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REGIONAL INTEGRATION, FRAGILITY AND INSTITUTION  
BUILDING: AN ANALYTICAL FRAMEWORK APPLIED TO  
THE AFRICAN CONTEXT

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**THIERRY VERDIER**

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## **Abstract**

The purpose of this paper is to discuss how regional integration processes may contribute to state-building and promote exit from fragility for countries characterised by weak state institutions. After presenting a simple conceptual framework to discuss the effects of external and regional integration on fragile states, we analyse the policy trade-offs that may arise in such contexts. The paper then reviews the specific regional experiences of Sub-Saharan countries and their inter-actions with fragility issues. Finally, we discuss policy implications for the EU in the context of its regional trade and development policies with African fragile countries. The central conclusions of the analysis are the following: 1) a two-tier approach to regional integration, which combines both top-down and bottom-up processes, is necessary; 2) the EU approach to regional integration in Africa should promote “Building-Blocks” and not “Stumbling-Blocks”; and 3) specific considerations should be given to make the trade integration strategy “fragility responsive”.

## **Keywords**

Regional integration, fragility, state building, Africa





## 1. Introduction\*

While the concept of country fragility may take various interpretations, there is, however, a general consensus that fragile countries are characterised by the presence of weak institutions and governance structures, and a fundamental lack of state capacity and/or political willingness to fulfil core state functions. These include security and protection, taxes and the provision of public goods, and the building up of legitimacy and a resilient relationship with civil society. Tackling such issues involves the implementation of state-building, and institution-building processes which have become leading priorities for the international development community. Currently, almost every major donor identifies state-building as one of its key objectives, especially in fragile states (Fritz and Rocha Menocal 2007). A good example of this is the elaboration of *The Principles on Good International Engagement in Fragile States and Situations* by the OECD DAC (2007), which stress that state-building should be the central objective of engagement in such settings. Recognising endemic violence, conflicts and civil wars as essential dimensions of fragility (though by no means the only ones), a growing number of donors (such as DFID, the OECD DAC, the UN and the World Bank) have sought to promote peace and development together, emphasising the connection between security and development, and the necessity to combine peace-building and state-building mechanisms in states afflicted by conflicts.

Much of the literature on country fragility and state-building takes a country-level state-centered approach and emphasises the problem of failures in the three dimensions of security, public services provision and legitimacy. Recognising that countries do not operate in isolation and that regional drivers of fragility may be important elements of the problem, there has been some recent attention devoted to the regional components of state fragility. Indeed, evidence suggests that fragility has far-reaching consequences beyond a state's borders. For instance, Chauvet and Collier (2004) estimate that, once a state reaches the World Bank status of Low-Income Countries Under Stress (LICUS),<sup>1</sup> a neighbouring state will lose 2% of their annual growth rate. At the same time, two thirds of the economic damage caused by reaching LICUS status will accrue to neighbours, rather than to the LICUS state itself.

In addition, when a country has weak institutions, and, in particular, when there are marked social divisions (compounded with minimal public participation in political processes), external shocks can trigger fragility. Shocks in terms of trade can be de-stabilising not only for one specific country, but also for neighbouring countries. Similarly, several case studies indicate that, through regional migration, conflict-induced population displacements and war economies, fragility in one country produces significant spillovers and externalities in terms of resource allocations, health issues and social frictions in neighbouring countries. West Africa with the spread of conflicts affecting Liberia, Sierra Leone, Guinea, Guinea-Bissau, Casamance and the Ivory Coast, is a clear example of this kind of regional fragility dimensions.

A regional perspective on fragility leads us naturally to turn our attention to regional processes of institution-building and the policy implications that can be derived from such an approach in order to emerge from fragility. Along this line, the purpose of this paper is to focus upon three basic questions:

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<sup>1</sup> The LICUS programme is a World Bank programme designed to address the special needs of low-income countries with unstable government and economic structure. The World Bank's criteria for eligibility in this programme include: 1) weak institutions and institutional performance, as measured by the World Bank's Country Performance and Institutional Assessment ratings, 2) severe internal conflict, 3) deteriorating socioeconomic climate that is not conducive to receipt and successful use of traditional development assistance, 4) risk of being abandoned by the international community for past poor performance.

1. How does regional integration interact with state fragility? What are the interconnections of institution-building processes in a regional context? Can regional arrangements help to promote a strengthening of state building processes in fragility contexts?
2. In the specific African context, what has been the logic of regional integration and how has it interacted with country fragility? Can a regional solution work to promote exit from fragility?
3. What are the policy implications for the EU, in particular, in the context of its regional trade and development policies with African fragile countries?

## 2. An Analytical Framework of Fragility and State-Building

In order to analyse the above-mentioned issues, it is useful to start from the basic components of state-building in a fragility context. Critical to the process of institution-building is the recognition of a set of core state competencies that need to be strengthened and supported by policy intervention (USAID 2005, Brinkerhoff 2007, OECD 2007, Whaites 2008). Though they take different labels in the literature, they can be categorised along three main dimensions:

4. *Surviving functions: Control, Security and Protection.* These include the capacity of the state to exert (at least on a given geographical territory) the “monopoly of violence”. It also includes the provision of security and protection of people and property, the effective implementation of the rule of law and the capacity to raise revenues in order to sustain the functioning of the state (Brinkerhoff (2007), Whaites (2008) and DFID (2008a)).
5. *The Delivery of basic public goods.* This relates to the effective provision of basic services (for example, health, education, and infrastructure) and the efficiency, capacity and transparency of public policy-making, regulation and fiscal arrangements.
6. *Political legitimacy and the Social Contract.* This dimension concerns the organisation of public and social governance systems, the implementation of democratic and participatory political principles, and the establishment of political representation and inclusiveness, which help to build a legitimate relationship between the state and civil society.

**Figure 1a: State-building and core functions**

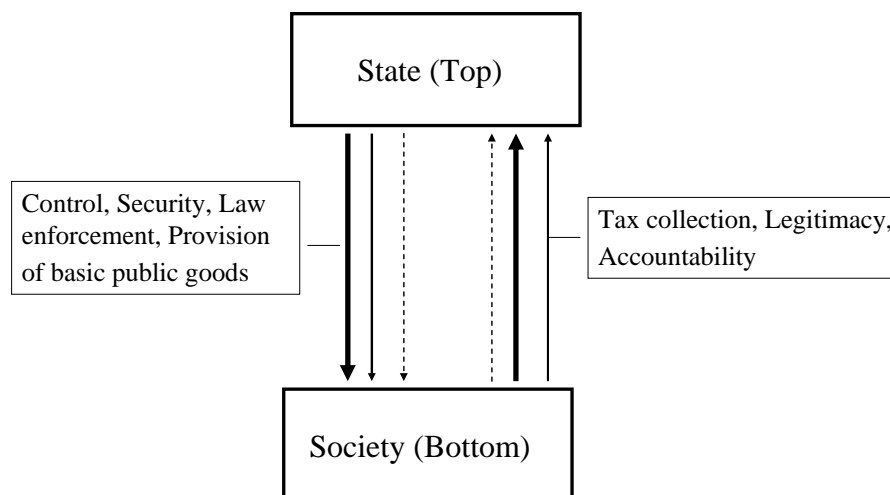
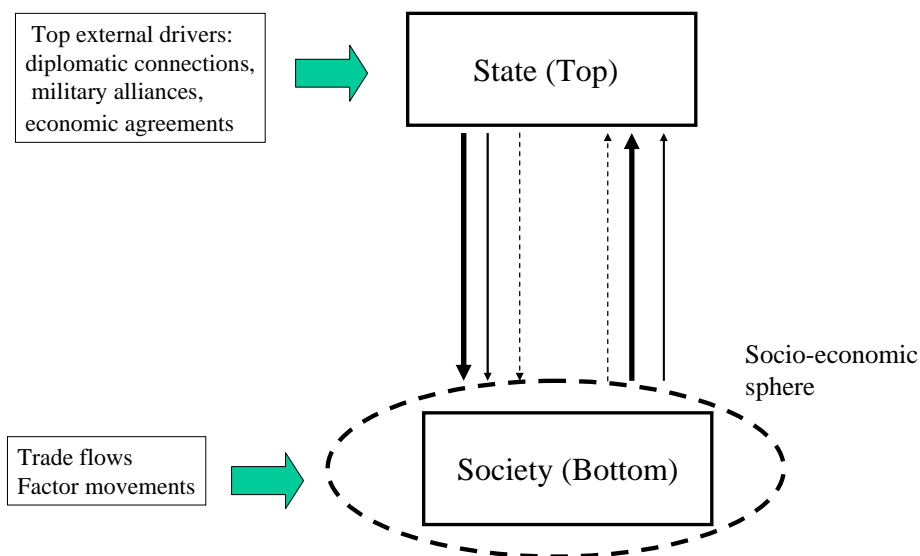


Figure (1a) illustrates the main issues schematically. It indicates the relationships that structure the political settlement between the state (or the élites) at the top, and society at the bottom. The various connections between the two *loci* should be understood as two-way dynamic links that reflect the

multi-dimensional nature of the social contract between the state and society. Dimensions of state-building such as security, protection and provision of basic services and policies tend to go vertically from the top to the bottom. On the other hand, tax revenues, public accountability and legitimacy dimensions are likely to go from the bottom to the top. In fragile states situations, some of these links will tend to be weak or inexistent (represented dotted lines in Figure 1a)). In addition, the intensity of the links should be thought as varying in time, consistent with the idea that fragility should be viewed as a dynamic process in which countries move along trajectories from stability towards conflict, crisis, and/or failure; and emerge from crisis towards recovery and stability. As noted indeed by OECD (2007) and USAID (2005), the process can be non-linear and asymmetrical, and, along pathways in and out of crisis, the different links of Figure (1a) can have increased or decreased intensity. Finally, as emphasised in the literature (Brinkerhoff 2007), Whaites (2008) and DFID (2008a)), there are complementarities and spillover effects between core state functions. Thus, the intensity of some links of Figure (1a) is likely to be correlated with the intensity of other links: improving one dimension is likely to facilitate improvements along another dimension, and *vice-versa*. In economic terms, there are “social increasing returns” in capacity-building across core state functions.

As fragile states do not operate in isolation, countries face various external drivers that interact and may impact on some of their fragile dimensions (Vallings and Moreno-Torres (2005)). In Figure (1b), these drivers may hit at the top level of élites and states (such as, for example, through diplomatic connections, international military or economic alliances and agreements) or at the bottom at the level of society, through socio-economic interactions with the rest of the world, like production, consumption and trade activities. Given a specific fragility structure of the country (illustrated by a collection of links of different intensities as in Figure 1b), these external drivers impact on the allocation of resources within society and have distributive consequences among individuals. The reactive actions and decisions of the élite and the concerned social groups may, in turn, affect the intensity of the vertical links between the state and society, and thus change some dimensions of the fragility structure in the country. As specific external drivers, regional processes are likely to affect the country through channels at both levels (Top and Bottom), eventually feeding back into the vertical relationships between the state and society.

**Figure 1b: State-building and external drivers**



### 3. Fragility, Conflicts and International Integration

The first step to discuss how regional processes interact with state fragility is to consider the linkages between economic integration and fragility, and, in particular, the interactions of fragility and international trade in goods and services. Several issues can be addressed here. What are the effects of international trade in a context of fragility and weak institutional settings? Conversely, how does trade openness affect fragility and the dynamics of institution-building and through which mechanisms?

The literature has identified several linkages between trade integration, fragility and state-building processes. As shown in Figure (1b), international economic integration is likely to have an impact, at least initially, at the bottom level in the economic sphere within which individuals interact. In this respect, economic theory predicts that the first immediate impact of trade integration in a given country is to change the structure of the relative prices of goods and services traded with the rest of the world. This implies the re-allocation of resources both across and within sectors of the economy. This, in turn, leads to effects on labour and capital markets and also to rent creation, destruction or rent shifting across individuals.

In a well-defined institutional setting in which security, property rights protection and contract enforcement are fully ensured by the state, economists tend to agree that trade openness results in global gains from trade. In weak institutional settings, however, this is no longer ensured. Also, even when there are potential aggregate gains from trade, the distribution of these gains may be conflict-generating and destabilising. It can contribute to fragility, especially when the country's institutions of conflict-management are inexistent or have been dismantled.

In addition, the structure of the comparative advantage of the country can affect this dimension. Indeed, the analysis of recent conflicts (Isham, Pritchett, Woolcock and Busby (2005)<sup>2</sup>) suggests that the exclusion of some threatening groups from the sharing of the resources of the state is made more likely when the country relies on "point-source" natural resources (fuels, minerals, and plantation crops (*i.e.*, sugar and cotton)) than when it relies on manufacturing and diffuse agricultural exports (animals, agricultural produce grown on small family farms (*i.e.*, rice and wheat). In the African context, examples such as the Biafra war in Nigeria in the late 1960, the civil wars in Angola and in the Democratic Republic of Congo abound. For instance, Collier and Hoeffler (1998) provide econometric evidence that the share of mineral exports in GDP significantly affects the incidence of civil wars. In contrast, diffuse agricultural or industrial exports, the production and benefits of which are widely-distributed across geographical areas, ethnic groups, or urban centres, do not seem to enhance the chances of civil violence erupting.

#### 3.1 The Ambiguous Consequences of Trade Openness in weak Institutional Settings

##### 3.1.1 Conceptual issues

Conceptually, the economic literature has mainly concentrated on the case of trade integration when the main fragility component of a country is the existence of conflicts, insecurity and the incapacity of the state to establish a "monopoly of violence". In this respect, recent theoretical work emphasises the potentially ambiguous consequences that trade integration may have in countries characterised by high levels of insecurity, predation and conflicts. In a context of imperfect institutions of governance and law enforcement, trade openness interacts with fragility through the way it affects the value of disputed resources, the opportunity costs of contestation, conflict and crime, and the occupational choice between productive or predatory activities. A central insight from these analyses is that the effects of trade integration depend on the pattern of trade in terms of the contested resource (exports

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<sup>2</sup> See, also, De Melo (2009) for a review of recent channels through which trade and accompanying microeconomic reforms play out in low-income natural-resource-based countries focusing on perennial crops subject to rent-extraction.

*versus* imports), and that the usual normative conclusions on the benefits of trade integration are significantly altered for economies characterised by insecurity and conflicts. (see Box 1.)

While these studies emphasise the impact of trade openness at the level of socio-economic interactions (namely, within the *locus* of society in Figure 1b), openness may also feed back on the nature of the relationships between the state and society. For instance, trade openness may interact with the nature of state institutions and the type of redistributive policies chosen by élites. An example of this is provided by the model of Segura-Cayuela (2006). When political élites are unwilling to contribute to the provision of public goods and have no state-capacity to raise taxes, they generally seek to appropriate resources through price distortions<sup>3</sup>. However, the extent of these appropriative policies is limited by the fact the élites' own business rents may, to some extent, be complementary to what non-élite social groups produce. In such a context, trade openness reduces the opportunity costs of appropriative price policies. Indeed, with trade integration, product prices are likely to be set outside the domestic economy, disconnecting, in a certain sense, the élites' benefits from the distortions that they impose on the local economy. This, in turn, induces them to manipulate relative domestic prices more intensively in order to extract rents from non-élite members. This reasoning suggests that trade integration may have harmful consequences in countries characterised by low political participation and weak élite concerns and responsiveness to the rest of society.

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<sup>3</sup> See Bates (1981) for an illuminating description of this in the African context.

**Box 1: The economic theory of trade openness in a fragile context**

Several recent theoretical analyses have considered the issue of trade integration in a context of fragility. Garfinkel, Skaperdas and Syropoulos (2008) discuss the case of an economy in which a potentially tradeable natural resource, such as oil or diamonds, is contested by different domestic groups who would like to take control of a contested territory where the resource lies. Due to imperfect institutions of governance and enforcement, claims to this territory can be settled only via overt conflict or the threat of conflict. The analysis shows that the effect of trade integration in the country is going to depend on the pattern of trade in terms of the contested resource. When the country is a net importer of the contested resource, trade integration induces less arming and less domestic conflict. In that case, free trade unambiguously yields higher welfare, both in terms of traditional aggregate gains from trade as well as in terms of reduced fragility (*i.e.*, less domestic conflict). On the other hand, when the country is a net exporter of the contested resource, trade integration induces more arming and conflict. In this case, the familiar gains from trade must be balanced against the increased costs of conflict. In particular, an increase in the international price of the contested resource could induce a conflict-induced “natural resource curse”. The paper also shows that the presence of conflicts may significantly modify the structure of comparative advantage of the country, inducing, in particular, a positive bias on the country’s net export of the contested resource. Thus, this analysis suggests that a country’s trade pattern is not invariant to the emergence of domestic conflict, and that it might not be justified to treat the trade patterns of fragile countries (prone to civil wars and other forms of domestic conflicts) as being indicative of their true comparative advantage either in empirical studies or for policy purposes.

Bo and Bo (2005) also present a theoretical framework that allows an analysis of how economic shocks and trade integration interact with a certain degree of state fragility that is characterised by the existence of resource appropriation activities. Discussing the impact of external trade shocks, the analysis emphasises that what matters is not only whether shocks are increasing income or not, but also on where they hit the economy and how they affect the relative scarcity of labour, and, as a consequence, the opportunity cost of crime or conflict. This, in turn, depends on the relative use of factors in the sector initially affected by the shock. Given that appropriation activities generally use relatively more labour than the whole economy, positive price shocks to labour-intensive industries tend to diminish social conflict, while positive price shocks to capital-intensive industries tend to increase it. The economic reasoning is as follows: typically, an increase in the price of a capital-intensive good will expand the capital-intensive industry and contract the labour-intensive one which abundantly releases labour relative to capital. This lowers wages, resulting in a lower cost of the appropriation activity relative to the amount of appropriable resources. Conversely, by the same economic intuition, a positive trade shock in the labour-intensive tradeable sectors is likely to increase the opportunity cost of appropriation activities.

Stefanidis (2007) considers the quite realistic context in which individuals have occupational choices between production and predation. He shows that international trade has a favourable effect on activity, skill allocation and property right protection in economies that are already in a “producer-friendly” equilibrium and have a strong institutional framework. In contrast, in fragile and “predator-prone economies”, international trade leads to further institutional deterioration and a more unfavourable activity allocation. An implication is this trade integration may have ambiguous normative consequences in “predator-friendly” countries.

3.1.2 Trade-offs of trade openness under Fragility

The previous analyses provide conceptual arguments to the idea that trade integration may not be beneficial in weak institutional contexts, and may, actually, even further contribute to the fragility of countries. There is, however, relatively little systematic empirical work on the economic impact of trade openness in fragile states. A notable exception is a recent study by Balamoune-Lutz1 (2008), which examines the contribution of institutions, social cohesion, and trade to development (*per capita* income) with an emphasis on fragile states in Africa. One statistical problem of such an analysis is the problem of small sample size and the difficulty to identify the causality from trade openness to

economic performances clearly. Nevertheless, the results are indicative that, beyond a certain level, openness to trade may be harmful to the economic performances in fragile states. This is also consistent with some former study (Baliamoune-Lutz and Ndikumana (2007)) using panel data from 39 African countries on the period 1975-2001, which found that institutions play an important role in the impact of trade openness on economic income.

Consistent with the previous conceptual discussions, the work is also indicative of the role of the structure of trade and the importance of export diversification. In particular, the analysis suggests that, while export diversification is negatively correlated to growth in Africa, it does, however, enhance the positive effects of trade openness on growth. These results indicate that, at least in the short-term, a trade-off may exist between trade liberalisation and capacity-building. Indeed, if a fragile state tries to improve its openness to trade, it may wind up with lower *per capita* income, which may lead to increased poverty and further fragility. The mid-term solution would be to induce a shift in the pattern of trade of the country and to promote a re-distribution of the gains from trade in ways which are less conducive to conflicts in the economy.

### 3.1.3 Trade openness, fragility and the dynamics of state failures

While fragility may affect the effectiveness of trade openness on economic outcomes, conversely, as suggested by theoretical analyses, trade liberalisation may also impact upon the degree of fragility of a particular country. In particular, trade openness may actually trigger conflicts and tensions.

An important part of the literature in political science and international relations has focused on the empirical links between trade openness and conflicts across countries, and assesses whether an increase of bilateral economic interdependence reduces interstate conflict. Two contrasting views prevail in this debate. Tracing itself back to Montesquieu, the “liberal view” emphasises the idea that mutual economic interdependence promotes peace. Trade interdependence limits the incentive to use military force in interstate relations, as it increases the opportunity cost of wars associated with the loss of trade. Alternative views suggest, however, that asymmetric economic interdependence could induce frictions and disputes across countries, and thus lead to negative consequences (Keohane and Nye 1973). A number of studies, such as Domke (1988), Barbieri (1996), Barbieri and Schneider (1999), Gartzke and Li (2003), have investigated the relationship between the various measures of bilateral trade interdependence and military conflict, while other studies (Barbieri and Peters (2003), (Martin, Mayer and Thoenig, (2008)), (Lee and Hyun Pyun (2009)), have also examined the role that global trade openness plays, checking for the level of bilateral trade inter-dependence. Although it is still being debated, this literature provides mild support for the “liberal view” that increased trade integration negatively affects the probability of bilateral conflict. However, the difficulty in identifying the direction of the causality between trade openness and conflicts remains an important issue. While inter-dependence may decrease the incentives for conflict, conversely, conflicts between countries significantly reduce international trade (Glick and Taylor (2006), Blomberg and Hess (2006)).

One recent study that tries to disentangle this two-way causality between trade integration and inter-state conflicts is that of Martin, Mayer and Thoenig (2008). This study emphasises the importance of the geographic nature of trade integration as a catalyser of peace or conflicts. In particular, it shows that bilateral trade reduces the probability of dyadic conflict, but “multilateral openness”, that is, global trade openness, increases the probability of interstate conflicts. The argument is that countries more open to global trade have a higher probability of dyadic conflict because multilateral trade openness reduces bilateral dependence to any given country, and thus lowers the opportunity cost of military conflict.<sup>4</sup> This result is indicative of the form that trade

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<sup>4</sup> In contrast to Martin, Mayer and Thoenig (2008), but using the same data set, COW of interstate conflict events for the same period 1950-2000, Lee and Hyun Pyun (2009) obtain the result that multilateral openness decreases the probability

integration should take to mitigate the external sources of fragility. Multilateral trade liberalisation should be associated with increased bilateral interdependencies, in order to reduce the risk of increased inter-state friction.

Drawing on this literature, albeit more appropriate for the discussion of the interaction between trade openness and state fragility, a number of analyses have investigated the linkages between trade integration and the emergence of domestic conflicts and civil wars. Again, two alternative perspectives are discussed in the literature. The first one conceives economic problems as the source of conflicts, instability and civil wars. According to this view, trade openness brings benefits and stimulates growth, and thus should contribute to peace and internal stability. Recent quantitative cross-country studies provide support for this perspective and indicate that economically-integrated countries are more stable than autarkic ones and less likely to experience civil wars (de Soya and Wagner (2003), Hegre *et al.* (2003), Bussmann and de Soya (2005), Barbieri and Reuveny (2005), Elbadawi and Hegre (2008)<sup>5</sup>). The alternative “anti-globalisation” perspective argues that foreign trade liberalisation has negative distributive consequences which may undermine the social fabric of a society and thus trigger conflicts, instability and fragility. (Brennan (2003), Stiglitz (2002)).

Focusing specifically on Sub-Saharan African countries which have been particularly prone to civil conflicts, recent empirical work suggests a possible trade-off which reconciles the previous conflicting views (Bussman, Schneider and Wiesehomeier (2005)). Looking at the effects of trade openness and trade liberalisation on the outbreak of internal wars in 37 sub-Saharan African countries for the period 1980-2000, the analysis tends to support the view that economic openness has a positive effect on peace and stability, once the restructuring of the economy is over. The results suggest, however, that, in the short-term, trade liberalisation may increase the risk of civil war and conflict during the implementation of the reform measures. A potential explanation stems from the fact trade openness may have long-term socially-stabilizing effects in developing countries as it is likely to generate benefits to the majority of the population (unskilled workers). However, trade liberalisation may also generate short-term conflict-prone effects as the immediate losers may oppose the process and trigger violent reactions.

As in the literature on international conflicts, an important methodological *caveat* needs to be noticed, though. An appropriate identification of the link between trade and civil war has to purge the reverse causality from domestic conflicts to trade openness. Indeed, as Bayer and Rupert (2004) show, civil war tends to reduce international trade significantly. Martin, Mayer and Thoenig (2009) explicitly consider the possibility of “two-way causality and explore the relationship from trade integration to domestic conflicts using the expanded version of the COW database” (Gleditsch (2004)). After demonstrating the extent and persistence of trade destruction due to civil wars, the analysis identifies two effects that trade can have on the risk of civil conflicts: first, trade integration may act as a deterrent if the gains from trade are put at risk during a civil war. However, at the same time, openness may also act as an insurance mechanism against war-induced local production damages, and thus lower the opportunity cost of civil wars. Given that there is access to additional resources from the outside, domestic agents are less concerned about the costs of destruction and the perturbations of local conflicts. The results indicate empirical support for the presence of the two mechanisms. Indeed, it is found that trade openness may deter the most severe civil wars (those that destroy the largest amount of trade), but, on the other hand, it may increase the risk of lower scale conflicts.

The previous discussions suggest potential various policy trade-offs between i) short-term risks of trade reforms and long-term gains from openness, and ii) the prevention of severe conflicts and persistent risks of lower scale tensions. One possible solution to such trade-offs may be related to the

(Contd.) \_\_\_\_\_

of interstate conflicts. The definition of openness that they use and the way they control for the reverse causality effect from conflict to global openness seem, however, to differ.

<sup>5</sup> Elbadawi and Hegre (2008) find no significant direct effect of trade openness on the risk of civil war, but their analysis indicates that openness may indirectly reduce the probability of civil conflicts, as it increases a country's rates of growth, which, in turn, reduces the risk of conflict both in the long-run and in the short-run.



implementation of compensation schemes to the immediate losers, in order to reduce the short-term risks of political instability and allow sufficient time for the economy to reach the long-term situation in which enough individuals benefit from the reform. Clearly, the capacity to implement such compensation mechanisms relates directly to the issue of institution-building in contexts which are initially fragile.

### **3.2 Dealing with FDI in a Fragility Context**

Beyond international trade, another dimension of globalisation that interacts with fragility and institution-building is Foreign Direct Investment (FDI). FDI plays a special role as a source of financial resources and technology transfer to the private sector. In addition, it may force competition in the local economy. This may improve the efficiency of the allocation of domestic resources, reduce both rents and the associated negative side-effects for public governance, such as, for instance, rent-seeking and corruption (Larrain and Tavares 2007). But FDI also brings its own challenges, especially for countries with weak governance and for those heavily dependent on natural resource revenues. Without appropriate incentives, foreign investors might also contribute to the maintenance of bad governance and corruption, participate directly or indirectly to the “war economy” and the funding of armed civil conflicts and warlords.

While the literature recognises the negative impact of bad domestic governance and corruption on FDI inflows (Wei (1997); Alesina & Weder (2002); Smarzynska and Wei (2001)), less work has investigated the reverse relationship of the effect of FDI on host country governance structures. However, recent work does provide some empirical indications on the nature of this relationship (Larrain and Tavares (2007) and Zhu (2007)). The first study discusses the two-way relationship between foreign direct investment and corruption, and tries to identify precisely the direction of causality from “exogenous” variations in FDI on the degree of corruption in the host country. Using a dataset covering a wide group of countries for the period 1981–2000, the authors construct an original set of instrumental variables relying on geographical and cultural distance between the FDI source and the host countries in order to measure exogenous time-varying changes in FDI inflows. The analysis indicates that FDI inflows (as a share of GDP) significantly lower corruption in the host country. These results are robust to the inclusion of several determinants of openness in addition to trade intensity and the average tariff level, including dependence on natural resources, ethnic fractionalisation, size of the economy and government expenditure.

Zhu (2007) extends this perspective by discussing how that the relationship between FDI and corruption is likely to depend on the level of development and the level of democracy of the host country. Again, there is the identification issue of causality from FDI to corruption. Using a measure of FDI remoteness<sup>6</sup> as an instrumental variable to deal with the endogeneity of FDI and checking for other factors that the literature has found to affect corruption (*i.e.*, legal systems, religion, natural resources endowment, and ethnolinguistic fractionalisation), the regression results provide empirical support for the fact that FDI inflows are likely to reduce corruption levels in more developed democracies, and increase corruption levels in less developed non-democratic countries.

This type of results again highlights a potential policy trade-off in terms of state-building capacity and FDI openness policies. Building strong democratic institutions may be a necessary condition to capture the economic benefits associated with FDI. This view is consistent with the policy-oriented perspective of Turner, Aginam and Popovski (2008), which emphasises the fact that, in post-conflict countries, FDI openness needs some form of regulation that should be designed to prioritise the quality of investment, rather than quantity. Clearly, an important implication for a positive contribution of FDI to the local economy is the implementation of a legal and accounting framework in investors’

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<sup>6</sup> FDI remoteness is defined as the geographical distance between host countries and the richest 20 economies in the world weighted by their real GDP *per capita*.

home countries, which encourages transparency and accountability. Solving this dilemma implies building a good investment climate and support for international initiatives to strengthen national and corporate governance, such as the UN Convention Against Corruption (UNCAC) and the Extractive Industries Transparency Initiative (EITI).

### **3.3 Integration, Exposure to Shocks and Conflicts**

An important feature of country fragility is related to how the country is able to react to political and economic shocks, and its resilience properties in terms of stability and public policy. From such a perspective, international economic integration, beyond affecting the flow of goods and resources crossing a country's borders, is also going to affect exposure to external shocks and fluctuations. When a significant share of a country's economy is related to international trade or FDI, fluctuations in international prices, terms of trade or capital flows may have considerable impact on the domestic economy, with consequences on fragility dimensions. Again, the literature has mainly focused on the dimensions of insecurity and violence by discussing the interaction between shocks and conflicts. Elbadawi and Hegre (2008), for instance, review three types of mechanisms through which shocks are translated into political violence and instability: i) social conflicts, ii) the balance of internal political power, and iii) the incentives for predation.

#### **3.3.1 Social conflicts**

First of all, external shocks may induce social conflicts through their economic consequences. For instance, negative terms-of-trade shocks may lead to short-term reductions in growth rates and a sudden rise in unemployment. Shock-induced policy reactions such as exchange rate devaluation and fiscal retrenchment have also important distributive consequences. Such events may typically generate social tensions and political conflict (Rodrik (1999)). In addition, in a context of weak state capacity and, in particular, the absence of appropriate government policies, a negative transitory shock may have persistent effects economically, and on the risk of conflict. Similarly, positive shocks may also lead to permanent distortions as the distributional conflicts triggered by the shocks themselves make the formulation of appropriate policies more difficult. As again emphasised by Rodrik (1999), these problems are likely to be compounded for fragile countries prone to latent social conflicts and for poor institutions for conflict management.

#### **3.3.2 Altering power balances**

Exogenous shocks may also alter the balance of power between a government and an armed opposition or an organisation that is considering military action. As shown, for instance, by Acemoglu and Robinson (2005), non-predictable variations in the power of the government may weaken the commitment capacity to negotiate political settlements. In weak institutional settings, a government temporarily affected negatively by a shock cannot commit itself to particular concessions that would avoid tensions with opposition groups. Such groups might, indeed, expect the government to renege on the agreement when its position improves and therefore prefer to initiate a conflict rather than negotiate a peaceful solution. Moreover, exogenous shocks also introduce uncertainty about the balance of power between adversaries and the potential outcome of the conflict which, in turn, may lead to increased conflicts and war.

#### **3.3.3 Increasing the incentives for predation**

Consistent with the conceptual literature on predatory conflict surveyed above, positive shocks may affect the incentives and opportunity costs of potential rebel leaders. An increase in the international price of an appropriable export commodity may trigger or intensify actions to secure access to it. A good example of this is the case of the mineral Coltan, for which the significant price increase in the

year 2000 clearly triggered conflict activity in the eastern region of the Democratic Republic of Congo (Hayes, (2002)).

### 3.3.4 Negative economic shocks and civil conflicts

Empirically, a recent study by Elbadawi and Hegre (2008) has investigated the plausibility of the previous mechanisms. The analysis indicates that, while there is weak evidence of a direct relationship between terms-of-trade shocks and the risk of armed conflict<sup>7</sup>, external volatility may still affect the risk of conflict indirectly, mediated by its negative effect on growth (which, in turn, has an effect on the probability of conflict). In addition, for low-income economies with poorly diversified export structures, poorly developed infrastructures and weak governments, terms-of-trade shocks may have compounded effects that interact with the already important tendency of these countries to be conflict-prone.

These results contrast somewhat with other works by Ciccone (2008) and Bruckner and Ciccone (2009), which consider the effects of negative economic shocks on the onset of civil conflicts in sub-Saharan Africa in the period between 1980 and 2006. The first study looks at the effect of rainfall levels on the outbreak of civil conflicts and finds some evidence of this: rainfall levels 10% below the country average raise the likelihood of civil conflict onset by almost 1 percentage point above the country average, and this effect is statistically significant at the 92% confidence level. The effect becomes stronger quantitatively and statistically when one accounts for common shocks to the probability of civil conflict onset (for example, that conflict onset became more likely after the end of the Cold War). Bruckner and Ciccone (2009) consider the effects of downturns in the international commodity export prices on the likelihood of civil wars for Sub-Saharan African countries.<sup>8</sup> The analysis indicates that downturns in international commodity prices did make civil war onset more likely, the results being robust when one checks for cross-country differences in the probability of civil war, for country-specific time trends and for common shocks to the likelihood of civil war across Sub-Saharan Africa. Quantitatively, a 20 per cent drop in the international export price index raised the probability of a civil war by around 1 percentage point.

## 4. Regional Fragility and Regional Integration

The previous discussion considered the general question of interaction between fragility and international integration. The regional level may, however, highlight some more specific features. Indeed, while the policy-making and academic literature on fragility and state-building has extensively discussed the importance of failures at country level, less attention has been given to the regional dimensions of fragility and the implications of cross-country linkages for state-building. Notwithstanding this, various examples, such as the Liberia-Sierra Leone-Ivory Coast conflicts in western Africa or the persistent instability situation in the Great Lakes Region and the East African Horn, suggest that a regional perspective is essential to explain the existence and persistence of many fragility or conflict situations in Sub-Saharan countries.

### 4.1 A Conceptual Framework Illustrating the Various Linkages

To organise the discussion on these issues, it is useful to reconsider the conceptual framework of state-building summarised in Figure (1a) and to extend it to the regional level. This is illustrated in Figure

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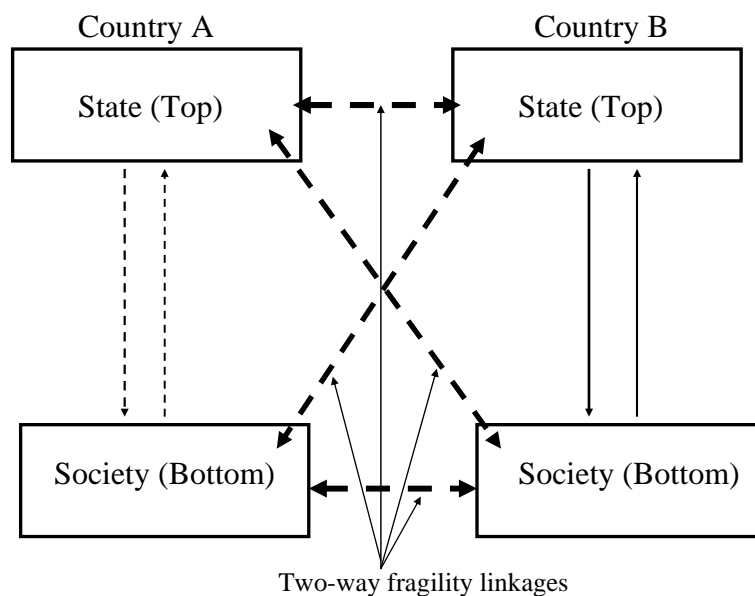
<sup>7</sup> For most empirical formulations of trade shocks, results are not significant, even after checking for the usual reverse causality fact that terms-of-trade shocks are likely to be themselves affected by conflict or by an expectation of conflict.

<sup>8</sup> Besley and Persson (2008) also examine the effect of commodity export prices on civil war incidence and onset across a wide range of countries, not restricted to sub-Saharan countries. Their focus is on the effect of export prices conditional to income and to civil war incidence, rather than the onset of civil war.

(2), which considers the illustrative situation of two countries A and B located in the same region. At country level, the structure of political settlement is just a replication of Figure (1a) with the state at the top and society at the bottom, and relationships between the two are illustrated by a collection of links, the intensities of which characterise the pattern of fragility of the country.

At regional level (*i.e.*, between the two countries), there are also various regional linkages through which fragility in one country (namely, a weakening of a vertical link in country A) may connect to political and socio-economic processes in the neighbouring country (in other words, it may affect a vertical link between the state and society in country B). Some of these linkages may be related to horizontal cross-country connections at the top (between members of the élites of the two countries), or horizontal cross-country connections at the bottom (between individuals of the two countries' societies). Some linkages could also be transversal connections, in other words, between the top of one country and the bottom of the other.

**Figure 2: Regional fragility linkages**



Such linkages are likely to induce significant fragility externalities across neighbouring countries. As already mentioned, there is empirical evidence that civil conflict in one country tends to produce considerable negative externalities for their neighbours. As shown by Chauvet and Collier (2004), there is a net annual loss of 1.5 percentage points of economic growth for countries that border on a Low Income Country Under Stress (LICUS). Since a LICUS country loses about 2.3 percentage points of growth, and has, on average, three neighboring countries, this result suggests that the estimated economic losses sustained by the region are much higher than the damage to the country itself.

One important observation worth mentioning is the fact that the preceding view implicitly assumes the idea of the regional “spillover” or “contagion” dimension of fragility or conflict, with a unidirectional linkage from one fragile country to the other neighbours. However, the one-off nature inherent in the “spillover phenomenon” may not adequately explain the proliferation of regional instability, especially in Africa (Lambach (2004), Studdard (2004)), Hentz (2007)). In contrast, the bi-directionality of regional linkages across countries suggests important complementarities and multiplier effects.

In the specific context of security and conflicts, these two-way regional linkages capture the idea of so-called “regional security complexes” as expanded by Buzan (1991) and Buzan-Waever-de Wilde

(1998) in the security literature. “Regional security complexes” are groups of states whose security concerns are interlinked to such a degree that they cannot meaningfully be analysed separately. This notion was further extended by Rubin (2002) with concept of “regional conflict formations”, which are sets of sub-national conflicts within a region, which develop mutually re-inforcing linkages. According to this view, regional clusters of intra-state instability occur as the result of interlinked conflict processes with local causes and trans-national connections. Thus, this approach not only emphasises the importance of the local causes of conflict, but also the trans-national interdependencies that participate in the persistence of these conflicts.

The concept of regional conflict formations can be usefully extended to the general notion of regional fragility clusters. Accordingly, a region consists of several states, each with its own domestic processes of institutional failures (be they security failures, public good provision failures or legitimacy failures). These processes are, however, regionally interdependent, as they are connected through various cross-country channels, which give rise to regional fragile clusters where state governance is weak or even almost entirely absent. In terms of our analytical framework, the regional re-inforcing character of fragility may be reflected by two-way relationships between one *locus* in country A and another *locus* in country B, as, for instance, illustrated in Figure (2).

## **4.2 The Regional Components of Fragility**

The literature has identified four types of interactions (military, economic, political and social) that structure the regional linkages of country fragility (Lambach (2004), Studdard (2004)). Though they are generally intertwined, it is useful, for analytical purposes, to discuss them separately and discuss their position in Figure (2).

### **4.2.1 Military interactions**

The first source of regional fragility linkage, especially for the case of security, relates to how armed violence and, in particular, military actions can affect neighbouring countries. These linkages may occur along cross-country horizontal links at the bottom, such as, for instance, in the case of small scale operations and cross-border raids by low-ranking soldiers and the damage they do to another country’s infrastructure. Military linkages are more significant when they involve actions by conflict parties, which export violence to neighbouring countries, or, conversely, interventions by outside actors in the internal conflicts of the original country. Examples of the former case include constructing bases in neighbouring countries or conducting large-scale raids against other countries. Examples of the latter situation include military invasions or support for armed actors across border lines. In terms of Figure (2), these actions may occur along horizontal links at the bottom, affecting common individuals in both societies.

Military interaction can, however, also occur through transversal links between the top of one country and the bottom of the other country, when, for instance, the military operations of rebel groups in one country receive support (political financial, logistical or military) from neighbouring governments. These transversal linkages will be supported by a variety of motivations: national security concerns, regional rivalry, economic predatory motivations towards foreign resources, or strategic foreign influence objectives on target states. A classical example, for instance, in the case of West Africa, is the Liberian government of Charles Taylor, who provided mercenaries, money, weapons and infrastructure to rebel groups directed against Sierra Leone in the hope of gaining control of the regional economic networks and diamond mines.

Two other military factors play an important role in the transmission and persistence of conflicts across countries. The first one is arms-trade networks and their regionalised nature. The second is the existence of mercenary networks. With regard to the arms trade, it has been observed that, after being imported into a conflict region, weapons typically become the objects of “secondary regional markets” run by smuggling- and trade-networks (Lambach (2004), Studdard (2004)). These military networks

are specifically flexible and resilient. In particular, they allow conflict-affected governments and rebel groups to defy arms embargoes by creating alternative regional routes for weapons circulation, concealing both the destination and the supplying source of the weapons. While these networks physically operate across borders along horizontal links at the bottom, they also generate interactions along transversal cross-national links through the way political-military regional alliances play a role in structuring and promoting arms supplies throughout the course of a conflict. Typically, the élites in a given country may ensure that their proxy rebel groups in another country have the capability of continuing the conflict directly by arms transfers or indirectly by facilitating trade between the rebels groups and regional arm trade networks.

Even in the absence of the extreme insecurity associated with civil conflict, weak public governance could also interact with such networks and contribute the regionalisation of arms flows. Local corruption and the weak monitoring of weapons flows inside a fragile country can be exploited by regional military networks and can result in the transfer of large quantities of arms to other neighbouring states, contributing, in turn, to increased fragility and the potential for conflict in these surrounding countries.

Beyond the existence of trade networks for weapons, the existence of mercenary networks also contributes to the formation and entrenchment of regional conflict situations. In this respect, an incomplete Demobilisation, Disarmament and Re-integration (DDR) process in a given post-conflict country may leave many young ex-combatants not well re-integrated economically or socially. Such individuals may be easily attracted by the economic reward of mercenary activity, filling the ranks of mercenary manpower available in the region. A good example of this is West Africa, where there is evidence that a large pool of local “mercenaries” exists, whose members have been recruited for various conflicts in the area (Human Rights Watch 2005). For instance, ex-Revolutionary United Front (RUF) fighters from Sierra Leone have subsequently been used as mercenaries in neighbouring Guinea and Liberia.

#### 4.2.2 Economic interactions

There are, of course, a number of economic channels through which the fragility in one country may affect neighbouring countries. For instance, these countries may react by raising their level of military expenditure, thus diverting resources away from more productive investment. In addition, the fragility in one country may imply reduced trade with (and for) its neighbouring partners. First, transaction costs may increase when transport and communication infrastructures are damaged. Second, depressed local economic conditions associated with fragility may reduce income and therefore deprive trading partners of an export market or a supplier of primary resources. Finally, external investors and traders may be more reluctant to invest and trade in the region because of fear of instability. In addition, tourists may be discouraged from visiting the region. In most cases, a combination of these factors will be responsible for the economic damages to neighbouring countries. These factors occur along the bottom links between the affected country and its neighbour(s) and along the horizontal drivers between the neighbouring country(ies) and the rest of world (as, for instance, in the case of reduced tourism or FDI due to the regional contagion effect).

In the context of fragile states, other more direct consequences can be due to the existence of shadow economies. As argued, for instance, by Pugh and Cooper (2004), shadow economies are permanent features which result from the survival and coping strategies of many poor and marginalised individuals in war-torn and conflict-prone societies. During conflict and insecure conditions, with no unified control of trade routes and borderlands, these economies are used by warlords, organised crime organisations and conflict parties to transport weapons and military equipment, export conflict goods such as drugs, timber, precious metals or diamonds, and conduct financial transactions. These economies represent a structural factor which facilitates economic

interactions in the region, and mainly operate along the horizontal bottom linkages at the intersection of the socio-economic spheres of both countries.

Sometimes, these economies reflect long-standing regional trading networks that existed before conflicts and instability. An interesting example of this is in West Africa, for instance, is the case of the Lebanese diamond traders' network that developed along an informal system of diamond production and exportation which originated from the colonial period. Taking advantage of this system, conflict actors in the region developed an extended supply chain from the alluvial diamond fields in Sierra Leone through intermediate control by Liberians and Lebanese, before eventual processing in neighbouring states such as the Gambia and Liberia. This system enabled rebel groups to escape the imposition of diamond sanctions on Sierra Leone, while, at the same time, allowing neighbouring states to exploit the regulatory regime by acting as intermediaries and re-exporting diamonds from their territory.

Even when they do not involve trade in conflict or illicit goods, shadow economies may also contribute to the persistence of regional fragility through the manipulation of regional tax systems and the circumvention of regulations. In the context of weak state-enforcement at borderlands and differences in regulatory regimes across neighbouring countries, shadow economies actors may be able to derive substantial revenues by evading formal tax collections and smuggling a variety of goods.<sup>9</sup> Even in situations in which there is no domestic war, fragility as reflected, for instance, by the degree of corruption among local customs officials and police could interact with the smuggling dimension of shadow economies to affect not only the country characterised by weak public governance, but also the neighbouring states, thus depriving them of legitimate tax revenues, and thereby contributing to their own state fragility.

#### 4.2.3 Political interactions

While most economic linkages of fragility across neighbouring countries are likely to occur along the bottom horizontal links, political linkages are likely to follow the top horizontal links, reflecting the existence of networks across political élites and the pattern of trans-national alliances that may exist between political leaders and groups. These linkages can, of course, contribute to the diffusion and persistence of regional instability, by structuring relationships and actions in the military, economic, and social spheres of the region. Indeed, pre-existing diplomatic patterns of alliance and enmity may significantly influence long-term strategic decisions made by military and political actors, and have an impact upon the process of military regionalisation. Again, a notable example is the case of West Africa with Félix Houphouët-Boigny, the president of the Ivory Coast, who supported Liberian warlord Charles Taylor, not only in order to install a regime closer to the Ivory Coast in an Anglophone country in the region, but also because of his long-standing personal enmity with Samuel Doe, who was then the Liberian president.

Furthermore, as mentioned, for instance, by Lambach (2004) and Söderbaum (2004), transnational political relationships also interact with shadow economies, which can be the *locus* of profitable political exchanges between the conflict actors of one country and their allied political élites in a neighbouring state. Valuable commodities or smuggled goods can be exchanged for political support and royalties to further common objectives or continue military campaigns.

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<sup>9</sup> Cross border smuggling of this type has been recurrent in South-east Europe where trafficking has involved a large network of illicit trucking to serve western European markets with drugs, prostitutes, and other smuggled goods. It is also a pervasive issue at the Afghan-Pakistan border region where a more open trade regime in Afghanistan, compared to Pakistan, has created strong incentives for smuggling and tax evasion.

#### 4.2.4 Social interactions

As another example of the bottom horizontal cross-country linkages, trans-national social networks are important agents of regionalisation of state fragility. They include familial, kinship, occupational, and diaspora groups. When state institutions are fragile and unable to provide basic public goods and services for livelihoods, family and clan networks may fill the gap and play a vital role in supporting the survival and coping strategies of impoverished and marginalised segments of societies. Such networks give access not only to essential public goods, but also to informal finance, employment and social insurance mechanisms. Because of globalisation, migration and urbanisation, these networks often extend their connections across national boundaries and thus participate in regional linkages across neighbouring states. In Sub-Saharan Africa, this is particularly salient, as national borders have often been drawn without regard for local social conditions, resulting in a sizable number of ethnic and identity groups crossing inter-state borders. In fragile contexts with lack of state control over the borderlands, these social networks can be used by non-state actors to recruit soldiers, obtain resources and information, trade conflict-goods and shelter refugees. They are, therefore, important factors of the regional expansion and persistence of state fragility.

Regional diaspora groups are specific networks that contribute, both through political and economic channels, to home populations. They can directly provide safety transfers or indirectly sponsor their cause politically in neighbouring countries. Diasporas can also contribute to the diffusion and persistence of regional conflicts by strengthening shadow economies in borderland areas. In particular, when central state authorities are fragile and cannot monitor remote areas, diaspora groups may fill the gap and provide local governance substitutes, undermining central authority and control, and thus contribute to the persistent fragility at regional level. In this respect, the case of the Somali Diaspora is an interesting example of the ambivalent role that the Diaspora may have with respect to conflict and fragility (see Box 2).

#### **Box 2: The ambiguous role of the Somali diaspora in conflict and peace building**

The case of the conflict-driven diaspora from Somalia is an interesting example. Based upon strong clan royalties and close social ties to their homeland, the diaspora has been a powerful substitute for the lack of governmental institutions in Somalia. Remittances to family members inside the country are a well-established practice with recent estimates of about \$1.6 bn to Somalia and \$700 million to Somaliland (Lindley (2007)). These remittances represent about 23% of the Somali household income (UNDP/World Bank 2003) with up to 40% of Somali households benefiting from the money sent by the diaspora (Chalmers and Hassan, 2008).

In terms of political engagement, the role of the Somali diaspora is a controversial subject and has been perceived as a double-edged sword which has contributed significantly to both conflict and peace building. In the early 1990s, financial obligations to support the clan in times of conflict made the diaspora a powerful engine fueling internal conflicts. Evidence collected in Norway indicates payment in 2004 of individual monthly sums of \$300 with relatively high frequency; these funds being often raised from opposing clans in conflict living alongside each other in Norway. Estimates of between \$500,000 and \$5 million have been reported for aggregate funds raised in support of clan conflicts (Horst 2008).

At the same time, diaspora intervention in support of local reconciliation and state-building has been a key ingredient for success, notably in Somaliland and Puntland. The Centre for Research and Dialogue (CRD) emphasises the crucial role of the diaspora in defusing tensions and providing finance to support clan conflict resolution. This was done through the financing of the rehabilitation of local facilities such as schools and health clinics and the support of local actors to establish administrations at local, regional and national levels (CRD 2007).

Since 2000, the diaspora has also been highly visible in the state institutions of Somalia, including Somaliland and Puntland, occupying top leadership positions in the state, political institutions and civil service. The prominent role of the diaspora in Somali politics is not, however, without controversy and opposition. The returning diaspora are at times criticised as opportunists who return to take the fruits of peacetime but who have had the opportunity to escape local conflicts without contributing locally to their resolution. (based upon Sheikh and Healy (2009)).



Refugee flows represent another fragility linkage that is related to the existence of cross-border social networks. As about 90% of refugees remain inside their home regions, (Schmeidl 2002), refugee flows are essentially a regional factor which can contribute to regional fragility clusters through different channels. First, they may increase social tensions with host populations in neighbouring countries by competing for jobs and depressing wages on the local labor markets. They may alter the ethnic or political balance within the area where they find shelter. In addition, refugee flows, especially in tropical and underdeveloped regions, can facilitate the diffusion of infectious diseases and epidemics (Collier *et al.* (2003), Montalvo and Reynal-Querol (2007)). In addition, exposure to massive arrivals of refugees have negative long-term human development consequences for local populations with increases in mortality for children under five, reduced height in early adulthood, or reduced schooling and literacy rates (Baez (2008)). Finally, refugees may also directly contribute to the spreading and persistence of regional military instability and conflicts. As civilian refugees are hard to screen from former fighters and refugee warriors, refugee camps can then be taken over and manipulated by rebel organisations for training, recruitment and shelter. All these features may, in turn, trigger host population reactions and generate fragility in neighbouring states.

#### 4.2.5 Complementarities of state fragility

It is important to note that the regional effects of state fragility on neighbouring countries are compounded when these countries themselves have some dimensions of fragility, such as, for instance, a weak capacity to shelter refugees, to control their borders and to cope with the economic externalities imposed by shadow economies. The weaker the initial state of its institutions, the more likely that statehood in a particular country is to be negatively affected by regional fragility linkages. The interaction of such processes across neighbouring countries suggests the possibility of accelerating the downward dynamics of state fragility at regional level, which, once triggered, may be difficult to reverse or contain. In terms of Figure (2), the intensity of regional fragility linkages may be re-inforced by the fragility of the vertical linkages between the state and society in each country.

### **4.3 Regional Integration and Fragility**

Conceptually, the right approach to solve the externalities associated with regional fragility linkages is to provide a solution through which regional actors may internalise the effects of their actions on neighbouring states. An obvious candidate for this is regional integration. Indeed, one of the most comprehensive examples of regional integration, the European Economic Community, came about precisely as the solution to solve a major problem of regional security among fragile European societies, in the aftermath of one of the bloodiest wars in history (Zecchini 2000).

#### 4.3.1 Economic integration

Regional integration can occur under different forms and at different levels of depth. The most immediate form (and the least compromising one politically) is discriminatory regional trade liberalisation and Regional Trade Arrangements (RTAs). The economic effects of such agreements are well-known. The static effects are traditionally articulated around the benefits of trade creation (when regional integration allows shifts of trade towards more efficient producers) *versus* the costs of trade diversion (when, in contrast, integration shifts towards inefficient producers inside the region) and governments lose previously collected tariff revenues on diverted trade. Thus, the net outcome of an RTA reflects the relative strength of these effects, which, in turn, depends on various economic parameters, such as the efficiency of the partner countries' producers, the initial level of tariffs levied by countries in the region, import elasticities on liberalised goods, and the protection levied against efficient non-party countries.

Regionally integrated countries with similar economic structures may also enjoy gains from trade due to size effects, larger markets and the exploitation of increasing returns to scale. Dynamically, they may also benefit from positive learning and trade-induced productivity effects. As shown, for instance, by Coe and Helpman (1995), trade can facilitate technological transfers between trading partners, thereby affecting their factor productivity. These dynamic technological effects are more likely to exist when at least one of the trading partners is already technologically advanced, thus suggesting that developing countries would gain more in terms of productivity from North-South RTAs than from South-South RTAs (Schiff *et al.* (2002)).

The economic aspects of regional integration may also go beyond simple trade liberalisation and involve “deep integration” elements, such as non-tariff barriers, technical and regulatory norms, and border controls. Harmonisation along these lines increases market access and competitive forces within the region, thereby maximising the gains from trade creation within the area. One remaining issue, however, is the need for more sophisticated institutional capacity in their implementation stage, something that may be a limiting factor for countries already characterised by weak state capacity.

One important economic aspect of RTAs in the context of fragile countries is the loss of tariff revenues associated with discriminatory trade liberalisation. Trade-diversion effects induce shifts from taxed imports from efficient non-partner countries to the “free-of-duty” imports of partner countries. They may, therefore, induce significant reductions on collected tariff revenues. When these revenues account for nearly 34 per cent of total government revenue, as is the case for many African LDCs (UNECA (2003)), regional trade integration without compensatory measures may significantly decrease the already meagre fiscal capacity of these states, thus contributing to their fragility. In general, the proposed solution to such a problem is to complement regional trade liberalisation with a fiscal reform which substitutes trade taxes with value-added taxes, as a way to maintain the fiscal revenues at their initial level. However, empirical evidence indicates that this may be quite difficult for Least Developing Countries (LDCs), which are often already characterised by a weak state capacity at raising taxes (Baunsgaard and Keen (2005)).

Institutionally, RTAs may provide “lock-in” mechanisms on policy-making and reforms. Signing an RTA with another country may help ensure some credibility for the implementation of domestic economic reforms. RTAs become commitment devices that may be particularly relevant for states with weak domestic commitment capacity. An RTA signed with a country characterised by a stronger institutional credibility, can be used to “transfer” part of this credibility to the authorities of another country with weaker capacity. The power of commitment of such a mechanism will depend on the provisions of the agreement and the intensity of trade between the signatories. Indeed, an agreement clearly associated with domestic reforms and endowed with specific sanction mechanisms is more likely to provide external commitment for domestic reforms. Similarly, the greater the intensity of the trade flows between the partner countries, the more credible the agreement is as a mechanism for engaging reforms.

#### 4.3.2 Political integration and the boundaries of the state

The political dimensions of regional integration are at the heart of the state-building *problématique*. They fundamentally relate to the basic issue of the size of governments and the question of the forces towards the consolidation or the fragmentation of nations. As surveyed by Collier (2006), the optimal size of the state hinges fundamentally on the conflict between economies of scale in production on the one hand, and the increasing size costs of control or diversity on the other. The boundaries of the state come as the point where the benefits of scale economies offset the control costs of the territory and the population expansion and the costs of satisfying diversity in preferences (see Box 3).

### **Box 3: Political Economy Theories of the Size of Nations**

The political economy literature underlines three distinct theories which depend on the source of scale economies: military technologies, the provision of public goods, and private non-tradeable goods.

The first approach emphasises the trade-off between military economies of scale and the increasing costs of maintaining a monopoly of force as the size of the nation becomes bigger (Findlay and Wilson (1987)). According to this view, conflict and military technologies benefit from scale advantages and tend to favour the emergence of large nations. On the other hand, big national entities bring the disadvantage of geographic distance, rapidly increasing the costs of territory control. This dimension is compounded when size comes with increasingly culturally-diverse populations, making it harder to develop a shared sense of legitimacy and thus increasing the costs of state enforcement.

The second approach focuses on the idea of the state as a mechanism which supplies a range of public goods to people with different preferences (Alesina and Spolaore (1997)). As public goods are produced under increasing return to scale, size effects induce efficient production of these goods. At the same time, however, larger states include individuals with more heterogeneous preferences. Thus, bigger states become less and less able to satisfy these diverse demands. Beyond some point, the tension between economies of scale and preference heterogeneity is such that groups at the periphery prefer to secede and supply their preferred public goods on their own.

Finally, the third theory of the size of the state is concerned with scale economies in the production of private goods. Again, states may not be large enough to exhaust scale economies. This argument, however, is only valid for the case of non-tradeable private goods, whose exploitation of returns to scale depends on the size of the local economy. Some of these non-tradeable goods may be important for the organisation and quality of governments and states. A typical example is media specialised in the financial, economic and political discussion of public policies and performance. Subject to strong knowledge-intensive economies of scale in production, these goods have a definitive non-tradeable character as the market for discussion on national policy issues is unlikely to be of major interest to people outside the country. For local political governance, such media are, however, important, as they enable the development and diffusion of informed discussions and monitoring on public policies by larger groups of the civil society. Large countries can support such specialised media, while, in contrast small-sized nations cannot. Thus, the level of understanding of both policy and governance, and the quality of public debates are likely to be lower in small societies which, according to this view, are likely to face weaker rule of law, unchecked political opportunism, and the under-provision of public goods.

(Based upon Collier (2006))

#### 4.3.3 The political dimensions of regional integration

The aforementioned forces leading towards political consolidation may result in important transition costs (such as wars and conflicts). An alternative to accommodate them more smoothly is for countries to enter into regional integration agreements that encompass some political dimensions. The typical example of this is the formation of regional trade *blocs* for “non-economic reasons”, such as security, peace, and development of political and social institutions.

The idea that regional trade integration may bring peace and security between neighbouring countries is based upon the more general argument, already expounded in section that increasing international trade might improve security across countries. Through increased economic interdependence and the building-up of economic interests in peaceable relations, international trade increases the cost of war. In addition, more trade means more interaction between peoples and governments, which leads to more familiarity with the neighbour’s culture and institutions, and, in turn, the building-up of mutual trust. Intense trade links also increase the security of access to the essential input of partners and reduce the threat of trade embargoes. On the political side, trade talks allow political and/or economic élites to communicate and provide the opportunity for them to form

coalitions for subsequent collaboration and consensual action. Interestingly, all these effects re-inforce each other, and lead to virtuous circles of integration of economic and “non-economic” dimensions.<sup>10</sup>

Regional integration agreements may not, however, always be effective routes to peace and security. In particular, when the distribution of the benefits and costs of integration is asymmetric, this may generate frictions and tensions between partner countries. The pattern of regional trade after integration may induce strong industry relocation and economic distributive effects within the region. Some countries may face economic losses to the extent that, without adequate compensation, they prefer to stay out of the integration agreement, at the cost of reduced security. Regional integration in such situations is perceived as being so unfair that it actually worsens intra-regional security. Indeed, Venables (2003) shows that sub-regional trade deals between low-income countries are likely to generate economic divergence, the poorest members of the integration scheme losing relative to the least poor members.<sup>11</sup>

An often cited example of this kind of situation in the African context is the case of the East African Common Market which included Kenya, Tanzania and Uganda. The strong economic asymmetry between Kenya and its partners ultimately led to the dissolution of the agreement. Indeed, Tanzania and Uganda complained about the income transfers which the common external tariff on manufactured goods created. They were also concerned about the effect of industrial agglomeration of the agreement in Nairobi, at the expense of Dar es Salaam in Tanzania and Jinja in Uganda. Failures to negotiate compensation mechanisms inside the region led to the collapse of the Common Market, the closing of the borders, and the confiscation of Community assets in 1978. This, in turn, generated an atmosphere of hostility and distrust which contributed to the conflict between Tanzania and Uganda in 1979. This example suggests that, to be politically successful, regional trade agreements should involve relatively evenly balanced partners. Along this line, the success of the EU can be attributed not only to a strong commitment to regional security, but also the fact that France and Germany, the key players in the EEC, were relatively on an equal footing after the Second World War.

Beyond the basic political objective to build regional peace and security, regional integration agreements may address other regional externalities such as migration flows. Typically, North-South agreements, such as NAFTA between the US and Mexico, or the Euro-Med Agreements between the EU and Mediterranean countries, are examples of regional integration experiences partly motivated by these considerations. Whether these agreements are able to mitigate migration problems depends upon whether trade and migration flows are complements or substitutes. The traditional analysis of trade theory holds that they are substitutes, so that increased trade integration is likely to reduce income or wage differentials and decrease labour migration incentives. More recent analysis on trade and social networks, however, indicates that trade flows and migration may well be complements. This dimension can be of particular relevance for poor and fragile countries. In such economies, informal and shadow sectors are important conducts of trade flows across countries. As activities in these sectors are articulated along various types of cross-border networks, regional trade and migration are likely to be complement. Further integration in such regions may, thus, induce more migration rather than less.

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<sup>10</sup> Schiff and Winters (1998) present a simple conceptual framework illustrating these ideas. They show that, when increased mutual imports provide additional security between neighbouring countries, it is worth subsidising these imports by lowering their price relative to other goods. Direct price subsidies would be the preferred instrument to achieve such a result. However, under tight fiscal budget constraints and political economic considerations, it might be easier to create a regional trade agreement whereby imports from the rest of the world are taxed, thereby lowering the relative price of intra-*bloc* imports, in order to achieve enhanced security.

<sup>11</sup> Interestingly Venables (2003) analysis shows that on the contrary regional integration arrangements between high-income countries generate forces for convergence.

#### 4.3.4 Regional integration and institution-building

One of the most interesting dimensions of regional integration agreements for our discussion of fragile countries is the fact that they may be used as the tools of institution-building. Entering in a trade *bloc* with strong “club rules” can help anchor democratic reforms and transfer credibility in member countries. Clearly, commitment to democracy and human rights will only be truly effective if the penalties for violating them are severe and their enforcement credible. The enforceability of such “rules” depends positively on both the value of belonging to the *bloc* and the credibility of sanctions in the case of non-compliance. The larger the common market of the *bloc* and the greater its bargaining power with the rest of the world, the larger the value of belonging to the *bloc*. With regard to sanctions, the credibility to apply them is likely to be greater if breaking club rules by one member entails a large cost to the other members. This cost may be direct and economic, but it may also be indirect and political, such as signalling and reputation effects.

This reasoning suggests some interesting implications in terms of the types of regional agreements that are more likely to help successful political institution-building. First, regional integration agreements between small low-income countries trading little with each other, are less able to impose serious sanctions on the deviators of the “club rules”. These agreements are therefore unlikely to be very effective. Conversely, trade *blocs* with large (important) partners will be more credible at enforcing “bloc-rules” and therefore will provide better anchors for political institution-building. Similarly, because interdependences are likely to be larger with close neighbours than with a distant country, regional integration agreements between neighbours are likely to be more effective institution-building mechanisms than those between distant partners.

Two other considerations may be added for the effectiveness of “club-rules” trade *blocs*. First, it seems unlikely that authoritarian regimes, or even countries with fragile democracy, will prove to be strong disciplinarians even if a democracy rule exists in the *bloc*. Second, the system should be such that a potentially credible enforcer has to see enforcement as an important issue for itself. This means that large and important partners should not use their superior (and credible) position in order to enforce for opportunistic motives. Enforcement of the “club rules” has to be itself a “rule-based” mechanism.

#### 4.3.5 Regionalism, pooling sovereignty and bargaining with third parties

Entering into a regional integration agreement necessarily implies some loss of control over particular dimensions of public policies. The extent of the loss of national sovereignty depends on the precise form of the agreement. For instance, a free trade area agreement only requires the obligation of free duty trade within the region, leaving each partner country the autonomy to choose its external tariffs against non-partner countries. A custom union is more binding, as countries adopt a joint external tariff, and also create a joint institution for the sharing of trade tax revenues. Other forms of integration are deeper than simple trade agreements, implying the building up of joint decision-making institutions on different domains (trade, currency, factor mobility, competition, fiscal or security issues). By doing so, regional integration agreements are also “pooling sovereignty” mechanisms through which members may be able to strengthen themselves in terms of economic leverage, political forces or cultural identity *vis-à-vis* the rest of the world.

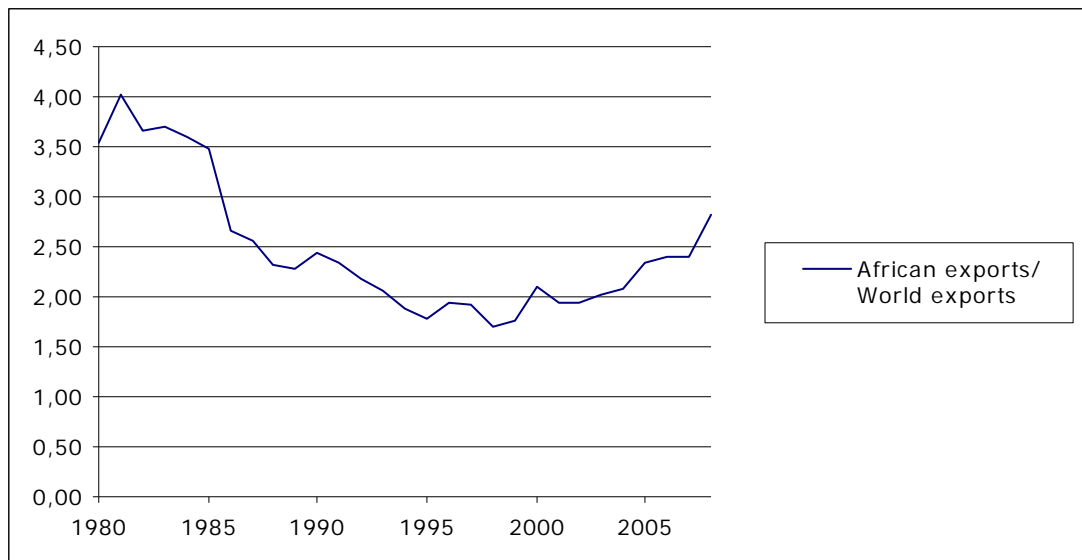
In this regard, an important function of regional integration is to re-balance the power asymmetries that exist in the international world. For small countries, regional co-operation (which can, but need not, involve trade preferences) can strengthen their bargaining position in bilateral and multilateral negotiations with other nations or with multilateral agents. By pooling their financial resources, time and expert knowledge, they are more likely to increase their limited technical capacity, reduce their negotiation costs, and gain political leverage by articulating common positions. The gains of such co-operation are easier to realise when these countries share common interests; the cost of international negotiations is high, and the issues to be dealt with are complex (Andriamananjara and Schiff, 2000).

## 5. Challenges of Regional integration in Africa: “Weak Trade” and “Weak States”

### 5.1. General Background: The Marginalisation of Africa in World Trade

The weakness and declining position of Africa in world trade patterns is widely-recognised. Indeed, over the last thirty years, Africa’s share in world exports has declined from almost 4 per cent in the beginning of the 1980s to below 3 per cent in the current period, as is illustrated in Graph 1.

**Graph 1: Africa's share in world exports (African exports/world exports), period 1980 to now**



The elements of such a situation have been well-documented: inefficient productive structures and small domestic markets, specialisation in the exportation of natural resources and commodities subject to price volatility, weak diversification in exportation patterns, poor policy and protectionist trade regimes, land-locked territories, high trade-costs due to weak infrastructure, corruption and bad governance systems, and disruptions due to local conflicts and insecurity.

There is, however, some debate on whether the observed pattern of African exports is consistent with an efficient utilization of its trading opportunities and fundamentals, or whether it reflects poor policy choices or weak infrastructure. Some analyses find evidence for the marginalisation of Africa in world exports, and assert that African losses in world trade are due to lack of product diversification and shrinking market shares for traditional goods (Sachs and Warner (1997), the World Bank (2000), Subramanian and Tamirisa (2001)). In contrast, other studies argue that Africa’s trade flows have been consistent with predicted patterns (Foroutan and Pritchett (1993), Rodrik (1998), Coe and Hoffmaister (1998)). These studies observe that African countries participate in international trade as much as can be expected according to international benchmarks for trade volume derived from a country’s income level, size, and geographic location.

Using a new dataset on trade protection (the Market Access Map database, (MacMap)), Berisha-Krasniqi *et al.* (2007) has revisited the issue of Africa’s trade performance. The merit of this database is that it captures a more comprehensive set of trade protection measures and allows for country-specific levels of market access. For the period 2001 to 2004, and checking for the existence of the two large-scale preferential trade arrangements for Africa: (the *Everything but Arms Initiative*, and the *African Growth and Opportunity Act*), the authors estimate the levels of existing market access for Africa, and they investigate whether or not Africa trades less than its predicted level. The results show that Africa has good market access at continent level, but that there are significant variations across

African countries, with 21 countries having better access than the world average and 32 countries having market access below that average. Using a gravity model to analyse the patterns of bilateral trade, the analysis also indicates that GDP, geographic distance, and protectionist barriers in foreign markets do not fully explain Africa's poor trade performance. Trade-related infrastructure, such as air and road transportation and communications infrastructure, are also important factors which contribute to the explanations for Africa's trade marginalisation. Moreover, looking more specifically at road density and cell phone density, the authors find that the marginal impact of cell phone density on trade performances is larger in countries characterised by larger road density. This analysis suggests some significant complementarities across types of trade-related infrastructure.

## **5.2 Formal Regional Integration: Pitfalls and Challenges**

### 5.2.1 Economic dimensions

Regional integration in Africa has a longstanding history. From an economic perspective, it has been considered an appropriate policy response to some of the key factors and supply constraints that may hamper rapid growth and sustained development in a typical African economy. These factors include small domestic market size, landlocked territory, poor infrastructure and the increasing trade marginalisation of Africa on world markets. Regional trade agreements are then thought to allow African countries to derive substantial economies of scale with larger regional markets, enhance domestic competitiveness, raise returns on investments and subsequently attract foreign direct investment, which, in turn, will lead to technology transfer and growth. In addition, regional agreements enable these economies to pool resources for the joint provision of a range of infrastructural projects. This, again, enables these economies to exploit economies of scale and to internalise the cross-country regional effects of such investments. Finally, a combination of several small countries in a regional *bloc* would enable them negotiate economic policy issues more effectively with other trading *blocs* or big private partners such as multinationals (Collier 2006).

In response to a context of global regionalism with proliferating regional agreements and a continuing process of marginalisation of the continent; African countries, like many other parts of the world, have followed the typical defensive strategy of creating more RTAs or strengthening the existing ones. The result has been a dense web of RTAs in which most African countries have multiple memberships.

While these agreements differ in many dimensions, they also share a number of common features (Yang and Gupta 2005). First, the proclaimed goals are overly ambitious. The desired level of regional integration is high and goes, to a large extent, beyond simple trade liberalisation exercises. Many RTAs are intended to be part of deeper regional integration schemes with other non-trade components. This often exceeds the limits of state capacity and the realistic political commitments that these countries can effectively deploy, leading to substantial implementation delays or policy reversals. Second, the primary focus is generally on intra-regional tariff reduction. One exception to this rule is the South African Development Community (SADC), which is also significantly involved in the co-ordination of regional sectoral projects, such as energy and infrastructure. Third, all these RTAs are characterised by different rules of origin (ROOs), some of which are quite restrictive. A typical example is again SADC in which the initially simple and uniform ROOs have been revised and become more restrictive, generating substantial restrictions to internal trade in the region.<sup>12</sup> Fourth, given that trade taxes represent almost one-third of the public revenue of a typical African economy, revenues losses are important concerns in the design and implementation of the RTA. This feature

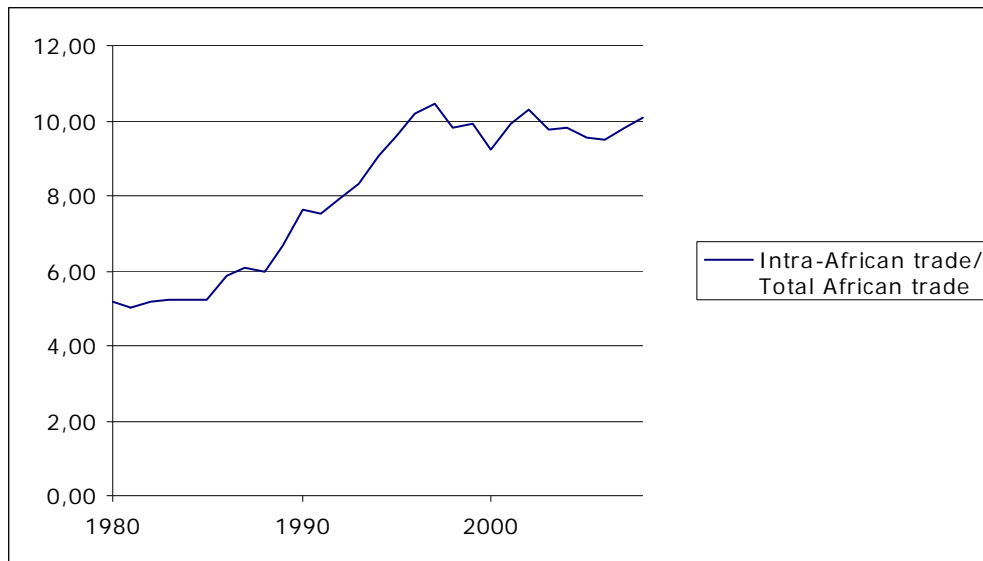
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<sup>12</sup> Initially, the SADC ROOs involved a minimum 35 % of the value added within the region, or a maximum of 60% of the value of total inputs. The rules have been revised to become product specific and to require also the use of detailed technical processes (Flatters 2002, Flatters and Kirk 2004).

may also be especially important for fragile countries with very limited capacity to raise additional taxes.

In terms of outcomes, it is widely recognised that the economic effects of RTAs in Africa have been rather disappointing. First, the impact of the RTAs on intra-African trade seems to have been small or insignificant. For instance, since the mid-1990s, as a share of the continent's global trade, intra-African trade has stagnated at about 10 per cent of total African trade despite the multiplication of efforts to integrate regionally (see Graph 2).

**Graph 2: Intra-African share of total African trade, period 1980 to now: (exports + imports of Africa to Africa) / (export + imports of Africa)**



As observed by Yang and Gupta (2005), while regional trade intensity in Africa (the share of intra-Africa trade in African trade normalised with Africa's share in world trade) may *appear* to be significant, this is due mainly to Africa's marginalisation in the global markets, rather than due to the performance of intra-regional trade. Empirically, the evidence that RTAs in Africa have an effect on intra-African trade is rather mixed. Some studies find that, whenever they had an effect on intra-African trade, these RTAs mainly caused trade diversion (Elbadawi (1997) Cerrere (2004)). Other studies find the impact of African RTAs on intra-regional trade to be insignificant (Kasekende and Ng'eno 1995; Lyakurwa, 1996; Robson, 1998).

Moreover, RTAs do not yet seem to have contributed much to Africa's export performance in world markets. As already mentioned, the share of Africa in world trade has declined from about 4 per cent in the 1970s to about 2 per cent at present. Africa's competitiveness in manufacturing has not improved, either. In fact, during the period 1970-2003, Africa's share of manufactured exports in global manufactured exports has stagnated at a meagre 0.5 per cent (Yang and Gupta (2005)).

The structural economic reasons for these outcomes are well-known and typical of South-South trade agreements. African countries exhibit similar market patterns and comparative advantage structures. They are mainly specialised in the few commodities and primary goods that they export to the developed countries from which they import manufacturing imports. Their trade pattern lacks regional complementarities (Yeats 1998). Moreover, despite the efforts to increase intra-regional trade, there are persistent Non-Tariff Barriers, be it because of high transaction costs due to weak trade-related infrastructure, corruption or conflicts (UNCTAD 2001, Portugal-Perez and Wilson (2008)), or because of the complexity and technical difficulty in implementing the myriad of the rules of origin associated to these agreements (Fanta 2008, Khandelwal 2004). For instance, in the case of the



Common Market for Eastern and Southern Africa (COMESA), the asymmetrical implementation of trade rules has hindered the development of intra-regional trade, rendering trade business formalities more difficult, uncertain and costly. As noticed by Fanta (2008), the majority of COMESA member states have not yet (or only weakly) implemented the COMESA simplified trade regime. Hence, Non-Tariff Barriers “such as non-acceptance of the rules of origin certificates, cumbersome bureaucratic procedures, and restrictive standards are common problems” which impede intra-regional trade (Khandelwal, 2004).

Insecurity and fragility have also been noticed as a major challenge for successful regional integration in Africa. ((UNECA, (2006), Fanta (2008)) As pointed out by these studies, conflicts and insecurity undermine regional integration by increasing transaction costs to trade, by diverting economic and governments’ resources away from integration, and by creating distrust that impedes regional co-operation.

In the “spaghetti bowl” of RTAs in Africa, multiple and overlapping memberships are also an important factor that contributes to the weak effectiveness of regional arrangements in Africa. (Geda and Kibret (2007), UNECA (2004), Yang and Gupta (2005), Feng and Genna (2005)). For instance, it is argued that multiplicity and overlapping membership affects the capacity of a state to commit to specific RTAs rules and obligations, thereby limiting the attainment of the goals set out. In addition, overlapping memberships impose strains in terms of both human capital and in terms of the financial resources that can typically exceed the capacity limit of African countries, thereby leading to delays or poor policy implementation (Jakobeit, Hartzenberg and Charalambides (2005)).

Another reason of weak effectiveness is when a state belongs to different regional *blocs* that have different tariff schedules, rules of origin, and implementation periods. These differences create harmonisation and legal uncertainty, especially when different trade arrangements apply to trade between two countries. In addition, the resulting effect of the multiple rules of origin generates a cumulative result of overlap which affects intra-regional trade for specific RTAs. Adding to this, overlapping membership generates “goal dilution”, in the sense that a state attempts to direct its undivided attention to the attainment of the goals of a single regional *bloc*.

An interesting systematic empirical study validating the previous argument is that of Chacha (2008). It examines the factors that affect the level of intra-regional trade among four regional trading *blocs* in Ssub-Saharan Africa: the Common Market for Eastern and Southern Africa (COMESA), the East African Community (EAC), the Economic Community of West African States (ECOWAS), and the Southern African Development Community (SADC). Looking at the period up to 2000,<sup>13</sup> the analysis shows that multiple memberships in various regional trade agreements negatively affect the intra-regional trade of a specific agreement. Interestingly, the analysis also indicates that weak transportation infrastructure (measured as the average percentage of the paved roads within each *bloc*), weak overall governance within the member states of each regional *bloc* (as measured by the Freedom House Political Rights score index) and conflicts within the *bloc* tend to have adverse effects on intra-*bloc* trade.

### **5.3 “Informal Regionalisation” and Regional Fragility**

Most economic analyses of regional trade integration in Africa have mainly been concerned with the impact of RTAs on formal intra-regional trade-flows. In the context of regional clusters of fragility, this might overlook the importance of informality in trade-flows that is associated with porous borderlands across fragile and instable countries. In Africa, it has been argued that such processes of “informal regionalisation” could be crucial dimensions to understand the impact of regional

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<sup>13</sup> The study period for COMESA is 1977 – 2000, EAC is 1989 – 2000, ECOWAS is 1971 – 2000, and SADC is 1976 – 2000. The year periods include five years prior to the formation of the *bloc* and then the successive life span of the *bloc* until the year 2000.

integration in Africa (Chabal and Daloz (1999), Vvan Dde Walle (2001), Fanta (2008), Söderbaum, (2004)).

In particular, the multiplication and persistence of conflicts in certain regions of Africa have stimulated the development of shadow economies and networks that reflect the coping strategies of marginalised communities, or the opportunism of non-state actors such as warlords and transnational crime organisations. Along these regional networks, intense informal or illicit trade-links connect different countries. A well-known example of such informal cross-border trade-flows in West Africa is the extended illicit-diamond supply chain that connects Sierra Leone, Liberia, the Gambia and Burkina Faso. Another example throughout Eastern Africa is the case of the trade in illicit small arms. Fanta (2008) reports, for instance, that, according to estimates of the South African-based Institute of Security Studies (ISS, 2000), in the year 2000, there were around 2 million illicit small arms and light weapons circulating within East Africa and the Greater Horn region (ISS, 2000).

Persistent conflicts and insecurity also have consequences on migration patterns and the movement of people and refugees. These migration flows are often complements to shadow trade flows within the region, and thus they contribute to informal regionalisation. In some cases, the grass-root forces of regionalisation may not be limited to refugee-flows triggered by regional instability. Informal intra-regional trade-flows may actually be sustained on a more constant basis through trans-border communities that tend to escape the formal control the state. An interesting example of this in the Eastern Africa Horn is the case of pastoralists groups whose territory often spreads across more than one state in the region. According to Markakis, (1994), the Great African Horn is the place with highest concentration of traditional pastoralists in the world. These groups contribute extensively to informal trade-flows within the region. Benefiting from the weakness of state control over cross-country borders, pastoralist networks not only conduct trade of small crop or livestock quantities over short distances, but also sustain significant trade volumes over long distances (Little (2007)).

While, by definition, it is difficult to assess precisely the importance of such shadow regional trade, casual observations suggest that this might be quite significant, especially in fragile regional clusters. For instance, it has been noticed in the case of Somalia, which has been without effective government control for the last 16 years, that the export trade in small stock from Somalia (including Somaliland) was much more dynamic in 1998 than during the period before 1991 when the country had a government.(Little, 2005). In addition, in the case of Ethiopia, during the period 1999-2000, the export of *Khat*, a mild narcotic traded informally in the Horn, was estimated to be the second most important source of export earning after coffee (Dechassa, 2001).

Systematic quantitative estimates of informal cross border food trade in Southern Africa are obtained through The Famine Early Warning System Network (FEWS NET). They suggest significant informal trade flows in the region. For example, Table 1 gives a sense of the importance of informal flows of maize for Malawi for the three periods under review 2005-2006, 2006-2007 and 2007-2008. Recorded informal imports represent between 36% to 76% of total imports in the country.

**Table 1: Malawi maize trade flows (thousand MT)**

<b>Period</b>	<b>2005/2006</b>	<b>2006/2007</b>	<b>2007/2008</b>
Total imports	456	166	79
Formal imports	176	31	3
Informal imports	165	80	60
food aid	115	56	17
Total exports	1	4	341
Formal exports	0	0	334
Informal exports	1	4	7
Informal imports as % of total imports	36	48	76

Source: Malawi National Early Warning Unit FEWS NET and informal Cross-Border Food Trade Monitoring System

What are the costs and benefits of such regional trade systems for fragile states in Africa? On the one hand, “informal regionalisation” is an essential part of the coping strategy of poor marginalised communities in a weak institutional context characterised by insecurity and a lack of access to basic public services. Thus, informal regionalisation processes contribute positively to the survival conditions of these individuals. In addition, when they are built on long-established trade networks, they reflect the functioning of traditional systems of both governance and rules that are useful alternatives to the lack of effective formal institutions in the region. For instance, these grass-root processes can serve as informal mechanisms of contract enforcement between buyers and sellers, filling the gap left by the absence of formal property right protection. In this sense, informal trade flows may be the only viable way of economic exchange in fragile regional clusters, and may, therefore, contribute to the realisation of some gains from trade.

Informal trade processes may, however, also impose significant costs to the region. First, as already mentioned, they often involve weapons and illicit goods, which contribute to the persistence and diffusion of regional conflicts. They are also the means through which trans-national criminal organisations secure human and financial resources, impacting negatively on the security of the countries in the region. Finally, they escape government control and taxation. By providing alternative means through which to conduct trade, they negatively affect the capacity of states to raise revenues, thereby contributing further to the fragility of the region. For instance, estimates of informal trade flows of bovine livestock from Chad to Nigeria show that about 65% of exports are informal, implying a loss of taxes revenues of about 4-5% of public revenue in 2001 (Massuyeau 2002).

#### ***5.4 Security, Sovereignty and Regional Integration in Africa: Old Ways and New Approaches***

The conceptual views mentioned in Section 4.3.2) on the optimal size of the state and the importance of scale economies in military force, public goods, and private non-tradeable goods, indicate that the typical African state is likely to be too small (Collier 2006). In addition, standard theory on internalisation suggests that both the supply of regional public goods (such as cross country transportation and network infrastructure), and the regulation of regional public ills, (such as neighbourhood arms races, disease control, and insecure borderlands), should be realised through intra-African arrangements.

Since the beginning of the post-colonial period, however, political dynamics in Africa have not led to the direction of the political consolidation of nations at continental level, and the extent of the regional integration of political power has also been limited due to little devolution of power to regional organisations. Indeed, the initial logic of political regionalism in Africa, as expressed by post-colonial Pan-African rhetoric, has rested on a strong attachment to state sovereignty, as was exemplified in the Charter of the Organisation of African Unity (OAU) through the principle of non-interference (Gandois 2005). Just after independence, the priority for African élites was to establish a certain degree of political consolidation within their own territories. Unable to resist any war of invasion at the time, it was in their joint interest to affirm their current borders as permanent. External sovereignty was, therefore, the counterpart of internal state weakness. As mentioned by Herbst (2000, p. 110):

“The OAU established a decision-making rule that preserved African borders and prevented any kind of external competition while requiring only minimal levels of effective domestic sovereignty.”

The same rationale for domestic regime survival explains the subsequent dynamics of regionalism (Clapham (1996), Fanta (2008)). The success or failure of a regional arrangement depends upon how the agreement is perceived as strengthening (or not) the domestic political position of leaders, who constantly weigh the advantage of membership against the opportunity cost of free-riding. As noted by Fanta (2008), the logic applies to regional security matters, such as, for instance, the opt-out from the Inter-Governmental Authority for Development (IGAD) by Eritrea once the latter felt that the

organisation had become too constraining for its own security objectives. The same weakness of political commitment also applies to economic matters, as, for instance, in the case of Tanzania, which withdrew from COMESA in the year 2000, not only to focus more on its membership to SADC, but essentially because the fast-track implementation of a Free Trade Area (FTA) by COMESA did not fit with the government's strategy to promote its national industry.

Despite the underlying logic of regionalisation in Africa, it has been argued that regional integration has not contributed much to the domestic political consolidation and security of African states (Andreatta, Ardeni, and Pallotti (2000)). Indeed, although Africa enjoys the highest number of RTAs, it is also the most civil war prone region in the world. However, more systematic investigations provide evidence that suggests that the institutional details of the RTA may matter for its effects on civil wars. For instance, using various datasets of the civil conflicts in Africa during the period 1950-1999,<sup>14</sup> Henderson, Powers, and Dietrich (2006) investigate the impact of RTAs on the onset of civil wars. Checking for the usual determinants on civil wars, the analysis differentiates between the types of RTAs (*i.e.*, those with military provisions, those with stipulations for democracy, and those without them). The results indicate that RTAs are, in general, associated with lower occurrences of civil war. However, RTAs with specific security provisions in the arrangement do not seem to have a significant conflict-dampening effect. Ironically, this suggests that the institutional design most directly associated with the prevention of armed conflict appears to be ineffective in preventing civil wars. The authors argue that it may actually reveal the very initial logic of African security regionalism that focuses more on the prevention of interstate wars, rather than on the prevention of intrastate wars. However, although indicative, it should be noted that the analysis faces the usual difficulty of identifying the direction of causality as civil war occurrence may also potentially affect the participation of a country in a specific RTA.

Though formally claimed, it should be noted that the affirmation of external sovereignty and non-interference has been an elastic notion in several areas of Africa. Specifically, in regional fragility clusters such as in the Great Horn, the Great Lakes Region or West Africa, it has been common for the governments in a given country to provide military or logistic support to rebel groups operating in a neighbouring country, and *vice-versa*. These phenomena have generated situations of domestic instability and fragility, masking "latent cross-country conflicts".

In the early 1990s, the traditional pan-African approach to regionalism changed and the norm of external sovereignty and the principle of non-interference started to get eroded. Given the persistent instability and insecurity in several fragile states in Africa, several peacekeeping and peace-building interventions have been led by regional organisations. In this respect, the intervention of the Economic Community of West African States (ECOWAS) Monitoring Group (ECOMOG) in Liberia created a decisive impulse that was subsequently formalised in its Protocol Relating to the Mechanism for Conflict Prevention, Management, Resolution, Peace-Keeping and Security of 1999 (Gandois (2005)). This new approach to sovereignty reframed as a responsibility to protect has now been extended to continental level as part of the Constitutive Act of the African Union. Associated with these facts are the financial, logistical, and operational mechanisms that allow participation at regional level in humanitarian and peacekeeping operations.

### **5.5 Regional-led Governance Building in Africa: Limits and Dilemmas**

In the case of fragile states characterised by weak governance structures and strong power asymmetries between élites and society, one important question is whether processes engineered at regional level can help contribute to effective state-building in these societies. Two conflicting perspectives prevail. The first one starts from the premise that regional policies have ultimately to be

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<sup>14</sup> The dataset used are the Correlates of War (COW) data on civil wars, the Fearon's (2003) data on violent civil conflicts, and the Nicholas Sambanis data on civil conflicts.

implemented at state level, and that weak states only produce weak policy-implementation. As Kuhnhardt (2008) notes: “weak states only produce weak integration”. The alternative view recognises both the importance of the regional inter-dependences that lead to fragility clusters (UNECA 2004) and the failure of a pure “state-centred” approach to capacity building (Kaplan 2006). It argues therefore that regional organisations have to be strengthened in order to tackle these problems effectively. Ultimately, the question rests on how far African states are willing to “pool sovereignty”, in order to allow regional processes to be sufficiently effective to alter and compensate institutional deficiencies at country level. While the first perspective takes as a starting point the traditional Pan-African approach with little devolution of powers to regional level, the second one assumes that it is possible to have some regional-led processes of governance-building in association with international actions from the outside.

In this sense, the new regional approach of the African Union (AU) and the creation of the New Partnership for Africa’s Development (NEPAD) can be interpreted as recent attempts to “pool sovereignty” in order to improve African governance. The instrument of NEPAD is the African Peer Review Mechanism (APRM). The mechanism was inspired by the OECD peer review process, which has been used as a means of bringing pressure to bear upon the national governments of developed countries. For African countries, there are potentially three pressure points. First, the APRM works as a signalling mechanism that puts pressure on countries to participate, as non-participants are shown as being fearful of criticism. Second, once a review has been completed, information is revealed that puts pressure on the countries to comply with the proposals both through peer and domestic civil society pressures. Thirdly, for the same reason, third parties, such as donors or investors, can use the results of the APRM to design and monitor their policies, thereby framing the incentives for reforms. Given that the APRM has only recently started, it is still difficult to assess its contribution to state-building and governance reforms in Africa. Peer pressure to participate has proved to be relatively effective, as a majority of countries have made a commitment to engage in the process. As of January 2009, 29 countries have signed the Memorandum of Understanding acceding to the APRM.<sup>15</sup> By now, ten countries have completed the process. While in most cases, the reviews appeared to be important efforts to assess governance structures and the kind of policies that need to be changed, it remains to be seen how these public assessments will lead to effective pressure and to the implementation of reforms.

Along with this new consultative approach, the AU has tried to set standards in various areas of governance. It has provided observers for elections and has set up an African Security mechanism to organise military peace-making and peacekeeping. While this represents a significant break with the old approach of non-interference, the effectiveness of the AU in these areas is, at best, mixed. As mentioned by Collier (2006):

“Its observers of elections have worked to more lenient standards than other observers. Of the several *coups* that have occurred in Africa since the AU came into existence, only one has been reversed by AU pressure, namely, Sao Tome, Principe, which is the smallest country in Africa. The AU has failed to reverse more recent *coups* in the Central African Republic and Mauritania. Similarly, the AU military intervention in Darfur, though a major step forward, has clearly not yet ended the killing.”

Conceptual considerations suggest that regional-led governance-building processes are more likely to be effective when the arrangement includes major (important) partners that are more credible at enforcing “*bloc*-rules”. At the same time, enforcement of the “club rules” has to be itself a “rule-based” mechanism, in that the major partners have to see enforcement as an important issue in itself

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<sup>15</sup> As at January 2009, the following 29 countries have signed the Memorandum of Understanding acceding to the APRM: Algeria, Angola, Benin, Burkina Faso, Cameroon, Djibouti, Egypt, Ethiopia, Gabon, Ghana, Republic of Congo, Kenya, Lesotho, Mali, Malawi, Mauritania, Mauritius, Mozambique, Nigeria, Rwanda, São Tomé & Príncipe, Senegal, Sierra Leone, South Africa, the Sudan, Togo, Tanzania, Uganda, and Zambia.

and should not use their superior (and more credible) position with regard to enforcement for opportunistic and hegemonic motives. This introduces an important policy dilemma in the sense that the characteristics which make a major member a credible enforcer of *bloc* rules are also precisely those which may induce it to become hegemonic. This ambiguity may generate mistrust within the *bloc* and may limit the effectiveness of the rule-based system that is to be implemented.

In the African context, this type of situation is illustrated with the examples of the two regional agreements with dominant partners: ECOWAS with Nigeria, and SADC with South Africa. It is true that the existence of a major player in the region has stimulated some leadership that allowed African security missions to be conducted on the continent (in Liberia with ECOMOG for the case of Nigeria, and in Lesotho with SADC for the case of South Africa). In both cases, though, there have been presumptions that the use of the regional mechanisms was *ex-post* rationalising some opportunistic motives. For South Africa, its position as a credible enforcer of “good governance rules” in SADC has also been somewhat undermined by the historical legacy of apartheid and the inherited degree of mistrust that still exists with its regional partners. As noticed by (Qobo (2007)), p. 17):

“South Africa’s claim to the status of ‘security manager’ in Southern Africa, although not officially pronounced, is not uncontested, especially by countries such as Zimbabwe which have previously enjoyed a status of a regional hegemon before South Africa was re-integrated into SADC.”

The enormous economic disparities between South Africa and its regional partners have also continued to feed the feelings of envy and the fear of regional hegemony, which have reduced its legitimacy as a regional leader. These have also stimulated other SADC countries to enter into alternative regional arrangements in order to countervail South Africa’s dominance, as, for instance, Zambia, Zimbabwe, Mauritius and Malawi, all SADC members, which are simultaneously participating in the Common Market for Eastern and Southern Africa (COMESA) FTA arrangement.

## 6. The EU Approach to Regional Integration in Sub-Saharan Africa

### 6.1 The European Union Economic Partnership Agreements

The European Union is the major trading partner for most African countries. Dating back to the Treaty of Yaoundé (1963), which formalised trade and development relationships between the European Economic Community and its former colonies, the EU has developed a specific approach to Sub-Saharan Africa. In 1975, the EU granted African, Caribbean and Pacific countries (ACPs) unilateral preferences under the Lomé Agreements (I-IV). As the discussion in Section 5 suggests, these preferences had limited success in achieving the intended goal of promoting economic development in ACP countries. Various reasons were identified to explain these disappointing results. As already mentioned, some of the well-known explanations hinged on supply-side constraints, and lack of “good governance” and institution-building. Another explanation is related to the unilateral character of the preferences, which was argued to have contributed to highly-protected and non-competitive economies (EC Green Paper 1996).

In such a context, and with the expiry of the last Lomé Agreement (IVbis), the EU has been engaged in a different approach, with the creation of WTO-compatible reciprocal trade agreements between the EU and regional *blocs* of ACP countries, by establishing so-called Economic Partnership Agreements (EPAs), which were to be in place by 2008.<sup>16</sup> EPAs are supposed to be asymmetrical

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<sup>16</sup> The WTO allows for preferences only when they are part of reciprocal free trade agreements or when they benefit developing countries (DCs) on a non-discriminatory basis. As the Lomé Conventions (and then the Cotonou preferences) are not reciprocal (EU exports do face tariffs when entering ACP markets) and are extended to only some DCs (and not

trade agreements which cover not only trade in goods and services, but also “behind the border” issues, such as competition, government procurement, intellectual property, and trade facilitation. According to the official line of the EC, this type of “trade agreement” is comprehensive and should be designed to retain the core objectives of previous EU-ACP trade arrangements. They should be development-oriented for ACP countries, combined with a deepening of regional integration, the enhancement of market access for ACP products in the EU market, and increased co-operation on services and trade-related issues. It is understood that, by improving their competitiveness, EPAs should help the integration of ACP countries into the global economy and promote their economic growth.

EPAs initially involved six ACP regional groupings, then seven with the EAC (East African Community), of which four (now five) are in Sub-Saharan Africa (Stevens and Kennan 2005). In an EPA between the EU and a regional grouping, the latter negotiates as a single *bloc*, though the agreement is signed bilaterally. The non-Least Developing ACP countries that do not belong to regional groupings which implement an EPA have two alternatives. They can implement a Free Trade Agreement with the EU as in the case of the South Africa’s FTA (the Trade, Development and Co-operation Agreement (TDCA)), or they can access the EU via the Generalised System of Preferences (GSP), which is, however, less favourable.

The EPAs were due to be concluded by 31 December 2007, the date of expiry of the WTO waiver for the Cotonou Preferences. However, the negotiation process was difficult, and, a few months before the 31 December deadline, little progress had been made in most negotiations. Given this, several regions and individual countries have initialled *interim* EPAs in order to avoid the situation whereby, if a WTO-compatible alternative was not agreed upon on the 1st of January 2008, many ACP countries would trade with the EU on less advantageous terms.<sup>17</sup>

In Sub-Saharan Africa, 18 countries have initialled interim EPAs (Stevens *et al.* (2008)). The remaining ACP countries, apart from South Africa, export to the European market under the EU GSP: the EU favourable “Everything but Arms” (EBA) sub-regime for the Least Developing Countries (LDCs), and the less favourable standard GSP for Nigeria, the Democratic Republic of the Congo, and Gabon. As mentioned, South Africa continues to export under its own FTA with the EU, (the TDCA).

## **6.2 The Uncertain Trade Outcomes of EPAs for Sub-Saharan Africa**

The outcomes of EPAs have been hotly debated in the economic and policy literature. Many economic and econometric studies highlight their uncertain outcomes. Theoretically, the net outcome depends on the balance between the trade creation and the trade diversion effects. Empirically, there are methodological issues, impact studies which rely on simulations based upon general or partial equilibrium models, the conclusions of which depend on the specific assumptions of the models. As noticed by Sindzingre (2008), and Delpeuch and Harb (2007), partial equilibrium methodologies are useful for issues that are easily quantifiable, such as identifying products which are vulnerable to import surges or losses in tariff revenue. However, these approaches cannot be used in the analyses of the total effects of EPAs. Conversely, Computable General Equilibrium Models allow for the modelling of global interactions across markets, but their results are subject to the specific closure rules used to solve the model. In addition, other dimensions such as aid effectiveness, the re-inforcement of the ACP productive capacity, the re-inforcement of institutions and trade capacity are difficult to quantify.

In order to assess the potential impact of EPAs on Sub-Saharan African countries, the first dimension to examine is the extent to which the dismantling of tariffs has an impact on protection. In this respect, Stevens and Kennan (2005) argued that most ACP countries could sign EPAs and still

(Contd.) \_\_\_\_\_

many DCs in Asia and South America), they are not compliant with WTO legislation. Until now, this situation was maintained through the granting of a waiver at the WTO. However, this waiver expired on 31 December 2007.

<sup>17</sup> To date, the Caribbean is the only region to have signed a full EPA.

avoid a rapid and substantial liberalisation if they chose to retain their highest tariffs. As high tariffs (which allow effective protection) are imposed on only a limited number of products, which do not represent much more than 20 per cent of their imports from the EU, the ACP countries could eliminate relatively low tariffs while retaining their protection on the 20 per cent of their trade that faces the highest tariffs rates. Similarly, Delpuech (2007) notices that, for most ACP countries, at least 50 per cent of total imports from the EU face tariffs of 10 per cent or less (that is, tariffs that are less protective). Removing these tariffs would allow ACP countries to fulfil a significant share of the effort asked in EPAs without considerably undermining their current protection scheme. This suggests that EPAs would not generate significant liberalisation and thus that the associated theoretical gains from trade could be relatively small.

It is difficult to get a consistent picture of the potential trade impact of the EPAs on Sub-Saharan African countries. The impact results are varied both on a regional and on a country basis, whether a partial equilibrium methodology is used (see, for instance, Fontagné *et al.* (2008), Zouhoun-Bi and Nielsen (2007)) or whether general equilibrium simulations are used (see Adjasi and Kinful (2006), Bouet *et al.* (2007), and Keck and Piermartini (2008)). For instance, Keck and Piermartini (2008), based upon a general equilibrium model (an extended version of GTAP model) show that this EPA is welfare-enhancing for SADC, and will lead to significant increases in real GDP. On the other hand, using a general equilibrium approach, Adjasi and Kinful (2006) have simulation results which show that, with the exception of the EU and Ghana, the rest of ECOWAS suffer GDP and welfare losses arising mainly from the adverse terms of the trade effects of the EPAs. Summarising the diversity of potential outcomes clearly, the study by Bouet *et al.* (2007) uses the MIRAGE model of the world economy. (a multi-sector, multi-region, computable general equilibrium model devoted to trade policy analysis). They find that the implementation of EPAs has an extremely varied effect on ACP countries. SADC and part of Eastern and Southern Africa in particular, and, to a lesser extent, the Caribbean and Pacific, would find it beneficial to conclude an EPA. On the other hand, for countries such as Senegal, Nigeria, the rest of Western, Eastern, and Central Africa, Angola, the Seychelles, and the Democratic Republic of Congo the implementation of an EPA does not lead to a surge in exports because they already benefit from very good access to the European market. Conversely, after liberalising their economies to European products, these countries are likely to experience a substantial increase in imports.

### **6.3 The Potential Effects of EPAs on “Fragility” Parameters of Sub-Saharan African Countries**

From the perspective of fragility and institution-building, what can the implications of EPAs for Sub-Saharan African countries? Three particular dimensions merit special attention: trade taxes, agriculture, and regional integration.

#### **6.3.1 Trade taxes are reduced**

From the perspective of fragility and state capacity-building, an important issue concerns the potential impact of EPAs on the tariff revenues of Sub-Saharan African countries engaging in such agreements. Given the importance of trade tax incomes in public revenues for African countries, a reduction of tariff revenues associated with reciprocal trade liberalisation could seriously hamper the capacity to satisfy the basic state functions - that have been outlined in Section 2 - adequately. In opposition to the variety of results obtained on the relative strength of the trade-creation *versus* trade-diversion effects, most impact estimates of EPAs on tariff revenues suggest that the losses may, indeed, be very significant (Delpuech and Harb (2007)). West Africa is likely to be the most affected region with loss estimates for ECOWAS varying from about 30% to up to 89.5% of tariff revenues (Busse *et al.*, 2004). These results indicate that, without appropriate compensating measures, EPAs may have significant negative consequences on the capacity of Sub-Saharan African states to raise public



resources. This is even the more important given that it is well-known that poor countries have difficulties in substituting trade taxes for VAT taxes (Baunsgaard and Keen (2005)).

### 6.3.2 Special attention should be given to agriculture

Another dimension of special importance for ACP countries (and SSA countries in particular) is the impact of EPAs on the agriculture sector. Given that it is the major employment sector of SSA countries, the sector directly connects the economic resilience of fragility situations by offering alternative opportunities to conflict- and insecurity-related activities. Agricultural performances in these economies are, however, often characterised by high volatility, low yields compared to international standards and concentration on a few primary commodities. Without due attention, integration with the international agricultural market may, therefore, force the sector to marginalisation with negative consequences for the economic resilience of these economies (Delpuch and Harb (2007)).

To date, there have been few systematic studies of the impact of EPAs on the agricultural sector. Given the importance of the informal economy, assessing the impact of trade liberalisation on the SSA countries is obviously difficult. Notwithstanding this, some NGO case studies that have discussed the impact of lowering agricultural tariffs in SSA, have suggested important negative outcomes for some agricultural sectors (such as, for instance, tomatoes and processed tomato products in Senegal, (Christian Aid (2005), and Action Aid (2005)). Delpuch and Harb (2007) also note that the degree of competition that SSA producers will face from EU products will depend on the Common Agricultural Policy (CAP) that the EU will implement and the degree of subsidisation of its products. Finally, given that agricultural sectors are the most protected ones, they are the most likely to see important trade diversion effects (Bouët *et al.* (2007)).

### 6.3.3 EPAs and Regional Integration in Africa: Building Blocks or Stumbling Blocks?

One of the claimed objectives of EPAs is to strengthen regional integration within Africa. Conceptually, EPAs could be opportunities for African countries to rationalise their web of regional integration agreements and the problems associated with overlapping memberships. In addition, from an institutional building perspective, these comprehensive agreements may be used as an external commitment mechanism for weakly institutionalised African states to undertake necessary internal reforms, anchoring themselves to the stronger institutional context of the EU.

There have been major concerns, however, about the actual potential of the EPAs to foster regional integration in Africa, and, in particular, around the ambiguity of EPAs as building-blocks or stumbling-blocks. An important difficulty has been related to the large Sub-Saharan African (SSA) country heterogeneity within the different EPAs groupings. Countries differ, first, in terms of their export structures, and therefore also in their strategic trade interests. For instance, oil-exporting Gabon does not have the same interests as more economically-diversified Cameroun

Second, the classification of countries as ACP countries, which includes LDC and non-LDC countries, has also created problems. In SSA, some countries are not part of the ACP group. As the LDCs can benefit from tariff-free access to the EU through the Everything But Arms initiative (EBA), they have weaker incentives to enter EPAs than non-LDCs. Moreover, for those who choose to stay with the preferential EBA agreement, they will have to implement new border controls with EPA-signing neighbours countries in order to prevent the transiting of European products through their borders.

Third, the different EPAs of SSA include groups of countries that exhibit higher degrees of integration than others (for example, the UEMOA within the EPA grouping of ECOWAS, the EAC within ESA and the SACU within SADC (Stevens *et al.* (2008)). As noted by the ODI-ECDPM study (Stevens *et al.* 2008), the interim EPAs in SSA proved to show large heterogeneity in their

commitments. In only one region, the East African Community (EAC), does more than one country have the same commitments as the others. In West Africa, only two EPA countries have initialled significantly different texts with different liberalisation commitments.

One crucial issue, in particular, comes from the fact that countries in the same regional *bloc* have signed EPAs with different lists of sensitive products, the harmonisation of which at regional level is a very difficult task, given the national specificities about budget losses and political economy forces. Lack of harmonisation will again necessitate border controls on the movement of EU products within regional groupings in order to ensure that the exclusion of a product in one country is not undermined by preferences for the same product in a partner country (Brenton *et al.* (2008)).

Even for the EAC, which has maintained a coherent regional configuration, it is argued that the consequences of a separate interim EPA may have an uncertain outcome for regional integration, as some EAC countries are also part of other regional integration processes (Tanzania, is a member of SADC, and Burundi, Kenya, Rwanda and Uganda are also members of COMESA) (South Centre (2008)).

## **7. “Fragility Responsive” Regional Integration and European Policy**

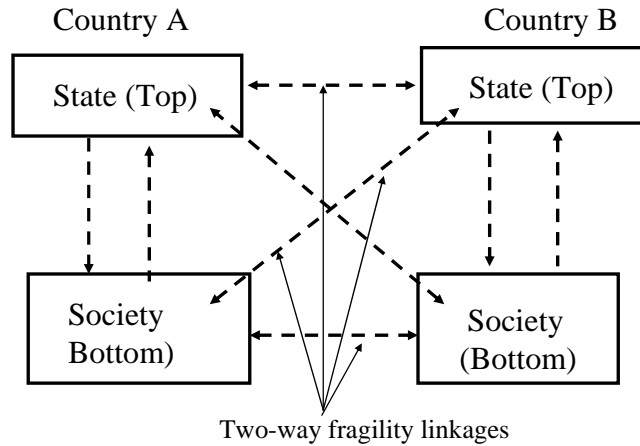
The various inter-dependences leading to regional fragility clusters in SSA suggest that policy responses should be targeted at the regional level. Conceptually, regional integration mechanisms which help internalise spillover effects across neighbours, or which compensate specific local institutional weaknesses, seem natural ways to tackle the problem. In the case of Sub-Saharan Africa, however, this approach has, at the every best, proved to be of limited success. As Section 5 suggests, because of poor governance, weak national institutional structures and/or lack of political will, regional policies have often been poorly implemented. At the same time, a pure “state-centred” approach to capacity building has also been recognised as facing strong limits (Kaplan 2006).

What can the role of EU policy be in this context? The discussion in Section 6 above indicates that the current regional approach of the EU towards the SSA does not integrate explicitly the specificities of a “fragility sensitive” institutional-building perspective for the SSA countries. This section investigates what the components of a more “fragility responsive” regional approach could be. In so doing, it suggests some policy implications which may help fill the gaps in this direction.

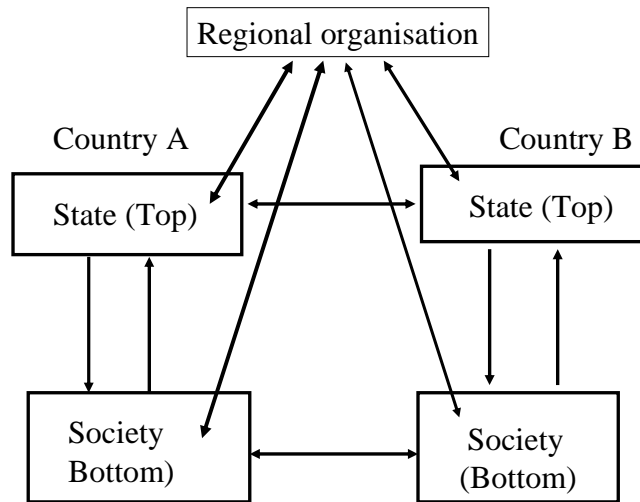
### **7.1 Analytical Considerations**

To organise the discussion, the simple analytical framework outlined in Section 4 may be useful. The regional problem of fragility clusters can be contrasted in Figures (3a) and (3b).

**Figure 3a: Regional fragility Cluster**



**Figure 3b: Benchmark Regional integration**

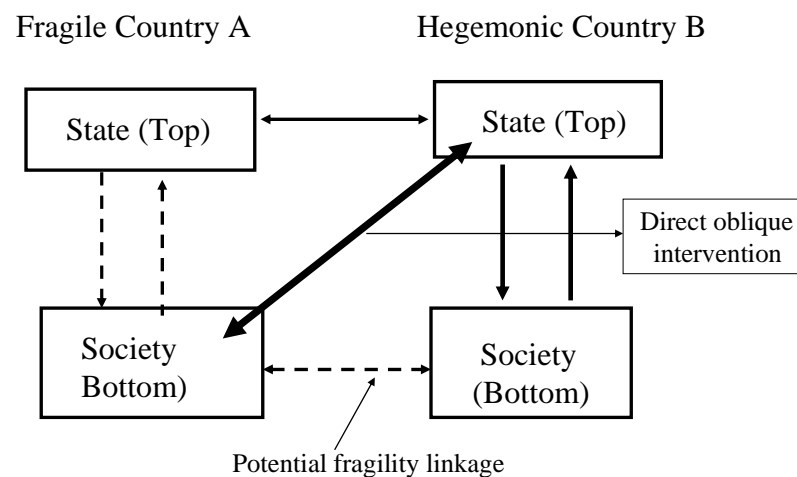


In Figure (3a), within-country vertical relationships between the state and society are weak, while cross-country links (horizontal and oblique) present features of fragility linkages as discussed in Section 2 above. This reflects the situation of weak states at full regional level with important negative re-inforcing effects along all the links. In contrast, Figure (3b) illustrates the benchmark situation, in which all the links are strong: strong vertical relationships between state and society within-country as well as across countries. In such a situation, a regional approach to solve economic, political or social externality issues across countries is the ideal solution. Civil societies at the bottom in all countries extend their strong vertical relationships with states also to include transversal linkages with the regional organisation. The subsidiarity principle applies. Member states devolve part of their sovereignty at regional level to a regional organisation in order to deal with regional and global externalities, while they maintain control on domestic policies that essentially have a local content.

Conceptually, the basic problem of a “fragility responsive” regional approach would be to move from a situation depicted in Figure (3a) in the direction of one depicted as Figure (3b). In a typical regional situation such as Figure (3a) in which all neighbouring states are weak, a top-down regional approach to the problem is unlikely to be an effective solution. As argued by Kuhnhardt (2008), “weak states produce weak regional integration”. As all links across the different spheres are weak, there is little hope for good regional policy design, implementation and political co-operation by the different governments, and little feedback/monitoring from society at the bottom. An entry point for policy for such a case might be to concentrate directly at the level of society (bottom level) and integrate as much as possible the regional dimension of fragility at this level. This could be done by stimulating actions that increase regional local positive externalities and mitigate negative spillovers at the bottom level. For instance, more effective peace preserving and security actions, and increased promotion of and co-ordination with traditional and grass-roots organisations that supply public services and infrastructure in borderland areas could help reduce the incentives for communities to participate in war-related regional economies, and could facilitate other, more positive, informal trade and productive activities.

From a regional point of view, a more interesting case is the mixed situation of fragility in some countries and sufficiently strong institutions in other neighbouring states. As is depicted in Figure (3c), country A is characterised by fragile vertical relationships between state and society while, in contrast, country B has reasonably strong vertical interactions. There are, however, regional linkages that may be factors of regional fragility. One important policy issue, in such a context, is whether regional integration is a mechanism that helps state-building in the weak countries and prevents the diffusion of fragility to the other stronger neighbours.

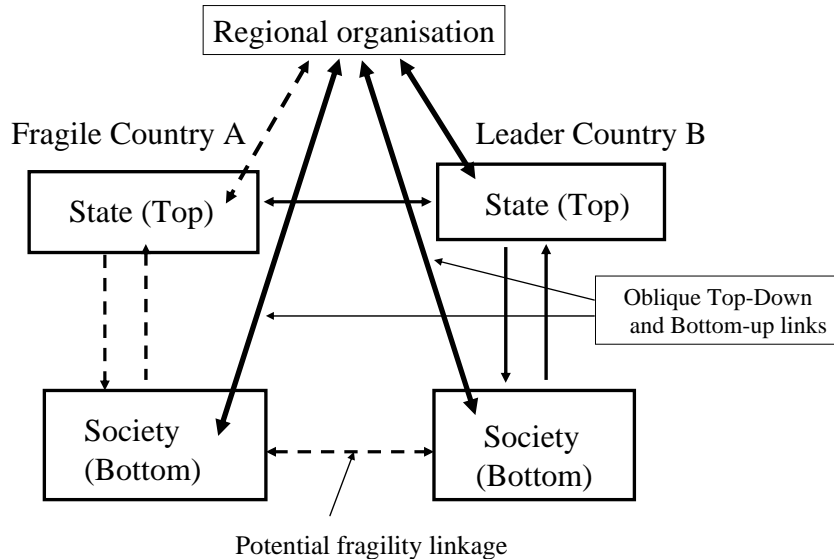
**Figure 3c: Regional Hegemony and Potential fragility Cluster**



In terms of Figure (3c), one direct way to compensate for the weak state-society relationship within country A and to mitigate the negative cross-country regional linkages would be to have the institutionally stronger state B directly strengthen the transversal link with the society of country A. In this case, state B directly imports its more resilient institutional structures to the society of fragile state A, and both societies are connected through strong links to state B. However, this type of direct intervention would not be beneficial or possible, if it were perceived as an hegemonic move of country B in the region. In that case, it would reduce the legitimacy of the implementation process locally and, would also, possibly, deteriorate the horizontal relationships between the two states. A better

alternative then would be the use of regional organisation, as depicted in Figure (4), which deals directly with the regional trans-country spillover and the regional public good effects.

**Figure 4: Regional Leadership and Fragility**



A number of elements are worth mentioning in this respect.

1. In order to be effective, there is a need for both the commitment and the leadership of the stronger state (i.e., the existence of a strong link between state B and the regional organisation). Funding and capacity should be sufficient to be able to build effective top-down links that can effectively reach societies and re-inforce their horizontal economic and social interaction. Areas related to the provision of regional public goods, such as peace, security, and infrastructure, are classical examples.
2. The regional leadership should be exerted in ways that are perceived as legitimate by the other weaker states in order to prevent a deterioration of the horizontal links across states. Thus, the organisation should be “rule-based” with a clear and transparent governance structure.
3. There should also be a strengthening of the bottom-up transversal link between the regional societies and the regional organisation. This is important for the feedback/monitoring of the regional organisation’s interventions. It is also important for the sustainability of the regional organisation. First, in stronger states with some degree of leadership, it creates constituencies that have an interest in “locking-in” the commitment of their country to the regional organisation. Second, bottom-up feedback from civil society builds legitimacy for the regional mechanism. Third, it may be an essential component of early warning systems that may provide a better understanding of the dynamics of fragility in weak areas and thus help design responses that prevent fragility diffusion and clustering which could be much more difficult to tackle later.
4. The strengthening of the bottom-up transversal link between the regional organisation and the society of a weak country can also be an important step towards state-building inside that country by strengthening the vertical relationships between the state and society. Indeed, the literature on state-building processes distinguishes two types of constraints in fragility contexts. The first one is a capacity constraint related to the state lack of administrative, human and technical resources to create and manage functional public institutions. The second constraint is associated with the political (un-) willingness of the state and its élites to actually implement socially beneficial institutions (DFID 2005). Clearly, regional action and pooled resources that locally promote

security, public service delivery, and civil society responses can alleviate the capacity constraint of neighbouring states in fragile situations. At the same time, the strengthening of bottom-up links between civil society and the regional level can also help reduce the willingness constraint. Indeed, as a mechanism that generates information on the deficiencies of the fragile country, it provides signals that can be used to stimulate and sustain peer pressure effects between governments at this level. It can also be used by external agents and donors. All these can create pressure that may force unwilling élites to accommodate, to some extent, their positions in their fragile countries.

5. In the context of fragility, there is the usual trade-off between bypassing the state and providing short-term efficient service delivery through non-state actors and long-term state legitimacy-building. Clearly, one may face the same issue when local actions are supported by regional organisations. Re-inforcing oblique links between civil society at the bottom and regional organisations at the top should be carefully managed so as not to crowd out the potential strengthening of vertical relationships within fragile countries. Thus, special attention should be devoted to ensuring that these links tend to develop in complementary ways, rather than as substitutes to each other. One possibility is to promote the funding and development of regional networks of local civil society organisations, such as, for instance, the Economic, Social and Cultural Council of the African Union (AU ECOSOCC). Such networks could become the locus of intense interactions and mutual consultations, allowing the exchange of information on best-practices, problem-solving issues and efficient pressure strategies that could raise the capacity of local civil society organisations to induce institutional change from their fragile state or unwilling élites.

## 7.2 “Fragility Sensitive” Regional Policy in the African Context

What are the entry points for external intervention, and what are the policy implications for Regional EU policy in the African context?

Entry points for external intervention can occur at several levels. In general, when “capacity” is the binding constraint of state-building in fragile contexts, a “state-centred” type of approach will enter at the state level (top) and provide resources which promote the capacity to comply with the three core state functions as described in Section 2. Budget support and “whole of government” approaches are generally acknowledged as being adequate to ensure ownership and legitimacy-building (Brinkerhoff 2007). In contrast, when “willingness” is the binding constraint, project aid (entering at the bottom level) is preferred.

A regional perspective, however, emphasises the explicit recognition of “regional linkages” and the possibility of “regional clusters of fragility”. In addition, taking a more global view of the issues, it highlights the role of external drivers at national and regional level. This indicates the regional level as a natural entry point.

Consistent with this perspective, in Accra 31 October 2007, the EU has engaged in a new comprehensive regional approach with the African continent under the Joint Africa-EU Strategy (the JAES). This approach is based upon the principles that:

“This partnership and its further development will be guided by the fundamental principles of the unity of Africa, the interdependence between Africa and Europe, ownership and joint responsibility, and respect for human rights, democratic principles and the rule of law, as well as the right to development. In the light of this new partnership, both sides also commit themselves to enhance the coherence and effectiveness of existing agreements, policies and instruments.”

Strategic priorities have been identified in along various political economic and social components, from peace and security, to trade and regional integration and other key development issues, such as the Millennium Development Goals. The first Action Plan (2008-2010) has been articulated around 8

Africa-EU Partnerships in specific areas (peace and security, democratic governance and human rights, trade and regional integration and other key development issues).

How can this strategy be seen from the perspective of institutional development and state-building in fragility contexts? While it does not explicitly acknowledge the problem of regional clusters of fragility in Africa, the Strategy clearly recognises the importance of regional action and co-ordination in areas associated with state-building, such as peace and security, and political governance. Some direct transversal fragility dimensions, such as migration, organised crime, and trafficking of arms and people, are also highlighted. In addition, there is an emphasis on strengthening oblique regional linkages by promoting the functioning of the African Peer Review Mechanism and the participation of civil society and non-state actors in regional processes.

So far most of the efforts of the JAES have been organisational and architecture building (Tywuschik and Sherriff (2009)). While this is necessary and useful to establish dialogue, trust and coordination between EU and AU stakeholders, expectations are high for further real delivery and funding commitments. Several policy prescriptions may make the JAES more “fragility sensitive” and help trigger regional led institutional building processes.

The above discussions have suggested various elements of a “fragility sensitive” regional response that can be included in the JAES framework.

#### 7.2.1 A systematic two-tier approach is needed for effective regional integration in Africa

While a top-down approach to the problem of regional fragility is important in order to integrate the various regional fragility linkages identified in Section 4), a bottom-up approach based upon the development of a strong responsive civil society that has stakes in the process of regional integration is also essential. Targeting resources for the explicit strengthening of non-state actors to participate in APRM processes and other regional consultations will increase the legitimacy of these processes and also allow interesting comparability across African states, stimulating further Peer Pressure Effects. It is important to ensure that the top-down and bottom-up approaches are complementary.

The JEAS already explicitly recognises the issue of civil society engagement in regional processes of institutional building with the roles of the Economic, Social and Cultural Council of the African Union (AU ECOSOCC) and the EU Civil Society Organizations (EU CSO) Steering Group. As emphasised though by Tywuschik and Sherriff (2009), the AU ECOSOCC and the EU CSO Steering Group are likely to face significant challenges to participate in relevant meetings in the future in view of the shortage of financial resources .in funding. Commitments by the EC to put additional funding to ensure Civil Society Organisations engagement remain so far unclear. A sustained and committed funding and consultative effort should therefore be made to ensure the viability of civil society engagement in this regional process.

#### 7.2.2 The right level of regional integration should be found

The above discussion on regional arrangements with weak states suggests that such a solution is unlikely to be effective without the existence of a regional leader committed to the functioning of the mechanism. Thus, it is important to identify the right contour at which a regional strategy is most effective to mitigate the effects of fragility. The Regional Economic Communities (RECs) might not be the right configuration. Indeed, while ECOWAS and SADC have natural regional leaders with Nigeria and South Africa respectively, the situation is more complex for COMESA or the Economic Community of Central African States (ECCAS), which overlap with some members of the more integrated EAC. In addition, special attention should be given to the provision of incentives for a “rule based” system at the sub-regional level, so that the locally-dominant country is perceived as a regional leader, rather than as a regional hegemon. This risk has been stressed by ECOWAS for Nigeria and SADC for South Africa.

Within the JEAS, the EU could contribute to the effective implementation of a subsidiarity principle based on trust that could be applied at an adequate sub-regional level. This could be done within each strategic partnership by promoting more sub-regional political dialogues with the relevant countries. Given the importance of local leadership for a regional solution to contribute to state building in the region, it is important to provide adequate incentives for regional leaders like Nigeria and South Africa to enter fully into their regional EPA and to provide leadership in the dynamics (so far they have not signed any interim agreement and are trading with the EC under other trade regimes).

#### 7.2.3 Make sure that the EU approach to regional integration in Africa is promoting “Building Blocks” and not “Stumbling Blocks”

One major difficulty is how to cope with the great heterogeneity of SSA countries in terms of their economic/political characteristics. In particular, the existence of the Everything but Arms (EBA) Initiative that provides full quota-free, tariff-free access to EU markets to LDCs, has complicated the EPA negotiation process by creating different trading environments and negotiating incentives for the LDCs and non-LDCs in SSA, some of which are members of the same RTAs in Africa. One way to promote ‘Building Blocks’ integration in SSA would be for the EU to provide EBA market access to *all* SSA countries signing EPAs. Also, the rules of origin (ROOs) under both the Cotonou Agreement and the EBA Initiative are complex and restrict SSA exports. They need to be reassessed and simplified in order to maximise the benefits of full market access under the EPAs.

#### 7.2.4 Care should be taken of the differential outcomes of integration in regional groupings

Given the substantial degree of economic heterogeneity that exists within African regional groupings, it is very likely that integration with the EC and the global market more generally will have significant differential impact across countries. In particular, configurations of sub-regional “Hub-and-Spokes” can emerge or be re-inforced, thus creating tensions and increased inequalities within the sub-grouping. Thus, special attention should be given in order to mitigate such situations and implement transfer mechanisms that reduce regional inequalities. Sub-regional investment projects should be designed and subsidised to favour local convergence.

Within the JEAS, political dialogues between the EC and sub-regional leaders may be targeted to stimulate their contribution to such sub-regional compensating mechanisms. In this respect, the EU could use its own experience to participate in the promotion of sub-regional structural funds.

#### 7.2.5 Towards a more “fragility responsive” EU Trade policy

The EPAs are likely to produce significant reductions in tariff revenues for the African countries which engage in them. Many fragile African countries are LDCs. As they are still enjoying EBC conditions of preferential access, they have not signed Interim Agreements. Notwithstanding this, a number of countries (such as the Ivory Coast, Burundi and Rwanda), which are still on the verge of fragility, or with limited public resources, have been engaged in EPAs. It is essential that their efforts at state-building are not hampered by important reductions in public tax revenues. This suggests that special attention should be made to compensate these losses and to promote fiscal adjustments. While the EPAs will include development co-operation provisions, there are no legally-binding quantitative funding obligations to facilitate these adjustments. Predictable and tangible commitments with regard to the latter by the EU would be essential to reduce the vulnerability of SSA countries which could be brought into a zone of fragility by negative shocks, especially in the current context of the economic global crisis. Furthermore, this would strengthen the policy coherence of the EPAs which aim to support development and regional integration in Africa.

As the discussion in Section 3 indicates, there may be threshold effects of globalisation in fragile countries. This suggests that specific consideration should be given to such threshold effects in the



design of a trade integration strategy. For instance, in the “Raw Material Initiative” of the EU and its first pillar on “Access to raw materials on world markets in undistorted conditions”, the EU should explicitly commit resources to promote mechanisms such as the EITI+<sup>18</sup> in order to ensure that it is “fragility responsive”.

Moreover, the mechanisms should take care of the sub-regional dimension of fragility clusters and the potential spillover effects on neighbouring countries. In particular, it is essential to recognise the importance of informal regional trade networks in mineral and raw material commodities in Africa and to design ‘conflict-sensitive’ trade integration strategies taking into account these dimensions.<sup>19</sup>

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<sup>18</sup> The Extractive Industries Transparency Initiative plus (EITI+) is an initiative by the World Bank to complement the EITI and seeks to develop national capability to handle the effects of commodity booms and to channel natural resource revenues into fighting poverty, hunger, malnutrition, illiteracy and disease.

<sup>19</sup> The case of regional trade in minerals from Eastern Democratic Republic of Congo is a good example of the importance of such a perspective for the design of a trade integration strategy of the Great Lakes Region (Garrett and Mitchell (2009)).

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