

# Another Misadventure of Economists in the Tropics? Social Diversity, Cohesion, and Economic Development

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## Abstract

*Several prominent economists have recently argued that ethnic and other forms of social diversity lead to economic failure. Apparently, serious social frictions caused by diverse preferences do not create conditions for the development of endogenous institutions that enhance good economic policies. Others, however, have shown that diversity reduces transaction costs within and between groups absent good public institutions, because of within-group social capital and ingroup policing in repeated dealings across groups. High diversity also reduces mass mobilization and forces consensus: ethnic diversity acts as a barrier against the concentration of absolute power. Using several measures of ethnic diversity, this study demonstrates that diversity and cultural difference reduce serious social frictions measured as the repression of political dissent. This study also finds that higher social diversity directly predicts higher levels of economic freedom, a proxy often used to gauge the market-friendliness of a country, the endogenous conditions often associated with economic success. The same results are true when a measure of the control of corruption is used. The results show that diversity enhances, not retards, the prospects for development and reduces social frictions. It may very well be that discourses of conflict, particularly the discourses of blame and recrimination based on ethnic ties where economic failure is apparent, is mistaken as the cause rather than the byproduct of crises, mistakenly attributed to historical conditions that have generated artificial borders. Empirically, diversity seems to foster, not displace, the preconditions for development.*

**Key words:** social diversity, development, human rights, economic freedom

## Introduction

The founding father of Singapore, Lee Kuan Yew, used the mantra ‘economic development requires discipline,’ which is apparently harder under conditions of ethnic and cultural fragmentation (Sen 1999).<sup>1</sup> Such thinking pervades arguments

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about the 'Asian way' to economic success that views democratic rights as an unnecessary hindrance, where the demands of diverse societal groups (ethnic groups) often threaten to derail development (Colletta, Lim & Kelles-Viitanen, 2001; Sen, 1999). Others, such as Amartya Sen, view suppression of societal demands by states as a convenient ruse used by the ruling elites to hold on to power (Collier, 2001; Sen, 1999). However, according to recent scholarship by some highly celebrated economists, economic progress, amply demonstrated by Singapore, does require discipline, particularly peace and harmony and internal agreement between social groups about basic policies that lead to broad-based development (Alesina et al., 2006; Easterly et al., 2006). William Easterly, in several celebrated books, has argued that social diversity prevents the social cohesion necessary to emerge that endogenously determines good policies. Accordingly, aid generally fails to produce results because social heterogeneity is bad ground to sow aid. Apparently, the more congruent territorial borders are with nationality, the better the chances for endogenous development (Easterly, 2006b). These arguments assume that much of the frictions and instabilities in developing countries has a basis in ethnic and social diversity, even if many suggest that diversity per se might have very little to do with civil and political violence (Collier, 2001; de Soysa, 2009; Fearon & Laitin, 2003; Mueller, 2000; Ward et al., 2010). In fact, the pessimistic view on social diversity has justified the creation of relatively homogenous states as a policy prescription, which might in fact be counterproductive to progress, if indeed diversity prevents unnecessary social instability. This study examines empirically the effect of ethnic fragmentation on serious social frictions proxied by state repression of human rights, a form of one-sided violence because ethnic fractionalization and other measures of ethnic configuration and discrimination add little to the prediction of civil war. Data on political repression is a better measure of serious social frictions because it captures the level of dissent against political rulers (Poe, 2004). Moreover, since the argument about social fractionalization and development failure works though the inability of these states to produce and maintain good (market-friendly) economic policies, I test this proposition directly by examining how fractionalization relates to an index of economic freedom, an index endorsed by William Easterly as a good approximation of capitalistic policies that lead to endogenous development (Easterly, 2006a).<sup>2</sup> Understanding political violence that journalists and casual observers brand as 'ethnic' (due to meta narratives generated

by violence itself) requires careful disaggregated study (Brubaker & Laitin, 1998; Kalyvas, 2003).

The claim that social diversity matters for socio-political and economic failure is drastic, and it presents normative and practical implications for billions of people around the world: All countries are generally ethnically fractionalized, so breaking them up into natural borders might be a solution because capital flows (such as aid, trade, and other market-based inducements) are doomed to failure where there is high ethnic diversity. Conditions that breed conflict because of high social diversity, thus, provide barren ground on which to sow development from outside. As Easterly and others argue, ‘good’ market institutions appear endogenously in the absence of social frictions generated by diversity. Are such policy prescriptions premature, though, particularly since many argue exactly the opposite? High social diversity could make countries safer (Collier, 2001; de Soysa, 2009; Fearon & Laitin, 2003; Laitin, 2008; Sen, 2006). As they see it, diversity is a source of good because, as New Institutional Economics (NIE) suggests, ethnic and other cultural ties can reduce transaction costs between groups and allow easier in-group policing; high diversity may prevent mass nationalist mobilization by large majorities; and diversity creates cross-cutting cleavages that necessitate social cooperation rather than promote conflict where cleavages become segmented or polarized (North Korea is ethnically homogenous). Diversity may force ethnic coalition building and create cross-cutting cleavages that force institutional arrangements for elite accommodation that is better for economy and society in the long run, such as the many consociational arrangements seen in such places as The Netherlands and Belgium (Collier, 2001; Lijphart, 1999; Posner, 2004a). In fact, relative homogeneity might be more problematic than diversity when it comes to serious conflict (Collier & Hoeffler, 2004; de Soysa, 2009; Esteban & Ray, 2008; Horowitz, 2000; Welch, 1998). This study evaluates these competing claims by assessing whether or not ethnic and cultural fractionalization directly predicts the level of social friction within a country, measured as the level of political repression, and whether it hampers the making of ‘good’ economic policy using William Easterly’s own measure of good economic policies. Since those who argue that diversity is problematic argue precisely that diversity hampers ‘capitalistic’ and open economic policies (by generating ethnic nepotism and state capture by the few, bloated inefficient states, and perverse taxation and public goods policies), I test the effect of diversity on an index of economic freedom, which should capture the extent of these market-

unfriendly policies (Gwartney & Lawson, 2005) and on an index of political corruption designed to capture patronage and ethnic nepotism (International Country Risk Guide, 2006).

### **Why social fractionalization?**

The issue of whether or not multiple national identities are a good or bad thing for national development is an old one. John Stuart Mill argued that for democracy to be stable, a country had to be homogenous, a theme that pervades the work of many current theorists of democracy (Dahl, 1982; Rabushka & Shepsle, 1972). Mill (1873) wrote that ‘it is in general a necessary condition of free institutions that the boundaries of governments must coincide in the main with those of nationality’ (quoted in Connor, 2004: 25). Recently, several economists have joined the chorus. Africa’s ‘growth tragedy’ may be attributable to high social fractionalization, which stymies development due to distributional conflicts, coordination failure, lack of property rights and economic liberty, and the problems associated with taxation and public goods provision (Alesina et al., 1999; Alesina et al., 2006; Alesina & Rodrik, 1994; Easterly & Levine, 1997; Kimenyi, 1997). Ethnic fractionalization is a major aspect of social dislocation. Easterly et al. (2006: 105) succinctly elucidate the connection between fractionalization and low social cohesion:

*Socially cohesive societies ... have fewer potential/or actual leverage points for groups, individuals, or events to expose and exacerbate social fault lines. ...*

Lord Acton, touted as perhaps the most learned politician of his time, asserted the opposite. He criticized the Millian view on social fractionalization. Contrasting liberal Britain with the Poland of his time, he asserted that the advance of ‘liberty’ was due to the presence of diverse opinion: ‘power corrupts and absolute power corrupts absolutely.’ Acton saw minorities playing a crucial role in the advance of liberty. These historical visions of how ethnicity matters for political outcomes infuse current discussions. I focus on ‘ethnic conflict’ as an outcome, because conflict is consequential, carrying implications for all other arenas of life, what the economists that find diversity to be problematic call social frictions.<sup>3</sup> There is no theory of ethnic conflict, but ethnicity is used as an analytical concept to understand violence, democratic and economic failure, and a host of other ills.<sup>4</sup> Not all violent conflicts have an ethnic dimension, but it is true

that in some conflicts, it is ethnically distinct groups that fight. Does the fact that an armed opponent of a state is ethnically distinct mean that something about identity itself matters beyond the fact that it helps organization? Or is ethnicity simply a convenient vehicle for the organization of narrow objectives? But why is this identity alone more salient? Moreover, ethnic groups may fight more often in less fractionalized societies.

For primordialists (essentialists), groups will necessarily clash since all other affiliations and considerations are subsumed by the ethnic tie. It is not easy for groups to go in and out of other identities, particularly when differences between people are stark (such as skin color). There are diminishing returns to ethnicity—there is so much you can do to change. Thus, the more ethnic difference that exists within encompassing state boundaries, the more likely that conflict will erupt, since groupness matters above all, and ‘give and take’ is less likely. For instrumentalists (constructivists), ethnic entrepreneurs are crucial. Conflict erupts only in particular times and places because identity is instrumentalized for narrower aims—the salience of identity forms around achieving particular objectives—thus ‘give and take’ should be more likely and there may be other constraints that would prevent open conflict. In fact, since violence can be costly to these entrepreneurs (usually elites), ethnic elites have an incentive to ‘police’ their groups, preventing violence (Fearon & Laitin, 1996). In fact, conflict does not occur because of primordial hatreds but because someone organizes it; and just as for ordinary rebellion, it might be the feasibility of organizing conflict that matters, not the fact that ethnic diversity exists.

In several recent articles and books, economists have devoted much energy towards understanding why economic policies and the delivery of aid have failed. According to many, it is endogenous institutions that ensure good economic and political governance. Most developing countries lack the preconditions for the emergence of good governance, largely because these countries have artificial borders where ethnic and cultural diversity act as hindrances to sound political and economic governance due to the many social frictions that arise from diversity. As Easterly (2006: 113) writes:

*In many ethnically divided countries today, politicians often exploit ethnic animosities to build a coalition that seeks to redistribute income to us from them.*

Thus, social frictions arise from simple ethnic discrimination and the real and perceived exploitation of minorities, regardless of the type of government in place. Easterly goes on to write (2006: 113):

*Different ethnic groups may have conflicting interests in public services: group A may want a road in their region when group B may want a road in their region; the more segregated ethnic groups are, the less likely group B voters are to use or care about the road in group A's region. This may cause voters to choose a lower level of public services overall.*

Political corruption is also pointed out as another affliction of ethnic diversity. According to Easterly (2006: 114), 'corrupt politics merge with ethnic politics as parties compete to win resources for their own ethnic groups.' High diversity also apparently inhibits trust, and low-trust societies supposedly suffer corrupt government due to collective action problems (Putnam, 1993).

The empirical evidence for ethnic diversity's effect on social and economic outcomes is not straightforward. On the one hand, there are issues about the proper measurement of diversity, where indicators measured according to varying definitions can yield different results (Alesina et al., 2003; Fearon, 2003). Nevertheless, most indicators are highly correlated with each other. On the other hand, what seems to be an obvious correlation—ethnic and cultural diversity and serious social frictions including the lack of democracy—is non-existent at best, but also often points in the opposite direction; that is, diversity predicts less political friction (Collier, 2001; de Soysa, 2009; Esteban & Ray, 2008). It could very well be that ethnicized political discourses under conditions of economic adversity are mistaken to be the cause, rather than a consequence. Moreover, it may not be diversity that matters but that relative homogeneity leads to polarization and ethnic nepotism, where large groups compete for position because of the fear of being permanently marginalized. If this is the case, then the greater the diversity, the better it might be for governance.

Instead of political conflict, some scholars find that cooperation between ethnic groups is much more common in reality (Fearon & Laitin, 1996; Sen, 2006). Paul Collier (1999a, 1999b) argues various ways in which higher diversity matters for making countries safer and enhances prospects for development. Even if high diversity, particularly under conditions of dictatorship, will likely reduce the level of public goods, ethnic ties will allow lower transaction costs in the absence of good institutions. Indeed, some find that ethnic elites tend to tax their own ethnic populations more because collection costs are lower than for taxing across groups

(Kasara, 2007). Such high taxes are likely to distort markets. In high diversity environments, there might be trade-offs between high government taxes and low public goods provision, but ethnic ties are likely to generate the social capital necessary for lowering transaction costs for economic activity related to investment and trade, and for generating networks of relationships that compensate for the lack of formal institutions governing markets. From a broader perspective, high diversity can create cross-cutting cleavages that moderate, rather than radicalize ethnic politics (Lijphart, 1977). Suppose that the median voter is likely in a poor country to lie across every ethnic group and suppose that voters are split between voting for an ethnic party or a party that favors redistribution. Such a configuration of voters will be much less likely to vote for redistribution than one with a homogenous society. North Koreans might in fact remain poor because they do not have rebellious minorities—as Lord Acton’s famous quote implies, ‘power corrupts, absolute power corrupts absolutely.’ Thus, higher ethnic and cultural diversity might be stabilizing, not the source of serious social frictions. I put this basic debate to the empirical test by assessing the effects of social diversity on political repression, the level of economic freedom (extent of market-friendly policies), and the level of political corruption.

## Methods & Data

This study uses regression analysis to test multivariate models predicting repression of human rights, the level of economic freedom, and the level of political corruption. I examine the most odious aspects of state repression, which are violations of physical integrity rights (CIRI) and the extent of political terror (PTS) (Cingranelli & Richards, 1999; Gibney & Dalton, 1996).<sup>5</sup> These are negative rights in that they capture arbitrary physical harm and state coercion with threat of harm against ordinary people. While the sources for the two datasets on repression are the same, mainly Amnesty International and US State Department Reports, the correlation is not perfect due to different definitional issues and thresholds. The correlation between the PTS scale and the CIRI human rights measure is  $r=-0.83$  (CIRI measures rights and the PTS measures repression, hence the negative relationship). Generally, there is high congruence among differently defined scales of repression (Landman, 2005). I follow the conservative strategy of using both measures.

Repression of physical integrity rights (CIRI) is coded on the basis of the following four criteria: extrajudicial killings or unlawful and arbitrary deprivation of life; disappearances; torture or inhumane and degrading treatment; and political imprisonment because of political activism and nonviolent opposition to government. These variables are coded on a scale of 0–2: 0 if 50 or more reported violations have occurred; 1 means that 1–49 reports occurred; and 2 means zero reports of violations. This information is then scaled using Mokken Scaling Analysis (MSA), which scales according to the frequencies and the severity of observed violations of human rights. Thus, the final physical integrity rights measure is an additive scale of the 4 repression categories named above stretching from 0 (no respect on any of the categories) to 8 (full respect for each of the categories). Some violations and partial violations show up on each of the 4 dimensions in between 1 and 7.

The PTS rates the yearly performance of countries on an interval scale of five categories:

1. if countries are under secure rule of law, political imprisonment and torture are rare, and the political murders are extremely rare;
2. if imprisonment for non-violent political activities is limited, torture and beatings are exceptional, and political murder rare;
3. if political imprisonment is extensive, execution and political murder may be common, and detention for political views is acceptable;
4. if the practices of level 3 are expanded to a larger segment of population, murders and disappearances are common, but terror affects primarily those who interest themselves in political practices and ideas; and
5. if levels of terror are population wide, and decision makers do not limit themselves in how they pursue private and ideological goals.

Ethnic fractionalization variables are the main variables of interest. They are categorized as the group size indicators (fragmentation), which are used in tests of the political economy models of political and economic failure (Alesina et al., 1999; Easterly et al., 2006). The issue of what an ethnolinguistic group is thorny, thus, I use several measures of fractionalization developed by at least two different sources, mainly Fearon (2003) and Alesina et al. (2003). I have already touched on

objections to the standard fractionalization measures based on the conflation of structure and ethnic practice in the identification of groups. Unlike others that have tried to identify ‘salient’ ethnic groups (Chandra & Wilkinson, 2008; Posner, 2004b), this study is interested in the total number of groups, or a measure that gets as close as possible to measuring the arithmetic structure of the ethnic and linguistic social map, self-identified or not. All three fractionalization measures have made different coding rules to identify and classify groups; this study will not judge who has it right but will follow the conservative strategy of testing all of them (Fearon 2003).<sup>6</sup> The ethnic fractionalization measures of Alesina and Fearon are correlated at  $r=0.74$ . The highest correlation is between Fearon’s ethnic fractionalization and Alesina’s linguistic fractionalization measure ( $r=0.88$ ). Moreover, since one of the main arguments of the pessimists on ethnic diversity is that cultural and other preferences prevent coordination and lead to diverse preferences on public goods issues, I use Fearon’s (2003) measure of cultural distance that measures the distance of the majority language from the largest minority’s language on a linguistic tree. Here, language acts as a proxy for the cultural distance between a majority and the largest minority within a country.

These main diversity measures are then tested on two other dependent variables. First, I test the direct effect of social diversity on the level of economic freedom, an indicator often used to measure the level of an economy’s market-friendliness (Gwartney & Lawson, 2005). Previous studies have used this measure to test the effects of neoliberal policies on growth (de Haan & Sturm, 2009); the effects of IMF conditionality on policy change (Boockmann & Dreher, 2003; Dreher & Rupprecht, 2007); and the effects of economic freedom on corruption (Graeff & Mehlkopf, 2003), on democracy (Feng, 2003), and on subjective wellbeing and happiness (Veenhoven, 2000). The Fraser Institute defines economic freedom as:

The central elements of economic freedom are personal choice, freedom of exchange, and protection of private property. When economic freedom is present, individuals are free to make economic choices such as how to use their time and other resources, what goods to consume, and what business and investment alternatives to pursue. Of course, they will often find it advantageous to cooperate with others and markets will coordinate their choices and bring them into harmony. ... Other things constant, freer economies will rely more on markets and less on government to answer these basic economic questions (Gwartney & Lawson, 1997).

The Economic Freedom of the World Index (EFI) incorporates 38 components designed to capture the degree to which government policy and institutions facilitate voluntary exchange, protect property rights, enforce contracts, support open markets, and minimize government entry into labor, capital and product markets (Gwartney & Lawson, 2005).<sup>7</sup> These various aspects are, in turn, aggregated into one single index that ranges from 1 to 10. Higher numbers indicate more economic freedom. The index is available for over 125 countries and reported in five-year intervals from 1970 until 2000, after which annual values are reported. The years in between the quintiles are linearly interpolated from 1970 until 2000, which allows us to estimate diversity's effects on economic freedom annually from 1970 to 2007. I use simple OLS regression analysis on a pooled dataset (TSCS data). The control variables and some issues with the testing method are discussed below.

Second, the measures of social diversity are tested on an indicator of the 'control of corruption' taken from a leading agency that provides risk services to companies investing abroad, the International Country Risk Guide developed by the PRS group (International Country Risk Guide, 2006). This indicator is ideal for measuring what William Easterly and others mention in terms of how ethnically divided countries suffer underdevelopment. The PRS takes such aspects as nepotism, ethnic favoritism, rent-seeking, patronage, and the potential that such corruption might destabilize the country through the threat of violence (see full definition on [www.prsgroup.com](http://www.prsgroup.com) and in the appendix). This measure is a continuous variable stretching from 1 to 6 and is available as an annual time series from 1984 to 2006.

### **Control variables**

I use similar control variables in all tests, but these controls are theoretically derived and used extensively in other empirical studies. Previous studies find several factors that influence the likelihood of repression. Democracy is an important predictor of respect for human rights (Davenport & Armstrong, 2004; Landman, 2005) as it is a predictor of economic freedom as well as the level of corruption (Lundström, 2002). The existence of organized, legal, political oppositions, a free press, and a civil society are constraints on leaders who may be tempted to violate citizens' rights, or be corrupt. Established democracies contain

norms of non-violent means of conflict resolution, such as protests, strikes, and other civil actions to make demands on government. Authorities responding to demands are constrained by laws of due process and political oversight. Davenport and Armstrong (2005) find, however, that democracy's effect is negative and most significant when the democracy score is relatively high. Following others (Fearon & Laitin, 2003), regime type is coded as a dummy variable taking the value 1 if the Polity IV (variable polity2) score is above 6 on the 11 point scale and 0 if below that.

The existence of violent armed conflict often leads to the curtailment of human rights, raising corruption and thwarting market-friendly policies. The empirical evidence on whether international war leads to human rights repression is mixed (Landman, 2005; Richards et al., 2001). I include only civil war and the time since the last conflict. In addition to entering a dummy variable denoting the existence of civil war, I enter a term for the legacy of conflict measured as the years of peace since the last conflict. Using the Uppsala/PRIO dataset that includes all conflicts with at least 25 battle-related deaths (Gleditsch et al., 2002), I compute the number of years of peace since the last conflict for both international and civil war variables.<sup>8</sup>

Economic conditions can affect the likelihood of repression. Poe et al. (1999: 294) state that 'in countries with economies characterized by scarcity, regimes will be more likely to repress domestic threats.' Henderson (1997) argues that in more developed states the population will be more content, and thus less repression is needed to keep control. Richer states also have higher state capacity (Fearon & Laitin, 2003). Moreover, richer people may have high opportunity costs for engaging in dangerous (violent) dissent (Collier & Hoeffler, 2004). I use Gross National Income per capita (GNI) in PPP terms (logged) (World Bank, 2010). Income level is also a catch-all variable that accounts for the level of social and government sophistication in terms of better policies and lower corruption. I also use the growth rate of income per capita, which proved not to be statistically significant, so it is left out for brevity.

Many find that countries that export natural resources, for a given level of per capita income, tend to have higher levels of political repression in line with theories of the 'resource curse' (de Soysa & Binningsbø, 2009; Ross, 2001). In fact, several find that natural resource wealth is a problem for governance and peace (Auty, 2001; de Soysa, 2002; Fearon & Laitin, 2003). Resource wealth raises the stakes for state capture and lowers the incentive of rulers to reform

(Acemoglu & Robinson, 2006; Jensen & Wantchekon, 2004). Indeed, the resource curse is also associated with bad economic policies and higher corruption (Leite & Weidmann, 1999). I enter a dummy variable that takes the value 1 if oil exports are greater than 1/3 of total export revenues and 0 if not. This variable is taken from Fearon and Laitin (2003) updated using the fuel exports per GDP contained in the World Development Indicators (World Bank, 2010).<sup>9</sup>

Several studies report that larger populations tend to be more problematic for peace and security than smaller states (Fearon & Laitin, 2003; Landman, 2005; Poe, 2004). For this study, population size is a particularly salient control since ethnic fractionalization is intimately connected with the size of a country (Alesina & Wacziarg, 1998). It should also be noted that the physical integrity rights can be affected by the size of the population because larger populations will most likely have very high frequencies of violations simply because of the numbers of people (scale effects). These data are also from the World Bank (World Bank, 2010).

Finally, I control for time trends in the data. Human rights data maybe affected over time in several ways, such as the definition of a human rights violation. Moreover, the apparatus for detecting violations have increased over time, such as the activities of Amnesty International and the US State Department, whose activities have surely increased over time. I enter year dummies to capture such potential time trends in the data. Time dummies also take care of any unobserved factors, such as the end of the Cold War, or global policy shifts that may affect human rights on a macro scale. I could also have controlled for how committed a country is to the norms of human rights respect by adding a variable measuring whether countries participate in human rights conventions, but the existing evidence suggests that this variable does not matter (Keith, 1999; Neumayer, 2005), neither do the legal traditions of countries. An examination of all of the variables did not show correlations that would lead us to be concerned about multicollinearity.

I estimate the primary dependent variable, the CIRI scale using linear regression models (OLS). This scale is an ordinal scale ranging from 0 to 8, and the ideal estimation process should be either ordered logit or ordered probit, depending on the nature of the distribution of the dependent variable (Long, 1997). Estimating a linear model if the thresholds are the same distance apart within the scale would not be such a problem, but given that the substantive nature of the cut-off points are hard to ascertain in the CIRI scale, I estimate linear models as most others do (de Soysa & Nordås, 2007; Landman, 2005; Poe et al., 1999). The closer

the scale approaches a normal distribution, the less biased is the linear estimator (Long, 1997; Winship & Mare, 1984). On preliminary examination, the CIRI looks relatively normally distributed. When using the five-point PTS scale, which is more clearly defined, I use ordered probit when estimating the PTS since the identification of cut-off points is relatively straightforward.

Ideally, the data should have been estimated in fixed effects models so as to assess the within-country variance associated with diversity and repression and other outcomes. However, it is not possible to run fixed effects models when the main variables of interest are time invariant. Thus, I run random effects models on TSCS data. The data are pooled across space and over time. Time-series, cross-section data (TSCS) may contain complicated correlation patterns within and across the panels because of the spatial and temporal nature of the data setup. I rely on the ‘panel corrected standard error’ method (PCSE) proposed by Neal Beck and Jonathan Katz (1995), which provides more accurate and apparently more conservative estimates of significance levels. PCSE also allows one to correct for autocorrelation with an AR1 process (Beck & Katz, 1995). Yet another estimating technique is the Newey-West method, which allows one to account for autocorrelation and obtain Huber-White corrected robust standard errors, which are robust to heteroskedasticity (Newey & West, 1987). With the ordered probit models, I obtain robust standard errors clustered on country, a method which is robust to heteroskedasticity and serial correlation even if there might be loss of efficiency (Wiggins, 1999). The summary statistics of each of the variables are described below (see appendix). The estimates of political repression are based on data for roughly 146 countries with over 1 million inhabitants covering the period 1980–2006 while the estimates for economic freedom and corruption are roughly for 125 countries for which data are available. The dataset is unbalanced, and the availability of data for all of the controls determined the size of the total dataset.<sup>10</sup> See appendix for country list.

## Results

I first test the effects of social diversity on the physical integrity rights index (CIRI). The results are presented in Table I.

**Table I. Estimates of the effect of Fearon's and Alesina's measures of ethnic and cultural fractionalization on physical integrity rights, 1981–2006**

	(1)PCSE	(2)Newey	(3)Newey	(4)Newey	(5)Newey	(6)Newey
	PHYSINT	PHYSINT	PHYSINT	PHYSINT	PHYSINT	PHYSINT
Eth. Fraction	0.906	0.923				
FEARON	(0.180)***	(0.146)***				
Income per cap.	0.420	0.401	0.342	0.394	0.338	0.354
Logged	(0.032)***	(0.028)***	(0.029)***	(0.028)***	(0.027)***	(0.027)***
Population size	-0.461	-0.425	-0.426	-0.429	-0.425	-0.419
Logged	(0.027)***	(0.022)***	(0.023)***	(0.022)***	(0.023)***	(0.023)***
Democracy dummy	0.842	0.954	0.941	0.993	0.960	0.976
	(0.105)***	(0.078)***	(0.080)***	(0.079)***	(0.079)***	(0.081)***
Oil exporter	-0.782	-0.749	-0.734	-0.729	-0.688	-0.767
	(0.101)***	(0.103)***	(0.105)***	(0.101)***	(0.102)***	(0.105)***
Civil War	-1.602	-2.180	-2.162	-2.186	-2.122	-2.179
	(0.106)***	(0.110)***	(0.110)***	(0.114)***	(0.110)***	(0.111)***
Years of peace	0.021	0.016	0.014	0.015	0.014	0.015
	(0.003)***	(0.002)***	(0.002)***	(0.002)***	(0.002)***	(0.002)***
Observation Year	-0.032					
	(0.009)***					
Eth. Fraction			0.095			
ALESINA			(0.162)			
Ling. Fraction.				0.856		
ALESINA				(0.141)***		
Rel. fraction.					0.499	
ALESINA					(0.142)***	
Cultural dist.						0.838
FEARON						(0.181)***
Constant	71.805	7.557	8.409	7.691	8.227	7.942
	(17.119)***	(0.433)***	(0.465)***	(0.423)***	(0.429)***	(0.435)***
Observations	3,316	3,316	3,292	3,217	3,293	3,242
Countries	146	146	144	141	144	142

standard errors in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%  
year dummies computed in all tests (not shown)

In Table I, column 1, using the OLS regression with panel-corrected standard errors (PCSE), Fearon's measure of ethnic diversity is positively correlated with higher physical integrity rights, a result that is statistically highly significant. Substantively, a unit increase in ethnic diversity can increase the level of physical

integrity rights by roughly 26%, which amounts to 11% of a standard deviation of the CIRI rights measure (see appendix for summary stats). This result also holds for a sample of only non-Western countries (results not shown). In column 2, the results hold also when using the Newey-West method. The control variables all confirm results reported by previous studies. Per capita income is associated with higher respect for physical integrity rights by governments, while country size reduces them. Democracy is associated with higher respect for rights, whereas oil exporters display lower levels of rights as argued by theorists of the natural-resource curse. Civil war incidence naturally lowers rights, while countries with longer periods of civil peace show higher levels of rights, results that are all reasonable.

In column 3, Alesina's ethnic fractionalization index is also positively correlated with respect for rights but is statistically indistinguishable from zero. In column 4, however, linguistic fractionalization, which is most strongly correlated with Fearon's ethnic fractionalization, is positively and significantly associated with respect for rights, a result that does not support his arguments about the social frictions associated with coordination failure and diverse preferences from cultural differences. In fact, an Alesina's linguistic fractionalization has the same substantive impact on rights as Fearon's ethnic fractionalization result (a standard deviation increase in linguistic fractionalization will increase rights by 11% of a standard deviation of rights). This result may seem trivial, but it's a whole lot more than what Alesina and co-authors' theories about the dangers of social fractionalization lead us to believe. In column 5, Alesina's religious fractionalization measure is also strongly correlated with higher respect for rights. Finally, in column 6, I enter Fearon's measure of cultural distance indicated by the closeness of linguistic affinity between the majority language and the largest minority within a country. As seen there, even cultural distance has a positive effect on government respect for the physical integrity rights of citizens, an indirect proxy also for the level of social frictions and dissent within a country. These results uphold even when I add a lagged dependent variable, which is a very conservative estimate of the variance (results not shown). Social diversity seems to lower, not raise the level of serious political dissent and state repression.

In Table II, instead of the CIRI rights measure, I use the PTS repression scale.

**Table II. Estimates of the effect of Fearon's and Alesina's measures of ethnic and cultural fractionalization on Political Terror, 1980–2006**

	(1)Oprobit	(2)Oprobit	(3)Oprobit	(4)Oprobit	(5)Oprobit
	PTS	PTS	PTS	PTS	PTS
Eth. Fraction.	-0.686				
FEARON	(0.251)***				
Income per cap.	-0.340	-0.282	-0.340	-0.286	-0.306
Logged	(0.054)***	(0.052)***	(0.055)***	(0.049)***	(0.049)***
Population size	0.226	0.226	0.232	0.225	0.223
Logged	(0.039)***	(0.042)***	(0.041)***	(0.041)***	(0.040)***
Democracy dummy	-0.754	-0.736	-0.803	-0.743	-0.780
	(0.112)***	(0.118)***	(0.113)***	(0.118)***	(0.116)***
Oil exporter	0.514	0.478	0.503	0.471	0.533
	(0.144)***	(0.144)***	(0.142)***	(0.139)***	(0.144)***
Civil War	1.369	1.342	1.376	1.329	1.360
	(0.141)***	(0.141)***	(0.155)***	(0.139)***	(0.140)***
Years of peace	-0.015	-0.013	-0.014	-0.013	-0.014
	(0.004)***	(0.004)***	(0.004)***	(0.004)***	(0.004)***
Eth. Fraction.		0.021			
ALESINA		(0.267)			
Lin. Fraction.			-0.652		
ALESINA			(0.246)***		
Rel. fraction.				-0.150	
ALESINA				(0.254)	
Cultural dist.					-0.767
FEARON					(0.277)***
Observations	3,769	3,746	3,659	3,746	3,690
Countries	145	144	141	144	142

robust standard errors in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

year dummies computed in all tests (not shown)

As seen there, almost all of the results remain unchanged despite a different testing method (ordered probit). These results, too, remain unchanged when using a lagged dependent variable in the model, suggesting that the association between diversity and state repression is robustly negative. Assessing the substantive impact with ordered probit is a bit more complicated than with OLS. I use the cut-off point of 4 on the PTS, when rights repression is somewhat severe, for computing a predicted probability for the entire model at the mean values of all the variables. I then raise the ethnic fractionalization variable by a standard deviation above the mean and recalculate the predicted probability holding all the other variables at their means and assess the difference in the two predictions. The predicted probability of the model with all variables at the mean was reduced by 33% when ethnic fractionalization alone was raised by a standard deviation above the mean. For comparison, doing the same exercise with per capita income reduces the predicted probability by roughly double the amount that was the case with

fractionalization, which suggests that fractionalization's effect alone on reducing political terror is not trivial. These results support at least two other studies that have assessed the impact of ethnicity on political repression (Lee et al., 2004; Walker & Poe, 2002). Having established that social fractionalization, even as measured by Alesina et al. (2003), does not predict higher levels of social friction, I move on to assessing social diversity's effect on good economic policy, which some assume does not come about because of social disarray attributed to high diversity.

Table III reports the results of social diversity's effect on the index of economic freedom (EFI).

**Table III. Effects of ethnic fractionalization on market-friendly economic policies, 1970–2006**

	(1)Newey	(2)Newey	(3)Newey	(4)Newey	(5)Newey
	EFI	EFI	EFI	EFI	EFI
Eth. fraction	0.718				
FEARON	(0.060)***				
Income per cap	0.460	0.443	0.413	0.460	0.438
logged	(0.015)***	(0.016)***	(0.015)***	(0.016)***	(0.015)***
population	-0.015	-0.007	-0.011	-0.009	-0.001
logged	(0.012)	(0.013)	(0.012)	(0.012)	(0.012)
democracy	0.031	0.030	0.029	0.062	0.037
	(0.044)	(0.046)	(0.045)	(0.045)	(0.045)
Oil exporter	-0.480	-0.505	-0.417	-0.433	-0.510
	(0.051)***	(0.052)***	(0.051)***	(0.051)***	(0.051)***
Civil War	-0.200	-0.189	-0.155	-0.202	-0.204
	(0.057)***	(0.060)***	(0.060)***	(0.060)***	(0.058)***
Peace years	0.005	0.003	0.002	0.005	0.004
	(0.001)***	(0.001)**	(0.001)*	(0.001)***	(0.001)***
Eth. Fraction		0.414			
ALESINA		(0.071)***			
Rel. fraction.			0.400		
ALESINA			(0.069)***		
Lin. Fraction.				0.759	
ALESINA				(0.064)***	
Cult. Distance					0.871
FEARON					(0.087)***
Constant	3.004	3.173	3.459	2.850	2.997
	(0.226)***	(0.249)***	(0.224)***	(0.225)***	(0.224)***
Observations	3,443	3,439	3,439	3,355	3,380
Countries	127	126	126	124	125

standard errors in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%  
year dummies computed with all tests (not shown)

As seen there, Fearon's ethnic fractionalization measure (column 1) is positively and statistically highly significantly associated with the index of economic freedom. Diversity seems to be positive for 'good' market-friendly economic policies as recommended by William Easterly himself. A standard deviation increase in ethnic fractionalization can raise the index of economic freedom by roughly 20% of a standard deviation of the EFI. Moreover, in columns 2, 3, and 4, all of Alesina's fractionalization measures predict higher levels of economic freedom. These results are robust to estimation with the PCSE method as well as a sample of non-Western countries (results not shown). Once again, the results utterly disprove the view that high social diversity prevents good economic policy conditions, net of income per capita and a host of sundry controls. Contrarily, the results support those who are more optimistic about the value of social diversity for preventing rent-seeking and other maladies that might be associated with relative homogeneity.

Finally, Table IV reports results of the effects of social diversity on the extent of the control of political corruption.

**Table IV. Effects of alternative measures of social fractionalization on market-friendly policies, 1970–2006**

	(2)Newey Economic freedom	(3) Newey Economic freedom	(4) Newey Economic freedom
Eth.fraction.	0.419		
Alesina	(0.071)***		
Oil exporter	-0.484	-0.398	-0.403
	(0.053)***	(0.052)***	(0.052)***
GDP/pc log	0.437	0.409	0.454
	(0.015)***	(0.014)***	(0.015)***
Population log	-0.008	-0.012	-0.010
	(0.013)	(0.012)	(0.012)
Civil War t-1	-0.192	-0.159	-0.198
	(0.063)***	(0.064)**	(0.064)***
civil peace years	0.003	0.002	0.005
	(0.001)*	(0.001)	(0.001)***
Democracy t-1	0.006	0.005	0.009
	(0.003)*	(0.003)*	(0.003)***
Relig. fraction		0.402	
Alesina		(0.069)***	
Linguist. Fract.			0.764
Alesina			(0.063)***
Constant	3.216	3.498	2.905
	(0.249)***	(0.224)***	(0.224)***
Observations	3,438	3,438	3,354
#countries	126	126	125

As seen in Table IV, the control of corruption is higher where ethnic diversity as measured by Fearon is higher. The result is statistically highly significant. A standard deviation increase in diversity will raise the control of corruption by roughly 11% of a standard deviation of the control of corruption index. A similar increase in per capita income for comparison would raise the control of corruption by 50% of a standard deviation. This is quite a bit more, but given the focus on diversity's effect of corruption, even a small positive effect that is statistically very unlikely to have been obtained by chance must be seen as a massive blow to the pessimists. However, the statistical significance of these tests is greatly diminished when only a non-Western sample of countries is tested and when a lagged dependent variable is in the model. Nonetheless, at no time do I find a negative association between ethnic diversity and political rights, economic freedom, or the control of corruption. The results taken together show ample evidence to suggest that diversity makes countries safer for development, not more dangerous.

A battery of further tests was run by alternating the specifications of the models by dropping some variables and adding others. In particular, homogenizing religions, such as Christianity and Islam, might reduce diversity, but these religions may have their own impacts on political repression and economic governance. Adding neither the majority share of major religions, nor the major geographical regions of the world, had any significant impact on the measures of ethnic and other diversity. By and large, the results obtained here suggest that ethnic diversity enhances the prospects for development, which does not warrant the recent negative press that diversity has received, particularly among economists that tend to blame social diversity as the source of frictions that prevent endogenous factors driving good economic management. It might very well be that where there is discord, some mistakenly interpret the cacophony of ethnic representation as a normal outcome of diversity than of conflict in general.

## Conclusions

A spate of recent scholarly work in economics blames social diversity, particularly the potential conflict that such diversity portends, on the development failure of poor countries (Alesina et al., 2006; Alesina & La Ferrara, 2005; Easterly, 2006b). Apparently, high diversity prevents public goods provision because of issues related to diverse preferences around taxation and public goods provision. Diversity is also blamed for being at the root of high social frictions that

lead to bad governance and economic mismanagement due to the lack of social cohesion. Aid efforts, among other interventions to help the poor, are seen as wasteful because the endogenous conditions based on diversity as a result of 'artificial borders' thwarts correct policies that enhance markets rather than bureaucracies and corruption (Easterly, 2006b). Others have argued just the opposite, taking a more favorable view of diversity because high diversity can act as a check on absolute and permanent majorities that may lead to rent-seeking and political polarization. Ethnic ties may act as mechanisms for reducing transaction costs in the absence of good institutions, as new institutional economics and theories of social capital suggest. Moreover, cross-cutting cleavages may also reduce the propensity for large-scale ethnic polarization because of offsetting interests, which may stimulate better institutions for managing pluralistic interests in society, such as proportional representation and other consociational arrangements. The theoretical stories about the promise and perils of ethnic diversity are equally plausible and the empirical evidence still rather mixed.

While many have shown that ethnic diversity potentially reduces the chances of civil war, this study demonstrates that it also reduces serious social frictions short of large-scale conflict, namely political repression of individual rights. This study finds also that higher social diversity directly predicts higher levels of economic freedom, a proxy often used to gauge the market-friendliness of a country. Contrary to the pessimists, ethnic and other social diversity predicts better conditions for entrepreneurial capitalism, the endogenous conditions often associated with economic success. The same results are true when a measure of the control of corruption is used. The results show that diversity enhances, not retards, the prospects for development. It may very well be that discourses of conflict, particularly the discourses of blame and recrimination based in ethnic ties where economic failure is apparent, is mistaken as the cause rather than the byproduct of crises, mistakenly attributed to historical conditions that have generated artificial borders. However, knowing how 'social diversity' matters for the success of societies is key because policy makers have reacted to conflict and crisis by advocating ethnically pure states as an answer to failure, which may in fact be counterproductive if diversity, which makes countries safer, is mistakenly undone to sow the seeds of future failures. Further research is certainly sorely needed to pinpoint other ways in which diversity is problematic to help policy undo some of the misadventures of economists in the tropics.

## Appendix

### Summary stats

Variable	Obs	Mean	Std. Dev.	Min	Max
CIRI physint	3,896	4.93	2.35	0	8
PTS	5,276	2.38	1.16	1	5
EFI	3,772	5.93	1.12	2.3	8.78
ICRG	3,087	3.08	1.38	0	6.16
Ethfrac_Fearon	5,495	.41	.28	.001	.92
Alesina ethf	6,435	.46	.25	0	.93
Alesina linf	6,279	.40	.28203	.002	.923
Alesina relf	6,474	.42	.23	.002	.86
Cult. distance	5,889	.30	.20	0	.73
Ln gdppc	5,548	7.5	1.56	4.03	10.9
Ln population	6,328	15.52	1.89	9.88	20.9
Democracy	5,620	.35	.47	0	1
Oil exporter	6,158	.16	.37	0	1
Civil War	6,030	.16	.37	0	1
Peace years	6,030	18.95	16.91	0	61

### Country List

USA, Canada, Haiti, Dominican Rep., Jamaica, Trinidad & Tobago, Guatemala, Mexico, Honduras, El Salvador, Nicaragua, Costa Rica, Panama, Colombia, Venezuela, Ecuador, Peru, Brazil, Bolivia, Chile, Argentina, Uruguay, UK, Ireland, Netherlands, Belgium, France, Switzerland, Spain, Portugal, Germany, Poland, Austria, Hungary, Czech Rep., Slovakia, Italy, Albania, Croatia, Slovenia, Greece, Bulgaria, Romania, Estonia, Slovenia, Latvia, Lithuania, Ukraine, Belarus, Armenia, Georgia, Azerbaijan, Finland, Sweden, Norway, Denmark, Guinea-Bissau, Gambia, Mali, Senegal, Benin, Mauritania, Niger, Cote d'Ivoire, Guinea, Burkina Faso, Liberia, Sierra Leone, Ghana, Togo, Cameroon, Nigeria, Gabon, Central African Republic, Chad, Congo, Democratic Republic of the Congo, Uganda, Kenya, Tanzania, Burundi, Rwanda, Ethiopia, Eritrea, Angola, Mozambique, Zambia, Zimbabwe, Malawi, South Africa, Namibia, Lesotho, Botswana, Swaziland, Madagascar, Morocco, Algeria, Tunisia, Libya, Sudan, Iran, Turkey, Egypt, Syria, Lebanon, Jordan, Israel, Saudi Arabia, Kuwait, United Arab

Emirates, Oman, Tajikistan, Kyrgyzstan, Uzbekistan, Kazakhstan, China, Mongolia, South Korea, Japan, India, Pakistan, Bangladesh, Sri Lanka, Nepal, Thailand, Cambodia, Laos, Vietnam, Malaysia, Philippines, Indonesia, Australia, Papua New Guinea, New Zealand.

### **Definition of the ICRG's 'Control of Corruption' indicator**

This is an assessment of corruption within the political system. Such corruption is a threat to foreign investment for several reasons: it distorts the economic and financial environment; it reduces the efficiency of government and business by enabling people to assume positions of power through patronage rather than ability; and, last but not least, introduces an inherent instability into the political process.

The most common form of corruption met directly by business is financial corruption in the form of demands for special payments and bribes connected with import and export licenses, exchange controls, tax assessments, police protection, or loans. Such corruption can make it difficult to conduct business effectively, and in some cases may force the withdrawal or withholding of an investment.

Although our measure takes such corruption into account, it is more concerned with actual or potential corruption in the form of excessive patronage, nepotism, job reservations, 'favor-for-favors', secret party funding, and suspiciously close ties between politics and business. In our view these insidious sorts of corruption are potentially of much greater risk to foreign business in that they can lead to popular discontent, unrealistic and inefficient controls on the state economy, and encourage the development of the black market.

The greatest risk in such corruption is that at some time it will become so overweening, or some major scandal will be suddenly revealed, as to provoke a popular backlash, resulting in a fall or overthrow of the government, a major reorganizing or restructuring of the country's political institutions, or, at worst, a breakdown in law and order, rendering the country ungovernable.

## Notes

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<sup>1</sup> Although ethnic fragmentation alone does not determine the degree of social cohesion, it is viewed as the underlying source of ethnic friction at the root of development problems. See Alesina & La Ferrara (2005) for review.

<sup>2</sup> I use the Index of Economic Freedom, a widely used measure of capitalistic economic policies that correlates well with economic growth and social development. This measure is also endorsed by William Easterly in his own work (2006a: 29–35).

<sup>3</sup> The question of what ethnicity actually is and how to measure it is a thorny one (Chandra & Kanchan, 2006). I am forced to rely on those whose measures I use in the empirical analysis: Alesina, Alberto, Arnaud Devleeschauwer, William Easterly, Sergio Kurlat, and Romain Wacziarg (2003); and Fearon (2003). In general, Fearon (2003: 7) defines a ‘prototypical’ group as one that fits the following criteria: common decent, members are conscious of common ties, members share distinguishing cultural features, these features are valued by the membership, the group has or remembers a homeland, and the group has an identifiable ‘shared’ history.

<sup>4</sup> See Brubaker and Laitin (1998) for a review of the various approaches in the study of ethnic conflict.

<sup>5</sup> The reader should refer to <http://ciri.binghamton.edu/index.asp> for detailed descriptions of the physical integrity rights data, sources, and methodology. The PTS data are available at [www.politicalterrorsscale.org](http://www.politicalterrorsscale.org).

<sup>6</sup> See Fearon (2003) and Alesina et al. (2003) for extensive discussion of measuring and categorizing ethnic groups.

<sup>7</sup> Data for the 38 components are used to derive ratings on five major areas: the size of government; legal structure and security of property rights; access to sound money; exchange with foreigners; and regulation of economic activity (credit, labor and business). A majority of the components are assessed based on objective data sources, but some also rely on perception based rankings by country experts.

<sup>8</sup> The peace years variables were calculated using the BTSCS program working with STATA. Beck, Nathaniel, Jonathan N. Katz, and Richard Tucker (1998: 1260–1288).

<sup>9</sup> The data are available at: <http://www.stanford.edu/~jfearon/>

<sup>10</sup> The replication data will be made available at <http://www.svt.ntnu.no/iss/Indra.de.Soyas/default.htm>.

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