

**Rivalry and Revenue:
State Building in the Middle East and North Africa**

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Abstract

Rulers struggle with external rivals who claim their territory alongside internal rivals who want to capture or secede from the state. War was often the historical solution for eliminating both types of rivals. Wars required increased revenue and the development of an administrative apparatus that formed the basis for modern bureaucratic states. Yet, contemporary rulers face additional constraints (e.g., relatively fixed borders) on their activities that largely rule out war as a solution to the problem of relatively weak states beset by internal and external challengers. This paper develops a fiscal sociology approach to investigate how contemporary rulers have adapted to their domestic and international environments in the search for revenue to build their states. The paper empirically investigates the role that war and external rivalries may play in stimulating revenue extraction in the contemporary Middle East and North Africa, as well as the role that civil wars and other forms of internal rivalry may play in diminishing such extraction. The empirical results from several cross-sectional time-series analyses demonstrate that war and external rivalry are positively associated with revenue extraction, while the effects of civil wars and internal rivalry are somewhat mixed.

Introduction

Rulers face a number of significant constraints and challenges as they attempt to build the contemporary developing state. Some of these challenges would be recognized by their early modern European forbearers whose activities produced the sovereign territorial state within which they must operate. Contemporary rulers similarly struggle with external rivals who wish to claim and rule their territory and population, alongside internal rivals who want to capture or secede from the state. Historically, war was often the solution for eliminating or neutralizing both external rivals and internal rebels. The prosecution of wars required increased revenue, which the ruler needed to extract from the subject population. The process of revenue extraction thereby required the development of an administrative apparatus that formed the basis for modern bureaucratic states. War making thus drove state making in early modern Europe in most predatory or bellicist theoretical accounts. Yet, contemporary rulers face additional constraints on their activities that largely rule out war as a solution to the problem of relatively weak states beset by internal and external challengers. I adopt a fiscal sociology approach to investigate how rulers have adapted to their domestic and international environments in the search for revenue to build their states given the different circumstances in which they find themselves as compared to earlier state builders.

I focus specifically on the Middle East and North Africa (MENA) in this paper. This region is an interesting test of predatory theories that stress the role of war and external threats in building strong states. War and interstate rivalry have featured prominently in the region, yet some analysts question whether these conflictual relationships have had state building consequences. The region also contains many rentier states, which are thought to have developed weak institutions as a result of the reliance on natural resource revenues. Oil has been

specifically targeted for its purported deleterious effects on state institutions. Many states in the region have also relied on foreign aid in lieu of direct resource extraction.

The results of several cross-sectional time-series analysis for the period 1960-2000 demonstrate that interstate war has stimulated both tax revenue extraction and total revenues, which include non-tax sources of income such as oil rents. Interstate rivalries also stimulate taxation and total revenues. Civil wars produce mixed effects, as they significantly reduce total revenue but not tax revenue. The presence of intrastate rivals has no significant state building effects. The rentier state hypothesis is confirmed as oil tends to increase total revenues while diminishing tax revenues. State building, at least from a fiscal sociology perspective, is occurring at minimal levels as a result of external threats in the region. Internal threats, on the other hand, seem to be kept in check by the state.

State Building in the Developing World

Predatory theories of state building focus on the impact of both internal and external competitors on the ruler's ability to control a specific territory and population for extractive purposes. According to Tilly (1985: 180), there are four different activities that rulers, or their agents, employ in the process of state building. The first is war making, whereby rivals located outside the territory the rulers are attempting to control are eliminated or neutralized. The rulers also engage in state making, where potential internal rivals are eliminated or pacified. The third activity entails the protection of the supporters of their rule. Finally, the rulers must find some way to extract resources from the population and territory they are attempting to control in order to carry out the activities that would allow them to solidify this control.

Tilly (1985: 180) argued that it was primarily the war making process that led to increases in the level of taxation and debt. Rasler and Thompson (1985: 491-492) suggest that

the state uses war as a tool to increase resource extraction in several ways, such as by influencing taxpayers' perceptions of an "acceptable" tax burden, providing a rationale for the expansion of the tax system, and showing the necessity for an increase in taxes to support increased military needs. This fundraising effort by the state will often turn into a debt raising process, especially during war, if the state is unable to extract sufficient resources from the population. Tilly (1985: 180) succinctly describes this relationship as one in which, "war, state apparatus, taxation, and borrowing advanced in tight cadence."

North, and other new institutionalists such as Levi, have also analyzed the impact that internal and external competitors have on the revenue generating ability of the state; or more specifically, how the constraints imposed upon the ruler affect the specification of property rights among the ruled. North and Levi argue that whenever there are close substitutes to the ruler (external or internal rivals), the ruler has less leverage in extracting income from society, therefore the ruled will retain a greater percentage of incremental income. Furthermore, other factors, such as resource possession, proximity to external rivals, or violence potential, may also impact the ruler's ability to extract resources (North, 1981: 27-29; Levi, 1981: 449).

It appears that predatory theorists share a common understanding of how the state developed in Europe. Rulers faced external and internal competitors (i.e., threats to their continued rule). In order to effectively deal with these threats, rulers needed to extract resources from the ruled. Since the extraction process necessarily involved bargaining among the ruler and groups representing alternate rulers, the overall amount of revenue captured by the state varied. Accordingly, success in the state building process has also varied according to the type and extent of threats posed by rivals.

But, can we extend this model to the developing world? Many scholars argue that the experience of the developing world in the 20th century does not resemble the European context of the 16th or 17th centuries. The incessant preparation for, and prosecution of wars for territory is often argued to be the reason that European states developed into strong, cohesive and capable polities (Cohen, Brown & Organski, 1981; North, 1981; Tilly, 1985; Tilly, 1992; Rasler & Thompson, 1985; Campbell, 1993). The kind of wars that ultimately produced great powers in Europe may have been short-circuited in the post-colonial developing world. For example, Tilly (1985: 185-186) suggests that as the European states completed decolonization and created the form of the state in the developing world, many of the internal struggles that produced consolidated, economically viable, and democratic states in Europe were not replicated, or according to Lustick (1997: 653-683), were not permitted. The state was transmitted in form, and certified by the United Nations, but the substance could not be put in place due to the deliberate prohibition of the processes that originally produced this type of polity.

The decolonization process that began after the close of World War II led to the emergence of a multitude of new states. These states were treated as formal equals to the colonial powers and other established states in the international system. Yet, a half century later, only a handful of developing states have achieved “empirical” as opposed to mere “juridical” statehood, with most still considered as some form of “quasi-state” (Jackson and Rosberg, 1982). As many have noted, sovereignty norms attached to statehood were adapted in ways that may have been helpful to these state builders in the short term, but have also generated unintended consequences over the long term. In particular, post-colonial states adopted the principle of *uti possidetis* (acceptance of colonial borders as legitimate state borders) and norms of nonintervention and noninterference. These normative principles have resulted in largely frozen

boundaries between states, thus removing interstate territorial competition as a driving force for state building in the developing world (Fazal, 2007; Atzili 2006/07).

Instead, interstate rivalry has become subordinated to the institution of sovereignty in the contemporary world. Since sovereignty now means that territorial aggrandizement is generally forbidden, rivalry serves the purpose of regulating conflict between states. In other words, rivalry has become an institutional feature of international relations as well. This is a somewhat different way of looking at interstate rivalries than currently prevails in the literature, which on the whole tends to emphasize the conflictual behavior of these relationships. Yet, the institutional approach to rivalry I advocate is still consistent with the conceptual language used by scholars. Diehl and Goertz (2000: 4) conceptualize an “enduring rivalry” as “a relationship between two states in which both use, with some regularity, military threats and force as well as one in which both sides formulate foreign policy in military terms.” Thompson (2001: 560) suggests that “strategic rivalries” occur when states view each other “as (a) competitors, (b) the source of actual or latent threats that pose some possibility of becoming militarized, and (c) enemies.” These conceptual definitions lend themselves to either a behavioral or institutional understanding of rivalry. Currently, most empirical work is rooted in a behavioral approach to rivalry, with Diehl and Goertz’s operational definition requiring a certain number of militarized interstate disputes in a certain time frame. Thompson’s operational definition does not require a dispute threshold; instead, he looks for evidence that the principal decision makers in both states view each other as rivals.

These types of rivalries are a pervasive feature of international relations. For example, Thompson’s classification finds 31 rivalries in Sub-Saharan Africa, 34 rivalries in the Middle East and North Africa, and 28 rivalries in Asia. Almost all states in these regions have

participated in at least 1 rivalry. Yet, the number of interstate wars and their duration is very small in comparison—2 in Sub-Saharan Africa, 8 in the Middle East and North Africa, and 9 in Asia in the post-World War II era. Most of the interstate conflict in these rivalries does not approach the severity of war and few even produce many casualties. The general contention of this paper is that rivalries are no longer the prime mover of interstate competition that generates strong states, but instead they serve to constrain and limit conflict in ways that are ritualized and symbolic. The symbolism of the rivalry allows state rulers to claim legitimacy in their revenue extraction and expenditure decisions based on external threat, but the threat is almost never a true threat to survival in the contemporary era. Thus, the state building wars of the early modern European era have few counterparts in today's developing world. While there may be exceptions to this general contention, I suggest that it is one of the primary reasons for the generally low levels of state building in the developing world.

I analyze the Middle East and North Africa (MENA) in this paper. This region is an interesting test for my view of interstate rivalries acting as a constraint on conflict, since wars have featured prominently in its history. Yet, other analysts have noted the lack of large-scale state building wars in the region equivalent to those experienced in Europe (Barnett, 1992; Lustick, 1997). The region also allows a consideration of the rentier state hypothesis, which blames the pervasiveness of natural resources (and specifically oil) for weak institutions in such states (Karl, 1997). The resource curse has been challenged by a number of scholars (Morrison, 2009; Smith, 2004), so the MENA region is a good location to examine competing hypotheses about the effects of oil in particular.

State Building in the Middle East and North Africa

Heydemann (2000) argues that attempting to compare the experiences in the Middle East to those of Western Europe during its formative period is misplaced. He argues that in the Middle East, in sharp contrast to Europe, war is not always made by the state and, furthermore, “war making has been indirect, mediated, and deeply transnationalized” (Heydemann, 2000: 9). Another point of divergence between the Middle East and Europe is the manner in which the states came into existence. In the Middle East, the vast majority of the states came into existence, as sovereign and separate entities, as a result of World War I and the subsequent collapse of the Ottoman Empire. According to Binder (1999: 11), the region was divided up to separate entities in a manner that would support Western interests:

the breakup of the region; the interposition of a clutch of would-be sovereign states in the Fertile Crescent among the better-established and internationally recognized states (Turkey, Egypt, and Iran); and the combination of natural barriers, long distances, and the limited contiguity of Middle East states, not to mention the culturally alienating consequences of the division of imperialist authority into English-speaking, French-speaking, and Italian-speaking colonial systems, minimized the degree to which any regional state might be able to assert its influence throughout the region.

These peculiarities in the creation and composition of these states would have important influences in their development.

World Wars I and II also influenced the processes of social transformation and state institutional change, but as an intervening variable rather than as the proximate cause (Heydemann, 2000: 10-11). Specifically, Heydemann (2000: 11-12) argues that indirect participation in World War II improved the capacity of the state to regulate both trade and agricultural production in place like Syria and Egypt, “but did little to alter the capacity of the state to tax.” With the end of World War II, the Middle East was no longer under the direct control of colonial powers and, at least on the surface, the states became responsible for their

own policies and actions. This independence, however, was not complete. The development of the states in the region was heavily influenced, and for some even constrained, by outside actors.

Lustick (1997: 653-683) argues that the forces constraining the development of the Middle Eastern state system were remarkably different from those faced by the early European states. European states were not constrained by the interference of outside powers, nor were they constrained by international institutions enforcing norms against territorial expansion as a result of the threat or actual resort to war. According to this argument, the interference of great powers and international organizations touting anti-belligerency norms to preserve the territorial status quo has led to the creation of weak states in the Middle East and Africa. Lustick (1997: 662) concludes that “international norms and great power policies have been responsible for blocking the emergence of a great power in the Middle East by deterring or preventing state-building wars from being fought to successful conclusions across existing Middle Eastern boundaries.” The underlying logic used to explain the lack of a great power also explains the lack of strong states generally in the region since the extractive capabilities of the states were also stunted as a result of this process.

Barnett (1992; 1995: 479-510) also draws explicit attention to the impact that external and internal threats have on state building efforts in the Middle East and North Africa. As Barnett (1995: 497) suggests, “not only do wars and external threats generally act as important impetuses behind the state’s penetration and control over society but also they can build a sense of ‘we-ness’ and develop a national identity.” He argues that while interstate conflict between Arab and non-Arab states may be useful for developing a pan-Arab identity, the “chronic infighting and rivalry” among Arab states serves to foster separate national identities. Inter-Arab rivalry allows the state to manipulate a variety of symbols including holidays, monuments, and

texts in service of the national identity, often to the exclusion of pan-Arabian identity. Thus, the “symbiotic relationship between the state’s extractive capacity and nationalism” that Herbst (1990: 117-139; 112) argues is absent in Africa may be more developed in the Middle East. Further, the oil wealth in the region offered some states the ability to become the primary material source of support for the people, thus ensuring politico-economic allegiance to the state rather than kinship groups. Overall, if Herbst and Barnett are correct in their assessments, then we would expect stronger states in the Middle East, at least for those rich with natural resources, than in Africa.

Barnett’s (1992) carefully researched study of Israeli and Egyptian war preparation strategies demonstrates the problems that two post-colonial, resource-poor developing states faced when attempting to increase their extraction in the face of a threatening external security environment. The ability of these two states to extract largely reflected the state administrative and social structures they inherited prior to independence.¹ Both states had to bargain with domestic societal actors in order to achieve their war preparation aims, despite their often presumed relative autonomy from society. Both exploited external threats, as well as the superpower rivalry, to augment their resources. As Barnett (1992: 261) concludes:

As the government is concerned with both its international and domestic opposition and viability, processes in both spheres shape and transform the state and its relationship to society. Just as the European state system was a product of and shaped by both the logic of capital accumulation and interstate violence, these themes and processes continue to be important factors in shaping the experiences of Third World states in the modern era.

¹Herbst (2000) also argues that extraction in Africa is a result of forces that predate independence, and even the colonial period. As the emerging independent states focused on retaining the organizational form of the state, they also chose to retain much of the colonial tax administration apparatus.

Gongora (1997: 323-324) argues that in the contemporary Middle East, war making can actually contribute to a decline in state power, as opposed to the opposite influence witnessed in Europe. Gongora (1997: 331) also argues that state capacity is not improved during war in the Middle East “because the type of warfare that prevails in the region—modern conventional warfare—marginalizes the value of domestic resources and increases the value of resources that are mainly externally derived: advanced weaponry, foreign currency, military assistance, and even skilled labor.” Heydemann (2000: 12) further asserts that the processes of war preparation and war making have tended to make the states in the region “highly porous.” This is primarily due to the fact that these states were heavily dependent on foreign assistance (both military and financial). According to Heydemann (2000: 12), “preparation for war is funded by foreign military assistance or rents of one form or another, war making is undertaken with imported weapons, global strategic networks and global norms of sovereignty and nonintervention are mobilized to secure local military advantage, and peace settlements are negotiated and guaranteed by external powers.”

Therefore, war making and war preparation for the states in the region is much more than purely a domestic policy or concern. Accordingly, a state’s ability to actively and successfully pursue these goals depends on continued external support. As illustrated by the Syrian case (Perthes, 2000; Clawson, 1989; Hawwa, 1994), when foreign sources of support dry up, the state is often forced to relinquish some aspects of control over the society in order to have the financial capacity to pursue its war preparation and war making goals. A key implication of this reliance on foreign support is that it “binds the processes of state building, state institutional formation, and the organization of state capacities to the maintenance of a level of threat, or perception of threat, sufficient to permit regimes to extract rents from regional and international

alliance networks” (Heydemann, 2000: 14). Accordingly, it is in the best interests of these states to maintain the perception that they are indeed in danger in order to keep the money and resources flowing from these sources. This view is suggestive of the role that interstate rivalries can play in maintaining Tilly’s protection racket in the MENA region.

This policy has domestic implications as well in that it usually results in an attempt to realize both domestic social mobilization and control through the use of militarism. These processes result in the following situation (Heydemann, 2000: 14):

Although war thus operates as a highly transnationalized phenomenon, the experiences of Syria and Iraq (as well as other states in the region) reaffirm its well-established importance in strengthening the capacity of states to mobilize and repress populations and to articulate especially aggressive forms of nationalist ideology. Yet...these capacities become embedded in and reproduced through war preparation and war making as routine modes of governance and domination, rather than emerging as responses to the exceptional and temporary exigencies of war. Indeed, it is precisely the normalization of war—the routinization of urgent threats to the nation, the transformation of the extraordinary into the everyday—that reflects the extent to which militarism organizes processes of state formation and state-society relations in number of Middle East states.

Furthermore, there is a strong connection between the amounts of external aid available and the levels of militarism and authoritarianism in the region. According to Heydemann (2000: 25), since states in the Middle East are able to avoid the intense mobilization of domestic resources, they are thus able to maintain and consolidate their authoritarian rule via militarism. Israel is the obvious exception to this, due to the fact that as a liberal democracy there is bi-directional influence between the people and the government. Additionally, the institutional structure of the state includes both controls and constraints on the military that prevent it from developing large amounts of political power.

Within the region, the military has also played an integral role in the process of nation building. The functioning of the military in this capacity has opened the door to some

unintended consequences. According to Heydemann, the manpower pressures created by mass armies have forced many states in the Middle East to include various social groups that had previously been excluded from the mainstream of the society. This inclusion, however, raises the possibility that these groups could (and have in the case of the 'Alawis in Syria) use their influence in the military to act against the state, thereby increasing the risks of regime instability (Heydemann, 2000: 19).

The Middle East also has a high propensity towards internally driven conflict due to the largely heterogeneous populations of the various states. According to Ibrahim (1998: 230), in Sudan, Lebanon, Iraq, Syria, Algeria, Morocco, Mauritania, Bahrain, and Yemen, "as many as 35 percent or more of the population differ from the Arab/Muslim/Sunni/Caucasian majority in one or more of the four ethnic variables (language, religion, sect, or ethnic group)." After independence, and through the present, the leaders of these states were faced with a multiplicity of challenges, stemming from how to deal with the external threat environment to how to forge a coherent state with a communal identity that would mitigate the possibility of internal conflict. Different states adopted different strategies in their attempt to effectively deal with the various challenges posed by internal groups.

Additionally, the states in the Middle East, in particular, as opposed to those that emerged in early Europe, have been described as rentier states since a large portion of government revenue comes from outside the state (Ross, 2001: 329). This revenue comes from a variety of sources, such as the sale of oil, workers' remittances, and foreign aid. Ross discusses a variety of implications of this reliance (and availability) of foreign funds in the region, some of which bear directly on the debate about the process of state building and resource extraction in the region. The rents collected by these states have allowed them to concentrate less on resource

extraction from the population (as long as the rents continue) (Ross, 2001: 332). These rents also provide the regimes with the resources necessary to prevent the formation or organization of rival social groups (Ross, 2001: 334). Finally, rents based on natural resources can facilitate an increase in military spending in response to either internal threats or in response to external threats. Accordingly, states in the region are likely to use foreign sources of income to extract fewer resources from the population, suppress internal opposition, and build up their military forces. According to Gause (1994: 123), the social contract of rentier states “rests upon provision of benefits *to* citizens, not extraction of resources (taxes and service) *from* them.” Consistent with Bates’s argument, those states with access to considerable foreign revenue—either from the sale of natural resources or through foreign aid—would be less likely to pursue Tilly’s state building activities.

The primary focus of this paper is therefore to analyze how the state building process (as measured by the ability to extract resources) was generally impacted by threats posed by external and internal rivals, in addition to economic factors and concerns specific to the Middle East and North Africa. I adopt what is usually referred to as a fiscal sociology approach to state building, which focuses on state revenues and expenditures (Campbell, 1993; Levi, 1988; North, 1981; Cheibub, 1998; Fauvelle-Aymar, 1999; Thies, 2005; Timmons, 2005). The revenue profile of a state can tell us a lot about its capacity, autonomy and legitimacy (Lieberman, 2002). The strength or capacity of a state is often gauged in terms of how much revenue it derives from direct income taxes versus other sources of revenue that require less extractive effort, such as international trade taxes, rents from natural resources and other forms of nontax revenue and foreign aid. Direct tax revenues that require extensive administrative structures are thought to provide a more solid platform for the state’s other activities than nontax revenues that are

channeled directly to the state. State autonomy from society is increased the greater the share of the country's wealth that it is able to extract and redistribute according to its own priorities. The state's legitimacy is also higher when it is able to extract revenues without a high degree of internal rebellion or noncompliance. A reliance on direct tax revenues is often seen as a marker of high legitimacy, since citizens are willing to turn over their wealth to the state. Conversely, reliance on indirect taxes or nontax revenues in large amounts is a sign of the failure to establish the state's legitimacy. The fiscal profile of the state therefore provides a broad picture of state building efforts that can be examined within specific countries over time and across countries and regions as well. We are therefore able to observe in a very tangible way the impact that both interstate and intrastate rivals have on state building efforts.

Research Design

The paper explores the effects of external and internal threats on state building by analyzing 21 states in the Middle East and North Africa from 1960-2000. I use two different measures of state fiscal capacity. First, I use the *tax ratio* measured as the state's tax revenue as a percentage of GDP, which is the conventional gauge of the state's extractive capacity (e.g., Campbell 1993; Cheibub 1998; Fauvelle-Aymar 1999; Thies 2005). The tax ratio is a measure of state strength reflecting the ability to extract resources from individuals and groups in society. It is the measure most closely associated with the predatory theory tradition that forms the basis for this empirical test. Second, I use *total revenue*, which is a measure of the government's income that includes both tax and non-tax revenue as a percentage of GDP. Since it includes non-tax revenue, the rentier state literature would expect total revenue to be less a measure of the strength of the state than the tax ratio. I also include lagged measures of both indicators to control for the stickiness of revenue collection, *tax ratio_{t-1}* and *total revenue_{t-1}*. The tax ratio and

total revenue variables are from an ongoing data collection effort by Johnson and Rabinowitz (2005).

The primary explanatory variables in this paper reflect measures of external and internal threat. In terms of external threats, I examine the effect of interstate war and interstate rivalries on state building efforts. *Interstate war* is operationalized as a dichotomous variable using the Correlates of War list of Interstate Wars. Thies (2005) allows interstate wars to have a 10 year impact window beyond their conclusion, which I adopt in this analysis as well to allow the shock of such an event to play out in society. War is expected to have a positive effect on the extraction of resources from society in the predatory approach, although many argue that it will not have state building effects in the modern developing world. I adopt Klein, Goertz and Diehl's (2006) updated measures of *enduring rivalry* and *proto rivalry* as measures of interstate rivalry. Enduring rivalries are long term militarized competitions between states, while proto rivalries tend not to have lasted as long or contained as many militarized disputes. Both measures of rivalry are coded "1" if a state is experiencing one or more rivalries in any given year, and "0" otherwise. I also draw upon both Thompson's (2001) operational measure of *strategic rivalry* for comparison. Given Thies's (2004; 2005; 2006; 2007) previous findings, I expect that rulers are able to use rivalries instrumentally to extract additional revenues from their population, reflecting Tilly's notion of a protection racket. Enduring and strategic rivalries should have a positive effect on revenue extraction, while proto rivalries may have a similar effect or non-significant effect since they do not reach the level of "threat" posed by their enduring counterparts.

In terms of internal threats, I draw upon the Correlates of War list of Intrastate Wars as a dichotomous indicator of *civil war*. Thies (2005) allows civil wars to have a 10 year impact

window, which I adopt here as well to allow the shock of such an event to play out in society. I also draw upon DeRouen and Bercovitch's (2008) definition of *enduring internal rivalry* to identify intrastate rivalries. They define an enduring internal rivalry as "internal conflicts between a government and an insurgency with at least 10 years of armed conflict in which there are at least 25 deaths—regardless of whether or not these years are consecutive" (p. 59). The effect that these indicators of internal rivals should have on the state's extractive capacity could be either positive or negative based on the literature reviewed in this paper. On the one hand, the state must raise sufficient revenue to effectively put down internal challenges to its rule, thus suggesting a positive effect on extractive capacity (e.g., Cohen, Brown, and Organski, 1981; David, 1991; Stubbs, 1999). The tax burden for dealing with internal challengers will thus fall heavily on groups that are relatively satisfied with the state's continued rule. However, rather than engage in repressive action, the state may bargain with internal rivals by reducing their tax burden in order to maintain its rule, or in some cases of extreme internal challenges (i.e., outright state failure), the state's ability to collect taxes may be significantly impaired in part or all of the territory formally included within its domain. Therefore, internal rivals may have a negative effect on extraction efforts (e.g., Jackson and Rosberg, 1982; Herbst, 1990; Desch, 1996).

The models are estimated using many of the standard control variables for predictions of revenue extraction (Cheibub 1998; Fauvelle-Aymar 1999; Thies 2004, 2005). Control variables are from the World Development Indicators (2001) or Penn World Tables (Heston et al., 2006), unless otherwise noted. I use the *polity* measure from Polity IV (Jagers and Gurr, 1995), which varies from -10 to +10, to capture the regime type of states in the region. Previous empirical findings on the effect of democracy on the tax ratio are mixed (Cheibub, 1998), and the MENA region dominated by authoritarian states are unlikely to help sort out these findings. *GDP per*

capita, *trade openness*, and *agriculture* as a percentage of GDP are all standard indicators of transaction costs. These three measures are thought to increase state revenues since they reduce transaction costs, while agriculture should reduce revenues since it increases transaction costs (Cheibub 1998). Official development assistance (*ODA*) per capita and public and publicly guaranteed *debt* as a percentage of GDP are included in the model as the literature suggests that these sources of international funds have prevented states from increasing domestic resource extraction (Bates 2001). Finally, I include a dichotomous measure of *oil* to account for the primary source of natural resource rents in the region. This measure is drawn from Fearon and Laitin (2003) and is coded “1” when a country obtains one-third or more of its export revenues from oil and “0” otherwise. The findings in this paper are not sensitive to the measurement of oil, as continuous measures of production (e.g., Humphreys, 2005) produce the same effects in the models. Oil should reduce tax revenues, while its rents should accrue to total revenue.

The choice of statistical method was driven by considerations about the nature of the data. Pooled cross-sectional time-series models often involve violations of the ordinary least squares (OLS) assumptions of homoscedasticity and uncorrelated error terms. While OLS estimates are unbiased in the presence of autocorrelation, these estimates are not efficient, and the variability of OLS coefficients affects the tests of statistical significance. I employ the Beck and Katz (1995) solution for these problems in OLS, “panel-corrected standard errors,” which is applicable to time-series dominated data (i.e., when the number of time points dominates the number of cross-sections). This procedure yields parameter estimates that are uncontaminated by the effects of autocorrelated and heteroscedastic errors.

The “de facto Beck-Katz standard,” while advantageous in many ways, has its own shortcomings when considering my specific modeling needs. The advantages of pooling include

overcoming the small-N problem to allow the estimation of more fully specified models, as well as being able to control for common exogenous shocks and unit-specific effects. Unfortunately, fixed-effects models that control for unit-specific effects eliminate time-invariant exogenous variables and bias the estimates of those variables that are almost time invariant. The almost-time-invariant and time-invariant variables central to the analysis in this paper—namely, the measures of external and internal threat—would be dropped from a standard fixed-effects model, and their estimates may be biased in the Beck-Katz approach as well, since the relationship between the unit effects and the time-invariant and time-varying variables is not properly specified.

Plümper and Troeger (2007) have developed a solution to both of these problems called Fixed Effects Vector Decomposition (FEVD) that allows for the appropriate estimation of time-invariant or rarely changing variables in a pooled cross-sectional time-series design. This technique proceeds in three steps. First, the technique estimates the unit fixed effect by running a fixed-effects estimate of the baseline model. Second, the technique decomposes the unit fixed effect into an unexplained part and a part explained by the almost-time-invariant or time-invariant exogenous variables by regressing the unit effects on the almost-time-invariant or time-invariant variables in the original model. Finally, the technique computes the correct standard errors for the coefficients of the almost-time-invariant or time-invariant variables, including adjusting for PCSEs.

Analysis

I first examine the effects of interstate and civil war on state fiscal capacity in Table 1. Model 1 demonstrates that interstate war has a positive effect on the tax ratio, increasing it by an average of 1.6 percent in years affected by the interstate war. Total revenue is increased by 2

percentage points in years affected by interstate war as shown in Model 2. War does have a slight stimulative effect on state building in the MENA, but certainly nothing on the much more dramatic order of what occurred in the European experience. Civil war, on the other hand, is not significantly related to the tax ratio, but reduces total revenue. Civil war is thus more likely to affect nontax sources of revenue, such as oil rents. Oil reduces the tax ratio and increases total revenue, much as expected. Increased levels of debt seem to have a positive effect on the tax ratio, but no effect on total revenue. ODA is insignificant in both models. In terms of the typical control variables, GDP per capita improves both tax and total revenue, while agriculture as a share of GDP reduces revenue. The lagged dependent variables both have strong, positive effects as would be expected. Their inclusion in the model improves our confidence that the statistical results are not being artificially inflated by considering each year's revenue generation as completely independent of the prior year.

[Table 1 about here]

I next examine the effect of enduring and proto rivalry as measures of external threat, alongside enduring internal rivalry as a measure of internal threat in Table 2. Enduring rivalries have positive effects on both the tax ratio (Model 3) and total revenue (Model 4) as expected. The effects are similarly sized to those found for interstate war. Proto rivalries significantly reduce total revenue, perhaps reflecting a drain on resources for short term conflictual relationships. Enduring internal rivalry, on the other hand, has no significant effect on either tax or total revenues. The rest of the findings are quite similar to those found in Table 1.

[Table 2 about here]

As a final comparison, I examine the effect of strategic rivalry on state fiscal capacity in Table 3. Strategic rivalry also exerts a positive effect on the tax ratio (Model 5) and total

revenue (Model 6). Enduring internal rivalry is not significantly related to either dependent variable. The remaining results are fairly consistent with the findings in the earlier tables.

[Table 3 about here]

Overall, the results seem consistent with my theoretical expectations. Predatory or bellicist theory generally expects that external threats should allow states to augment their fiscal capacity, which ultimately builds stronger states. War has traditionally performed that function in the international system. The paper theorized that anti-belligerency norms and norms against territorial revisionism may have served to disable that link between war and revenue extraction in the contemporary developing world. At least in the case of the MENA region, bellicism still holds some sway. Thies's (2004) more generalized version of this story, that interstate rivalries may be performing a similar state building function was supported by the data. Rulers may be able to run a Tilly-esque type of protection racket, even in a region where they are generally not dependent upon popular support. The effects of civil war and internal rivalries are not especially clear in this region, though Thies's (2004; 2005; 2006; 2007) findings in other parts of the world generally confirm a negative effect on fiscal capacity. Oil exports are clearly influential in the state's fiscal capacity in the MENA region, though not determinative. Most notably for predatory theory approaches, external threats still drive revenue extraction in the contemporary Middle East and North Africa.

Conclusion

This paper developed a predatory theory approach to state building in the developing world. While predatory or bellicist theory is typically framed in terms of the effects of war on revenue extraction, the paper built on previous work to suggest a more general understanding of this relationship. In the contemporary world, norms against territorial revisionism and

aggression largely rule out interstate war. Instead, interstate rivalries may be a substitute that serves to constrain the actual conflict between states, yet still allow the maintenance of a threat level that can be instrumentally used to increase revenue extraction. As Tilly originally suggested, states may be running a protection racket. Ironically, the protection racket may actually be much more visible in the contemporary era.

The MENA region is an interesting place to test ideas about the interplay between external and internal threats in producing the modern state. War has certainly figured prominently in the region's contemporary history. The empirical results demonstrated that wars have promoted increased tax revenue extraction and total revenue extraction. These results cast an interesting light on the rentier state hypothesis. The classic rentier state literature would probably not be terribly surprised that war might stimulate total revenue, since part of that revenue is from natural resource rents like oil. Yet, war also stimulates tax revenues in the MENA region. This is probably unexpected by rentier state theorists, and more in line with traditional predatory theory approaches. Future research should definitely look more closely at the sources of tax revenue to see how autocratic rulers are able to strengthen tax revenue generation from a public to whom they are unaccountable. Oil exports are important to the region, as they depress tax revenues and improve total revenues, but oil exports are clearly not determinative of state building in the region. External conflict, in the form of interstate wars and interstate rivalries, still strongly shape the state building efforts of MENA states. Both the traditional predatory theory approach and Thies's modified approach seem supported by the empirical analyses presented in this paper.

This paper is slated to be merged into a chapter on my book. The chapter will focus on the effects of external and internal conflict on the fiscal profile of the Middle Eastern state. In

addition to the statistical results presented in this paper, the book will also include a number of in-depth case studies that trace the effects of such conflicts on revenue and expenditure decisions. While the statistical results are suggestive, they require much stronger foundations in the actual decision making processes that connect threats to fiscal decisions. Through this combination of quantitative and qualitative analyses, I hope that we can arrive at a better understanding of state building in the Middle East and North Africa.

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Table 1: The Effect of Interstate and Civil War on State Fiscal Capacity

| Variable | <u>Model 1 (Tax Ratio)</u> | | <u>Model 2 (Total Revenue)</u> | |
|------------------------------|----------------------------|-------------|--------------------------------|------------|
| | Coefficient | Std. Error. | Coefficient | Std. Error |
| Interstate War | .016*** | .004 | .020*** | .005 |
| Civil War | .001 | .005 | -.033*** | .007 |
| GDP per capita | .000** | .000 | .000* | .000 |
| Trade openness | .000 | .000 | .000* | .000 |
| Agriculture | -.004 | .028 | -.148*** | .037 |
| Oil | -.009* | .004 | .022*** | .006 |
| ODA | .000 | .000 | .000 | .000 |
| Debt | .013* | .006 | .006 | .007 |
| Polity | .000 | .000 | .001 | .001 |
| Tax Ratio _{t-1} | .735*** | .027 | | |
| Total Revenue _{t-1} | | | .678*** | .027 |
| Constant | .029*** | .009 | .083*** | .012 |
| Adj. R ² | .87 | | .87 | |
| F | 329.97*** | | 437.76*** | |
| N | 551 | | 551 | |

Note: ***p<.001, **p<.01, *p<.05

Table 2: The Effect of Enduring Rivalries on State Fiscal Capacity

| Variable | <u>Model 3 (Tax Ratio)</u> | | <u>Model 4 (Total Revenue)</u> | |
|------------------------------|----------------------------|-------------|--------------------------------|------------|
| | Coefficient | Std. Error. | Coefficient | Std. Error |
| Enduring Rivalry | .014*** | .004 | .012** | .005 |
| Proto Rivalry | .002 | .003 | -.010* | .005 |
| Enduring Internal Rivalry | .009 | .005 | .000 | .006 |
| GDP per capita | .000 | .000 | .000 | .000 |
| Trade openness | .000 | .000 | .000* | .000 |
| Agriculture | -.003 | .028 | -.130*** | .037 |
| Oil | -.008* | .004 | .024*** | .006 |
| ODA | .000 | .000 | .000 | .000 |
| Debt | .012* | .006 | .009 | .007 |
| Polity | .000 | .000 | .001 | .001 |
| Tax Ratio _{t-1} | .741*** | .027 | | |
| Total Revenue _{t-1} | | | .690*** | .027 |
| Constant | .021* | .009 | .075*** | .013 |
| Adj. R ² | | .87 | | .87 |
| F | | 300.36*** | | 396.58*** |
| N | | 551 | | 551 |

Note: ***p<.001, **p<.01, *p<.05

Table 3: The Effect of Strategic Rivalry on State Fiscal Capacity

| Variable | <u>Model 5 (Tax Ratio)</u> | | <u>Model 6 (Total Revenue)</u> | |
|------------------------------|----------------------------|-------------|--------------------------------|------------|
| | Coefficient | Std. Error. | Coefficient | Std. Error |
| Strategic Rivalry | .027*** | .006 | .039*** | .007 |
| Enduring Internal Rivalry | .004 | .005 | -.010 | .007 |
| GDP per capita | .000*** | .000 | .000* | .000 |
| Trade openness | .000 | .000 | .000* | .000 |
| Agriculture | -.002 | .027 | -.119*** | .036 |
| Oil | -.010* | .005 | .015** | .006 |
| ODA | .000 | .000 | .000 | .000 |
| Debt | .013* | .006 | .007 | .007 |
| Polity | .000 | .000 | .000 | .001 |
| Tax Ratio _{t-1} | .741*** | .027 | | |
| Total Revenue _{t-1} | | | .683*** | .027 |
| Constant | .011 | .009 | .053*** | .012 |
| Adj. R ² | | .87 | | .87 |
| F | | 328.36*** | | 434.73** |
| N | | 551 | | 551 |

Note: ***p<.001, **p<.01, *p<.05