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journal homepage: www.elsevier.com/locate/euroecorevTerror networks and trade: Does the neighbor hurt?[☆]José De Sousa^{a,b,c}, Daniel Mirza^{d,e,*}, Thierry Verdier^{f,g,h}^a U. Paris Saclay, France^b RITM, France^c CREST, France^d LEO-CNRS, U. Tours, France^e CEPII, France^f PSE France^g ENPC-ParisTech, PUC-Rio, France^h CEPR, United Kingdom

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ABSTRACT

This paper studies how network-related terrorism redistributes trade flows across countries, including those countries that are not a direct source of terror. We first develop a game theoretical framework with imperfect information on the spatial location of transnational terrorism to show how the resulting security measures produce a non-monotonic effect on the distribution of trade across countries. Neighbors adjacent to terror, even when they do not source it, have trade reduced through enhanced security measures, while countries farther away benefit from those security measures. Second, to empirically assess the distortional effects of terrorism on trade, we first estimate the structural gravity equation derived from our theory. Then, armed with the estimates of the partial effect of neighbor terror on bilateral trade, we perform a counterfactual experiment and confirm the non-monotonic general equilibrium effect of neighbor terror on trade.

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1. Introduction

This paper studies how global terrorist networks distort trade across countries. It theoretically and empirically investigates the relationship among transnational terrorism networks, security reactions and the reallocation of trade flows across countries. Our starting motivation builds upon the three following observations.

First, terrorist networks have been playing an increasingly important role in the expansion of terror in the world since the 1990s. In 2014, more than twenty identified groups worldwide had joined or established close relationships with Al-Qaida. Additionally, in the last couple of years, the world has been observing a dramatic increase in the number of groups that have chosen to pledge allegiance to (or at least coordinate most of their actions with) the Islamic State. Hence, while

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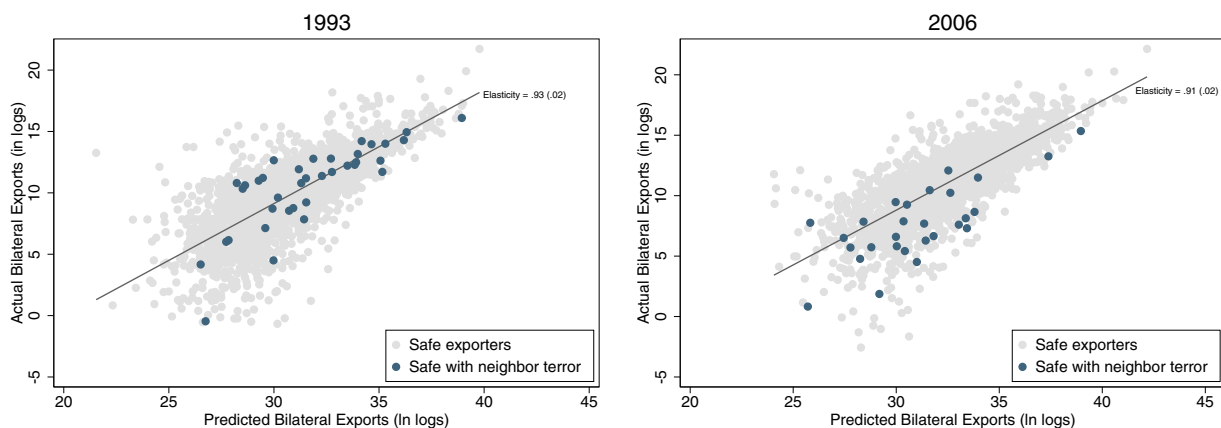


Fig. 1. Bilateral Exports of Close-to-Terror Countries and Deviation from Potential.

Notes: Each dot stands for one pair of countries involving a ‘safe exporter country’, that is, a country with no terrorist incidents reported in the previous 5 years. However, some of these exporters, depicted by a dark blue dot, have neighbor(s) who commit terrorism against the importer in the pair. The neighbor relationships are defined based on shared characteristics: a border, an official language, and a religion. The figures in 1993 and in 2006 contain the same sample: 2116 country pairs composed of 53 exporter and importer countries. Each figure plots the actual bilateral exports (in logs) against the predicted bilateral exports (in logs). The predicted flows between exporter i and importer j are exports predicted by a simple gravity equation ($\ln(\text{GDP}_i) \times \ln(\text{GDP}_j) / \ln(\text{DIST}_{ij})$).

The elasticity coefficients from the OLS regression of the log actual exports on the log predicted exports are reported with standard errors. (For interpretation of the references to color in this figure legend, the reader is referred to the web version of this article.)

the collective share of terror networks in total transnational incidents was no more than 5% in the 1990s, it climbed at a yearly average of approximately 20% in the 2000s to reach more than 60% in 2014.¹ Although most of the incidents have been concentrated in certain areas (the Middle East, North and Sub-Saharan Africa, and Central and East Asia), the number of countries and nationalities involved have multiplied by a factor of almost 4 since the 1990s. By 2014, those groups were at the source of approximately 1000 *transnational* incidents in approximately 20 locations against people from more than 35 nationalities amounting collectively to more than 3000 victims, a figure that is equivalent to the 9/11 attacks.

Second, as terrorist networks expand and the level of transnational terrorism threat consequently rises, countries sourcing terrorism *and* countries that are likely to host terrorist cells are more closely monitored. The US Department of State reports recent evidence of active monitoring in Northern Mali, where Al-Qaeda in the Islamic Maghreb (AQIM) and affiliated groups have exploited the political chaos to expand their presence. The US Department of State writes, “[We] are monitoring the actions of AQIM and other extremist and terrorist organizations in the north, and continue to work with the international community to address this evolving threat. [We] continue to enhance our work with Mali’s neighbors, to increase their capacity to secure their borders, disrupt AQIM supply lines, and contain the spread of extremist groups.”² Monitoring goes hand in hand with more restrictive security measures, such as increased checks at borders, restrictions on visa allowances or immigration controls. A quick look at the cross-country differences in the number of US non-immigrant visas issued to foreign nationals offers evidence of this restriction. In 2002, after the September 11 attacks, almost every country experienced a reduction in visa allowances, although some countries, especially Muslim ones, have been more affected than others (Cainkar, 2004).³

Third, security measures increase the costs of international trade (see Anderson and Marcouiller, 2002; Anderson and van Wincoop, 2004; Mirza and Verdier, 2014). The broadening of such measures may cause a country close to the location of terror to face negative trade spillovers without necessarily being a source of transnational terrorism itself.⁴ Fig. 1 illustrates this idea by comparing the trade performance of two types of countries. The first type concerns countries that are “safe from terror” in the sense that neither they nor their geographical and cultural neighbors have not been involved in any incident

¹ Transnational incidents are defined as such when they involve incidents perpetrated by some group against some (physical or human) foreign targets or when they are located in a foreign country. Calculations are from the authors based on data from the Global Terrorism Database, a recent and publicly available data set. See <https://www.start.umd.edu/gtd/>.

² The rest of the quote is also very insightful “We assist Mauritania and Niger through the Trans-Sahara Counter Terrorism Partnership, which is designed to help build long-term capacity to contain and marginalize terrorist organizations and facilitation networks; disrupt efforts to recruit, train, and provision terrorists and extremists; counter efforts to establish safe havens for terrorist organizations; and disrupt foreign fighter networks that may attempt to operate outside the region.” (see <http://www.state.gov/p/af/rls/rm/2012/201583.htm>).

³ On average, Europeans and Asians experienced a 15% and 23% decrease, respectively. Muslim countries experienced a 40% decrease with a large variance from –1% for Eritrea to –67% for Saudi Arabia.

⁴ See Section 3 and Appendix B for a detailed presentation and discussion of the data.

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