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# SUSTAINABLE AGRICULTURAL DEVELOPMENT: THE ROLE OF INTERNATIONAL COOPERATION

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## INTRODUCTION

Over the last 50 years the economic performance of most developing countries and of all Eastern European countries has been disappointing. Moreover, the last five years have led to the fall of Eastern Europe's postwar political and economic system. There seems to be agreement that socialist economies have proved less efficient than market economies. Hence, most Eastern European countries (including the Soviet Union) are in the process of adopting market economies. Similar changes are occurring in many developing countries.

Of course, I do not dare challenge the widely accepted argument that markets are one of mankind's most important social inventions (Meade). Instead, I intend to consider whether specific shortcomings of agricultural markets can only be rectified by government interference. The reasoning is based on Corden's statement that 'theory does not "say" – as is often asserted by the ill-informed or the badly taught – that "free trade is best". It says that, given certain assumptions, it is "best"' (1974, p. 7). The task of this paper is to discuss whether the performance of agricultural markets can be, and has actually been, improved by government interference, in developed and developing countries, and in those in transition between socialism and markets.

## CLARIFICATION OF CONCEPTS AND DEFINITIONS

Markets are institutional arrangements which facilitate the exchange of goods and services and, thus, allow for the division of labour. A free market, that is a market without government interference, is efficient if it results in a higher level of individual utility than any other means of coordinating economic decisions, such as bureaucracy (central planning), dictatorship, voting or negotiating. Economists often assume that markets are efficient if they are Pareto-efficient, that is if it is not possible to increase the welfare of one individual without impairing the welfare of others. It has to be noted that this definition of efficiency is based on value judgements as it neglects distributional aspects and relies on the individualistic paradigm. Managed markets are ones in which government interference is employed in the pursuit of certain

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objectives. Managed markets are efficient if they result in a higher level of individual utility than free markets.

As with the term 'efficiency', any definition of agricultural development will necessarily be based on value judgements. It is plausible that policy makers in developed countries will have a different perception of agricultural development from those in developing countries. Both are likely to employ a broad definition of 'development' which includes more dimensions than agricultural productivity alone. The present state of government interference in agricultural markets is supposedly the consequence of a wide set of policy objectives. Hence the question is whether free markets are better than managed markets at generating allocative efficiency and satisfying other selected policy objectives.

One problem requires initial clarification. While it may be possible to model the agricultural sector and the overall economy under free market conditions it is less clear what kind of managed markets should be used for comparison. One point of reference could be markets managed in an optimal way to overcome the deficiencies of free markets. Markets managed in this way would, by definition, be more efficient than free markets. An alternative would be to take the present state of market intervention as a reference and to investigate whether free markets would be more efficient.

## THE CASE OF DEVELOPED COUNTRIES

Free trade advocates generally blame agricultural policy makers for the high degree of protection in most developed countries. Some even wonder why the General Agreement on Tariffs and Trade (GATT) is needed to lower protection rates since individual countries should have an interest in reducing protection themselves. If there is any economic rationale for the present degree of protection it must lie either in failure of free agricultural markets to maximize economic efficiency or in pursuit of policy objectives which cannot be maximized by market forces alone.

Arrow and Debreu have demonstrated that market economies are only Pareto-efficient under certain circumstances, such as a complete set of markets and perfect information (Stiglitz, 1986, p. 257). As these conditions are not met in reality, there *may* exist a set of taxes, subsidies and broader government interference which *could* make everyone better off. However, there is general agreement among policy analysts that the present state of interference in developed countries is not cost-efficient and not necessarily an improvement on the situation which would otherwise prevail. Past experience will be discussed in relation to five statements.

*First, free markets have most likely become more efficient in directing agricultural development than they were in the past.*

— The price instability supposedly inherent in free agricultural markets has been used to justify intervention. However, prices would be less unstable now, under free trade, than they would have been in the past because the regional and intertemporal integration of markets has improved. Lower communica-

tion, transport and storage costs as well as institutions such as futures markets and insurance schemes would contribute to more stable prices.

— Market intervention is mainly pursued because agricultural incomes are supposedly too low under free market conditions. However, if labour markets are highly integrated, differentials in labour income will reflect opportunity costs. Interference on product markets, which is the predominant type of intervention, will have a greater effect on the number of people employed in the sector than on their labour income per unit of time.

*Second, present policies have become increasingly inefficient over time.*

— According to the previous statement, the economic environment has changed. Hence policies should also have changed to remain efficient. However, experience teaches that fundamental changes in policies are rare. Instead, policy measures are difficult to reform and the reform which does occur rarely implies changes in the set of policy instruments, but only the addition of new policy instruments (Petit, 1989).

— As the agricultural sector becomes more integrated into the general economy, old policy instruments, especially interference on product markets, become less efficient in transferring income to farmers.

*Third, policy evaluation based on the pure theory of welfare economics can be misleading, because it neglects both the costs of regulation, fraud and evasion, and political economy aspects.*

— Based on welfare economics, a hierarchy of policies can be set up for any given externality. For example, deficiency payment systems are supposedly superior to direct price support for correcting externalities on factor or product markets. However, experience in the EC – the tomato and olive oil scandals – illustrates that deficiency payment systems open the door to fraud. The same holds true for personal transfer payments if the group of recipients is open-ended. The attractive German social security system for farmers has enticed many non-farmers to enter agriculture on a part-time basis.

— Reasoning based on pure welfare economics ranks uniform protection rates higher than non-uniform protection rates. However, import control is much easier than export control. EC experience proves that administrative costs rise and fraud is much more prevalent if protection covers export commodities. The EC, for example, agreed to participate in the embargo of the Soviet Union in 1980. While it can be assumed that the EC administration tried to enforce this embargo, EC agricultural exports to the Soviet Union increased by roughly 500 per cent over the preceding years in 1980.

*Fourth, the performance of agricultural markets and agricultural development are not mainly directed by government intervention on agricultural markets, but by macro-economic policies and the macro-economic environment.*

— The importance of the exchange rate for agriculture in the United States has been analysed in detail by Schuh (1976, 1981).

— The experience gained from the liberalization of New Zealand's economy (Sandrey and Reynolds, 1990) illustrates the importance of the macroeconomic environment for agriculture.

— Experience gained in the EC supports the hypothesis that unemployment and wage rates in non-farm sectors have a greater influence on farmers' income than agricultural policies.

*Fifth, economists could play a greater role in reforming policies in developed countries if they focused their research more on the effects of alternative institutions and the ex post evaluation of policies.*

— There is ample evidence that the outcome of policy decisions depends on existing institutions. The EC's agricultural financial system, for example, leads to divergent national interests that make it difficult to reach decisions which are in line with overall EC welfare.

— Continuing evaluation is needed to inform policy makers *and* the public of the effects of past policies as compared to alternatives. This might encourage policy makers to act more in the public interest and less in the sole interest of the farming community. Evaluation should also measure the institutional costs of regulation, such as administrative and lobbying costs, and fraud.

### THE CASE OF DEVELOPING ECONOMIES

Developing countries rely even less than developed countries on markets for directing agricultural development. Equity and food security arguments make it understandable that developing countries intervene more. However, the decline or stagnation of many developing economies has most likely been abetted by government interference. In the following discussion I draw attention first to external and then to internal trade in agricultural products.

#### *Misleading arguments for external trade interference*

Some countries intervene in external agricultural trade because they espouse a particular definition of food security, namely autarky. Such a policy *cannot* be called efficient, either in terms of pure economic efficiency or in terms of food security. In general, a country can best feed its population if it participates in the international division of labour and abstains from autarkic policies (McIntire, 1981; Valdés and Siamwalla, 1988, pp. 103).

#### *Plausible arguments for external trade interference*

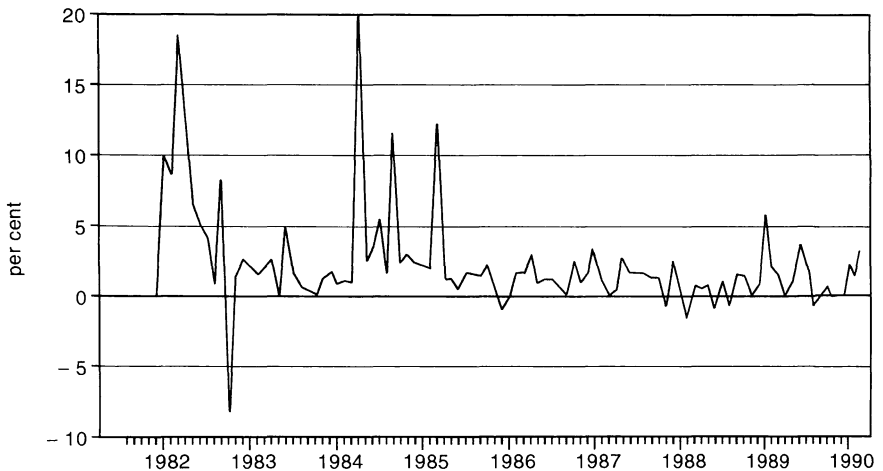
Past research has illustrated the importance of macro-economic policies and especially exchange rates for agricultural development (Valdés, 1989). Free agricultural trade can hardly be recommended if exchange controls are applied and a foreign exchange allocation system is in place. Exchange controls normally imply over-valuation and depressed prices for tradables such as agricultural products. Under these conditions, agricultural markets will not be able to play their normal role in directing agricultural development.

However, even if market exchange rates do reflect the shadow prices of foreign exchange, free external trade *may not* maximize economic efficiency and contribute to food security in an efficient way. First, intervention in foreign trade may be advisable because of unstable import or export parity prices. This instability can be caused by fluctuations in world market prices

for agricultural commodities and/or exchange rates, although the second cause is most likely more relevant for developing than for developed countries, as the fluctuations of the Chilean Peso against the US Dollar illustrate (Figure 1). Since developing countries have not yet established institutions such as future markets which help farmers to reduce the risk of exchange rate and commodity price fluctuations, and because farmers in developing countries are more risk-averse than those in developed countries, governments may be well advised to stabilize import and export prices within a price band, as has been done in Chile (Muchnik and Allue, 1991, pp. 67).

Second, interference in external agricultural trade may also improve internal allocation and food security in the case of land-locked countries which are characterized by a wide margin between import and export parity prices. Koester (1986) reports that export parity prices for maize at some locations in South-East Africa were negative in 1977/8, while import parity prices at most locations were twice as high as world market prices at East African ports. Some of these countries are self-sufficient in normal years but either exporters or importers in others. In such a situation, world market prices would destabilize internal markets. Moreover, since private traders and stockholders face significant risks in holding carry-over stocks, free markets will not result in a

**FIGURE 1** *Monthly parity change Chilean peso against US dollar*



cost-efficient trade-off between external trade and stockpiling. Interference in the storage sector might improve welfare and food security.

Third, there is evidence that many developing countries aim at perfect self-sufficiency in food even in cases in which they could be exporters. Their export potential might not be used because export markets are not secure and planning for exports is too risky. This risk can follow from (a) variability in production which makes the potential exporter an unreliable source of supply for importers; (b) variability in production in importing countries which makes the demand for exports unreliable; and (c) variability in export prices due to unstable world market prices. If potential exporters want to mature as reliable sources of supply they have to hold large volumes of stocks that are unlikely to be held without government assistance.

Fourth, the need to produce public goods may justify other types of intervention in external trade. Taxing agricultural exports may be necessary to generate public revenue. This cause of interference is not due to market failure in agriculture, but to market failure elsewhere (Stiglitz, 1991, p. 430).

These theoretical arguments for intervention in external agricultural trade do not prove that current intervention in most countries actually increases efficiency. It may be that developing countries would be better off without trade interference because of by-product distortions and poorly designed policies. There is ample evidence that countries which have interfered less have performed better than others (Papageorgiou, Choksi and Michaely, 1990). The latter have, in many cases, merely substituted policy failure for market failure. Empirical studies in the last decade have contributed to our understanding of the political economy of state interference, lending support to the notion that it is better to accept some market failure in order to avoid the effects of policy failure (Krueger, 1990; Jones and Krueger, 1990).

There is some concern that external trade liberalization by a group of similar countries – for example neighbouring countries in Africa – could depress world market prices and make them worse off since all would seek to export the same commodities. However, empirical studies do not support this presumption (Koester, Schafer and Valdés, 1990; DeRosa and Greene, 1991).

### *Internal trade*

Internal trade in agricultural products is heavily regulated in most developing countries. Policy makers often claim that food security is so important that it cannot be left to the vagaries of the market. There are some reasonable arguments which support the thesis of inefficient internal agricultural markets. First, functioning markets depend on institutions which define and secure property rights and which facilitate the exchange of commodities. If these institutions do not exist in the early stages of development, a rationale for state interference exists. Second, wealth and income distribution – both of which affect the outcome of the market process – are very uneven in many developing countries. Hence the market may yield results which are unacceptable for society and some interference may be justified.



However, this does not imply that all governments which rely less on markets and more on intervention are actually accelerating agricultural development. While it is difficult to identify all those policies in developing countries which actually contribute to economic efficiency, equity and/or food security, it is possible to specify which policies are most likely to be counterproductive with respect to such objectives.

Many governments, especially in Africa, mistrust private traders and support monopolistic parastatals which conduct trade in the main agricultural commodities. These parastatals are supposed to implement the governments' food policy via guaranteed prices. However, there is evidence that marketing margins in African countries are higher than in other developing countries, owing to parastatals (Ahmed, 1988). Furthermore, numerous studies prove the inefficiency of parastatal pricing policies, especially if pan-seasonal and pan-territorial prices are enforced. Under these conditions, prices on parallel markets are more unstable than under a more liberal system, and private stockpiling and transport are crowded out. The consequential reduced use of traditional storage and transport systems places an additional drain on the public sector and results in economic costs for the society.

It is probably true that market failures are more severe than elsewhere in poor and backward countries, but the same is also true of government failure (Stern, 1991, p. 429). Interference, which may be based on sound arguments, can often not be implemented adequately because of a lack of manpower and information, and the influence of interest groups. It is mainly as a result of the political economy of intervention that trade interference in domestic markets is so inefficient. The fact that many countries are reluctant to liberalize internal trade, despite evidence that current intervention conflicts with all or most of the officially stated objectives, is also due to political considerations.

### TRANSFORMING A COMMAND ECONOMY INTO A MARKET ECONOMY

Most Eastern European and some developing countries are in the process of moving from a command to a market economy. It is hoped that allowing market forces to direct development will improve economic performance. However, the evidence so far is not at all overwhelming. It indicates that introducing market forces abruptly may not produce the expected results. There are grounds for believing that the state should not – at least for a transition period – withdraw from economic activities. While a government's tasks will be different during this transition period than under the command economy, it may even be that total government activity should increase. The efficiency of markets in directing agricultural development during the transition period will be discussed in relation to external and internal trade interference.

### *External trade*

The formerly centrally planned countries have some freedom in designing their agricultural trade policies because they are not subject to most GATT regulations. Therefore, it seems worthwhile to explore whether they need specific agricultural trade policies.

It is well established in trade theory that the equalization of a nation's domestic and border prices will only maximize economic efficiency if there are no externalities in domestic production or consumption, and the nation is a price taker on world markets. External free trade will not maximize efficiency if domestic markets do not function well, as will be the case when an economy is in transition between socialism and free markets. A lack of market institutions, deficient communication systems, poorly defined property rights, an inadequate legal system and the fact that the population is not acquainted with the workings of a market economy will all contribute to high transaction costs.

A major determinant of transaction costs is the risks involved in the exchange of commodities under uncertainty with respect to future market conditions. A trader who wants to export knows neither the selling price which he will receive when he delivers his products abroad nor the future foreign exchange rate. This price uncertainty is especially high for exporters in countries which are in transition because many institutions, such as futures markets, do not exist. Inadequate communication networks and under-developed trade links enhance this uncertainty. It can be expected that these transaction costs will decline over time if trade is permitted. Since resources might be misallocated if current transaction costs are used as a point of reference, society may be well advised to intervene in foreign trade.

Trade policy could also be used to ease the speed of adjustment. It may be argued that free agricultural trade would cause 'unacceptable' social hardship for the farming population, unemployment and social unrest. This is actually a traditional argument for agricultural protection in many developed countries. However, countries in the transition phase should beware of the lessons learned in developed countries, which indicate that agricultural protectionism tends to become permanent as the farm lobby perennially advances the social hardship argument. Indeed, protectionism, by generating unfounded expectations, may be the cause of future social hardship.

A specific trade policy for agricultural products may help to exploit the trade preferences granted by some developed countries. Preferential access to developed markets may generate direct income transfers if adequate policies are instituted.

Most of these arguments for managed external trade during the transition phase are based on the hypothesis that intervention at the border is more efficient than internal policy measures. This may be the case because governments lack the administrative capacity needed to institute internal measures. However, it should be noted that while trade policy *could* contribute to the achievement of the objectives stated above, whether it does contribute depends very much on the trade situation of the economy and the instruments applied. As noted above, intervention in import trade is easier to administer than intervention in export trade. However, if a country both exports and imports

agricultural products, border protection for imports alone will distort domestic price ratios. By-product distortions will be the consequence. To avoid this, trade measures will also have to include export subsidies which are costly and lead to fraud. Hence countries may be better off restricting intervention to those importables for which the costs of by-product distortions are lower than the expected benefits. It may even be best for a country to abstain from direct trade intervention altogether and concentrate instead on stabilizing import and export prices. In general, in designing agricultural trade policies, countries are well advised to build in flexibility and reversibility. Furthermore, since trade intervention is more easily justified in the transition period than it is in later periods, policies which are hard to abandon or reform should be avoided.

### *Internal trade*

While it may be too early to draw general conclusions from the liberalization experience of the Eastern European countries, some insights can be gained already (Klaus, 1991; Koester, 1991). First, agricultural development does not result from liberalizing agricultural markets alone. More important impulses – at least during the transition period – can be generated by macro-economic stabilization policies. Of particular importance are exchange rates and monetary stability. If the exchange rate is set below the shadow rate, that is, if the currency is revalued as occurred in the case of the German Democratic Republic (GDR), sectors producing tradables, such as agriculture, will be taxed. As a result, the agricultural sector will come under stronger pressure to adjust than it would have at equilibrium exchange rates. The significance of monetary stability in the first stage of the liberalization process can be illustrated for the case of Poland. The inflation rate in Poland was roughly 1000 per cent in the latter part of 1989. Real interest rates were highly negative. Hence storage costs were much lower than expected gains from sales in future periods and there was a strong incentive to withhold supply: Poland faced a shortage of some food supplies despite having an exceptionally good harvest. This situation had completely changed by the middle of 1990. The inflation rate had dropped far more than nominal interest rates, leading to a real interest rate of some 30 to 40 per cent. This interest rate – together with uncertainty about future prices – has made stockpiling an extremely risky undertaking. Hence intertemporal price relationships are very weak, which affects agricultural prices more than others because farm production is highly seasonal. It may be more reasonable from a private point of view not to store between surplus and deficit seasons, but rather to export in the surplus season and to import in the deficit season. Clearly, this can be very costly from a macro-economic point of view. Internal prices will drop to export parity levels in the surplus season and rise to import parity levels in the deficit season. The resulting instability could affect agricultural production adversely and cause social hardship. Hence the government may decide to stabilize internal prices by interfering in the storage sector.

Second, the move to a market economy exerts pressure on collective farms to adjust. The agricultural sector can only cope with this adjustment if the

necessary institutional flexibility exists. For example, if collective farm managers are not allowed to dismiss workers and if the transfer of land is inhibited, then the ability to adjust will be marginal. Hence, the liberalization of product markets must be complemented by changes in the legal and institutional framework. What is needed is not just the removal of old and discredited institutions but their replacement by new institutions which enable markets to function.

Third, liberalization is expected to result in economic benefits because individuals are allowed to respond to private incentives. However, the intensity of this response not only depends on the magnitude of the incentives, but also on human behaviour. If individuals are not used to collecting information, assessing the consequences of alternative actions and accepting risk, then private incentives will not necessarily lead to economic success. Hence the liberalization process must be supported by institutions which coordinate extension, training and the dissemination of market information.

Fourth, the farm sector in command economies was often integrated into the rural economy in a different way from that which prevails in market economies. In the case of the GDR, the entire rural economy was dominated by collective farms and most rural economic and social activities were coordinated by them. If restructuring is left to market forces, many collective farms could collapse as their most profitable branches could be sold off, leaving behind a financially unsound core. Government interference could help to avoid this outcome.

## CONCLUDING REMARKS AND SUMMARY

- (1) There is much support for the hypothesis that markets are not efficient in directing agricultural development. This support can be summarized as follows (Stern, 1991):
  - (a) Market failure reduces the efficiency of agricultural markets. This market failure is more severe in developing countries than in developed countries and is most pronounced in economies that are in a transition phase from a command to a market economy.
  - (b) Societies and governments also pursue non-economic objectives. The income objective is the most important argument for state intervention in developed countries and the food security objective often dominates debates about agricultural policy in developing countries.
  - (c) Governments might be inclined in specific cases to reject the individualistic paradigm underlying a market economy. Individual preferences may be overridden by governments in developing countries that wish to improve food security, or when external effects – including the responsibility for future generations – are taken into account.
- (2) However, these arguments do not necessarily imply that a society with government intervention will be better off than one without. Government or policy failure has to be balanced against the negative effects of

no intervention. There is ample evidence that policy failure is often worse than market failure (Krueger, 1990; Meier, 1990). The causes of policy failure lie not only in suboptimal instruments, timing and intensity, but also in governments that pretend to know more than they really do (Hayek, 1989). Optimistic governments fail to take into account sufficiently the indirect effects and by-product distortions of intervention and their inability to withdraw intervention and change policy tools when circumstances change.

- (3) Nevertheless, it would be an exaggeration to assert that no government intervention is justified. The final judgement depends very much on the state of the economy and on the governments' ability to implement rational policies.

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## DISCUSSION OPENING – WALTER J. ARMBRUSTER\*

Professor Koester is to be commended for his insightful examination of the efficiency of markets in directing agricultural development across the array of industrialized, developing and formerly centrally planned countries. His purpose was to ask whether market performance is improved by government interference in the different stages of development.

Koester defines a free market as being efficient 'if it results in a higher level of individual utility than any other means of coordinating economic decisions...'. He argues that 'managed markets are efficient if they result in a higher level of individual utility than free markets', and then poses the question as to 'whether free markets are better than managed markets at generating allocative efficiency and satisfying other selected policy objectives'.

### *Developed Countries*

As Koester points out, most developed countries practise intervention to correct perceived failures of free market economies to maximize economic efficiency or achieve other policy objectives. One frequent rationale for intervention is to provide adequate information to help markets function better. Environmental goals also frequently trigger intervention because of the difficulties of internalizing the costs involved. Typically, of course, attempts to ensure higher, more stable, or adequate income is a major rationale for intervention. It has become increasingly clear, however, that performance of agricultural markets and agricultural development are affected more by macro-economic policies and influences than by agriculture-specific policies.

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Koester provides supporting evidence for his thesis that current levels of government intervention in developed countries are neither cost-efficient nor always better than what would exist in their absence. He then argues that economists could play a greater role in reforming developed country policies by focusing research more on the effects of alternative institutions and evaluation of policies. They could then inform policy makers and the public of the effects of past policies, leading to future decisions more in the public than in the farmer-specific interest.

His argument is an interesting hypothesis, but one that I think has received ample testing in developed countries. Certainly, within the United States there is a large body of literature analysing policy effects and comparing them with specified alternatives. Evidence suggests that economic analysis may play some role in policy decisions but probably not an overriding one. It takes more than economic analysis to change policies made through the political process. The political arena has many actors with strong self-interest. Agricultural and food system participants have proved skilled at lobbying for and achieving their particular policy goals, even though they may appear narrow, in spite of analyses of public interest impacts. Surely the debate leading up to the Food Security Act of 1985 in the USA ranks it as one of the most widely analysed and discussed agricultural policy development processes ever. Yet many question the effectiveness of all that input in shaping the final content of legislation.

I pose two questions for agricultural economists. Has an adequate amount of sound economic analysis been conducted on policy alternatives in most countries? Is it possible to increase the influence of economic analysis to achieve better subsequent policy and, if so, how?

### *Developing countries*

Koester believes that developing countries interfere with the market even more than developed countries in directing agricultural development. He identifies plausible arguments for external trade interference which are supported by studies cited. However, he argues that 'these theoretical arguments for intervention in external agricultural trade do not prove that current intervention in most countries actually increases efficiency'. He concludes that it is better to accept some market failure in order to avoid the effects of policy failure.

While this is an interesting conclusion, its application leaves me somewhat perplexed. How much market failure is acceptable to avoid the effects of policy failure? Can economists adequately measure various degrees of market failure and determine the trade-offs with possible policy failure? Or would it be better to adopt policies to deal with perceived market failures but concentrate on designing them so that they correct the market failure and phase out when that is achieved?

Turning to internal agricultural trade, Koester argues that the market may yield results unacceptable to society, since wealth and income distribution, which integrally influence market outcomes, are so uneven in many developing

countries. Particularly in early stages of development, some interference may be justified to facilitate exchange of commodities.

As Koester sees it, while interference may be justified by sound intellectual arguments, implementation is often difficult. Besides lack of manpower and information, the influence of interest groups also affects implementation and leads to inefficiency best described as the much dreaded policy failure. He then concludes that many countries hesitate to liberalize internal trade even in the face of evidence that policies fail to meet official objectives because political considerations override.

I do not find that conclusion very startling, since any intervention in a market economy is driven by the political process which determines its type and level. Once created there is a tendency for 'property rights' to be appropriated by participants in the marketing system. This increases the difficulty of reversing policies initiated by groups with enough political strength to obtain the intervention. Perhaps the best hope when creating interventions in developing countries is to have a well-defined phase-out as part of the initial political agreement built into the implementation process.

Although economists could hypothesize a number of limitations on intervention, the real question is whether we can design efficient, politically feasible policies that help rather than hinder progress in developing economies. Can we design them with built-in decision points for their removal when they have accomplished their purpose but not yet wreaked havoc on the economy? Would more research on policy implementation alternatives be helpful in achieving policy objectives?

### *Transition economies*

Koester then turned to the case of transforming command economies to market economies, which is surely one of the most interesting current topics. He argues the need for government involvement in the transition period during which markets are not likely to operate well because of 'a lack of market institutions, deficient communication systems, poorly defined property rights, an inadequate legal system and the fact that the population is not acquainted with the workings of a market economy'. All of these features will contribute to high transaction costs.

Koester suggests that transition countries learn from developed countries 'that agricultural protectionism tends to become permanent as the farm lobby perennially advances the social hardship argument. Indeed, protectionism, by generating unfounded expectations, may be the cause of future social hardship.' He suggests that, in designing agricultural policies, transition countries need to incorporate flexibility and reversibility. Indeed, designing new institutions to allow markets to function efficiently requires attention, not only to physical infrastructure and the legal framework, but also to the extension, education and information-providing institutions. The creation of such institutions is necessary for a successful economy, even though the costs involved might appear to diminish the perceived rate of transition.



I raise the same questions as for developing economies: Can we design and implement efficient, politically feasible policies? Can we incorporate decision points? Do we need to research policy implementation alternatives?