EFFECT OF TRADE LIBERALIZATION AND GROWTH ON POVERTY AND INEQUITY: EMPIRICAL EVIDENCES AND POLICY OPTIONS

Wayan R. Susila[1] and Robin Bourgeois[2]

Pengaruh Liberalisasi Perdagangan, Kemiskinan dan Ketidakmerataan: Bukti Empiris dan Pilihan Kebijakan

[1]*Lembaga Riset Perkebunan Indonesia, Jl. Salak No. IA Bogor*
[2]*Centre for International Cooperation in Agronomic Research for Development (CIRAD), UPR Politiques et Marches, Montpellier, F-34398 France*

ABSTRAK

Penelitian-penelitian yang menganalisis hubungan antara liberalisasi perdagangan, kemiskinan, dan pemerataan berujung pada perdebatan. Dampak dari pasar terbuka dan pengurangan kemiskinan menghasilkan pandangan yang pro (Anderson, Jha *et al*., dan Bhattasali *et al*.). dan kontra (Coller and Dollar, Twyford, Medeley, and Abbotts) secara tajam. Di sisi lain, dampak pasar terbuka terhadap distribusi pendapat bersifat lebih konklusif. Kesimpulan ini berlaku juga untuk kasus Indonesia. Dua kelompok kebijakan disintesa dari studi ini yang mencoba mensinergikan liberalisasi perdagangan dan pertumbuhan dengan kemiskinan dan pemerataan untuk wilayah Asia dan Pacific. Kelompok kebijakan pertama adalah liberalisasi perdagangan yang berpihak pada pengurangan kemiskinan yaitu 1) mengoreksi ketidak-seimbangan; 2) meninjau ulang tentang timbal-balik kebijakan; 3) perlakuan yang spesial dan berbeda serta fleksibelitas; dan 4) isu-isu perdagangan yang menjadi kepentingan khusus negara berkembang. Kelompok kebijakan kedua berkaitan dengan kebijakan domestik yang berpihak kepada orang miskin yaitu 1) memperbaiki ketidak-seimbangan penguasaan asset/lahan; 2) perbaikan infrastruktur di pedesaan; 3) menciptakan iklim investasi yang kondusif; 4) mendorong penciptaan lapangan kerja yang berpihak pada orang miskin; dan v) meningkatkan penelitian dan pengembangan bidang pertanian.

Key words: *liberalisasi perdagangan, kemiskinan, pemerataan*

ABSTRACT

Studies assessing the link between trade liberalization, poverty and equity come up with debatable results. The effect of open markets on poverty alleviation is usually divisive between pros (Anderson, Jha, *et. al*., dan Bhattasali *et al.*) and cons (Coller and Dollar, Twyford, Medeley, and Abbotts), while effect on equity is more conclusive. These conclusions are also true for Indonesia case. Two policy insights are derived from studies review to reconcile the benefits of trade liberalization and growth with poverty alleviation and equity improvement in Asia and the Pacific. The first one relates to pro-poor trade liberalization through 1) rectifying imbalances; 2) rethinking reciprocity; 3) special and differential treatment and flexibility; and 4) trade issues of special interest to developing countries. The second is related to pro-poor domestic policies that include 1) reducing assets/land inequity, 2) promoting rural infrastructure, 3) creating conducive investment climate, 4) promoting pro-poor employment, and v) promoting agricultural research and development.

Key words: trade liberalization, poverty, equity

INTRODUCTION

Trade liberalization, growth, poverty, and equity have been and will be the main inter-related issues in international forums and international organizations. These issues are daily debated by almost all international organization, central and local governments all over the world.

Trade liberalization, initiated with Havana Charter in 1940, has completed four rounds, through the Dillon Round (1960-1962), the Kennedy Round (1963-1967), the Tokyo Round (1973-1979), the Uruguay Round (1986-1993), and is still on-going through the Doha Round since 2001. The high subsidy in developed countries, attaining to US$ 318 billion per year (World Bank, 2003), unfair distribution of the benefits of trade liberalization (Abbot, 2003; Madeley 2004; Twyford, 2003) and sluggish development of the Doha Round witness that the goals of making trade more efficient and fairer, especially in agriculture, have not been satisfactory realized (Abbot, 2003; Finger 2002).

The World Trade Organization (WTO) Doha Round was expected to be signed on 1 January 2005. The progress of the round is very slow because of a deadlocked in some important agricultural issues, mainly market access, domestic support, and export subsidies. Since July 2006, the Doha Round was suspended indefinitely after a succession of failed attempt to reach agreement on farm subsidy and tariff and modalities (Schott, 2006).

Evidence indicates that poverty is still a daunting concern for most developing countries. Half the world or nearly three billion people live on less than two dollars a day (Shah, 2004) and around 985 million live on extreme poverty on less than one dollars a day (Mukherjee, 2007). Moreover, most of the extremely poor live in the Asia-Pacific region, home to about 693-720 million of extreme poverty (ADB, 2004). This condition has caused over one billion children (more than half of those living in developing countries) suffer from severe effects of poverty and 674 million (over a third) are living in conditions of absolute poverty. Every 3.6 seconds someone dies of hunger, 24,000 people every day, and about 75 percent of them are children under five. Unfortunately, the number of people living in extreme poverty has increased by 0.5 billion since 1995 (Gordon *et al.*, 2003). If this trend cannot be reversed this would cost developing countries future productivity losses at a present discounted value of US$500 billion or more (FAO, 2004b).

For some scholars, trade liberalization has been perceived as a mean to induce economic growth, leading to poverty reduction (Anderson, 2004). Others state that trade liberalization weakly links with poverty reduction, or even, that it tends to worsen income distribution and equity. Trade liberalization has a negative impact on equity, such as in China and the Philippines (Ravallion, 2005; Giraud, 2002; Bhattasali *et al*., 2004).

These divisive opinions led this paper to undertake a review of various studies on the links between trade liberalization, economic growth, poverty and equity, supported by empirical evidence at regional and national level. The objective is to provide a clearer pictures and more precise information about the magnitude and the direction of these links and to derive policy implications for poverty alleviation.

The paper is focuses first on trade liberalization-poverty alleviation links. Then, trade liberalization and equity improvement is discussed, followed by an analysis of the relationship between economic/agricultural growth and poverty. The paper concludes with some policy options related to poverty alleviation and equity improvement.

TRADE LIBERALIZATION AND POVERTY ALLEVIATION

Many studies have been done to assess the links between trade liberalization, and poverty. The results mainly vary with the schools of thought, methods, state of development of region/country under the studies, and assumptions, not only in terms of magnitude of the relationship, but also in the direction of the links/relationship.

This divergence of results is used to classify these studies into two main groups, namely, (i) those supporting the role of trade liberalization in poverty alleviation and (ii) those questioning this role. In the first group, authors find that, with different magnitudes, trade liberalization has a positive impact on poverty alleviation. In the second one, it is found that there is unclear relationship between trade liberation and poverty alleviation.

Positive Effects of Trade Liberalization on Poverty Alleviation

Many studies found that trade liberalization have had a positive impact on growth, leading to poverty reduction effects. These findings, with different magnitudes, are stated for example in studies conducted by ADB (2004), Anderson (2004), Jha *et al.* (2004), Collier and Dollar (2004) and

Bhattasali *et al*., 2004). The general assumption behind these findings is that trade liberalization improves production and market efficiency, leading to positive net benefit/surplus in the world market. This net benefit will in turn induce economic growth and, to a certain extent, will reduce poverty.

Applying a quantitative model (Global Trade Analysis Project/GTAP), Anderson (2004) shows the magnitudes and the distribution of the monetary impacts of trade liberalization on developed and developing countries. He estimates total impacts at around US$ 254 billion of which US$ 164.7 billion relate to agriculture. Developing countries would benefit of 42.7 percent of the total impact. If developing countries want to maximize their benefits from the trade liberalization in the Doha Round, they also need to free up their own domestic product and factor markets so their farmers are better able to take advantage of new market opportunities abroad. Full liberalization of Organization for Economic Co-operation and Development (OECD) farm policies would boost the volume of global agricultural trade by more than 50 percent, but would cause real international food prices to rise by only 5 percent on average. Most developing countries and households would thus be better off in terms of some poverty indicators, such as, income and food security (Anderson, 2004).

A World Bank study (Bhattasali *et al*., 2004) also states that in 24 developing countries that have increased their integration into the world economy have achieved higher growth in incomes, longer life expectancy and better schooling. These countries, home to some 3 billion people, enjoyed an average 5 percent growth rate in income per capita in the 1990s compared to 2 percent in rich countries. Many of these countries, such as China and India, have adopted domestic policies and institutions that have enabled people to take advantage of global markets and have thus sharply increased the share of trade in their GDP. People in these integrating countries saw their wages rise, and the number of people in poverty decline.

The positive link between trade liberalization, especially in agriculture, and poverty alleviation is further supported in the case of India by Jha *et al*. (2004). They found that agricultural trade liberalization has potential benefit for poverty alleviation in India since barriers such as tariff peaks, tariff escalation, and domestic support and export subsidies restrict effective market access of Indian agricultural products to developed country markets. India's own tariffs have few peaks and are applied to only 1.3 percent of the tariff lines, against 20 percent in developed countries. With full trade liberalization in agriculture, India, as a net food exporting country, would likely see significant welfare gains. For example, exports would increase by 13 percent if trade distorting domestic support in developed countries were reduced.

Approximately 100 million people could be then lifted out of poverty by liberalizing developed countries agriculture. The authors indicate that poverty alleviating effects of multilateral liberalization would be increased if adequate reforms were made at the domestic level. Capacity building initiatives are required to help Indian farmers integrate well into the international market and also to meet quality issues in order to overcome the exacting regimes of sanitary and phyto-sanitary measures, along with consolidation of land holdings, better infrastructure, better use of IT, and marketing reforms (Jha *et al.*, 2004).

Using an integrated computable general equilibrium (CGE) micro-simulation approach, Cororaton and Cockburn (2005) show the positive impact of trade liberalization on poverty in the Philippines. Tariff cuts implemented between 1994 and 2000 generally reduced poverty, primarily through substantial decrease in consumer prices. However, a paradoxical results was that poverty reduction is much greater in the National Capital Region, where poverty incidence is already the lowest, compared to rural areas, where poverty incidence is normally highest

Questioning the Effect of Trade Liberalization on Poverty Alleviation

Contrasting with these optimistic findings on the role of trade liberalization on poverty alleviation, many studies find that this role is at least unclear and even could be negative. Bhattasali *et al*. (2005) for example found that in some countries trade liberalization has poverty alleviation impacts, but opposite results are true in other counties. In other worlds, not all countries have successfully integrated into the global economy since some 2 billion people - particularly in sub-Saharan Africa, the Middle East, and the former Soviet Union - live left behind countries. On average, these economies have contracted, poverty has risen, and education levels have increased less rapidly than in more globalized countries (Collier and Dollar, 2004**)**.

Twyford (2003) indicates that the impacts of trade liberalization on poverty levels depend on many factors, such as, the initial distribution of income and assets, what poor people produce, buy and sell, and how internationally competitive the national producers are. Nepal for example has opened its markets most rapidly and deeply but has poor records in poverty reduction (Twyford, 2003). Meanwhile, China and Viet Nam are clearly among the most successful globalizers, through aggressive promotion of exports along with careful management of imports, and they have achieved impressive results in poverty reduction (Twyford, 2003).

The role of trade liberalization on poverty is also questioned by Madeley (2004). There is now less confidence that the mainstream trading system can help the poor. The benefits of liberalization to low-income agricultural producers are likely to be very limited. At the start of the 21st century trade does not seem to be helped some of the world's poorest communities to escape from poverty. Trade liberalization and the rules of international trade are having a detrimental impact on many of the world poor and the environment. For more substantial gains (towards food security) countries will have to encourage the expansion of their domestic food production sectors (Madeley, 2004).

Abbots (2004) also states that the global trading system is still very much biased against the poor. An average poor person faces twice the level of trade tariff than an average rich person does. Political interests underlying various policies of developed countries cause some imbalances between developing countries and developed countries.

Weak links between trade liberalization and poverty reduction are also found by Ravallion (2005). His work based on empirical approaches casts doubt on any presumption that greater openness to external trade is the key to rapid poverty reduction. Equally, doubt was cast on any presumption that trade openness hurts more poor people than it helps. Pooled data on spells of poverty reduction across countries and over time, matched with measures of the extent of trade openness, does not reveal any correlation between rates of poverty reduction and expanding trade volume. Focusing on the longest time periods available for each country, one can unearth a positive correlation between greater trade openness over time and rates of poverty reduction. However, the correlation is rather fragile, and the data is more suggestive of diverse impacts of trade openness on poverty. Based on the data available from cross-country comparisons, it is hard to defend the view that trade openness is, in general, a powerful force for poverty reduction in developing countries (Ravallion, 2005).

From those all studies, we may infer that the impact of trade liberalization on poverty alleviation is still very much debatable. As Twyford (2003) states the evidence on the impacts of trade liberalization on poverty reduction is at best mixed, open markets are neither inherently good nor inherently bad for poverty reduction.

With respect to Indonesia, the debatable roles of trade liberalization on poverty alleviation have been inevitable. Although the debates are not as distinctive as in the world context, the different position of the experts on the Indonesian perspective are easily identified. Studies by Indrawati (1995), Hertel *et al.* (2002), Brooks and Sugiyanto (2005) are some studies that indicates the positive roles of trade liberalization on poverty. On the other hand, studies by Amang and Sawit (1997) and Sitepu (2002), indicates that trade liberalization has a negative impact on poverty and food security. However, most studies agree that to get benefit from trade liberalization, various complementary and distributional policies are required (Hardono *et al*., 2004).

TRADE LIBERALIZATION AND EQUITY

Compared to the impact of trade liberalization on poverty that is very much debatable, the findings on the impact on equity are more conclusive. Some studies found it at best ambiguous, but most of them indicate that the impact is worsening equity, especially across countries. Significant different levels of supports between developing and developed countries mostly explain these findings.

In 2002, for example, direct support to farmers by countries belonging to the Organization for Economic Co-operation and Development (OECD) totaled around US$235 billion, three quarters of the total OECD support estimate of US$318 billion. Subsidies by this group of countries account for over 90 percent of trade-distorting domestic support and export subsidies reported to the WTO. The figure is particularly striking if one considers that in high-income countries such as those belonging to the OECD, agriculture employs around 5 percent of the labor force and contributes only 2 percent to gross domestic product (GDP). In low-income countries, however, the sector provides around 70 percent of the labor force and contributes 36 percent to GDP (FAO, 2003).

Producers of soybean, corn, and sorghum in developing countries continuously face tough competition from producers in the USA as the 2002 Farm Bill established national loan rates for each commodity. These loan rates basically form the domestic support policy for the agricultural sector in the USA. For corn and grain sorghum, these rates reach $1.95 per bushel and will remain at that level through 2007 (FSA, 2007). The national soybean rate is unchanged at $5.00 per bushel. Developing countries cannot provide this kind of support and their producers face un-levelled playing ground.

The question of whether trade liberalization is a factor aggravating economic inequalities, between, as well as within countries is drawing more and more scientists' attention. The results of most long-term series analysis show that inequality - after decreasing or stabilizing for several decades - was back on the rise during the eighties and nineties. Related to this process, the role of trade liberalization is ambiguous. It may be an enticing factor for the poorest countries to catch up with more developed ones, as long as they enjoy some assets such as a strong and legitimate state system (Giraud, 2002).

A clear negative impact of trade liberalization on equity is found in the case of the Philippines documented by Cororaton and Cockburn (2005). Although trade liberalization implemented between 1994 and 2000 was generally poverty reducing, as indicated earlier, tariff cuts lowered the cost of local production and brought about real exchange rate depreciation. Since the non-food manufacturing sector dominates exports in terms of share and intensity, the general equilibrium effect of tariff reduction resulted in an expansion of this sector and a contraction of the agricultural sector. This, in turn, led to an increase in the relative returns to factors, such as capital, used intensively in the non-food manufacturing sector and a fall in returns to unskilled labour. As a result, inequality worsens as rural households depend more on unskilled labour income.

Similar results are also found with trade liberalization in China. Bhattasali *et al*. (2005) indicates that trade liberalization boosted China's economy but at the same time recommends that China make policy adjustments to balance the uneven distribution of benefits between rural and urban regions.

GROWTH AND POVERTY ALLEVIATION

As agriculture remains a key sector providing livelihoods of most of the Asian poor who still leave in rural areas the links between economic growth in general, and agriculture sector growth in particular, and poverty are essential. Most studies found that there is a positive link between economic growth and poverty alleviation, although the magnitude of the relationship varies.

Kraay (2006) postulates that growth contributes to poverty if growth is pro poor, that is if growth causes the magnitude of poverty indicators decline. Based on this, three potential sources of pro-poor growth were identified, namely: (1) a high rate of growth of average income; (2) a high sensitivity of poverty to growth in average income; and (3) a poverty-reducing pattern of growth in relative incomes. Changes in poverty in a large sample of developing countries during the 1980s and 1990s are empirically decomposed into these three components. In the medium to long run, most of the variation in changes in poverty can be attributed to growth in average income, suggesting that policies and institutions that promote broad-based growth should be central to the pro-poor growth agenda. Most of the remainder of the variation in poverty is due to poverty-reducing patterns of growth in relative income, rather than differences in the sensitivity of poverty to growth in average incomes. Changes in relative incomes account for only 30 percent of the variance of changes in the headcount measure of poverty in the short run, and only three percent in long run. Growth in average incomes accounts for virtually all of the remaining 70 percent of the variance in the short run, and 97 percent of the variance in the long run, while cross country differences in the sensitivity of poverty to growth are very small (Kraay, 2006).

In the case of Asia and the Pacific region, Asian Development Bank (2004) conducted a study to identify the relationship between growth and poverty. Using 18 Asia and Pacific countries and 111 “spells”, defined as a time period over which income/expenditure and poverty data from comparable and contiguous household surveys spaced at least 3 years apart are available, the results indicate that on average, growth is strongly associated with poverty reduction. In particular, a one percent growth is associated with a 1.5 percent decline in the incidence of $1-a-day poverty on average. However, growth is only one factor among others influencing poverty. It explained only 43 percent of the variation among this set of developing countries. Interestingly, the relationship between growth and poverty reduction appears much tighter when one examines growth spells in developing Asia. Each percent of growth is associated with an almost 2 percent decline in poverty incidence on average. In addition, growth explains 65 percent of the variation in changes in poverty on average among the developing member countries.

A comparison of the effect of growth on poverty reduction between China and South Asia is also enlightening. Almost 93 percent of approximately 690 million people living with less than US$1 a day in Asia can be found in South Asia and the China. However, China has had more success over the last two decades in reducing poverty compared to South Asia. There are three main reasons for this. First, economic growth in South Asia has been lower than that in China. While China experienced an economic growth more than 10 percent in the last three years, South Asia’s growth was below 8 percent. Second, rural incomes in particular, have grown much more slowly in South Asia than in China, and since a large majority of the poor reside in rural areas, they disproportionately benefit when economic opportunities in rural areas expand rapidly. Finally, industrial growth in South Asia has not generated as much employment for less-skilled workers as it has in China (ADB, 2004).

Some studies found also that the pace of poverty reduction depends both on the rate of average income growth, the initial level of inequality, and changes in the level of inequality (Klasen 2005, Bourguignon 2003). There appear to be linkages between initial income or asset inequality and growth where high initial inequality is harmful for overall economic growth, and thus for poverty reduction, at least in environments of very high income or asset inequality. Similar results also appear to hold true for gender inequality, particularly in education (Klasen, 2005). In particular, poverty reduction will be faster in countries where average income growth is higher (Dollar and Kraay, 2002), where initial inequality is lower and in situations where income growth is combined with falling inequality. Pro-poor growth as defined by Kraay (2006) pays off, as well as lower initial inequality and reductions in inequality during the growth process do.

The combination of rapid economic growth and strong pro-poor policies accounted for a significant part of the reduction in poverty in Viet Nam, according to (Cord and Rama, 2004). In 1993, 58 percent of the population lived in poverty, compared to 37 percent in 1998 and 29 percent in 2002. Progress was also substantial in non-income indicators, from education enrollment to infant mortality. Poverty is expected to be reduced to 15 percent by 2010 if the seven percent growth experienced during the 1990’s is maintained.

Sectoral growth in agriculture is also found as a key for poverty alleviation. An estimated 2.5 billion people in the developing world depend on agriculture for their livelihoods (FAO, 2004a). Therefore, agricultural development, and investment, is often considered as the first step in fighting poverty. In most poor countries, agriculture is still the largest employer, job creator and export earner. Research has shown that for every dollar spent on agriculture, another two dollars is generated for a developing country's national economy (FAO, 2005). Historically, agricultural development can generate increased incomes, which lead to savings and investments, and finally to reduce poverty (Rahman, 2004). However, poverty data shows a weakening relationship between agricultural growth and poverty alleviation. In Asia, a one percent increase in agricultural output was associated with almost 0.6 percent decrease in poverty in the 1970s and only slightly over 0.1 percent in the 1980s (ILO, 2005).

Yet, increase in agricultural productivity, especially yields, is still perceived as an effective strategy to reduce poverty**.** Recent research shows that a one percent increase in agricultural yields reduces by between 0.6 to 1.2 percent the percentage of people living on less than $1 per day and claims that no other economic activity generates the same benefits for the poor (DFID, 2003).

Another study in Bangladesh, China, India, Indonesia, Pakistan, and Vietnam indicates a significant contribution of agricultural productivity improvement on poverty. Estimated elasticity of poverty with respect to crop productivity performance varies across countries from –0.15 to –4.42 with the average of –0.29. Elasticity estimates are much higher in China (-4.42), followed by Viet Nam (-0.91) and much lower for South Asia countries (from –0.15 to –0.28). These findings are consistent with those relating initial inequities in resource distribution and poverty level. Where inequities and resource distribution are high, poverty levels also tend to be high, and poverty elasticities are low (Hussain, 2005).

A study on the links between industrial growth and poverty was conducted by Hasan and Quibria (2004), using a recently constructed cross-country data set on absolute poverty. They found that the poverty-growth linkage is strongest in East Asia and that this linkage is essentially driven by growth in the industrial sector. By contrast, industrial growth has had little positive impact on poverty reduction in other regions. These findings are consistent with the notion that East Asia's greater success in poverty reduction lies in its greater openness and market orientation, which created a pattern of labor-intensive industrial growth that led to rapid growth in employment and poverty reduction (Hasan and Quibria, 2004).

POLICY OPTIONS IN MAKING TRADE LIBERALIZATION WORK FOR THE POOR

This review of the findings from studies dealing with trade liberalization, growth, poverty alleviation and equity indicates that trade liberalization has potential to reduce poverty if it is designed with purposefulness and implemented in a fair and efficient. They pinpoint that not only external trade matters, domestic policies have also a key role. The following discussion will focus how trade liberalization and domestic policies can be directed to reduce poverty.

Directing Trade Liberalization to the Poor

Making trade liberalization work for the poor should theoretically not be an issue to be discussed, as it is explicitly expected to do so. Yet, evidence from the review indicates that it is not the case. Thus, the question is how to manage and formulate the Doha Round to achieve its main goal, that is, development?

Following some arguments that trade liberalization is still biased in favour of developed countries and that the net benefits are not fairly distributed, Abbott (2003) comes with an approach, called Critical View (CV), to take advantage of the opportunities trade liberalization may offer for developing countries to reduce poverty. Sticking to the basic and ultimate goal of trade liberalization as development and fair trade being the means to achieve it, under this approach, the basic question of trade policy is not whether a national measure is *trade*-distorting but whether it is *development*-distorting.

Accordingly, several issues can be construed as obstacles to the Doha Round as a development inducing process. These issues are limited market access of agricultural and manufactured products and services of developing countries, subsidies and support of industrialized countries to their agricultural sectors, Trade-Related Aspects of Property Rights (TRIPS), and reciprocity issues. Consequently, under the Doha Round, this approach would emphasize the following points.

Rectifying Imbalances

Policies that cause imbalances between Developing and Industrialized countries and inhibit development should be eliminated or reduced. These policies include TRIPS, general agreement on trade in services, and subsidy policies in ICs. Indonesia has a great interest in these issues and need to prepare a clear policies, especially on trade in services and reductions of subsidies in ICs.

Rethinking Reciprocity

It is unfair to expect "full reciprocity" between developing countries and industrialized countries because of differences between economic capacity, the various political situations, and the vulnerability of developing countries. An alternative offered by this approach is to place reciprocity based on the relative state of development. With this respect, Indonesia can request special treatments in bilateral, multilateral forum when negotiations involving developed countries.

Special and Differential Treatment (SDT) and Flexibility

SDT is intended to improve the markets for Developing Countries in Industrialized ones and to give flexibility to the former to intervene in their markets for the sake of development. Indonesia is the main player of the issues and has a special interest on various products such as rice, and sugar.

Trade Issues of Special Interest to Developing Countries

Under the Doha Round, issues that are the main concern of Developing Countries should be prioritised. These issues include their export vulnerability due to technical inferiority price risk, and the dependency of developing countries on only a few exportable commodities. Indonesia has special interest on textile and textile products, foot ware, and fish products.

Formulating Pro-Poor Domestic Policies

Many papers have discussed the formulation and implementation of pro-poor policies highlighting some important issues that need to be prioritised (Intizar, 2005; Ilyas, 2004; Jitsuchon and Methakunnavut, 2004; Uku 2004; Riddle, 2004; Collier and Dollar, 2004). Five are highlighted thereafter since they directly relate to the way trade liberalization can be made working for the poor, as revealed by the results of the review.

Improving Assets/Land Inequity

Inequality, especially in terms of productive assets such as land, is attributed to poverty. A study by the International Water Management Institute and ADB in Bangladesh, China, India, Indonesia, Pakistan, and Vietnam indicates that land equity is one of the most determining factors in poverty reduction. A one percent decrease in land distribution based Gini coefficient would reduce poverty by 0.38 percent (Intizar, 2005). The relationship between inequitable land distribution and poverty is also indicated by Ilyas (2004) for the case of Pakistan. Improvement in productivity can mitigate poverty only through equitable redistribution of land and other assets. Indonesia has to promote and speed up the redistribution of productive assets, especially agrarian reform and access to credit.

Improving Rural Infrastructure

While there is clear consensus on the importance of infrastructure, access to, quality of, and financial needs for infrastructure services remain staggering. In rural areas in low-income countries, only 20 percent of the population has access to electricity, and less than 2 percent has access to a telephone line (Uku, 2004). Public investments in infrastructure (including roads and electricity, irrigation), especially in rural areas, have positive impacts on agricultural productivity growth and rural poverty reduction (Collier and Dollar, 2004; Uku, 2004; ADB, 2004). Impro-vement of infrastructure plays an important role in poverty reduction in China, Thailand, and Vietnam For example, road development has the third largest impact on rural poverty reduction in Thailand (Jitsuchon and Methakunnavut, 2004). Meeting the challenge of increasing access to quality infrastructure services will require sizable investments, around 7-9 percent of GDP for all developing countries (Uku, 2004). Indonesia has to prioritize the improvement of infrastructure, mainly road, irrigation system, electricity, and marketing facilities in the rural areas.

Promoting Conducive Investment Climate

Accelerating growth and reducing poverty require governments to ensure a healthy investment climate by limiting the policy uncertainties, added costs, and barriers to compete that confront firms of all types. Based on the survey conducted by the 2005 World Development Report involving more than 6,500 businesses throughout East Asia, policy risks, macroeconomic instability, and corruption are key obstacles to conduct business in the region. Improving policy predictability alone can increase the likelihood of new investment by more than 30 percent. Moreover, stronger competitive pressure can increase the probability of innovation by more than 50 percent. Macroeconomic instability and corruption together with weak contract enforcement and onerous regulation cost more than 25 percent of sales - or more than three times what firms typically pay in taxes. China's investment-climate reforms over the last two decades are said to have helped lifting 400 million people out of poverty, and the manufacturing value added in China and South Korea alone is much larger than all global aid flows (Neal and Fossberg, 2004). For Indonesia, improvement of business climate, mainly on consistent regulation, macro economic policies, labour policies, and infrastructure improvement are urgently needed.

Promoting Pro-Poor Employment

To reduce poverty, rapid growth of the sectors where the poor intensively work and the sub-regions where they reside is a priority. Promoting agricultural sector is critical to significantly reduce poverty (ADB, 2004). However, current trends show that off-farm activities are on the rise everywhere in Asia, and have to be promoted as well as complementary diversified options offered to the poor in rural areas (Booth, 2002). For Indonesia, promoting agriculture and labor intensive sectors such as textile and textile products, foot ware, small and medium enterprises are examples of the sectors that have to be prioritized.

CONCLUSIONS AND POLICY IMPLICATIONS

A review of studies on the links between trade liberalization, growth, poverty alleviation and equity shows that findings are far from being consistent. It is not only a question of magnitude; the sense of the relationship is also divisive. Meanwhile, trade liberalization is mostly regarded as having negative effects on equity, or at best ambiguous effect. Growth, and particularly agricultural growth, is usually considered as positively linked with poverty alleviation. This is particularly true in the case of countries that have experienced the highest growth level. However, growth does not always account for the biggest part of poverty alleviation. Other factors, such as the initial level of inequality in income and asset distribution and its evolution, are found to determinant as well.

In many studies of the impact of trade liberalization domestic polices come as recurrent issues with emphasis on their orientation towards poverty reduction. This means that given the lack of evidence of any intrinsic virtues of trade liberalization for poverty alleviation, only a combination of purposeful trade liberalization measures and pro-poor domestic policies can make trade liberalization work for the poor.

In this paper three issues related to trade liberalization and four issues related to pro-poor domestic policies are identified based on the review. The former constitute the minimum paraphernalia that is needed to ensure that would ensure that the on-going process under the Doha Round would not yield the removal of trade-distorting policies but that of development-distorting policies. These include rectifying imbalances, rethinking reciprocity, special and differential treatment and trade issues of special interest to developing countries.

Pro-poor domestic policies that would make trade liberalization work more for the poor can also be drawn from this review. Basically they consist in promoting investment in sectors that would most benefit the poor either through wide ranging effects of specific focus. Improving assets/land inequity and promoting pro-poor employment are measures that have directly impact on the poor by conveying the potential benefit of trade liberalization to the poorest area. At the same time, improving rural infrastructure and promoting a conducive investment climate constitute pre-conditions for agricultural as well as off-farm opportunities generated by trade liberalization to pervade in rural areas where most of the Asian poor live or from where they come.

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