Article Type: Book Review

***The Economics of Conflict: Theory and Empirical Evidence*, edited by Karl Wärneryd (Cambridge: MIT Press, 2014), pp. 304.**

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In recent years, the world has witnessed a series of violent conflict in the form of rebellions, uprisings, and civil wars, particularly in Africa and the Middle East. These events have spurred much interest in the study of the causes and consequences of conflict and, as a result, an emerging field known as the economics of conflict has come under the spotlight.

In fact, thanks to the large mass of research that has been generated by scholars within the field, the time seems ripe for a textbook. However, readers who crave a systematic exposition and are thus drawn to this book because of its title – *The Economics of Conflict* – may be slightly disappointed; the book is merely a collection of papers presented at the 2011 CESifo Venice Summer Institute Workshop.¹ That said, the book is not without merit. On the contrary, the editor, alongside anonymous referees of the book, deserves credit for compiling an exceptionally diverse set of papers in this volume.

The book is organised into two parts: theory (chapters 1-4) and empirical (chapters 5-9). The theoretical chapters have little synergy apart from the use of contest functions to model conflict; indeed, these chapters examine conflict in a variety of settings. Similarly, the empirical chapters address a wide range of questions using cross-country and country-specific data. I provide a brief overview below, to help the uninitiated navigate the book, and to direct those who are looking for something more specific to the relevant chapters.

¹ As a matter of fact, no comprehensive textbook on the economics of conflict exists to date, although handbook volumes such as Justino et al (2013) and Skaperdas and Garfinkel (2012), and a survey article by Blattman and Miguel (2010) may be useful.

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First, the theory chapters. In chapter 1, Konrad poses the “alliance puzzle”, that is, why do we observe alliance formation in conflict when the strategic disadvantages of free-riding and holdup often make alliance members worse off? To answer this, he presents six considerations that would either offset or nullify these strategic disadvantages. For example, if the strength of a combined military force is higher than the sum of individual armies, then investments into the alliance in equilibrium may be enhanced due to strategic complementarity. These results are helpful for thinking about alliances in general, but especially in military conflict.

Chapters 2 and 4 analyse political conflict. In chapter 2, Cubel studies the political viability of fiscal equalisation by considering the circumstances in which regions might disagree with the distribution of payoffs and initiate political conflict. Several factors come into play in determining conflict. Size, for example, is an important aspect since smaller regions have more to fight for since their per capita post-conflict payoffs are higher. Most importantly, Cubel emphasizes that full equalization is possible only when regional budgets are used to fund pure public goods; as the degree of publicness in the regional budget decreases, political conflict becomes more likely. Turning over to chapter 4, Jia and Liang examine the effect of power structure on the stability of political regimes. In particular, they set up a three-player (central government, local government, and plotter) game in which the plotter can initiate a coup to overthrow the central government, given an existing power structure – centralised or decentralised. Since the local government cannot commit to fight or not to fight against a victorious plotter, these twin effects of limited commitment generate opposing incentives for the plotter: on the one hand, a decentralized regime is easier to defeat; on the other hand, it is more difficult to hold on to power. The model thus predicts an inverse-U relationship between decentralization and the initiation of coups.

Finally, Fiaschi revisits the natural resource curse hypothesis in chapter 3. He argues that conflict over resources, alongside other defining features of weak institutions, can create a poverty trap for low income countries. Notably, he shows that rent-sharing without social

conflict is feasible in a repeated game, but depends crucially on capital investments and population growth. The model is useful for explaining the persistence of poverty in the long run.

Crossing over to the empirical chapters, I shall first mention the ones that use cross-country data. In chapter 5, Caruso, Costa, and Ricciuti provide a nice summary of military junta in 48 African countries for the period 1970-2007. They identify three key correlates: per capita income, ethnic fractionalisation, and previous external threat. The first two are reasonably well-known, while the third merits further explanation. The authors use lagged interstate hostilities as their measure of previous external threat. The result suggests that the military is likely to become more powerful after having faced an external threat, which may subsequently raise the odds of having a coup. Cross-country evidence again features in chapter 8. There, Stroup and Zissimos look at how the IMF's Structural Adjustment Program (SAP) may sometimes provokes social unrest. Since SAP involves trade liberalization and a cut back in government spending, land owners in countries with a comparative advantage in primary products will benefit disproportionately, and income inequality will rise and redistribution is bounded by austerity measures. Using an assortment of social unrest measures such as political assassinations, industrial strikes, and so on, they provide suggestive evidence that balance of payment crises (which lead to SAP) are associated with some (but not all) forms of social unrest.

Next, Evia, Laserna, and Skaperdas examine the relationship between social conflict and economic growth in Bolivia in chapter 6. While conflict is negatively correlated with per capita income growth in general, they find that it is negatively correlated with endogenous sources of growth (investments) but positively correlated with exogenous sources of growth (terms of trade). An important takeaway is that investments generate disincentives for conflict, while windfall gains intensify rent-seeking and appropriative competition. In chapter 7, Bove and Elia assemble a unique monthly dataset of opium prices and conflict events in 15 Afghan provinces over a period of five years, and exploit variation across time and space to uncover the relationship between the occupational choice and conflict. They find that violence, as measured by the number of conflict events, increases (decreases) the supply (price) of opium. Abstracting

from possible demand shifts due to fighting amongst antigovernment groups, this result suggests that conflict compounds the level of insecurity which fosters greater supply and lower prices.

Finally, Cassar, Grosjean, and Whitt study the effect of conflict exposure on cooperation and trust in Tajikistan, in chapter 9. Using survey and experimental approaches, they find that conflict exposure creates a long term “conflict gap”, that is, an attitudinal difference toward in-group and out-group members of the society. Specifically, experimental results show that ex-combatants from the Tajik conflict exhibit less generosity, less trust, and less cooperation, when compared with non-combatants. Survey evidence further demonstrates that the link between combat exposure and lower trust exists in out-group but not in-group behaviour.

In conclusion, the book is essentially a collection of papers. For the general reader (or economist who work outside the realm of conflict), these papers do an excellent job of showcasing the depth and diversity of the field. For those working within the field, the book represents a selection of recent contributions, some of which may be of interest.

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