L. ALAN WINTERS

TRADE POLICIES FOR POVERTY ALLEVIATION

HOWEVER IT IS DEFINED, POVERTY IS NOT A DIRECT RESULT OF INTERNATIONAL trade. Rather, poverty reflects low earning power, few assets, poor access to communal resources, poor health and education, powerlessness, and vulnerability. It does not matter what causes these features so long as they exist, nor what relieves them if they can be relieved. Trade policy matters only to the extent that (a) it affects the direct determinants of poverty and (b) relative to the whole range of other possible policies, it offers an efficient policy lever for poverty alleviation (more poverty bang for a buck of forgone opportunities).

Trade liberalization may have adverse consequences for some—including some poor people—that should be avoided or ameliorated to the greatest extent possible. My fundamental belief, however, is that trade liberalization aids growth, which, in turn, aids poverty alleviation. I also believe that a widespread reform will contain enough positive elements so that, in general, only a few people will end up as net losers. Trade policy should therefore generally not be closely manipulated with an eye to its direct poverty consequences. It should, rather, be set on a sound basis overall, with recognition that some modification may be inevitable for political and other reasons. The primary way to deal with poverty is through general antipoverty policies.

Trade Reform and Poverty

International trade scholars have long understood that although for small countries, trade interventions are generally inefficient and wasteful, their inefficiency is usually dominated quantitatively by their redistributive effects. That is, the net losses from intervention will generally represent large positive effects for some people and households and large negative effects for others. Correspondingly, although removing interventions will generally be income enhancing overall, it is likely to generate both winners and losers.[1] For example, liberalizing an import sector typically redistributes real income from producers to consumers as prices fall, and between different factors of production in such a way that some gain while others lose more than average.

The important positive issues are empirical: does trade liberalization generally create poverty, and under what circumstances might it do so in specific cases? In Winters (2000a), I develop a detailed taxonomy linking trade shocks to household and individual poverty and extract 11 key questions that help to answer the latter question (see Box 5.1). Finding an instance in which a trade reform causes poverty may not constitute a refutation of an intellectually interesting hypothesis, but it does pose a

Will the effects of changed border prices be passed through to the rest of the economy? Trade policy and shocks operate primarily through prices. If price changes are not transmitted—for example, because governments continue to fix the internal prices of goods that they have ostensibly liberalized internationally—the most direct effects on poverty, whether positive or negative, will be nullified.

Is reform likely to give poor consumers access to new goods? Perhaps the most direct effect of trade reform on poverty is through the prices of goods and services in which poor households have large net positions. The biggest price shocks occur when either the initial or final price is finite and the other is infinite (that is, when there is no market). A shock that completely undermines an important market—say, for a cash crop or a form of labor—is likely to have major implications for poverty. Similarly, making new opportunities, goods, or services available to the poor can greatly enhance welfare.

Is reform likely to affect different household members differently? Within a household, claims on particular goods and endowments of particular assets (labor) are typically unevenly distributed. It is possible that poverty impacts will be concentrated on particular members—usually females and children, who may lose personally even when the household gains in aggregate.

Will spillovers be concentrated on areas and activities that are relevant to the poor? The sectors of an economy are interlinked, and, if substitutability is high, a shock will be readily transmitted from one sector to another. Frequently the diffusion will be so broad that it has little effect on any particular locality or sector, but sometimes—for example, where trade in services is very local—the transmission is narrow but deep. Then it is necessary to ask whether the second-round effects have serious poverty implications. Agricultural stimuli can confer strong propoor benefits on local economies via benign spillovers.

What factors are used intensively in the most affected sectors? Changes in the prices of goods affect wages according to factor intensities. Predicting either the price effects or the factor intensities of affected sectors can be complex, as was seen with the Latin American reforms of the 1980s and 1990s. In addition, if factor supplies show some elasticity, part of a trade shock will show up as changes in employment rather than in factor prices. At the limit, a factor with a perfectly elastic supply will experience only employment effects. This is most pertinent for labor markets. If the prevailing wage is determined by subsistence levels, switching people from one activity to another has no perceptible effect on poverty. If, however, the trade-affected sector pays higher wages (because, say, it has an institutionally enforced minimum wage), increases in activity will tend to reduce poverty, and declines will tend to increase it. The formal-informal divide is important in this respect. In all this, it is important to remember the difference between the functional and the personal distribution of income. Falling wages for unskilled labor generate poverty only to the extent that the poor depend disproportionately on such wages.

Will the reform actually affect government revenue strongly? One's immediate reaction is that cutting tariffs will reduce government revenue. Although at the limit this is clearly true (zero tariffs yield zero revenue), many trade reforms actually have small or even positive revenue effects, especially if they convert nontariff barriers into tariffs, remove exemptions, and get tariff rates down to levels that significantly reduce smuggling. Even where revenue falls, it is not inevitable that expenditure on the poor will decline. That, ultimately, is a policy decision.

Will reform lead to discontinuous switches in activities? If so, will the new activities be riskier than the old ones? If a trade liberalization allows people to combine "national" and "international" activities, it is most likely to reduce risk: foreign markets are likely to be less variable than domestic ones, and even if they are not, risk spreading is likely to decrease overall risk. If, however, trade reform leads to more or less complete changes in activities, there is a possibility that risk will increase, if the new activity is riskier than the old one.

(continued)

Does the reform depend on or affect the ability of poor people to take risks? The very poor cannot bear risk easily. Because the consequences of even small negative shocks are so serious for the poor, they may be unwilling to take opportunities that increase their average income if the chance of losses also increases. This might leave them with only the negative elements of a reform package. Similarly, if a reform makes it more difficult for the poor to continue their traditional risk-coping strategies, it may increase their vulnerability to poverty even if it raises mean incomes.

If the reform is broad and systemic, will any growth it stimulates be particularly unequalizing? Economic growth is the key to sustained poverty reduction. Only if it is very unequalizing will it increase absolute poverty.

Will the reform imply major shocks for particular localities? Large shocks can create qualitatively different responses from smaller ones; for example, markets can seize up or disappear altogether. Thus, if a reform implies very large shocks for particular localities, mitigation through phasing, or, better, through compensatory and complementary policies, could be called for. There is a trade-off, however, because, typically, larger shocks will reflect bigger shortfalls between current and potential performance and hence larger long-run gains from reform.

Will transitional unemployment be concentrated on the poor? The nonpoor typically have assets that carry them through periods of adjustment. The situation might be unfortunate for them, but it is not poverty strictly defined. The poor have few assets, so even relatively short periods of transition could induce a descent deep into poverty. If the transition impinges on the poor, there is a strong case for using some of the long-run benefits of reform to ease their adjustment strains.

Source: Winters (2000a).

real policy question: should we automatically condemn a trade reform because it means that one poor person loses or one person is pushed into poverty? I believe very strongly that we should not. Rather, the identification of hardship arising from a generally desirable policy reform should stimulate the search for complementary policies to minimize the adverse consequences and reduce the hurt that they cause. Rejecting any reform that adversely affects any poor person is a recipe for long-run stagnation and for an ultimate increase in poverty. Even the requirement that no household fall temporarily into poverty is likely to be extremely restrictive in poor countries. The more utilitarian view that the number of households (or persons) in poverty should not increase is more appropriate, although even then, consideration of the depth of poverty is required.

All judgments ultimately must be quantitative, not just qualitative. In practical circumstances, it is easier to identify losers from trade policy than potential gainers. Losers are identifiable, concrete, and personified (see Krueger 1990), whereas the gains are diffuse and appear merely prospective and theoretical. For this and other reasons, losers will usually be better able to articulate their interests than gainers, and so the volume of opinion is not a sufficient indicator of the relative strengths of the pluses and minuses of a policy change. This is particularly true given that the poor are generally much less able to advertise and defend their interests than are wealthier groups.

In what follows, I explore three responses to the possibility that trade reform can create poverty: manipulating trade policy itself, compensating the losers or the poor, and pursuing complementary policies to try to ensure that as few people as possible are net losers.

Can Trade Policy Be Managed to Alleviate Poverty?

One natural response to the possibility that trade liberalization could exacerbate poverty in certain sections of a society is to "manage" liberalization in a way that eliminates or at least reduces the problems. At the conceptual level, this is just common sense: poverty alleviation is arguably our highest priority, whereas trade policy is just a means to an end. It makes sense to marshal all the tools we have toward achieving our principal goals, and indeed, it would be perverse to do anything different.

But on a practical level, the question is *how* to use trade policy to achieve poverty objectives. First, there is the possibility that we do actually have goals other than poverty alleviation—for example, as regards average incomes, security, foreign policy, or environmental sustainability—and these would need to be factored in. Second, even leaving aside additional objectives, we need to decide which measure of poverty we are aiming at: there are choices even among income- or consumption-based measures, let alone among the various concepts and dimensions that characterize modern views of poverty. Third, there may be questions about trading poverty in one region against that in another, and there will certainly be, fourth, tradeoffs between poverty today and poverty tomorrow. Fifth, what else figures in the policy packages among which we are deciding? Are other policy instruments frozen at current levels, so that the question is only one of how trade reform impinges directly on the real incomes of the poor? Or can we presume that other policies will be optimized, so that, say, boosting incomes in the top decile at the expense of higher prices for the poor is acceptable because it will permit a redistribution via the tax-benefit system that more than offsets the initial growth in the income gap? These questions illustrate that saying "manage trade policy" is not helpful until one specifies *how* to manage it.

Don't Do It

One response to the fear that a trade liberalization will cause poverty is, "don't do it." But even if the direct effect of a reform might be to worsen poverty overall, this is not generally a satisfactory response. Although it has proved difficult to isolate the effects of trade liberalization on economic growth empirically, the predominant view is that it has an important role. The well-publicized cross-country studies that supported this view in the 1990s (for example, Dollar 1992; Sachs and Warner 1995; Edwards 1998) have recently received rough treatment from Rodriguez and Rodrik (2001). The latter argue, with some justification, that these studies' measures of openness are flawed—in particular, because they either are endogenous (at least as much due to growth as a cause of growth) or include much more than just trade policy—and that their econometrics are weak. But Rodriguez and Rodrik do not argue that trade liberalization is harmful to growth, nor do they deal with other evidence for a beneficial relationship, such as the manifest failure of closed economies and the findings of a number of case studies (see, for example, Srinivasan and Bhagwati 1999). Thus while Rodriguez and Rodrik should certainly inspire greater modesty in policy advice and renewed research efforts, they have not (yet) reversed the presumption that openness is likely to boost long-run growth.

The difficulty of establishing an empirical link between liberal trade and growth arises at least partly from two difficulties, both of which should inform our policy attitude. The first is the difficulty of measuring trade stances once one comes inside the boundary of near autarchy: tariffs need to be aggregated, quantitative restrictions assessed and then aggregated, and the degrees of credibility, vulnerability to lobbying, and enforcement measured (see Winters 2000b). This suggests that while one should staunchly recommend openness, one needs to be cautious about declaring particular regimes open or not. Which was the more open in 1997, Brazil, or Chile? Both had average most-favored-nation (MFN) tariffs of around 11–12 percent, but in Chile there appeared to be little discretion and little sensitivity to industrial lobbying, whereas in Brazil political pressures could be observed almost every day.

The second difficulty is that, although liberal trade policies are likely to be beneficial under any circumstances (because they enlarge the set of opportunities), a quasi-permanent effect on growth almost certainly requires combination with other good policies as well. The latter point is made repeatedly by the IMF and the World Bank in their policy advice.[2] Krueger (1990) has argued that openness is likely to be correlated with better policy in a number of dimensions, and supporting evidence for this assertion might be detected in Ades and Di Tella (1997, 1999), on corruption, and in Romer (1993), on inflation. Thus, openness brings advantages not only on its own but also as part of a constellation of policies designed to ensure efficiency and competition in markets, and transparency and predictability in policymaking.

The second part of the openness-poverty link concerns the connection from growth to poverty.

Growth needs to be strongly biased against the poor before it is likely to worsen poverty absolutely. (The effect on inequality is a different story but, in my view, a distracting one.) There are examples of such a negative relationship (see, for example, White and Anderson 2000), but they are equally balanced by cases in which growth disproportionately favors the poor. Thus, Dollar and Kraay's (2001) finding that, on average, growth *is* good for the poor does seem to be robust (as it was in the earlier work of Gallup, Radelet, and Warner 1998), and so does their conclusion that growth driven by trade liberalization is no different in that respect. A challenge to the latter view can be found in the early work of Lundberg and Squire (2000), but on further investigation they too concluded that trade liberalization benefited the poor, albeit by less than it helped better-off households.

To conclude, I would argue that although there remain a number of pressing research questions in the area, a liberal trade regime almost certainly assists poverty alleviation in the long run. Thus, liberalization should have a place in the armory of a poverty-conscious government. This does not imply a call for the immediate dismantling of all trade restrictions, and it certainly does not imply that opening the border is all that is needed, but it does, I believe, mandate a serious and credible commitment to openness in the foreseeable future.

Don't Do It All

A second response is, "don't do it all: while everyone is in favor of liberalization in general, certain sectors or products should be exempt." In fact, all countries have such exceptions (agriculture in Europe and clothing in the United States, for example), but that does not necessarily make them good economics. Considering overall economic performance, there undoubtedly are cases in which an isolated intervention in trade would be beneficial to immediate economic welfare—where externalities, information failures, or just random shocks can be usefully overcome by a well-judged intervention. But given the difficulty of identifying these cases, of preventing their capture by interest groups, and of avoiding giving a systemic signal that lobbying for intervention pays, it is not clear that it will be beneficial overall to pursue them. Thus, although one does not need to progress all the way to free trade to reap the benefits of liberalism, the general case for planning a series of exceptions is not strong. One needs very compelling evidence of the efficacy of such interventions, and such evidence is, on the whole, missing. Simply appealing to the experience of East Asia is not persuasive; it is not beyond dispute that these countries' trade interventions were important or beneficial (Lee 1996 suggests the opposite for Korea), and it is far from certain that other countries have the policymaking institutions to be able to replicate East Asian policy stances effectively.

In addition to efficiency considerations, we must recognize that trade liberalization is a political act and that governments must generate sufficient political support to sustain the reform. Even the most rigorous reforms need tempering for political reasons; see, for example, Edwards and Lederman (1998) on Chile, where certain agricultural goods were granted special protection in the form of price bands. Recognizing the need for such compromise is not the same as recommending it, however, and it is important to remember that the poor are even weaker in political markets than in economic ones. Rarely will protecting the poor and reaping significant political support for a reform coincide. Governments are well advised to do everything possible to avoid using the instruments of trade policy for political purposes. One of the most powerful tools for avoiding political pressures is uniformity—explicitly treating all commodities equally. Such a motivation was clearly articulated in Chile as it entered its big reform in the mid-1970s (Edwards and Lederman 1998).

There may be a stronger case for exceptions to liberalization for the sake of direct poverty alleviation: the outcome is objectively measurable and can arguably be isolated politically from general intervention. Thus, if particular products can be clearly identified with the poor as either consumption or production goods, it may be justified to postpone their liberalization significantly. There are, however, some important caveats to such a recommendation. First, the calculation needs to be rigorous in defining "the poor" whose interests are being protected. (Ravallion and van de Walle 1991 show how in Indonesia the poor and the very poor had conflicting interests in rice liberalization.) Second, the products do need to be tightly linked to the poor in order that the distributional gains of protecting them are not offset by efficiency losses elsewhere in the economy. The goods concerned need to be of great significance to the poor—almost always, a foodstuff on the consumption side, and frequently an agricultural good on the production side—and of little interest to other sections of society. On the latter dimension, for example, it was reported in the 1970s that in addition to any effects on the poor that Egypt's bread subsidies may have had, they also made it worthwhile for pig farmers to feed their stock on fresh bread.

Third, close monitoring is required to ensure that the desired effects do actually emerge. An important goal to keep in mind is that the poor continue to have access to the effects of the policy and do not get hustled out of the way by more articulate and powerful middle-class interests. In general, the poor fare very badly in discretionary allocation mechanisms precisely because they are marginalized politically and socially, as well as economically. Thus, for example, export restrictions to keep down the price of a local staple will probably not benefit the poor if low prices mean that nonprice rationing is required.

Fourth, a long-term plan is needed to help reduce the dependence of the poor on the policy intervention. Otherwise, the intervention just amounts to stopping the clock, which offers little prospect of long-run development.

Overall, "don't do it all" is not a suitable policy recommendation. The politics, especially protecting the interests of the poor, will be easier if the government can explicitly reject special pleading on the grounds that everyone is receiving equal treatment. De facto, there may be—there may have to be—some slippage in such an attempt, but it seems to me undesirable to go into the process expecting or recommending slippage. The only exception I would make would be for temporary exemptions for goods or services that can be clearly and closely linked to the poor. A high burden of proof should be placed on candidates for such exemptions to prove their efficacy.

Don't Do It Now

"Don't do it now" is a more useful response than the others in some circumstances. For example, trade reform in the midst of recession seems likely to give rise to more, and more durable, transitional unemployment than reform in a boom. Again, where investment is necessary to allow the production of export-quality goods, it may be desirable to allow time for that to occur. There is, however, a world of difference between committing to policies with long adjustment periods and postponing liberalization because "the time is not ripe." The key is credibility that reform will actually occur. Adjustment costs may be lower if adjustment can be spread somewhat through time, but they are probably increased if adjustment is resisted in the hope that the threat of liberalization will go away. Several trade reforms have been accelerated once they have been launched; examples include implementation of free trade in the European Economic Community, of the Kennedy Round tariff cuts, and of the tariff cuts planned in the Association of Southeast Asian Nations (ASEAN) Free Trade Agreement. Usually the acceleration happens at the behest of the private sector, presumably because, once it is accepted that reform will occur, business is keen to adjust rapidly.

Thus, undertaking a major trade liberalization in phases is probably desirable, just as the Uruguay Round, for example, permitted long adjustment periods. The phasing should, however, not merely entail postponing the largest adjustments longest; it should pay attention to the different adjustment needs of different sectors and to the interactions between different parts of the package. For example, if the inputs and outputs of a particular sector are liberalized at very different rates, the sector could face either negative or excessively positive incentives for production during the transition.[3] Whatever the transition period, credible commitment to the final goal is important, for without it, neither current nor potential future activities will look desirable, and there will be a diversion of effort into lobbying.

Compensatory Policies for Developing Countries

If trade liberalization causes poverty among certain sections of society, the next question is whether society can offset the effect directly. Despite the theoretical attractions of lump-sum budgetary transfers for economists, governments are not generally attracted to them because of their cost, their transparency (and the transparency of their abuse), and the appearance that they do little to cure "the problems" that individuals face. Rather, assistance is usually offered, if at all, in terms such as retraining, relocation assistance, and temporary income support. In fact, while these approaches probably do have a contribution to make, even they face severe difficulties.

Official retraining has mixed success under any circumstances, and, what is worse, it is difficult to separate those cases where trade is to blame from those where it is not. Unless one is willing to underwrite almost any adjustment, identification of cases is a major difficulty. Making a general commitment, however, is not attractive because of the potentially huge cost and because doing so shifts private risk to the public sector, with all the attendant moral hazard problems. It is not the role of the state, nor is it feasible, to absorb every negative shock that might afflict individuals. Yet it is difficult to make a moral case as to why trade shocks warrant adjustment assistance while other shocks do not.[4]

A further complication arises in giving compensation in a way that encourages rather than discourages adjustment. European agricultural policy is essentially designed to protect farmers from the consequences of declining comparative advantage, yet it has the effect of rewarding current, not former, farmers. Compensation may be decoupled from current output but not from farming as an activity.

In cases where liberalization leads to the loss of jobs, government can insist on, and perhaps help finance, redundancy payments. These payments can help some people avoid poverty, if they use their money productively, but they are not guaranteed to do so. (See Winters 2000a on the "new poor" in Zimbabwe.)[5] Moreover, redundancy payments typically reward past service, not current need, and so they are not particularly well targeted for poverty alleviation purposes.

General compensatory policies, including safety nets, are designed to alleviate poverty from any source directly. They replace the problem of identifying the shock with the task of identifying the poor. Ideally, countries should already have such programs in place. Indeed, a major part of the effect of these programs arises from their mere existence rather than their use: they facilitate adjustment by assuring the poor that there is a minimum (albeit a barely acceptable one) below which they will not be allowed to fall. Such schemes, if trade-adjusting countries do already have them, offer the advantages over tailor-made schemes of automaticity, immediacy, and a degree of "road-testing," and they also avoid the problems associated with targeted trade adjustment assistance. If they are sensibly constructed, they need not entail huge expenditure; there is little chance of moral hazard problems if the thresholds are set low enough; and, since relieving poverty is more or less universally recognized as a responsibility of the state, there is little argument about the legitimacy of such interventions.

Targeting is a major problem for safety nets, not only technically but also because the middle classes are often better able to access them than the poor. Sustainability is another difficulty; a major trade shock could put severe financial pressure on a scheme just at a time when it is most needed. Ravallion (1999) offers some useful thoughts on setting up safety nets. Workfare is a good start, provided that the wage is low enough, that there is little or no administrative discretion in its application, and that the tasks set are seen to be of communal interest. In fact, Ravallion suggests that local communities select the projects to be undertaken under workfare and that better-off communities should be asked to cofinance the projects. Workfare has to be supplemented, however, by schemes to provide food to people such as the elderly and infirm who cannot work and to children (through, for example, food-for-education schemes). These supplementary schemes may be tripped on and off according to need, but they should have a permanent infrastructure and sensitive and quick triggers. Expenditure on safety nets is almost by definition countercyclical, and so a firm commitment by government is required to ensure that the money does not dry up in times of greatest need.

Examples of useful safety nets can be found in Bangladesh. According to the Consumer Unity & Trust Society,

> It is generally recognized that programs such as Food for Education (FFE), Vulnerable Group Development (VGD), Test-Relief, and Food for Work positively induce alleviation of poverty. For example, during the unprecedented floods of 1998, about 4.5 million VGD cards were distributed in Bangladesh, which provided crucial help at a critical time. The FFE program has helped increase school attendance of poor children by 21%. (CUTS 1999: 110)

The safety nets in Zambia and Zimbabwe, by contrast, are currently regarded as too poorly run and underfunded to be able to offer serious assistance to losers from trade liberalization.

Safety nets are not the only answer to the threat of increasing poverty from trade liberalization, but they are an important part of the response. They can generally be targeted better than other policies, and they are not very distortionary of market forces. If countries do not have safety nets already, they should consider setting them up as part of the context for a trade liberalization that may create short-term poverty. The safety nets should not, however, be trade shock–specific.

Complementary Policies for Better-Functioning Markets

A critical issue concerning the poverty impacts of trade liberalization, especially for surprises connected with it, is the functioning of markets. Trade liberalization must be accompanied by monitoring to determine whether any markets are failing. Policies designed to ensure that markets continue to function or to develop, where required, will have high payoffs for both aggregate income and poverty alleviation. Some important circumstances are discussed next.

Infrastructure Support

Potential opportunities for poor producers to benefit from a more open trading regime have been lost because critical infrastructure was either absent or had deteriorated. In both Zimbabwe and Zambia remote farmers found their opportunities constrained by inability to reach major market centers. In the same way, many of the benefits from relaxed retailing regulations and from availability of new or cheaper goods have been confined to urban and periurban areas.

Market Institutions

The poor frequently seem unable to attain the economic mass required for the establishment of markets that, once in place, may be viable. Policy should aim at the creation of the market as an institution, not at the ongoing subsidization of market activity. One aspect of facilitating the participation of the poor in markets may be to find means to allow them to combine very small consignments of inputs or outputs into reasonably sized bundles and so reduce transactions cost sufficiently to make dealing with poor producers worthwhile. Horticulture in Zimbabwe offers an illustration of a successful policy of this kind (Winters 2000a). Although horticulture is relatively underdeveloped in most of the smallholder areas, increasing numbers of resettled and communal households are now becoming involved as producers of the main crops. This has primarily been the result of "outgrower" schemes and of sourcing or subcontracting by large-scale commercial farms. The Horticultural Promotion Council (HPC) estimates that around 3,000 small-scale farmers are now growing for export on a contract basis, accounting for approximately 10 percent of Zimbabwe's exports.[6] In January 1999 the HPC established the Small-Scale Linkage Programme, designed to provide communal and resettled farmers with the knowledge and skills to produce high-value, off-season export crops.

Credit Markets

Development economics affords many examples of how missing credit markets have prevented development, and the same phenomenon is visible in responses to trade liberalization. Thus, for example, achieving minimum consignment size might entail hiring draft power or seasonal labor, but this is not possible without credit. Similarly, establishing informal businesses in areas such as trading may require more capital than the poor can raise. These cases in which the poor are not able to respond to incentives as strongly as the less poor replicate the results of López, Nash, and Stanton (1995) in their panel study of Mexican agriculture.

Labor Mobility

The secret of spreading the benefits of increasing labor demand widely is labor mobility. If markets are segmented for cultural or geographic reasons, breaking down these barriers through information and facilitating physical mobility will have an equalizing effect.

Establishing Businesses

If the regulations for establishing new businesses are cumbersome, if the businesses' ability to obtain inputs (especially utilities) is weak, or if regulations on expansion and on labor recruitment and separation are restrictive, this could curtail the willingness of entrepreneurs to start or expand operations. A success story of business deregulation is the growth of maize hammer milling in Zimbabwe. Following domestic deregulation, 3,500 new hammer mills opened, mainly in rural areas, and the share of hammer millers in total maize milling has increased to almost 80 percent.[7] These mills are mechanically simple and robust (being based on swinging or rotating hammers in a grinding chamber) and can be used by unskilled labor. They provide quality maize meal products to nearby customers in poor communities, saving them significant transport costs. In 1995 hammer mills were estimated to employ 7,512 permanent workers (751 in urban areas); when casual workers and rural activities are included, the sector employs some 13,000 workers. About 18 percent of the employees in urban hammer mills are female, as are 8 percent of the employees in rural areas.[8]

Prerequisites or Concomitants?

In many cases actual policy debate appears to hinge on whether complementary policies of the sort just described should be prerequisites for a trade liberalization. "Everyone accepts that trade liberalization is desirable in the long run," the argument goes, "but various supporting policies must be in place before it is attempted." Here, even more than in the matters discussed above, we have no formal analysis to fall back on. There is a literature on sequencing reform within the trade sector and between trade and capital accounts, but there are no convincing empirical generalizations about sequencing in the sense discussed here. Moreover, the question is only partly economic; part of it is political and concerns whether a reform postponed is a reform preempted.

I argued above that there may well be a case for phasing in a reform over a long period provided that the final destination is clear (and not likely to be contested) and that the transition is well designed and does not amount just to postponing all effective change until the last moment. Given that a well-conceived and well-executed reform generates a potentially infinite-lived stream of benefits, whether this occurs over three years or, say, nine years is not that important. The same logic applies to delays required to put complementary policies in place (or, indeed, to compensatory mechanisms if that is the route chosen). Thus, for example, there may be a case for delaying the *implementation* of a liberalization while legislation on business formation or labor market operation is put in place and plans for protecting market institutions are laid.

This is not, however, a license to postpone the design, announcement, and locking in of the reform itself. Any of these delays—for example, announcing that liberalization is necessary but that its form will be worked out once certain other reforms have been implemented—would seem likely to result in the worst of all worlds. It would create uncertainty and incentives to lobby government and, indeed, would look to many commentators like a de facto reluctance to liberalize trade. In particular, in the absence of a clear and monitorable plan for specific pieces of infrastructure, a general wish to wait until the roads or ports are "ready" is just a recipe for indefinite postponement. A credible plan for liberalizing the borders—albeit one with significant transition periods—will be an important stimulus to reforming these other areas in ways that will typically have other benefits as well.

It is also well to record that there are disadvantages as well as advantages to phased adjustment. Populations can certainly suffer from reform fatigue and would actually be more comfortable with a definite, even if ambitious, reform plan than with one that drifts into the indefinite future. Phased adjustment implies a longer time spent out of equilibrium, and in most discussions it is not proved that the integral of shallow adjustment costs over a long period is smaller than that of deep costs over a shorter period.[9] Moreover, delay postpones the benefits of full reform. Finally there are likely to be aggregate gains from trade reform even in the absence of complementary policies. A trade reform increases opportunities for desirable exchange, and these will exist even with poor infrastructure, and even though there would have been more opportunities had the infrastructure been better. And this applies to the poor as much as to other people. It is possible that in the absence of complementary policies, the poor will suffer (say, because of rising prices) whereas with such policies they will gain because they will receive income gains to offset the price rises. But there is no general theorem to this effect; the case remains to be made.

Conclusion

Trade reform almost invariably brings with it two changes that help in the battle against poverty: it induces efficiency in the use and allocation of resources (the economist's beloved static gains), and it fosters long-run growth. It also entails temporary adjustment costs that reduce incomes immediately, although these costs are almost always outweighed by the long-term benefits. Finally it has a host of direct and indirect effects on poverty that could go either way, depending on consumption and production patterns and on the nature of reform.

The general presumption is that reform will help alleviate poverty, but the direct and indirect effects just mentioned make it likely that some will lose from liberalization—especially one that is narrowly focused sectorally—and it is certainly possible that some of the poor will suffer. Still, others will gain, and these will quite possibly include others among the poor. Thus, tradeoffs are necessary. There is no alternative to case-by-case analysis if policymakers wish to predict and preempt adverse effects, even though prediction is very difficult. One must be alive to the possibility that "predict and preempt" policies will be captured by powerful interest groups. Given these groups' strong interests in trade policy and the apparent ease with which trade policy can be captured (because its domestic costs are usually hidden and the issues can be so easily presented in terms of standing up to foreigners), there are grave dangers in setting out to manipulate trade policy directly to avoid adverse poverty impacts. Only in the most obvious cases are the dangers likely to be worth incurring.

My general prescription, then, is for a rigorously liberal trade policy (even though it is recognized that some slippage may occur for political reasons). General compensatory policies should then be used to cure immediate hardship, and complementary policies should be pursued to enlarge long-term gains. Assessing likely impacts in the design of policy reforms is of great importance. The set of questions posed in Box 5.1 can help policymakers in the design and implementation of reforms.

Notes

Preparation of this chapter was supported by Globkom, the Parliamentary Commission on Swedish Policy for Global Development, to which I am most grateful. I also thank Costas Michalopoulos for comments on the outline and Rosie Bellinger for logistic help.

1 I say "generally" because second-best considerations or market failures could reverse the result.

2 Mosley (2000) argues that the attempts of the IMF and the World Bank to prove this proposition have not been very successful. (His attempts to prove the contrary are similarly flawed, however.)

3 Technically, the effective rate of protection (ERP) could become very distorted. In Zambia, Oxfam and the Institute for Development Studies (IDS) found decreases in the ERP for maize, as fertilizer prices (which were said to account for 76 percent of the cost of production) increased by more than output prices. This accounts for the loss of output there.

4 See Decker and Corson (1995) on the U.S. Trade Adjustment Assistance Program, which doubles the length of unemployment insurance coverage, from 26 to 52 weeks, for workers certified as displaced by trade liberalization. After serious abuse in its early years, when it was merely a transfer (over 70 percent of claimants went back to work for the employer from whom they were said to have been displaced), a training element was added. This had the effect of screening out claimants who did not want or need training, but it apparently did nothing to increase the earning power of recipients.

5 The "new poor" are retired public sector officials who have not managed to invest their redundancy payments sufficiently productively to maintain themselves above poverty levels.

6 These small-scale "outgrowers" tend to supply the four main packinghouses in Zimbabwe, which are the large-scale producers that seek to add volume and diversify risk.

7 The 1995–96 Zimbabwe National Hammer Miller Status Study, funded by the U.S. Agency for International Development.

8 Ibid.

9 This is not to deny the possibility—as, for example, if a major shock creates hysteresis in labor markets—but it needs to be proved.