

Trade and poverty

March 18, 2006, The Kathmandu Post

By Puspa Sharma

Poverty has always been an overriding concern of various development efforts in Nepal. However, it was only since the Seventh plan (1985/86 – 1989/90) that poverty reduction had been stated as an explicit objective.

In the early nineties, the government initiated an extensive economic reform agenda that included liberalizing trade, investment and foreign exchange rate, rationalizing tariff structure and the tax system and promoting exports. These reforms were initiated in order to accelerate economic growth and expand employment opportunities with the ultimate objective of reducing poverty.

As a result, the Nepali economy was transformed into a more open, market-oriented economy making the country open and trade dependent economies in South Asia. These reforms helped in accelerating growth in the non-agriculture sector that included trade and contributed in keeping urban poverty at low levels by increasing employment and income generating opportunities. However, in terms of overall poverty, Nepal is still ranked the poorest in the region..

The major achievement after initiating open and market oriented policies in the early nineties was the increase in exports from nearly eight percent of GDP in 1996/97 to almost 14 percent in 2000/01. This growth, however, was mainly because of Nepal's trade concentration with India and the benefits that Nepal derived out of the Indo-Nepal trade treaty of 1996, and thus it was short-lived.

In 2001/02, exports to India as well as to other third countries declined sharply. The major reasons behind this decline were the global recession, imposition of quotas on Nepali exports by India and the deteriorating security situation at home. Whereas it was felt that trade would play a role in promoting economic growth and thus contribute in reducing poverty, concentration of trade, both commodity-wise and destination-wise, resulted in external shocks. We remained complacent with our trade concentration with India and the benefits we were deriving out of the bilateral trade treaty. We could not foresee the need to diversify our products and market. The result is that despite the economic reforms undertaken, we still lag behind in trade with other countries.

Nepal's trade concentration has always been prone to external shocks. Under the quota system, the Nepali garment and textile industry undoubtedly flourished favorably. Being the

second leading source of foreign exchange and providing direct and indirect employment opportunities to over a hundred thousand people, it was a major contributor to the Nepali economy.

Although it did not have any direct link with the rural economy, it was linked with rural poverty by means of the internal remittances that its workers used to send home. The expiry of the Multi Fibre Agreement (MFA) in December 2004 was a major setback for the industry after which it experienced a continuous decline in exports resulting in the closure of most of the production units and consequently in the loss of employment of its thousands of labor force.

However, the expiry of the MFA that ended the quota system is not the only reason for the poor performance of the industry. Had it been so, other South Asian and South East Asian countries too would not have fared better in the post-MFA era. Our complacency with the performance of the industry during the quota system blinded us from seeing its future. We neither intended to diversify our products nor the export markets. Had we recognized our comparative advantage and worked on it prior to the end of the quota system, we would still be confidently demonstrating the role of garment and textile trade in substantial reduction of poverty.

Even in other sectors, Nepal has not been able to translate the gains from trade into poverty reduction. Being an agrarian economy, Nepal has comparative advantage in the export of different agricultural products like honey, tea, vegetables, vegetable seeds, fruits, ginger and other products like herbs. Based on arbitrary international standards and other technical barriers set by the importing countries, these products of our export interest are often barred from getting exported to the destination markets. There are several cases of setting up of such barriers for Nepali products by India and many other European countries.

Developed countries have committed time and again to help the least developed countries (LDCs) integrate into global trade. Of those several commitments, providing duty and quota free market access to almost all the LDC products and providing trade related technical assistance are the major ones. These commitments have even been emphasized in Goal eight of the Millennium Development Goals (MDGs) – Developing a global partnership for development. But the implementation aspect of these commitments has been utterly disappointing. We have, on the one hand, internal problems of supply side bottlenecks, on the other, the external problems are no less severe.

The sole objective of the tenth plan, which is the Poverty Reduction Strategy Paper (PRSP), is achieving a "remarkable and sustainable" reduction in the poverty level by almost eight percent, from 38 percent to 30 percent, during the plan period.

Of the different measures undertaken, boosting internal and international trade for growth in the non-agriculture sector has been taken as an important measure by the tenth plan. It is during this plan period that Nepal has gained membership of the World Trade Organization (WTO), South Asia Free Trade Area (SAFTA) and the Bay of Bengal Initiative for Multi Sectoral Technical and Economic Cooperation (BIMSTEC).

It has been widely accepted that open economies grow faster than closed ones. The steadily increasing economic growth rates of China and India after liberalization should be an inspiration. Although trade has not been tied strategically with poverty reduction efforts in Nepal, in the light of its memberships with these different multilateral and regional trade bodies, it remains to be seen how it utilizes these memberships for enhanced trade that would lead to greater growth and poverty reduction.