Nation Building and Economic Growth *

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Abstract

Nation building, the simultaneous allocation of economic aid and military assistance in conflict and post-conflict environments, has cost the world trillions of dollars over the last half century. Yet few attempts have been made to quantify the potential economic growth effects for the recipient country from the provision of this aid. While foreign aid potentially crowds out private investment during normal times, economic and military aid together may foster security and thereby encourage private investment during times of conflict. Using a forty-five year panel dataset, we construct a measure of nation building with a three-way interaction term between military assistance, economic aid, and conflict regime. Considering that slow growing countries may be less likely to receive aid, we instrument for economic aid by estimating donor-to-donee aid flows using United Nations voting and colonial legacy histories. We find that spending on nation building does have a positive effect on economic growth. Once conflict ceases, however, we find that continued military operations coupled with economic aid harms growth. The results hold whether a single country or a multilateral group performs the nation building operation.

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