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Economic Foundation and Stability

A Study on a Theory of Change

Supervision
Dr. oec. Urs Heierli – University of St. Gallen
Gabriele Siegenthaler – Swiss Agency of Development and Cooperation

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Clivaz Audrey	09-606-351
Schmitz Olivia	09-611-989
Zoller Viola	09-613-399
Züger Lisa	09-611-427

Abstract

This paper analyses the correlation between economic foundations and stability in the context of fragile states and the Message on Switzerland's International Cooperation in 2013–2016. The analysis will focus on three indicators of the Peacebuilding and Statebuilding Goal Nr 4: equality, employment and natural resource management. It will be examined whether it can be theoretically and empirically confirmed that an improvement of the mentioned indicators will lead to more stability. From a theoretical point of view the examined correlation could be confirmed, however, empirically there is little evidence for drawing an universalistic conclusion that confirms a direct positive impact of equality, employment and natural resource management on stability. The main reasons for lacking empirical evidence are the varying contexts of the analysed states and overlapping effects of different policies.

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List of Abbreviations

AfDB	African Development Bank Group
CFW	Cash for Work
DFID	Department of International Development
DIIS	Danish Institute for International Studies
ECA	Excess Crude Account of Nigeria
EITI	Extractive Industries Transparency Initiative
FFW	Food for Work
HDI	United Nations Human Development Index
IDPS	International Dialogue of Peacebuilding and Statebuilding
IMF	International Monetary Fund
INCAF	International Network on Conflict and Fragility
MDG	Millennium Development Goals
OECD	Organisation for Economic Co-operation and Development
PSG	Peacebuilding and Statebuilding Goals
SDC	Swiss Agency for Development and Cooperation
SME	Small and Median Enterprise
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Program

1. Introduction

According to the Organisation for Economic Co-operation and Development [OECD] 1.5 billion people live in fragile and conflict affected states and these states are the farthest away from reaching the Millennium Development Goals [MDG] (OECD, 2011, p. 3). Knowing this fact, one cannot be surprised that fragile states are also in the focus of the Swiss Agency for Development and Cooperation [SDC]. In the Message on Switzerland's International Cooperation in 2013–2016 (Botschaft über die internationale Zusammenarbeit 2013–2016) it is clearly said, that Switzerland is strengthening its commitment in fragile states until 2016 in order to address their superior goal of reducing poverty in this world (Swiss Federal Administration, 2012, p. 3).

In 2008, hence around four years before the SDC announced its enhanced commitment in fragile states, the International Dialogue of Peacebuilding and Statebuilding [IDPS] was established to better and more effectively address challenges of fragility. It was widely recognized, that existing development approaches have failed to achieve fast enough progress in fragile states and therefore a New Deal for addressing state fragility was needed. The result of this New Deal was a framework, which helps focus on and observe progress towards reduced fragility. The heart of the New Deal consists of five Peacebuilding and Statebuilding Goals [PSG], while PSG Nr. 4 addresses the importance of stable economic foundations. The assumption which lies behind PSG Nr. 4 is that improvements in the area of employment, equality and natural resources management will lead to more stability. The question which arises from this assumption is whether it can be theoretically and empirically confirmed that an improvement of the economic foundation will lead to reduced fragility, respectively increased stability. Thus the research topic of this paper is to find evidences whether such a *Theory of Change* exists. The answer to this will not only provide a possible basis to evaluate the concept of the New Deal, but will also help SDC to strategically align their commitment in fragile states. In order to answer the outlined question, the first chapter of this paper will prepare the reader for the actual analysis, by first giving an overview on the methodology and the idea of New Deal and second by defining the terms fragility and stability. What follows is the analysis which is structured in three parts. First the topic of equality and stability will be discussed in chapter 3, then the focus will shift to the effects of employment on stability and finally chapter 5 will analyse if and how natural resource management can lead to stability.

2. Methodology and Definitions

The following chapter will specify the methodology of this paper, by introducing the concept of New Deal and how it defines the scope of the analysis. Furthermore an attempt to define the key terms fragility and stability will be made.

2.1 New Deal

As already mentioned in the introduction, New Deal was created because development goals were not achieved fast enough, respectively not as fast as planned. Especially fragile states were lacking far behind the Millennium Development Goals, what made clear that without a structured approach on how to track and finally reduce fragility, not even one fragile state will achieve the MDG by 2015. As part of the International Dialogue of Peacebuilding and Statebuilding, a group of 19 fragile and conflict-affected countries, development partners as well as International Organisations came together to develop a framework, which should help to promote effective ways out of fragility and to build peaceful states. In order to track the progress, 5 PSG were developed:

1. Legitimate and inclusive politics: Foster inclusive political settlements and conflict resolution.
2. Security: Establish and strengthen people's security.
3. Justice: Address injustices and increase people's access to justice.
4. Economic foundations: Generate employment and improve livelihoods.
5. Revenues and services: Manage revenue and build capacity for liable and fair service delivery. (International Dialogue on Peace- and Statebuilding, 2010, p. 2)

The PSGs help to focus attention and resources on key priorities that enable fragile countries to build peaceful societies. There are seven piloting countries, which all agreed on monitoring progress towards those PSGs on national level by reporting on a set of simple and practical indicators. (International Dialogue on Peace- and Statebuilding, 2010, pp. 1-4) As for this paper only PSG Nr. 4 is relevant, the rest of the goals will not be further discussed. Here only the indicators of PSG Nr. 4 will be listed:

Figure 1 Indicators of PSG Nr. 4
Source: INCAF, 2012, pp. 15-16

1. Productive Resources and Prospects for Growth	2. Jobs, Livelihoods and Private Sector Development	3. Natural Resource Management
i) % of population with access primary and feeder roads and affordable electricity	i) Level of economic diversification by productive sector	i) Ratio of local/foreign employment in natural resource sector
ii) Income inequality among regions (gini coefficient)	ii) Number of new registered businesses and SMEs	ii) Existence and quality of regulatory framework for natural resource management
iii) Level of economic diversification by productive sector	iii) Share of food in household expenditure	iii) Perception of participation in and benefits from natural resources
		iv) Ratio of natural resource production in country to total revenues to government

In order to analyse whether there exists a connection between the well-being of a country's economy and its stability (= *Theory of Change*) theoretical and empirical evidences on the indicators which are included in PSG Nr. 4 will be collected and an overall conclusion will be drawn. However, to analyse all the indicators individually would go beyond the scope of this paper, that's why only part of the indicators will be covered by the three areas of the analysis, which are equality, employment and natural resource management in general.

2.2 Fragility and Stability

The following chapter will provide the reader with a definition of fragility and stability as it is understood in the context of this paper and why fragility actually matters.

2.2.1 Definition of Fragility and Why it Matters

While searching for a clear and universal definition of fragility, one will quickly realize that no standardized or generally accepted definition of fragility or fragile states exists. However, there are many institutions and International Organizations which formulated their own definition. The OECD for example defines fragile states as followed: "States are fragile when state structures lack political will and/or capacity to provide the basic functions needed for poverty reduction, development and to safeguard the security and human rights of their populations" (OECD, 2007, p. 2). Similarly, the UK Department of International Development [DFID] defines fragile states as "those where the government cannot or will not deliver core functions to the majority of its people, including the poor" (DFID, 2005, p. 3). And finally the World Bank identifies fragile states as states, which "share a common fragility in two particular respects: State policies and institutions are weak in these countries: making them vulnerable in their capacity to deliver services to their citizens, to control corruption, or to provide for sufficient voice and accountability. [And] they face risks of conflict and political instability" (World Bank, 2005, p. 1).

Although every definition sounds different, there are certain criteria, which are included in most of the definitions and these criteria will serve as the definition of fragility or fragile states for this paper:

- Rule of Law is not ensured
- Security is not ensured
- Human Rights are fully or partly restricted
- Legitimacy of government is questionable
- Basic Services for citizens are not guaranteed

There are several institutions, which have developed an index to categorize countries as fragile or stable. Examples for such indexes are "Fragility index of the Country Indicators for Foreign Policy" (CIFP, 2012), the "State Fragility Index" (CSP, 2012) and the "Failed States Index" (FFP, 2013), while the latter provides probably the most extensive and easy accessible index, with datasets from 2005-2013. The "Failed States Index" analyses countries on the basis of twelve criteria in the areas of economy, social affairs and politics (FFP, 2013).

Having the most important criteria of fragile states in mind, it is not surprising to hear that fragility has large negative impacts on the state itself and eventually even on the whole world. Weak and non-legitimized governments are possible reasons for civil wars and other civil unrests (DIE & UNDP, 2009, p. 7). Such wars and unrests can easily expand to other countries what could be seen in the case of the Arab Spring, which started in Tunisia but expanded to the whole region. Fragile states are thus seen as a threat to international peace and security (Iqbal & Starr, 2008, p. 318). Furthermore, fragile states are a hotbed for national and international terrorism, armed conflicts and organized crime such as drugs trafficking or trafficking in human beings (Kaldor, 2007, S. 64). These are just some negative effects of fragile states, the list would go on. However, these examples are enough to show that addressing fragility definitely matters and that it is not only in interest of the respective state but also of the international community to reduce fragility and work towards stability. What stability exactly is, respectively how stability can be defined will be discussed in the next chapter.

2.2.2 Definition of Stability

Having defined fragility, it makes sense to also define stability as the opposite and the favoured condition. While fragility is a condition in which things are not quite predictable but rather arbitrary, stability stands for order and reliability. The same as it was the case for fragility, counts also for the term stability: there is not one correct or universally accepted definition. In the sense of Esteban and

Ray (2001) a political system is stable if no group or community can be better off by initiating a revolution. Or as it Claude Ake (1975) notes: "Political stability is the regularity of the flow of political exchanges. The more regular the flow of political exchanges, the more stability" (p. 273). A more differentiated approach takes Leon Hurwitz (1973) who sees the most common and direct understanding of political stability as the absence of domestic civil conflict and violent behaviour. Furthermore he mentions that "A stable polity is seen as a peaceful, law-abiding society where decision-making and politico-societal changes are the result of institutionalized and functional procedures and not the outcome of anomic processes which resolve issues through conflict and aggression." Finally, according to Marcus Agnafors (2013) "stability refers to the capacity of public authorities to maintain their function and implement laws and policies given the elements within the domain over which they exercise power" (p.441).

Here again, the common and most important criteria of the different definitions will be listed and serve as the definition of stability for this paper:

- Reliable political and legal procedures
- Guarantee for material and intellectual property
- Decisions taken by the state must be foreseeable and comprehensible
- Absence of violence and coercion
- Legitimacy of government

However, it seems important to mention at this point, that stability does not mean rigidity or inelasticity. Even though a political system is stable, it should be able to adapt to changes, which are coming from inside and outside the system. It should not avoid changes, but rather be able to handle changes adequately. (Sandschneider, 1995, p. 118) Furthermore it has to be said that a stable country not only fulfils the criteria, which are mentioned above for political stability, but also aims to reach social and economic stability.

After having gained an overview on the methodology of this paper and the definition of stability and fragility, the focus will now shift to the analysis of whether an improvement of economic foundations will lead to stability or reduced fragility. In order to do that, the three areas of the PSG goal nr.4 will be analysed separately before chapter 6 will draw an overall conclusion.

3. Equality and Stability

The first part of the PSG goal nr. 4 includes the indicators about productive resources and prospects for growth on inequalities. Concerning these indicators, this chapter will focus on the second one, income inequality. It will, however, go further and also discuss socio-economic, political and cultural inequalities. In order to understand the relation between inequalities and stability, vertical and horizontal inequalities will first be defined. Second, the sources and consequences of inequalities will be discussed. Third, possible policy changes to reduce inequalities will be analysed theoretically and empirically by means of examples and two case studies. Finally, a *Theory of Change* will summarize the main findings of this chapter and answer the question whether less inequalities and thus more equality can lead to more stability

3.1 Vertical and Horizontal Inequalities

3.1.1. Definition

Inequalities arise in many domains. In this paper, economic, political and cultural inequalities will be discussed with focus on the economic ones, namely income inequality Income inequality is the result of an unequal distribution of income across the members of an economy and can be calculated by several indicators. The indicator used most frequently is the Gini coefficient, which measures the degree of inequality in the population. The Gini coefficient goes from 0 to 1 with 0 representing perfect equality and 1 perfect inequality (United Nations Conference on Trade and Development [UNCTAD], 2012, pp.45, 74).

We can differentiate between vertical and horizontal inequalities. Vertical inequality shows the difference in income of individuals in a homogenous population and focus thus on economic inequality. Horizontal inequality on the other hand shows inequalities between groups with different economic, social, cultural or political status, with different identities. (Maier, 2010, p.15) Economic inequalities include the above mentioned income inequality and discrimination in access to ownership and employment. Social inequalities result from discrimination in access to education, health care or housing. Political inequalities reflect the unequal opportunities to participate in political processes and take offices. Finally, cultural inequalities reveal the difference in recognition of different groups, for example language and religion. (Stewart, 2009, p.5)

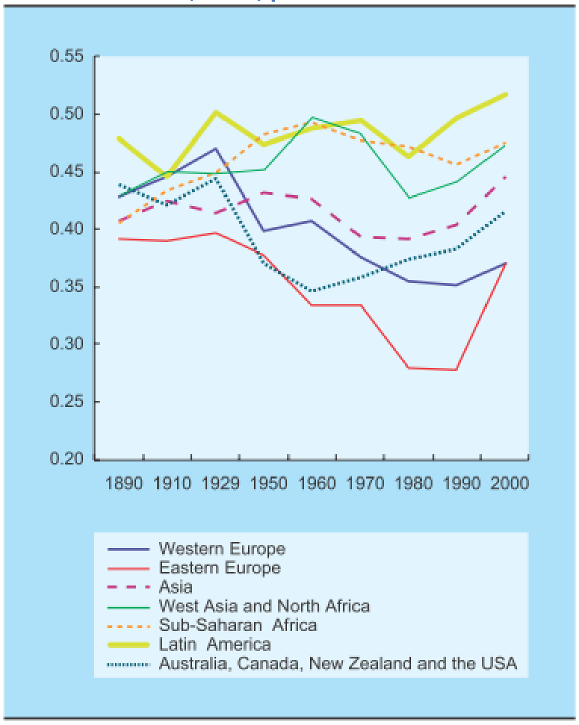
3.1.2. Evolution and Status

Income inequality differs both across region and time. As shown in Figure 2, in most developed countries, income inequality decreased greatly from 1929 till 1950 and moderately until 1980. However, between 1980 and 2000 the Gini coefficient rose again considerably.

In developing countries, such as African countries, inequality rose until 1950 and remained high since then. Latin America experienced a stable but high level of inequality. However, inequality tends to rise or fall in the different countries of Latin America due to political factors like changes in government. These two regions have the world's highest inequality.

In total, East and South-East Asia have lower level of income inequality than Latin America and Africa. However, there can be seen high differences between the several countries in this region, with high Gini coefficient in countries such as Singapore and Thailand and lower Gini coefficient in the Republic of Korea or Taiwan.

Figure 2 Gini Coefficient by Regions, 1890-2000
Source: UNCTAD, 2012, p. 51



Overall, there has been an increase in income inequality in every region since 1980 as it is shown in the graph on the right. Furthermore, income inequality is generally higher in poorer countries than in richer ones (UNCTAD, 2012, pp.51-52).

3.2 Sources of Inequalities

3.2.1. Vertical Inequality

Through his analysis of income inequality in the United States of America, Joseph Stiglitz (2012, p.60) identifies different sources of vertical inequality, mostly found in developed countries. Through globalization, low skilled jobs were displaced to countries where the salaries are much lower. Due to this outsourcing, many low-skilled employees lost their job and thus their revenue, which consequently increased inequality. Furthermore, due to the race to the bottom wages in industrialized countries were lowered as well. Moreover, the economies of developed countries are experiencing unbalanced growth. The income of the richest part of the population increases rapidly whereas the income of the poorest part doesn't grow. However, the greatest source of income inequality is rent seeking at the top of the economy. Stiglitz defines rent seeking as "getting income not as a reward to creating wealth but by grabbing a larger share of the wealth that would otherwise have been produced without their effort" (2012, p. 32). People accused of rent seeking are trying to receive economic benefits through political favours. Politics influence the market through regulations but politic is influenced by lobbying of big corporations. Thus economic inequality leads to political inequality and political inequality leads to economic inequality. It is a vicious circle that leads to a distortion of the market as well as market failures. Thanks to their political power, the richest share of the population can lobby, for example, for tax cuts and thereby inequality rises even further. The deregulation of the finance sectors is one of the best examples of rent seeking and its negative consequences are a cause for financial crises. (Stiglitz, 2012, pp. 34, 48,)

3.2.2. Horizontal Inequalities

Four major sources of horizontal inequalities can be identified. The first one is discrimination in taxation and allocation of public spending. Preferential taxation or discrimination in access to health care, education and public employment to only certain groups of the population increases horizontal inequalities. The second source is high asset inequality. This source is particularly important in agrarian societies where land possession means revenues. Different ethnic groups have different access to land possession. As a consequence, assets inequality thus leads to income inequality. The third source is economic mismanagement and recession, as the latter puts a strain on the economy. However, due to corruption, the burden of the recession does not affect all parts of the population in the same way. The elite can protect itself, while disadvantaged groups pay the biggest price. Lower growth also affects disadvantaged groups stronger than the elite increasing further the income inequality. The last source is resource rents. Unfair distributions of resources are often found in resource rich countries leading to inequalities. (Murshed & Tadjoeddin, 2007, pp. 18-19) The consequences of natural resource management will be discussed later on in chapter 5.

3.3 Consequences of Inequalities

Income inequality has numerous consequences, not only economic, but political and social ones too. As mentioned before, economic inequality and political inequality causes each other in a vicious circle. Thus income inequality leads to political inequality. In a democracy, economic power, for example big corporations, can influence political decisions through lobbying and contributions to candidates. A perfect example of this is the contribution to candidates for the presidency of the United States. One person, one vote is replaced by one dollar, one vote. (Stiglitz, 2012, p. 121) In authoritarian regimes, political favours and influences are won through corruption made possible by economic power (Maier, 2010, p. 21). Through economic and political power, the richest part of the population can influence for example taxation, and thereby introduce taxation that are preferential for high incomes but are economically inefficient. Furthermore, social policies targeting poverty and inequality reduction are not appreciated by richest groups, which will use their influence to make their implementation impossible. (United Nations Development Program [UNDP], 2011, p. 187)

Income inequality also leads to unequal opportunities. Poor people cannot invest in education and thus do not learn higher skills that would enable them a higher revenue. They also cannot invest in the education of their children, which for the most part will not be able to get out of poverty, consequently reinforcing income inequality. (Maier, 2010, p. 14) Through their poor education, poor people also can't participate and contribute to the economy to the full extent of their potential capabilities, which prevents a faster economic growth (Hilker, 2012, p. 4).

Horizontal inequalities lead furthermore to frustrations in the disadvantaged groups. These frustrations evolve in socio-political tensions and erode the social cohesion, for example through competition for scarce resources, which will be discussed in chapter 5 (Hilker, 2012, p. 4). These frustrations and tensions may cause strikes, demonstrations and even lead to civil violence. Violent political movements are more prone to appear and lead an anti-regime rebellion. Additionally, crime rate increases with higher inequality. (Correa-Cabrera, 2004, pp. 15-16, 24) There are a lot of examples of violent events caused in part by horizontal inequalities among others the genocide in Rwanda, conflicts in Kosovo, Nepal, Sudan, riots in the US in 1970s and in the UK with Asian minorities (Stewart, n.d, p.15).

3.4 Policy Changes

Through the different consequences named above, we can see that there is a strong link between inequality and fragility. To sum up, high inequalities lead to political instability, social unrest, increased criminality and increased poverty. All of these factors are responsible for instability and fragility in a state. In the following chapter, possible policy changes aiming at reducing horizontal and vertical inequalities will be discussed and illustrated by examples and two case studies, Malaysia and Northern Ireland.

3.4.1. Vertical Inequality

Investment in Education and Infrastructure

As mentioned in the previous chapter, one of the consequences of income inequality is an unequal opportunity to get an education among the different groups of a population. Poor parents can’t pay for the education of their children and these children get stuck in the poverty trap. The goal of investing in education is to make it accessible to everybody. If everyone has the same starting opportunity, children of poor houses may have a better chance of escaping the poverty trap and thus reducing inequality. Investment in education can take the form of state support for public school and scholarship to enable access to poor children (Stiglitz, 2012, p. 276). However, investment in

education can only reduce inequality if the educated youth has job opportunities after their education. This will be discussed in chapter 4.
Investment in infrastructure has the same goal as investment in education: universal access. If people have access to basic infrastructures such as electricity, water or transportation, they will be able to take their place in the economy more easily, earning an income and thus reducing inequality. (Hilker, 2012, pp. 10-11)

Economic and Tax reforms

Another consequence and at the same time reinforcing source of income inequality is preferential taxes for high income. As mentioned above preferential taxes are a consequence of inequality because the richest part of the population uses their economic power to influence politics. However, it is at the same time a source of inequality because richer people play relatively lower taxes. Furthermore, every cut in taxes represents lost in revenues for the state. These lost revenues could otherwise be used to implement social policies for example to invest in education or infrastructure as mentioned above. In order to reduce inequality, progressive taxes should be implemented, meaning, the higher the income, the higher the paid tax. The progressive tax itself reduces income inequality. Moreover, the additional revenues can be used to further reduce inequality through social policies. As mentioned in chapter 3.2.1, rent seeking is one of the sources of income inequality. Economic reforms need to be passed by the government in order to reduce corporate power, for instance by giving more power to the shareholders. As a consequence, bankruptcy, competition and anti-trust law have to be reinforced. Since the financial sector is responsible for inequalities through its rent seeking behaviour, it needs to be reformed through more transparent and competitive banks, less bonuses and no offshore banking centre. Through these policies, the market should be more efficient. (Stiglitz, 2012, p. 269-275)

3.4.2. Horizontal Inequality

Policy chances aiming at reducing horizontal inequality can be separated in three categories: policies to address socioeconomic, political and cultural inequalities. These three categories can, for most of the policies, be divided in three further categories: direct, indirect and integrationist approaches. Direct approaches target the disadvantaged groups directly. These policies are successful in the short run. However in the long run, they might increase the importance of identity and tensions between the groups, alienating the non-beneficiary groups. Indirect approaches are general policies directed at reducing inequalities between groups. By not targeting any particular group, there is less risk of increasing tensions but the policies are less efficient. Integrationist approaches want to reduce the importance of group boundaries and raise for example national identity. These policies, however, risk hiding and not reducing inequalities. (Stewart, 2010, p. 20) In the following chapters, several policy changes will be described following this categorization. This is however not an exhaustive list of every possible measures. Furthermore, it is important to keep in mind that these policies might not be effective in every situation. The context must always be analysed first.

Socio-economic Policies

As mentioned above, social and economic policies can be separated in direct, indirect and integrationist measures.

Direct policies can affect assets, income and employment, education or health. In order to reduce inequalities in land possession, the government may redistribute it more equitably, through redistribution of its own property. Furthermore, regulations of purchases and ownerships can advantage a previously disadvantaged group. Privatisation terms and bank regulations such as credit allocation can be changed in favour of a specific group. Subsidies and preferential training can help a targeted group to integrate the economy. Moreover, non-discriminatory housing policies have to be put in place. Employment policies can also reduce inequalities. These will, however, be discussed in chapter 4. Direct policies concerning education through quotas for university students can be implemented. Another direct measure is the improved access to health services in poorer areas as well (Brown, Langer & Stewart, 2007, p. 18).

An indirect measure which can be implemented is the progressive tax system discussed under vertical inequality. This system as well as anti-poverty programs benefit disadvantaged groups without targeting them directly. Furthermore, enforcing human rights and anti-discrimination laws achieve the same goal since disadvantaged groups are mostly suffering under human rights violations. For instance, Peru named a Defensorio del Pueblo (public advocate) to defend the rights of indigenous peoples. In case of regional disparities, regional development policies can address horizontal inequalities. Regions might be worse off due to adverse geographical or climatic conditions. Often the infrastructure is more developed in privileged regions and thus increases the inequalities. For example, in Mozambique, the state invested in the privileged South and not in the underdeveloped Centre and North. Thus, this should be reversed through investments in deprived regions. Moreover, different ethnic groups often work in separate economic sectors, in some countries as consequence of colonialism and its division of labour. Another indirect measure is thus the implementation of economic programs targeting the sectors in which the disadvantaged groups are working. Furthermore, fiscal policies can reduce horizontal inequalities by favouring investment in specific regions or economic sectors through tax incentives. Additionally, in many countries, the state is one of the major employers. In case of horizontal inequalities, privileged groups will be overrepresented in the bureaucracy while disadvantaged groups won't be hired. A formal policy is needed to reduce these inequalities. For example, the constitution of Ethiopia stipulates that the different ethnicity must be proportionally represented at every level of the government. An equal representation of the different groups in the bureaucracy means an equal opportunity at a job and thus an income. (Brown, Langer & Stewart, 2007, p. 14, 16-17)

Integrationist measures can reduce horizontal inequalities through economic policies, including for example fiscal incentives, promoting economic engagement across ethnic groups. Furthermore, multicultural schools must be promoted as education plays an important role in integration by uniting students of different identities in the same school and by teaching a shared vision of their country. Moreover, the organization of national and multicultural events strengthens the national identity. For example, the support of national sport teams can greatly help integration. (Stewart, 2010, p.22)

These measures are just a selection of the possible ones. However, according to the country's economy a restructuration of the whole economy might be needed. Unequal opportunities and asymmetry in social capital and economic assets will hold back disadvantaged groups even if the policy changes named above are implemented. In such case, a restructuration of the economic activity across groups is necessary. (Brown, Langer & Stewart, 2007, p. 19)

Political Policies

To avoid conflicts due to horizontal inequalities, one of the essentials is that the different groups of a population are able to participate in the political decision-making processes and have the right to a share of the political power in their country.

The electoral system plays an important role in the participation of the citizens. A direct measure to enable every group a fair representation in parliament and government is to use separate electoral rolls for the different groups. Hence, the seats are not allocated according to regions but to groups. This has been implemented in Cyprus to ensure a balanced representation of Turkish and Greek Cypriots and in New Zealand for a fair representation of the Maori society. Another possibility is to keep a single electoral roll but to have a fixed number of seats for specific groups. India implemented this policy. Representatives of the Scheduled Castes have the right to 15% of the parliament seats but every citizen, not just members of the Scheduled Castes, can vote for them. These direct measures, however, risk increasing the group identity. Concerning indirect approaches, the introduction of proportional representation can achieve a greater balance than a majority system, which excludes most minorities (Brown, Langer & Stewart, 2007, p. 11-12).

To raise integration, political parties are another important factor. In multi-ethnic countries, political parties often represent one ethnic group and elections can thus lead to violence. By introducing broad-based coalitional parties, the party represents more than the interests of one group. For example, in Ghana and Nigeria, political parties must have members and representatives in the whole country. Since the different ethnic groups often live in different regions, this obligation leads to the creation of multi-ethnic political parties (Brown, Langer & Stewart, 2007, p.12).

Changes in the electoral system lead to more equality in the parliament. Measures to enforce more equality at the executive level are necessary as well since the executive maintain most of the power, for example the distribution of resources, one of the causes of horizontal inequalities.
Power-sharing measures are easier to implement in new constitutions, for example in a post-conflict environment. Here the measures can't as easily be separated in direct, indirect and integrationist but in formal and informal ones. Formal measures include the election of representatives of different groups for the highest executive posts. For example, in Lebanon, the three highest political offices have to be occupied by representatives of the three main ethno-religious groups: the president is a Maronite Christian, the prime minister a Sunni Muslim, and the speaker a Shi'a Muslim. Another possibility is a rotation after every period between representatives of the major groups. For example, in Bosnia-Herzegovina, representatives of the Bosnian, Croat and Serb communities are chairman of the three-member presidium in turn. These measures however don't have to be formal. In Ghana, for instance, it is expected that the president and the vice-president should be one from the South and the other from the North even without constitutional obligation. (Brown, Langer & Stewart, 2007, p.13)

Cultural Status Policies

Policies aiming at cultural status inequalities do not involve the redistribution of wealth. However, they are as important to prevent tensions building up and leading to a conflict. These policies concern three areas: religious practices, language policy and ethno-cultural practices.
The recognition of only one official religion is the greatest source of religious inequalities, but some measures can be taken to reduce these inequalities. Every religion should have the possibility to build their places of worship and burial grounds. Religious ceremonies should be recognized and if possible be public holidays. Official state functions should represent all major religions. (Stewart, 2010, p. 24) Ghana represents a good example of promoting religious equality. Even though Muslims represent a minority, Ghana recognizes Muslim's holiday and actively support the pilgrimage to Mecca. (Brown, Langer & Stewart, 2007, p. 24)
Concerning language policies, having one national language is considered to promote cohesion. However, minority groups speaking a different language might feel excluded and disadvantaged. The recognition of several minority languages can thus reduce cultural inequalities. However, having several national languages has costs due among others to translations. Education plays an important

role for language recognition. Teaching in several languages increases costs but also generates benefits, not only culturally but economically. If a minority language is recognized and taught, the economic prospects of this minority will increase. Furthermore, studies show that students learning in their own language will perform better. (Brown, Langer & Stewart, 2007, pp. 25-26)
The recognition of cultural practice is also an important step toward equality. One factor is the treatment of customary law practices. The implementation of a plural legal system will increase the access of the minorities to the legal system and reduce cultural inequalities. For instance, Guatemala acknowledged the different law practice of its indigenous peoples and Nigeria introduced the Islamic Shari'a. (Stewart, 2010, p. 24)

Empirical Cases

Malaysia and Northern Ireland both suffered from high inequalities. This two cases show how the above mentioned can be implemented to reduce these inequalities, with focus on the socio-economic measures.
After the independence in 1957, the population of Malaysia consisted of 62% Bumiputera, 30% ethnic Chinese and 8% Indians. The Chinese part of the population was economically privileged compared to the Bumiputera as the Bumiputera were for the most part poorly educated farmers. Here are some numbers to illustrate the large inequalities between the Chinese and the Bumiputera. As mentioned before, Bumiputera were less educated and earned in average less than half as the Chinese. Furthermore, only 8% Bumiputera were registered professionals. On top of that, they owned less than 2% of capital on the stock exchange. However, since Malaysia had democratic institutions, the political power was in the hand of the majority Bumiputera. These inequalities led to tensions and finally to violent riots in 1969, Bumiputera against Chinese. (Stewart, 2002, p.20) Following these riots, the government implemented the New Economic Policy in 1971 to strengthen national unity. This policy had two goals: "to reduce and eventually eradicate poverty'" and to restructure the "Malaysian society to correct economic imbalance so as to reduce and eventually eliminate the identification of race with economic function" (Second Malaysian Plan 1971-75). The first goal was achieved through several anti-poverty policies aimed at developing the rural areas among other through the extension of social services. The second goal included one measure to increase the 2% capital ownership of the Bumiputera to 30%. Moreover, in order to improve the education of Bumiputera, quotas for public school were implemented according to the share of population. Furthermore, access to credit was facilitated for Bumiputera. (Stewart, 2006, p. 10)

These measures were able to reduce the horizontal inequalities but not eliminate them entirely. The share of capital of the Bumiputera increased and the income differences between Chinese and Bumiputera decreased as shown on figures 3 and 4.

Figure 3 Share of Capital Ownership as Ratio of Population Share
Source: Stewart, 2007, p. 11

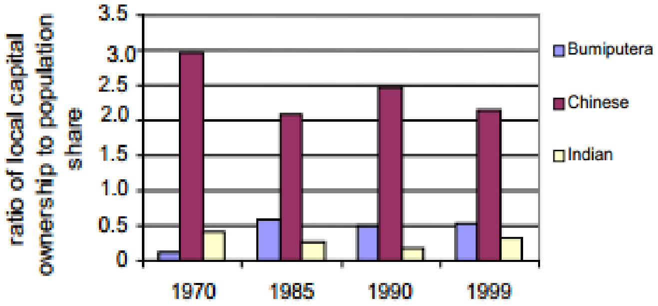
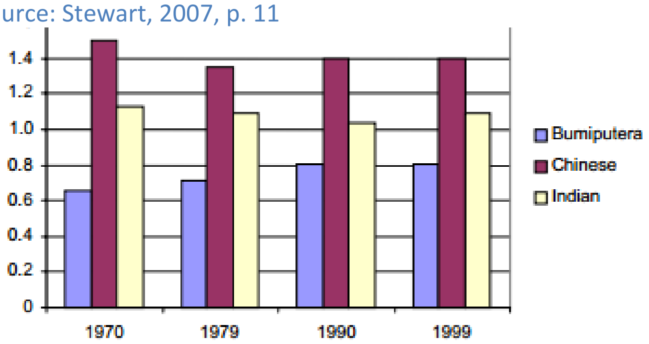


Figure 4 Income in Malaysia: Mean Incomes Relative to Average
Source: Stewart, 2007, p. 11



Moreover, the number of registered professional Burmiputera increased as well, as figure 5 shows.

Figure 5 Professional Employment in Malaysia
Source: Stewart, 2007, p. 11

	Share of total registered professionals as a ratio of population share, %			
	1970	1980	1990	1999
Bumiputera	0.08	0.24	0.47	0.47
Chinese	2.03	2.12	1.86	1.80
Indian	2.91	2.18	1.65	1.94
Standard deviation	1.45	1.10	0.75	0.81

Their effectiveness diminished from the mid-1980s and horizontal inequalities stayed stable since then. Equality in employment kept increasing as a result to the measures concerning education. The policies did not entail efficiency lost for the economy as Malaysia's rapid economic growth at that time shows. The success of the policies can also be seen in the fact that there has been no other violent manifestation since 1973, even after the financial crisis of 1997 that caused anti-Chinese manifestations in Indonesia and Thailand. The political participation of the Chinese increased a little, but was still strongly limited. (Stewart, 2006, pp. 10-12)

Horizontal inequalities between Catholics and Protestants in Northern Ireland were present since the first colonization by English Protestants in the 16th century. At the end of the 19th century, the Protestants controlled the economic resources and had political control, being the majority. Hence, the Catholics suffered not only from economic but also from political and social inequalities. Catholics were poorly educated and had an unemployment rate twice as high as the Protestants.

Jobs accessible to Catholics were low-skilled jobs with lower income. The province had some decision-making authority delegated by the British government. However, due to democratic institutions, the protestant majority had the political power. The Catholics were also discriminated in the public sectors where only 8% of the recruits at the Royal Ulster Constabulary (police) were Catholics, even if they counted 40% of the population. There was also discrimination in housing policies. These inequalities increased during the 20th century leading up to violent conflicts in the 1970s. (Stewart, 2002, p.27)

After these events, the British government implemented several measures to reduce the inequalities. First, the government passed two Fair Employment Acts in 1976 and 1989 aiming at reducing employment discrimination. Furthermore, they introduced policies to reduce inequalities in the access to housing and education. These policies were highly successful: by the 1990s, the socio-economic inequalities mostly disappeared. There was no longer any discrimination in access to higher education. Thanks to better access to education, the difference between the unemployment rates and the income level of the two groups were greatly reduced and thus income inequality diminished as well. Additionally, discrimination in housing was reduced. (Stewart, 2006, pp. 12-13) The British government also tried to reduce political inequalities through the Good Friday Agreement. The Agreement shared the executive, legislative and security power among the two religious communities, for example through collective presidencies. It also granted greater autonomy to the communities for certain public functions, for instance education. Proportional vote was introduced for the new Northern Ireland Assembly and the community had a veto power which was granted for important issues. (McCrudden, 2013) Moreover, through the Police Acts of 1998, 2000 and 2003, the number of catholic police recruits has increased to 50%. A sum up of this evolution is shown in figure 6.

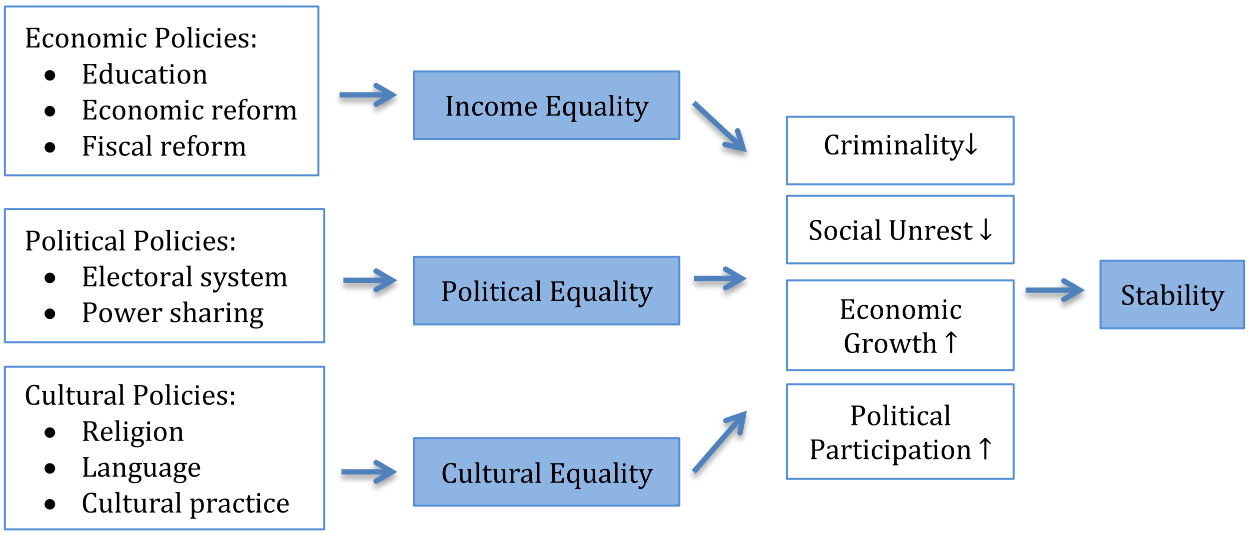
The measures put in place at the end of the 1970s achieved their goal of reducing inequalities, but it took over thirty years. Even though it took a long time, the measures were able to reach their most important goal, peace among Catholics and Protestants. (Stewart, 2006, p. 14)

Figure 6 Changes in inequalities from 1970s to 1990s
Source: Stewart, 2009, p. 36

3.5. Preliminary Conclusion

In the previous chapter, we discussed vertical and horizontal inequalities, their sources, consequences and the relation between inequalities and stability. Possible policy changes to reduce vertical and horizontal inequalities were then presented. The main findings of the previous chapter will now be put together in a *Theory of Change* to find out whether inequalities reduction can lead to stability.

Figure 7 Theory of Change: Equality and Stability
Source: Own illustration



As seen in the *Theory of Change*, the implementation of the policies mentioned above could lead to more political, economic and cultural equality. More equality will then lead to increased economic growth, less criminality, more political participation and thus less social unrest and conflicts. Through these four evolutions, stability can therefore be achieved.

Looking at this *Theory of Change*, it might seem easy to put the required policies into practice. However, it is important to keep in mind that these policy changes cannot just be implemented as they are. The particular context of the country must be analysed and the policies must thus be adapted to the specifics of the country. Another important point to acknowledge is that equality among humans and among groups, even though it has economic benefits, is mostly a moral statement. Furthermore, in a country with high inequalities, these inequalities privilege the elite and the government in place. Policy changes, however, need to be implemented by the same government. Consequently, having the necessary support for them is very difficult. This is why the most successful examples of inequalities reduction happened after conflicts or violent riots, as in Malaysia and Northern Ireland. Witnessing the dramatic consequences of the inequalities might be the necessary trigger for governments to put in place the measures needed.

To sum up, reducing economic, political and social inequalities will lead to more stability. This fact has been confirmed by much theoretical work, but empirically only by few case studies. Due to the specifics of every country, empirically, the *Theory of Change* can thus only be partly confirmed. However, the necessary measures are difficult to implement due to lack of support from the respective governments.

4. Employment and Stability

The following chapter will examine the second dimension of the PSG goal 4, namely Jobs, livelihoods and private sector development. The focus will hereby lay on the first part, the level of employment, which is described as a main index for measuring economic participation and access to income. It is mentioned that the creation of employment helps a country to recover after a conflict. The two further points, the number of new registered businesses and Small and medium enterprises (SMEs) as well as the share of food in household expenditure will be only examined secondarily (INCAF). To analyse the relation between employment and stability, in a first step, some introductorily information and definition will be given. Secondly, the theoretical and empirical evidence of the relation between employment and stability as well as the evidence between different intermediate steps will be discussed (*Theory of Change*). And finally, possible solutions as well as a short preliminary conclusion will be offered.

4.1 Theory of Employment Creation in Fragile Environments

In the following chapter some general information regarding employment creation in fragile states will be given. Firstly, the challenges and opportunities of employment programs in fragile environments will be discussed. Secondly, three possible tracks of employment creation will be offered.

4.1.1 Challenges and Opportunities of Employment Creation in Fragile States

The promotion of employment in post-conflict situations is a difficult task. In fragile contexts the infrastructure are greatly destroyed, private investment and exports are stalled, jobs destroyed and wages driven down. Furthermore, the situation is often characterized by added burden of uncertainty and insecurity (ILO, 2009, p. 15).

In this situation policy changes are important to build up a stable and sustainable environment. However, these kinds of policy interventions are often difficult to implement. Firstly, since the implementation of the programs is taken place prior to the creation of peace, rule of law or stable environment, effective policy changes are difficult to implement. Secondly, in situations of deteriorating governance, where there is an increasing risk of conflict, the government may be unwilling to engage in dialogue with its own population or the international community (Holmes et al., 2013, p. 8).

To implement employment creation programs in fragile environments, it is crucial to have a solid knowledge of the underlying economy of the country. Here a good understanding of the institutions regulating the economy is required. In addition to the formal institutions it is also critical to pay attention to the informal institutions that regulate economic activity. Furthermore, it is important to understand the different dimensions and dynamics of fragility to affectively implement employment creation programs (ILO, 2009, pp. 16-17 & Hilker, 2013).

An immediate challenge is to restore markets and access to markets for goods, services and labour affected by the conflict. To stabilise the country it is crucial to create short-term employment. Hereby the reintegration of ex-combatants and refugees is an important task. However, at the same time sustainable employment, changes of macroeconomic policies and institutions are important (Holmes et al., 2013, p. 8).

On the other side, fragility can also lead to opportunities for donors. In post-conflict countries, where peace resulted from a negotiated peace agreement, it is easier to re-balance power relations, redefine political settlements, legislate new forms of participation and reform institutions. This *window of opportunity* is often not very long lasting and programs should be integrated quickly to use this potential (Hilker, 2012).

In fragile states governments are often willing to act but too weak to effectively react to the situation. In these situations, a range of non-state, informal and civil society institutions have greater legitimacy and capacity than the state. In some cases, these institutions may provide valuable routes to empower poor people and can support bottom-up processes to strengthen state-society relations and empower citizens to make demands and hold institutions to account (Hilker, 2012).

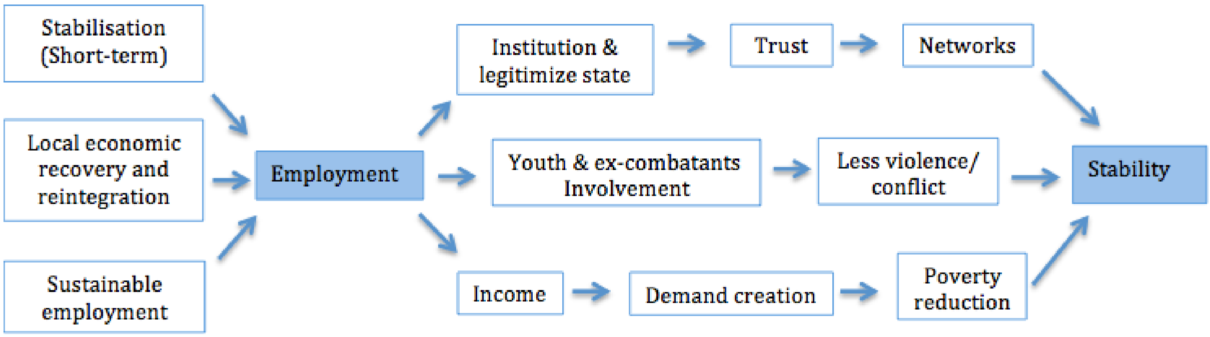
4.1.2 Different Tracks of Employment Creation

To create a coherent and comprehensive strategy for post-conflict employment promotion and reintegration de Vries and Specker (2009) identified three tracks of employment creation that have to be taken into account in programs. It is important to consider all three tracks. Though all three tracks are observed in any phase of recovery, their intensity differs according to the situation in the country. While all three tracks promote employment, they have a different focus: respectively stabilization, reintegration and long-term employment creation. The first track is stabilization. It shall steady income generation and emergency employment to consolidate security and stability, target specific conflict-affected individuals and help to kick-start the economic and social recovery. The second track is the local economic recovery for employment opportunities and reintegration. The goal is to promote employment opportunities at the local level, where reintegration ultimately takes place. It should thereby consolidate the peace process and the reintegration. It includes for instance capacity development of local government, community driven development programs and local economic recovery programs. The third track is the creation of sustainable employment creation and decent work. The ultimate goal is the promotion of sustainable long-term development. It includes the support for macroeconomic and fiscal policies, support for the financial sector and business development services and the promotion of labour-related institutions that enhance employability (de Vries and Specker, 2009).

4.2 Theoretical and Empirical Evidence

In the next section the theoretical as well as the empirical evidence of the *Theory of Change* will be discussed. It shall be tested if employment creation can lead to poverty reduction, creation of state legitimizing factors and the reduction of violent outbreaks due to youth empowerment, which all lead to more stability. To get a clearer structure and to find better evidence for the employment – stability correlation the *Theory of Change* shall be split in three strings: employment creation reduces poverty by creating income and demand; employment reduces violent outbreaks and employment strengthens confidence, trust and social networks due to state legitimizing factors. The literature generally talks from a positive relation between employment creation and stability. The empirical evidence between employment and stability is much harder to verify. There can be seen different problems related to the empirical evidence. First, there are little studies that directly examined impacts on stability. More often it is about the inverse relation that unemployment leads to fragility. Second, most of the studies just measure the impact immediately after the implementation and can therefore not see long-term effects. This is intensified through the focus on the process and output indicators in particular the number of jobs created rather than impacts on stability. The following picture shows the *Theory of Change* between employment and stability.

Figure 8 Theory of Change: Employment and Stability
Source: Own illustration



4.2.1 Employment and Poverty Reduction

In the first part the relation between employment and poverty reduction shall be discussed. Employment creation can reduce poverty directly by generating household income and indirectly by stimulating economy through the creation of demand. From an economic viewpoint, results of job creation are the allocation of earning opportunities to lift households out of poverty, improvement of living standards and reduction of the variation of their main income source. Further path to improved material and subjective well-being are higher earnings in farming, access to off-farm small enterprise activities, migration of family members to cities and transitions to formal sector employment (World Bank, 2011, pp. 8-10). The mainstream development literature sees employment as central determinate of the nexus between growth and poverty reduction.

There is strong empirical evidence that employment creation generally increases incomes and thus reduces poverty in low-income countries in non-fragile states at both micro and macro levels. A significant body of research decomposes the effect of various factors on poverty, demonstrating the critical role of unemployment as a major cause of poverty in middle- and low-income countries. This literature detects employment as a main mechanism for the transmission of economic growth to poverty reduction both directly and indirectly by providing incomes while also stimulating demand at both the macro and micro levels (see for examples Islam (2004) and Essama-Nssah and Bassole (2010)).

Whether this impact applies as well to fragile states was evaluated in various studies. Six of them will be discussed in the following part. The first study concerns a Food for Work (FFW) intervention, meaning programmes where individuals receive a general food ration for their household in exchange for work, in Ethiopia. The study conducts a survey data from 200 randomly selected households, 25 per cent of whom were FFW beneficiaries, during the programme participation. The finding of the study was an increase in household consumption, a negative impact in own production and an increased intake of calories (Gedamu, 2006). A study of Jones (2004) concerning Cash for

Work (CFW) intervention in Afghanistan tested the impact on poverty reduction with interviews of beneficiaries and key informants. CFW is a short-term intervention used by humanitarian assistance organizations to provide temporary employment in public projects, providing cash in exchange for work. The findings are a reduced seasonal migration, reduced sale of assets, provision of community assets as well as reduced soil erosion and water stress. A study by Mattinen and Ogden (2006) regarding a CFW intervention in Somalia is showing a positive impact on consumption and on asset creation as well as stimulation of local economy, stimulation of local trade and increased land cultivation. In another case study on Somalia interviews have shown CFW and FFW can lead to reduced reliance on horizontal redistribution, increased food purchase and purchase of productive investment. A study in Niger conducted by Oxfam (2006) was testing the impact of a CFW intervention by group discussions in 16 villages, interviews with 63 households and key informant interviews. The study noted a reduced seasonal migration, increased frequency of meals, improved quality of food and a reduction in asset sales. The last study conducted by Gilligan and Hoddinot (2006) is the only study also concerning long-term effects of a FFW intervention. The results are a significant positive impact on consumption, a significant reduction in perceived famine risk compared to increase among control and significant impact on growth in food consumption and food security as well as a slower growth of livestock holdings compared to control group.

In addition to assessments of the impact on income poverty multiple aspects of poverty were identified in the studies, namely consumption, distress selling of assets, calorie intake, impact on perceived famine risk, livestock holding, seasonal migration, prevalence of horizontal redistribution, extent of agricultural activity and access to infrastructural assets. The results were exclusively positive, with the exception of one study (Gilligan and Hoddinot 2006), which noted a lower growth rate of livestock holdings among beneficiaries than in the control population, alongside different positive indicators of poverty impact. Furthermore, Gilligan and Hoddinot were the only ones who tested long-term impacts. A main reason of the positive long-term effect was the reduction in household asset losses due to distress selling as a result of the wage. The other studies were only testing short-term effects and therefore do not show indirect and spill over impacts.

4.2.2 Youth and Ex-combatants Involvement & Reduction of Violent Outbreaks

In the next part, the relation between employment creation and the reduction of violent outbreaks shall be discussed. Firstly, the theoretical evidence should be analysed, hereby the greed or opportunity as well as the grievance perspective will be discussed. In a second part, the relation shall be proved empirically, by quantitative and qualitative studies.

In contexts where young people are increasing in number, have fewer opportunities for education and income generation, there is mounting concern that these youth will get involved in violence and therefore threaten local and global peace, stability and development. There are different dimensions of exclusion, namely economic, political and social exclusion as well as cultural exclusion. In regard to economic exclusion, factors like unemployment, underemployment and lack of livelihood are central (Hilker & Fraser, 2009, p. 12). The non-working youth can be seen as a serious potential for conflict in fragile contexts. Furthermore, employment programs create income, which is an important factor for the stabilization of a country. A lack of peaceful income possibilities is often one of the main explanations for the participation in rebel and criminal groups, thus employment creation could reduce the incentives to participate in conflicts. Consequently, an increased employment can get the unemployed youth and the ex-combatants off the streets and thereby can shrink outbreaks of violence (Kükenshöner, 2012, p. 1).

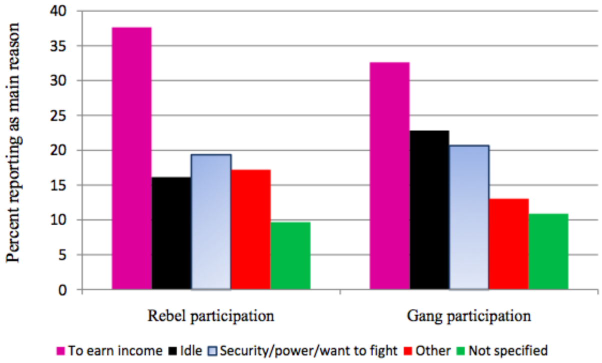
The *greed* or *opportunity* perspectives regard armed violence as the consequence of individual choices to maximise economic, social or political benefits. Rebellion becomes reasonable when the potential gains from joining an armed group outweigh the benefits of not fighting and pursuing alternative income-generation opportunities (Urdal 2007). From this approach, the costs of organising rebellion are lower where there is a large youth population, which is relatively cheap to recruit, and where there are high levels of poverty (Collier and Hoeffler 2004). This perspective supports broadly targeted youth job creation opportunities in countries with large youth populations to reduce the risk of armed conflict by raising the opportunity cost of rebellion.

Another approach is the *grievance* perspective, which regards armed violence as a response to relative deprivation or exclusion. These perspectives are more concerned with the societal or group dynamics of violence. They justify job creation schemes on the grounds that they can reduce inter-group grievance. Group employment schemes such as public works initiatives may also help to build solidarity amongst beneficiaries. This approach encourages more targeted youth job creation interventions, based on an appropriate understanding of the context of the various ethnical and cultural inequalities that cause conflict (Walton, 2010, p. 3)

The guidelines of the International Labour Organization (ILO) describe employment creation as both, a method of providing alternatives to fighting for the youth (an opportunity perspective), whilst also highlighting a grievance perspective by pointing on the importance of reducing inequalities and improving relations between different ethnic and cultural groups (ILO, 2010).

Reintegration programs for ex-combatants form an important part of employment creation programs in fragile states and is primarily designed to reduce the security risk posed by this group. These projects have more short-term goals and are more concerned with managing conflicts than conflict transformation or peace building. As with more general job creation schemes, there is a danger in these programmes of overstating economic opportunity as a motivating factor in youth violence (Walton, 2010, pp. 3-4).

Figure 9 Potentially Explosive Situations
Source: World Bank (2011) p. 6



There has been some research over the past few years, which examine the linkages between exclusion and violence. The evidence mostly falls into two classifications: 1) Quantitative studies 2) Smaller-scale case, mostly qualitative studies (Hilker & Fraser, 2009, p. 13).

One example for the quantitative studies is the survey for the World Development Report 2013 in selected fragile states on the reasons for rebel or gang participation. It shows that a lack of peaceful income possibilities is the main motive for participation in rebel and criminal groups. It demonstrates that a non-working youth is a serious potential for conflict in fragile contexts.

Although there are not a lot of these large-scale statistical analyses linking levels of unemployment to risk of violence, there are many case studies that claim that youth unemployment can lead to instability and conflict. One example is the case study of Sommers (2007). It shows that many of the numerous urban young rebels in Liberia in 2004 were frustrated, unemployed ex-combatants. And it suggests employment creation as a main instrument for the prevention of conflicts.

Another study is the one of Ofem & Ajayi (2008), which evaluates the impact of youth empowerment strategies on conflict resolution in Nigeria by using youth restiveness as indicator of instability. They conducted a survey of 200 young people from 10 communities to test its impact. The results of the study demonstrate that youth educational programs, provision of infrastructures and credit facilities showed significant effects as tools for conflict resolution. Employment opportunities and income indicated positive results yet they were not significant. As a conclusion the study has shown that a proper youth empowerment framework can distract attention to current issues that result to youth restiveness.

The literature indicates that there are several reasons for youth engagement in armed violence, that these motivations need to be understood in relation to each specific context and that there may be substantial variation in the motivations of individual youth within any given context. In-depth case studies suggest that youth unemployment may provide part of the explanation of why armed violence occurs (Cramer 2010). However, even if frustration as a result of lack of livelihood opportunities plays a part in encouraging youth violence, social and political grievances are often more central. Although many early recruits of rebel groups such as the Revolutionary United Front in Sierra Leone or the People's Liberation Front in Sri Lanka were unemployed, the encouraging cause behind violence was not unemployment per se, but rather grievance against an unjust and corrupt system that increasingly excluded the youth (Walton, 2010, p. 2).

Therefore we can see that the youth plays an important part in relation to violent outbreaks respectively stability in fragile states, from an opportunity perspective as well as from a grievance approach.

4.2.3 Legalize State & Strong Institutions, Trust & Networks

In addition, employment is not just a source of income but it can also stabilize thank to its state legitimizing factors. Fragile states often experience crises of legitimacy in the sense that citizens may not accept the state’s basic right to rule. State legitimacy and the development of trust between state and society can be seen as a critical dimension. Employment creation is closely tied to state legitimacy, trust in institutions and the willingness to engage in society. Thereby it can strengthen citizens’ confidence in state and fellow citizens and involvement with state institutions. Consequently, employment can have a positive influence on social cohesion by strengthening the relationship between people. This is important in situations where many people have lost their trust in social relationship as well as in the state institutions (Holmes et al, 2013, p. 7).

Employment is furthermore linked to our personal identity, our beliefs and our values. This can be seen in evidence implying connections between employment status and confidence in institutions and a willingness to engage in civil society (World Bank, 2011, p. 8).

Conflict exists in all societies and need not necessarily to be negative or destructive. Where strong governance and robust social and political systems are existent, conflicts can be solved constructively and methods found for groups to follow their objectives peacefully. However, in situations of fragility with poor governance and weak political and social systems, grievances, disputes and competition for resources are more likely to cause a violent conflict (Hilker & Fraser, 2009, p. 10). This will be discussed more detailed in the chapter 5 of this paper.

In this part we can see the importance of the second and third track by de Vries and Specker (2009). Even if the two former chapters have shown already that the pure employment creation is not enough, here it gets most clear. The simple employment creation due to income generation and emergency employment is not sufficient to bring a fragile state back to stability. There is a need of support for state institutions, so that the state can autonomously create a more sustainable environment for its economy.

One example for a case study in regard to the relation between state and societies in fragile states is "The Legitimacy of the State in Fragile Situations" by Bellina et al (2009). This report suggests that legitimacy concerns the very basis for how state and society are linked and to what extent the state's authority is justified. Fragile states often have ineffective and poor connections with their society. Interventions in fragile situations must therefore focus on relations between state and society and must be adapted to the context. This adaptation to the context is crucial, because the expectations of the citizens differ greatly to the expectations of the external actors. Furthermore, strategies must be tailored specifically for each situation since there are significant differences between the countries.

4.3 Recommended Actions

As developed from de Vries and Specker (2009) the employment creation programs have to take all three tracks into account. As shown in the last chapter, various dimensions have to be taken into account. Various factors, as well as short- and long-term perspective have to be included to implement a coherent program. Furthermore, in each fragile state can be seen a different situation and therefore, first of all an assessment of the context is required, to understand the context of the conflict, labour market opportunities and local needs.

The conflict-prone environment and lack of vital basis services in fragile states often require implementing fast-acting measures with direct effects on income. However, to make the process sustainable at the same time reintegration, the creation of an enabling nation, environment and longer- term activities are crucial (de Vries and Specker, 2009). Therefore, employment in fragile contexts should be promoted through both multi-sectorial projects aimed at directly bringing stabilisation or developing peace, as well as through sectorial projects to improve the framework conditions for the private sector (Kükenshöner, 2012, p. 1).

Regarding the emergency employment, relatively simple, but highly labour-intensive projects of infrastructure measures like schools or roads and the re-cultivation of agricultural lands (cash-for-work measures) should be used (de Vries and Specker). These methods last around three to five months and can offer returnees a first chance to earn money and to get work experience. How many short-term jobs can be established depends directly on the existing size of the investment capacity (Kükenshöner, 2012, pp. 1-2).

Cash-for-Work programs can promote the re-establishment of agricultural production, recreate rural infrastructure and foster market linkages. These sorts of programs lead to widespread economic benefits and can therefore help the economy and livelihood to recover. The Food-for-Work programs are particularly reasonable in parts with a high food insecurity level. To strengthen both of these projects, short or ad hoc trainings can be arranged to offer relatively simple, urgently needed skills (de Vries and Specker, 2009, pp. 39-40). Trainings for the workers are especially important in fragile

environments since a long period of violent conflicts often leads to a lack of well-qualified labour forces (Kükenshöner, 2012, p. 2).
These short-term workers create additional demand, for example for food, which causes indirect short-term employment. A study in Sierra Leone has indicated that every 100 directly created jobs cause five to ten additional jobs alone for food vendors. In addition, the operation of newly created infrastructure leads to direct long-term employment, such as teachers for new schools. These indirect long-term employment effects are considered to be much greater but are more difficult to measure (Kükenshöner, 2012, p. 2).
Alongside this stabilization focus, programs should keep in mind the second track, the local economic recovery for employment opportunities and reintegration. For this track, private sector development and micro-finance are crucial factors. The focus lies here on enhancing consumption and improving markets rather than simply creating jobs. It is hereby important to use existing organization for micro-finance and work directly through local entrepreneurs (de Vries and Specker, 2009).

Finally, the third track can be summarized as the creation of an enabling nation environment. The setup of official capacity should start as soon as possible, so that the state can assume its economic responsibilities (de Vries and Specker, 2009). As a strong private sector is decisive over the long term for a high employment rate, improvement of framework conditions for the private sector in fragile contexts is crucial. In particular small and micro businesses play an important role in creating long-term employment (compare to PSG goal 4.2 c.). However, these enterprises face massive challenges in fragile contexts due to problems like lack of electricity, lack of access to financial services, corruption and poor transportation (Kükenshöner, 2012, p. 2). In addition, the support for social dialogue between government, employers and workers is important to create a stronger political and economic environment (ILO, 2009).

The quality of employment in regard to the type of job, the sector, duration, wage levels and terms of employment and others, are crucial elements in influencing the degree to which employment contributes to poverty reduction. The main point affecting the extent to which employment can form an effective poverty reduction mechanism is the amount to which employment can be promoted in high productivity sectors. Some of the theoretical literature on employment and fragile states reveal the importance of the quality and distribution of employment in defining its impact on poverty, by highlighting the importance of the possibility for the poor to have access to jobs and the sectors in which employment is offered (Holmes et al., 2013, p. 5).
In regard to the youth employment programs some additional factors have to be considered. Firstly, programs have to be founded on wide-ranging analysis of the context regarding the particular youth

population, heterogeneous motivations and the specific causes of youth violence. Secondly, it is important to involve the young people when designing, implementing and evaluating the program. Thirdly, it is crucial to build particular measures to guarantee that the programs reach the youth. Finally, it is essential to address both structural and proximate factors, which lead to exclusion and violence (Hilker & Fraser, 2009, p. 43).

4.4 Preliminary Conclusion

To sum up, chapter 3 makes clear that there is a correlation between employment and stability. Although it is often difficult to find significant empirical evidence to prove the different relationships, most of the case studies found a positive relationship between employment and stability. The correlation can have different explanations, which were analysed in chapter 4.1.1., namely poverty reduction due to income generation, creation of state legitimizing factors and the reduction of violent outbreaks due to youth empowerment. A combination of the various positive factors leading from employment creation to stability can cause a stronger explanatory.

To effectively implement employment creation programs it is important to include various factors, as well as short- and long-term perspective. Furthermore, in each fragile state can be seen a different situation and therefore, first of all, an assessment of the context is required, to understand the context of the conflict, labour market opportunities and local needs. For this purpose the model by de Vries and Specker is the starting point, because it is not only regarding short- term employment but also implementing support for macroeconomic and fiscal policies as well as for the financial sector and capacity development of local government.

5. Natural Resource Management and Stability

The last category of the PSG goals focuses on natural resource management, thus in the following part natural resources and their effects on stability will be discussed.

In the 1950s and 1960s, the dominant hypothesis was that natural resource richness implies economic prosperity. This was the so-called *big push* view, because it was assumed that wealth would raise demand and therefore income. Though, as many natural resource-rich countries began to experience economic, social and political difficulties compared to resource-poor ones, the *resource curse* hypothesis began to gain attraction. This hypothesis brings into focus the harmful effects of revenues from natural resources, both in economic and political way (Fosu & Gyapong, 2011, p. 257). In fact, natural resources have not always fostered growth and development, but in many cases they seem to have provoked instability and conflicts (Lewin, 2011, p 88).

In general, natural resource management is associated with the following three problems (Danish Institute for International Studies (DIIS), 2008, p.1): 1) State fragility 2) Lack of economic development and 3) Persistence of repressive regimes, with little ability or desire to enhance growth and welfare for their people.

However, the introduced resource curse is not inevitable, like the cases of Botswana, Chile, and Norway show: These countries profited highly from their natural resource wealth (International Monetary Fund (IMF), 2007, p.1). Thus in the following chapters the focus lies on questions like which factors led to the achievements of Norway and the challenges in Nigeria, as both countries are rich in oil? Or why is Botswana more stable and has greater economic prosperity as Liberia, or Chile rather than Sierra Leone?

To answer these questions this part will first give some theoretical insights, following by empirical evidences to underpin the findings. Finally, some recommendations regarding natural resource management will be provided.

5.1 Introduction and Definition

This chapter focuses first on different classifications of natural resources and then on the connection between natural resource management, the economic performance of the respective countries as well as their implications for fragility.

First of all, natural resources are highly diverse. Oil, fisheries, soil or water, just to give a short list, are very different from each other in their physical and economic characteristics as well as the problems, which can occur in their management (Edwards & Hone, 2002, p. 76). Moreover, there is an important difference between natural resource abundance and natural resource dependence. The term abundance refers to the amount of natural capital that a country has in its disposal, like mineral deposits, oil fields, forest farmland and so on. On the other side dependence is related to the extent of which a nation relies on these natural resources for its livelihood and development. (Gylfason, 2011, p. 10)

One other fundamental distinction can be drawn between tradable and non-tradable resources as the amount of revenues of internationally traded resources depends heavily on the situation on the world market for these resources, especially prices (Edwards & Hone, 2002, p. 79).

5.1.1 Challenges of Natural Resource Management

This chapter focuses on both the economic and political implications of the resource curse that a natural resource-rich country can face as well as their negative consequences on a country’s stability.

Economic Challenges

Among others, Lipschitz (2001, p. 1) concludes from his studies that natural resource-rich countries often show a relatively poor economic performance compared to not resource-rich countries. Also Frankel (2010, p. 3) states that it has been observed for decades that the possession of natural resources does not necessarily lead to economic success. For example many African countries like Nigeria, Sudan, and the Congo are rich in oil, diamonds, or other minerals, but their peoples continue to face low per capita income as well as low quality of life.

The broader context shows that since World War II, the economies of natural resource-rich countries typically have a growth path picturing a mountain: good performance during times of global economic boom, followed by a strong downturn (Woolcock, Pritchett & Isham, 2004, p. 76). One reason for this is the volatility of the world prices for natural resources and especially the price of oil and natural gas are highly volatile. This volatility of world prices thus leads to volatility of revenues from natural resources (Frankel, 2010, p. 10). The uncertainty resulting from this volatility is vast, especially as many resource-rich countries are dependent on these revenues: In Algeria, Angola and Sudan oil and gas made up more than 90% of exports and after the end of the civil war in Sierra Leone in 2002, 96% of their exports were diamonds (African Development Bank Group (AfDB), 2012, p. 18). Another problem is that prices are very hard to predict and that boom periods are usually followed by decreasing prices (Gelb, 2011, p. 64).

This volatility and dependence on export make natural resource-rich states vulnerable to the so-called *Dutch Disease*. This term refers to the effect that results from the real appreciation of the currency caused by a booming export sector (Lewin, 2011, p. 84). Because of these currency appreciations and thus the higher wages, other export sectors become less competitive on the world market. As a consequence, these sectors diminish and the economy becomes very dependent on natural resource exports (Wohlmuth, 2007, p. 10). This also explains the sectorial shifts in economies in times of natural resource booms (Jerome, 2007, p. 85). In this context it is to notice that countries, whose economies are not diversified, usually have low economic growth (DIIS, 2008, p. 2).

Political Challenges

Besides this usually weak economic performance and possible threats to the economy as outlined above, natural resource-rich states face internal challenges. As a matter of fact, many countries that are exporters of natural resources, especially in Africa, are considered to be failed states according to the "Failed States Index" (see chapter 2.1.1) of 2013. Moreover, countries that are highly dependent on revenues from natural resources score lower on the "United Nations Human Development Index" (Jerome, p. 82). In other words, they are fragile states and it is not surprising that weak public institutions, political instability, unequal distributions of wealth as well as high levels of corruption are common characteristics of these countries (Woolcock et. al., 2004, p. 76).

In assessing the question why natural resource-rich countries score low on these indexes, one answer is, that more often than not, natural resources and their revenues are mismanaged (Jerome, 2007, p. 82). Woolcock et al. (2004, p. 82) highlight in this context that natural resources typically go together with highly concentrated ownership. In fact, Lewin (2011, p. 82) found out that in almost all developing countries, the government has the ownership over the natural resources and is therefore the main recipient of the revenues. This constellation can lead to different problems, like rent-seeking and corruption as well as efficiency losses. It is also not surprising that this easily accessible wealth, concentrated in the hands of the government, often co-occurred with dictatorships and predatory regimes. In this context, Fosu and Gylfason (2011) even state that the “revenues often provide the grease for maintenance of dictatorships” (p. 261). As a consequence, in these states natural resource rents are captured and redistributed in non-transparent ways to advance the interests of favoured constituencies within the public sector, the military or regional or ethnic groups (Auty, 2004, p. 318). This inequality of the revenue distribution can generally lead to fragility as was described in chapter 4. Though, as it will be discussed later on this concentration of ownership also provides a way to effectively manage natural resources, so that these negative consequences can be avoided.

However, the case of Nigeria supports the negative theoretical relation. Nigeria is Africa’s fourth largest economy and highly dependent on the oil sector, as over 90% of export revenues are generated by the export of crude oil (Aigbokhan, Alabi & Ailemen, 2007, p. 115). Even though nearly the entire oil production of Nigeria’s crude oil and therefore the revenues come from the Niger Delta, the area is one of the most underdeveloped regions of the country. This unequal way of revenue allocation and redistribution caused frustration and feelings of hostility among the people of the Niger Delta, as they believe that they have been used and exploited. Moreover, this people believe that they are the worst off, due to the negative impacts of oil exploration. (Aigbokhan et al. p. 116) This also goes together with indicator 3 iii) from the PSG goal nr. 4 about natural resource management, which were described in chapter 2.1. This indicator states that the lack or even the perceived lack of adequate distribution of government revenues and income generated from natural resources can be a key driver of conflicts (INCAF, 2012, p. 16).

A second answer to the question asked above is, that natural resource-rich countries often experience social unrest. In fact, resources, like diamonds or oil, have been associated with causing and financing civil wars in several countries (IMF, 2007, p. 1). Moreover, natural resource-rich countries relapse more often in a conflict compared to countries with conflicts not related to natural resources (AfDB, 2012, p. 18).

Furthermore, Wohlmuth (2007, p. 7) highlights in his studies that in general economic decline, income inequality, rent seeking by ruling elites and competition for the control over minerals can be observed as causes of civil conflicts. On top of that, when looking at the explanations of civil wars he mentions poverty levels, slow growth rates, difficulties in developing strong institutions and high levels of corruption. In this context three types of conflicts can be identified. These categories were initially developed for Ethiopia. However, they provide a good framework also for other resource-rich countries. The study distinguished between the three following categories: 1) competition for positions of power (intra-elite struggles), 2) popular revolts against those in power (struggles between ruling elites and the people), and 3) struggles between the impoverished people over resources. In a nutshell, conflicts and civil wars are caused by elites that are competing for resource rents, by elites that claim for ownership of resources and by problems that arise because the environment, especially the water resources are negatively affected by the exploitation of natural resources. (Wohlmuth, 2007, p. 8) Here, it is also to say that natural resource abundance may also leads to military coups, when several groups compete for power in order to get rents from natural resources (Fosu & Gyapong, 2011, p. 263).

The African Development Bank Group (2012, p. 18) found out in their review of fragile states in Africa that over the last 60 years, natural resources are linked to 40%-60% of international conflicts every year. Furthermore, trade in natural resources, especially diamonds and timber, has financed at least 18 conflicts since 1990, for example in the Democratic Republic of Congo, Liberia, Sierra Leone and Nigeria. Therefore as seen above, proper management of natural resources and thus the revenues are crucial, as competition for controlling them can be a cause of conflict (AfDB, 2012, p. 18).

5.1.2 Wrap Up

In the last two chapters the economic and political aspects of the resource curse were discussed. As a conclusion, five main challenges and thus drivers of fragility can be identified: low economic growth, negative effects of Dutch Disease, concentration of ownership and thus incentives for corruption and unequal distribution of the revenues, low transparency and accountability as well as civil conflicts and wars related to and over natural resources. Therefore it can be said that the negative effect, namely fragility, of natural resource *mis*management is proven.

However, as seen in the introduction these negative impacts of natural resources are not inevitable, neither in economic nor political terms. Among others, Wohlmuth (2007, p. 11) points out that the resource curse can be avoided by pro-active policies. Here institutional quality and sound economic policies are seen as the crucial factors to promote the economy. This analysis is similar to the observed risks of civil conflicts: The risks decline with a higher quality of institutions and with improved economic and social situation. Therefore it is important to rethink the management of natural resources, not only because mismanagement can lead to state fragility, but also as a good resource management offers ways towards stability (DIIS, 2008, p. 1). The next chapter focuses on factors, which could help to reduce the harness of natural resource abundance and thus enhance stability.

5.2 Theory of Natural Resource Management

This chapter will first outline the opportunities of a good resource management, then discuss what good governance is and finally present the *Theory of Change* for the natural resource part.

5.2.1 Opportunities of Natural Resources

As seen above natural resources cannot only lead to fragility, but it can be one of a country's most critical assets for peace building and maintaining stability (AfDB, 2012, p. 18). Also the Danish Institute for International Studies (2008, p. 2) highlights that natural resources can lead to fragility, but can on the other hand provide a potential way out of fragility, given that the inflow of capital can be put for good use, as then the state has the resources that it need to reduce poverty as well as implement development programmes and public services (AfDB, 2012, p. 18). Therefore the key question is how a country can ensure that its abundance in resources remains a blessing (IMF, 2007, p. 1). Thus, which strategy should a country choose to foster growth and stability? And how can the revenues from natural resources be used to enhance stability?

In this context, the African Development Bank Group (2012, p. 27) states that poor governance is both a cause and a result of conflicts. Moreover, according to the United Nations [UN] (2014), countries with good governance are less likely to be violent and poor. The explanation is that when people are allowed to speak they will use less violence as a solution and when the poor get a voice, governments do more likely implement policies which reduce poverty. In fact, good governance provides a setting for equitable distribution of benefits from growth and natural resource wealth. On the other side, the UN (2014) states that the greatest threats to good governance are corruption, violence and poverty, because all of them undermine transparency, security, fundamental freedoms as well as political and economic participation.

Also Sala-i-Martin and Subramanian stressed in a study from 2003, that institutions are important as an explanatory variable. Moreover, the study shows that the impact of resource wealth is strongly linked to institutional qualities and that the natural resource endowments have little influence per se (2003, p. 23). In addition Mehlum, Moene & Torvik report in their study that good institutions can prohibit the damaging effects of resources (Gylfason, 2011, p. 29). Last but not least, the African Development Bank Group (2012, p. 18) highlights that the quality of a country's institutions is a crucial factor for its rate of economic growth as well as how inclusive that growth is. This finding goes together with the indicator 3 ii) of the PSG goal nr. 4 which measures the existence and quality of regulatory framework for the natural resource management as discussed in chapter 2.1 (INCAF, 2012, p. 16).

One other positive effect of strong political institutions is the state's ability to execute economic policies aiming to diversify the economy and thus as seen above enhance economic stability (Gelb, 2011, p. 64). One argument for diversification is that diversified countries perform better over the long run. Another important factor is the rate of population growth. Here long run prosperity and social stability requires employment (see also chapter 4). Consequently, the purpose would be to switch towards a labour-intensive economy, as for example direct employment creation in the mineral sector is often low. Another argument for diversification is the insurance against the volatility of world prices, especially in countries, which are heavily dependent on only a few export goods (Gelb, pp. 60-62). So it can overcome the problem of the Dutch Disease mentioned above.

As a summary, it can be said that good governance and strong political institutions can reduce the risk of fragility, as they help to reduce the harnesses explained in the chapters about the economic and political challenges. But, then the next question arises: What is good governance and how should these political institutions look like?

5.2.2 Good Governance and Strong Institutions

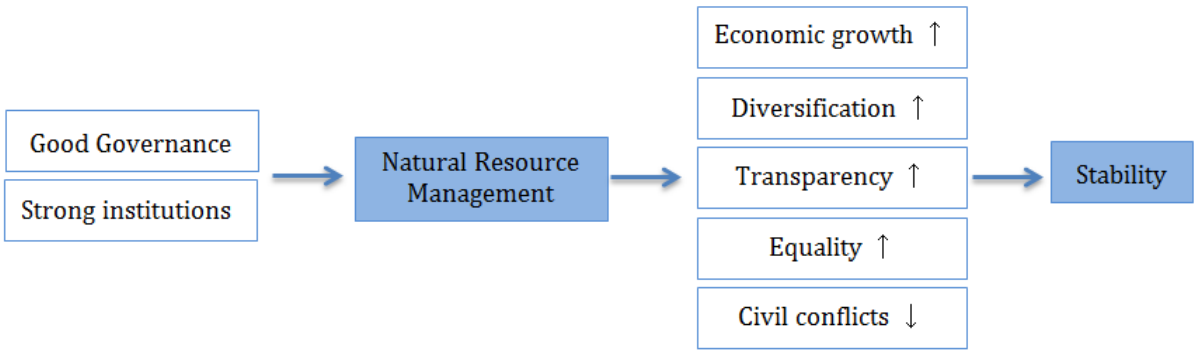
For the UN the term "good governance" refers to the degree to which a country's institutions and political processes are transparent. This includes key activities like elections and legal procedures, which should be accountable and free of corruption. Therefore, good governance promotes equality, rule of law, participation, accountability and transparency in an effective and enduring way. In practice, this means the realization of free, fair and frequent elections, representative legislatures, and an independent judiciary (UN, 2014). In Mehlum's et al. (2002, pp. 1-20) study, the institutional quality is calculated by the average of the following indicators: rule of law, bureaucratic quality, corruption in government, risk of expropriation, and government repudiation of contracts. Thus, a large value of these indexes indicates a high institutional quality. They concluded that the threshold for good institutions is computed at 0.93 in a 0.0 to 1.0 interval (Fosu & Gyapong, 2011, p. 268).

Besides that, the International Monetary Fund [IMF] developed a guide on resource revenue transparency. It provides resource specific good practices, which were directly collected from experiences of resource-rich countries (IMF, 2007, p. 5). This good practices are divided in four categories: 1) Clarity of roles and responsibilities (for example, the government's ownership of resources as well as the power to grant rights to explore, produce, and sell these resources should be well established in legislation) 2) Open budget process 3) Public availability of information and 4) Assurance of integrity (IMF, 2007, pp. 7-10). The guide suggests that countries need to establish priorities among the provided practices both over time and according to their specific circumstances. However, according to the IMF a high immediate priority should be given to improve the quality and public disclosure of data on resource revenue transactions. Equally high priority should be given to establish clear policies regarding the pace of extraction and the use of resource revenues (IMF, 2007, p. 6).

In this context, the question whether democracy is the one and perfect solution for good economic performance draws attention. The broader context shows, on the one hand, that none of the East Asian high performing economies were democratic during the first years of rapid growth and development, and on the other hand the fact that many democracies are economically not really successful could mean that democracy is neither sufficient nor necessary for growth and development. However, in the case of natural resource-rich countries, democracy may be an important factor, because in general, it seems that a democratic government dependent on natural resource wealth is more likely to be responsive to development needs and its people than a dictatorial one (Lewin, 2011, p. 85). Also Gylfason (2011, p. 22) shares this view by pointing out that democrats are less likely than dictators to use resources to consolidate their political power. In a study, he compared the relationship between initial income and democracy for 164 countries during 1960-2000. The democracy variable is defined by an index which runs from 0 (dictatorship) up to 10 (full-fledged democracies). In brief, he found out that democracy is good for growth (Gylfason, 2011, p. 27).

As a summary, the findings from above are shown in the following *Theory of Change* for natural resource management. Here, it is to notice that all the main challenges mentioned above would improve.

Figure 10 Theory of Change: Natural Resource Management and Stability
Source: Own Illustration



5. 3 Empirical evidences – Case Studies of Countries

The next chapter focuses on empirical evidence to prove the theoretical insights from the chapters above. In order to complete this task, different examples of countries which are both rich in resources and stable will be discussed. Due to restriction in space only two successful countries will be presented: 1) Norway with focus on fiscal policy, and 2) Botswana and its leadership.

5.3.1 Norway

Norway is rich in oil and today the earnings from oil constitute a quarter of its GDP and half of its export earnings. Norway's fiscal policy and the management of its wealth were important in stabilizing the national economy (Gylfason, 2011, p. 21). As mentioned above, Mehlum et al. made a study about institutional quality. With an institutional quality score of 0.96, Norway is beyond the above mentioned threshold and is thus considered as one of the non-resource-cursed countries. Moreover, it is often considered as a case in favour of the view that resource richness can enhance growth (Fosu & Gyapong, 2011, p. 269). Here three key features of Norway's approach will be highlighted (Gylfason, 2011, p. 21):

1) From the beginning, the oil reserves of Norway were defined by law as common property resources. In other words, Norway established clear legal rights for its citizens over the resource rents.

2) On this legal basis, the government absorbed about 80 per cent of the resource rents over the years and only used a relatively small portion of the total. It puts the rest aside in the Government Pension Fund.

3) Further, the government implemented both economic and ethical principles to manage the use and exploitation of the oil for the benefit of current and future generations.

According to the guide from IMF, the Norwegian Government Pension Fund can be seen as the best practice for a resource-related fund, as it is part of a coherent fiscal policy strategy. In doing so, it follows two main goals: it aims both to achieve a smoothing and long-term public spending as well as make it independent from volatile oil revenues (IMF, 2007, p. 32). In other words, the fund intends to delink the economy from the up and downturns of oil prices. Last but not least, it wants to minimize the corrosive power of resource richness explained above. (Gylfason, 2011, p. 21, Fosu & Gyapong, 2011, p. 269).

As a summary it is to say that Norway established strong institutions and good governance to manage their natural resources. This finding supports the developed *Theory of Change*.

5.3.2 Botswana

Botswana is another success story as it has been largely free of corruption and civil conflict since independence (Lewin, 2011, p 88). Botswana's major natural resource is diamonds. Its mining started in the 1970s, and since the 1980s the country is a key player in the global diamond market. Today, rents from diamonds account for about a third of GDP, three fourths of exports, and more than half of government revenues. Botswana has created a successful economy and thus achieved a strong rate of growth, which is on average nine per cent since the 1970s (IMF, 2007, p. 32). In fact, very few, if any, mineral-rich countries in Africa are as peaceful and productive as Botswana (Lewin, 2011, p. 85).

Part of its success is the leadership, which, since its independence, has fostered governance structures that have ensured stability as well as social and economic progress (Lewin, 2011, p. 82). Particularly the leadership of its first president, Seretse Khama, was crucial. The discovery of natural resources can easily lead to civil conflicts and even a state's dissolution. To prevent this from happening, Khama's party asserted the state's rights on all mineral resources and implemented a natural resource management system (Lewin, p. 85). This is an example of the positive correlation of concentrated ownership and management of natural resources, as introduced in the theoretical part above, as the government implemented coherent and prudent economic policies, dealing effectively with both large and variable diamond revenues. Consequently, it was successful in avoiding the resource curse. Moreover, appropriate monetary policies have contained inflation as well as stabilized the exchange rate and thus helped to avoid a real appreciation and a loss in competitiveness (Dutch disease). In addition, similar to Norway, significant portions of diamond revenues have been saved (IMF, 2007, p. 33). On top of that, the government established property rights and the rule of law as well as maintained a high degree of transparency. These efforts created trust in the government: The people believe that the government aims to serve the citizens and to promote development and that it is not the instrument of a group or individuals for the purpose of getting power over the revenues and thus wealth (Lewin, 2011, p. 82).

As a conclusion, in Botswana's case, the key to successfully harnessing natural resources lays in good governance and good policies. Even though governance has not been perfect in Botswana, it has been stable enough (Lewin, 2011, p 88). This reflects also the score of 0.70 on Mehlum et al. index of quality of institution (Fosu & Gylfason, 2011, p. 268). After all, Botswana's institutions were strong enough to transform its terms of trade growth to stable economic growth (Fosu & Gylfason, p. 270).

To make this success more clear Fosu and Gayapong (2011, pp. 258-263) compared in a study the case of Nigeria with the one of Botswana, as both countries are very similar in their starting point but very different in their development paths as well as their today's situation. First of all, Nigeria only scores 0.31 on the scale of institutional quality of Mehlum et al., meaning that Nigeria has a high risk to fall into the resource curse. In fact, the growth rate of Botswana's GDP is significant above Nigeria's one. Moreover, in contrast to Botswana, where there has been no major conflict since independence in 1966, Nigeria has experienced a number of civil conflicts during the 50 years since independence. As described above, Botswana has implemented quite strong governance institutions, however, Nigeria scores very different on all the governance measures presented in the in the following table (Note: LIEC = Legislative Index of Electoral Competiveness, EIEC = Executive Index of Electoral Competiveness, XCONST = Degree of Constraint on the Government Exekutives)

Figure 11 Governance Indicators of Botswana and Nigeria
Source: Fosu & Gyapong, 2011, p. 262

Governance indicators, Botswana and Nigeria, 1975–2004

	Botswana			Nigeria		
	1975 –79	1995 –99	2000 –04	1975 –79	1995 –99	2000 –04
Political Rights	6.0	6.0	6.0	3.2	1.8	4.0
Civil Liberties	5.2	6.0	6.0	4.2	2.8	3.6
LIEC	6.0	7.0	7.0	1.0	1.0	7.0
EIEC	6.0	7.0	7.0	2.0	2.0	7.0
XCONST	5.0	6.6	7.0	2.8	2.2	5.0

On top of that, as mentioned above military coups can also occur when several groups struggle for power in order to get revenues from natural resources. Here, Botswana and Nigeria are also very different regarding their post-independence political instability: While in Botswana there were no successful or failed coups or plots, Nigeria experienced six successful coups between 1956 and 2011, two failed coups and six coup plots. (Fosu and Gayapong, pp. 258-263).

5.3.4 Wrap Up

As a conclusion from the theoretical and empirical evidences described above it can be said that strong political institutions and good governance are necessary conditions for enhancing stability. In general, the *Theory of Change* theoretically developed in chapter 5.2.2 got underpinned with the empirical evidences from the case studies of Norway, Botswana and Chile. However, no empirical evidences about fragile natural resource-rich countries that implemented governance structure and thus became stable could be found. This raises the question whether the implementation of governance structure in fragile states is really sufficient for enhancing stability.

5.4 Preliminary Conclusion

The answer to the question asked above, whether the implementation of governance structure in fragile states is really sufficient for enhancing stability, is probably "No". One explanation is that governance structures are rooted in a countries history. Furthermore, the broader context of a country is crucial, for example if the population of a country is ethnically diverse or not. Consequently, it would be easier said than done for example to suppose that Nigeria just has to adopt the same governance structures than Botswana to become more stable. (Fosu & Gyapong, 2011, p. 270) The two following examples will illustrate the finding that it is not sufficient to just copy good practices from other countries:

1) One evidence is the implementation of a natural resource fund. As seen above, Norway was very successful with this policy. In 2003, Nigeria established the Excess Crude Account [ECA], in order to

save revenues during periods when the oil price is above benchmark. However, unlike the case of Norwegians Pension Fund, Nigeria's ECA does not have a well-defined legal framework for its operation. This makes it possible for powerful political groups to get money from it. For example, between 2008 and 2009, the weak governance structures allowed extensive ad hoc withdraws, reducing the ECA balance by almost 85 per cent, or 16 billion dollars, in just 18 month. Another difference is that Norway undertook steps in order to be able to well manage the revenues from petroleum exports and integrated the petroleum sector into the rest of the economy by ensuring forward and backward linkages. Moreover, the development of the non-oil sectors was actively supported by the government of Norway. Consequently, the important lesson here is that it is not sufficient to just set up a fund, but that the necessary legal and political framework should complement its establishment. On top of that, the context and history of the country has to be respected. (Fosu & Gyapong, 2011, p. 269)

2) The second evidence deals with the country Liberia, which is very rich in natural resources, namely iron ore, diamonds and gold but highly unstable. In 2009, with the help of the African Development Bank Group, Liberia became the first African country and only the second in the world which achieved compliance with the Extractive Industries Transparency Initiative [EITI] standards. The EITI is a voluntary agreement between governments, the private sector and civil society with the aim to improve transparency in the relationships between the actors mentioned above and enhance accountability in the revenue management. In short, the goal of these standards is to ensure that all payments between the government of Liberia and the extractive companies are transparent. (AfDB, 2012, p. 27) However, it is to notice that Liberia is still regarded as highly unstable according to the Failed State Index and that over the last five years, a majority of the country's indicators worsened to varying degrees (Fund for Peace, 2013).

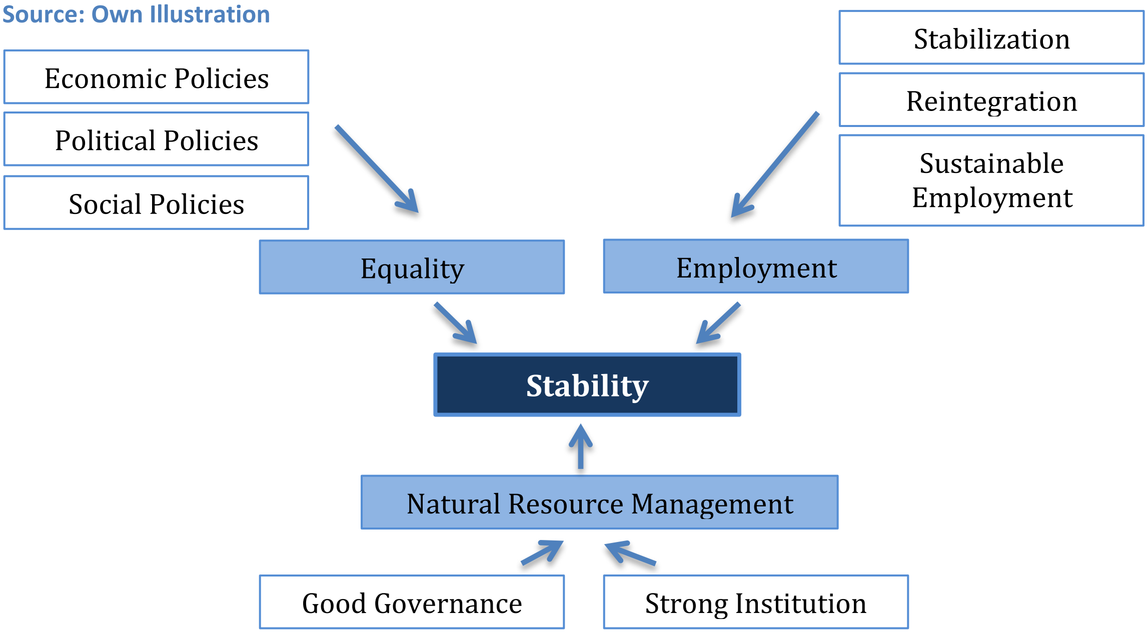
As this two examples show it is not enough to just set up political institutions and strong government, but these structures must be well integrated in the country's broader context as well as respect the nation's history. However, implementing good governance and political institutions is still a key factor of success as this setting allows the country to implement further reforms and policies and thus enhancing stability. This finding can also be transferred to other, namely non resource-rich countries, as there the successful implementation of reforms, for example in form of employment-programs (see also chapter 4), also enhance stability.

To sum up, it can be said that for the *Theory of Change* theoretically developed, no clear empirical evidences could be found, that is a fragile state that implemented good governance structure and thus become stable. It could only prove that countries that have a strong governance structure in the beginning are not likely to experience the resource curse.

6. Conclusion

The research topic of this paper was to find evidence whether an improvement of economic foundations will positively affect the country's stability and thus provides a way out of fragility. In order to address this topic, three key areas of a country's economic foundations, as suggested by the New Deal, were analysed. The main findings of this paper are summarised in the following *Theory of Change.*

Figure 12 Theory of Change: Economic Foundations and Stability
Source: Own Illustration



Findings in the area of equality showed that although more equality is theoretically leading to more stability, empirical evidence is only available in a few case studies. Theoretical work and several studies proved that inequality is a cause for fragility, but the correlation between equality and stability could not be fully confirmed empirically. The main reason for missing evidence is that usually governments of fragile or instable states are not willing to incorporate measures to reduce inequality as the governments themselves benefit from an unequal distribution of wealth.

In the area of employment it became clear, that several factors indicate a correlation between the employment level of a country and its stability. Various theoretical models describe that a higher employment rate has stabilizing effects due to poverty reduction through income generation, creation of state legitimizing factors and the reduction of violent outbreaks through youth empowerment. There are some case studies from which the theoretical findings could be confirmed empirically, however, the evidence is mostly not significant, respectively, there is no absolute empirical proof that employment programs directly lead to more stability or reduced fragility.

A similar conclusion can be drawn in the area of natural resource management. Researchers are convinced that a good management of natural resources through good governance and strong political institutions stabilizes a country. In addition, several empirical findings proof the negative effects, the so-called resource curse in both political and economic ways, of a mismanagement of natural resources on stability However, it first of all seems difficult for fragile countries to implement adequate policies for good governance and second it is not even proven which measures could be applied to all countries as best practice, as the context and the history of the countries varies a lot. Although there are success stories where good governance was a necessary condition for a comprehensive natural resource management and thus stability (for example Norway), evidence that can be seen as universalistic is missing. Therefore, the correlation between good management of natural resources and stability can empirically only partly be confirmed.

Having said this, it is important to highlight that a combination of policies from all three areas seem the most effective in reducing fragility. As it was implied several times during the analysis, all areas are connected and thus influence and support each other (e.g. strong political institutions highlighted in natural resource management may have supportive effects on employment programs). Programs addressing fragility should thus incorporate complementary policies from all parts of economic foundations.

Answering the overall question whether an improvement of the economic foundations leads to more stability, it can be said that yes, from a theoretical point of view that definitely can be confirmed, but empirically, there is only little evidence and can thus only be partly confirmed. One major reason for lacking evidence of a correlation between an improvement of economic foundations and stability can be seen in the overlapping effects of different policies. In other words, it is difficult to prove that measures which aimed at improving the economic foundations directly lead to stability, as the increase in stability might also be the result of measures in the political or social area. This issue gets intensified by the fact that the results of economic programs often only get observable in the long-term, but the evaluation of the program is usually taking place immediately after the end of the program. In short, it is difficult to directly evaluate, which policies lead to which outcome as an outcome usually is the result of the interplay of various policies with different time ranges.

Even though this paper could not fully confirm a direct positive impact of equality, employment and natural resource management on stability from an empirical point of view, it became clear in all three areas that the negative form of the indicators - inequality, unemployment and natural resource mismanagement – constitutes a cause of instability or fragility. Hereafter, aiming at reducing fragility the Swiss Agency for Development and Cooperation should thus focus on eliminating the causes of fragility what according to the findings of this paper implies programs that target the reduction of inequality, unemployment and natural resource mismanagement.

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