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Next Steps in Cote d'Ivoire:
Economic Costs and Consequences

Testimony to the Senate Committee on Foreign Relations
Subcommittee on African Affairs

by

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on

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Next Steps in Cote d'Ivoire: **Economic Costs and Consequences**

Mr Chairman, Ranking Member Lugar, members of the committee, I am honored to testify before the Committee on Foreign Relations Subcommittee on African Affairs on the economic costs and consequences of the recent post-election crisis in Cote d'Ivoire, which lasted from November 28, 2011 until the ouster of former president Laurent Gbagbo on April 10, 2011.

The views expressed in this testimony are my own. They are informed by my work at the United States Institute of Peace (USIP) which provides analysis, training and tools to help prevent, manage and end violent international conflicts, promote stability, and professionalize the field of peacebuilding. In directing the Sustainable Economies Center of Innovation at USIP, I lead research and field work on economic dimensions of peacebuilding in conflict-affected countries like Cote d'Ivoire. We leverage extensive partnerships in conflict zones to deepen our understanding of complex and evolving dynamics on the ground and sharpen our insights on remedial strategies that are both practical and effective. I also draw from first-hand knowledge of the Ivorian domestic economic and political environment, having lived in Cote d'Ivoire from 1998 to 2000 during my tenure as a senior macroeconomist at the African Development Bank Group. As a development economist, I have followed events in Cote d'Ivoire closely for over two decades.

Economic Roots of the Crisis

The evolution and structure of the Ivorian economy is central to understanding the current crisis. Since the 1940s, agricultural exports have been the mainstay of the economy. Pro-private sector policies adopted by the first president, Felix Houphouet Boigny, established a tradition of strong, export-led growth in the 1960s. Houphouet Boigny promoted investment, minimized price distortions, facilitated trade by improving vital infrastructure and provided credit/extension services for farmers. Within a decade Cote d'Ivoire had become a world leader in cocoa exports, macroeconomic performance was robust and the Ivorian economy was a regional powerhouse. However, these gains masked growing regional inequalities. While the vast amount of manual labor required for cocoa plantations in the South was provided by migrant workers from the North (a significant proportion of whom were from neighboring countries), most of the farms and agro-businesses were owned by the relatively more prosperous Southerners. The main political party, the PDCI (*Parti Démocratique de Côte d'Ivoire*; the democratic party of Cote d'Ivoire) had its base in the South and ensured that most government and private sector investment was concentrated in the South.

By the mid-1970s the structural dynamics of the cocoa industry had effectively created a two-tier society based on an increasingly accentuated North-South divide. Infrastructure, services and amenities were virtually non-existent in the North. Health and education facilities were woefully deficient and economic opportunity was limited. The opposite was true in the South. Deep poverty and deprivation in the North were in stark contrast to the advancement and burgeoning wealth in the South. That Abidjan (the commercial capital in the South) earned the moniker 'Petit Paris' speaks to the vast disparities that existed. The discovery of oil and gas reserves in 1975 and Cote d'Ivoire's ascendency as a regional financial hub in the 1980s only served to widen the gap, as the structural arrangements established in the cocoa industry were replicated in the oil and gas sectors. Relatively little of the nation's wealth made its way to the North.

The oil shocks and commodity price downturn of the early 1980s delivered a double blow to the Ivorian economy. As export earnings fell and import bills rose, the government introduced a program of stringent austerity measures. This unpopular program coincided with increased calls for more meaningful political and economic participation by groups in the North. There was restlessness in the South as the impacts of the cuts began to deepen, assets lost value and Southern political dominance was threatened by calls from most Northerners for greater inclusion in the political process. There was also restlessness in the North as groups with ethnic ties to neighboring countries felt marginalized and were convinced that they were bearing a disproportionate share of the austerity measures (particularly unemployment and lower wages). The fault lines had an ethno-religious element. The predominately Christian South is mainly comprised of members of the Baoule ethnic group, while the predominantly Muslim North is made up of a number of smaller ethnic groups.

The economic and political turmoil of the 1980s and 1990s sowed the seeds of discord that led to the violence that typified the first decade of this century. Houphouet Boigny successor, Henri Konan Bedie, compensated for his relatively poor political and leadership skills by playing on the now openly fractious North-South divide. The overthrow of Bedie in 1999 and the subsequent de facto partition of the country in 2002 further accentuated the relative deprivation of the North.

The 2010 elections were the first truly national elections in Cote d'Ivoire, with credible candidates fielded from all regions. The November 28 presidential runoff pitted the incumbent Laurent Gbagbo of the Southern-based FPI (*Front Populaire Ivoirien* – Ivorian Popular Front) party against the Northern-based RDR (*Rassemblement des Republicaines* – Rally of Republicans) candidate Alassane Ouattara. Although regional and international observers adjudged Ouattara to have been the winner, Gbagbo contested the results. The country's Constitutional Council nullified some 600,000 votes in the North and declared Gbagbo president. Both candidates held swearing-in ceremonies. This set the stage for a five-month stalemate that ended with the forcible ousting and arrest of Gbagbo on April 10, 2011.

Economic Costs of the Post-2010 Elections Stalemate

Even though the Ivorian economy had been reeling from almost a decade of violent conflict and political instability, the post-elections stalemate imposed additional economic costs. Analysts estimate that conflict over the past decade has cost Cote d'Ivoire some $8.7 billion in lost trade within West Africa; global estimates will be much higher.[1] The full economic

[1] Philippe Egoumé-Bossogo and Ankouvi Nayo, "Feeling The Elephant's Weight: The Impact of Côte d'Ivoire's Crisis on WAEMU Trade," International Monetary Fund Working Paper No.11/80, April 1, 2011. www.imf.org/external/pubs/cat/longres.aspx?sk=24784.0

costs of the post-elections crisis are still being assessed. There is also some evidence of substantial trade diversion to neighboring countries as traders and investors vote with their feet. The combination of significant financial losses and potential structural changes in trading relationships could constrain Cote d'Ivoire's recovery.

The Ivorian economy became a post-elections battleground as Gbagbo sought to solidify his hold on power by controlling revenue streams from the cocoa industry, petroleum sector and financial sector. Even though the economy had been weakened, it still held the prospects of significant current and future revenue streams, which Gbagbo needed to pay salaries, provide basic services and prosecute the ongoing civil war. For his part, Ouattara put in motion a series of events that sanctioned economic activity in a bid to prevent Gbagbo from controlling state economic assets. Both sets of action had serious economic costs.

Costs to the Cocoa Industry

Cote d'Ivoire is the world's leading cocoa exporter. It contributes some $1.3 billion in annual revenues, making it a lucrative revenue source. The main 2010 harvest was almost over when the unrest started and most farms and storage facilities were neither damaged nor destroyed. An estimated half a million tonnes of cocoa were already in pre-shipment storage facilities. Gbagbo started to run out of financing options in early 2011 as financial sanctions imposed by the West African central bank, the BECAO (*Banque Centrale des États de l'Afrique de l'Ouest*; the central bank for francophone West Africa), the European Commission and the United States started to take effect. He attempted to wrest control of the industry after failing to convince major exporters to pre-pay taxes and otherwise support his cause. Outtara countered by successfully orchestrating a ban on cocoa exports and the three main exporters (Cargill and Archer Daniels Midland of the U.S., and Swiss-based Barry Callebaut AG) suspended exports.

These developments imposed a number of costs. First, fears of a prolonged supply disruption put upward pressure on world cocoa prices, which hit a 32-year high of $3,775/tonne on March 4. The 7 million Ivoirians involved in the cocoa industry did not benefit from this price hike since exports were suspended. Second, on account of the sanctions an estimated 450,000 tonnes of cocoa was not exported and remained in warehouses for months.[2] Although rotting was minimal (only about 10 percent), many analysts believe that the quality could have deteriorated forcing exporters to accept much lower prices. Third, cocoa prices could also be dampened by the supply glut that will be created as the stockpile is released. The combined effects of these factors could run into tens of millions of dollars in losses.

In addition to these macro level costs there are a number of farm-level costs that might be even more pernicious.[3] Post-elections insecurity led to the displacement of roughly 1

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[2] David Brough and Nick Edwards, "Cocoa Stores in Ivory Coast Still Useable," Reuters, April 6, 2011, www.reuters.com/article/2011/04/06/us-cocoa-ivorycoast-idUSTRE7352PP20110406

[3] Orla Ryan, "Ivory Coast Cocoa Farmers Get Taste Of Politics," Financial Times, February 14, 2011. www.ft.com/cms/s/0/f1ee97b8-3864-11e0-959c-00144feabdc0.html#axzz1MXmYe2C4

million, while 150,000 fled to neighboring countries. Many of these were members of the industry's large workforce – including those involved in buying and transportation. Farmers who had not transported their produce to the warehouses in the port city of San Pedro before the onset of the unrest faced serious difficulties. First, a liquidity crunch meant that buying agents did not have cash to pay farmers for their produce.[4] Checks were not clearing and the Gbagbo administration imposed limits on withdrawals. Second, various militia 'taxed' cargo on the highways. Third, most of the usual transporters and buyers had fled. And, fourth, warehouses were full and not accepting any new produce. Consequently, farmers sought alternative channels to sell their produce --- most of which was smuggled via neighboring countries. During the first four months of 2011, the cocoa marketing agency in neighboring Ghana recorded a 50 percent increase in exports over the same period in 2010.[5] Smuggling cost the Ivorian economy millions in lost business and revenue.

Farmers were also forced to accept significantly lower prices for their produce (at a time when prices were peaking at record highs). Without other viable options, the farmers had to sell to the few buyers with liquidity, who took advantage of the crisis to underpay for the cocoa beans. So, while Cote d'Ivoire's farmers had to contend with much higher prices for food and fuel, they received only 50-60 percent of what that they would normally have been paid for their produce. This situation compounded their hardship, increased household debt burdens and constrained their ability to invest and fully prepare for the coming season.

Cote d'Ivoire's cocoa marketing woes persisted even after the ousting of Gbagbo. Liquidity remains problematic, tax and tariff payments are complicated because customs officials do not accept checks and credit is still scarce. These constraints require urgent action if the costs to the economy and cocoa farmers are to be minimized.

Costs to the Petroleum Sector

With production levels below 60,000 barrels per day and 100 million in proven oil reserves, Cote d'Ivoire is not a major oil producer.[6] However, the sector accounts for roughly one-third of the country's export. Cote d'Ivoire also has significant refining capacity that services both domestic and regional markets. Potential new oil and gas fields could boost output. For example, Block CI-112 off the western coast could hold over 2 billion barrels of crude reserves, while Block CI-40 along the southern coast could hold up to 200 million barrels. Insecurity will impact the likelihood (and quality) of investment. Promising exploration for new oil and gas fields were suspended because of the post-elections crisis. Texas-based Anadarko Petroleum Corporation and UK-based Tullow oil halted exploration in fields that analysts believe could have doubled Cote d'Ivoire's output in a few years.[7] One of the new

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[4] Loucoumane Coulibaly, "Ivory Coast Cocoa in Disarray from Crisis-Farmers," Reuters, February 2, 2011. af.reuters.com/article/investingNews/idAFJOE7110GX20110202

[5] The Ghanaian authorities attributed the increase to a bumper crop but analysts believe that that Ivorian cocoa accounted for some of the increase.

[6] U.S. Energy Information Administration. "Côte d'Ivoire," Country Analysis Brief, August 1, 2010. www.eia.doe.gov/countries/country-data.cfm?fips=IV

[7] Edward Klump and Eduard Gismatullin, "Anadarko, Tullow Halt Ivory Coast Oil Exploration on Violence," Bloomberg, February 24, 2011. www.bloomberg.com/news/2011-02-24/anadarko-tullow-halt-ivory-coast-oil-exploration-on-violence.html

fields could potentially add an estimated 550 million barrels to the proven reserves. Although not a major setback (as exploration is likely to resume shortly), the delay will result in increased costs and increased wariness by investors.

Costs to the Financial Sector

A major financial issue in the post-election crisis was the payment of the country's $29 million coupon payment on $2.3 billion Eurobond issue. These dollar-denominated bonds were basically past-due Brady Bonds owed to commercial creditors that were rescheduled in April 2010. This is the second time this stock of debt has been rescheduled. In spite of a January 10, 2011 letter signed by then-finance minister, Desire Dallo, promising to make the coupon payment within the 30-day grace period (the payment was due on December 31, 2010), this obligation was not honored. This increases the country's risk profile in the eyes of potential investors and could impact the cost of borrowing.

Implications for the United States

The economic costs and consequences of the Ivorian crisis impact U.S. interests.

First, because leading U.S. agro-business firms (Archer Daniels Midland and Cargill) are heavily invested in Cote d'Ivoire, continued instability, structural bottlenecks and weakened institutions in that country could affect their bottom line. The same is true of the lucrative chocolate industry in the United States. Opportunities for diversification are slim in the short- to medium-term. The windfall harvests (such as experienced in neighboring Ghana in 2010) and anticipated increases in export volumes in Indonesia (following an expected downward revision of export taxes later this year) are unlikely to cover the shortfall if Cote d'Ivoire's cocoa industry does not recover expeditiously.

Second, uncertainty in Cote d'Ivoire's petroleum sector could further heighten concerns about the reliability of supply from West Africa, which accounts for about a fifth of U.S. oil imports. Some analysts believe that pending exploration could more than double output in that country over the medium-term. Existing facilities also need to be upgraded to enhance efficiency. Prospective investors will be concerned about Cote d'Ivoire's creditworthiness given recent defaults on bond payments.

Third, continued weak economic performance would undermine efforts to build stable, reliable democratic governance in Cote d'Ivoire, which is a strategic objective of the United States. Furthermore, failure to address the plight of thousands of small-holder farmers would make IDPs and refugees less likely to return.[8] [9] There is evidence that economic conditions weigh heavily on the minds of the displaced. Large displaced and disaffected

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[8] Ange Aboa and Loucoumane Coulibaly, "Ivory Coast Cocoa Trade, Banking Poised to Restart," Reuters, April 26, 2011. af.reuters.com/article/topNews/idAFJOE73P0HX20110426

[9] Jane Byrne, "Ivory Coast Cocoa Trade Resumes but Credit Issues Remain, Analysts," FoodNavigator.com, May 5, 2011. www.foodnavigator.com/Financial-Industry/Ivory-Coast-cocoa-trade-resumes-but-credit-issues-remain-analysts

groups could compromise national and regional stability and make communities less stable and conflict more intractable.

Options for Action

Some analysts anticipate a swift economic recovery for Cote d'Ivoire, given its resource endowment and middle income ranking.[10] This is highly unlikely in view of the macro and micro challenges already outlined. Rebuilding conflict-affected states, like Cote d'Ivoire, is a complex undertaking. The comprehensive guidelines in USIP's "Guiding Principles for Stabilization and Reconstruction" are applicable in the Ivorian context.[11] This publication emphasizes the collectively-reinforcing nature of policy instruments that should be applied in such cases. These include sustainable economies, security, effective governance, the establishment of the rule of law and social well-being. This is the key to success in Cote d'Ivoire.

Given the nature of economic factors that precipitated and sustained violent unrest in Cote d'Ivoire, efforts at economic transformation should be anchored on two Es: equity and employment.[12] A history of stark regional and ethno-religious schisms combined with deep distrust contributed to the violence and unrest of recent months. An important peace dividend would be the establishment of conditions that facilitate equal access and opportunity for all. Targeted programs to redress these imbalances could include expanding the provision of infrastructure and services, targeted "access to credit" programs and capacity building initiatives. These must be designed in a conflict-sensitive manner. By this I mean that care should be taken to avoid rewarding 'spoilers' and it must not be presented a zero-sum solution (i.e. groups in the South should not feel punished or excluded, or vice versa).

Cote d'Ivoire's youthful population is a great asset but it could also be a potential powder keg. High rates of unemployment and under-employment could precipitate disquiet and unrest.[13] This is particularly worrisome when a significant proportion of the unemployed have been involved in the violence and there is a proliferation of small arms and light weapons across the country. In addition to developing training and retraining programs, serious thought should be given to the development of labor-intensive infrastructure programs. In addition, close attention should be paid to initiatives that promote the development of small and medium scale businesses. Cote d'Ivoire is a middle-income

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[10] Scott Stearns, "UN Expects Swift Economic Recovery in Ivory Coast," Voice of America News, April 14, 2011. www.voanews.com/english/news/africa/UN-Expects-Swift-Economic-Recovery-in-Ivory-Coast-119858994.html

[11] See Beth Cole et al (eds), Guiding Principles for Stabilization and Reconstruction, United States Institute of Peace and U.S. Army Peacekeeping and Stability Operations Institute, USIP Press, Washington DC. The conclusions in this manual are echoed in the World Bank's 2001 World Development Report: Conflict, Security and Development.

[12] I refer to economic transformation and not reconstruction because the pre-existing economic structure is often part of the problem. Reconstruction could involve a reestablishment of the status quo; this is why transformation is a much better approach in conflict-affected countries.

[13] George Fominyen, "Returning Ivoirians Fret Over Lack Of Work, Security," AlertNet, May 12, 2011. www.trust.org/alertnet/news/returning-ivorians-fret-over-lack-of-work-security/

country with a number of core economic activities (agriculture, minerals, finance and services) around which a wide range of small businesses could thrive. Policy-makers should resist the temptation to rely on the public sector (particularly security services) to absorb the bulk of the unemployed, directly or indirectly.

Although the United States and other development partners already provide significant humanitarian and development assistance to support economic recovery, political stability and security in Cote d'Ivoire, the needs remain great and expectations are high.[14] Consolidating the fragile peace necessitates proactive economic interventions by international partners in the following areas:

- Address the immediate needs of the cocoa farmers and implement social safety net programs to mitigate the impact of indebtedness caused by recent events.
- Invest in programs to improve cocoa yields, minimize post-harvest losses and improve the quality of the beans.
- Ease bottlenecks by supporting the expansion of cocoa marketing networks, extensions services and credit facilities.
- Technical assistance to improve external debt management and restore credibility in international financial markets.
- Establish effective monitoring and evaluation programs that are both credible and consistent.
- Create mechanisms to engage the private sector and civil society in the provision of humanitarian and development assistance.
- Clearly connect short-term assistance (such as security, humanitarian and repair of physical infrastructure) with longer term initiatives (such as strengthening state institutions, fostering inclusive and participatory governance, and promoting market development).
- Pay particular attention to small scale farmers and marginalized groups who have borne a disproportionate share of the economic consequences of the recent unrest.

Conclusion

In the months leading up to the 2010 elections Cote d'Ivoire benefited from a substantial rescheduling of its debt and millions in debt relief.[15] It also stood to benefit from an economic reconstruction package worth over half a billion U.S. dollars. These programs will be reinstated relatively quickly. The World Bank announced that it will fast-track the release of some $100 million in humanitarian assistance and expedite the delivery of $3 billion in debt relief.[16]

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[14] "Development Partners Discuss the Urgency of Recovery for Cote d'Ivoire," World Bank, April 20, 2011 http://go.worldbank.org/B6S8DK4HE0

[15] International Monetary Fund, "Cote d'Ivoire: Second Review Under the Three-Year Arrangement Under the Extended Credit Facility, IMF Country Report No. 10/228, July 2010

[16] Nicolas Cook, "Côte d'Ivoire Post-Gbagbo: Crisis Recovery," Congressional Research Service, April 20, 2011. www.fas.org/sgp/crs/row/RS21989.pdf

The French government has pledged an additional $577 million, the European Commission $260 million and so far the United States has provided $33.7 million.[17] However, care should be taken to avoid falling victim to a numbers game. Throwing money at the problem will probably worsen the situation. What is needed is a coordinated, comprehensive and conflict-sensitive approach to economic recovery in Cote d'Ivoire.

The views expressed in this testimony are those of the author and not the U.S. Institute of Peace, which does not take policy positions.

[17] USAID. "Côte d'Ivoire- Complex Emergency," Fact Sheet # 6, May 14, 2011. Last modified May 13, 2011. reliefweb.int/sites/reliefweb.int/files/resources/Full_Report_639.pdf