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REQUEST TYPE: Book Chapter
USER BOOK TITLE: War, hunger, and displacement : the origins of humanitarian emergencies: Volume 2: Case Studies.
GZN CATALOG TITLE: War, hunger, and displacement
CHAPTER TITLE: El Salvador: Economic Disparities, External Intervention, and Civil Conflict
BOOK AUTHOR: JK Boyce & M Pastor
EDITION: E.W. Nafziger, F. Stewart, and R. Vayryn
VOLUME: 2
PUBLISHER:
YEAR: 2000
PAGES: 365-400
ISBN: 9780198297406
LCCN:
OCLC #: GZN OCLC #: 43811073
CROSS REFERENCE ID: [TN:1698020][ODYSSEY:illiad.library.umass.edu/AMH]
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El Salvador: Economic Disparities, External Intervention, and Civil Conflict

MANUEL PASTOR AND JAMES K. BOYCE

1. Introduction

Complex humanitarian emergencies (CHEs) in the developing world are defined by Nafziger and Auvinen (Chapter 3, Volume 1) and Väyrynen (Chapter 2, Volume 1) as total social crises involving both high levels of death and extensive displacement and movement of populations. Such 'complex' emergencies can be distinguished from 'natural disasters': CHEs occur, in part, because of political economic factors—and, often humanitarian aid to victims is delayed or derailed because of political factors that have diminished the effectiveness of the local government.

While each complex humanitarian emergency has its particular circumstance, the emerging literature suggests at least five working hypotheses as to the *economic* causes and patterns of CHEs in general:

(i) CHEs are more likely to occur in the context of slow or negative growth—or when there is a sudden stop in the economy in the face of rising expectations.

(ii) Such a situation can induce a scrambling for resources amongst competing economic actors. Whether a CHE emerges depends, in part, on whether the society can achieve a consensus over distributing the burden of adjustment.

(iii) This political economy problem of resource competition and adjustment consensus will be worse when the country in question has a skewed class or ethnic structure. Indeed, such preexisting inequality can itself provoke the initial crisis; for example, a civil war to redistribute key assets, such as land, can be the cause of the CHE as can ethnic conflicts.

(iv) CHEs in circumstances which include an inequality of opportunity are more likely when there is a geopolitical reason for external actors to intervene on one side of the distributional struggle. This was especially true in the cold war era but the risks of external intervention—

and the possibility that such intervention will exacerbate rather than resolve the CHE—remain today.

(v) CHEs involving civil conflict can become 'vicious circles': social upheaval slows investment, and the resulting growth slowdown triggers a new round of social unrest. Reversing the cycle involves new policies, some of which must be far-reaching enough to address the fundamental causes.

This list of hypotheses does not exhaust the range of economic causal factors, nor does it address the question of political factors: in many cases, problems of inadequate democratization can trigger social conflicts and make it more difficult to resolve conflicts once they are underway. As a result, no political economy analysis would be complete without some consideration of political arrangements, opportunities, and obstacles. Still, on the economic side, these five working hypotheses offer one way to organize the narratives of case studies as we continue to search for common patterns and possibilities.

The Central American civil wars of the 1980s, occurring in El Salvador, Guatemala, and Nicaragua, neatly square with these hypotheses. Beneath the explosion into violence lay a long-simmering set of tensions due to inequity in the distribution of a key physical asset, land (Wickham-Crowley 1992). Overlaid on this class dynamic, particularly in Guatemala, was a set of ethnic differences between a largely indigenous peasantry and a *criollo* ruling class. The economic slowdowns of the 1980s, partly because of falling commodity prices and the generalized macroeconomic crisis that shook most of Latin America in that decade, added a spark to this kerosene-soaked tinder. An additional factor in the Central American story was the United States, which intervened actively to support its own preferred winners in each country.

Once there was an eruption of armed conflict, most countries experienced a downward economic spiral. While a poor growth record and an inequitable distribution of the fruits of economic development may have been the fundamental causes of the conflict, the conflict itself slowed economic growth as investors, noting the insecure social structure, held back from new investment and engaged in debilitating capital flight. Meanwhile, the various civil conflicts also fundamentally changed the social structure of the countries in question, partly because massive outmigration due to the war depleted human capital and partly because the economic disruptions of war shattered old élite coalitions and created a recomposition of business leadership.

If we learn to understand the central determinants of civil conflict and the resulting humanitarian emergencies, the central policy question is what to do once the downward spiral has stopped and the populace of the country in question is ready to build again toward a functioning economy and viable civil society. Such an outcome is not inevitable: countries can remain in very persistent crises. But when the opportunity is, in fact, there for a new set of post-emergency social and economic arrangements, policy makers need to be supportive.

The imperative of such peace-building is one reason researchers and analysts have decided to search for the causes of complex humanitarian emergencies. After all, if inequality, stalled growth, and negative external intervention can trigger a crisis, perhaps equity, sustainable development, and positive external influence can resolve a contemporary crisis and prevent future CHEs. In the same vein, if slow growth and war come together in a downward spiral in a humanitarian emergency, surely rapid growth, social equity, and the building of peace can and should be packaged together to produce a 'virtuous circle'. Indeed, failure to achieve broad improvements in living standards would fuel social tensions and heighten the risk of renewed civil wars—and a return to war would shatter hopes for economic revival. As a result, economic policy in the post-conflict period has the added charge of addressing the uneven distribution of assets and opportunities that helped trigger the conflict in the first place.

This chapter addresses the economic causes of conflict-driven CHEs and the related question of how best to couple peace-building and new economic policy. The focus throughout is on the civil war in El Salvador; along the way, however, we offer some comparative reflections on the peace process underway in 1999 in Guatemala as well as a few words about Nicaragua, a country which deserves an entirely separate treatment given the particularities of the US role in fomenting conflict in that country. Section 2 begins our analysis by discussing the economic causes of conflicts and the resulting humanitarian emergencies in Central America, again with particular attention to El Salvador. Section 3 discusses the short-run issues of economic and political stabilization, including the problem of financing the costs of peace. Section 4 considers the longer-term policy concerns related to the economic causes of conflict, and argues strongly for seeing the complementarity among growth, equity, and the prevention of complex emergencies. Section 5 offers some concluding observations on theory and policy, particularly for the practice of the international financial institutions (IFIs) that may provide aid to societies both in the midst of, or just recovering from, CHEs.

2. The Causes of Conflict

During the past two decades, Central America was swept by civil wars and the resulting humanitarian emergencies. El Salvador's 12-year civil war, for example, claimed some 75,000 lives. Four decades of armed conflict in Guatemala have killed approximately 100,000 people (World Bank

1995: 2). Many more people have been forced to flee their homes, with some estimates suggesting the displacement of one to two million Central Americans, nearly half of whom crossed international borders (Fagen 1988). Armed conflict also severely damaged the region's economic infrastructure and the costs in terms of foregone investments in physical, human, and natural capital have been high.

The causes of conflict in the region are longstanding and deep, but they centre on the distribution of income and land in the economic sphere, and on the oligarchic structure of state power in the political sphere. El Salvador is a case in point. The roots of the country's civil war of the 1980s can be traced to the latter half of the nineteenth century, when El Salvador became a major producer and exporter of coffee. The volcanic slopes of central and western El Salvador are well-suited for growing coffee. Most of these lands were held by indigenous communities in the mid-nineteenth century as communal property. In response to the opportunities presented by coffee, communal property was abolished by state decree in 1882. By the turn of the century the indigenous communities had been forcibly evicted, and the country's best coffee lands converted into *latifundia*, large estates owned by the 'Fourteen Families' who formed the core of the ruling oligarchy.[1] The result was among the most inequitable patterns of land distribution in the world.

The expropriation and concentration of landholdings 'freed' labour to work on the coffee estates. Much of this labour was required only for the harvest. For the remainder of the year, the seasonal labourers survived on *minifundias*, very small holdings where they grew subsistence crops such as maize and beans. A central aim of the coffee oligarchy was to keep this labour cheap and available, a goal often achieved by deploying military forces to maintain rural law and order and suppress intermittent peasant revolts.

In short, El Salvador's agrarian structure—a highly unequal distribution of land coupled with an available, proletarianized labour force—arose not from free exchanges among optimizing individuals but rather through conflict and repression. Maintaining the distribution of land and income opportunities in the face of popular reactions required intimidation, bloodshed, and other forms of organized violence. During the Great Depression, for example, the slump in world coffee prices placed severe stress on El Salvador's oligarchical agro-export economy. Coffee growers responded by slashing wages and employment. Discontent mounted, and a peasant revolt broke out in 1932. The Salvadoran Communist Party, founded three years earlier and led by Farabundo Martí, helped to lead the uprising, but it was not a carefully-organized affair. The military quickly

[1] As Bulmer-Thomas (1987: 340) notes, in fact some 60 families, rather than 14, came to dominate the country's economic, social, and political life.

crushed the revolt, and government forces killed 10,000–30,000 people in *la matanza*, the slaughter, an event indelibly imprinted on the country's historical memory.

While this organized violence was one dramatic way to perpetuate the underlying inequality, another reproductive mechanism was simply an undemocratic political system. While the electoral trappings of democracy were sometimes present, most observers conclude that political repression was the norm; not surprisingly, between 1932 (the year of *la matanza*) and 1980, all but one Salvadoran President hailed from the ranks of the military. A concerted attempt by moderate forces to elect a civilian leader, José Napoleón Duarte of the Christian Democratic Party, in the 1972 polling was thwarted by widespread fraud. Subsequent protests were suppressed and Duarte was forced into exile. Leftist and other forces began to consider the possibility of armed revolution as one vehicle for social change and by 1979, some guerrilla activity had begun.

Hoping to forestall revolution and to address the pressing need for reform, a left-leaning group of military officers staged a coup in October 1979 creating a new government which also incorporated some reformist civilian leaders.[2] The new 'junta' had two faces. On the one hand, the military nature of the government inclined it to the usual acts of repression to maintain order. In January 1980, for example, the largest demonstration in El Salvador's history, one aim of which was 'to pay homage to the compañeros who had died in the 1932 uprising', was fired on by paramilitary forces, killing scores and wounding hundreds (Montgomery 1995: 108–9). On the other hand, the new government was also inclined toward making certain structural changes to ameliorate the underlying sources of conflict. In March 1980, for example, the government promulgated an agrarian reform which nationalized large estates (see below). It also nationalized the banks and forced the export marketing of coffee and sugar to occur through government channels. While these policies were too little and too late to stem the rising tide of the conflict, they did tend to weaken the power of the traditional élites. Some of these groups responded by organizing right-wing 'death squads' which targeted leftist leaders and community organizers.

The most famous victim of these death squads was the Archbishop of San Salvador, Oscar Romero, a national figure who was consistent in his

[2] The actual history is a bit more complicated than the smooth and continuous picture we present in the text. The initial junta was dominated by the military; in January 1980, the leading civilian leftist politicians became convinced that real change would not occur and resigned from the junta, giving the new government an even more military tint. José Napoleón Duarte, the failed candidate of 1972, joined the junta in March 1980 and oversaw the agrarian and other reforms. While his presence gave a civilian cover to the military and made it easier to garner US support, most observers conclude that his power in the junta phase was limited, particularly since he had virtually no control over the military. His role, however, paved the way for his election to the presidency in 1984 with heavy US assistance.

calls for social justice, dialogue, and peace. Assassinated during a mass, Romero quickly became a symbol of the limits to 'voice' and change under the new government. The limits were even more sharply etched when the thousands of people who gathered in central San Salvador for his funeral were attacked with bombs and machine guns by military forces, leaving scores dead. By the end of 1980, the bulk of the leftist opposition concluded that the avenues for peaceful opposition to the government had been closed. On 10 January 1981, the Farabundo Martí National Liberation Front (FMLN), a group named after the communist leader executed during *la matanza*,[3] launched a military offensive (Acevedo 1996). Sporadic guerrilla warfare, roving death squads, and chaotic street demonstrations had 'matured' into full-fledged civil war.

2.1. *Economic and political contours of the Salvadoran conflict*

Nafziger and Auvinen (Chapter 3, Volume 1) stress the economic backdrop to the outburst of civil war and other humanitarian emergencies, an insight we presented in the introduction as our first hypothesis: CHEs are more likely to occur in the context of slow or negative growth. As noted earlier, a variant of this hypothesis is that such CHEs may be particularly likely when the economy slows after a period of economic expansion and hence rising expectations.

What then was the pattern of economic performance in the period immediately preceding, and during, the initiation of armed conflict in El Salvador? As can be noted in Table 12.1, economic growth was actually quite healthy in 1977 and 1978. In the political confusion of 1979, both growth and private investment dipped; by 1980, private investment had fallen to less than half its 1978 level and GDP plummeted as well. This would suggest that economic performance played a role but not in a simple lock-step fashion of poor growth, more upheaval. Indeed, the pattern is more in line with our notion of rising expectations making it difficult to cope with a slowdown. Political scientists have long contended that revolutions are made in eras of such rising expectations; El Salvador would seem to be a case in point.

The Salvadoran case also seems quite consistent with hypotheses two and three: slowdowns will induce competition over resources by competing actors and this conflict will be more intense when there is pre-existing inequality in the distribution of the resources necessary for survival. Documenting the pre-existing inequality in El Salvador is difficult, in part because data on income shares are available for only a small number of years. Moreover, such figures are subject to significant problems of inter-

[3] The FMLN was formed in 1980 by an alliance of five parties; for details, see Montgomery (1995: Chapter 4).

pretation, not the least of which is the problem of 'second guessing' whether individuals surveyed underestimate or overestimate their reported income and, if so, by how much in each income bracket. The most reliable comparative data presently available for El Salvador are based on two income and expenditure studies undertaken in 1977 and 1990–91. As reported by Gregory (1992) in a study commissioned by USAID/El Salvador, in 1977 the poorest 20 per cent of the Salvadoran population received only 5.5 per cent of total household monthly income.

Virtually all modern observers of the sociology and economics of El Salvador agree that this poor income distribution was driven fundamentally by the structure of land tenure; in the 1970s, for example, El Salvador was estimated as being one of the top five countries in the world in terms of concentration of land ownership (Seligson 1995: 44). This highly unequal distribution of assets had impacts beyond the countryside: the rural landless and land-poor also placed pressure on urban and industrial labour markets since their migration from the low-opportunity rural areas tended to dampen wage gains, particularly for unskilled workers, in urban El Salvador. Certainly, the poor distribution of land contributed to the resentment by popular classes, a structural feature many authors have associated with the likelihood of revolution.[4] Not surprisingly, the FMLN found its strongest support in the countryside, particularly among landless and land-poor peasants. This is one reason why the junta of the early 1980s sought to repair the damage with limited land reform.

If land distribution was a key issue, why did the March 1980 agrarian reform fail to stem the outbreak and acceleration of conflict? The answer lies partly in the reform itself and partly in the dynamics of the conflict. The first phase of the reform took nearly 500 of the largest properties (15 per cent of the land, with the taken properties consisting of cattle ranches as well as cotton, sugar, and coffee estates) in just a few months; the subsequent two phases were intended to redistribute an additional 40 per cent of El Salvador's larger properties over a much longer time period.[5] While the first phase did occur and benefited nearly 40,000 families who were then organized into peasant cooperatives, the new owners were challenged by high debt, inadequate credit, and low levels of government support; these additional factors presented particular difficulties as much of the land (60 per cent of which was pasture or fallow land, including forests

[4] See the discussion in Seligson (1995: 43–4), especially his review of Wickham-Crowley (1992) and Huntington (1968).

[5] The percentage of land refers to the total farmland as of 1971, the last full census of land available at the time of writing; see Wood (1994) and Seligson *et al.* (1993) for details. Seligson (1995) makes good use of a new database which provides a partial picture of ownership in the 1990s in the countryside. Owners under Phase I of the reform were allowed to 'reserve' up to 100 to 150 hectares and were to be compensated for the rest; this naturally led to them keeping the most productive land. For a general view of the changing agrarian structure in El Salvador, see Seligson (1995).

Table 12.1. Macroeconomic performance in El Salvador, 1977–97

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986
GDP (growth) (annual %)	5.0	5.3	−4.2	−11.8	−10.5	−6.3	1.5	1.3	0.6	0.2
Inflation (Dec.–Dec.)	14.9	13.4	14.8	18.6	11.6	13.4	15.3	9.4	31.9	30.3
Investment (as % of GDP)										
Private	13.9	15.6	11.5	6.4	6.2	6.5	7.0	7.6	8.7	10.6
Public	7.3	5.8	6.1	7.1	7.3	6.1	4.6	3.9	3.3	2.5
Real currency value[a] (1980 = 100)	90.8	95.5	97.2	100.0	105.2	115.2	128.9	140.4	172.6	120.8
International trade (US$ mil.)										
Exports	974	802	1,132	1,075	798	700	758	726	679	778
Imports	−861	−951	−955	−897	−898	−800	−832	−914	−895	−902
Trade balance	113	−149	178	178	−100	−100	−74	−189	−216	−124
Current account	37	−279	32	34	−251	−120	−148	−189	−189	−17
Trade balance (as % of GDP)	4.4	−4.8	5.2	5.0	−2.9	−2.9	−2.1	−5.1	−5.7	−3.3
Current account (as % of GDP)	1.5	−8.9	0.9	0.9	−7.3	−3.5	−4.2	−5.2	−5.0	−0.5
Reserves less gold (US$ mil.)	211	268	143	78	72	109	160	166	180	170

[a] Real value of currency uses period average exchange rate, Salvadoran consumer prices, and the US wholesale price index, all from IFS CD-ROM.

Notes: GDP growth from USAID. Inflation calculated from International Financial Statistics (IFS), CD-ROM, March 1999. Exports, imports, trade balance, current account, and reserve position also from IFS, March 1999. Dollar GDP

and mountains) was regarded as poor for agricultural purposes and therefore required significant new investment. The second phase, which was to involve 25 per cent of land holdings and would have had a sharp impact on the profitable coffee sector, was never implemented. The third phase was intended to allow peasants to buy small plots they were renting; this was less politically threatening but even this fell far short of expectations, distributing only one-third as much land (5 per cent of the total landholdings) as had been anticipated for this phase. Moreover, since beneficiaries already needed to be renting to receive land under Phase III, this did little to help the landless whose frustrations were driving them to support the FMLN.

While the inadequacy of the land reform design and the half-hearted government commitment are keys to explaining the failure of agrarian reform to forestall civil war, equally important was the dynamic of the war itself. The government was coupling reform measures with rising military repression of populist forces; as a result, even leaders of open, non-violent political organizations began to fear for their lives and went into exile. In this context, land reform was seen by many as a purely manipulative effort

1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
2.5	1.9	1.0	4.8	3.6	7.5	7.4	6.0	5.0	2.5	4.0
19.6	18.2	23.5	19.3	9.8	19.9	12.1	8.9	11.4	7.4	1.9
10.7	9.5	9.8	11.2	12.3	13.2	13.9	15.0	15.3	15.2	n/a
2.9	3.1	3.5	2.5	2.8	4.0	4.0	3.7	3.4	3.9	n/a
142.6	164.2	184.1	160.9	156.9	166.4	186.7	203.2	215.2	231.0	241.3
590	611	558	644	587	598	1,032	1,252	1,651	1,787	2,414
−939	−967	−1,220	−1,310	−1,291	−1,560	−1,994	−2,422	−3,113	−3,030	−3,521
−349	−356	−663	−666	−705	−962	−962	−1,170	−1,462	−1,242	−1,107
−68	−129	−370	−261	−212	−195	−123	−18	−262	−169	96
−8.8	−8.5	−15.2	−13.8	−13.3	−16.1	−13.8	−14.5	−15.4	−11.9	−9.7
−1.7	−3.1	−8.5	−5.4	−4.0	−3.3	−1.8	−0.2	−2.8	−1.6	−0.8
186	162	266	415	287	422	536	649	758	937	1,308

to calculate trade and current account balance as a percent of GDP from World Tables, 1998, CD-ROM, except 1997 GDP which was author's estimate. Private and public investment from 'Trends in Private Investment in Developing Countries: Statistics for 1970–96' data set by Jack D. Glen and Mariusz A. Sumlinski; on the World Bank's International Finance Corporation web site.

to derail a progressive agenda, the other face of which was a continuation and deepening of organized violence (Lungo 1996). Finally, the FMLN was convinced in the early 1980s (as the reform began) that they could win a military conflict with what seemed to be an unpopular government; thus, the insurgents had little incentive to persuade landless and land-poor peasants to wait out the reforms to see what they would bring.

Part of what thwarted the FMLN's hopes for military triumph is related to our fourth hypothesis on the role of geopolitics and external actors in CHEs: the conflict in El Salvador was affected by the presence of important external actors with agendas that went far beyond the specifics of the Salvadoran society itself. The junta and its successors, including the government of José Napoleón Duarte (the 'unsuccessful' candidate in the derailed 1972 elections) who was elected president in 1984, decided to forego attempts to seek dialogue with the FMLN and instead committed to a military strategy to counter this group's objectives and forces. Such a confrontational attitude was made possible by the financial and political support of the US government, which in a 1981 white paper characterized the Salvadoran conflict as 'a textbook case of armed aggression by communist powers'.[6] While the global rivalry between the US and the Soviet Union, which was being waged in earnest in the 1980s, was not a sufficient condition for civil war, it did help to exacerbate and lengthen the conflict as well as to reduce the incentives for peaceful resolution (particularly given the rent-seeking opportunities that emerged in an economy flush with foreign economic and military aid).

Finally, El Salvador offers evidence for our fifth hypothesis: upheaval itself worsens economic performance and exacerbates the conflict. As the conflict broke out in 1981 and 1982, economic growth suffered, a trend helped along by a sharp decline in world growth and hence El Salvador's export revenues (see Table 12.1). The years 1983 and 1984 brought a tepid recovery but there were clear investment and other costs to the continuing civil war (see Table 12.1). Part of the investment slowdown was due to direct fears that new assets might be lost via military destruction (either because of economic sabotage by the FMLN or because of collateral damage by the government's military forces); part was due to the fact that attempts to address the structural causes of the crisis (such as land reform and nationalization of the marketing boards) discomforted traditional élites.

Yet, unlike many countries experiencing complex humanitarian emergencies, the Salvadoran economy did not experience complete collapse. Note from Table 12.1 that it retained positive, albeit low, growth rates through the post-1983 period of the 1980s; because the population continued to grow, per capita income fell consistently over the period. The ability to avoid total collapse was largely due to external transfers from the US, which helped to finance the military and directly propped up the economy. At the same time, US support for El Salvador in international financial organizations increased the country's bargaining leverage with regard to the severity of the usual structural adjustment package. As a result, the Salvadoran government enjoyed a degree of macroeconomic leeway unavailable to many small countries facing the debt and other shocks of the 1980s. In 1984–85, for example, the Christian Democratic government was able to forego the usual fiscal discipline imposed by the IFIs on dependent economies, and with implicit US and IMF support, expanded both military spending and public employment (with the latter designed to quell some of the accumulating social pressures).

This relative level of largesse and macroeconomic leeway did create its own set of economic problems. Without the usual fiscal discipline, inflation crept above 30 per cent by 1985. During the following year, the US had become less forgiving of fiscal laxity and the Salvadoran government, under pressure from the US Agency for International Development, adopted a typical 'orthodox' economic package which combined fiscal

[6] Cited by Whitfield (1994: 405).

restraint and currency depreciation. As is typical in developing economies, the depreciation part of the package pushed up both import and domestic prices; as a result, inflation remained above 30 per cent in the 'adjustment' year of 1986.

While the inflation rates of 1985–86 were low by contemporary Latin American standards, they represented a record high for the country's post-World War II history. The government therefore turned to a macroeconomic strategy based on stabilizing and defending the exchange rate, with the hopes that this would serve as an anchor that could dampen domestic price increases. For most developing countries, such a strategy would be infeasible but, once again, El Salvador had the advantage of massive flows of external resources. Through most of the 1980s, this consisted largely of official transfers to support the government; growing throughout the period, however, were worker remittances sent by those who had fled the conflict and were working in the US and elsewhere.

Such remittances were therefore themselves a product of the war and may play an important role in other emergencies. Besides indirectly supporting the exchange rate (and therefore helping to limit inflation), such flows helped poorer citizens to maintain their standards of living.[7] However, unfavourable official exchange rates (as well as distrust of the government) meant that remittances were often sent through unofficial channels, limiting the ability of the government to track dollars in the domestic economy and to use them more efficiently to prop up the local currency. To address this issue, the administration of Alfredo Cristiani, who took the Presidency in 1989 in the name of the rightist ARENA party, decided to set a single exchange rate to eliminate the black market incentive and simultaneously opened up currency exchange shops to channel and better capture incoming dollars.[8] These policies were effective. By 1993, remittances had risen to 108 per cent of exports (from 41 per cent in 1989). By 1994, remittances stood at nearly 10 per cent of GDP, more than double the volume of official external assistance (see Table 12.2); by the following year, remittances reportedly topped US$ 1 billion and then reached US$ 1.2 billion in 1997.[9]

Thus, much as there was no simple lock-step from slowed growth to a CHE in the Salvadoran case, the war and the resulting CHE did not lead

[7] According to a poll of the Salvadoran homes that receive remittances, 74 per cent goes to food and clothing, 8 per cent toward housing, 5 per cent to savings, and 4 per cent to the education of the family's children. See Lafitte Fernandez (1997).

[8] Cristiani represented what has been variously described as the 'agro-industrial', 'modern', or 'more moderate' wing of El Salvador's ruling elite, and his ascendancy to the presidency marked a shift in the balance of power within the ARENA party. For discussion, see Wolf (1992), Paige (1993), and Johnson (1993).

[9] There are significant problems with separating remittance flows within the current account movements and various analysts estimate different volumes of flows. We are using a consistent series in Table 12.2. Our figures for 1995 through 1997 came via press and other reports, including estimates available from the US Embassy in El Salvador.

Table 12.2. Macroeconomic significance of family remittances, 1979–94

Year	Remittances (millions of US $)	Remittances as % of exports	Remittances as % of net transfers	Remittances as % of GDP
1979	49.2	4.4	95.7	1.4
1980	59.6	5.5	86.5	1.7
1981	74.7	9.5	92.4	2.2
1982	87.3	12.5	42.0	2.4
1983	97.0	12.8	35.7	2.4
1984	121.0	16.7	38.4	2.6
1985	101.9	14.7	31.9	1.8
1986	134.5	17.8	35.0	3.4
1987	168.7	28.5	29.4	3.6
1988	194.0	31.9	38.1	3.5
1989	203.7	41.0	39.2	3.5
1990	322.1	55.4	56.6	5.9
1991	518.0	88.1	94.6	6.8
1992	686.0	114.7	91.7	8.1
1993	789.0	107.8	89.4	8.1
1994	870.0	104.7	n/a	9.7

Source: Boyce (1996, Table 4.3), based on data provided by the Fundación Salvadoreña para el Desarrolo Económico y Social and Banco Central de Reserva de El Salvador.

to a simple downward spiral in terms of growth; instead, El Salvador's 'low-intensity' war was matched by 'low-intensity' growth. Where the downward spiral does seem to have had clear effects was in the realm of distribution.

While we have noted that remittances tended to soften the worst of the blows to the urban poor, many of whom had displaced relatives working in the US, the conflict and economic disruptions continued to produce inequality. As noted above, the 1977 household income survey indicated that the poorest 20 per cent of the Salvadoran population received 5.5 per cent of total household monthly income; by 1990–91, that share had fallen to 3.4 per cent. If we also recognize that per capita income declined over this interval by roughly 25 per cent, we can see, as Gregory (1992: 5–6) notes, that the decline in the share of income flowing to the lower deciles 'would not begin to provide a true measure of the deterioration of living standards among the country's poor'. The population living in what the World Bank describes as 'poverty and extreme poverty' grew from 51 per cent to 56 per cent over roughly the same period.[10]

[10] The shifts in poverty and extreme poverty come from CEPAL (1993: 7) and cover 1980 to 1990 while the changes in household distribution are detailed in Gregory (1992). Gregory believes the distributional shift is overstated, particularly in the lower deciles, because of significant underreporting of income. While the reallocation upward may be less than that reported in the text, it is still likely to have been substantial.

With the economy underperforming and distribution worsening, the Cristiani government was soon forced to tackle more actively the issue of peace. Initially, the government sought to continue the combination of low-intensity conflict and intermittent peace talks with the FMLN begun under Duarte's government, placing peace on the back-burner as policy makers focused on developing and implementing a new agenda of neoliberal economic reforms. However, two dramatic events in November 1989 pushed the peace process along. The first was an FMLN offensive which brought the war to the capital and dispelled illusions that either side could soon win the war in a strictly military sense.[11] The second was the murder of six Jesuit priests at the University of Central America in San Salvador, an event which laid bare the government's permissive attitude toward military excesses (as well as private death squads) and thereby created new international pressures to resolve the conflict.[12] As a result of both events, and perhaps also the waning of the cold war, US policy shifted to favour a negotiated settlement, altering one of the external factors that had sustained the war. Conveniently enough, President Cristiani was probably uniquely situated to lead such a domestic policy shift: as occurred when US President Richard Nixon opened up US relations with mainland China, few questioned Cristiani's 'anti-communist' credentials and this may have made entreaties to the FMLN more politically palatable to an uneasy Salvadoran élite.

In any case, the movement toward peace negotiations should not be seen as a sudden awakening of élite leaders to the fundamental justice of guerrilla demands. Rather, there was a growing awareness that the 'vicious cycle' of economic slowdown and intense social conflict was damaging the potential economic performance of the country. This gave business leadership, many of whom had little taste for land redistribution or other demands of the leftist opposition, a concrete reason to seek a resolution of the conflict. In doing so, awareness rose that some of the underlying issues would need to be addressed by economic policy in the context of bringing, and building, peace.

Another element in this new political opening was the fact that the business class had been recomposed by both the war and a variety of neoliberal reforms enacted under the aegis of international financial institutions (IFIs) through the 1980s. With an overvalued *colón*, conflict in the countryside, a nationalized marketing board, and a limited land reform, the importance of the traditional landed élite had declined. Meanwhile, a new

[11] The realization that the war was unwinnable was also important in encouraging negotiation in Guatemala; see Jonas (1996: 150) and Perera (1996a).

[12] The six priests, and a housekeeper and her daughter, were slain on the night of 15 November 1989. Suspicions immediately focused on the military. After the war these suspicions were confirmed by the findings of the Truth Commission for El Salvador (1993). For a thorough account, see Whitfield (1994).

business élite based on commercialization and an emerging *maquila* industry (both emerging from a project of trade liberalization and economic 'opening') was gaining ground;[13] for this group, an end to the war held out the prospect of improved individual and national economic performance.

2.2. *Bringing peace*

The Salvadoran Peace Accords, signed in Chapultepec, Mexico in January 1992, represented a major achievement in a dialogic or consensual approach to resolving a civil war-style complex humanitarian emergency. Both sides of the conflict overcame suspicion to detail a process to end armed struggle and allow the leftist opposition to enter more safely the realm of traditional politics, including electoral processes. But even more important is that the peace agreement did not limit itself to the details of a truce but rather sought in a limited way to address at least some of the causes of the conflict.

The potential for organized violence was to be reduced through demobilization of armed combatants, a purge of military officers guilty of human rights abuses, the disbanding of paramilitary forces, and the creation of a neutral police force, the National Civilian Police (PNC). A more equitable distribution of power was to be achieved through the strengthening of democratic institutions, including reform of the judiciary, free elections open to participation by all parties, and the creation of a permanent Human Rights Ombudsman's office. As for the problems of economic inequality, a very modest approach was taken which involved land transfers to ex-combatants and FMLN supporters, microenterprise and housing assistance for ex-combatants, and some expansion of poverty alleviation programmes. Such a 'land for peace' approach may be a hallmark of other attempts to resolve CHEs in general and civil conflicts in particular.

The implementation of the Peace Accords was beset by a number of delays. These were sometimes blamed on financial constraints, but the basic reasons for the delays were generally political: the process of negotiation did not end with the signing of the Accords. For example, the purge of the army officer corps occurred only after substantial delays and required strong international pressure. The land transfer programme and the establishment of the PNC were also subject to serious delays. Failures to fulfil the expectations of demobilized ex-combatants have had serious implications for public security. Ex-combatants are widely cited as a factor in a rise in the country's crime rate, and protests by ex-combatants periodically threaten to rekindle organized violence.

[13] The general liberalization was part of the Salvadoran government's adoption of the 'Washington Consensus' on the need to deregulate the economy and stress the private sector; see Williamson (1990).

There have, however, been some historic successes. The March 1994 elections represented a landmark in the implementation of the Peace Accords. The ARENA party won the presidency, the largest share of seats in the Legislative Assembly, and the vast majority of municipal elections, while the FMLN, participating in elections for the first time, finished second in the presidential race and won a number of Assembly seats. While marred by incomplete voter registration and polling irregularities, the elections were peaceful and the outcome was regarded as reasonably fair by most observers.[14] The 1997 elections actually saw a shift in power and political space as the FMLN, having moderated politically and engaged in more grassroots organizing since 1994, won the mayorships of the capital and other large cities, and captured nearly as many seats in the Legislative Assembly as the main right-wing party, ARENA.[15]

As important as the recuperation of the political system has been the generalized recovery of the Salvadoran economy. If our hypothesis about cumulative effects and 'vicious cycles' is correct—that is, that upheaval breeds economic slowdown breeds upheaval—then peace should bring an economic dividend. The evidence suggests that, in the Salvadoran case, it did. Over 1992–95, private investment recovered and annual growth surged. A worrisome trend was the increasing overvaluation of the Salvadoran currency, the *colón*, which along with an ongoing programme of trade liberalization led to swelling imports and a trade imbalance hovering between 14 and 16 per cent of GDP.[16] Remittances, themselves a

[14] The Secretary-General of the United Nations reported that 'the elections were held under generally acceptable conditions, without any major acts of violence, although serious flaws regarding organization and transparency were detected' (UNSC 1994: 2–3.)

[15] With allies in other right-wing parties, ARENA was still able to garner a majority of the vote in the Assembly but the left and its allies won enough votes to block budgets and constitutional changes. Many observers believe that the negative consequences of ARENA's neoliberal reforms on lower-income groups provided some of the ammunition for the FMLN's strong showing.

[16] Table 12.1's series on the balance of payments indicate a substantial jump in exports (and imports) between 1993 and 1994–95. While this might seem to signal a new health in the Salvadoran economy, part of this change was due to a change in accounting methods rather than real improvement. In 1993, the IMF made a shift in its balance of payments methodology and asked countries to count in the goods payments flows exports and imports for the in-bond (or duty-free) processing zones; previously, the net returns (or value-added) on such transactions had been counted in services. Some countries were able to fully revise their series, updating data for previous years; Mexico was, for example, able to do so because it had long kept separate track of the *maquila* industry. Others simply made the change as of 1994, implying a discontinuity in the meaning of the series; El Salvador may be one of these, according to officials at the Fund. To investigate this indirectly, we went into the *International Financial Statistics* database and compared the international transactions series (which are taken from customs records and do not include in-bond goods) to the balance of payments series (which are reported in Table 12.1 and taken from money flows). El Salvador transactions and payments series are quite similar until 1994. After this, there is a major break, with the balance of payments series jumping up dramatically (as reported in Table 12.1) but with the transactions data posting far more modest increases (for example, US$ 844 million of exports in 1994 and US$ 998 million in 1995); however, the trade balance in the two

product of the displacement of peoples produced by the war, helped to fill the gap although some observers (Boyce 1996) began to question the wisdom of the overall reliance on remittances as well as the exchange rate policy. By 1996–97, the peace dividend had less impact: growth slowed, although the trade deficit shrank to more manageable levels.

Thus, the Chapultepec Accords responded to some of the underlying causes of civil conflict in El Salvador and, as such, immediately helped the country make progress toward a new 'virtuous cycle' of growth and improved social justice. However, the social justice side of this equation has been more limited and steps in this direction have been quite timid. If, in fact, inequity and arbitrary rule contributed to the civil war, further progress on the peace front will require a deepening of economic reforms to achieve a more equitable distribution of wealth and income; moreover, continued strengthening of democratic institutions will be necessary to ensure the rule of law and create the space for the poor and disenfranchised to exercise voice in the setting of public policy. In the absence of such far-reaching economic and political reforms, the roots of organized violence and the possibility of popular reaction will remain. Notwithstanding the historic achievements since the signing of the Accords, de Soto and del Castillo (1994a: 16) observe that 'it would be premature to label El Salvador a success story'.

2.3. Recent conflicts in Central America: unifying themes

During the past two decades, two other Central American nations, Guatemala and Nicaragua, have also been torn by war. While experts in, and citizens from, these countries are likely to stress the unique situation and dynamics of each case, we would suggest that they share with El Salvador four unifying themes in the genesis of conflict: (i) extreme economic inequalities; (ii) profoundly anti-democratic political structures; (iii) a history of violent repression, which often targeted the indigenous ethnic population in an indiscriminate fashion; and (iv) a set of negative interventions by powerful external actors, especially the US.[17]

Table 12.3 presents some basic data on the growth performance of each country in the period leading up to their respective conflicts. All three

accounting methods (transactions and payments) remains relatively close (within US$ 50 million). While some of the divergence could be due to a real increase in *maquila* operations, a development strategy which was indeed being stressed by El Salvador in the mid-1990s, it is our guess that the shift in accounting is responsible for a large share of the 'increase'. Moreover, the fact that the trade balance in both methods is similar suggests that if *maquila*'s were indeed on the rise in real and not simply accounting terms, they were not significant net generators of foreign exchange.

[17] On Guatemala, see Carmack (1988) and Jonas (1991). On Nicaragua, see Lafeber (1983) and Williams (1986). For a general overview of the economies of Central America, see Weeks (1985).

countries experienced substantial growth prior to the eruption of their political and economic crises: real income per capita grew substantially from the early 1950s through the mid-to-late 1970s. Thus, as noted above for El Salvador and stressed by Nafziger and Auvinen (Chapter 3, Volume 1) in their analysis, civil war stems from a population's perception of relative deprivation. Again, the variant of hypothesis one that focuses on rising expectations seems to have more explanatory power.

Table 12.3. El Salvador, Guatemala, and Nicaragua: pre-conflict economic growth

Indicator	El Salvador	Guatemala	Nicaragua
GDP per capita (1970 US $):			
1949/51 average	273.4	309.0	219.2
Peak (1974–80)	486.6	519.5	479.0
Growth rate of GDP per capita	201	107	305
(% per annum, 1949/51 to peak)	(–1978)	(–1980)	(–1974)

Source: calculated from data in Bulmer-Thomas (1987: 312-2).

Moreover, as noted in our hypotheses two and three, conflict was rooted in inequalities which growth alone could not redress. As in El Salvador's coffee boom in the nineteenth century, the benefits of rapid growth in Central American agricultural exports after World War II—notably cotton and beef—were very unevenly distributed. In many cases, peasants were driven from the land, as the spread of export agriculture created 'zones of expulsion' (Bulmer-Thomas 1987: 161; see also Williams 1986). In the political sphere, all three countries were characterized by what Baloyra (1983) termed 'reactionary despotism'. And all three shared histories of resistance and violent repression: *la matanza* in El Salvador; the Nicaraguan peasants' struggle against the US Marines and Somoza's National Guard in the 1920s and 1930s, led by Augusto Sandino; and the toppling of the democratically elected Arbenz government in Guatemala by the CIA in 1954.

A complete analysis of the causes of recent Central American conflicts would undoubtedly include other factors, and would take due account of the variations among countries, each with its own distinctive history. Still, there is widespread recognition, along the lines of our second and third hypotheses, that the most basic causes have been the concentration of economic wealth and political power. The US, in line with our fourth hypothesis, had a big role in the civil wars of the 1980s, funding an armed counter-revolution in Nicaragua, financing the military response of the government of El Salvador, and maintaining a supportive relationship with a repressive army in Guatemala.[18] Finally, each of the conflicts led to

[18] For more on the US in Guatemala, see Jonas (1996).

a downward spiralling of the economy which eventually gave an incentive to all actors to seek a peace which could restore the conditions for growth.

But peace itself is not enough to produce sustained economic recovery (Nicaragua's mediocre performance in the 1990s being a case in point). Instead, the causal chains implied by our hypotheses must be recognized and made part of any post-conflict programme. Specifically, peace-building efforts need to: (i) address the underlying distributional causes of conflict, and (ii) incorporate a more progressive role for external actors. The long civil wars in the region—and the social exhaustion that led to a search for peace—have, at enormous cost, opened the possibility for a historic shift in the concentration of assets and nature of foreign intervention/action. The challenge for willing countries and international policy makers is how best to take advantage of this opportunity.

3. Economic Policy in the Conflict Period and the Post-conflict Transition

In this section, we examine the economics of peace-building, partly as a way to illustrate the power of our causal hypotheses. If we are right about the causes of complex humanitarian emergencies in the Salvadoran/Central American cases, then economic strategies which restore growth and ameliorate distribution should contribute to the (re)construction of civil society in the wake of a conflict. As we will see below, the frequent analytical confusion about the causes of conflict—a confusion this project seeks to clear up—is mirrored by a confusion about how best to address the consequences of conflict. In the post-conflict transition in El Salvador for example, both local authorities and international agencies could have done more to make economic policy consistent with peace; in light of that experience, in Guatemala, the government authorities and international agencies appeared, at the turn of the century, to exhibit somewhat greater sensitivity.

In considering how best to shape economic policy in the context of a CHE or post-CHE period, three broad sets of issues are of paramount importance. The first concerns the problem of financing the immediate costs of rebuilding. In the case of civil conflicts, such costs include the establishment of new democratic institutions, the reintegration of ex-combatants into civilian life, and the repair of physical infrastructure; in the wake of any complex emergency, society itself must be reconstructed. Contemporary economic theory typically takes for granted the basic underpinnings of an economy, including a well-defined and socially accepted distribution of property or 'initial endowments'; a legal system effective at enforcing property rights and contracts; and a state able to per-form necessary economic tasks not fulfilled by markets, such as the provision of public goods. All of these preconditions are compromised or shattered by most CHEs, especially civil war, and they do not spring forth spontaneously upon the signing of a peace agreement. Thus, institution-building is a necessary component of post-conflict transition, and financial and other capacities must be there to accomplish the task. The mobilization of resources for the peace process and institutional rebuilding is a political problem as well as a financial problem. External actors must deploy appropriate conditionalities if their aid is to support the momentum of the peace process and 'crowd in' domestic resources for peace-related needs.

The second set of issues concerns the need for macroeconomic stability, the importance of which is generally most stressed by the IFIs, particularly the IMF and, more recently, the World Bank. Complex emergencies in general and civil wars in particular often generate underlying inflationary pressures; while these pressures are sometimes relieved by the presence of external aid to the government at war, a distortion of economic resource allocation and a deterioration of real incomes for the poor—who are least protected from inflation by wage indexation and asset-price appreciation—are the general results. Given the demands of consolidating peace and (re)constructing institutions, it is tempting to consider a simple expansion of demand to buoy the economy and keep all domestic actors (temporarily) satisfied. This, however, risks macroeconomic crisis in the future and so post-conflict adjusting countries need to maintain some degree of fiscal discipline even as they seek to finance the requirements of peace.

A third set of issues concerns the longer-term interrelationships among economic growth, income distribution, and peace. As noted above, conflict-driven CHEs such as civil wars often arise from a perceived imbalance of income and wealth; unless this is corrected, the seeds for war are sown once again. Fortunately, recent research suggests that ameliorating inequity can actually produce better economic policy and faster economic growth. We tackle this issue in some detail in the penultimate section of the chapter and there too we touch on some of the broader issues of institution-building, especially with regard to the formalization of democratic practices. In this section, however, we focus on the challenges of economic management in both the conflict and post-conflict periods, emphasizing the issues of financing and macroeconomic stability.

3.1. Economic stabilization v. political stabilization: is there a trade-off?

Once a country is locked in a complex emergency, short-run economic stabilization is bound to suffer. Tax revenues will fall, due to both economic collapse and evasion. Government expenditures will remain pressed, by military demands in the case of a civil war and by immediate civilian needs in the case of other emergencies. It is no surprise that nations in the midst of CHEs resort to an inflation tax to try to bridge the gap.

This implies that short-run economic policy during the post-conflict period faces potentially conflicting challenges. On the one hand, some degree of economic discipline is necessary in order to recuperate the domestic economy. On the other hand, political stabilization requires the successful implementation of the measures negotiated in any peace agreement and this, in turn, requires adequate funding. Raging inflation and raging social conflict each have the potential to dampen private investment and impede long-term recovery. Thus, economic policy cannot be judged with regard to its 'soundness' without looking at the conflicts and trade-offs between political and economic stabilization.

For example, while fiscal discipline is usually to be applauded, there is a large intermediate terrain between adherence to rigid macroeconomic targets and profligate deficit financing of government expenditures. In particular, to the extent that deficits are connected to the building of peace and not the waging of war, they may have positive spillovers (through increased security and political stability) to investor confidence. Indeed, analogous to the familiar short-run trade-off between inflation and unemployment depicted in macroeconomics textbooks, there may exist a trade-off between the size of the government budget deficit on the one hand and the social tensions arising from inadequate peace expenditures on the other. This situation is depicted in Figure 12.1; the figure is backward-bending to indicate the possibility, often viewed as probable by the IFIs, that beyond some point the net effect of increased government budget deficits may be to fuel social tensions, for example, by sparking hyperinflation.

One crucial issue, of course, is exactly where on this curve the economy rests; another is whether policy priorities can induce shifts in the curve

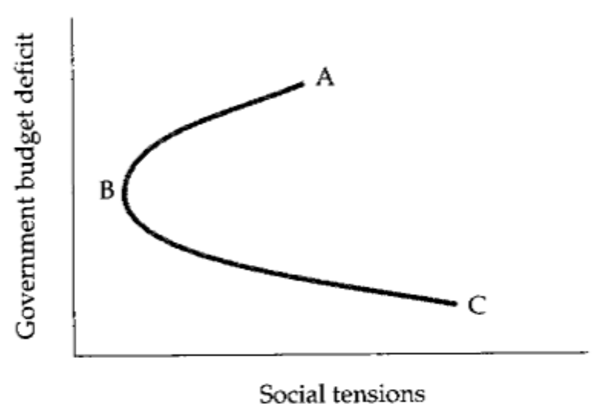

Figure 12.1.

(that is, create a better set of trade-offs such that lower social tensions are consistent with more modest budget deficits). On the first issue, IFI officials tend to assume that countries are on the AB portion of the curve, suggesting that a relaxation of budget deficit targets would jeopardize macroeconomic stability and ultimately endanger the peace process itself. Meanwhile, those responsible for the peace consolidation component of the post-conflict transition have often argued that these special circumstances require some relaxation of the budget constraint in order to better fund peace-related programmes; this view suggests that the economy is in BC territory in which rising deficits might cause some minor macroeconomic disruption but could wind up having a positive net impact on social stability.[19]

Since determining where we are on the curve is difficult—the factors behind the trade-off rely not just on actual macroeconomic outcomes but also on the ability of political actors to mobilize against negative economic effects—one strategy that all sides could potentially agree on is a shift leftward of the curve, such that any given deficit is consistent with a lower level of social tension. In this case, the argument would be not about aggregate expenditure ceilings but rather about government fiscal priorities.[20] Attempts to use IFI influence to improve the trade-off—to promote 'deficit-neutral' shifts in revenues and spending designed to increase funding for peace accord programmes or for reforms that could attack the root causes of the CHE—can be labelled 'peace conditionality'.

3.2. *Fiscal policy, institutional reforms, and peace conditionality in El Salvador*

While some external resources have been provided to the Salvadoran peace process, the IFIs have made clear that amounts will be limited and declining. If we accept this as a constraining factor, then the key policy issue is whether the IFIs have used their leverage to insist on tax enhancement and expenditure reallocation.[21] On the tax front, El Salvador has

[19] For example, an August 1993 study on the 'Economic Consequences of Peace in El Salvador', undertaken by the secretariat of the UN's Economic Commission for Latin America and the Caribbean, concluded:

> [I]t might be necessary to explore the possibility, should the situation arise, of slightly extending the deadline for reducing inflation or of pursuing trade liberalization less vigorously. Within limits, setting more flexible quantitative goals for the stabilization programme might be an acceptable sacrifice, since it would secure the higher goal of ensuring the governability of a society that has, for years, been in the throes of a disastrous civil war (CEPAL 1993: 12.)

[20] In the case of El Salvador, IFI officials have suggested that budget constraints have not actually been especially tight, given the presence of US and other external aid.

[21] We argue in Boyce and Pastor (1997) that El Salvador also let go a unique set of macroeconomic opportunities. Because of remittances, dollars were in abundance and the *colón* was overvalued. The government could have modestly stepped up public investment spending,

seen a modest and steady rise in taxes as a percentage of GDP since the sharp decline of the late 1980s.[22] However, the World Bank (1994b: 182) reports that total government revenue in 1992, at less than 10 per cent of GNP, was the lowest of any middle-income country in the world. Moreover, the recent shift toward reliance on a value-added tax has made the tax system more regressive, rather than using it as one instrument for redressing distributional inequities; it was also reportedly a factor in plunging the economy into an economic slowdown in 1996.[23]

On the spending side, military expenditure was the most obvious candidate for budget cuts to free more domestic resources for programmes mandated by the Peace Accords. By the time of the accords, military spending had already been reduced from the high levels experienced during the more heated phases of the war: in 1984, for example, defence spending as a share of GDP was twice what it was as peace was arriving in 1992.[24] However, even in that latter year, 'in the Western Hemisphere, El Salvador allocated the largest share of total [government] spending for defence (16 per cent) in 1992, and the smallest share for social security and welfare (3 per cent)' (Abdallah 1995: 77). Clearly, this sort of distorted spending pattern had exacerbated the Salvadoran situation by underfunding the social sector even as it fed an ongoing military effort; backing out of the emergency would necessarily involve freeing up resources to deal with social issues.

Salvadoran military spending has indeed declined since the war came to a close. Yet the military has continued to absorb a substantial amount of scarce government resources. The share of Salvadoran GDP devoted to the military in 1993 was 1.7 per cent, according to the IMF (1994: 45), remaining far above the prewar level of 0.7 per cent of GDP.[25] During that same year, the government spent only 0.5 per cent of GDP on health and 1.6 per cent on education, with the former figure representing a decline in spending as a share of GDP and the latter only a slight increase. In 1996 military

further encouraging private investment, and thereby expanding the economy; the resulting deterioration of the *colón* would have helped the export sector.

[22] From a decadal peak of 15.7 per cent in 1977, the tax take as a percentage of GDP slumped steadily to 10.6 per cent in 1983–84, modestly recovered, then plunged again to fall to a low of 7.6 per cent by 1989. Improvement since has been by less than half a percentage point a year.

[23] An additional factor may be a moderation in the growth of remittance inflow as Salvadorans displaced by the war begin to return home and those in the US begin to shift their loyalties and spending to their new home. We warned of this possibility in Boyce (1996) and argued that the government should begin a slow process of accumulating reserves because this could create insurance against a slowdown in the remittance flow and allow a real depreciation of the domestic currency.

[24] The figure for defence spending is 4.4 per cent of GDP (Boyce 1996: 306); the 1992 figure for military spending is 2.2 per cent, as taken from IMF (1994: 26, 45).

[25] Different sources provide conflicting data on defence expenditures. Compared to the IMF data reported in the text, government budget data generally show somewhat lower defence expenditures and somewhat higher education and health expenditures.

expenditure continued to remain substantially above the prewar level, at 1.0 per cent of GDP (IMF 1997).

Why has this relatively slow progress on expenditure reallocation not been a bigger issue between the IFIs and the government of El Salvador? The IMF has traditionally tended to focus on aggregate government expenditure rather than its composition, leaving the details to adjusting governments; in El Salvador, it chose not to alter its approach despite the special circumstances of this war-torn country.[26] A World Bank official closely involved with El Salvador policy stated that the Bank 'never discussed explicitly' the issue of defence expenditure, also suggesting that the issue lies outside the Bank's mandate and competence. However, this reluctance of the IFIs to venture into the terrain of expenditure-shifting in El Salvador is not entirely consistent with the public posture of these institutions, which in recent years have drawn attention to the need to reduce military (or more broadly, 'unproductive' public) expenditures[27]—and it is certainly inconsistent with a broad, multi-actor strategy to tackle the root causes of conflict.

Indeed, there has generally been a lamentable lack of coordination between economic policy and post-CHE social consolidation. The institutional disconnection between economic policy and peace-building has been manifested in the division of labour between the Bretton Woods institutions (the World Bank and the IMF) and the United Nations: in El Salvador, economic policy has been the province of the former, the peace process the province of the latter. Writing in the March 1994 issue of *Foreign Policy*, Alvaro de Soto (who negotiated the Salvadoran Peace Accords on behalf of the UN Secretary-General), and de Soto and del Castillo (1994b) depict the resulting situation by means of a metaphor: El Salvador is a patient on the operating table 'with the left and right sides of his body separated by a curtain and unrelated surgery being performed on each side'.[28]

What about the US, the principal financier of the Salvadoran military during the war? Following the signing of the Peace Accords, US military aid was scaled down to US$ 23 million in the year 1992.[29] While such

[26] The government's November 1991 Letter of Intent to the IMF did include a commitment to reduce military spending from 22 per cent of recurrent expenditure in 1991 to 20 per cent in 1992 (IMF 1991: 58). This provision does not appear to reflect an IMF initiative, however.

[27] See Boyce (1995). For reviews of the debate regarding appropriate IFI policy on military expenditures, see Ball (1992) and Kan (1993). For a characterization by the Fund of 'possibly excessive military spending' as unproductive government spending (along with such traditional targets as overstaffed civil services, generalized consumer subsidies, and inefficient public enterprises), see *IMF Survey* (1997).

[28] For a more general analysis of coordination problems between the UN and Bretton Woods institutions, see Childers and Urquhart (1994: 77–87).

[29] The US provided over US$ 1 billion of military assistance during the 1980s (CRS 1989: 26). This figure includes only direct support via the Military Assistance Programme, Foreign Military Sales Programme, and International Military Education and Training Programme.

cutbacks in US military assistance were accompanied by substantial US funding for Peace Accords programmes, initial conditionalities with regard to progress on peace-related issues were not as strong as they might have been, partly because, in the words of one official, 'we ourselves didn't have the political will'.

This was particularly true in the case of the land transfer programme. It is important to recall that land transfers were limited to ex-combatants and some residents of former conflictive zones, and that most landless or land-poor individuals were left out of the programme by design; this implied that the longer-term inequalities of assets and opportunities that lay at the root of El Salvador's conflict were addressed obliquely at best. Yet even this limited programme of 'land for peace' faced administrative impediments—such as the need to ensure that all back taxes on the land have been paid, or that all joint owners (some of whom cannot be traced) sign the various transfer documents—that could have been removed, for example by presidential decree. Moreover, the land could have been transferred as an outright gift, rather than saddling the new owners with a debt for its purchase. The Salvadoran government was politically unwilling to take these steps, partly because authorities remained uneasy about tithing land to individuals who were on the other side of a civil war. The US, the main funder of the land transfer programme, chose not to pressure the government to be more forthcoming; the result was a land transfer programme which, in the words of a USAID memorandum, is 'doomed to failure because, quite simply, it is designed to fail'.[30] While this indictment may be overly harsh—there have been some concrete benefits to those who did receive land—many could reasonably conclude that the Salvadoran government and its international allies came up short, particularly given the unique opportunity to have the land transfer programme evolve into a more far-reaching reform.[31]

While we have concentrated on economic causes and consequences, there is clearly an interplay with political factors. Indeed, in terms of promoting improved distribution, political 'space' for the advocates of the poor and the landless can be critical. This suggests that one area where the IFIs and other external actors could be indirectly helpful is with regard to promoting *governance* reforms which encourage democracy and allow the populace a larger role in the determination of economic policy; this, as

[30] The latter quote appears in a May 1994 USAID memorandum titled 'Land: The Impossible Dream'. For further discussion of donor policies in post-war El Salvador, and of the extent to which they exercised peace conditionality (or failed to do so), see Boyce (1995) and Fagen (1996).

[31] Interestingly, one area where the land to ex-combatants programme was relatively successful was in the area of gender-equity. For example, females were around 29 per cent of the FMLN land beneficiaries and men and women fighters who formed a couple received land in their own names. See Deere and León (1997).

noted above, would create a sort of 'back door' route to encourage a more progressive tax system and less regressive expenditures.

With regard to such governance issues, the record of the US is mixed. As early as 1991, the US included in its Economic Support Fund (ESF) programme measures to strengthen democratic institutions, especially the judiciary (see Belt and Lardé 1994: 7). In 1993–94, for example, the US held up deliveries of police vehicles and equipment until the Salvador government agreed to remove the controversial former head of the National Police's Narcotics Unit from his position as deputy director of the new civilian police force. Still, as noted above, US officials have allowed government manipulations to stall the land transfer process.

While governance issues, including the legal framework, judicial reform, and the strengthening of democratic institutions, were once viewed as outside the purview of the IFIs, IMF Managing Director Camdessus, speaking in June 1994, included 'good governance, that is, publicly accountable and participatory government that serves the interests of all of society rather than sectional interests' as a crucial ingredient in the 'recipe for success' in structural adjustment and economic development (*IMF Survey* 1994: 209). Similar pronouncements have been heard from the World Bank (World Bank 1994a). Yet the practice of the IFIs in El Salvador has fallen far short of the pronouncements: in their own project lending, the IFIs have contributed nothing to the various high-priority programmes mandated by the Peace Accords nor have they deployed formal conditionality or informal policy dialogue to support these programmes indirectly.[32]

The leverage of external actors is strongest in the immediate post-conflict setting, when foreign resources are extremely scarce and new sets of domestic alliances have not yet congealed. As peace settles into place, external influences may be less important; this is particularly true in El Salvador where the government has been able to replace its dependence on US transfers with a new reliance on workers' remittances.[33] The time for IFIs to exert maximum effect is in the initial post-conflict or post-emergency period. In our view, more could have been done in El Salvador with regard to both economic and political reform.[34] The failure to do so could present the risk of future CHEs—or at least the possibility of simmering social tensions which will eventually dampen economic performance.

[32] A noteworthy exception is a US$ 20 million Inter-American Development Bank (IDB) loan to El Salvador to support judicial reform, approved in March 1996. This loan, in effect, expands the notion of 'infrastructure' considered appropriate for IDB lending beyond the traditional foci on physical works and human capital investment to include the strengthening of democratic institutions.

[33] Indeed, one key policy issue between the US and the Salvadoran government is the latter's desire for the former to continue to permit Salvadoran immigrants to reside in the north and send remittances south.

[34] An internal World Bank evaluation (World Bank 1998a) reaches a similar conclusion.

3.3. *The peace process in Guatemala: a learning curve for the international community?*

In Guatemala, negotiations to end Latin America's longest guerrilla war took the form of a series of separate accords—on human rights, indigenous peoples, refugee resettlement, socio-economic issues, and the military—between the government and the rebel Unidad Revolucionaria Nacional Guatemalteca. The negotiators reached an accord on socio-economic issues in May 1996 and concluded the accord on military issues in September 1996; the final accord was signed in December of that year.

During this process, the IFIs took a more pro-active stance than in neighbouring El Salvador. At the request of Jean Arnault, the United Nations Moderator of the Guatemalan Peace Negotiations, representatives of the Inter-American Development Bank (IDB) and the World Bank met in 1995 with negotiators from both sides to discuss drafts of the socio-economic and agrarian accord—even before a formal peace had been reached on the usual political and military issues.[35] Such involvement may have affected the stance of the IFIs as well as the outcome of the negotiations. The World Bank representative at the Informal Donor meeting for Guatemala held in Paris in June 1995 stated that 'there is wide scope for reducing defence outlays' in Guatemala—a striking departure from the earlier reticence of the IFIs on this issue in El Salvador (IDB 1995a). On the other side, an IDB representative to the negotiations around the socio-economic and agrarian issues believed that IFI influence had helped to produce an accord which was more 'realistic'.[36]

In the various accords, the government pledged to improve health and education and to provide low-cost credit for land acquisition by Guatemala's poor.[37] The 1996 military accord included promises to reduce military spending and personnel by a third in 1997.[38] The IDB launched a US$ 50 million project for 'support of the consolidation of peace' in Guatemala which resembled a social investment fund targeted to ex-conflictive zones, with special measures to guarantee 'the full participation of the beneficiary communities' (IDB 1995b).[39]

The socio-economic accord also mandated annual increases in the ratio of taxes to national income, targeting increases from 8 per cent of GDP prior to the accord (the lowest ratio in Latin America) to 12 per cent by the

[35] The meetings, held separately in Washington with Guatemalan government negotiators, and in Mexico with commanders of the URNG, were conducted so quietly that many senior IFI officials remained unaware of their existence.

[36] The assessment comes from a personal interview, May 1996.

[37] See *Los Angeles Times* (1996). See also Acuerdos de Paz (1997).

[38] See Perera (1996a and 1996b). See also Acuerdos de Paz (1997).

[39] The IDB's growing influence in Central America is indicated by the fact that it now chairs the consultative Group for Guatemala, which met in Brussels in January 1997 to formalize aid pledges after the signing of the final peace accord.

year 2000. In addition, the accord specified that the tax system shall be 'fair, equitable and, on the whole, progressive'. Meeting these fiscal commitments would be no small achievement. In the 36 years preceding the accord, Guatemala's tax ratio averaged less than 8 per cent (Casanegra *et al*. 1997: 2)—testimony to the deeply entrenched resistance of the country's ruling élite to taxation for social spending.

During a May 1997 visit to Guatemala, IMF Managing Director Michel Camdessus announced that the key condition for an IMF stand-by agreement would be compliance with these tax-revenue targets. And in marked contrast to the Salvadoran experience, the World Bank has explicitly linked its aid to implementation of the peace accords: while proposing to lend US$ 310 million to Guatemala over a three year period, the Bank cautioned that 'we would be prepared to lower our lending to about US$ 200 million if the government were no longer making progress along the lines of the Peace Accords, in particular the Socio-economic Accord' (World Bank 1998b: 22).

Regrettably, the IFIs have been less attentive to the distributional side of the tax coin: they have not pressed vigorously to make taxation more progressive in Guatemala, instead clinging to the conventional wisdom that distributional objectives are more easily addressed through expenditures. Yet the incidence of the tax burden is critically important, not only because it too can affect the well-being of the poor, but also because it affects the political sustainability of tax reforms. In a context of democratization, the latter issue is particularly germane: public perceptions as to the fairness of tax policy, as well as the efficacy of government expenditure, will determine whether Guatemala secures the fiscal underpinnings of a lasting peace.

While this review suggests that IFI policies in Guatemala may not entirely replicate the shortcomings of earlier policies in El Salvador, the real test of 'peace conditionality' is still to come. Obviously, the size of aid is important and a more substantial investment by the IFIs would be helpful to implementing the accords. Yet while the IFIs have made key pledges regarding funds, they are unlikely to devote a significant level of new resources to support the Guatemalan peace process. Thus, what may be most essential is continued IFI pressure to realign expenditures, tax sources, land ownership, and other distributional opportunities with the objectives of peace consolidation. The key here will be the IFI willingness, as Camdessus warned, to withhold funds unless socio-economic progress is made. Such an approach will, in the short- and medium-term, provide the right incentives and thereby help in addressing the root causes of conflict in that country.

4. Growth, Distribution, and the Causes of CHEs

Those who are concerned about preventing CHE's must also have a longer-term vision of what measures must be taken to address the root causes. Given our economic hypotheses (i) to (iv), we would suggest that any approach must: (i) restore sustainable growth; (ii) create policy consensus and reduce the political economy problems encountered when the economy hits crisis; (iii) ameliorate inequalities in assets and opportunities that are the underlying reasons for the political economy problems; and (iv) avoid the heavy hand of partisan external intervention. These are tall orders for any economy and society, particularly given the traditional view that targeting distribution will tend to diminish aggregate economic performance, a view which implies that our imperatives (i) and (iii) are themselves in conflict.

Fortunately, recent empirical and theoretical work has suggested that enhanced equity in fact can have a positive impact on growth, partly for the political economy reasons hinted at above (that is, that unequal prior distributions make it more difficult to arrive at a consensus about burden-sharing in the context of slowed growth). Alesina and Perotti (1993) and Persson and Tabellini (1994), for example, stress how a more equal distribution of physical assets and income yields a policy atmosphere more conducive to the protection of property rights and therefore innovation. Rodrik (1994) correlates growth with a more even distribution of land and more equal access to primary school. Birdsall and Sabot (1994) also emphasize how equity promotes a higher level of investment in basic education and hence human capital while Galor and Zeira (1993) set up a theoretical model in which uneven access to credit blocks the poor from acquiring the necessary capital to make full use of their talents.

Even the World Bank, in its widely publicized study, *The East Asian Miracle*, notes that equity was a source of political legitimacy for the high performing Asian economies (p. 158); that land reform in Taiwan likely advanced both land productivity and political stability (p. 161); that successful land reform in China, Japan, Korea, and Taiwan 'helped to lay the foundation for rapid, shared growth' (p. 169); that investment in widespread primary education laid the foundation for growth; and, finally, that the failure of the Philippines to share this success is attributed to the fact that 'Philippine policy making has historically been captive to vested interests that have shaped economic policy to protect and enhance their privileged position, often to the detriment of national well-being' (p. 169).

This range of findings suggests that there may be a happy complementarity of peace, equity, and growth.[40] The range of specific microeconomic

[40] A further complementarity is between physical, human, and *natural* capital (see Segura and Boyce 1994). As Nafziger (1996) notes, humanitarian emergencies frequently result in the

or institutional policies that could directly target improving equity is broad and, we believe, doable. These include agrarian reform (especially going beyond the simple granting of land to ex-combatants which is usually intended simply to quell dissent in the immediate wake of a CHE); the creation of employment guarantee programmes for the rural poor (oriented toward infrastructure projects so as to build physical capital complements to private investment); programmes of microlending and microenterprise development; the use of privatization revenues to generate or subsidize projects with direct positive impacts on the poor; and the encouragement of community-based organizations and development projects.[41] All are likely to have a positive impact on both growth and distribution.

The question, of course, is how to get domestic governments to engage in such a set of strategies. This runs into the classic focus of political economy: even if a policy is believed to be superior, it will only be taken up if some constituency can recognize their interests, agree on a particular implementation strategy, overcome the usual collective action problems, and confront traditional policy makers with a new approach. This is a tall order for the poor, who are usually scrambling to make ends meet in daily life and hence face problems in attaining a high level of internal organization.

This political economy problem is one of the reasons why a new IFI emphasis on equity improvement might be so helpful; in short, if external actors are to intervene, they should at least weigh in on the side of those least able to defend themselves in the contemporary domestic arrangements. Another helpful step would be continued political reform such that the poor, once they can consolidate their voice, can make sure that it will be heard. In Central America, as elsewhere, a central element of the structural adjustment programmes backed by the IFIs has been the 'modernization' of the state. In practice this has primarily meant efforts to trim the size of the state by privatizing state-owned enterprises and eliminating certain agencies and functions, coupled with attempts to increase the efficiency of what remains. But while efficiency improvements may create the economic 'space' to address equity, only *democratization*—both in the broad sense of promoting a more equitable distribution of power and in the narrower sense of strengthening democratic institutions such as free elections, the protection of human rights, and the administration of justice—can create the political space to insure that equity will remain a top

destruction of the natural environment, a pattern that was certainly characteristic of El Salvador (see Acevedo, Barry and Rosa 1995). Truly sustainable development requires a reversal of this damage and a new attention to internalizing the externalities that result in excessive soil depletion and other growth-limiting practices.

[41] For other ideas on social policy in the wake of conflict and economic disruption in Latin America, see Thorp (1995).

concern. And such democratization of policy and politics is the key to *preventing* CHEs.

While some have argued for 'technocratic insulation', defined in *The East Asian Miracle* as the ability to formulate and implement policy 'with a minimum of lobbying for special favours from politicians and interest groups' (World Bank 1993: 167)—recent studies have suggested that democratic structures are actually consistent with improvements in private investment and economic performance, partly because they enhance political stability and help guarantee that technocrats in fact pursue the public interest (see Pastor and Hilt 1993; Pastor and Sung 1995). In Central America, democratic accountability is critical, particularly since successful economic policy will require the interventions outlined above and citizen access and oversight will be necessary to reduce rent-seeking and other unproductive behaviour. Moreover, in the wake of a negotiated settlement to a civil war or other complex emergencies, the political essence of which is the creation of checks and balances on the exercise of power, technocratic insulation is not a real possibility.[42]

This extended discussion of post-conflict policy as well as the fundamentals of appropriate development may seem tangential to a paper whose starting point is understanding the economic causes of complex emergencies. Yet ultimately our search for such causes is intended to serve a purpose: the prevention and/or resolution of the sort of emergencies that, by the very fact of their political and economic causation, are possible to avoid or address. In general, the United Nations has been asked to step in to provide emergency aid and/or help in peacefully ending civil conflicts. But bandages and diplomatic sutures do not heal wounds; the fundamental factors behind conflict-driven emergencies must be understood and confronted by all international and domestic actors—and then addressed in post-conflict economic policy.

The international community can and should do better. The first step is improving our analysis, a task to which this chapter seeks to contribute. But ultimately, the most critical factor will be the political will of the relevant actors. The chaos of CHEs is driven by rational interest-seeking in irrational and unequal political-economic structures. Attacking these fundamental features with external conditionality may appear to be an unwarranted intrusion into a realm traditionally reserved for domestic states. Yet if the United Nations and others are expected to pick up the pieces from 'man-made' disasters, surely other international actors (especially the IFIs) have a role, responsibility, and right to consider whether inequitable domestic arrangements are imposing broad costs not simply on the directly affected national populations but also on the international system which must finance the recovery.

[42] This is in contrast to the situation facing an occupation government installed by external powers after an international conflict, as in post-war Korea and Japan.

5. Conclusions

Complex humanitarian emergencies (CHEs) have complex economic and social causes. Each situation is necessarily unique, dependent on a particular array of class arrangements, élite defences, and/or environmental stresses. Yet analysts and policy makers must look for the general patterns on the causes side, if only to have a set of appropriate policies available on the remedy side.

In this search for causes, the emerging literature seems to have identified five common economic factors: slow or stopped growth, particularly in the context of rising expectations; difficulties in apportioning burden-sharing; underlying inequities that are fundamentally responsible for the burden-sharing challenge and often for the CHE itself; external actors who negatively complicate the scenario; and the cumulative and mutually-reinforcing effects of a downward spiral of social conflict and economic downturn. All of these factors were present in Central America in the 1980s and played a key role in triggering and sustaining the conflicts.

In El Salvador, the particular focus of this chapter, the slowdown of the late 1970s hit against a crest of rising expectations. Underlying inequalities, particularly in the distribution of land, made lower classes less than eager to share the bitter fruit of a slowdown. Frustrations boiled over into a military coup, guerrilla activity, and eventually a full-fledged civil war. The flames of conflict were fuelled by an external superpower, the US, willing to accept accelerated conflict and a rising death toll in order to prevent the extension of influence by a rival superpower. And as the conflict continued, both distribution and growth suffered mightily.

If slow growth, poor distribution, and negative intervention come together to force a downward spiral, it seems appropriate that inducing growth, ameliorating inequality, and encouraging positive external pressures would be part of a package to resolve such emergencies. However, a negotiated conclusion to a civil war inevitably poses the short-run problems of securing the financial and political preconditions for implementation of the peace accords; a similar set of dilemmas would seem to be present in many other sort of CHEs as well. Countries must therefore weigh the need to achieve macroeconomic balance against the desire to fund sufficiently post-conflict social programmes. Priorities need to shift in order to make budget room for post-conflict initiatives and to diminish the fiscal, and hence political, influence of the military; we call this 'peace conditionality' and suggest that IFIs could help in this process. In El Salvador, there was some movement in this direction but less has been done than would be optimal. The unfolding peace process in Guatemala offers an opportunity to build on the Salvadoran experience, opening the space for proactive policies which will avoid conflicts in the future.

Over the long run, the consolidation of peace in countries emerging from civil war—*and* the prevention of future complex emergencies in most developing country contexts—often hinges on both reactivating economic growth and forging a more equitable distribution of wealth and power. Both peace and growth can benefit from an improved balance in the distribution of income and wealth; enhanced investment in human, natural, and physical capital; and increased democratization to achieve balance in the distribution of power. We can, in short, reduce the likelihood of having to exert post-CHE 'peace conditionality' if IFIs and other international actors earlier in the process were able to exert 'equity conditionality'.

Such broad claims to reorient the development process may seem ambitious for a project whose focus is the causes and dynamics of complex humanitarian emergencies. But our ongoing discovery of the causes of such CHEs cannot be relegated merely to the task of improving prediction of the timing of CHEs. Of course, such an 'early warning' system would be helpful, partly since it would allow the relevant UN institutions to more quickly rush aid to affected parties. Yet the agenda could and should go far beyond this monitoring function: once we know that certain development styles tend to fall into CHE-type crises, it would be useful to rethink the tasks of the IFIs and other external assistance actors in the development process.

This is an ambitious challenge, but it is one which must be faced. In El Salvador and elsewhere, lives have been lost and dreams have been shattered; roughly 10 per cent of the population has been forced to abandon the country of their birth and personal and family ambitions have been sacrificed. While economists have been able to estimate the monetary costs of destroyed infrastructure, halted investment, and foregone growth, these human costs are painfully difficult to quantify. If the problematic tasks of quantifying such human costs and categorizing case-specific causes can be bypassed through a concerted effort to prevent complex humanitarian emergencies in the first place, this would be real progress.

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