Impacts of Economic Crises on Regional Integration Process: Lessons from the 2008 Global Economic Crisis and 2010 Euro Zone Crisis

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Abstract - This paper is on the possible impacts of economic crisis on regional integration. It focuses on the possible impacts of the 2008 global financial and economic crisis (GFEC) and the 2010 Euro Zone sovereign debt crisis on regional integration process. The author identifies and analyses various possible ways in which the two economic crises can negatively affect the regional integration process in the East African Community (EAC). These ways include but are not limited to the impacts of the crises on the availability of funds needed for the integration process, derailment of the macroeconomic convergence criteria, and protectionism tendencies among others. It is concluded in the paper that economic crises in general and the 2008 global and financial crisis and the 2010 Euro zone sovereign debt crisis in particular may slow, derail or even halt the regional integration process in the EAC. Areas for further research based in this paper include a need for detailed country-specific empirical case studies to take this essentially theoretical and conceptual paper to the next level.

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I. Introduction

The 2008 global financial and economic crisis (GFEC) started to manifest itself officially on 15th of September 2008 in the United States of America (USA). Since then it has spread not only to the financial sector but also to the real sectors of the economy. Geographically, it has spread too many parts of the world especially in Europe and Asia where the first round effects were rapidly experienced. In Africa in general and Tanzania in particular, the crisis has been mainly seen in form of second round effects (bounce-on effects) in the real economy.

The 2008 crisis is also termed the credit crunch, economic turmoil, economic downturns, global meltdown, and financial meltdown. For the purpose of this work, the term economic crisis will be used. The crisis has been termed ‘the current’ to distinguish it from a similar crisis that was experienced in the 1930s that resulted into the Great Depression. The 2008 crisis manifested itself in form of severe credit, banking, currency, and trade crisis.

The crisis has many and closely linked causes, impacts and responses as well as many results of the responses. Within less than three years after the crisis, there have been many, far-reaching and closely linked impacts of the crisis at individual, household, community, country, sub-region, region and global levels... There have also been many and far-reaching responses to the crisis. The responses have aimed at halting the crisis, reducing its negative impacts, preventing a new crisis in the future and even exploiting opportunities that have unfolded from it.

The crisis has been among the leading current and contemporary global discourse issues since it saw the light of the day. This is so in the academia, policy and decision making, among practitioners as well as the general public.

II. The 2008 Economic Crisis

According to Eghan (2010), economic crises usually refer to a long-term economic state characterised by slow growth or setback in economic activity; rising unemployment; low prices; and low levels of trade and investment. In this section, some few basic issues related to the 2008 economic crisis are outlined. These include the meaning and nature of the crisis, and causes as well as impacts of the crisis.

a) Meaning and nature of the 2008 crisis

According to One (2009), the global economic crisis is also called the Great Depression II of 2009 and it is several times more severe than the Great Depression of 1929. This cannot be perfectly correct because the crisis began in 2008 and not in 2009.

Akbar (2008) correctly argues that the crisis has been a major financial crisis. It became prominently visible in September 2008 with the failure, merger or conservatorship of several large United States-based financial firms including but not limited to Goldman Sachs, Morgan Stanley, J.P. Morgan, Bank of America,

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b) Causes of the 2008 economic crisis

There are many and closely related causes of 2008 economic crises. Some of the causes that have been put forward in the literature are outlined in this section.

Moyo (2010), outlines some of the underlying factors that set the stage for the 2008 crisis. These include but are not limited to prolonged economic boom for two decades preceding the crisis accompanied by surging house prices at a rate which was unsustainable especially in United States of America; rapid expansion of credit leading to accumulation of debt several times the size of Gross Domestic Product (GDP) with significant proportion of the credit owed by marginal, doubtful and barely credit worthy clients (sub-prime borrowers) in the U.S; and emergence of new, innovative types of financial instruments and over-expansion of predatory lending practices such as adjustable rate mortgage that tended to obscure the true position of lenders and capacity of borrowers to service their liabilities.

Moyo (ibid) further outlines that the crisis was also caused by the rapid expansion of securitization whereby loans (mainly to non credit worth borrowers) were bundled together and sold to other lenders. Then the resulting paper transaction was used as a basis for further lending thereby making the financial markets highly leveraged. Inter alia, sub-prime mortgages were bundled into mortgage-backed securities or collateralized debt obligations and sold to investors.

Weak regulatory mechanisms and oversight is another cause of the crisis that has been correctly outlined by Moyo (ibid). This cause has also been captured by Ngowi (2009 and 2010) and Adei (2010). The key argument is that the monetary authorities (The Federal Reserve Bank of USA) did not catch up with things till it was too late. This was made more difficult because balance sheets of the financial institutions had become more complex as the companies exploited earlier American legislation to hide the true state of the companies.

Similar to other scholars, such as Adei (ibid) and Ngowi (ibid) Sikod (2009) attributes the crisis to asset price bubble. This interacted with new kinds of financial innovations that masked risk with companies that failed to follow their own risk management procedures and with regulators and supervisors such as the Federal Reserve Bank (the Fed) that failed to restrain excessive risk taking.

Rwegasira (2010) citing the Bank of Tanzania – BoT – (2008) captures very well the fact that the turmoil in global financial markets has resulted in lack of confidence in financial markets that has severely curtailed credit in global markets (the credit crunch). The source of the crisis was sub-prime mortgages offered by financial institutions in the United States. The effects of those mortgages quickly spread across the West and other parts of the world.

Oke (2009) correctly argues that the crisis was triggered by the failure of sub-prime mortgage loans in the United States and it became prominently visible in September 2008. As alluded to by many other authors, this author captures well the fact that the crisis began with failure of large financial institutions in the United States of America. It then rapidly escalated into a global credit crisis. As a result there were a number of US and European banks failures. Also there were declines in various stock indices.

Mutahi (2009), argues that the crisis began in July 2007 when a loss of confidence by investors in the value of securitized mortgages and banks in the United States started. However, this is not exactly the case. This was just among the signs of the crisis and not the beginning of the crisis itself.

According to Akbar (ibid), Evans-Pritchard (2007) and The Economist (15th May and 22nd May, 2008), the underlying causes leading to the crisis had been reported for many months before September 2008, with commentary about the financial stability of leading U.S. and European investment banks, insurance firms and mortgage banks consequent to the sub-prime mortgage crisis. The failures of large financial institutions in the United States rapidly evolved into a global crisis resulting in a number of European bank failures and declines in various stock indexes, and large reductions in the market value of stock (Norris: 2008) and commodities worldwide (Evans-Pritchard, ibid).
c) Impacts of the crisis

The crisis has had many and far-reaching direct and indirect as well as short-term and long-term impacts across the globe. Given the source and nature of the crisis, it is the developed countries that have been more affected than the developing ones. However, the impacts of the crisis have been continuously unfolding over time.

Literature on the various impacts of the crisis has emerged over time. The literature include but are not limited to Ngowi (2009a) on employment and official development assistance (ODA); Ngowi (2009b) on investments in human capital; Ngowi (2009c) on the climate; Ngowi (2009d) on Tanzania and Ngowi (2009e) on Africa.


The general and common factor among the cited works on the impacts of the crisis include liquidity problem and the de-leveraging of financial institutions especially in the United States and Europe, which further accelerated the liquidity crisis. It is causing fears and declining consumers and investors sentiments in the market thereby reducing aggregate demand. Other impacts include currency crisis with investors transferring vast capital resources into relatively stronger currencies. This in turn is leading many emergent economies to seek aid from the International Monetary Fund. (Landler, 2008 and Fackler, 2008, quoted on Ngowi, 2009a).

Other general impacts of the crisis include reduced aggregate demand of goods and services across the globe. This is due to limited liquidity and related problems such as all-times low consumer sentiments that are emanating from the crisis. The reduced aggregate demand in turn is leading to reduced production of goods and services with the necessary result of reducing demand for and employment of factors of production including labour. The implications of reduced employment of factor inputs include reduced incomes to the factors and their owners in general and reduced standard of living and possibility of vulnerability to poverty for labour in particular.

In some countries, migrant workers, (foreign labour) are likely to suffer more by being the first to be laid-off. This will have many and far-reaching implications on the countries and individuals dependent on transfers from migrant workers in form of remittances. The crisis is culminating into a worrisome meltdown in the economies of most developed countries.

The actual extent of impacts of the crisis depends on a number of issues. These include but are not limited to the degree to which a particular country is integrated into the dynamics of global investment flows, trade integration, information technology and vibrant financial security arrangements. It will also depend on the extent to which a country is marginalized from the dynamic processes above. The kinds of policies that will be put in place by individual governments independently and in collaboration with the global community to solve and mitigate the impacts of the downturn will determine inter alia, the severity and length of the crisis.

III. On the Euro Zone Sovereign Debt Crisis

The European sovereign debt crisis is usually referred to as the Euro zone crisis. This is arguably an extension of the 2008 economic crisis. Its main cause are huge government debts that arguably result from some forms of responses to the 2008 economic crisis especially the economy-wide economic stimulus packages and sector as well as industry-specific bail outs.

According to Ibrahim (2012), the Euro zone crisis has made it difficult or impossible for some countries in the Euro area to re-finance their government debt without the assistance of third parties. Several Euro zone countries and the PIIGS (Portugal, Ireland, Italy, Greece and Spain) family of countries in particular (Greece especially) have been in the need of bailout from fellow Euro zone countries especially the strong economies of Germany and to a point though that of France. The Euro zone has even looked at as far as China for some kind of bailout through, inter alia, persuasion for more Sino-imports from the Euro zone.

There are various causes of the crisis across the Euro zone countries. In several countries, private debts arising from a property bubble were transferred to sovereign debt as a result of banking system bailouts and government responses to slowing economies post-bubble. In Greece for example, unsustainable public sector wages and pensions drove the debt increase.

the Euro zone as a monetary union without fiscal union contributed to the crisis too.

According to Matlock (2010) 4 and The Economist (2011) 5, concerns about sovereign debt crisis intensified in early 2010 and thereafter. The Economist (ibid) informs further that in May 2010 a rescue package worth €750 billion aimed at ensuring financial stability across Europe was approved. This was done by creating the European Financial Stability Facility (EFSF).

By August 2012, the global economic situation was not very healthy. This is partly due to negative trends in some key indicators in some leading global economies as documented in the box below. The negative trends imply inter alia, less revenue from trade, investments, remittance and aid to Africa and by extension, less revenue in African government coffers and therefore less financial resources to enhance public sector performance.

**Box 1 : Key changes to world economic forecast from August 15th 2012**

<table>
<thead>
<tr>
<th>Country</th>
<th>2012 GDP Growth Forecast</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States of America (USA)</td>
<td>1.7%</td>
</tr>
<tr>
<td>Germany</td>
<td>0.5%</td>
</tr>
<tr>
<td>Japanese</td>
<td>1.5%</td>
</tr>
<tr>
<td>Germany's Euro zone demand</td>
<td>2.2%</td>
</tr>
<tr>
<td>Excluding Japan, Asia and Australasia</td>
<td>2.1%</td>
</tr>
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</tr>
<tr>
<td>Source: Economist Intelligence Unit, August 2012 Global Economic Forecast</td>
<td></td>
</tr>
</tbody>
</table>

**IV. Possible Impacts of the Two Economic Crises on Integration Process in the Case of EAC**

The central thesis of this paper is that economic crises in general and the 2008 global financial and economic crisis and the 2010 Euro Zone sovereign debt crisis in particular stand to negatively affect regional integration process in the EAC. In this section, various routes via which this can happen are outlined.

a) Financing integration process and projects

The various activities in the integration process at country and regional level need funds. In times of economic crisis such as the 2008 GFEC and the 2010 Euro Zone sovereign debt crisis such funds are extra scarce. This is because partly the funds come from donors who are highly affected the crises. In times of crises such as there, government’s own sources of revenues including but not limited to taxes, fees, funds accruing from various kinds of investments including Foreign Direct Investment (FDIs) are highly reduced in times of economic crisis.

Fund from remittances from a country’s sons and daughters in the Diaspora also tend to get dramatically reduced and countries also find it difficult and extremely costly to raise funds through sovereign borrowing. For example, Tanzania and Kenya had to shelve infrastructure Euro bond borrowing due to the 2008 crisis. Keeping in mind that infrastructure is among the key components in integration process, then integration process in this area may be slowed. Germany is among the donor countries that are much supporting the EAC integration process. Yet it has to deal with struggling fellow Euro Zone economies in general and the PIIGS (Portugal, Italy, Ireland, Greece and Spain) in particular.

b) Trade: Protectionist tendencies

In the time of the 2008 economic crisis, some countries came out with policy responses taking the form of protectionist tendencies. Such slogans as “Buy American”, “Buy Tanzanian”, but also “Buy East African” have been noted. Protectionist tendencies like “buy Tanzanian”, or “Buy Kenyan” are against regional integration in general and free regional trade in particular. In the box below, some protectionist tendencies during the 2008 crisis are outlined.

**Box 1: Protectionist Tendencies as Policy Response to the 2008 Economic Crisis**

Among the major challenges of attaining the G20 goals of addressing the economic crisis are the protectionist tendencies amongst some of its members. As part of solving domestic problems posed by the economic downturn some countries have embraced protectionism of some kind. The world has recently seen barriers to free trade in place. These have taken the forms of tariff and non tariff barriers. Such slogans as “buy American, buy Chinese, buy European, buy East African” have been seen and heard. Trade partners of these protectionist countries and regional blocks may retaliate. This will be adding salt to the injury in the world that aims at escaping the crisis through shared growth that by and large comes from free international trade. To the extent some members of the G20 are practicing some forms of protectionism; it will be a huge challenge to address the crisis as per the November 2010 Seoul Summit goals.

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c) Monetary Union

The EAC’s next stage in the integration process is formation of a monetary union with possible single currency. However, there are many criteria that have to be fulfilled before this rather ambitious stage is attained. Among other things, experience from the Euro zone sovereign debt crisis may require the EAC Partner States to pose for a while until all the macro-economic convergence criteria are in place. Worries on whether EAC is ready for a monetary union has been discussed by the author of this paper earlier on. Some of his views are captured in the box below.

Box 2: East African Monetary Union: Are We Ready?

The East African Community (EAC) has come a long way as a regional trading bloc. After the resurrection of the defunct EAC, it has graduated from a customs union to a common market within a decade or so. The aim now is to move into the next stage of deeper integration which is a monetary union to be followed by what stands to be a complex political federation project. Noble as the monetary union plans are, the need to debate on whether the time and conditions for a meaningful EAC monetary union are ripe or not cannot be overemphasized. The author gives his contribution in this article.

i. Understanding Monetary Union

A monetary union is said to be in place when two or more sovereign countries are having a single currency. They may also have different currencies but have a fixed mutual exchange rate. This exchange rate has to be monitored and controlled by one central bank or several central banks with closely coordinated monetary policies. It is a form of regional trading bloc with a single market, harmonized interest and taxation rates with a common currency. It different from a mere currency union which does not involve a single market. Among the known monetary unions include the Economic and Monetary Union in the European Union and the West African Monetary Union.

ii. Pro and cons of Monetary Union

Monetary Union is good as a deeper stage of integration. It potentially makes businesses and investments as well as movements of people and capital within the block much easier. It would remove currency convergence transaction costs and risks. However Monetary Union may be tricky in the event of financial and economic crisis. An individual country within the block may not be able to manipulate its monetary policy (especially the exchange rate instrument) to address the crisis. This has been among the problems that confront Greece, Ireland and Portugal in the context of being in the Euro Zone family.

iii. Are conditions ripe in EAC?

The EAC Monetary Union is planned to see the light of the day come 2012. The target date for is too ambitious and highly unrealistic given the situation on the ground. There are too many pieces and bits that have to fall in place in the complicated jig-saw puzzle before we can have a meaningful monetary union. Some of these pieces and bits are outlined in what follows.

iv. People’s understanding is wanting

The PEOPLE - especially the men and women in the market places in the streets of our towns and valleys and mountains of our country sides need to know what Monetary Union is and what is in it for them. Arguably, even the earlier stages of custom union and common market are not yet understood by many. Instead of bombarding the people with deeper integration, first let them absorb the new realities brought by the earlier stages of integration. This is because the integration should be built on a strong foundation with the PEOPLE as its base as opposed to leaders especially politicians as the base. This needs time much beyond 2012.

v. Convergence criteria not in shape yet

Other key issue that does not allow the birth of the Monetary Union this time around includes the much needed macro-economic convergences. A number of economic variables have to converge if the envisaged Monetary Union is to make sense. These include inflation, budget deficits, and national debt as percentage of gross domestic product (GDP), interest and exchange rates and many more. Most of these convergence criteria cannot be met ‘tomorrow’. For example inflation is supposed to converge somewhere around 5%. But the reality on the ground in Tanzania for example does not indicate that inflation will be tamed at this low rate soon. It is now over 7% and likely to go up given the power crisis and the sky-rocketing pump prices. Elsewhere in the region inflation trends are not encouraging either. Other convergence issues include harmonization of monetary and fiscal policies and their various instruments.

vi. Fast-tracking is not necessarily good

There is a need to avoid a ‘too rapid’ deeper integration. Care for more quality of integration rather than ticking boxes showing that stages XYZ have been covered is necessary. We should not hasten all these other stages of integration so as to reach the political federation part of it as soon as possible. There is a need to let things evolve naturally although some catalysts are necessary, even if we wanted the Monetary Union or political federation for that matter - since yesterday.

vii. What should be done now?

Fortunately, forming a monetary union is a process not an event. As the preliminary process continues, the focus should be on strengthening what has been achieved so far. Extra care should be taken before moving into greater integration including say, admission of new member states like Southern Sudan and Democratic Republic of Congo.
d) Macroeconomic convergence criteria

Macro-economic convergence criteria must be met before the integration process moves to the stage of a full monetary union. Due to the 2008 economic crisis and the 2010 Euro zone sovereign debt crisis however, there is a possibility that these criteria will be derailed thereby affecting the integration process negatively. For example, such macro-economic convergence criteria as economic-growth in Tanzania had to be scaled down from 7% to about 5% due to the 2008 economic crisis. Other convergence criteria that stand to be derailed by the two economic crises include but are not limited to Balance of Trade (BoT) that may be negatively affected due to reduced export volumes that affect export earnings. Other criteria include deficit in the national budget and national debt as percentages of Gross Domestic Product (GDP) which tend to be negatively affected due to widening of deficits and debts in times of economic crises.

V. Conclusions and Policy Implications

Based on the discussion above, it is concluded that economic crises can defer or even derail regional integration process. This will happen if, inter alia the macroeconomic conversion criteria are disturbed due to bleeding of economies in such turbulent and tumultuous times. It may also be derailed due to protectionist tendencies as policy responses in times of economic crisis. However, economic crises can also be a reason for countries to hold tight to each other through regional trade albeit such limitations as similarities in economies endowment.

VI. Areas for Further Research

This paper is by and large theoretical and conceptual in nature. There is a need for empirical and detailed studies on some or all of the issues identified in this paper.

References Références Referencias


Web Sources


APPENDIX

i. Appendix 1: A List of Conference/Commissioned Papers on the 2008 Economic Crisis written by the author of this paper.


v. The current global financial crisis and its implications on investment in human capital: The case of Tanzania – a forthcoming publication (2012) at the Journal of Institute of Public Administration, Mzumbe University Tanzania


vii. The current global financial crisis and its implications in Tanzania: A focus on official development assistance (ODA) – a paper commissioned by ILO Tanzanian, January 2009

viii. The earth in the world of economic crisis: Is the crisis good for the environment? some opportunities and challenges – a paper presented at the Earth Day, at the Embassy of the United Republic of United States of America (USA) Tanzania, April 2009


