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For a New Economics of Resettlement:

A Sociological Critique of the Compensation Principle

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Abstract

Many development projects intended to alleviate poverty end up increasing poverty by displacing large numbers of people without reestablishing them viably, despite the use of compensation payments for assets lost. This paper appreciates the contribution of economic science to matters of compensation. However, it also subjects the theory of compensation to critical scrutiny and deconstructs the current practices of compensation to highlight their fallacies, distortions, and unsatisfactory outcomes. In particular, the paper critiques:

(a) the economic theory that predicates the socio-economic recovery of those displaced only on the principle of compensation for asset losses;
(b) the resettlement policies that tolerate an internal mismatch between policy objectives and policy means; and
(c) the methodology that planners often employ in appraising projects with resettlement, which is inadequate to the task.

The author argues that the magnitude of the combined material and non-material impoverishment risks and losses experienced by those displaced far exceeds the redeeming powers of narrow compensation-centered solutions offered by conventional economics. He identifies a structural incongruity in policies which define their goals as improving or restoring resettlers' livelihoods, and rely only on compensation as the virtually sole means for achieving either of these goals. The paper outlines several basic limitations and flaws in compensation that reinforce the main poverty risks inherent in forced displacements, as demonstrated in the author's analytical model of impoverishment risks and reconstruction (IRR) in resettlement.

To complement compensation for damages and make the policy goals in resettlement achievable, targeted investment financing channeled to those displaced is necessary as part of the regular development projects' investments. The author argues in favor of a shift from the "economics of compensation" towards an "economics of resettlement with development", that will pursue the final goal of affected peoples' sustainable reestablishment rather than be focused narrowly only on compensation delivery, regardless of final overall recovery. Additional investment resources for resettlement with welfare improvement can be secured in several ways, outlined in the paper, often through equitable sharing of the project-generated benefits with those displaced.

Biographical note

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Michael M. Cernea

Central in the socio-anthropology of population displacement is the impoverishment of those displaced and the options for resettlement with development. Several basic questions are now of increasing concern to many governments, to development agencies, and to the public at large. Why does development-induced displacement so often cause impoverishment? How can resettlers' basic rights and entitlements be protected and their impoverishment be prevented?

Displacement: a perverse companion of development

Many development projects that aim to reduce poverty by building new infrastructure, industrial platforms or irrigation systems, or even establishing parks and road networks, also cause forced population displacements because they need land and "right of way". Such displacements are one of the most perverse social pathologies of induced development.

After having long been dismissed as occasional "secondary effects," involuntary displacements have now come to be widely recognized as a major economic, ethical, and political problem in induced development. This perception shift is explained by several factors: displacements' size; frequency; catastrophic poverty effects; social research findings; and no less, the rising combativity of those displaced. Numbers are staggering. In India alone, more than twenty million people were forcibly displaced by development interventions between 1950 and 1980; of these, 75% -- that is, 15 million people—have ended up *worse off* than before resettlement (Fernandes, Das, and Rao, 1989). In China, no less than 40-45 million people have been displaced over fifty years (1950-2000). Chinese self-estimates, for instance, indicate that out of more than twenty million people displaced by water and dam projects alone, just about one-third were "resettled well"; of the rest, one-third were resettled only "so-and-so" and one-third were resettled "not well"(Shi, Su and Yuan, 2002). Some individual large scale projects may each displace tens or even hundreds of thousands of people.

Because displacements are such a costly development pathology, efforts are being constantly made to avoid them. Indeed, certain project-caused displacements can be fully avoided, for instance, by optimizing technical project design. In other cases, project-generated displacements are so badly conceived that the projects that cause them should not be allowed to proceed. But assuming that, ideally, all badly conceived projects were preempted, and that all avoidable displacements could be avoided, would the need for displacement disappear? Unfortunately, not. There would still remain many programs that are vastly beneficial and indispensable overall, but which would also entail some unavoidable population displacements and relocations, with their likely chain of dire consequences.

Furthermore, the need for such projects is not passing with time. This need is a regularity of development. In my estimate, it is more likely that the frequency of displacements may increase, even if their magnitude will be kept in check better. Demographic growth, urbanisation, and the inelasticity of land will continue to require changes in the current use-patterns of lands and waters. This guarantees that the displacement problems will remain a permanent issue on the development agenda.

If the need for some projects that entail relocation cannot be avoided, can something be done to prevent their destructive, impoverishing effects? The response, as I will argue further, points towards changing the economic concepts and analytical methodologies that govern how displacement is planned and implemented, and how resettlement is financed. Without correctly understanding the severe impoverishing consequences of displacement, the inequities between gainers and losers from such projects will be surely amplified and perpetuated: more than a few displaced people will end up *worse off*, poorer than before the project. New poverty will take root under the wings of programs that aim to reduce pre-existing poverty.

Some critics of current displacement practices propose a "remedy" that is unfeasible and counter-productive: they call for renouncing *all* development projects that entail resettlement, however justified these projects are on development and poverty-reduction criteria. This is a conservative, untenable proposition. Should such projects not be carried out, their developmental and poverty-reduction benefits will not occur either.

Therefore, the stark choice is: should the cost of reducing poverty for some be paid by impoverishment of others? Or, can ways be found to eliminate or reduce impoverishment through displacement?

This concern for preventing impoverishment brings us to the key issue of compensation, the subject of this paper. Compensation is the usual operational "remedy" employed universally as a means of restitution for project-caused asset-dispossession, economic disruption, and income loss. *But is this instrument capable of performing the function attributed to it?*

The same question gets heightened relevance if elevated to the policy level. Policies on involuntary resettlement define as their objectives to improve or at least restore resettlers' prior livelihoods and incomes. "Improving or "restoring" are *two distinct goals*. Yet, for achieving one or another of these grand goals, these policies prescribe as *the basic means* -- the payment of compensation for lost assets, at replacement costs. We thus arrive at the *fundamental question that must be asked frontally* at the policy level: *Are goals and means correctly matched within* *resettlement policies themselves*? Is this policy means capable of delivering the intended policy goals?

If the answer is affirmative, and if the means are indeed applied, projects with resettlement will not any longer create gainers and losers, but rather only gainers. The challenge would be only to correctly implement these means, for achieving the desired goals. But if the means, *horrible dictu*, are not up to the goals, then even the best implementation of insufficient means cannot achieve the pursued goals.

Notwithstanding the criticism that can be leveled at the inefficiencies of compensation -- and considerable criticism will be expressed further -- it must be unambiguously stated from the outset that compensation is not just important in resettlement, it is indispensable: full compensation for losses is one of resettlers' rights and entitlements. Yet in the practice of resettlement, despite compensation, most resettlers end-up worse off and impoverished. Unfortunately, mainstream economic theorists do not revisit the thinking upon which loss evaluation and compensation are based, and impoverishment effects are allowed to continue.

In this paper, we will explore the links between goals and means in resettlement, focusing on compensation as both principle and practice. We will and we will also extend the discussion from compensation to the broader issues of resettlement economics.

Critique, Convergence and Divergence

In two recent books -- *The Economics of Involuntary Resettlement* (Cernea 1999), and *Risks and Reconstruction* (Cernea and McDowell 2000) -- I brought up the economic inconsistencies in dealing with resettlement explicitly to the attention of my colleagues-economists (immediately those at the World Bank, but more broadly the development economics profession at large). Crossing disciplinary boundaries, I expressed an invitation to development economists to critically reexamine the economic thinking and methodology that guide resettlement operations in projects. My own critique placed into discussion: the weaknesses of compensation theory and practice; the arbitrariness of valuations of losses; the inadequacy of the cost-benefit analysis (CBA); and the absence of distributional analysis in projects with displacement.

To address these difficult issues, I called upon "the expertise of *professional* economists (since) a solid economic methodology is indispensable for resettlement projects….". That call emphasized that "the economics of resettlement….holds generous promise for research and for consistent translation of knowledge into long overdue analytical tools" (Cernea 1999, pp. 13, 25).

There has been little response from economic quarters so far. The same methodologies continue to reign by inertia and cognitive dissonance, despite the feedback from practice.

However, in a recent international conference at Cornell University (November 2001), a leading development economist, Ravi Kanbur, joined this debate and directly responded to some of the issues outlined above (see Kanbur's paper in this publication, and also Kanbur 2003). Kanbur takes as his conceptual grounds the Raceto's improvement principle – its change-justification and ethical implications—applying it to projects that cause involuntary displacements. From these grounds, he rightly states: "…whether to go ahead with a project which creates losers as well as gainers even after attempts at redress, often to those who have been displaced…has to be a central question in development analysis and policy." Kanbur readily admits that the position of economic science on compensation "is a position often critiqued by other disciplines." To dispel underestimation, Kanbur undertakes a respectful walk through the history of economic thinking, demonstrating convincingly "how economics has struggled mightily within itself to arrive at a position" on the theory of compensation. This theoretical retrospective begins with Pareto's improvement principle and ends with a recent (1999) discussion by Stiglitz, who favors a cost-benefit-analysis using weighted sums of gains and losses according to an equalitarian scale. We readily agree that Kanbur's demonstration is convincing *as far as the type of losses* historically addressed in past economics are concerned. But one of the key questions was not asked in Kanbur's paper: the question of whether the type of massive, simultaneous and near-total dispossession of assets of many people of their productive and income-sources, characteristic in forced displacement, is of the same nature with the situation previously considered in economics, and thus prone to the same remedy.

Even without asking this question, however, Kanbur ends his analytical retrospective with open dissatisfaction, concluding that the development economics position has not tested out successfully: "This way of doing things does not seem to have panned out in practice, especially in the context of development projects" (Kanbur 2003).

Indeed, it has not. And crucial in Kanbur's conclusion is the specification about ineffectiveness *"especially in the context of development projects."* This "project context" together with today's "policy context", are to me of primary interest.

For such projects that entail displacement, Kanbur recommends a big policy step forward over the traditional granting of compensation, a step that is ahead of mainstream development economics: given inefficiencies in compensation, he suggests not just reinforcing the use of weights in project appraisal or CBA, but also proposes that compensation mechanisms be complemented by the introduction of "generalized safety net" measures.

There are at least three important points of convergence between my and Kanbur's discussion of compensation. First, we agree that direct compensation mechanisms are necessary, should be employed, and should be improved. When displacement and its entailed losses occur in projects, compensation performs a prima facie positive function. Second, there is convergence and agreement that compensation mechanisms are not able to fully do the job, that reliance solely on these mechanisms is tantamount to depriving resettlers of part of their due, and that correctives or supplementary resources need to be introduced. Third, that the absence of explicit equity criteria, resulting in the creation of gainers and losers from the same project, the absence of a distributional perspective, and the un-weighted ways in which cost-benefit analysis is routinely practiced, obscure project-induced inequities and allow impoverishment to occur.

The introduction of generalized safely nets in addition to compensation would certainly add an important lever for enabling resettlers to overcome the risks of impoverishment. As Kanbur suggests, such "redistribution mechanisms and safety nets (would) come to the fore to complement project-specific compensation… would prevent destitution as the result of a project on which compensation was not paid" (2003). This recommendation may turn out to be seminal. It deserves to be explored further. Operational questions are: how to design such safety mechanisms, whether they are politically feasible and practicable, and how can they be included in resettlement policies. We can only agree with Kanbur's call that: "a joint theory of project-specific compensation and generalized automatic safety nets now awaits development" (2003). How to design safety nets as germane measures to remedy the in-built limitations of compensation, needs, of course, to be explored further. The definitions of eligibility and of amounts are complex matters. Delivery mechanisms would raise additional questions. But the need to fill in the gaps uncovered by compensation alone makes it necessary to face these usual difficult question linked to safety nets.

Yet besides our essential agreement with Kanbur's analysis, on several issues our argument diverges from his, not disagreeing but rather following a different logical path.

First, our critique of the compensation principle is more severe. We argue that compensation is *structurally* unable to resolve the task of restoring incomes and livelihoods to where they would be in the absence of forced displacement. Because of the very nature of compensation, it is doubtful that even with additional safety net measures, however useful these may be, compensation means could fulfill the functions and burden that economic policy and theory assign to it in restoring and improving pre-project livelihoods.

This inconsistency is compounded by the use of un-refined project economic analytical techniques. These techniques, in turn, being confined to compensation as the lone economic remedy, prevent the realistic financing of resettlement: they fail to lead to the allocation of commensurate resources for post-displacement reconstruction, rationalize under-financing, and contribute to project-induced impoverishment.

Furthermore, while Kanbur addresses only the theory of compensation, our attempt is to take the critique beyond this theory and pursue the argument several steps further than compensation itself. The issue at stake is much bigger. We believe that the debate must be elevated to the level of policy and must also be extended to the broader area of the economics and financing of resettlement. The need to arrest impoverishment creep under unsound resettlement calls for re-examining the overall approach to resettlement and specifically two of its building blocks: the congruence between policy goals and means, and the economic/financial basis on which resettlement operations are predicted and planned.

The ultimate policy objective in involuntary resettlement – as adopted by some governments and by agencies such as the World Bank, the Asian Development Bank, and OECD countries' aid agencies -- is to resettle with improving or at least restoring[1] the income and livelihood levels of those displaced. The policy premise is that full compensation at replacement cost for assets lost would be adequate to achieve the goal. In light of the many lessons learned in recent years, we argue against this entrenched assumption as being unwarranted and confined. Logical/historic analysis (as done by Kanbur), as well as massive bodies of empirical evidence accumulated over the last two decades defy the assumption about compensation as panaceum.

Because of this incomplete match of means to goals, the goals of improving incomes and livelihoods are inherently destined to remain most often unreachable. Anticipation on the next parts of this paper, we argue that what is necessary to help lift the displaced people *above* their pre-project livelihood levels, in our view, is **investment financing.** By its nature and functions, investment financing is a different development tool than compensation. Development-oriented investments must be used as a <u>supplemental means</u> over and above compensation resources to match the policy goals in resettlement. At the conceptual level, this requires shifting from the current compensation-centered economics of resettlement to an income-improvement centered economics for achieving resettlement with development. Why this is necessary will be explained further.

The sociological perspective

[1] "Restoring" and "improving" livelihoods are two different levels in the policy objectives. Obviously, restoring at pre-project levels, when those levels were poverty levels, is a minimal objective, and entails moral hazards, yet even this simple "restoration" is not accomplished in many resettlement processes. "Improving" requires a different strategy and more resources.

Returning to Kanbur's analysis, it is now our turn to respond to one of his questions. Indeed, after expressing dissatisfaction with the "conceptual compromise" in development economics on the distribution of gains and losses in the case of displacement, Kanbur is loyal to his belief in interdisciplinary compensation (2002) and tosses the question back: "How would other disciplines respond to the same challenge?"

Sociology and anthropology are the two disciplines with the longest history of research on forced displacements. Their empirical findings have led to understandings and theorizing that cast indeed a different light on displacement and recommend alternative responses.

Anthropological research on development-caused involuntary displacement has a distinguished intellectual record. From its beginnings it has covered sites located in both developed countries (Richardson, Herbert Gans, a.o) and in developing countries (Roy Burman, Scudder, Colson, Mahapatra, Fahim a.o). Early investigations were followed by a spectacular explosion of research in the 1980s and the 1990s (see bibliographies by Guggenheim 1994; Rodrigo-Lin and Maninder Gill, forthcoming 2003). Sociologists from developing countries, particularly India, Brazil, China, Mexico, Egypt, and Nepal, have added richly to the literature by reporting the displacement effects of many development projects, and by making policy recommendations.

This research has brought back, time and time again, a very critical and empirically substantiated challenge to the "compensation principle" in situations of mass displacement. Perhaps the most frequent common finding in early resettlement studies (too many to be listed here: see the resettlement bibliography by Guggenheim (1994), and Lin Rodrigo and Gill, (2003) was precisely the finding that compensation – for a multiplicity of reasons, both intrinsic and extrinsic to compensation – simply was not able to genuinely compensate and secure the productive and enduring reestablishment of those displaced. Recent resettlement research continues to bring new confirmation to the same conclusion (Nayak, 2000; Prasuranam, 1999; Guha 2001; König and Diarra, 2000; Kibreab, 2000; Bhattarai, 2001; Schmidt-Soltau, 2002)

The dominant, most important and universally corroborated finding has been that in developing countries a vast number of displaced people have ended up worse off, poorer than they were before development projects displaced them. These outcomes fly in the face of official development discourse. Can it be that compensation was not delivered in all these impoverishing projects? Not at all. Research has reported compensation as an universally applied “remedy”, but also as universally insufficient and inherently prone to distortion.

We will detail further the sociological perspective on the compensation principle and practice under two headings: the faces of under-compensation and the impoverishment risks imposed on displacees.

The faces of under-compensation

It is first necessary to reach clarity on the very nature of compensation payments and on the functional difference between them and development investments.

Compensation is not a new investment. The function of compensation in projects is not the same as the function of investment made in new infrastructure: the function is damage substitution. Simply put, compensation only returns to the displaced people something that was taken away from them. By definition, it does **not** provide them with anything more than simple repayment, that is with nothing above what they had before. (Most often, as we shall see, it provides them with *less* than was taken from them, but for a moment we leave this aspect aside, and will return to it a bit further). Being even at its upper limit, theoretically, no more than the equivalent of what those uprooted had before and were forced to lose, it cannot be argued that by some miracle compensation can produce an improvement in livelihood levels compared to pre-displacement levels. Thus, as a policy “goal”, improvement is practically born dead.

Compensation is delivered usually in cash, and sometimes in kind. When it takes the form of cash, it transfers upon those displaced all the risks related to the market-use of cash for acquiring replacement assets. These severe risks are well known.

Evidence demonstrates irrefutably that the purchasing power of cash compensation typically ends up being less than necessary to repurchase the assets lost (even if compensation is paid at replacement costs). The transaction costs, the production time wasted, the start up costs of a new productive activity, etc. are also to be born from the same “compensation”, further eating down into its effective value. These factors subvert replacement at par. Various cultural pressures and immediate needs often divert fractions of the compensation proceeds away from asset replacement. Land markets are often limited, prices go up under sudden demand, and the worth of compensation goes down. In other words, the practical effectiveness of compensation as a restorative instrument is hobbled.

Social research has generated also another huge body of empirical findings that reveals the **practical** limitations of the compensation principle. This evidence shows that compensation as a remedy tool is vastly impaired by its extreme vulnerability to administrative distortion, twisting, subtraction. The most frequently reported forms of under-compensation (and implicit externalization of costs) as a result of this vulnerability are:

- Undercounting of condemned assets for which compensation is due, and thus not paid (Parasuraman, 1999; Mahapatra, 1999)
- Arbitrariness and market-defying subjectivity in the valuation of assets, with consequent partial- or non-replacement of lost assets (Nayak, 2000; Ota and Agnihotri 1996);
- Un-recognition of non-physical losses, difficult to measure, and failure to account for non-market income and costs (König and Diarra, 2000; Pandey, 1998)
- Under-compensation resulting from the late disbursement of compensation to those who are left assetless for an unacceptable time period (Mahapatra, 1999; Guha 2001; Gibson 1993);
- Subtraction by corrupt officials of part of the compensation money before it reaches those rightfully entitled (Maybury-Lewis, 2003; Parasuraman 1999);
- Under-compensation because of lost consumer surplus from existing assets (Pearce 1999);

- Preemptive exclusion of some common assets from consideration (Kibreab, 2000; König and Diarra 2000; Schmidt-Soltau 2002);
- Asset-price upward changes occurring after the determination of compensation, which diminish the purchasing power of compensation recipients (Downing and Garcia-Downing, 2002); and
- Recipients unaccustomed to handling cash tend to misdirect compensation money and are soon left both assetless and cashless (Mahapatra, 1999; Nayak, 2000; Hakim, 2000;).

It is fair to ask: Should the economic theory that legitimizes the "compensation in principle" be faulted for the distorted administrative application of compensation tools by incompetent or corrupt officials? The answer, obviously, is negative. Yet, when a tool that seems powerful in theory turns out in practice to be weak, and prone to chronic flaws, the theory surely cannot remain aloof, indifferent to feedback. There is a scholarly and ethical responsibility to search for and recommend alternatives.

How Arbitrary Can Compensation Get?

An explosive four-day standoff took place in August 2002 in the small town of San Salvador Atenco, Mexico, as a result of plans to expropriate land and displace local farmers for building a new airport for Mexico City. The Government-sponsored airport project had offered farmers an arbitrarily-set low price as compensation for the 3000ha earmarked for expropriation. For about a year, affected farmers have been resisting compensation and displacement. *No consultation about compensation rates had been initiated with the villagers.*

State officials rejected the farmers' protests and, instead, sent in the police, who arrested and imprisoned ten of the farmers' leaders. The villagers responded by the thousands: they demonstrated, blocked a nearby four-lane highway, and took fifteen officials hostages, threatening to kill them unless their leaders were freed. The stand-off lasted four days and grabbed headlines in the international press, greatly embarrassing the Mexican Government. After four days, the police freed the farmers' leaders, and farmers released their hostages. Realizing that under-payment will not work, Government authorities recalculated the compensation and suddenly announced a huge—700%-- increase of its original offer. At this point, however, the antagonized farmers declined. The Government announced the cancellation of the airport project.

Many aspects of this case deserve analysis, but most relevant to the argument of this paper is the arbitrariness of the compensation calculations. Both the initial low compensation and the subsequent seven-fold increase suggest how – despite claims to objective valuation – in practice, subjectivity prevails. In this case again, it was twined with a transparent attempt to externalize costs. Had the farmers accepted the initial compensation offer, impoverishment would have been certain.

The inefficiencies and incompleteness of compensation are implicitly recognised in practice when some countries introduce patchwork "repairs" intended to compensate for the defects of compensation in displacement. These repairs take the form of ad-hoc "grants" or "allowances", payable to displaced people over and above the compensation. For instance, in India there is a "solatium grant", which derives its name from the concept of "solace". It is given to help overcome the intangible hardships entailed by displacement, but it is practiced haphazardly, with vast and subjective differences from state to state, project to project.

Sometimes, the amount and number of allowances or grants, or even the valuation of assets for compensation tariffs, are subject to a negotiating process between affected people and project or government authorities. When such negotiations and arbitrations are conducted fairly, compensations are often enhanced, approaching replacement costs. Yet most often the weakest communities, may get the least, because their weakness reduces their bargaining capacity – an essential flaw in compensation systems which are not regulated by law. The happenstance practice of such grants can be seen, in my view, as one more reason in support of Kanbur's recommendation to introduce generalized safety net provisions.

Manipulating the Right to Compensation

Some project authorities often try to diminish or deny legitimate compensation entitlements, thus directly subverting development ethics, policy and law. One instance of such unethical manipulation in India was described by Maybury-Lewis (2003).

Under Indian law, tribal groups and scheduled castes are entitled to special consideration and compensation when displaced. The administrators of a major project, however, wanted to reduce the compensation payments. One way to do this was to deny the tribals their claim to tribal status. Indeed, the author did so, claiming that they can notice some Hindu features in the tribal culture and these were not real tribals and therefore were not entitled to full compensation. This was *"an instance driven by an interest in cutting compensation costs, rather than by a subtle understanding of cultural similarities and differences."*

David Maybury-Lewis (2003)

There is a vast gap between what the current economic methodology produces for determining compensation, on the one hand, and the cumulative losses plus re-establishment costs incurred in real life by displaced people as a result of expropriation and relocation, on the other hand. Because this large gap is not covered in project economic methodology, resettlers suffer multiple deprivations. This gap is also unregulated by law and rights-protection policies. This supports my argument about the need to go beyond compensation and articulate a more complete "economics of resettlement", fully placing in the service of the resettlement policy's declared *objectives*. The goals of a policy should be taken as the logical guiding compass for the economic reasoning developed towards applying that policy. When policy goals become the tone, compass, the question to be asked will change to: *what array of economic and financial means, and what set of indicators and analytical techniques, must be mobilized in order to reach the policy goals of improving resettlers means and livelihoods?*

The Impoverishment Risks in Displacement

The losses and inequities that are not covered by compensation become starkly visible through their consequences: the impoverishment of most resettlers. There is a specific and dramatic structure to the poverty effects germane to forced displacement[2]. For this, I will refer to a research I undertook to **identify regularities** in the displacements' outcomes.

Submitting empirical data reported by many researchers worldwide to a comparative analysis, we distilled a "model" of basic impoverishment risks recurrent in displacement; we also defined the counteraction strategy needed to match, contain or mitigate these impoverishment risks

2 The empirical material supporting this model cannot be reproduced in the present article. For a detailed presentation of the Impoverishment Risks and Reconstruction (IRR) Model for resettling displaced population, see Cernea 1997, 2000. See also the book-length study by Mahapatra (1999), who tested the IRR model through a vast secondary analysis of empirical findings available in India's resettlement literature; see also studies by Downing 2002; Kibreab 2003; Pandey 1998; Guha 2001; Schmidt-Soltau 2002.

(Cernea 2000). This model unbundles the syncretic, multifaceted process of impoverishment into its primary components. Evidence reveals the following fundamental and recurrent risks: (a) landlessness; (b) joblessness; (c) homelessness; (d) marginalisation; (e) increased morbidity and mortality; (f) educational losses; (g) food insecurity; (h) loss of common property; and (i) social disarticulation (Cernea 1997, 2000).

Before forced displacement actually begins, these processes can be defined only as *impending* risks – risks of losing property, civil rights, and identities. But if preventative or alternative counteractions are not initiated, these potential hazards become actual losses and the hard realities of impoverishment. The cumulative effect of these processes is the decapitalization of resettlers, the rapid onset of multidimensional impoverishment or the aggravation of poverty for those already poor.

The intensity of each impoverishment risk tends to vary depending on local conditions, population group, type of project, or type of displacement. Outcomes range in severity. But in most cases, empirical research found chronic impoverishment well entrenched even long after, and despite of, the payment of compensation. This tells us that -- in case after case after case – compensation came up short and was unable to prevent impoverishment. If resettlers become worse off, it is nearly always an indicator that project costs have not been properly internalized. They were transferred on to resettlers who end up poorer than they were before the project. The principle of compensation and the practice of compensation have not proven capable of preventing cost externalization.

Resettlers' losses in income, assets, rights, are multi-sided – economic, social, cultural, in cash and in kind, in opportunities, in power. Resettlers lose not only natural or man-made physical capital but also human and social capital, through the unraveling of patterns of social organization and of mutual help networks. The income lost is not only cash income, but also wealth that is psychological in nature, including culture, status, and identity.

This is how forced displacement becomes the cultural-economic equivalent of an earthquake that shatters production systems and social networks, undermines identity, and plunges those affected on a downward poverty spiral. Field studies have vividly reconstructed how displacements instill loss of confidence in self and in society and renders much human capital obsolete. Cultural effects, combined with the seizure of assets accumulated through prior generations' labor, result in the near killing of enterprise and entrepreneurship. Discouragement strikes deeply at the human ability for recovery.

These cultural and psychological pains and losses -- whose lethal combination has been revealed through perceptive sociological research – inflict in turn long-term harm to resettlers. This harm is additional to the measurable market value of the physical assets subject to compensation. We are led to conclude, therefore, that the magnitude and span of the material and non-material *impoverishment* of displacees exceed by far the redeeming powers of compensation-centered solutions.

Indeed, it is against this total process of impoverishment through displacement (not just against the loss of physical marketable assets) that the insufficiency of the compensation principle and practice appears in full light. Many of these real costs to resettlers are not even considered for possible compensation since they cannot be monetised. Other losses as well are not recognized in project economic planning. The guidelines for project economic analysis thus fail to adhere to the essence of the compensation principle. They fail to capture the full costs of dislocation and reestablishment and therefore fail to legitimize in technical-economic terms full restitution to project losers.

To conclude, the link between compensation and impoverishment is direct, in that the decapitalization of displacees is only partially repaid through compensation. For the resettlers compelled to cover this net difference out of their own livelihood, the outcome is "new poverty"(Downing, 2002). The policy message embodied in the IRR model is that the impoverishment risks imposed on resettlers can be brought under control only through an *encompassing* development strategy supported by development investments. It cannot be tamed through piecemeal measures based solely on compensation for damages (Cernea, 2000).

The case for investment: achieving resettlement with development

Perhaps the most important critique of the compensation principle's inadequacies, additional to those outlined above, is that it leaves un-addressed the time dimension of recovery. Displacement being a major set-back, it becomes necessary to finance a "catch up" effort for re-development. Empirical social research and secondary analyses have documented that forced displacements interrupt the meager growth that the pre-project communities might have experienced on their own (Scudder 1997, Mahapatra 1999). Such communities not only lose assets, but also forgo the growth which without the project might have continued. While the affected groups are set back, other surrounding communities continue their self-development path.

For the displaced people to "restore" their living to where it would have been without the project, they need to "catch up"; that is, they need to recuperate the time lost due to displacement interruption by accelerating the pace of development, achieving a faster pace than, say, the surrounding communities. But such acceleration would require a surplus in investment. The compensation, however, would only provide for past asset replacement, but not for investment that could accelerate progress to enable displaced communities to catch up for the lost time.

Analysing the income curve of resettlers after displacement, Pearce (1999), Cernea (1988, 1999), and Shi and Hu (1994) have shown that the replacement of capital through compensation (even if it were to happen in full, which as argued in this paper it never does) could secure at best the same pace of development as before. But it would not be able to overcome the time lost and thereby achieve "catch up". It is only through additional investments that the re-climbing path of re-development could become steeper and make up for the lost time relative to unaffected communities (see Pearce 1999). The resettlers fully suffer "relative deprivation" compared to their non-displaced neighbors. Unfortunately, the *principle of investing* in sound resettlement is still far from being established, either in the economics of resettlement, or in practice.

Yet, it must be said that recommending investment financing for the resettlement of displacees is not an unheard of, radical idea.

Indeed, investments of public resources have been and are routine practice in all and every single new land settlement project, when resettlers are not forcibly displaced, but simply invited to settle new lands brought into development. This has been the practice in, for instance, all land settlement projects supported by national governments in Asia and Africa over the last 40 years, many of them financially assisted by the World Bank or ADB. If it is conceivable to channel public resources for the development of resettled populations that are not dispossessed but rather endowed with new valuable assets, is it not even more logical to allocate financing for the re-development of forcibly resettled populations, subjected to sacrifices in the name of development? In fact, investment financing is a basic principle in all rank and file poverty-reduction development projects, not just in land settlement projects.

Furthermore, the argument for development investments can also rest, in many situations, on the premise that those who give their lands to the new project are in fact "investors of equity" in those new projects. As investors they are entitled to a share of the benefits. Upfront investments are nothing more than an advance on those benefits. This issue is certainly more complex and requires a broader discussion than this paper allows.

The counter argument to making investments in addition to compensation for resettlers' benefits typically invokes the scarcity of resources and competing demands. Scarcity is an undeniable constraint. But if the project delivers its benefits to some and generates losses to others, as so often is the case, one response is long known in economics (and is mentioned by Kanbur): taxing the new benefits would provide managed tax revenues, resources which can help readjust the balance between losers and gainers. Establishing project-related mechanisms for more equitable sharing of benefits can provide the resources necessary for complementing sheer compensation with incremental investments financing. This approach would surely go much farther towards making resettlers better off, not impoverished and worse off, and towards achieving *resettlement with development*.

The objective need for investing in resettlement to improve resettlers' conditions above pre-project levels is also demonstrated by comparative research between involuntary and voluntary resettlement programs. One special study was carried out in the World Bank to compare the design and financing of these two types[3] of resettlement projects (Eriksen 1999). The study led to unanticipated and paradoxical findings: in project after project, the voluntary resettlers on new lands (who were **not** dispossessed at their point of departure, but fully maintained ownership of their assets, were able to sell or transfer to relatives) were financed with substantial public investment resources, including free land, tools, tax holidays and financial incentives, often training, etc., to enable them to build a new and sustainable economic/productive basis; they were also endowed with added common property assets. On the contrary, the project components designed to support involuntary resettlement did not provide any *additional* investments to the tens of thousands of forcibly uprooted people compelled to make sacrifices and abandon their immobile possessions: graveyards, prayer houses, etc. (Eriksen 1999). Only payments for imposed expropriation were included in these projects, in the form of compensation; regarded as payment for loss only, in a zero-sum equation[4]; no financing was provided in any of the projects studied towards the additional costs of reconstruction and no investment support made towards achieving improved livelihood levels.

This different treatment of voluntary and involuntary resettlement not only discriminates and defies logic and equitability. The comparative study demonstrated that the conceptualization of forced resettlement in project design and financial provisioning has been long dominated by a non-development philosophy and a narrow economic theory.

Securing additional investments for involuntary resettlers should not raise problems different in nature than securing investment resources for financing voluntary resettlement schemes. In the

[3] The study used a simple yet ingenious methodology. A total of 18 projects financed by the World Bank in five countries (Ghana, Brazil, India, China and Indonesia) were identified and paired on a country by country basis. Each pair consists of one project supporting voluntary resettlement and one project in the same country containing an involuntary resettlement component. Appraisal reports were used for *ex-ante* data and completion reports for *ex-post* data. This is the largest set of data submitted so far to such study, and is richer than data available on projects financed from domestic sources alone. Several variables – from type of farm model, household income, and method of project risk assessment, etc. were examined. The findings of this comparative research persuasively demonstrated that in nearly all cases, the differences within the pair of projects were to the direct detriment of people forcibly displaced. Failures in involuntary resettlement were shown to originate from errors of strategy, from inadequate or absent economic analysis, and from non-allocation of targeted financing for resettlement components at project appraisal stage. The study argued that changes of paradigm and method are imperative.

[4] The zero-sum, however, is not achieved in practice, as we have argued in the previous sections, because of the various distortions that reduce actual compensation. The real net result is cost externalization and under-compensation.

case of projects that entail involuntary resettlement, the benefits of the project itself can be anticipated and counted on as a source for these investment. Similarly, Kanbur's important recommendation for introducing generalized safety net mechanisms for resettlement projects, to complement compensation.

For a new economics of resettlement

A comprehensive economics of resettlement must rest, in our view, on at least two cornerstones: compensation resources and investment resources for financing resettlers' development. Broader speaking, it must articulate the full economic rationale and the tools for achieving the overall recovery and improvement of resettlers livelihoods, rather than dealing selectively with only one or another component of the economic processes inherent in displacement and successful resettlement.

Re-examining the economic conceptualization of resettlement means several things. First, it would require economic research on resettlement processes, research that would place compensation within the *specific* economic cultural and financial canvas of displacement and resettlement processes. It also demands re-examining the set of analytical methods and techniques employed in calculating the economics and financing of resettlement operations in development projects. This implies also overcoming the limitations of wholesale CBA, and analyzing the *distribution* of costs and benefits among project stakeholders (Cernea 1999). Such redesigned economics would help create consistency between the economic/financial *means* and policy *goals* in resettlement.

In development-induced resettlement the *policy goal* is not simply to compensate for specific losses. The policy goal is broader: to enable the uprooted displacees to re-establish themselves productively and improve their livelihood. While compensation is *one* of the means to meet this objective, it is not in itself sufficient. Development oriented investment resources, over and above the compensation of condemned assets must be channeled to the resettling population, if its accelerated development is pursued genuinely. This is little recognized in development economics and in project planning practice.

A brief walk through the evolution of the policy goal in resettlement, as described in some of the most authoritative policy documents of the World Bank, tells us the following.

(1) In 1980, when the first World Bank policy on resettlement was issued, the policy objective was defined as "to restore [to their pre-project levels] and if possible improve" the income/livelihood standards of resettlers (World Bank 1980).
(2) In 1986, this policy goal was strengthened, with the important addition that dismantled production systems need to be reconstructed: verbatim, "all involuntary resettlement operations should be conceived and executed as development programmes" (World Bank 1986).
(3) In 1988, when the Bank's policy guidelines were first published by the Bank, the concept of "restoring" was explicitly defined as reaching higher than pre-project levels; that is, reaching a level that includes the growth that would have occurred "without the project" (Cernea 1988).
(4) In 1990, the policy goal was again enhanced, being defined as "improving, or at least restoring" (instead of the previous wording "restore and if possible improve") the income and livelihoods levels of resettlers. It specified further that "all involuntary resettlement should be conceived and executed as development programs, with resettlers provided sufficient investment resources and opportunities to share in project benefits". (World Bank 1990)

Two elements appear clearly: First, the resettlement *policy goal* was never defined as just paying compensation, but as a complex socio-economic reconstruction process. Second, there has been a gradual elevation of the objective to be achieved in resettlement.

Yet despite this raising of the bar through several policy stages from 1980 until 2000, there has been no re-examination of the economics expected to underpin advances in policy. Nor has these been corresponding change in the financial instruments allocated to support the higher policy goal — i.e., the partial shift in emphasis from restoration toward improvement. . The array of financial means mobilised to implement the more demanding policy objectives has remained the same. An insufficiently financed mandate was created.

To sum up, the justification for *investment* as part of the financing of each resettlement component over and above compensation rests on three solid grounds:

- First, on economic grounds, forced displacement requires enabling those displaced to secure an accelerated path to catch up for forgone growth.

- Second, on policy consistency grounds, there is a deep mismatch inside many formal resettlement policies between high goals and insufficient means. The means of compensation are not commensurate with the goal of restoration, let alone the goal of improvement and development.

- Third, on poverty reduction grounds, it is unacceptable to allow new poverty to creep in under projects aimed at reducing existing poverty.

The policy framework for investing in resettlement and broadening the economic foundations of resettlement operations is gradually emerging stronger. For instance, the revised resettlement policy issued by the World Bank in November 2001 states unambiguously that:

> "resettlement activities should be conceived and executed as sustainable development programs, providing sufficient *investment resources* to give the persons displaced by the project the opportunity to share in project benefits" (World Bank 2001, my emphasis-MMC).

There is, however, still very little in this rewritten policy document about the procedures and norms by which such investments and participation in project benefits are to be allocated and implemented. Such procedures await now elaboration and application within the revised policy.

Important building blocks are already available for conceptualizing the new economic foundations for resettlement operations. Much can be learned, for instance, from progress in environmental economics, from other domains of development economics, from the vast research on poverty reduction and social protection, and from the (still few) direct studies on resettlement economics. (e.g., Pearce 1999; Kanbur 2003; Shi Guoqing and Hu 1994, Downing 2002). The vast and growing store of research in anthropology and sociology on the economics of displacement, on risks, and on secondary effects, provides a rich source of empirical data, knowledge, and theory. In short, the challenge to economists, sociologists, anthropologists – to jointly articulate a new comprehensive economics of resettlement – is not only important and overdue, but can now be met successfully.

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