

**Outsourcing War:
The Evolution of the Private Military Industry after the Cold War**

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Abstract

In this paper, we study the evolution of private military corporations (PMCs), which are for-profit organizations that subcontract military field services to sovereign authorities as well as to others. Between Eisenhower's famous "military-industrial complex" speech in 1961 and the post-9/11 war in Iraq, PMCs were transformed from relatively minor subcontractors to major companies with unique capabilities that made them strategically central to the sovereign military organizations from which they had grown. Throughout this period, PMCs exhibited a "hybrid organizational form" as delineated within organizational economics. Our purpose is grounded theorizing in which we derive insights about the evolution of PMCs as hybrid organizational forms. Our analysis suggests that hybrid forms of organization enable transactions and capability development that are not possible within either markets or hierarchies. Hybrid forms may thus represent a conduit for institutional entrepreneurship and the emergence of new industry structures. Their intertemporal characteristics warrant further theoretical study.

“[W]e have been compelled to create a permanent armaments industry of vast proportions...In the councils of government, we must guard against the acquisition of unwarranted influence, whether sought or unsought, by the military-industrial complex. The potential for the disastrous rise of misplaced power exists and will persist... [I]n holding scientific research and discovery in respect, as we should, we must also be alert to the equal and opposite danger that public policy could itself become the captive of a scientific, technological elite.”

Dwight Eisenhower – January 17, 1961

Eisenhower’s warning about the military-industrial complex was issued in the wake of a transformation in the character of combat. Prior to World War II, the armaments required for combat operations were principally constructed ad hoc in response to wartime demand on a “just in time” model. Armaments were mainly limited to personal weaponry, and particularly to handheld firearms. World War II changed the profile of armaments to large-scale weapons platforms and the massive deployment of transportation equipment, including aircraft, trucks and other types of armoured vehicles. Subsequent deterrence strategies of the United States and the Soviet Union required the continuous operation of armaments industries rather than the “just in time” approach that had been the norm over centuries of recorded combat. Eisenhower was concerned that competition in the private sector could lead to such technological sophistication in armaments that specialists would be required to govern their deployment. Private firms with scientific capabilities for armament manufacture might ultimately wield sufficient power to control the fates of nations.

In this article, we argue that private corporations participate in decisions that can influence the fates of nations, but not strictly because of their technological sophistication in the sense that concerned Eisenhower. Some 50 years after Eisenhower’s speech, private military corporations (PMCs) such as Blackwater (now renamed Xe), Aegis Defence Services, DynCorp, and Military Professional Resources Inc. (MPRI) subcontract field services to a range of organizations, and particularly sovereign military agencies such as the US Department of Defence and the British

Ministry of Defence. Their scale, activities, goals and capabilities are the subject of considerable controversy as PMCs have come to account for almost 50 percent of US spending in Iraq (Scahill 2007). The contractual duties of PMCs are principally defined in terms of field services (such as combat, security, training, transportation and communications) rather than technology, although technology (ranging from missile systems operation to data-center services) is involved in PMC activity. In some instances, the capabilities of PMCs make possible the attainment of specific military objectives in the sense that concerned Eisenhower.

The analysis in this paper involves grounded theorizing focused on PMCs since the time of Eisenhower's speech. Our interests are in both ascertaining what can be learned from PMCs for theory regarding hybrid organizational forms, and in posing questions for subsequent theoretical analysis on hybrids that arise from the PMC example. We address a range of questions regarding the character of the PMC industry including: How do contemporary PMCs differ from the bands of roving mercenaries that have been involved in warfare through nearly all of recorded history? Why have the militaries of sovereign nations such as the United States and the United Kingdom come to rely on PMCs so centrally?

Our main interest, however, is in developing questions for theory regarding hybrid organizational forms. We begin by exploring the definition of hybrids, which Williamson (1991) characterized as contracts and other intermediate forms of organization between markets and hierarchies. Since Williamson's seminal work, the definition of hybrids has developed to reflect the unique capabilities and diverse market participation of firms that execute contracts (Menard, 2004). Our argument progresses with the assertion that PMCs are archetypical hybrids, emerging first as limited contracting bodies following Eisenhower's speech, and then as fully developed organizations with unique capabilities that earn profits by operating in tandem with sovereign military authorities by the time of the second Iraq War.

The core of the paper is an historical analysis of five, overlapping periods that unfolded after the Cold War and during which PMCs developed from simple contractors to complex corporations that enable sovereign nations to accomplish goals that could not otherwise be achieved. The drivers of change across these periods are broad institutional trends including privatization, globalization, and foreign policy, representing shift parameters that exogenously influence the relative costs of alternative governance structures (Oxley 1999; Williamson 1991).

For the analysis, we define PMCs as legally incorporated entities that offer battlefield services for hire and that take as their customers – at some points in time although certainly not in every instance – sovereign military authorities. Many PMCs also offer complementary services designed to avert battlefield intervention, such as negotiations, advisory, and intelligence services (Singer 2003). Although PMCs remain a relatively small segment of the total military-industrial complex, they now constitute a major industry, comprised of large transnational enterprises with uniformed military ranks, doctrine, discipline, and capable of providing companies of commandos and battalions supported by combat helicopters and fighter jets. Many remain small, however, operating as virtual companies that rely on databases of qualified personnel and specialized subcontractors on a contract-to-contract basis.

Theoretical questions suggested by the analysis include: What motivates hybrids' emergence and development over time? What influences the development of capabilities within hybrids rather than markets or hierarchical organizations? Under what conditions are hybrids sustainable as stand-alone entities with unique capabilities? How does the relationship between hybrids and hierarchical authorities co-evolve? Do hybrids always operate between markets and hierarchies or on their own institutional logic, or do they represent a 'third way' in which economic exchange may be organized? How general is the intertemporal path observed among PMCs?

Our findings emphasize that hybrids may provide a bridge to new, distinctive industry structures. PMCs emerged from sovereign militaries first as small, immaterial contractors but grew through time into substantial firms with distinctive capabilities. As they developed, these capabilities made possible the achievement of military objectives that could not be achieved by sovereign military authorities alone. PMCs were not only transaction-cost minimizing, but also transaction-enabling. As a result, by the beginning of the second Iraq War, major sovereign military authorities had become dependent on PMCs. The process by which the bilateral and multilateral dependency developed between the hybrid PMCs and hierarchical sovereign military authorities was integral in the establishment and rapid rise of the PMC industry.

A BRIEF HISTORY OF PRIVATE MILITARIES

As a military general, Eisenhower must have known that reliance on private military services is common in the history of war. Greek and Nubian men, for example, fought for the Egyptians as early as the Late Bronze Age. Mercenaries took Jerusalem from the Roman Empire during the Sixth Crusade, and the British hired Hessian forces during the American Revolution (Brauer 1999). Indeed, prior to the late 19th Century, employment of private militaries was the predominant mechanism for marshalling fighting forces and conscription was rare. Only after the industrial revolution, as military technology advanced, did states begin to conscript and maintain standing armies to protect national interests. As a result, the language of war reflects traditions related to outsourcing. Singer (2003, p. 24) explains that words such as “freelances” and “companies” emerged originally during the Middle Ages to describe roaming bands of soldiers for hire. These traditions continued into the 20th Century guided by an institutional logic that left private military actors free to operate internationally, subject to state control.

By the early 21st Century, PMCs operated very differently. A specific incident illustrates the change. In March 2004, after the ambush and brutalization of four employees of the PMC

Blackwater in Fallujah, US President George W. Bush declared that the United States could not stand idly by (Scahill 2007). The US responded by escalating the Baghdad offensive, which was deemed essential on military as well as ideological grounds as the strength US military operations in Iraq depended critically on the presence of PMCs. Had the US not responded aggressively, the authority and effectiveness of PMCs could have been stymied, with implications potentially as consequential as conscription in the US.

Five years later, the Iraq Reconstruction Corporation (IRC), depicted in Table 1, was established as the governing body for allocating sovereign and private military resources toward the rebuilding of the country. Not only are PMCs central to IRC operations, but British PMC Aegis Defence Services was contracted to design and establish the organization. The IRC's hybrid structure was a deliberate design choice. Thus, a different mechanism than Eisenhower's "scientific, technological elite" had come to govern some command-and-control decisions: a decentralized, partially controlled confluence of actions taken with deliberation by different organizations with varying objectives. Sovereign militaries now routinely use PMCs as outsourcers whose battlefield capabilities make possible initiatives that they could not otherwise undertake alone – if at all.

Insert Table 1 about here.

As a result of their deep and increasingly well-known involvement in major international and intrastate conflicts, PMCs are the subject of intensive public debate. Kofi Annan, former Secretary-General of the United Nations, decried PMCs and famously declared that they would never be relied upon by the UN – even as member nations such as the United States and the Britain relied upon them routinely. After the 2004 Abu-Ghraib prison scandal illuminated the reliance of US military operations in Iraq on PMCs, the popular media reported extensively on the involvement of PMCs in the conflict. More recently, when it became apparent that US military contracted two PMCs to provide combat training to Georgian Special Forces commandos in the months preceding Georgia's

August 2008 military assault in South Ossetia, the central role of PMCs in US military operations became even clearer. In Britain, a scandal erupted when the media suggested that the British military regularly relied on PMCs to perform operations in Iraq that were illegal under British law.

Public objections to PMCs reflect a range of concerns. For one, the timeless challenge of contracting for private military services is well known: a divergence of incentives around the desirability of conflict itself. Put starkly, PMCs profit from conflict, and thus may not pursue peace even when resolution does not compromise the interests of the contracting sovereign (Shearer 1998). Broader concerns regarding PMCs include the scale, scope and centrality of their roles, the unprecedented limitations on liability they enjoy operating as corporations with enforceable contracts, their adherence to international law and involvement in command decisions, as well as pay differentials between PMC employees and sovereign soldiers. Despite these concerns, proposals to license and regulate PMCs have been rebuffed for fear of further legitimizing their activities. Resolving questions about whether and how to regulate PMCs requires an understanding of why and how they emerged, and why and how they operate in tandem with large hierarchical organizations such as sovereign military forces.

PMCs AS ARCHETYPICAL HYBRIDS

PMCs are archetypal of the hybrid organizational form, accepting assignments that would otherwise be performed or worked around by the hierarchical organizations whose interests they represent. Williamson (1991, p. 2) explains:

“... [T]he hybrid mode is located between market and hierarchy with respect to incentives, adaptability and incentive costs. As compared with the market, the hybrid sacrifices incentives in favour of the superior coordination among the parts. As compared with the hierarchy, the hybrid sacrifices cooperativeness in favour of greater incentive intensity.”

Although transaction-cost theories on the nature of hybrids are as yet developing, five major constructs have emerged as central in their characterization. Williamson (1991) proposes that hybrid

organizations (separate from hybrid transactions) operate under *incentive mechanisms* and *administrative controls* distinctive from those in markets and hierarchies. In later work, Williamson (2005) conceives hybrids as a discrete form of organization with unique characteristics that distinguish them from markets and hierarchies. Building on his (1999) paper, Williamson suggests that hybrids may employ mechanisms of *adaptation and coordination under probity hazards* that are distinct from those of markets and hierarchies. Additionally, in his survey, Menard (2004) discusses *bilateral or multilateral dependency* between hybrids and hierarchies built on *asset specificity* as a defining characteristic. Below we discuss each of these constructs in relation to PMCs.

Incentive Mechanisms

Williamson (1991) argues that hybrid organizations are superior to hierarchies in their incentive intensity, although not as incentive-intense as markets. The identification in contracts of targeted levels of performance shapes the objectives of hybrid organizations, which deploy resources to achieve the stipulated aims. Because hybrids are contractually protected from competition under specified conditions and for particular periods of time, incentives are blunted. This blunting of incentives is required to provide hybrids with sufficient stability to enable administrative coordination (their second characteristic, discussed below).

The intensity of PMC incentive systems is significantly greater than in the traditional hierarchical arrangement of conventional military employment. Pay for performance in PMCs is so attractive as compared to military pay that retired US army personnel have actively formed PMCs or sought out employment from PMCs for duty in Iraq as a lucrative alternative to accepting a voluntary commission from the US Army.¹ The reputation of PMCs is made on effectiveness in achieving objectives, even by taking risks or incurring costs that would not be acceptable to sovereign militaries. The four Blackwater personnel who drove into Fallujah on that fateful day in

¹ PMC employees can earn 5-15 times more than a US soldier; the CEO of a large PMC can earn 10-100 times more than a four-star general in the US Army.

March 2004, for example, were deployed on a reconnaissance and recovery task that would not have been executed with as few personnel or equipment under conventional US military procedures.

In later work, Williamson (1999) suggests that “consummate” performance rather than “perfunctory” performance may characterize hybrids with highly refined incentive structures. Consummate performance occurs when objectives are clear and organizations are unconstrained by administrative protocols. PMCs have achieved consummate over perfunctory performance. PMCs became essential to the sovereign military operations precisely because they could perform functions and operate in geographies where conventional military activity was not possible, timely or efficient. One of the earliest post-Cold War era PMCs, Executive Outcomes, became so notoriously effective that it ultimately disbanded precisely because its reputation became an anchor on the organizations that sought to contract with it.

PMCs often outperform the market in blunting incentives sufficiently to assure coordination both within the PMC and between the PMC and the hierarchical partner, rendering consummate performance that is more efficient than would be possible through market exchange. Imagine that the Angolan government sought to hire each of the former South African Defence Forces (SADF) soldiers employed by Executive Outcomes on the open market. The Angolan government would have had to assure compatibility in the training, command structure, skill base, communication systems and leadership functions of the hired individuals. An advantage of this arrangement according to Williamson’s (1991) theoretical argument would have been each individual’s high-powered incentive to perform consummately. Yet the tasks of coordination would have been daunting, especially for a government already strained to the limit in managing its sovereign military. The viability of hiring retired SADF soldiers – once foes of the Angolan army – would have been at issue. Achieving consummate performance by contracting on performance objectives for the unit represented a major opportunity.

PMCs also demonstrate that contract law in the form of arbitration or litigation may not be required to achieve the level of performance normally associated with market incentives. Rather, reputational capital, developed over time as PMCs perform various missions and accumulate specialized assets, may be sufficient to assure the strength of incentive systems as compared with spot-market contracts for labor. Indeed, contracts with PMCs are often informal rather than only formal – particularly when the PMC is engaged to challenge the sovereign authority of an incumbent government, i.e., when the national rule of law is precisely the subject of conflict. The ability of PMCs to coordinate the deployment of specialized assets, especially in controversial assignments, permits PMCs to achieve greater incentive compatibility than is available through markets.

Administrative Controls

Williamson (1991) indicates that hybrid forms offer superior administrative controls to markets but weaker administrative benefits than hierarchies in the accomplishment of a task. The history of PMCs reflects Williamson's logic. The culture of zealousness – passionate adherence to mission – may be greater in some PMCs than sovereign militaries. PMC personnel tend to ascribe to and reinforce a culture of adherence to mission that rivals and occasionally surpasses sovereign military organizations in intensity. Conformance to military administrative procedure is a hallmark of many PMCs. PMCs offer opportunities for administrative control unavailable in markets, and unconstrained by requirements for documentation, adherence to procedure, and decision rules that typically characterize sovereign military authorities. The strength of administrative controls may thus be enhanced in PMCs as compared to sovereign military organizations because high-powered incentives are embedded within hierarchical structures to create administrative benefits without sacrificing of incentive alignment.

The story of PMCs is, in many ways, a tale of passionate commitment and ideological zeal. Former US generals serving as the chief consultants at MPRI cultivated skills in training and

negotiation precisely because of their personal preferences to avoid armed conflict whenever possible. PMC's founders tend to be tied ideologically to the missions they pursue, services they provide, and renowned for their commitment to the ideals of military discipline and the rigors of military life. The veterans employed by PMCs demonstrate by revealed preference their predilection for service, and while little systematic information is available, anecdotal evidence suggests that some of their discharges may have been encumbered by controversy. Thus, while the conventional customs, rules, command structures, training, and specialization of military hierarchy mark the formal administrative systems of PMCs, making them at least comparable to hierarchy on this dimension of governance, the intensity of commitment to the culture of military life may render administrative controls even more potent in PMCs than in hierarchical military organizations.

Adaptation and Coordination under Probity Hazards

Williamson (1999) discusses the commitment of executing parties to achieve consummate performance as “probity.” Probity refers to the loyalty and rectitude with which the commitment to an objective is discharged. Williamson introduced probity to emphasize the specificity of some extreme transactions including sovereign tasks: “foreign affairs, the military, foreign intelligence, managing the money supply, and, possibly, the judiciary” (1999, p. 321). In such transactions, the sovereign is highly dependent on the professional excellence of the contractor. Failure to achieve agreed-upon objectives may result very large losses for the sovereign. Transactions characterized by probity hazards thus involve stakes well beyond the parameters of the transaction itself, and distinguished by “their needs for loyalty (to the leadership and to the mission) and process integrity” (1999, p. 324). Remedies to probity hazards include loyalty, professional excellence, adherence to principle, procedural safeguards, and social conditioning (1999, p. 323-4).

Probity hazards are extensive in transactions for private military services for many reasons. First, PMCs possess capabilities and a willingness to perform duties that branches of the national

military cannot perform either because of their riskiness or their policy implications (Singer 2003). PMCs are not bound by the same constraints to authority as sovereign forces, and their absence enables heroic, passionate or even zealous execution of duties. Second, reputational capital is tied to both PMCs and the particular individuals in their employ. To the extent it is tied to the corporation, PMCs attenuate the consequences for individuals of probity violations, particularly when PMCs act under the limitations on liability afforded them as corporations. Third, contracts themselves may be difficult to interpret and may not stipulate contingencies that would otherwise guide decisions in the field.² Responding to private incentives rather than executing contractual objectives with “loyalty and rectitude,” subcontractors may make decisions differently from a sovereign’s military forces. In some instances, this may mean that PMCs do not pursue objectives with commitment, as was famously the case when the Condottieri in 10th Century Italy fought against mercenaries in vast numbers, with more than 10,000 troops on each side (Singer 2003). Because all of the troops were hired mercenaries, only a few casualties were incurred as neither side fought with intensity. Fourth, the “loyal and righteous” choice may be difficult to discern because of the multiple facets of the interests of parties to private military contracts. The complexities of the sovereign’s interests alone may not be identified, and confusion may be compounded as field personnel also consider the interests of their employers. Finally, intertemporal movement in interests may further complicate a field officer’s choices. Acting with integrity may mean something different each day. Slow movement of information into the field may thus exacerbate probity hazards.

The probity hazards associated with sovereign transactions expose contracting parties to the potential for poor adaptability and coordination (Williamson 1999). Yet PMCs are hired precisely because of their abilities to adapt and coordinate more readily than is possible within hierarchical

² The presence of probity hazards creates a transactional environment that favors renegotiation. For example, in France, 56% of defense procurement contracts are renegotiated, and such renegotiations cause an average price increase of 4.6% per contract, with some increases reaching 30% (Oudot 2007).

organization or through markets. Probity is associated with greater flexibility and learning than under other transactional forms. Thus, whereas Williamson (1991) anticipated compromises in adaptability vis-à-vis markets and coordination vis-à-vis hierarchies, PMCs as hybrids deliver both more effectively.

For example, after brokering a 1994 agreement between Muslim and Croat factions in Croatia to join forces against Serbian aggressors, the Pentagon referred the Croatian Defence Minister to MPRI, and with US government approval, the company signed a contract with the Croatian government in January 1995 to supply a team of 14 military advisers led by retired US Army Major General John Sewall to train the Croatian army into a NATO-style force that could maintain regional stability. The MPRI contract effectively circumvented a 1991 UN arms embargo (which the US had approved in the Security Council) that prohibited the US from directly selling arms or providing military training and advice to any of the warring parties (Singer 2003).

Bilateral or Multilateral Dependency

A critical facet of the hybrid form of organization is “bilateral or multilateral dependency” in which the buyer and the seller of services are co-dependent. PMCs typically operate in tandem with other interests in pursuit of a unified objective. Even in working alone, however, they may exhibit bilateral dependency as when Executive Outcomes was called upon because of the experience of its former SADF personnel in combat against União Nacional para a Independência Total de Angola (UNITA) rebels in Angola and Namibia, or when MPRI was contracted in Bosnia following its experience in Croatia.

The PMC example also illustrates how bilateral dependency emerges over time. Initially dependent on sovereign military authorities for trained personnel, administrative culture, and contracts, PMCs have developed capabilities that make them equally essential to the operation of sovereigns. Multilateral dependency arises from the co-specialization of PMCs in executing missions

under contract to sovereigns or other authorities. A prominent example arises from the reputations of PMCs. Contracting with PMCs such as Blackwater and Executive Outcomes that became infamous for their field strategies allows sovereigns to signal their intentions. Local combatants may be intimidated, or negotiating parties may be assuaged, for example, by participation of a PMC with a reputation for effectiveness in its domain of operations. Indeed even rumor of a Blackwater or Executive Outcomes contract may suffice to enable a sovereign to achieve certain military objectives. Such bilateral dependencies – with sovereigns dependent on PMCs and vice versa – arose throughout the post-Cold War era.

Multilateral dependency is also a salient feature of PMC operations. PMCs often work collaboratively under contract to sovereigns and in conjunction with secondary subcontractors. As PMCs have specialized by geography and function, and as they have accumulated experience in working together, sovereign nations have increasingly assembled contracts as pieces of a puzzle to accomplish military operations in Iraq and elsewhere.

Asset Specificity

Asset specificity is replete in sovereign military transactions, as the skills, equipment, resources, and relationships necessary for military activities are not normally useful in other applications (McDonough 2005).³

Human capital among PMCs is strikingly strong. The founders and leaders of PMCs typically have backgrounds in sovereign military leadership. Eeben Barlow (Battalion Commander South African Defence Force, retired) of Executive Outcomes, Tim Spicer (Lieutenant-Colonel Scots Guards, retired) of Sandline International (and more recently of Aegis Defence Services), David Walker (Major British SAS, retired) of Control Risks Group, Alistair Morrison (Colonel British SAS, retired) of Defence Systems Limited, and Vernon Lewis (Major General US Army, retired) and Carl

³ Although markets for personal security services are currently expanding rapidly (Singer 2003).

Vuono (General and Chief of Staff US Army, Retired) of MPRI, for example, were not only highly skilled military leaders, but also experienced in the regions in which their firms were subsequently active. PMC personnel are often former members of elite Special Forces units, with training in reconnaissance and analysis of intelligence, accustomed to interacting with foreign nationals, and offering a high level of experience, professionalism and discipline. PMCs often market their services by direct reference to the skills and experience of their principals in military service, especially in elite forces. MRPI, for example, boasts “more generals per square foot than the Pentagon.” Others refer to their effectiveness in particular domains or regions of operations.

Physical capital associated with military applications principally includes protective gear, arms and transportation equipment, although many other forms may also arise. Basic physical capital is typically available on open markets, often inexpensively (Singer 2003). Advanced equipment, definitive in field operations, such as specialized helicopters, night-enabled firearms, and armoured vehicles can be more difficult to procure and expensive, however.

Social capital arises within PMCs and between PMCs and sovereign nations, with these relationships constituting social networks (Powell 1990). PMC personnel have shared operational and combat experience and are often deployed in the battalions that were previously formed for sovereign military operations. Trust and cohesion develop over time among PMC personnel as they complete missions together. Relationships among PMC personnel are central to their effectiveness. So too are relationships between PMCs and sovereign nations. MPRI, for example, was called upon to train troops in Croatia precisely because of the relationships its principals had developed while serving in key positions within the US Armed Forces. In addition to strong, often life-long ties with sovereign military leaders, many PMCs are located in national capitals and near military installations, permitting their leaders to continue to participate in the same professional and social circles. The social capital developed in these networks shapes and is further shaped by the transactions

undertaken by the PMCs in conjunction with and on behalf of sovereigns (Granovetter 1985).

Relational capital and reputational capital are also essential to the effectiveness of PMCs in achieving transactional outcomes that are not possible through either markets or hierarchies. Relational capital, identified by Baker et al. (2002) as “informal agreements sustained by the value of future relationships,” are a central facet of the connections between PMCs and their clients. The accumulated stock of informal relations struck through contracts over time is central to the profile of effective PMCs. As PMCs develop relationships with sovereign governments, they come to embody specific knowledge (in the sense of Kogut and Zander 1993) that leads them to become preferred partners for sovereign authorities, and to the accumulation of specific skills for performing functions in particular geographic and/or technical areas that makes them essential to particular operations. Concomitantly, PMCs accumulate reputational capital that can both enhance and stymie their effectiveness in writing and executing contracts (Klein, Crawford and Alchian 1978; Klein 2007). This reputational capital is embodied in (a) the joint actions of employees that worked together in teams both within PMCs and across PMCs and sovereign authorities, (b) the trademarks, identifiers and brands of PMCs and (c) the detailed knowledge of combatants of PMC operations in conflict settings (i.e., in Angola, the effectiveness of Executive Outcomes became legendary).

The implications for transaction governance of each form of capital are complex. On the one hand, asset specificity tends to create transactional hazards that may make PMCs vulnerable in contracting. On the other hand, large numbers of sovereigns and non-sovereigns seek to contract for private military services, and trust can develop between parties even under incomplete contracts (Mayer and Argyres 2004; Zhou and Poppo 2008). The specialized capabilities of individual PMCs may be particularly valuable in the circumstances of a localized conflict. The value of a PMC’s capabilities also may reflect the simultaneous resolution of multiple transactional negotiations. For example, the engagement of a PMC such as Executive Outcomes for a particular operation may be

viewed as imperative if the opposing force in the conflict has capabilities that only Executive Outcomes has successfully combated in the past. Thus, importantly, transactional possibilities and command-and-control opportunities are defined in part by PMC capabilities.

THE EVOLUTION OF PMCs AFTER THE COLD WAR

The intertemporal development of PMCs as hybrids in the five decades since Eisenhower's speech constituted a path from ad hoc contracting to highly refined corporate entities that ultimately constituted an established industry. How did PMCs create command-and-control opportunities that previously had not been available to sovereign authorities, and how did they come to be charged with command-and-control responsibilities in Iraq, Afghanistan, and elsewhere? Our answer to this question rests on the assertion that the emergence of the PMC industry was shaped by transitions in underlying social, political and economic conditions, including privatization and globalization, after the end of the Cold War. These transitions reflected fundamental changes in 'shift parameters' that over time influenced the relative costs of alternative governance structures in favor of hybrid PMCs' accumulation of capabilities, rather than their integration within sovereign military agencies.

Cold War Era

In the years following World War II, the bipolar Cold War logic dominated military activities. Clear authority, centralized decision-making, coordinated resource deployment, well-defined roles, and the secure passage of information through command-and-control hierarchies were critical to effective military post-war reconstruction and intelligence. Military capability centered on preparation for high-intensity, interstate combat based on highly technical equipment and skills (McDonough 2005). Sophisticated assets such as long-range missiles were located strategically and governed in ways that would facilitate their rapid deployment if necessary. Land, sea and air operations developed based on highly technical platforms for deploying resources on a massive scale. Yet the incidences of their deployment were relatively rare in comparison to the scale of operations (McDonough 2005).

Military organization was designed to deploy these technologies, if they were to become necessary, in highly coordinated responses on a vast scale. Thus, organizational performance was defined principally by coordination rather than by adaptation; incentive structures encouraged adherence to well-defined lines of authority; and administrative structures became legendary for their bureaucracy. The Cold War regime was thus associated with an extraordinary strengthening of hierarchical, sovereign military institutions, as would be suggested by Williamson (1991).

Some of the most important military assets that developed during the Cold War, particularly weapons platforms and transportation systems, rested on technologies that had been developed in the private sector. Before WWII, the primary role of private contractors such as Booz Allen Hamilton and Vinnell Corporation was to provide logistical support such as transportation, medical services, and provisioning. During the Cold War, the increasing technical complexity of military equipment and hardware led the military to rely increasingly and to develop close relationships with contractors such as DynCorp, Northrup Grumman, and SAIC as technical specialists working side-by-side with deployed military personnel. Throughout this period, military subcontracting for interstate conflict tended to be highly specialized and technical, involving the provision of circumscribed sets of services that were deeply embedded within sovereign military agendas. Clear lines of authority, rigorous training processes and highly centralized decision systems were vital to subcontracted military processes. The introduction of sophisticated information technologies into field operations amplified the complexity and diversity of military hierarchies enabling coordination and communication at many levels: geographic, cross-functional, and inter-organizational.

During this period, the first corporate ventures formed with the express purpose of selling military services began to appear. Among them was WatchGuard International, established in 1967 by Sir David Sterling, founder of the British SAS. Employing former British SAS personnel, the company's mission was to safeguard British interests by providing military services and advice,

security for heads of state, and Special Forces training to developing countries, particularly in Africa and the Middle East. It attempted to formalize its relationship with the British government, which was known to contract with private forces to support its foreign policy and Colonial interests, by committing to providing its services only with government consent (Kinsey 2006). By 1970, however, it had become clear that the formality of the relationship made government deniability of covert actions undertaken on its behalf by WatchGuard impossible. Watchguard had achieved a reputation that barred some kinds of sovereign contracts despite – and even perhaps as a result of – its effectiveness in executing them. Seeking profits elsewhere, Watchguard sought and found customers in emerging multinational corporations (MNCs) that sought to develop in the same geographic areas where the company had operational expertise. Thus, the organization’s reputation and other specialized assets were transferred into a new market.

This pattern emerged as characteristic for PMCs. Initially seeking contracts from sovereign military authorities, successful firms often later broadened their customer bases to include MNCs, particularly those in resource extraction industries and/or operating in developing countries. These companies sought out PMCs to provide solutions for their security and intelligence needs, which in turn encouraged the formation PMCs structured as corporate entities to limit their liability (Kinsey 2006). In the UK, these included Control Risks Group, established in 1975 by former British SAS Major David Walker, and Defence Systems Limited, formed in 1981 by former SAS Colonel Alistair Morrison, and in the US, Kroll, founded in 1972 by Manhattan Assistant District Attorney Jules B. Kroll. Although such firms also took on government contracts to train foreign militaries, this fact was not widely publicized to avoid media scrutiny and public opposition (Kinsey 2006).

Thus, even before the end of the Cold War, a precedent had been established for the formation of PMCs reflective of and symbiotic with sovereign military hierarchies. These firms implemented administrative systems designed to meet the particular requirements of the large

organizations they served. Incentive systems tended to reflect the pay schemes of the military except for owner-founders, who quickly came to profit, often handsomely, from their ownership shares. Performance was judged principally on criteria that emphasized effective coordination with the large organizations that were the principal buyers of PMC services.

Post-Cold War Era: Berlin to Mogadishu

The end of the Cold War, marked by the fall of the Berlin Wall in 1989 and the disbanding of the Soviet Union in 1991 brought deep cuts in military budgets and an end to massive permanent troop deployments in Europe, the US, and the Soviet Union. Deployments also withdrew from African and Middle Eastern countries as well as from republics that broke from the Soviet Union in December 1991.⁴ The SADF also downsized at roughly the same time as the conflict waged in Angola and Namibia ended, and the two-year National Service requirement phased out. Downsizing was reinforced by the economic ideology that rose to prominence during the Reagan-Thatcher era, which, based on the idea that the market could deliver public services more efficiently, saw government functions, from power generation to transportation to prisons, privatized. Many countries followed downsizing with armed forces professionalization, replacing conscripted forces with more expensive all-volunteer forces, and increasing further demands for leaner and less expensive armed forces.

A primary impact of the end of the Cold War was thus the unemployment of a large number of military personnel, many of whom had specialized technical skills, and all of whom shared a familiarity with the administrative culture and systems of sovereign militaries. This massive wave of unemployment was accompanied by the disposal of large caches of arms, specialized transportation

⁴ US military troops, for instance, declined from 2.1 million in 1989 to 1.3 million in 2001 (US Department of Defence, Directorate for Information Operations and Reports). Other NATO countries conducted similar reductions. The Soviet Union/Russia declined from 5.2 million in 1987 to less than 1.0 million in 2001. Worldwide troops fell from 11.9 to 6.0 million in developed nations and from 17.0 to 14.7 million in developing nations (U.S. Department of State).

equipment and armed vehicles onto open markets. Surplus military equipment also became available with the de-militarization of Europe and the collapse of the Soviet Union.⁵ Breakaway republics, in particular, eagerly sold former Soviet military assets to obtain foreign currency to bolster their faltering economies, resulting in unprecedented availability of sophisticated military equipment, including the versatile fleet of Soviet helicopter transport and gunship aircraft. Soviet AK-47 assault rifles were available on secondary markets for a few hundred dollars; used tanks and aircraft for a few tens or hundreds of thousands of dollars.

At the same time as the skilled personnel and armaments and equipment became available to form PMCs, a new type of demand for their services began to emerge. Beyond dealing with the new distribution of power, one of the great challenges facing developed nations was to decide how to respond to the revolutionary and ethnic civil wars multiplying in developing and newly independent regions that had previously been a battleground of the Cold War, where fragile states, absent their Cold War patrons, struggled to maintain security and control. As Figure 1 illustrates, while the threat of interstate conflict declined during the post-Cold War period, intrastate conflict escalated.

Insert Figures 1-3 about here.

These new intrastate conflicts differed notably from prior interstate conflicts.⁶ Although more frequent, intrastate hostilities were more limited in geographic scale, entailed localized combat between untrained and poorly equipped forces, and so generated fewer casualties than in interstate conflicts. Figures 2 and 3 illustrate the trend in conflict intensity, by region, over the period. As the

⁵ Unwanted arms at the end of the Soviet-Afghan war, for example, transformed northwest Pakistan into a regional arms trading center where buyers could choose from Chinese, East European and Israeli arms, as well as stocks of captured Soviet arms (e.g., rocket-propelled grenade launchers and AK-47s), and locally-produced cheaper arms (Phythian 2000).

⁶ These conflicts blurred “the distinctions between war (usually defined as violence between states or organized political groups for political motives), organized crime (violence undertaken by privately organized groups for private purposes, usually financial gain) and large-scale violations of human rights (violence undertaken by states or politically organized groups against individuals ... [and between] “internal and external, between aggression (attacks from abroad) and repression (attacks from inside the country)” (Kaldor 1999, p. 2).

figures show, the number of conflicts resulting in more and less than 1,000 deaths per year (both military and civilian) increased steadily during the Cold-War, but in the years immediately following the end of the Cold War, conflicts resulting in more than 1,000 casualties fell substantially, while those resulting in fewer than 1,000 deaths continued to rise. Despite their smaller absolute tolls, these intrastate conflicts were brutal, with combatants frequently disregarding established rules of war, committing atrocities against non-combatants, and precipitating **large-scale** humanitarian crises.

These developments revolutionized how Western countries responded militarily. Sovereign deployments shifted away from permanent installations and toward engagement on a temporary, 'as needed' basis to represent state interests in interstate conflict and to aid in the de-escalation of intrastate conflicts when they arose. Interventions typically required specialized capabilities in peacekeeping, crisis response, security, forces training, and pre-emptive negotiations as well as, and often rather than, combat. Small deployments were the norm with operations highly divisible and 'contractible' and with performance often judged on the achievement of military objectives rather than on the execution of functions – an emphasis on adaptation rather than coordination. Timelines for responding to incidents were also relaxed, with many characterized by ramp-up periods of several months or more rather than the hours, days or weeks for planned responses during the Cold War. Flexible, small-scale approaches became critical to military effectiveness, while massive land-sea-air operations based on permanent troop deployments and highly technical weapons platforms became obsolete (Fredland and Kendry 1999). Quick adaptation to shifting conditions became a hallmark of successful military action in this environment.

Initially, Western nations seemed prepared to engage their downsized militaries cooperatively to resolve regional ethnic and nationalist conflicts and aid humanitarian disasters, for example, launching international interventions in Northern Iraq and the Balkans in 1991 and Somalia in 1992. In this environment, however, the hierarchical bureaucratic structures essential for the efficient

deployment of high-technology weaponry during the Cold War constrained flexibility. American and British militaries were unable to marshal the kinds of detailed, on-the-ground knowledge necessary to succeed in combat operations in these settings. No longer did strategies based on the deployment of state-of-the-art technology succeed. Western troops were neither trained nor equipped for low-intensity civil wars, involving complicated ethical agendas, blurred boundaries between combatants and civilians, and loose military hierarchies.

The mismatch of sovereign military capabilities became vividly evident during an October 1993 incident in Mogadishu, Somalia, where US forces, relying on technically sophisticated armaments but little local knowledge famously and tragically failed in a mission to secure a strategically important area of the city, resulting in the deaths of 18 US military personnel and wounding of another 73. Mogadishu marked a turning point. What had become clear was that type of specialized knowledge most relevant to the success of military missions in intrastate warfare was detailed understanding about local context, issues and capabilities.

Post-Cold War Era: Filling the Security Vacuum

Developed nations were hampered by administrative structures that were not designed for the quick, locally tailored responses required to succeed in the ethnic and revolutionary intrastate conflicts proliferating in the developing world. Sovereign military structures were unable to adapt quickly to changing local circumstances. And the incentives for participation in intrastate conflicts were complicated by unresolved questions about the macro- and micro-political interests previously defined under the relatively simpler bipolar alliances forged during the Cold War. After Mogadishu, the US, and Western nations more generally, refrained from deployments in regions deemed not essential to their national interests, such as in Rwanda in 1994.⁷ Instead, Cold War presence, commitment and solidarity were replaced by a policy of active disengagement and arguments in

⁷ In Rwanda, the US expressly decided against deploying its forces too thinly across multiple fronts (US President Bill Clinton later stated regret for his decision to conserve forces for use in Bosnia-Herzegovina).

favor of localized responsibility for peace, security, and economic development (Avant 2005).

Unable to clearly define their interests or to mount armies effectively in intrastate conflict, the ambivalence of Cold-War-era sovereign authorities created a vacuum in security and policing in conflict areas. This, in turn, created opportunities for PMCs to contract directly with developing states to provide security details and even combat forces. Unlike their sovereign counterparts, PMCs were typically willing and able to become involved directly in the intrastate conflicts of developing nations that erupted as the Cold War ended. Thus, for fragile states lacking support from the great powers and unable to field sufficient armed forces to provide security for their citizens, PMCs provided a means of reaffirming political control and some semblance of order. Indeed, as Kinsey (2006, p. 60) notes, it is not surprising under these conditions that “governments decided to employ private forces to fight on their behalf.” Despite the considerable hold-up and probity hazards associated with such contracts, in a world in which revolutionary and ethnic groups and military coups frequently overthrew governments, there were few alternatives.

Combined with availability of skilled military personnel and surplus military equipment, this demand prompted a wave of PMC founding. Among the first to exploit conflict opportunities emerging at the end of the Cold War was Executive Outcomes (EO). EO was founded by in 1989 by Eeben Barlow, former SADF Battalion Commander, with its personnel tending to have the same background. Initially established to provide intelligence training to SADF Special Forces, with the end of Apartheid, it began to conduct security and intelligence operations in Angola, Botswana, and Namibia for De Beers and other South African mining companies in the early 1990s. EO carried out its first major military operation in Angola in 1993. The company was hired on behalf of the Angolan government by Anthony Buckingham, a senior advisor to several North American oil companies. Their objective, to recapture and defend oil reserves at Soyo from UNITA rebels, was accomplished with 24 well-trained and equipped troops and three armoured helicopter gunships.

EO's performance resulted in a \$40 million contract with the Angolan government to train and supply weapons to government troops and provide protection against UNITA. Shortly after the contract was renewed in 1994, government troops' success forced UNITA to sign a peace accord with the Angolan government. Singer (2003) offers evidence that EO's success led to its control by a group of British-based entrepreneurs (including Buckingham) who established a consortium of related military companies (e.g., Alpha 5, Bridge International, Saracen International, Shibata Security, Teleservices International, Lifeguard, Ibis Air) and resource extractions enterprises (e.g., Branch Energy, Heritage Energy, Ranger Oil, DiamondWorks).

EO's success in Angola convinced the government of Sierra Leone, in collaboration with Branch Energy, which had significant mineral interests in the country, to enter into a \$35 million contract with EO in April 1995 to provide military support and advice to its army. Since 1991, Sierra Leone had sought military assistance from Britain to contend with the Liberian-backed Revolutionary United Front (RUF) with which it was embroiled in a deadly civil war. Although its ties with Britain were strong (the British Navy used Sierra Leone's capital city, Freetown, as a staging port during the Falklands War), the British Ministry of Defence declined the request. At this point, Sierra Leonean government officials and army officers turned to PMCs for help.

Initially, Channel Islands-based Gurkha Security Group (GSG), comprised of former British Army Gurkhas, was contracted. Despite their fierce reputation, GSG refused to accompany the army in operations and failed to improve the security situation. Then, in February 1995, 20 Gurkha troops and their Canadian commander were killed in a RUF ambush; the remaining Gurkhas left shortly afterward (Avant 2005). When EO arrived in May 1995, RUF forces were within 20 kilometres from Freetown. By January 1996, EO had secured the capital city, regained control of the country's diamond fields, and destroyed RUF headquarters (Kinsey 2006). Former UN diplomat, Tejan Kabbah, was elected president the next month, and signed a peace agreement with

the RUF in November 1996. A key provision of the agreement inserted at RUF's insistence was that EO would depart by January 1997. In May 1997, with support of the national army, Major Paul Koroma led a successful coup and joined forces with the RUF.

Thus, PMCs were not only integral militarily to developments in the region, but through reputation, relationships and allegiances had a major impact on economic and political stability. A turning point had occurred, with PMCs generating command-and-control options through their relational and reputational capital and detailed organizational knowledge. Military options that had not previously been conceived became possible.

Post-Cold War Era: Implementing Foreign Policy

By the mid-1990s PMCs had established themselves as viable commercial ventures and carved a niche for their services among leaders of developing countries facing internal political crises and threats to their authority.⁸ Developed nations benefitted greatly from these arrangements, which, by improving security in developing regions, helped protect their commercial interests and maintain the flow of key resources. Western leaders expressed little opposition to PMCs because their activities limited the need to put sovereign troops in harm's way when national interests were not clearly at stake (Kinsey 2006). PMCs were thus performing services that governments (tacitly) approved of, but hesitated to do themselves because of political, military or financial costs.

Along with the continued emphasis on force reductions and privatization to cut costs, these benefits appear to have prompted the Western governments, particularly the US, to begin using PMCs to promote their foreign-policy agendas. PMCs enabled governments of developed nations to succeed in conflicts by reducing the engagement timeframe and even by avoiding troop deployment altogether. When Western countries did become embroiled in unpopular conflicts, PMCs could serve as 'force multipliers' enhancing sovereign forces' effectiveness by freeing them to

⁸ As well as MNCs seeking protection for their oil and mineral extraction facilities and reserves, and NGOs and IGOs combating humanitarian crises resulting from the conflicts.

focus on core activities. PMCs also enabled governments to circumvent constraints on military activity, either self-imposed (e.g., Congressional limits on troop deployments in the US) or by international agreement (e.g., UN embargos).

The US reliance on PMCs reached a turning point with interventions in Bosnia, Croatia, and Angola in 1995. Military Professional Resources Inc. (MPRI) was founded in 1989 by retired US Army General Vernon Lewis, and joined in 1993 by General Carl Vuono, who, as US Army Chief of Staff from 1987-93, oversaw operations in the first Gulf War. MPRI was established to provide defence and security training, organizational expertise, and leadership for US interests. With US government approval, the company signed a contract with the Croatian government in January 1995 to train an army into a NATO-style force that could help maintain regional stability vis-à-vis Serbia in the Yugoslav civil war. The MPRI contract effectively circumvented a UN embargo prohibiting provision of military support to any of the warring Balkan countries, enabling the US to pursue its policy of creating a counterbalance to Serbia in the region.

In August 1995, the MPRI-trained Croatian army broke the UN ceasefire, launching an offensive that provided the first major victory against the Serbs. The triumph had a major impact on the outcome of the war, leading to the Dayton Peace Accord in November 1995 (Singer 2003). As part of that accord, MPRI signed a similar contract with the Bosnian government. Also in 1995, as part of a US government deal with Angola, MPRI won a contract to train a Rapid Intervention Force – a contract previously held by EO. Since then, MPRI has worked extensively for the African Crisis Response Initiative, a US program to improve the military strength of the African countries of Senegal, Malawi, Benin, Mali, and Kenya.

These developments marked a significant turning point. PMCs had translated their experience in developing countries into capabilities that were unavailable elsewhere. Rather than developing states contracting directly with PMCs for combat-related services, Western governments

were now contracting with PMCs to train and equip developing states' military and security forces. PMCs thus became an instrument of Western foreign policy, working to improve the military capabilities, and thus security and stability of developing countries. Proponents of PMCs pointed to their efficiency: By contracting PMCs on a contingency basis, sovereigns could increase flexibility and focus on core capabilities simultaneously. This 'just-in-time' logic reversed of the traditionally espoused 'just-in-case' logic reflected in such military practices as stockpiling and mothballing (Spearin 2005). The implications of this new logic were not lost on observers, who noted that, while PMCs had historically depended on developed nations for human, organizational and reputational capital, these new contracts revealed the emerging dependency of Western sovereigns on PMCs.

Although outsourcing is less deeply rooted in British military history, Britain too began to deploy PMCs in support of its foreign policy during the mid-1990s. Consistent with its covert use of private force to support its interests during the Cold War, this involvement was not as evident as in the US. As Kinsey (2006, p. 64) explains, the British Foreign Office had a list of companies deemed competent to carry out specialized or general military training. If a politically sensitive request for military assistance were received, the Foreign Office might ask one of these PMCs to take it on.

Exemplary of such activity was Sandline International's 1997 contract to assist Sierra Leone's exiled President Tejan Kabbah return to power. Sandline was formed in 1996 by Tim Spicer, retired Lieutenant-Colonel in the Scots Guards and a former EO employee, to supply military and security services to governments and multinational organizations. The Kabbah contract stipulated creation of a military force in Nigeria to repel the junta from Freetown and the Kono diamond fields. In addition to enhancing the Nigerians' combat capability, Sandline was to supply weapons, mortars and ammunition purchased from Bulgaria. In exchange for mining concessions, a group of investors with mining interests in Sierra Leone, agreed to cover the contract's cost. The operation, which aimed to restore a democratically elected government recognized by the British government, was

undertaken with support from the British High Commissioner, senior civil servants, and thus, Sandline believed, approval of the Foreign and Commonwealth Office of Great Britain.

In 1998, however, a British investigation began into whether the arms supplied by Sandline were in breach of a UN arms embargo against Sierra Leone. Now known as the ‘arms to Africa’ affair, the controversy, which stemmed from confusion over whether the UN embargo applied to the government in exile, resulted in a lengthy investigation into allegations that the British government had been complicit in the illegal supply to Sierra Leone through Sandline. This and other investigations, which ultimately cleared Sandline (see Kinsey 2006 for further discussion), were critical to formalizing the place of PMCs in British combat and military support operations, and to fostering a more transparent relationship between the British government and PMCs. They also contributed to Sandline’s demise, its reputation irreparably tarnished by the public controversy.

By the end of the 1990s, IGOs (independent government organizations such as the United Nations), and NGOs (non-governmental organizations such as Oxfam) were also coming to rely on PMCs to support their activities because they too found it increasingly difficult to maintain the security of their personnel and to execute humanitarian and disaster relief efforts in conflict and unstable regions. The British PMCs ArmorGroup, Global Risk Strategies and Northbridge Services Group, and the American PMC, Kroll, for example, operate under contract with numerous IGOs, including UN agencies, USAID, the ICRC, as well as a NGOs, including the International Rescue Committee, CARE, Caritas, and the World Wildlife Federation (Schreier and Caparini 2005).

Figures 4 and 5 show the rise and diffusion of PMCs during the Post-Cold War period. By 2006, more than 200 PMCs were operating on every continent except Antarctica. The figures show that, while the phenomenon of a rising PMC industry was rooted in the 1970s, the number of PMCs increased steadily after the Cold War ended, and sharply after the 9/11 attacks on the World Trade Center and the Pentagon. The figures also show that most PMCs are based in the US, Britain, the

Middle East (mainly Israel) and Africa (mainly Angola and South Africa). Their locations reflect, in part, the concentration of excess military capacity either available or created by the end of the Cold War in these regions. Figures 6 and 7 show that the number of PMC operations (i.e., contractual engagements) increased concomitantly, first in Africa, after the end of the Cold War, then in Europe after the fall of the Soviet Union, but most dramatically after in the Middle East after 9/11.

Insert Figures 4-7 about here.

Post-Cold War Era: 9/11 to Iraq

Since 9/11, the number of PMCs working for the US Departments of State and Defense increased notably, escalating the interdependence of US military forces and PMCs. Consider, for example, that during the first Gulf War, the ratio of military troops to contractors was 50:1. By the second Gulf War it reached 10:1, with much of this increase resulting from contracts for the provision of military security and intelligence services by PMCs (Singer 2003).

Increases in the number of PMC personnel were accompanied by a dramatic rise in the scope of outsourced activities – with the controversial and unprecedented subcontracting of command-and-control decisions and mission-critical responsibilities. In Iraq, the US military relied on PMCs to, among others things, run the Combined Air Operations Center, target precision guided missiles, operate biological and chemical detection systems, fly unmanned Predator and Guardrail surveillance aircraft, and operate the 4th Infantry Division’s digital command-and-control systems (Isenberg 2004). Camp Doha in Kuwait, which served as the launch-pad for the US invasion in Iraq, was built, operated, and secured by PMCs (Schreier and Caparini 2005).

After the initial combat operation, US and British reliance on PMCs increased further still. KBR, former division of energy firm Halliburton, provided critical logistical support. Northbridge Services Group, a British PMC staffed by former CIA, SIS and Special Forces personnel, provided intelligence and counterintelligence services. CACI International and Titan Corporation provided

civilian interrogators and interpreters to the Abu Ghraib prison, where contractors worked closely with military police and intelligence detachments. The British Department for International Development (DFID) employed British PMC Control Risks Group to provide strategic intelligence advice. MPRI trained US soldiers to run convoys on supply routes vulnerable to ambushes, roadside bombs, and land mines. Vinnell was contracted to train up to 35 Iraqi battalions of 1,000 troops each, having experience in just such an activity in Saudi Arabia during the late 1970s. DynCorp recruited, trained, equipped, and sustained a 700-member US contingent responsible for training and equipping a 135,000-member Iraqi police force. The British Foreign Office and DFID awarded British PMC ArmorGroup control of the Iraqi police mentoring program in Basra.

Finally, and most visibly, the security challenge of the post-war insurgency in Iraq created unprecedented demand for PMCs to protect civilian officials and reconstruction workers as well as military and nonmilitary buildings, infrastructure and convoys. The Office of Reconstruction and Humanitarian Assistance (ORHA) and its successor, the Coalition Provisional Authority (CPA), contracted Control Risks Group for risk assessments and security support. American PMC Custer Battles and British PMC Olive Security were contracted to provide security for reconstruction firms including Bechtel, General Electric, and Fluor (Isenberg 2004; Schreier and Caparini 2005). US-based Blackwater guarded L. Paul Bremer, the head of the CIA, and John Negroponte, the US Ambassador to Iraq, among numerous others. Johannesburg-based Erinys International was hired to defend oil sites and pipelines, as well as to recruit and train 14,000 Iraqis to aid in performing the duties. British PMC Aegis Defence Services, launched by Sandline founder Tim Spicer, was contracted by the CPA to provide security on all major Iraqi government projects following the handover of sovereignty. As noted earlier (see Table 1), Aegis was also central to establishment of the Iraq Reconstruction Corporation, which was staffed jointly by PMCs and military personnel.

Thus, by start of the second Iraq war, PMCs had become regularized as an integral part of

developed nations' military operations, and essential to the achievement of their military objectives. The administrative systems of PMCs and sovereign nations had become deeply intertwined. Mutual interdependency had escalated dramatically, with such deep expertise embedded in various PMCs that sovereign agencies including the US Department of Defence and British Ministry of Defence relied upon them for command-and-control operations and mission-critical support, as well as critical security and policing functions. The achievement of both coordination and adaptation without compromise depended on deployment of PMCs, particularly on missions that might prove controversial, difficult or dangerous to conventional military forces. Military strategy itself had thus become shaped, in part, by the capabilities available through PMCs, and the relationships that had emerged between PMCs and US and British military command central to their roles in modern conflict. The hybrid operations of PMCs had emerged fully as Western militaries sought to fill gaps in their expertise, and free their limited sovereign forces to focus on core activities.

IMPLICATIONS

Our analysis raises several questions for the transaction-cost literature and points to the opportunities for enriching theory in the field of strategic management by integrating insights from the transaction-cost literature with those from the agency and capabilities literatures. First, as hybrid organizations, PMCs not only minimize transactions costs, they also maximize possible transaction outcomes. By deploying PMC capabilities in particular settings, otherwise inconceivable military objectives become possible. The objectives of PMC transactions are thus endogenous.

Second, the markets in which PMCs interact with sovereign governments and other actors themselves emerged endogenously and dynamically after World War II. In part, these markets emerged as new kinds of transactions became possible because of particular PMC capabilities, and in part, they developed in response to shifting institutional conditions and national interests after the Cold War. Initially, as military assets were released by the downsizing of sovereign militaries, early

PMCs formed to acquire and redeploy them for profit. With time, PMCs developed specialized capabilities deployed in tandem with the specific assets co-created with sovereign military hierarchies, leading to an increased formalization of PMCs, and institutionalization of markets for PMC services.

Third, PMC capabilities are specific assets in the sense of organizational economics (Williamson 1975), and have become the fulcrum of the interdependency between PMCs and the sovereign agencies that purchase their services. Bilateral dependencies between PMCs and sovereign governments that have emerged over time that define the hybrid status of PMCs have thus also emerged endogenously. Whether and how PMCs interacted with hierarchy and markets was shaped by the specific assets that developed over time in sovereign militaries, markets, and PMCs as a result of shifting historical circumstances after the end of the Cold War. So too are the relational, reputational, and social capital that PMCs have accumulated an artefact of these historical circumstances. Today, these PMC assets are themselves an instrument of war: Merely contracting with a particular PMC can provoke a response in the enemy.

Fourth, the social capital flowing back and forth across PMCs and sovereign military authorities was critical to mitigating transactional hazards and enabling hybrids to steward unique capabilities essential to the achievement of military goals by sovereign authorities. The former military leaders operating PMCs such as Watchguard, Sandline and MPRI, were trusted implicitly within sovereign military hierarchies. One of the most interesting facets of the development of PMCs is the social embeddedness of their transactions (Granovetter 1985). The social capital of PMCs makes possible transactions that would otherwise be untenable for sovereign states.

Fifth, the coevolution of specific PMC capabilities, markets, and transaction goals demonstrates that the goals, constraints and parties to a transaction are all endogenously determined by historical and dynamic circumstances. Our analysis illuminates how the overall architecture of

assets, capabilities, resources and skills simultaneously induces both the structure of governance and the performance of institutions. PMC governance, including its incentive systems, administrative structures, adaptive capabilities and capacity for coordination (Williamson 1991) were not ‘designed’ to achieve a desired balance of adaptation and coordination at the lowest possible transaction cost. Nor were they optimized based on the specific requirements for performance in a single situation given the established levels of asset specificity at a particular point in time. Instead, the governance of private military activities emerged through a constrained development process, shaped both by established administrative structures and broad historical trends such as the, emergence of globalized MNCs, legitimation of privatization, and political resistance to conscription. PMCs were forward-looking as well as constrained by history in the way that they developed.

Sixth, the organizational economics literature emphasizes that varying approaches to contract enforcement apply to markets, hierarchies and hybrids. Williamson (1999) specifically associates litigation with markets, forbearance with hierarchies, and arbitration with hybrids. In the case of PMCs, these distinctions break down as no sovereign authority may be available to enforce contracts. Instead, our analysis indicates that contracts involving PMCs are enforced by reputational concerns that carry weight because they seek to interact with sovereign authorities and other parties in multiple contexts and over time. The rapid demise of Blackwater following its expulsion from Iraq for “improper conduct and excessive use of force” illustrates vividly the critical role of good reputation; whether Blackwater’s successor, Xe, can escape its shadow remains uncertain. Thus, the integrity of individual transactions involving PMCs depends on the prospect of future transactions involving the principals engaged by PMCs, regardless of whether these principals are employed by the contracting firm.

Finally, our analysis raises questions about how to identify and define hybrid forms. Based on criteria currently available within transaction-cost theory, PMCs are hybrids, and yet the

endogeneity of many elements of the transaction system indicates that mechanisms of governance across markets, hybrids and hierarchies are mutually determined. Hybrids are not compromises between markets and hierarchies that minimize transaction costs; they can *outperform* both markets and hierarchies in adaptation, coordination, incentive and administrative characteristics. The transactions enabled by hybrids may be explained by social networks (Powell 1990), and yet our analysis suggests that the networks of interrelated military personnel employed both by PMCs and sovereign states are endogenously shaped through the evolution over time of the hybrids. Hybrid performance depends both on environmental characteristics and on the path by which capabilities develop within hierarchies, hybrids and markets.

CONCLUSION

The core of our contribution is an argument that PMCs evolved as hybrid organizations through a series of broad institutional shift including privatization, globalization, and foreign policy since the end of the Cold War in 1989. We chronicled the development of PMC governance since the Cold War illustrating, as Eisenhower foreshadowed, that PMCs have accumulated expert capabilities that can be uniquely deployed to pursue objectives under high-powered incentives that are not available through sovereign military organizations. The trust, relational capital, leadership, and formal governance that has accumulated over time between PMCs and sovereign military authorities, together with the battlefield capabilities uniquely available through PMCs, has made them central to military operations of the United States, Britain and other nations (e.g., Australia and Canada). An implication for further research is the potential role of hybrids as bridges between established institutions and newly institutionalized industry structures

Our analysis points to the need in the field for an intertemporal theory of transaction governance in general, and hybrid organizational forms in particular, that draws on theories from organizational economics in parallel to and integrated with a dynamic theory of capabilities (e.g.,

Helfat and Lieberman 2002, Agarwal, Audretsch and Sarkar 2007, Eisenhardt and Martin 2000, Helfat 1997, Teece Pisano and Shuen 1997, Winter 2003) to understand how markets, hierarchies and hybrids emerge as mechanisms governing exchange. Such an understanding depends neither exclusively nor even principally on the design of incentive systems and administrative control systems in the interests of transaction performance. Rather, elements of governance are shaped by prior governance systems inherited from regimes with different performance goals, cultural imperatives, social structures and institutions (Helfat and Lieberman 2002). Relational, reputational and social capital appears particularly important specific assets in hybrid organizations that shape the very nature of transactions as well as influence the costs of transacting through hybrids (Agarwal Audretsch and Sarkar 2007, Eisenhardt and Martin 2000). Thus, as Williamson (1991) observed, but few have acknowledged, transaction-governance systems are embedded in a larger scheme of organizational, institutional and environmental factors such as the urgency of the US after 9/11 in pursuing its military goals in Iraq, the general legitimacy of privatization, and the accumulated reputational capital of PMCs in particular functional areas.

Were Eisenhower's concerns justified? Our analysis suggests that public policy has become, at least in part, shaped by the operation of private institutions, including PMCs and the markets for subcontracted services, where incentive incompatibilities and probity hazards are legion. Yet control is not in the hands of a technological and scientific elite who seek to craft public policy for private benefit. Science and technology is not at the forefront. No individual or group of individuals is in charge. Instead, our analysis points to the operation of markets themselves – the confluence of excess supply thrown off by the end of the Cold War and excess demand resulting from shifting institutional and foreign policy regimes – promoted extensive privatization of military services, including command-and-control operations. Avant (2005, p. 6) explains that “in effect, the shift to private guardians changes who guards the guardians.” With the market guarding the guardians,

public policy is not controlled by an elite, but, rather, by the interplay of supply and demand. The effective regulation of PMCs as a major global industry depends on an enriched understanding of the organizational, institutional and environmental context through which PMCs built capabilities, acquired legitimacy, and developed as hybrid organizations from relatively small subcontractors to large, strategically central partners in war.

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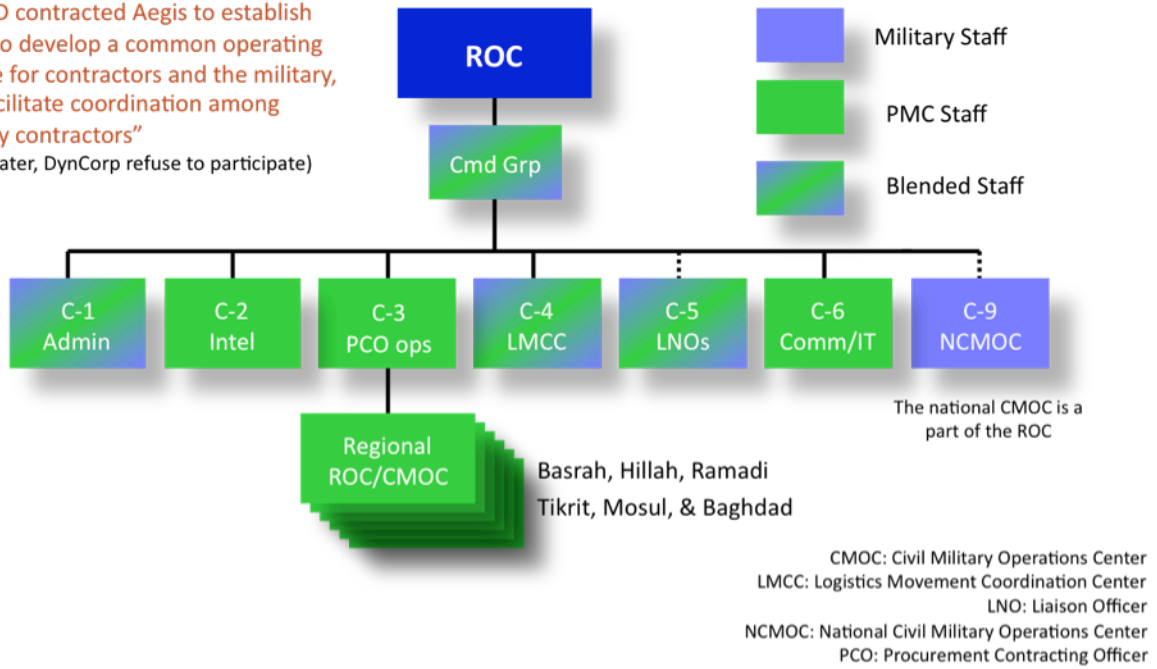
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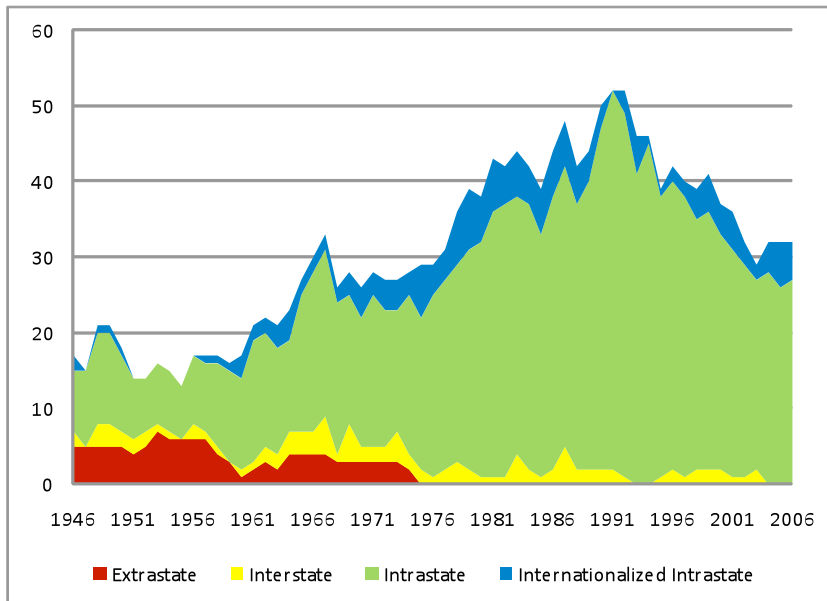
Table 1: Iraq Reconstruction Corporation Operations Center

US DoD contracted Aegis to establish ROC "to develop a common operating picture for contractors and the military, and facilitate coordination among military contractors"
(Blackwater, DynCorp refuse to participate)



Source: Col. Christopher T. Mayer, Chief of Staff, Defense Reconstruction Support Office

Figure 1: Global Conflicts



Source: Department of Peace and Conflict Research at the University of Uppsala

Figure 2: Global conflicts with more than 1000 deaths

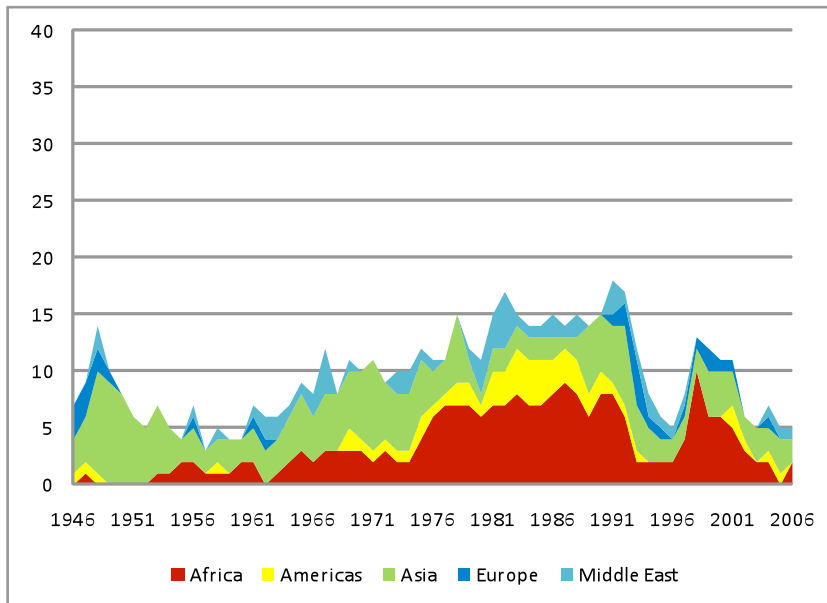
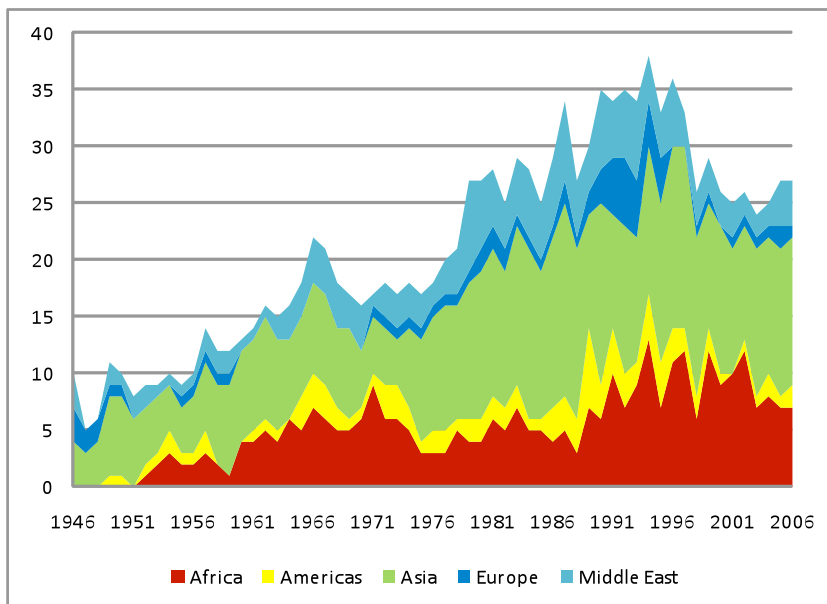


Figure 3: Global Conflicts With Less than 1000 Deaths



Source: Department of Peace and Conflict Research at the University of Uppsala

Figure 4: Number of PMCs

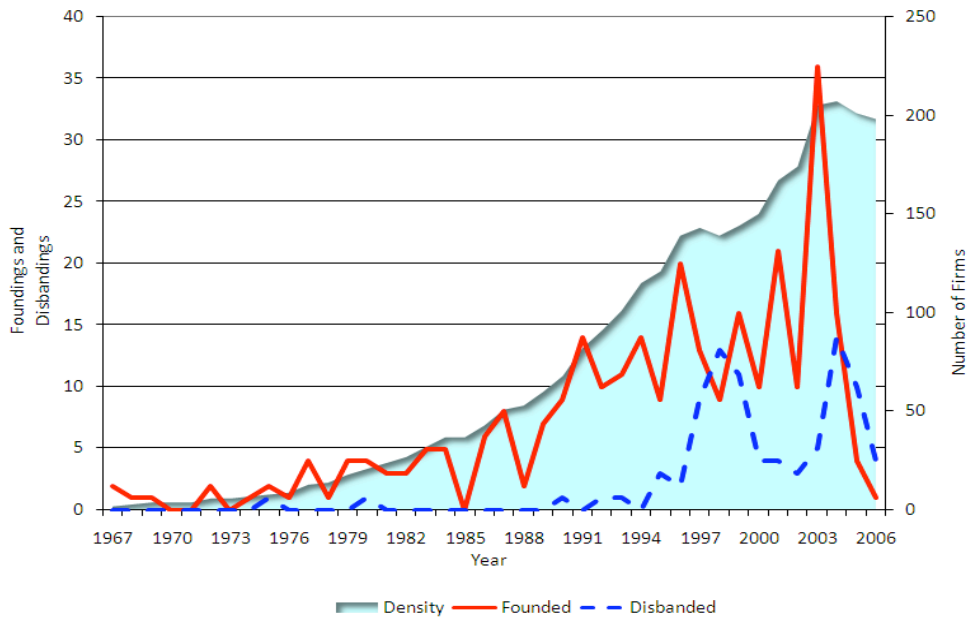
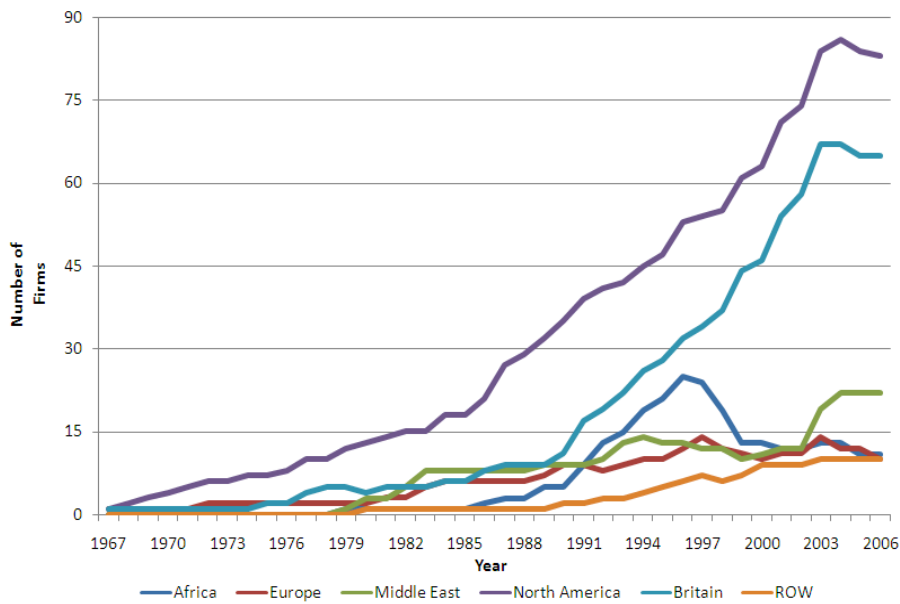


Figure 5: Number of PMCs by Region



*Sources: Dunar, Mitchell and Donald (2007), Various, authors' compilation

Figure 6: PMC Operations

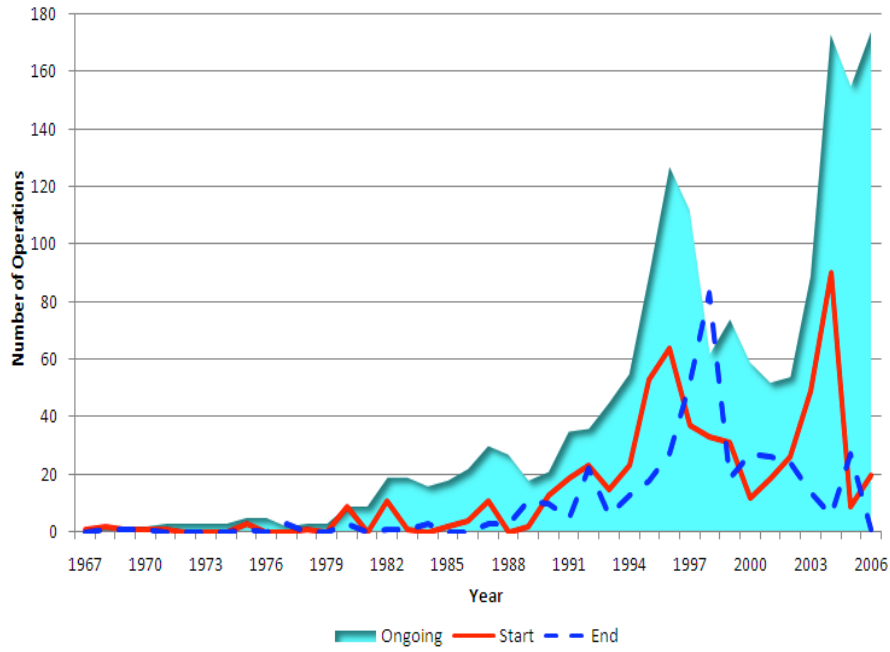
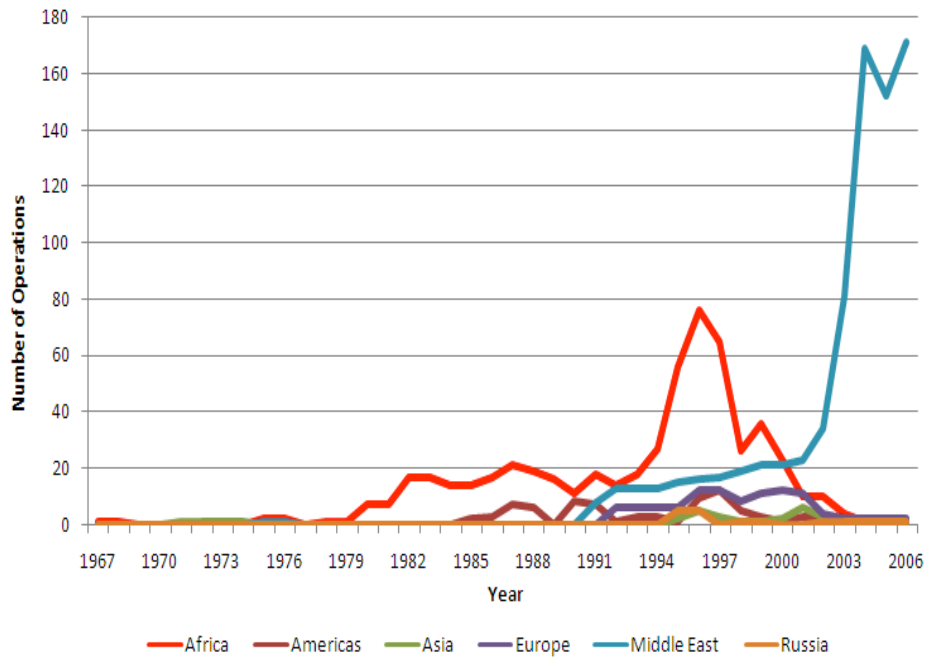


Figure 7: PMC Operations by Region



*Sources: *Private Military Companies: Options for Regulation*, FCO 2002; various, authors' compilation