

# **Peace, War and International Security: Economic Theories**

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## **Abstract**

This paper considers the economic theories that are relevant for the study of peace war and international security . It presents different levels of generality, starting with the big questions of international security, which are usually the domain of international relations, before moving to general economic theoretical perspectives and then focusing on some specific developments in economics and security. More specifically it reviews the economics of security, distinguishing neoclassical theories, Keynesian and institutional, Marxist, and monopoly capital, before discussing the issues involved in the debate between the schools of thought. The economics of conflict is then considered, starting with the approach economists have taken –mainly neoclassical, before considering more general political economy perspectives.

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## **Introduction**

Peace, war and international security is an area in which economists are often conspicuous by their absence, to a degree that rivals the importance of economic issues to the problems at hand. It is getting to the point where the supposed 'imperialism' of economics in the social science (Fine, 2001) is reversed and the political scientists, international relations and other such groups exclude the economists and take on the economics themselves. It is not unusual to find studies of post conflict reconstruction in which economics is surprisingly found to be important. In the case of the World Bank it came as a great shock to the other social scientists when economists started to argue that economics might have a major role to play in understanding civil wars (Collier et al, 2003). Economics do have the gift of overstatement and a tendency to state unpleasant truths in a clear and precise way that can disturb other social scientists. Their indignation and overreaction reflected this and more recently the debate has reached a more civilised recognition of the complexity of such issues (Arnson and Zartman, 2005). This is in many ways the fault of the economics profession who have tended to build up a core set of areas in which it is easy to publish and left a periphery of areas, such as defence economics from which papers submitted to general journal are considered not to be of interest to the general profession.

In considering the economic theories that are relevant for the study of peace war and international security one has to consider the overlap between the social sciences and has to think of an organisational framework upon which to hang the discussion. One useful approach is to consider different levels of generality of the analysis. To consider the answers to the big questions of international security, usually the domain of international relations, and then to move to the general economic theoretical perspectives, before focusing on some specific developments in economics and security. This is the approach taken here. A short overview as this cannot but fail to provide an in adequate coverage of the extent and detail of theories, but hopefully will serve to bring out the main developments and their context.

The first section outlines some general perspectives on international security followed by a brief schematic outline of the main theoretical approaches. Then it considers the economics of security distinguishing neoclassical theories, Keynesian and institutional, Marxist, and monopoly capital. The second part considers the economics of military spending and the issues involved in engaging in debate between the schools of thought. The economics of conflict is then considered, starting with the approach economists have taken –mainly neoclassical, before considering more general political economy perspectives. The final section presents some conclusions.

### **I. The economics of security**

The economics of security has been developed around three different perspectives. The first, dealing with the link between the objectives of national security and economic development, where the old opposition between liberalism and mercantilism still remains relevant. The second approach uses economic models to study conflicts and militarism and the third approach considers the consequences of militarism on the growth and the stability of capitalist economies, from a Marxist, Keynesian, or institutionalist perspective.

#### **I.1. General perspectives on international relations: the opposition between mercantilism and liberalism**

An important debate has been taking place in international relations that has implications for economics. It raises the question of whether conflict is inherent to interstate relations, as stated by the mercantilists and subsequent economists, or whether the rise of international trade and capitalism support the pacification of the international relations, as suggested by the liberal view. At the beginning of

capitalism”, the dominant mercantilist perspective considered the nation state as needing to produce wealth in the form of gold and this required running trade surpluses –encouraging exports and discouraging imports in a world in which trade volumes were considered fixed. This was one of the first instances of significant government intervention in the economy and encouraged wars in Europe and imperialism as the powers fought over available markets. Clearly creating wealth would require military strength, which in turn would require economic strength. In such a system economic openness only comes with a hegemon to provide the collective goods of security and stability, but that state will only do so if it is in its own best interest (Kapstein, 1992; Goodwin, 1991; Heckscher,1955).

More recently this has developed to a neo mercantilist perspective and is linked with a realist perspective on international relations, which see countries and states motivated primarily by the desire for military and economic power or security rather than ideals or ethics. The ceaseless economic war between nations justifies economic interventionism, with trade restrictions and subsidies for national firms. The military strength may go with the economic development, through economic intelligence, technological spillovers or imperialist foreign policies. War is considered an irreducible human trait in earlier works but curable in more modern ones. In general, conflict will be inevitable unless there is some dominant hegemonic force –Pax Britannica, or more recently US hegemony (Waltz, 2000).

In contrast the liberal perspective that developed from the work of Adam Smith see capitalism as the best way to create wealth and maintain individual freedoms. Laissez faire capitalism and the global division of labour allow all to benefit from trade, it is no longer a zero sum game. States intervene because of market failure and the public good nature of defence means they have to provide it, but it is seen as costly to the economy. Globalisation promotes peace and free trade with competition both internationally and domestically. War is likely to be very costly and should disappear with the spreading of economic liberalism, as all countries would get richer thanks to the rise of international trade. This liberal economic theory is directly linked with the political theory of the society of states at an international level. Despite the condition of anarchy, in the sense of the lack of a ruler or world state, governance is provided by the key institutions that regulate international relations, treaties, diplomacy and the mutual recognition of sovereignty. This was followed by more recent developments of the idea of democratic peace (following from Kant’s perpetual peace), which implies that democracies do not fight each other. More recently the theory of democratic peace has had globalisation added to it, suggesting at first a role for multi layered governance structures to deal with weak states with anti capitalist and anti liberal attitudes which were reinforcing their backwardness in a globalising world. But more recently this has been replaced by the US hegemony pursuing democracy within states and protecting democracy from external aggression<sup>1</sup> (Gleditsch and Hage, 1997).

This new orthodoxy, which sees war as a result of pre or anti capitalist sentiments and groups; sees the solution to conflict as a global neo-liberal system; accepts that military action might be needed in the shorter run to create the right conditions (dealing with rogue states and terrorists); that sees the need to maintain the basis to produce the means of destruction through high military spending; that accepts the hegemonic role of the US is certainly not what was expected at the end of the Cold War and represents a limited view of the world that is coming into question with the continuing problems in Iraq and Afghanistan. Contrary to the predictions of the first liberal economists, the worldwide spreading of economic liberalism does not induce a decrease of world military expenditures. It was not demilitarisation that followed the cold war but remilitarisation with closer integration of the civil and the military, through homeland security and the privatisation of defence functions (Lovering, 2003). It is also not without its conceptual problems. The liberal perspective can be argued to oversimplify the nature of capitalist development –focusing on particular problems it may be fine, but for the big picture it is lacking. There are also alternatives, both idealist (as opposed to rationalist) and Marxist, the latter drawing out the importance of economic processes and emphasising the inherent tendencies within capitalism to conflict and imperialism. These are discussed below.

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<sup>1</sup> This also reflects recent Democratic peace: that have to make everyone a democracy even by force then will get peace.

Within these world views economists have often ignored the general context they operate in and how their theories fit into them. Yet clearly the discourse of international relations can often provide the context and points of reference within which debates on the economics of security take place.

## I.2. Neoclassical Theories and Arms Races

Theoretically the basic neoclassical perspective would see the state as reflecting national interests and it provides security, recognising the trade off guns v butter. Defence is considered a pure public good (though in actual fact the state is usually providing security for itself rather than the population –e.g. nuclear shelters tended to be for the state officials and politicians). There are developments of this simple perspective to arms race models, the importance of property rights, the analysis of alliances- burden sharing free riding and rational agent theories of conflict.

As is characteristic of neoclassical economics, which sees itself as the science of the social sciences providing tools with which to analyse any social setting, its approach to analysing war is ahistorical. As Hirshleifer's book starts that a basic economic problem is simply the possibility of predation and conflict, rather than production and exchange. Despite the existence of such analysis in Adam Smith traditional economics has tended to ignore the former and focus on the latter<sup>2</sup>

A related literature but one which has developed a clear perspective in which military effort can be explained in terms of one country reacting to increases of another. This started with Richardson's (1960) 'arms race' model supposes two countries whose military expenditure/level of arms/military capability,  $m_1$  and  $m_2$ , are related at time  $t$  by the equations:

$$\frac{dm_1(t)}{dt} = a_1 + b_1m_2(t) - c_1m_1(t)$$
$$\frac{dm_2(t)}{dt} = a_2 + b_2m_1(t) - c_2m_2(t)$$

Where  $a_i$  are exogenous 'grievance' terms,  $b_i$  are 'reaction' terms, whereby each country responds to the military capability of the other, and  $c_i$  are 'fatigue' terms, usually representing some internal limitations on a country's military spending/capability. Interestingly this was not well received by the US government as it implied that arms races had no 'good' and 'bad' guy but were simply the result of one reacting to the other. This basic model has been developed theoretically and empirically in a variety of ways, including the explicit modelling of rational economic decision-making, different dynamic specifications, game theory approaches, and empirically with the use of approaches such as co-integration. The search for clear empirical evidence of 'arms races' has, however, met with rather limited success, with even apparently obvious examples as the Cold War superpower arms race proving ambiguous and very much dependent on specification<sup>3</sup>.

An early attempt to deal with strategic effects more generally by Rosh (1988) developed the concept of a security web where, instead of dyadic relationships neighbours and other countries (such as regional powers) that can affect a nation's security as being part of a country's Security Web. Rosh calculates the degree of militarisation of a nation's Security Web by averaging the military burdens of those countries in the web, finding it to have a significant positive effect on a country's military burden. More recently, a

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<sup>2</sup> In addition we could consider new classical theory tends to take a rather different perspective as it considers transitory and permanent shocks to the growth of the economy and recognises war as a permanent shock.

<sup>3</sup> India and Pakistan provides one of the few examples where researchers have been able to provide consistent evidence of a Richardsonian arms race. Numerous attempts have been made to estimate arms races for Turkey and Greece, using a variety of theoretical and econometric models, without clear evidence of an arms race emerging (Brauer, 2002; Dunne, Nikolaidou and Smith, 2005)

number of authors, including Dunne and Perlo-Freeman (2003a and 2003b) and Collier and Hoeffler (2002), have sought to generalise the concept of an arms race by looking at the demand for military expenditure across a large group of countries, using either cross-section or panel data, incorporating a range of economic, political and security variables, and including variables for the aggregate military expenditure of neighbours and rivals. These models have typically shown that a country's military expenditure is significantly and positively influenced by that of those around them. Dunne and Perlo-Freeman (2003b) break this down, finding that the significant positive influence comes through the military spending of 'Potential Enemies'<sup>4</sup>. They suggest that this indicates, if not an arms race as such, then at least arms race-like effects, or spillover effects, where there is some tendency towards an action-reaction pattern of military spending between hostile nations. In addition, Murdoch and Sandler (2002, 2004) have focussed on the 'spillover effects' of military spending. Dunne and Smith (2007) provides more detail on the econometric issues.

### **I.3. The analyses of the role of militarism on capitalist economies**

Whereas the liberal perspective grants little importance to military expenditure, other schools of economic thought emphasised the specificity of this particular form of public expenditure and its role in the long-term survival of capitalism.

#### ***Keynesian, Marxist and Institutional Economists***

A basic Keynesian perspective would see military spending as one component of government spending, with effective demand/multiplier effects. In this way military spending can be good for an economy, getting out of recession and helping plan expansions in effective demand. It is generally accepted, however, that war would have a negative impact upon the economy. This approach has also been combined with a form of institutional analysis which would take it beyond a liberal perspective and sometimes close to the underconsumptionist theory discussed below (Pivetti, 1989, 1992).

In response institutionalists have provided a more complex understanding of the processes at work and the role of military power and conflict<sup>5</sup>. The institutionalist perspective is predicated on existence of MIC (Eisenhower), where internal pressures for increases in military spending and forces are independent of threat. They create inefficiencies in the economy and so can have negative economic effects, particularly as the nature of defence production changed during the cold war and became very different from civil). This can also have other externality effects through influences on the civil sector and crowding out (Melman, 1970; Dunne, 1995) A more Marxist interpretation, would suggest that the capitalist mode of production still would not necessarily be wonderful if military spending and the MIC were removed.

Melman (1974) underlines the harmful effects of militarism on the American economy such as the loss of competitiveness, the development of the bureaucracy, the fall in productive investment. Evoking the development of a militaro-industrial complex, he uses the concept of a "permanent war economy", with limited spillover effects from the military to the civil sector. Similarly, Dumas (1986) presents the military production as an economically non-contributory activity, which channels valuable productive resources and their outputs. The opportunity cost of the military activity is measured by the economic value that could have been created by using the same labour and capital for consumption or investment.

#### ***The Marxist perspective***

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<sup>4</sup> Which includes actual enemies

<sup>5</sup> This literature overlaps with the Marxist perspective outlined below.

The Marxist perspective is rather mixed. Indeed, Marx had little to say on militarism and it was Engels who provided most of the specialist writing even when jointly penned. His main statement is in *Anti-Duhring* and was influenced by Clausewitz, though there he argued there were no benefits to war only the prospect of financial ruin, Wars were won by technology, but this led to ruinous arms races, such as the Dreadnoughts (Engels, 1987). Militarism can certainly be considered as having an impact within the context of Marx's crisis theory, but this gives a complex story, with different form of crisis (financial collapse, long waves, cyclical downturns) and mechanisms (realisation, distributional, rising OCC, disproportionalities). These are usually not monocausal but the backdrop is the law of the tendency for the rate of profit to fall plus countervailing tendencies and militarism can potentially have positive or negative effects. As a result there have been considerable disagreements among Marxists.

Following Marx, Kautsky considered the need for capitalism to expand its markets by colonial expansion but suggested that this plays a contradictory role, as it has costs. Boosting consumer demand benefits capitalists but they will resist if it is funded by a tax from profits. Lenin developed his analysis of imperialism from Kautsky, essentially providing a pseudo mercantilist view that war is the continuation of economic competition by other means.

Luxemburg offered an analysis based on the expanded reproduction schema, suggesting that there could be positive effects depending how military spending was financed. Taxes on workers change composition, taxes on profits reduce overall profit, deficit finance will provide demand stimulus if below full employment. There would also be social and ideological benefits and military spending provides an external market. She stated that the military sector made it possible to release a surplus that is generally higher than that which would have been obtained in other sectors. But at the same time, the fixed capital becomes increasingly significant relative to the variable capital which is, in the Marxist theory, one of the factors of the fall of the rate of profit in a capitalist economy. It is thus necessary to distinguish the short-term effects of militarism, which are beneficial, and the long-term effects, which are negative, since they accentuate the internal contradictions of the capitalist mode of production. Bukharin developed an opposing view, arguing that military expenditure cuts into surplus value and so hinders reproduction and so rather than helping realise surplus value it destroys the production of value.

Luxemburg's contribution has given rise to controversy: for some economists, it is a theory of underconsumption, with military expenditure a way to invest the surplus without increasing production capacities. For others the theory shows the important role of military expenditure as a stimulant of the capital accumulation, by its encouraging technological progress and destroying the internal obstacles to capitalist expansion. By 1939 the Stalinist orthodoxy was underconsumptionist, as it suited Stalin to see the West as needing military spending to overcome crisis and so to be economically dependent on its military spending (Semmel, 1981)

The debate continued after the Second World War, with some Marxist economists defending the idea of a positive impact of military expenditure on the capitalist system, presenting militarism as a factor in the stabilization of capitalism. Kidron (1969) focusing on the threat of overproduction, rather than underconsumption, saw military spending as diverting capital from accumulation so creating a 'permanent arms economy'. Thus, overproduction and unemployment were contained in the 1950s and 1960s thanks to a high level of military expenditure, which prevented over-investment and which generated technological spillovers to the civil sector, while favouring exports. While military expenditure slowed down economic growth, by inducing a high level of profit tax, it also slowed down the growth of the organic composition of capital in civil activities, by diverting resources which could have been used for the productive investment. Thus, the permanent arms economy represents a powerful means by which to thwart the fall of the profit rate.

The theory of underconsumption is the only economic theory that has military spending as an integral and important part of capitalist system. Based on Baran and Sweezy (1966) 'surplus' approach to Marxist

analysis<sup>6</sup>, that emphasised the monopoly nature of the post war system, this approach saw military spending as important in preventing realisation crises, through absorption of surplus without raising wages or capital. Other government expenditure could not do this. Baran and Sweezy were more circumspect than later proponents of the effective demand/underconsumption Pivetti (1989b) and Cypher (1987), who suggest that military spending conscious instrument of economic policy and military spending has a stimulating effect on economy<sup>7</sup>.

Later long wave analyses were developed from Kondratief's attempts to periodise cycles of capitalist development. Mandel seeing high organic composition of capital in military production accelerating the decline in rate of profit, and the wave of post war prosperity resulting from countervailing tendencies. In a more general analysis the Regulation school, argued that regimes of accumulation existed, coordinating production and consumption and dealing with the contradictions between the forces of production and social relations. They identify a move from competition to monopoly regulation, with changes in the nature of the superstructure and governance (Aglietta, 1987 ; Lipietz, 1987). In the US the Social Structures of Accumulation School of saw an accord between capital and labour, that allowed prosperity in the US, though country and historically specific (Bowles et al, 1985; Kotz et al, 1994). Neither of these two approaches explicitly focused on military spending, but Serfati (1995) developed the regulation approach to consider the military industrial complex within the globalised world economy. Rather it is just one facet of US hegemony which was a factor in the post war "Golden Age". One can integrate military spending into the analysis but it is very different to the story told, particularly defence production. There are indirect benefits for the US from its international hegemony that outweigh the direct costs, but they are at the expense of the economy and it was these negative effects on the economy that showed up in the long run. For Europe these indirect effects were less clear

Even if one rejects the specifics of the Marxist analyses it is still possible to see Marx's method as providing valuable contributions to understanding the economics of international security. To see the processes as historically specific, contingent rather than deterministic and as contradictory/dialectical processes which reflect the balance of power between groups within society. It is interesting that this is close to the approach Kennedy (1987) took implicitly, seeing empires as growing as a result of their military development, through building empires, but in the end empire overstretch forces them into decline.

## II. The Economics of Conflict<sup>8</sup>

The international strategic environment has become considerably more complex since the end of the Cold War. In the industrialized countries, armament industries and armies have been transformed, while elsewhere there has been the emergence of new actors, such as terrorist groups and the "lords of war", as well as a multiplication of the new conflicts, often internal rather than inter-state. All of these have presented a challenge to contemporary economic analysis and this section considers how economists have responded, to understand the causes, conduct and consequences of conflicts; to identify the characteristics of new conflicts; and to consider the economics of peace.

### II.1. The causes, conduct and consequences of conflicts

There have been three strands to the linkage between economics and generalised conflict that can be identified, namely the consequences, causes and conduct of war (Dunne et al, 2006). The first strand is the need to understand the causes of conflict, particularly when there may be economic elements in those

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<sup>6</sup> Basically identifying value with observed quantities, so for example profit in price terms is seen as the money representation of surplus value. (Baran & Sweezy, 1966)

<sup>7</sup> Evidence goes against this but that certainly didn't bother Pivetti. See Smith & Dunne (1994) and Pivetti (1994)

<sup>8</sup> This section is based on early versions of Dunne, Garcia Alonso., Levine. and Smith (2006).

causes. The liberal view can only explain interstate conflicts as resulting from unjustified trade measures or of a foreign policy contradictory with the general interest of the population. The mercantilist-Leninist view presents war as the continuation of economic competition by other means. Also institutionalists would see conflict as likely because of the vested interests in the MIC. Though interestingly in the Cold War the last thing anyone wanted was to use some of the advanced weapons systems in earnest –they often did not work, as in the case of early cruise missiles. Recently, some economists have explained civil war in poor countries as often driven by attempts to control natural resources like oil or diamonds<sup>9</sup>.

Most economists have tended to ignore issues of conflict and security, often assuming exogenous provision of property rights, that is that there is a sovereign or state whose duties include protecting the society from the violence or invasion of other societies and establishing a legal system which administers justice and enables exchange and investment to proceed with security<sup>10</sup>. This may be a reasonable first approximation for some times and places, but is certainly not for others, including much of the world today. However, there is now a fairly large literature concerned with endogenous property rights. When conflict is an option, the resulting distribution of property reflects agents' ability to protect their resources from others or steal resources from others. The simplest models have individuals who can allocate their time between investment in growing food, stealing food from others and defending the food they have from theft by others. Typically the models will have a number of agents each subject to a budget constraint, with production possibilities for various goods, including military ones and exchange possibilities. This includes attempts to understand civil wars, Collier (2000), Gershenson et al. (2000), Sambanis (2002); to integrate the models of production and exchange with models of conflict and struggle, Rider (2002); to understand intervention in conflicts by third parties (Siqueira 2002); to consider issues of terrorism, organised crime, post-conflict demobilisation and reconstruction, etc.

A common formulation is that the objective function of a state, say welfare, depends on consumption and security, a function of own and opponents armed forces. Welfare is maximised subject to a budget constraint, thus determining the optimal level of armed forces. Security can have many levels depending on what the threat is<sup>11</sup>.

The second strand is the use of economic analysis to improve the effectiveness of the prosecution of war. This runs from Adam Smith's discussion of the relative effectiveness of standing armies and militias to twentieth century applications of economics, and other types of applied mathematics, to develop effective military tactics and strategies. The application of game theory to nuclear targeting is a classic example; von Neumann was the model for Dr Strangelove.

In the literature which deals with potential conflict with an identified enemy the analogy to the production function is the conflict success function, CSF: the inputs are the investments in fighting efforts of the two sides and the outputs are their relative degree of success in the conflict: either the probability of winning or the share of the pie that goes to each side<sup>12</sup>. While there is a vast military literature on success in battle, there is relatively little econometric work on conflict success functions<sup>13</sup>.

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<sup>9</sup> See Kaldor (1999) and Collier (2000)

<sup>10</sup> Coulomb (1998) discusses Smith's writing on defence economics, which showed a clear awareness of the need for security before trade could take place.

<sup>11</sup> From 1945 to 1989 the central concern was the potential conflict between NATO and the Warsaw Pact; a classic arms race between two militarised powers. In many parts of the world, such arms races continue to be important. Other countries face internal threats against which military preparations are effective. These are mainly poor countries, but also include Spain and the UK. Some countries, such as the US feel threatened by external non-state actors. Some states want to project power to intervene for human rights or other ways, while some, such as the small European powers, have no obvious threats but retain military forces as a general insurance policy. Given US military dominance there is a natural international concern about what its security objectives in fact are.

<sup>12</sup> There are two main functional forms used in which success depends either on the ratio of the forces or the difference of the forces. Hirschleifer (2000) provides a discussion of CSF, with many military and non-military examples, which captures the spirit of the literature.

<sup>13</sup> An exception is Rotte and Schmidt (2002), who use a data set of 625 battles 1600-1973 to estimate an equation to explain victory by the attacker in battle: a zero one dependent variable. The explanatory variables include the force-ratio of the two sides and expert assessments of relative advantages in leadership, surprise, morale, logistics and intelligence which were



One problem with this type of analysis is that it either treats aggregate military strength as a single aggregate, or distinguishes just between labour and capital, members of the armed forces and their equipment. In fact determining the optimal force structure involves four main choices for both labour and capital. The first choice is the number of varieties of types of forces: army, navy, airforce, each made up of specialised types of soldiers, sailors and airmen, each with distinct roles and associated equipment. There is some substitution between these varieties, a target may be destroyed by a tank shell, a bomb dropped from an aircraft or a cruise missile launched from a submarine. The second choice is the quality of those forces, determined by R&D for equipment and training for labour. The third choice is the quantity of each. The final choice is whether they are obtained domestically or from abroad. This choice is primarily important for equipment, where security of supply for spares in case of conflict is often important, but does occur for labour for those countries that use foreign soldiers<sup>14</sup>.

The third strand is the need to understand the economic consequences of War and adjust policy accordingly. From Ricardo on the Bullion Controversy, provoked by the suspension of the Gold Standard during the Napoleonic Wars, through to Keynes, on how to pay for the Second World War, managing the war economy has been a central question<sup>15</sup>. Within much of the developing world, particularly Africa, civil wars are a major cause of economic dislocation and the international financial institutions are struggling to come to terms with this linkage. In particular, managing post-conflict reconstruction and providing incentives for combatants to return to civilian life has proved difficult<sup>16</sup>. We shall return to this below.

## II.2. The new economics of conflict

The period since the end of the Cold War has seen major changes in the economics of preparing for war. New threats appeared, budget constraints changed with large cuts in military expenditure during the 1990s, major innovations in military technology took place, and they resulted in changes in the structure of the arms industry, the armed forces. Two concepts became central to in the development of military discourse, the Revolution in Military Affairs (RMA), the term used for the way that changes in technology were transforming fighting, and Asymmetric Warfare, the term used for the way that opponents would respond to a dominant military power by fighting in ways that the dominant power did not expect or prepare against. Several examples, like certain African conflicts or the attacks of September 11, showed that the technological superiority was not a guarantee of security nor of victory in the event of war. However the RMA testifies to a constant search for technological improvement by major powers and the existence of hostile zones to the mode of Western development has led to a persistence of instability, with a return of the strategies of predation.

### *The RMA*

The RMA is potentially the latest of a sequence of technological changes that have transformed the military<sup>17</sup>. Such revolutions usually also change the balance of power, as one group or country adopts the new technology faster than their antagonists and use it to change the way war is fought. The technological changes can involve new products, like the tank, or new processes, forms of organisation, like Blitzkrieg,

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significant; and training, defensive posture, and technology, which were not significant. The estimates bring out the importance of the intangibles of battle: leadership, morale, etc; but even with all these included the fit is low, with a pseudo R squared of less than a third: outcomes of battles are relatively unpredictable even with the benefit of hindsight. As they point out there is a sample selection problem. We only observe a battle when both sides think they have a reasonable chance of winning, otherwise it does not take place.

<sup>14</sup> Such as the UK with the Gurkhas and France with the Foreign Legion.

<sup>15</sup> Indeed Stone (1988) refers to work by Gregory King in 1695 on the question of how long England could sustain the war against the league of Augsburg.

<sup>16</sup> See Harris (1999)

<sup>17</sup> Definitions of the RMA tended to emphasise the way that improvements in information technology, precision targeting and smart munitions created the possibility of a new form of network-centric warfare.

that make better use of existing products. In the military, process innovation tends to be much slower than product innovation, particularly in peace-time. In general, new technologies have been most effective when used in ways that are unexpected by the enemy and have often been associated with the rise of new revisionist powers.<sup>18</sup> Actual weapons are very R&D intensive: small performance advantages over the enemy can translate into victory, but getting that last 5% of performance is very expensive. This produces a race to improve technology and the real cost of weapons has grown at between 6 and 10% per annum between generations. Because the weapons are so expensive the gaps between generations get longer and as a result much military equipment is very old.<sup>19</sup>

Old economy military technology was very centralising; rapid cost growth between generations of weapons means that almost nobody, not even the US, can afford it. Most military equipment is obsolete in commercial terms before it enters service, because it takes on average seven years to develop and deliver it<sup>20</sup>. Current fighting power is very much old economy, the question is whether this will change and what a new economy military might look like. The new-economy civil industries tend to have high fixed costs but low marginal production costs, eg software is expensive to develop but cheap to produce in quantity. They tend to have network effects, the more people who use the product the more effective it is, and innovation tends to be a series of winner-take-all races. At any moment in time a single firm, which produced the killer application, tends to dominate the market; but when innovation is rapid their dominance is precarious<sup>21</sup>. Most weapons production does not show these characteristics. Although they do have high development costs, they are also so costly to produce that they are limited to small batches with long gaps between generations. A further consequence is that innovation is slow. The defence industry is fragmented and the market leaders are the same old firms who have been producing weapons for decades. The arms industry is still waiting for the killer applications that displace most of the competition, typical of the new economy<sup>22</sup>.

Cost is central to the RMA and it is there are clear issues of affordability, especially as governments continue to support legacy weapons systems<sup>23</sup>. Government's attempts to make defence more affordable include acquisition reform; use of commercial-off-the-shelf, COTS, technology; improved logistics and the like, which, it is hoped, will generate a revolution in defence business affairs which will pay for the RMA, but history of past procurement reform does not encourage optimism. A recurring theme in military procurement reform is the attempt to learn from the commercial world and the thrust of reform has been to commercialise the military, by importing private sector practices into military organisation. However, because military time-horizons are so long, much of the equipment is old and there are major problems of obsolescence, since commercial markets, particularly in electronics, do not support systems and devices designed to last for decades<sup>24</sup>.

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<sup>18</sup> For example the Japanese defeat of the Russians in 1905, through the use of the latest technology and a more effective strategy. Also while some military revolutions concentrate power, because the equipment is so expensive and specialised that only an elite can afford it; the rise of the armoured knight in their siege-proof castles, for instance. Other revolutions disperse power as they put cheap capability into mass hands; the guns that displaced the knights and castles (Freedman, 1994 ; Parker, 1988).

<sup>19</sup> e.g. the B52, still being extensively used, is a 1950s bomber with newer avionics and weapons.

<sup>20</sup> Eurofighter, not yet in service, is based on early 1980s designs; and when it enters service, it will do so without its main missile, Meteor, which is mired in collaborative politics.

<sup>21</sup> Netscape fell to Microsoft and Yahoo fell to Google. Bresnahan and Greenstein (1999) discuss some of these issues.

<sup>22</sup> There are some new economy elements. The Global Positioning System, GPS, is a system of military satellites that has spawned a myriad of commercial applications. The system was expensive, but receivers are cheap. GPS was crucial in the 1991 Gulf War. For the first time in desert warfare, commanders could rely on soldiers knowing where they were.

<sup>23</sup> Mathews and Treddenick (2000) in their collection of essays on managing the RMA conclude 'ultimately, however, managing the RMA means finding the resources to make it a reality' (p97) and, 'a technical revolution is only feasible if it is affordable' (p4). Some spreadsheet simulations for NATO countries provide the conclusion: 'Given the RMA is assumed to be characterised by increasing equipment intensity, it appears that no country, including the US, would be able to undertake the RMA without either significant reductions in personnel numbers or significant increases in defence budgets, or some combination of both' (p113).

<sup>24</sup> The Department of Defense has a special programme DMEA (Defense Microelectronics Activity) for the manufacture of replacement parts no longer supported by the commercial market.

The changes taking place are significant. During the 1991 Gulf War 9% of the ordinance dropped consisted of 'smart' (precision-guided) munitions, while in the 2003 Iraq war it was over 90%<sup>25</sup>. The increase in sophistication and cost of the most advanced military equipment, means it is impossible even for relatively rich countries to maintain a comprehensive defence industry the nature of confrontations and conflict has changed. It is unlikely that two sets of allies will face each other with similar weapons and tactics, as in the two world wars. It is more likely that there will be an asymmetry between antagonists and this will likely change the nature of the conflict<sup>26</sup>.

### *The new wars*

The idea of asymmetric warfare is not new but the changing nature of conflict in the modern world, for example in Iraq, suggests that asymmetric responses are likely to become increasingly important.<sup>27</sup> Definitions have emphasised asymmetries in technology, what each side fights with; asymmetries in tactics, how each side fights; or asymmetries in the stakes, the costs of defeat to each side<sup>28</sup>. Much of the military discussion prior to the coalition attack on Iraq in Spring 2003 centred on the extent to which Iraq could neutralise technological superiority by using guerrilla tactics and urban warfare.

The challenge to researchers is to develop models that can deal with such asymmetries and provide insights into the behaviour of adversaries. Dunne et al (2006) develop a game theoretical model that attempts to capture the main features treating asymmetric warfare as involving either different technologies, types of weapon, or different tactics, ways of fighting, though in practice it may often involve both. The contestants are also asymmetric; there is an incumbent and a challenger: government facing potential rebels, dominant power facing potential revisionist power. Such conflicts are often characterised by periods of armed peace interspersed by outright war as one or other side of both sides decide to attack. Fighting over a prize, e.g. the revenue derived from a natural resource such as oil, diamonds or drugs, each side has to invest effort in preparing for conflict and chooses its tactics (or technology) and its military strategy: attack or defend. In the first period the incumbent makes decisions on effort and tactics; in the second period the challenger makes decisions about effort and tactics, conditional on those of the incumbent; in the third period they simultaneously decide to attack or defend and receive their payoffs.

The asymmetry arises because one side can gain an advantage by choosing to fight in a way that the opponent is not prepared for, i.e. choosing tactics very different from the enemy<sup>29</sup>. Such a situation is most likely to arise when the conflicting powers are themselves asymmetric in nature. The most likely scenario is an incumbent power with dominance in available resources, but committed to a certain type of technology, and a smaller challenger, with limited resources but more flexibility in choice of technology. Most incumbent powers one could think of tend to have military capabilities whose characteristics are very similar and when similar sized powers engage in conflicts or arms escalation they do so with those

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<sup>25</sup>Both the strap-on kits, JDAM (the GPS guided Joint Direct Attack Munition) and WCMD (Wind Corrected Munitions Dispensers) were cheap in military terms because they used more commercial development programmes and commercial components

<sup>26</sup>The military distinguish three levels of analysis: the strategic, the conduct of the war as a whole; the operational, the conduct of a campaign; and the tactical, the conduct of a particular engagement with the enemy, e.g. a battle. Since the meaning of strategy is different between the military and game theorists, who use it to refer to state contingent moves, we will always refer explicitly to military strategy, rather than strategy, when we refer to the planning of a war as a whole (Dunne et al, 2006).

<sup>27</sup>Indeed, one feature of the Lanchester square law formulation is that numbers matter more than technology.

<sup>28</sup>Despite having massive technological and military superiority; the US withdrew from Lebanon in 1983 after a suicide bombing killed 241 troops and from Somalia in 1993 after a battle in Mogadishu, in which television covered the brutal treatment of two American corpses and one injured prisoner. In neither country did the US have large stakes.

<sup>29</sup>For instance, before World War II, French tactics were largely defensive based on the Maginot line, which the Germans outflanked with a Blitzkrieg attack in 1940 defeating superior British and French forces. In the late 19th century, the machine gun was a major technological advance, which gave the British a great advantage in Colonial Wars; but the Boers were largely able to neutralise this advantage through their tactics and although the British did eventually win it was a longer and more expensive war than they expected.

very similar technologies. The Cold War, for instance, was mainly a vertical arms race, with similar types of technology on both sides and effort/quality the main strategic variable (Walker, 1994). Having invested considerable resources in a particular conflict technology and having developed the industry to produce it (and export it), incumbent countries would find it difficult to change (Dunne et al, 2006).

The post-Cold war era has led to many other changes in the nature of conflicts. Within the wider literature the political economy of conflict underwent considerable changes as it confronted the post Cold War environment. The end of proxy wars and superpower involvement had not reduced conflict, though it had reduced their intensity, it had changed them. Civil or intra state wars were the most common and the nature of war had clearly changed. Kaldor (1999) considered the new wars to be very different and only understandable within the context of political economic and military globalisation. There was a blurred distinction between war and organised crime and while local the wars tended to have a transnational connection. There were no real military battles as in the past but skirmishes and in general civilians were targeted by militia. New war economies were seemingly based upon plunder and black marketeering and sometimes supported by aid and were sustained through continued violence. This was not helped by the tendency of the 'international community' to work with the protagonists to broker peace deals rather than the civil society that existed outside of the conflict (Kaldor,2006).

A harder look at the endemic and continuing conflicts in Africa was particularly challenging and it started to become clear that the continuing struggles needed some source of income, that this was often resources and that it was possible that the resources control had become the object of the struggle overtaking any previous goals. That it was not a breakdown of the system but a way of creating a new system of income and profit and power. When the World Bank group led by Collier started to investigate the economics of civil war starting what became known as the greed versus grievance debate there was a profound impact on the subject area. Collier and Hoeffler produced a series of careful and detail empirical studies which looked at the cause of conflict and explanations for their continuation/duration<sup>30</sup>. The results suggested that it was greed (often represented by the proportion of primary commodities in GDP and other such indicators) rather than grievance that explain civil wars. There was little impact of the factors that had tended to be assumed of primary importance in the past. There was a furious response and a lively debate. The results was to accept that grievance may be involved in starting conflicts, but that that they are likely to be captured by more economic concerns over time. Collier (2000) focuses on feasibility durability and opportunity of civil war explained by greed rather than actual start of conflict. More recently their work has become more nuanced as better data has become available and Collier and Hoeffler (2008) emphasises opportunity. When this work was being produced there was no real reason why this should have been done in the context of a neoclassical model of rational agent, other than publishing in the economics journals, but it was<sup>31</sup>. A lot of the responses were not. Cramer (2002) makes an interesting point, from a Marxist perspective, arguing that some conflicts may be the primitive accumulation stage of development, that concentrates wealth to allow industrialisation and, while painful, may be a necessary part of development, rather than some simple greed or grievance trade off .

Important findings came out of these debates that have important implications for policy. It is important to recognise that war economies have a logic and incentive structure, that shell or shadow states exist as do commerce and trade links and financial links within such structures and that the distinction between criminal and non criminal transactions is rather blurred in such environments. It is important that international agencies recognise this and that the design of peace accords reflects this complexity. Otherwise policies will have unforeseen and potentially catastrophic effects, for example criminals may be maintaining vital trade links within a conflict zone, to simply normalise trade relations without proving an alternative could lead to serious problems, such as famine in particular local areas (Duffield, 2001).

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<sup>30</sup> For example Collier and Hoeffler (1998) and (2002)

<sup>31</sup> It is also interesting to note the materialist nature of the analysis, that conflict should be understood by material rather than ideological consideration, that could almost place it in the Marxist fold.

### II.3. The economics of peace

We saw earlier that concepts of eternal peace and the democratic peace, suggest that peace is a normal state for republics and democracies. In general one would have to see peace as the absence of war and the schools of thought would differ on how this is perceived. The mercantilists would certainly see conflict as inevitable and peace as the gap between wars, with realists taking a Clausewitzian perspective on war as the extension of politics. Marxists would also suggest a conflict ridden development process of capitalism with some arguing for tendencies to armed conflict through attempts to overcome inherent contradictions and crisis, including new forms of imperialism, though not all. Institutionalists would see the MIC vested interests creating arms spending in economies, though it would not necessarily be in anyone's interest to go to war –though it could be. Liberal and neoclassical perspectives would see peace as the best situation for accumulation and so seek to identify economic incentives for it.

In terms of the effectiveness in the prosecution of peace this will clearly require the development of peacekeeping and peace making forces and related equipment, which could be very different to what is available now and have implications for the nature and extent of the DIB and its related vested interests. In addition, The development of international governance structures that operate considerably better than those at present will be required as well as the recognition of wider concepts of security. To develop successful policies and support for post conflict reconstruction (following from previous discussion) it is clear that we have to understand economics of war better to make a better job of designing and maintaining peace accords and designing reconstruction packages that makes the incentives of peace greater than those of a return to war<sup>32</sup>.

During the Cold War there was considerable debate about the economic impacts of reducing military spending and how to deal convert resources to civil uses. This now seems like a strange debate as the argument that cutting military spending would lead to significant economic problems is difficult to argue given the degree of cuts after the Cold War and the relative success of the affected economies. There are of course transition costs but these are no longer seen as significant. Swords to ploughshares is no longer considered sensible, but the macro, and meso conversion policies of industrial restructuring relevant. It is an interesting debate to look back on and there are some useful analyses (Gleditsch et al, 1996)

Peace does not necessarily mean demilitarisation and reduced military spending, but if it does then the evidence suggests improved economic performance is possible. It is in fact likely to lead to moving resources away from existing defence industrial bases to other civil sectors and this should have positive effects. It should also allow the focus to move from military to alternative concepts of security, such as human and environmental. This could improve the situation for developing countries as well as the poor in developed countries. It could also provide increased demand for industry, through investment in alternative technologies. This could also allow policies to reduce inequalities, support sustainable development etc and so improve the economic situation for all countries. Improved trade and wealth should reduce the likelihood of conflict, but the experience of this century does make one wary of making such statements with confidence. Nevertheless, it is difficult to see anything but economic benefits resulting from peace.

### III Conclusions

This paper has considered the economic theories used to understand peace war and international security. In doing so it started by outlining the theories that dominate international relations and provide the context for economic debate. It then identified a number of different schools of thought that differ in their understanding of the nature of international relations and the propensity for conflict. The dominance of

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<sup>32</sup> See the papers in the Economics of Peace and Security Journal (2006).

the neo conservative perspective seems to be on the wane, but the context for the debate on the economics of conflict still remains a liberal realist one, with an expectation of democratic peace.

Economics theories of conflict are seen to provide very different perspectives but do provide useful insights into aspects of national and international security. They also provide tools with which to analyse the new developments in the international security environment, namely the Revolution in Military Affairs and Asymmetric Warfare. It is also possible to develop the framework to analyse the economics of peace and some pointers have been provided of the issues that need attention.

Clearly economics has an important role to play in this area, despite the dominance of other subject areas in the general debate. What is needed is more recognition of the importance of the economics of security and the value economists can bring to the existing literature, but also a recognition of the value of the contributions of the other subject areas, by economists. One only has to read copies of the Economics Peace and Security Journal ([epsjournal.org.uk](http://epsjournal.org.uk)) to see the important contributions economists have made and the range of subject areas that require their attention, eg issues on water conflict, peacekeeping and peacemaking. It is to be hoped that economists continue to take up these challenges and make a contribution to the achievement of security and peace in the modern world.

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