State-building

Job Creation, Investment Promotion, and the Provision of Basic Services

BY PAUL COLLIER

Rigorous research on state-building is still in its infancy. In this article, I take three issues that are important and distinctive to state-building situations and discuss what research can potentially contribute. The issues are by no means exhaustive; they are merely a sample of what needs to be a more comprehensive engagement between scholars and practitioners. There is unfortunately a wide gap between what practitioners need to know and what research can currently show with reasonable confidence. There is a further wide gap between what is known and what is likely to be feasible for researchers in the next few years. At least practitioners should be aware of where they must make decisions unsupported by solid evidence; more ambitiously, they can encourage research into those issues that are both feasible and significant.

Low per capita income is now avoidable if governments adopt policies that are conducive to private economic activity and employment generation. While superficially all governments want growth, some do not translate this into day-to-day practical decisions. Thus, a minority of low-income developing countries lack functional economic policies and state capacity to facilitate economic growth, stability, and peace. The populations of these countries are among the neediest on Earth, and meeting their needs requires approaches that work swiftly. Given the current limitations of state performance, the solutions need to focus on host government reform policies and alternatives for delivering basic services, rather than depending on building state capacity that can only work in the long term. The three important and distinctive issues for building state capacity and encouraging policy priorities that are beneficial for economic growth and stability are establishing incentives for practical local economic reform policies, creating an environment

Dr. Paul Collier is Professor of Economics and Director of the Centre for the Study of African Economies at Oxford University. This article was originally developed for the International Growth Centre (IGC) State-Building Workshop. The IGC (www.theigc.org) is a research institute that offers independent advice on economic growth to developing countries. It is based at the London School of Economics and Political Science in partnership with Oxford University.

that supports private economic investment, and enhancing the delivery of basic social services by the host government.

Governments are not homogenous entities; it is the reformers in low-income developing countries who are most likely to advocate for practical policies to promote economic growth. What donor actions and incentives would make it more likely for local reformers to win their struggles for economic growth?

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Policy decisions that are conducive to private economic investment activity and employment generation are most likely to raise postconflict and other low-income countries out of poverty. The emphasis here is upon those policies that are distinctive to postconflict conditions and the early stages of recovery from prolonged poverty and stagnation. I focus on policies that might speed the recovery of private investment; on which sectors are likely to have the best opportunities for early growth and the impediments that could be eased by policy reform; and by the benefits and strategies for employment generation. In each case, the question is, given what we know (at varying degrees of confidence), what important policy choices might be informed by feasible further research?

Government capacity enables the delivery of basic social services by the host government, and likewise such delivery of goods and services enhances the perception of government capacity. In what follows, I discuss how the delivery of basic social services could be improved in the conditions typical of these difficult postconflict and economically stagnant environments.

Incentives to Promote Private Economy

While practitioners tend to emphasize the need to build capacity, economists focus more on the need to align incentives. A persistent lack of capacity is seen as evidence that the incentives to acquire the capacity are too weak. Along these lines, one likely explanation for the persistence of low income is that the government lacks the incentive to promote growth. Historically, the most common motivation for governments to adopt growth-conducive policies was the need for tax revenue. Other motivations may also be important and applicable in the fragile state context.

Promoting Revenue-motivated Growth. Growth generates government revenue conditional upon an effective tax system. Hence, an important current hypothesis in political economy is that government investment in the machinery of effective taxation is a precondition for development, not so much because of what tax revenues buy as because they induce the government to provide a legal system.[1] Some governments have chosen not to build an effective tax system, and hence, on the above hypothesis, they lack the incentive to provide the rule of law, which in turn promotes economic growth. If the government is not capturing any of this growth, it has no interest in promoting it. Presumably the reluctance to build effective tax systems originates from either the costs of building these systems being atypically high, or the benefits being atypically low.

Revenue-motivated growth could indirectly be promoted by donors if they were able to address these impediments. Costs might be atypically high in some states because of the lack of skilled personnel or because norms of corruption have become so entrenched that taxation merely generates income for tax collectors rather than the state. Clearly, the costs of tax collection vary among states. The degree to which the economy is monetized, the degree to which transactions involve third parties or generate written records, and the proportion of transactions flowing through chokepoints such as ports are all observable. Furthermore, in something approaching a natural experiment, in some countries the International Monetary Fund encouraged governments to take revenue-raising away from the civil service and give it to Independent Revenue Authorities (IRAs), which selectively rehired staff and paid higher wages in return for monitored performance. There may be scope for research on whether variations in the costs of tax revenue, both among countries and over time (including quasi-exogenous institutional innovations such as the IRAs), explain the emergence of the rule of law and subsequent economic development. Such research might provide some guide as to the importance of the ability to raise taxes for state development.

The benefits of building a tax system might be atypically low for several reasons. Building state capacity is an investment, and so one possible explanation for a lack of investment would be if some governments had atypically short time horizons. However, despite the prevalence of coups and rebellions, the incumbents of many dysfunctional states have enjoyed long tenure, so this explanation seems unlikely, at least superficially. It is potentially testable because our knowledge of the risks faced by incumbents has now advanced to the point at which expected tenure could be modeled.

A second possible explanation as to why the benefits of a tax system might be atypically low is if there are alternative sources of revenue. The most prominent alternative sources are aid and resource rents. Since both are important in dysfunctional states, this explanation has some plausibility. It is clearly a testable proposition: states vary considerably in aid receipts and the approach of José Tavares is a reasonable way of tackling endogeneity.[2] Similarly, their natural resource revenues vary considerably over time, and the component due to world prices can reasonably be treated as exogenous.

If this model of state development and its impediments is right, then the implications for policy are potentially radical. Aid, especially in the form of budget support, and revenues from resource extraction, should both be curtailed in these environments. Aid could be confined to modalities that kept it out of government control, avoiding fungibility by being tied to expenditures that the government would not itself wish to provide (that is, the opposite of "country ownership"). Revenues from natural resource extraction could be curtailed either by the Chinese model of selling extraction rights directly for infrastructure rather than for revenue, or by the radical option of discouraging resource extraction itself (for example, by imposing international conditions on companies that made these environments unviable).

A third possible explanation for atypically low benefits from investing in tax capacity is that the economy is currently so small and informal that the investment would not pay off until the distant future. In other words, economies have to grow to a certain size and formality

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U.S. Air Force (Joseph Swafford)

before government investment in a tax system is a paying proposition. For example, the much slower rate of state formation in post-Roman Britain than in post-Roman continental Europe is sometimes attributed to the exceptional and total collapse of the post-Roman economy in Britain so that there was no basis for revenue.[3]

The policy implications of this explanation are radically different. Leading with tax effort might even be detrimental. If the formal economy is only a small proportion of the overall economy, even a modest ratio of tax/gross domestic product may have significant disincentive effects. Furthermore, if reported profits cannot be trusted, de facto tax collection may depend on observable signs of profitability of which the most obvious is investment. In contrast, aid and revenues from resource extraction may be benign, financing the initial development of the economy to the critical level at which the government chooses to invest in tax capacity.

A fourth explanation for atypically low benefits from tax revenue is if the governing elite would not benefit significantly from public spending. If, for example, the core interest of the elite is for private goods rather than public goods, public policy might be most effective if it generates direct opportunities for elite rents, rather than raising revenues that are then appropriated by the elite. Historically, the counter to this argument has been that elites benefit from public spending on property rights and defense since this maintains their own power. However, leaders may gain patronage from the insecurity of property rights, and if the main threat to the regime is from coups and rebellions rather than from international invasion, then high military spending may have ambiguous effects on elite security. Famously, Mobutu Sese Seko chose not to spend on his army. Other than security, the elite may indeed perceive little benefit from public goods: poorly motivated public employees may be unable to provide services at a quality that satisfies elite tastes, and donors may insist on a composition of public spending that favors low income groups.

If this explanation is correct, the policy implication may be that the international community either should decisively override elite interests or acquiesce to them. Power-sharing structures, such as the Governance and Economic Management Assistance Program in Liberia and the Interim Commission in Haiti, by limiting the ability of elites to frustrate development, may enable the economy to develop to the level at which interests change. But the other extreme, in which donors give governments the freedom to serve elite interests unashamedly, might also work by aligning elite interests with growth. The conventional donor conditionality discouraging defense spending and encouraging expenditures on primary education and primary health care could therefore inadvertently be detrimental. It leaves elites in control of taxation but prevents them from benefiting from revenues.

Nonrevenue Motivations for Growth. Although the desire for revenue is one obvious reason why governments might want to promote private economic activity, there are others. One alternative to revenue motivation is if governments become accountable to well-informed citizens. Faced by such accountability, governments that wish to survive have no choice but to focus on developing the economy. A potential advantage of accountability as a way of motivating government is that it provides a more generalized influence on the composition of public spending than just efficacy for growth. Thus, a revenue-motivated government would indeed choose to invest in the rule of law. By contrast, an accountability-disciplined government would also spend on public goods that enhance general well-being but are not cost-effective investments from the perspective of elite interests, such as health care and education.

Historically, accountability to citizens followed, rather than preceded, economic development. However, now that the accountability of government to citizens is normative, it may be possible to use international pressure to reverse the historical sequence. Since the fall of the Soviet Union, there has been just such an attempt targeted on the governments of low-income countries. Although to date, this attempt has largely been unsuccessful, it may have failed because of the particular strategies adopted by the international donor community (such as the priority given to elections over institutions). In this case, the appropriate international policy would be to revise and reenergize efforts for accountability, perhaps by harnessing new technologies to inform citizens.

Another way to motivate government is nationalism. Arguably, the governing Chinese elite are concerned neither to maximize state revenues nor to serve the preferences of ordinary citizens, but rather to build a country that is strong and respected. Not only does nationalism provide an inducement to effective government by motivating ordinary public sector employees—both tax collectors and service providers—but it also lowers the costs and raises the benefits of taxation. On this account of state capacity, the key policy is building a shared sense of identity. Historically, identity has usually grown out of international conflict, making the testing of revenue-driven motivation versus identity-driven motivation difficult. However, Edward Miguel argues that identity can be built by less costly policies.[4]

Implications for a Research Agenda. The state has a critical role in promoting private economic activity through providing the rule of law, such as establishing a legal system that protects contracts and property rights. Hence, to explain failures in the rule of law and the provision of other public goods, a reasonable starting point is that the government lacks sufficient interest in economic growth to provide these public goods. I have sketched several possible reasons why a government might lack such an interest. Unfortunately, the policy implications of these different explanations are radically different, yet we do not currently know which is correct, whether generally or conditional upon context. The historical evidence from the development of Organisation for Economic Co-operation and Development states points to the stimulus as being the need for revenue to counter international security threats. However, this fact is perhaps of only limited relevance because of the major changes in the international environment and the distinct modern circumstances of low-income developing states.

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One approach to adjudicating among the various explanations would be to take as the pertinent population all the states that at time X were low income and lacked the rule of law. Time X should be well after independence so domestic political forces have had time to reshape their colonial inheritance, but sufficiently distant from the present that several of these societies have subsequently built the rule of law (and related public goods). Research could then investigate the sequences best suited to building the rule of law in contemporary conditions.

How to Promote the Economy

I now turn from the issue of motivation of government to the economic policies—beyond building the rule of law—that a government might take to promote an economy starting from poverty and stagnation. Such economic conditions are commonly the legacy of internal conflict. These economies are distinctive in being capital-scarce, in the structure of opportunities, and in great need of employment generation.

Investment. Poverty, stagnation, and conflict leave a distinctive economic legacy. Investment in both physical and human capital will have been below replacement rates. The counterparts of underinvestment are accumulated unexploited opportunities for investment, and accumulated offshore assets in the form of flight capital and a diaspora. Private investment faces atypically severe impediments of risk, infrastructure, and regulation. Applied research can quantify these impediments and the practical scope for addressing them.

Risk. As to risks, Jakob Svensson shows that the decision to exploit opportunities for investment in a low-income postconflict society depends upon the "bad news principle": the critical impediments to investment are the severe downside risks. These risks are largely concerned with fears of government actions. Both donors and governments can do something about them. The most obvious donor policy would be political risk insurance that covered worst case scenarios. Governments can potentially address investor fears either by adopting commitment technologies or by other actions that reveal the economy to be investor-friendly. There is scope for both policy experiments and analytic and empirical research. Analytically, governments often do not understand the bad news principle, the rationale for commitment technologies, or that an effective signal is an action too costly to be imitated by a government that is not genuinely investor-friendly. Empirically, there is good data both on foreign direct investment and on perceived investor risks. Hence, it should be possible to quantify how sensitive private investment is to specific risk-reducing actions.

Infrastructure. There has been little quantitative work on the returns to infrastructure in the poorest societies. However, it is now becoming researchable. For example, a new International Monetary Fund (IMF) database[5] provides time series estimates of the public capital stock for many countries up to 2003, and the World Bank is in the process of generating further data. The IMF study also estimates the return on public capital. These are the necessary building blocks for estimating the legacy of underinvestment. While such estimates could not be definitive, they would be a considerable improvement on the wish lists drawn up for the typical postconflict donor-pledging conference.

Regulation. On regulatory policies for investors, the World Bank's *Doing Business* surveys now provide an objective and comparable measure. Potentially, such data sources could be used to compare the payoff to risk reduction, infrastructure, and regulatory reform as means of attracting private investment.

Capital Repatriation. Foreign investors typically start from considerable ignorance about low-income postconflict societies because there has been little point in acquiring information. The best informed, and therefore the earliest investors, are likely to be among the diaspora and the owners of flight capital. They constitute major opportunities for the poorest societies as often most of their capital and skills are abroad. The scope for reversing flight has been little studied, but it appears to be a function of the standard variables of expected returns and perceived risks.[6] Data on capital flight remain poor, but can be inferred indirectly through several standard approaches.

Diaspora Return. The scope for the return of the diaspora is both ripe for policy experiments and a researchable process. Stocks of emigrants return at different rates to different low-income (and postconflict) societies from the same country of emigration. This is now readily observable from Organisation for Economic Co-operation and Development census data.

Sector-specific Issues. In a low-income economy with a legacy of poor infrastructure and regulation and high perceived risk, the tradable sector is likely to be uncompetitive.

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The sole exception will be where there are location-specific rents as with resource extraction. Other than in resource extraction, most business opportunities therefore are likely to be in the internationally nontraded sector. Within the nontraded sector, the key subsector is likely to be construction because it supplies the nontradable capital goods—the structures—that complement investment in equipment.

Natural Resources. By far the most important private investment that postconflict countries are likely to attract is for resource extraction. Resource extraction does not usually generate many jobs, but it does generate rents that can be appropriated by government. The potential sums involved are enormous relative to all other aspects of the economy. Afghanistan is now estimated to have $1 trillion in unexploited subsoil assets. More generally, in low-income countries, discovered subsoil assets are only around one-fifth per square mile that of the Organisation for Economic Co-operation and Development. Resource extraction is the last frontier for discovery.

Managing the discovery and extraction process faces particular problems of agency, asymmetric information, and time inconsistency. Failure to address these problems can lead both to under-exploitation (hence the low incidence of discovery to date) and to low rates of revenue-capture for government. These issues have not been adequately investigated using analytic and quantitative techniques in

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the context of the poorest countries. One of the few such studies illustrates why common sense is unlikely to be sufficient.[7] Massimo Guidolin and Eliana La Ferrara analyze the impact of peace in Angola on the valuation of foreign private investment in diamond extraction. Contrary to expectation, they find that peace *reduced* the value of these investments.[8] A possible explanation is that peace improved the bargaining power of the Angolan government and so reduced the commercial value of extraction rights. Many resource extraction companies are publicly quoted and have market valuations and are required to release information about their activities. There are also new databases on contracts and revenue payments being generated through transparency initiatives, notably the Extractive Industries Transparency Initiative, so it should be possible to estimate the payoff to enhanced transparency.

The astounding payoff to research on auction theory that netted the British government £20 billion from selling 3G mobile phone rights illustrates the potential profitability of managing resource extraction. At one end of the spectrum, the government of Iraq recently auctioned management contracts for the extraction of oil from existing wells, getting a highly advantageous deal in which the government retains all the oil and pays reputable oil companies a modest service fee per barrel extracted. At the other end of the spectrum, many postconflict governments sell the rights to resource extraction through opaquely negotiated deals with obscure companies that acquire option rights to resources that they need not exploit for many years. There is considerable observable international variation in the rate of rent capture and in investment rates. Some of this variation occurs because differences in objective conditions, such as geology, affect optimal choices. However, much of the variation occurs probably because some governments make major mistakes or cannot overcome their internal problems of agency.

The Natural Resource Charter sets out guidelines on international standards for the management of resource-driven development, and also links the standards to an international process of research so new knowledge feeds back into improved policy advice. It is a useful model for more comprehensive research-informed policies for fragile states.

Construction. The construction sector is at the heart of postconflict recovery. It supplies the nontraded capital goods, mostly purchased by the public sector—such as roads, power plants, and ports—that are fundamental to modern economic activity. The inherited stock is likely to be grossly inadequate.

Because investment typically will have been low for many years, the construction sector will have withered away so that a quantum increase in demand, such as is typical of postconflict and policy reform situations, collides with limited supply. The elasticity of supply in the construction sector thus determines whether the sector becomes a bottleneck. Potentially, public policy can flatten the supply curve at several points in the production cycle of a structure: the availability of land can be impeded by unclear legal rights; the availability of key inputs such as cement can be impeded by trade restrictions or transport bottlenecks; the market structure of the construction sector can be insufficiently competitive because of government procurement practices that exclude new entrants; and key construction skills can be scarce because of market failure in training.

There is seemingly no quantitative study of the construction sector in postconflict and recovery situations, or any special attention paid to it in policy discussions. No international data set exists, so data would need to be gathered through field work.

Employment. Should employment generation be an objective in postconflict societies, and if so, how should it be achieved? While economists know plenty about employment generation in general, there is as yet no serious work on the distinctive issues raised by employment generation in postconflict situations. If employment of young men reduces conflict risk, employers confer an externality on society. Analytically, the shadow wage is below the actual wage and may even be negative. An old tradition in development economics urged the use of shadow wages in development planning. The key critique of that tradition was that rather than offset market distortions (wages being set above market levels), it was preferable to break rigidities in the labor market. However, postconflict wage distortion is not due to rigidities in the labor market, but rather a potentially very large externality.

Does It Affect the Risk of Conflict? There is now reasonable statistical evidence that both the level of income and its growth rate reduce the risk of civil war.[9] The application to the specific context of the postconflict environment poses more acute statistical problems, but

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such analysis as has been feasible finds the same associations.[10] Given the inherent plausibility of the hypothesis, and the robust evidence for it in the more general context of proneness to civil war, it seems reasonable to assume that the same relationships hold in the postconflict context, where risks of conflict are likely to be higher.

Turning from overall economic activity to employment, and in particular youth employment, there is less macrostatistical evidence of a direct link to the risk of conflict. Some studies find associations with the demographic structure of the population, with risk increased by the age group 15 to 24. While there are many other explanations for such an association, this is clearly the age group for rebel recruitment. Thus, it is a plausible supposition that societies are at risk primarily from their young males, analogous to the distinctive age and gender propensities to violent criminality apparent in virtually all societies. There is not, to my knowledge, any macrostatistical evidence linking conflict risk to the employment opportunities for young males. There is, however, arresting new evidence from a survey of the motivations for recruitment to rebel groups undertaken for the *World Development Report*.[11] The report finds that a lack of employment opportunities is by far the most cited motivation for recruitment, and is much more important than any political grievances. The hypothesis is inherently plausible from the microtheoretical perspective of choices between activities: the choice among employment opportunities is more likely to be motivated by payments (in cash and kind) than by political objectives, the payoff of which is a highly uncertain public good in the distant future.

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The Holy Grail of quantitative research would be to compare the efficacy of public resources spent on employment creation for young males against other strategies such as targeted policing. Ideally, this would come with an estimate of the rate at which the returns to each strategy diminish so they can be equated at the margin. Such precision is likely to be beyond the horizon of feasible research: decisionmakers will judge based on their best guess as to the likely magnitudes. A less demanding objective, which might just be feasible, is to show that resources spent on employment creation are cost-effective in the lesser sense of having a substantial payoff. Since the costs of conflict are known to be enormous, it follows that almost any effect of employment on conflict risk that is statistically significant is likely to be economically significant. Furthermore, since the resources during the transition from conflict come predominantly from the international community and are probably highly endogenous to evidence of effectiveness, this lesser goal may be more pertinent than the notional ideal.

How might the efficacy of employment creation for the reduction of the risk of conflict reversion be estimated? Both explanatory and dependent variables are difficult to observe. As to the explanatory variable, although the labor force data for postconflict societies is pitiful, it should in principle be possible to generate crude estimates of youth employment from the preconflict employment structure of the economy and data on how the overall structure of the economy has changed as a result of conflict. Since large differences in employment opportunities among postconflict societies are likely, even crude estimates may be revealing.

The readily observable dependent variable is the reversion to conflict. But given that any causal connection from employment opportunities to conflict is likely to run through recruitment to rebel forces, a superior dependent variable would be changes in rebel recruitment in one or more postconflict (or even conflict) countries. It should sometimes be possible to infer changes in recruitment either from studies of the composition of a rebel army (for example, at the point at which it is disbanded), or from military estimates of its size made at different times. These changes in size may be statistically relatable to observed or inferred changes in employment. A variant on the above may be to relate observed or inferred changes in recruitment to observed changes in the opportunity cost of labor. For example, it is known that during the massive Russian civil war of 1919–1921, recruitment fell and desertion peaked during harvest time.

U.S. Marine Corps (Mark Fayloga)

Likewise, in many conflict-prone societies such seasonal patterns and variations of weather and the causal connection with the opportunity cost of male labor of different age groups are clear enough.[12] On balance, the quantitative study of rebel recruitment offers more promising opportunities of convincing results than the macroapproach of observing employment and the reversion to civil war. However, such quantitative study depends upon opportune fieldwork, such as during rebel demobilizations.

Generating Jobs. One hypothesis on employment generation in postconflict settings that is potentially testable is "forgetting by not doing": that the necessary skills for employment are limited because skills atrophy during conflict, necessitating targeted employment generation policies. This could be tested by using in-country variations in the intensity of conflict to study differences in firm-level employment generation. Researchers have analyzed other factors to explain analogous fluctuations and their connection to variations in conflict intensity. Timothy Besley and Hannes Mueller used in-country variation in conflict intensity to explain variations in house prices in Northern Ireland.[13] Edward Miguel and John Bellows researched variations in conflict intensity in Sierra Leone to explain variations in political participation.[14] Marguerite Duponchel and I have attempted to relate data on conflict variation to firm-level employment data.[15] Unfortunately, the only employment data, from a survey conducted by Duponchel, contains limited pertinent information. Controlling for other characteristics, firms in conflict areas shed employment more rapidly during conflict and in the postconflict period have a higher demand for training. This suggests that conflict has destroyed skills. There is scope for a purpose-designed, firm-based employment survey in a postconflict society to use variations in conflict intensity to develop such ideas more thoroughly.

If skill shortage is a major constraint for firms, the policy implications are reasonably clear. At low levels of per capita income, investment in generic skills is well understood as problematic: firms are reluctant to finance it because the returns accrue to employees, while employees are unable to finance skill acquisition themselves because they face financing constraints. One option for targeted post-conflict employment generation policies is to encourage the return of emigrants who have maintained and acquired skills while abroad. Another approach is to subsidize in-firm training. A third is to establish government-financed technical schools.

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Government Capacity and the Provision of Basic Services

The constraint on enhanced delivery of basic services in low-income fragile states is not necessarily financial, but rather is a challenge of capacity and incentives. As the Public Expenditure Tracking Surveys of the World Bank have shown, often only a small fraction of the public money allocated for services such as education and health care actually is spent for this purpose.

The provision of basic services raises difficult issues concerning the performance of employees and how costs are financed. If public servants have not internalized the goals of the organization, there are few other means of providing incentives to perform. During the 1990s, the approach favored by donors to address the problem of a dysfunctional public sector was to introduce standard market discipline through cost-recovery—that is, users would purchase services. This approach has generally been found to be a mistake. The poorest households are not in a position to purchase services at levels appropriate to actual costs. Furthermore, providing free services potentially maximizes usage, thereby enhancing public perception of government capacity. However, policy has not yet shifted to the corollary of how, if services are not to be sold through the market, service-providing organizations are to be disciplined into being cost-effective. There are various ways of providing such a discipline.

One is conventional civil service reform, introducing performance targets and rewards. In nearly all of the societies that currently lack adequate state capacity, this approach has been encouraged by donors for the past four decades. It has proved to be difficult for three primary reasons. First, poor performance may well be a locally stable equilibrium. Second, the target-reward system is easy to game because individual performance is difficult to monitor. Third, incentives may further undermine intrinsic motivation. It is time to think of alternative approaches for providing incentives for building such capacity.

The radical approach often favored by economists is a voucher-type system for schooling and insurance for health care. There has been some research on this model, although not, I think, in the most difficult environments. An advantage of this approach is that it would enable the provision of services to be private while finance would be public. However, while it may be the best solution in some contexts, it faces both political and administrative obstacles that make it infeasible in most countries.

An intermediate approach involves Public Service Agencies (PSAs) contracting and monitoring.[16] The PSA channels public money from donors and the host government to organizations that provide the services, including nongovernmental organizations, churches, local governments, and firms, while monitoring their performance. Hence, the assessment of organization performance is undertaken centrally rather than by users. Since the PSA is allocating resources, it can also set criteria such as standards, geographic coverage, and unit costs. Hence, the PSA provides the government with more direct control than a voucher/insurance system, and yet, as with the voucher/insurance system, it does not necessitate the public sector directly providing the services.

There is a lot of research testing specific interventions that might improve the performance of public sector employees in specific contexts of developing countries, but little that evaluates alternative systems. The work of George Akerlof and Rachel Kranton on employee motivation has not been substantially applied in the context of the breakdown of public sector performance.[17] What is needed is not simply smart individual rational choice theorists, but a larger research program in collaboration with a government that is interested in experimenting with not only minor innovations but also greater reform involving alternative systems.

Such opportunities can only come about at times of structural change, such as early postconflict years, new governments, or natural catastrophes, when governments face up to the wide gulf between their aspirations and what reasonably can be achieved.

Conclusion

Since stability and economic security in postconflict settings are high international priorities, and given the link with income level and growth rate, donor funding is likely to be found for whatever approach can be shown to work to raise the income level and growth rate at a reasonable cost. Building domestic state capacity is the long-term goal, yet low-income societies emerging from conflict do not have the luxury to wait for such a capability to emerge. Certain economic policies can be put in place even with low government capacity to stimulate employment creation and other public goods for rapid positive effect. Establishing incentives for practical local economic reform policies, creating an environment that supports private economic investment, and enhancing the delivery of basic social services by the host government contribute to security and stability as they also build state capacity. **PRISM**

Notes

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