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Part Two: Chapter 7

Improving the Trade–Poverty Relationship through National Development Strategies

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Improving the Trade–Poverty Relationship through National Development Strategies

Chapter

7

A. Introduction

The improvements in the international trade regime discussed in the previous chapter should provide a framework for linking trade more effectively with poverty reduction in the LDCs. However, whether or not the increased opportunity for poverty reduction will be translated into reality depends on whether it is grasped at the national level. The fundamental priority here is that Governments formulate and implement national development strategies that integrate trade within them in a way that effectively promotes sustained development and substantial poverty reduction. This is critical because it is the area where the LDCs themselves potentially have the most leverage to make trade work for poverty reduction.

National development strategies will work best not simply if the international trade regime is enabling but also if increased and effective international financial and technical assistance is provided to the LDCs to help develop their production and trade capacities. The scale of investment needs, the paucity of domestic financial resources and technical know-how, the trade-off between domestic resource mobilization and poverty reduction, and the marginalization of the LDCs in international private capital flows all imply a need for such assistance. Policy incoherence between international assistance and national trade objectives, insufficient and misdirected aid for trade, and the failure to facilitate and nurture national ownership of trade and development policies can all undermine national efforts to grasp opportunities which changes in the international trade regime provide.

Whether or not the increased opportunity for poverty reduction will be translated into reality depends on whether it is grasped at the national level.

This chapter discusses how trade can be integrated into national development strategies in the LDCs, and how these efforts can be supported through international assistance for trade capacity development. For most LDCs, national strategies for poverty reduction are embodied in the Poverty Reduction Strategy Paper (PRSP), and it is intended that international assistance priorities be linked to these documents. The chapter thus begins (section B) by examining how trade issues are currently treated in the PRSPs. The evidence shows that it is a misconception to believe that trade issues are absent from the PRSPs. But there are various weaknesses in the way in which trade is integrated within them. Sections C and D propose an approach to integrate trade more closely into poverty reduction strategies. The essence of this approach is that it involves "two-way mainstreaming" of both trade and development into poverty reduction strategies.[1] Section C focuses on the first part of the approach and the question of integrating development into poverty reduction strategies by anchoring the latter in a broader national development strategy. A critical issue here is the choice of development strategy in the newly liberalized open economy, and a number of "post-liberal" development strategies are outlined in the annex to the chapter. Section D examines the second part of the approach, setting out a methodology for integrating trade into development-oriented poverty reduction strategies and noting the importance of establishing a durable trade policy framework within which this can be applied. Section E discusses policy issues in relation to international assistance for trade capacity development. The concluding section summarizes the major points.

B. Trade in Poverty Reduction Strategy Papers: Recent country experience

1. The evolution of the PRSP approach

In discussing how trade issues are treated in PRSPs, it is important to recognize that the PRSP approach has evolved considerably since it was first introduced at the end of 1999. As discussed in *The Least Developed Countries Report 2000* and *The Least Developed Countries Report 2002*, the first generation of PRSPs essentially sought to integrate pro-poor public expenditure patterns with deeper and broader structural reforms and the macroeconomic policies adopted in earlier structural adjustment programmes. In retrospect, this should not be seen as surprising. The preparation of the PRSP was introduced as a policy conditionality in the context of the Enhanced HIPC Initiative with the aim of ensuring that savings from debt relief were channelled into direct poverty reduction. It is in that context that the emphasis on social-sector expenditure arose. The more recent PRSPs are still linked to policy conditionality for debt relief within the HIPC Initiative, but they have tended to focus much more on the sources of growth and the ways in which it be made more pro-poor.

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Table 57 summarizes the priority actions identified in the Action Matrices of the most recent 13 full PRSPs completed in the LDCs as of March 2002. From the table it is clear that there is diversity, but in a number of the PRSPs a common pattern is emerging in the approach of many of the poverty reduction strategies since mid-2002. This common pattern has four basic pillars:

(i) Ensure strong and sustainable economic growth;

(ii) Develop human resources;

(iii) Improve the living conditions of the poor and vulnerable;

(iv) Ensure good governance.

In addition, the PRSPs generally treat cross-cutting issues such as gender, environment and HIV/AIDS.

Within each of these basic pillars, a number of common concerns also arise. Under pillar one continued emphasis is placed on stabilization, liberalization and privatization, as in the old structural adjustment programmes. But investment in basic infrastructure (transport and communications, energy, and water and sanitation), private sector development, export promotion and the creation of a better investment climate have also emerged as priority concerns in most recent PRSPs. Under pillar two, the priorities are adequate health and education systems and also labour market policies. Under pillar three, social protection, micro-finance and food security are recurrent concerns. Under pillar four, the recurrent objectives are the establishment of efficient, accountable and transparent management of public resources, democratic decision-making, decentralization of basic services to local levels of governance and the prevention of corruption and fraud.

TABLE 57. MAJOR PRIORITY ACTIONS IN RECENT PRSPS OF LDCS

	Benin (Dec. 2002)	Cambodia (Dec. 2002)	Chad (June 2003)	Ethiopia (July 2002)	Gambia (April 2002)	Madagascar (July 2003)	Malawi (April 2002)	Mali (May 2002)	Nepal (May 2003)	Rwanda (June 2002)	Senegal (May 2002)	Yemen (May 2002)	Zambia (March 2002)
1. Ensure strong and sustainable growth	x	x	x	x	x	x	x	x	x	x	x	x	x
Stabilize macroeconomic framework	x	x	x	x	x		x	x	x	x	x	x	x
Pro-poor fiscal policies	x	x	x	x			x	x	x	x	x	x	x
Monetary policy		x	x				x		x	x	x	x	x
Private sector promotion	x	x	x	x	x	x	x	x	x	x	x	x	x
Export promotion		x	x	x		x	x	x	x		x	x	x
Develop basic infrastructure	x	x	x	x	x	x	x	x	x	x	x	x	x
Roads	x	x	x	x	x	x	x	x	x	x	x	x	x
Energy	x	x	x	x	x		x	x	x	x	x	x	x
Water and sanitation	x	x	x	x	x	x	x	x	x	x	x	x	x
2. Development of human resources	x	x	x	x	x	x	x	x	x	x	x	x	x
Adequate health system	x	x	x	x	x	x	x	x	x	x	x	x	x
Adequate education system	x	x	x	x	x	x	x	x	x	x	x	x	x
Adequate labour market policy	x	x	x	x	x	x	x	x	x	x	x		x
3. Improve living conditions of the poor	x	x	x	x	x		x	x	x	x	x	x	x
Social protection	x	x	x		x		x		x	x	x	x	x
Micro-finance schemes	x	x	x	x	x						x		
Food security	x	x		x			x	x	x				x
4. Good governance	x	x	x	x	x	x	x	x	x	x	x	x	x

Source: UNCTAD secretariat compilation, based on Poverty Reduction Strategy Papers.

The new emphasis on sources of economic growth is a welcome development since it is through sustained economic growth that poverty reduction will take place in LDCs. The nature of the PRSPs still reflects the limitation of national capacities for policy analysis and the consequent need to rely on external expertise. According to senior African policy experts at the third annual meeting of the African learning group of PRSPs, "While the PRSP is an important conceptual shift in development thinking, there is still a lack of symmetry between the objectives and priorities of the PRSP and sectoral plans and strategies. In particular, macroeconomic projections in some PRSPs appear to be too optimistic and inconsistent with country realities. In a number of cases, the growth strategies are not country-specific" (ECA, 2003). The IMF and World Bank similarly point to the problem of "weak links in many PRSPs between overall strategic goals and priority public actions" (IMF/World Bank, 2003: 21). This is particularly evident in relation to the pursuit of strong and sustainable economic growth. Although increased attention is paid to sources of economic growth, "the choices of priority public actions in PRSPs are still not derived from the identified growth sources and risks. In some cases, this is because PRSPs have not adequately identified future sources of growth to guide policy choices. Yet, even where analysis of the sources of growth was undertaken, priority areas are not always linked to the identified obstacles to growth. Thus, proposed public resource allocations are not informed by potential returns on investments in different activities" (ibid.: 20).

The PRSPs are evolving away from the old structural adjustment programmes towards new growth strategies which seek to include the poor. But this transition is still incomplete.

The current situation with regard to the PRSP approach can best be understood as one in which the PRSPs are evolving away from the old structural adjustment programmes towards new growth strategies which seek to include the poor. But this transition is still incomplete. There remain strong concerns about how the ideal of national ownership and policy autonomy can actually be realized in situations where capacities are weak and aid and debt relief dependence are high (see UNCTAD, 2002, for more on the tension between conditionality and ownership).

2. The treatment of trade issues in PRSPs

The way in which the PRSPs treat trade issues needs to be understood against this background. There is a general impression that trade is not integrated within the PRSPs. This view underpinned the first evaluation of the Integrated Framework for Trade-Related Technical Assistance in 2000, which recommended that the IF be reoriented to ensure that trade is mainstreamed within PRSPs. This has also been suggested by NGOs, notably Christian Aid, which has argued that trade issues are absent from PRSPs, and particularly the participation process, because the issue of trade reform is "too hot to handle" (Ladd, 2002). The major systematic published analysis of trade in PRSPs, which includes PRSPs up to July 2002, concluded as follows: "…first, the extent and depth of trade coverage in completed PRSPs is limited…Second, the trade content that does exist within PRSPs is rarely underpinned by poverty analysis…Third, within existing PRSPs, some trade policy choices have been considered, but few developing countries go beyond a simple discussion of standard export promotion measures. Supply-side issues which facilitate trade and complement trade policy e.g. infrastructure, marketing, etc. appear to be well-covered in PRSPs and, therefore, require urgent donor attention and resources" (Hewitt and Gillson, 2003: 15–16).

Trade issues have come to occupy a much more central place in the PRSPs. The main problem now is not that trade is not integrated within the PRSPs, but the way in which it is being treated.

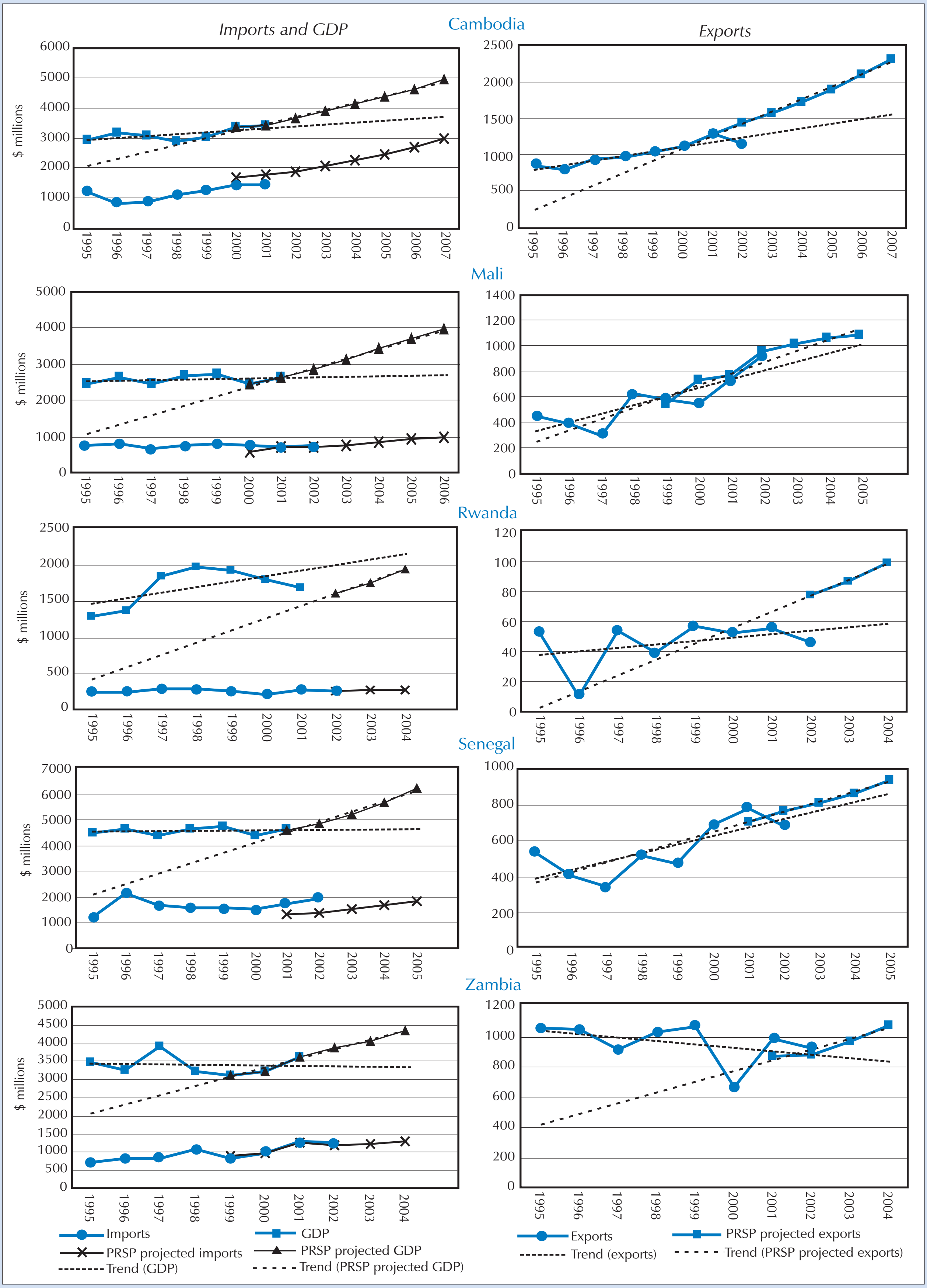
Systematic analysis of how trade is treated in the PRSPs of LDCs indicates that there is indeed some validity to the view that trade was not treated in the PRSPs in the past. But with the evolution of the PRSPs towards growth strategies which seek to include the poor, trade issues have come to occupy a much more central place in the PRSPs. The main problem now is not that trade is not integrated within the PRSPs, but the way in which it is being treated.

Trade issues are dealt with in the recent PRSPs of the LDCs in two ways. Firstly, projections of export growth and import growths are part of the macroeconomic framework. These projections occur in all PRSPs and are one of the major quantitative targets in the document. Because of this, trade is already right at the heart of every PRSP. Secondly, the main text of the PRSP includes a wide range of trade objectives and trade policies related to those objectives. In most of the PRSPs prepared by the LDCs there is no separate trade section. But there is no reason to believe that these documents downplay the importance of international trade for both economic growth and poverty reduction.

Chart 42 shows projections of trends of GDP, exports and imports within the macroeconomic frameworks of five LDCs for which it is possible to make comparisons with trends in the recent past. There are four general tendencies in the projections. Firstly, it is expected that GDP growth will be higher than the trend growth rate of the last five years in all cases. Secondly, it is expected that export growth will be higher than the trend growth rate of the last five years in all cases except one, namely Senegal. Thirdly, it is expected that the import intensity of growth will decline in all cases but one. This is contrary to the evidence of what has happened after trade liberalization (see chapter 5). Moreover, in three of the five countries import growth is also projected to grow at a slower rate than GDP.[2] Fourthly, the major part of the increase in GDP is expected to come from export expansion. The only exception, Senegal, is the only country in which an acceleration in the export growth rate is not expected, and it follows that the source of accelerated economic growth is unclear.

These trade objectives in the macroeconomic framework "float freely", having no connection with the more detailed trade objectives and policy measures contained in the main text of the PRSP. There is no analysis of the links

Chart 42. Past trends and projections of GDP, exports and imports in the macroeconomic framework of selected LDCs
($, million)



Source: UNCTAD secretariat estimates. The projections are the figures contained in the PRSPs, whilst past trends are based on World Bank, *World Development Indicators 2003*, CD-ROM; and on UN COMTRADE from UNCTAD, *Handbook of Statistics 2003*.

Note: The PRSPs' figures for Mali and Senegal were in local currency and were changed into dollars using the estimated exchange rate included in the PRSP of Mali. The PRSP's GDP figure for Rwanda was also in local currency and was changed into dollars using the exchange rate for 2002 of 511.85, taken from IMF, *International Financial Statistics 2003*, CD-ROM. All data are in current dollars.

between trade and growth. But all the PRSPs include increased openness as an objective. Openness is not always defined in the PRSPs, but it is generally understood as either reduced or more rationalized tariff barriers, or an increased contribution of exports to GDP. The general assumption seems to be that increased openness and/or increased exports will accelerate economic growth. Although it is not often stated, the growth strategy that implicitly underpins these PRSPs is primarily an export-led growth strategy.

Although it is not often stated, the growth strategy that implicitly underpins these PRSPs is primarily an export-led growth strategy.

Table 58 summarizes, as well as possible, the trade policy objectives and policy measures contained in 13 PRSPs as of March 2002. Undertaking such a synopsis entails some qualitative judgements. But it is clear that, as well as openness, increased competitiveness and export diversifications are important objectives in almost all the PRSPs. The development of tourism is seen as important in 12 countries, export-oriented manufacturing in seven countries and high-value-added agricultural products also in seven countries. There is much less consideration of import issues, with no PRSP mentioning better procurement as an objective, one mentioning infant industry protection and five mentioning the need to reduce the import content of domestic consumption. In terms of policy measures, improving infrastructure is seen as the most important issue. Export promotion is identified as a trade policy measure in eight cases, financial incentive schemes for exporters in four cases and the creation of an

TABLE 58. SPECIFIC TRADE POLICY OBJECTIVES AND INSTRUMENTS IN RECENT PRSPS OF LDCS

	Benin	Cambodia	Chad	Ethiopia	Gambia	Malawi	Madagascar	Mali	Nepal	Rwanda	Senegal	Yemen	Zambia
Trade policy objectives													
Openness	x	x	x	x	x	x	x	x	x	x	x	x	x
Export diversification	x	x	x		x		x	x	x	x	x	x	x
Increase competitiveness	x	x	x	x	x	x	x		x		x		x
Development of high-value agricultural products		x		x	x	x	x		x		x		
Development of export-oriented manufacturing activities		x	x	x					x	x		x	x
Trade facilitation	x	x			x	x	x		x		x		x
Tourism development	x	x		x	x	x	x	x	x	x	x	x	x
Reduce import content of domestic consumption to decrease BOP deficit		x		x	x	x					x		
Strengthening production and consumption linkages				x									
Trade policy instruments													
Suitable exchange rate policy				x	x	x	x		x	x		x	
Export promotion policies		x		x	x		x	x		x		x	x
Financial incentive schemes for exporters	x		x					x	x				
Policies aimed at reducing economic weaknesses (e.g. regulatory, geographical and infrastructure)	x	x	x			x	x	x	x		x	x	x
Regionalism	x		x				x			x		x	x
Free economic zones/EPZ		x			x		x					x	x
Cascading tariffs							x						
Infant industry protection		x											
Commercial diplomacy		x											x
Access to developed countries' markets		x					x				x		
Market exports abroad									x				x

Source: UNCTAD secretariat estimates, based on Poverty Reduction Strategy Papers.

export processing zone in five cases. Surprisingly, a suitable exchange rate policy is only mentioned in about half the PRSPs (7). Enhanced regional relationships are important for six countries. However, there is no analysis of demand-side constraints on exports, and only a few of the PRSPs identify commercial diplomacy and access to developed country markets as a means of achieving trade objectives.

An important feature of the way in which the PRSPs treat trade issues is that trade development is closely related to issues of private sector development, the improvement of the investment climate and also the development of productive sectors. Indeed, one reason why it is difficult to isolate the trade objectives and trade policy measures in the PRSPs is that trade is treated in an integrated way with the development of productive capacities and also private sector development. There is an important insight here which should not be lost through an effort to give greater priority to trade per se. The linking of trade to private sector development and the development of production capacities within the PRSPs are an important signal from the LDCs to their development partners on the best way to support trade development in these countries.

One reason why it is difficult to isolate the trade objectives and trade policy measures in the PRSPs is that trade is treated in an integrated way with the development of productive capacities and also private sector development.

Trade objectives and trade measures are, nevertheless, treated in quite a general way. There is no analysis of the impact of past trade policies as a basis for moving forward. There is also little analysis of the links between trade and poverty.

One influence on the content of trade within PRSPs has been the implementation of the Integrated Framework for Trade-Related Technical Assistance (IF). This initiative, which will be discussed in more detail in section E, has led to a much fuller treatment of trade in the Cambodia PRSP. This PRSP differs from almost all the other PRSPs because employment generation is a central focus of the strategy. But this reflects the priority of the Government rather than the influence of the IF. The IF has also led to the inclusion of a more-focused section on trade in the Mauritania PRSP Progress Report. However, in contrast to these cases, the influence of the Diagnostic Trade Integration Study (DTIS) on the Madagascar PRSP appears to be negligible. This may reflect the fact that the DTIS was only finished in June 2003, one month before the completion of the PRSP.

Through the macroeconomic framework, quantified trade targets are at the heart of all the PRSPs.

Finally, it is worth noting that how the PRSP works also depends on the practices of the LDCs' development partners. The PRSPs are intended to work as a nationally owned strategy to which the donors and the international financial institutions gear their operations. But in practice, according to senior African policy makers, "Africa's partners have been very slow in changing adjusting their aid policies to the PRSP approach" (ECA, 2003). Hewitt and Gillson (2003: 9) find that "in a number of cases" PRSPs were consistent with IMF Poverty Reduction and Growth Facility (PRGF) programmes and World Bank Poverty Reduction Support Credit (PRSC) programmes. But 4 of the 10 LDCs in their sample of countries were exceptions. Loan documents did not mention the agricultural-development-led-industrialization strategy of Ethiopia; referred to food import subsidies and adjustment to trade taxes which were not mentioned in the Malawi PRSP; provided much more sectoral discussion of trade policy than the Tanzania PRSP; and included discussion of regional and preferential trade agreements not mentioned in the Uganda PRSP (ibid.: 9–10).

To sum up, although spread widely in the documents, trade is covered in the PRSPs. Through the macroeconomic framework, quantified trade targets are at the heart of all the PRSPs. Moreover, the implicit underlying growth strategy in all of them seems to be export-led growth based on the adoption of an open trade regime. The way in which the PRSPs link the issues of trade development, private sector development and the development of productive sectors has important implications for donor support for trade development. It implies that isolating trade policies as the mechanism of trade development is likely to run counter to the approach which is common in many PRSPs.

The main weakness in the way trade is treated in the PRSPs is the same weakness as that which generally pertains to all policy issues in the PRSP, namely the overall strategic goals are only loosely related to priority public actions. This is particularly evident in the lack of any connection whatsoever between the macroeconomic framework and trade objectives. There is also an imbalance in the PRSPs between the way in which they treat exports and imports, and between demand-side and supply constraints in analysis of trade. The documents do not have a methodology for linking trade with growth and poverty reduction.

C. Mainstreaming development into poverty reduction strategies

The main weakness in the way trade is treated in the PRSPs is the same weakness as that which generally pertains to all policy issues in the PRSP, namely the overall strategic goals are only loosely related to priority public actions.

This section and the next one set out an approach to mainstreaming trade within poverty reduction strategies. The approach is a development approach that is founded on the view that substantial poverty reduction in the LDCs requires sustained economic growth and the development of productive capacities. Its analytical focus is not on the process of adjustment, identifying how poor people are affected during trade liberalization and identifying the complementary policies which need to be in place to alleviate poverty during trade policy reform and to ensure that poor people benefit from this process.[3] Rather, it focuses on identifying trade development objectives that are important for sustained economic growth and long-term development, and the trade policies, including trade liberalization, and non-trade policies, that can facilitate the achievement of those objectives.

This development approach has two steps. Firstly, the poverty reduction strategy is anchored in a national development strategy. Secondly, trade policies are integrated within the development-oriented poverty reduction strategy.

1. The elements of a development-oriented poverty reduction strategy

The basic idea of anchoring a poverty reduction strategy in a national development strategy and thus producing a development-oriented approach to poverty reduction strategy is set out in *The Least Developed Countries Report 2002*. The essence of the approach is that priority public actions within the three-year poverty reduction strategies would be derived from an overall long-term national development strategy. The development strategy contains a long-term vision of national development objectives; the strategic elements required to achieve these objectives and their sequencing; and the policy measures and processes required to achieve the objectives. Within a development-oriented approach to poverty reduction strategies, short-term and medium-term issues of macroeconomic stabilization and improvement of the efficiency of resource allocation would not be ignored. But poverty reduction strategies should be anchored in long-term development strategies rather than being dominated by short-term macroeconomic goals of stabilization together with perpetual economic reform aimed at increasing the efficiency of resource allocation. The approach would seek to achieve substantial and sustained poverty reduction through development rather than to ensure that during stabilization and adjustment poverty is alleviated.

From the analysis in this Report, the basic objective of a development-oriented poverty reduction strategy in the LDCs should be to promote rapid and sustained economic growth in a form that will increase average household incomes and consumption substantially. As shown in chapter 2, part two, in situations of mass poverty, doubling average household incomes and consumption should go a long way to reducing the incidence of extreme poverty by half. This can be achieved through a combination of (i) growth-oriented macroeconomic and trade policies which seek to accelerate the rate of capital accumulation in a sustainable way and relax the balance-of-payments constraint; and (ii) sectorally-focused productive development policies which seek to build productive capacities and accelerate learning through meso-level policies (aimed at specific sectors or addressing intersectoral coordination problems) and micro-level policies focused on enterprise development. These policies need to be applied in a way in which the working-age population becomes more and more fully and productively employed. Policies to prevent intra-country marginalization must also be put in place. These should be particularly aimed at increasing the assets of poorer social groups and also the productivity of those assets, including through agricultural reform, SME development and micro-credit. Micro-export projects can also be used to develop export activities in poor communities. An effective and innovative approach to formulate and implement such projects has been elaborated by the International Trade Centre (ITC) (see box 17).

Poverty reduction strategies should be anchored in long-term development strategies rather than dominated by short-term macroeconomic goals of stabilization together with perpetual economic reform.

Trade policy is an essential and integral component of the whole set of policies that are together designed to achieve the growth and poverty reduction objectives. The other policies are not complementary to trade policy; rather, all complement one another. Trade policy alone is unlikely to be sufficient to meet even national trade objectives. This requires macroeconomic policies that are appropriate (in terms of the level and stability of exchange rates and also interest rates) and sectorally-focused productive development policies (including enterprise development, research and development, and the building of technology capabilities, physical infrastructure investment, human resource development, and financial policy to ensure that enterprises have access to credit).

Trade policy is an essential and integral component of the whole set of policies that are together designed to achieve the growth and poverty reduction objectives. The other policies are not complementary to trade policy; rather, all complement one another.

2. The choice of development strategy

Within this general framework it is possible to envisage different development strategies being implemented. The choice of development strategy is a critical issue as it has very important effects on future poverty reduction prospects. Indeed it is this choice, much more than any poverty-oriented projects, that can do most to ensure that the growth process is broad-based and inclusive. As Adelman (1986) has put it with particular clarity, "If one takes the initial distribution of assets and the structure of institutions as given, the major determinant of the course of income inequality and poverty becomes the overall development strategy chosen" (p. 56).

"If one takes the initial distribution of assets and the structure of institutions as given, the major determinant of the course of income inequality and poverty becomes the overall development strategy chosen"

The reasons why the choice of development strategy is so important, Adelman explains, is that "Each strategy is associated with a special configuration of the structure of production and a particular pattern of factor

Box 17. Micro-Export Projects: The Export-Led Poverty Reduction Progamme of the International Trade Centre (ITC)

In 2002, the International Trade Centre (ITC) launched the Export-Led Poverty Reduction Programme (EPRP). The goal of this programme is to integrate poor communities into international markets. The programme is innovative, with similar potential in the international trade as micro-credit has had in the field of finance.

The EPRP approach rests on two main pillars: (i) the development of the entrepreneurial capacity of the poor with regard to exporting; and (ii) linking that capacity to proven export market opportunities. EPRP projects focus on five sectors based on analysis of demand in regional or international markets and the employment and income-generating potential of these sectors for poor communities. The sectors are:

- Agricultural products (fresh and processed)
- Textiles (fibres and clothing)
- Animal skins leather and leather goods
- Light manufacturing
- Community-based tourism

The viability of proposed projects in the above sectors are assessed via feasibility studies by interested national governments, and together with the ITC, which analyses international market trends, a final project blueprint and action plan is put in place. The feasibility studies address ten key considerations (see box chart 4 below):

1. *Identifying winning products and growth markets.* Projects are selected on the basis of the growth potential of the product in question, and the existence of stable demand for the product. An attempt is made to identify products that can mobilize dormant or under-utilized production capacities by adapting them to the specifications of a clearly identified product-market demand.

2. *Product development, product adaptation, standards and quality.* The product to be exported must be competitive in international markets and meet international quality requirements. The ITC provides technical assistance for this purpose (i.e. assistance at this stage could involve aiding producers in seeking ISO certification, technological support in production and adaptation of the product to the market, or assistance in quality control and packaging). Other examples of assistance are aiding producers with trial orders before a large-scale export order is made to identify and correct any potential problems.

3. *Selecting and organizing poor producers.* The ITC plays a role in ensuring poor producers are organized in some type of network – in cooperatives and other modes – through which they can achieve a sufficient scale to produce, market and distribute their products. In this respect the ITC identifies, trains, and provides funding for local NGOs, whose role would be to build networks/structure the grouping of poor producers, or to ensure increased participation of producers in an existing grouping, in addition to facilitating their training in marketing, production and entrepreneurship. In many countries, groups of export producers have been formed, referred to as "Export Production Villages" (EPVs).

4. *Selecting the right product market for the producer organization.* A key aspect is the ability of the productive organization (poor producers) to sustain production under competitive conditions, as well as its ability to productive organization to meet changing competitive demands. Attention is paid to the strength of the exporter in international markets (see next point).

5. *Linking producers to buyers.* Another crucial element of the EPRP is identifying a "middleman" to link producers and international buyers. This may be an export house, a production house (in the case that products need to be further processed before export) or a producer cooperative, capable of gathering market intelligence and with knowledge of export markets and product requirements. The "export value chain" can take multiple forms, for example, EPVs may export directly or producers may subcontract to other exporters. It is important that there is an equitable relationship between producers and intermediaries/exporters with respect to the sharing of benefits of exporting.

6. *Financing and credit.* Because inaccessibility to credit is one of the major obstacles for small producers to start-up export operations, part of the ITC's role is to find alternative credit sources for EPRP projects, including via formal micro-credit schemes, export-contractors, or other means. The underlying premise is that although government or donor-sponsored funds may be utilized initially, more self-sufficient financing schemes must be set up in the long run to ensure the viability of the project in question.

7. *Human resources.* The development of appropriate managerial skills with a view to making poor producers self-sufficient in the long-run is a key issue addressed via training. The training needs for partners at various levels of the "export value chain" are identified at the outset of the project.

Box 17 (contd.)

8. *Support services*. These are provided by international development organizations, local NGOs, and the private sector. They are necessary to build the capacities of producers and exporters. A needs assessment is done at the outset of the project and adapted throughout the process.

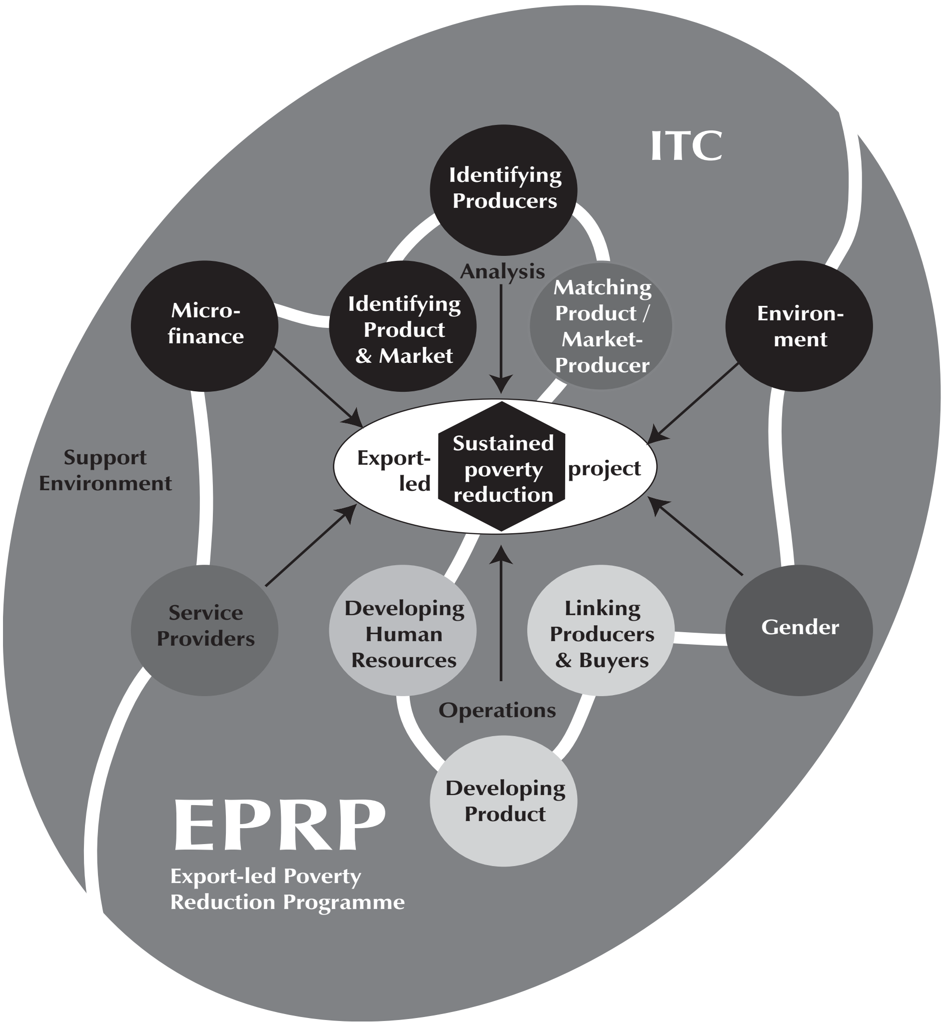
9. *Gender*. Women's participation and their contribution are important considerations in the EPRP.

10. *Environmental considerations*. The production of environmentally friendly products is also considered.

These criteria are not only the "building blocks" of this ITC Programme, but also simultaneously serve to define and guide project benchmarks during the process. For the project to be viable all of the building blocks must be in place. In addition, the entire process is benchmarked, and attention is paid so that it fits the country's national development strategy and priority areas, and that it is complementary to the work of other development partners. Up to the present, the ITC has already launched pilot projects in 11 countries: Afghanistan, Bolivia, Brazil, Cambodia, China, El Salvador, the Islamic Republic of Iran, Kenya, Nepal, South Africa and Viet Nam.

The EPRP is an important initiative due to its potential in enhancing the productive capacities of poor, small-scale producers. The programme also develops networks to share best practice in order to multiply the effects of localized micro-export projects,.

Box Chart 4. The 10 building blocks of ITC's Export-led Poverty Reduction Programme



Source: ITC (2001a); Raghavendran (2003).

use. It is the development strategy that determines the pre-tax, pre-transfer (i.e. the primary) distribution of income. It governs the speed of absorption of labor into the modern sector, the extent of the income gap that develops between the modern and the traditional sectors, and the degree of income inequality within sectors" (ibid.: 56). She continues: "Once the choice of development strategy has jelled, policies and programs aimed at changing the primary distribution of income can accomplish very little. This is true of both transfer programs and poverty-oriented projects. The size distribution of income tends to be quite stable around the trend established by the basic choice of development strategy. Following any intervention, even one sustained over time, the size distribution of income tends to return to the pre-intervention distribution. Only large, well-designed, complementary packages of anti-poverty policies and programs can change the primary distribution of income somewhat; but, to be effective, they must essentially amount to a gradual change in the overall development strategy" (ibid.: 56).

Given the importance of the choice of development strategy for poverty reduction, a critical question facing the LDCs at the moment is what development strategies can be adopted in a newly liberalized open economy and what policies can be adopted to implement such strategies.

3. Post-liberal development strategies

Given the importance of the choice of development strategy for poverty reduction, a critical question facing the LDCs at the moment is what development strategies can be adopted in a newly liberalized open economy and what policies can be adopted to implement such strategies. There is, in short, a need for clear thinking about post-liberal development strategies.[4] These are development strategies that would be pursued after trade liberalization and that can be implemented in an open-economy trade regime in which incentives are biased in favour neither of exports nor of imports and in which there is no discrimination between agriculture and manufacturing sectors.

Export-led growth is one obvious post-liberal development strategy. It is the growth strategy that, in some form or other, implicitly underpins many of the recent PRSPs. But from the analysis in this Report, it is unlikely that an export-led growth strategy in its pure form will of itself lead to a virtuous trade–poverty relationship in the LDCs. In the context of the LDCs, where most of the population lives at or below income levels which are sufficient to meet only their basic needs, export-led growth is generally synonymous with an exclusionary growth trajectory with benefits concentrated in an enclave.

It is possible that a hybrid strategy combining export-led growth with a basic needs strategy is emerging...

Against this background, it is possible that a hybrid strategy combining export-led growth with a basic needs strategy is emerging. Within this new synthesis, the export-led growth part of the strategy is founded on trade liberalization together with deepening "behind-the-border" measures, such as trade facilitation, to tackle internal rather than border constraints on international trade, and also measures to increase the export supply response to trade liberalization. Increased efforts may also be made to foster linkages so that the effects of export growth reach poorer groups and poorer regions. At the same time, the basic-needs part of the strategy focuses on providing basic social services to the population, and ensuring that there is some minimal safety net to offset the worst adjustment costs of trade liberalization for poor groups and also to provide some protection against any increased post-liberal vulnerabilities. This part of the strategy tends to be financed by the LDC development partners. They are allocating development assistance increasingly to meet social expenditure.

This strategy is certainly likely to result in a more positive trade–poverty relationship than in a pure export-led growth strategy. However, it remains to be seen whether it will be sustainable or inclusive. As limited international assistance becomes absorbed more and more in basic needs provision, it is less available for developing the production sectors and private sector development. The great danger of this strategy is that countries will end up with a deepening debt problem. Increased inclusiveness could be achieved through seeking, at the outset, to change the distribution of assets and the structure of institutions. But in the absence of this, transfer programmes and poverty-oriented projects will be working against the grain of the effects of the development strategy for poverty reduction.

...However, it remains to be seen whether this strategy will be sustainable or inclusive.

Some argue that the deficiencies of an export-led growth strategy are so great that there is a need now for "domestic-demand-led development strategies" (Palley, 2002). This view is particularly associated with the conviction that there is a fallacy of composition in the sense that while an export-led growth strategy might work for one country or a few countries, the simultaneous pursuit of export-led growth by many developing countries will lead to adverse terms-of-trade shifts and "diminishing returns to export-led growth" (Blecker, 2002). This Report has not examined this issue, focusing instead on the question of the inclusiveness of export-led growth in the LDCs. However, the analysis in the Report strongly indicates that export growth is important for the LDCs (see also Felipe, 2003). An appropriate approach to achieve a more virtuous trade–poverty relationship may be an open development strategy which seeks to achieve adequate export growth rather than export-led growth (on this idea, see Vos et al., 2004). In an export-led growth strategy export expansion is the major demand-side component of economic growth. By contrast, in a strategy that seeks adequate export growth, both export expansion and domestic demand expansion are important demand-side components of economic growth. There is thus more balance between domestic demand and export expansion in the process of growth.

There are various possible open development strategies in which export growth is an important component but in which there is more balance between domestic demand and export expansion in the process of economic growth.

There are various possible open development strategies in which export growth is an important component but in which there is more balance between domestic demand and export expansion in the process of economic growth. These include but are not limited to:

- A balanced growth strategy based on agricultural productivity growth and export-accelerated industrialization;
- An agricultural-development-led industrialization (ADLI) strategy – which includes infrastructure investment and technological progress in agriculture together with forward linkages into processing activities – with an export component;
- Development and diversification through management of mineral revenues;
- Development of natural-resource-based production clusters;
- A triadic development strategy which includes the promotion of competitive tradables, employment-intensive non-tradables and labour-saving technological change in subsistence-oriented activities.

The key features of these alternative post-liberal development strategies are set out in the annex to this chapter.

4. Policies for promoting development

Whatever strategy is followed, new types of policies will be required in order to promote development in the new open trading environment. A key insight which must be grasped here is that free trade is not the same as laissez-faire. One of the strongest advocates of the benefits of free trade, Jagdish Bhagwati, has emphasized this point, recognizing the effects of distortions or market failures on the case for free trade. He writes that "free trade could not be declared the necessarily best policy for a small country in the presence of a distortion". But "if the distortion was in domestic markets… a domestic policy, suitably designed and targeted to offsetting that distortion, could be combined with free trade to produce the best outcome" (Bhagwati, 2001: 26–27). It is also notable that the most successful experiences of development and poverty reduction in developing countries, namely those in East Asia, have involved a combination of outward orientation with domestic intervention, the latter seeking to support rather than supplant market mechanisms (see, *inter alia,* Bradford, 1994, and UNCTAD, 1994, 1996).

In implementing post-liberal development strategies, public policies in LDCs should use market-supporting mechanisms aimed at market creation, market development and market acceleration.

In implementing post-liberal development strategies, public policies in LDCs should use market-supporting mechanisms aimed at market creation, market development and market acceleration. These policies should not simply provide the right price incentives, but also create the right institutions and the infrastructure necessary for a modern market economy to function properly. The provision of public goods that address the current gaps and shortages in the productive sectors of LDCs is vital. New investment should also be directed towards increasing the absorption capacity of imported technologies and new techniques of production throughout the economies of the LDCs. Infrastructure investment is a particular priority (see Ali and Pernia 2003; GRIPS Development Forum, 2003). A major effort must be made to develop the domestic enterprise sector that is oriented towards production rather than simply exchange. Particular emphasis must be placed on small and medium-size enterprises, and supporting what has been called the "missing middle" in the LDC enterprise structure (UNCTAD, 2001). New market-oriented approaches to agricultural development need to be devised to fill the vacuum left by the dismantling of old commodity marketing boards.

What is promising here is that there are major advances in thinking about new agricultural policies and industrial policies that are market-supporting. With regard to new agricultural policies, Kydd and Dorward (2002) have suggested that in rural areas of LDCs a key focus should be to address coordination failures which are present when the failure of one's own investment is due to the absence of complementary investments by other players at different stages in the supply chain" (p. 9). This involves encouraging appropriate asset-specific investments through institutional arrangements in which the State is a co-equal, not dominant, partner and a much greater role is given to producers' associations and trade associations (see also Kydd, Dorward and Poulton, 2002). There is also now an expanding body of experience regarding policy successes on which new agricultural policies can build (Gabre-Madhin and Haggblade, 2003). In terms of the new industrial policy, a central focus is on building competitiveness through developing more knowledge- and information-intensive systems of production. There is much experience on how the State can animate and guide private enterprise towards the achievement of development objectives, though these approaches have generally not been applied under a free trade regime (see Amsden, 2001). Following the East Asian approach, priority might be given to rationalization and modernization of specific priority sectors in specific contexts (see Ohno, 2003). The example of the cashew nut processing industry in Mozambique offers an example of what needs to be done (see box 18).

Box 18. Is it possible to turnaround the cashew nut processing industry in Mozambique?

The case of the cashew nut processing industry in Mozambique exemplifies the challenge of promoting development in a liberalized trading environment. Following Independence in 1975, the government banned the export of raw cashew nuts to stimulate domestic processing before export. As part of its economic reforms, the Government lifted the ban on exporting raw cashew nuts in 1991/92 and then gradually reduced export quotas and export taxes (see Cramer, 1999). This, together with the liberalization of cashew marketing, was envisaged as a pro-poor trade policy which would increase producer prices and allocate resources more efficiently. Producer prices did indeed rise but the magnitude of the farmers' net gain was very small. Indeed it has been estimated that each cashew growing household gained $5.29 per year, a sum which was equivalent to four days' wages at the minimum Mozambican wage of $1.65 per day (McMillan et al., 2002). But, the newly privatized processing factories were unable to compete at the new liberalized prices and many of them went bankrupt soon after the liberalization. In 1997, these factories employed 10,086 workers. But by 2001 none of the highly mechanised factories were still operational, and the four factories that remain open employed 625 people at full capacity. Factory closures exacerbated a severe unemployment problem in Mozambique.

Can this situation be turned around? Processing – the conversion of the raw cashew nut into a cleaned kernel – is a key activity within the cashew industry's value chain. According to Technoserve (2003), the high quality, semi-finished product can be worth $3,500 per metric ton compared to $400–575 per MT of raw nut. The export of cashew as raw nuts, rather than as kernels, thus represents a major loss of potential employment and income generating added value. Is it possible to promote and expand the higher-value processing component of the cashew industry in the new economic environment?

Amongst possible solutions, Technoserve (2003) argues for a sectoral restructuring programme to address the basic constraint on development of processing activities which is the market-pricing gap. The producers receive prices for their raw nuts that are too low to justify investments in better care of existing trees and/or planting of new trees. Yet at the same time, in order to compete with exporters of raw nuts, the prices being paid by existing inefficient processors are too high for them to make adequate profits and returns on their investments. In this context, Mozambique's entire cashew industry must be restructured if it is to compete successfully in the worldwide cashew business and regain its former leadership position.

In the last four years there have been some new entrants to cashew processing. These are small and medium-scale units located in rural areas. The restructuring process, according to Technoserve (2003) should facilitate this trend focusing on the following issues:

1. Profitability

- Profitability in the cashew industry relies heavily on the quality of the final product (whole and white kernels). This requires improving the procurement process by: (i) identifying good quality nut producing areas, (ii) introducing grading standards and (iii) providing incentives for good quality nut purchase and production.
- Within the production chain it is important to continuously train the workers in order to achieve higher efficiencies and productivity.

2. Producer support

- Processors should identify, and help develop, good smallholder producer associations, and should, on a contractual basis, provide them with technical support thus introducing better cultivation practices.
- Wherever possible processors should support development of community nurseries to provide a ready source of improved seedlings to growers.

3. Processing

- Technical management of processing activities needs improvement in order to meet benchmarking standards by (i) using appropriate processing techniques and machinery to prevent quality loss, (ii) training the workforce to ensure competitive capacity, and (iii) gradually introducing international food processing standards. This requires greater use of technical experts.

4. Marketing

- To help enlarge and consolidate the Mozambican processors' market share, effort should also go into creating a country's brand name for cashew kernels.

Box 18 (contd.)

- The industry should be assisted to introduce second-level processing, thereby adding more value to the product in-country.

5. Financing

- Entrepreneurs (processors) need assistance in securing timely financing to avert delays in purchasing. Effort should go into creating an adequate and reliable credit system based on inventory credit / warehouse receipts in order to supply the whole industry at acceptable conditions.

6. Business plan development

- Processors need help in developing simple clear business plans. This will help introduce sound financial practices and planning and will enable processors to approach financial institutions to secure adequate and timely financing.

7. Policy environment

- The Cashew Business Association should be transformed into an effective forum for solving the problems of private cashew businesses. It should become the opinion leader of the sub-sector, coordinating and making more effective stakeholder influence on the decision- makers.

To succeed in creating an internationally competitive industry, such a sectoral restructuring strategy should be part of a broader development strategy. The international trading environment for cashew nuts is highly imperfect (Cramer 1999), and this may hamper success. But the pressing constraints are within the country. Addressing these will require "a combination of a clear vision, coordination of sector agents, capacity and will to enforce policy change and industry standards, and mechanisms and will to mediate contest and tensions between and within firms " (ibid.: 1262). With such a combination at the sectoral level and also growth-oriented macroeconomic policies, processing cashew nuts could become a key part of an agricultural-development-led industrialization strategy in Mozambique.

Source: Based on Cramer (1999), McMillan et al. (2002) and Technoserve (2003).

D. Mainstreaming trade in development-oriented poverty reduction strategies

1. A methodology for integrating trade in development-oriented poverty reduction strategies

The sustainability of economic growth will be threatened if export expansion is not sufficient to meet the import demand associated with faster growth. This is particularly important in the LDCs because of the import sensitivity of their economies.

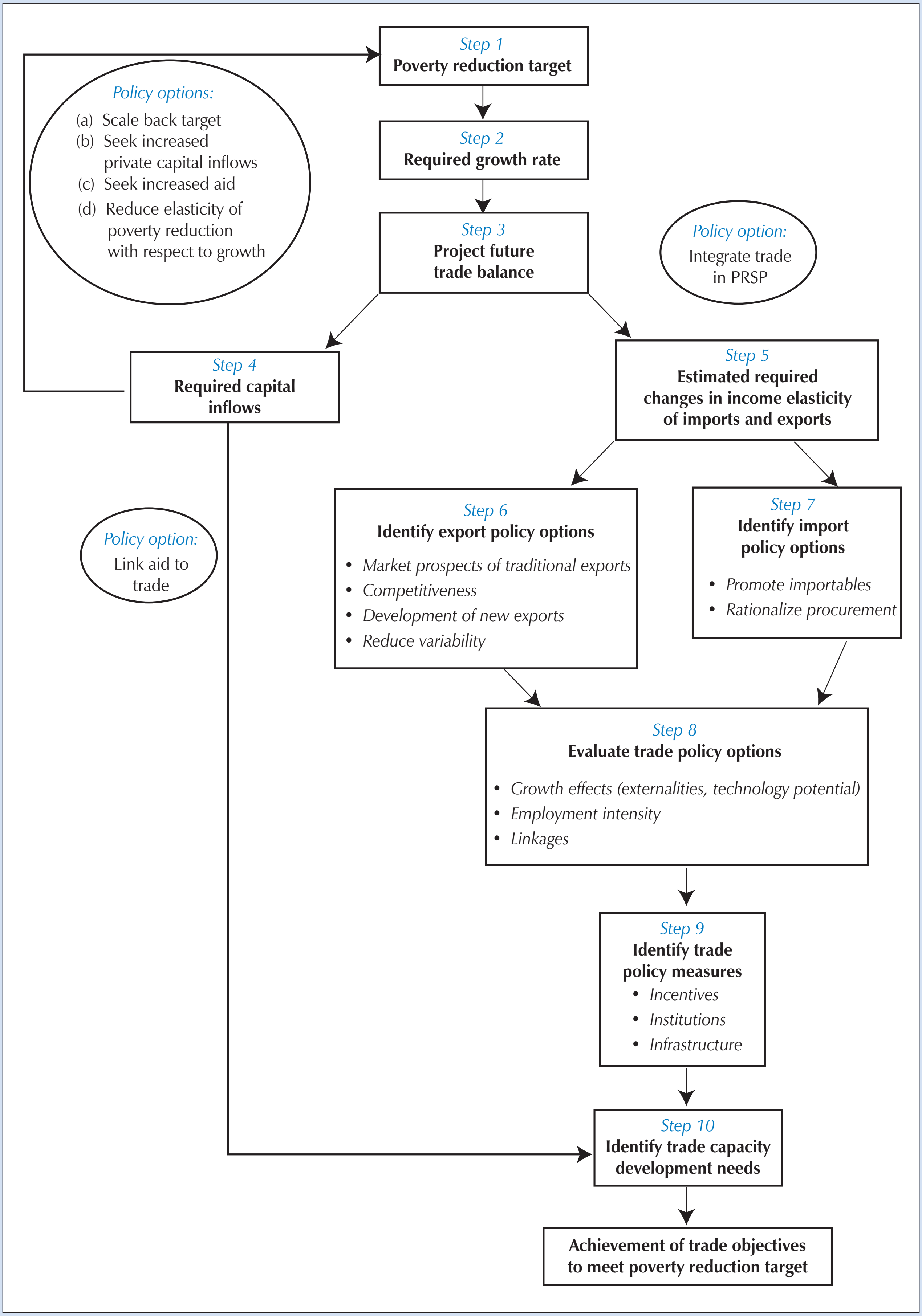
This section sets out a possible methodology for mainstreaming trade policy into a development-oriented poverty reduction strategy or national development strategy. The methodology is based on the view that substantial poverty reduction in the LDCs requires sustained economic growth and that the balance of payments is a major constraint on achieving this. Increased efficient investment, and associated technological change and productivity growth, are the basic source of economic growth. But the sustainability of economic growth will be threatened if export expansion is not sufficient to meet the import demand associated with faster growth. This is particularly important in the LDCs because of the import sensitivity of their economies. Due regard must thus be given to the "foreign exchange productivity of investment" (Hussain, 2001: 95).

The methodology, which is systematized on the basis of a proposal by Hussain (2001), is iterative, as shown in chart 43, but it has ten main steps.

Step one to step four

Firstly, poverty reduction targets are established and an estimate is made of the growth rate required in order to achieve these targets. This estimate requires analysis of the elasticity of poverty reduction with respect to economic growth in the country concerned.

CHART 43. METHODOLOGY FOR MAINSTREAMING TRADE INTO POVERTY REDUCTION STRATEGIES



Secondly, projections are made of the capital inflows which are required in order to meet the target poverty-reducing growth rate. These projections should initially assume no change in the key parameters governing export and import growth in the country concerned. Thus import growth should be projected on the basis of past performance in terms of price and income elasticities of demand for imports. Export growth should be projected on the basis of past trends in export volume and terms of trade. If export expansion is not sufficient to meet the import demand associated with the growth rate, capital inflows are required in order to meet the target poverty-reducing growth rate.

Thirdly, the future financing gap is estimated on the basis of the difference between required and expected capital inflows.

Fourthly, policy scenarios are elaborated to address this financing gap. If trade is not integrated into the poverty reduction strategy, there are four basic policy scenarios:

(i) Scale back poverty reduction targets so that they are "realistic" given likely future trends in private capital inflows and international aid;

(ii) Seek to attract more private capital inflows;

(iii) Seek to attract more international aid;

(iv) Reduce the elasticity of poverty reduction with respect to economic growth.

There are two key parameters that should be the focus of attention: the income elasticity of demand for imports and the income elasticity of demand for exports.

Step five

The policy options can be considerably increased if trade is integrated into the poverty reduction strategy. This is the fifth step in the methodology. Instead of asking "What are the external resources required in order to achieve the poverty-reducing growth target, assuming no change in the trade parameters?", the central question is "What changes in the trade parameters are required in order to achieve the poverty-reducing growth target, assuming no change in the financing gap?"

There are two key parameters that should be the focus of attention: the income elasticity of demand for imports and the income elasticity of demand for exports. The smaller the income elasticity of demand for imports, the smaller the increase in imports which is associated with an increase in national income. The higher the income elasticity of demand for a country's exports, the larger the increase in exports as a result of a given percentage increase in world income. The fifth step concentrates on these two parameters, and estimates:

- The income elasticity of demand for imports that would allow the country to grow at the target poverty-reducing growth rate with no change in the financing gap and no change in export parameters;
- The income elasticity of demand for exports that would allow the country to grow at the target poverty-reducing growth rate with no change in the financing gap and no change in the import parameters.

The first estimate indicates the maximum extent to which the import intensity of economic growth needs to decrease in order to ensure sustainable growth. The second estimate thus indicates the maximum extent to which the responsiveness of national exports to growth in global demand must increase in order to ensure sustainable growth.[5]

With this fifth step, trade issues can now be integrated in the poverty reduction strategy. This can be done by focusing on the identification, formulation and implementation of policies that can reduce the income elasticity of demand for imports and increase the income elasticity of demand for exports in a way that supports the sustainability of economic growth at the rate required to meet the growth target. Policies need to address both the import side and the export side of trade development. In the way in which the policy problem has been stated so far, action on either side is equivalent. But in practice, because some capital inflows are debt-creating and because many LDCs have a legacy of unsustainable external debt, it is necessary to ensure that the rate of export growth exceeds the interest rate on external debt. It is necessary that export expansion be sufficient to meet not simply the import demand associated with faster growth but also the servicing of the external debt. If external indebtedness increases too much, the sustainability of the growth process will be seriously compromised as more and more foreign exchange earnings are eaten up in debt service payments and, in response to increasing indebtedness and associated internal domestic policy problems, capital inflows collapse. This implies that particular attention needs to be paid to exports.

It is necessary that export expansion be sufficient to meet not simply the import demand associated with faster growth but also the servicing of the external debt.

Step six to step nine

The sixth step is to identify policy options for increasing the income elasticity of demand for exports. The analysis here can begin with examination of the demand growth prospects characteristics of a country's major traditional exports. Traditional exports may be defined in various ways, but essentially they denote the major products in the export composition of the country in the recent past. For commodity exporters in particular, these are likely to be low.[6] The next questions that arise are:

- To what extent is it possible to increase the income elasticity of demand for exports through improved competitiveness in traditional exports? In this case, the increase in income elasticity of demand requires that the country increase its share of the global market for its traditional products.
- What new products and sectors can be promoted to increase the income elasticity of demand for exports? In this case, such an increase occurs through changing the proportion of dynamic products in the export composition.
- What new markets can be accessed in order to increase the income elasticity of demand for exports? In this case, such an increase occurs through changing the geographical destinations of exports to more dynamic markets.

The overall aim should be not simply to increase the income elasticity of demand for exports but also to decrease the variability of export growth. This may be a further reason for export diversification.

These questions serve to define trade development goals in terms of competitiveness and diversification. Questions of instability of export growth also need to be considered here. The overall aim should be not simply to increase the income elasticity of demand for exports but also to decrease the variability of export growth. This may be a further reason for export diversification.

The seventh step is to identify policy options for reducing the income elasticity of demand for imports in the same way. The analysis may begin here by determining whether there are any opportunities for efficient import substitution given the costs of producing domestically versus the costs of importing. The poverty-reducing effects of export growth are likely to be enhanced if increases in domestic demand are not met wholly by imports and if there is some import substitution. Particularly important are backward linkages effects from export activities in which local suppliers provide inputs of various types to support export production, and also the activities of domestic SMEs in serving the domestic market, particularly the majority of the population, who are poor and live in remoter regions. Promoting the domestic production of importables in a newly liberalized trading environment is likely to be a considerable policy challenge. Thus, alongside the identification of opportunities for efficient import substitution, policy options for better import procurement practice need to be identified. In the context of the untying of aid, the LDCs need to give particular attention to improving government procurement. This is likely to account for at least 13 per cent of GDP in many LDCs (ITC, 1999) and the limited evidence shows that the figure is as high as 30 per cent in one LDC (Odhiambo and Kamau, 2003). Reducing costs of government procurement can thus have a very high economic pay-off. It is also possible to improve the access of SMEs to government procurement in ways which do not compromise efficiency goals (see ITC, 2000). Joint procurement on a subregional basis may also offer economies of scale.

Poverty issues can be integrated into the analysis by examining the employment intensity of specific export activities and also the linkages that they have with the rest of the economy. The analysis may reveal difficult trade-offs in terms of what is most promising in purely economic terms and what is most promising in terms of poverty reduction.

The eighth step is to assess these policy options in terms of their growth and poverty reduction effects. Thus, for example, the identification of promising export products and sectors would start by taking account of comparative advantage (see Schydlowsky, 1984, and Redding, 1999), and also demand growth prospects in world and regional markets (see, for example, Diao et al., 2003). It would also consider the magnitude of the local value-added, externalities associated with these products and their potential for learning. Poverty issues can be integrated into the analysis by examining the employment intensity of specific export activities and also the linkages that they have with the rest of the economy. The analysis may reveal difficult trade-offs in terms of what is most promising in purely economic terms and what is most promising in terms of poverty reduction. An example of this is upgrading. The demand growth prospects are much higher than those of traditional exports, but the ability of this to generate widespread poverty reduction may be limited. The assessment of these options will also relate to the development strategy chosen.

The ninth step is to identify the specific trade policy measures through which the trade objectives can be achieved. There is an increasing body of knowledge on best practices to promote exports in general (ITC, 2001b), and also non-traditional exports in particular (Helleiner, 2003). There is also wide agreement on best practices to reduce import costs through rationalizing supply and procurement (see box 19). The identification of trade policy measures, as well as the identification of policy options, needs to be done in the context of a durable trade policy framework (see below).

Step ten

The tenth step is to identify priority trade-related capacity-building needs that are required in order to achieve the trade objectives and successfully implement the policy. This is a matter not simply of technical assistance but also of financial assistance. At this point the relationship between capital inflows and trade development objectives is seen as a synergetic mutual interrelationship rather than an arithmetic relationship in which increasing capital inflows reduces the need for the achievement of trade objectives, or vice versa. Capital inflows which help to meet trade-related capacity-building needs help to close the financing gap in the short term but can also serve to reduce reliance on capital inflows, and particularly aid inflows, in the future. Both aid and FDI inflows can

Box 19. Best practices to reduce import costs through better procurement

It is possible to reduce import costs through (i) planning and managing supply, (ii) sourcing and managing suppliers, (iii) evaluating offers and contracts, and contract management, and (iv) logistics and inventory management. The best practices in each of these areas are:

1. Planning and managing supply

- Reduce excessive variety of imported items (through internal standardisation) – thus allowing for consolidation of suppliers, greater leverage in negotiations with suppliers through larger purchase quantities, consequent reduction in unit logistics and inventory costs.
- Apply international/national standards for imported products/services wherever possible — to ensure quality and avoid waste, allow sourcing under better conditions from a wider range of supply alternatives.
- Use performance-based purchase specifications, to the extent possible.
- Apply value analysis/value engineering techniques to specifications for procurement of high value imported equipment and other goods/services (to obtain better value at reduced cost).
- Improve forecasting of import requirements/demand, to reduce oversupply or stockouts, and avoid waste.
- Reduce lead-time for imported supplies through better management, reducing inventory costs and avoiding waste due to obsolescence resulting from changing market conditions/demand.
- Adopt effective supply strategies for imported goods & services, based on careful assessments of supply risks and costs.
- Consolidate requirements & imports (e.g. through group purchasing or purchasing consortia of SMEs) to achieve economies of scale and improve negotiation leverage with suppliers.

2. Sourcing/supply markets/managing suppliers

- Identify and procure from the most competitive sources of supply, breaking away from traditional supply patterns where relevant.
- Understand evolving supply markets, in order to know the best moment to enter the market, avoid supply risks and unforeseen costs, and know how to secure better prices & supply conditions from suppliers, etc.
- Learn to take the best possible advantage of tied aid (wherever this cannot be avoided) by tying oneself to the most competitive source of supply – i.e. first identify the best sources of supply for a requirement, and only then arrange aid financing to procure for it.
- Rationalise the supply base for imported items by consolidating suppliers.
- Carry out careful supplier appraisals, to ensure reliability and lowest total delivered cost.
- Develop long-term supplier partnerships, wherever appropriate.

3. Evaluating offers, contracting and contract management

- Evaluate suppliers' offers on the basis of total cost of ownership / life-cycle cost techniques when purchasing high value items such as equipment – rather than considering just the paying price – in order to better understand and reduce total costs.
- Develop effective negotiation skills in order to obtain the best possible supply conditions for imports and develop win-win relationships with suppliers.
- Apply contractual arrangements (e.g. performance-based contracting) that protect the importer against unforeseen costs and risks.
- Implement effective contract management systems to avoid cost overruns, delays and other problems in importing.

4. Logistics and inventory management

- Organise import logistics arrangements to minimise risks and optimise costs (e.g. through cargo consolidation, effective assessment of shipping alternatives, reducing shipping lead-times, etc.)
- Optimise inventory levels of imported goods to reduce purchase and holding costs through effective demand management, lead-time reduction, and careful assessment of supply risks and required levels of safety stocks.
- Organise efficient in-country logistics, warehousing and distribution for imported goods.
- Use effective IT systems to monitor, control and expedite the logistics process.

Source: ITC (2004).

play an important role in supporting the development of trade-related capacity building. But the former is particularly important in most LDCs given the marginalization in private capital inflows and also the public goods nature of many trade-related capacity-building needs.

2. The importance of improving the trade policy process

The trade policy process needs to include institutional capacities to implement the policy, including clear definition of the roles of different actors and also resources allocated to implement recommended actions.

This methodology is a proposal that may be refined. But to work at all, the methodology needs to be used and refined in the context of an effective trade-policy-making process. The priority here, as the OECD/DAC *Guidelines on Strengthening Capacity for Trade Development* stress, must be to establish a durable trade policy framework through which the trade development interests of a country can be identified and ways to realize them are implemented (OECD, 2001).

According to these Guidelines, the major elements of a durable trade policy framework are the following:

- A coherent trade strategy that is closely integrated with a country's overall development strategy;
- Effective mechanisms for consultation among the three key stakeholders: government, the enterprise sector and civil society;
- Effective mechanisms for intra-governmental coordination;
- A strategy for enhanced collection, dissemination and analysis of trade-related information;
- Trade policy networks, supported by indigenous research institutions;
- Networks of trade support institutions, such as institutions that offer technical assistance on product quality standards, package design consultants, commercial banks and other financial institutions that offer trade credit, freight forwarders and shippers, training institutions, consulting firms and overseas commercial representatives;
- Strong linkages amongst private sector organizations involved in trade;
- A commitment to outward-oriented regional strategies.

A major problem in many LDCs is that the trade policy process works very poorly.

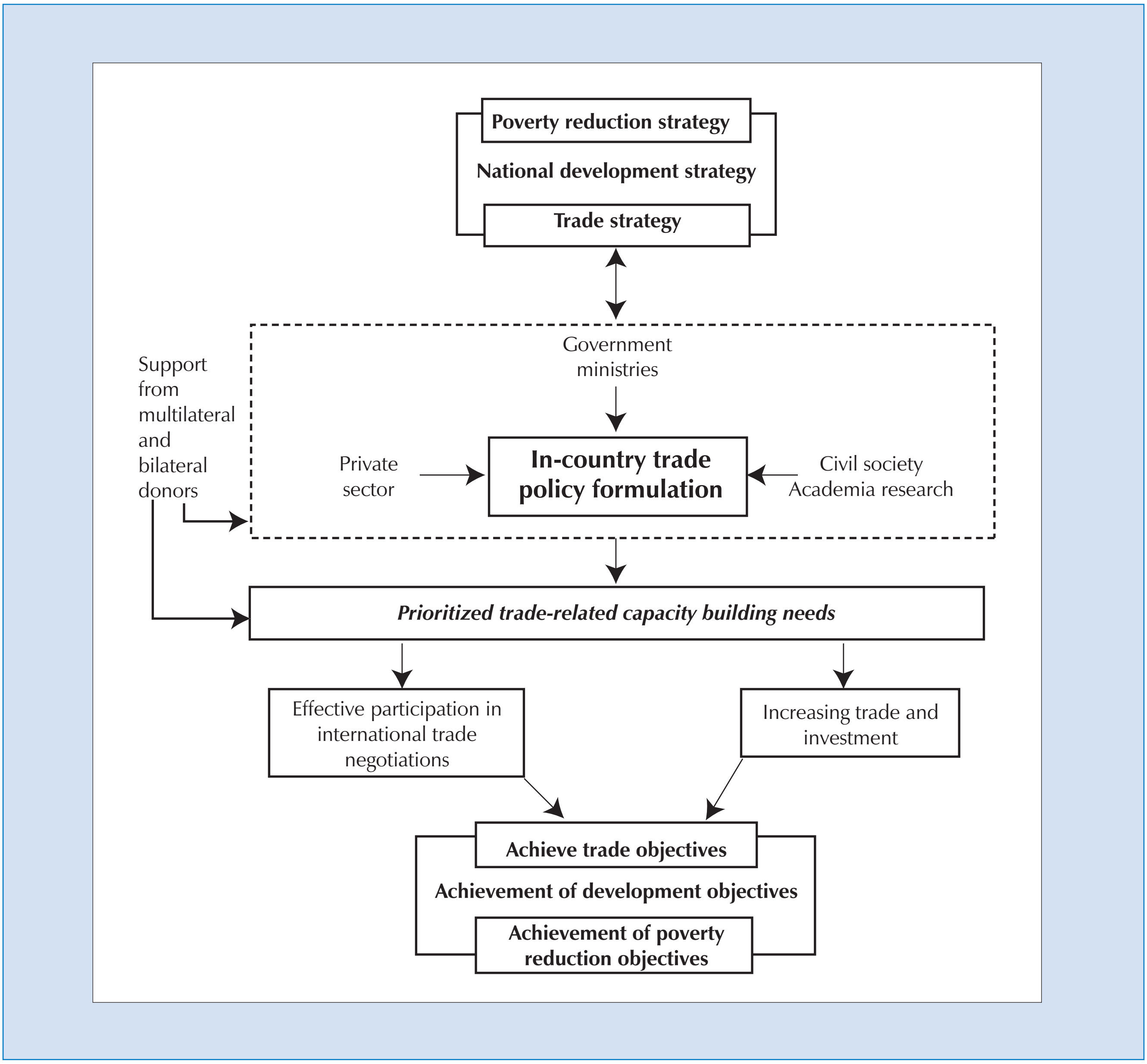
The trade policy process needs to include institutional capacities to implement the policy, including clear definition of the roles of different actors and also resources allocated to implement recommended actions. A major problem in many LDCs is that the trade policy process works very poorly, with deficiencies including a general lack of resources within trade ministries and trade-related institutions; a lack of capacity to identify policy options and assess their relative merits; a lack of coordination within the Government between the trade ministry and the finance ministry and also amongst the various trade ministry and various sectoral ministries; and weak coordination with stakeholders, particularly the private sector. The methodology outlined here provides a basis for orienting discussions with the trade policy process in terms of identifying a country's trade interests and translating these into policies. But without improvements in the whole trade-policy-making process in line with suggested best practices, the methodology is unlikely to work in terms of either better trade policy formulation or implementation.

E. How donors can support trade capacity development

International assistance can play an important role in supporting the achievement of national trade development objectives. It can do this through assistance for trade capacity development, which is defined here, following Solignac Lecomte (2001: 5), as "technical and financial assistance granted by donor agencies to improve developing countries' capacity to trade internationally". As chart 44 shows, this involves two broad types of activity – support to strengthen trade-policy-making and negotiating capacities, and support to build the export base, the competitiveness of exporters and the efficiency of importers.

International assistance can play an important role in supporting the achievement of national trade development objectives.

Chart 44. National development strategy and the trade policy process



Source: Based on OECD (2001) and Prowse (2002).

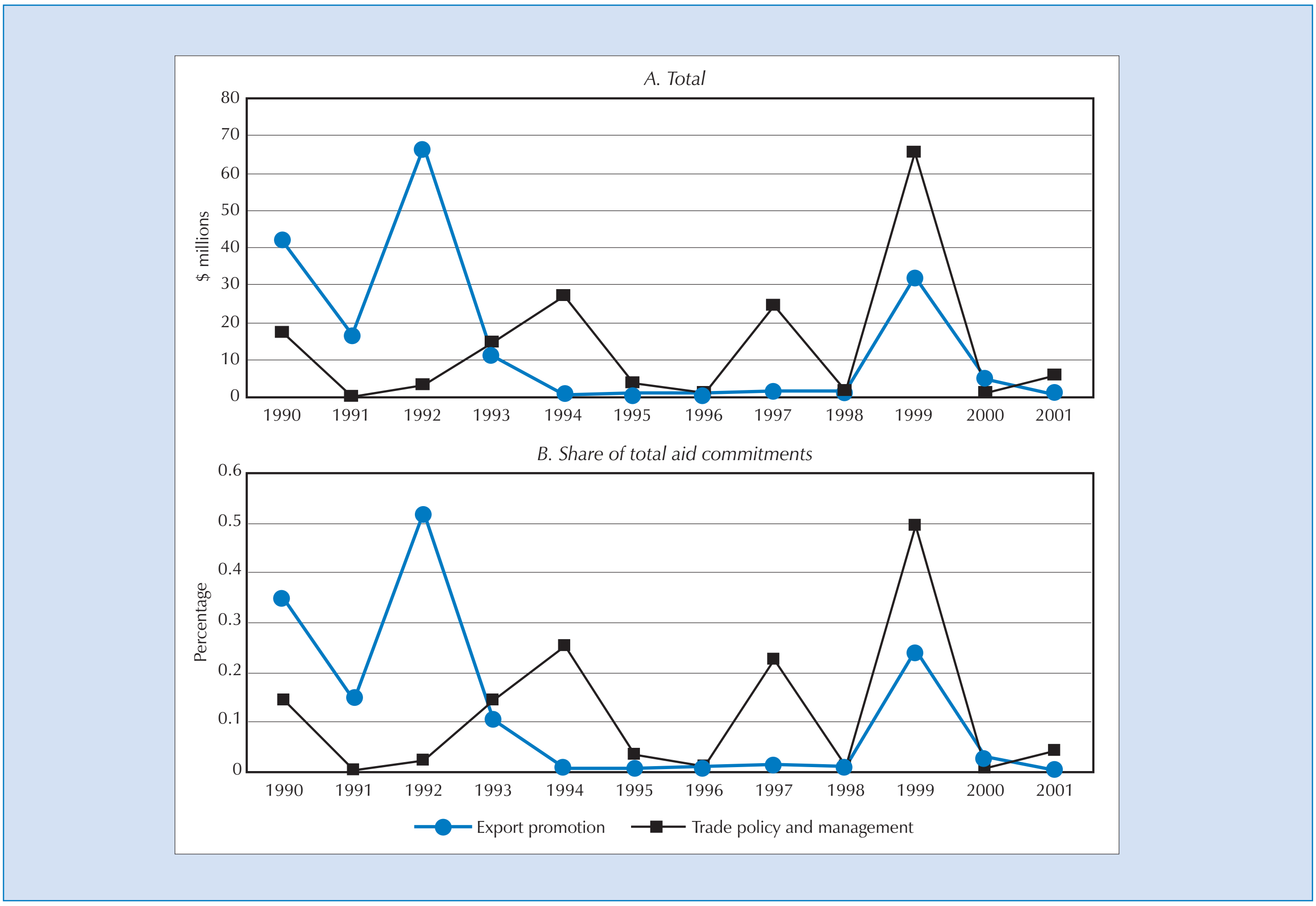
Past trends of aid commitments to the LDCs indicate that assistance for trade capacity development has not been a major donor priority.

This section looks at some general features of international assistance for trade capacity development in the LDCs, including the scale and composition of assistance, some of the risks for donors and recipients which reduce the effectiveness of "aid for trade", the role of the Integrated Framework for Trade-Related Technical Assistance, and the need for increased policy coherence between debt relief and trade capacity development.

1. The scale and composition of donor support for trade capacity development

Trends in international assistance for trade capacity development can be estimated using data on aid commitments to trade policy and administration and to export promotion within the OECD Creditor Reporting System database (CRS). These data should be treated with care as sector-related aid that might also have supported trade development is not included. However, the OECD/CRS provide the best available information on past trends in aid for trade development in the LDCs. This section relies on this source, and also on the new WTO/OECD database, which has been established to rectify data deficiencies, and which provides a more detailed view of international assistance for trade capacity development in the LDCs 2001 and 2002.[7]

Chart 45. Trends in Aid[a] to the LDCs for trade policy and management and export promotion, 1990–2001



Source: UNCTAD secretariat estimates, based on OECD, Creditor Reporting System database (available at http://www.oecd.org/dataoecd/50/17/5037721.htm).

Note: Aid for export promotion and trade policy and management do not include sector-related aid.

a Both bilateral and multilateral aid are included.

Charts 45A and 45B show the trends in total bilateral and multilateral aid commitments to trade policy and administration and export promotion in the LDCs for the period 1990–2001[8] as recorded in the OECD/CRS. During this period, total bilateral and multilateral aid commitments for trade policy and management to all the LDCs was on average $13.8 million per year, which was equivalent to 0.1 per cent of total aid commitments. In 7 of those 12 years aid commitments for trade policy and administration were less than $6 million for all the LDCs. Regarding export promotion, total bilateral and multilateral aid commitments to the LDCs during the period 1990–1999 were on average $17.5 million per year. The latter data series may be somewhat misleading because the problem of sectoral classification of data is likely to be particularly serious.[9] But overall, the past trends of aid commitments to the LDCs indicate that assistance for trade capacity development has not been a major donor priority.

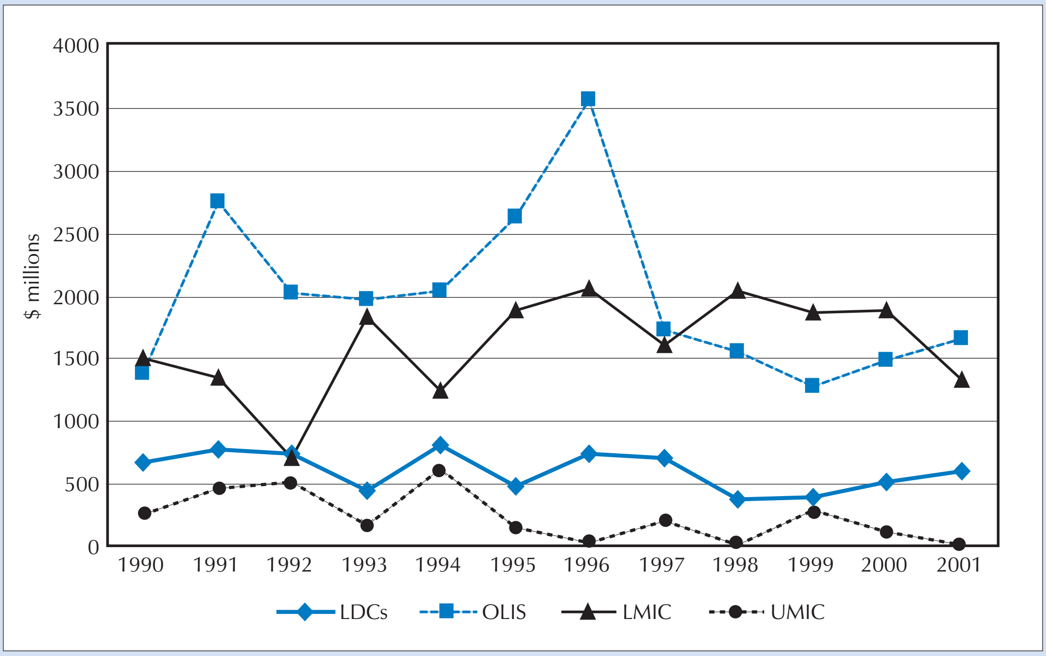
It is vital that the upturn in international assistance following the Monterrey Consensus be also associated with a shift in the composition of aid back towards building production capabilities and not simply meeting basic needs and providing social infrastructure.

It is possible to obtain a wider view by looking at aid commitments for trade-related infrastructure. This is also difficult as there is no agreed definition of what this is. Estimates are reproduced in chart 46 based on a working definition of trade-related infrastructure that includes aid for transport and storage (less education and training in transport and storage) plus telecommunications.[10] It is apparent that aid for trade-related infrastructure to the LDCs, defined in this way, has not changed much in current dollars, although there is a slight tendency towards a decline during the decade. However, in real per capita terms, aid for trade-related infrastructure declined by 43 per cent from 1990 to 2001.

This pattern should be seen as part of a general tendency to decrease the proportion of aid to LDCs going to productive development as more goes to social sectors, and also debt relief and emergencies. As aid inflows declined in

Chart 46. Trends in aid for trade-related infrastructure[a] to LDCs, other low-income countries (OLIS), lower-middle-income countries (LMIC) and upper-middle-income countries (UMIC), 1990–2001

($ millions)



Source: UNCTAD secretariat estimates based on OECD Creditor Reporting System database.

a For a working definition of aid for trade-related infrastructure, see text.

the 1990s there was also a compositional shift away from economic infrastructure and services (particularly transport, and communications and energy) and production sectors (agriculture, industry, trade and tourism) towards social infrastructure. In the early 1980s, 45 per cent of total bilateral aid commitments by DAC member countries to LDCs went to economic infrastructure, production sectors and multi-sectoral and cross-cutting issues was 45 per cent. But in 2000–2002, this had fallen to 23 per cent. In real terms, external assistance to agriculture in the LDCs in the 1990s was half the level it was in the 1980s (UNCTAD, 2000, 2002). It is vital that the upturn in international assistance following the Monterrey Consensus be also associated with a shift in the composition of aid back towards building production capabilities and not simply meeting basic needs and providing social infrastructure. The monitoring of the scale, composition and effectiveness of aid at the recipient country level remains as pertinent as ever.

According to the WTO/OECD database, aid commitments for trade policy and regulation and for trade development were only 0.5 per cent and 1.5 per cent, respectively, of total aid commitments in 2002.

The recently established OECD/WTO database provides a detailed breakdown of aid for trade-related technical assistance and capacity building in 2001 and 2002. This covers trade policy and regulations, trade development, and infrastructure. The latter includes all aid for transport and storage, communications and energy, and no attempt is made to isolate what constitutes trade-related infrastructure. In 2001 and 2002, infrastructure constituted 77 per cent and 81 per cent respectively of the aid for trade-related technical assistance and capacity building going to the LDCs. In 2002, the LDCs received $1.4 billion in the areas of transport and storage, communications and energy, which accounted for 9 per cent of total donors' commitments to LDCs in that year. Road transport is the most important component of infrastructure aid. But it is striking that very little international assistance goes to improving communications infrastructure in the LDCs (see table 59).

According to the database, the LDCs received $159 million for trade policy and regulations in 2001 and $75 million in 2002. The major priorities in 2001 were for meeting technical barriers to trade (TBT) and sanitary and phytosanitary measures (SPS), and in 2002 it was aid for negotiations on Economic Partnership Agreements). The LDCs received $408 million for trade development in 2001, and $249 million in 2002. The major priorities in 2001 were for business support services and trade finance, and in 2002 they were for business support services and market analysis and development in the agricultural sector for trade development.

There have been some positive signs in terms of increased private capital flows to infrastructure in the LDCs, and in some countries this is now a more important source of capital inflows for infrastructure than official assistance.

This new database indicates that the data on aid commitments in the OECD Creditor Reporting System are likely to underestimate aid for trade policy and administration and export promotion. But even with the fuller picture provided by the WTO/OECD database, aid commitments for trade policy and regulation and for trade development were only 0.5 per cent and 1.5 per cent, respectively, of total aid commitments to LDCs in 2002. It is, therefore, important that more priority be given to these activities.

Increased financial assistance for trade-related infrastructure should also be a priority in the LDCs. A major effort must be made in this regard to meet the quantitative targets in the United Nations Programme of Action for the Least Developed Countries for the Decade 2001–2010. But there is little information on the scale of the needs or costs (see, for example, Fay, 2001, and Fay and Yepes, 2003). Table 60 shows that there have been some positive signs in terms of increased private capital flows to infrastructure in the LDCs, and in some countries this is now a more important source of capital inflows for infrastructure than official assistance. But there are limits to the types of infrastructure

TABLE 59. AID FOR TRADE-RELATED TECHNICAL ASSISTANCE AND CAPACITY BUILDING FOR THE LDCS, 2001 AND 2002

	2001			2002		
	$	Percentage of:		$	Percentage of:	
	Thousands	*sub-category total*	*grand total*	*Thousands*	*sub-category total*	*grand total*
Trade policy and regulations	**158 611**	**100.0**	**6.3**	**75 046**	**100.0**	**4.3**
Trade mainstreaming in PRSPs/development plans	11 360	7.2	0.5	3 317	4.4	0.2
Technical barriers to trade (TBT) and sanitary and phytosanitary measures (SPS)	69 599	43.9	2.8	2 206	2.9	0.1
Trade facilitation procedures	51 636	32.6	2.1	10 949	14.6	0.6
Customs valuation	136	0.1	0.0	137	0.2	0.0
Tariff reforms	..	0.0	0.0	49	0.1	0.0
Regional trade agreements (RTAs)	9 682	6.1	0.4	50 350	67.1	2.9
Accession	102	0.1	0.0	472	0.6	0.0
Dispute settlement	4	0.0	0.0	100	0.1	0.0
Trade-related intellectual property rights (TRIPS)	436	0.3	0.0	410	0.5	0.0
Tariff negotiations — non-agricultural market access	108	0.1	0.0	696	0.9	0.0
Rules	111	0.1	0.0	191	0.3	0.0
Training in trade negotiation techniques	1	0.0	0.0	92	0.1	0.0
Trade and environment	482	0.3	0.0	2 068	2.8	0.1
Trade and competition	916	0.6	0.0	510	0.7	0.0
Trade and investment	130	0.1	0.0	300	0.4	0.0
Transparency and government procurement	4	0.0	0.0	198	0.3	0.0
Trade education/training	12 882	8.1	0.5	2 171	2.9	0.1
Trade development	**407 640**	**100.0**	**16.3**	**249 109**	**100.0**	**14.4**
Business support services and institutions	165 857	40.7	6.6	82 407	33.1	4.8
Public–private sector networking	2 032	0.5	0.1	691	0.3	0.0
E-commerce	112	0.0	0.0	1 173	0.5	0.1
Trade finance	134 501	33.0	5.4	39 711	15.9	2.3
Financial policy and administrative management	3 179	0.8	0.1	15 755	6.3	0.9
Formal sector financial intermediaries	117 415	28.8	4.7	18 848	7.6	1.1
Informal/semi-formal financial	13 801	3.4	0.6	4 427	1.8	0.3
Trade promotion strategy and implementation	35 414	8.7	1.4	50 336	20.2	2.9
Agriculture	20 234	5.0	0.8	8 477	3.4	0.5
Fishing	82	0.0	0.0	2 437	1.0	0.1
Industry	14 162	3.5	0.6	22 723	9.1	1.3
Tourism	193	0.0	0.0	15 149	6.1	0.9
Market analysis and development	69 724	17.1	2.8	74 791	30.0	4.3
Agriculture	52 198	12.8	2.1	67 450	27.1	3.9
Fishing	17 257	4.2	0.7	595	0.2	0.0
Industry	238	0.1	0.0	6 192	2.5	0.4
Infrastructure	**1 942 108**	**100.0**	**77.4**	**1 405 020**	**100.0**	**81.3**
Transport and storage	1 096 695	56.5	43.7	610 487	43.5	35.3
Transportation policy and adm. management	87 673	4.5	3.5	110 310	7.9	6.4
Road transport	981 728	50.5	39.1	408 583	29.1	23.6
Water transport	16 074	0.8	0.6	43 632	3.1	2.5
Air transport	2 491	0.1	0.1	42 470	3.0	2.5
Communications	99 681	5.1	4.0	68 058	4.8	3.9
Energy	745 732	38.4	29.7	726 474	51.7	42.0
energy policy and adm. management	262 438	13.5	10.5	158 230	11.3	9.2
electrical transmission	175 523	9.0	7.0	478 176	34.0	27.7
gas distribution	183 000	9.4	7.3	..	0.0	0.0
gas-fired power plants	49 257	2.5	2.0	..	0.0	0.0
hydroelectric power plants	4 226	0.2	0.2	41 013	2.9	2.4
solar energy	30 756	1.6	1.2	2 651	0.2	0.2
Total	**2 508 359**		**100.0**	**1 729 174**		**100.0**

Source: UNCTAD secretariat estimates, based on WTO/OECD database (http://tcbdb.wto.org).
Note: The database has a more detailed classification.

TABLE 60. PRIVATE CAPITAL FLOWS FOR INFRASTRUCTURE AND AID FOR TRADE-RELATED INFRASTRUCTURE TO LDCS BY COUNTRY, 1990–1994 AND 1998–2002

(Annual average, $ millions)

Countries	Private capital flows	Aid flows	Total	Private capital flows	Aid flows	Total
	1990–1994			*1998–2002*		
Afghanistan	-	..	-	14.0	1.5	15.5
Angola	-	42.7	42.7	15.1	10.1	25.2
Bangladesh	23.2	246.8	270.0	76.0	249.1	325.1
Benin	-	33.6	33.6	18.1	38.6	56.7
Bhutan	-	7.0	7.0	-	7.8	7.8
Burkina Faso	-	29.0	29.0	7.3	26.2	33.5
Burundi	0.1	22.0	22.1	3.1	-	3.1
Cambodia	6.0	21.7	27.8	28.4	38.6	67.0
Cape Verde	-	13.5	13.5	-	7.7	7.7
Central African Republic	-	34.3	34.3	-	16.0	16.0
Chad	-	29.7	29.7	2.6	34.2	36.8
Comoros	-	3.1	3.1	-	0.8	0.8
Dem. Rep. of the Congo	-	35.5	35.5	73.9	1.9	75.8
Djibouti	-	14.6	14.6	10.0	3.9	13.9
Equatorial Guinea	-	2.9	2.9	4.4	0.5	4.9
Eritrea	-	0.9	0.9	8.0	0.5	8.5
Ethiopia	-	75.7	75.7	-	161.5	161.5
Gambia	-	7.2	7.2	1.3	0.1	1.4
Guinea	-	39.1	39.1	1.6	13.3	14.9
Guinea-Bissau	-	8.5	8.5	-	4.4	4.4
Haiti	-	11.2	11.2	3.9	0.5	4.4
Kiribati	0.2	1.1	1.3	-	0.1	0.1
Lao People's Dem. Rep.	-	67.0	67.0	27.3	53.6	80.9
Lesotho	-	4.4	4.4	4.7	9.7	14.4
Liberia	-	0.0	0.0	-	0.0	0.0
Madagascar	1.0	37.5	38.5	4.1	56.1	60.2
Malawi	-	27.0	27.0	6.3	33.4	39.7
Maldives	-	3.0	3.0	-	1.2	1.2
Mali	-	32.7	32.7	8.5	28.8	37.3
Mauritania	-	14.4	14.4	19.9	6.3	26.2
Mozambique	-	136.9	136.9	113.5	107.3	220.9
Myanmar	-	0.4	0.4	-	1.0	1.0
Nepal	-	65.1	65.1	19.7	52.0	71.7
Niger	-	3.3	3.3	-	7.4	7.4
Rwanda	-	33.2	33.2	3.1	0.1	3.2
Sao Tome and Principe	-	2.8	2.8	-	1.2	1.2
Senegal	-	29.0	29.0	49.4	49.6	99.0
Sierra Leone	-	26.7	26.7	4.7	0.5	5.2
Solomon Islands	-	5.2	5.2	2.0	1.9	3.9
Somalia	-	4.6	4.6	0.4	0.6	1.0
Sudan	-	8.2	8.2	-	0.0	0.0
Togo	-	7.2	7.2	1.0	3.3	4.3
Tuvalu	-	0.5	0.5	-	-	-
Uganda	0.9	60.3	61.2	39.1	54.3	93.4
United Rep. of Tanzania	0.4	242.3	242.6	64.0	88.7	152.7
Vanuatu	2.2	2.5	4.7	-	4.7	4.7
Samoa	-	8.1	8.1	-	5.2	5.2
Yemen	5.0	29.8	34.8	68.0	12.1	80.1
Zambia	-	34.6	34.6	10.4	36.2	46.6
LDCs	**39.0**	**1 566.8**	**1 605.8**	**713.8**	**1 232.4**	**1 946.3**

Source: UNCTAD secretariat estimates based on World Bank, PPI database (available at http://rru.worldbank.org/PPI/), and OECD Creditor Reporting System database.

Note: For definition of trade-related infrastructure, see text.

investment in which the profit-oriented private sector is interested and thus the need for increased official assistance to meet the major physical infrastructure development needs in the LDCs remains important.

2. Risks and priorities of trade capacity development

Given the major role which trade can play in poverty reduction, there is a strong case for increased assistance for trade capacity development. But analysis of past practice has identified some risks for donors and recipients alike. Solignac Lecomte (2003: 6) identifies the key underlying source of these risks as follows: "As the development objectives of developed countries (as donors) overlap with their commercial interests (as trading powers), they may be prone to decide upon what type of assistance to provide according to their own interests rather than those of recipient countries". On the basis of analysis of the experience of donors and recipients in Africa and the Caribbean he identifies four major risks of trade capacity development:

Mainstreaming trade in aid policies is as important as mainstreaming aid in poverty reduction strategies.

- Negative discrimination. "Donor countries may be reluctant to provide assistance in areas they perceive as being detrimental to their own interests…In the various countries studies, no instance was found of a donor project that promoted trade interests of the recipient country that were diametrically opposed to those of the donor" (p. 17).
- Positive discrimination. "Donors may be tempted to 'positively discriminate' in favour of trade-related assistance which they see as generating benefits for their own economies and firms (e.g. the implementation by developing countries of their commitment under TRIPs) one of the most successful TCD projects in Senegal was the upgrading of fisheries production processes to safety and quality standards imposed by the EU" (p. 17).
- Tied aid. This is falling as a source of risk owing to the implementation of the recommendation that aid to LDCs be untied. But this does not cover technical assistance and "classical aid-tying issues…arise in policy-focused projects involving a high proportion of technical assistance" (p. 17).
- Buy-off in negotiations. "The support granted by donors for enhancing the recipient's negotiating capacity may alter the negotiator's goal and incentives. For any country, effective negotiating capacity means the ability to formulate and defend its own trade interests. Being supported in this by a donor country who happens to be sitting at the same negotiating table (for instance, in the WTO) is a contradiction in terms" (p. 17).

The recommendation that most forms of aid to the LDCs (excluding food aid and technical cooperation) be untied offers an opportunity for a conceptual revolution in which international assistance is not related to the donor's trade development objectives, but rather to the recipient's trade development objectives.

These risks, which are particularly associated with bilateral aid, reduce the efficiency and effectiveness of assistance for trade capacity development from the point of view of the recipient. Another problem that has been identified is the lack of donor coordination. There are also weaknesses in donor capacity. Describing the situation in 2001, Solignac Lecomte states as follows: "Among donors, locally based agencies had very few trade specialists to represent them. Indeed relatively few donors actually engage in trade capacity development projects. If more emphasis were placed on such activities, many agencies would not be in a position to identify and start projects due to inadequate incentives and capacity, especially in the field. Policy-makers in the capitals do not always have access to sufficient trade expertise, whilst the agencies responsible for actually implementing trade policy very rarely have access to such expertise. The tendency of many donors to concentrate on basic needs has reinforced this 'anti-trade bias' " (p. 19).

One implication of this analysis of past practices in trade capacity development is that bilateral aid for trade capacity development might be increasingly channelled through multilateral entities to reduce the risks mentioned above. But in addition to this, it is clear that mainstreaming trade in aid policies is as important as mainstreaming aid in poverty reduction strategies. The recommendation that most forms of aid to the LDCs (excluding food aid and technical cooperation) be untied offers an opportunity for a conceptual revolution in which international assistance is not related to the donor's trade development objectives, but rather to the recipient's trade development objectives.

Trade capacity building should be seen as part of a wider objective of the development of productive sectors and also of private sector development.

Given the weaknesses of the trade policy process in the LDCs, one major priority of trade capacity development should be to foster an efficient trade-policy-making process in which (i) the country's trade interests are clearly identified within an overall development strategy; (ii) these interests are translated into policies and negotiating goals; and (iii) roles and distributed and resources are allocated to implement these policies and to promote these interests (Solignac Lecomte, 2003: 3). The other major priority should be to build up private-sector capacities to export and import efficiently. Poor trade performance is rooted in weak production capacities. Thus trade capacity building should be seen as part of a wider objective of the development of productive sectors and also of private sector development.[11]

3. The Integrated Framework for Trade-Related Technical Assistance

There are some positive initiatives to improve international assistance for trade capacity development. The OECD/DAC has prepared an excellent manual on best practices in trade capacity building (referred to above), which is relevant to both LDCs and their development partners. The OECD/WTO database has been established to provide greater visibility to the scale and composition of assistance. Various donors have also sought to put greater emphasis on rectifying some of the deficiencies noted above.[12] The Joint Technical Assistance Programme (JITAP) has successfully combined a process-oriented approach that brings together a range of in-country stakeholders and three trade-focused international agencies (ITC, UNCTAD and WTO), with an output approach. But the major initiative through which donors are seeking to improve the efficiency of trade capacity development is the Integrated Framework for Trade-Related Technical Assistance (IF).

The major initiative through which donors are seeking to improve the efficiency of trade capacity development is the Integrated Framework for Trade-Related Technical Assistance.

The IF is an evolving initiative of the LDCs' development partners that was introduced in 1997 as a response to the Uruguay Round Decision on Measures in Favour of Least Developed Countries, which called for "substantial increased technical assistance in the development, strengthening and diversification of their production and export bases including those of services, as well as trade promotion to enable them to maximize the benefits from liberalized access to markets" (GATT secretariat, 1994: 441). There is a more complete discussion in *The Least Developed Countries Report 2002*. In brief, however, the first evaluation, completed in June 2000, identified several weakness of the approach at that time: poor links of the process of trade capacity building with overall development strategies, weak ownership, inadequate coordination and inadequate funding. On this basis, it was decided that a revamped IF should be put in place, whose major aim was to help countries integrate trade within their poverty reduction strategies or development strategies.

Chart 47. Integrated Framework process flow chart

Entry process

1. Submission of request and explanatory memorandum by the LDC for inclusion in the IF

2. Technical review of the request by the IFWG on the basis of a technical assessment prepared by the World Bank

3. Consideration of the LDC's request by the IFWG on the basis of the technical review

4. Endorsement by the IFWG / IFSC to officially include the requesting LDC in the IF programme

DTIS process

5. Preparatory mission to the field, normally led by the World Bank, involving close collaboration with agencies and donors to define the scope of the DTIS and to lay down the working arrangements for management of the IF process (e.g. IF focal point, national steering committee)

6. At the request of the LDC, pre-DTIS capacity-building activities may be organized by the IF agencies to increase awareness and understanding of the IF

7. Main mission to the field led by the World Bank with participation of other IF agencies and donors

8. Preparation of the DTIS with the World Bank as the lead agency

9. IF national workshop to discuss the DTIS and Action Matrix

10. After the IF national workshop, the DTIS (including the Action Matrix), reflecting the outcome of the workshop, is finalized and adopted by the Government

Follow-up process

11. Incorporation of policy action in the DTIS Action Matrix into the country's national development plan, such as the PRSP, and identification of donor support for technical assistance needs contained in the Matrix

12. Consultative Group/Round Table meeting, to be complemented by an implementation meeting, as necessary*

13. Implementation of concrete projects by the Government from the Action Matrix involving donors and agencies

*Window II funding is available to bridge the gap between the DTIS completion and the CG/Round Table meetings. During implementation meetings, donors can express their interest in supporting the Government in executing parts of the Action Matrix. Following that, the Government, in consultation with those donors, can start the formulation and execution of concrete projects.

Participation in the IF involves a number of different steps (chart 47). However, the central building block of the whole process is the completion of the Diagnostic Trade Integration Study (DTIS). This study, whose preparation has generally been led by the World Bank, includes the identification of sectors of export potential, supply-side constraints on trade, human and institutional capacity constraints, measures to be taken to implement and apply international and regional trade agreements, and implications of analysis and recommendations for growth and poverty reduction. It also includes an Action Matrix that identifies the trade-capacity-building priorities. The DTIS is discussed at a national workshop by the Government and stakeholders. After this point, the trade-capacity-building priorities should be integrated into the overall national development strategy (or PRSP). Concrete trade-capacity-building projects then must compete with priority projects in other sectors for donor funding.

To finance the activities of the IF itself, a trust fund has been created with two Windows — Window I finances the DTIS, and Window II serves as an interim

TABLE 61. SUMMARY TABLE OF THE IF ACTION MATRICES AS OF APRIL 2004

Priority actions covered in Action Matrix	Burundi *2003*[a]	Cambodia *2001*	Ethiopia *2003*	Guinea *2003*	Lesotho *2003*	Madagascar *2003*	Malawi *2003*	Mauritania *2001*	Nepal *2003*	Senegal *2002*	Yemen *2003*
Macroeconomic policy/institutional support for export development	x	x	x	x	x	x	x	x	x	x	x
Elaboration of a full poverty reduction and growth strategy (integration in the PRSP)	x									x	
Implementation of monetary and fiscal reforms	x	x	x	x	x	x	x	x	x	x	x
Debt management	x						x				
Regulatory environment for investment	x		x	x	x	x	x	x	x	x	x
Improve private/public sector dialogue			x	x	x	x	x	x			x
Trade policy	x	x	x	x	x	x	x	x	x	x	x
Strengthening institutional capacity	x	x	x	x	x	x	x	x	x	x	x
WTO accession		x	x				x		x		x
Tariff and duty drawback and tax reforms	x	x	x	x	x	x	x		x	x	x
Trade facilitation	x	x	x	x	x	x	x	x	x	x	x
Customs	x	x	x	x	x	x	x	x	x	x	x
Procedure	x	x	x	x	x	x	x	x	x	x	x
Governance	x	x	x	x	x	x	x	x	x	x	x
Institutional reform	x	x	x	x	x	x	x	x	x	x	x
Transport	x	x	x				x		x	x	x
Improvement of transit transport	x	x	x	x	x		x	x	x	x	x
Export Promotion/Diversification	x	x	x	x	x	x	x	x	x	x	x
Improvement of supply chain	x	x	x	x	x	x	x	x	x	x	x
Improvement of productivity, quality and standards	x	x	x	x	x	x	x	x	x	x	x
Increase export of non-traditional exports through implementation of a national export promotion strategy	x	x	x	x		x	x	x		x	
Access to credit	x	x	x	x	x	x	x	x	x	x	x
Sectoral priority sectors											
Fisheries		x		x		x		x		x	x
Agriculture		x	x	x		x	x	x	x	x	x
Livestock		x	x			x		x			
Handicrafts				x						x	
Manufacturing			x				x		x	x	
Tea, coffee, tobacco	x	x	x			x	x		x		
Tourism			x	x		x	x	x	x	x	
Electricity/water			x		x		x		x		
Telecommunications					x	x	x				x
Cultural industries		x									
Labour services										x	x
Infrastructure				x	x		x	x		x	
Rehabilitation of infrastructure				x	x		x	x		x	
Establish dialogue with commercial users				x			x	x		x	
New ways of financing infrastructure projects				x			x	x		x	
Poverty reduction			x								x
Connect poor households to local, regional and national markets			x								
Market information, studies on access issues and impact assessment of policy reforms			x								x

Source: Integrated Framework, Diagnostic Trade Integration Studies.
a Year of validation of the Action Matrix.

bridging mechanism for priority capacity-building activities that have been identified in the Action Matrix. As of 31 March 2004, Window I had total pledges amounting to $12.5 million and disbursement amounting to $10.8 million. Window II had total pledges of $8.6 million and total disbursements of $5.5 million.

Table 61 summarizes the activities identified in the Action Matrices of the DTIS of the 11 LDCs that are members of the IF. As of March 2004, one project has benefited from Window II, but a number of projects are under consideration.

In order to ensure that the findings of the DTIS can be taken into account in the design of the PRSP, the timing of the Diagnostic Trade Integration Study should be phased to be at least six months in advance of the completion of the PRSP or relevant Progress Report.

The IF is an important initiative. However, despite the revamping, the LDCs themselves have continued to express concerns about what it has delivered. As the Coordinator of the LDC Group in the WTO put it at the ninth meeting of the IF steering committee on 16 May 2003, “the IF has placed a great deal of emphasis on diagnostic activities, rather than on outcomes”.

As the DTIS is the building block of the IF it is clear that its content is vital for the overall outcome process of trade mainstreaming. As earlier parts of this Report have shown, there is much useful information in the DTIS. But a major difficulty has been the inability to elaborate a methodology that puts the relationship between trade and poverty at the heart of the DTIS rather than as a separate chapter tacked onto the study. In this chapter, this Report has sought to make a constructive response to this problem by suggesting a methodology for integrating trade into development strategies and poverty reduction strategies. It is also recommended that, in order to ensure that the findings of the DTIS can be taken into account in the design of the PRSP, the timing of the DTIS should be phased to be at least six months in advance of the completion of the PRSP or relevant Progress Report.

Another key issue regarding the DTIS as an instrument for mainstreaming trade in the PRSP is the effects that it has on country ownership of national policies. All stakeholders recognize that country ownership of the DTIS is critical for successful mainstreaming. There is no better way of securing commitment by the countries in the follow-up to and implementation of the recommendations emerging from the DTIS.

Developing production and trade capacities of the LDCs will require not only technical assistance but also greatly increased levels of international financial assistance.

Against this background, special care needs to be taken to ensure that the DTIS is carried out in a way that promotes country ownership. It is clear that although some countries have the capacity to assert ownership, others do not and in these cases this capacity would need to be strengthened. The so-called pre-DTIS activities have an important role to play here. Country ownership can also be facilitated by making the establishment of a durable trade policy framework (as defined in the OECD Guidelines on Strengthening Capacity for Trade Development) the basic criterion to measure whether mainstreaming has taken place. This would ensure that mainstreaming is an ongoing and sustainable process rather than a one-shot outcome.

4. Policy coherence between debt relief and trade capacity development

Developing production and trade capacities of the LDCs will require not only technical assistance but also greatly increased levels of international financial assistance. In this regard, it is encouraging that one of the points in the “Spirit of Monterrey” discussion at the Heads of State retreat at the UN International Conference on Financing for Development, held in Monterrey from 18 to 23

March 2002, was "We undertake to assist the world's poorest countries to double the size of their economies within a decade, in order to achieve the MDGs [Millennium Development Goals]". Official capital inflows are likely to contribute the most to this undertaking. However, the potential role of debt relief in trade development should not be ignored. Deeper debt relief can serve to improve the overall investment climate. Moreover, HIPC assistance can provide an additional source of finance for directly building production and trade capacities.

The need for greater policy coherence between debt relief and trade capacity development is all the more pressing because there are 32 LDCs which are HIPCs.

The need for greater policy coherence between debt relief and trade capacity development is all the more pressing because there are 32 LDCs which are HIPCs and, as the representatives of creditor countries agree, "the HIPC Initiative alone will not provide overall debt sustainability for the HIPCs" (World Bank, 2003: 77). The most likely future prospect for many completion point HIPCs, including the LDC-HIPCs, within the next five years is thus likely to be what Edwards (2002) has analysed for the case of Nicaragua, namely "an extremely severe external sector adjustment [which] is likely to require a massive real exchange devaluation [which] in turn will introduce fiscal difficulties in the future" (p. 531).

There is general agreement that debt sustainability depends on economic growth, productive investments and also increasing and stabilizing export earnings through diversified exports.

There is general agreement that debt sustainability depends on economic growth, productive investments and also increasing and stabilizing export earnings through diversified exports. Representatives of the debtor countries themselves argue that the most important risk to achieving the HIPC Initiative objectives is "the need to overcome longstanding vulnerabilities of the HIPC economies" (World Bank, 2003: 75). Dependence on primary commodities, volatile markets and lack of access to key markets are seen as "major impediments to growth and stability in exports", and building resilience to external shocks "remains an important challenge" (ibid.: 75). But because the Initiative has sought not only to enable debt sustainability but also to have a catalytic effect on poverty reduction, HIPC assistance has generally been targeted at social sectors up to now. Thus, for the 13 HIPCs which reached decision point after July 2000 and which had specific numerical targets for how HIPC savings would be allocated, on average 65 per cent of the savings were focused on social sectors, 13 per cent on rural development, 8 per cent on infrastructure, 4 per cent on governance and 2 per cent on structural reforms (World Bank, 2003: 34).

In short, as the evaluation of the HIPC Initiative has concluded, "its design is not consistent with the stated objectives" (World Bank, 2003: 55). In effect, the HIPC Initiative approach has been the channelling of assistance to alleviate the effects of the debt problem, rather than tackling its causes. Certainly, domestic mismanagement played some role in the build-up of the debt. But trade problems are at the heart of the genesis of the debt problem in the case study countries in the World Bank OED Report. As the latter puts it, "Most countries became severely indebted in response to terms of trade shocks and a subsequent decline in revenues, but continued maintenance of overextended public sectors. Their economies were particularly sensitive to export commodity price fluctuations, with adverse weather conditions also playing an important role in the agriculture-dominated economies. The main problem is the high concentration of export earnings in one or a few natural resource or agricultural commodities" (World Bank, 2003: 81).

This Report has established the existence of important indirect links between trade and poverty reduction that work through the development of productive capacities. There is thus no need for development partners to believe that trade development is too far removed from the cutting edge of direct poverty reduction. To the extent that trade issues are included in the PRSPs in a coherent way that links policy measures to strategic goals, there is a strong case for facilitating the wider use of HIPC assistance for the development of productive sectors and for trade development. This would increase the coherence of the HIPC Initiative itself and could contribute additional and perhaps catalytic resources for trade capacity development. But in the end, if countries are not to be left running faster in the same place as before, highly indebted and very poor, there is a need for re-enhanced debt relief and additional international financial assistance provided in a way that is consistent with the development of productive and trade capacities.

LDC Governments can strengthen the links between international trade and poverty reduction by mainstreaming both trade and development into their poverty reduction strategies.

F. Conclusions

The main message of this chapter is that LDC Governments can strengthen the links between international trade and poverty reduction by mainstreaming both trade and development into their poverty reduction strategies. Contrary to common conceptions, trade issues are at the heart of the PRSPs. Export and import growth targets are included in all of them as part of their macroeconomic frameworks, and most also include various trade objectives, such as improved competitiveness and diversification, as well as a range of trade policy instruments, such as infrastructure investment and export promotion. An export-led growth strategy is implicit in many of them. But despite the fact that trade issues are present in the PRSPs, trade objectives and trade instruments are treated in a general way, and there are weak links between strategic goals and priority public actions. This weakness is a general problem with the PRSPs rather than a specific problem of the way in which trade is included in them.

The chapter proposes a methodology for integrating trade into poverty reduction strategies. The methodology focuses on changes in the income elasticity of demand for imports and for exports that are required in order to achieve and sustain growth rates necessary for the poverty reduction target of a country. It also involves analysis of the policy options and instruments to achieve these changes. It is argued that this methodology will only work if there is a durable trade policy framework, including government and the private sector, through which the trade development interests of a country are identified and ways of giving effect to them are implemented. The basic elements of a durable trade policy framework are set out in the OECD/DAC Guidelines on Strengthening Capacity for Trade Development (OECD, 2001).

In an LDC context in which there is generalized poverty and most people live at or below income levels sufficient to meet their basic needs, an export-led growth strategy is not likely to be associated with an inclusive growth process.

The links between international trade and poverty reduction can best be strengthened if a poverty reduction strategy is anchored in a national development strategy. The choice of national development strategy is central to future poverty reduction prospects. It governs such key influences on poverty as the rural–urban income gap, the rate of agricultural productivity growth and industrial employment generation.

The evidence of this Report suggests that in an LDC context in which there is generalized poverty and most people live at or below income levels sufficient to meet their basic needs, an export-led growth strategy is not likely to be associated with an inclusive growth process. Against this background, it appears that a hybrid strategy that combines an export-led growth strategy with a basic needs strategy (focused on providing basic social services) is emerging, with the latter leg of the strategy being met through international financial assistance. This approach, which could be called export-led growth with a human face, is certainly going to lead to a more virtuous trade–poverty relationship. But as limited international assistance becomes absorbed more and more in basic needs provision, it is less available for developing the production sectors and for private sector development. The great danger of this strategy is that countries will end up with a deepening debt problem.

There is a need for alternative post-liberal development strategies. These are strategies implemented in an open economy in which incentives are biased in favour neither of exports nor of imports and in which there is no discrimination between agriculture and the manufacturing sectors.

The Report thus argues that there is a need for alternative post-liberal development strategies. These are strategies implemented in an open economy in which incentives are biased in favour neither of exports nor of imports and in which there is no discrimination between agriculture and the manufacturing sectors. Export-led growth and export-led growth with a human face are two such strategies. But it is also possible to elaborate other strategies which seek to achieve adequate export growth rather than export-led growth. The Report identifies five such strategies:

- A balanced growth strategy based on agricultural productivity growth and export-accelerated industrialization;
- An agricultural-development-led industrialization (ADLI) strategy – which includes infrastructure investment and technological progress in agriculture together with forward linkages into processing activities – with an export component;
- Development and diversification through management of mineral revenues;
- Development of natural-resource-based production clusters;
- A triadic development strategy, which includes the promotion of competitive tradables, employment-intensive non-tradables and labour-saving technological change in subsistence-oriented activities.

These are likely to be relevant in different contexts.

Better national development strategies, increased and effective international assistance and a more enabling rather than more constraining international trade environment together can ensure that the major role which international trade could play in poverty reduction in the LDCs becomes a reality.

New types of development policy are required in order to promote development in the new open trading environment. The commitment to an open trade regime does not necessarily imply the need for laissez-faire within a country. Rather, there is a need for a mixed economy in which there is a balance between the State and the market. Governments should use market-supporting mechanisms aimed at market creation, market development and market acceleration. Domestic policies should be used to address coordination failures and to correct distortions in domestic markets, which in situations of underdevelopment are manifold.

It is important that efforts to integrate trade and development into poverty reduction strategies be actively supported through increased and effective international financial and technical assistance to build productive and trade capacities. An important feature of the way in which the PRSPs treat trade issues is that trade development is closely related to the issue of private sector development, improvements in the investment climate and also the development of productive sectors. This is an important signal from the LDCs to their development partners on the best way to treat trade development in those countries.

The evidence shows that aid for trade has not been a major priority in the past and its effectiveness is likely to have been undermined by biases arising from the overlap between the development objectives of developed countries (as donors) and their commercial interests (as trading powers). Mainstreaming trade into aid policies is as important as mainstreaming trade into development strategies.

Finally, it is important to emphasize that although appropriate national development strategies are a sine qua non for making international trade a more effective means of poverty reduction in the LDCs, success will not be assured unless there are supportive international policies as well. The policy configuration that will do most to strengthen the relationship between international trade and poverty reduction is one which has three pillars. The first pillar is better national development strategies that integrate trade issues as a central component. The second is increased and effective international assistance to build productive capacities and trade capacities, and support private sector development. The third pillar is a more enabling rather than more constraining international trade environment. Together these three pillars can ensure that the major role which international trade could play in poverty reduction in the LDCs becomes a reality.

Annex to chapter 7

Alternative post-liberal development strategies

The five strategies outlined here, which are not exhaustive, underline the fact that there are a number of alternative post-liberal development strategies. As defined in the main text, these are strategies that can be implemented in an open trade regime in which incentives are biased in favour neither of exports nor of imports and in which there is no discrimination between agriculture and manufacturing sectors. This Report does not advocate one over the other. It is up to the countries themselves to decide what is most appropriate for them on the basis of their goals and also an evaluation of both demand and supply constraints on what they are doing. This choice may also lead to the view that what is best is export-led growth or export-led growth with a human face.

1. Balanced growth based on agricultural productivity growth and export-accelerated industrialization

This strategy is the most fully elaborated development strategy outlined here. It is applicable to countries which (i) are predominantly agrarian in the sense that, initially, the majority of the labour force is employed in agriculture; (ii) have a small industrial sector alongside agriculture; and (iii) have surplus labour in rural areas owing to a large labour supply in relation to the available land. The strategy seeks to promote development and poverty reduction through a process of industrialization, linked in a balanced way to the development of the rural economy and agriculture. Over time there is a structural transformation in which the proportion of the working population engaged in non-agricultural occupations increases, and the population of working age becomes more and more fully and productively employed. For sustained growth and substantial poverty reduction to occur, various domestic conditions have to be put in place (see Fei and Ranis, 1997). These are as follows:

- Agricultural productivity must rise at a rate sufficient for the production and marketing of enough food to be able to feed the entire population, including the increasing fraction of the population working outside agriculture. This requires continuous technological progress in agriculture, and institutional and organizational changes, including land reform.
- The growth rate of the industrial labour force must be faster than the growth rate of the total labour force. The growth of the industrial labour force depends on the rate of industrial capital accumulation and the employment intensity of industrial investment, which depends on the rate of technological change and the nature of technological choices, particularly whether innovations have a labour-using bias. The effort which is required, in terms of the rate of capital accumulation and the labour-using bias of innovation, to ensure that sufficient industrial employment is created depends on the rate of population growth. The higher the rate of population growth, the greater the effort needed.
- There must be balance in intersectoral labour markets. The number of new employment opportunities created in industry must be in step with the number of persons released from agriculture.
- There must be balance in intersectoral product markets. The domestic intersectoral terms of trade should not shift against agriculture or industry, and must provide sufficient incentives for farmers to purchase consumer goods and modern inputs, as well as a financial surplus for savings and investment, and real urban wages which enable workers to live at a consumption standard which is slightly above that in rural areas (a condition for labour transfer to occur) but not too high to eat into industrial profits and thus slow the industrial accumulation process.
- There must be balance in intersectoral financial markets. Until the economy's centre of gravity moves to the industrial sector and retained profits of industrial enterprises become a key component of domestic savings, the major source of finance for industrial accumulation must come from the agriculture sector. The intersectoral flow of finance out of agriculture, together with retained profits within the industrial sector, must be sufficient to meet the demand for industrial investment but not so great that it undermines agricultural productivity growth.
- The whole process of balanced intersectoral growth must take place at a rate which satisfies a society's impatience to emerge from generalized poverty. As agricultural productivity increases it may be expected that there will be an upward creep in the basic consumption standard and also in rural incomes and wage rates. But if all the agricultural productivity gains are consumed by farm households themselves, the fraction of the

population employed outside agriculture cannot rise. Increasing real wages and the labour share similarly eats into industrial profits.

In successful cases, international trade, as well as international capital inflows and technology imports, have facilitated the realization of these domestic conditions. In the early stages agricultural exports enable imports of consumer goods, capital goods and raw materials that are necessary for supporting the development of domestic industrial capacities. After an initial import substitution phase, the development of labour-intensive manufactures exports accelerates the process of structural transformation and increase in the proportion of the labour force productively employed outside agriculture. Later on, exports of labour-intensive manufactures support the development of exports of more skill-intensive and capital-intensive manufactures. International trade supports the employment intensity of the industrial accumulation process because capital goods can be imported and thus the establishment of basic capital goods industries, which tend to be more capital-using than labour-using, can be delayed in the early stages of the development process.

This strategy has been the basis for sustained economic growth and poverty reduction in successful industrializing Asian economies with surplus labour. In these cases, the trade policy has been a mix of import protection and export promotion in the context of very gradual liberalization, and this has been linked to proactive guidance of the process of capital accumulation and technical progress within the domestic economy. Amongst the LDCs, Bangladesh may be seen as a successful application of the balanced growth strategy (see Arndt et al., 2002). In this case, too, trade liberalization has been gradual.

2. A strategy of agricultural-development-led industrialization with primary exports

This strategy is an agriculture-first strategy with the added dimension that agro-industrial development is promoted. The major focus of the strategy is a shift in the sectoral emphasis of public investment towards agriculture (Adelman, 1984). This should be directed to improving primary production technology, rural infrastructure and the marketing system. Improvements in agricultural productivity focused on small- and medium-scale farmers should encourage domestic demand for intermediate and consumer goods produced by domestic industry. Improving the productivity of agriculture and letting farmers share in the fruits of improved productivity build a domestic mass-consumption market. In this situation, industrialization can be agricultural-development-led rather than export-led. But the process of agricultural development can be facilitated through agricultural (and agro-industrial) exports.

This strategy is being pursued by Ethiopia, and is written into its PRSP, but there have been mixed results thus far. Analysis has shown that the agricultural-development-led (ADLI) strategy is not subject to a fallacy-of-composition problem (i.e. it works if one country applies it, but not if all countries apply it) and that its realization would yield benefits for rich countries as well as poor countries (Adelman et al., 1989). The relevance of this strategy to sub-Saharan African has been questioned because of the lack of technologies for sustainable high-productivity food agriculture in fragile tropical ecological environments and the expected low responsiveness of domestic manufacturing industries to the expansion of demand associated with agricultural development (Adelman and Vogel, 1991). However, econometric modelling has demonstrated the superiority of the strategy in Mozambique (Jensen and Tarp, 2004). Bhaduri and Skarstein (2003), though not explicitly working on the topic, also set out some conditions for the successful implementation of an ADLI-type strategy.

3. Development and diversification through management of mineral and oil revenues

This strategy is less well defined than the first two strategies, but there is an increasing body of knowledge on best practices for development in mineral- and oil-based economies. The strategy needs to be adapted to the cycle of mineral exploitation. In the early stages, there is rapid expansion of the mining sector and the key issue is to manage Dutch disease effects – the appreciation of the exchange rate and a weakening of the competitiveness of non-mining tradables in agriculture. In early maturity, there is a slowdown in mining expansion and the encouragement of diversification becomes increasingly important. In late maturity, the mineral sector loses its dynamism as reserves are depleted and other sectors take over as the main sources of economic growth (Auty, 1999).

Throughout the process the central issue is the mechanism for the management of revenues from extractive industries. These revenues should be derived from a taxation system which (i) creates sufficient incentive for investors and (ii) secures a fair share of mining revenues for public use. At the macroeconomic level, the objective is to achieve sound and sustainable management of government expenditure and revenues, including mineral revenues. This requires the adoption of sound fiscal rules, the application of conservative price forecasting and the development of a savings strategy aimed at dealing with temporary revenue fluctuations. Earnings stabilization and sterilization are particularly important in economies whose domestic financial market is too small to absorb excess funds and hence to stem Dutch disease effects (Mayer, 1999).

Diversification can be promoted through using part of resource revenues to improve conditions for establishment of new businesses, for example, through well targeted investment in physical and human infrastructure. Experience from Botswana and Chile seems to show that such efforts yield the best results when the new businesses are linked to the mineral sector in a strategy utilizing the dynamism of natural resource based production clusters (see below). This also means that the regional scope of new activities may be quite narrow, and that broader based diversification has to be supported through building of capacity, particularly human capital.

Separating mineral revenue flows from other revenues makes their management more transparent to policy makers, administrators and the public, can assist in the build-up of pressure to spend incautiously. But a non-renewable natural resources fund should function in support of, not a substitute for, good fiscal management. To be transparent, sound and effective funds must be founded upon three broad principles: (i) a consolidated budget framework whereby the fund is channelled through the general government budget and treasury system; (ii) a liquidity constraint on the government budget, implying that assets accumulated in the fund should not be counterbalanced by new borrowings from other sources; and (iii) limits on domestic investment from the fund in order to maintain the fund's objective of savings strategy (Daniels, 2003).

At regional or local levels, development of mineral projects often leads to demand for special fiscal treatment from the community where the project is located and in extreme circumstances these have led to secession movements or civil war. Such demands are also usually rooted in the perception that the economic benefits from mining projects are unequally distributed and reach only a very small portion of the population, while the rest are exposed to negative effects in terms of rising prices, pressure on public services and social problems arising from an inflow of migrants. Regional or local governments can benefit from special expenditure programmes or revenue instruments. Whereas the former better protect fiscal integrity at the national level, the latter provide local communities with a guaranteed source of funds from which to finance investment in public services. However, since mining projects usually do not start paying taxes until several years into operation, whereas expenditure needs arise much earlier, during construction, revenue sharing systems do not fully solve the problem of distribution of revenues. Overall, the need for a consultative and participatory process is at the heart of the matter

4. A development strategy founded on natural-resource-based production clusters

This strategy seeks to promote the development of incipient natural-resource-based production clusters (Ramos, 1998). These production clusters are sectoral and/or geographical concentrations of enterprises engaged in interlinked activities based on the exploitation and processing of natural resources and the related supporting industries. Analysis of "mature" production clusters in countries which are now developed and also rich in natural resources, such as the Scandinavian countries and Canada, makes it possible to identify a typical process of production cluster formation which includes (i) natural resource extraction with little processing; (ii) greater processing before export and also import substitution of some equipment and inputs (typically under licence to the domestic market); (iii) development, alongside unprocessed and processed natural resource exports, of exports of goods and services originally produced for import substitution purposes, usually in undemanding markets; and (iv) all types of goods exported, including more sophisticated processed goods, inputs and machinery for demanding markets, and design, engineering and consultancy services. This whole process takes a long time, as Ramos illustrates with the case of Finland. The development strategy would seek to accelerate it, following the direction of the natural evolution of market forces (ibid.: 124). In this strategy, particular attention needs to be given to activities that might need more foreign direct investment, the identification of key technologies for the development of the cluster and also infrastructural needs in terms of physical infrastructure, human resources, and scientific and technical knowledge.

This strategy has been proposed as being particularly relevant for countries that are rich in natural resources. The resources can be either agricultural or mineral, and so this strategy could be linked to the last two. It has been advocated as being particularly relevant to Latin America (Ramos, 1998). It is also clear that it has played an important role in the development process in South-East Asia, where the Governments of Malaysia and Thailand followed a dual strategy of promoted exports based natural resources and exports based on abundant low-cost labour (Reinhardt, 2000). The Malaysian approach is likely to be particularly relevant to LDCs.

5. A triadic strategy of employment-led growth

This strategy has been proposed as being particularly relevant for LDCs seeking to escape the poverty trap and promote an inclusive development process (Sachs, 2003). The key to inclusive development is not simply higher rates of economic growth but also the maximization of the employment intensity of growth. Financing non-inflationary sustained growth in LDC-type economies depends on the following: increasing import capacity (through export promotion, import substitution and elimination of non-essential imports); an elastic supply of food and other wage goods to meet the increased demand of additionally employed and/or better remunerated workers (through removing institutional obstacles to agricultural development in particular); and increasing domestic savings (which can come partly as a result of a higher rate of overall growth and partly as a result of an increasing share of savings in GNP).

Within this macroeconomic framework, a triadic strategy should be adopted which addresses tradables, non-tradables and also subsistence activities. High priority should be given to consolidation and expansion of tradable sectors. The more labour-intensive these sectors are, the better it is from the point of view of employment generation. But international competition implies that there may be little margin of freedom in terms of choice of technique, and thus growth within the tradable sectors may have a relatively low employment intensity. Thus the second part of the strategy should be to promote all opportunities for employment-intensive growth in non-tradable sectors. These sectors include infrastructure and housing; basic services (education, health, sanitation, communication, post and public administration); technical services, repair and maintenance, and most transportation services; and also perishable foodstuffs and buly agricultural products. These activities do not face international competition and there are thus much greater possibilities for increasing the employment intensity of growth. There are also opportunities to reduce the savings constraint on investment through exploiting "non-investment sources of growth" (such as better utilization of existing productive capacities and improved maintenance of the existing stock of infrastructure, equipment and buildings) and also non-monetary investment (for example, self-help housing in urban centres and creation of simple rural infrastructure through labour). Finally, the third part of the triadic strategy entails rationalizing and modernizing subsistence activities. This is particularly important in an LDC context not because there is a self-contained subsistence sector, but because a large proportion of the total time available for work is devoted to subsistence activities. Technical innovations in subsistence farming, the supply and storage of water and energy, and cooking, to name but a few subsistence activities, can have an immediate positive impact on personal well-being and also release time to devote to other activities.

Notes

1. The notion of "two-way mainstreaming" was proposed by Lakshmi Puri (2003).
2. The projected GDP growth rates over the period 2002–2004 in Mali, Rwanda and Zambia are 9.9 per cent, 10 per cent and 6 per cent respectively, whilst the projected import growth rates are 8.2 per cent, 2.8 per cent and 4.8 per cent respectively.
3. For a lucid discussion of this approach to mainstreaming trade in PRSPs see McCulloch, Winters and Cirera (2001).
4. The term "post-liberal development strategy" is due to Carter and Barham (1996).
5. Estimates for some African LDCs, based on the growth rates required in order to meet the goal of reducing the incidence of poverty by half by 2015, are given in Hussain (2001).
6. For some estimates for Africa see Ng and Yeats (2002).
7. This database is available at http://tcbdb.wto.org
8. The data for 2002 and 2003, although available, were not taken into account because their provisionality may have altered the evolutionary trends of the series.
9. The series for export promotion from multilateral institutions end in 2000.
10. Within the OECD Creditor Reporting System this is defined by codes 210 and 22020 less 21081.
11. This point is also made in OECD/ECA (2003) which in clarifying the scope of trade capacity building states that: "Comprehensive approaches are required which address *trade policy* constraints together with constraints in *producing and getting products to markets*. Trade capacity building must embrace both the short-term WTO negotiating and implementation agendas with the longer-term supply-side development agenda. Trade capacity building should include also the capacity to influence the agenda setting of international trade rules. And it should not focus solely on compliance with those rules, as market access alone has limited benefits if supply-side issues are not addressed. Finally, the focus should be on imports as well as exports. Increased technology transfers via imports of advanced goods and services is itself a form of capacity building."
12. For a summary of recent initiatives see the WTO/OECD database.

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