Three decades of trade liberalization, any lessons for the world?

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Traditional theory purports that trade liberalization, regional or bilateral, extends global production frontiers outward, thereby opening the gates of opportunity to both developing and developed nations. Nevertheless, liberalization has not been reciprocal and the expected benefits unforthcoming. Under the circumstances, the question remains, what has been achieved and is a better deal possible in the future?

Trade theory

Complete trade liberalization could raise worldwide economic growth by $287 billion per year by 2015 according to a recent Word Bank study that was presented at the Global Issues Seminar, April 2006. It states that two thirds of this expansion would go to the industrialized countries. Despite being lower than earlier calculations, the role of trade in spurring the global economy cannot be underestimated according to the report.

A broad consensus purports that Trade liberalization invariably leads to the creating of new markets in the domestic economy with employment generation and consequent reductions in poverty whilst concurrently diminishing other markets and having the reverse impact on poverty. Sri Lanka is a case in point. The net impact may be positive or negative at the macro level depending on how the process is managed, but the transformation is invariably painful at the micro-level, to those that bear the brunt of change.

Other factors such as labor absorption are also significant. For instance, where the market that thrives from trade liberalization is labor intensive, we can conclude that the impact on poverty alleviation will be positive. Evidence also suggests that export led strategies have tended to favor the industrial sector rather than the agricultural sector. Moreover, small scale agricultural producers were found to be worse off following Sri Lanka's trade liberalization initiatives in 1977 according to a study done by the Institute for Policy Studies (IPS) for a project initiated by CUTS-CITEE on the linkages between trade, development and poverty reduction for which IPS and Law & Society Trust (LST) are research and advocacy partners from Sri Lanka respectively.

However, with the global economy expanding at between two and three per cent and Asia in particular experience double digit growth rates, liberalization connects the domestic economy to the wider world. On the down-side, it exposes the domestic sectors to greater risks and external shocks. For example, the July 2006 war in Lebanon resulted in the return of thousands of Sri Lankan housemaids who had been affected by the conflict.

Liberalization has also tended to raise the overall standards of organizations, human resources and produce. For instance, Sri Lanka's tea sector, for long at the frontline of the exports is now having to obtain health, safety and quality certifications like the H.A.C.C.P (*Hazard Analysis and Critical Control Points)* in order to stay in the European market. Certification calls for higher standards of hygiene, better machinery and technical expertise and serves to improve working conditions.

Reality gap

However, in reality, the rhetorical position of trade theory has not materialized in a global context at the WTO level. Fading support for the WTO, even amongst INGO's like Oxfam who recently withdrew its support for the talks, is an indication that the WTO critics are winning the debate. The ostensible consensus has been that no deal is preferable to a 'bum deal'. Moreover, accusations of sidelining the all-important issues of poverty and farmer livelihood concerns in the developing world due to brinkmanship between the EU and the USA have been voiced by critics in the UK and elsewhere.

One of the main factors that can be attributed to the unsatisfactory performance of the least developed countries (LDC's) since the Uruguay round (1986-93) is the gap in information and knowledge that is required to capitalize on possible synergies. Here, the figures speak for themselves. According to trade data, the share of developing country manufactured goods in the total imports of developed countries has fallen from 23.2 per cent in 1990 to 9.9 percent in 2004. So why then are developing nations striving to partake in an exercise that has proved thus far to be fruitless?

According to some analysts, current 'aid for trade' packages that are given to the LDC's are valued in the range of four billion US$ and are aimed at meeting the cost of regulatory and intuitional adjustment. However, it is said that the mechanisms in which these funds are distributed tend to promote corruption amongst the ruling elites and officials. Thus, far from serving to alleviate poverty, the net impact will tend to further limit agricultural livelihood opportunities. However, as the 'aid for trade' debate is one that it infinitely complex and deserving of exclusive discussion which will hopefully be covered in a forthcoming research article in under this theme.

Politics, raison d'être

Trade has additional benefits that can serve towards reducing conflict. According to academic studies, it has been shown that gradual increases in trade between nations reduces the risk of conflict by a proportionate and significant degree. This aspect of regional trade agreements could perhaps explain their proliferation throughout all parts of the globe in recent decades.

Regional integration agreements have additional advantages of proximity, enabling possibilities to share in joint infrastructure and energy projects, collectively combating pollution, forming a common policy on natural resource usage like fishing, and strengthening the bargaining power of the member states.

Running concurrently with the tendency towards regionalism, has been the proliferation in bilateral agreements in recent times. Such agreements can asymmetrically serve the interests of both an individual LDC and a developed economy. The US has inked FTA's with 13 countries and is negotiating with an additional ten. Beijing has a dual policy of establishing an East Asia Free Trade Zone as well as securing bilateral agreements with individual nations. China has already signed or is negotiating bilateral agreements with all players in the region including Australia, New Zealand, Japan and the Asean states. Meanwhile, the EU is seeking to tighten up economic agreements with the 69 African, Caribbean and Pacific nations, many of whom were former colonies.

Sri Lankan experience

Sri Lanka first initiated economic liberalization in 1977 making it one of the first to do so in Asia and the impacts were felt immediately. The strategy sought to promote exports, revamp the tariff system, reform the exchange rate mechanism to a managed float, and woo large amounts of FDI with incentives like the FTZ schemes. New institutions like the Export Development Board were also formed in order to facilitate the process. The fiscal stance was also shifted towards a greater focus on infrastructure development as opposed to welfare programs.

A second wave of reforms took place in 1989/90 that saw the introduction of additional incentives for FDI, finance sector reforms, further non-tariff concessions and a new privatization drive.

The observed impacts according to the IPS were an increased share of public investment in GDP, a rising budget deficit due to the higher public investment not being accompanied by a comparable increase in saving rate, and consequently, inflation.

However, FDI picked up momentum up until 1983 when the ethnic riots sparked off a period of instability throughout the country that also triggered the Marxist JVP activists. Nevertheless, FDI into the garment sector continued and the sector officially overtook tea as the nation's number one export in 1986. However, the period from 1983-89 was characterized by widespread political turbulence and commercial activity was seriously stifled. In 1987 GDP growth was only 1.5 per cent.

Whilst exports grew, imports rose at a faster rate, as they still continue to do so. For example, whilst the garment sector was spearheading the export growth drive, it was also increasing the import bill as some 60 per cent of the inputs were imported. Moreover, the growth in garments took place concurrently with the demise of the textile and handloom industry. For workers who were able to switch sectors, the damage was limited but for others the human cost of transformation was difficult.

However, many found that working overseas in the Middles East was an attractive option. Between 1977 and 1982, an estimated half a million migrant workers took up employment in the Middle East. This phenomenon served to keep the country's current account balance in surplus as these low skilled workers send back their remittances. Today, well over one million are said to be working overseas, mainly in the Middle East and they send an estimated $2.2 billion per annum. Remittance earnings account for more foreign exchange than tea exports and are only surpassed by garments. In its absence he national economy would be in a completely unsustainable deficit situation.

However, the social cost of promoting large scale migration of labor, predominantly female housemaids, is often underscored by successive governments that need foreign currency to pay their import bills. At the household levels, families sans mothers, are known to have a high incidence of alcoholism, child abuse and school drop-outs. Families without fathers also suffer comparable problem whilst money is sent from abroad to meet their basic needs.

Conclusion, inconclusive

In Sri Lanka, it has not been possible for researchers and academics to assert with certainty the relationship between trade liberalization and poverty reduction due to the facts that mass migration, ethnic riots, civil unrest and civil war have had a greater impact on the economy and people.

Trade per se is entirely positive, both in theory and practice. However, when the 'devil is in the detail', international pacts and WTO agreements can result in asymmetrical benefits or outright losses for developing nations. It is also worth noting that more and more, the human element of economic development is excluded as growth figures are churned out. Trade liberalization, even when the agreements are reciprocal, will inevitably result in transformations that will impact negatively on some people's livelihoods. The ability for workers to switch sectors, travel geographically, acquire new skills, and other considerations such are gender bias will determine the real benefits of trade liberalization.