises and collecting a cut on the illicit trade that at one point he offered to pay off Colombia's national debt in exchange for amnesty. The offer was rejected—but he did, in fact, have enough money to make good on the offer. Escobar was killed by the police in 1993, but his legacy of violence continued for another decade (Clawson and Lee 1996; Gugliotta and Leen 1989; assassin gang figures from Salazar 1991).

The drug trade and the associated market for assassinations were not the only contributors to the violence that emerged in the city. Unlike the era of *La Violencia*, the rise of Colombia's leftist insurgency did not leave Medellín untouched. The war, waged initially by leftists who had been left out of the power-sharing agreement that ended the civil war in 1958, displaced tens of thousands of people from the countryside, contributing to Colombia's urbanization and Medellín's growing population. It also sparked a right-wing backlash as anticommunists and former victims of the insurgents formed paramilitary units, often backed informally by state agents, to attack leftist guerrillas and sympathizers. During the 1990s, both insurgents and paramilitaries entered the trade in narcotics to fund their operations, and they fought each other for control over territory within Medellín as well.

A final source of violence came in response to the breakdown in social order. As life became dangerous, many communities formed self-defense groups, many young people joined gangs, and some community members engaged in "social cleansing" of drug dealers, street children, prostitutes, homosexuals, and others they considered deviant or dangerous. Amid the chaos, common crime exploded (table 6.1).

Table 6.1 Medellín, Colombia: Summary of Key Crime and Violence Indicators and Coping Mechanisms

| <i>Indicators</i> | <i>Results</i> | <i>Data (%)</i> |
|---|---|------------------|
| Cost to business (Holmes, Gutiérrez de Piñeres, and Curtin 2008; World Bank Enterprise Survey 2010) | Loss to GDP (Colombia) | 6.3% (1998 data) |
| | Firms paying for security | 65.2% |
| | Firms identifying crime, theft, and disorder as a major constraint | 7.5% |
| Homicide rate (Felbab-Brown 2011) | 100 per 100,000 population (2009 data) | |
| Identified in CAS or CPS as a major issue | Yes, CPS 2012–16 (World Bank 2011b) | |
| Transparency International Corruption Perceptions Index rank (TI 2011) | 80 of 182 (Colombia) | |
| Private sector coping mechanisms | Exit | |
| | Direct participation in the local violence | |
| | Self-defense, with businesses taking measures such as hiring private security firms, installing security systems, and often paying off the criminals who had extorted them | |
| | Advocacy, including (a) private donations to organizations involved in peacemaking and antiviolenence programs; (b) collective efforts by businesses and Medellín's Chamber of Commerce, directly contributing to the city's social inclusion policies; and (c) public-private partnerships | |

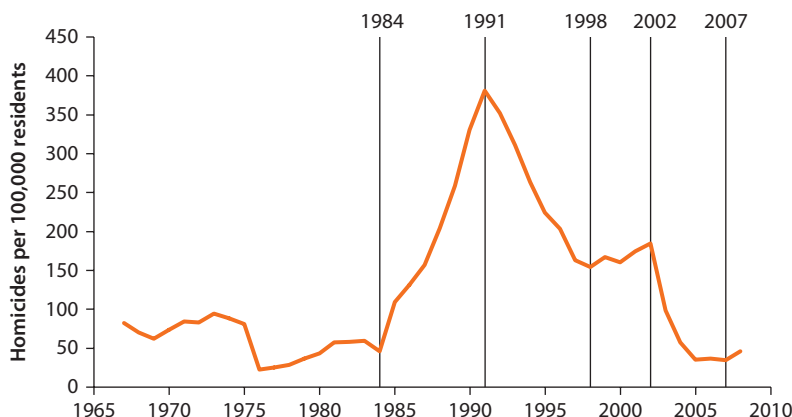
Note: CAS = country assistance strategy; CPS = country partnership strategy; GDP = gross domestic product.

Medellín's homicide rate skyrocketed beginning in 1984 when Escobar's criminal network declared war against the government, then declined beginning in 1991 as it began losing ground to its rivals and the state. Violence rose again in 1998 as paramilitaries entered the city to eject leftist militias by force, and it peaked once more in 2002, but it declined rapidly once the leftists—targeted by paramilitaries, drug traffickers, and the state alike—were defeated. In 2004, what became known as the “Medellín Miracle” began: homicide rates plummeted, the city embarked on ambitious reconstruction and development campaigns, and the city's economy began to recover. Although the decline in homicide rates stopped in 2005 and rates were clearly rising again by 2007, Medellín's turnaround remains one of the most impressive examples in the world of a city overcoming complex violence through a combination of public, private, and public-private efforts.

This case study offers a brief look at Medellín's violent history, reviews some of the most important responses to that violence (both contributing and mitigating) primarily by the private sector, and considers some lessons that might be derived from the experience.

Violence in Medellín

Medellín's homicide rate in 1984 was 46 per 100,000 population; by 1985 it was up to 109, and it peaked at 381 in 1991 (though Medellín's most violent month was at the end of the following year, in December 1992, when 647 people were killed, an annualized rate of approximately 465 per 100,000). The homicide rate declined overall during the 1990s, with some fluctuation, falling to 154 in 1998, but it then began rising again, to 184 in 2002 (Secretaría de Gobierno Municipal de Medellín n.d.). By 2007, it had dropped to 34, Medellín's lowest level since 1978 (see figure 6.1). The rise in homicides in the mid-1980s through 1992 was

Figure 6.1 Homicide Rates in Medellín, Colombia, 1965–2008

Source: Secretaría de Gobierno Municipal de Medellín n.d.

accompanied by a rise in other forms of violence as well; the correlation coefficients between various homicide figures and various violent crime figures range from 0.55 to 0.90 (calculations based on Lamb 2010). The correlations would have been higher, but most reports of nonhomicidal forms of violence and threats of violence were falling in the late 1990s, when the homicide rate was rising again. For example, reports of battery fell from 2,418 incidents in 1999 to 902 in 2008; kidnapping fell from 28 to 5; and extortion (involving a threat of violence, usually against business owners) dropped from 373 to 63 during the same period (Policía Metropolitana del Valle de Aburrá n.d.).

The decline in violence after 2002 was impressive. In addition, one source estimated that the number of gangs operating in the city fell by half between 2003 and 2005 (from about 200 to about 100), while the number of less formal “street crews” fell from about 6,000 to about 4,000 during the same period (Ramírez 2008). The number of homicides fell from about 3,300 or 3,700 in 2002 to about 770 or 780 in 2007, depending on the source of the data (it rose again to more than 1,000 in 2008) (Secretaría de Gobierno Municipal de Medellín n.d.).

The rise and fall of violence in Medellín has mirrored that of Colombia as a whole, partly because its levels of violence were so high relative to other cities. Medellín’s contribution to Colombia’s overall homicide rate was 21 percent in 1990, for example. But as Medellín’s violence declined, so did its contribution to Colombia’s: it was down to 4 percent of the country’s homicides by 2004.

It is difficult to tease out the main trends in Medellín’s violence, but an extensive analysis of the data suggests that most of Medellín’s organized violence changed from being perpetrated for a combination of political, social, or economic motives (during the 1980s and early 1990s) to being largely due to economic motives (by the late 1990s and early 2000s) as groups perpetrating political and social violence were increasingly lured by easy money or infiltrated by organized

criminals (and the leftist insurgents turned to drug trafficking and kidnapping for new revenue sources after the collapse of their former patron, the Soviet Union). Nonetheless, most of the city's violence was not due to organized crime. Rather, most of Medellín's violence was due to common crimes perpetrated by individuals acting alone (Lamb 2010). But there was an important relationship between organized violence and common crime: "The spikes in [organized] violence created a context in which the rule of law was too weak to control [interpersonal] violence, and those who engaged in the latter often used that broader context to their own advantage, either by recruiting or deceiving collective-violence organizations to carry out personal vendettas, or simply by taking advantage of the environment of impunity" (Lamb 2010, 339).

In Colombia, and especially in Medellín, there has long been a culture of respect for individual accomplishment, successful outcomes have been valued more than proper processes, and social trust has been in short supply. It has been argued that this combination of cultural factors gave Colombia a "competitive advantage" in illicit trades because it had a ready supply of ambitious, entrepreneurial individuals willing to break the law to make money. It also has been an export economy for centuries—first gold, later coffee—so the basic knowledge and infrastructure for exporting illicit goods already existed. Medellín's challenge today is to rebuild a social order capable of reducing opportunities to break the law and to build social trust so that cooperative action can become a force multiplier for the city's natural entrepreneurial spirit (Thoumi 2005; Vargas 2004, 107). The decline in violence over the past decade gave the city's leaders an opportunity to build both.

Public Sector Responses to Violence

As violence declined and the city's government, civic, and business leaders worked actively to improve development and give citizens options beyond supporting or acquiescing to crime and violence, Medellín's economy and its business climate both improved dramatically. The city's gross domestic product (GDP) more than doubled in six years, from about \$8 million in 2003 to nearly \$17 million in 2009. In 2003, it was ranked as the 38th best city in Latin America to do business; it was 15th in 2010. The number of visitors to Medellín nearly tripled between 2004 and 2010, from about 55,000 visitors to about 163,000. In Colombia as a whole, the number of tourists grew from 557,000 in 2000 to 2,385,000 in 2010 (Garde 2011).

Over the years, Colombia's leaders had tried a wide range of efforts to bring about peace, including heavy-handed law enforcement in violent neighborhoods, a constitutional change in 1991 to make it possible to negotiate peace with politically motivated armed groups, a National Anti-Violence Strategy the same year, various demobilization and reintegration programs for insurgent and paramilitary members, and negotiations with drug trafficking organizations.

Medellín's leaders have made such efforts as well, including police raids, nonaggression pacts and cease-fires between gangs, demobilization and reinsertion programs, trainings for local peacemakers, and education campaigns.

During the 1990s, the city (a) established a program called *Promoción de la Convivencia Pacífica en Medellín y su Área Metropolitana*; (b) worked to improve community policing and the justice system; (c) trained and empowered communities and their locally elected community action boards (*Juntas de Acción Comunal*, or JACs) to contribute to conflict resolution and antiviolence programs; (d) established an office focused on peace (*Asesoría de Paz y Convivencia*); and (e) developed a regional security plan called Medellín at Peace. At the end of the decade, the city implemented the *Programa de Convivencia Ciudadana de Medellín*, focusing at first on giving gang members reasons to enter civil life and later on preventing young people from joining gangs in the first place. The efforts built upon the successes and failures of previous efforts, and the cumulative effect was to build institutional competence over time (CIDEAL 2005; Duque 2000).

After Medellín's leftists were defeated in joint military-police-intelligence campaigns (and, separately, joint narco-trafficker-paramilitary campaigns) in 2002 and 2003, the national government negotiated a demobilization agreement with the main organized crime and paramilitary bosses who had been rivals of the insurgents. Many Colombians believe the expulsion of leftists from Medellín was helped by an explicit but secret agreement between state forces and illicit actors, in which the former would give the latter de facto impunity in exchange for minimizing their participation in both violence and illicit businesses. Whether such an agreement was ever made (explicitly or implicitly), neither side must have kept its end of the bargain for very long: illicit activity continued, and the state arrested the top bosses after a few years. Still, the demobilized fighters were given opportunities to build legitimate businesses and other associations. Figures are not available, but it is extremely likely that some significant portion of Medellín's illicit profits over the years have been reinvested in the legal economy and have contributed positively to the region's economic development.

Sergio Fajardo became mayor in 2004 after creating a coalition of public, community, and business leaders (*Compromiso Ciudadano*) and campaigning by foot in the city's poorest neighborhoods. Once in office—and to take advantage of the window of opportunity provided by the defeat of the leftists and the demobilization of the rightists—he began an aggressive social outreach program in the neighborhoods where the city had rarely ventured before and that therefore had long been controlled by gangs and organized criminals. He improved financial transparency to persuade the city's business leaders to pay more taxes, improved management and revenue collection of the public services utility, and raised additional funds from foreign governments. The increased funding was used to address longstanding problems of social exclusion, in an effort to give people living in the city's poorest and most violent neighborhoods a stake in the system and a reason to stay out of illegal groups and illicit markets. Inclusive policies were multifaceted:

- *Physical and social inclusion.* One aspect of inclusion is simple physical presence or connection to the outside. During his campaign for mayor, Fajardo walked in poor neighborhoods and talked about the importance of pro-poor economic policies. During his tenure, the size and presence of the community police

(more trusted in poor neighborhoods than the regular police) were increased, the education budget was greatly enhanced, and private schools were recruited to help manage public schools. Most visibly, new school and library buildings—including some designed by internationally renowned architects—were constructed in poor neighborhoods. The city's cable-car system, begun in 2000, was completed in 2004, connecting several formerly isolated hillside neighborhoods with the downtown public transportation system and thus physically connecting those communities with the rest of the city and neighborhood microenterprises with the broader market. One study found that the homicide rate decreased 66 percent more and reports of violence decreased 75 percent more in the neighborhoods newly connected to the rest of the city than in similar neighborhoods that did not receive such infrastructural investments between 2003 and 2008. To connect one particular hillside neighborhood that previously had been accessible only by hundreds of steps, a 1,200-foot escalator was installed in 2011 (Cerdá *et al.* 2012).

- *Political and economic inclusion.* Another aspect of inclusion is participation. Fajardo established a participatory budgeting system and included significant public consultations in the preparation of the city's development plan. The city's participatory policies empowered the JACs to decide how small amounts of city money would be spent in the neighborhoods they represented, including identifying projects and awarding contracts to local small businesses. The system created a new source of revenue (city contracts) for small businesses and gave citizens better access to decisions that affect their lives at the local level (Lamb 2010, 235–36; Restrepo Mesa 2007). In addition, a network of business support centers (*Centros de Desarrollo Empresarial Zonal*, CEDEZOs) was created throughout the city to provide support and technical advice to microenterprises, and the Banco de las Oportunidades was established to provide low-interest microloans. Candidates for mayor in 2011 proposed establishing a similar bank to grow SMEs because the CEDEZOs are not equipped to help microenterprises grow in any significant way (Bateman, Duran Ortiz, and Maclean 2011; Beszterczey and O'Neil 2011).

Fajardo and his successor, Alonzo Salazar, also launched public campaigns against violence—including “*A Mi Ciudad No Vuelve La Violencia*” (“Violence Will Not Return to My City”) in 2008—and worked to improve the city's overall economic and business climate, with an emphasis on sectors identified as offering Medellín a competitive advantage in national and global markets (see the discussion of “clusters” in the next section).

Private Sector Responses to Violence

Despite recent progress, companies in Medellín, as well as in Colombia more generally, continue to be concerned about crime and violence even today. Almost a third of Colombian enterprises report “crime, theft, and disorder” as major constraints to their businesses, and almost three-quarters pay an average of about

1.3 percent of their annual sales for security (World Bank Enterprise Surveys 2010). These are long-standing concerns, and over the years private businesses and entrepreneurs have coped with Medellín's violence in a number of ways:

- *Exit.* Many businesses in violent neighborhoods that had been subjected to threats simply closed shop and left the neighborhood, the city, or the market.
- *Perpetrate.* Because much of the city's economic activity during the 1980s and 1990s was based on illicit profits, it is no surprise that many businesses participated directly in the violence. Some hired assassins to kill union organizers or business rivals. Some security companies went far beyond providing security professionals for other businesses: they extorted businesses to hire them by threatening to kill the proprietor, harm his or her family, or burn the business down. In addition, some of the fighters who had demobilized in the early 2000s saw an opportunity in the participatory budgeting system, and they bribed or threatened JAC leaders to steer city contracts to their own small businesses; some even won elections as JAC officers themselves amid allegations that they intimidated voters. By 2009, several JAC presidents had been killed, and dozens of people with links to the demobilized crime bosses had been elected (Agencia de Prensa IPC 2009; Lamb 2010, 335–65).
- *Defend.* An obvious response to a rise in crime is self-defense, and businesses took a number of measures, including hiring private security firms, installing security systems, and, in many cases, paying off the criminals who had extorted them. In Medellín, extortion rackets are known as *vacunas* (vaccines): as long as the criminals are paid, the business is immunized against attack. In one notorious case, neighbors watched two teenagers burn to death, trapped inside a bus that had been set on fire because the bus owner hadn't paid the *vacuna* (Medina Franco 2006).
- *Advocate.* Aside from offering private donations to organizations involved in peacemaking and antiviolence programs, some businesses, individual entrepreneurs, and their private foundations worked collectively—with each other or with the city—to multiply the effects of their efforts. Medellín's Chamber of Commerce and businesses involved in the clusters (further described below) have been particularly active in collective efforts, and many have made direct contributions to the city's social inclusion policies. For example, in December 1992, the city's business leaders published an open letter to the perpetrators of that month's massive wave of violence, encouraging an end to the attacks. In the mid-2000s, the foundation set up by Empresas Públicas de Medellín, the public utilities company, built parks around some of the libraries that had been constructed in poor neighborhoods. Early in Fajardo's tenure, several Chambers of Commerce, private sector foundations, and a private university recognized the importance of social inclusion and participation in keeping Medellín safe and prosperous, and they set up a program with the mayor's office to collect and disseminate quality-of-life data in Medellín for planning

and assessment purposes. And, to strengthen the city's legal economy, business leaders worked with the city beginning in the 1990s to determine the state of the city's economic development, potential competitive advantages, and main challenges, and they encouraged the use of a "cluster" model to position Medellín as a national and global economic competitor. The Medellín cluster system is a public-private partnership to generate economies of scale for SMEs, and to meet their technical and infrastructural needs, in key economic sectors. The 2004–07 development plan included two lines of operation based on the cluster model, and today Medellín has six clusters: power, textiles and garments, construction, business tourism, medical and dental services, and information technology and communications (El Tiempo 1992; Medellín-Antioquia Chamber of Commerce 2006; Medellín Como Vamos n.d.).

Lessons Learned

Violence has begun to rise again in Medellín, but there is no shortage of people and institutions in the public and private sectors with experience in negotiating with, investigating, fighting, or reintegrating criminals and gangsters—or in giving residents a stake in a stable system by including them in the city's social and economic development and political processes. Because Medellín's recent successes have not been due to any single factor, all of those experiences will be needed to keep the violence from getting out of control again. In fact, for many years, without success, the state had tried the following:

- *Taking a hard line against leftists (and some drug traffickers)*—but it did not manage to oust the leftists from Medellín until the early 2000s, and the collateral damage those earlier efforts had caused in the peripheral communities alienated tens of thousands of residents from their government (yet still left them subject to the depredations of the paramilitaries and other major crime figures);
- *Cutting explicit peace deals or implicit quid pro quos with crime bosses*—but those efforts had no real lasting effect on violence until after all the leftists were gone and the leader of the narcotrafficker-paramilitary alliance again had a monopoly on illicit activity (and even then the lull in violence and illicit behavior did not last more than a few years); and
- *Providing social services and some economic assistance in poor neighborhoods*—but as long as these efforts were done in isolation, they had little overall effect on violence.

What worked in Medellín was a blended approach: a hard-power strategy against leftists, a co-optation strategy with the narcotrafficker-paramilitary alliance, and a legitimization strategy with citizens. This was not a preconceived strategy, however; it worked out as a matter of both foresight and luck. The professionalization of the security forces had begun in the 1990s, and they became capable enough on the battlefield only in the early 2000s. The timing came just a few years after the country's leftist insurgents in the countryside had definitively delegitimized themselves during failed peace talks in the late 1990s,

so they had no public support to draw on. The co-optation worked mainly because the narcotraffickers had allied with the paramilitaries as part of a political strategy to give themselves the legal status they needed to demobilize and enjoy immunity from prosecution (criminals as such had no such right). Fajardo inherited the results of both strategies. He even disdained the co-optation, but he had the foresight to use the breathing room the demobilization had offered to try to rebuild the citizen-state relationship and consolidate those gains. He was also lucky to have inherited some of the most high-profile efforts, such as the cable-car system and the cluster initiative, which made it possible to start rebuilding the relationship and the economy immediately.

Other cities facing similar situations need not rely on luck, but rather can use foresight based on lessons derived from the Medellín experience:

- *Diversify the strategy.* In violent situations, some parties to the violence will be irreconcilable, others can be co-opted, and residents can be both the main victims and—if given a chance—the most important resource for lasting peace. The number of people who have to be fought should be limited to the irreconcilables. The co-optables can be dealt with later. Residents do not need to be won over immediately, but they will oppose whichever side they consider most abusive and unfamiliar, so hard-power efforts against violent actors should seek to minimize collateral damage in the short term. In the long term, all else being equal, residents will side with whoever treats them best, so as soon as the irreconcilables are defeated and the co-optables co-opted—and even before, if possible—every effort should be made to build a constructive relationship with residents to consolidate the gains.
- *Learn, experiment, and professionalize.* The national military and police reforms begun in the late 1990s were based on lessons learned since the 1980s, but they did not bear fruit in Medellín until 2002 (before then, the security forces had too often depended on paramilitaries for victory in battle). Medellín itself has a long history of urban and strategic planning and of working in partnership with the business and academic communities for planning and assessment. As a result of this strong learning culture, civilian institutions and nongovernmental organizations (NGOs) have experimented with program and institutional designs and have been able to build success upon success. Training of workers, and strategy and program design, should be based on evidence of what has and has not worked, and the professionalization of civilian and military personnel and their institutions should be progressive and cumulative.
- *Be inclusive.* Civic engagement by business leaders, academics, and advocacy and citizens groups should be encouraged. Lack of social trust prevents cooperative action against violence and limits how much revenue people are willing to pay the government. Fajardo's transparency gave business leaders a reason to pay taxes; his strong management of the public utilities company gave citizens a reason to pay their utility bills. Those efforts helped build trust in his

administration, but as important, it contributed to the revenue needed for larger-scale investments to physically connect residents in peripheral communities to the rest of the city. Likewise, the participatory budgeting system and development planning consultations gave citizens opportunities to feel included in broader city processes. The point is to give residents both opportunities and reasons to move closer to the city than to the violent actors.

- *Be strategic about developing legal alternatives.* Although it is important to be strategic in countering violence (see earlier), it is also important to develop the legal economy so that people have options other than illicit activity. The cluster system was not explicitly designed as a violence-coping mechanism, but identifying the most promising growth areas of the local economy and lowering the cost barrier for SMEs to enter those sectors is a sound approach to developing legal alternatives to illicit trades. The discussion by mayoral candidates of establishing an SME bank to fill the gap between microfinance and commercial banking is promising as well.

Although some of Medellín's business leaders had at one time been participants in the violence that engulfed the city, most have wanted a peaceful city: violence is bad for business (most businesses, at least). The most enlightened have worked closely with the city to improve not only the economic and business climate but also the living environment for Medellín's residents to give them a stake in the system and reduce prospects for violence in the future. The public-private efforts to draw citizens closer to the city and to give them opportunities beyond organized crime have paid off, although the work is not yet done.

Case 2: Rio de Janeiro, Brazil—The *Favelas* and the Private Sector: An Increasingly Safe Bet?

By Patricia Melo

Crime and violence affect the lives of millions of people in Brazil, with 40,974 people murdered in 2010, by far the most of any Latin American country. The evidence extends deeper than just murders: there were 39,693 incidents of rape and 811,705 recorded robberies in 2010. Finally, 2009 saw 544,766 Brazilians assaulted and 1,195,402 victims of theft. Domestic violence is also a serious problem in the country. Indeed, despite Brazil's considerable growth since 2003 (lifting 22 million people out of poverty), it remains among the 10 most unequal countries in the world, and the direct costs of crime are still significant, amounting to 3–5 percent of GDP per year. Crime is also consistently cited as a major constraint to business growth. Crucially, Rio is the state with the highest homicide rate—with the poorest neighborhoods or shanty towns, known as *favelas* (examined in this case study), which are associated with extreme poverty and informal urbanization and which exhibit the highest rates of all (table 6.2).

According to the World Bank's Brazil Country Partnership Strategy (CPS) 2012–15, the government of Brazil is deploying many initiatives to increase its

Table 6.2 Rio de Janeiro: Summary of Key Crime and Violence Indicators and Coping Mechanisms

| <i>Indicators</i> | <i>Results</i> | <i>Data (%)</i> |
|--|--|----------------------------|
| Cost to business (World Bank Enterprise Survey 2009) | Loss to GDP (Brazil) Firms paying for security Firms identifying crime, theft, and disorder as a major constraint | 3.0–5.0% 67.7% 77.7% |
| Homicide rate (Ministry of Justice 2008) | 30.8 per 100,000 population | |
| Identified in the CAS or CPS as a major issue | Yes, CPS 2012–15 (World Bank 2011a) | |
| Transparency International Corruption Perceptions Index rank (TI 2011) | 73 of 182 (Brazil) | |
| Private sector coping mechanisms | Private sector finances pacification programs in the <i>favelas</i> National and multinational companies invest in the pacified <i>favelas</i> : Procter & Gamble builds factory in the pacified Cidade de Deus and creates 500 jobs; Natura establishes microfinance marketing scheme with women in the pacified <i>favela</i> Complexo do Alemão; Light S. A. helps clean up the Santa Maria <i>favela</i> by offering money for paper, plastic, aluminum, and lead waste | |

Note: CAS = country assistance strategy; CPS = country partnership strategy; GDP = gross domestic product.

outreach to vulnerable populations and improve their living situations (World Bank 2011a). The government is scaling up successful endeavors to prevent crime and violence and promote socioeconomic inclusion with a focus on the residents of the *favelas*. The World Bank Group plans to provide support for the Brazilian government in this area by “i) helping increase the sustainability of slum upgrading investments and consolidate the achievements of crime and violence prevention initiatives, and ii) helping revitalize economic activity in the *favelas* through the International Finance Corporation engagements with a network of social entrepreneurs to make impact investments in a sustainable manner in these neighborhoods” (World Bank 2011a). This case study describes the role of pacification units coupled with public-private sector response in the form of financing security programs and business investments in postviolence communities of Rio de Janeiro.

Rio de Janeiro

Rio de Janeiro is the second-largest city in Brazil, with approximately 6.3 million inhabitants, and it represents the second-largest contributor to the national GDP. Although the city ranks among the world’s major metropolises, one-fifth of its population lives in the *favelas*, which have little infrastructure and few public services and are generally controlled by heavily armed gangs involved in drug trafficking. Violence is an everyday occurrence for law enforcement officials and the thousands of businesses and millions of residents in and around the *favelas*. Investment in security is twice that of education, five times that of health, and 50 times that of housing (CICS 2005). Because Rio has not been traditionally known as a violent city, many believe that the main cause for this change was the expansion of the illegal trade in drugs and arms.

Also, because of the lack of state providers of basic services and police, *favelas* are more susceptible to de facto control by drug factions. This, in turn, makes it

harder for economic and social development to take place, and it represents a barrier to entry for businesses, investors, development agencies, and crime prevention projects. Because of the risks and costs, high crime and violence rates hamper the city's attractiveness to investors and business operators. There are numerous public, private, and nongovernmental efforts to prevent and reduce violence in the country, and one of the most innovative and effective has been the approach implemented in Rio de Janeiro.

A Public-Private Partnership in Rio's Favelas: Win-Win Solutions

The history of drug trafficking in Rio can be traced back to the 1950s, with an increase in the levels of violence in the *favelas* in the 1980s and 1990s due to drug traffickers' need to protect their territory from attacks by rival factions and the police. For the police to become more efficient in the fight against crime and more responsive to the *favela* communities, the Rio de Janeiro state government under Governor Sérgio Cabral Filho launched in 2008 the Pacification Police Unit (*Unidade de Polícia Pacificadora*, UPP) program.

The UPP is a law enforcement initiative aimed at reclaiming *favelas* controlled by narcotraffickers and private militias. However, UPP is more than just a policing effort. The UPP program targets *favelas* where some public utilities and services have been taken over by a criminal organization, which becomes the basis for extortion of neighborhood businesses and for tax evasion. The UPP program comprises measures such as intensive policing and improvements in social services to meet the needs of local communities, while inhibiting criminal activities. Each new UPP is composed of trained policeofficers who are present in the pacified *favelas* 24 hours a day. As of January 2011, the program has deployed about 3,000 policeofficers in 16 *favelas* with a combined population of 215,000 inhabitants.

The public security aspects of the UPP program are accompanied by an integrated and targeted social program called UPP Social, administered by the Rio de Janeiro municipal government. The UPP Social consists of a coordination mechanism that maps government, private sector, and civil society programs and interventions, and channels them toward the achievement of specific goals aimed at consolidating peace and promoting long-term social development of the *favelas*. Together, UPP and UPP Social seek to provide sustainable public security and full democratic participation to residents of UPP-receiving communities. The World Bank has supported the UPP Social through the Rio Metropolitan Governance Development Policy Loan (DPL), which was the first subnational DPL to include a component on citizen security, and the Rio Technical Assistance Loan (TAL). The Bank has also developed studies on changes in community life in *favelas* with UPPs.

The UPP program has political support from federal, state, and municipal governments as well as strong support from the public. The private sector plays an important role in financing part of this initiative and in following up with investments and jobs creation, thus contributing to social and economic development in the pacified areas. For instance, the Group EBX plans to donate

R\$20 million (approximately US\$12 million) per year until 2014, and firms such as Coca-Cola Brasil, Souza Cruz, Light, Metrô, Banco Bradesco, and the Brazilian Soccer Confederation expressed interest in investing in the effort.

As of late 2011, the UPPs had been established in 18 of Rio de Janeiro's *favelas*, including Cidade de Deus, Dona Marta, and Morro da Babilônia. Preliminary results are encouraging. In areas served by the UPPs, violent crime has fallen dramatically while property values have increased. Moreover, preliminary results from public polls and ongoing research projects suggest the powerful effects that the pacification process is having in the lives of those communities. A recent survey of *favela* residents found that 86 percent of those interviewed in *favelas* with UPPs believed that safety had greatly improved, and 72 percent felt that outsiders had greater respect for them after the UPPs were installed. Among those without the UPP, 72 percent considered the UPP a positive initiative, and 70 percent would support receiving the program (IBPS 2010; World Bank 2011e). By 2014, the government plans to increase the number of pacified *favelas* to 47 and to deploy about 12,500 policemen in 45 *favelas* covering about 800,000 people or roughly 75 percent of *favela* residents in the city of Rio de Janeiro.

New Opportunities for Private Businesses

Only a few years after the implementation of the UPP program, Rio is witnessing the opening of a previously inaccessible market with huge economic potential and pent-up demand for a broad array of goods and services. Significant investments have followed the pacification program because of the increased security. With an eye toward meeting the demands of the hundreds of thousands of consumers and potential consumers who live in the pacified *favelas*, national and multinational companies are eager to see and support the installation of the UPPs.

One of the boldest commitments was from the multinational company Procter & Gamble (P&G), which produces food and hygiene products. P&G installed a factory in Cidade de Deus shortly after the *favela's* pacification was complete. The firm received property tax reductions from the municipality. According to Governor Sérgio Cabral, the installation of the P&G manufacturing plant in the Jacarepaguá area has generated 500 jobs. Representatives from Philips (a manufacturer of TVs, Blu-Ray Players, DVDs, VCRs, and audio systems) have expressed interest in establishing a factory in the Morro de Dendê (Ilha do Governador) if a UPP is established there. Municipal authorities have confirmed that the pacification of the area will take place by 2014.

Projeto Comunidade

Another successful effort is the *Projeto Comunidade* (Project Community) from Natura, a Brazilian manufacturer and marketer of skin care, cosmetics, perfume, and hair care products founded in 1969. The project was launched in 2011 and is helping to revitalize the local economy in the Complexo do Alemão *favela*

after the pacification process. The *Projeto Comunidade* offers noncash credit to women interested in working as Natura representatives (Koul 2011). This credit may be exchanged for Natura products, which then must get sold within 21 days. A study conducted by Natura found that existing debt was deterring women from becoming representatives for the cosmetics firm, so the firm increased the maximum debt allowed for new representatives from R\$200 (US\$125) to R\$500 (US\$315).

The project also allows women who have debts of more than R\$500 to obtain the products required to become representatives by paying money up front or by applying for a microcredit loan through a Natura partnership with Santander Microcrédito, a for-profit microlending institution. The latter involves establishing a “solidarity group,” whereby a loan is taken with at least one other person, each borrowing a particular amount but with the responsibility for paying back collectively. If one individual cannot pay, the other member(s) must make up the difference. Loans are not given in cash, but rather in credit to be redeemed for cosmetic products. As an extra step to reduce risk, Natura offers its resellers financial management courses and training in sales techniques at no charge.

With this approach, Natura has found a way to break into the *favela* market using local representatives, and the women develop a source of steady income. For its part, Santander Microcrédito has begun to develop a new group of clients for financial services in the *favelas*.

More Business Involvement in the Favelas

Light S. A., the Brazilian energy company working in the generation, transmission, distribution, and marketing of electricity in Rio de Janeiro, is currently running a *favela* cleanup program. Recycling programs are helping to improve life in the *favelas* by cleaning up neighborhoods and boosting household wealth. The Light project pays residents R\$0.10 (US\$0.05) per kilogram of paper and plastic. It also pays R\$2.50 (US\$1.40) per kilogram of aluminum and lead. The project has helped improve the Santa Maria *favela*, where police have been working since 2008 to take back the neighborhood from the control of violent drug gangs.

An interesting scene after the establishment of a UPP in a community is the strong presence of sellers for the Sky cable television operator. In each pacified *favela*, a sales booth is set up and cable TV packages are offered at accessible prices. In the Morro de São Carlos *favela*, 140 Sky employees were authorized in the area, resulting in more than 1,000 contracts signed in only seven days. This would have taken three months to achieve under normal circumstances.

The investment choices of the two multinational firms, combined with local business activities, demonstrate that the pacified *favelas* offer access to an important consumer market as well as significant strategic advantages, such as tax credits, access to land at low prices in central areas of the city, and a cheaper labor force. With peace in the *favelas*, business opportunities are on

the rise. The pacification program is making it easier, more cost-effective, and safer for businesses to access the areas of the *favelas* and expand their work and access to an attractive market. This public-private recipe seems to be working because now many people have a lot to lose if crime and violence return to the *favelas*.

Policy Implications

The Rio city government has played a fundamental role in the launching and implementation of the UPP program while also functioning as a channel to enable private sector investments in the pacified *favelas*. To encourage investments in formerly crime-ridden areas of the city, the government provides private sector firms with business incentives, such as tax reductions and cheaper land and work forces. The concept of “enterprise zones”—areas intended to revitalize distressed urban or rural areas through the provision of tax incentives and financial grants—seems feasible for future development programs. This would further support the development of the pacified *favelas* by attracting investments and creating job opportunities for the local communities. Capacity-building programs would need to be in place to address the lack of a skilled labor force in the communities. The design and execution of such training programs could be done by private sector firms, public entities, or both.

Lessons Learned

The UPP program has been well received by Rio residents, and some *favelas* without UPP units have started lobbying for one. In areas already served, violent crime has fallen and social services were brought into the communities. For businesses, the UPP program is enabling access to the *favelas* and to a vast new market with an enormous economic potential. However, even though private sector firms will find low-cost labor in the pacified areas, they are likely to face a limitation: *favelas* dwellers lack capabilities and skills because of their scarce opportunities to gain access to education.

The program has shown some weaknesses and has been criticized as limited in terms of scope and benefits. For instance, UPP officers reportedly lack resources such as bulletproof vests and weapons. The first UPP units were established in fairly affluent *favelas* in the south of Rio, and allegations of abuse and corruption have arisen involving members of the police force. There is a sense that crime has migrated to the *favelas* that are not yet pacified. The effort is regarded as a major success, but the question is whether the UPP will be able to transform the underlying relationship between the police forces and the residents—by creating a more progressive force with the necessary institutional support to discourage corruption and by addressing the underlying causes of drug trafficking and violence, including poverty, underemployment, and lack of government presence and protection.

Case 3: Jamaica—Coping with Violence in Paradise²

By Maria Ariano and Mike Goldberg

Jamaica is famous for its coffee, mountains, beaches, and reggae music—offering a complete tourist experience. In 2009, the number of tourist arrivals to the Caribbean island (including overnight visitors and cruise passengers) almost equaled the total population of about 2.8 million people (World Bank 2011d). In fact, tourism is the largest source of foreign exchange (42 percent), and it has helped Jamaica to generate investments amounting to an average of 30 percent of GDP per year. On the surface, Jamaica is a great opportunity for investors and a tourist paradise.

But Jamaica is also a world leader in crime and violence, which is the most pressing problem that the country faces and poses a growing threat to the country's economic base and social welfare. Fueled by high unemployment among at-risk youth (30 percent in 2011 among those ages 15–24) and weak public institutions, Jamaica's rate of crime is shocking: preliminary data for 2009 estimate that there were 52 murders for every 100,000 inhabitants (UNODC 2011). This murder rate is among the top five in the world. The cost of interpersonal violence in 2006 was estimated to be about 5 percent of GDP.³

High crime and violence rates in Jamaica have been increasing since the late 1980s and are mainly due to organized gangs in inner-city communities and to the transshipment of drugs. These are not isolated issues—they are linked through networks and financing. Weaknesses in institutions and public sector practices have contributed to opportunities for crime and violence as well. Overall, such high crime rates have a negative impact on the investment climate, discourage both domestic and foreign business investment, and stifle economic growth.

Furthermore, although Jamaica improved its performance to a ranking of 87th (of 178 countries in 2010) from 99th in 2009 in the Transparency International Corruption Perceptions Index, it still falls well behind other nearby tourism destinations (Barbados, Costa Rica, Panama, and Trinidad and Tobago) (TI 2011). There is a continued general perception that a significant proportion of the state's resources move along political lines through contracts, which ignore the established procedures because of weak rule of law.

The Effect of Crime and Violence on the Private Sector⁴

According to the 2010 *Country Policy and Institutional Assessment*, a recent World Bank Enterprise Survey found that 55 percent of Jamaican business managers identified crime as a major constraint to business (World Bank 2010c). The business costs of crime and violence are also higher in Jamaica than in 129 other countries (out of 133 total), according to the Global Competitive Index 2009–10 (World Economic Forum 2009; table 6.3).

In 2002, the World Bank conducted a detailed business victimization survey of 400 firms as part of the background studies for the 2003 Country Economic Memorandum, with a diverse sample of firms in terms of size, location,

Table 6.3 Jamaica: Summary of Key Crime and Violence Indicators and Coping Mechanisms

| <i>Indicators</i> | <i>Results</i> | <i>Data (%)</i> |
|--|--|------------------|
| Cost to business | Loss to GDP | 5.0% (2006 data) |
| (World Enterprise Survey 2010; World Bank 2010b) | Firms paying for security | 65.9% |
| | Firms identifying crime, theft, and disorder as a major constraint | 46.1% |
| Homicide rate (UNODC 2011) | 52.2 per 100,000 population | |
| Identified in the CAS or CPS as a major issue | Yes, CPS 2010–13 (World Bank 2010b) | |
| Transparency International Corruption Perceptions Index rank (TI 2011) | 86 of 182 | |
| Private sector coping mechanisms | Individual firms: strategies to increase firms' security and make them less vulnerable to crime, and to adjust the organization of business activity to reduce opportunities for crime; in some cases, accommodations with criminal networks Corporate social responsibility Public-private partnership to create a program to support information sharing and reporting on violence and crime | |

Note: CAS = country assistance strategy; CPS = country partnership strategy; GDP = gross domestic product.

and sectoral origin (Francis *et al.* 2009; World Bank 2003).⁵ The survey shows that criminal victimization of Jamaican firms is high. About 65 percent of all firms in the sample reported that they had experienced one or more forms of criminal victimization during 2001. Thirty-three percent of all firms were violently victimized (robbery, extortion, and protection); 52 percent suffered various forms of theft; 50 percent experienced fraud; and 7 percent, other forms of criminal victimization. Also, some Jamaican firms experience crime regularly and in multiple forms. About 27 percent of firms faced incidents of theft at least quarterly, of which 9 percent experienced theft weekly.

However, crime affects businesses not only directly but also indirectly, leading to higher costs of doing business (for example, increased security costs) and the diversion of investments and working capital from business expansion and productivity improvements. Unsurprisingly, more than half of the surveyed firms reported that crime increased their security costs. As shown in figure 6.2, 39 percent of the interviewed managers responded that they were less likely to expand their business because of crime, and 37 percent reported that crime discourages investments that would improve productivity. Often firms shut down and relocate to less crime-prone countries. Other analyses have also found that fear of crime causes individuals to avoid economic activities and locations that are perceived as exposing them to the risk of being victimized by crime.

It is important to specify that not all industries are affected equally by crime and violence.⁶ The effects of crime on security costs are felt the most in tourism, distribution, manufacturing, processing, and entertainment (see table 6.4).

The case of the tourism sector, in which Jamaica has a natural comparative advantage, shows clearly how crime and violence can affect firms' competitiveness in the long run and hinder the development of more advanced models of

Figure 6.2 Impact of Crime on Selected Business Practices in Jamaica, 2001

Source: Francis *et al.* 2009; World Bank 2003.

Table 6.4 Victimization of Firms, by Sector and Type of Crime in Jamaica, 2001

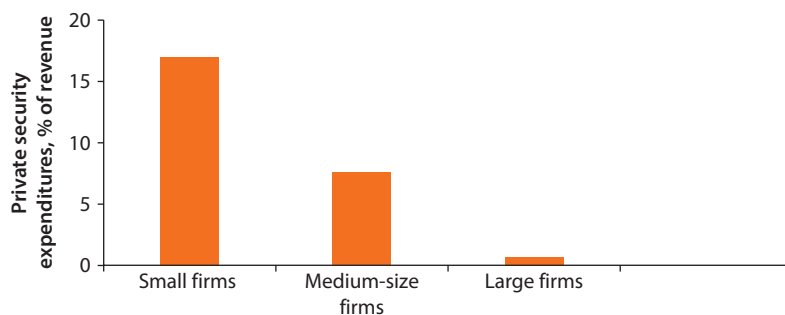
| Sector | Theft (%) | Fraud (%) | Violent crime (%) | No. of firms surveyed |
|-----------------------|-----------|-----------|-------------------|-----------------------|
| Finance | 5 | 65 | 10 | 20 |
| Tourism | 72 | 43 | 41 | 32 |
| Manufacturing | 47 | 47 | 21 | 53 |
| Agriculture | 81 | 38 | 41 | 53 |
| Construction | 44 | 48 | 28 | 25 |
| Transport and storage | 43 | 39 | 12 | 23 |
| Entertainment | 46 | 46 | 9 | 33 |
| Logistics | 53 | 63 | 24 | 79 |
| Mining and quarrying | .. | .. | .. | 8 |
| Other | 33 | 47 | 12 | 51 |
| All sectors | 52 | 50 | 33 | 377 |

Source: Francis *et al.* 2009; World Bank 2003.

Note: .. = negligible.

production and service delivery. Jamaica's tourism sector is traditionally characterized by SMEs in hotels and restaurants, but most investment and expansion in accommodations over recent years have been concentrated in larger and all-inclusive hotels, whose importance in the sector has grown consistently over time.⁷ A study conducted by Alleyne and Boxil (2003) found that although crime has discouraged tourists in Jamaica, the growth of all-inclusive hotels has mitigated this negative effect of crime. However, all-inclusive hotels typically do not foster significant backward links to the rest of the local economy. A new business model for tourism that goes beyond airlines, cruise lines, and hotels (such as ecotourism) cannot succeed if tourists are unwilling to leave all-inclusive resorts because of a fear of crime. As a result, even if tourism has grown in Jamaica, the

Figure 6.3 Private Security Costs as Percentage of Firm Revenue, by Firm Size, in Jamaica, 2001



Source: Francis *et al.* 2009; World Bank 2003.

Note: Firm size levels are 5–19 employees (small), 20–99 (medium), and 100+ employees (large).

country has lost market share worldwide and in the region, and it has not been able to keep up with world growth rates in the sector.

Company size is an important factor in a firm's exposure to crime. Small firms are far more likely to provide opportunities for harassment and crime. Data from Jamaica show that security costs pose the largest burden for small firms. As shown in figure 6.3, small firms pay security costs equal to 17 percent of their revenue on average, compared with just 0.7 percent of revenue for large firms.

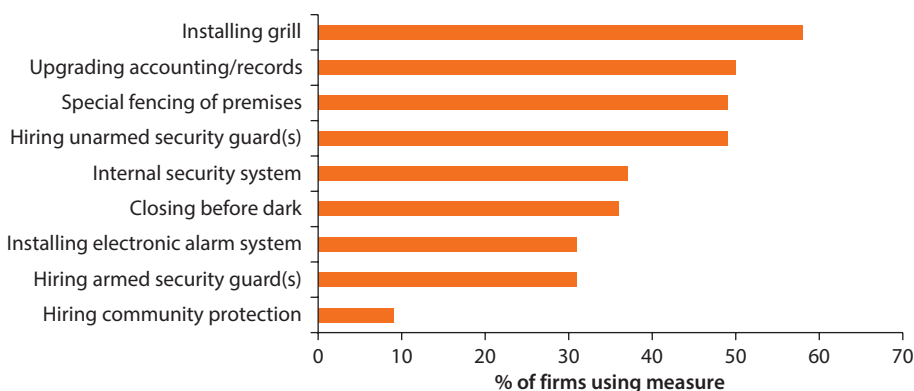
Finally, because most entrants start out small, the effect of crime and violence on smaller firms acts as a barrier to entry for potential entrants and inhibits growth. Size-based vulnerabilities may be accentuated by the area in which firms are located.

The Private Sector's Responses to Crime and Violence⁸

In Jamaica, firms try to respond to this challenging context with a variety of individual and collective coping mechanisms. The main elements of these strategies are "target hardening" (making the firm less vulnerable to crime), adjusting the organization of business activity to reduce opportunities for crime, and in some cases striking an accommodation with criminal networks. This section analyzes some of these coping mechanisms, starting with firms' individual ones and proceeding to collective ones.

Strategy 1: Individual Responses by Firms

The coping mechanisms adopted by individual businesses to protect themselves from crime and violence are varied and not limited to security measures narrowly defined. As figure 6.4 shows, physical security measures are the most common: 58.3 percent of businesses have installed protective grills on buildings, 49.3 percent have special fencing, and 31.0 percent have installed alarm systems. Nearly half have unarmed guards, and a remarkable 30.8 percent of firms have armed guards.

Figure 6.4 Crime Protection Actions by Firms in Jamaica

Source: UNODC and World Bank 2007.

Interestingly, whereas small firms tend to install metal grills and fence the premises, large firms use fences and security guards.⁹

Many firms (about 36 percent) have adopted adjustments that involve more directly changing the organization of business activity as well. For instance, they close before dark. This practice has especially high costs in the manufacturing sector, where second shifts are not used and productive capacity consequently sits idle. Often security costs associated with multiple shifts of technical and managerial staff are too high for these types of operations to be feasible. Crime and violence also affect efficiency in manufacturing through absenteeism, low productivity, and limited ability to attract experienced managers and technical staff.

Strategy 2: Corporate Social Responsibility

Among coping mechanisms by individual firms, there is the interesting case of Sandals, which is one of the largest tourism services providers in Jamaica, with all-inclusive resorts scattered across the island. One of its jewels is the coastal resort on Montego Bay on the northern coast of Jamaica, which was opened in 1981. While it is conveniently located near the airport, it is also within half a mile of the low-income, occasionally volatile neighborhood of Flankers.

As an individual firm, Sandals decided to develop a proactive approach to the risk of high crime and violence, which could have high costs for the resort hotel. Sandals Foundation has offices in Montego Bay and has worked with local formal and informal community leaders to design specific interventions. For instance, there is an internship program for groups of at-risk youth from Flankers, who learn a variety of hospitality industry skills, such as cooking, cleaning, and customer service. For most of the young people, this was the first formal sector job they have ever had. This is complemented by interventions in Flankers, such as support for the Peace & Justice Center (shown in figure 6.5), which provides social activities, special programs for women, and mediation services for the

Figure 6.5 Flankers Peace & Justice Center, Jamaica, Built with Support from Sandals Foundation



Source: ©Flankers Resource Centre. Reproduced, with permission, from Flankers Resource Centre; further permission required for reuse.

community. To demonstrate that it is a good neighbor, Sandals also supports an animal shelter and literacy and education programs. This outreach approach helps to keep violence in check in Flankers, while allowing Sandals to continue to welcome large groups of tourists to its resort in Montego Bay.

Strategy 3: Information Sharing

Given the high victimization of firms in Jamaica, institutional support from the criminal justice system is vital. Consequently, reporting is considered a critical first step in appealing for institutional support. For this reason, the Private Sector Organization of Jamaica (PSOJ) established a partnership that could support information sharing and reporting.

The PSOJ was established in 1976 as a fund and has grown into a national organization of private sector associations, companies, and individuals that work together to promote a competitive and productive private sector. The program was established under the direction of the president of the Jamaica Hotel and Tourist Association with US\$1.3 million in funding, and it is similar to programs operating in Canada, the United States, and numerous other countries around the world. It was converted into a limited liability company in 1991. The PSOJ established the Crime Stop Partnership in 1989, creating a network of private firms, communities, the police, and the media, designed to involve the public in the fight against crime. Crime Stop encourages the public to give information by

offering total anonymity to all callers and a cash reward for information that leads to an arrest, recovery of stolen property, or seizure of illegal drugs or guns. The counselors work on a shift basis to ensure 24-hour, seven-day-a-week monitoring of the telephones, in close coordination with the police.

The moderate operational costs are covered by contributions from participating actors and interest earned on the original endowment and subsequent private sector contributions. The costs of the program include the administration, advertising, and payments for the rewards. The sources of income are the following: (a) media companies, which provide free time and space, design, and production facilities for regular advertisements, posters, and stickers; (b) the police, which provide office space and personnel to answer the telephone hotlines; (c) the PSOJ Secretariat, which provides free accounting services; and (d) interest accrued on the Capital Investment Fund (made up of private sector donations), which pays all cash expenses.

By September 2009, the Crime Stop program had paid out more than US\$185,000 in rewards and had received 18,953 calls, which led to 1,942 arrests. The police had also recovered property valued at about US\$2 million and destroyed narcotics worth about US\$5 million.¹⁰

Strategy 4: Public Project to Support Microfinance

Along with private sector coping mechanisms, a World Bank–financed effort targeted the 16 most violent neighborhoods in Kingston and Montego Bay. In 2006, the government's Jamaica Social Investment Fund (JSIF) and the World Bank launched the Jamaica Inner Cities Basic Services Project to improve the quality of life in 12 Jamaican inner-city areas and poor urban informal settlements. The JSIF improved access to basic urban infrastructure and financial services, funded land tenure regularization, and enhanced community capacity and improvements in public safety. This project illustrated how the public-private microfinance support system could target high-crime neighborhoods as part of a broader engagement in communities with high levels of violence.

The project design included an innovative microfinance component to provide access to finance by private microfinance institutions (MFIs) for microbusinesses in high-crime urban neighborhoods. This component was intended to provide financial services in 16 inner-city neighborhoods in Kingston and Montego Bay, selected for their historically high rates of crime and violence. The MFIs stated that the instability and violence in the area created higher risks for them and would result in higher costs of client identification, monitoring, and contract enforcement. Because the MFIs had loan capital available, the project's microfinance component set up a competitive output-based approach (OBA), which generated bids from four MFIs for a least-cost subsidy to build microfinance portfolios in the neighborhoods using the MFIs' own capital. The maximum subsidy was set at 40 percent of the projected portfolio, and the use of the subsidy was untied.

Of the 10 MFIs informed about the experiment, four offered bids. Although one was disqualified because of poor financial performance, three bids were

received for subsidies ranging from 16 percent to 35 percent. Commitments from the three MFIs (Jamaica National Small Business Loans Ltd., City of Kingston Cooperative, and Access Financial) amounted to J\$44 million (US\$570,000). However, a loan portfolio of only J\$1.98 million (US\$91,000) was disbursed in the neighborhoods. Shortly after the first round, the JSIF Board of Directors decided to discontinue the experiment, stating that the potentially risky productive credit approach was not completely compatible with the basic-services approach the social fund program promoted. While the effects on crime and violence were minimal in this case, the pilot showed that innovative approaches to provide local microbusinesses with access to finance could be a useful tool in a broader public-private crime and violence toolkit and are worth further exploration.

Although the model failed to reach scale, the simple rules of the game to explicitly encourage MFI investment in high-crime, high-violence neighborhoods are instructive. The model was built on best practices in microfinance, leaving the credit risk and mitigation measures up to the individual MFI. Expectations were made clear from the start. The participating MFI was expected to market its products in the communities, use its own capital to lend to clients it selected using its normal due diligence review, and monitor and collect the loans. Because this was not a guarantee scheme, the MFI had high incentives for loan collection. The MFI was not supposed to offer subsidized interest rate loans, choose high-risk borrowers, or approve loans to clients recommended by the JSIF or other institutions. Finally, the subsidy provided by the JSIF could be used however the MFI chose and was not linked to having a physical presence in the neighborhoods.

Lessons Learned

The case of Jamaica shows how crime and violence affect the competitiveness and productivity of businesses over time and that there is a range of ways to respond. In particular, the effects of crime and violence impede firms' ability to compete and adapt the structure of production that offers them opportunities for growth, improved productivity, and profits. This situation is worsened by institutional weakness and the lack of clear, well-defined leadership. The final result is a huge loss for the country in terms of growth and competitiveness. This case study also shows that not all firms are affected equally by crime and violence and that smaller firms are more vulnerable to crime and pay a higher price to continue their activity in the market. The examples also show different paths to private sector engagement and coping mechanisms in response to high crime and violence. While Sandals demonstrates that individual firms have options, the PSOJ's efforts show that bringing the public, private, and civil sectors together can mitigate risk. At the same time, the JSIF approach to incorporate microfinance into an urban infrastructure and services project did not reach the anticipated scale, but it shows that innovative financial services could benefit crime- and violence-affected neighborhoods, under the right market and social conditions.

Only time will tell whether the combination of individual, collective, public, and private initiatives will help to transform Jamaica into the paradise of previous years, or fail to stem the tide of crime and violence. These examples, however, can help other countries that are reliant on tourism and foreign investment to choose from a growing menu of options that may fit their business culture and social and economic challenges.

Case 4: Mexico—Public-Private Responses to Violence

By Gabriela Enrique

A series of crises hit Mexico during the last quarter of 2008 and the first quarter of 2009. Having transformed its exports from commodities to manufacturing consumer durables to be exported mostly to the United States, the Mexican economy became significantly vulnerable to the disruptions of the global economic crisis. Annual economic growth in 2008 was down to a meager 1.3 percent, and GDP actually fell by 6.5 percent in 2009 (INEGI n.d.). In 2009 alone, foreign investments contracted by 41 percent, production was down 25 percent, and 46,000 jobs were lost in Ciudad Juárez and 39,000 in Tijuana from export-driven manufacturing companies (UNCTAD 2011). The situation was exacerbated by the AH1N1 influenza epidemic, which is estimated to have reduced GDP by 0.3–0.5 percent in April 2009 (World Bank 2011f). In addition, organized crime involved in drug trafficking, kidnapping, and other crimes further dampened growth, increasing corruption and reducing security in various parts of the country. A recent study estimates that crime and insecurity cost Mexico at least 1 percentage point of GDP growth (*El Informador* 2008) and other indicators painted a dismal picture (table 6.5).

Table 6.5 Mexico: Summary of Key Crime and Violence Indicators and Coping Mechanisms

| Indicators | Results | Data (%) |
|---|--|----------|
| Cost to business (<i>Bloomberg News</i> 2009; World Enterprise Survey 2010) | Loss to GDP | 3.0% |
| | Firms paying for security | 42.8% |
| | Firms identifying crime, theft, and disorder as a major constraint | 29.1% |
| Homicide rate (UNODC 2011) | 22.7 per 100,000 population | |
| Identified in the CAS or CPS as a major issue | Yes, CPS 2008–13 (World Bank 2008b) | |
| Transparency International Corruption Perceptions Index rank (TI 2011) | 100 of 182 | |
| Private sector coping mechanisms | Cluster initiative and public-private partnership: creation of a private sector forum, transformed later into a nongovernmental organization Public-private partnership: leverage of social media to promote accountability Corporate social responsibility by groups of firms with the civil society: mobile applications to find gangs and foster accountability with local government | |

Note: CAS = country assistance strategy; CPS = country partnership strategy; GDP = gross domestic product.

The Perfect Storm: A Global Economic Crisis and a Rise in Cartel Violence

Cartels competing for the control of a \$35 billion yearly market of cocaine in the United States generated record levels of violence in 2010 (UNODC 2011). In particular, violence rose sharply along the United States–Mexico border, where about 90 percent of the cocaine consumed in the United States crosses (UNODC 2011). National homicide rates increased almost threefold in four years—going from 8 murders per 100,000 inhabitants in 2007 to 22 by 2010. Other types of crimes also grew as cartels diversified and challenged local authorities with their power. In Tijuana, kidnappings increased by 200 percent, violent theft of businesses by 500 percent, and murders by 80 percent from 2006 to 2009. By 2009, drug organizations were taking over Juárez, charging SMEs between US\$100 and US\$500 in extortion fees per incident. In Mexico City, between 2009 and 2010, violent theft from SMEs increased by 50 percent, car robberies by 18 percent, and assault of logistics providers by 70 percent. By 2011, almost a third of the firms operating near the border or in Mexico City had been victimized by crime and had gone through supply-chain blockages; 45 percent of them reported feeling less secure than in the previous year; and 60 percent perceived violence against employees as the main threat to their businesses, while 30 percent perceived extortion as the main threat (American Chamber of Commerce 2011).

In general, firms have been adapting by training employees in crime prevention and investing in security around their physical and financial assets. However, many challenges arise every day as the type of crimes and the intensity of violence in Mexico evolve. Today, the perception is that sales, procurement, and logistics departments are the most vulnerable divisions because they operate in public spaces and are constantly exposed to threats of violence (American Chamber of Commerce 2011).

In spite of dynamic challenges, firms are finding innovative solutions that can be implemented at the individual firm level, by business associations, or by entire industry sectors. Most of these mechanisms are driven by a profound belief that it is up to the private sector—where effective and powerful actions can be found—to turn around increased levels of crime and violence while driving economic growth and prosperity. In cities like Tijuana, clusters of firms are focusing on the city's key competitive advantages as a way to cope and drive sustainable growth to the region. Other cities in Mexico leveraged public-private forums to address crime and violence. In Ciudad Juárez, SMEs have found in web-based social networking a tool to coordinate with the federal police and turn their neighborhoods into safe and thriving business areas. In Mexico City, local NGOs, SMEs, and large corporations are developing mobile apps to reduce local police red tape, monitor gangs' operations, and foster accountability from local authorities.

Strategy 1: Cluster Initiatives Based on Regional Competitive Advantages

From 2006 to 2009, Tijuana's main indicators of economic activity decreased significantly: tourism fell by 34 percent, employment by 9 percent, *maquila*

(factory) production by 13 percent, and foreign direct investment (FDI) by 63 percent. Violence, on the other hand, reached record levels in 2009. Bank assault incidences increased 16-fold between 2006 and 2009, creating significant challenges for local development (INEGI n.d.). In response, *Tijuana Innovadora (TI)* was launched in October 2010 as an initiative to enhance and promote the city's key competitive advantages: its proximity to technology-driven corporations in California; its highly educated labor force (relatively cheaper than that of the United States); and its coordination with public bodies to bring about sustainable change through crime reduction and pro-business reforms.

In early 2010, José Galicot, a local businessman, decided to take action and design a plan that could turn the city around. First, he partnered with local business leaders and local management from export-oriented manufacturing companies and established weekly meetings where participants discussed challenges and proposed several strategies to recover the city's entrepreneurial spirit. Second, he met with the federal government to provide the private sector's insights while designing the city's security plan. Finally, Galicot established a binational committee with business leaders from Tijuana and San Diego as well as Tijuana's top economic development authority to work on problems shared on both sides of the border.

TI started as a widely publicized private sector forum, bringing together global business and media leaders, and evolved into a dynamic NGO that works on the city's strategic development. At the forum, the main speakers included Al Gore, Carlos Slim, Wikipedia founder Jimmy Wales, Twitter cofounder Biz Stone, and Apple cofounder Steve Wozniak. More than 700,000 people and 100 international corporations attended the two-week event. Local firms showcased their products as a way to attract talent and investors. Working sessions around strategic growing sectors were facilitated by national and international industry experts. Opportunities for the digital media, automotive, biotech, entertainment, and green-technology industries were the main focus. Business opportunities flourished. Chris Anderson, the editor-in-chief of *WIRED* magazine, found a partner to start a water preservation project in the city that involves teenagers and educates them on global warming challenges. For the CEO of Toyota, *TI* was a breakthrough. First, Toyota decided to keep its Tijuana plant running, and more than 3,000 jobs were kept. Second, after witnessing the cost and innovation abilities of local engineers and scientists compared with those in Japan and the United States, he decided to explore establishing a research and development unit in the city. Many California-based biomedical companies participated and have since been exploring investment opportunities. Documenting and following up on the newly found opportunities were among the main challenges. *TI* also worked closely with national and world media to spread the word on the city's renewed competitive drive. The event has been featured in the media more than 5,000 times in 36 different countries.

It was after such initial gains from the cluster initiative that the government came in, helping the forum evolve into an organization funded jointly by manufacturing companies; local business associations; and the federal, state, and

municipal authorities. Today, the organization is run by Galicot, who serves on its board of directors; is composed of local business leaders; and works on projects around local innovation, entrepreneurship, and investment attraction.¹¹ Like many other organizations created during a global economic downturn, *TI* faces significant funding challenges as it competes with many development-enhancing initiatives. The founding team currently works on developing income-generating programs, beyond the revenues created by the forum, to turn into a self-sustaining organization. According to Galicot, the success of *TI* relies on integrating stakeholders, acknowledging talent, and building a strong global community that interacts around the city's projects and businesses.¹² By the end of 2011, coordinated efforts between federal forces (including the military), the state and municipal government, and local business associations started to pay off. Kidnappings decreased by 53 percent, violent theft to businesses and banks by 70 percent, and murders by 25 percent. Economic indicators are also improving: tourism increased by 18 percent, employment by 9 percent, production by 24 percent, and FDI by 90 percent only in 2011 (DGIE n.d.). Business organizations from Ciudad Juárez, Mazatlán, and Acapulco are now contacting *TI*'s team to implement their model of social change.

The Tijuana case shows the critical role of private sector leadership in rebuilding regions in challenging environments and fostering accountability from the local government. Proactive business leaders can coordinate and elicit support from different levels of government to alter perceptions about business opportunities in localities hard hit by crime. As a result, local champions recognized by a diverse range of stakeholders—the private sector, the public sector, and the international community—can arise. Although competitive advantages are different from city to city, it is important to note that it is the focus on regional business opportunities what helped Tijuana draw attention from the global community. For nonborder cities, other competitive advantages can be identified. Opportunities can be found in local talent, the ability to develop new markets, proximity to growing markets, and the presence of cluster institutions or ongoing investment climate reforms. Keeping the global community interested in the city by identifying and enhancing local advantages needs to be a priority.

Strategy 2: Entrepreneurial Leadership and Use of Social Media to Promote Accountability

Pronaf is a neighborhood in Ciudad Juárez next to the border between Mexico and the United States. Homicides caused by confrontations among drug cartels took the lives of more than 7,000 people from 2007 to 2009.¹³ Drug organizations extort business owners, use SMEs' services and products without paying for them, and torture and kidnap anyone not cooperating with them. By 2009, only 20 percent of SMEs operating in 2006 were still in business in Pronaf.

In spite of the generalized terror, there were still many business opportunities for tourism and entertainment. In October 2010, David Alamillo, an entrepreneur, decided to organize the remaining 40 SMEs operating in Pronaf and partner with the federal government as a mechanism to cope with the growing wave of

crime and violence. First, he renamed the area Zona Segura to communicate that change was happening. In parallel, government coordination—municipal, state, and federal—strengthened the local government capacities while fostering accountability around the “*Todos somos Juárez*” program. Then, in partnership with the federal police, security checkpoints were established around the commercial area. Finally, in November 2010, a local campaign was launched that used both traditional media and social networking to coordinate the efforts among participating SMEs on zero tolerance of criminal activities. Guidelines were provided to monitor gang activities, prevent crime, and file complaints directly with the federal police. Alamillo and others tweet daily about the progress made and the benefits of visiting Zona Segura while encouraging new entrepreneurs to join. Hashtags—monitored Twitter trends—were developed to report crime and extortion threats.

From 2010 to 2011, because of the partnership between local NGOs, *maquilas*, SMEs, and the federal government, the city reduced the incidence of crime and violence and captured the leaders of several drug organizations. Crime declined by 45 percent, extortions by 40 percent, kidnappings by 50 percent, and violent crimes by 51 percent (DGIE n.d.). Local entrepreneurs responded by filing new incorporation deeds for their businesses. By September 2011, 175 SMEs were operating in Zona Segura. As of spring 2012, there were 284, and Alamillo recently noted the absence of kidnappings, robberies, and extortion payments by SMEs to drug organizations reported for 10 consecutive months. This area is now a high-end entertainment neighborhood with restaurants, museums, theaters, hotels, banks, travel agencies, sport centers, and hospitals. The model of Zona Segura is also being implemented in Acapulco.

Lessons Learned

The precondition of public-private forums as a mechanism to cope with crime and violence depends on the presence of champions, often from the private sector. Champions with a clear vision can arise from unconventional places. David Alamillo saw in Pronaf an opportunity to prove to the rest of Ciudad Juárez the benefits of coordinated work between the private and public sectors to pacify entire neighborhoods and drive growth. Although local authorities were unable to respond to organized crime, this case illustrates how partnerships between SMEs and federal police forces are also possible. Alamillo developed a direct communication channel with a strong and credible partner while building solid relationships among stakeholders. Social media proved to be a powerful tool to facilitate communication, coordination, and increased participation of SMEs in security-enhancing efforts. For SMEs implementing a similar initiative, it is crucial that it be designed around a clear business opportunity to build momentum and keep participants encouraged. On the other hand, this initiative can hardly be implemented where there are no credible and effective public sector partners for the private sector, like the Mexican federal police.

Cluster initiatives as a response to violence also can be powerful in turning around a situation of violence. Not every region will have the same competitive

advantages around which the business leaders can rally. In Tijuana's case, the competitive advantage was its proximity to San Diego. It is important to identify a region's unique competitive advantages, such as an educated work force, cultural assets (for tourism), institutions of collaboration, knowledge institutions, and research and development capability.

Although there are examples in other parts of the world where the public sector plays a greater leadership role in public-private forums, the Mexico cases illustrate the importance of private sector leadership, as box 6.1 illustrates. In the United States, the Arizona optics cluster, San Diego's biotech corridor, and Silicon Valley started with private entrepreneurial leadership in a manner similar to the Tijuana case. In cases where capable private sector leadership exists, the public sector has an important role in providing inputs to private initiatives,

Box 6.1 The Case of Mexico City: Mobile Apps to Find Gangs and Foster Accountability with the Local Government

Mexico City was overwhelmed by crimes such as car thefts and robberies in businesses, homes, taxicabs, and bus stations. In many cases, the local police force collaborated with organized crime and was often unable to investigate, prosecute, and reduce crime levels.

In 2007, a group of 30 firms and 10 local NGOs established the city's *Consejo Ciudadano*. They started operations with the slogan "going from protest to positive action" and the goal of reducing crime and engaging the civil society by developing a series of online, text-messaging, and mobile tools to report crimes, file complaints, and map violent areas.

In 2009, the program Condesa 2.0 was launched in one of the most dynamic areas of Mexico City, where hundreds of small restaurants and retail stores operate. It was meant to be used directly where crime has occurred and to further simplify reporting, investigation, and case follow-up. Any SMEs in the area can download Condesa 2.0's app to have the latest reports on crime and to report any robbery. An innovative feature of this program is the use of "citizen agents": young professional civilians who visit crime victims and provide legal and psychological assistance. They bring a laptop and a printer to file the report instantly, communicating directly with local police and following up on the prosecution of criminals. These civilians link complaints to different programs such as the Citizen Report, which maps and monitors crime activity on a neighborhood basis. Users of Condesa 2.0 feel a positive change. In the area where it was used, from 2010 to 2011, robberies in bus stations decreased by 33 percent, taxicab assaults by 58 percent, car robberies by 53 percent, pedestrian assaults by 35 percent, and robberies of local businesses by 23 percent; in addition, key members of several gangs have been arrested and prosecuted.

From this case we can learn how champions can be created and institutionalized from joint efforts between SMEs, large corporations, and the civil society. This case also illustrates how mobile technologies can provide accessible tools to empower businesses and civilians to participate in crime prevention. Similar to the Juárez case, developing a direct communication channel with local authorities and following up on crime reports proved to be key elements of success.

keeping the focus on public goods, helping identify and address policy constraints, and acting as allies. Cluster initiatives and public-private forums can also be induced through government initiatives. Public-private forums can “prime the pump” of private leadership and improve coordination with the public sector to address crime and violence issues.

Case 5: Nepal—Private Sector’s Varied Responses to Violence and Crime

By Bertine Kamphuis

Crime and Violence in Post-CPA Nepal¹⁴

In Nepal, following the signing of the Comprehensive Peace Agreement (CPA), which ended the 1996–2006 Maoist insurgency and facilitated the reentry of the Maoists into mainstream politics, new forms of political violence and contestation with ethnic and regional agendas emerged, particularly in the Tarai region and the eastern hills. At the same time, old forms of politically backed violence persist—or even flourish—in the wake of the “postconflict” surge in public and donor spending.

The Maoist movement has undergone structural transformation that makes it unlikely to violently challenge the state again in the near term. However, violence has not ceased with the peace agreement. It takes many forms and varies across the different regions of Nepal, ranging from armed group and mafia violence in the eastern and central Tarai to disruptive ethnic activism in the western Tarai and eastern hills as well as frequent *bandhas* (shutdowns) and *chakkajams* (road-blocks), party clashes (for instance, around student elections), and clashes over tenders in urban areas and district headquarters (International Crisis Group 2010, 13). Businesses are common targets of criminal and violent groups; however, not all businesses are equally affected, and some have established close ties with these groups.

Impact of Crime and Violence on Firms

According to World Bank Enterprise Survey data for Nepal in 2009, Nepalese firms generally consider “political instability”—including armed conflict and insurgency, civil unrest, frequent changes in government and regime, politically motivated labor disruptions, strikes, *bandhas*, and closures—to be the most important obstacle constraining the investment climate. Ninety percent of the firms surveyed perceived political instability to be a major or severe obstacle to their business activity. In this survey, crime did not feature as an important obstacle for the vast majority of firms (see table 6.7); also the costs for hiring security firms in Nepal were about the same as in the South Asia region (Afram and Del Pero 2012, 24–28). On a daily basis, however, Nepalese firms operate in interdependent networks that connect business, political, and criminal actors, transcending legal and illegal boundaries with varying (perceived) legitimacy.

In post-CPA Nepal, armed group and mafia violence has been particularly prevalent in the eastern and central Tarai. Although some of the groups have political roots, most violence is linked to extortion. Armed groups tend to operate with near impunity, with political interference hindering law enforcement (International Crisis Group 2010). Businesspeople are frequent targets of extortions and abductions for ransom—and, in some districts, even killings. In a 2009–10 study, businesspeople expressed concern over a perceived increase in the number of criminal gangs, many of them armed (Crozier, Gündüz, and Subedi 2010, 9). Extortion comes in various shades; there is a gray area between voluntary contributions and extortions (often referred to as “forced” donations) that the World Bank’s Enterprise Surveys do not necessarily capture (see table 6.6).¹⁵

With many ethnic and regional activists agitated by the lack of an explicit reference to federalism in the 2007 interim constitution and an electoral system unfavorable to smaller parties, ethnic and regional activism and political mobilization gained momentum. As a result, the interim constitution’s first amendment added the word “federal” and introduced proportional representation (UNDP 2008). However, frustrated with the delays in the constitution writing process and increasingly doubting its results, ethnic groups have since then further toughened their stance; this was reflected in disrupting protests, particularly in 2009, when an estimated 700 different *bandhas* were called, most of them in the Tarai. Nepalese firms have incurred substantial losses because of shutdowns and roadblocks. From the April 2006 ethnic uprising until November 2007, there were about 100 *bandhas*. In 2009, an estimated 55 business days were lost because of civil unrest and trade union action. These losses add to the already high burden of losses due to power outages and theft, robbery, vandalism, arson, informal payments or gifts to public officials, and the costs of security. In total, the costs associated with these investment climate weaknesses

Table 6.6 Nepal: Summary of Key Crime and Violence Indicators and Coping Mechanisms

| Indicators | Results | Data (%) |
|--|--|--|
| Cost to business (Pradhan 2009; World Enterprise Survey, 2009) | Loss to GDP Firms paying for security Firms identifying crime, theft, and disorder as a major constraint | 3.0% (1996–2006 data) 44.1% 6.6% |
| Homicide rate (UNODC 2011) | 2.8 per 100,000 population | |
| Identified in the Interim Strategy Note as a major issue | Yes, ISN 2012–13 (World Bank 2011c) | |
| Transparency International Corruption Perceptions Index rank (TI 2011) | 154 of 182 | |
| Private sector coping mechanisms | Individual: exit, relocate, delay investment, pay higher protection costs, collude with violent groups, exploit new business opportunities Collective: share cost of security services, lobby for government action, engage in public-private dialogue on reforms, act as a mediator Hydropower sector: delay investment, reorient the business model, negotiate protection with local communities | |

Note: GDP = gross domestic product.

accounted for 36 percent of total annual sales and are substantially higher than in comparator countries. In that same year, at least 500 firms in the Sunsari-Morang industrial corridor, in eastern Tarai, shut down because of a lack of supplies due to the strikes and blockages (Afram and Del Pero 2012, 27; Alexander, Gündüz, and Subedi 2009, 27; Crozier, Gündüz, and Subedi 2010; *Kathmandu Post* 2007).

Violence is regularly employed to influence bidding processes and the allocation of state resources. To win bidding processes, competitors regularly collude with political party youth wings, armed groups, or criminal gangs, who in turn are protected by politicians. This nexus between political parties and *gundas* (youth gangs) is not new to postinsurgency Nepal (International Crisis Group 2010, 19). Following the peace agreement, investment in public works and development projects increased in Nepal. Regulation for public procurement has been adapted in recent years to avoid conflicts of interest and ensure competitive bidding. In practice, however, this legal framework is entangled with informal but publicly well-known arrangements involving *gundas* or armed groups. Generally protected from law enforcement by political parties, *gundas* are hired by contractors, for instance, to physically prevent competitors from submitting bidding documents or to violently enforce their rules of the game (Strazzari and Kamphuis 2012, 65–66).

Violence has affected businesses in varying ways. During the insurgency, particularly, Maoist-led closures, strikes, and extortion directly targeted big industry and large-scale businesses considered to be linked to elite power centers or firms primarily employing labor from India, evading taxes, or providing little local investment. In the post-CPA period, similar variations can be observed, with firms involved in extralegal practices reportedly being more at risk of extortion through blackmail (Crozier, Gündüz, and Subedi 2010, 12; Dhakal and Subedi

Table 6.7 Strategies of Nepalese Firms to Cope with Political Instability, Crime, and Violence

| <i>Firm responses</i> | <i>Examples</i> |
|--|--|
| Individual | |
| Exit, relocate, delay investment | Relocation of manufacturing to India (relocation more difficult for industries with sunk costs and unmovable infrastructure such as hydropower plants) |
| Incur higher protection costs | Hydropower firms that incur workable protection costs through local arrangements with village leaders |
| Collude with violent groups | Collusion around bidding processes (construction contracts, wood procurement) |
| Business entry | Private security firms |
| Collective | |
| Share cost of security services | Industrial parks, syndicates |
| Lobby for government action; act as mediator; engage in public-private dialogue on reforms | Federation of Nepalese Chambers of Commerce and Industry, Nepal Business Forum |

Source: World Bank Enterprise Survey for Nepal 2009.

2006). Thus, despite some general trends, crime and violence affect Nepalese firms in a variety of ways.

Coping Strategies

Nepalese firms cope in a variety of ways with political instability, crime, and violence—some more successfully than others. Individual firm responses (summarized in table 6.7) include exit, adjusting business practices by incurring higher protection costs or giving in to extortion demands, colluding with violent groups to influence bidding processes, and exploiting new business opportunities. To cope, firms sometimes cooperate to share the costs of private or public security services or to lobby the government.

Frequent responses to the mix of shutdowns, roadblocks, violence, and extortion (in addition to an already challenging business climate of regular power outages and trade union activism) have included business exit through closure or relocation (particularly to India) or substantially scaling down operations. Manufacturing firms were hit particularly hard because they are susceptible to political conflict, trade union activism, crime, and violence. In response, new protection markets have been created. A private security industry has filled this gap; as of 2009, it consisted of close to 700 registered private security companies, employing approximately 25,000 people and largely operating in a regulatory vacuum (Aayushma 2009, 225–38; International Crisis Group 2010, 43).

That many businesses are not passive bystanders in an environment of high crime and violence is reflected in some common business practices, such as the use of coercion and violence around bidding and the collection of monopoly and protection rents. Although businesspeople, especially in the Tarai, have complained about reduced profitability due to increased insecurity, inflated security costs, and extortion, some firms do well in this environment. As one Tarai-based entrepreneur put it, “The security situation is a blessing in disguise” because it blocks competition from entering the market.

Dealing with extortion and forced donations has become part and parcel of his business.¹⁶ Doing so effectively created interesting monopoly or oligopoly rents. The privatization of road tax collection in Nepal, for instance, has been accompanied by a mix of legal and extralegal practices to win the bidding process for the (annual) authority to collect taxes on a certain strip of road. Although substantial efforts are undertaken to get the official license, the actual taxation practices reportedly deviate substantially from the legally fixed charges.¹⁶ Having legally been awarded a monopoly position, these businesses can informally collect substantial monopoly rents.

In response to crime and violence, firms operating in the same industrial park or corridor have sometimes cooperated to share the costs of private or public security services. For instance, in two Tarai districts, the local chambers of commerce financed police control rooms and special police task forces dedicated to industrial security.

Businesses have also organized to lobby the government, for instance, for the implementation of an announced Industrial Security Force, which would be a

dedicated armed police force to safeguard the security of industrialists and businesspeople. Moreover, to improve the effectiveness of public-private dialogue and enhance the inclusiveness of business and investment-climate reform efforts, an economywide, national-level public-private dialogue, the Nepal Business Forum (NBF), was officially established in 2010 under the Office of the Prime Minister.¹⁷ The NBF brings together divergent leading business associations, sector-specific business associates, and individual businesses. One of its six working groups is dedicated to improving the business environment, labor relations, and industrial security. The Eastern Regional Business Forum (ERBF), an informal partner of NBF, has worked with the police to reduce illegal electricity consumption and reduce the intensity of protests in industrial areas. With NBF, the ERBF has also helped to reduce nonofficial taxation (World Bank 2012).¹⁸

Business associations have sometimes mediated conflicts. During the insurgency, the Federation of Nepalese Chambers of Commerce and Industry (FNCCI), an umbrella organization, continued to operate. Its network of local chambers of commerce continued to exist, even in areas where the government had no presence.¹⁹ When the Maoists in 2004 announced the closure of several enterprises, the FNCCI responded by establishing a task force to engage in collective discussions first without, subsequently indirectly, and thereafter directly with leaders of the Maoists' trade union. Eventually, in return for the release of Maoist trade union leaders by the government and an agreement by businesses to engage with trade unions on workers' welfare issues, the Maoists withdrew their threat to close down almost 50 factories (Dhakal and Subedi 2006, 415–16).

Doing Hydropower Business²⁰

The hydropower sector in Nepal has been at the center of much of the conflict, sometimes violent, over access to business opportunities and benefit sharing. Hydropower plays an important role in Nepalese street-level, inter- and intra-party, and international politics. It arouses the “seductive dream of the 83,000 MW [megawatt] hydro potential that the cascading waters of this land is supposed to hold” (Gyawali 2001, 29). Because of the gap between this dream and daily power shortages, which are crippling the economy and dictating Nepalis' everyday routines, the power shortages are a major source of frustration, frequently expressed in newspaper reports and through protests and blockages (*Kathmandu Post* 2011a; Manandhar 2011).

In the remote villages in the Nepali hills where hydropower sites are located, a wide range of actors attempt to collect benefits from the hydropower firms, with limited interference or explicit support from central and local government officials. Newspaper reporting and an in-depth study of four projects suggest that hydropower firms incurred substantial costs because of forced donations, extortion, obstructions, and strikes on a regular basis. Obstruction ranged from sit-in protests with a crowd of villagers voicing various social demands and preventing project staff from entering the site, to some unemployed youth blocking the water flow to the plant and demanding jobs, to a few antagonist contenders

hindering trucks of another contractor, to a single woman in front of the project gate claiming the company still owes her money for the land she sold (*Himalayan Times* 2011; Nepalnews.com 2011; interviews in Ilam, Sindhupalchok, and Kathmandu, May–June 2011). Construction of hydropower plants was regularly delayed, and operations had to be stopped on various occasions.

Because of high sunk costs, hydropower projects are effectively spatially fixed, making them susceptible to this kind of extortion or forced donations through obstructions. Developers can more easily opt out (and, for instance, relocate) during the preparation phase should local obstruction be fierce or claims be considered too high. Once substantial investments in its main infrastructure have been made, relocation of the hydropower project is practically not an option.

In response to these obstacles to hydropower development, some firms delayed their investment in major infrastructure. Other investors in hydropower projects have reoriented their business model away from the long-term expected returns on electricity generation and toward the ample rent-making opportunities that the major hydropower infrastructure and transportation contracts offer through overpricing (inflating costs) or underdelivering (using substandard material) during the initial years of preparation and construction of the hydropower plant. These opportunities were facilitated by banks that willingly extended loans, coupled with minimal oversight in the banking sector, until a credit crunch and the burst of a real estate bubble forced many banks to become more cautious in their lending practices. Still other firms tried to establish local protection arrangements with village leaders, some more successfully than others, as the next section discusses in greater depth.

Hydropower Firms: Buyers at a Local Protection Market

To guard against obstructions, hydropower companies tended to invest substantial resources and time to establish local protection arrangements. They generally sought to establish close relations with a local power broker (often consolidated through company employment or a construction contract), to whom they turned to deal with the company's village affairs. A company would usually, through this interlocutor, attempt to establish a dedicated committee of Village Development Committee (VDC) power holders who could secure the company against obstructions. However, various local (would-be) power holders organized themselves in committees—and each committee would seek to become the company's dedicated committee. They used preexisting power positions, the prospect of future benefits (jobs, construction contracts, and so forth), or the threat of being excluded from such benefits to convince villagers to trust their committee with company affairs.

The success of hydropower firms in establishing workable local arrangements varied across regions. Where the company provided a substantial source of contracts, jobs, and public investments and not many alternatives were around (as was the case in some of the villages in the remote eastern hills), it was easier for its (appointed) interlocutor to maintain a monopoly position. The

interlocutor, however, also depended much more on the company to maintain his position, which is why he had more to gain from supporting the company. This experienced in the eastern hills differs from the experience in Sindhupalchok, a district near the capital, Kathmandu. In Sindhupalchok—where village leaders tended to have strong links to centrally based patronage networks, and there were plenty of alternative sources of wealth around—would-be power holders had few incentives to nurture the companies. Moreover, this situation made it harder for these village leaders to establish a local monopoly position because contenders (supported by the next hydropower project in the area or another political party) kept emerging. Not unsurprisingly, the local arrangements around the hydropower projects in Sindhupalchok were more *ad hoc* and more closely reflected a typical “protection racket.” This was particularly the case concerning a hydropower project in a former Maoist stronghold, where, after the insurgency, no effective protection arrangements were established at all. Instead, in their bid for contracts, different small groups organized obstructions, sometimes mobilizing larger groups behind “social” demands or simply obstructing the project operation itself.

Although the central government proclaimed a hard-line policy against vandals who obstruct much-needed electricity generation, government officers at local levels (including central-level politicians from the areas where hydropower projects are located) actively supported, facilitated, or left room for nonstate arrangements between hydropower companies and local would-be regulators. Following a range of violent and destructive obstructions, in June 2011 the government announced plans to deploy the Nepalese Army to secure hydropower projects from future vandals, especially the 900 MW Upper Karnali Hydropower Project, a controversial export-oriented, Indian-led project whose buildings were burned the month before (*Kathmandu Post* 2011a). In everyday practice, however, district government officials have explicitly told most companies that they cannot rely upon the police 24 hours per day, seven days per week, and instead have to make local arrangements.²¹

Lessons Learned

The observed variance across Nepal in crime and violence and the intersector and intrasector differences in business coping strategies suggest that regional and sectoral studies can add value in addition to country-level studies. Operating within the same official legal framework, hydropower firms across different parts of Nepal, for instance, have coped with crime and violence in a variety of ways. In environments of high crime and violence, analyzing the mix of local arrangements between businesses and their protectors, and between state and nonstate protection providers, might give additional insight into the “business environment” in which firms operate. More systematic data collection will be needed to clarify whom firms buy protection from and seek protection against—for example, by including questions on this topic in the World Bank’s Enterprise Surveys.

It is too early to tell whether the Nepalese private sector can successfully support or participate in local crime and violence prevention efforts. The examples show opportunities for collaboration among business owners; however, Nepal has also shown how such cooperation can be used to exclude others from entering the sector, by creating closed networks of “business syndicates.” Joint public-private initiatives for improving business security, as the examples in the Nepalese hydropower sector show, can take the form of protection rackets. Economywide, regional, or national public-private dialogue is a more inclusive instrument, bringing together divergent interests (legacy businesses, new entrepreneurs, large-scale industries, and SMEs) to address business and investment climate concerns. Joint initiatives, however, should be supported with caution to ensure that they are founded on transparency, accountability, and inclusiveness rather than coercion.

Case 6: Rwanda—Turning the Tide of Violence in Postconflict Settings through Value Chains

By Kwang W. Kim

The year is 2001. Seated on a porch in the African countryside, President Paul Kagame had a calm demeanor that blended well with the haunting calm and beauty of the place after one of the darkest periods in the history of Rwanda. There is eeriness to the silence. The dogs could not be heard barking. When a foreign advisor next to him noticed this, the president replied with his soft-spoken voice: “The dogs were feeding on the cadavers.” He paused. “We had to kill them all.”²²

During the late 1990s and early 2000s, this landlocked country faced the challenge of rebuilding the nation after the 1994 genocide, which resulted in the deaths of between 800,000 and 1 million Tutsis and moderate Hutus, and left 3 million Rwandan citizens (38 percent of the population) displaced internally and externally (Vandendries 2003). Years after the genocide, the situation

Table 6.8 Rwanda: Summary of Key Crime and Violence Indicators and Coping Mechanisms

| <i>Indicators</i> | <i>Results</i> | <i>Data (%)</i> |
|--|--|-------------------|
| Cost to business | Loss to GDP | 32.0% (1990–2001) |
| (IANSAs, Oxfam, and Saferworld 2007; World Enterprise Survey 2011) | Firms paying for security | 89.8% |
| | Firms identifying crime, theft, and disorder as a major constraint | 10.3% |
| Homicide rate, 2008 (UNODC 2011) | 17.1 per 100,000 population | |
| Identified in the CAS or CPS as a major issue | No CAS 2009–12 (World Bank 2008a); Yes (World Bank 1998) | |
| Transparency International Corruption Perceptions Index rank (TI 2011) | 49 of 182 | |
| Private sector coping mechanisms | PPM: Participatory value chain approaches (working groups) in tourism, coffee, tea, and leather industries | |

Note: CAS = country assistance strategy; CPS = country partnership strategy; GDP = gross domestic product; PPM = public-private mechanism.

remained bleak.²³ This case study shows the initial response by the public and private sectors emerging from conflict, including how they addressed the following economic, population, and political pressures:

- *Economic factors* in early 2000 were characterized by unsustainable debt levels (US\$1.26 billion in nominal terms), even with enhanced Highly Indebted Poor Country (eHIPC) assistance; lack of a diversified export base; ongoing draughts; and the rising cost of food.²⁴
- *Population grievances* abounded in a low-investment environment with a finite quantity of land and jobs; 110,000 suspects of genocide awaiting trial under weak institutions; and a rising number of individuals living in poverty (from 40 percent in 1985 to 60 percent in 2000, and a per capita income of US\$220 per person—one of the lowest in the world and below the Sub-Saharan average of US\$470).²⁵
- *Politics* in such a deeply divided country—between the majority Hutu (roughly 85 percent) and minority Tutsi (15 percent) populations—was characterized by ethnically based political parties (a major environmental factor that permitted the genocide) and continuous weakness in the judicial system (Vandendries 2003, 6).

After a relatively short period of devastating genocidal violence, Rwanda faced the formidable challenge of sustaining its fragile peace. By 2010, the country was experiencing a remarkable turnaround. The country became a star reformer in Africa, doubling its GDP per capita to US\$1,150 while dramatically improving its Doing Business indicators (World Bank 2010a).²⁶ By 2012, Rwanda was ranked 45th in the world in ease of doing business and 8th for ease of starting a business.

Hotel Rwanda

President Kagame reflected on the week in 2001 when he was locked in a Kigali hotel conference room with his cabinet and a small group of foreign advisors to strategize about the country's future. Among the outcomes, there was an explicit choice to restart growth through "value chain working groups," initially focusing on three key industries: coffee, tea, and tourism. They also decided what *not* to do: focus on commodity and low-value product exports. This growth strategy served as a rationale to launch the Rwanda National Innovation and Competitiveness Project (RNIC), whereby the government and the private sector jointly created a shared competitive vision for the future.

All three industry value chains emphasized participatory private sector leadership with active government involvement, but tourism posed a unique set of challenges. When this work began in 2001, "given the country's recent history and the almost constant security risk postings issued by the diplomatic community in Rwanda, many considered it almost laughable to view tourism as a serious industry to develop" (Henning, Donohue, and Kacou 2008, 3). Unlike coffee and tea, tourism did not have a recent historical track record to build on.

International arrivals were estimated at fewer than 3,000 per year versus 34,000 in 1984. Leisure visitors who wanted to visit the gorillas in Rwanda usually crossed the border from Uganda just for a few hours; Rwanda was capturing little value from tourists outside low-priced gorilla permits (Henning, Donohue, and Kacou 2008). Moreover, tourism-related support institutions were in a shambles, disorganized, and, with the exception of mountain gorillas, lacking the tourism assets (attractions and infrastructure) required to succeed in the global tourism industry (Henning, Donohue, and Kacou 2008).²⁷ Despite such odds, global industry trends—particularly the rise of high-end, nature-based tourism—served as an opportunity for Rwanda to prioritize this sector.

Strategy: Value Chain Working Groups and Action Plans

Tourism was one of the early participatory value chains prioritized (along with coffee, tea, minerals, and leather) as part of the RNIC. The collaborative Tourism Working Group (TWG) launched by the RNIC exhibited the following characteristics:

- *Participatory private sector leadership.* The TWG, while initially government funded, enabled the private sector to take ownership and leadership. The working groups were intended to encourage leadership by the private sector that was inclusive, reflecting the wide range of value chain actors and firms of different sizes. The inclusion of SMEs was particularly important in an environment where violence and conflict loomed. Although large hotel operators participated (such as Milles Collines and Novotel), the agenda of TWG meetings was driven by the small players such as tour operators, travel agents, and small hotels. The meetings used international facilitators to address product development, industry coordination, market research, and access to finance issues, under the framework of public-private policy dialogue.
- *Emphasis on “high-value, high-spend.”* Early on during this process, the TWG made an explicit decision to focus on high-value versus mass tourism. “Yield,” or the amount of money each tourist spends (calculated as number of visitors times length of stay times amount spent per day), was the key metric to watch (Henning, Donohue, and Kacou 2008, 15). Also reflecting this focus was the TWG’s decision to recommend that policy makers raise gorilla permit prices while turning down mass tourism opportunities such as Point d’Afrique, a charter airline. As a result, the industry made an explicit decision to focus on nature-based tourism (projected at US\$55 million in receipts and US\$320 per visitor per day spent by 2010), while placing “explorers” (of cultural-heritage sites, amounting to US\$31 million in receipts, US\$220 per visitor per day) as a second-best segment.
- *Industry action plans.* A five-step participatory process was employed to develop the action plan: (a) situation analysis, (b) industry goals, (c) market

intelligence, (d) industry positioning, and (e) action guidelines (Henning, Donohue, and Kacou 2008, 12–13). Although quick wins were critical to help build momentum, the TWG worked for months to come up with a comprehensive industry action plan to serve as a shared road map for both the public and private sectors. Strengthening cooperation and institutions was particularly important in postconflict Rwanda. Taking time to institutionalize these working groups to address structural coordination issues and lack of trust has been a major hallmark of the TWG. Familiarization trips²⁸ for international tour operators—key gatekeepers in shaping perceptions of global destinations—served as critical actions to improve the perception of the country as a safe place to visit and to raise awareness of tourism services such as lodging, food, and beverages. Other action plan items included upgrading national parks; raising the price of gorilla permits through the Rwandan Development Board; establishing a primate certification program for visitors completing a full route in the North (mountain gorillas) and the South (chimpanzees); targeting marketing campaigns to key tourism channels that attracted the highest-spending visitors (international tour operators); developing standards for tourism actors; conducting trust-building activities between the Tourism Chamber and the Banking Association; and integrating local firms and producers into hotel and restaurant supply chains (Henning, Donohue, and Kacou 2008, 30).

- *Policy issues* (Henning, Donohue, and Kacou 2008, 22–27). The government was instrumental in kick-starting the national competitiveness program and the TWG. It also participated in the other industry working groups, providing real-time feedback and actions as discussions took place. One of the most important policy changes has been institutional, redefining the roles of the Tourism Board (ORPTN) and the Rwandan Investment Promotion Agency (RIEPA), while increasing the responsibility of the private sector. The TWG became the de facto mediator between these and other value chain actors, such as between tour operators and hotels. Moreover, the TWG helped businesses (particularly small ones) to better understand constraints, which over time helped Rwanda become one of the star cases in the World Bank's Doing Business reforms. The TWG also approved the creation of commercial courts in 2006, the lack of which had been a major source of constraint facing the private sector. Other reforms that took place either as inputs from the working groups or in parallel have sought to improve access to finance, especially by smaller firms such as tour operators and transport companies. These reforms include (a) property rights reforms in the form of a revised land-use bill in 2005 that established a single law to govern land rights and formalize the collateralization process through a titling system and cadastres registry; and (b) an International Finance Corporation (IFC)-supported program to shift from collateral-based lending to more flexible criteria, including two leasing windows to commercial banks.

Results

Rwandan tourism receipts increased from US\$4 million in 1995 to US\$218 million in 2010, while investment in tourism rose from US\$13 million to US\$94 million over the same period (World DataBank n.d.). The boom in visitors was followed by a revival in high-end construction, with 350 lodging accommodations built or renovated all over Rwanda, including boutique ecolodges charging US\$350–600 per night. Although many factors contributed to these results, the Rwanda leaders' explicit 2001 decisions, which were made in that hotel conference room, to focus on participatory approaches to value chains were instrumental in putting the country on the path of participatory growth. Challenges still remain, such as the lingering negative image following genocide, the vulnerability of gorilla-focus tourism, a low number of holiday travelers, and poor ground transportation.²⁹

On balance, Rwanda's working group approach showcased tourism's potential in a postconflict situation. It resulted in *economic growth* in a sector with a significant presence of micro, small, and medium enterprises (MSMEs). It improved *economic diversification* with the creation of off-farm employment that helped mitigate population pressure. It also addressed *income inequality* by focusing on tourism segments with links to the poor, including crafts and employment from non-enclave hotels, restaurants, and transportation services. Finally, it also helped improve the *global public perception of the destination* with familiarization tours that helped transform the opinion of international tour operators, who often serve as the gatekeepers of the global tourism industry.

Policy Implications

One of the major implications of the Rwanda case is that the government has a strong role to play as a catalyst to enable private sector growth in fragile, conflict-affected, and violent environments. The participatory nature of the value chain development is critical, and the TWG has been a key feature of this model. The government has played an important role in launching, monitoring, and evaluating value chain working groups, with the support of international expertise and facilitation. In the case of Rwanda, the TWG was a result of a national competitiveness program (RNIC) and the creation of a shared vision with the private sector on the meaning of competitiveness. These factors resulted in coordinated public-private actions that led to a wide range of policy reforms, many of them driven by working groups in the tourism, coffee, and tea sectors. Additionally, President Kagame's repeated statements that tourism would be a priority sector helped mobilize public and private sector focus with clarity and assurances from the nation's top leaders.

The implication for the multilateral organizations is the importance of designing value chain projects that are participatory to address key coordination and trust issues within the industry and between the public and private sectors. This is particularly important in fragile, conflict-affected, and violent environments, where the level of trust is low and institutions are weak. Inspired by the Rwandan

participatory model, the Guatemala Enhancing MSME Productivity Project has a strong value chain component (US\$19 million out of US\$32 million) that outlines a process leading to an action plan involving partnerships with several World Bank Group teams.³⁰

Lessons Learned

One of the major preconditions of the Rwanda model is the presence of strong champions. President Kagame's leadership was instrumental in catalyzing a shared vision of competitiveness and launching the working groups. But the success of Rwanda's working groups would not have been possible without the presence of—and ongoing input by—the private sector leadership, including a group of SMEs in the tourism industry.

Implementing working groups in Rwanda was more challenging than in other parts of the world, in part because of the absence of reliable data to support fact-based decisions. In some respects, however, it was also easier because of the useful tension and urgency created by the looming violence in a postconflict situation, which resulted in receptivity to new ideas and new institutional structures and reforms facilitated by the TWG (Henning, Donohue, and Kacou 2008, 13).

Taking time for the working groups to develop action plans was instrumental in building trust and strengthening coordination links within the value chain as well as between the private and public sectors. At the same time, *quick wins* were instrumental to build momentum among stakeholders. Balancing these long-term and short-term benefits are particularly critical in fragile, conflict-affected, and violent environments, where institutions are weak and social capital low.

Focusing on opportunities—not just constraints—matters. Despite the overwhelming constraints to developing a tourism industry (and lacking a robust track record), identifying global trends such as the rise of the high-value ecotourism segment served as a powerful uniting force among the tourism stakeholders.

Other concerns identified by the TWG included (a) the mismatch between the business development services needed and what was offered; (b) insufficient links with local communities around the national parks; and (c) slow development of private sector leadership, even though “pockets of excellence” existed. The latter concern was exacerbated by the historical predominance of the public sector in the tourism industry (through its government arm, the Office of Tourism and National Parks, ORPTN).

Facilitators serving as “neutral brokers” among the stakeholders played an important role in building trust, collaboration, and business links. The facilitators played a key role in organizing working groups, brokering conversations, coordinating technical assistance according to the needs of the group, and creating links among different working groups and other value chains (for example, coffee and tea). They helped structure decisions for working group members at each meeting (the frequency varying according to the needs of the group, ranging from once a month to once a week).

Institutions were created or strengthened to support the TWG and others. The TWG initially played a key role in strengthening the private sector and serving as a bridge between the private sector and the public sector's ORPTN. In 2006, as the private sector became more organized, the National Tourism Chamber of Rwanda was created with the support of the Private Sector Federation (Rwanda's top organization for business chambers and associations).

Afterword

The year is 2010. After the tragic period of genocide, Rwanda is rising (*Fast Company* 2009). Returning to the streets of Kigali, the foreign advisor noted that "there isn't a mango peel in the streets" (*Washington Post* 2010). Most strikingly, there is the sound. The dogs are barking again.

Notes

1. Information in this and the next paragraph are from Cañas and Emilio 2001a; Ceballos Melguizo 2001; Lowenthal and Rojas Mejia 2010; and Lamb 2010.
2. This section draws extensively from the Country Partnership Strategy for Jamaica (World Bank 2009).
3. This figure includes government spending on crime control (3.1 percent of GDP), private expenditure on security (1.3 percent of GDP), public health costs of treating victims or perpetrators (0.3 percent of GDP), private health costs of violence-related hospitalizations (0.1 percent of GDP), and direct production-related losses due to mortality and morbidity of workers because of crime (0.2 percent of GDP). It does not take into account nonmonetary costs such as pain and suffering of victims and their families and the human welfare loss related to living in fear of being victimized (UNODC and World Bank 2007).
4. This section draws extensively from the 2011 Country Economic Memorandum and its background materials (World Bank 2011d).
5. For more details on survey methodology, see annex 6.2 of the 2003 Country Economic Memorandum (World Bank 2003) and Harriott (2003).
6. World Bank focus groups held in April 2010 (World Bank 2011d).
7. All-inclusive hotels accounted for 75 percent of total rooms in 2009, up from less than 60 percent in 2004, and 35 percent of all units, compared with 26 percent in 2004.
8. This section draws extensively from the 2011 Country Economic Memorandum (World Bank 2011d).
9. Needless to say, this has led to a rapid expansion of the private security business.
10. Conversions of the Jamaican dollar to U.S. dollar are based on the exchange rate of March 28, 2012.
11. There is special leadership training for the youth, whereby more than 400 teenagers are exposed to entrepreneurial role models in both San Diego and Tijuana. The training ends with a business plan competition and the Tijuana Youth Awards.
12. The conference ended with a global community dance. Business leaders, volunteers, community members, and people born in Tijuana but living all around the world

danced for peace to communicate that the city was changing and that its population was focused on transforming Tijuana into an innovative, competitive, and forward-looking city.

13. National Security Statistics on drug related homicides, 2006–11 (INEGI n.d.).
14. The author thanks Jacob Rinck and Gabi Afram for their valuable comments on an earlier draft of this contribution.
15. The Enterprise Survey questions on crime focus on theft, robbery, and vandalism, while the questions on corruption focus on bribe payments to public officials.
16. Interviews in Birganj, Nepal, February 16, 2011.
17. The passage of the Nepal Business Forum Executive Order has been supported by the active involvement of all three Nepalese prime ministers during the project's first phase ("Nepal Business Forum Phase I") and involves participants from 16 line ministries and 23 private sector agencies.
18. For a further discussion of public-private dialogue, see chapter 4, box 4.1.
19. Interview with FNCCI representative in Kathmandu, February 25, 2011.
20. This case example is based on Kamphuis (forthcoming).
21. Interview with businessman, Kathmandu, Nepal, April 28, 2011.
22. Michael Fairbanks, adviser to President Paul Kagame, conversation with the author, 2011.
23. The World Bank (1998) CAS outlined three development challenges for Rwanda: to overcome the legacies of the genocide and stabilize the livelihoods of its citizens, to achieve peace and stability, and to improve the standard of living of the population. The CAS proposed, and the Board of the Executive Directors endorsed, the proposals that (a) Rwanda be treated as a special case for international assistance to help make transition to peace and development; (b) the International Development Association (IDA) provide an exceptional US\$80 million in assistance for one year (FY99); and (c) a report be prepared by the end of the year to review progress and prepare a new IDA support proposal.
24. Rwanda's debt analysis is from Vandendries (2003, 6). GDP per capita fell from US\$630 in 1993 to US\$340 in 1994, remaining flat at around US\$560 in 1990s (World Bank n.d.).
25. Poverty data from Vandendries (2003, 1).
26. From 2004 to 2010, the number of procedures to start a business decreased from nine to two, and the time to start a business decreased from 18 days to 3.
27. Such assets would include international-standard hotels and restaurants, a functioning financial system, knowledge of markets, tourism institutions, and trained professionals.
28. These are tours where travel agents, operators, and journalists become familiarized with the destination, including location, facilities, and amenities.
29. See the World Bank's Sub-Saharan Africa Tourism Database (<http://go.worldbank.org/ALVNILZAZ0>).
30. Participating World Bank Group teams include the Sustainable Development Network, the Finance and Private Sector Development Network, the World Bank Institute, the Poverty Reduction and Economic Management Network, the International Finance Corporation, and the Multilateral Investment Guarantee Agency.

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"Adaptability is the hallmark of firms in the private sector, as business leaders constantly confront an array of challenges: gaining access to finance and raw materials, keeping up with changing production techniques, and recruiting and retaining staff. But how do companies adapt to threats like crime and violence? Knowing more about the range of choices that business managers must weigh, as they try to make rational decisions in fragile countries and conflict-ridden situations, is important to delivering effective support to them - especially the kind of analytical, technical and financial support that the World Bank can provide.

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Crime and violence now disrupt the economic landscape in many countries. Governments, private-sector associations, and international organizations need to understand how business leaders deal with such threats. *How Firms Cope with Crime and Violence* outlines various decision-making strategies - and thus enhances our knowledge of business' ability to build thriving firms, create long-term wealth and promote civic cohesion."

- Dr. John Hamre, President of the Center for Strategic and International Studies



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