

# LIBERALISM IN THE POST-9/11 WORLD\*

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## Abstract

*The current approach to the war on terror is largely ineffective. Central to this approach are negative sanctions against actual and potential terrorists coupled with attempts to spread liberal democracy through war, occupation and reconstruction. We argue that negative sanctions are unsuccessful and in many cases counter productive in reducing terrorism. Further, we postulate that efforts to impose liberal democracy in weak and failed states via occupation and reconstruction have in large part failed. Only by returning to a position of principled non-intervention can the war on terror ultimately be won. (JEL: B 52, B53, O17)*

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## I. INTRODUCTION

Defined by the U.S. Department of Defense as the “unlawful use of – or threatened use of – force or violence against individuals or property to coerce or intimidate governments or societies, often to achieve political, religious, or ideological objectives” (quoted in Frey 2004, pp. 9), terrorism has a long and storied history.<sup>1</sup> The term ‘terrorism’ originated during the French Revolution’s “Reign of Terror” (1793-1794). In that period, Robespierre’s Jacobins executed 12,000 people who were deemed to be enemies of the Revolution. Over the following two hundred years, terrorism has manifested itself in a number of forms and locations throughout the world. The topic of terrorism received renewed and increasing attention in the Western world at the beginning of the new millennium with the World Trade Center attacks on September 11, 2001. On that date, two passenger airplanes were hijacked and deliberately flown into the two towers of the World Trade Center in New York City. A simultaneous attack took place against the Pentagon with a single plane while another airplane crashed in Pennsylvania.

The 9/11 attacks involved the use of modern technology by foreign hijackers to inflict harm upon innocent civilians. Terrorists effectively turned instruments of progress into weapons of destruction targeting clear symbols of modern western society. In total, the 9/11 related casualties were approximately 3,000 people from over 90 countries. Further, the 9/11 attacks marked the beginning of the modern “war on terror.”<sup>2</sup> The wars and ongoing reconstruction efforts in Afghanistan and Iraq were two early manifestations of this larger effort to eradicate terrorism. To understand the magnitude of the war on terror, consider the monetary costs. Funding for homeland security increased drastically

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<sup>1</sup> On the history of terrorism, see Parry 1976, Sinclair 2003, Shughart forthcoming and Wieviorka 1993.

<sup>2</sup> Major terrorist attacks since 9/11 have taken place in Bali (2002), Madrid (2004), Beslan (2004) and London (2005).

after 9/11 including \$64 billion in emergency funds for 2001 and 2002. In total, between 2001 and 2003, total funding for homeland security increased by 240%.<sup>3</sup> It is difficult to obtain the exact costs to date of the war and reconstruction in Iraq. However, estimates range from \$100-\$200 billion.<sup>4</sup>

In the post-9/11 world, it would appear that liberalism has little to offer. In the face of the threat of terrorist, the U.S. federal government has significantly increased its level of intervention in a wide array of activities as evidenced by the Patriot Act. From increased federal involvement in airport security to widening the legality of the ability of the federal government to engage in surveillance and the detention of terrorist suspects, the federal government is seen by most as the key player in the larger war against terror.<sup>5</sup> It is our contention that the line of reasoning underlying these policies is in need of revision. A return to a political economy of classical liberalism, and not a reliance on government war socialism is the most effective means of reducing terrorism.

While both authors of this paper are committed non-interventionists in foreign policy, we do not argue in this paper from the perspective of first-principles. Instead, for the sake of argument in this paper we attempt to argue as pure economists and limit our discussion to questions that are of an empirical nature. The core thesis of our paper is that the current approach to the war on terror is ineffective. Central to the current policy approach is the belief that negative sanctions against actual and potential terrorists coupled with attempts to spread liberal democracy through war, occupation and

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<sup>3</sup> Source of homeland security spending: <http://www.heritage.org/Research/NationalSecurity/bg1731.cfm>

<sup>4</sup> For an estimate of the costs of war that is based on Congressional appropriations see, <http://www.costofwar.com/>

<sup>5</sup> We take the end goal of the war on terror to be an end to anti-American terrorist acts that aim to kill innocent American citizens. We do not address the loss of life in foreign countries that are a direct result of US military intervention.

reconstruction will improve the situation both abroad and domestically.<sup>6</sup> In short, an empirical conjecture is being put forth by those supporting current efforts --- raise the cost to terrorists of engaging in terrorist activities and the likelihood of another terrorist assault against the U.S. will decrease. Given existing preferences, we argue that negative sanctions are unsuccessful and in many cases counter productive in reducing terrorism. Further, we postulate that efforts to impose liberal democracy in weak and failed states via occupation and reconstruction have largely failed.

In what follows we analyze current efforts to reduce terrorism through an economic lens. In section 2 we exam why negative sanctions have been largely ineffective in reducing terrorism. In section 3 we turn to the logic of conflict and cooperation in the context of occupation and reconstruction. Economic theory predicts that we should observe cooperation where mutually beneficial gains exist. Of course in reality we often observe the persistence of conflict in such situations. We consider some of the factors that contribute to this disconnect between theory and reality. Understanding these factors sheds light on the inability of foreign governments to effectively impose liberal democracies as desired. We conclude by postulating that liberal values are critical to overcoming the threat of terrorism. It is our contention that only by returning to a position of principled non-intervention can the war on terror ultimately be won. This return to liberal principles will have the dual effect of reducing

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<sup>6</sup> Throughout the analysis we are careful to use the term “liberal democracy.” As Fareed Zakaria (2003) has emphasized, “democracy” is often confused with “liberal” or “constitutional democracy.” Democracy deals with the method of selecting government officials while constitutional democracy deals with the goals of government – the protection of individual rights, the rule of law, etc. In the absence of constitutional liberalism, democracy will not necessarily yield the desirable results. The election of Hitler in Germany or the elections in Iran, considered by most to be a corrupt sham, provide but two illustrations of the point that democracy in itself is not enough to obtain the desired outcome of liberalism.

terrorist attacks against the U.S. *and* providing a mechanism for peacefully finding common ground between differing belief systems and cultures.

## **II. REDUCING TERRORISM: WHY NEGATIVE SANTIONS ARE INEFFECTIVE**

The central element of current terrorist policy is negative sanctions or what Frey (2004) refers to as utilizing a “stick” to combat terrorism. The logic behind negative deterrence, seen along the lines of Becker’s crime and punishment model (1968), is twofold. First, the aim is to increase the probability of detecting potential and actual terrorists. Second, negative sanctions focus on increasing the penalty of being caught. Overall, the end goal is to increase the “price” of engaging in terrorist acts. Negative sanctions impose a cost on the terrorist, or potential terrorist, and may include such things as fines, imprisonment or execution and usually involve police and military force. Analyzing the market for terrorism will add insight into whether negative sanctions have the desired effects. In considering the market for terrorism, and subsequent attempts to deter terrorist activity, we employ the standard assumptions of economic analysis – rational calculation and purposive action.

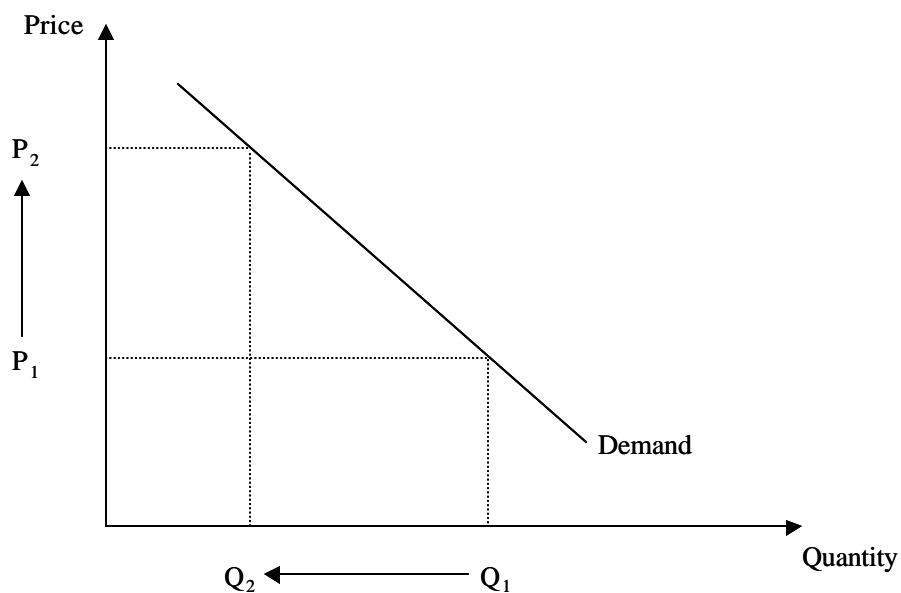
The market for terrorism consists of suppliers who are those individuals who are willing to carry out or supply terrorist acts and demanders who demand that terrorist activities be carried out.<sup>7</sup> Following Iannaccone (2003), we focus on the demand side of the market. The logic here is straightforward. While there is an ample supply of

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<sup>7</sup> The market for terrorism is unique in that in many cases the demanders and suppliers are the same individuals. For instance, Osama bin Laden is both demander and supplier of terrorism in the same way that an executive at Wal-Mart both is the supplier of goods and the demander of those goods to the extent that they shop at Wal-Mart.

individuals willing to supply terrorist behavior, there is a limitation on the demand side of the market. This limitation is due to the fact that there are usually not many organizations that want to recruit terrorists. As such, focusing on the demand side of the market is critical to understanding how to reduce terrorism.

Figure 1 illustrates the demand for terrorists and the subsequent impact of negative sanctions.



**FIGURE 1: TERRORISM AND RATIONAL DETERRENCE – ELASTIC DEMAND CURVE**

The motivation behind negative sanctions is that an increase in the price of engaging in terrorist acts ( $P_1$  to  $P_2$ ) reduces the quantity of terrorist acts demanded as illustrated by movements along the demand curve ( $Q_1$  to  $Q_2$ ). The quantity of terrorism can be

measured either by the number of terrorist acts or the magnitude of those acts as measured by the death and injury of innocent civilians.

Given the above, it would seem that the current policy of negative sanctions should be effective in raising the price and reducing the quantity of terrorism demanded. However, as those who have analyzed the war on drugs using the tools of economics have noted, it is critical to consider the elasticity of the good being analyzed (see Becker, Murphy and Grossman 2004). Considering the elasticity of demand for terrorism is important in understanding the effects of efforts to detect and punish. In other words, it is critical for policymakers to consider how individuals will react to changes in the price of the illegal good.

When one considers the demand for terrorism, there is good reason to believe that the demand curve is relatively inelastic. This is due to the fact that most terrorists are willing to pay an extremely high price to engage in terrorist activities.<sup>8</sup> These terrorists believe they are “doing the right thing” regardless of the costs associated with carrying out the related act.<sup>9</sup> At the extreme, fanatical terrorists are willing to pay the ultimate price (i.e., their life) to engage in terrorist activities. Osama bin Laden, for example, in a statement from October 6, 2002 states that the defensive jihad must continue because the U.S. has shown no signs of regret for its “previous crimes” against Muslims and instead that the “criminal gang at the White House” is continuing its attack on the Islamic world and therefore:

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<sup>8</sup> As Michael Scheuer (2005) has argued, from the point of view of Islamic terrorists they are fighting a defensive jihad. It is not western secular culture that incites bin Laden, but U.S. acts that challenge God’s word, attack Muslims, and occupy Muslim lands. The importance of Scheuer’s work is that it focuses our attention on the beliefs and preferences of those we are attempting to defeat in a military campaign.

<sup>9</sup> For a comprehensive analysis of the logic of suicide terrorism, see Pape (2005).

I am telling you, and God is my witness, whether America escalates or de-escalates the conflict, we will reply to it in kind, God willing. God is my witness, the youth of Islam are preparing things that will fill your hearts with fear. They will target key sectors of your economy until you stop your injustice and aggression or until the more short-lived of us die. (quoted in Scheuer 2005, pp. 17)

Bin Laden and other Islamic leaders of the defensive jihad are motivated by their love of Allah, and their hatred of US military acts and geo-politics policy that is damaging the Muslim world. For our purposes this reflects a set of given preferences that are reflected in a relatively inelastic demand curve for terrorist acts.<sup>10</sup>

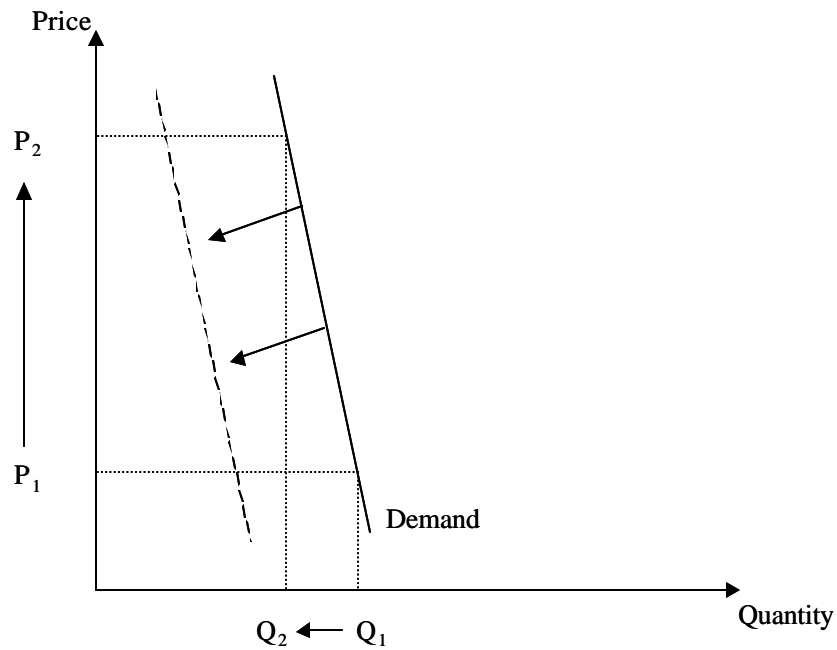
This realization has implications for terrorist policy and the “war on terror.” Given the inelasticity of the demand curve for terrorism, efforts to raise the price of engaging in terrorist acts will have a disproportionately small impact. This is illustrated in Figure 2 by the solid demand curve.

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<sup>10</sup> Consider, for example, the recent video statement by London suicide bomber Mohammed Sadiq which played on Al-Jazeera where he states: “Our words are dead until we give them life with our blood” ... “I, and thousands like me, have forsaken everything for what we believe. Our driving motivation doesn’t come from tangible commodities that this world has to offer” ... “Your democratically elected governments continuously perpetuate atrocities against my people all over the world, and your support of them makes you directly responsible, just as I am directly responsible for protecting and avenging my Muslim brothers and sisters. Until we feel security, you will be our targets, and until you stop the bombing, gassing, imprisonment, and torture of my people, we will not stop this fight.”

Source: <http://www.memritv.org/Transcript.asp?P1=835>





**FIGURE 2: TERROSIM AND RATIONAL DETERRENCE – INELASTIC DEMAND CURVE**

As Figure 2 illustrates, a relatively large increase in price ( $P_2 - P_1$ ) has a disproportionately small effect on the change in the quantity demanded of terrorism ( $Q_1 - Q_2$ ). The main implication is that raising the price of engaging in terrorism through negative sanctions will be relatively ineffective in preventing the most extreme forms of terrorism. Instead of policies that lead to a movement along the demand curve, what is ultimately needed is a shift in the entire demand curve inward as illustrated in Figure 2 from the solid demand curve to the dashed demand curve.<sup>11</sup>

<sup>11</sup> In short, the more effective policy from the point of view of attaining the stated US goals must move from the eradication of the terrorist threat in a crime and punishment framework to one of winning the hearts and minds of generations of Muslims.

The underlying logic of this realization is straightforward. Even if current anti-terrorist policies effectively capture the current generation of terrorists, such policies would fail to shift the underlying preferences or demand of future generations of terrorists. As long as more individuals demand terrorism in future periods, punishing current demanders does not change the underlying preference driving that demand. Only by shifting the underlying preferences of current and future generations of potential terrorists will the end goal of the war on terror actually be achieved. A few points will further illustrate the ineffectiveness of policies that lead to movements along the solid demand curve.

Consider that government attempts to protect against terrorist acts cannot effectively protect all potential targets. For instance, resources may be allocated to protecting federal buildings but those resources cannot be simultaneously used to protect “soft” targets such as malls and other public areas. Raising the price of one type of terrorist act causes terrorists to substitute to a relatively lower cost set of terrorist activities. It does not cause them to leave the terrorism business. In other words, the underlying preferences and market conditions have not been changed. Examples of substitution may include switching to targets that are too costly for the government to protect, substituting the modes of carrying out attacks, or employing a new type of terrorist laborer – a different sex, age, education, etc. In short, terrorist organizations will act in an entrepreneurial manner, constantly seeking out their opponent’s weakness where they can maximize the damage done given the constraints they face.

Further, raising the cost of terrorism may be counterproductive in that negative deterrence may increase the level of public attention attached to certain terrorist groups or

activities. One of the main aims of terrorist organizations is to maximize publicity (Frey 2004, pp. 122-3). Allocating resources to deterrence or detection may increase the attention paid to terrorists and terrorist organizations. Ultimately these policies may assist the terrorists in achieving their end goals of attention and publicity. Consider for instance the attention given to terrorists when a government announces military strikes or raids or the increased security of a certain potential target.

Finally, the current emphasis on negative deterrence may actually contribute to the strength of the general demand for terrorism. As Frey (2004, pp. 33-6) indicates, deterrence policy creates a negative-sum situation where neither the terrorists nor the combating powers wins. Coercive action is met with coercive action and this spirals into a continuous process of negative-sumness.<sup>12</sup> Both parties are made worse off and neither may achieve their end goals. In such an instance, the war on terror turns into a classic prisoner's dilemma situation. Both parties would be better off if they could credibly commit to cooperate but instead both end up defecting.

Given the ineffectiveness of negative sanctions for the reasons discussed above, the focus of policy toward terrorism must drastically change. Instead of focusing on policies that lead to movements along the demand curve, focus must be placed on shifting the entire demand curve inward as illustrated in Figure 2. The logic underlying this claim is straightforward. Given an inelastic demand curve, raising the price of terrorism does reduce the quantity demanded but only by a relatively small amount. At the same time, negative sanctions fail to remove the underlying demand or preference for terrorist acts.

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<sup>12</sup> For more on the negative-sum nature of conflict see Boulding (1962) and Schelling (1960, 1984, pp. 269).

Only by changing the fundamental market conditions and preferences of those that participate in the market, characterized by a shift in the demand curve inward, will the underlying demand for terrorist acts actually change in future periods. Unless there is buy in from the individuals within the country where a demand for terrorism exists, sustainable deterrence will not occur. While negative deterrence can stop some terrorist acts, it is not a long-term solution to delegitimizing the fundamental demand and acceptance of terrorism as a means for resolving disagreement. It is precisely because current policies are ineffective in changing the underlying preferences driving the demand for terrorism that we must look elsewhere for strategies to reduce terrorist activities. The question then turns to determining the best means for shifting the entire demand curve and changing the fundamental economic, social and political conditions where a demand for terrorism exists.

### **III. ILLIBERAL MEANS TO LIBERAL ENDS?**

In addition to engaging in negative deterrence of actual and potential terrorist activities, the United States and other foreign governments have attempted to reduce future terrorist acts by “spreading democracy” to weak, failed and conflict-torn states.<sup>13</sup> These efforts have traditionally involved military occupation and reconstruction with the aim of establishing self-sustaining liberal political, economic and social orders. President Bush recently reiterated this position in his second term Inaugural Address when he indicated that U.S. foreign policy will aim to “...seek and support the growth of democratic

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<sup>13</sup> Eizenstat et al. discuss the characteristics of weak and failed states. The weakness of states can be measured along three margins performed by the governments of strong states: security, the provision of basic services, and the protection of essential civil freedoms. Failed states do not provide any of these functions while weak states are deficient along one or two of these margins (2005, pp. 136).

movements and institutions in every nation and culture, with the ultimate goal of ending tyranny in our world.”<sup>14</sup>

The logic behind these efforts is that those countries with dysfunctional or absent states often provide a safe haven for terrorists and terrorist organizations. If these countries can be transformed into liberal democracies, terrorism will be severely reduced if not eradicated. In the context of the demand for terrorism discussed in Section 2, if liberal ideals can be spread to weak and failed states, the fundamental conditions and preferences will change, shifting the demand curve inward. In short, effective reconstruction efforts will shift the demand curve for terrorism inward as illustrated in Figure 2.

Given the increasing relevance of reconstruction in the post 9/11 world, a fundamental question comes to the forefront. Can foreign governments effectively establish liberal democratic institutions in weak and failed states at will?<sup>15</sup> Based on the historical record, the answer is a resounding no. Consider Table 1, which shows the U.S. led reconstruction since the late 1800s.

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<sup>14</sup> Inaugural Address available at: <http://www.whitehouse.gov/news/releases/2005/01/20050120-1.html>

<sup>15</sup> As Gause (2005) discusses, simply establishing democracy in the Arab world will not reduce terrorism and will most likely generate outcomes that are not favorable to the U.S.

<b>Country</b>	<b>Years</b>	<b>Democracy After 10 Years</b>
Iraq	2003-present	N/A
Afghanistan	2001-present	N/A
Haiti	1994-1996	No
Panama	1989	Yes
Grenada	1983	Yes
Cambodia	1970-1973	No
South Vietnam	1964-1973	No
Dominican Republic	1965-1966	No
Japan	1945-1952	Yes
West Germany	1945-1952	Yes
Dominican Republic	1916-1924	No
Cuba	1917-1922	No
Haiti	1915-1934	No
Nicaragua	1909-1933	No
Cuba	1906-1909	No
Panama	1903-1936	No
Cuba	1898-1902	No

**TABLE 1: U.S. RECONSTRUCTION EFFORTS, 1898-PRESENT<sup>16</sup>**

Table 1 shows the countries where U.S. led reconstruction efforts have been attempted as well as the years of occupation. Liberal democracy is measured by the Polity IV index which measures the level of democracy or autocracy in a country (Jagers and Marshall 2003).<sup>17</sup> In Table 1, a country with a Polity IV score greater than +3 ten years after the end of occupation is considered to be a successful case of reconstruction.<sup>18</sup>

<sup>16</sup> Source: Pei (2003).

<sup>17</sup> The Polity IV Index ranks the political institutions of a country on an additive eleven point scale (0-10). The authors compute a combined “polity score,” by subtracting the Autocracy score from the Democracy score. The resulting scale ranges from +10 (strongly democratic) to -10 (strongly autocratic). Institutionalized democracy, as defined by the authors, consists of three key elements: (1) the presence of institutions and procedures through which citizens can express their preferences, (2) the presence of institutionalized constraints on the executive, and (3) the guarantee of civil liberties for all citizens in both their daily lives and political participation (Polity IV Project, Dataset Users Manual, pp. 13). The authors define autocracy “in terms of the presence of a distinctive set of political characteristics.” Specifically, autocracies “suppress competitive political participation. Their chief executives are chosen in a regularized process of selection within the political elite, and once in office they exercise power with few institutional

Economics can offer insight into reconstruction efforts and their ultimate success or failure. Thomas Schelling (1960) was one of the first economists to apply economic insights to conflict and cooperation. Schelling pointed out the difference between games of pure conflict (negative or zero-sum games) and games of pure cooperation (positive-sum games). This general framework can be applied to the situation of occupation and reconstruction (see Cowen and Coyne 2005). In the context of reconstruction, conflict includes such things as terrorism, looting and general insurgency. In contrast, cooperation includes peaceful interaction and exchange around liberal ends.

Economic theory predicts that conflict should not persist where gains from exchange exist. Specifically, the Coase theorem indicates that conflict should be unlikely as all parties peacefully bargain to realize the mutual gains of interaction and exchange. Of course one observes the persistence of conflict of various magnitudes in various locations throughout the world. While the Coase theorem is an imperfect model of the world, it serves as a useful foil to understand the various factors that facilitate or constrain the predicted outcome of cooperation. In other words, within the occupation and reconstruction context, it is important to understand the factors that contribute to, or prohibit, the transformation of situations of conflict into cooperation. In what follows, we consider several factors which influence the level of conflict or cooperation in weak or failed states.<sup>19</sup> Our aim is not to gauge the magnitude of these factors, which will vary

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constraints.” Following Pei and Kasper (2003), we take a score greater than +3 (Iran’s current score) ten years after exit to be a successful case of democracy.

<sup>18</sup> The range of Polity IV index seeks to register the strength of democracy or autocracy. To put a score of +3 in context, Iran currently scores a +3. As such, we are holding the success or failure of past reconstruction efforts to an extremely charitable standard. By employing these benchmarks we are asking, “Did U.S.-led reconstruction efforts generate a political order that is equivalent to present day Iran?”

<sup>19</sup> The identification and analysis of these factors draws on previous work by Cowen (2004), Cowen and Coyne (2005) and Coyne (2004, 2005, 2006).

depending on the context, but rather to understand how they may constrain the achievement of the desired outcome of self-sustaining mutually beneficial cooperation.

### *Transaction costs and property rights*

The standard response to the Coase theorem is that the presence of high transaction costs and/or a lack of well-defined property rights will constrain the achievement of the predicted outcome. Given this, both factors must be considered in the context of occupation and reconstruction. Transaction costs – in the form of various parties, factions, etc. meeting and bargaining – may indeed be present but one should not expect these costs to be overly prohibitive. The occupying forces seek to play the role of mediator in which they bring the relevant parties together to the bargaining table. The aim is to strike a mutually beneficial agreement between the various parties involved.

The presence of well-defined and enforceable property rights may be more of a problem. If party A cannot trust that party B will not cheat them, an agreement may not be reached. Similar to the bargaining situation, the occupying forces, in the role of mediator, often monitor and enforce any agreement that is reached. However, occupying forces have often failed to be effective in the role of enforcer. Oftentimes, elites in reconstructed countries have reneged on the specifics of the agreement reached under the guidance of foreign occupiers.

For example, Horacio Vásquez Lajara was elected president of the Dominican Republic on the eve of U.S. exit in 1924. Vásquez ignored the constitutionally dictated term limits established under U.S. guidance and remained in office for six rather than the



stipulated four years. This initial disregard for the constitution led to a military led coup resulting in autocratic rule for the next several decades.

In sum, the transaction costs associated with bargaining during reconstruction are not likely to be a significant barrier. Enforcement is more likely during the occupation while occupying forces have resources dedicated to upholding any agreement reached. However, it is unclear that foreign powers can effectively enforce agreements over the long-term. This commitment problem may result in parties defecting from agreements once occupiers exit causing the cooperative agreement to unravel.<sup>20</sup>

#### *Social capital and the art of association*

The notion of social capital has been receiving increasing attention from social scientists. Social capital emphasizes the role of social networks and connections. More specifically, social capital can be defined as the existence of a certain set of informal values or norms that are shared among members of a group. These shared norms and values facilitate cooperation and coordination (Fukuyama 1999: 16; Putnam 2000, pp. 18-20).

In the context of reconstruction, social capital around shared norms by heterogeneous members of a society is critical for achieving a shared liberal ethic around meta-level political, economic and social institutions (Coyne 2005b). In short, the art of association that characterizes a liberal order requires a certain type of social capital that provides norms of trust, loose ties, respect for private property and the rule of law.

A fractionalized country with many heterogeneous groups that are not interconnected is less likely to share an ideology and ethic. In other words, it is less

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<sup>20</sup> For a discussion of the commitment problems faced by reformers in the Soviet Union, see Boettke (2001). A similar argument can be made in the context of reconstruction.

likely that common knowledge around the ends of the reconstruction will evolve (Coyne 2004). In contrast, a society characterized by social capital fostering loose ties is more likely to share a common ideology and ethic given that heterogeneous groups and individuals are connected.

Examples of this last point would be “high trust” societies such as Japan and Germany which are often considered to be the two most successful U.S.-led reconstruction efforts (Fukuyama 1996, pp. 149-255). While individuals and groups in these societies differ on many margins, there is a shared ethic consisting of a minimal level of trust, honesty and respect that pervades almost all daily activities. This underlying ethic that arises when a society shares a certain set of values, allows for the movement from personal to impersonal exchange. The widespread sharing of values requires a certain connectedness among individual members of the society.<sup>21</sup> Social capital encompasses the norms and values to facilitate such interaction and cooperation.

Different societies will have varying endowments of social capital. Given that social scientists and policymakers do not have a firm understanding of how to create social capital anew, the existing endowment in countries characterized by weak and failed states is an exogenous constraint on reconstruction efforts. In many cases, the endowment of social capital will constrain the achievement of self-sustaining meta-institutions which are the very goal of reconstruction efforts.

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<sup>21</sup> It is important to note that the existence of social capital that fosters bridging ties does not guarantee a successful reconstruction. This is due to the existence of the “dark side” of social capital that include shared norms around perverse ends which run counter to general progress. In other words, social capital can be seen as a necessary, but not sufficient, condition for post-conflict reconstruction. It is necessary because interconnectedness is needed to share the required ethic across a society. However, it is not sufficient because it is possible for social capital to exist around perverse ends that oppose reconstruction efforts.

### *The meta-game and nested games*

Reconstruction efforts focus on resolving the meta-level game of creating self-sustaining liberal institutions at the national level. Oftentimes, these efforts overlook the fact that there are nested games embedded within the general meta-game.<sup>22</sup> These nested games are often the result of historical interactions and experiences which occurred prior to reconstruction efforts. In many cases, these nested games constrain the achievement of a solution to the general meta-game. Indeed, the nested games may be so complicated that the meta-game cannot be easily characterized let alone solved.

One example of how nested games can constrain the larger reconstruction meta-game is the case of Somalia. Somalia has existed with no central government since 1991. Further, no central government has ever evolved endogenously although exogenous forces established a government in 1960. Historically the clan, and not any notion of a central state or nation, has been the most important source of identity in Somalia. The result has been many small, overlapping and simultaneous games between the various actors throughout Somalia both within and across clans. Solutions have evolved to these mini-games which allows for widespread cooperation but the nature of these games also constrain the achievement of the larger reconstruction game.

Indeed, attempts by foreign governments to construct a central government and solve the Somalia meta-game have exacerbated conflict. These efforts lead to a large bargaining game between the many dispersed parties throughout the country. In this context players want to establish their reputation as a “power player” within the political process. In turn, this situation leads to a struggle, oftentimes violent, for control of

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<sup>22</sup> For the importance of considering the entire network of games that individuals are involved in to fully understand their behavior, see Ostrom et al. (2002) and Tsebelis (1990).

power. The process of conflict continues until the attempts to solve the meta-game end, after which social relations can again be characterized by the many nested games which existed prior to the attempt at reconstruction (see Coyne 2005a).

The desire of parties to establish a firm reputation in the reconstruction bargaining game may intensify divisions and contribute to the failure to solve the meta-game. The parties involved in the reconstruction game realize that they will be involved in further interactions with the other parties in future periods. As such, they may seek to establish a “tough” reputation in the attempt to gain an edge in future interactions. In such a case, it is precisely because there will be future interactions and gains to be had that parties may fail to strike an agreement (Cowen 2004, pp. 3-4). Both parties will hold out for a greater share of the available surplus resulting in a negative-sum situation where an agreement cannot be reached and neither party benefits.

#### *Expectations and self-deception*

While the specifics of each reconstruction situation will differ, in each case there is some set of expectations where the meta-game is one of coordination rather than conflict. If the expectations of the citizens of the country being reconstructed country are aligned, at least to some degree, with the aims of the reconstruction, there will tend to be a greater degree of coordination.

As recent work in behavioral research illustrates, a critical element of expectation management is how outcomes relate to expectations. This realization can be applied to the situation of reconstruction (Cowen and Coyne 2005, pp. 38-40). For instance, work by Diener (1984) and Frank (1989, 1997) concludes that individuals value their current

state of affairs relative to their expectations. Behavioral research in the area of wage rigidity adds further insight into expectations in the context of conflict (Cowen 2004, pp. 5).

In this latter area of research, economists seek to answer why involuntary employment exists. Employers and employees, following the assumptions of economics, should negotiate lower wages. Both parties would be better off as compared to a situation where the worker is laid off. One explanation for the failure to negotiate such an agreement is that employers fear that employees will engage in uncooperative behavior because employees, under the renegotiated contract, will receive less than they believe they should (see Bewley 1999). In the context of reconstructions, this research indicates that a disjoint between expectations and outcomes may lead to the persistence of conflict. When individuals are forced to participate in an agreement that provides an outcome which “pays” less than they expected, they may very well refuse to act in a cooperative manner.

In some cases it will be preferable for individuals to have low expectations and in others it will be better if individuals have higher expectations. It may appear that it is always preferable for the populace to have low expectations so that there can never be backlash against occupiers. However this overlooks that a successful reconstruction requires an investment on the behalf of the citizens of the occupied country. For instance, in order for impersonal social and economic interaction to take place, individuals must have an (high) expectation that their property rights will be respected.

To generalize, low expectations are beneficial when the citizens in the occupied country will tend to blame the occupying forces for the every minor mistake. Things

such as infrastructure beyond basic necessities, welfare and other acts of “goodwill” fall into this category. In other situations, it will be beneficial if the populace has high expectations so that they will make the necessary investment to participate and further the reconstruction process.

Occupying forces can seek to influence expectations to some extent but they cannot completely control the expectations held by the citizens of the occupied country. There is some range over which individuals have pre-conceived expectations which cannot be significantly influenced. For instance, individuals may lack “meta-rationality” meaning they fail to have realistic expectations of one’s abilities and the prospects for achieving one’s desired ends. Indeed, self-deception can be seen as a contributing factor to political failure (Cowen, forthcoming). In the context of reconstruction, each party may have unrealistic expectations of what they can realistically achieve in the larger reconstruction game. The achievement of a long-term sustainable agreement may be constrained where each side possesses unrealistic and disjointed expectations of what they deserve and can ultimately achieve.

#### *The knowledge problem and unintended consequences*

Austrians emphasize the role of local knowledge which cannot possibly be possessed by those designing and carrying out government interventions. Indeed, the dynamics of intervention indicate that one intervention creates a new set of incentives for both political and private actors. These incentives may create a set of circumstances that prevent the achievement of the desired goal and require additional interventions on the part of political agents. However, these subsequent interventions again cause the

underlying incentive structure to shift. The process then continues in a similar manner (see Mises 1977 and Rothbard 1977).

In the context of reconstruction, foreign governments can never have full and complete information of how to effectively craft and implement self-sustaining liberal political, economic and social orders. Policies that may appear to generate the desired outcome may have undesired consequences in future periods. These unintended consequences may in turn generate the need for further government interventions which in turn create a new set of unintended consequences.

To illustrate this, consider the case of U.S. intervention in Afghanistan in the late 1980s. The aim of the U.S. intervention was to assist Afghanistan resistance forces in expelling the Soviet Union. After achieving the desired goal, the U.S. removed itself from the situation in Afghanistan. The result was various factions within Afghanistan turning against one another. The ensuing civil war created an environment in which the Taliban and al Qaeda assumed significant positions of control ultimately resulting in further U.S. interventions in 2001 (Eizenstat et al. 2004, pp. 139). Further, in some cases, the weapons that the U.S. had provided to resistance forces to expel the Soviet Union were used against U.S. troops during the recent war. Current reconstruction efforts will likewise have unintended consequences in future periods which may cause preclude cooperation over the long-term.

#### *Public choice issues*

Most studies of reconstruction fail to consider the motivations of the various actors that comprise the occupying forces. Indirectly, these studies assume benevolence on the part

of occupying forces. Occupiers often state the ends of reconstruction efforts as the establishment of a liberal democracy. The assumption of benevolence coupled with the stated ends of reconstruction efforts leads one to conclude that occupiers take the most effective steps known to achieve the stated ends.

Public choice theory, which demands symmetry of behavioral assumptions applied to both private and public actors, leads to a very different conclusion. Public choice theory dictates that if one assumes that private economic actors act in a self-interested manner, the same assumption must be applied to those in the political and public realm. This has major implications in the context of reconstruction efforts.

There is a wide array of actors involved in the reconstruction process. Politicians, bureaucrats in a wide range of government offices and bureaus, military personnel and interest groups all have different ends that they are pursuing in the wider reconstruction context. In many cases, these individual interests may conflict with the end goal of achieving a self-sustaining liberal order. For instance, politicians aim to maximize votes, while bureaucrats aim to maximize their budget. As such, one should expect politicians to tend to be more optimistic about the status of reconstruction efforts while bureaucrats will tend to be more pessimistic, demanding more resources to achieve the stated ends.

Further, there will often be conflict between the aims and goals of different agencies within the same government. For instance, there is tension between the missions and activities in the CIA and FBI in the United States (see Scheuer 2005, pp. 185-192). Likewise, special interest groups may seek to influence the allocation of resources and aid in the occupied country. The various interests at play will also influence the picking of political winners within the occupied country. Recently, there



have been several critical analyses of the current efforts to reconstruct Iraq (see for instance Diamond 2005 and Phillips 2005). These authors discuss the tensions between the various parts the U.S. government, military and intelligence agencies which have, in many cases, limited the effectiveness of reconstruction efforts.

In sum, a complete analysis of occupation and reconstruction requires a consideration of the motivations of actors in the public realm. Actors in the public realm face a set of incentives that will often lead them to act in a manner inconsistent with the stated ends of reconstruction efforts. Indeed, there is no feedback mechanism in the public sphere to ensure that the most efficient and effective steps will be taken to achieve the stated ends. The pursuit of private interests by public actors may contribute to the persistence of conflict. Put differently, public actors may fail to take steps that would result in cooperation if those activities fail to align with their private interests.

### *Summation*

Historically, reconstruction efforts have failed to consistently establish self-sustaining liberal democracies. As Table 1 indicates, excluding Afghanistan and Iraq, the United States has had a success rate of approximately 26% since 1898. Further, it is not just the case that reconstruction efforts that fail leave the country in question just as well off as prior to the attempted reconstruction. Such a view suffers from a “nirvana fallacy” where it is assumed that foreign governments can achieve a better outcome as compared to the status quo in weak and failed states, and at worse will leave the country no worse off. This assumption overlooks the possibility that reconstruction efforts may, on net, cause more harm than good (Coyne 2005a). For instance, the overall level of cooperation has

been higher in Somalia when foreign governments are not present or involved in attempts to establish a central government. Efforts to exogenously establish a central government have increased conflict instead of accomplishing the intended goal of increasing cooperation.

As outlined in the previously subsections, there are numerous factors which may preclude the achievement of a cooperative solution around liberal orders in those countries characterized by weak and failed states. This is not to say that reconstruction efforts can never successfully achieve the desired goals, but rather to indicate that foreign governments lack a clear understanding of how to achieve such ends on a consistent basis. Given the inability of foreign governments to effectively change the underlying preferences and conditions as desired, it is far from clear that occupation and reconstruction are effective means in achieving the stated ends of eradicating terrorism.

#### **IV. CONCLUSION: WHAT ROLE FOR LIBERALISM?**

Recently, Michael Novak (2005) has pointed out that there is a “universal hunger for liberty.” This hunger cuts across national and cultural boundaries. While Novak’s conclusion should be a source of optimism, he fails to consider the most effective means of satiating the universal hunger. Our analysis indicates that attempts to protect and spread liberty through negative sanctions against terrorists and attempts to impose liberty via occupation and reconstruction are largely ineffective. How then is the universal hunger for liberty to be satisfied? Or stated differently, how are we to close the gap between “the West and the Rest?”<sup>23</sup> Whatever the answer, our analysis indicated that

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<sup>23</sup> This phrase is borrowed from Mahbubani (1992).

steps must be taken to shift the entire demand curve for terrorism inwards. It is our contention that the key to achieving this end lies in a return to fundamental liberal principles of non-intervention and a commitment to free trade. Only by returning to these principles can the underlying preferences, and hence the demand curve for terrorist acts, shift as illustrated in Figure 2.

These liberal principles have a long history in the United States.<sup>24</sup> As George Washington emphasized in his farewell address in 1796:

The great rule of conduct for us in regard to foreign nations is, in extending our commercial relations to have with them as little political connection as possible. So far as we have already formed engagements let them be fulfilled with perfect good faith. Here let us stop...It is our true policy to steer clear of permanent alliances with any portion of the foreign world...<sup>25</sup>

On July 4, 1821, Secretary of State John Quincy Adams made clear his view of America's role in the international arena in a speech to the House of Representatives:

America does not go abroad in search of monsters to destroy. She is the well-wisher of freedom and independence of all. She is the champion and vindicator only of her own...She well knows that by once enlisting under banners other than her own, were they even the banners of foreign independence, she would involve herself beyond the power of extrication, in all the wars of interest and intrigue, of individual avarice, envy, ambition, which assumed the colors and usurped the standards of freedom. The fundamental maxims of her policy would insensibly change from liberty to force (quoted in Scheurer 2005, pp. 200).

The logic behind pursuing principled non-intervention with a commitment to free trade is grounded in basic economic reasoning. Specifically, the gains from exchange model indicates that individuals who engage in exchange expect, *ex ante*, to be made better off due to the interaction. The gains from exchange manifest themselves in a number of ways. Economic gains, in the form of prosperity and standards of living, are one clear manifestation of trade. William Cline estimates that worldwide free trade could help 500

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<sup>24</sup> For an intellectual history of free trade see Irwin (1996).

<sup>25</sup> Source of quote: <http://www.liberty1.org/farewell.htm>

million people escape poverty while simultaneously injecting \$200 billion annually into developing nations (2004). Perhaps more importantly, trading partners are less likely to engage in conflict because the aggressor incurs part of the cost of their actions in the form of foregone future exchanges.

Free trade also provides potential benefits beyond economic gains. As Cowen (2002) indicates, trade in cultural products increases the menu of cultural choices available. Cultural exchange causes cultures to become more homogeneous on some margins but simultaneously increase heterogeneity on other margins. As such, the possibility of exchange provides the ability of the exchange of cultural practices and ideas. Free trade can be seen as a means of finding a common ground between cultures and the potential for enemies to be transformed into trading partners. Along similar lines, free exchange allows for the imitation of both formal and informal institutions across national borders. As such, it is a means of generating social change through peaceful interaction. A commitment to non-intervention as outlined by Washington and Adams will reduce the U.S.'s exposure to terrorist attacks in other countries. It will also allow different cultures to find areas of commonality serving as a foundation for coexistence.

A common objection to this course of action is that Islam is fundamentally opposed to Western culture and values. However a detailed analysis of terrorism indicates this is not the case. As Pape indicates, "The United States has been exporting cultural values that are anathema to Islamic fundamentalism for several decades, but bin Laden and the al-Qaeda organization did not turn toward attacking the United States until after 1990, when the United States sent troops to Saudi Arabia, Qatar, and Bahrain" (2005, p. 52). Indeed, Pape's analysis of suicide terrorism concludes that past and current

suicide campaigns are not driven by Islamic fundamentalism, but instead are driven by foreign occupation of the terrorist's homeland.

In sum, a commitment to the liberal principles of free trade and non-intervention will have two key benefits. First, if Pape's analysis is accurate, the number of terrorist attacks against the United States should decrease with the end of occupation. Second, free trade offers a means of finding a common ground between cultures. Instead of inducing reform at the point of a gun, free trade provides a means of peaceful evolution.

Of course free trade in goods, services, culture, ideas and institutions depends on the existence of some core values such as tolerance and respect for property (see Coyne 2005b). We must recognize that some countries may not possess these prerequisites.<sup>26</sup> However, as past reconstruction efforts demonstrate, these preconditions cannot be imposed at will. Institutions that are imposed on societies where the fundamental conditions and preferences are not in place to serve as foundation will fail to "stick" and operate as desired. In short, attempting to export liberal democracy at gunpoint severs the voluntary nature of exchange. As such, the coerced parties are less likely to voluntarily accept the "good" being exported once the gun is removed.

It is not simply a matter of the desired liberal institutions failing to stick. Additionally, efforts to export liberal democracy via occupation can be counter productive. As Huntington points out, "Western efforts to propagate such ideas [liberal democratic values and ideas] produce instead a reaction against 'human rights

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<sup>26</sup> As Ludwig von Mises pointed out: "The problem of rendering the underdeveloped nations more prosperous cannot be solved by material aid. It is a spiritual and intellectual problem. Prosperity is not simply a matter of capital investment. It is an ideological issue. What the underdeveloped countries need first is the ideology of economic freedom and free enterprise and initiative that makes for the accumulation and maintenance of capital as well as for the employment of the available capital for the best possible and cheapest satisfaction of the most urgent wants to the consumers. In no other way can the United States contribute to the improvement of the economic conditions of the underdeveloped countries than by transmitting to them the ideas of economic freedom" (Mises 1952, pp. 173).

imperialism' and a reaffirmation of indigenous values..." (1993, pp. 41). It is critical to realize that in many cases establishing a liberal political, economic and social order via occupation is simply not an option. Given that imposing the necessary values and preferences is often not in the feasibility set, the best that can be done is to offer the possibility of free trade of goods, services and ideas.

With increases in technology available at decreasing costs, there is reason for optimism. With the advent of new technologies such as the Internet, cell phones and other telecommunications technologies, the world is interconnected and integrated as never before. This should allow for the continual exchange across the several margins discussed above. On the flipside, these same technologies allow small groups of individuals to engage in acts that pose potential threats of massive proportions. The tension between these two possibilities poses what is perhaps the greatest challenge in the world today.

Given this challenge, we have attempted to show that while a position principled non-intervention coupled with a commitment to free trade is not a panacea, it is the most effective means available to generate sustainable social and political change along liberal lines. We are not arguing that governments shouldn't protect their citizens against immediate terrorist threats. Instead, it is our contention that while current anti-terrorist efforts may be effective in rooting out existing terrorists, they are largely ineffective in changing the underlying preferences that will drive terrorism in future generations.

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