INTERNATIONAL TRADE AND TRADE-OFFS FOR THIRD WORLD CONSUMERS: A MATTER OF ENTITLEMENTS

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A discussion of "International Trade and Trade-offs for Third World Consumers," by Michael R. Reich, Harvard School of Public Health. Prepared for the International Conference on Research in the Consumer Interest, organized by the American Council on Consumer Interests, August 13-16, 1986, Wingspread Conference Center, Racine, WI.

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The economic position of consumers in developing countries is difficult to conceptualize. For many nations the development time between being a subsistence economy and having a monetized market is now compressed from centuries to decades. Because imported Western goods are often believed to be superior they are highly sought after. That they may malfunction or be hazardous or overpriced are not likely to be primary concerns to consumers who face absolute scarcity every day and are continuously at risk from disease, death and war.

Dr. Reich has provided some intriguing insights into the position of Third World consumers by superimposing on their markets three of the consumer rights established in the western world -- information, choice and redress. These rights are implemented with great difficulty in the Third World, particularly for imported products. In the end, he implies that those who sell to Third World countries bear a special responsibility for the health and safety of their consumers. Although it may be easy to agree with this on ethical grounds, I suggest that determining the mechanism for establishing and enforcing that responsibility must be an integral part of the agenda for research in the interests of international consumers.

In this discussion paper, I will comment briefly on Dr. Reich's paper, and suggest some additional trade-offs. Then I will propose a conceptual framework in which the incentives and costs associated with consumers' safety can be examined from a behavioral and an economic perspective. Finally, the role of national and international organizations that could, theoretically, act on consumers' behalf will be discussed.

Trade-offs and Trade

Reich's enlightened observations about the position of Third World consumers in the market for imported goods gives us a rich appreciation for the conditions and incentives that leave them with little bargaining power. The reasons range from abject poverty and lack of written language to chicanery and exploitation by western sellers and governments. Special problems arise when inappropriate technology is accompanied by inappropriate information, or worse, false advertising. Though international trade theoretically increases choices, this may not be achieved if imports replace local production or irreversibly damage the environment.

Although the title of Reich's paper speaks about trade-offs, benefits and costs of international trade to Third World consumers are not discussed. The potential for imports to make major positive contributions to agricultural development, industrial employment, per capita incomes and health and sanitation are ignored. Many developing country governments would argue that these benefits outweigh the costs of accidents incurred through the use and misuse of individual products by individual consumers. For example, the early importation of DDT into Thailand dramatically decreased the incidence of malaria, opened up vast new areas of land to rice and corn production, increased local food consumption, improved nutrition, and facilitated agricultural exports. The U.S. Agency for International Development (U.S.A.I.D.) no longer allows its aid money to be spent on chemicals containing DDT. It does, however, allow the purchase and use of phostoxin, a biodegradable pesticide that is very dangerous to humans in the short run. Its safe use requires the wearing of special clothing which is generally not available. The decision to trade off the long-term, environmental hazards of DDT for the deadly, short-term hazards of phostoxin has clearly been made for Third World consumers. However, it has been decided by an international development agency. This illustrates the real and difficult trade-offs facing Third World countries and their advisors. These trade-offs involve economic development (growth in national income and production) vs. environmental protection vs. the cost of accidents to individual consumers and society.

Trade-offs associated with Third World countries' development of exports are not mentioned by Reich but the production of food and other goods for local consumers must compete with resources used to produce export goods. Exports, however, increase foreign exchange and enable Third World countries to buy and sell in the international market. Not coincidentally developing exportable commodities is a major goal of most Western development projects and the countries in which they work.

Enforcement of the three consumer rights identified by Reich -- information, choice and redress -- require different types of policy solutions. Using the traditional two-pronged fork of consumer policy, improved information and choice clearly belong to the prong labeled "information" (or "education"). Redress requires the second prong -- "protection".

Given the dearth of product information in Third World markets, consumers' search costs are very high, even though the value of time is very low. High search costs imply that the price and quality of goods will vary much more in the Third World than in better informed markets (Stigler). Consumers in markets featuring very poor information will ultimately accept the risks in using products without adequate information because the marginal cost of acquiring more information outweighs its benefits at a much lower level of information.

The provision and acquisition of better product information is a "market enhancing activity". It facilitates trade. Extremely good information enables consumers to protect themselves. However, consumers in many Third World countries are so far away from achieving any semblance of self-protection via information and education that, as argued by Thorelli, protection must be the policy priority if the costs and incidence of product related accidents are to be diminished.

Redress is aided by information, but it requires protection. Protection implies some form of government intervention and regulation. It implies altering the rules of the game. It implies, to use Kerton's terminology, changing the institutional "framework" in which market transactions take place. More abstractly, it involves reassigning entitlements (sometimes called property rights). It means, at least for very risky products, that the market rules must be converted deliberately from "caveat emptor" to "caveat venditor".

Trade-offs and Entitlements

A useful taxonomy for thinking about consumer rights (the entitlement to prevail) is provided by Calabresi and Melamed. It is a blend of the economic theories of social cost and legal property rights. These theories have been applied by natural resource economists who speak about the social costs of externalities (Bromley). Negative externalities in consumer markets include accidents which occur because of product hazards, malfunctions or misuse.

The theory of social costs may further be linked to trade theory by considering the relative profitability of trading in a particular country. Profitability is partially a function of institutional arrangements that determine which parties will bear the social costs of consumers' accidents and which parties are responsible for the transaction costs of trade. Transaction costs are generally defined to include costs of search and negotiation, while social costs are attributed to post-purchase phenomena such as the costs of misinformation, accidents, and waste. None of these costs are ~~not~~ likely to be reflected in the selling price of products, but they are ultimately born by members of society.

Calabresi and Melamed's taxonomy, adapted for consumer product markets, is outlined in Table I. It assumes a world where transaction costs are high and where some extra-market authority (government) is necessary to allocate resources consistent with the values of society. First, entitlement is assigned. Then, one of three types of rules is invoked to protect or change entitlements. These rules have major implications both for consumers' protection and for sellers' profitability.

The prevalent case in Third World consumer markets is case II on Table I where seller B is entitled to prevail and that entitlement is protected by a property rule. That is, seller B (or for that matter developed country B) can interfere with consumer (or country) A's life-style -- sell anything that consumer A will buy -- until A takes action to stop B. Since the burden for initiating action to stop B or to change the entitlement rests with A, A's resource constraints such as income and education largely determine the probability that any action will be taken.

If there existed a national or international organization capable of making and enforcing a change in property rule II, it could, for example, pass a law that no seller's goods could enter a Third World country until the seller disclosed to the official import authorities all the potential risks and hazards of the use of that product in that country. The import authorities (acting on behalf of consumers) must then give, or withhold, permission to sell in that country. This is a case of informed consent, a minimum ethical standard in international trade suggested by Reich. The burden of taking action is, under property rule I, on the seller whose income and education constraints are far less severe than those of consumers. Shifting the responsibility for the transaction costs to the seller changes the entitlement, and "caveat venditor" replaces "caveat emptor." In either case, a market solution is implied.

Entitlements may also be protected by liability rules. They require a third party to determine the level of enforcement and compensation. Product liability rules under tort law in the United States are an example of liability rule III. Consumers are entitled to be compensated for harm caused by a defective product, the amount of which is determined either by an insurance company or the courts. A similar set of institutional arrangements would need to exist in the Third World for liability rules to be workable.

A modicum of safety and health may be viewed as an inalienable right of consumers who cannot be informed or otherwise be protected.

Inalienability implies that some trades may not be allowed because "dreadful accidents" are intolerable and the transaction costs of preventing these accidents are so great that they would not be undertaken if only property or liability rules apply. Again, institutional arrangements such as an international, governing body would have to protect this right.

International Agencies and Consumers' Rights

Reich lists some of the international organizations that have tried to increase the flow of information and a few that have tried to assist with a system of redress. While recognizing the political and developmental problems surrounding the evolution of governing bodies that have the will and the resources to change the form of consumer entitlements, a few examples come to mind. As mentioned earlier, international development agencies, such as U.S.A.I.D., the U.N. Food and Agricultural Organization (FAO), and the World Bank, have considerable influence in the countries where they work. They could, if so inspired, make aid contingent upon local enforcement of consumer rights. Several developing and socialist countries have foreign trade offices that monitor and control certain imports. They could, if so inspired, monitor the safety and efficacy of consumer products.

If, through the efforts of organized consumer groups, the mass media or other consciousness-raising agencies, basic consumer rights came to be supported by world opinion leaders, it is possible that some changes in the institutional framework in which Third World trade takes place could be made. Changing the rules of the game implies, however, a redistribution of costs and profits. Research could appropriately address questions about the direction and magnitude of that redistribution.

Changes in entitlements could increase the sellers' costs, decrease profits, and potentially stop the importation of some products into the Third World. Research questions might be: (1) How much would the internalizing of transaction costs decrease sellers' profits? (2) What is the probability of an accident and what would it cost for the seller to reimburse a Third World consumer for harm or malfunction? (3) How much will the government system to enforce entitlements cost? (4) Who will pay for it? Some puzzling methodological questions will arise. For instance, how does one calculate the value of life and limb in the middle of the Kalahari or the heart of Santiago? How do westerners handle the problem of preferences for risky products in the face of absolute scarcity? How do we handle the cases where the risks of harm from a hazardous product are perceived as trivial compared to the daily risks of living?

Reich's paper does not lead us to a clear set of policy solutions or set us on a clear path of research. Perhaps it is because the choices are not at all obvious. Some philosophical questions, as well as cross-cultural issues surround research into the trade-offs faced by Third World consumers whose countries engage in international trade. Careful benefit/cost analyses of different entitlement scenarios could provide useful information for international trade policy decisions but, ultimately, consumer rights, as defined by the Western world, will have to be enforced at the local level.

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TABLE I.

Entitlement Belongs To:	Entitlement Protected By:		
	Property Rule	Liability Rule	Inalienability
A. Consumer (Caveat Venditor)	I. A must consent to B's interference with his/her lifestyle (property). A must agree to accept risky products after full disclosure of characteristics and dangers.	III. A must be compensated for the actions of B, e.g., for harm done by the use of a defective product. A third party determines the fair compensation.	V. B may not interfere with A under any circumstance. Stopping the sale of products that threaten life and limb would not be compensated.
B. Seller (Caveat Emptor)	II. B can act to interfere with A's lifestyle (property) and can be stopped only if A bribes B to stop.	IV. B can be stopped from selling harmful products but only if A compensates B for losses incurred due to stopping.	