
The role of private sector development in a fragile region: an inclusive policy approach to overcoming limited public sector employment in Indian controlled Kashmir¹

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Abstract: *The Fragile State (FS) is an emerging concept of study and private sector development (PSD) in Fragile States (FSs) is much novel in this scholarship. The literature is fragmented across disciplines with little consensus on the definition of FS. Although PSD is reflected as an inalienable part of FS development, there is a lack of consensus between various schools of thought on best policy practices. These differences are rooted in debates, which on the one hand see conflict as a threat to PSD, and on the other seeing the Private Sector (PS) as a threat to an already fragile society; beyond these are challenges of poor governance and ineffective economic policy. While considering these debates, this study focuses on the underlying policy issues that fall within various paradigms of PSD in Indian Controlled Kashmir (ICK). It explores how ICK is a Fragile Region (FR) rather than a FS, and within this nature of fragility why PSD is under-nurtured and how it can be facilitated to overcome the limited public sector employment avenues. The study uses the critical approach based on mixed-method secondary data analysis with more inclination towards interpretivism. Evidence shows that ICK shares some characteristics with FSs, but its unique and differential socio-political nature makes it a Fragile Region (FR) rather than a FS. Within this situation of fragility the threat of conflict to PSD has reduced, and the*

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predatory nature of the Private Sector to local society is less manifested. However, the lack of an investment friendly policy, and an enabling governance environment, are daunting for PSD. Owing to the limited availability of literature, and the lack of a coherent model, this study proposes a framework - 'an inclusive approach to PSD'. The framework contends that in order to develop a conflict-sensitive PS, facilitating an enabling governance environment, and feasible economic policy reforms have to be complimentary to each other. Further, such private sector interventions will enhance employment opportunities and will reduce pressure on limited public sector avenues, once assurances against various threats and multi-stakeholder participation in the policy process have been seriously considered.

Keywords: *Indian-controlled Kashmir, Fragile State, Fragile Region, Private sector Development, Employment generation.*

1. Introduction

The concept of FS is relatively new (Carment. D., Prest. S., & Samy, Y., 2010) to the study of conflict environments and the role of PS in socio-economic development of such environments is novel in this scholarship. There is limited literature on PS's promotion of longer-term employment in FS (GSDRC, 2009), but with growing empirical evidence on poverty as a common factor of conflict (Mcleod & Davalos, 2008) fostering PSD as a counter-response has become a serious debate in the policy arena. The examples of PSD in some of the FSs from the last decade have shown that PSD creates employment opportunities and raises revenues through PS taxation, which in the long run support in strengthening the state-society social contract, state accountability and legitimacy and act as an important redistributive mechanism to correct horizontal and vertical inequalities (Mcloughlin, 2011). Arguably, some examples have also shown that in some cases, not being conflict

sensitive and properly regulated, PS has undermined fragile societies and has exacerbated conflict by feeding warlords. Although literature has suggested some measures to overcome such limitations, there is still lack of a coherent inclusive approach, which this study has tried to bring together by focusing on PSD in ICK. The approach focuses on the multi-dimensional aspect of fragility and PS, in order to foster a stable PSD in such societies.

One of the commonly found mistakes while debating about the economic development in ICK has been its unhelpful comparison with various states of Indian. This has not only a led mismatched understanding of local issues, but also planning and implementation of faulty interventions. The ICK, unlike these states, is a prisoner of one of the world's longest interstate conflicts (Arshad, 2004) where self-agenda based policies of the rulers of the region have historically ignored the needs of a majority of its residents, deprived of equal access, opportunities, or a political voice (Rai, 2004; Mir, 2003). The proliferation of conflict is rooted within this system of ignorance and manipulation (Habibullah, 2008), which has cost not only over 70,000 lives of Kashmiris, but also played a major role in the underdevelopment of the region (Schofield, 1997). Hence, considering such a complex contextual nature of being politically an ill region with economic stagnation, this study has tried to put ICK within the FS debate and to find out why PSD is under-nurtured and how it can be facilitated to strengthen the employment avenues and economic growth of the region. The study argues that persistence of fragility, and the lack of sustainable PSD in the region has created alarming unemployment and increased pressures on public sector jobs. This in turn has made the public sector an overly preferred method of employment, therefore

entrenching the practices of corruption and nepotism and an increase in the region's socio-economic insecurity. By proposing an 'inclusive approach to PSD', the study does not argue that supporting the PS is a cure. Political settlements lay the ground for future stability, however the injecting of optimism and hope through employment generation and economic growth can be a significant contributor to both peace and development (Peschka, 2011; Gerson, 2001).

2. A debate on Fragile States and the position of ICK within this debate

The overall conceptual construction of FSs is based on fragility caused by civil or political conflict, or by the underdeveloped nature of states. However, 'there is no internationally agreed definition of the term FS' (Mcloughlin, 2011: 9), because of which policy makers have adopted the concept in their own ways (Carment. D., Prest. S., & Samy, Y., 2010), giving certain direction to the argument about PSD.

Within academia 'some see FS as an inherently political label reflecting Weberian ideals of how a 'successful' state should function, whereas others have taken it further, by linking it to a range of transnational security threats and humanitarian concerns such as mass migration, environmental degradation and terrorism' (Mcloughlin, 2011: 8). Based on the presence of strong informal systems alongside the formal systems in some post-colonial states, Bratton and de Waal (1994) have defined them as 'Neopatrimonial states' and Reno (1998) as 'Warlord states'. A range of authors have defined them from the internal breakdown of formal systems, such as the failure of states or at risk of failing (Stewart & Brown, 2010), or a state's institutional volatility which undermines the predictability

and accountability of public decision making processes (Anderson, 2008). Other definitions extend to non-state interferences, such as being caught in one of four traps: the conflict trap, the natural resources trap, the trap of being landlocked with poor relationships with neighbors and the trap of poor governance (Collier, 2007).

While ICK has been variously defined from being a borderland issue (Zutshi, 2010), to a failure of social contract (Chandhoke, 2005) these definitions are inadequate and come within the ambit of FR when ICK is reflected through the lens of FS thinking. The region is caught in a conflict trap, where contest is not just between India and Pakistan, but a third important party to conflict is the region itself (Koithara, 2004). This trap has made the region vulnerable to both internal and external border shocks from 1947 onwards and landlocked it, with Delhi becoming the only root of contact with the rest of the World (Ashraf, 2004). Furthermore, the legitimacy of the region is undermined by the central government of India's (CGI) desire to serve its own political needs. This has led to a 'violation of social contract and failure in channeling democratic practices' (Chandhoke, 2005: 23).

Being surrounded by these features, normatively ICK does fall within the definition of FS. However, considering that the region is within the control of the Union of India and all its socioeconomic and political decisions have the hierarchical binding of central government of India (CGI), it becomes a FR rather than a FS by itself.

3. Debates on PSD in Fragile State's

There is an agreement that PSD is an inalienable part in FSs development (Siegle, 2011).__However, there is a

contestation between various schools of thought over *when* and *how* PSD should be facilitated. The *traditional school* argues that PSD should follow after first-generation imperatives of demobilization, and humanitarian assistance, whereas the *contemporary school* believes that an early PSD can provide opportunities for economic growth and stability by improving the standard of living (Peschka, 2011). Further, the *Investment climate approach* aims at creating a suitable investment climate related to both foreign and local investment by improving the economy at the macro-level. In contrast the *Interventionist approach* focuses more on the promotion of local PS with more reliance on donor interventions. While there is some overlap between various schools of thought, the practitioners of respective schools tend to dismiss each other (Sweeney, 2008: 51-66), creating hurdles in the way of extending a broader policy framework. This contestation and a lack of consensus is mainly rooted in three socio-economic and political debates within which a FS is caught. While one of the debates visualises the existence of conflict as a threat to PSD, the other sees the presence of PS as a threat to a fragile society and beyond these two debates are the concerns of endemic gaps in the governance system and economic policy of such states.

The *threat of conflict to private sector investment* is mainly because there is a lack of legal and physical security and chances of return of conflict. The guarantee of a complete rule of law with basic security, a properly functioning judicial system, clear property rights and regulatory system are very unlikely in FSs (Peschka, 2011). This severely disrupts and reshapes PSD, increases PS's reluctance to invest and creates extensive rent-seeking opportunities (Ibid). It is even argued that, if the conflict is formally over, there is a 40% possibility of return conflict within a decade following the end of violence (Collier, P., Hoeffler, H., &

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Söderbom, M., 2008). This places major limits on the shape and activities of both foreign and domestic investors, and consequently limits their interventions to short-term job creation (GSDRC, 2009: 8-11).

The flip side of this debate reflects that the companies in FSs have been historically considering the risks and threats posed to their own interests, without being sensitive to the impact of their activities on local communities (Bray, 2010: 5; 2009). The experiences from resource rich, war-torn and institutionally weak countries such as Nigeria's Niger Delta and Sierra Leone have shown extensive socioeconomic and environmental costs from extractive companies. The new waves of neoliberal economic policies in countries such as Haiti have undermined state legitimacy and led to higher unemployment rates due to local manipulations (GSDRC, 2010). The launch of universal relevance free trade models in such states were actually based on the priorities of donors and multilateral corporations, with little choice for local government, which devastated local rice producers, the rural economy and the labor market (Peschka, 2011: 30). Such over-time predatory experiences of PS interventions have created serious concerns around its further extension to these states.

Beyond these two extreme positions, another debate of concern is that FSs are caught in enormous *bureaucratic hurdles and have limited business protection* (Peschka, 2011: 13). Due to the human and material capacity distortion by war these states are not able to effect change, either from a practical or from an ideological perspective (Sweeney, 2008: 19). The absence of a well-governed system leads to the extraction of rent from investors and corruption at all levels (Mills & Fam, 2006: 28). This creates the unpredictable

enforcement of business and trade regulations and makes rational business planning difficult (USAD, 2009: 51). Very often, owing to clientelism and nepotism, such investment is dominated by elite families. They undermine the representation of less organized and powerless people, therefore distort healthy market development (Anderson, 1999; Peschka, 2011: 10; Mcloughlin, 2011).

In addition to bureaucratic hurdles, the distortion of the basic infrastructure and the lack of a business friendly climate are also serious issues of concern around PSD in FSs. This includes asset distortion, lack of access to electricity, transport, communication and finance, macroeconomic instability, depleted national fiscal base, dependence on import duties (Peschka, 2011), poor market analysis (Wilson, 2002) and the lack of consistent monitoring and evaluation (USAID, 2009). The absence of these measures keep not only international, but also local PS away from entering FSs and working effectively for large-scale employment generation. The loss of assets especially among local enterprises shrinks their purchasing power, and market contribution and make it harder for them to resume economic activities (Sweeney, 2008: 17).

Owing to these contesting debates, PSD in FSs has remained not only a sensitive area of intervention, but also a very narrowly focused approach without a long-term vision to support the large-scale employment generation and economic growth of these states.

4. PSD in ICK - Challenges and Possibilities

Prior to partition in 1947, the PS was booming in Kashmir, having its regular trade caravans across Central

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Asia, China and Turkey (Ashraf, 2009; Habibullah, 2004). The partition of India was the beginning of confrontation and the manipulation of regional society by the Central Government of India and regional rulers, and discontent over the political economy of the region (Chandhoke, 2005). The 1989 rebel uprising brought PS to a complete halt. It pulverized infrastructure, hampered important sources of livelihood and pushed the region towards economic stagnation (Hussain, 2012; Seema, 2009), with little effort from the government to re-establish it. The overtime sharp demographic transition, the fall of the agrarian economy, small land holding size, and the increase in the educated unemployed by 48% (Schaffer, 2005; Mercy Corps, 2011) exacerbated the unemployment situation with limited available avenues. The economy became highly dependent on government funds and the public sector emerged as the employer of first preference and last resort (Hussain, 2012; Habibullah, 2004; Schaffer, 2005).

A dramatic shift has occurred over the last few years. Though the inner game of political manipulation and people's agitation against it continues, there has been a substantial change on the socioeconomic and political fronts, which invite the possibilities for creating a conflict sensitive PSD.

While the conflict is considered as one of the major threats to PSD in FSs, in the case of ICK this threat has been overly emphasized. It is not that conflict does not matter, but that this threat to the extension of PS has reduced considerably. This is evident from the increasing stabilization of state regimes and some progressive 'first generation investment' (Peschka, 2011: 26). The patrimonial single party rule of the National Conference (NC) broke for the first

time in 2002, and since then the region has been run by coalition governments. There has also been substantial improvement in the security and livelihood of people, after 2003 Indo-Pak ceasefire (Schaffer, 2005) and declining over time insurgency (SATP, 2012). With these improvements there has been a proportional increase in PSD. Noteworthy is the initiation of telecommunication liberalization in 2002, the establishment of a software technology park in 2001 with the assistance of the central government joined by a non-resident Kashmiri and an American entrepreneur (Schaffer, 2005) and minor progress in the banking sector and hotel industry (MacAskill & Pradhanm, 2012). These developments have contributed to employment generation in both rural and urban areas and have shown reduced levels of threat of conflict to investors. While it is now argued that investing in Kashmir is no longer a roll of the dice (Ibid), considering the prolonged crises of the region, basic security is going to be an issue until a political understanding is reached (Schaffer, 2005). Such insecurities need to be addressed through an inclusive and conflict sensitive approach where a business-friendly legal framework and assurances against threats are in place for all investors.

With regard to the predatory elements of private sector investment, the region has extensive natural resource richness in both non-extractive and extractive sectors such as hydro-electricity, agriculture and horticulture, tourism, handicrafts, pharmaceuticals, minerals, petroleum and forestry (Schaffer, 2005; Rangarajan, et al., 2011). This resource richness, with prolonged regional fragility can create possibilities of PS predation as experienced in the case of some of the FSs earlier in this paper. While it is clear that in a conflict situation expectation of neutrality from private investors is marginal (Anderson, 1999), at the same time it is strongly argued that, 'there is no economic ideology other

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than one rooted in the movement of capital and competition which has succeeded in getting the greater number of people out of poverty, in the fastest time' (Dambisa, 2010: 154). Hence, the choice is not between 'Yes or No?' of PSD, but properly regulated PSD with minimized costs and maximized benefits. Considering these conditions a viable option in the region is to facilitate initial investment in the non-extractive sector, while being sensitive to the local conflict and then decide further extension based on initial achievements and the available possibilities.

The much clearer obstacle that has been daunting all PSD initiative in the region is a weak system of governance and economic policy. In the arena of economic policy the region lacks proper incentives, investment subsidies, infrastructure, a comprehensive regulatory framework and adequate resource input (IBEF, 2010). The demolished infrastructure of the 1990s has not been completely rebuilt (Ali, 2010), and fewer efforts are taken in creating new ones. The lack of financial security is a threat to overall PSD, in particular it has constrained the local businesses (Habibullah, 2004). While the regional industrial policy of 2004 has put in place a few credit subsidies and tax benefits, 'these incentives didn't make much difference because investors are not reassured about their business prospects and the security' (Schaffer, 2005: 22).

The issues in governance are more pressings than economic policy gaps, in fact the weak governance system adds predominantly to the narrow economic policy. Throughout the history of ICK both regional and national regimes have been corrupt and have manipulated the conflict and people of the region for their own political and economic interests. The National Conference's (NC's) single

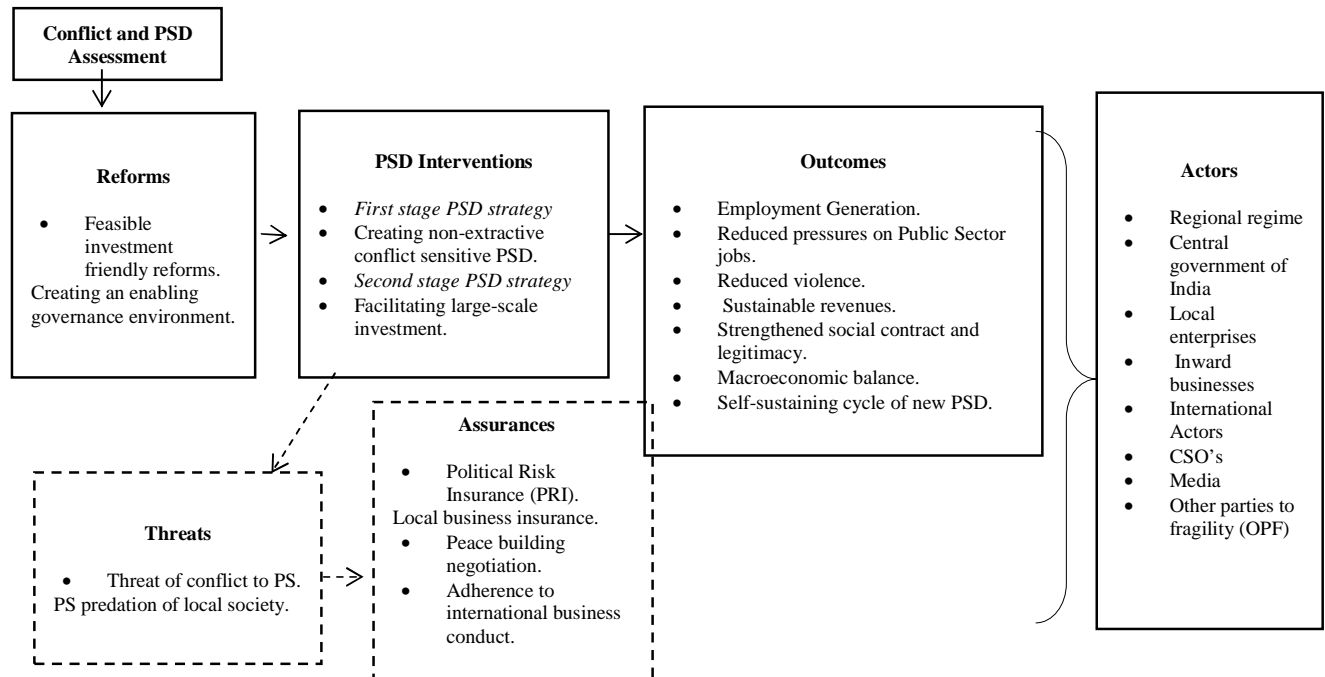
rule from 1947 until 2002, in particular, has rooted large-scale corruption and nepotism (Ibid). With post 1990's eruption of large-scale unemployment and public employment dependencies (Ibid) the filling of limited available jobs strengthened the practice of elite connections and nepotism (Hussain, 2012) and sustained the tolerance of corruption (Schaffer, 2005). Further, with the exacerbation of regional financial problems since peak insurgency 100% of its budget has been financed by the CGI, with only 20% pay back (Habibullah, 2004). With decreased insurgency, such budgetary dependency could have been reduced through the strengthening of PS and PS taxation in the region. However, due to the hierarchy of political motivations and misguided planning the region has been in continuous financial debt, evident from an outstanding of Rs. 31272 crore in the financial year 2010-11 (Tak, 2012). The existence of such policies since the 1947 partition has been dissuading major business and [other international actors] from investing and tapping the human capital of the region (Habibullah, 2004).

To address both the issues of weak governance and poor economic policy facilitating, an enabling governance environment and feasible PSD friendly reforms are indispensable (Mills & Fam, 2006). Without such systems a stable and extensive PS investment cannot be facilitated in the region.

5. Facilitating an inclusive approach to PSD in ICK

The complexities reflected in all the three debates mentioned above have created diverse ways of approaching PSD in FSs, with little effort towards a comprehensive framework. Considering these complexities, along with the contextual geopolitical and socioeconomic challenges to PSD in ICK, a framework is proposed below, which addresses

these issues in a holistic way, in order to facilitate an inclusive and conflict sensitive PSD.



To reduce the assumptions and make PS interventions more targeted *in-depth conflict and PS assessment* is imperative. This includes detailed analysis of the local processes such as geography, history, knowledge systems and the political economy of the region. Once the assessment has taken place the next stage is to make *feasible reforms within the system of governance and economic policy*. As explored earlier, that both these systems have gaps in ICK, hence their strengthening should be parallel to each other in order to smooth the path to PS development. The existing economic policy needs to go beyond its narrow focus towards incentives for both local and inward investors. In addition, a

comprehensive regulatory and legal system governing commerce and the consumer have to be in place and functioning properly. This includes: clear, soft but properly regulated entry and exit procedures, especially the ones related to land lease and its extension issues, ease in marketing, labour protection and regulation, quick and transparent mechanisms of dispute resolution and multi-level monitoring. The licensing of micro-finance institutions alongside large-scale commercial banks is especially essential to widen the access to micro-enterprises and the rural informal sector (MaLeod & Davalos, 2008).

In addition to economic reforms, building the government's human and technical capacity at all levels and in all areas is also pivotal to enhance PSD policy traction (Mills & Fam, 2006). The regional regime's strict adherence to the accountability and transparency measures such as the existing Right to Information Act and widening of a 'recent E-governance initiative' (IBEF, 2010: 44) will strengthen democratic processes by removing the endemic corruption and clientelism at the institutional level. Furthermore, in the current system of state-region dichotomy, the revival of centre-regional relations by delivering ownership of investment decisions to the regional regime, while CGI takes a facilitative role, is critical for both regional regimes' productive functioning and unobstructed PSD in the region.

These reforms and other mechanisms will clarify and strengthen the basis from which facilitating conflict-sensitive *PD interventions* in a non-extractive sector will be feasible. Considering the pressing need for quality infrastructure in the region (Schaffer, 2005; Chandhoke, 2005) the first priority for government and donors is to fund construction and reconstruction of essential infrastructure and to

organise 'indigenous drivers' (local entrepreneurs) (UNDP, 2008: 49) in cooperative enterprises with subsidized capital and business development funds. Second, in order to remove the tendency of focusing on just a few business practices, market development and a value chain approach should be adopted. Owing to a huge export potential in the region (Habibullah, 2004; Singh, 2004) the diversification of cooperatives towards export orientation can remove the tendency of new entry driving down profit among traditional non-traded retail industrials (MaLeod & Davalos, 2008). Finally, the inward actors and investors can either network with local businesses or set up direct ventures in non-extractive sectors. Initially, in order to reduce their possibilities of hijacking local markets or government systems, or creating conflict entrepreneurs, a public private partnership (PPP) is a more suitable model. As mentioned earlier, such experiments have already started in IT and the hotel industry (Schaffer, 2005; MacAskill & Pradhanm, 2012) and these can be further extended to other sectors of horticulture, agriculture, manufacturing, insurance banking and small power plants.

In the long-run this first generation local and inward investment will create the ground for larger-scale PSD, which can be facilitated once well-functioning businesses and governance regulatory systems are in place.

As mentioned earlier the threat of conflict in the region has reduced, but owing to the persistent nature of fragility, some strategic *assurance measures against expected threats* of conflict to PS, and of PS to local society are necessary. The provision of 'political risk insurance' (PRI) will not only strengthen inward PSs confidence, but will also minimise the risk of their breaching by the local regime and sustain their

interventions. While the local PS does not fall within the scope of PRI (Peschka, 2011), facilitating regional level PRI, and investing in insurance banking by inculcating a culture of insured local businesses will increase the security of local PS as well as extend the scope for more employment. The continuity of peace building negotiations, especially the continuation of ceasefires adds a lot to the stability in lives as well livelihoods. These efforts need to be continually strengthened so that a feasible PS investment ground is created even in the peripheries of the region. Moreover, assuring adherence to international business conducts such as the UN Global Compact and Equator Principles from investors will minimize their social and environmental costs and create a symbiotic PSD (UNDP, 2004).

In the form of *outcomes* this comprehensive approach will bring multiple dividends. It will create extensive employment opportunities and will therefore reduce pressures on public sector jobs and related practices of corruption and nepotism. In addition, the sustainable revenues from PS taxation can enhance investment towards the fulfillment of social development goals (SDGs) (UNDP, 2004) such as education, health, and welfare benefits. The fulfillment of these SDGs can further contribute to the overall human wellbeing and society-state social contract. In the long run, the benefits from monetary and trade flows can also address the macroeconomic imbalances mainly the region's long standing financial dependency and deficit and will generate large-scale investment opportunities for both local and inward investors.

The functioning of this framework is very arduous, unless *multiple-stakeholders* are not acknowledged and included in the policy process. The *regional regimes and CGI* are key actors whose political will and commitment is instrumental

in the overall success of this policy process. As *International actors* have been very effective in facilitating PSD in FSs, their access to [ICK] will mainly contribute to the overall physical infrastructural development and human and technical capacity building of civil servants and entrepreneurs. They will also act as a vital link between inward and external investors (Sweeney, 2008: 36). The regional *civil society organizations (CSOs)* are needed to facilitate and advocate for poor and vulnerable groups to participate in the PSD process, provide localised inputs, and trace the predatory side of PSD. The Private Sector itself: *local businesses and inward investors* have common, as well as differential priorities and interests. Both of them need a space at all levels of policy process to dialogue and negotiate (USAID, 2009). Though *other parties to the fragility (OPF)* are not direct stakeholders in the PSD policy processes they are politically significant in keeping it going, especially keeping the present border ceasefire standing and facilitating continuous peace negotiations (Schaffer, 2005). Finally, the *media* has a great potential to contribute if it changes its attitude from portraying only the negative happenings of the region, which scares investors, towards reflecting on the business prospects of the region and acting as a watchdog by keeping an eye on the on-going progress and any harm done by such development.

6. Conclusion and Policy Implications

Seeing ICK's under-nurtured private employment sector through the lens of a FS discourse has helped to unpack its underlying interlinked challenges. No doubt, the threat of conflict to PSD has reduced in the region, and the threat of PS to local society is not yet manifested, but giving due attention to both of them, along with the issues of weak

governance and limited economic policy, is very instrumental in creating a conflict sensitive PSD in the region.

While the study borrows a lot from the FS discourse. It puts forth various implications for understanding a fragile situation, and PSD in such a situation and proposes a framework 'an *inclusive approach to PSD*' to facilitate a systematic and sustainable PSD within these situations. First, the way in which fragility is defined in a particular situation influences the thinking and direction of PSD. Therefore, it is important to move out from the fixed or limited categorisation of FS, or FR to a more localised approach, which is based on historical socio-economic and geo-political processes and current situations of a particular region or a country. *Second*, the portrayal of conflict being the main barrier to PSD, as in the case of ICK, can often be misleading. The PSD can remain crippled, even when the threat of conflict is minimized, because the gaps in governance and economic policy are equally undermining. Hence, the adaptation of an '*inclusive approach to PSD*' in FRs like Kashmir is helpful to move beyond the unilateral policy approach, towards identifying and understanding multi-dimensional aspects of PSD and targeting them cautiously. The approach is a whole of subsystems, which believes in the process of careful *analysis of contextual socio-political and economic processes*, followed by *feasible economic policy and governance reforms*. While the assessment and reform measures will create a healthy environment for *conflict sensitive PS interventions*. With protection against various expected *threats of conflict society to PS, and vice versa* and *multi-stakeholder involvement*, these PS interventions will not only generate extensive employment by reducing public job sector pressures, but will also make policy process more participatory and sustainable. In the long-run such a functional system can create large-

scale investment and employment opportunities coupled with the region's socio-economic and political stability.

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