an UNCERTAIN FUTURE

the Vulnerability of Djibouti's Location as an Economic Asset

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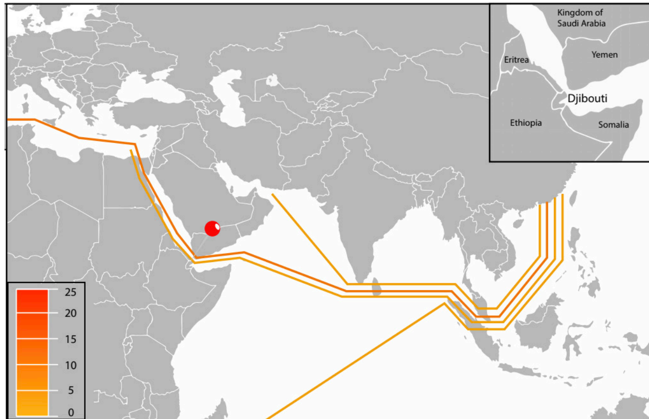
ABSTRACT

How did Djibouti, a country the size of New Jersey, go from a sparsely populated desert to drawing comparisons to 1940s Casablanca, a city filled with intrigue and pivotal powers "rubbing elbows with each other?". Djibouti can thank its location. The country's location on the Horn of Africa allows it to offer a secure location for shipping conglomerates looking to refuel safely and disembark goods destined for the interior of Africa, as well as governments launching military operations in the Middle East and Africa. As a result, Djibouti has built an economy similar to those of countries that exhibit symptoms of the so-called "resource curse." However, the more pressing issue facing Djibouti is not the symptoms of a "resource curse," but rather the growing threats to the value of its land. Djibouti's neighbors Somalia, specifically the region of Somaliland, and Eritrea are becoming more attractive destinations for foreign investment. China poses another threat. While China may appear an economic benefactor, the strings attached to its investment ultimately hurt recipients. Benefactors of Chinese investment tend to default on their loans, which Djibouti is in serious risk of doing. In the past, when countries have defaulted on their loans, China has gained the lease on the new infrastructure.

I. THE "RESOURCE CURSE"

Djibouti serves as an important trading port because of its proximity to critical shipping routes. The Asia-Mediterranean and Asia-North Europe routes pass by the country as they travel through the Gulf of Aden into the Red Sea or vice versa. Djibouti serves as the only viable option for ships to refuel or disembark goods destined for interior Africa. As will be discussed later, Somalia and Yemen do not currently have stable governments that can facilitate trade, and Eritrea's oppressive dictatorships and poor human rights record deters states and corporations from entering into economic relations with it. Therefore, Djibouti remains the only country that governments and corporations can work with safely and not face public backlash. As a result, the majority of Djibouti's GDP comes from services that result from its strategic location. Services comprise over 70% of the country's economy and have tripled the size of Djibouti's economy since 2000.[1] The country's economic hotspots revolve around its port on the Red Sea, military bases, and the railway that connects to Ethiopia.[2] Without its location and the economic interests it serves, Djibouti's economy would certainly collapse.Djibouti serves as an important military location because of its proximity to the Middle East, African conflict zones, and piracy hotspots. The United States, China, France, Italy, and Japan all currently have bases in the country, and Saudi Arabia is also exploring the option of building one there.[3] These countries decided to build strongholds in Djibouti in order to serve their economic and military interests. Djibouti's neighbor, Somalia, serves as the launching point for pirates looking to exploit cargo ships traveling around the Horn of Africa. Countries establish bases in Djibouti to place naval forces that can quickly respond to piracy situations.[4] Djibouti also lies in close proximity to the Middle East and conflict zones in Africa. For example, the missions launched from Camp Lemonnier, the United States base in Djibouti, are drone strikes or classified special forces operations in Yemen, or nearby African countries like Somalia and Mali.[5] Countries lease the land to build these bases; the United States pays Djibouti $30 million a year to retain its position within the country.[6] The money from military base leases further bolsters Djibouti's economy.

Countries that rely on one commodity to support their economies are subject to an economic phenomenon known as the "resource curse." The "resource curse" refers to the issues a one-pronged economy faces, which include corruption, wealth inequality, widespread poverty, and neglect for the development of potentially lucrative industries.[7] Many countries in sub-Saharan Africa also experience this issue. For example, Nigeria controls massive reserves of crude oil, and the presence of this resource fo-



cuses all investments on ways to exploit the commodity. As a result, the government and investors neglect Nigeria's potential as a producer of livestock and food. The agricultural industry has become so underdeveloped that Nigeria is forced to import most of its food.[8] "Resource cursed" states also have centralized authoritarian governments that operate on patronage and corruption. In a country like Nigeria, citizens must have direct access to the oil industry to obtain wealth. The Nigerian government controls the distribution of wealth from the commodity, and only friends or those who bribe officials get a portion of the revenue. As a result, only 1% of Nigerians gain 80% of the revenue from oil. Oil has caused widespread corruption, wealth inequality, and economic mismanagement within Nigeria.

Geographic location acts as Djibouti's critical commodity. As discussed previously, the country's economy relies on its proximity to trading routes and the military interests of foreign powers. Because of this dependence, Djibouti demonstrates the symptoms of a "resource curse." President Ismail Omar Guelleh operates the state with a tight grasp because he and his allies need to control the revenue accrued from Djibouti's strategic location to control the country. While the country displays some features of a democratic polity, Guelleh's ruling party crushes dissent. The political opposition has the ability to publish its own newspapers and radio broadcast, but harassment by the Djiboutian government prevents these parties from gaining broad popularity.[9] Guelleh maintains power through his control over real estate valuable to China, the United States, and other major powers. Guellah also heavily favors his own ethnic group. Guellah belongs to the Issa group, and disburses more patronage to the Issa than the Afars, the other significant ethnic group in Djibouti.[10] Controlling the rights to land are critical to his regime. He rewards those individuals who act to o legitimize his government. Guellah has created an unequal society with one favored ethnic group that relies on real estate revenues. Djibouti and the power of its president are dependent upon the value of the country's strategic location.

In order to boost the revenues he has access to, President Guelleh directs investments towards trade infrastructure and economic ventures that flow into the coffers of the state.[11] As a result, the relationship between the governed and government is weak. Jennifer Brass asserts

that the social contract in Djibouti is virtually non-existent, as Guelleh's government does not rely on citizens for taxes and returns none of the political goods associated with a conventional social contract.[12] By practice, not design, the Djiboutian economy has become virtually state-run. The government expresses no interest in promoting private enterprise, demonstrated by its abysmally low property rights score of 19%, which lies 10% below the average for sub-Saharan Africa.[13] Djibouti will maintain a strong economy as long as foreign countries see its land as valuable, but as competition increases, or China finds a way to control the land, the country's economy and government will deteriorate.

Unlike Nigeria, Djibouti has no alternative course of action if the value of its main resource falls. Djibouti has almost no natural resources, and its arid desert conditions cannot support agriculture.[14] If oil loses enough value to a point at which it can no longer support Nigeria's economy, the country could shift to agriculture or mining, but Djibouti does not have this option. Thus, the threats to the value of Djibouti's land are significantly more important than threats to the value of its oil, like the growth of renewables,. Djibouti's economy has no back-up plan. If its land loses value, the country's economy and government will collapse.

II. POTENTIAL COMPETITORS TO DJIBOUTI

Two other countries boast the same valuable location as Djibouti: Eritrea and Somalia. Eritrea, however, poses little threat to Djibouti. Eritrea was an Italian colony until 1941, when it became a British protectorate. In 1952, the British handed over control to Ethiopia, and it remained part of Ethiopia until 1991, when conflict broke out and Eritrea gained full independence.[15] Since then, the country has remained an oppressive dictatorship. In 2016, a UN Commission of Inquiry looked into human rights violations within the country. Sheile B. Keetharuth, who served on the Commission, found that "the Government has made no effort to end ongoing human rights violations," and described these violations "as amounting to crimes against humanity."[16] The Eritrean government forces its citizens into indefinite military service, confiscates citizens' currency, and controls all the country's media outlets. As a result, foreign powers tend to avoid entering into economic and military relations with Eritrea to avoid the public backlash they would attract from doing business with an oppressive government. To the benefit of Djibouti, nothing indicates this will change. Unlike Somalia and Somaliland, Eritrea has received no interest from foreign investors, pointing to a future in which Eritrea's eco-

nomic infrastructure will not be able to compete against Djibouti's. Also, Eritrea has shown no signs of changing its repressive government or ending human rights abuses. Due to the presence of a stable and more reputable neighbor, countries ignore Eritrea and invest in Djibouti.

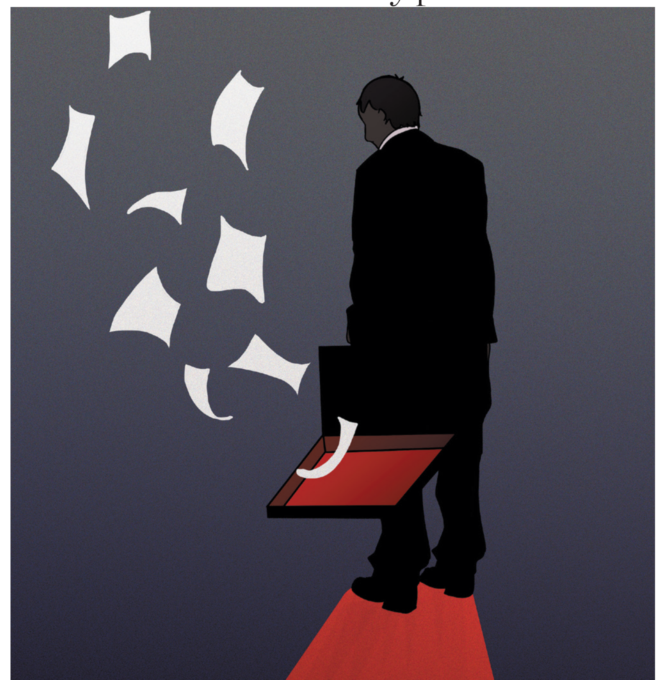
Djibouti's other coastal neighbor is Somalia. Countries shy away from Somalia not because of an autocratic government, but lack of a functioning one. The country has been embroiled by piracy, transnational terror groups, and armed conflict since its civil war in the 1990s. Shipping companies are still concerned about the threat of piracy as well. In the first half of 2017, Somali pirates attacked 9 vessels traveling around the horn of Africa.[17] The lack of state capacity attributes to this problem. The United Nations classified Somalia as a fragile state, which refers to a country that has some form of a functioning government, but is in imminent danger of collapsing.[18] The security threat poses too high a risk for countries to ship goods through Somalia which has resulted in nations launching military operations in the country, but not the construction of permanent bases. Since these operations are typically airstrikes, foreign powers have a longer range in which they can build a base, meaning they do not have to build a base in Somalia. Rather, they choose to build bases in Djibouti, which provides a secure location to launch these strikes from.

Despite this reality, Somalia may become a target of foreign investment in the near future. The country has demonstrated over the past few years a steady upward trend towards becoming a secure state. While its current state may not initially indicate a potentially prosperous future, Somalia has demonstrated improvement nonetheless. Its current status as a "fragile state" is an upgrade from its previous status as a "failed state", which Somalia held before 2015.[19] More recently, the Heritage Foundation was able to collect data on economic freedom in Somalia, and early results show promise. From its score in 2017 to its current 2018 score, Somalia's property rights score jumped over 25 points and lies only 5 points below the average score of Sub-Saharan Africa.[20] The rise of Somalia will eventually threaten the value of Djibouti's location. Djibouti's property rights score has fallen in the past few years due to endemic corruption. In fact, Somalia's property rights current score stands 14 points higher than Djibouti's. A stable Somalia offers states a longer coastline, meaning that naval bases do not need to be in such close proximity to each other as they are in Djibouti. Because Djibouti is small, the Chinese and US naval bases in Djibouti are only 7 miles away from each other. Somalia still lacks the security needed to court foreign investment, but the demonstrated improvements in this area, indicate that Somalia will not remain as a "fragile

state".

However, the area of Somalia, called Somaliland, can threaten Djibouti's monopoly in the short run. Somaliland operates as a de facto autonomous country within Somalia. The territory operates as a functioning democracy with high state capacity and legitimacy. Somaliland already boasts growing large ports on the Gulf of Aden and the Port of Berbera which transit 1.25 million TEU[21] per year.[22] In comparison Djibouti's port transported roughly one million TEU per year .[23] In April 2018, DP World, a shipping conglomerate owned by the government of Dubai, invested 450 million into Somaliland to expand Bebera's port capabilities[24]. Somaliland is receiving the investments for the infrastructure needed to compete with Djibouti's shipping industry. The central government of Somalia tried to prevent the project from taking place and banned DP World from the country, but the central government demonstrated no ability to enforce this measure.[25] Similar to Djibouti, foreign states are starting to recognize the value of Somaliland's location. Once Somaliland can court more foreign investment it will become a formidable economic competitor to Djibouti.

DP World complicates the relationship between Djibouti and Somaliland. DP World is currently developing the Port of Berbera expansion. Once the port can facilitate mass trade, DP World will operate and profit from the port. Until very recently, DP World also operated a major port in Djibouti, but Djibouti's government ended DP World's contract to operate the port on the basis of an unresolved legal matter dating back to 2012. DP World has turned to the International Courts to arbitrate the decision and Djibouti indicated that they plan on buying DP World's stake in the port to settle the matter[26]. Therefore, Djibouti's attempts to shut out DP World from their only port on the Horn



of Africa has led to a greater incentive to grow the port and make Somaliland a competitor to Djibouti. Even further, in early March, Ethiopia bought a 19% stake in the Port of Berbera, adding Ethiopia to the list of actors that have an incentive in growing the Port of Berbera.

III. THE THREAT OF CHINA

China also wields significant influence over the future of Djibouti. Djibouti is a critical military and economic port for China and, as a result, the Chinese invest billions into the country. China is currently financing the construction of a railroad between Djibouti and Ethiopia as well as the "mega" Doraleh Multipurpose Port. However, the financial realities of Djibouti predict that Djibouti will not be able to pay back these loans. The Center for Global Development, a non-profit research organization, believes that Djibouti will most likely default on these loans.[27] Once Djibouti defaults, they will be at the mercy of China.

Countries in Southeast Asia offer a glimpse into what China will do once Djibouti defaults on its loans. Sri Lanka lies on a trade route critical to the Chinese economy. In the mid 2010s, Sri Lanka, like Djibouti, looked to China to finance infrastructure projects in the country, including a trading port. The country defaulted on the loans and settled the debt by swapping debt for equity. China walked away from the deal with a 99-year lease on the port. China offered a similar deal to Pakistan, which also lies on an important trade route, and built the Pakistani port of Gwadar. Similar to Sri Lanka, Pakistan defaulted on the loans and now China holds a lengthy lease on the port.[28] Hopes of controlling these ports motivates China's financing to these countries. China loans to economically vulnerable countries that are in need of financing for infrastructure projects with the promise that these projects will help the recipient economy in the long run, knowing that in all likelihood, these countries will not be able to pay back these loans. Djibouti sits in the same position as Pakistan and Sri Lanka, and unless they reshape their repayment strategy, their port will end up in Chinese hands.

Whether or not Djibouti defaults on its loans, the Chinese insistence to use Chinese labor to build these infrastructure projects severely inhibits Djibouti's ability to solve its country's unemployment problem. Unemployment in the country lies just below 60%.[29] Chinese funded infrastructure projects use local labor, but Chinese workers occupy technical and administrative positions. The learning potential from these projects are squandered by China's decision to bring in foreign engineers and managers. The lack of education in Djibouti could attribute to China's decisions, but Djibouti should insist on measures in future contracts with China that require the training of Djibouti's workers as engineers or managers. The lack of human capital in Djibouti will leave its average citizens out of the benefits on Chinese investment. Laborers can only access the wealth created by Chinese investment in a miniscule amount. At some point, the lack of expertise will hurt Djibouti. Eventually the rate of construction will slow due

to either lack of real estate or Djibouti losing its monopoly on ports on the Horn of Africa. When this occurs, Djibouti will have an overflow of labor and more unemployment.

IIII. CONCLUSIONS

Djibouti faces a very real possibility of the economic growth that its location has brought them ending and regressing. Somaliland can become a formidable economic competitor that can serve as a realistic alternative to Djibouti's ports. As of now, Somaliland's Port of Berbera is too small, but the port will continue to grow due to massive amounts of foreign investment. China may gain the lease on Djibouti's newest and largest port if Djibouti's defaults on its loans, meaning Djibouti can be shut out of its own value. The pathways to mitigating the damage this would cause to Djibouti are unfortunately minimal. Djibouti's lack of natural resources means opportunity for a diversified economy is low. For both threats, Djibouti should maximize the revenue from the ports and military bases and invest in education with the purpose of creating a skilled workforce that can support diversified industries. If China takes over its ports or if the Port of Berbera becomes a competition, Djibouti will have industries to fall back on to curb China's or Berebera's influence. Djibouti must be serious about democratizing their country to turn to Western financial institutions such as the IMF for debt relief and then to the World Bank for future projects. While, instability in surrounding states could always keep investors in Djibouti, the future is not clear.

The outlook for Djibouti is not optimal. In order for Djibouti's economy to survive it must turn from a patrimonial state into a democracy that meets the standards of the World Bank in order to refinance its loans. It must avoid taking unpayable loans from the growing, expansionist China, which would likely result in disaster.. It must also grow enough human capital to reform its economy into a service based economy. The only thing Djibouti directly controls is democratizing the state and growing human capital. However, Guellah and his regime have no incentive to do either of those things. Defaulting on loans and entering into a lopsided deal with China for Guellah is a better option than loosening his grip on the country and educating his citizens, the latter of which requires money Guelleh knows he does not have to spend. Unfortunately, Guelleh and the government of Djibouti will likely do nothing to mitigate the eventual damages of devalued real estate to the Djiboutian economy.

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