

Policy Note 1

**Sustained Poverty Reduction Requires
Trade Liberalization and an
Export-Oriented Economic Growth Strategy**

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**SUSTAINED POVERTY REDUCTION
REQUIRES
TRADE LIBERALIZATION AND AN EXPORT-ORIENTED
ECONOMIC GROWTH STRATEGY**

I. Causes of Poverty in Zambia and Requirements for its Reduction

From the perspective of the poor Zambian households, their poverty, or low real income, is due to two overriding factors: 1) inadequate schooling, health and other social services and 2) insufficient productive employment opportunities. So, conversely, sustained poverty reduction requires better health, education and other social services sustained by domestic resources and more productive employment opportunities. Social services are provided for the most part by Government agencies that are themselves strapped for funds. The lack of productive and remunerative employment opportunities can be attributed to 1) not enough new jobs being generated, 2) low returns to farming, and 3) low wages for existing jobs in the rural and informal sectors of the economy where most of Zambian workers are.

Expanded and improved social services require either more government revenue allocated to, or an increase in private ability to pay for, them—or a combination of both. Increasing government allocations of course depends in part on a change in budgetary priorities, more effective tax collection and more efficient government use of available resources, but primarily on higher economic growth to increase the revenue base. Increasing private household ability to pay for services requires higher household income, which must derive from more productive employment—generated also through higher economic growth. Higher economic growth is a *sine qua non* for major improvements in the provision of health, education and other social services.

Creating more productive employment opportunities, on the other hand, requires economic growth of a certain pattern. **More rapid generation of new, productive jobs** requires 1) higher levels of investment in labor-intensive activities with growing market potential, 2) the availability of capital for such investment, 3) appropriate technology to produce marketable products, 4) a conducive, favorable investment climate, and 5) improved marketing information and skills. **Increased returns to farm production** require 1) higher prices for outputs and/or lower relative cost of inputs, 2) a growing demand for farm products, 3) more efficient market institutions and infrastructure, and 4) greater flexibility in meeting changing market demands. **Higher real wage rates** require 1) higher demand for labor leading to reduced unemployment, 2) more productive jobs (as above), and 3) better education and workforce skills (from improved social services). Real wage rates are determined by the labor market and cannot be increased for the country as a whole, no matter how hard the government tries to do so, until unemployment and serious underemployment are reduced to low, transitional levels. Productivity and thus wages for particular individuals or specialized groups, and eventually for the entire labor force, can be improved through education and skill enhancement, if there is a market demand for their services.

II. Export-Oriented Growth is Essential for Sustained Poverty Reduction

An export-oriented policy framework is the only way to achieve broadly based, employment-oriented economic growth that can be sustained at high levels for a long period of time. No other path has proven successful.

To achieve more rapid generation of new, productive jobs, exports tap into world market demand that is growing rapidly and will continue to do so, providing a growing demand for Zambian industrial and agricultural goods and for services (like tourism, which is considered an export of services), thereby increasing productive employment. An export, free market orientation favors Zambia's comparative advantages in land- and labor-intensive production, *for both domestic and export markets*, increasing profit potential and therefore investment in those kinds of industrial and agricultural activities. This increases returns to the owners of land and labor resources—Zambian farmers, farm labor and industrial workers—thus reducing poverty. Enhanced export potential also attracts foreign investment to provide scarce capital and to bring in the technology and training necessary to succeed.

For farm products an export orientation provides growing demand for higher value farm products and food processing, increasing returns to farmers and their workers, thus reducing poverty in rural areas. Furthermore, maintaining an export-oriented, market value of the kwacha in world markets (the real exchange rate) will assure the appropriate kwacha border prices of outputs relative to the kwacha costs of imported inputs. This will raise prices for export crops and encourage domestic production of inputs that Zambians can produce for themselves at lower cost, increasing domestic value added and income, and further reducing poverty.

Regarding **real wage rates**, an export orientation increases the demand for labor, providing more productive jobs both in and out of agriculture, thereby reducing unemployment and underemployment. This eventually causes real wage rates to rise, reducing poverty. Foreign investors also provide skills training and experience which accumulate in the workforce, augmenting government-sponsored training programs to enhance productivity.

Export earnings provide an exogenous income and expenditure stimulus that has a **positive multiplier effect** on the domestic economy. Real economic growth rises by more than the export proceeds alone, as they are spent by the firms and workers who receive them on domestic input supplies and household consumption. This increases the income of many other workers not directly engaged in export production themselves, further raising household income and reducing poverty.

III. Key Elements of an Export-Oriented Economic Growth Strategy

Success of an export-oriented economic growth strategy, and any sustained reduction in poverty, will require Zambia to join the world market economy without reservation. This means 1) trade liberalization (reducing tariffs to a low and uniform rate and eliminating non-tariff barriers to trade)—which benefits Zambia even if undertaken unilaterally, 2) maintaining a market-oriented, freely convertible foreign exchange rate that is allowed free adjustment to differential inflation rates and to changes in market demand and supply between Zambia and its trading partners—thus maintaining a real rate of exchange that will inspire investor confidence more than trying to control the nominal rate of exchange, 3) creating a favorable investment climate for both foreign and domestic investors, 4) export marketing and infrastructure development, including development of internal and external communication and transportation networks, and 5) improved education and skills training.