WELFARE GAINS FROM LIBERALIZED BANANA TRADE AND A NEW INTERNATIONAL BANANA AGREEMENT

Henk L.M. Kox

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Abstract

The European Union import policy for bananas grants preferential trade access for ACP bananas and discriminates against bananas from other sources. It is shown that such trade discrimination cannot be defended by development-related motives. As a form of aid transfer to banana-exporting ACP countries, the EU import regime is highly inefficient. The effective value of financial transfers is low, while there are large associated welfare costs to domestic consumers and to non-preferred export countries. Liberalization of banana imports would create huge welfare gains which can easily be used to compensate potential losers. It is proposed that the compensation package is given the form of an International Banana Agreement. The presence of third-party gains from trade liberalization can be used to negotiate non-EU involvement in the international agreement. The agreement makes it possible to reconcile a commitment to free banana trade, promotion of ecological sustainability in banana production and promotion of socio-economic development interests of banana-exporting countries.

Introduction

Bananas form the fifth largest tropical export crop. About 40 per cent of all exports have the European Union as destination. The European banana import regime affects many developing country producers of export bananas. This article argues that a reform of the European banana import regime could pave the road to an International Banana Agreement that reconciles market efficiency goals, development goals and environmental goals.

Most European countries have a long tradition in regulated banana import policies. Signing of the Rome Treaty which formed the basis for the European Community, was even postponed for a few days until a separate Banana Protocol was added to the Treaty. The 1992 unification of the internal European market brought a uniform European import regime for bananas. It is closely entangled with the Lomé Agreement between the European Union and former colonies in Africa, the Caribbean and the Pacific regions (ACP). ACP countries enjoy privileged access to the European market, mainly to the detriment of producers in Central and South America. Because a large part of Latin American banana exports is dominated by three large US companies, these exports are often adduced to as ‘dollar bananas’. Large-scale production methods makes dollar bananas generally much cheaper than ACP-bananas.

1 The author is with the Economics Department and the Economic and Social Institute of the Free University in Amsterdam (Address: De Boelelaan 1105, 1081 HV Amsterdam, Netherlands, tel.: +3120.444.6143, fax: +3120.444.6127, email: hkox@econ.vu.nl)
Increasing friction over the current EU banana market regime has accumulated between the commercial parties and countries, inside and outside the European Union. The item nearly caused a trade war between the USA and the EU. After complaints by governments of dollar banana countries and the USA before WTO trade panels, the WTO Appellate Body in 1997 came with a final verdict that makes a change in European banana policy unavoidable. Also from another perspective, change is laying ahead. The current Lomé Agreement between the EU and the ACP countries has to be renewed in the year 2000. In its Green Paper the European Commission (1996) announced that revision of the agreement is desirable from several perspectives. The Banana Protocol of the Lomé Agreement which considerable constrained the EU’s policy margin expires in December 2002. At that time also the Framework Agreement of the EU with four dollar banana suppliers expires. Therefore, institutional and legal possibilities for substantial change come into sight.

The article has the following structure. Section 2 is an attempt to disentangle the different lines of argument in the debate for revision of the present EU banana regime. In the subsequent three sections three major aspects of this debate are dealt with in further detail. Section 3 surveys the evidence on welfare costs and benefits of the banana regime. An important element in the discussion on the European banana policy is about the best way to help those countries which are extremely dependent on banana exports. Section 4 answers the question whether differences in economic and social development of banana-exporting countries can justify the present EU banana policy. Section 5 focuses on environmental aspects of banana production in relation to trade preferences. Section 6 launches a proposal to use potential welfare gains from liberalized EU banana trade in a package deal that compensates the potential losers in ACP countries. The package deal is shaped in the form of an International Banana Agreement. The final section summarizes the overall conclusions.

**Overview of the banana trade controversy**

Debate on the EU banana regime has been criticized from different view angles: welfare considerations, development arguments, competition policy, environmental considerations and arguments related to labour standards. Proposals to reform the import regime reflect the different perspectives. In order to clarify further discussion first an attempt will be made to disentangle the different threads of argument.

**EU consumer welfare** Many studies by now have documented and analyzed welfare costs and distributional consequences of the current banana regime. Due to the import regime, European consumers pay much higher prices and have lower banana quality. The import regime creates free quota rents which for European banana marketing companies, at the expense of consumers. Banana producers in ‘dollar banana’ countries are artificially put at disadvantage by the regime. Research findings on this issue will be presented in section three of this article.
**Development objectives.** The prime motivation for the present EU banana regime is that it helps poor countries whose economy is highly dependent on banana exports, i.e. the ACP exporters in general and more in particular for the Caribbean Windward Islands. The questions whether such claims are justified and whether a discriminatory import regime for bananas is an efficient instrument to serve these goals form the subject of section four of this article.

**Competition policy for the banana industry.** Competition policy is a subject matter that has become increasingly intermingled with discussion of the EU banana regime. Welfare analyses of the EU banana scheme are sometimes criticized, pointing at the fact that a free EU banana market will be an oligopolist market, dominated by three large US banana multinationals. However, the prime goal of the EU banana regime was not to change the market structure of the industry, but rather, to help the economies of the banana-dependent former colonies. The EU has more targeted instruments (e.g. based on articles 85 and 86 of the Rome Treaty) to intervene in case of market power abuse by large banana companies.\(^2\) Even with an oligopolist market structure, market prices for bananas in open markets (USA, Germany before 1993) have been far lower than in the regulated EU market.

**Environmental issues.** A further line of argument in the debate on the EU banana policy relates to environmental considerations. ACP bananas, particularly those from smallholders in the Caribbean region, are generally produced in an environmentally more sustainable way than bananas from large estates in the dollar banana countries. Ecological sustainability in the latter case is often threatened by large amounts of pesticides which end up in the local environment, causing harm to humans, wildlife, local ecological systems. In smallholder banana production little or no pesticides are used, due to the costs of such inputs and due to lower pest incidence in small-scale, inter-cropped production systems. Mono-crop banana plantations are more pest-prone, while the companies’ desire to meet premium consumer demand for long, unblemished bananas leads to additional use of chemical pesticides and growth regulators. The productivity gap between ACP smallholder production of bananas and large-scale production in ‘dollar banana’ plantations might shrink when negative environmental externalities caused by banana production were taken into account. However, it does not follow that dollar bananas should receive a less preferential treatment in EU banana policy. Most environmental externalities caused by banana production are local externalities, without massive transborder welfare effects. If local environmental externalities dominate the scene, policy primacy should rest with local or national governments in the producer countries, rather than with the European Commission. If EU consumers prefer bananas which are produced in an environmentally sound way, then it does make sense to arrive at voluntary ecolabelling schemes for bananas. Some are already in operation in the EU. They create a

\(^2\)Effectiveness of these instruments has been shown in 1973 and in 1992 with regard to market power abuse by Chiquita.
basis for product differentiation and price premiums for bananas (from ACP countries or elsewhere) which have been produced in an ecologically sound way.

**Arguments related to labour standards.** Some proposals for reform of the EU banana import regime suggest that more weight should be given to minimum social standards in banana production. Particularly the banana multinationals have a long record of union-busting and denial of workers’ rights in banana-producing countries.³ Their plantation labourers have widely suffered from health hazards (diseases, infertility, lethal accidents) related to the excessive use of agrochemicals in large-scale banana production. Central American banana estates have used pesticide types like DBCP of which application has long been forbidden in their countries of origin.⁴ Epidemiological research shows disquieting results. The incidence of workers suffering pesticide intoxication is estimated to be 3 per cent of the working population in all developing countries. For Costa Rica in general it is 4.3 per cent, while for the banana region in Costa Rica, Región Huetar Atlántica, it is 6.6 per cent (Anon., 1992a; Hernandez and Witter, 1996: 175). Because of these intolerable working conditions and labour practices, it has been proposed to apply social minimum criteria in European trade preferences for bananas (WINFA, 1997). However justified the social claims by plantation workers in dollar banana countries may be, their position is only indirectly related to the EU import regime for bananas. The companies often stress that they operate according to national legislation of the production countries. If this is not the case, then banana worker unions may of course sue them in local courts. When unions find insufficient support for their rightful claims in national legislation, then the most obvious step is to undertake political action to improve such legislation. International support from trade unions which organize workers in other parts of these vertically-integrated banana companies is the next step; this is the very task of international labour union organizations. Since banana companies with own brand names are very keen to avoid a negative consumer imago, banana worker unions may well strengthen their case by joining with consumer organizations and NGOs in EU import markets. It is neither obvious nor necessary that these issues be linked to a reform of the EU banana regime. Indeed, it can be argued that job opportunities of plantation workers will increase due to a liberalized banana trade. Improved bargaining positions vis-i-vis their employers may lead to higher wage levels, improved labour union rights and better labour conditions.


⁴ Although domestic use of the highly toxic pesticide DBCP was forbidden in the USA in 1977, it has been widely applied by the US banana companies during the period between 1965 and 1990. These companies now have been named in class action lawsuits on behalf of more than 10,000 banana workers in 11 developing countries. The banana worker suits allege that as early as 1961, research by Dow Chemical and the University of California indicated that DBCP is highly toxic, and that its vapours alone can do damage to sperm cells, livers and kidneys (cf. Mokhiber & Wheat 1995). The companies which produced the chemical have offered an out-of-court settlement (Banana Trade News Bulletin, Nov. 1997).
Conclusion. The European import regime for bananas has become subject of lobby activities by various parties. Labour standard issues, competition policy arguments and environment-related arguments cannot form justified motives for further trade discrimination. The real issues which deserve further analysis are welfare effects of the import regime and the validity of development-related considerations which motivate the present policy. Voluntary ecolabelling schemes for bananas could well become part of the compensation package for potential losers of a liberalized European banana trade. These issues will subsequently be dealt with in greater detail.

**Welfare analysis of the present EU banana regime**

Welfare analysis of a policy makes it necessary to identify relevant parties and their welfare interests. Some will gain and others will lose when the EU banana import regime is reformed. Table 1 lists welfare positions of producers, traders, consumers and governments. I will be used as a vantage point for a more detailed discussion.

Consumer *interests*. In money terms, the largest welfare concerns European consumers. They pay much higher banana prices than they would have had to pay with completely free trade. The reference point can be the German banana market where imports were completely free before 1993. Other countries (Benelux, Denmark, Ireland) till then applied a uniform 20% tariff on banana imports, or used a combination of import quota and tariffs (UK, France, Italy, Spain, Portugal) Portugal and Greece).

Import quotas were used to grant preferential trade access for former colonies in Africa and the Caribbean. Some countries also used quotas to preserve part of their national markets for domestic but expensive production of bananas: Spain (from Canary Islands), Portugal (Madeira), Greece (Crete), France (Guadeloupe, Martinique). Pre-1993 differences in consumer prices for bananas are shown in Graph 1. Consumers in countries that applied both tariffs and quota paid the highest prices for bananas, followed by those that just applied a simple import tariff, with consumers in the open German market paying the lowest price. It is worth noting that price in

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5 Also Sweden, Austria and Finland had open banana markets before their entry in the EU. Germany had negotiated free banana imports in a special protocol of Rome Treaty.
Germany were lowest even though the German market was and is dominated by large oligopolist banana companies.  

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### Table 1

**Dominant welfare positions with regard to liberalized EU banana imports**

<table>
<thead>
<tr>
<th><em>Player</em> groups</th>
<th>Dominant parties</th>
<th>Main welfare interests</th>
</tr>
</thead>
</table>
| **Consumers**   | EU consumers     | - Price level of bananas  
                  |                   | - Banana quality  
                  |                   | - Concern on ecological sustainability and social conditions  
|                 | US consumers     | - Effect of EU banana regime on US consumer price  
                  |                   | - Banana quality  
                  |                   | - Concern on ecological sustainability and social conditions  
| **Producers**   | Producers of the Windward Islands | - Trade opportunities in EU  
                  |                   | - Income and employment opportunities from banana exports  
|                 | independent banana producers in dollar banana countries | - Trade opportunities in EU  
                  |                   | - Profits from banana exports to EU  
|                 | Producers in the non-Caribbean ACP countries | - Income and employment opportunities from current banana exports to the EU  
|                 | European producers and French 'overseas territories' | - Income and employment opportunities arising from bananas produced under the Common Agricultural Policy of the EU  
                  |                   | - Income and employment opportunities arising from bananas  
| **Traders**     | Banana trading companies which market ACP bananas in the EU | - Market share in EU  
                  |                   | - Profits from (free) quota rents  
                  |                   | - Investment in dollar banana countries to meet market demand under EU import licenses  
| **Governments** | EU Commission and EU governments | - Food cost levels for EU consumers  
                  |                   | - Revenue collection from import tariffs and quota rents  
                  |                   | - Bureaucratic costs of implementing current EU banana regime  
                  |                   | - Goals of EU development policy  
                  |                   | - Reform of EU common agricultural policy  
                  |                   | - Renewal and revision of Lomé Agreement  
|                 | Governments ACP countries | - Direct incomes generated by banana exports to EU  
                  |                   | - Positive economic externalities of banana exports  
                  |                   | - Export diversification opportunities  
                  |                   | - Trade and aid benefits under the Lomé Agreement  
|                 | US government     | - Protection of profit interests of US banana multinationals  
                  |                   | - Low banana prices for US consumers  
                  |                   | - Control of immigration from the Caribbean  
                  |                   | - Control of drug imports from the Caribbean region  
                  |                   | - Political stability in the Caribbean  

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6 Deodhar and Sheldon (1995) show that the German banana market was and is not a fully competitive market, but they found no evidence that oligopolist firms applied collusive dump pricing methods. Moreover, US prices are even considerably lower than German prices. Therefore, German banana prices before 1993 can well be taken as an approximation of prices under an open trade regime.
Many estimates are available of the welfare costs for EU consumers, using different models, assumptions and base years. Annex Table A2 presents eight of these estimates. The combined annual welfare loss for EU consumers is estimated to be in the range between 579 mln and 1600 mln US dollar. This is the amount that could be gained when in 1993 the European banana trade would have been liberalized.

However, the EU in 1993 decided for a uniform European banana import regime built on origin-dependent quota, tariffs and import licenses. European and ACP bananas were given preferential trade access with a quota level higher than what these producers delivered up to then. Remaining import demand could be provided by other countries under a uniform import tariff (100 ECU/ton). Because of the different national banana policies, introduction of the policy package had a differentiated effect on consumers in EU member countries. The largest welfare loss fell upon German consumers. Several estimates of their combined loss are presented in Annex Table A1, using different assumptions and estimation methods. The estimates quantify the welfare loss for German consumers between 106 mln and 800 mln annually. Put otherwise, this is approximately the welfare gain for Germany that could be achieved by again converting EU import policy to an open trading system. All estimates agree that the 1993 banana regime had the most positive effect on consumer welfare in France and the UK, which formerly had the most policy-distorted banana markets. Graph 2 shows that these countries experienced a fall in real import prices compared to prices in 1989. The same happened in Spain, Portugal and Greece (not shown in graph 2).

![Graph 2](image)

Real import prices increased in all other EU countries. Estimates of the overall welfare effects for EU consumers give mixed results, depending on the applied model, the underlying assumptions and the

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7 Further details can be found in EC Council Regulation 404/93 and in Hallam and Peston (1997: 8-13).

8 Note that import prices do not coincide with consumer prices, because of trade margins and because some EU countries have an ‘own’ banana production (Greece, Spain, Portugal, France).
choice of reference period. Borell (1994; 1997) estimates that the total welfare loss for European consumers increased due to the 1993 reform, from 1600 mln to 2300 mln US dollar. Guyomard et al. (1996) also found an increase, but only by a negligibly 2 mln US dollar, while Euro PA (1995) estimated that the total European welfare cost due to the reform decreased by 600-800 mln US dollar.

In a forward-looking perspective it is only interesting which welfare gains for EU consumers can be accomplished by liberalizing banana trade. Comparison of banana import prices with those prevailing in non-EU countries yields a first approximation of the potential gains. In Table 2 current and historical import prices are related to those in the USA. It appears that in 1996 EU import prices are generally double those prevailing the USA; only part of this difference can be explained by transport costs. The

<table>
<thead>
<tr>
<th>Country</th>
<th>1996 average import price a) in US$/ton</th>
<th>1996 Price ratio (USA=1.00)</th>
<th>1989 average import price a) in US$/ton</th>
<th>1989 Price ratio (USA=1.00)</th>
<th>Real price increase b) in %, 1989-96</th>
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<tr>
<td>USA</td>
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<td>100</td>
<td>356</td>
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<td>428</td>
<td>117</td>
<td>398</td>
<td>112</td>
<td>-13.3</td>
</tr>
<tr>
<td>New Zealand</td>
<td>465</td>
<td>127</td>
<td>506</td>
<td>142</td>
<td>-25.8</td>
</tr>
<tr>
<td>Japan</td>
<td>531</td>
<td>145</td>
<td>573</td>
<td>161</td>
<td>-25.3</td>
</tr>
<tr>
<td>EU countries</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>France</td>
<td>632</td>
<td>173</td>
<td>788</td>
<td>221</td>
<td>-35.3</td>
</tr>
<tr>
<td>Italy</td>
<td>709</td>
<td>194</td>
<td>466</td>
<td>131</td>
<td>22.8</td>
</tr>
<tr>
<td>Germany</td>
<td>750</td>
<td>205</td>
<td>482</td>
<td>135</td>
<td>25.7</td>
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<tr>
<td>Un. Kingdom</td>
<td>759</td>
<td>208</td>
<td>701</td>
<td>197</td>
<td>-12.7</td>
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<tr>
<td>Ireland</td>
<td>761</td>
<td>208</td>
<td>422</td>
<td>118</td>
<td>45.5</td>
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<tr>
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<td>216</td>
<td>528</td>
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<td>524</td>
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<td>Belgium</td>
<td>880</td>
<td>241</td>
<td>414</td>
<td>116</td>
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</table>

Notes: a) Average import unit values for bananas from all sources. b) Nominal 1996 import prices have been converted in constant 1989 US dollars by the deflator for the US GDP. Data sources: import data from UNSD COMTRADE database, Geneva; deflator for US GDP is from IMF, International Financial Statistics.

price difference with the USA and other OECD countries with open banana import regimes has clearly deteriorated since 1989. Given these price differences, it should not come as a surprise that all estimates of the welfare effect for EU consumers in case of liberalized banana trade, show a huge potential gain, ranging from 800 to 2300 mln US$ (cf. Annex Table A2). It should not be too difficult to compensate potential losers of liberalized trade from such a huge amount. Matthews (1994: 19-21) calculated that a combination of liberalization with full financial compensation to banana-exporting ACP countries (340 mln ECU) would still yield a net welfare surplus for European consumers (126 mln ECU).

A liberalized EU banana trade may also affect consumers in the USA and other import countries. In the short term they might see banana prices go up; and this effect may last until production capacity has
adapted to higher EU import levels. This future course of events results from standard international trade theory. When a large import country like the EU opens up its markets, this causes world market shortages (at least temporarily) which push up the world market price. Adaption of banana supply capacity by large companies could be relatively fast, because they have the short-term possibility to diminish the share of rejected sub-standard bananas.

Producer interests. Together, world banana producers would benefit from EU trade liberalization. Total world demand levels would go up, and also world market prices for bananas increase, at least in the short to medium term until production capacity has been adapted. The largest gains in banana exports will be booked by the most competitive producers, i.e. the producers in dollar banana countries. Dominant producers in this region still are the US banana multinationals, but national producers like

![Graph 3 of banana production a), 1992-93](image)

Note: 1) F.o.b. costs mainly consist of labour and material inputs in crop husbandry, harvesting, packing and handling. Cost estimates for Costa Rica and Colombia only include variable costs. Source: compiled by Hallam & Peston (1997: 23) from FAO-data (Review of costs of production, trade and distribution of bananas in selected countries. Rome, 1994) and CIRAD-data (Evaluation de la compétitivité des productions des bananes des pays ACP. Rapport Final, Montpellier 1995).

Noboa (Ecuador) have expanded fastly. The position of US banana multinationals has somewhat changed since the early 1990s, since they have built up production capacity in African ACP countries and in Europe (Dole), in order to be eligible for lucrative EU import licenses. ACP producers lose their preferred trade access to the EU. Since their cost price levels are much higher than in case of dollar banana producers (cf. Graph 3), they may not be able to benefit from larger EU demand. Worse, they probably lose considerable parts of their current EU import shares (e.g. Ross-

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9 The opposite happens when a large country imposes tariffs and quota (see e.g. Krugman and Obstfeld, 1994; Deardorff, 1994). The price decrease in non-EU countries between 1989 and 1996 as shown in Graph 2 and Table 2 reflects increased protectionism in the EU, although improved productivity in banana production may also explain part of the price fall.

10 Moreover, in Latin America they increasingly leave banana production to outgrowers, national companies who run the plantations and supply bananas on a contract basis.
Robinson, 1997). Smallholder banana producers in high-cost ACP countries, like the Caribbean Windward Islands, form the most periled group of producers. High cost prices of their bananas are partly related to small plot sizes and hilly terrains.

Banana producers in the EU or in so-called ‘overseas territories’ will also be affected negatively by an open EU banana market, since these producers are mostly high-cost producers. Their income position is, however, less in peril because they are entitled to deficiency payments under the EU Common Agricultural Policy, and possibly also under the EU’s regional development programmes. These payments will compensate income shortfalls and facilitate investment in a broadened production base.

**Traders’ interests.** Trading companies which market ACP bananas in the EU have been among those who benefited most of the 1993 policy reform. European traders were granted free import licenses for the formerly open EU countries (new market area), whereas they were also allowed to market 30% of all dollar bananas (new product) alongside their traditional trade in ACP bananas. Allotment of dollar banana licenses led to vocal protests by US banana companies backed by the US government. The protest culminated in threat of US trade retaliation, and in a WTO panel procedure. In 1997 the Appellate Body of the WTO decided that the EU should alter its quota allocation system.

Government interests. The European Commission’s policy margin with respect to banana imports is constrained by obligations following from international treaties (Lomé, Framework Agreement with Latin American banana producing countries, WTO). EU policy concerns with respect to a liberalization of banana imports include consumer welfare, development policy, implementation costs and tax receipts. Development aspects of the EU trade regime are dealt with in next section. The present banana import system requires detailed market intervention with specific tariff quota for specific economic activities like producing and purchasing, transport and ripening of bananas.” The associated bureaucracy costs are high. Most of such costs are avoidable in an open market system combined with direct aid transfers. Banana import taxes are now collected on dollar banana imports. Complete liberalization mean that these import levies are foregone; the loss will be partly compensated by higher receipts of value-added taxes.

Caribbean governments have repeatedly stressed that banana exports to the EU are a lifeline for their economies, claiming that without these exports their economies will collapse. According to them considerable parts of agricultural employment and incomes would disappear due to EU import liberalization, while a large share of total foreign exchange earnings would be lost (cf. CBEA, 1997/98).

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11 E.g. quota redistribution was found necessary each time that production of Caribbean Windward Islands was hit by tropical hurricanes.
Opposite claims have been voiced by governments of dollar banana countries: an open EU market would increase their agricultural jobs and incomes, while their export earnings would increase.

The US government so far has primarily chosen to represent the position of US banana companies, rather than appreciating the fact that the EU banana policy has (unintentionally) lowered banana prices for US consumers or that it has contributed to economic and social development in the Caribbean. The US government has also stated that their other interests in the banana trade conflict include: maintaining political stability in the Caribbean, controlling immigration and drug trade from this region. It has therefore announced its willingness ‘to work with the EU to help the Caribbean producers in a way that does not hurt US companies and Latin American producers” (USTR, 1996).

Conclusions. The largest gains from EU trade liberalization will be recorded by European consumers, followed by the most competitive world market producers, i.e. those in dollar banana countries. High-cost ACP producers like the Windward Islands and privileged European traders stand to lose most.

Development contribution

The major objective of EU banana policy has been the promotion of social and economic development in ACP countries. The relevance of this development goal, and the effectiveness of the banana import regime in achieving it, will be investigated on the basis of the following questions:

- Are banana-exporting ACP countries less developed than dollar banana countries?
- Are ACP economies more dependent on banana exports than dollar banana countries?
- Do ACP countries have other weaknesses in their external economic relations compared to dollar banana countries?
- Do trade preferences boost social and economic development?
- Are trade preferences a necessary instrument to boost social and economic development?
- Are trade preferences an efficient instrument for transfer of development aid?

Starting with the first question, Table 3 brings together a number of development indicators for both country groups. Each country group appears to consist of poor and relatively better-off countries. The group of ACP banana falls apart in two subgroups, the Caribbean and the African countries. Caribbean countries have relatively high levels of real income per capita. The first six of them have income levels comparable with or higher than European countries like Poland, Bulgaria, Romania and most former member states of the Soviet Union. The UNDP’s Human Development Index data also indicate that most Caribbean states are in the category most developed countries. The story is quite different with

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12 In terms of population size, the group of African countries is by far the largest (28 mln.); the first six Caribbean countries in Table 3 have a combined population of one million, while Jamaica and the Dominican Republic together count ten million people.
### Development characteristics of countries exporting bananas to the EU

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<td>72.0</td>
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<td>Cameroon</td>
<td>2120</td>
<td>0.468</td>
<td>62.1</td>
<td>55.1</td>
<td>..</td>
<td>31.4</td>
<td></td>
</tr>
<tr>
<td>Côte d’Ivoire</td>
<td>1688</td>
<td>0.386</td>
<td>39.4</td>
<td>52.1</td>
<td>18</td>
<td>46.3</td>
<td></td>
</tr>
<tr>
<td><strong>Dollar banana countries</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costa Rica</td>
<td>5919</td>
<td>0.889</td>
<td>2889</td>
<td>76.6</td>
<td>19</td>
<td>6.6</td>
<td></td>
</tr>
<tr>
<td>Panama</td>
<td>6104</td>
<td>0.864</td>
<td>2239</td>
<td>73.2</td>
<td>26</td>
<td>11.2</td>
<td></td>
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<tr>
<td>Colombia</td>
<td>6107</td>
<td>0.848</td>
<td>2678</td>
<td>70.1</td>
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<td></td>
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<tr>
<td>Ecuador</td>
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<td>2587</td>
<td>69.3</td>
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<td>15.2</td>
<td></td>
</tr>
<tr>
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<td>2050</td>
<td>0.575</td>
<td>2306</td>
<td>68.4</td>
<td>47</td>
<td>22.0</td>
<td></td>
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<tr>
<td>Guatemala</td>
<td>3208</td>
<td>0.572</td>
<td>2255</td>
<td>65.6</td>
<td>53</td>
<td>35.3</td>
<td></td>
</tr>
<tr>
<td>Nicaragua</td>
<td>1580</td>
<td>0.530</td>
<td>2296</td>
<td>67.3</td>
<td>44</td>
<td>27.2</td>
<td></td>
</tr>
</tbody>
</table>

Notes: a) The Human Development Index is a combined index of (adult literacy and school enrollment) Countries are ranked between 1 (best) and 0 (worst). b) Percentage of the population living at an income of $1 per day or less. c) Combined index for the percentage of the population without access to safe water, health services, mortality expectation below the age of 40, adult illiteracy and the percentage of underweight children under age five. The index ranges from 0 (no deprivation) to 100 (deprivation for total population). d) Percentage of population under national poverty line, according to Inernet site of Caribbean Banana Exporters Association. Data sources: UNDP (1997), World Bank (1997).

regard to Cameroon and Côte d’Ivoire which have much lower income levels, while also performing poorly on other development criteria. The three first dollar banana countries in Table 3 also do well on most development criteria. Slightly worse is the situation in Ecuador, and much worse in Nicaragua, Guatemala and Honduras where large parts of the population remain in extreme poverty. Development in the latter three countries is between that of Caribbean and African ACP countries. It can be concluded that development levels neither generate an objective criterion for trade discrimination against dollar banana countries, nor do they generate an objective reason for granting generic trade preferences to ACP countries.

A further question is whether ACP countries are more dependent on banana exports than dollar banana countries. Table 4 presents indicators on export-dependency. It is shown that in only three countries banana exports contribute ten per cent or more to domestic income: Dominica, St. Lucia and St. Vincent. These island economies depend for more than half of their total exports on banana exports to the EU. Export dependency is also high in Belize. All other ACP countries have a more diversified
### Table 4: Bananas and export dependency

<table>
<thead>
<tr>
<th>Country</th>
<th>Banana exports to EU as % of total exports, 1995</th>
<th>Exports as % of GNP, 1994</th>
<th>Banana exports as % of GDP, 1993/1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACP countries</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dominica</td>
<td>56</td>
<td>24 b)</td>
<td>11.9</td>
</tr>
<tr>
<td>Grenada</td>
<td>3</td>
<td>10 b)</td>
<td>0.9</td>
</tr>
<tr>
<td>Saint Lucia</td>
<td>76</td>
<td>19 b)</td>
<td>10.2</td>
</tr>
<tr>
<td>Saint Vincent</td>
<td>58</td>
<td>25 b)</td>
<td>9.7</td>
</tr>
<tr>
<td>Belize</td>
<td>20</td>
<td>20 b)</td>
<td>2.3</td>
</tr>
<tr>
<td>Surinam</td>
<td>6</td>
<td>23 b)</td>
<td>3.2</td>
</tr>
<tr>
<td>Jamaica</td>
<td>5</td>
<td>63</td>
<td>0.8</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>7</td>
<td>25</td>
<td>0.1</td>
</tr>
<tr>
<td>Cameroon</td>
<td>6</td>
<td>30</td>
<td>0.7</td>
</tr>
<tr>
<td>Côte d’Ivoire</td>
<td>3</td>
<td>47</td>
<td>0.7</td>
</tr>
<tr>
<td>Dollar banana countries</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costa Rica</td>
<td>19</td>
<td>41</td>
<td>6.0</td>
</tr>
<tr>
<td>Panama</td>
<td>42</td>
<td>110</td>
<td>2.9</td>
</tr>
<tr>
<td>Colombia</td>
<td>5</td>
<td>19</td>
<td>0.7</td>
</tr>
<tr>
<td>Ecuador</td>
<td>13</td>
<td>27</td>
<td>3.4</td>
</tr>
<tr>
<td>Honduras</td>
<td>9</td>
<td>41</td>
<td>6.5</td>
</tr>
<tr>
<td>Guatemala</td>
<td>3</td>
<td>20</td>
<td>0.8</td>
</tr>
<tr>
<td>Nicaragua</td>
<td>4</td>
<td>25</td>
<td>0.3</td>
</tr>
</tbody>
</table>


Export and production structure. In the poorest ACP countries banana exports contribute less than one per cent to domestic income. Only three to seven per cent of their total export earnings stems from banana exports to the EU. The contribution of banana exports to domestic income in Honduras, Costa Rica, Ecuador and Panama is three to eight times higher than in most ACP countries. Of all dollar banana countries, EU imports have the highest contribution to domestic income in Panama and Costa Rica. Summing up, economic dependency on banana exports to the EU is highest in the three Windward Islands, followed by Panama and Costa Rica. Differences between the rest of the countries in Table 4 are relatively small. Motives related to export dependency cannot form a valid reason for a discriminator.

Trade preferences could perhaps be warranted when the balance of payments of ACP countries had structural weaknesses in comparison with dollar banana countries. Table 5 presents a number of indicators on non-trade sources of convertible foreign currency. The last column shows the percentage of exports earnings that again leaves the country in the form of debt-servicing obligations (interest and repayment of loans). As far as data are available, no systematic difference appears to exists between ACP countries and dollar banana countries. Development aid flows appear to contribute more to GNP in ACP economies than in dollar banana countries. Foreign direct investment in most cases contributes
more to the economies of ACP countries than to that of dollar banana countries. Column 4 indicates that the wealthiest dollar banana countries have more access to international private capital markets. Commercial finance (bank loans and export credits) from this source is non-concessional and implies future debt-servicing obligations. Even though some dollar banana countries have more access to the international market for commercial credits, it can be concluded that ACP countries do not lack alternative non-trade sources of foreign exchange. These data do not support claims that ACP countries have a stronger relative dependency on export earnings from bananas.

### Table 5 Capital Flows and Non-Trade Sources of Foreign Currency

<table>
<thead>
<tr>
<th>Country</th>
<th>Total net official development assistance received</th>
<th>Net foreign direct investment as % of GNP</th>
<th>Total net official development assistance received</th>
<th>Private flows from all DAC countries</th>
<th>Debt service ratio (debt service as % of exports)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>received a) 1995, (3) as % of GNP</td>
<td>of GNP, 1993</td>
<td>received a) 1995 in US$ min</td>
<td>1995 (mln US$)</td>
<td>1994</td>
</tr>
<tr>
<td>ACP countries</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dominica</td>
<td>12.1</td>
<td>5.0</td>
<td>24</td>
<td>134</td>
<td>..</td>
</tr>
<tr>
<td>Grenada</td>
<td>4.2</td>
<td>9.2</td>
<td>10</td>
<td>-9</td>
<td>..</td>
</tr>
<tr>
<td>Saint Lucia</td>
<td>9.6</td>
<td>7.1</td>
<td>47</td>
<td>12</td>
<td>..</td>
</tr>
<tr>
<td>Saint Vincent</td>
<td>20.5</td>
<td>13.4</td>
<td>47</td>
<td>-11</td>
<td>..</td>
</tr>
<tr>
<td>Belize</td>
<td>3.0</td>
<td>1.8</td>
<td>16</td>
<td>-3</td>
<td>..</td>
</tr>
<tr>
<td>Surinam</td>
<td>27.6</td>
<td>-10.4</td>
<td>77</td>
<td>155</td>
<td>..</td>
</tr>
<tr>
<td>Jamaica</td>
<td>2.7</td>
<td>2.3</td>
<td>108</td>
<td>252</td>
<td>21</td>
</tr>
<tr>
<td>Domin. Rep.</td>
<td>1.2</td>
<td>2.0</td>
<td>134</td>
<td>229</td>
<td>17</td>
</tr>
<tr>
<td>Cameroon</td>
<td>6.5</td>
<td>2.1</td>
<td>444</td>
<td>-187</td>
<td>17</td>
</tr>
<tr>
<td>Côte d’Ivoire</td>
<td>22.0</td>
<td>0.4</td>
<td>1200</td>
<td>-20</td>
<td>40</td>
</tr>
<tr>
<td>Dollar banana countries</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costa Rica</td>
<td>0.3</td>
<td>3.9</td>
<td>25</td>
<td>319</td>
<td>15</td>
</tr>
<tr>
<td>Panama</td>
<td>0.8</td>
<td>-0.6</td>
<td>50</td>
<td>3433</td>
<td>35 b)</td>
</tr>
<tr>
<td>Colombia</td>
<td>3.7</td>
<td>1.6</td>
<td>231</td>
<td>1604</td>
<td>30</td>
</tr>
<tr>
<td>Ecuador</td>
<td>1.5</td>
<td>0.9</td>
<td>235</td>
<td>917</td>
<td>22</td>
</tr>
<tr>
<td>Honduras</td>
<td>14.1</td>
<td>1.1</td>
<td>411</td>
<td>-12</td>
<td>34</td>
</tr>
<tr>
<td>Guatemala</td>
<td>1.3</td>
<td>1.6</td>
<td>215</td>
<td>22</td>
<td>11</td>
</tr>
<tr>
<td>Nicaragua</td>
<td>48.1</td>
<td>2.7</td>
<td>662</td>
<td>-57</td>
<td>38</td>
</tr>
</tbody>
</table>


Trade preferences may operate like a producer subsidy from abroad. Development economics literature suggests that producer subsidies can be warranted in two cases. The first case regards producers in a start-up phase when it is not yet possible to reap the commercial fruits of initial investments, economies of scale and learning-by-doing. This is the so-called infant industry argument. When producers have no access to commercial loans to finance their start-up phase, governments could subsidize them to bridge the period before they have gained commercial viability and can face market competition by themselves. For this argument to be valid, a pre-fixed time schedule for phasing out the subsidies (preferences) is
required. Without it, the subsidies or preferences become a form of open-ended ‘socializing’ of private losses. Former European colonies have been granted preferential trade access for bananas since the very start of the European Community. Graph 3 has, however, shown that production costs in many ACP countries are still far from competitive. After so many years, preferences (subsidies) to these producers can no longer be defended with the infant industry argument. When no incentives or real possibilities exist to make producers more efficient and competitive, endless subsidy (preference) schemes will be required.

The second case for producer subsidies exists when banana production generates positive external effects for other sectors of the economy. Positive externalities occur for instance when banana production creates environmental benefits, supports labour training, contributes to basic agricultural research, or makes communication, transport or infrastructure available to the rest of the economy. The fact that these positive external effects cannot fully be commercially exploited by banana producers themselves, could then lead to a lower production level than is socially desirable. In that case, governments may subsidize production till it has reached a socially preferred level. By granting trade preferences for this motive, the EU Commission puts itself in the role of the government in the country where the positive externalities arise. In the Caribbean region, banana exports may well generate positive externalities for the economy in the form of lower shipping costs, because banana reefer offer spare transport capacity at relatively low freight costs (e.g. Hallam & Peston, 1997). Other economic sectors benefit from this advantage as well. Environmental benefits (tree crop cover on erosion-prone slopes) and the crop’s role in supporting rural production systems could perhaps also be considered as positive externalities. The presence of positive externalities has to be assessed case by case, and could warrant the use of subsidies for banana producers. Generic trade preferences form a much too broad-spectred instrument for this fme-tuning job. The positive externality created for the Windward Island by the presence of the banana shipping services could be captured by subsidizing the shipping lines with EU aid for the continuation of their services.

Improvement of competitiveness and diversification form essential elements of economic development in high-cost mono-export economies. Sticking to traditional primary export products may block dynamic incentives for economic growth. Primary exports seldom form dynamic growth sectors in developing country economies and growth impulses mostly come from labour-intensive manufacturing exports (e.g. Fosu, 1996; Kox, 1997; Sachs and Warner, 1995). Therefore, subsidizing a stagnant primary sector may well have high opportunity costs in terms of missed growth opportunities. Trade preferences generate additional income for banana traders and producers, but investment in diversification need not come from these agents. Inadequate development of infrastructure like roads, port facilities and communication links has been established to be a major bottleneck for diversification in the Eastern
Caribbean region (FAO, 1996). Governments, rather than the banana sector, has to undertake investments in roads, ports, industrial estates and education programmes that can form the basis of new export activities. Therefore, direct EU aid to governments would probably be more effective in supporting diversification of exports and production than indirect price subsidies to the banana sector. Of course, diversification takes time, and small banana producers may not benefit from it, while some live at the edge of poverty (e.g. in Dominica, St. Lucia). Direct, lump-sum income may be needed to bridge the transition phase. Local governments or local development agencies are in the best position for low-cost distribution of income deficiency payments to smallholder export producers. Trying to accomplish this goal by generic trade preferences is like using a battleship for killing mosquitoes.

![Graph 4: Aid transfer effectiveness of banana regime, before 1993](image)

Note: a) Of each $5.30 cost to consumers $3 flowed into marketing margins of EU marketers. About $0.40 went into tax revenue and other internal EU transfers. Net costs to the EU are estimated to be $1.90. About $0.90 of this went into having bananas produced by relatively inefficient producers. Only $1 formed an effective aid transfer to ACP counties (Borell, 1997a).

Trade preferences form a very ineffective device for transferring development assistance to ACP countries. Research by Borell and Yang (1992; 1997a; 1997b) showed that the EU banana regime was very ineffective in generating aid transfers to banana-dependent ACP countries. They calculated that, before the 1993 reform, EU consumers paid $1610 mln (through high banana prices) to deliver $302 mln of effective aid to 11 preferred supplier countries. In other words, it cost $5.30 to deliver $1 of net banana-related aid. The flow of funds is shown in Graph 4. After the 1993 reform, transfer efficiency of EU banana policy has even deteriorated: it now costs EU consumers $13.25 to effectively transfer $1 of benefit (Borell, 1997a; 1997b). EU marketers have been the main beneficiaries of the 1993 policy.

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13 E.g. yields per hectare in 1995 of Costa Rica, Ecuador and St Lucia compared as 5.6: 3.0: 1 (FAO 1998).
package. They realized marketing margins about double the size of what they are in the USA. From the perspective of the EU’s development policy, the banana regime has proven to be an inefficient device for transferring aid to banana-dependent ACP countries. The costs of direct development aid to replace a possible loss of banana exports to the EU are moderate. The four ACP countries which depended most on banana exports to the EU (cf. Table 4) together export 125 mln ECU of bananas to the EU in 1995. The effective value of trade preferences represent only half this amount. Even if the EU would buy these country’s entire bananas exports and dump it in the sea, this seemingly wasteful action would still create a large welfare gain compared to the present banana regime.

Conclusions. Preferential trade access for ACP countries and trade discrimination against dollar banana countries cannot be justified by differences in the development level of both country groups. With exception of four small Caribbean countries, ACP economies do not depend more on banana exports to the EU than dollar banana countries. No other economic characteristics of both country groups could be identified that warrant the present trade discrimination. Trade preferences for ACP banana exporters cannot be justified by the infant industry argument; their lack of competitiveness in the world banana market is not of a temporary character. Any positive externalities associated with banana exports can more efficiently be generated through direct aid. Direct development aid also forms a better way to promote diversification of exports and production structures of banana-dependent countries.

Banana trade and the environment

Most environmental effects of banana production are of a local scope, and do not cross national boundaries. It is not evident, therefore, that environmental effects of banana production should play a role in reform of international banana trade. Moreover, WTO rules do not allow for trade discriminatory measures based on environmental characteristics of the production process when these characteristic do not affect the banana product itself. This section argues, however, that there is a positive reason to include environment-related issues in a package deal to compensate potential losers of a liberalized European banana trade.

Environmental effects of production. Tree crops like bananas may offer valuable ecological services. When maturing, they protect soils against erosion in hilly areas, their shadow helps water conservation and humidity regulation, while they may provide a natural habitat for animals. The occurrence of such positive ecological services depends on production scale and production methods. Varied, inter-cropped production systems, like in large parts of smallholder banana production, are more likely to generate positive environmental effects than mono-crop production systems. Monocrop production of bananas in large areas is an ecologically vulnerable production system. High levels of chemical plant protection
inputs are needed to protect plants against insects, bacteria and fungi. Irrigation and fertilizers are amply used to boost crop yields.

Pesticides are applied through broad-spectre air-spraying and through pesticide-containing plastic bags put around the racemes. Airspraying affects all life forms in or near the banana plantations. It caused health problems for banana workers and their families: diseases, infertility, and lethal accidents. It also causes water pollution and other disturbance of local ecological balances. Effects may be felt beyond production regions, e.g. in coastal areas or through pesticide accumulation in migratory birds and fish (e.g. Colitt, 1994). Ever increasing pesticide quantities or pesticide toxicity are required as the abated organisms develop resistance. Pesticide use may be stimulated by subsidized pesticides, lacking penalties for negative externalities and inefficient application routines (e.g. inadequate disposal of pesticide-containing plastic bags). Heavy use of pesticides is partly caused by demand side conditions. Western consumers have got used to undamaged and unblemished fruits. Pesticides are seldom applied to non-export bananas, plantains and cooking bananas.

For construction of banana plantations large areas are deforested with strong temporary erosion effects. The wash water of banana packing plants often still contains agrochemicals residues, causing off-site water pollution. Finally, banana production generates huge amounts of organic waste (leaves, raceme stem, part of sub-standard bananas), some 3.5 ton for every ton of export bananas. Traditional dumps are open-air sites, often situated along river banks. The organic waste has a high biological oxygen demand leading to fish kill in surface waters. Also nondegradable waste like agrochemical containers and pesticide-impregnated plastic bags is created which often end up in open-air dumps.

**Banana trade and environment.** An important new development is that consumer in OECD countries increasingly prefer ‘green and clean’ bananas, i.e. bananas without pesticide residues, produced in an environmentally sound and socially acceptable way. An EC-commissioned study by Eurobarometer in 1997 revealed that around three quarters of the Europeans would buy so-called ‘fair trade’ bananas.

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14 One report from Costa Rica mentions: “Fertilizers, insecticides and herbicides are applied 22 times during the growth cycle [...]. In addition, 1.4 litre per hectare of fungicide is applied from airplanes 45 times in one growth cycle. Of this, 15% is lost to wind drift and falls outside the plantation; 40% ends up on the soil rather than on the plants; and approximately 35% is washed off by the rain. This results in a 90% loss of the estimated 11 mln. litres of fungicide, water and oil mix applied each year tot the banana production regions of Costa Rica” (Hernandez and Witter 1996: 175). On the ecological impacts of banana cultivation see inter alia: Dinham (1993); Hernandez and Witter (1996); IUCN (1992); Linnemann et al. (1993: 97-102); Slutzky (1994); Stover and Simmonds (1987); Wheat (1996).


16 Organic waste could at least partially be used for animal feed and paper manufacturing, but these practices are not yet practiced on a wide scale. Banana multinationals in Central America have undertaken some attempts at plastic recycling.
grown under ethically-approved conditions in developing countries, provided that such bananas would be recognizably present in their shops alongside ‘standard’ bananas. A total of 37% of EU consumers said that they were prepared to pay a premium of 10% above the price of ‘standard’ bananas, for bananas grown in accordance with environmental and social standards laid down by bodies such as ILO and UN. A conservative EU estimate quantifies the ‘fair trade’ market segment at 300-400,000 tons per year, that is 8-10% of the total EU market. The fact that EU consumers have such outspoken preference for bananas which are produced in an environmentally sound way, forms a strong basis for an ecolabelling scheme for bananas. Some ecolabelling schemes for bananas, joined in EUROBAN, are already in operation in the EU. The change in consumer attitudes is illustrated by the rapid rise in market share (to 10%) of Max Havelaar ‘Oké’ bananas soon after their introduction in the Dutch market.

Ecolabelling creates a basis for product differentiation and price premiums for bananas that have been produced in an ecologically sound way. The existence of such price premiums creates new market opportunities for ACP bananas produced by smallholders under socially acceptable conditions and without intensive application of agrochemicals. If these aspects are included, productivity differences between large-scale produced bananas from dollar banana countries and smallholder bananas from the Caribbean will become smaller. The aforementioned estimate of the ‘fair trade’ market segment in Europe surpasses total ACP banana exports to the EU. Under a liberalized banana trade regime, the price premiums for eco-bananas will offer market shelter for exports produced by ACP smallholders. It is therefore essential to protect such market premiums for eco-bananas. For large banana companies the stakes are high. They wrestle with the change in preferences, since for them there are trade-offs between sustainability, productivity and profits.

Ecolabelling schemes and the price premium they protect, can only survive with consumer confidence in their trustworthiness. Cheating and free-rider behaviour would eventually undermine credibility. Consumer goodwill also erodes when a confusing jumble of competing ecolabels arises. Large banana companies already tied to jump on the bandwagon of the ‘fair trade’ movement. The initial success of banana ecolabels in carving out niche market price premiums induced Chiquita in 1995 to start its ‘ECO-OK’ ecolabel programme directed at certification for its Costa Rican plantation, although the label completely disregards agrochemical use (Van de Kasteele, 1997). If cleverly marketed, such labelling initiatives might cause confusion and eventually undermine consumer trust in ecolabels.

19 Del Monte manager Murray recently stated: “We definitely feel that ethical production is the key to keeping us in business”, recognising a customers demand for sustainably produced bananas (Wilson 1998).
Protection of the niche market for premium eco-bananas makes it essential that issuing and monitoring of ecolabels is kept completely apart from the operators who trade in ecolabelled bananas. Ecolabelling for bananas preferably should be done by an independent organization which is acceptable for the entire banana industry. Next section explores the idea that this could be become part of an international package deal for a liberalized banana trade.

**Conclusions.** Most dollar bananas come from pesticide-intensive large plantations, while most Caribbean (ACP) bananas stem from smallholder production where production is more environmentally sustainable. WTO rules preclude the use of trade discrimination on the basis of this difference. Voluntary, market-supported developments offer better perspectives for the future. The sharp rise in environmental consumer consciousness creates a substantial niche market for eco-bananas with price premiums that at least partially compensate for higher production costs of smallholder banana production from ACP countries. In the longer term, large banana companies can be expected to enter this market. ACP bananas will only keep their market position if they succeed in strengthening their overall production efficiency. Ecolabels and market premiums for ecobananas can be a dynamising instrument for achieving an overall change in the industry towards environmentally sound production methods. In the short term, ecolabelling schemes could be an important element in a package to compensate potential losers of liberalized banana trade.

*The role of an International Banana Agreement*

Reform of the EU banana policy has become unavoidable for several reasons. The EU has agreed to modify its banana import policy in order to comply with the decision of the WTO’s Apellate Body. The EU’s first proposals did not indicate a decision to liberalize banana imports. WTO-incompatible elements of the present import licensing scheme will be adapted, but ACP trade preferences remain intact. A more profound change might come when the Fourth Lomé Agreement and its Banana Protocol expire. The European Commission is proposing a successor agreement which makes a distinction between countries which are and those which are not capable of rapidly integrating into the world economy. While supporting the former group’s capabilities to integrate in the world market, the latter group will be eligible for poverty-focused development assistance (European Commission 1996). Generic trade preferences for all ACP countries would not fit into this approach. With regard to bananas, this section sketches a policy alternative that could well fit into this new line of thinking.

*Article 1 of the Banana Protocol states: “In respect of its banana exports to the Community markets, no ACP State shall be placed, as regards to its traditional markets and its advantages on those markets, in a less favourable situation than in the past or at present.” The Appellate Body of the WTO rejected that the current EU banana regime can be defended on basis of this article (WTO 1997).*
A new International Banana Agreement forms the core of the proposal. The proposal for an International Banana Agreement is based on the following considerations:

I. Liberalization of banana trade creates gains for several market players: EU consumers, governments of dollar banana countries, US government; multinational banana companies.

II. All importing and exporting countries would benefit from promotion of banana consumption, improved banana market efficiency and improved trade statistics. All market parties gain from preserving consumer trust in bananas as a product, including aspects like healthiness and taste, and confidence that bananas are produced under acceptable ecological and social minimum conditions.

III. Compensation of potential losers of trade liberalization is made easier when part of smallholder ACP banana production can be sold under a banana ecolabelling scheme that provide a price premium to compensate for higher production costs.

IV. Compensation remaining losses for is easier done on a burden-sharing basis by all potential winners. It creates mutual goodwill and speeds up the liberalization procedure. The USA has already declared its willingness to co-operate with the EU in this area, in the light of its non-banana interests in the Caribbean region (USTR, 1996).

V. Safeguarding price premium for eco-bananas depends on a the presence of a simple and reliable ecolabel issued by an independent, high-standard international organization.

An International Banana Agreement. The aforementioned issues could be promoted by an International Banana Organization, functioning under the umbrella of an International Banana Agreement. The latter would be an agreement between governments to regulate common interests with regard to banana production, trade and consumption. The agreement is created for an agreed time period (e.g. 5 years), with the possibility of renewal. The agreement aims at reconciling a commitment to free trade, ecological sustainability of banana production and socio-economic development interests of banana-exporting countries. The International Banana Agreement would only govern international trade in bananas of the Cavendish variety, which is the dominant export banana. Member countries periodically convene to initiate programmes for implementation of the goals of the agreement and to assess progress with regard to ongoing projects. The agreement needs a secretariat, called the International Banana Organization (IBO), which implements and prepares decisions of the council of member countries. Box 1 identifies a number of specific tasks for the IBO. The IBO needs not become a large organization. Specific projects and monitoring tasks can be done on a contracting basis by external organizations and consultants.
Operating modalities of the International Banana Agreement can only be worked out in negotiations between potential member countries. FAO and/or UNCTAD offer the most appropriate international platform for preparing the agreement, through consultation with potential member countries, preparation of a negotiation document, and a multi-country negotiation roundtable.

**Box I: Potential task areas for the International Banana Organization**

* Management of a **Smallholder Competitiveness Fund** which provides cheap loans to governments and small-farmer co-operatives from developing countries for projects which aim at strengthening production efficiency and market competitiveness. Qualification criteria and operating modalities have to be worked out.

* Management of a **Banana Diversification Fund** providing low-interests loans and gifts to governments of high-cost, high-dependency export countries for projects to diminish their structural dependence on banana exports.

* Create and promote a credible international ecolabel for bananas: guarantee a universal banana ecolabel, issue certificates of origin for certified producers, periodical monitoring of certified producers.

* Management of a **Banana Environment Fund** formed by voluntary contributions by member countries, private companies and international organizations. It provides cheap loans for capital-short national banana producers in developing countries which want to convert their traditional production methods into more environmentally sound production methods, but which have no access to commercial credit to finance the necessary investments. Project proposals have to be endorsed by the member country’s government, and repayment is conditional upon performance. Further qualification criteria and operating modalities have to worked out.

* Promotion of international banana consumption and ecologically sustainable banana production

* Provide consistent statistics on international banana production, trade and consumption.

* Responsibility for regular daily relations with member countries and international organizations (UNCTAD, FAO, Common Fund for Commodities, EU, World Bank, Caribbean Banana Exporters Association, etc.).

* Offer a platform for periodic consultation with environmental and development NGOs and private sector representatives

* Operate as secretariat for the member country council.

21 A similar environment fund, based on voluntary contributions by member countries, was founded under the International Cocoa Agreement in 1997.
The agreement enters into operation when a sufficient number of governments have committed themselves and have ratified the agreement. The required minimum country participation can be formulated in terms of X % of world imports (e.g. 60%) and Y % of world exports (e.g. 60%) in a reference year. Participation of large import markets like the USA, EU and Japan would greatly improve the chances of success.

The International Banana Agreement could operate under the auspices of UNCTAD, like in the case of other international commodity agreements. It would also become associated with the UN’s Common Fund for Commodities which has separate financing facilities for projects that boost the position of production countries in marketing and distribution of primary commodities.22

**Positioning of involved parties** For the EU, liberalization of its EU banana imports would even be beneficial without an International Banana Agreement. The latter’s Smallholder Competitiveness Fund and Banana Diversification Fund make it possible to realize EU policy goals through a joint effort with other importing countries. Moreover, the agreement makes it possible to deal simultaneously with environmental issues through the Banana Environment Fund and the ecolabelling scheme. The EU could transfer part of its current Lomé obligations to the new IBO.23

Potential gains are to be achieved for those parties which in the past refused to participate in an International Banana Agreement: export countries, the USA and large banana companies. The new agreement does not, however, aim at market and price intervention (e.g. by quota systems), while ecolabel scheme is voluntary one. The prospect of free trade in bananas and free entry to the European market makes co-operation by these players much more likely. The US could bring part of its Caribbean development policies under the new agreement. Some Latin American countries may have initial reservations because of the possible initial impact of the ecolabelling scheme on their exports of ‘standard’ bananas. The scheme is however a voluntary, consumer-driven one, and private banana companies in their countries may wish to participate because of the potential price premium that can be earned. There is strong evidence that sticking to old-fashioned, ‘dirty’ production methods leads to future backwardness and competition disadvantage.24 Kaimowitz (1996) has shown that environmental policy innovation in Latin America was often induced from abroad. However, the strongest incentive for Latin American countries to participate will be the additional export opportunities arising after EU import liberalization.

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22 The funding mandate of the Common Fund allows for projects to improve the environmental record of banana production, diversification programmes, and programmes to improve competitiveness of smallholder production of bananas.

23 The agreement does not rule out the EU’s (or any other participating government’s) possibilities to undertake additional bilateral and more concessional development assistance programmes in the countries concerned.

24 Porter and Van der Linde (1995); Pimentel et al. (1993); Whittaker et al. (1995); UNCTAD (1996b).
Caribbean countries can be expected to have strong initial reservations against conclusion of the new International Banana Agreement. However, once it exists, they will be better off by joining the agreement. Membership makes them eligible for the agreement’s funding of investments in alternative production and export sources. African ACP countries have less reasons for opposing the new agreement than Caribbean countries could have. They are not very dependent on banana exports and might be among the main beneficiaries of the competitiveness assistance fund and the ecolabel program.25 African countries could benefit from increased world demand after banana trade has been liberalized.

**Consumer information under an International Banana Agreement.** The agreement can become a strong stimulus for environmental innovation in the banana sector, both through its Banana Environment Fund and through its ecolabel scheme. An ecolabelling scheme issued under auspices of the agreement preferably has to be supported by all member countries. Even though it is voluntary, the ecolabel’s position is strengthened when member production countries endorse the IBO ecolabel’s qualification standards. Rather than starting with full-fledged, high-profile one might start by defining common minimum standards for qualification. Minimum environmental standards might be adapted from those used by Euroban: biodiversity (protection of natural areas), pesticides and nutrients (documentation, control and reduction); prevention of erosion and water pollution; reduction of solid waste (control, composting, re-use). Over time, the member country council may decide on tightening certification standards of the IBO ecolabel.

A strong IBO-supported ecolabel for bananas will secure a price premium for banana produced in an ecologically-sound way. In the short term, this will offer market opportunities for smallholder banana producers from high-cost export countries. In the longer term, the ecolabel will support an overall upgrading of environmental standards and working methods in the banana sector.

**Final remarks**

Some parties in the EU banana conflict adopt a backward-looking perspective, taking pre-1993 positions as their point of departure. The present EU banana regime, apart from its often-contested drawbacks, has the large advantage that it created a common benchmark situation for all EU countries. For the first time since Rome Treaty was negotiated, colonial histories can no longer paralyze discussion between EU-members. The present EU banana import regime has been defended by

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25 For instance, in the Ghanaian Volta River region a plantation has been set up as the first plantation in Africa that will operate according to ‘fair trade’ production criteria (Banana Trade News Bulletin; No. 11112, November 1997).
development-related arguments. The paper has however shown that these can no longer support the discriminatory EU trade regime for bananas. Other relevant changes since the early 1990s include the increased WTO-membership of banana-producing countries, and the increased consumer attention for environmental and social conditions in banana production. All these changes in policy variables make it possible now to look forward to future welfare benefits which become possible by changes in the present EU banana regime.

The largest gains from EU trade liberalization will be booked by European consumers, followed by competitive world market producers in dollar banana countries, and multinational banana companies. Most short-term losses will be borne by high-cost Caribbean smallholders and privileged European traders. The group of most-affected Caribbean export producers is limited in size, which makes it relatively easy to compensate them. The compensation package can be given the form of a new International Banana Agreement that reconciles a commitment to free trade in bananas, promotion of sustainable banana production and promotion of socio-economic development in banana-exporting countries.

**Annex tables**

**Table A1**

<table>
<thead>
<tr>
<th>Source</th>
<th>Method</th>
<th>Estim. welfare loss German consumers</th>
<th>Welfare change other ‘players’ in Germany</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guymard et al. (1996)</td>
<td>Simulation with static partial equilibrium model. Elasticties partly estimated (Denmark, France, Italy and UK), partly assumed, partly from literature. Reference prices 1989-91. Deficiency payments neutralize effect on EU banana producers. Constant margins between import c.i.f. prices and export fob prices assumed.</td>
<td>106 mln US$ (91 mln ECU)</td>
<td></td>
</tr>
<tr>
<td>3orell (1997)</td>
<td>Simulation with static partial equilibrium model. Elasticities partly estimated, partly assumed</td>
<td>800 mln US$</td>
<td></td>
</tr>
</tbody>
</table>
### Table A2

**Estimates of welfare costs of European banana regime (before and after 1993) compared with free trade in bananas**

<table>
<thead>
<tr>
<th>Source</th>
<th>Method</th>
<th>Comparison before/ after 1993</th>
<th>Welfare costs for EU consumers</th>
<th>Net welfare costs for EU:</th>
</tr>
</thead>
<tbody>
<tr>
<td>McInerney and Peston (1992)</td>
<td>Simulation with static partial equilibrium model.</td>
<td>before 1993 banana regime</td>
<td>approx. 1600 mln US$</td>
<td>approx. 575 mln US$</td>
</tr>
</tbody>
</table>

**Note:**
- a) quoted in Hallam and Peston (1997).
- b) Applied estimation methods, data sources, discussion of data quality and precise econometric results are sometimes kept hidden from readers, e.g. Read (1994), Matthews (1994).
References


Borell, B. (1997b) ‘Well within reach - a low cost way to comply with the WTO banana decision using tariffs’, Australian Centre for International Economics, Canberra.


