

Zimbabwe's Experience With Trade Liberalization

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Abstract

The paper investigated Zimbabwe's experience with trade liberalization for the period 1980 to 2004. The study used three approaches, namely changes in policy, changes in quantities and changes in price to analyse the country's trade policy during this period. These approaches indicated that the country's trade liberalization was not consistent with policies that the government implemented between 1980 and 2004. The study also found out that the country's liberalization process was credible and sustainable during the Economic Structural Adjustment Programme (ESAP) period (1991 through to 1995), after which credibility was lost when the liberalization process became unsustainable. Reduced credibility was a direct result of policy reversals that were instituted after 1995 while a combination of accumulated balance of payments (BOP) deficits and budget deficits resulted in payments incompatibility, making trade liberalization unsustainable. The study also found that the political economy of the whole trade liberalization process was largely dominated by government (and to some extent individual politicians) with minimal input from the private sector (that is, producers and consumers).

The analysis therefore pointed to one main policy recommendation, that is, for the country to reap the benefits of trade liberalization, it has to be consistent in its trade policy. Whilst in the short term, negative effects (in the form of reduced government revenue, for example) maybe experienced, it is in the long run that benefits start to accrue. Policy makers also need to be reminded that trade liberalization should be a process not an event and therefore a long time horizon is required when formulating and implementing trade liberalization policies.

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Abbreviations

BOP	Balance of Payments
CFU	Commercial Farmers Union
c.i.f.	Cost, insurance, freight
COMESA	Common Market for Eastern and Southern Africa
CSO	Central Statistical Office (Zimbabwe)
CZI	Confederation of Zimbabwe Industries
EPZs	Export Processing Zones
ERS	Export Retention Scheme
ESAP	Economic Structural Adjustment Programme
FCAs	Foreign Currency Accounts
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
IIIR	Index of Implied Import Restrictiveness
IFS	International Financial Statistics (of IMF)
IMF	International Monetary Fund
ISI	Import Substitution Industrialization
MERP	Millennium Economic Recovery Programme
MFN	Most Favoured Nation (principle of the WTO)
NAFTA	North American Free Trade Agreement
NRP	Nominal Rate of Protection
NTBs	Non-tariff Barriers
OGIL	Open General Import License
QRs	Quantitative Restrictions
SADC	Southern African Development Community

UDI	Unilateral Declaration of Independence
WTO	World Trade Organization
ZIMPREST	Zimbabwe Programme for Economic and Social Transformation
ZNCC	Zimbabwe National Chamber of Commerce

1. Introduction

The promotion of free trade across countries or regions is premised on the conventional wisdom of international trade which assumes that once an economy eliminates government distortions, the “invisible hand” will set prices which will reflect the correct cost of production and resources, resulting in optimal allocation of resources. This theory further asserts the need to dismantle quantitative restrictions on imports; reduce or eliminate import duties, making the local currency convertible for current account transactions; eradicate bureaucratic government red tape and other impediments to foreign direct investment; and improve customs procedures (Rodrik, 2006). These actions are viewed as necessities for increased specialization which in turn leads to capital accumulation and technological advancement in production. Specifically, some of the advantages assumed to be the benefits accruing to a trade liberalizing country are: increased optimal resource allocation, access to technology, boost in both local production and employment, and access to a wider range of goods and services.

On the contrary, this trade liberalization process may result in unintended negative consequences resulting in the creation of adjustment costs, encompassing a wide variety of potentially disadvantageous short-term outcomes. These outcomes may include a reduction in employment and output, the loss of industry and firm-specific human capital, and macroeconomic instability arising from balance-of-payments difficulties or reductions in government revenue (Matusz and Tarr, 1999). The size of the adjustment costs, however, depends on the speed with which resources make the transition from one sector to another.

Thus, given this ambiguity about the impact of trade liberalization on the economy, one can, therefore, consider trade liberalization as a ‘two-edged’ sword, with both positive impacts and negative consequences.

Whilst most African countries implemented trade liberalization policies at various levels (bilateral, regional and multilateral) from the early 1980s, Zimbabwe’s experience has not been consistent with the policies that the government has implemented over the years. Starting with import substitution industrialization (ISI), the country massively liberalized its trade regime beginning in the 1990s before reversing the whole process towards the end of that decade. Whilst the government has committed itself to a plethora of trade liberalization agreements since the 1980s, from regional (the Southern African Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA)) to multilateral (the World Trade Organization (WTO)), the implementation of these agreements has proved to be more problematic. By categorizing

the period under analysis (1980 to 2004) into three sub-periods, namely pre-Economic and Structural Adjustment Programme (ESAP) (1980–1990), ESAP (1991–1995) and post-ESAP (1996–2004), a number of trade liberalization episodes will be depicted. To help investigate these episodes, the study employed the method of Reinikka (1994b)¹ and traced changes in three main factors: policy changes, changes in prices and quantitative changes. Among other trade liberalization measures, these three approaches confirm that Zimbabwe's trade liberalization has not been consistent with the policies that the country has implemented over the years.

Problem statement

Several studies investigating the extent of trade liberalization and the economic impact of such processes have been conducted both in developed and developing countries (for example, Reinikka, 1994b; Ncube et al., 1999; Mattoo et al., 2001; UNCTAD, 2005). Despite numerous studies on the subject matter, the effect of trade liberalization remains ambiguous. Some evidence supports the notion that trade liberalization has a positive effect on the economy while negative effects of trade liberalization on the economy are also supported by literature.

In the Zimbabwean context, Ncube et al. (1999) show that trade liberalization did take place for the period 1991 to 1995 with some positive benefits, especially on the financial sector. Nevertheless, given the changes in the trade regimes which followed after 1995, our study analysed the country's trade liberalization for the years after 1995. However, in order to have a chronology of liberalization episodes for the country since independence, the paper analysed the period covering 1980 to 2004.

The study also investigated the extent to which the liberalization was sustainable. The paper further investigated some of the reasons why trade liberalization was sustainable, and provided explanations for why it was not.

Whilst the Ncube et al. (1999) study also analysed trade liberalization in Zimbabwe for the period ending 1995, our study extended the research to 2004. The period after the Ncube et al. (1999) study was characterized by some interesting policy shifts. For example, from 1995 to 2000 the government implemented the Zimbabwe Programme for Economic and Social Transformation (ZIMPREST) which, among other things, reversed some of the liberal trade policies which had been implemented in the 1991 to 1995 period. At the same time, the period 2000 to 2004 becomes a case in point in that it significantly highlights the political economy of policy reversals on the country's trade policy.

Objectives of the study

Given the above background, the study's twofold objectives were therefore to:

1. Analyse the extent to which Zimbabwe liberalized its trade regime; and
2. Investigate whether the trade liberalization was sustainable.

The structure of the study is as follows. Section 2 provides a brief summary of the

country's trade regime. Specifically, this section outlines the importance and significance of export and import trade to the economy of Zimbabwe. The country's principal exports and imports, and major export destinations and import sources are also presented in this section. Section 3 provides literature review. Given that the study's main objectives were to analyse issues, literature review has been categorized into two parts, one which contains review of studies that were done on the extent of trade liberalization and another which presents past studies that were conducted in other countries on sustainability of trade liberalization. The methodology employed to achieve the objectives of this study is presented in Section 4. In line with the two objectives of this study, the methodology is in two parts, one which deals with measurement of trade liberalization and another dealing with sustainability of trade liberalization. Section 5 employs the methodology outlined in Section 4 to outline the extent of trade liberalization in Zimbabwe. The extent of credibility and sustainability of trade liberalization are the subjects of the analysis presented in Section 6. Section 7 provides study conclusions and policy recommendations.

2. Zimbabwe's trade regime

Total trade, which comprises exports and imports, is important to the economy of Zimbabwe. The importance of exports to the country emanates from their positive contribution to economic growth. Theoretically, the positive impact of exports on the level of economic activity is understood to work both through the demand and supply sides of any economy. On the demand side, an increase in exports will cause induced consumption, investment and government expenditure, calling for the supply side to positively respond so as to satisfy the requirements of the induced demand.

Following Blumenthal (1972) and Jaffee (1985), the total impact of exports can be broadly divided into three parts. Firstly, there is a direct effect; since the value added by exports is part of gross domestic product (GDP) (in the Keynesian framework²), a rise in exports implies a rise in GDP. In the case of Zimbabwe, statistical figures from Zimbabwe's Central Statistical Office (CSO) indicate that for the five-year period covering 2000 to 2004, exports contributed an annual average of above 40% towards the country's GDP. This contribution is significant and shows the importance of export trade to the country.

Secondly, export industries affect growth through their effect on other backward and forward industries. That is, for export industries to produce for exportation they demand raw materials and inputs from other industries (the backward linkage). At the same time, the export industry supplies intermediate inputs to other domestic industries besides exporting. Because of these linkages, the export sector will provide an overall positive impact on the growth of the domestic economy.

Lastly, since exports are a source of foreign exchange, besides other sources such as international aid, foreign direct investment, offshore loans and grants, they affect growth via imports, especially of vital production inputs and raw materials. Given Zimbabwe's production activities depend on imported inputs and capital equipment, these purchases can be made by using the foreign currency earned from exports (among other sources of foreign currency).

However, even though imports are considered as "leakages" from the income circulation model within the Keynesian framework, they are also important for a country's economic growth. The significance of import trade to Zimbabwe can be categorized into four parts. Firstly, imports provide vital inputs in the country's production system. Given

that some of inputs which are required in production may not be adequately provided locally (for example, fertilizer), the country will have to depend on imports. Secondly, and most importantly, in the recent years import trade has been the most dependable channel through which the country has managed to ensure food security for its citizens against a background of decline in food production since 2000. Thirdly, imports have resulted in technology transfer, especially in the mining sector. Given the connectedness of the country's mining sector, this sector has over the years managed to import state of the art production equipment. Lastly, through imports, the country has managed to procure essential products such as medical drugs, electricity and other products which the country could not produce for one reason or the other.

The country's major or principal exports and imports are shown in Table 1. The tabulated information indicates that for the time period reported, the country's annual average exports and imports were US\$1,694 million and US\$2,232 million respectively, while the highest major exports and imports products were beverages and tobacco. Overall, the country's exports comprised agricultural and manufactured products while imports were dominated mainly by fuel, machinery, transport equipment and chemical products.

The country's major export destination countries include USA, UK, Zambia, Switzerland, South Africa, Malawi, Japan, Germany, China and Botswana. Zimbabwe sources its major imports from Botswana, USA, UK, South Africa, Japan, South Korea, Germany, France and China.

Table 1: Zimbabwe's principal exports and imports trends

	Principal exports as % of total exports					Principal imports as % of total imports				
	Total exports (US\$ millions)	Food & live animal	Beverages & tobacco	Crude inedible material	Manuf'd goods	Total imports (US\$ millions)	Mineral fuel	Machinery & transport equipment	Chemicals & related products	Food & live animals
1990	1,474	19.4	23.5	14.8	30.3	1,847	15.6	37.4	15.5	2.3
1991	1,323	13.5	33.6	12.3	30.0	2,043	12.5	41.0	16.3	0.9
1992	1,252	7.0	35.4	11.9	30.4	2,206	11.8	36.0	11.8	14.4
1993	1,322	11.5	29.8	14.0	28.0	1,820	14.8	35.1	13.9	8.4
1994	1,725	22.9	24.6	12.7	23.8	2,243	9.8	41.8	16.3	2.4
1995	1,861	16.7	26.1	13.2	28.5	2,661	9.0	42.3	13.8	3.7
1996	2,101	15.9	35.3	12.6	22.1	2,809	10.4	42.3	13.4	7.1
1997	2,116	17.1	27.8	15.8	23.0	3,018	10.2	38.7	14.8	4.2
1998	1,775	17.8	28.9	18.3	20.1	2,794	15.9	38.8	15.3	4.4
1999	1,887	15.9	34.5	15.6	20.8	2,178	14.2	34.2	16.5	4.7
2000	1,797	14.3	31.8	19.8	21.7	1,807	18.4	34.2	17.6	3.2
2001	1,191	7.5	49.1	15.4	25.6	1,702	42.9	29.3	15.0	1.9
2002	1,886	9.3	16.7	21.3	37.1	2,077	33.8	19.9	11.7	9.6
2003	1,204	5.1	9.4	16.7	36.6	1,541	15.8	1.7	0.3	0.8
2004	2,501	7.3	17.3	11.0	29.3	2,739	38.6	13.4	5.9	2.1
Average	1,694	13	28	15	27	2,232	18	32	13	5

Source: CSO (2005).

Zimbabwe's trade policy regime and macroeconomic performance

Zimbabwe lacks a properly laid out trade policy document or framework for a specific period in which trade objectives, targets, policies and linkages with other macroeconomic growth and development targets are clearly laid out and linked. Elements of trade policy come in various documents such as annual budgets, ministerial pronouncements and macroeconomic policy documents. This makes it difficult to analyse the country's policy orientation.

During the pre-ESAP period, the country's trade regime was characterized by control of imports through licensing, quotas and extensive bans, high tariff protection, administrative exchange rate allocation and various non-tariff barriers. The Government of Zimbabwe intervened in the economy by controlling prices, wages and interest rates. These policies, however, proved to be futile by the beginning of the 1990s as the country experienced a general economic decline and there was a need for a shift from protectionism to liberalization.

In 1991, with the support of the Bretton Woods institutions, namely the World Bank and the International Monetary Fund (IMF), Zimbabwe embarked on an autonomous structural adjustment programme, commonly known as ESAP with trade as a key component. The country also made a commitment in 1995 to reduce tariffs under the WTO Uruguay Round. Thus, trade liberalization in this period saw the lifting of restrictions on trade through removal of non-tariff trade barriers and the reduction of tariffs. The country embraced this move to enhance domestic productivity, efficiency, improved quality and low prices, which ultimately lead to improved consumer welfare. Thus, it is only in this sub-period that meaningful trade liberalization took place in Zimbabwe.

The post-ESAP period, however, saw introduction of policies which reversed most of the trade liberalization stances which were implemented in the ESAP period. This period witnessed increases in trade tariffs, implementation of import and exchange controls, among other policies. These anti-liberal policies were aimed at reducing the country's balance of payments (BOP) deficits, accumulated over the years. Import and exchange controls were further tightened from 2000 to deal with other economic problems such as foreign currency shortages, besides BOP ills.

In terms of overall macroeconomic indicators, the information in Table 2 shows the country's performance trend. Although a mixture of both good and poor performance, most indicators show that the country performed relatively well in the pre-ESAP period (that is, 1980 to 1990). For example, during this decade GDP growth and trade balance were both positive while inflation hovered at below 15%. However, after the ESAP period, the performance of most of the indicators tabulated worsened, with inflation drifting upwards from high inflation figures (averaging 27% between 1991 and 1995) to extremely high levels, reaching an annual rate of 599% by 2003. Foreign reserves continued to dwindle, from a peak of US\$830 million in 1996 to a low level of US\$131 million by end of 2003.

Table 2: Macroeconomic performance

Year	1980–1985	1986–1990	1991–1995	1996	1997	1998	1999	2000	2001	2002	2003
Nominal Ex Rate (Z\$/US\$) (annual average)	1.1	1.7	35.2	10.8	18.6	37.4	38.1	55.1	55.03	55.03	826.44
Inflation (End period)	13.5	12.9	27.6	16.4	20.1	46.7	56.9	55.2	112.1	198.3	598.7
Real sector											
Real GDP growth (%)	6	4.6	1.4	9.7	3	-0.8	-2.1	-6.1	-3.6	-11.3	-8.6
Exports (US\$ millions)	738	944	1442	2496	2424	1925	1924	2200	1574	1396	1204
Imports (US\$ millions)	711	839	1585	2247	2654	2020	1675	1907	1826	1820	1541
Trade balance (US\$ millions)	27	105	-142	259	-230	-95	249	317	-252	-424	-337
Current account											
Incl. official transfers (US\$ millions)	na	na	Na	87	-65	74	189	-289	-389	-218	-249
Overall BOP balance (US\$ millions)	na	na	Na	4	-740	-289	0	-171	-194	-496	-335
Government debt											
Foreign debt (% of GDP)	45	46	65	55	59	109	68	58	31	52	74
Domestic debt (% of GDP)	29	32	27	38.1	32.8	29.8	33.9	44.9	27.4	20.4	10.7
Budget deficit (% of GDP)	na	-2.6	-4.1	-6.9	-7.2	-3.7	-5.8	-19.6	-6.0	-0.2	
Fragility indicators											
Foreign reserve (US\$ millions)	333	319	560	830	272	296	478	288	121	128	131

Source: RBZ Annual Report (2004).

3. Literature review

Several studies have been done on trade liberalization, mainly for developing and transition economies. Papageorgiou et al. (1991) enumerate 36 liberalization episodes across 19 countries. The study used policy changes over time across countries as the main methodology. The ingredients of the liberalization episodes in the study sample reveal that tariff reduction and reduction of quantitative restrictions are the policy variables that feature most across the sample countries. Other policy changes such as elimination of import licence restrictions; exchange rate devaluation and reductions in import controls are also reported in some of the countries.

Ncube et al. (1999) carried out a comprehensive study on trade liberalization and regional integration in Zimbabwe for the period 1991 up to 1995. The study analyses a number of policy changes affecting trade directly and indirectly. The manufacturing sector was among the highly protected sectors in the period before ESAP, with foreign currency allocation and import bans being the most common policy protection variables. However, the introduction of ESAP brought about the changes in trade policy shifting from rational access to foreign exchange and extensive bans on imports, to market-based allocation of foreign exchange and rights to import subject only to tariffs, which were themselves reduced (Ncube et al., 1999).

Whalley (1991) reports the results of an evaluation of liberalization in 11 countries. The research analysed changes in the scale and intensity of reforms over time across the sampled countries. Most policy variables that were investigated included changes in tariffs, quantitative restrictions (such as quotas), elimination of import restrictions and exchange rate policies. After tracing these policy variable changes, the study inferred that trade liberalization did occur in the countries which were studied.

Reinikka (1994b) investigated the extent of trade liberalization for Kenya for the period 1967 to 1990. The research methodology is a combination of two approaches. Firstly, the study analysed changes in prices, and specifically investigated the average implicit index, which was calculated as the ratio of the domestic ex-factory price index and the import price index. At the second stage, the researcher compared and contrasted

the implicit tariff index (a variant of price changes) and policy changes which took place over the entire period. Overall, the investigation concludes that a combination of the index's strong declining trend, and changes in trade policy imply that "substantial trade liberalization took place in Kenya since the late-1960s" (Reinikka (1994b:48).

Sustainability of trade liberalization

Lewis (2004) provides case studies on the sustainability of trade liberalization for four Latin American countries, though the experiences of only Chile and Mexico are presented in this section.

Chile liberalized trade unilaterally and multilaterally by reducing tariffs to all trading partners in a non-discriminatory fashion. The country was the Latin American pioneer of trade liberalization during the mid 1970s and has sustained a relatively open trade policy to date, even though it had a brief period of increased tariffs during the 1980s. Lewis (2004) argues that Chile has had an overall durable trade policy that has survived recessions, financial crises, and political transitions as a result of its unilateral trade opening.

Mexico's trade liberalization route has been different to that of Chile. Mexico, unlike Chile, experienced a relatively regional liberalization, signing the North American Free Trade Agreement (NAFTA) as one of the major regional commitments to trade liberalization. In fact, Lewis considers Mexico as one of the most prolific signers of free trade agreements in the world which has resulted in the country continuing to liberalize and decrease tariffs over the years. The peculiarity of Mexico's trade regime is also shown in that although non-tariff and tariff boundaries have been eliminated within formal trade agreements, trade barriers have increased for all other countries highlighting an increasing disparity in the degree of Mexico's openness. Overall, Mexico's trade regime illustrates a durable regional approach that has survived recessions, financial crises and political transitions, yet has seen limitations on the overall expansion of its trade worldwide.

Despite the existence of past studies on extent of trade liberalization and sustainability, this paper will contribute to the body of knowledge. This contribution is twofold. Firstly, the paper provides an analysis of the extent of trade liberalization in Zimbabwe by extending the period beyond 1995, the extent of the study by Ncube et al. (1999). Secondly, this study also investigated the extent to which that trade liberalization was sustainable for the period 1980 to 2004. This analysis has not been done for such a period on Zimbabwe.

4. Methodology

Trade policy is typically a complex exercise involving removal of or reduction in quantitative or administrative imports restrictions, temporarily replaced by tariff surcharges, unification and subsequent reduction on tariffs, and introduction of direct incentives to exporters (Thomas and Nash, 1991). This complexity has resulted in the identification of trade liberalization episodes being far from straightforward. However, despite the difficulty, unambiguous identification of trade liberalization episodes is important if we wish to study the economic performance of liberalizer's vis-à-vis sustaining protection.

Three approaches to measure and identify trade liberalization episodes have been used in literature (for example, Reinikka, 1994b): (i) changes in policies; (ii) changes in prices; and (iii) the resulting changes in quantities. In an attempt to achieve the study's objectives, this paper employed these three approaches. Each of these three approaches uses more than one technique to measure and identify trade liberalization episodes. This study, therefore, employed the most appropriate techniques from each of these three approaches.

Changes in policies

Policy accounts

One method of determining a liberalization episode and its duration is to examine actual changes in policy instruments, such as shifts in import licensing practices, tariffs, export incentives or the exchange rate. Introduction of policy marks the beginning of an episode, and when the changes are completed, stopped or reversed, the episode ends. This approach is a useful way of distinguishing episodes, for example, when studying the speculative response by the private sector to trade reforms which lack creditability.

When frequent changes in policy are made, with some policies rapidly reversed, it may not be possible to determine whether the trade regime has become more liberal by examining policy changes alone. Changes made in trade policy instruments may not necessarily surface at the aggregate level as they may be in opposing directions, or

influenced by other policies and variations in economic conditions. For example, a trade policy may reduce border tariffs, say, for specific capital goods and at the same time increase import duties on specific agricultural goods. In such a case, these opposing effects may cancel each other out at the aggregate level.

The changes in policy approaches are useful for dating liberalization episodes, but will obviously not generate a quantitative indicator (unless one is willing to admit the subjective judgements of country authors, as was done in a World Bank study, Papageorgiou et al. (1991)). Thus, quantitative measures or criteria that tell us whether various policy changes surface in aggregate data become paramount.

Changes in prices

Implicit tariff measures

The domestic price (ex-factory) of an importable good may be written as:

$$P_{mi} = P_m \times e(1+t_i) \quad (1)$$

where P_{mi} = domestic price (ex-factory) of an importable good;
 P_m = cost, insurance and freight (c.i.f.) import price (in dollars);
 e = the exchange rate (domestic currency per dollar); and
 t_i = the implicit tariff rate.

Given the observations on world prices, domestic prices and the exchange rate, Equation 1 may be used to derive an implicit tariff index as follows:

$$t_i = \frac{P_{mi}}{e \cdot P_m} - 1 \quad (2)$$

The implicit tariff is, therefore, the ratio of the domestic price of a given group of importables (commodities) relative to their world price minus one. Trade liberalization can then be measured as a reduction in this tariff index (Equation 2). According to Reinikka (1994b), this index captures changes in the nominal rate of protection, which is the combined effect of nominal tariffs and tariff equivalents of quantitative or non-tariff restrictions. In the absence of sufficient information on its actual levels, the study derived the implicit tariff index indirectly by using available deflators. In what follows, the implicit tariff index consistently refers to the average implicit tariff index for Zimbabwean imports and it was calculated by using the average domestic ex-factory price and its world price equivalent for these goods.

Changes in quantities

Trade intensity measures

Trade intensity is measured as the ratio of trade (imports (M) plus exports (X)) to GDP. One objection of the trade intensity measure is that imports are financed by both export revenue and by capital flows. Therefore, a change in the trade intensity measure (M + X)/GDP may simply pick up an increase in aid flows. Also, the use of the GDP variable is difficult to defend. For example, an increase in real income as a result of terms of trade

improvement will lead to an increase in trade intensity. The measure will then indicate trade liberalization even if no policy changes and no substitution effects have taken place either in production or in demand.

Import counter-factuals/notional imports

This method is a variant of the trade intensity measure and was developed by Narasimhan and Pritchett (1993) for quantitative assessment of the magnitude of import compression. The effect of trade policy or import restrictiveness is measured by comparing actual imports from the notional/counter-factual level of imports demanded. The notional demand for imports M_d is derived as a simple log function of real income y and the real exchange rate RER :

$$M_d = \alpha + \beta Y + \delta RER \quad (3)$$

If parameters α , β , and δ are known, Equation 3 could be used to calculate how actual imports over time deviate from the notional demand. The deviation could be used as an indirect measure of import restrictiveness. As the parameters are not known, Narasimhan and Pritchett (1993) use average estimates derived from other empirical studies for income elasticity β and price elasticity δ ($\beta = 1.25$ and $\delta = -1$). In order to obtain a value for constant α they assumed that in the 1970s the actual and notional demands coincide. The index of implied import restrictiveness (IIIR) is then defined as the percentage deviation of M_d from the log of actual imports M .

A drawback of the above two quantity-based measures is that they are likely to pick up changes in the extent of illegal trade. For example, trade liberalization might result in a large increase in official imports at the expense of smuggling, with little change in imports. Unlike a price-based measure, a quantity-based measure would then give an unrealistic indication of the change in incentives for consumers and producers.

Sustainability and impact of trade liberalization

This section presents the methodology used to achieve the second objective of the study. The study investigated sustainability of trade liberalization on the Zimbabwean economy by carrying out an analysis of official published documents for appropriate trend figures and also by reviewing relevant literature.

5. Extent of trade liberalization in Zimbabwe

Changes in policies

Pre – ESAP period

Regulation of foreign trade has been a key feature of the Zimbabwean economy. During the Unilateral Declaration of Independence (UDI) between 1965 and 1980, the economy was placed under United Nations sanctions and the then regime implemented ISI. Due to these sanctions, the country was not able to secure enough foreign aid and the fact that there were relatively few exports, foreign currency shortages became a major source of the country's problems. ISI was meant to reduce the country's dependency on the international market in the face of sanctions while import controls were meant to facilitate the effective use of the scarce foreign exchange.

Thus, at independence in 1980, the country inherited this heavily controlled economy. The new government continued with the import substitution development strategy which saw it imposing several policy controls on trade, foreign currency use, interest rates, price and exchange rates. Specifically, the government was rationing foreign currency, there were import bans and quotas, and prices were regulated.

However, by the end of the first decade after independence (1980–1989), the Zimbabwean economy was already experiencing industrial inefficiency, low productivity, market distortion, increasing public sector spending and low rate of employment. Furthermore, investment levels were falling due to uncertainties associated with foreign currency allocations; the paucity of foreign currency resources; erratic and low rate of economic growth which averaged 3.2% (barely above the population growth of 2.9%) annually; and the sluggish export growth and an unstable macroeconomic environment

characterized by high budget deficits and growing inflation. Thus, during this period no trade liberalization took place.

Economic Structural Adjustment Programme 1991–1995

To address the problems experienced in the pre-ESAP period, the government decided to implement trade liberalization among other macroeconomic liberalization programmes from 1991. Like many other developing countries, Zimbabwe implemented a comprehensive trade liberalization programme in 1991 that was meant to reverse a long tradition of control in the economy. The government agreed to adopt the market reforms (ESAP) recommended by IMF and the World Bank which guaranteed inflows of foreign currency and BOP support. The programme contained most of the elements of the orthodox Washington Consensus and trade liberalization was the policy driver.³ The liberalization was designed to be gradual and implemented over the 1991–1995 period.

Several trade policy changes took place during this period. For example, by 1994 all current transactions were outside government control and the only restrictions left on the capital account concerned returns to investments made before independence and holding foreign assets abroad. This period also saw the dismantling of the existing import controls, industrial licensing, and fixed exchange rate regime that were associated with the pre-ESAP regime.

The main objective of ESAP in the area of trade was to ensure adequate trade liberalization which would see complete abolition of quantitative controls and the reduction and harmonization of tariffs and duties. The specific trade-related objectives of ESAP as outlined in the Government of Zimbabwe (1992) Framework of Economic Reform were:

- Removal of export incentives;
- Phasing out of import licensing regime;
- Elimination of foreign currency controls;
- Reduction of tariffs and creation of a tariff band ranging from 0% to 30%;
- Removal of surtax and raising of the minimum duty to 10%; and,
- Achieving export growth rate of 9% a year over 5 years (from 1991 to 1995).

Most of these trade policy objectives were implemented. Specifically, the liberalization of trade opened up the current account transactions and implementation of a market based exchange rate system which allowed the exchange rate to be market determined. Major trade liberalization milestones were the removal of selected input items from the quantitative import controls to Open General Import Licence (OGIL), introduced during the second half of 1990. Another milestone was the removal of foreign currency controls and the introduction of foreign currency accounts (FCAs) in January 1994. This allowed a 60% retention which was then increased to 100% in July the same year. Thus, for Zimbabwe trade liberalization only started after 1990.

After implementation of the above policies between 1991 and 1995, the government conducted some internal reviews of the ESAP period and the findings revealed that whilst some objectives of the programme were met some remained a pipe dream. This led the government to pursue a successor programme which was meant to correct all the ills of ESAU, called ZIMPREST.

Post-ESAP period

ZIMPREST: 1996–2000

When ESAP expired in 1995, the government was not eager to pursue economic reforms resulting in a two-year gap between the implementation of ZIMPREST and the expiry of ESAP. Most policies were reversed mainly due to poor macroeconomic performance; deficiencies in trade policies and sequencing of liberalization; fiscal indiscipline; exchange rate mismanagement; monetary policy mix; and incompetence of economic managers to understand the substances and process of trade liberalization.

In October 1998, the government reversed its policy and increased tariffs on finished products with local substitutes or those considered luxuries. In fact, tariff duties were increased to levels much higher than those of the pre-ESAP period. This was done in an effort to restore stability in the foreign exchange market, curtail import pressure on the exchange rate and to generate government revenue whilst protecting the local manufacturing industry. The rapid depreciation of the currency in 1999 was followed by the introduction of exchange controls which were meant to peg the local currency against major foreign currencies such as the US dollar, South African rand and the British pound sterling. The government started to apply the main border taxes, namely custom duties, import tax (which was essentially sales tax on imported goods) and a surcharge. Table 3 gives a snapshot of some of the tariff lines whose duty was hiked.

Table 3: Selected tariff increases (%) from 1998 tariff structure rationalization

Product item	Pre-ESAP (1980–1990)	ESAP (1991–1995)	Post-ESAP (1996–2004)
Buses	30	25	50
Other commercial vehicles	65	25%–65	95%–100
Private vehicles	65–85	60%–80	100
Motor vehicle parts	30	15	50
Bicycle parts	30	15	50
Furniture	50	40	80
Selected shoe components	30	30	65
Surtax on above commodities	20	10	15

Source: Ministry of Industry and International Trade (2006)

As a result of these inconsistencies and other factors such as high inflation, decline in economic growth; deficits in trade balance, BOP and fiscal balance, and runaway foreign debt growth, ZIMPREST did not meet most of its targets.

Millennium Economic Recovery Programme (MERP) 2000–2002

As a result of the above challenges, the government realized the need to respond to the unfolding economic crisis and a new programme called the Millennium Economic Recovery Programme (MERP) was implemented in July 2000 to December 2002. Its major objectives were to stabilize prices, resolve the foreign currency crisis and stimulate growth among others. However, this programme was never officially published due to

differences in government on the way forward to address the existing problems. Due to macroeconomic instability since 2003, the macroeconomic policies (including trade policy) for Zimbabwe have changed frequently. Furthermore, the government stopped publishing some of the policy documents.

Overall, compared with the ESAP period when Zimbabwe implemented trade policy in full, liberalization during the post-ESAP period was characterized by numerous reversal and anti liberalization policies. Table 4 compares these two periods.

Table 4: Trade liberalization policies measures

Scope	Pre-ESAP (1980–1990)	ESAP (1991–1995)	Post-ESAP (1996–2004)
Domestic and border trade policies	<ul style="list-style-type: none"> - Price controls - import licences on most products 	<ul style="list-style-type: none"> - Removal of import licences - Tariff reductions - Tariff structuring - Domestic price deregulation 	<ul style="list-style-type: none"> - Introduction of price controls on selected products - Increase in tariffs - Import licensing on some goods
Regional trade policies and liberalization	<ul style="list-style-type: none"> - Founding member of SADC - Founding member of COMESA 	<ul style="list-style-type: none"> - Signed SADC Trade Protocol - Commitment to zero duty in COMESA 	<ul style="list-style-type: none"> - Mid-loading of reduction in tariffs - Increase in some tariffs on regional imports (SADC and COMESA) - Behind schedule on COMESA October 2000 deadline
International policies	<ul style="list-style-type: none"> - No significant GATT (WTO) tariff bindings 	<ul style="list-style-type: none"> - WTO tariff binding and reductions compliance 	<ul style="list-style-type: none"> - Tariff bound at high levels than applied rates - Applied tariffs increased
Foreign exchange policy	<ul style="list-style-type: none"> - Restricted foreign currency accounts - Foreign currency allocation 	<ul style="list-style-type: none"> - Removal of controls on foreign exchange and remittances from abroad 	<ul style="list-style-type: none"> - Pegged exchange rate to US\$ - Suspension of foreign currency accounts - Foreign currency allocation
Export incentives	<ul style="list-style-type: none"> - Presence of export retention scheme 	<ul style="list-style-type: none"> - Removal of export retention scheme and other incentives 	<ul style="list-style-type: none"> - Tobacco levy introduced - Introduction of export incentives in budget

Source: Own compilation

4Policy volatility and liberalization episodes in Zimbabwe

Papageorgiou et al. (1991) define an episode of liberalization as commencing at a point at which a significant policy change towards liberalization was implemented and ending with either a reversal or when no further policy trend in either direction is apparent. Although it is conceptually simple, identifying trade liberalization episodes empirically is far from straightforward. Liberalization episodes can be determined by examining actual changes in policy instruments, such as shift in import licensing practices, tariffs, export incentives or the exchange rate. The introduction of policy changes marks the beginning of an episode, and when the changes are completed, stopped, or reversed, the episode has come to an end. Another method of identifying episodes would be to define quantitative measures or criteria that are able to tell us whether or not the various policy changes surface in aggregate data. In this case the study used the implicit tariff index.

Although Zimbabwe's trade liberalization has been somewhat unusual, the country did not have numerous policy reversals during the first episode of trade liberalization, (1991–1995). Whilst the reform was aid supported, the government was not desperate for aid money. Thus, donor involvement did not lead to a threat of a potential time inconsistency. However, the incentive systems which were implemented by government were subjected to frequent changes and the implementation was rather indiscriminate. This may have given rise to a low degree of supply response, resulting in industry failing to see the many steps of liberalization as constituting a logical sequence of “gradualism” hence read them as policy reversals (Ncube et al., 1999).

The country experienced serious fiscal challenges in the post-ESAP period which resulted in the cumulative effects of government failure to tackle the budget since the beginning of ESAP (Davies, 2004) leading to a budget deficit, which threatened the maintenance of the whole liberalization process. This problem was also compounded by the exhaustion of the aid that the country was receiving. These two problems (among others) resulted in significant shifts in policy causing the numerous policy reversals. Some of these specific reversals are presented in Table 4. Table 5 summarizes the components of Zimbabwe's liberalization episodes until 2004.

Table 5: Components of liberalization episodes for Zimbabwe

1990–1991	- Liberalization of merchandise imports - No depreciation of the real exchange rate
1991–1993	- Devaluation of the dollar followed by continued depreciation of the currency - Liberalization of imported inputs - Liberalization of the financial sector
1993–1995	- Most goods were placed on OGIL except those that were strategic such as fuel - Announcement of tariff reduction changes (some to a level of 100% and this indicated an intention of government to do the same in future) - Exports subsidies removed - Liberalization of foreign exchange regime leading to currency convertibility
1995–1997	- Implementation of WTO commitments - Reduction in import tariffs - Conversion of non-tariff barriers into tariff equivalency - Export incentives removed (with the exception of duty drawbacks and export financing schemes)
1998–1999	- Implementation of export processing zones (EPZs) - Rationalized tariff structure
2000	- Signed the SADC Protocol on Trade, which committed it to tariff phase downs on 1 September 2000
2003–2004	- Devaluation of Zimbabwean dollar

Source: Own compilation.

Changes in prices

Implicit tariff index as quantitative indicator of trade policy

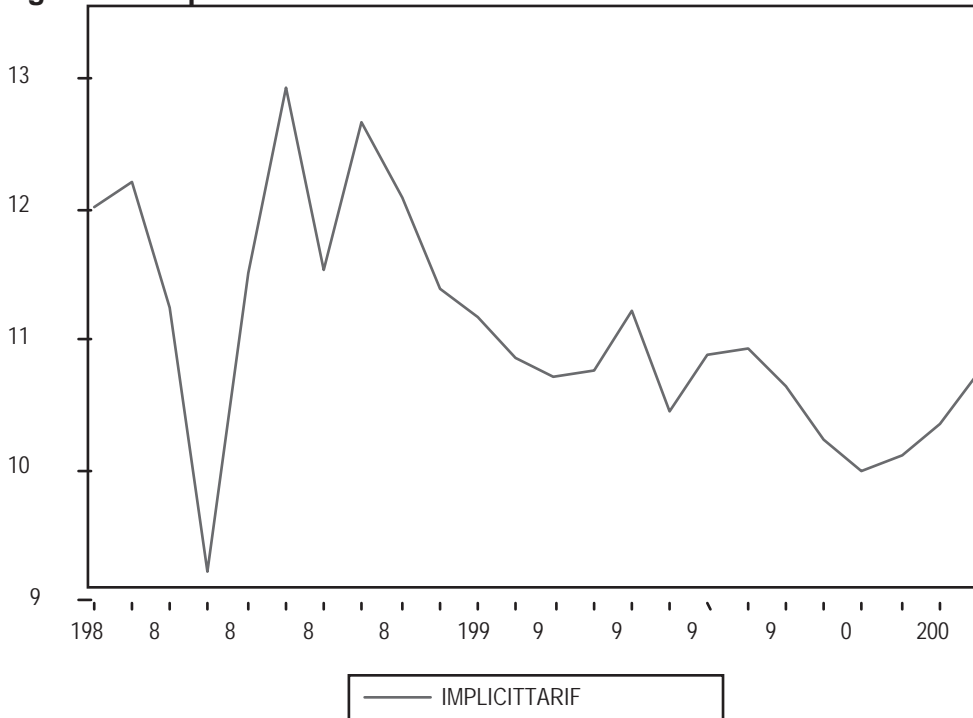
The implicit tariff index is presented and analysed in this section. This tariff traces changes in prices, and is the ratio of the domestic price of given importable relative to their world price (minus one). It captures changes in the nominal rate of protection (NRP), which is the combined effect of nominal tariffs and tariff equivalents of quantitative or non-tariff restrictions. In this section the implicit tariff index consistently refers to the average implicit tariff index for Zimbabwean importables, and was calculated using the average domestic ex-factory price and its world price equivalent for these goods.

Derivation of implicit tariff index for Zimbabwe

The study made use of data from CSO and the IMF International Financial Statistics (IFS) CD-ROM database. Domestic price (ex-factory) of importables were from CSO while c.i.f. import price (in US\$) and the exchange rate (domestic currency per US\$) were from IFS. These data were at aggregate level. Figure 1 depicts the implicit tariff index for Zimbabwe for the period 1980-2003. The index showed a general fall in the

nominal rate of protection for Zimbabwe for the period 1988 through 2003, although there were variations in between. (The horizontal axis shows the years, while the vertical axis indicates the implicit tariff index values).

Figure 1: Implicit tariff index for Zimbabwe: 1980–2003



Instead of calculating the implicit tariff index monthly or quarterly, data limitations forced the study to only derive the implicit tariff index at the annual level. Therefore, the index may not be a sufficient guide if one wishes to investigate speculative behaviour in response to changes in trade policy which took place on monthly/quarterly basis. For example, if more than one policy change takes place during one year, they may even out one another in the annual index, but still induce speculative behaviour. Yet a quantitative index is important as it can tell us whether trade at the aggregate level became any more liberal after a series of relaxations and subsequent tightening of quantitative restrictions (QRs) over time.

Implicit tariff index versus a narrative of liberalization episodes

Based on changes in trade policy instruments alone, a number of trade liberalization episodes can be distinguished for Zimbabwe for the pre-ESAP, ESAP and post-ESAP periods. This study briefly describes each episode as a narrative of events. The narrative is then compared with the corresponding implicit tariff index reading in order to determine whether the observable changes in trade policy are reflected in the index (that is, at the aggregate level), or alternatively, whether the chosen quantitative measure of trade policy picks up known changes.

The pre-ESAP period was characterized by an independent Zimbabwe inheriting an ISI strategy whose tenets included import controls, price and exchange rates controls. However, due to massive government expenditure in the two to three years following independence, especially on infrastructure (roads, schools and hospitals) activities, there was a need for imports to aid those activities and as such import tariffs had to be supportive. This is picked by the fall in the index from 1981 to 1983 (Figure 1). The drought of 1982–1984 and the severe foreign currency shortages of 1987 had the government attempting to minimize BOP problems: it introduced controls ranging from import licences to foreign currency controls. As such, the tariff index reflected this trend.

With the introduction of ESAP in 1991 came major changes in government policies across the board. The programme meant the move towards implementation of structural adjustment programmes and a lot of policy adjustments had to be made. ESAP was a comprehensive programme that aimed to reorient the economy towards market-driven development. Trade liberalization was among its major components. Trade liberalization meant that government controls over allocations of foreign exchange and import licences were dismantled gradually over five years (1991–1995) by sequentially putting import goods on an OGIL list. Such goods could be imported in any quantity without import permits. However, the original plan was altered after a couple of years and the Export Retention Scheme (ERS) replaced OGIL. ERS allowed exporters to retain part of their foreign earnings in the form of import certificates and to sell these at a market-determined price. During the course of the reform the foreign exchange allocations were reduced and in January 1994 both OGIL and ERS were abolished. Subsequently, market forces determined the exchange rate, although with occasional interventions by the Reserve Bank (Bjurk and Durevall, 2000). As can be seen in Figure 1, this trend is partially depicted for 1991 to 1992. Tightening of import controls is evident beginning 1993 and peaking in 1994, a scenario that is not supported by trade policies that were being implemented in those years (Figure 1).

Several changes occurred during the post-ESAP era. By subdividing this period, 1995 through to 1997 coincided with the implementation of WTO commitments, which called for tariffication of non-tariff barriers (NTBs) and reduced import duties. The tariff index, however, showed a picture of tightening of import controls. A possible explanation could be that the conversion of NTBs resulted in relatively higher import duty for a given imported product than in the case where mixed duty (ad valorem and non-ad valorem duty) was used; the general environment was therefore that of restricted trade.

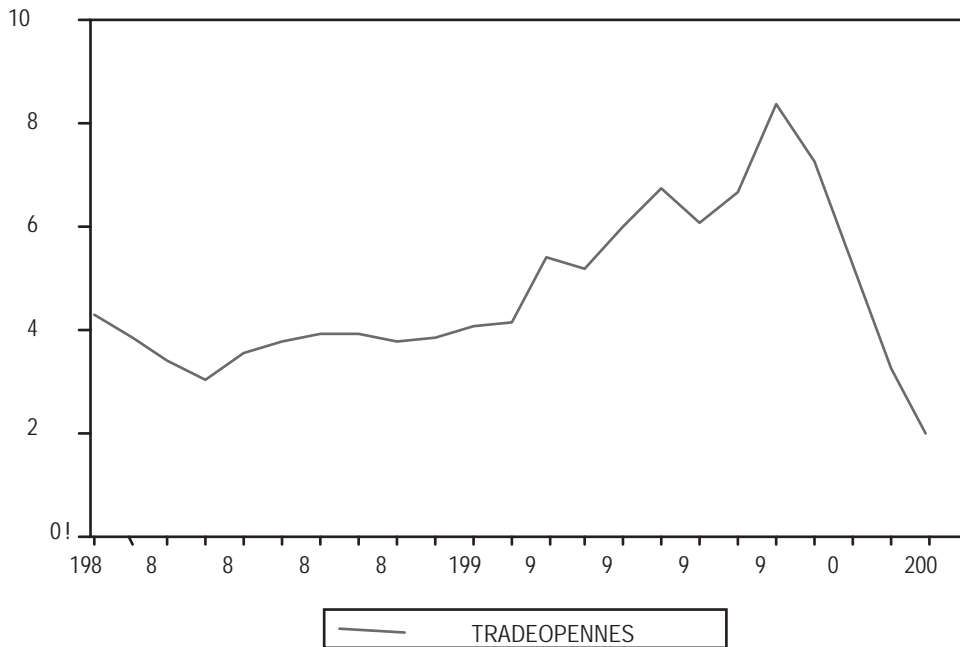
Policy reversals started in 1998, and the index only picked these changes, especially from 2000. Because of the failure of the ESAP programme (from government's point of view) and the beginning of domestic macroeconomic problems, the government reversed some of the policies it wanted implemented. Import licences were introduced; the exchange rate was pegged; while FCAs were suspended. Furthermore, the applied most favoured nation (MFN) import tariffs were increased. Although the country started implementing the SADC tariff phase down schedule in 2001, the negative impacts of the other mentioned policy changes outweighed the SADC tariff phase down.

Changes in quantities

Trade intensity measure

The trade openness index/trade intensity measure (Figure 2) shows the merchandise trade for the period 1980-2003. This index does not correctly trace the trade liberalization of Zimbabwe (especially for the period up to 1998) as spelt out in the respective trade policies which were implemented then. (The horizontal axis shows the years, while the vertical axis indicates the trade openness index values)

Figure 2: Trade openness index

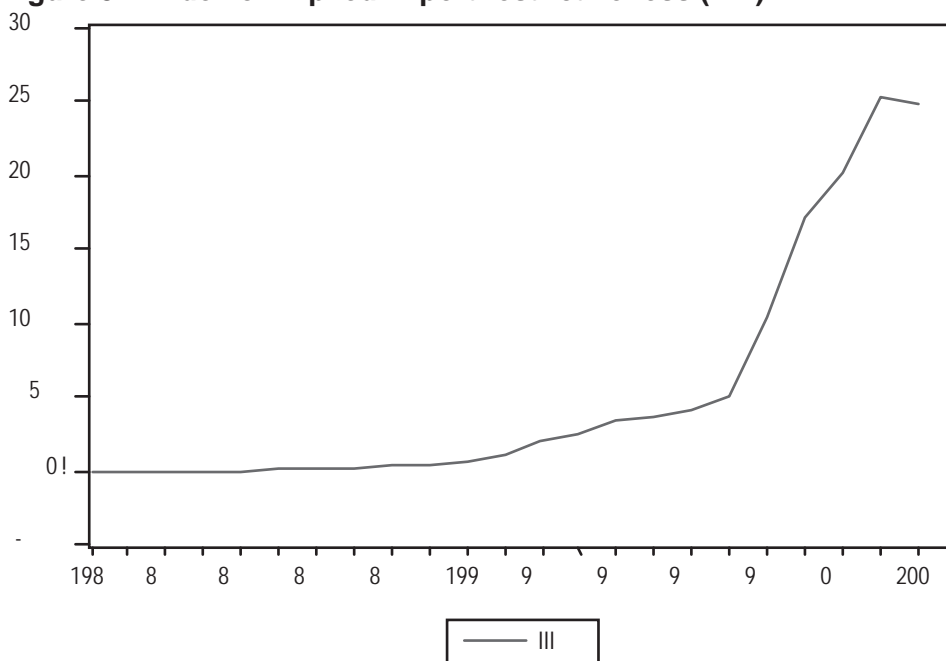


Although the index partially depicted the liberalization in the early 1980s (though in a lag fashion), overall it showed a general increasing openness from 1984 until 1998. For this period, the index did not pick the various anti-liberalization policies that were implemented in between. As pointed out earlier, the failure of this measure to reflect the various trade policies may be attributed to its inability to dichotomize the financing of imports, either by export revenue or by capital flows. For the period under study, up to 1998, Zimbabwe had had considerable capital inflows in the form of aid and donor funds, besides export revenue. The index, however, closely picked the liberalization trend from 1999 to 2002.

Notional imports—Index of implied import restrictiveness (IIIR)

In this sub-section the study derived IIIR which can capture changes in access to imports. IIIR is the percentage deviation of the log of notional imports from the log of actual imports. The higher the percentage deviation, the more difficult it is to access imports. IIIR for Zimbabwe is depicted in Figure 3 for the period 1980-2003. (The horizontal axis shows the years, while the vertical axis indicates the IIIR index values)

Figure 3: Index of implied import restrictiveness (IIIR)



The index was calculated following Narasimhan and Prichett (1993). Data on real exchange rates and imports was obtained from IFS, while real income (GDP) figures were obtained from World Bank development indicators database.

This IIIR index did not pick all the import tariff changes that occurred before 1997. In fact, until 1997 it showed that notional imports and actual imports were more or less equal, especially before 1990; thereafter the difference between the two series started to occur. The index indicated that the actual demand for imports was below its notional demand from 1991, a scenario that indicates tightening of imports controls. One of the possible reasons why the two import series did not deviate from each other, especially in the late 1980s, could be because the imports mainly comprised essential goods which the country could not do without. Among these goods were fuel, medical drugs, capital equipment and input raw materials. From 1991 the percentage deviation started to significantly increase. While trade policies from 1991 onwards were towards liberalization (under the ESAP programme), a possible explanation for the deviation could be the fact that there were changes in consumer preferences towards imported goods brought about by liberalization.

The period between 1997 and 2002 is pictured as having a percentage deviation of greater than 50%, reaching slightly above 250% in 2002 (Figure 3). Although the various trade policies that were implemented during this period and the implicit tariff index in Figure 2 showed some upswing, IIR depicted a different trend altogether. At least two reasons could be put forward to explain the difference between IIR and the implicit tariff index. Firstly, the algebraic difference between the two showed that the implicit tariff index is a weighted average calculation while IIR is merely a subtraction of one series from the other, hence more sensitive to absolute differences. Secondly, although some policies should have brought the notional and actual imports series closer to each other, one major problem that has bedevilled the economy is foreign currency shortage. Therefore, in as much as other trade policies may have been liberalized, imports continued to be curtailed by unavailability of foreign currency.

Summary of extent of trade liberalization from the three approaches

Table 6 provides a summary of the extent of trade liberalization based on the three approaches explained above. The tabulated overall conclusion showed that since independence in 1980, Zimbabwe partially liberalized its trade regime between 1980 and 1990 and also between 1991 and 1995 while the country's trade regime was not liberal for the period 1996-2004. Zimbabwe's trade regime, therefore, was not liberal (Table 6).

Table 6: Summary of the extent of liberalization from the three approaches

Trade liberalization indicator	Trade Policy regime	Period		
		1980–1990	1991–1995	1996–2004
Changes in policies	Liberal		x	
	Partially liberal			
	Not liberal	x		x
Changes in prices	Liberal			
	Partially liberal	x	x	
	Not liberal			x
Changes in quantities (Openness)	Liberal		x	
	Partially liberal	x		
	Not liberal			x
Changes in quantities (IIR)	Liberal	x		
	Partially liberal		x	
	Not liberal			x
Conclusion (Combined)	Liberal			
	Partially liberal	x	x	
	Not liberal			x

Source: Own compilation.

6. Credibility and sustainability of trade liberalization

Collier et al. (1999) argue that there are basically three necessary conditions for trade liberalization to be credible: macroeconomic compatibility, the absence of systematic forecastability and time consistency. This section analysed Zimbabwe's trade liberalization with regards to its credibility and sustainability following these three conditions.

Macroeconomic compatibility

Macroeconomic compatibility constitutes two sub-components, balance of payments and fiscal balance.

Payments compatibility

Economic theory postulates that the BOP is in equilibrium when private domestic agents willingly hold the supply of money. Trade liberalization like the one in Zimbabwe, which lowers implicit tariffs without changing other policies, lowers the domestic price of importables which then lowers the price level since importables are part of the expenditure. This will in turn reduce the transaction demand for money which is a function of the price level and the quantity of expenditure and the resulting excess supply of money is a payments deficit. Trade reform in Zimbabwe has been achieved through a series of exchange rate devaluations. Zimbabwe liberalized its trade restrictions too generously relative to the depreciation of the exchange rate and this gave rise to an unsustainable BOP deficit (Ncube et al., 1999). During the first phase of liberalization (that is, between 1990 and 1991) Zimbabwe liberalized her imports extensively and they increased in dollar terms by 24% compared with before the liberalization period. Exports remained

constant and the country did not experience any depreciation of the currency. This led to a huge current account deficit of around US\$500 million by 1991. Signs of payments incompatibility were noticed, as imports became too cheap resulting in private agents, especially in the manufacturing sector, engaging in speculative behaviour by hoarding most of their imported raw materials.

With the existing payments incompatibility, the government had to devalue the currency to restore compatibility. However, this was seriously affected by the 1992 drought and the ensuing financial liberalization. The government had to borrow to procure food and this resulted in the current account deficit rising to US\$842 million. Ncube et al. (1999) estimated that there was a payments deficit of about 20% and, given such a condition, intelligent private agents speculated that there would be either depreciation or tightening of trade restrictions which resulted in speculative hoarding of imports and deferral of investment due to increased uncertainty. However, with a good rainy season between 1993 and 1994, the country enjoyed increased output that led to a reduction in foreign borrowing and the current account deficit fell to US\$282 in 1993. The devaluations that followed established the real exchange rate at close to its level and by April 1994 there was virtual convergence between the official and market exchange rates.

However, this compatibility was short-lived as the second phase of liberalization showed that the policy was resulting in payments incompatible and could have been conducive to inducing speculative hoarding had it not been for the prevailing high interest rates in the economy. By 1995 Zimbabwe's policy stance was already payments incompatible. This was recognized by private agents who felt firstly that the liberalization process might be reversed; secondly that the government would not allow sufficient exchange rate devaluation; and thirdly that the government was unlikely to have significant expenditure cuts due to the approaching elections.

In an effort to establish a completely home grown programme to address the deficits that came with ESAP, the government introduced ZIMPREST as a successor to ESAP. However, the period from 1996 was characterized by BOP deficits, as the government could not obtain any foreign aid amidst increased capital outflows and referrals on investments. The exchange rate was fixed at US\$1 = Z\$55 between 2000 and 2003 and a major devaluation was done in 2003 to Z\$825. With increased openness of the economy, the agents continued to import whilst exports were falling resulting in a ballooning deficit. The country's foreign reserves continued to fall and reached a low of US\$131 million in 2003 from a high of US\$830 million in 1996. Up to 2004 private agents had lost any clear direction on the government's liberalization policy and they continued with the speculative behaviour. This resulted in agents not sending any of the earned foreign currency to the official market leading to a thriving parallel market for foreign currency.

Given that the exchange rate was fixed, the short-run consequence of trade liberalization was the worsening of the current account. At the same time, since funds were not available to finance the deficit, the country had to eat into its reserves. As the deficit ballooned trade liberalization became increasingly unsustainable.

The above situation caused a serious problem as far as consistency of trade reform was concerned. Without access to adequate financing coupled with the worsening of the current account balance, trade liberalization in Zimbabwe became increasingly unviable

after 2000. When private agents took this into account, they could not consider the reform as credible. Despite the increased efforts by the government to put new incentives for business, economic agents failed to respond by investing. The chance of running into a short-run consistency problem is higher the stronger the overall investment response. A trade reform that stimulates total investments requires substantial imports of investment goods above the imports directly following from reform. Hence, depending on the foreign exchange constraint, it may be the case that only trade reforms that fail to stimulate investments are consistent with the short-run foreign exchange constraint.

The flexible exchange rate regime solved the financing problem of the fixed exchange rate regime. A depreciation that followed had the effect of cutting drastically into unskilled workers real wages resulting in a huge destabilizing deprivation of a large section of the population. The short-run consistency problems of the fixed exchange rate regime resurfaced as social unrest and strikes emerged when the real wage drop became bigger. The unrest between 1998 and 2000 may have been a result of these developments and such unrest could have caused the government to reverse the trade liberalization. In cases like these, reforms could only have been made credible if the economic agents believed that the government was committed to liberalization. These developments have seriously depressed investments. The ensuing land redistribution programme that came with increased economic challenges had catastrophic consequences both for investments and production.

The abortion of trade reform in Zimbabwe could have been due to self-fulfilling expectations. That is, trade reform succeeds if it is expected to succeed while it fails if it is expected to fail. The reason for the failure was largely the lack of foreign exchange. Because the current account balance failed to improve, the government was forced to reinstate trade controls. Hence, expectations about failure could have proved self-fulfilling as the lack of investment response itself generates prolonged trade deficits leading to the abortion of reform.

Fiscal compatibility

Trade liberalization tends to have significant impacts on revenues and expenditure. Zimbabwe has always used tariffs as instruments to raise revenues; as such the government retained high taxes, tariffs and surcharges to ensure that it gets adequate revenues. Since 1991, the trade liberalization process in Zimbabwe has caused a substantial deterioration in the budget with the country experiencing a 13.4% budget deficit in 1995. By 2000, the budget deficit had reached 19.6% (Reserve Bank of Zimbabwe, 2003). These figures point to the fact that the policy stance was fiscally incompatible.

System forecasting

As pointed by Collier et al. (1999), the idea that some aspects of macroeconomic policy might be systematically forecastable and that this would alter the effectiveness of policy is due to Robert Lucas. Zimbabwe's trade policy has generally been responsive

rather than proactive. That is, the trade policy has been altered in response to the state of the world, and that has made the trade policy endogenous. For example, as alluded to under payments compatibility, to deal with payments incompatibility the government had to alter its trade liberalization policy by means of currency devaluations which saw massive devaluation of the local currency to the US dollar of 92%, 19% and 41% in December 1991, January 1993 and January 1994 respectively (Reserve Bank of Zimbabwe, 2004). The presence of external shocks over the years, such as the 1991/1992 drought, 1998 food riots and 2000 land reform, meant that a majority of the citizens expected the government to change the trade policy. Thus, such actions made the trade policy predictable from the public's point of view and this meant that the policy was not credible.

Time consistency

A key conclusion from literature is that timing of reforms matters. Ncube et al. (1999) note that time inconsistency is a potential political trap and if the trap exists the very actions that would lead to the success of the liberalization process in economic terms would lead to it being reversed politically. Private agents always question whether government has a rationale for liberalizing now and subsequently reversing the liberalization process.

For Zimbabwe, liberalization was not mainly affected by time inconsistency as the government inherited the control regime from UDI. Hence, the control regime was to an extent an "accident" and the country had every good reason to dismantle it. Moreover, the politics of decontrol in Zimbabwe was predominantly internal rather than being imposed by Western donors. Zimbabwe's industry, through the input from the Confederation of Zimbabwe Industries (CZI), opted to move from being pro-control to being pro-liberalization as this was likely to ensure increased access to foreign markets and accessibility of inputs from other countries, especially to an economy emerging from siege. This gave the government the need to adopt liberalization not as a short-term strategy but rather a long-term one.

However, during the liberalization process, in the mid 1990s, agents could not view the liberalization process as time inconsistent. Whilst this did not mean there was no potential for policy reversals, it meant there was no political trap whereby economic success would lead to political failure. Nevertheless, during the late 1990s, when the country started to experience numerous challenges, the government had to try to maintain credible expectations. With increased BOP, increased fiscal deficits, the government failed to fulfil the expectations of industry.

The only element of time inconsistency in Zimbabwe came from the foreign aid linked to the liberalization programme. This, according to Ncube et al. (1999), has the potential to appear as a deal in which reform is the price the government pays in return for the aid. However, for Zimbabwe aid was considered temporary considering that the country was destined to achieve substantial growth rates. The government did not start liberalization from a position of economic crisis hence was not desperate for aid.

The country's liberalization process could not be seen as time inconsistent by well informed private agents. This, however, does not mean there was no potential for policy

reversal, but that there was no political trap whereby economic success would lead to political failure

Political economy of trade liberalization

The political environments within which economic agents operate have an important influence on the range of information available to them as well as the set of incentives and disincentives. Bigsten and Durevall (2003) argue that successful economic reform requires an underpinning of sound institutions which includes secure property rights; agencies that regulate the conduct in goods, services, labour, asset and financial markets; fiscal and monetary institutions to maintain macroeconomic stability; institutions for social insurance; and institutions for conflict management. Like most African countries, Zimbabwe's political environment has been typified by severe restrictions on political and civil liberties. A glimpse at political rights and civil liberties indexes from Freedom House shows that the country's ratings since independence have been above 4, indicating a repressive environment according to this index's criteria.⁵

The country's one-party rule has been championing the economy's trade policy for the whole period under review (1980–2004). As a way of trying to get the inputs of producers before the adoption of the first meaningful economic liberalization reform (ESAP), the government made some consultations (in the period 1988–1990) with organizations such as CZI, the Zimbabwe National Chamber of Commerce (ZNCC) and the Commercial Farmers Union (CFU). Overall, these producer organizations supported liberalization, as they believed that the new policy would be a panacea for economic problems such as low investment, insufficient export incentives, restrictive trade policy, foreign currency access and promotion of export incentives (Ncube et al., 1999). However, the trade policies, especially with regards to tariff hikes, which took place in 1998 were a product of government dictated decisions justified by reference to the country's BOP problems (deficits). Thus, government effected most policy reversals without any serious consultations, if any, with the non-public sector.

Although the main purpose of any trade policy reform is supposed to result in the betterment of the country and its citizens, Davies (2004) argues that, overall, the country's economic reforms since independence have been shaped to benefit individual politicians within the ruling party and not necessarily to benefit the economy. Thus, though the country has been hailed to have implemented some of the reform programmes during ESAP quicker than the scheduled timetable, World Bank officials, who were helping the country implement some of these policies, considered the move to be unwise. Specifically, World Bank officials regarded the faster implementation of these programmes "as needlessly creating hardship and political antagonism for no gain privately" (Davies, 2004: 12).

7. Conclusions and policy recommendations

The study's choice of three approaches (that is, changes in policy, changes in quantities and changes in price) for the analysis of trade policy for Zimbabwe has shown that trade liberalization was not consistent with the policies that the government implemented between 1980 and 2004.

The study also found out that the country's liberalization process was credible and sustainable for the period 1991-1995, after which credibility was lost and the liberalization process became unsustainable. Reduced credibility was a direct result of policy reversals that were instituted after 1995 while accumulated BOP deficits and budget deficits resulted in payments incompatibility, thus making trade liberalization unsustainable. The study also found that the political economy of the whole trade liberalization process was largely dominated by government (and to some extent individual politicians) with minimal input from the private sector (that is, producers and consumers).

The analysis, therefore, pointed to one main policy recommendation: for the country to reap the benefits of trade liberalization, it has to be consistent in its trade policy. Whilst in the short term, negative effects (in the form of reduced government revenue, for example) maybe experienced, it is in the long run that benefits start to accrue. Policy makers also need to be reminded that trade liberalization should be a process not an event and therefore a long time horizon is required when formulating and implementing trade liberalization policies.

Notes

1. The authors believe this methodology to be suitable to deal with the first objective.
2. The Keynesian framework expresses: $GDP = \text{consumption} + \text{investment} + \text{government expenditure} + \text{exports} - \text{imports}$.
3. The Washington Consensus is a set of policies promulgated by many neoliberal economists as a formula for promoting economic growth in many parts of Latin America and other parts of the world by introducing various market-oriented economic reforms. These reforms are designed to make the target economy more like that of developed countries such as the United States. These policies include: fiscal discipline, redirection of public expenditure, tax reform, interest rate liberalization, a comparative exchange rate, trade liberalization, liberalization of inflows of foreign direct investment, privatization, deregulation and secure property rights.
4. Whilst the period of study is 1980 to 2004, the authors only managed to find meaningful trade related components of liberalization for the period 1990 to 2004.
5. Both ratings are calculated on a scale of 1–7, with a score of 7 indicating the most repressive societies. Zimbabwe's political rights and civil liberties' rates have been oscillating between 3 and 4 for the period 1980 to 1986, while from 1987 onwards the indexes for both categories were oscillating between 6 and 7, indicating a repressive environment.

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