10. Informal cross-border trade and smuggling in Africa
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10.1 INTRODUCTION: THE AFRICAN TRADE PUZZLE

The low level and discrepancies of recorded intra-African trade flows have been noted for at least 30 years (Berg 1985; Yeats 1990). This situation has continued or even expanded despite structural adjustment programs involving trade liberalization and extensive integration schemes aiming to promote formal integration. There are some 30 regional blocs in Africa, and on average each of the 53 countries on the continent are members of four often overlapping groups (Yang and Gupta 2005; UNCTAD 2009). Yet official intra-African trade accounts for only about 10 percent of total African exports and imports, far below other regions of the world (Keane et al. 2010).

Casual observation in the countries themselves, however, reveals that informal cross-border trade (ICBT) is thriving almost everywhere in Africa. There have been numerous case studies of ICBT in the last two decades, most by sociologists, anthropologists and political scientists rather than economists; Lesser and Moisé-Leeman (2009) survey a few of these studies. These studies cover a great many border areas in Africa, including, among others: the Horn of Africa – Somalia, Ethiopia, Kenya (Little 2005; Teka and Azeze 2002); Southern Africa – South Africa, Zimbabwe, Malawi, Zambia, Mozambique (Ndlela 2006; Mijere 2009; Macamo 1999); Kenya–Uganda (Ackella-Ogutu 1997); Congo (MacGaffey 1991; Kabamba 2013); Uganda (Titeca 2009; Titeca and de Herdt 2010); Nigeria–Cameroon–Chad (Roitman 2004; Amin and Hoppe 2013); Benin–Togo–Niger–Nigeria (Igué and Soulé 1992; Azam 2007; Golub 2012; Hashim and Meagher 1999; Galtier and Tassou 1998); Senegal–The Gambia (Golub and Mbaye 2009); Ghana–Togo–Burkina Faso (Chalfin 2001); Sierra Leone (Pritchard and van den Boogaard 2013).

Informal trade can involve two types of illegality, in the goods themselves (for example, narcotics) or in the manner of trading (evasion of customs duties and regulations). Both types of illegal trade occur in Africa. West Africa serves as an important locus for international trade by organized crime in narcotics, notably cocaine (United Nations Office on Drugs and Crime 2013). Cocaine produced in South America is often transshipped to Europe via West Africa and increasingly methamphetamines are produced in Nigeria and exported to Europe, the Middle East and Asia. However, although most informal trade is illegal in the narrow sense that it is unreported and fails to comply with statutory tax rates and other regulations, the products involved are generally not in themselves illegal to trade or use. This chapter focuses on unreported trade of legal goods. Such trade in legal goods has varying degrees of illegality in terms of its intentions and compliance with tax and regulatory statutes. Four kinds of unrecorded cross-border trade in legal goods can be distinguished.

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1. *Official transshipment of imports and exports*. Coastal countries often act as hubs for land-locked countries, or even for coastal countries whose ports are congested or which contain regions that are more easily reached from a foreign port. This trade is official and recorded by customs, at least in principle, but is often not included in the country's trade statistics as reported in national documents and standard international data sources such as the IMF *Direction of Trade Statistics* and the UN Comtrade database.

2. *Cross-border trade in traditional food grains and animals*. Trade in traditional agricultural products and livestock in bordering countries may involve little or no intent to deceive the authorities, as peasants and herders ignore artificial and un-policed borders, traversing areas as they have for centuries, mitigating surpluses and shortages of staple foods, thereby alleviating price fluctuations and contributing to food security and poverty reduction.

3. *Parallel trade of primary product exports and consumer goods imports*. This involves efforts to evade export and import taxes or regulatory compliance. To the extent that customs authorities in Africa do not measure these goods, they are not recorded as African exports or imports, but if the origin or destination is outside Africa, they may be captured by mirror trade data in the partner country in another continent.

4. *Unofficial re-exports of legally imported products*. A particularly significant component of unofficial trade in Africa involves 're-exports' whereby goods are imported formally into a low-tax or low-cost country with the intent of then transshipping them clandestinely into neighboring countries with higher taxes, restrictive import quotas, costly trade facilitation services or tougher regulatory standards. Re-exports involve a complex mix of formal and informal practices and legal and illegal trade, reflective of the complexity of the informal sector in Africa.

Categories 2–4 constitute ICBT but only the last two can be considered smuggling. Discussions of ICBT often fail to distinguish between these forms of unrecorded trade, but they may have quite different causes and welfare effects. For example, smuggling has very different implications from ICBT in traditional agricultural products. On the other hand, in practice, these various types of cross-border trading activities may be intertwined and difficult to distinguish empirically. For example, goods may be declared for transit but intended for use in the domestic market or for smuggling into neighboring countries.

This chapter surveys the literature on ICBT in Africa in economics and other social sciences. Many of the examples are drawn from West Africa, the author's area of expertise, but attention is also devoted to other parts of sub-Saharan Africa. Section 10.2 summarizes the economic theory of smuggling, showing that smuggling can be either welfare-enhancing or reducing. Section 10.3 presents approaches to studying smuggling, considering several quantitative and qualitative techniques. Section 10.4 discusses the social organization of cross-border trade, emphasizing the integration of ICBT with the informal sector, which plays a dominant role in most African economies. Section 10.5 discusses the causes of widespread ICBT, including: artificial and porous borders inherited from the colonial area; weak border enforcement; uncoordinated trade and other policies among neighboring countries, leading to large price differences that provide the immediate impetus to smuggling; and ethnic and religious kinship groups

straddling borders. Section 10.6 presents case studies in West and East Africa illustrating these issues. Section 10.7 assesses welfare effects and policy responses, and section 10.8 concludes.

10.2   THEORETICAL MODELS OF SMUGGLING[1]

Many of the key contributions, starting with Bhagwati and Hansen (1973), use general equilibrium models, but partial equilibrium versions capture all the main points and are easier to exposit. As Azam (2007) notes, the analysis is essentially a traditional 'Vinerian' focus on trade creation and trade diversion. Smuggling may increase trade flows, that is, lead to trade creation, but also diverts legal trade into illegal smuggling, that is, trade diversion. The net welfare effect is in general ambiguous, as it is in classic customs union analysis. Bhagwati and Hansen (1973) argue that smuggling is generally harmful because in their model trade diversion dominates. Deardorff and Stolper (1990), using the same methodological framework, argue, in effect, that under 'African conditions' of heavily distortionary government policies, trade creation tends to dominate. In these models, the welfare effects of smuggling turn on the magnitude of the real resource cost involved in smuggling compared to legal trade and on whether or not smuggling wipes out legal trade or the two forms of trade occur simultaneously (parallel trade).

   Bhagwati and Hansen (1973), Deardorff and Stolper (1990) and subsequent contributions model a small country importing a good subject to a tariff with the possibility of smuggling to evade the tariff. Smuggling involves a real resource cost greater than that associated with importing legally under free trade. Part of this cost could be incurred by the government's efforts to curb smuggling.

Case 1

Smuggling is assumed to be competitive and to have a constant marginal cost of s in excess of legal imports. Figure 10.1 shows the effects of smuggling where P_F is the exogenous free trade (world) price, $P_T = P_F + t$ is the domestic price with tariff (t) in the absence of smuggling and $P_S = P_F + s$ is the domestic price when smuggling occurs, where $s < t$ as smuggling won't occur if s exceeds t. In this case, all illegal trade will vanish. Relative to the tariff equilibrium, smuggling expands imports from M_T to M_S (trade creation), but M_T imports are diverted from legal trade to smuggling. Consumer surplus expands by areas $a + b$ and the government loses tariff revenue of $a + c$. Smugglers obtain zero profits (they only cover the cost s). In this scenario, therefore, national welfare is $b - c$, where b is the efficiency gain from trade creation while c is the cost of trade diversion. The net effect of smuggling is therefore ambiguous and depends on the magnitudes of t and s. Clearly, the lower the smuggling cost s relative to the tariff t, the higher the likelihood that smuggling is welfare-enhancing.

Case 2

Now consider the case where smuggling involves no extra resource costs but smugglers earn profits due to entry barriers, with s now being the profit margin of smugglers.
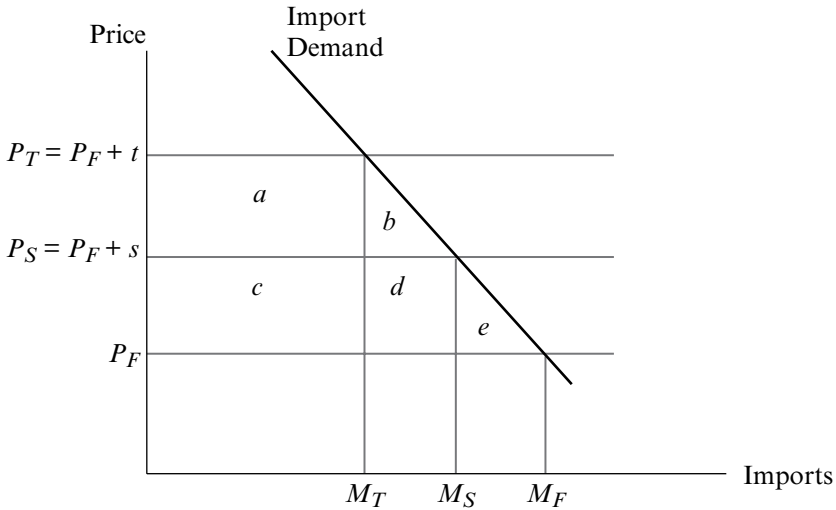
Figure 10.1   Effects of smuggling with constant marginal cost of smuggling

Smuggler profits are now $c + d$, and the net welfare from smuggling grows to $b + d$, that is, smuggling is now solely trade-creating and welfare-enhancing, as smuggler profits replace lost customs revenue, leaving only gains from trade. Intermediate situations between cases 1 and 2 are possible.

Case 3

Smuggling involves no resource cost and is competitive, as in case 1, but smugglers import some goods legally in order to provide 'cover' for their smuggling operations, as in Pitt (1981) and Thursby et al. (1991). In this case the marginal cost for smugglers is a weighted average of P_T and P_F, depending on the shares of imports brought in legally and paying tariffs versus those smuggled in and evading the tariff. In this case, informal trade is equivalent to a tariff reduction. Welfare unambiguously increases for a small price-taking country where the optimal tariff is zero.

Case 4

Smuggling is subject to an increasing marginal resource cost such that the supply curve for smuggling is upward sloping, as in O'Connell (1992) and Daubrée (1995) amongst others.[2] In equilibrium, it is now possible that both official and unofficial sales are occurring, as shown in Figure 10.2. Under these assumptions, the domestic price remains unchanged at world price plus tariff, and the total quantity imported is unchanged. That is, smuggling leads to a one-for-one reduction of legal trade, with smuggled goods substituting for some but not all legally-imported goods. In this situation, smuggling clearly imposes a welfare loss since smuggling is 100 percent trade diverting. More formally, in Figure 10.2 consumer surplus is unchanged, the
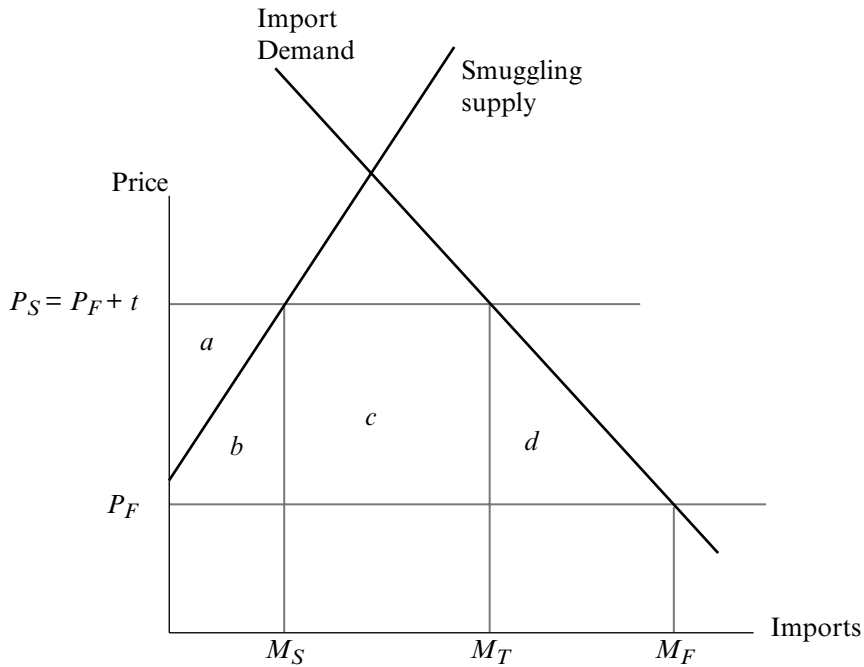
Figure 10.2   Effects of smuggling with increasing marginal cost of smuggling

smuggling producer surplus gain is *a* and government tariff revenue loss is *a* + *b*, for a net loss of area *b*. This is a welfare loss because part of what would otherwise be a pure transfer *a* + *b* from the government to smugglers gets wasted as an increased resource cost of the relevant imports. This is a case of directly unproductive profit-seeking by smugglers.

If protection takes the form of a binding quota rather than a tariff, Azam (2007) shows that smuggling is trade-creating and hence welfare-improving. Similar considerations apply to exports, and are presented in some detail in Azam (2007).

In summary, standard trade theory suggests that smuggling may be welfare-enhancing or reducing depending on the costs of smuggling relative to the magnitude of the distortions giving rise to smuggling. This approach, while asking pertinent questions, is rather narrow and leaves out many important aspects of the causes and consequences of smuggling that are addressed in other social sciences.

10.3   METHODS FOR ESTIMATING ICBT

Smuggling is inherently difficult to measure. Nevertheless, the magnitude and nature of smuggling can be inferred through a combination of case studies drawing on interviews and local press reports and inferences from official trade data. Qualitative and quantitative analysis are complementary for understanding ICBT where the 'complexity is best addressed by a multifaceted approach' (Ellis and MacGaffey, 1997, p. 25).

1. *Mirror trade data.* 'Mirror' trade data are often used to assess the extent of smuggling. This involves comparing recorded imports of a country to total recorded exports from the rest of the world (ROW). If the source country's reported exports exceed the destination country's reported imports by more than can be explained by trade costs, smuggling is inferred (e.g. Fisman and Wei 2004; Fisman et al. 2008; Berger and Nitsch 2008; Mishra et al. 2007). Intra-African smuggling, however, cannot be fully apprehended with mirror data, since official trade statistics from both the exporting and importing country fail to record this cross-border trade. For example, smuggling cannot be inferred directly from recorded Benin–Nigeria bilateral trade, which is very small as recorded by *both* Benin and Nigeria.

    Nevertheless, used creatively, mirror data can help capture some dimensions in ICBT in Africa. Raballand and Mjekiqi (2010) and Golub (2012) use mirror data to show that Benin imports an unusually large amount of certain products, in excess of what can be explained by domestic consumption and production, and infer that the residual is re-exported unofficially, using equation (10.1).

    Unofficial re-exports = Recorded imports + Domestic Production −
    Domestic Consumption   (10.1)

    Domestic production data may be difficult to obtain, but in many cases production is small relative to imports. Domestic consumption data are also unlikely to be available, but it can be assumed that usage of basic consumer goods such as rice, sugar, cloth and clothing is similar within a region, given the generally similar level of per capita incomes and lifestyles. For example, if imports of cloth are very high in Benin relative to Nigeria, it is reasonable to infer that Benin is importing to re-export to Nigeria, particularly if combined with observed incentives to smuggle and anecdotal or other information corroborating such activities. This method is discussed in detail below in the case studies of West Africa (Togo, Benin, The Gambia).
2. *Domestic customs data.* National customs offices often collect far more information than they report in official statistics in national publications and reproduced in international organizations' databases such as the IMF Direction of Trade and the UN *Comtrade.* For example, in Benin and Togo, most goods arriving into the country are classified into categories 'for domestic use', 're-exports' and 'transit'. Obtaining this information from customs and deciphering it poses challenges, and probably requires onsite visits and contacts within the government.
3. *Price differences across borders.* Instead of measuring quantities of products traded unofficially, price differences across borders giving rise to ICBT can be studied. If arbitrage through ICBT were perfect, such price differences would not be observable, but in fact, transport costs and other impediments to trade mean that price differences persist even in the face of large-scale ICBT. To the extent that observed price differences can be explained by different government policies, the *prima facie* case for expecting smuggling to occur is strengthened. This method is illustrated in the Gambia–Senegal (Golub and Mbaye 2009) and the Somalia–Ethiopia–Kenya (Little 2005; 2010) case studies below.
4. *Observation of borders.* A common approach to quantifying trade flows is observation of trader activities at border crossings. This method has the advantage of direct

observation rather than inference and can be a crucial source of information for understanding the modalities of trade. However, it may be very difficult to obtain a full picture of some types of trade in this way, for various reasons. The number of trucks arriving at the border can be counted but the exact contents of the trucks may not be easily ascertainable. Moreover, routes taken by ICBT are varied. Some traders cross at official border posts, with partial or full cooperation of customs officials, but others attempt to evade customs checkpoints, going through the bush or by water. In many instances, border posts are few and far between and it's difficult for traders to pass through official crossings even if they would prefer to do so.

5. *Interviews*. There is no substitute for talking to knowledgeable traders and officials in the countries themselves. The difficulty here is that these individuals may be suspicious of the motives of researchers and not be inclined to talk at all or if they do, may not reveal the full truth. Nevertheless, researchers have had considerable success with this method, particularly when trust is developed by repeated contacts over time (Titeca and de Herdt 2010). By obtaining the perspective of a diverse group of participants and cross-checking their responses, one can eventually develop a detailed understanding of the operation of ICBT, how it has evolved over time, and the key policy issues. Mahmood (2008) learned the details of ICBT by riding on trucks for 48 hours with cattle traders in Kenya.

Overall, a combination of interviews, observation, and gathering and analysis of quantitative data is the best and probably the only viable approach to understanding ICBT. Relatedly, an interdisciplinary approach combining history, political science, sociology and anthropology as well as economics is most likely to be fruitful.

> The work of the macroeconomist is often akin to that of a detective, trying to find the relevant clues to choose among different possible models. There is not yet any better solution than going to visit the country that one wants to analyze, and trying to put the right questions to the right people. *Bon Voyage*! (Azam, 2007, p. 239)

10.4   THE ORGANIZATION AND MAGNITUDE OF ICBT

ICBT must be understood in the context of the overwhelming role of the informal sector in Africa. The informal sector exists around the world, but is most dominant in Africa (Schneider and Enste 2002; Benjamin and Mbaye 2012; Steel and Snodgrass 2008; La Porta and Schleifer 2011; Guha-Khasnobis and Kanbur 2006). ICBT is closely connected to domestic wholesale-retail trade, in which the informal sector plays a particularly prominent part. In fact, the informal sector is so pervasive and the breakdown of state institutions so complete in parts of Africa that some go as far as to say that the distinction between formal and informal economies has become meaningless (see discussion in Meagher 2010, Chapter 2) and the informal sector is the real economy (MacGaffey 1991).

Several key features of the informal sector identified in recent literature are prominent in ICBT. First, informality is a continuum rather than a dichotomy. Many firms straddle the formal and informal sectors, and almost no firms are totally formal. ICBT involves a complex interplay of formal and informal operators and practices. Second, the informal

sector is quite heterogeneous. In particular, informal firms can be separated into large and small operators. While the vast majority of informal firms are very small and involve survival activities such as petty trading, large informal firms play a major role in some sectors, notably commerce, with a national or even international scope. Intricate relationships link the formal, large informal and small informal firms (Benjamin and Mbaye 2012, Chapter 4). Third, although informal, ICBT is highly organized, with elaborate 'practical norms' (Titeca and de Herdt 2010; Chalfin 2001) and division of labor. Numerous specialized semi-official intermediaries are involved, such as customs clearance agents known as *transitaires* in Francophone countries (Benjamin and Mbaye 2012) and *chattermen* in Sierra Leone (Pritchard and van den Boogaard 2013). Fourth, ethnic and religious networks play a large role in organizing the informal sector, and are particularly important in ICBT given that their populations often straddle national borders. The role of kinship groups throughout ICBT in Africa is discussed further below.

Governmental authorities' role in ICBT is also complex, varying from complicity to outright conflict. In the case of Nigeria, observers frequently allege that high government officials are involved in organizing, profiting from and protecting smuggling networks (Egg and Herrera 1998; Hashim and Meagher 1999). As such, these networks often operate quite openly and without fear of government crackdowns. In some cases, however, customs officials are engaged in ongoing conflicts with informal operators. Several of the largest informal operators in Senegal have been imprisoned and have faced heavy fines for involvement in smuggling sugar, one of the most politically sensitive and highly protected sectors in Senegal (Benjamin and Mbaye 2012). In other cases, customs officials and traders develop practical norms, that is, codes of conduct for both parties that involve compromises between compliance with payment of duties and fees versus tolerance for evasion. In north-west Uganda, for example, local customs officials occasionally declare threshold days or tax-free moments, when traders are exempt from duties or pay greatly reduced rates, once customs officials have met the threshold level of revenues demanded by the central office (Titeca and de Herdt 2010). These compromises evolve over time based on the bargaining strength of traders and customs officials as both parties attempt to develop codes of conduct that enable mutually beneficial and stable relationships. In countries where states have largely collapsed, traders develop alliances with non-state actors to stabilize the institutional environment. In the Congo, for example, Nande traders work with the Catholic church as well as local militias, even providing free hotel stays to militias in exchange for protection (Kabamba 2013).

Duty collection at border crossings is generally well below statutory rates and consists of a mix of official and unofficial payments whose rates are partly fixed by precedent and partly negotiated. Titeca and Kimanuka (2012) show that the extent of official versus unofficial 'tax' collection at border posts varies greatly in the Great Lakes region, with Rwandan officials collecting mostly official taxes whereas in the Congo the bulk of payments are unofficial. Competition between border posts for revenue can influence the size of payments that officials demand and traders are willing to pay (World Bank 2013). Ruptures of these relationships occur occasionally and can be very costly for both parties.

Women often play an important role in ICBT, although the extent varies greatly among regions. MacGaffey (1991) points out that the subservient role of women in Congo (then Zaire) was exacerbated by family regulations of the colonial period, pushing women

into informal trading, including ICBT, which continued into the post-colonial period. In Zimbabwe, women constitute 85 percent of the traders (Ndela 2006). In the Great Lakes region, Titeca and Kimanuka (2012) estimate that 85 percent of small-scale traders are women. In some countries, women are often confined to particular products or activities, such as *eru* (a leafy vegetable) in Cameroon (World Bank 2013). In regions with high insecurity and harsh environments, as in Somalia, young men dominate trading (Teka and Azeze 2002).

ICBT has increasingly become globalized, with trading networks extending across continents. Anthropologist Gordon Mathews (Mathews and Yang 2012; Mathews 2013) has interviewed African, particularly Nigerian, traders in Hong Kong and China, where they come to order counterfeit goods and copies of brand-name products for delivery to Africa. One of the most developed international trading networks involves the Mouride Muslim sect in Senegal, with traders traveling to Dubai, Asia, Europe and Africa, using a mix of traditional practices and modern technology (Golub and Hansen-Lewis 2012). Traders have established regional groupings, or *daras*, combining religious, social and business functions wherever they go. Funds are transferred between Senegal and other countries without paperwork but with complete trust and reliability. Women increasingly participate in this globalization of the Mouride network (Sall 2013).

The volume of ICBT is often estimated to be much larger than official cross-border trade, with large variations depending on the country, concepts of trade used (trade in domestically produced goods or re-exports), and methodology of estimation. For example, World Bank (2013) found that bilateral Cameroon–Nigeria trade of domestically-produced goods was $230 million, compared to officially-recorded flows of $10–40 million in 2011. Including re-exports, ICBT between Cameroon and Nigeria rises to about $1 billion. Likewise, as described in the case studies below, ICBT in West Africa and the Horn of Africa vastly exceeds reported bilateral trade. In the cases of The Gambia, Togo and Benin (see section 10.6) imports for re-export to neighboring countries are 3 to 5 times larger than total imports for domestic consumption, whereas official bilateral trade with neighbors is negligible. Estimates by the Ugandan government of ICBT, reported in Afrika and Ajumbo (2012), are considerably lower, at 50 percent of official Ugandan imports and 2 percent for exports in 2009. Likewise, Macamo (1999) estimates that Mozambique's unofficial trade with neighbors in 1995–96 averaged about one third of formal trade, but with large variations among these neighbors – trade with Swaziland was overwhelmingly informal whereas the reverse is true for trade with South Africa.

10.5   CAUSES OF ICBT

ICBT in Africa reflects historical, geographical and institutional commonalities across the continent. At the same time, national and regional particularities also influence the specific forms of ICBT. A confluence of factors contribute to the prominence of ICBT: long traditions of regional trade preceding the colonial era; artificial borders imposed by the colonial powers, largely maintained as African nations became independent around the early 1960s; strong ethnic and religious ties uniting people across borders; uncoordinated and often highly interventionist policies in the newly independent states,

particularly with regard to trade policies; weak state institutions, which undermine the effectiveness of the enforcement of these policies, and widespread corruption; and inability of governments to control movements of people and goods across artificial borders.

Trading Traditions

Long traditions of regional short- and long-distance trade throughout Africa preceded the colonial era, based on resource endowments, agro-climatic conditions, population density and weather fluctuations, that is, comparative advantage. These same factors continue to drive contemporary ICBT, along with institutional and policy developments in the colonial and post-colonial periods.

Artificial National Borders

Prior to the colonial era, hard geographical borders did not characterize states in Africa, with rulers having only loose control over territory and movements of people (Herbst 2000, Chapter 2). At the Berlin conference of 1884 the colonial powers divided up Africa among themselves, creating territorial borders based on their de facto zones of control. These boundaries arbitrarily separated regions with long-standing ethnic ties and often without clear geographical separators (Young 1994). These colonial borders remained the basis for national boundaries following the end of colonialism in the early 1960s. Moreover, governments are unable to effectively prevent unofficial crossings along long borders with few human or natural barriers, making evasion relatively easy.

Uncoordinated and Ineffective Economic Policies

The newly-independent post-colonial nation states developed their own economic policies, but more often than not these policies were wielded irresponsibly in the first few decades of independence and not coordinated among neighboring countries. Governments intervened massively but ineffectively in industry. Trade policies were of particular importance as they served both to protect local industries and generate government revenues (Berg 1985). Taxes on international trade have historically provided an unusually large portion of government revenues in Africa, dating back to the colonial period and continuing to the present day. Direct taxes on income and wealth are difficult to enforce in Africa due to lack of state control over much of the population (Herbst 2000, p. 116). In a context of weak states and porous borders, these large differences in import protection, subsidies, price controls, exchange-rate misalignments and other policies between countries have provided an impetus to smuggling (Boone 1989; Berg 1985; Egg and Herrera 1998). Many countries, particularly those pursuing import-substitution strategies most vigorously, adopted very high import barriers, including tariffs and import prohibitions. The high levels of protection have impeded legal trade within Africa and provided very large incentives for smuggling, while almost completely failing in their intended effects of promoting viable domestic industries.

Although statutory trade barriers have declined in many countries, actual implementation is highly variable and non-tariff barriers remain pervasive. Lengthy and costly procedures and demands for unofficial payments induce traders to avoid official border

crossings (Afrika and Ajumbo 2012). In cases where traders do pass through official border posts, payments are negotiated between traders and officials. Cameroon has resorted to stipulating minimum duties per vehicle (World Bank 2013). Traders now generally pay more in formal and informal payments than the minimum but considerably less than the statutory duties, subject to bargaining and competition between border posts in revenue generation. In the Great Lakes region, particularly in the Congo, traders are often subject to a variety of taxes by different agencies and their multiple representatives (Titeca and Kimanuka 2012). Some of these agencies are not officially authorized to be present at the borders, but nonetheless collect payments from traders.

Weak States and Strong Informal Sectors

ICBT is part of the informal sector in Africa more generally, as discussed above. Recent literature views informality as a choice conditioned by the costs and benefits of formal versus informal status, for example Benjamin and Mbaye (2012, Chapter 6); Perry et al. (2007); Kanbur (2009); Djankov et al. (2003); Loayza et al. (2005); Johnson et al. (2000). The institutional environment in turn affects the balance between these costs and benefits. Formalization permits greater access to public services but also requires compliance with regulations and payment of taxes. The higher the quality of public services and the lower the costs of compliance with tax obligations and regulations, the more firms will opt for formal status. The extent to which the government enforces rules and sanctions non-compliance is also critical. In many African countries, public services are poor while tax rates are high and procedures very complex. Governments' limited monitoring and enforcement capabilities and widespread corruption enable informal enterprises to conceal their activities and evade taxes. Another major problem is lack of cooperation among different government agencies, particularly between customs and tax authorities. For ICBT, weakness of the state is most manifest in terms of inefficacy and corruption of customs and inefficient and costly trade facilitation.

Smart (2013) observes that the inability to eradicate smuggling ('illegal persistence') reflects social attitudes regarding the legitimacy of government rules as much as the economic distortions created by those rules usually stressed by economists. Smart (1999; 2013) analyzes various forms of illegal persistence, related to perceptions of legitimacy. The general perception that governments are corrupt undermines tax morale (Perry et al. 2007) and reduces the sense of obligation to comply with civic and legal obligations. Thus, a vicious circle of state weakness and informal practices can develop. In contemporary Africa, marginalized ethnic groups or refugees often undertake ICBT. Informal trade obtains legitimacy as part of the struggle against oppression and for survival. This is the case in North-West Uganda from which former President Idi Amin originated, but which became marginalized when President Museveni took power in 1986 (Titeca and de Herdt 2010).

Political Instability and Civil Conflict

In more extreme situations of failed states and civil wars, as in Sierra Leone (diamonds), Somalia and the Congo, there is little possibility of formal trade (Little 2005; Titeca and de Herdt 2010). In such situations, military power and illicit trade go together (Roitman

2004). Alternatively, ICBT can take on a political dimension as the embodiment of opposition to the regime in power. In some cases, informal trading networks developed in opposition to the colonial powers. For example, the Mourides in Senegal arose in part in opposition to the French in the late nineteenth century (Golub and Hansen-Lewis 2012).

Poverty and Unemployment

Even in countries without civil wars, the collapse of state-supported formal private sectors and state-owned enterprises in much of Africa in the aftermath of economic mismanagement in the 1960s and 1970s and structural adjustment policies in the 1980s and 1990s has entailed widespread unemployment and poverty (Meagher 1995). The informal sector and ICBT have filled the gap through a combination of 'low-income demand-pull' from consumers seeking inexpensive goods and 'cheap-labor supply push' of entry of unemployed workers into ICBT (Macamo 1999).

Kinship Networks

Kinship networks often play a major role in informal cross-border trading in Africa (e.g. World Bank 2013; Golub and Hansen Lewis 2012; Little 2005; Meagher 2010; MacGaffey 1991), both substituting for and undermining official institutions. In Africa, allegiance to traditional sources of authority is often far more binding than to the modern state. Kinship groups often originated many centuries prior to European colonization, and have adapted to the colonial and post-colonial economic environments. On the positive side, the social and religious bonds linking the members of the group enable complex and flexible trading strategies with property rights and contract enforcement provided by group solidarity rather than formal rules. Religious affiliation and belief plays a major role in many groups' solidarity. The bonds of trust, norms and enforcement mechanisms provided by kinship networks enable contract fulfillment, access to financing, and information exchange without documentation or official involvement (Putnam 1995; Fafchamps 2004). Kinship groups play a particularly important part in international trade, helping to overcome transaction costs created by lack of information and differences in business practices across countries (Rauch 2001). On the negative side, however, informal networks can be exclusionary, accepting or even promoting antisocial behavior and violation of the rules and norms in the formal economy (e.g. Adhikari and Goldey 2009; Field 2003; Portes 1998).

Often several ethnic groups operate within the same country but in different regions. Examples where ethnic groups living in adjacent countries play a major role in ICBT include the Mourides in Senegal and the Gambia (Golub and Hansen-Lewis 2012), the Yoruba in Eastern Nigeria and Benin (Golub and Hansen-Lewis 2012, Igué and Soulé 1992), the Igbo in Cameroon and Southern Nigeria (World Bank 2013), the Hausa in Northern Nigeria and Niger (Hashim and Meagher 1999), the Burji in Northern Kenya and Ethiopia (Mahmood 2008), the Nande in Eastern Congo (Kabamba 2013), and the Lugbara in north-western Uganda and north-eastern Congo (Titeca 2009). Aker et al. (2014) provide a recent interesting illustration of the role of kinship groups in integrating markets across countries. They find that there is no border price discontinuity for trade

in millet and cowpeas across the Niger–Nigeria political border, as long as that trade takes place between markets of the same (Hausa) ethnicity. There is a border effect, however, when cross-border trade is between Hausa and non-Hausa markets as well as a statistically significant price discontinuity across the virtual border between Hausa and Zarma regions within Niger.

10.6   CASE STUDIES OF WEST AND EASTERN AFRICA

As discussed in section 10.3, several complementary methodologies are used to study ICBT, including interviews, mirror trade data, national-level unpublished customs data, and observation of border crossings. This section illustrates the methods and findings of empirical research on ICBT with examples from West and East Africa, respectively.

Case Study 1: The Re-export Trade in West Africa[3]

Historical, geographical and institutional context
The vagaries of colonial history and post-colonial nationalism have been particularly pronounced in West Africa (Figure 10.3). The Francophone countries of the region have joined in the West African Economic and Monetary Union (WAEMU) to form a single currency and a customs union,[4] but this agreement leaves out contiguous Anglophone countries, including The Gambia and Nigeria, which are members of the larger but less integrated ECOWAS[5] but not WAEMU. Moreover, unlike WAEMU, ECOWAS has made slow and limited progress towards liberalization of intra-ECOWAS trade flows, in part due to Nigerian opposition. ECOWAS and WAEMU have agreements allowing free circulation of goods in transit within the region, but these provisions have never been applied in practice in either WAEMU or ECOWAS. Trucks line up for days or even weeks at border crossing points. In addition roads are often poorly maintained and there are numerous checkpoints slowing commercial traffic.

The Gambia is perhaps the most extreme example of the illogical borders inherited from the colonial era and the patchwork nature of regional integration. A tiny Anglophone country of 1.5 million people, The Gambia is completely surrounded by much larger Francophone Senegal (population 13 million) except for a 60 km border on the Atlantic Ocean. Despite the geographical, ethnic and cultural ties that link them, political and economic cooperation between Senegal and The Gambia has been minimal. Both countries are members of the largely ineffectual ECOWAS, but Senegal is a member of WAEMU while The Gambia is not.

Likewise, Francophone Togo and Benin are in WAEMU but Anglophone Nigeria is not. Benin and Togo are small countries with populations of 10 million and 7.5 million respectively in 2012, near Nigeria, the most populous country in Africa (170 million). Benin and Togo on the one hand and Nigeria on the other, like The Gambia and Senegal, have made no efforts to harmonize economic policies despite their long shared border and long-standing ethnic ties between their people. Quite the contrary, in fact: The Gambia, Benin and Togo have deliberately sought to take advantage of the high levels of protection in their larger neighbors (Igué and Soulé 1992; Heilbrunn 1997; Lambert 1994). Benin has the advantage of sharing a long border with Nigeria, by far the
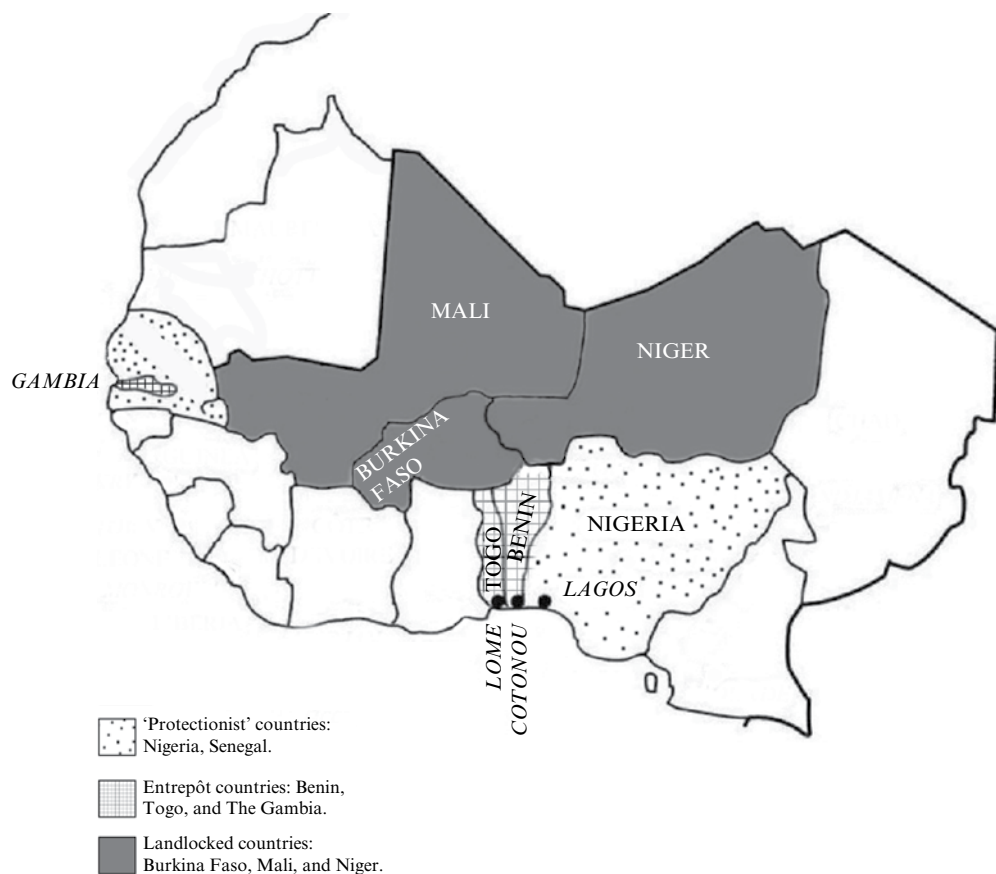
Figure 10.3   Map of West Africa, by trading status

largest economy of the region. Togo in turn has a long border with Benin, so that traders must cross through Benin or take a circuitous route through Burkina Faso and Niger to Nigeria. This disadvantage is particularly acute for perishable or bulky products. Lomé's port, however, permits access to larger ships than Cotonou's, requires less frequent dredging, and has generally been better managed (World Bank 2009; 2010).

Operation of re-export networks

Gambia–Senegal. Goods are brought into The Gambia by a handful of large wholesale importers, many of whom are Lebanese or Mouride. The wholesalers then sell much of their merchandise to other traders, often Mauritanians, who have shops all along the border, and who in turn sell to small-scale traders, typically market women, from countries in the region, mainly Guinea-Bissau, Guinea-Conakry, Mali and of course Senegal. These petty traders then smuggle the goods into Senegal either by going through the bush or paying off customs officials at the official border posts. Alternatively the wholesalers in Banjul sell directly to Senegalese businessmen who then transport the goods to the frontier in large trucks. At the border, the trucks can then be unloaded and the goods

smuggled through in smaller quantities, as described above, or cross the border with the connivance of customs officials. Social, religious and cultural ties amongst the participants, notably through their frequent affiliation with Mouride Muslim brotherhoods, greatly facilitate these transactions. Goods can also be brought into Senegal by sea using pirogues operating at night. The sprawling informal markets in Dakar, notably Sandaga, and in other cities, are substantially supplied by contraband, much of it flowing from The Gambia, with the tacit acquiescence of the Senegalese authorities.

Benin–Togo–Nigeria. As in Senegal–The Gambia trade, sophisticated and well-organized networks largely control ICBT, with many small operators involved on the margins. For bulk items such as rice, wheat and sugar, importers purchase directly from international brokers with whom they are in regular contact. For some products such as cigarettes, the foreign companies have local representatives. Importers of second-hand goods such as used cars often travel abroad or have foreign correspondents, providing information about sourcing opportunities. A variety of trading networks linked by cultural, ethnic or commercial ties operate in the re-export trade, including the Yoruba, centered on Porto Novo, which operate with a high degree of cohesion thanks to ethnic and religious affinities, groups of women importers, and various intermediaries, again mostly women. As in Senegal, Lebanese and other Arabs are also involved. Unofficial re-exports can cross the border by land or water. By land, there are numerous and ever-changing tracks used by traders along the long border with Nigeria. A complex network of canals is also used, with new canals being dug when customs agents patrol existing routes. Specialized warehouses for various goods destined for re-export are located in Cotonou and along the border. A network of markets dots both sides of the Benin–Nigeria border, with sister markets on either side of the frontier. Togolese traders have developed elaborate circuits for smuggling goods unofficially into Benin, both for the Beninese and Nigerian markets.

Trade policies and trade facilitation

Differences in national trade policies are the most significant determinant of re-export patterns, given the incentives that wide disparities between neighboring countries provide. Trade facilitation (customs, port management and so on) is also very important.

The Gambia and Senegal. Senegal followed highly restrictive trade and pricing policies during the first decades following independence in the 1960s, with very high tariffs and opaque non-tariff barriers. As in much of Africa, Senegal moved towards more market-oriented economic policies as part of its structural adjustment policies in the late 1980s and 1990s, following serious fiscal and financial crises, culminating in the implementation of the Common External Tariff (CET) in WAEMU countries in 1998–2000, which greatly reduced the infamous complexity and lack of transparency of Senegal's tariff structure. However, discretionary supplementary import taxes can be applied to politically sensitive products, including flour, sugar, rice, tomato paste, cigarettes and cooking oil. In the case of sugar, notoriously protected in Senegal for decades, the special taxes are very high.

The Gambian government has sought to maintain a more liberal trade regime than Senegal to facilitate its role as a trading hub. The import tax differential in the 1970s through to the early 1990s between Senegal and The Gambia was very large, with Senegalese import duties alone as high as 100 percent for goods such as textiles, while Gambian duties averaged around 30 percent. In 2000 and subsequently, in response

Table 10.1   Comparison of trade taxes and wholesale prices: Senegal and The Gambia, 2006 (%)

	Import taxes*			Wholesale price difference
	Gambia	Senegal	Difference	Senegal–The Gambia
Bulk items				
Sugar	22.5	103.8	81.3	90.5
Flour	22.5	56.6	34.1	33.2
Rice	16.8	22.7	5.9	13.1
Other consumer goods				
Cigarettes	58.0	97.7	39.7	29.4
Cooking oil	22.5	56.6	34.1	57.9
Tomato paste	28.3	56.6	28.3	62.6
Tea	28.3	37.3	9.0	23.1
Candles	39.8	44.8	5.0	70.4
Canned sardines	39.8	44.8	5.0	19.1
Matches	39.8	44.8	5.0	70.5
Mayonnaise	39.8	44.8	5.0	56.1
Toilet soap	39.8	44.8	5.0	24.9
Milk powder	22.5	27.1	4.6	39.5

Notes: Import taxes (* includes sales taxes, fees, and other special taxes) expressed as percentage of value of imports; difference in percentage points. Difference in wholesale prices is Senegal price as percentage of price in The Gambia.

Source: Customs in The Gambia and Senegal and authors' computations.

to the implementation of the WAEMU CET, The Gambia simplified and reduced its customs duties.

Table 10.1 provides a summary comparison of The Gambia's and Senegal's import taxes as of end 2006 for some of the key re-export products (Golub and Mbaye 2009). In all cases, Senegal's taxes are higher and sometimes much higher. The greatest differential is for sugar, where the Senegalese composite tax rate is about 80 percentage points above the Gambian tax rate. Table 10.1 also shows the difference in wholesale prices for these same products. The price differences in Table 10.1 match quite well with the differential rates of protection, especially for the bulk commodities (90 percent for sugar and about 10 percent for rice). The high differential for sugar accords well with the extraordinary protection of the sugar industry in Senegal. The low price difference for rice is consistent with the liberalization of the sector in Senegal, and reports by Gambian wholesalers themselves that they have largely abandoned trade in rice except for the local market.

Nigeria, Togo and Benin. Differential trade and taxation policies and practices between Nigeria, Benin and Togo are known to be among the main cause of re-exports between Benin, Togo and Nigeria, according to the available literature (Igué and Soulé 1992; Soulé 2004; Perret 2004; Morillon and Afouda 2005; Azam 2007; Raballand and Mjekiqi 2010; Golub 2012). Nigeria's import barriers have been among the highest in the world and vary greatly over time, as illustrated in Table 10.2. Nigeria has been

Table 10.2   Selected import barriers in Nigeria, 1995–2013 (tariff rates in %)

	1995	2001	2007	2013
Beer	Banned	100	Banned	Banned
Cloth and apparel	Banned	55	Banned	Banned
Poultry meat	Banned	75	Banned	Banned
Rice	100	75	50	100
Sugar	10	40	50	60
Tobacco and cigarettes	90	80	50	50
Used cars*	Banned	Banned	Banned	Banned
Used tires	Banned	Banned	Banned	Banned
Vegetable oil	Banned	40	Banned	Banned
Wheat dough	Banned	Banned	Banned	65

Notes: *Defined as more than 8 years old in 1994–2002, and more than 5 years in 2002–04, 8 years since 2004–08, 10 years since October 2008, and currently 15 years.

Source: Soulé (2004), Nigerian customs data provided by the World Bank, Nigerian import prohibition list, available at https://www.customs.gov.ng/ProhibitionList/import.php, online reports (for 2013).

reluctant to fully comply with ECOWAS's tariff harmonization agreements. Nigeria maintains a changing list of import bans, some of which are shown in Table 10.2, but the extent to which these bans are enforced has also varied and exemptions are often granted. Overall, Nigerian trade policy operates with an enormous complexity and opacity over and beyond the very high import barriers. On the other hand, some products in Nigeria are highly subsidized, such as petroleum products and fertilizer, spurring large-scale unofficial imports into Benin from Nigeria, some of which are in turn re-exported to other countries.

In 1973 Benin and Togo both explicitly adopted policies to spur re-exports, with the goal of maintaining lower import barriers than those in Nigeria. The WAEMU CET in theory constrains Benin and Togo's tariffs, but customs in both countries retain substantial discretion, as illustrated below in the used car trade. Togo allegedly seeks to undercut Benin by lowering actual applied duties of imported goods below WAEMU levels. In order to contend with rising competition from Togo, Benin too is said to permit under-invoicing of imports and flexible application of import duty rates (Golub 2012).

Port efficiency and customs practices

The Gambia's relatively efficient customs are well-known, especially in comparison to the more complex and bureaucratic procedures in Senegal. While merchandise can languish for days or even weeks in most African ports, including Dakar, in Banjul clearance usually occurs within 24 hours (Golub and Mbaye 2009). Likewise, Cotonou in Benin is much more efficient than Nigerian ports, and Togo's Lomé is more efficient still.
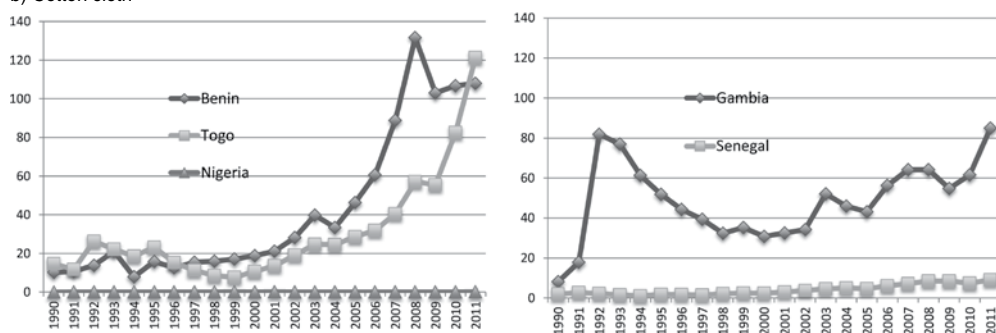
Border closures and crackdowns

Occasional efforts to crack down on smuggling by Senegal and Nigeria can lead to sharp but temporary drops in the re-export trade. While traders are to some extent able to

a) Cars
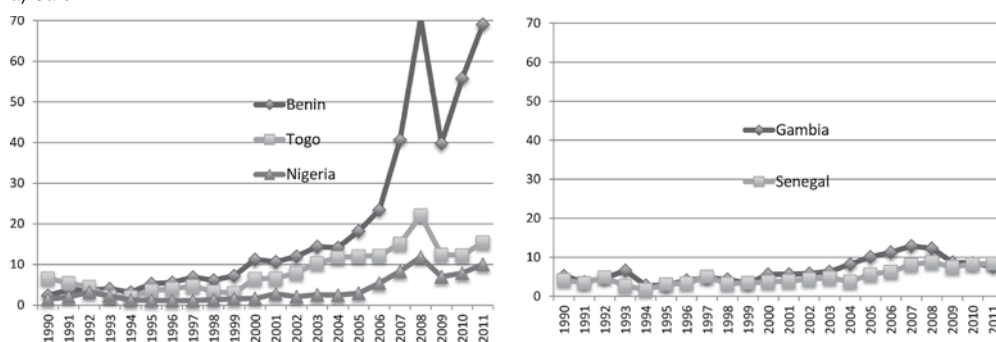
b) Cotton cloth

Source: UN Comtrade (trade data), World Bank World Development Indicators (population) and authors'
calculations.

*Figure 10.4   Imports per capita, as measured by world exports to designated country
(US$)*

avoid the official border crossings and slip across the frontier in the bush, much of the
trade passes through official border posts.

Evidence of the pervasiveness of unrecorded ICBT
Smuggling tends to be concentrated in a limited number of products that are highly
protected and/or subsidized in Nigeria and Senegal. The products involved are
well known and frequently discussed in the popular press. As discussed above, the
prevalence of smuggling can be assessed through an integrated analysis involving the
volume of recorded trade flows combined with anecdotal information in the countries
themselves.

Figures 10.4a–d show the level of per capita imports for many of the key products
involved in the re-export trade for The Gambia–Senegal and Benin–Togo–Nigeria (see
Benjamin et al. 2013 for more details). Imports are measured by rest-of-world (ROW)
exports to the country in question, using the UN *Comtrade* database. While there is
some domestic production of these products, which is, after all, why they are protected,
it is typically low relative to domestic consumption or not large enough to explain
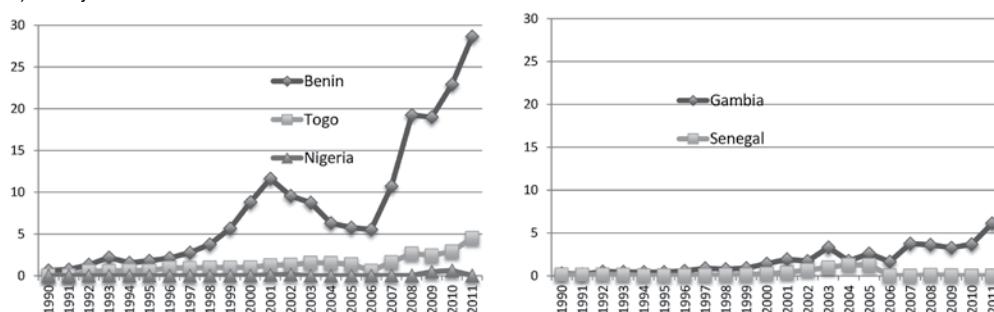
c) Sugar
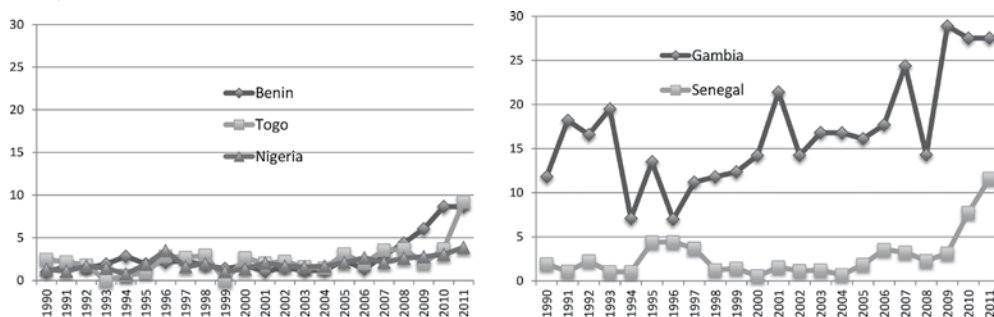
d) Poultry meat

Figure 10.4   (continued)

the very large differences in import patterns displayed in these figures. For products where Nigeria and/or Senegal have high import barriers as shown in Tables 10.1 and 10.2, imports in The Gambia and/or Benin/Nigeria are unusually large. For example, imports of used cars beyond a certain age are banned in Nigeria. Togo and especially Benin have developed a car-import value chain largely to supply the Nigerian market (Golub 2012). Car imports have grown rapidly and are very high in Benin relative to Nigeria, reaching about $70 per capita since 2007 (Figure 10.4a), seven times the ECOWAS average level of about $10 per person. Togo's per capita car imports are also above Nigeria's and average ECOWAS levels, although far below Benin's, due to Togo's geographic disadvantage relative to Benin in supplying the Nigerian market and the relatively high cost of transshipping cars. Senegal has until recently had no limits on the age of used car imports, and Gambian and Senegalese imports have been similar. On the other hand, both Senegal and Nigeria have highly protected but inefficient textile firms. Perhaps no product is of more importance to low-income but fashion-conscious West Africans than cotton cloth. Imports of cloth in Benin, Togo and The Gambia far exceed those in Nigeria and Senegal (Figure 10.4b) and the ECOWAS average levels of fabric imports of about $7 per person in the late 2000s. Togo's greater success in smuggling cloth relative to cars probably reflects the fact that cloth is easier to transport and Togo's historical role as a regional center for the textile industry.

Figure 10.4c suggests that smuggling of sugar into Nigeria from Togo and Benin is minor despite high tariffs in Nigeria, but the very high protection of sugar in Senegal is

Table 10.3 Effective tax rates on transit, Benin and Togo

	Benin						
	2002	2003	2004	2005	2006	2007	2008
All goods	1.3%	4.6%	4.7%	4.5%	4.3%	4.8%	4.5%
Used cars	3.2%	10.9%	10.7%	9.9%	9.4%	12.6%	13.5%
Cloth	0.7%	2.6%	3.1%	2.5%	2.0%	1.2%	0.4%
	Togo						
	2002	2003	2004	2005	2006	2007	2008
All goods	0.3%	0.3%	0.3%	0.4%	0.4%	0.4%	0.5%
Used cars	0.3%	0.2%	0.2%	0.2%	0.3%	0.2%	0.3%
Cloth	0.6%	0.3%	0.3%	0.4%	0.4%	0.5%	0.8%

Source: Togo and Benin customs data on duties collected, and author's collections.

reflected in The Gambia's large level of imports. Finally, poultry has also been on the list of banned items in Nigeria since the early 2000s. Poultry imports into Benin have surged from a few dollars per person in the late 1990s to nearly $30 in 2011 (Figure 10.4d). Nearly all of Benin's imports are intended for Nigeria (Golub 2012). Probably due to the high cost of refrigerated transport and Togo's geographical disadvantage, Togo's imports of poultry are much lower than Benin's.

Customs practices with a focus on the used car market in Benin, Togo and Nigeria
This section illustrates the interplay between government policies and the re-export trade through an analysis of tax competition between Benin and Togo in the lucrative used car market. Both Togo and Benin have special 'transit' regimes for imported goods destined for re-export with lower tax rates than imports for domestic use. Goods imported in transit status are usually declared for land-locked countries to the North of Benin and Togo, but in practice are mostly in fact destined for Nigeria.

Table 10.3 shows the effective tax rate on transit in the two countries, dividing total customs receipts by import values, using unpublished customs data obtained by the author during visits to the two countries (Golub 2012). In Benin, Table 10.3 indicates that tax receipts on transit were low in 2002 at an average effective rate of 1.3 percent for all goods and 3.2 percent on used cars. In 2003, Benin raised transit taxes considerably, especially on used cars, with the average rising to 4.6 percent and the rate on used cars jumping to nearly 11 percent. These tax increases in Benin, along with the border closing between Nigeria and Benin in 2003 in response to a political dispute, contributed to the sizeable decline in Benin's transit trade and the large increase in Togo's in 2003. It thus appears that Benin sacrificed some of its transit trade in order to collect a larger amount of revenue. Togo, on the other hand, collects very little revenue on transit and re-exports, in order to boost competitiveness. Benin's transit trade nevertheless recovered impressively after its 2003 slump, until the world recession of 2009.

Togo's taxes on transit trade have fallen over time and are now considerably below Benin's. In the 1980s, Togo's transit taxes averaged about 8 percent. In the early 1990s

transit taxes were lowered to about 4 percent and in the 2000s fell to 0–2 percent. Table 10.3 confirms that actually-paid taxes on transit are very small for Togo, well below 1 percent for most goods, although they edged up in 2008. For used cars in transit, Togo's tax rate increased from 0.3 percent to a still minuscule 0.5 percent in 2008. The effective transit tax rate on cloth in Togo also rose slightly to about 0.8 percent in 2008.

The greater speed and lower cost of port services in Lomé over Cotonou also probably result from the pressure on Togo to remain competitive.[6] It appears that these very low taxes on transit and re-exports in Togo and the competitiveness of the port are consistent with a strategic decision by the government of Togo to promote the role of Togo as a hub and compensate for the higher costs of reaching Nigeria from Lomé relative to Cotonou.

Competition in the used car market is particularly intense and significant given the substantial value added and employment provided by trade in used cars. Table 10.4 shows the volume of cars imported into Togo and Benin, by customs status. Benin's imports of used cars averaged around 200 000 per year over 2000–08, with a dip in 2003 and 2004 and a surge in 2008 to over 300 000. Of these imports, about 8000 are declared for domestic consumption and the rest in transit, ostensibly mostly to Niger but in practice overwhelmingly intended for Nigeria, where used car imports have been restricted, as seen earlier. Togo's imports are less than half of Benin's, averaging about 70 000 per year in recent years, peaking at above 90 000 in 2003 and again in 2008. About the same number as in Benin are declared for domestic use, leaving the remaining 80 percent for transit. Togo's imports of used cars for both domestic use and transit dropped precipitously in the first 5 months of 2009, for reasons discussed below.

Customs officials in Togo and Benin exercise substantial discretion in valuing goods, particularly used cars for which the value depends on the model and year, which can be difficult to verify. Figure 10.5 shows the average customs valuation for imported cars in Togo and Benin, distinguished by customs status into imports for domestic use and transit. Until 2008, Benin maintained relatively high customs valuations on cars imported for domestic use, but apparently lowered the latter in 2008. In late 2008, meanwhile, Togolese customs dramatically raised the average values on imported cars, doubling the values for cars declared for the domestic market and raising values for cars in transit by about 25 percent. Meanwhile, in Benin, valuations of imported cars for domestic use, which were considerably higher than in Togo through 2007, were lowered sharply in 2008 and 2009. Not coincidentally, in Benin a large increase in cars was declared for the domestic market in 2008 and 2009 from an average of about 8000 in 2002–07 to 20 000 in 2008–09. Benin's imports declared as transit also rose sharply in 2008 to 321 000 before falling back in the first 5 months of 2009 to an annual rate of 235 000. In June 2009, in the face of a public outcry, the Togolese government again altered its policy, with reductions of 15 to 30 percent in used car valuations.[7]

**Case Study 2: Livestock Trade in Eastern Africa**

Livestock is the most significant product in ICBT in the Horn of Africa, centering on Somalia, Ethiopia and Kenya (Little 2005; 2010; Little and Mahmood 2005; Mahmood 2008; Teka and Azeze 2002). Cattle and other animals are shipped or trek from Somalia and Ethiopia into Kenya for meat consumption, with the Northern Kenyan town of Garissa as the main distribution center, as shown in Figure 10.6. This trade falls in the

Table 10.4 Number of imported cars, by customs status, 2000–09

Togo

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009*
Total	57263	83301	80354	91767	70967	67415	75125	67873	91933	46587
Domestic use	10146	8592	9955	9784	7771	7993	9037	9179	11406	5401
Transit	47117	74710	70398	81984	63196	59422	66088	58694	80527	41456

Benin

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009*
Total	203027	251405	245051	207147	144030	153911	203599	257664	321008	235872
Domestic use	NA	NA	7509	9817	6110	7822	7071	8968	19208	21039
Transit	NA	NA	237542	197330	137920	146089	196528	248696	301801	214833

*Note:*   * First 5 months of 2009, annualized.

Source: Benin port of Cotonou, Togo customs, and author's calculations.
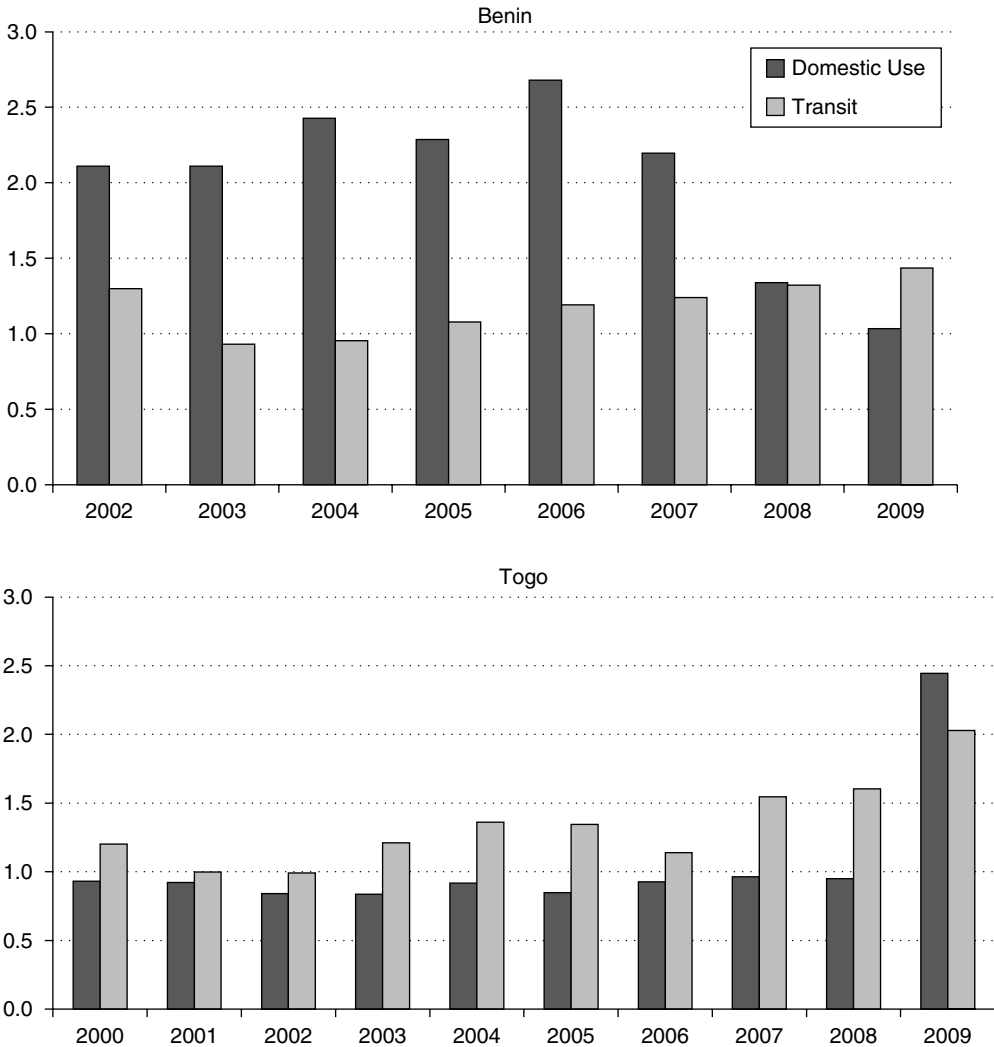
Source: Benin and Togo customs and author's calculations.

Figure 10.5 Average customs valuations of used cars (CFA francs per car) 2000–09

category of ICBT in traditional products, and is not primarily based on taking advantage of differential trade barriers, unlike the previous case study of West Africa. Formal border posts are few and far between. It is an 'openly informal economy' (Little 2005, p. 18). Differential policies do play a role, but a lesser one, and governments sometimes seek to control ICBT, although not very energetically or effectively, given the general recognition of the importance of this trade. Other traditional food staples are also traded informally in the region including maize and sorghum as well as some of the same re-exports as in West Africa, for example, sugar, wheat flour, tea, clothing (Little 2005, Table 1).
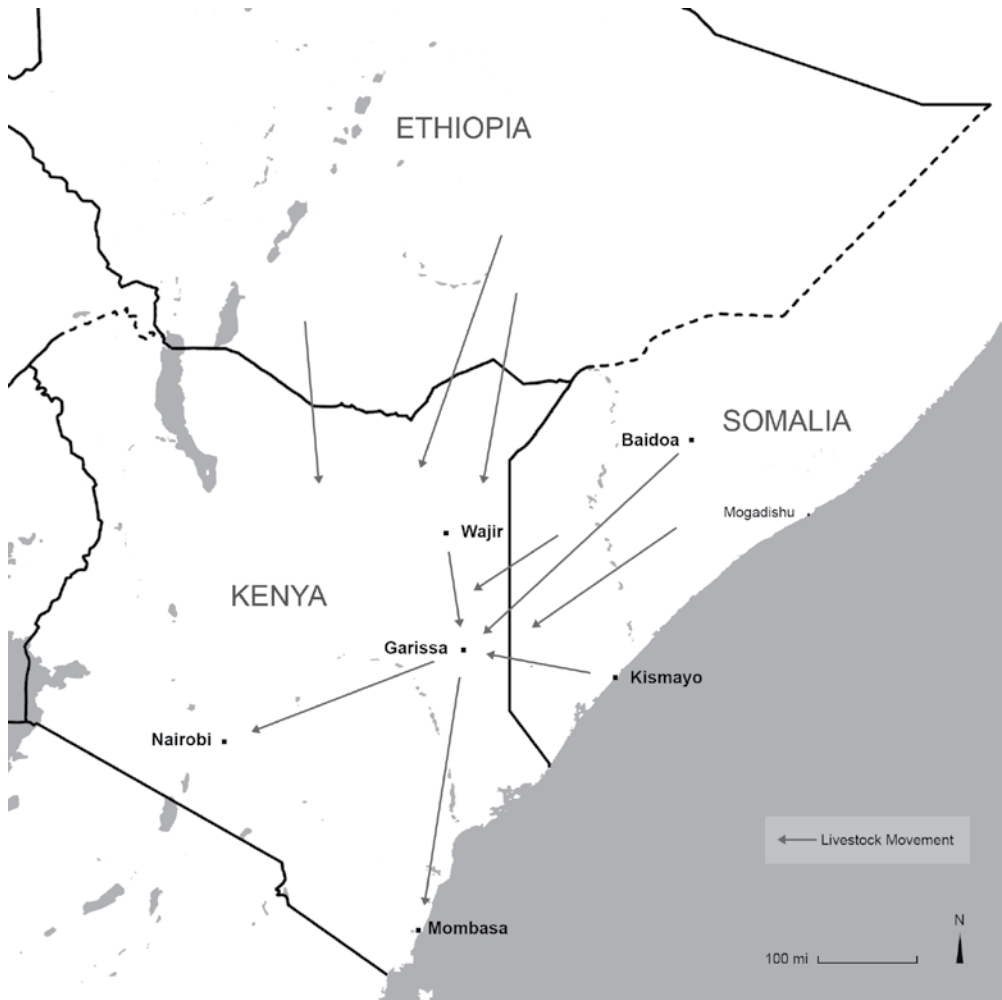
Source: Umwah Welfare Trust, available at http://www.uwt.org/site/article.asp?id=621.

Figure 10.6   The flow of livestock trade in the Horn of Africa

Geographical and institutional context

As for other forms of African ICBT, livestock exchanges predate the colonial period and were part of the long-distance caravan trade. The region is characterized by arid and semi-arid climates and covers a very large area. Cattle often trek over great distances in response to regional price differentials. The main consumer market driving the livestock trade is in Kenya. In addition, Somalia serves an entrepôt for exports of livestock from other countries, especially Ethiopia, to the Middle East, although these exports dropped in the early 2000s due to an import ban in Saudi Arabia following an outbreak of Rift Valley fever in Somalia.

Somalia and Ethiopia have become a major source of animals for meat consumption in Kenya, particularly in Nairobi, since Kenya liberalized its meat market in the early 1990s. Prices of cattle are typically 20–25 percent higher in Nairobi than in Ethiopia and Somalia. In the early 2000s, Somalia provided about 16 percent of the Kenyan market (Little 2005).

Causes of ICBT in the Horn of Africa

As in other cases, ICBT arises out of regional comparative advantage due to climate differences, resources and population distribution, on the one hand, and economic policies on the other. Regional differences in weather, political conditions, income levels and policies translate into flows of cattle and other traditional products. The relatively high incomes in Kenya, the collapse of the state in Somalia, and the vast area for grazing in Ethiopia and Somalia are all important. This trade plays a crucial role in regional food security, through its responses to shocks to regional supply and demand, and differing comparative advantages in production. In areas near the border, markets in neighboring countries may simply be more conveniently accessed than markets within a country. Herding communities have little sense of national identity, and kinship groups, as elsewhere in Africa, are not confined within national borders.

Divergent policies in an environment without natural topographical separators and ethnic and cultural connections among people within the region play, as usual, a prominent role. The collapse of the government in Somalia in 1991 following the war provided a major stimulus to ICBT. Little (2005) estimates that cattle sales increased at the main market town of Garissa on the Kenya–Somalia border about five-fold between the late 1980s and the late 1990s, all of it unofficial. Official institutions and market infrastructure were destroyed by the war, and in the absence of a functioning state in Somalia, there was little alternative to ICBT. The lingering insecurity affects trade routes. For example, tensions in the region between their home in the Kismayo area (see map) and the Kenyan border have locked out cattle from the Harti ethnic group in the Kenyan market (Little 2005, p.6). On the other hand, Ethiopia has a strong although perhaps overly interventionist state with high trade barriers (Teka and Azeze 2002). Ethiopia attempts unsuccessfully to interdict ICBT. Reportedly, Ethiopian officials refuse bribes but the border is too vast for them to control.

Functioning of ICBT in livestock

As in West Africa and elsewhere, ICBT in the Horn of Africa involves a complex and heterogeneous group of actors. Large- and small-scale traders operate in tandem. Formal transport infrastructure and services, such as veterinary services and banking, are almost non-existent. Consequently, clan relationships have become even more important in fostering market functioning in Somalia given the non-existence of state institutions. 'In these volatile, risky environments, Somali traders rely on their extensive kinship ties and on members of their clan and sub-clans' (Little 2005, p.9). Trust and stability offered by clan relationships have enabled the development of quite sophisticated informal institutions supporting informal trade.

As elsewhere, kinship networks in Somalia enable a sophisticated cross-border financial system, in some cases extending to other continents. Somali *hawilaad* remittance companies transfer funds within Somalia or between Somalia and cities around

the world at much lower commissions than international companies such as Western Union. Given the paucity of official information, market participants in Somalia turn to informal local brokers (*dilaal*) to bring together buyers and sellers and help them reach agreement on prices, thereby enhancing market functioning. These brokers are expert in accurately assessing animal health and weight and recommending an appropriate price. Despite the dramatic rise in insecurity, fees and functions of *dilaal*, brokers have not changed much since 1988. If there is a temporary glut in Nairobi, *dilaal* can communicate to suppliers in Somalia and elsewhere, in which case traders may remain at Garissa or in Somalia itself, until market conditions become more favorable to sellers.

Long-distance trekking over hundreds of kilometers has well-established procedures. Traders taking herds of approximately 100 cattle recruit a staff of three trekkers and a security guard for the trip, which can take up to a month. The head trekker is responsible for oversight, including making payments to militias and clans to assure secure passage of the herd. Another of the trekkers is typically a younger relative of the head trekker who assists with protection and physically demanding tasks. The third trekker is responsible for procuring food.

Sometimes, trucks take the animals from the border to the destination cities in Kenya, Nairobi and Mombasa. On the return trip, the traders purchase foods in Kenyan cities that are scarce and higher priced in Somalia. In this way, livestock trade contributes to improved food security both through the incomes the traders and herders obtain from selling their animals for better prices as well as by increasing the supply of foodstuffs in Somalia.

Cattle traders in Kenya are subject to pervasive insecurity, particularly theft, in an environment with little or no formal rules and protections. Insecurity sometimes induces traders to opt for trucking animals rather than trekking, even though the latter is less costly. These traders rely on various institutional mechanisms to increase trust and predictability in their transactions, including ethnic networks and partnerships (Mahmood 2008).

ICBT in livestock is important throughout the region and operates in broadly similar ways on different routes. There are some differences, however. Trade between Ethiopia and Kenya (E/K) differs somewhat from trade between Somalia and Kenya (S/K) (Little and Mahmoud 2005). Both involve a combination of trekking on foot and trucking. The E/K trade involves a larger variety of ethnic groups, so trust is more difficult to establish, making for more precarious contract enforcement. E/K traders have responded through partnerships among traders to exchange information and provide mutual support in collecting debts and transferring funds with reduced risk of theft.

10.7   SMUGGLING AND DEVELOPMENT

The economic theory of smuggling reviewed in section 10.2 suggests that ICBT can be welfare-enhancing or reducing depending on the economic environment and the nature of smuggling. More generally, ICBT has costs and benefits. On the positive side, the contribution of ICBT to income and employment in Africa is difficult to measure, but is certainly large. ICBT accounts for the preponderance of total trade in many countries, providing a major source of income and employment for many people; Afrika and

Ajumbo (2012) estimate that ICBT provides income for 43 percent of Africans. ICBT and related services generate considerable employment for young people (e.g. Roitman 2004). In the case of Benin, Golub (2012) estimates that re-exports contribute as much as 20 percent of GDP, about half of which is from the used car trade. In the absence of formal sector employment opportunities, ICBT provides a source of employment of last resort. The cheap goods delivered through ICBT to low-income consumers are also a boost to living standards. Trade in foods alleviates food security both through the incomes it generates in rural areas, and the distribution of staple products from relatively abundant to scarce regions.

Overall, however, the pervasiveness of ICBT arises primarily out of fundamental economic weaknesses even if it ameliorates some of the symptoms of economic dysfunction. For some entrepôt nations, ICBT contributes substantially to fiscal revenues, but for most countries, unrecorded trade entails substantial losses of revenues, reducing state capacity to fund public goods. Trading, particularly for small-scale survival traders, often women, is arduous, dangerous and low-paying, with little scope for sustained gains in living standards. The continued prevalence of informal trade constitutes a 'Devil's Deal' or prisoner's dilemma (Tendler 2002; Titeca and Kimanuka 2012) that perpetuates itself but does not serve the long-run interest of either the government or the private sector.

Thus, the gains from ICBT rest on a fragile foundation and are unlikely to be conducive to long-term development. It could be argued, as in Deardorff and Stolper (1990), that tariff competition serves a positive social function by circumventing distortions. But the first best policy is the elimination of the distortions that are the *raison d'être* of this trade. The sustainability of trade strategies that are substantially based on preying on distortions is highly questionable. Harmonization of trade policies, improved trade facilitation and more effective border controls would curtail ICBT. ICBT undermines formal trade with unfair competition. Moreover, smuggling contributes to an acceptance and even admiration of tax evasion and corruption.

Harsh crackdowns on traders without resolving the underlying distortions only cause hardship. For example, when President Mugabe's regime destroyed the market stalls in Zimbabwe under Operation Murambatsvina it also ruined numerous low-income families without any offsetting benefits (Ndlela 2006). Policies should distinguish between large and small informal operators. For large informal traders who could be formal but choose to remain informal, a combination of carrots and sticks should diminish the incentives promoting or allowing illegal and opportunistic behavior. Small-scale operators require assistance in transitioning to formal status. A few countries' governments, notably Uganda, are studying ICBT and developing policies to assist small-scale traders (Afrika and Ajumbo 2012). This leads to paradoxical situations, where governments enact edicts to ban unofficial payments! Some countries such as Senegal and recently Zimbabwe have sought to encourage gradual formalization through simple lump-sum presumptive taxes, but these are difficult to implement effectively and compliance is low (Benjamin and Mbaye 2012, Chapter 6). Reduction, harmonization and simplification of trade barriers and regulations and stronger state institutions, particularly customs administration, are important for all traders. Traders will formalize when it is cheaper to pay duties and comply with regulations than pay bribes and incur costs to evade detection.

10.8   CONCLUSIONS

Smuggling in Africa is flourishing due to a confluence of factors: long traditions of regional trade preceding the colonial era; artificial borders imposed by the colonial powers, largely maintained as African nations became independent around the early 1960s; strong ethnic and religious ties uniting people across the borders; uncoordinated and often highly interventionist policies in the newly independent states, particularly with regard to trade policies; weak state institutions, which undermine the effectiveness of the enforcement of these policies, and widespread corruption, which reduces the legitimacy of the state and undermines tax morale; inability of governments to control movements of people and goods across these artificial borders; and widespread poverty and unemployment, which has spurred both the demand for and supply of informal markets.

Cross-border trade straddles the formal and informal sectors in a highly complex and well-organized system that operates quite similarly in different countries. For example re-exports start with large formal enterprises that import goods through official channels and a sophisticated distribution chain that then transships through informal mechanisms, involving a network of large and small operators. The prevalence of smuggling can be documented through an integrated analysis involving the volume of recorded trade flows and case studies based on anecdotal information in the countries themselves.

ICBT provides a major source of income, employment and sometimes, paradoxically, government revenues, given that goods are imported legally prior to being re-exported unofficially. This trade rests on a fragile foundation, however, and is unlikely to be conducive to long-term development, given its dependence on policy distortions and its underground character.

Interdisciplinary approaches involving a combination of quantitative and qualitative methods are the most fruitful for understanding ICBT, using case studies as a point of departure. Economists should learn from and collaborate more with anthropologists, sociologists, historians and political scientists with expertise in case study methodology and who provide useful inductive analytical perspectives that complement the more quantitative and deductive approach of economics.

NOTES

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1. This section draws on Azam's (2007, chapter 2) excellent summary of the literature on the theory of smuggling, providing a more abbreviated treatment.
2. See Azam (2007) for further discussion of the conditions under which the supply curve for smuggling is upward sloping.
3. This section draws on Golub (2012) and Golub and Mbaye (2009).
4. The members of WAEMU are Benin, Burkina Faso, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal and Togo. All but Guinea-Bissau are Francophone.
5. In addition to the members of WAEMU, ECOWAS includes the Anglophone countries Cape Verde, The Gambia, Ghana, Liberia, Nigeria and Sierra Leone.
6. Based on Chapter 4, 'Transportation and Trade Facilitation', of *Togo Country Economic Memorandum* (World Bank 2010).

7. To what extent was the sharp drop in sales in Togo in the first part of 2009 attributable to the rise in valuations versus the economic downturn in Nigeria? Some insight can be obtained by comparing Togo and Benin's imports. Togo's car sales fell sharply in the first 5 months of 2009 (annualized) over 2008, by 53 percent for the domestic market and 49 percent for transit, an overall drop of 50 percent. In Benin, overall car imports were down too, but only by 26.5 percent, with cars for domestic use up 9.5 percent while cars imported in transit were lower by 29 percent. This suggests that the Nigerian crisis explains about half of the decline in Togo's sales and that the new higher valuations were also hurting Togo's competitiveness.

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