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The economic benefits of justice: Post-conflict justice and foreign direct investment

Benjamin J Appel

Department of Political Science, Michigan State University

Cyanne E Loyle

Department of Political Science, West Virginia University

Abstract

Post-conflict states represent an important research agenda for scholars studying foreign direct investment (FDI). While leaders of post-conflict states have strong incentives for trying to attract international investments, multinational corporations (MNCs) may view these states as high-risk since the reoccurrence of violence in the aftermath of civil conflict is common. Consequently, leaders of post-conflict states desperate to receive FDI to help ignite their stalled economies must convince MNCs that their state is a stable and secure place to invest in. Drawing on the recent literature that identifies the importance of domestic and international institutions for securing FDI, this article argues that post-conflict justice (PCJ) institutions can help post-conflict states attract investment. The domestic and reputation costs associated with implementing PCJ allow states to send a costly and credible signal to international investors about the state's willingness to pursue the successful reconstruction of the post-conflict zone. Under these conditions, uncertainty is lessened and foreign investors can feel more confident about making investments. Post-conflict states, therefore, that choose to implement PCJ are more likely to receive higher levels of FDI compared with post-conflict states that refrain from implementing these institutions. Statistical tests confirm the relationship between justice institutions and FDI from 1970–2001. Post-conflict states that implement restorative justice processes in the post-conflict period receive higher levels of FDI than those countries that do not implement a process.

Keywords

civil conflict, foreign direct investment, post-conflict reconstruction, transitional justice

Introduction

Post-conflict states represent a challenge for researchers of foreign direct investment (FDI). While these states may be high-risk targets for international investors, they have strong incentives for trying to attract international investments. FDI, for instance, is widely recognized as one of the most important engines of economic development. Early investment can inform other investors and potential trading partners that the post-conflict state has positive economic prospects. Economic development is also one of the most important factors in reducing the recurrence of conflict (Collier et al., 2003; Bigombe, Collier & Sambanis, 2000). Beyond the benefits of economic growth for states, new leaders can use FDI as a domestic indicator of their ability to govern and secure their own legitimate tenure in office. Given the importance of FDI, how can leaders in the aftermath of civil conflicts attract FDI and what can these leaders

Corresponding author:
cyanne.loyle@mail.wvu.edu

do to instill confidence with international investors that their investments will be secure in the post-conflict state?

In this article, we address these research questions and assess the determinants of FDI following the end of civil conflicts. As we argue below, leaders of countries emerging from conflict have incentives to signal to multinational corporations (MNCs) and other potential investors that they are on a stable trajectory and unlikely to descend back into violence. Leaders can signal this stability by implementing post-conflict justice (PCJ) institutions.[1] Specifically, we argue that by implementing PCJs, leaders of post-conflict countries are able to send a costly signal to international investors that they are committed to stability, particularly through the reduction of conflict. This is possible for two interrelated reasons. First, PCJs offer a signal of stability by providing a process of acknowledgement and reconciliation and through strengthening the political legitimacy of the host government. Second, due to both the costly nature of implementing PCJs domestically and the international reputational effects for reneging on PCJ commitments, potential investors are able to recognize the credibility of this signal. Taken together, when a country implements a PCJ, MNCs can have greater confidence that their investments will be secure and they are consequently more likely to invest in such locations. In the empirical analysis, we find strong support for our theoretical argument in that post-conflict states that choose PCJs are more likely to receive FDI compared to similar states which fail to implement these institutions. Our results are robust to standard explanations (i.e. political and economic) of FDI inflows and a variety of statistical estimators and model specifications.

Our article offers at least three contributions: first, we contribute to the burgeoning literature on the determinants of FDI in post-conflict states. By finding strong support for our theoretical argument on PCJs, we identify a new way that leaders can attract FDI under such conditions. Second, we identify post-conflict justice institutions as a signaling mechanism to the international community, particularly MNCs and other investors. To our knowledge, our theoretical framework is the first to connect these domestic institutions with international behavior. Finally, we use statistical techniques to control for the non-random nature of PCJ selection to ensure the robustness of our results, which previous research on PCJs has neglected to do.

The remainder of the article is organized as follows. First, we briefly review the existing literature on the determinants of FDI. In so doing, we identify a primary concern of potential investors – the security of their investment. In this section, we describe the extra commitment problems that investors face in post-conflict states, namely the country's ability to signal stability in light of recent conflict. Second, we introduce the role of PCJ institutions and how they contribute to stability in post-conflict states through acknowledgement, reconciliation, and increasing domestic political legitimacy. Third, we introduce our theory and argue that PCJs are able to mitigate the uncertainty investors face in post-conflict societies by sending a costly signal of the commitment to a stable future. Fourth, we present our research design and review our empirical results. Fifth, we conclude with the implications of our theoretical argument and directions for future research.

The problem: FDI and credible commitment

According to the World Bank's World Development Indicators (2009), foreign direct investment (FDI) is defined as 'the net inflows of investment to acquire a lasting management interest (ten percent or more of voting stock) in an enterprise operating in an economy other than that of the investor'. For example, Intel invested USD 300 million to build a microprocessor plant in Costa Rica in 1996. Likewise, Telekom Malaysia, as part of a consortium of telecommunication companies, invested over USD 1.2 billion in South Africa in the 1990s.

Traditionally, scholars have argued that positive economic conditions can increase FDI inflows.[2] Economists, for instance, have shown that states with larger economies, higher growth rates, and stronger economic development attract greater levels of FDI (e.g. Brewer, 1993; Crenshaw, 1991; Oneal, 1988; Rummel & Heenan, 1978). Likewise, nations with lower capital controls, trade barriers, and lower taxes are also more likely to receive FDI (e.g. Agarwal, Gubitz & Nunnenkamp,1992;

[1] In brief, PCJs are temporary justice processes (e.g. trials, truth commissions, reparations programs and other accountability procedures such as amnesty agreements, exile or purging) implemented following a period of conflict to address wrongdoings that took place during that period. Our operational definition of PCJ is elaborated further below.

[2] Dunning's (1981) ownership, location, and internalization (OLI) framework provides the theoretical foundation for much of the recent literature on FDI flows. A review of this work is beyond the scope of our article, but we simply note that our argument fits within the location aspect (i.e. advantages of host states) of Dunning's framework.

Gastanaga, Nugent & Pashama, 1998; Rodrik, 1996). Finally, other socio-economic features, such as human capital, education, and the size of the labor force have been shown to influence the behavior of international investors (e.g. Blomström & Kokko, 2003; Mankiw, Romer & Weil, 1992; Noorbakhsh, Paloni & Youssef, 2001).

Despite the contributions made by economists, other scholars, most notably political scientists, have criticized the economics-only explanations for their inability to fully explain the variation in FDI inflows (e.g. Buthe & Milner, 2008; Jensen, 2003). Specifically, these scholars argue that economic arguments overlook the problem of credible commitments regarding the safety of investments. That is, since FDI is a long-term investment with costly divestitures, MNCs must incorporate the future behavior of a host state into their decisionmaking calculus as there is always some uncertainty about the trajectory of a potential host state. MNCs, therefore, look to invest in locations that can minimize risk to their investments over the long term.

Scholars argue that one of the primary reasons for this future uncertainty is the threat of political instability, including potential for violence in the host state. Domestic discord can make potential host states less attractive for investors because the resumption of conflict may harm business interests (e.g. Clague et al., 1996; Knack & Keefer, 1995; Jun & Singh, 1996). The most obvious way civil strife can affect MNCs is when the violence is directed at their operations in the host state (e.g. attacks on Shell Oil in Nigeria). There are also important indirect effects of conflict on the behavior of governments. As Li (2006) argues, for example, governments engaged in conflict or anticipating war may have incentives to restrict capital flight, increase capital controls, and enact higher tax rates. In other words, political instability can lead to greater government interference in the economy reducing profits for MNCs (Flores & Nooruddin, 2009). In short, as Li (2006: 236) concludes, '[T]he implication is that anticipated events of political violence can make an otherwise desirable investment location undesirable, deterring future investment flows, and render an existing investment site less attractive, reducing reinvestment, limiting expansion, and potentially inducing preemptive divestment.'

To address the commitment problem investors face, the literature turned to the role of domestic and international institutions. Several scholars, for instance, have shown that a variety of domestic institutions (e.g. number of veto players, democratic institutions, property rights, etc.) associated with political stability can increase FDI inflows (Bollen & Jones, 1982; Crenshaw, 1991; Henisz, 2000; Jensen 2003, 2006). Likewise, several scholars have found that states with greater respect for human rights across different dimensions (e.g. physical integrity rights, labor rights, etc.) attract more FDI (e.g. Blanton & Blanton, 2007, 2009; Kucera, 2002; Neumeyer & de Soysa, 2006). Finally, Buthe & Milner (2008) in their work on developing nations show that if a state can credibly commit to liberal economic policies, they are more likely to receive FDI.

While scholars have made important advances in studying what can mitigate the commitment problem, additional research is necessary if we are to understand the variation of FDI in *post-conflict* states since these states have a greater likelihood of returning to conflict. In other words, post-conflict states have a greater amount of uncertainty compared with other states, exacerbating their commitment problem. Despite these challenges, we believe that it is possible for post-conflict states to become relatively attractive places for MNCs to invest.[3] As we argue in greater detail below, we believe that states that implement post-conflict justice (PCJ) institutions achieve this by sending a credible signal to potential investors regarding the future stability of the host state.

To this end, we first introduce the concept of post-conflict justice and explain how these institutions signal stability. Second, we show how PCJs are a credible signal rather than merely cheap talk. Taken together, the credible signal reduces uncertainty and foreign investors can feel more confident about their investments.

Post-conflict justice as a signal of stability

To begin, post-conflict justice is defined as any process initiated within five years following an armed conflict that attempts to address wrongdoings which took place during

[3] MNCs have incentives for investing in post-conflict countries. As Flores & Nooruddin (2009: 6) argue, 'the post-conflict period likely offers potentially lucrative rebuilding opportunities'. There are two primary reasons for this (Moloo & Khachaturian, 2009): first, due to damage incurred during conflict, there is likely to be demand for infrastructure projects, providing investment opportunities for outside investors. Second, many states engulfed with civil war have abundant natural resources attractive to investors. MNCs also have reasons to invest early in the post-conflict phase as there are consequences for delaying. Early investment allows investors to potentially avoid competition and thus have proprietary access to lucrative contracts. Furthermore, early investments are often less expensive. As the state emerges from conflict and begins to develop economically, there is likely to be a corresponding increase in the costs of doing business in the state, such as higher labor costs.

that conflict (Binningsbø et al., 2012).[4] PCJs include processes to address several forms of past grievances, such as crimes against humanity, war crimes and/or systematic violations of human rights (e.g. torture) and may target the state (former regime), dissident groups or all former combatants. Our modern conception of post-conflict justice began with the trials at Nuremburg and Tokyo in 1945–46 and contains such diverse processes as the International Criminal Tribunal for the former Yugoslavia (1993), the South African Truth and Reconciliation Commission (1995), and the Special Court for Sierra Leone (2002).

Within the current literature, PCJ can be classified into two categories: *restorative justice*, which seeks to restore or bring dignity to victims, such as truth commissions or formal acknowledgement procedures (i.e. reparations programs) and *retributive justice* which focuses on a specific, individualized punishment for participants in a given conflict, such as trials, exile or purges (Gibson, 2004). PCJs that focus on restorative justice seek to reveal the truth while publicly acknowledging individual suffering. With our interest on the types of institutions that can send credible and costly signals of stability to the international community, we focus on restorative measures because these processes are generally more expansive, more public, and more costly to implement compared with retributive justice.[5] Specifically, we study truth commissions and reparations processes.[6]

PCJs serve as a signal of stability because they are implemented to prevent violence and increase stability in a post-conflict country (e.g. Elster, 2004; Hayner, 2011; Kritz, 1995; Lie, Binningsbø & Gates, 2007; Zalaquett, 1995).[7] While each type of PCJ uses different techniques to achieve this goal, there are two main mechanisms through which stability is increased: (1) acknowledgement and reconciliation and (2) domestic political legitimation.

First, PCJs are designed to reduce violence in a given country through acknowledgement and reconciliation. Conventional wisdom argues that a failure to adequately deal with the past will lead to private justice, retribution killings, mob justice, and the potential future resumption of conflict (Huyse, 1995). PCJ is therefore a process through which to address individual (and group) grievances, hold individuals accountable for past actions, and reconcile clashing populations. PCJ is able to address grievances by calling attention to systematic patterns of abuse within a population, as well as tackling the grievances which may have led to the armed conflict in the first place. Addressing these grievances can prevent the resumption of conflict on these very issues. For example, by using the information gathered during a truth commission to highlight violence and abuses suffered by a particular group, leaders can decrease the chances that the group will return to armed conflict over those issues as their grievances have been publicly addressed. In addition, by addressing violations from the previous conflict, PCJ decreases the likelihood of revenge or retribution killings by individual victims of past wrongdoings. Public knowledge of past wrongdoings holds individuals and groups accountable for past actions. Whether this accountability is punitive or symbolic, acknowledgement of the individuals responsible for offences can reduce the desire for widespread vigilante violence against those individuals.

Furthermore, by recognizing different forms of violence and bringing information to a victimized population, PCJs are able to reconcile individuals and address the causes and legacies of the conflict (Kritz, 1995). By openly acknowledging and addressing past crimes, both victims and perpetrators are able to publicly wrestle with the past together (Hayner, 2011). This public form of reconciliation allows for individual wrongs to be openly discussed and permanently resolved. In this way, addressing the historical legacies of conflict and reconciling conflicting populations decreases the chances that violence in the country will resume.

Second, PCJs increase stability by strengthening the political legitimacy of the current ruling government. PCJs can be used to increase the legitimization of a particular group, often in times of democratic consolidation (Boraine, 2006; Herz, 1982; Nalepa, 2010; O'Donnell & Schmitter, 1986). New governments or leaders distance themselves from past violence through the implementation of PCJs by demonstrating a clear adherence to the goals of acknowledgement and reconciliation as outlined above. In this way,

[4] Following the convention used in the PCJ dataset (Binningsbø et al., 2012), we refer to these processes as post-conflict justice instead of transitional justice as we are referring specifically to processes related to an armed conflict. See Arthur (2009) for a discussion of the term.

[5] Retributive institutions are also more likely to suffer from what Elster (2004) calls 'pure political justice' such as political manipulation or show trials.

[6] In the remainder of this article, therefore, when we refer to PCJ we specifically mean the above restorative processes. We define and discuss these categories more specifically in the measurement section below.

[7] A more critical strand of the transitional justice literature suggests that peace and stability may be more likely through amnesty or other negotiated post-conflict agreements (Snyder & Vinjamuri, 2003/04). Loyle & Davenport (2011) challenge the normative goals of post-conflict justice processes more generally, suggesting instead that these institutions can be used for deleterious political gains. Despite the critical views emerging in recent work, one of the main goals ascribed to PCJ remains the prevention of conflict and future instability and as such the implementation of PCJ displays a costly commitment to the expectation of future stability.

PCJs usher in a political legitimacy that may have been absent or systematically ignored during the previous period. For example, by implementing a reparations program for victims of torture, a new government can publically demonstrate that these past actions were wrong and will not be repeated. New research on truth commissions by Taylor & Dukalskis (2012) included in the volume finds that public truth processes successfully contribute to a country's democratization efforts. By establishing a new adherence to public acknowledgment of past wrongs and by opening up the justice process to political participation, PCJs strengthen a newly emerging democratic citizenry and contribute to the stability of that government (Guttmann & Thompson, 2000).

Post-conflict justice and credible commitments

The second step in our argument asserts that PCJs serve as a *credible* signal of domestic stability. This is true for two primary reasons: (1) PCJs carry both domestic political and financial costs for leaders who are considering implementing such an institution, and (2) PCJs are public and internationally recognized processes which raise the reputational elements associated with abiding by them.

First, implementing PCJ is a costly signal both politically and financially. Domestically, leaders implementing PCJ make a promise to their constituency that they will address the wrongdoings of the past. By committing to implement a process, a leader offers a public good and raises expectations about his future behavior (Grodsky, 2010). Failing to follow through could have domestic political consequences such as being voted out of office. In addition, implementing PCJs signals to opposition party members a leader's intention to address past wrongs (Nalepa, 2010). In this case, failing to follow through on the political commitment to support a PCJ can cause fractionalization and party infighting. Furthermore, PCJs carry a heavy financial burden at a time when resources are often limited. In the post-conflict period leaders must choose where and how to expend the little financial and professional resources which may be available. By prioritizing justice and stability in the post-conflict period, leaders signal to future investors that they are committed to this type of reform above others.

Second, PCJs are public processes recognized as being consistent with international norms and standards, which raises the reputational ante for leaders who implement these institutions. The United Nations (2010), Amnesty International (2007), and the International Center for Transitional Justice, for example, have all developed monitoring guidelines for implementing justice processes. By choosing to reconcile past wrongdoings through PCJ, leaders create a window for international actors to evaluate and monitor their actions. As such, leaders that implement one of these institutions put their reputation for compliance with international standards on the line. In particular, when states carry out justice processes they send a signal to the international community that they are the type of state that abides by international norms. Leaders who remain committed to this process develop a favorable reputation for compliance with established norms and obtain the benefits (e.g. receive greater FDI). In contrast, leaders who fail to uphold their commitment to these standards are viewed as unreliable partners by members of the international community. Given this, other actors will be reluctant to enter into agreements with them and they will be less able to receive the benefits of future cooperation (e.g. Guzman, 2008; Tomz, 2007). Therefore, leaders who implement PCJs will be less likely to undermine such processes in order to avoid the international costs associated with doing so.[8]

In sum, in the aftermath of civil conflict, leaders want to be able to demonstrate to MNCs that investments will be secure in their country. Despite the challenges, we believe that PCJs can help post-conflict leaders achieve this objective. When leaders implement PCJs, they send a signal to investors that their country is stable; in addition, the signal is credible because of the costs of implementing these institutions along with the reputational costs for failing to abide by them. As such, as investors are more confident about the future stability of the post-conflict state, they are more likely to invest their resources in that country. In contrast, when leaders fail to implement a PCJ following civil war, international investors are left with little information about the future of the state. This uncertainty can act to reduce the likelihood that they will invest in the state since they have less trust in the safety of their investments. Therefore, we propose the following hypothesis:

> *Hypothesis:* FDI is likely to be greater in a post-conflict state where there is a PCJ compared with a post-conflict state that lacks a similar justice institution.

[8] There is an additional implication of our argument. Similar to the literature on human rights and FDI cited above, when MNCs invest in states deemed to be relatively peaceful, they do not have to fear a domestic backlash for investing in a contentious location with potential humanitarian abuses. Thus, MNCs avoid these audience costs by investing in stable locations. We thank an anonymous reviewer for turning our attention to the importance of the human rights literature for our argument.

Research design

We use data from the Post-Conflict Justice dataset (Binningsbø et al., 2012) to test our theoretical expectations. This dataset includes PCJ activity related to all extrasystemic, internationalized internal and internal armed conflicts with at least 25 annual battle-related deaths as coded by the UCDP/PRIO Armed Conflict Database (Gleditsch et al., 2002). We focus on internal armed conflicts, including internationalized conflicts, in developing nations from 1970 to 2001.[9] Moreover, following Flores & Nooruddin (2009), we combine conflicts in the same state but involving different non-state actors into one post-conflict episode.[10] Based on these guidelines and accounting for missing data, our final dataset includes 95 civil conflicts.

As we focus on the post-conflict period, we take great care in constructing this part of our dataset. First, following Collier, Hoeffler & Söderbom (2008), we use a ten-year period succeeding the end of the conflict in our analysis.[11] Moreover, we use ten years because in the Post-Conflict Justice dataset a state is coded as having a PCJ if the institution is selected within five years following the end of the conflict. As a result, we believe that the time period used to measure FDI growth should be longer than the time period used to code the justice institutions. We then collapse the entire ten-year post-conflict period into one observation. We use this snapshot of the post-conflict period as the unit of analysis in our study. We do this for four reasons.

First and foremost, as our theoretical interest is on the change in FDI inflows in the post-conflict period, we believe a ten-year snapshot rather than a unit of analysis based on yearly observations is more appropriate. A snapshot of the post-conflict period better corresponds to our theoretical interest – the presence or absence of PCJ in the post-conflict period and changes in FDI inflows.[12] Second, FDI as well as the other economic-related variables are likely to be very unstable in the post-conflict period with large changes from year to year which may complicate the analysis. Third, an alternative would be to use survival analysis to measure FDI recovery in the post-conflict period compared with pre-conflict FDI numbers.[13] Although event history can be useful in some analyses, such as conflict reoccurrence, we would lose information unnecessarily by doing this. For instance, instead of the actual amount of FDI inflows that we use in this analysis, a recovery-based analysis collapses the amounts of FDI into a dummy variable. Fourth and more practically, as is well documented, FDI datasets contain large amounts of missing data. Using the snapshot-based analysis allows us to overcome this problem in some post-conflict episodes, although we still lose 15 conflicts because of missing data on the FDI variable. Overall the snapshot-based analysis is the optimal way to analyze our research question.[14]

Finally, to measure our response variable we use net inflows of FDI, measured as total FDI inflows minus total FDI outflows of capital.[15] We acknowledge that there is debate in the literature as to how scholars should measure FDI. Some use net FDI inflows as a percentage of GDP (Buthe & Milner, 2008; Jensen, 2003), while others prefer net FDI inflows (Li & Resnick, 2003).[16] We use net FDI inflows below because GDP is likely to be very unstable in the aftermath of civil conflict.[17] Once we have FDI for ten years, we subtract FDI in the first

[9] Since we focus our analysis on the post-conflict period, we only include civil conflicts terminated before 2001. We do this to create a post-conflict period (2001–06) long enough to include in the analysis. We acknowledge that this post-conflict period is shorter than the rest of the analysis (ten years), but we wanted to include as many cases of civil conflict as possible. Moreover, we do not believe the shorter timeframe biases our results. Since more PCJs are implemented in the post-1989 period, these reduced post-conflict periods actually favor the null hypotheses of lower-levels of FDI (assuming that longer periods allow for a greater inflow of FDI). Furthermore, there is no reason to expect that the shorter post-conflict periods are more or less likely to receive PCJs; that is, PCJs are randomly distributed across the shorter periods. Consistent with the existing literature, we focus only on conflicts in developing nations (e.g. Blonigen & Wang, 2005; Collier & Hoeffler, 2002; Flores & Nooruddin, 2009; Buthe & Milner, 2008).

[10] Since FDI is a state-level variable, we believe it is necessary to collapse all conflicts in a single country into one observation. Put differently, we believe it is necessary that our unit of analysis corresponds to our research question.

[11] If conflict reoccurrence took place within ten years, we end the post-conflict interval when the new conflict began.

[12] Put differently, PCJ is a constant in the post-conflict period. The entire episode receives a 1 if a state implemented at least one PCJ (either a truth commission or reparations process) within five years and 0 otherwise.

[13] Flores & Nooruddin (2009) use survival analysis to test for GDP recovery.

[14] We acknowledge that by using the snapshot instead of yearly numbers we lose observations which results in a relatively small sample. Nonetheless, we believe as discussed above that the snapshot provides the best way to test our theoretical argument.

[15] As Jensen (2003) argues, net FDI inflows is a more appropriate measure than total FDI flows when the theoretical focus is on what states can do to attract FDI, as it is in our analysis.

[16] See the exchange between Choi (2009) and Li (2009) for more information on this debate.

[17] As a robustness check we estimate our models on FDI/GDP. Our results remained the same. Results are available in the supplementary online appendix that is included below and are part of our replication materials.

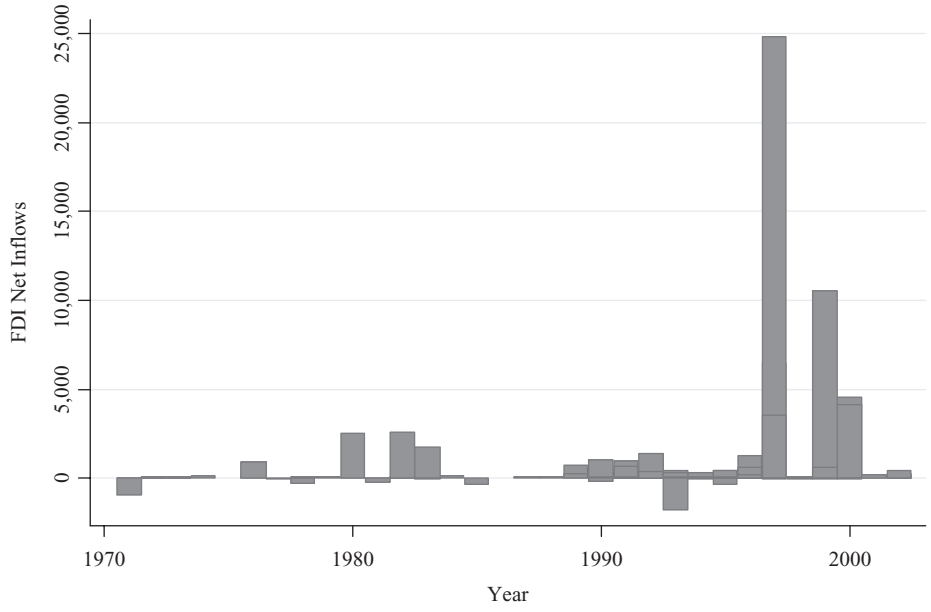

Figure 1. FDI net inflows in post-conflict states, 1970–2001

year after the conflict from FDI in the tenth year after the conflict.[18] The final variable gives us the difference in net FDI inflows across the ten-year period. In our analysis, we measure FDI inflows in millions of dollars.

Figure 1 shows the difference in net FDI inflows (in millions USD) for the ten-year post-conflict period for the 95 states in our analysis. A few interesting patterns emerge from our data. First, net FDI inflows (in millions USD) range from –USD 1,858 (Indonesia in 1993) to USD 24,836 (Russia in 1997) with a mean of USD 38 (Bangladesh in 1993).[19] The descriptive statistics also suggest that the data are right-skewed, with a greater number of countries experiencing very high levels of FDI compared with the number of states that witness large negative FDI. Finally, the inflows of FDI have increased over time with higher levels occurring in the post-Cold War period.[20]

Measurement

Post-conflict justice institutions

As outlined above, we create a measure of PCJ implementation from the Post-Conflict Justice (PCJ) dataset. While a conceptual overview is provided above, here we provide the operational definition for each type of PCJ and the relevant coding specifications.

In the PCJ dataset, truth commissions are defined as 'officially-sanctioned, temporary investigative bodies that focus on a pattern of abuse over a particular period of time' (Binningsbø et al., 2012). Truth commissions are established to investigate past wrongdoings and are not necessarily accompanied by formal legal prosecution and trials. Unlike trials, truth commissions attempt to address archetypal violence rather than working to prosecute individuals. These are information-gathering bodies that typically focus on victim's experiences and mechanisms of social reconciliation.

Similarly, reparation programs allow the government or those responsible for the violence to directly compensate or address the material grievances suffered by civilians. In the Post-Conflict Justice dataset, reparations are defined as 'compensation given to an individual or group who were harmed in some way during the conflict' (Binningsbø et al., 2012). These efforts can include individual support such as monetary compensation for those who lost a family member during the war or communal efforts such as the rebuilding of roads or schools in a conflict-affected area. These programs provide short-term support and long-term acknowledgement to those who suffered from the conflict while documenting individual abuses.

Next, we review some summary statistics for our key independent variable. Across the 95 conflicts, 18 of them

[18] If the first or tenth year of data was missing for a given conflict, we used the first and last available years in the ten-year interval (i.e. third year subtracted from ninth year).

[19] As a robustness check to account for this outlier, we included a control variable for Russia in our statistical analysis. Our results remained robust.

[20] For this reason, we control for the Cold War in our analysis.

implemented at least one PCJ institution. It is also useful to gain an understanding of the general relationship between FDI and PCJs in our data. The overall mean for FDI inflows is approximately USD 760 (again measured in million dollars). The mean value for FDI when there is no PCJ is only USD 425, while it is USD 2,188 for states that implemented a PCJ. At first glance, the general patterns in our dataset reinforce our theoretical argument on the importance of PCJs for attracting FDI. Of course, despite this initial evidence, it is necessary to estimate the relationship controlling for other factors, as well as the non-random nature of PCJ implementation.[21]

Control variables

Based on the existing literature for both FDI and post-conflict states, we include several control variables. Our controls can be grouped into three categories: (1) economic variables, (2) political institutions, and (3) conflict variables. In addition, we include a Cold War variable in all of our equations to account for the increase in FDI in the post-Cold War world.[22]

Economic controls. We incorporate several variables related to an increase in FDI inflows. In brief, *economic development* is measured as GDP per capita, *economic size* is measured as GDP, and *economic growth* is measured as GDP per capita growth. Consistent with the extant literature, we believe that all three variables should be associated with higher inflows of FDI. All variables are measured using current international dollars and are taken from the World Development Indicators (2009). We also include a measure of *exchange rate fluctuations* to account for the stability of the currency. Our expectation is that greater currency instability should be associated with less FDI. Following Blanton & Blanton (2009), we measure this variable as the ratio of the exchange rate in a given year (relative to the US dollar) to its mean value over the previous two years. Exchange rate data are taken from the Penn World Tables 6.3 (Heston, Summers & Aten, 2009).

In addition, we include the KAOPEN Index, which is a measure of capital account openness (Chinn & Ito, 2008). We expect that states with higher levels of openness and therefore a preference for FDI will be more likely to receive FDI inflows. The variable is a continuous measure that ranges from –1.8 to 2.5 in our data and is taken from Chinn & Ito (2008). Finally, we include a measure of labor force participation (measured as the number of people that could be economically active (ages 15–64) as a percentage of the total population) and the average female life expectancy. Both variables are from the World Development Indicators (2009).[23] For all of the economic control variables, we use the first year available in a given country following the end of the conflict. We do this to avoid any potential problems of reverse causality.

Political institutions. We include two variables to measure domestic political institutions. For both measures, we believe FDI will be greater when the post-conflict state is more stable. First, we include a democracy variable since democratic states are viewed as more secure and stable compared to non-democratic states (e.g. Jensen, 2003: 200). In our empirical analysis, we include the full net-Polity scale (autocracy–democracy) which ranges from –10 to 10 (Marshall & Jaggers, 2002). Some scholars have questioned the democracy–FDI link and instead have argued that political stability is important to international investors, irrespective of regime type. Therefore, to measure political stability independent of regime type we include a veto player based variable that measures the degree of domestic political constraints (Henisz, 2002). This is a continuous variable that ranges from 0 to .86 in our data with higher numbers indicating more veto players and greater stability. Again, we include the first available year in the post-conflict period for both variables to avoid any problems of reverse causality.

Conflict. We include several variables to account for the nature of the political conflict. First, we expect more intense and difficult civil wars (i.e. longer duration and greater damage) to be followed by lower levels of FDI. Our logic is that as the intensity of the civil war increases, investors will be more likely to fear for the security of their investment in the post-conflict period. Second, we include two variables – *peace agreements* and *victory* – to operationalize how the conflict ended. We expect conflicts that ended with victory or a peace agreement to be more likely to receive FDI than other termination

[21] See Gibson (2006) for a discussion of the potential endogenous nature of a PCJ process.

[22] For instance, in our data, the average amount of FDI inflows is USD 236 million during the Cold War and USD 967 million after it ended.

[23] As a robustness check, we included variables for female secondary school enrollment and a measure of raw material (total ore, metal, and fuel) exports. Our PCJ variable remained significant in the equations with these additional variables. We do not include these variables in the final equations in the article because of problems of missing data.

types such as battle fatigue. *Duration* is simply measured as the total number of days of the conflict episode. *Damage* is a continuous variable that measures the amount of pre-conflict GDP lost by the end of the conflict. *Victory* is a dummy variable that equals 1 if one side emerged as the clear winner in the conflict. *Peace agreement* is also a dummy variable that is coded 1 if the disputants ended the conflict with an agreement. We relied on the UCDP/PRIO Armed Conflict Database (Gleditsch et al., 2002) to code these variables.[24]

Results

We use OLS to estimate our equations using Stata version 10.[25] We also estimate expected values and the percentage change for all the statistically significant variables. Overall, we estimate five equations based on the different set of control variables. We first estimate an equation with the economic-only explanations plus our PCJ variable of theoretical interest. We then do the same for the political institutions and conflict variables, as well as an equation with only the PCJ variable. We then estimate a full equation including control variables. We estimate the equations to assess the robustness of PCJ across different specifications. Finally, as a robustness check discussed in greater detail below, we use a pre-estimation matching procedure called coarsened exact matching (CEM) to help account for the non-random nature of PCJ implementation and any concerns over potential bias in our statistical results.

Post-conflict justice

Across all five equations, we find that when a post-conflict state implements a PCJ, the country receives higher levels of FDI compared with a post-conflict state without such a process (Table I). The result is robust across all five specifications, including the full model with all of the appropriate control variables. Regarding the effect of PCJ, we find a state that implements a PCJ receives approximately 1,960 (again in millions USD) more FDI. The results in Table II are even more dramatic. When a post-conflict state has a PCJ, the amount of FDI inflow is approximately 358% greater compared with post-conflict states that fail to implement justice institutions.[26] Overall, then, we find strong, consistent, and substantive support for our key hypotheses on the role of PCJs in helping post-conflict states attract FDI.

Economic variables

As expected, we find fairly strong support for the economic variables in our analysis. *Economic size*, *economic growth*, and *exchange rate fluctuations* are significant in both equations, while the KAOPEN index is significant only in the full equation. On the other hand, we find no support for *economic development*. Regarding the substantive impact, as the *economic size*, *economic growth*, *exchange rate*, and the KAOPEN index go from small to large values (25th to 75th percentile), a post-conflict state receives about 189%, 58%, –3%, and 49% more FDI, respectively. In sum, we find that economic variables are still a strong predictor of FDI inflows, even in the aftermath of civil conflict.

Domestic political institutions

We find mixed support for domestic political institutions. *Political constraints* are statistically significant in the expected direction, but *regime type* is negative and statistically significant. While the finding for regime type is contrary to our expectations, it is not entirely surprising. Resnick (2001), for instance, finds that in transition economies, democratic states receive less FDI. More substantively, when we move political constraints from low to high levels, FDI inflows increase by 207% indicating that policy stability is an important predictor of FDI. On the other hand, FDI inflows decrease by 113% in more democratic states compared with less democratic states (a move on the net-Polity scale from –8 to 8). The mixed results suggest that more work is needed to further assess the relationship between domestic institutions and FDI in post-conflict episodes.

[24] As a robustness check, we included two human rights variables – Physical Integrity Rights and Workers' Rights from the Cingranelli-Richards (CIRI) Human Rights Dataset (Cingranelli & Richards, 2010). As we discussed above, both variables have been shown to be important predictors of FDI inflows. Our PCJ variable remained robust to the inclusion of these variables. We omit these variables from the final set of equations because they are only available for the 1980 period, which reduces the total number of observations in our sample. We prefer to present the results for the largest sample size, especially since our PCJ variable remained unchanged even when we included the human rights variables in the analysis. The results are available as part of our online appendix.

[25] Our tests of statistical significance are based on one-tailed tests.

[26] As a robustness check, we included variables for other forms of justice institutions, such as trials, amnesty, exile, and purges. As expected, we found no relationship for these types of PCJs and FDI inflows. The result for our PCJ variable remained statistically significant.

Table I. The effect of PCJ on net FDI inflows in post-conflict states

	Economic EQ	*Institutions EQ*	*Conflict EQ*	*Final EQ*
Post-conflict justice	1532.6***	1654.7**	2590.5***	1960.3***
	(629.4)	(722.9)	(845.0)	(703.0)
Economic development	−0.0576			−0.111
	(0.134)			(0.133)
Economic size	1.05e-08***			1.10e-08***
	(1.67e-09)			(1.74e-09)
Economic growth	0.724			37.40*
	(21.30)			(23.24)
KAOPEN Index	132.6			198.8
	(208.0)			(201.6)
Exchange rate	−49.22***			−42.52***
	(13.56)			(13.89)
Labor force	14.72			9.844
	(25.45)			(25.53)
Life expectancy (Female)	17.39			3.475
	(30.29)			(32.99)
Political constraints		4389.1***		2558.0**
		(1366.3)		(1459.6)
Democracy – Polity		−99.64*		−90.17*
		(61.24)		(56.31)
Damage			10.01	28.38***
			(10.59)	(10.24)
Duration			−25.54	0.811
			(42.52)	(35.54)
Peace agreement			−2498.0***	−1215.1*
			(885.4)	(793.8)
Victory			−1321.9**	−33.97
			(642.4)	(650.7)
Cold War				81.53
				(654.1)
Constant	−2011.6	−632.6*	1418.3***	−1278.3
	(2677.9)	(459.2)	(510.0)	(2852.3)
Observations	95	95	95	95
Adjusted R^{12}	0.370	0.128	0.105	0.422

Standard errors based on one-tailed test in parentheses. Statistical significance based on two-tailed tests. * p < 0.10, ** p < .05, *** p < .01.

Conflict variables

We find no support for the conflict-based variables and FDI in post-conflict states. Contrary to our expectations, as states experience greater damage to their economy, they receive higher levels of FDI. Specifically, when we move from low to high economic damage (25th to 75th percentile), FDI inflows actually increase by 85%. Similarly, conflicts that ended with victory or peace agreements receive less FDI, but again the results just miss significance. The weak results indicate that either the characteristics of the conflict itself are unrelated to how investors feel about the security of their investments, or again more theoretical and empirical work is needed to understand this relationship.

Table II. The impact of changes in PCJ on the expected value of FDI

Independent variables	*Percentage change of FDI growth*
PCJ (No to Yes)	358
Economic size (25th to 75th percentile)	148
Economic growth (25th to 75th percentile)	58
KAOPEN Index (25th to 75th percentile)	49
Exchange rate (25th to 75th percentile)	–3
Damage	85
Political constraints (25th to 75th percentile)	207
Regime type (–8 to +8)	–113

To estimate the expected values we first move the covariate of interest from the low to high while holding all the other covariates at their real value. To compute the first difference, we subtract the baseline expected value (covariate at low values) from the expected value following the change in the covariate of interest. We then divide the first difference by the baseline expected value.

Robustness checks

To gauge the robustness of our results, we use a matching method to account for the potential non-random nature of our PCJ variable. Since post-conflict states often strategically implement PCJs (Gibson, 2006), our key explanatory variable of theoretical interest may be endogenous to some unmeasured factors which may bias our results. For instance, there may be elements that explain both the implementation of the PCJ and greater FDI inflows. If, for instance, a post-conflict state with relatively high levels of social unification implements a PCJ, then it could be the relatively strong domestic harmony (the cause of the PCJ) and not the PCJ itself that contributed to higher levels of FDI. When this happens, the error term and the independent variable of interest (i.e. PCJ) are correlated, which can lead to biased and inconsistent results. We use the matching procedure described below to alleviate any potential concerns.[27]

More technically, as Iacus, King & Porro (2011) argue, the primary motivation for matching is to create a more balanced dataset that can help reduce model dependence, statistical bias, and heterogeneity in the empirical analysis. In a balanced dataset, the empirical distributions of pre-treatment control variables are roughly equivalent. Put differently, the idea is to create a dataset in which the control variables in the treatment (observations with PCJs) and control groups (observations without PCJs) are more similar in order to more directly assess the causal impact of the treatment effect (PCJ).

In this article, we use coarsened exact matching (CEM), an algorithm recently developed by Iacus, King & Porro (2011) to account for endogeneity and related problems.[28] The CEM procedure works in five steps. First, we create a new dataset that contains the treatment variable and the control variables from our original model. Consistent with the goal of matching, we include only the control variables that are associated with the implementation of the treatment (e.g. PCJ). Second, we coarsen or recode each control variable to create a variable with a smaller number of categories, in which substantively indistinguishable values are grouped together in the new categories. For example, a net-Polity variable (1–20) could be coarsened into non-democratic, mixed, and democratic regimes. This coarsening is either done manually or by an automated procedure.

Third, we create strata or categories that include all possible combinations of the values from all of the coarsened variables. For example, a second control variable, GDP, could be added and coarsened into low-income, middle-income, and high-income states. The strata would then include (1) non-democratic, low-income, (2) non-democratic, middle-income, (3) non-democratic, high-income, (4) mixed, low-income, and so forth. Once the strata are created, observations from the data are placed in the appropriate strata (e.g. non-democratic, low-income states are put in stratum 1). Fourth, strata that include at last one treated (PCJ) and one control unit (no PCJ) are retained, while the remaining strata are dropped from the data. For example, if there are no 'non-democratic, low-income' states that implemented a PCJ, then this stratum would be dropped. Fifth, the coarsened variables from the reduced dataset are returned to their original values (e.g. 1–20 on the Polity scale) and the final model is then estimated on the reduced data using standard techniques (OLS, logit, etc.). These results based on the matched data provide greater confidence that we are estimating the true causal effect of PCJs on FDI inflows.

We use *peace agreements*, *victory*, and *damage* as the control variables to construct the new dataset. All of these variables are theorized to affect the implementation

[27] An alternative technique is to use instrumental variables. A major limitation of this approach is that the instrument (or predictor) of PCJ cannot be correlated with the outcome of interest (FDI). Unfortunately, we doubt that such a variable exists.

[28] The authors argue that CEM is superior to other methods including propensity score matching.

of PCJs; we therefore believe it is necessary to account for them in this part of the analysis since our primary motivation for using matching is the non-random nature of our treatment variable. In other words, we are matching on the conflict variables to obtain a dataset with more similar post-conflict situations. After running this pre-estimation procedure, we are left with 75 observations and a much more balanced dataset.[29]

The second step then is to estimate our model on the reduced, balanced data. In Appendix A, we present the results of the matching process. As the results indicate, our PCJ is still statistically significant even when we account for the potential non-random nature of it. For instance, when the response variable is net FDI inflows, a post-conflict state receives USD 2,959 more FDI compared with states without these institutions.[30]

In sum, we find that across different specifications (including altering the response variable and control variables) and accounting for the non-random nature of justice institutions, PCJs increase the amount of FDI in post-conflict states.

Conclusion

Post-conflict states struggle to signal to potential investors that they can credibly commit to securing their investment. In this article, we argued that it is possible for post-conflict states to attract all-important FDI despite the obstacles in these situations. In short, we argued that justice processes enable post-conflict states to signal to international investors that they are committed to domestic stability and focused on preventing the resumption of conflict through the reconciliation of groups and acknowledgement of grievances. We expected MNCs and other investors to be more likely to invest in a state when they are confident about the security of their investment. As a result, we theorized that FDI would be higher in post-conflict countries which were able to signal stability through the use of PCJ.

In a series of statistical tests including accounting for the non-random nature of PCJs, we find strong statistical and substantive support for our hypothesis. Our findings have implications for scholars and policymakers of post-conflict states, FDI, and PCJs. First, our findings support the argument made by political scientists on the importance of minimizing political risks for investors. Second, this analysis demonstrates the relevance of focusing on domestic political determinants for FDI inflows in post-conflict countries. Finally, by showing that PCJs can act as a signal to minimize investor risk, we have identified a previously unknown role for justice institutions. While most research has focused on the domestic context and its relationship to PCJ implementation, our findings indicate that the international environment is also important.

Our theoretical argument and findings suggest several fruitful avenues for future research. For example, while we include an aggregated measure of PCJ, future efforts should focus on disaggregating PCJs to theorize and test the relationship between different types of justice institutions and FDI growth. Additionally, since our study confirms the political determinants of FDI, scholars should now consider how investors respond to different signals, especially in post-conflict locations. Finally, regarding the important role of PCJs in both domestic and international affairs, scholars would be well served to focus on whether these institutions increase other economic variables, such as trade and foreign aid.

Replication Data

The dataset, codebook and do-files for the empirical analysis in this article can be found at http://www.prio.no/jpr/datasets.

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[29] As discussed earlier, the matching procedure prunes both treatment (PCJ) and control group (non-PCJ) observations. Additionally, the level of imbalance goes from .9 to .2. Perfectly matched data sets have an imbalance of 0.

[30] Our results are robust using FDI/GDP as the response variable.

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Appendix A: Coarsened exact matching procedure

	Net FDI inflows	*FDI/GDP*
Post-conflict justice	2949.5***	5.274**
	(842.7)	(2.371)
Economic development	−0.207	0.000685
	(0.203)	(0.000571)
Economic size	1.00e-08***	−5.42e-12
	(2.00e-09)	(5.64e-12)
Economic growth	95.41*	0.264*
	(62.31)	(0.175)
KAOPEN index	81.09	−0.230
	(252.3)	(0.710)
Political constraints	1644.7	−1.901
	(1873.3)	(5.271)
Victory	−61.54	−2.269
	(1190.8)	(3.350)
Duration	58.03	0.0568
	(45.29)	(0.127)
Damage	46.59**	0.108*
	(26.63)	(0.0749)
Peace agreement	−1423.1**	-1.665
	(736.5)	(2.072)
Cold War	−345.1	−0.0622
	(1029.5)	(2.896)
Democracy–Polity	−76.89	−0.0215
	(71.90)	(0.202)
Exchange rate	−36.09**	0.0246
	(18.30)	(0.0515)
Labor force	−16.43	0.0824
	(34.64)	(0.0975)
Life expectancy (female)	−26.67	−0.0435
	(48.25)	(0.136)
Constant	2518.0	−1.439
	(3858.4)	(10.86)
Observations	75	75
Adjusted R^{12}	0.408	0.028

Standard errors based on one-tailed test in parentheses. * p < 0.10, ** p < .05, *** p < .01

BENJAMIN J APPEL, b. 1979, PhD in Political Science (University of Maryland, 2012); Assistant Professor of Political Science, Michigan State University (2012–); current main interests: international law and organizations and conflict processes.

CYANNE E LOYLE, b. 1980, PhD in Political Science (University of Maryland, 2011); Assistant Professor of Political Science and International Studies, West Virginia University (2011–); Assistant Director of the Northern Ireland Research Initiative and co-creator of the Post-Conflict Justice (PCJ) database; current research interest: the strategic government use of post-conflict justice.