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# A Review of Methodological Approaches used to Analyse the Impact of Trade Liberalisation on Growth and Poverty in South Africa

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## ABSTRACT

In May 2010, the Department of Trade and Industry finalised its draft Trade Policy and Strategy Framework document, following the release of the 2010/11–2012/13 Industrial Policy Action Plan in February. The publication of both documents has brought the debate about South Africa's trade policy to the fore, particularly in view of the emphasis on a strategic tariff policy informed by industrial policy and directly oriented towards the government's national development goals. While few would disagree that employment creation and poverty reduction are the most pressing of these goals, and that a wide range of economic and social policies are required to address the South African economy's structural problems, the debate on the role of trade policy in this policy mix has been highly polarised.

Disagreement on the impact that trade liberalisation has had on growth, employment and poverty is central to the trade policy debate. This impact has been assessed in South African literature using a variety of methodological approaches, including household and industry-level analyses, case studies on particular sectors, and computable general equilibrium modelling. A critical review of the methodological approaches used to explore the impact of trade liberalisation in South Africa on growth and poverty in particular is preceded by a re-examination of key features of the theoretical debate on trade liberalisation and the controversies surrounding the associated empirical evidence. The appropriateness of the questions and concerns highlighted in the literature on 'trade reform' in South Africa are then considered, in the light of the recent emphasis on using trade policy to meet the country's national and regional development goals.

An important reason for the polarised and ideological debate on trade, growth and poverty has been the persistent view that a 'free trade' system is a relevant benchmark, and argues that the theory and evidence are not as compelling as proponents contend. Instead, alternative scenarios should be evaluated against those that are relevant for industrial and other development goals rather than relative to an unrealistic free trade ideal. In the debate, the broader state of play in multilateral, regional and bilateral trade negotiations and the associated obligations and pressures should also be appreciated.

The dialogue on 'trade reform' in South Africa should move beyond simply characterising the debate as one between 'free trade' and 'protectionism'. The appropriate question is rather how to manage trade sensibly, in order to allow for growth without creating balance of payment difficulties and policy space to promote the structural change necessary to create jobs.


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## ABBREVIATIONS AND ACRONYMS

| | |
|---|---|
| ASGISA | Accelerated and Shared Growth Initiative for South Africa |
| CEPII | Centre d'Etudes Prospectives et d'Informations Internationales |
| CGE | computable general equilibrium |
| DPRU | Development Policy Research Unit |
| dti | Department of Trade and Industry (South Africa) |
| EFTA | European Free Trade Association |
| ERP | effective rate of protection |
| EU | European Union |
| FTA | free trade area |
| GDP | gross domestic product |
| GEIS | General Export Incentive Scheme |
| GTAP | Global Trade Analysis Project |
| IPAP | Industrial Policy Action Plan |
| MFN | most favoured nation |
| MIDP | Motor Industry Development Programme |
| NAMA | non-agricultural market access |
| R&D | research and development |
| SACU | Southern African Customs Union |
| SADC | Southern African Development Community |
| TDCA | Trade, Development and Co-operation Agreement |
| TFP | total factor productivity |
| WTO | World Trade Organization |

## INTRODUCTION

South Africa's Trade Policy and Strategy Framework document identifies the government's major national development goals as, *inter alia*, employment creation, economic growth, poverty reduction, industrial development and restructuring and the promotion of high-value-added exports.[1] Few would disagree that employment creation and poverty reduction are the most pressing of these concerns. There can also be little argument that the structural problems of the South African economy require extensive state intervention through a wide range of economic and social policies. However, trade policy is one area in which the economic and social debate is more polarised. This debate has come to the fore with the release in February 2010 of the government's new Industrial Policy Action Plan and the role envisaged for trade policy.

Central to the trade policy debate is the impact of trade liberalisation on growth, employment and poverty in South Africa. The process of trade liberalisation initiated by the apartheid government in the early 1990s, which accelerated with the post-apartheid government's signing of the Marrakech Agreement in 1994, formal accession to the World Trade Organization (WTO) in 1995 and the implementation of the Growth, Employment and Redistribution Strategy in 1996, has been well-documented.[2] In the 2000s, the stalling of the Doha Round of multilateral trade talks saw further liberalisation take place, primarily as part of negotiated bilateral and regional trade agreements, such as the Southern African Development Community (SADC) free trade area (FTA), the Trade, Development and Co-operation Agreement (TDCA) with the EU[3], and preferential trade agreements with the European Free Trade Association (EFTA) and Mercado Común del Sur (also known as the 'Common Market of the South').[4]

The extent of trade liberalisation in South Africa is the subject of much discussion in the literature. In the past decade, the focus has been on the extent to which protection has in fact fallen in the South African economy, by considering nominal versus effective protection rates, measures of changes in the anti-export bias and the continuing complexity of the tariff structure.[5] While Bell[6] points out that South Africa's liberalisation in the 1990s went well beyond its required Uruguay Round commitments, a dominant strand of the literature in the 2000s concludes with the presumption that the country should not only simplify significantly its tariff schedule, but also unilaterally liberalise tariffs.[7]

The literature on the impact of trade liberalisation in South Africa has focused on the effects of liberalisation on trade volumes, employment, prices and productivity using a variety of methodological approaches.[8] With respect to the impact of trade on poverty in South Africa, the South African Trade and Poverty Project undertook a comprehensive investigation that included industry and household level analyses, sector-specific case studies and a general equilibrium overview.[9] After critically reviewing the methodological approaches adopted to explore the impact of trade liberalisation, in particular on growth and poverty, in South Africa, this research considers whether the literature on 'trade reform' in South Africa is asking the right questions about harnessing trade policy to meet the country's national and regional development goals. Finally, an attempt is made to identify the important policy questions for the country's development path.

## THE IMPACT OF TRADE LIBERALISATION ON GROWTH AND POVERTY

The impact of trade liberalisation on poverty has been analysed through its effect on both economic growth and income distribution. The growth–poverty link has been the subject of much scrutiny, with the argument that liberalisation leads to a reduction in poverty (at least in the long term) being countered by analysts who dispute either the purported influence of trade liberalisation on economic growth, or that of growth on poverty reduction.[10] The income-distribution link, which relates to the view that trade liberalisation lowers inequality both internationally and within developing countries, and can thereby reduce poverty through redistribution, is even more vigorously contested.

In the South African context, such debates are highly pertinent, given the disappointing growth and employment generation since the democratic transition, coupled with rising inequality and the persistence of extreme poverty.[11] Research by the Development Policy Research Unit (DPRU)[12] into recent trends in income inequality underlines South Africa's position as one of the most unequal societies in the world. Furthermore, the research finds that not only has the increasing income inequality eroded the potential for growth to alleviate poverty, but also economic growth has become less pro-poor in recent times.[13] South Africa's continued engagement in multilateral, regional and bilateral trade negotiations makes it appropriate to re-visit the trade, growth and poverty debate and its implications for the role of trade policy in South Africa's national development strategy.

### The static versus dynamic effects of trade

Conventional trade theory distinguishes between the static and dynamic benefits of trade liberalisation. The static gains from trade refer to once-off resource reallocation changes that increase allocative efficiency in an economy, as countries specialise in line with their (static) comparative advantage. These are reinforced by the expected dynamic gains from trade, which include greater competition, technological and knowledge diffusion, as well as higher investment and more rapid capital accumulation.[14] The static and dynamic gains are expected to increase the level and growth rate of income respectively.

However, the restrictiveness of the assumptions underlying traditional comparative advantage theory is well-known. These assumptions include full employment before and after trade, balanced trade and homogeneous products. The first implies no adjustment dislocation for factors of production, the second that the balance of payments will take care of itself as trade flows change, and the third suggests that the type of good a country specialises in is irrelevant.[15] In addition, the static framework by itself cannot explain what will happen to growth per se. Static resource reallocation gains from trade, as measured by the traditional Harberger triangles, have typically been found to amount to 1–2% of gross domestic product (GDP), considered to be insufficient to generate sustained changes in GDP growth.[16] Furthermore, in reality employment losses will offset the welfare gains, expected price benefits to consumers may not be forthcoming and balance of payments difficulties may arise. According to Santos-Paulino and Thirlwall,[17] for example, while theoretically the impact of trade liberalisation on the balance of trade or the balance of payments will be ambiguous (irrespective of the proposed adjustment mechanism),

important output and employment consequences may arise during the adjustment process, particularly in developing countries.

Winters[18] suggests that taking into account welfare rectangles related to rent-seeking, and the impact on consumption and production gains of allowing for imperfect competition, may amplify considerably the magnitude of the static gains from trade liberalisation. However, Ocampo and Taylor,[19] and Chang[20] have challenged the orthodox perspective on the costs of rent-seeking, and the new trade theories based on imperfect competition can just as well provide additional arguments for intervention as reinforcing the case for open trade policies.[21]

When assessing the impact of trade liberalisation on growth, employment and poverty, developing countries must therefore be concerned with the dynamic effects of trade. Benefits may include the potential to take advantage of dynamic economies of scale in a larger international market, which will however entail recognising a dynamic notion of comparative advantage. Using a static conception of comparative advantage to guide specialisation and trade in a developing country may hinder economic development for a number of reasons. These include the lower price and income elasticities of demand for many agricultural and primary goods as well as traditional labour-intensive manufactures, supply instability particularly in the case of agricultural production, adverse terms of trade effects, and a reinforced dependence on developed country trading partners (and the health of their economies) for imports of technology- and skill-intensive products and capital goods.[22]

From a dynamic perspective, the impact of specialisation and export growth, in terms of beneficial linkages and spillover effects between different sectors in an economy, varies significantly across commodities. As Thirlwall and Pacheco-López[23] argue, the type of product in which specialisation occurs therefore makes an important difference, since increasing versus diminishing return activities have quite different output consequences. This view suggests that comparative advantages need to be created and facilitated, which in turn has important implications for trade and industrial policy.[24]

A further dynamic effect of trade is its role in diffusing technology and disseminating knowledge. This aspect is elaborated in 'new' growth theory models, which connect trade and endogenous growth via technological and knowledge spillovers.[25] In addition, other technology models stress linkages between capital goods imports and growth, with some of them suggesting that increased research and development (R&D) activity will follow liberalisation.[26] These new growth models contrast with traditional growth theory that treats technical change as exogenous. For example, in the neoclassical Solow growth model, trade does not affect the steady state growth rate per se, although Winters[27] points to liberalisation's potential impact on transitional growth rates in the move to a higher but parallel growth path. Essentially, though, the endogenous growth models allow for the possibility of permanently higher growth rates as a result of trade.[28]

However, like the new trade theory, endogenous growth theory can provide arguments for protection, for example to stimulate investment in knowledge-intensive industries in order to increase long-run growth rates. In this view, free trade may inhibit growth if it results in the contraction of increasing returns activities or research-intensive sectors, or if it promotes specialisation in lower-technology products than would otherwise be the case. Further, the expected benefits from technological spillovers may not be forthcoming if technology transfer is not simple or if absorptive capacity is weak.[29]

As noted earlier, conventional theory makes the case for trade liberalisation on the basis of both the static and dynamic benefits of trade. There are convincing arguments for focusing on the dynamic impact of trade in developing countries, given the limitations of the static comparative advantage framework for economic growth and development. However, theoretical models tend to provide ambiguous conclusions with respect to the dynamic effects, as evidenced in the literature connecting trade and growth. Deraniyagala and Fine[30] indicate that 'a general feature of conventional arguments on the dynamic effects of trade liberalisation is that they are not located within a coherent theory of industrial performance'. Despite the contributions of new trade and new growth theory to the analysis of the dynamic effects of trade, it is not possible to argue *a priori* that trade liberalisation increases growth rates permanently, or indeed leads to convergence. The implications for analysing the impact of trade on poverty and income inequality are discussed later in this paper. Trade liberalisation has also generated enormous empirical literature that explores the connections between trade, growth, income inequality and poverty. While this entire body of empirical work cannot be surveyed in detail here, an examination of its key features is important to place the discussion on South Africa in context.

### Trade liberalisation, growth and poverty

The empirical literature that relates trade liberalisation or openness to economic performance generates much controversy, as Winters explains:[31]

> The evidence suggests that openness enhances growth, at least over the medium term, but the methodological problems preclude our being wholly certain. Cross-country studies face problems in defining and measuring openness, in identifying causation and in isolating the effects of trade liberalisation. Case-studies avoid some of these problems but cannot confidently be generalised. Attempts to model the links explicitly – specifically to relate productivity to openness – face similar problems of identification but on the whole provide a somewhat more convincing account of the benefits.

Rodriguez and Rodrik[32] extensively criticised earlier cross-sectional studies such as those by Dollar,[33] Edwards[34] and Frankel and Romer[35]. Key difficulties relate to the measures used for liberalisation or openness, the determination of causality and the econometric methodology employed. More recent reviews of empirical work include Thirlwall and Pacheco-López,[36] Deraniyagala and Fine,[37] and Winters.[38] Winters[39] notes the importance of distinguishing conceptually between openness and trade liberalisation, but then appears to equate changes in openness with trade liberalisation, which he later qualifies: changes in openness, measured by changes in the trade to GDP ratio, may actually be generated by or associated with interventionist policies.[40]

Using decade-on-decade changes in the trade–GDP ratio between 1975–79 and 1995–97 to proxy changes in trade policy, Dollar and Kraay[41] attempt to address some of the criticism of the earlier cross-sectional studies. Using this measure, they classify the top third of developing countries in their sample as 'post-1980 globalisers' and the bottom two-thirds as 'non-globalisers'. They find that the 'globalising' group has reduced tariffs by an average of 22 percentage points compared to 11 percentage points for the

'non-globalisers',[42] and show that the 'globalisers' have experienced higher per person GDP growth than the 'non-globalisers'. What is not stated, but is evident from Figures 1 and 2,[43] is that 'non-globalisers' have trade to GDP ratios that are on average more than twice as high in the 1980s and a third higher in the 1990s than those of the 'globalisers'. Furthermore, in the 1980s, the trade-weighted average tariff was about 31% for 'non-globalisers' and just under 60% for 'globalisers'; in the 1990s, the average tariff was about 20% for 'non-globalisers' and about 35% for 'globalisers'. In other words, the average tariff of the 'globalisers' was still 75% higher than that of the 'non-globalisers'. The 'non-globalisers' are therefore 'more open' and have significantly lower average tariffs that the 'globalisers'. The results of this part of the analysis of Dollar and Kraay[44] are therefore somewhat misleading. For example, Kiely[45] notes that poor primary-product exporters with low growth but high and stable trade to GDP ratios will be classed as 'non-globalisers'.

According to Winters,[46] the causation problem (that is, the question of whether trade liberalisation is the cause or the consequence of increased growth) is more severe when trade to GDP ratios are used in the analysis because of potential endogeneity problems, but is also an issue with direct measures of trade policy such as average tariffs. Kiely,[47] Chang,[48] and Wade[49] note how China and India's growth accelerations pre-date much of the move to greater openness, and point out that the wide range of remaining interventionist policies, including high import tariffs, defies the common portrayal in parts of the literature that these two countries are model adherents to Washington Consensus reforms.

The third critique of the cross-country empirical studies on trade and growth relates to shortcomings of the econometric methodologies employed. For example, studies that include countries of widely differing development levels in a single-equation cross-country regression neglect the heterogeneity of the cross-sectional units.[50] Even more sophisticated cross-sectional and panel data econometric studies that address some of the earlier methodological concerns, such as Dollar and Kraay,[51] and Greenaway *et al.*,[52] are subject to more general criticisms about the use of econometrics to explore growth theory.[53]

Winters[54] and Fine[55] discuss the relationship between trade and growth through the impact of liberalisation on productivity growth. As Fine[56] argues, the theoretical connection between static resource reallocation effects and long-term productivity growth is weak in conventional trade theory. The view, that increased competition is sufficient to generate productivity increases and promote technological change, neglects the potential role of imperfectly competitive market structures in stimulating innovation. Nonetheless, large empirical literature exists on trade and productivity growth.

Winters[57] distinguishes between cross-country and cross-sectoral studies for individual countries that address this relationship. A prominent cross-country study by Coe *et al.*,[58] constructs measures of developing countries' access to developed countries' stocks of knowledge in accordance with capital goods imports from the latter. This is in line with the dynamic perspective outlined above, in which the capital goods imports of developing countries are expected to lead to knowledge spillovers and stimulate R&D. Winters[59] notes that, while this measure has been found to have a significant positive impact on total factor productivity (TFP) growth when interacted with openness, the study does not explore alternative potential channels of knowledge dissemination. Other research investigates the impact of trade liberalisation on TFP growth across sectors for individual

countries. A number of these suggest that greater import competition leads to productivity increases, but other sources of productivity increases identified as important include scale economies, cheaper imported inputs and exporting.[60] According to Fine,[61] the extensive empirical evidence for TFP has been mixed. In addition, sectoral studies fail not only to distinguish the impact of macreconomic policy from trade policy influences, but also to control other sources of productivity increase such as those identified above. Firm-level studies have been criticised for not establishing the link to dynamic efficiency gains and technological upgrading.

The discussion thus far suggests that both the theoretical and empirical analysis of the relationship between trade liberalisation and economic growth yield ambiguous results. Trade liberalisation cannot be presumed per se to accelerate growth. The empirical methodologies used to explore this connection have been subjected to severe critiques, and as a consequence, renewed attention has been paid to the advantages of case study analyses and approaches.[62]

The second aspect of the trade, growth and poverty link requiring consideration is the view that growth acceleration, if it does occur, will necessarily result in poverty reduction. Lübker *et al.*,[63] consider in some detail the conclusions of Dollar and Kraay[64] regarding growth and the poor, and particularly their assertion that the basic World Bank policy package will raise growth across countries irrespective of their structural characteristics without having a significant impact on the distribution of income. The empirical work is criticised in terms of the theoretical modelling, serious data flaws and the definition and testing of the policy variables. In particular, the question under investigation – whether the income of the poor rises 'proportionately, less than proportionately or more than proportionately to average income' – cannot be clearly answered using equations that regress a component of an average on the average itself.[65] The econometric methodology and the policy inferences that are drawn from the results are seriously called into question.

Dagdeviran *et al.*,[66] argue that economic growth is at best distribution-neutral and growth on its own provides too blunt an instrument for poverty reduction. To ensure that growth benefits the poor, income- and asset-redistribution policies must be combined with a focus on poverty reduction. Oya[67] notes that, although the linkages between growth, inequality and poverty may be decomposed in the literature, much of the emphasis remains on growth bringing about 'trickle-down' results in the long-term and not sufficiently on redistribution. Most importantly, the effects on and through employment are neglected from both analytical and empirical points of view.

### Trade liberalisation, trade performance and the balance of payments

According to Pacheco-López and Thirlwall,[68] the literature on trade liberalisation and trade performance has tended to focus on liberalisation's impact on the growth rate of exports without considering adequately its impact on the growth rate of imports or on the balance between the two. This tends to reflect the conventional view of a self-adjusting balance of payments or of deficits as a kind of consumption smoothing with no impact on real variables in the long run. However, this view neglects the potentially important impact of liberalisation on the balance of payments and its implications for growth and development.

On the export side, to the extent that trade liberalisation reduces the bias against exports, export performance is expected to improve as a consequence of liberalisation. However, as for economic growth, the step from the effects of static resource reallocation to the impact on the growth rate of exports is not so readily discerned. Empirical analysis of the impact of trade liberalisation on export growth has yielded mixed results depending on the econometric methodology adopted, the measure of liberalisation used, as well as the policy context (and in particular the presence or otherwise of additional export promotion policies) and global economic conditions.[69]

Thirlwall and Pacheco-López[70] surveyed studies of the impact of trade liberalisation on import growth. Empirical work on individual development countries found significant effects on import growth and the income elasticity of import demand. A study by Santos-Paulino and Thirlwall,[71] which considered trade liberalisation's impact on import growth using a panel of 22 countries, found significant increases in import growth and an increase in the responsiveness of imports to domestic income and exchange rate changes. The same panel was used to explore the effect of liberalisation on export growth and the trade balance, as well as the current account of the balance of payments. While import growth increased overall by approximately six percentage points, export growth for the same group rose by two percentage points.[72] The empirical results for the trade balance equations found the trade balance worsened by about 2% of GDP. These findings are consistent with the results of studies by Santos-Paulino,[73] Pacheco-López and Thirlwall,[74] and Parikh.[75]

Thirlwall and Pacheco-López[77] argue that the balance of the empirical evidence indicates that trade liberalisation in developing countries leads to the trade-off between growth and the balance of trade deteriorating. This raises questions about the implications of a balance of payments constraint on growth for development prospects and poverty reduction. While it has been argued that the trade and poverty literature has, in general, neglected this important aspect, the discussion later on trade flows and the balance of payments suggests that a number of South African studies have, by contrast, engaged with this debate quite explicitly.

### Trade liberalisation, income distribution and poverty

As noted earlier, the influence of trade liberalisation on poverty has been examined with reference both to its effect on economic growth and its impact on income distribution, and the trade-growth-poverty link was discussed above. This section looks at the income-distribution link and, specifically, the view that trade liberalisation lowers inequality within developing countries and can thereby reduce poverty through redistribution.[78]

In conventional neoclassical trade theory, the Stolper-Samuelson theorem[79] is used to consider the effect of trade on income distribution within a country. Based on a restrictive set of assumptions, Stolper-Samuelson predict that opening or liberalising trade in an unskilled-labour abundant country will expand production in (unskilled-labour intensive) export sectors and contract (skilled-labour intensive) import-competing production, as a result of relative price changes. In response to accompanying changes in factor demand, the nominal wage of unskilled relative to skilled workers rises, as does the unskilled real wage.[80] Therefore, trade liberalisation in an unskilled-labour abundant country is expected to reduce skilled-to-unskilled wage inequality. The impact on poverty then depends on

whether the incomes of poor households increase above the poverty line as a consequence of the rise in the real wages of unskilled workers.

The shortcomings of this analysis are severe. The adjustment mechanism relies on a long list of orthodox assumptions, including perfect mobility of production factors across domestic sectors, full employment, homogeneous products and constant returns to scale. In addition, non-traded goods and possible missing markets before or after trade liberalisation need to be taken into account.[81] It is also evident that middle-income developing countries like South Africa may be unskilled-labour abundant relative to trading partners in Europe, but skilled-labour abundant compared to key trading partners on the continent. In terms of poverty effects, Winters[82] points out that unskilled workers, engaged in the production of tradables in sectors which expand following trade liberalisation, may be neither the least-skilled workers nor from the poorest households.

Cattaneo and Dodd[83] note that extensions of conventional trade theory can offer insights into the potential poverty effects of trade liberalisation.[84] These include frameworks that allow for sector-specific labour, imperfect markets, increasing returns and transitional adjustment costs. For example, drawing on the specific factors model, households close to the poverty line, which depend on the wage earnings of sector-specific labour in industries that contract following trade liberalisation or experience the loss of a wage-earning job, will be vulnerable. In addition, if food prices increase with trade, the effect on the real earnings of mobile labour owned by poor households could be severe, since the impact on these real earnings depends on consumption patterns in this framework.[85]

The distributional consequences of trade liberalisation have been less extensively modelled in the new trade theory based on economies of scale and product differentiation. Krugman[86] explores some of the distributional implications in a specific-factors model under monopolistic competition.[87] The existence of economies of scale and product differentiation generates intra-industry trade, but net trade based on comparative advantage still exists. As in the conventional specific factors model, the real income of sector-specific labour in the industry with a (net) comparative advantage increases while that of sector-specific labour in the industry with a (net) comparative disadvantage falls. However, a welfare gain to both types of specific labour accrues due to increased variety (provided that the opening of trade is reciprocal). Therefore, both types of labour can benefit from trade, although labour specific to the expanding sector benefits relatively more. The limitations of this approach include its special assumptions, particularly regarding demand for variety which may have limited relevance at very low per capita income levels.

However, from an employment point of view, if intra-industry specialisation follows liberalisation, then adjustment costs may be alleviated, as it is easier to move to different lines of work within the same industry.[88] This argument may have important implications for industrial policy. Work has also been done, which draws on the new economic geography that considers the spatial impact of trade liberalisation within countries. Stevens *et al.*,[89] consider the implications of trade liberalisation on the geographical location of industry and rural-urban inequality and poverty. The impact on real wages once again depends on assumptions made about factor mobility, with lower real returns persisting on the periphery in the presence of immobile factors, which may include labour that is most vulnerable in terms of basic skills.

McCulloch *et al.*,[90] develop a more nuanced conventional framework to analyse the impact of trade on poverty, by recognising the importance of some of the institutional

and social factors neglected by the orthodoxy. The effect of trade liberalisation is analysed through three channels of influence of trade on poverty: the distribution channel (affecting price transmission), the enterprise channel (affecting wages and employment) and the government channel (affecting taxes and government spending).[91] With respect to price transmission, the framework recognises a variety of factors that must be considered when the impact of price changes on households is assessed. Such an approach begins to move away from the orthodox presumption that liberalisation will necessarily benefit poor households via lower import prices. The second channel recognises that the impact of trade liberalisation will be felt through both wages and employment and emphasises the need to explore these effects for those in vulnerable households, where the consequences of the loss of wage employment will be severe. The final channel of influence highlights the effect of trade liberalisation on government revenue via its impact on trade taxes, and the associated implications for government spending. The importance of tariff revenue varies widely, but is a significant concern in many developing countries. In addition, McCulloch *et al.*,[92] consider the degree to which liberalisation 'restricts a government's ability to manage spending and taxation in a way that affects poverty'. The extent to which the current WTO structure constrains the pro-poor and industrial policy is an ongoing debate that has recently been reinforced by concerns regarding pressure on developing countries for deeper commitments in bilateral and regional trade agreements.[93]

Kanji and Barrientos[94] explore a sustainable livelihoods approach to the analysis of trade and poverty, in response to the critique that the McCulloch *et al.*,[95] framework is still too market-oriented, despite its incorporation of imperfect markets, institutions, gender aspects and vulnerability. The livelihoods approach moves away from income- and consumption-based conceptions of poverty to include vulnerability, insecurity, isolation and powerlessness more explicitly. Capabilities and social assets are considered in addition to material assets.[96] The impact or consequences of trade liberalisation are assessed more fully with reference to these factors, rather than simply by looking at outcomes in terms of wages or income measures. Scoones[97] has recently discussed enhancing livelihoods perspectives to ensure that they remain relevant and connected to ongoing 'broad picture' debates on issues such as globalisation and environmental change. He acknowledges the important role such perspectives play in linking the livelihoods of the poor to broader institutional and policy structures, but highlights the need for more analysis of political and power relations and how these are determined by dominant economic processes. For example, the sensitivity of peasant livelihoods in Southern Africa is a strong reason to reconsider the wisdom of further trade liberalisation.

It is evident from this discussion that a complete assessment of the distributional and poverty consequences of trade shocks needs to move beyond the confines of orthodox trade theory and its basic extensions. What is required is to recognise institutional and social factors and a broader conception of poverty, as well as issues of power and politics. In light of the diverse theoretical perspectives discussed in this section, it is unsurprising that empirical research on the trade, inequality and poverty connection has yielded widely varying results. While it is evident that the poverty rate may fall even as wage and income inequality increase, a growing body of empirical evidence calls for greater recognition of the importance of income distribution in the analysis of the impact of trade liberalisation on poverty. Some of the findings of this literature include a greater responsiveness of

poverty to income distribution than to growth, and a lower growth elasticity of poverty in the presence of high or rising income inequality.[98]

Thirlwall and Pacheco-López[99] have surveyed recent evidence on trade liberalisation and income inequality in developing countries. Significant literature now suggests that, contrary to traditional trade theory's predictions, the trend towards greater skilled-to-unskilled wage inequality in many developed countries is also evident across a broad range of developing countries.[100] Cornia and Court[101] report that income (as opposed to just wage) inequality is rising from already high levels in most of Latin America and parts of Africa, and inequality has sharply increased in China. A comprehensive survey by Goldberg and Pavcnik[102] points to increasing inequality within developing countries across a wide range of measures, while Milanovic[103] finds that the income share of low- and middle-income groups is adversely affected by greater openness. It is evident that the impact of trade liberalisation on poverty will be more complex and ambiguous once the effect on inequality is properly considered.

## EMPIRICAL METHODOLOGIES TO ANALYSE THE IMPACT OF TRADE LIBERALISATION

As noted previously, the literature on the impact of trade liberalisation in South Africa has focused on the effects on trade volumes, employment, prices and productivity using a variety of methodological approaches. The impact on poverty specifically has been explored through the South African Trade and Poverty Project, which involved industry and household level analyses, sector-specific case studies and a general equilibrium overview.[104] This section will critically review the methodological approaches adopted to explore the impact of trade liberalisation in South Africa on growth and poverty in particular, with reference to the earlier theoretical and empirical discussion.

### Partial equilibrium approaches

Any review of empirical research on trade liberalisation in South Africa dating back to 1994 is complicated by the fact that the democratic transition was accompanied by a wide range of policy changes and the country's reintegration into the international community. For example, many studies on price or employment changes in a partial equilibrium context did not explicitly include trade liberalisation or openness measures, but tended to attribute certain trends implicitly or explicitly to liberalisation, despite the numerous other policy changes that took place concurrently in the 1990s.[105] More recent studies have incorporated tariff protection measures that have generated significant debate, and problems remain with the sensitivity of results to the tariff data used (despite significant improvements in the last five years) and the choice of the import price index in particular.

### Effective rates of protection and the anti-export bias

The effective rate of protection (ERP) has been widely used to measure the overall structure of protection for a sector's output by taking into account the nominal tariff on the final good as well as the nominal tariffs on inputs into the production of the final

good. In South African literature, the concept has been used to explore the extent to which South Africa has liberalised its trade since the early 1990s,[106] as well as in econometric work on the impact of trade liberalisation on trade flows and the balance of payments.[107]

Holden[108] has argued that the extensive use of ERPs in the South African literature has ignored the serious limitations of the concept as a trade policy measure. Edwards[109] reinforces this view in a critique of how the concept has been measured and interpreted in the studies of Fedderke and Vaze, and Rangasamy and Harmse.[110]

According to Greenaway and Milner,[111] the theoretical critique of the ERP concept is related primarily to the problem of 'drawing general equilibrium inferences from a partial equilibrium measure'. The substitutability and scale problems of ERPs limit their predictive content, making it problematic to draw inferences about resource pulls as ERPs change and, in particular, calling into question their use as a trade policy measure in econometric estimations of the impact of trade liberalisation. Deraniyagala and Fine[112] explain that the same ERP in two different sectors may reflect quite different underlying input and final good tariff structures. A change in the tariff structure may thus cause entirely different changes across the economy depending on the relevant demand and supply elasticities, with different value-added consequences:[113]

> it is erroneous to presume that shifts in effective rates of protection act in a relatively uniform, linear fashion within economic sectors, simply serving to shift output marginally in unambiguous directions in response to the induced raising or lowering of prices. This takes no account of the competitive structure of industries and the role of strategic behaviour (by both domestic and foreign firms), for which differential pricing in export and domestic markets can be crucial in the presence of economies of scale and scope, and market imperfections.

The South African literature has also extensively used anti-export bias measures, in which changes in the anti-export bias are analysed to draw inferences about the effectiveness of trade liberalisation as a means of improving the country's export performance. In empirical work on South Africa's export performance, Edwards and Lawrence[114] recently used the concept, constructing a measure of the implicit export tax resulting from tariff protection on inputs. The export tax variable captures 'the proportion of value added at world prices lost by domestic exporters to higher input costs associated with tariff protection'.[115] The anti-export bias is then calculated using the export tax variable and the ERP. Two problems with these measures can be highlighted. The first is that the anti-export bias concept could be subjected to a similar set of criticisms as the ERP. The second is that the impact of export and related incentives should be included in measures of the anti-export bias in the economy.[116] Some of these export promotion polices have significantly affected the incentive structure in South Africa.

### Trade flows and the balance of payments

Edwards and Lawrence[117] explore the impact of trade liberalisation on trade flows and the trade balance in South Africa. As noted earlier, the relative size of such impacts has important implications for the ability of developing countries to grow rapidly without encountering adverse balance of payments difficulties. This aspect has often been neglected in empirical work on the impact of liberalisation on trade and growth.

On the import side, the econometric estimations are conducted for aggregate merchandise imports using quarterly data for the period 1962 to 2004.[118] The tariff protection measure is the collection rate including import surcharges, which were particularly significant during the serious balance of payment problems of the mid- and late-1980s. As expected, import volumes are found to be strongly affected by trade liberalisation from 1991. Some uncertainty apparently surrounds the question of whether the import price variable is inclusive of tariffs or not,[119] which would presumably have important implications for the results and requires further clarification. The use of an alternative import price series was found to render the coefficient on the tariff variable insignificant.

Edwards and Lawrence[120] analyses the changes in the composition of trade flows at the manufacturing sub-sector level for exports, but not for imports. Imports are considered separately only in the aggregate and enter into the trade balance panel estimation at the sector level, net of exports. However, if (as the aggregate results for imports suggest) imports are going to respond substantially to investment changes, then a sectoral analysis needs to be included on the import side as well as the export side. This type of analysis could also feed into studies that focus on the employment consequences of the changing patterns of trade, which are a key concern in the South African literature.

The export side of the analysis by Edwards and Lawrence[121] explores the growth and composition of South Africa's manufactured exports since 1990. While it is evident that export growth occurred contemporaneously with tariff reduction, the relative importance of trade liberalisation and other policies such as the General Export Incentive Scheme (GEIS) and the Motor Industry Development Programme (MIDP) has been the subject of some debate in the literature.[122] The relative impact of GEIS for the period 1990–1997 needs to be more explicitly recognised and analysed. For the late 1990s and 2000s, a detailed assessment of the impact of specific sector programmes on export growth, and in particular the importance of linkages to sectors that have benefited indirectly from programmes such as the MIDP, is required. Black and Roberts[123] highlight the need for an even more disaggregated analysis of export performance at the sector level, given the heterogeneity of sectors such as machinery and equipment. A significant proportion of the exports of this sector relate to the auto industry, while such linkages have also strongly influenced the growth of leather products and engineering textiles (seatbelts and airbags). According to Black and Roberts,[124] 'the MIDP ... underpins improved export performance across manufacturing, including machinery and equipment, leather products, and rubber products, in which auto components dominate export performance'. They argue, that by requiring firms to increase exports progressively in order to obtain a given level of duty-free imports, the programme encourages firms to act to ensure supplier competitiveness and stimulates the development of a supply chain that includes foundries and plastics industries, with positive consequences for product development and productivity.

In light of this discussion, even if trade liberalisation stimulated export growth in the 1990s and early 2000s, it is hard to see how the static resource reallocation effects of further unilateral liberalisation could, on their own, generate the kind of export dynamism required to accelerate export growth substantially in South Africa. It is also important to emphasise that the export markets themselves are not assured and depend on a host of complex factors and conditions abroad. The results of Edwards and Lawrence's[125] import estimations suggest that a GDP growth rate of 6%, as targeted by the Accelerated and

Shared Growth Initiative for South Africa (ASGISA), would be associated with an import growth rate of approximately 8%, which implies that an export growth rate of more than 8% would be required to reduce South Africa's current account deficit. While the capital account surplus has thus far expanded to accommodate the deficit, South Africa may be vulnerable to a balance of payments constraint on growth.[126]

### The benefit-incidence of tariff liberalisation and employment effects

Edward and Lawrence, Daniels and Edwards, and Pauw *et al.*,[127] recently addressed the question of whether South Africa's current tariff structure contributes to poverty. Essentially, the poverty argument is that the tariff structure is inefficient, as higher prices make consumers at all income levels worse off, and this inefficiency disproportionately affects the poor.[128] The obvious flaw in this argument is that 'while the possibly lower prices resulting from import liberalisation will tend to benefit those fortunate enough to keep their jobs, the net effect on the working class is likely to be negative'.[129] This criticism is important because the partial equilibrium simulations show that tariff reduction would cause significant job losses.[130] The counter-argument has two parts: first, job losses will not have a large effect on poverty because only a small share (<20%) of the income of the poor comes from employment in tradeable sectors;[131] second, the loss of consumer surplus outweighs the value of jobs saved.[132] Essentially, this literature argues that poor people are more sensitive to the price effect of the tariff structure (i.e. consumer surplus losses) than the employment effect (job losses).

However, evidence reviewed by Cattaneo and Dodd[133] suggests that the expected benefits of liberalisation for consumers in terms of lower prices have not necessarily been forthcoming. Various reasons for this relate to the more open trading environment, even though they may not be attributable to trade liberalisation per se. Important factors include exchange rates, world price fluctuations of key foodstuffs and the effect on efficient domestic producers of exposure to competition from subsidised overseas production. The analysis should factor in the reality experienced by many South Africans of the loss of wage employment in the face of rising international food prices.

A useful starting point is to account explicitly for job losses and weigh such job losses against consumer surplus gains. However, a number of questions need to be raised at three levels of analysis. Firstly, the interpretation of any set of employment/consumer surplus results, in particular the impact of employment changes on poverty, is critical, while the conclusion that job losses would not have a major impact on poverty needs to be interrogated. Secondly, the detail of the partial equilibrium framework needs to be questioned. For example, assumptions made about supply elasticities and export demand elasticities are often unavoidable, but the results and policy inferences drawn from them should be qualified accordingly. Similarly, the estimations are based on an assumption of perfect access to export markets and, as such, take no account of limitations to and difficulties associated with such access. In addition, the disaggregated results again suggest that much of the consumer surplus gains comes from a few industries (including motor vehicles).

A final point of overriding importance is that, even taken at face value, these estimates do not suggest that trade liberalisation (or partial liberalisation) per se can be a major force for poverty reduction and employment creation. This raises the third set of criticisms,

which relate to the partial equilibrium framework itself. The implicit assumptions are about the industrial structure that underlies the partial equilibrium approach and that the only policy alternative involves further liberalisation of trade. The former assumption is illustrated in Edwards and Lawrence's[134] example of uneven protection of South African fruit farmers, which assumes that liberalising trade in fruit would necessarily benefit downstream producers in the canning industry. However, it does not take into account the possibility that the canning industry would not survive if domestic fruit production collapsed. Cattaneo[135] highlights the importance of geographically discrete integrated production chains, which may also be of significance in the Southern African regional context.[136]

### Computable general equilibrium modelling

The use of increasingly sophisticated computable general equilibrium (CGE) models have addressed some of the criticisms of partial equilibrium approaches to analysing the impact of trade liberalisation. Such models allow for the estimation of the impact of alternative multilateral, regional and unilateral liberalisation scenarios on, *inter alia*, welfare, output, trade flows, prices, and consumption, and have increasingly been used in policy analysis in developing countries. CGE macroeconomic modelling exercises are often complemented by the use of partial equilibrium models or (more recently) CGE micro-simulation models that provide finer detail on poverty and distributional aspects of the liberalisation impact.[137] While a detailed technical analysis of CGE modelling is beyond the scope of this paper,[138] an attempt will be made to highlight some of the advantages and controversies surrounding the way such modelling is used in the study of trade liberalisation impacts on growth and poverty.

The multi-sector, general equilibrium framework of a CGE model may be multi-region or country-specific, allowing for the analysis of interactions between sectors within an economy as well as (for global models) international linkages.[139] The advantage of these models is that they are able to utilise huge datasets to provide quantitative estimates of the effects of liberalisation and the resulting interactions that take place within an economy. Key weaknesses are that the results critically depend on the quality of the data used and on the modeller's assumptions, particularly with respect to the closure rules.[140] Although the critique about data and assumptions is also applicable to most of the partial equilibrium approaches discussed above, the CGE modelling approach is so complex and sophisticated that policy advice emanating from such work is often subject to less critical scrutiny and so is more open to abuse or special agendas. This state of affairs is exacerbated if the assumptions are not made explicit when the results are reported and are not subjected to sensitivity testing. Replication investigations should also be conducted on the results.

According to Sandrey,[141] a key point of departure is whether CGE modelling is appropriate even in a given context, as simpler data analysis techniques may yield better insights than an inappropriate model. Mabugu and Chitiga[142] suggest that CGE modelling is most suitable where indirect effects are likely to have a significant impact on resource reallocation. A number of global CGE models now exist such as the Global Trade Analysis Project (GTAP) model (developed at Purdue University), the Modelling International Relationships in Applied General Equilibrium model (developed at the Centre d'Etudes Prospectives et d'Informations Internationales – CEPII), the World Bank LINKAGE model

and the Michigan world production and trade model.[143] In order to compare results across some of these models (which differ in their structure, assumptions, model parameters and data), attempts have been made to harmonise the dataset on which the simulations are based. According to Ben Hammouda and Osakwe,[144] the Market Access Map database is now used for modelling work using GTAP, LINKAGE and CEPII models.

An important development is that the modelling process allows for intra-group variation in responses to trade liberalisation or other policy changes. CGE modelling that aggregates across households and treats all households in a given income category as homogeneous cannot adequately capture the distributional and poverty consequences of trade policy changes. To address this deficiency, CGE micro-simulation models have emerged. The procedure is then either to have a CGE macro model and a micro model with household data operating in sequence, or to combine the two by including the household data in the CGE model.[145] Then, typically, poverty measures and inequality indices are constructed for the poverty and distributional analysis, using CGE results on households.

Mabugu and Chitiga[146] stress that a major controversy over the use of CGE modelling concerns the selection of the closure rules for the model. This essentially relates to which variables are to be considered exogenous or endogenous and what assumptions are made about how markets adjust. A common assumption is that product markets are perfectly competitive, but much variation and controversy surround the closure rules that are specified for the labour market. The rule chosen has significant implications for the findings concerning the employment and wage effects of trade liberalisation. The balance of payments closure chosen is also important. For example, the current account may be treated as exogenous (and the exchange rate allowed to adjust) or the opposite closure may be applied. Indeed it is recognised that 'the choice of closure determines the results of CGE models'.[147]

An additional problem concerns the estimates adopted for key elasticities in CGE models. These parameters may be derived econometrically, but such estimates are often themselves criticised for the underlying estimation methods. Alternatively, elasticities may be drawn from other empirical studies, or the general literature, which could be inappropriate or ad hoc. Ben Hammouda and Osakwe[148] specifically criticise the use of Armington elasticities[149] as key parameters in CGE modelling work on most African countries because of the model's underlying assumption regarding countries' abilities to influence prices.

Other factors that are not accounted for by CGE modelling processes are export market access issues, the balance of power in trade negotiations and strategic behaviour between countries and firms. Static models neglect adjustment, and inappropriate assumptions are generally made regarding the revenue impact of liberalisation. Ben Hammouda and Osakwe highlight the critical importance of trade tax revenue in many African countries and, in light of empirical evidence to date, question the assumption that domestic sources of tax will readily be able to replace trade tax. Applying CGE models to trade liberalisation tend to abstract from this important issue by holding government revenue constant through changes in domestic taxes.

Despite these serious criticisms and limitations, two important developments should be highlighted with respect to CGE modelling of the impact of trade liberalisation in South Africa. The first is the increasing use of micro-simulation models in conjunction

with macro CGE models to analyse the distributional and poverty impacts of trade liberalisation. An example is the work of Hérault (2006, 2007), discussed by Mabugu and Chitiga.[150] Although the CGE macro model is static, alternative closures are run that include one neoclassical and two Keynesian closures. Overall poverty incidence is found to decline, but inter-group inequality rises across simulations. Compared to earlier, static approaches, the advantage of this modelling work is that it makes greater use of micro-household survey data.

The second important development in CGE analysis in South Africa is the emergence of the use of dynamic CGE models, which address some of the shortcomings of the static modelling framework. For example, Thurlow[151] has employed a sequential dynamic CGE model to explore poverty and distributional effects arising from simulations of the impact of trade liberalisation on growth in South Africa, and has further explored whether a differential impact exists by gender. The results suggest that growth has accelerated due to trade-induced technological change, although the incidence of poverty has only fallen marginally and inequality has worsened.[152] While emphasising that caution is needed when using the results of CGE modelling to develop policy, these findings reinforce the view that growth on its own has been insufficient to address South Africa's major poverty and employment challenges.

## TRADE POLICY AS A COMPONENT OF SOUTH AFRICA'S NATIONAL DEVELOPMENT STRATEGY

The literature on trade liberalisation in South Africa has a marked lack of consensus on a number of fronts, including the extent of trade liberalisation (particularly in the 1990s) and the way in which trade liberalisation has driven or contributed to trade flow patterns and trends in employment, consumer prices, inequality and poverty since 1994. The release of the 2010 Industrial Policy Action Plan (IPAP) and the Trade Policy and Strategy Framework document has heightened the debate about South Africa's trade policy direction, given the objective of following a strategic tariff policy, informed by industrial policy and the government's national development objectives. This objective stands in stark contrast to the view that remains in a dominant strand of the South African literature: that the government should commit itself to further unilateral tariff reductions.

The perspective that South Africa should unilaterally liberalise its trade further appears to rest on the view that the country's growth in non-commodity exports has in large part been due to trade liberalisation, and that additional liberalisation will significantly increase such export growth further.[153] However, at the same time, the most favoured nation (MFN) tariff liberalisation stalled in 2000, and attempts to pursue a strategic tariff policy are likely to be administratively too complex and captured by industry lobby groups.[154]

Edwards *et al.*,[155] note that South Africa's current MFN tariff levels are below average compared to other middle-income countries and have declined to a similar degree since 1994. They argue, nonetheless, that South Africa's MFN tariff liberalisation has stalled since 2000 and only modest liberalisation has been pursued in the past decade, primarily through trade agreements with the EU and SADC. However, it should be emphasised that South Africa's imports from the EU, EFTA and SADC together accounted for about 40% of South Africa's total imports in 2008.[156] By the end of the TDCA implementation period

in 2012, approximately 86% of South Africa's imports from the EU will be liberalised, and by 2015, the tariff phase-down for the Southern African Customs Union (SACU) EFTA free trade agreement will be completed. Under the SADC FTA, imports from SADC already enter largely duty-free into South Africa.[157] In addition, the 2009 WTO Trade Policy Review of SACU found that the tariff structure was simplified further between 2002 and 2009 (such as the decrease in non-ad valorem tariff lines from 25% to 3.2%) and the simple average tariff rate fell 3.3 percentage points (both overall and for manufacturing).[158]

South Africa is apparently in line with other middle-income developing countries regarding its current MFN tariff levels and preoccupation with negotiating preferential trade agreements in recent years. The latter aspect obviously needs to be seen in the broader context of the problems of the Doha Round of multilateral trade negotiations, and not as peculiar to South Africa. Indeed, a consequence of the Doha Round impasse is a trend to pursue regional and bilateral trade and investment agreements.

Edwards *et al.*,[159] characterise South Africa's pursuit of preferential trade agreements as 'a mechanism to complement multilateral agreements through securing market access', and as the reflection of 'a strong mercantilist ethos amongst bureaucrats in the ministry of trade and industry'. They argue that, in the case of the FTA with the EU, South Africa's interests were 'also driven by the desire to send out a positive signal to investors about South Africa's commitment to trade reform and to address broader development issues including aid and support for industry'. Apart from the apparent contradiction in these statements, in response to the first, the general trend towards the negotiation of preferential trade agreements may reflect the current and ongoing failures of the multilateral process. Indeed, such failures at multilateral level may be seen largely as a consequence of the generalised mercantilism most evident in the EU and the other 'majors' at the WTO.[160] In addition, a growing literature is analysing the extent to which North–South regional and bilateral trade negotiations are being used to obtain deeper obligations for intellectual property and investment policy from developing countries, in exchange for increased market access. Industrial policy space, which would still be available under WTO obligations, is thus being closed off to developing countries.[161]

Against the background of the current failure of the Doha Development Round, developing countries are seeking other platforms from which to pursue their development strategies. In this context, the South African literature has seen a revival of debates on the developmental state,[162] which could provide an opportunity to move away from discussing matters such as the extent to which South Africa liberalised its trade in the 1990s and 2000s and being preoccupied with detailed debates on alternative trade liberalisation measures that are based on inappropriate underlying assumptions. Although the release of the 2010 IPAP was accompanied by press reports on the possibility of either a uniform or an irrational case-by-case reversal of previous tariff cuts, most commentators have a more nuanced view of IPAP when read in conjunction with the 2010 Trade Policy and Strategy Framework document.[163] In light of South Africa's national development goals and the linkages between trade, growth, inequality and poverty, the relevant question for South Africa is 'what system and rules of trade are best for economic development and poverty reduction?'[164]

Part of the answer is that the system must allow space for creating dynamic comparative advantages in developing countries, and hence strategic trade and industrial policies. In emphasising the importance of developing dynamic comparative advantages and the

concept of 'self-discovery',[165] Thirlwall and Pacheco-López[166] argue that the essential question is not one of a choice between the absence of trade versus free trade, but rather 'the sensible management of trade' in order to allow for growth that avoids balance of payments difficulties, policy space to develop new comparative advantages, and the strategic use of tariffs and subsidies to protect infant industries to promote structural change.

This raises the orthodox concern about a government's ability to 'do', or oversee an effective policy of selective intervention and the fear that special interest groups and rent-seekers will capture the process. Extensive literature does address both of these issues,[167] although a detailed discussion is beyond the scope of the present paper. However, the tendency to argue by elimination should be avoided. The view that capacity and institutions are weak should not be accepted as a valid argument for free trade, but rather as one for capacity- and institution-building. For example, even before national and regional positions have been adopted, South Africa and most of its SADC partners are under pressure to negotiate new generation issues, such as government procurement and intellectual property rights, with developed country trading partners. Domestic capacity is being developed just as it was developed to participate in complex WTO work programmes. In the same way, capacity will develop where necessary in the field of strategic trade and industrial policy.

## CONCLUSION

The methodological approaches used to explore the impact of trade liberalisation on growth, employment and poverty in South Africa, with reference to the theoretical and empirical debates on the linkages between trade, growth and poverty on the one hand, and trade, income inequality and poverty on the other have been considered. The debate on 'trade reform' in South Africa focuses on the right questions when developing a trade strategy that addresses the country's national and regional development goals.

The theoretical and empirical debate on trade, growth and poverty has been highly polarised and indeed ideological. An important reason for this is the persistent view that a 'free trade' system is a relevant benchmark. However, the theory and evidence are not nearly as compelling as the proponents contend. Indeed the weaknesses in the arguments are well-known, as not only have they been pointed out by heterodox writers, but also new directions within orthodox economics such as new trade and endogenous growth theory have developed as a consequence of such limitations. The economic and social debate on trade policy in South Africa is also polarised, but is more developed and nuanced than might be expected given some of the broader controversies, which suggests that fruitful ground for engagement exists.

The technical literature in South Africa has significant expertise on alternative trade policy and protection measures (as well as their shortcomings), the composition of the country's tariff structure, tariff preferences, duty rebates and rules of origin, as well as the relevant econometric and modelling techniques. This literature should engage firstly with the extensive technical literature on the theory and practice of selective intervention and also with historical perspectives on industrial policy in Europe, the US and East Asia.[168] Ocampo and Taylor[169] argue that 'neither intervention nor liberalisation packages can be evaluated outside history, contrary to the main thrust of mainstream economic theory'.

Assessment of alternative scenarios should be benchmarked relative to industrial policy and development goals, rather than to an unrealistic free trade ideal. Account also needs to be taken of the literature that addresses the broader context of the state of play in multilateral, regional and bilateral trade negotiations. The complexities, rules, obligations and pressures of the trade law and trade negotiation aspects of trade policy need to be integrated into the debate.

In conclusion, the dialogue on 'trade reform' in South Africa should move beyond the unhelpful portrayal of the debate as one between 'free trade' and 'protectionism'. Indeed, the South African literature should reject such a simplistic depiction. Research activity in this field should be directed at finding ways to use trade and industrial policy as effective instruments of South Africa's national development strategy. Other areas of economic and social policy must be co-ordinated with trade and industrial policy. Neither trade liberalisation nor the economic growth that has occurred has been able to address the problem of poverty in a context of rising inequality and severe joblessness. Accelerated growth is in any event unlikely to be forthcoming (in the short term at least) due to external and other constraints and obstacles to structural transformation.[170] South Africa will accordingly need strong and effective social policy 'that should be conceived ... as a key instrument that works in tandem with economic policy',[171] while attempting to use trade, industrial and other economic policies to bring about the structural change required to grow and diversify manufacturing production and exports, and create jobs.

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