



ACP-EU Trade and Aid Co-operation Post-Lomé IV:
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Summary

A special protocol of the Lomé Convention assures preferential treatment of bananas exports to the European Union from 'traditional ACP exporters. The Lomé protocol has until recently been successful in maintaining ACP exports but less successful in raising competitiveness of ACP exporters. The Lomé preferences have been delivered by the EUs banana trade regime. Without the preferential treatment accorded by the EU regime, ACP exports could not compete on EU markets because of high costs and variable quality compared to Latin American supplies. The EUs banana policy has been challenged in the WTO. The WTO Panel found against aspects of the regime and the EU has lodged an appeal. Some ACP exporters, notably the Windward Islands, are highly dependent on banana exports in terms of contribution to GDP and employment. The loss of banana trade preferences could lead to the loss of the banana industry in certain ACP states, with far-reaching economic and political effects. Whatever the outcome of the WTO case, it is essential to raise the competitiveness of ACP banana exports, and the trade development provisions of the Lomé protocol need to be emphasised. A smaller industry producing higher quality bananas is the likely result. Diversification opportunities in the Windward Islands are limited. Competition on world markets for alternative horticultural crops is severe. Tourism development thus far has arguably contributed little to the local demand for agricultural products.

8.1 Introduction

A special protocol of the Lomé Convention has assured preferential treatment of banana exports to the

European Union from 'traditional ACP banana exporters. The mechanisms by which these preferences are delivered are those of the EUs banana trade regime. Indeed, the need to satisfy the Lomé commitment was perhaps the major motivating factor in the development of the EUs common banana trade policy. The Lomé Protocol and the EU banana policy are therefore inextricably linked, and consideration of the future of the Lomé commitment cannot be divorced from consideration of the future of the EU regime. Since its introduction in 1993, the regime has been under attack not only from those Latin American banana exporters who regard it as discriminatory, but also from the US for the same reason, and from certain EU members, notably Germany, who regard it as costly and inefficient. The regime has recently faced a challenge in the WTO, and the Interim Report of the WTO Panel has found against certain aspects. An appeal is currently being prepared by the EU. The outcome of the WTO case will be a major influence on the future of the Lomé Protocol. The stakes are high for all the banana exporting countries, but for some highly dependent ACP exporters in the Caribbean the Lomé Protocol is vital not only to their banana trade, but to their very economic survival. The weak competitive position of ACP banana exports vis-à-vis Latin American exports (so-called 'dollar bananas') means that preferential trade arrangements with the EU are essential if ACP production is to be maintained. Relatively few ACP countries are directly affected by the WTO judgement. However, the outcome of the WTOs deliberations has a wider significance beyond banana trade, since it provides a test case of the sustainability of Lomé preferential trading arrangements after the Uruguay Round.

8.2 The Lomé banana protocol

Article I of Protocol 5 to the Fourth Lomé Convention states that:

"In respect of its banana exports to the Community markets, no ACP State shall be placed, as regards access to its traditional markets and its advantages on those markets, in a less favourable situation than in the past or at present."

This implies a legal obligation on the part of the EU to maintain access to EU markets for bananas from traditional ACP exporters on at least as favourable a basis as had been enjoyed by those exporters up to the signing of the Convention in 1990. This is a highly specific commitment, and one which would be difficult to meet by means other than those of the current EU banana regime. Article 1 has not surprisingly attracted most attention in discussions of banana trade policy, but the Lomé commitment has a broader content which should not be overlooked. This involves trade development aimed at expansion of ACP-EU trade through improving ACP access to EU markets and enhancing ACP competitiveness in those markets. Thus, the banana protocol envisages EU assistance to improve competitiveness at all stages of production and marketing by ACP exporters, and financial assistance mainly through the STABEX scheme. Article 2 of the banana protocol provides for activities to "improve the conditions for the production and marketing of bananas", and mentions research, harvesting, packaging and handling, internal transport and storage, marketing and trade promotion. As the future of the preferential trade arrangements has become less certain, so these trade development measures become increasingly important. The ACP banana exporters need to consider what is the most appropriate form for these provisions.

8.3 The EU Banana Regime

Under Article 115 of the Treaty of Rome, individual EU member states were allowed to determine their own banana trade policy prior to 1993. However, this was subject to the general requirement that imports from ACP countries should enter duty free, while imports from non-Community or non-ACP countries should be subject to the 20% Common External Tariff (CET). Thus, at the time of the signing of Lomé IV, each member state of the European Community pursued its own banana trade policy. Delivery of the

Lomé commitment rested on a limited number of member states - UK, France and Italy - and mainly reflected past colonial ties with certain ACP banana exporters. In general, this commitment was taken on willingly by the importing countries concerned.

In practice, more than half of the Community's imports of ACP bananas were into the UK. The UK guaranteed a market for exports from the Windward Islands, Jamaica, Belize and Surinam. These countries exported almost exclusively to the United Kingdom. The Windward Islands were the major supplier with about half of the market and rapidly increasing export volumes. Licences were issued to import dollar bananas to meet any estimated shortfall between demand and imports from the preferred exporters. France guaranteed two thirds of its market for production from its overseas departments, Guadeloupe and Martinique. The remaining third was allocated to supplies from Francophone Africa, especially Cameroon and Côte d'Ivoire. Imports from other sources were permitted under licence only when there was a supply shortfall from the preferred sources. Italy guaranteed a market for imports from Somalia, although the bulk of Italy's imports were from Latin America under quota and subject to the 20% common external tariff (CET). Outside these preferential arrangements, the largest Community market, Germany, obtained all its supplies from Latin America. These entered duty free under a special dispensation under the Treaty of Rome. Belgium, Denmark, Ireland, Luxembourg, and the Netherlands also obtained all their imports from Latin America, but subjected them to the CET. Greece, Portugal and Spain are self-sufficient to varying degrees.

With the creation of the so-called 'Single Market' all barriers to trade within the EC were to be removed by 31st December 1992. The removal of obstacles to trade in bananas from one European Community state to another opened previously protected markets to imports of low-cost dollar bananas, and meant that the protective and preferential trading arrangements operated by certain member states could no longer be sustained. Supplies from ACP exporters and European Community producers could not compete on a free market, not even with the protection of the 20% tariff on dollar imports. This called for the harmonisation of member states arrangements, in a common banana trade policy presumably by somehow extending the preferential trade arrangements of UK, France and Italy to all EC states so that honouring the Lomé commitment became a Community concern. Unlike the previous arrangements, this commitment has not been taken on willingly by all member states.

However, a banana trade policy for the European Union as a whole needed to satisfy more than just the Lomé commitment: the single market requires unobstructed trade between member states; there is an obligation to maintain Community production in the Canary Islands, Crete, Madeira and French overseas departments of Guadeloupe and Martinique; any protection against lower cost dollar supplies must be compatible with obligations not to raise tariffs or introduce new restrictive trade measures under the GATT; since ACP and domestic supplies are inadequate to meet demand, dollar supplies must continue to provide a significant proportion of requirements; finally, the impact of any trade policy on the interests of consumers must be considered. Not surprisingly, given these sometimes conflicting objectives, discussion of the shape of the common banana policy was heated.

Needless to say, those member states with free or relatively free markets - Germany and the Benelux countries - favoured the most liberal options of either a free market or a tariff regime, since anything else would lead to higher prices. On the other hand, France, Greece, Portugal, Spain and the United Kingdom with domestic production or preferential suppliers to protect favoured the more protectionist regimes. Given such strong differences of opinion within the European Community, and the intense lobbying by exporting countries and banana companies, it is not surprising that the European Commission's proposed regulations were not presented until August 1992, leaving little time for discussion and agreement if they were to be adopted by the end of December. However, the likely basic features of the regime - quotas on dollar banana imports and the controversial mechanisms for allocating import licences - were becoming clear following the DGVI Background Note on a proposal for the regime released in February 1992.

A compromise agreement was not reached until December 1992. This was formally approved in March 1993, and the system introduced from 1st July, making bananas the only exception to the single market.

The elements of the regime were set out in Regulation 404/93. The new regime allowed tariff-free imports from each traditional ACP country up to the maximum quantity they exported to the Community in any year up to and including 1990. This provided for a quota of 857,700 tonnes distributed between the traditional ACP exporters as follows: Côte d'Ivoire 155,000 tonnes; Cameroon 155,000 tonnes; Somalia 60,000 tonnes; Madagascar 5,900 tonnes; Cape Verde 4,800 tonnes; St. Lucia 127,000 tonnes; Dominica 71,000 tonnes; St. Vincent 82,000 tonnes; Grenada 14,000 tonnes; Jamaica 105,000 tonnes; Belize 40,000 tonnes; and Surinam 38,000 tonnes. Under the 1994 'Framework Agreement, ACP exports above this level - non-traditional ACP trade - may also enter tariff free up to 90,000 tonnes within the overall quota for imports from non-traditional ACP suppliers. Cameroon, Côte d'Ivoire and Belize have been allocated about one third of these 90,000 tonnes. Non-traditional ACP imports over the quota were subject to a tariff of 750 ECU per tonne - a lower rate than for over-quota dollar supplies. A tariff of 100 ECU per tonne was to be charged on imports of dollar bananas initially up to two million tonnes (approximately the quantity imported in 1990). Subsequent adjustments to the dollar quota under the so-called 'Framework Agreement raised this to 2.2 million tonnes in 1995, or 2.11 million tonnes after allowing for non-traditional imports from ACP countries of 90,000 tonnes, and reduced the in-quota tariff to 75 ECU per tonne. The Framework Agreement, signed by Colombia, Costa Rica, Nicaragua and Venezuela, gave country-specific quotas to the four signatories (of 21%, 23.4%, 3% and 2% respectively) who undertook not to complain to the WTO about the EU regime until 2003. The quota was raised again in 1996 by 353,000 tonnes to 2.533 million tonnes to cover the additional requirements following the accession of Austria, Finland and Sweden in 1995 (353,000 tonnes being the annual average consumption in these countries between 1991 and 1993). Dollar imports in excess of the quota faced a prohibitive tariff of 850 ECU per tonne, around 170% at current prices, in the regime as introduced. Provision was made through the licence allocation procedures for traders who marketed Community and traditional supplier ACP bananas between 1989 and 1991 ('category b traders) to cross-subsidise this activity: they are allocated import certificates to sell 30% of the dollar supplies. Operators who marketed dollar or non-traditional ACP supplies ('category a traders) are awarded 66.5% of the certificates, and the remaining 3.5% of certificates go to operators who started marketing dollar or non-traditional ACP supplies in 1992 ('category c traders). Following the raising of the quota to 2.553 million tonnes in 1996, the allocation to 'category a importers was increased to 70% and the allocation to 'category b importers reduced to 26% to reflect the fact that the new member states had relied on dollar imports prior to accession. Although the 'category b allocation was reduced in percentage terms, in volume terms it remained unchanged. A further amendment made at this time was to introduce provision for 'category c traders to earn 'category a status after three years. The distribution of certificates to individual traders is based on their average volumes traded in the previous three years multiplied by a coefficient relating to the extent of their involvement in the import and distribution chain. The chain is divided into three: purchase and transport of bananas to the EC (coefficient=0.57); customs processing on arrival (coefficient=0.15); and ripening and selling to wholesale (coefficient=0.28). In practice most operators would undertake all these activities. The regime provided for deficiency payments to EU suppliers, including overseas territories, on production up to 854,000 tonnes. This quantity is distributed between the various suppliers: Canary Islands 420,000 tonnes; Madeira 50,000 tonnes; Crete 15,000 tonnes; Guadeloupe 150,000 tonnes; and Martinique 219,000 tonnes. A direct payment of 1000 ECU per hectare is also available to those producers ceasing production. At the conclusion of the Uruguay Round, the banana regime, including the Framework Agreement, was explicitly accepted as part of the package.

The significance of the 'Banana Protocol to the discussions of the creation of an EU banana regime must be stressed. Any proposal for a regime had to pass the test of not placing the ACP traditional exporters in "a less favourable situation than in the past or at present". The UK, France and Italy were relatively high-

price markets and, as such, were attractive targets for the multinational banana companies - Chiquita, Dole and Del Monte. If dollar bananas had been allowed free access on to these markets, or access subject only to a 'reasonable tariff there is no doubt that they would have been able to force the ACP fruit out by an aggressive price and marketing policy. This would have contravened the requirement set out in the banana protocol of the Lomé Convention. If ACP bananas were forced out of these markets, there would have been nowhere else for them to go. The price would be unattractive for other European consumers who would still have full access to dollar bananas if duty-free dollar bananas from Germany, for example, were allowed to circulate freely in the Community. The banana multinationals would have been given a free hand in the EC, at the expense of the Community's traditional partners. Therefore, the ACP exporters would have been left in a worse position on their traditional markets and it would have been impossible to fulfil the Lomé IV commitments. Apparently, this view of how the banana market would operate after the European Single Market came into force strongly influenced the European Commissions view of what Europe's banana trade policies should be.

8.4 The Lomé Protocol and ACP Banana Trade

The *Lomé Protocol* might be regarded as successful in the sense that it has allowed access to the EU market and ACP banana exports to the EU broadly to be sustained. ACP exporters have fared less well since the replacement of the various national arrangements with the common regime which has exposed ACP fruit to competition from dollar fruit and to lower prices on previously protected markets. Without preferential trading arrangements, and arguably preferential trading arrangements of the specific kind provided by the EU banana regime, the ACP exporters would have no chance of competing on the EU market, or perhaps any other market, with dollar imports from Latin America. The loss of such preferential arrangements implications for certain ACP exporters would be potentially devastating. However, while the *Lomé Protocol* might have been successful in maintaining exports, it has provided little incentive to improve the competitiveness of ACP bananas. Costs of production and marketing are high and quality variable. In some cases, the returns to banana growing have encouraged expansion of production into unsuitable areas causing environmental damage - clearing of rain- forest and consequent flooding in the Windwards, for example. The need to improve competitiveness must be taken seriously by the ACP exporters. There have been a number of attempts to improve quality in the Windward Islands, and producers have made some progress towards meeting the requirements of export markets. However, the UK is effectively the only market and market share has been lost even there. Fruit quality has struggled to reach the standards required by the multiples which account for ninety per cent of retail banana sales. Under the EU's common banana regime retailers now have the option of turning to dollar supplies if these better meet their needs, so ACP quality and quality control have got to be competitive. EU Regulation 2686/94 provides for assistance in the adaptation of ACP production conditions, and there has been a quality improvement scheme in the Windwards. STABEX funds might also be used for this kind of purpose. However, progress is slow and time is short.

The traditional ACP exporters are almost totally reliant on the EU market: the Caribbean exporters export 100 per cent to the EU, while the West African exporters export some 95 per cent. This compares with the 25-30% of dollar exports which go to the EU market. EU imports from different sources are shown in Figure 12.1. Within the EU market, most ACP supplies are to the UK: by 1996, for example, the UK was taking all of the Windward Island exports.

Figure 8.1 EU Banana Supply 1988-94 by Source

Note: The Dominican Republic is a non-traditional ACP banana exporter. Her exports have increased markedly after 1991 and are plotted separately on the chart above.

Source: Eurostat

The importance of the banana trade to the economies of the ACP countries varies from one exporter to another. The Windward Islands of St. Lucia, Dominica and St. Vincent are a special case of extremely high dependency with 50-60% of their export earnings coming from bananas. For Somalia, bananas have accounted for more than 20% of total exports. Elsewhere the extent of dependency is less. Bananas are also a major source of income and employment for St. Lucia, St. Vincent and Dominica. In these three Windward Islands, bananas provide 16-17% of GDP. In Dominica and St. Lucia a third of the labour force is involved in the banana industry, while in St. Vincent the figure is as high as 70%. Obviously, such dependency means that the economies concerned are particularly exposed to the risk of exogenous shocks to their production and market opportunities. Any variations in the preferences accorded to them by the Lomé protocol are potentially disastrous.

Measures to reduce dependency on bananas in the Windward Islands have frequently been discussed and implemented. However, the profitability of banana production has militated against diversification. In some ways the islands are captives of the banana trade. This is not only because the returns to bananas cannot be matched by alternative export crops, but also because the regular weekly harvesting and shipping schedule for bananas is a significant part of any diversification strategy. The dilemma was summarised by the former Prime Minister of St. Lucia, John Compton: "Without ships there can be no diversification, and without bananas there can be no ships". In any case, alternative export crops suggested, such as exotic fruits and vegetables, would face stiff competition on uncertain world markets from high quality exports. Scope for the development of manufacturing industry is limited, while the economic and social benefits of tourism are not generally agreed upon.

While yields of the Caribbean exporters have increased, the prevailing smallholder production and ecological conditions mean that they remain substantially lower than those achievable on the plantations of Latin America. Without continued preferential trading arrangements to guarantee markets for higher cost ACP supplies production, at least on the current scale, could not be sustained. Given the topography of the Caribbean islands, plantation production and the possibility to reap economies of scale is not generally possible. Plantation production on a medium to large scale has been developed in the more favourable locations of Cameroon and Côte d'Ivoire, mainly under multinational control. These locations can compete in husbandry, harvesting and packing and volumes produced allow a regular shipping schedule, but shipping costs remain high and fruit quality variable (Fabre, 1994).

Precise inter-country comparisons of costs between dollar and ACP exporters are problematic because of limitations in the quality of the data. Exports to the EU market in 1994 from Ecuador, Colombia and Costa Rica received f.o.b. prices of \$4.2/box, \$5.1/box and \$5.2/box respectively. Guatemala received \$3.7/box and Honduras received \$3.8/box. Caribbean ACP producers received f.o.b. prices of around \$9/box, and African ACP producers received around \$8/box. The price gap between ACP exporters and even the least competitive dollar exporters is up to 80%. While in the longer term there may be some scope for improving the competitiveness of ACP production, preferential trade arrangements appear to be essential for the foreseeable future. These average figures mask significant variation from farm to farm in efficiency and costs. Even in the Windward Islands there are growers who could compete at little more than world prices.

8.5 The WTO Case

It is clear that the Lomé protocol is vital to the ACP banana exporters. Its fate is inextricably tied to that of the EU banana regime, since without the regime in something like its current form it is not clear that the Lomé commitment could be delivered. However, the regime, and hence the Lomé commitment, has been under threat from internal as well as external sources ever since its introduction. Much of this was predictable. It was clear that the Single European Market would require a single banana trade policy, and given the limited competitiveness of ACP supplies it was clear that a regime similar to that actually introduced would be necessary to meet the Lomé commitment. Such a policy would inevitably provoke a challenge by dollar exporters, and would be unpopular with Germany. It is therefore, surprising that the EU and ACP exporters should have been so apparently unprepared for the WTO case, and its likely outcome.

Given the hostile environment, it is inconceivable that trade preferences for ACP banana exporters might be enhanced. The best scenario from an ACP exporter point of view would be maintenance of the *status quo*. The alternative would presumably be some kind of preferential tariff arrangement, perhaps as part of free trade areas. The worst scenario would obviously be the removal of the current regime with little time to adjust. Unfortunately, the ACP exporters will have little influence on the continuation or otherwise of the preferential trade arrangements for bananas. That is largely in the hands of the WTO.

Obviously, the final outcome of the WTO case is crucial. Previous GATT rulings have already been against the regime. In January 1994, a GATT panel established at the request of Colombia, Costa Rica, Guatemala, Nicaragua and Venezuela found that the EU policy violated GATT. The operation of the b-licence system was regarded as against mfn provisions and it was also judged that preferences for ACP bananas could not be justified. The 'Framework Agreement of March 1994 meant that four of the five complainants dropped the case, and the EU was able to block Guatemalas efforts to have the report adopted by the GATT Council. In December 1994, the EU obtained a GATT waiver until 29th February 2000, allowing certain preferential treatment required to meet the Lomé commitment. The EU takes a wider view of the application of the waiver to include the banana protocol while the US argues that its applicability is limited to a waiving of the tariff preferences provisions of Article 1.1. The b-licences are particularly problematic. If the ruling against the particular mechanisms of the policy is eventually confirmed, then this does cast doubt on the ability of the EU to deliver the Lomé commitment.

The WTO challenge began in September 1995 when Guatemala, Honduras, Mexico and the US requested consultations on the regime. This request was based on the view that the regime was inconsistent with Articles I, II, III, X and XIII of GATT 1994, Articles I and III of the Import Licensing Agreement and Articles II, XVI and XVII of GATS. The consultation period ended in November 1995. In February 1996, the same countries plus Ecuador again requested consultations on legal grounds which now included the Agriculture Agreement and the TRIMS Agreement as well as those cited previously. The complainants requested a panel at the Disputes Settlement Body in April 1996 but the EU objected. However, a panel was established following a further request in May.

The WTO complaint argued that the mfn provisions of GATT Article 1 were violated in that the EU regime discriminated against Latin American exporters by higher tariff rates than were chargeable on non-traditional CAP exports. The allocation of country specific quotas to traditional ACP, non-traditional ACP and BFA exporters but not to other exporters was regarded as a violation of Article XIII on 'Non-discriminatory administration of quantitative restrictions. It was further argued that the resulting allocations do not reflect the situation which would have ruled in the case of a free market: allocations to Ecuador and certain other Latin American exporters outside the BFA were regarded as unjustifiably small. The licensing system was the object of particular concern and criticism. This was seen as discriminating against Latin American bananas in being unnecessarily administratively burdensome contrary to GATT Articles I and X and the Licensing Agreement. The b-licenses transferring quota rents and market share to

EU distribution firms were seen as discriminating against US firms in violation of the provisions of GATS.

The Interim Report of the Panel appeared later than expected in April 1997. While the general principle of preferential treatment, in the form of zero tariff rates, for traditional ACP exporters was not an issue, the mechanisms by which the preferences are delivered have been found to be inconsistent on sixteen counts with the EUs obligations in GATT and elsewhere. The country specific tariff quota allocations other than those for traditional ACP exporters have been found inconsistent with GATT Article XIII notwithstanding the fact that these were written into the Agreement on Agriculture. As expected, the b-licenses and activity function rules have been particularly criticised as inconsistent with GATT Articles I, III and X, the Licensing Agreement, and GATS Articles II and XVII. The panel decided that the licensing system discriminated in favour of traditional ACP exporters and that the EUs obligations were not waived by the Lomé waiver as far as these aspects of the regime were concerned.

The US claimed after the judgement that it wanted a solution which would allow WTO-consistent trade preferences for the Caribbean exporters, but did not make clear what form such preferences might take. President Clinton has suggested enhancement of the Caribbean Basin Initiative, but the value of this to the Caribbean states is regarded as limited.

The EU has exercised its right of appeal to the WTOs Appellate Body. Appeal proceedings should be completed within a maximum of 90 days. However, appeals are limited to 'issues of law covered in panel reports and legal interpretations developed by the panel.

The WTO case is not the only legal challenge to the EU banana regime. Challenges have been brought in the European Court of Justice by Chiquita Banana Company in 1993, the German Government (supported by the Netherlands and Belgian Governments) in the same year, and by the German Government on three occasions in 1995. All these challenges failed, but this does not imply the end of opposition to the regime within the EU. Outside the EU, the US opened an investigation of the EU regime in 1995 under the unfair trade practices provisions of Article 301 - the so-called '301 Action.

8.6 The Future for ACP Banana Trade

The detailed effects of a loss of the current EU regime would obviously depend upon the regime introduced to replace it. However, there is little doubt that in any changes to the *status quo*, ACP exporters would lose out to dollar exporters, and that Caribbean exporters would suffer most. For traditional ACP banana exporters, therefore, the preferred option must be continuation of the current EU banana trade regime to maintain the Lomé commitment. However, there is little that the ACP states can do to secure this option beyond working to ensure that the strongest possible response to the WTO Panels Report is made, both within WTO and outside.

While continuation of the *status quo* might be the best scenario from an ACP exporter point of view, the probability of this option materialising is uncertain, especially against the background of multilateral trade liberalisation, and an apparent desire by the EU to strengthen links with Latin America. In any case, the current arrangements are less than perfect. The protocol and the EU regime only concern *traditional* ACP exporters, and the Caribbean exporters at least are relatively wealthy. Non-traditional exporters, such as the Dominican Republic, have enjoyed little benefit. Traditional exporters have benefited from the protocol in the form of market access, although their position has become less favourable since the introduction of the EU common banana regime, and they have typically been unable to achieve their full quotas. The existence of the protocol arguably has militated against serious efforts at raising

competitiveness and diversification. There may be some argument for quotas to be reallocatable to those best able to fill them. How the benefits of preferential trade have been divided between growers and importers is beyond the scope of this chapter, but the case for trade preferences may also be weakened if it is not clear who benefits. Windward Island growers have recently received less than 10% of the UK retail price. The question of quota rents has been discussed in Chapter 7.

If the Interim Report findings are upheld then the question is raised whether the preferential treatment to ACP exporters can be delivered without the specific mechanisms - the licensing arrangements and country specific allocations - of the current regime. Clearly this needs to be considered, but it is not apparent how ACP exporters could compete without the subsidy element offered by the b-licenses. Whether this could be delivered in some other way which is compatible with the WTO needs to be addressed. Quotas alone would not necessarily guarantee a market for ACP fruit, and prices would not necessarily be such as to allow profitable exports up to quota levels.

If the current regime is overthrown, one possible replacement would be some form of tariff system. The income of the traditional banana exporters is such that they would be excluded from non-reciprocal arrangements, although if the banana trade is lost this might no longer be the case. There may be a case for arguing for a different basis for permitting non-reciprocal preferential trade arrangements - dependency or vulnerability, for example.

Tariff preferences alone, at least at realistic rates, would not be sufficient to offset the competitive advantage of the dollar exporters. The tariff preference would have to be enough not only to offset the differences in costs of production, but also to offset the premium which dollar bananas appear to earn on EU markets. This has been estimated at around 20% (Raboy *et al*, 1995). Again, it is clear given the hierarchy of production costs, that Caribbean exporters would require the greatest tariff preferences to survive, while West African exporters might be competitive with significantly lower preferences. Whether a sufficiently large tariff preference could be engineered would depend upon the tariff equivalent of the current regime. However, it seems likely that the tariff equivalent would be too high to be politically acceptable.

If the extent of tariff preferences was insufficient to ensure that ACP exporters could find a market for their bananas, then some kind of subsidy might be used to bridge the gap. Such schemes have been favoured by a number of authors (see, for example: Read, 1994; Raboy *et al* 1995). In this scheme tariff revenues could be transferred, for example, as subsidies to ACP exporters. There is some precedent for such transfers, since compensation for income losses due to the EU policy was included in Regulation 2686/94. However, it is unlikely that such a scheme would be acceptable to the WTO, and it may maintain uneconomic and unviable production. A further problem with this approach is that where ACP and dollar supplies are available at similar prices, it is likely that dollar bananas would be preferred by many European consumers, and ACP exporters would find it difficult to maintain market share against the multinational importers of dollar bananas. Prior to the introduction of the EU policy, for example, ACP bananas could enter Belgium and the Netherlands duty free, while dollar bananas faced a 20% tariff, but even so dollar bananas took all the market. The trade preferences accorded to ACP exporters might therefore have little practical benefit. The issue of the competitiveness of ACP bananas arises again. Whatever the trade policy in operation, it is vital that ACP competitiveness is raised. Any transfers to ACP exporters therefore should be tied to quality improvement.

The creation of free trade areas with the EU with the attendant possibility of non-reciprocal trade preferences has been discussed in the Commissions Green Paper and elsewhere in this report. For Caribbean countries the analysis here indicates quite minor import increases and little overlap with EU

products. The creation of such a free trade area might include the adoption of the EU banana policy for its domestic producers, putting ACP exporters in the same position as Martinique and Guadeloupe. However, such a policy would be expensive for ACP countries to operate unless some acceptable means of providing EU funds to subsidise it could be found. There would also be no guarantee that bananas produced with the support of the policy would find a market for the same reasons as outlined above.

If the appeal is unsuccessful, the WTO judgement comes into force. At least until recently it appears that the EU had not made contingency plans for this possibility. In the short-term the ACP states might wish to press the EU for proposals in this regard, and specifically how the preferences can continue to be delivered if the current mechanisms are unlawful. Whatever the outcome of the WTO case there will continue to be a question mark over the EU policy.

Whatever the future of trade arrangements for ACP bananas, the issue of competitiveness must be addressed. Obviously this applies *a fortiori* in the case of reduced trade preferences, but Windward Island bananas have lost market share recently even in the UK, their last remaining market, and in spite of the operation of the EU regime. Even if the status quo was maintained therefore competitiveness must be improved. The ACP exporters need to press for further assistance in raising competitiveness and diversification, and the trade development provisions of Lomé need to be stressed. Efforts in this direction in the past have been disappointing, not least because of the high returns guaranteed by the Lomé protocol. The introduction of the EU policy exposed ACP exporters to a greater degree of competition from dollar suppliers, and the loss of the regime would remove the safety net further. Competitiveness will best be achieved if the incentives for higher quality are available down through the banana production and distribution system. Quality control systems are open to abuse, and these too might best be implemented earlier in the production and marketing chain, perhaps through inspection and approval of producers. If a tariff system replaces the current regime, then the ACP exporters need to explore the scope for alternative forms of subsidy compatible with WTO. Again, if these are to be of lasting benefit they should be tied to quality improvement.

The urgent need for quality improvement will inevitably mean a contraction in the size of the industry in the Windward Islands. This then raises the question as to whether the volumes of high quality fruit which could be produced would be sufficient to justify a regular shipping schedule. It is vital that any contraction in the industry should take place in a managed way rather than catastrophically and the ACP exporters need to argue for adjustment aid.

Smaller volumes of ACP bananas especially from the Windwards might be marketed in different ways to exploit their particular characteristics such as their 'greener' or more 'organic' or 'integrated production system. As such they might find profitable niche markets throughout Europe, but again quality is essential. The potential size of such markets should be investigated. There may be some scope for market diversification. Central and Eastern European countries, and the countries of the former Soviet Union offer rapidly growing markets for bananas. However, dollar supplies are already established on these markets. Markets in other developing countries are limited since all tropical countries have their own production. Product diversification out of banana production is necessary, but as noted earlier, the options are limited. Export markets for alternative horticultural crops would be problematic for many of the same reasons that exports of bananas are problematic, notably competitiveness. Tourism development offers some potential, but so far has arguably contributed little, given the high import content of the all-in package tourism. The scope for increasing the sales of local agriculture into tourism needs to be raised by enhancing the quality and service element of local food supplies and encouraging the hotel trade to buy local. However, tourism markets for agricultural products cannot support the scale of agriculture associated with banana production. Furthermore, diversification can take years. ACP banana exporters may have months.

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