

## **Will the banana trade war ever end?<sup>1</sup>**

**Hervé Guyomard, Chantal Le Mouël, Fabrice Levert, INRA and CEPII, F**

**Jahir Lombana, University of Göttingen, G**

**November 2004**

One key policy issue facing the world banana market is the choice by the European Union (EU) of the tariff on imports of “dollar” fruits from Latin America (LA) which would take effect 1 January 2006. In theory, what should change at that date is the EU import regime, not the level of support and protection offered to European producers and African, Caribbean and Pacific (ACP) countries.<sup>2</sup>

### **1. The EU banana import regime in a nutshell**

Numerous complaints to the World Trade Organisation (WTO) have necessitated successive reforms of the EU banana trade regime since the establishment of the Common Market Organisation for Bananas (CMOB) in 1993.

Before that date, European countries pursued their own trade regimes. The Single European Market of 1992 provided the impetus to eliminate internal EU border restrictions since it would be no longer possible to enforce Article 115 of the Treaty of Rome to prevent intra-community trade. From 1993 to 1998, the trade regime consisted of two tariff-rate quotas. The ACP quota allowed the twelve traditional ACP producer countries to enter the EU market duty free up to a maximum cumulated volume of 857,700 tonnes per year.<sup>3</sup> During this first period, there were country-specific allocations of the ACP quota. The annual quota for dollar and non-traditional ACP countries was initially set at 2 million tonnes with an in-quota duty of 100 euros per tonne. It was progressively raised up to 2,553 million tonnes from 1995 (following EU enlargement) with a reduced in-quota duty of 75 euros per

---

<sup>1</sup> Paper initially prepared for presentation at the FAO informal expert consultation on banana trade policy, 28-29 October 2004, FAO, Roma.

<sup>2</sup> Within the EU, the banana-producing territories are Guadeloupe and Martinique (France), the Canary Islands (Spain), Madeira and Algarve (Portugal), Crete and Lakonia (Greece).

<sup>3</sup> The twelve traditional ACP countries are Belize, Cameroon, Cape Verde, Dominica, Grenada, Ivory Coast, Jamaica, Madagascar, Somalia, St Lucia, St Vincent and the Grenadines, and Suriname. The non-traditional ACP countries comprise the rest.

tonne. Following the so-called Framework Agreement of 1994, there were also country-specific allocations of the dollar quota to four LA countries (23.4 % for Costa Rica, 21.0 % for Colombia, 3 % for Nicaragua and 2 % for Venezuela).

The 1998 reform of the CMOB that came into force on 1 January 1999 considerably simplified the import and export licensing system, allocated nearly 90 % of the dollar quota to the four main LA exporters (Ecuador, Costa Rica, Colombia and Panama) and suppressed the country-specific allocations of the ACP quota. Each traditional ACP country could export as much as it wanted up to a cumulated annual volume of 857,700 tonnes for the twelve traditional ACP suppliers.

Despite these changes, the regime remained under heavy scrutiny. A new WTO panel initiated in January 1999 concluded that the modified EU policy was still not fully compatible with WTO rules. After two unsuccessful proposals, on 10 November 1999 and 4 October 2000, the EU finally adopted a regulation on 2 May 2001 to implement a new banana import regime in line with understandings arrived with both the United States and Ecuador. The mutually agreed solution is a two-step process towards a tariff-only regime that should enter into force no later than 1 January 2006. During the transitional period 2001-2005, bananas continue to be imported into the EU under a two tariff-rate quota system through import licences distributed on the basis of past trade. The transitional regime also includes a transfer, from 1 January 2002, of 100,000 tonnes from the quota reserved to ACP suppliers to the non-reserved quota.

## **2. Impacts of the various forms of the CMOB on banana exports to the EU**

Since the establishment of the first CMOB in 1993, EU producing regions have benefited from income support under the form of coupled direct aids. This income support policy has resulted in a positive growth rate of exports from EU territories, 2.38 % over the period 1993-2003. EU territory supply represented 18.24 % of EU consumption in 1990-1992. It now represents 18.85 % of this consumption (average 2002-2003). EU imports from ACP countries represented 16.13 % of EU consumption in 1990-1992. This share increased to 18.81 % during the period 1993-1998 where there were country-specific allocations of the ACP quota. It decreased to 18.03 % in 1999-2001 where there were no longer country-specific allocations of the ACP quota. It now represents 18.46 % of EU consumption (average 2002-2003). After an important decrease during the first years of application of the CMOB, EU imports from dollar zone countries stabilised and then have increased. Over the whole period 1993-2003, the growth rate of dollar zone exports to the EU is slightly positive (0.34 %). Their share in EU consumption however has continuously decreased with a much more pronounced decline during the first version of the CMOB (from 65.63 % in 1990-1992 to 63.34 % in 1993-1998, 62.95 % in 1999-2001 and 62.69 % in 2002-2003). Figure 1 summarises these evolutions.

(Insert Figure 1)

Over the period 1993-2001, EU imports from traditional ACP countries always remained below the ACP quota limit of 857,700 tonnes. But while exports from Caribbean countries have decreased, exports from West African countries (Cameroon and Ivory Coast) have increased. Figures 2 and 3 also show that the various versions of the CMOB have had differentiated impacts on Caribbean and West African country exports. More specifically, the decline of Caribbean country exports appears much more pronounced after the cancellation of country-specific allocations of the ACP quota in 1999. Inversely, exports from West African countries have mainly increased after that date. While Caribbean country exports represented 58.54 % of total ACP exports to the EU in 1990-1992 and still 44.85 % in 1993-1998, they now only represent 24.18 %. By contrast, the share of exports from Cameroon and Ivory Coast to the EU has continuously increased, from 34.68 % in 1990-1992 to 61.68 % in 2002-2003. One non-traditional ACP country, the Dominican Republic, has substantially increased its exports to the EU. While this country represented 2.64 % of ACP exports to the EU in 1990-1992, its share is now equal to 13.66 %. For a large part, these volumes correspond to organic and/or fair trade bananas mainly exported to the United Kingdom.

(Insert Figures 2 and 3)

### **3. Estimating the tariff equivalent of the tariff-rate quota system: The price-gap method versus the simulation approach**

As agreed by the Council of European Ministers in 2001, the move to a tariff-only regime in the EU should theoretically take place no later than 1 January 2006. On 2 June 2004, the European Commission (EC) has thus proposed to the Council to open WTO negotiations and negotiate the import tariff for bananas with the relevant producer countries. In the course of the negotiations to the move to the tariff-only regime, the EC will seek to respect its WTO commitments, safeguard the interests of EU producers by providing a level of support equal to the current one and maintain a level of preference to the ACP countries equivalent to that offered currently by the enlarged EU-25 (EC, 2004).

Studies that have attempted to estimate the tariff equivalent to the current tariff-rate quota regime can be divided in two groups according to the methodology used.

Studies in the first group employ the price-gap approach as codified in the Attachment to Annex 5 of the Uruguay Round Agreement on Agriculture (URAA). The price gap is measured as the difference

between internal and external prices. The internal price is representative of the wholesale price in the domestic market. External prices should be evaluated by CIF unit values or, when these values are not available or appropriate, either by average CIF unit values in a near country or from FOB unit values in an appropriate exporter adjusted by adding an estimate of insurance, freight and other relevant costs to the importing country. Assuming that the internal price is the landed CIF price of EU imports from ACP countries and EU territories and the external price is the landed CIF price of EU imports from dollar zone countries, Borrell and Mauer (2004) find a tariff equivalent of 64 euros per tonne. Raboy (2004) defines the internal price as the CIF price in the EU of ACP-sourced bananas and proposes four alternative approaches for the external price, i.e., (i) the price in a near market (Norway), (ii) the price in the US market adjusted to convert it into an estimate of the EU price, (iii) the average price in six Central or Eastern European countries and (iv) the average CIF price in the EU. Estimated price gaps range between 50 and 75 euros per tonne. Raboy adds “portions of the simple tariff [of 75 euros per tonne] to the price gap to produce the range of plausible possibilities that measure the tariff equivalent to the total current regime”. As a result, the tariff equivalent would range between 106 (50 % of the current tariff is added) and 143 euros per tonne (100 % of the current tariff is added). NERA and OPM (2004) calculate the price gap by the difference between FOB export prices of Caribbean suppliers (the internal price) and dollar zone suppliers (the external price). Based on average prices from 1999 to 2002, they find a tariff equivalent of 259 euros per tonne.<sup>4</sup>

In the second group of studies, tariff equivalent estimates are based on partial equilibrium models of the world banana market. Tariff equivalent estimates are higher in that case, for example between 182 and 239 euros per tonne for Guyomard et al. (2003), 300 euros per tonne for the FAO (2003) and 353 euros per tonne for Kersten (2003).<sup>5</sup> In addition, Guyomard et al. illustrate the high sensitivity of the tariff equivalent to the euro / US dollar exchange rate. If the euro strengthens (respectively weakens) vis-à-vis the US dollar, then the estimated tariff equivalent increases (respectively decreases). More specifically, any decrease in the euro / US dollar parity by 10 percent increases the estimate of the tariff equivalent by about 12 euros per tonne.

Both types of methodologies suffer from drawbacks. Approaches based on simulation results require in particular reliable estimates of supply and demand functions (elasticities) while approaches based on the price-gap method require that prices used reflect accurately internal and external prices. The problem is not really the internal price as the latter is likely to reflect the essential of protection effects

---

<sup>4</sup> In principle, insurance, freight and other relevant costs should be added to transform FOB prices into CIF prices. NERA and OPM note that “transport costs from the Caribbean ACP countries to the EU are, if anything, higher than from dollar sources”. They conclude that their FOB price comparison is likely to underestimate the real price gap.

<sup>5</sup> The NERA and OPM estimate (259 euros per tonne) however is higher than the upper bound of the price interval estimated by Guyomard et al. (239 euros per tonne).

linked to existing quotas and tariffs. The problem is mainly the external price as the latter is the price that should prevail under free trade. This problem directly relates to the question of quota rents and the extent to which they are accounted for in the external price when the latter is approximated by the CIF import prices in the EU from dollar zone suppliers. The near country alternative does also pose problems. Raboy has difficulty to explain why the 2002 external price constructed from Norwegian prices is higher than the internal price. The fact that import prices in Central and Eastern countries are much lower than Norwegian prices suggests that the supply of dollar bananas is far from being perfectly competitive. Drawbacks of CIF prices lead NERA and OPM to calculate the tariff equivalent on a FOB price comparison. Even if transport costs are not accounted for in that case (see footnote 5), NERA and OPM claim that the corresponding measurement error is smaller than under any other combination of prices. They however note that “some quota rents could also be included in the prices as they are also likely to be transfer prices in many cases”.

In the remaining of the paper, we provide a new evaluation of the tariff-only regime using an updated version of the multi-country partial equilibrium model of the world banana market developed by Guyomard et al. (1999a, 1999b, 2003). This updated version considers a 2000-2002 base year and includes the ten new Member States as integral part of the EU-25. We also show that dynamic effects of the tariff-only regime on exports from Caribbean Islands, West African states and dollar zone countries are likely to be different from static impacts, whatever the level of the tariff applied on dollar fruits.

#### **4. Static and dynamic effects of the tariff-only regime: An assessment for the EU-25**

We find that a tariff of 227 euros per tonne with a tariff preference of the same amount granted to ACP bananas would be equivalent to the current situation, i.e., the situation that prevails in 2003. A lower tariff would lead to greater consumption in the EU, lower EU import prices, greater EU imports from dollar zone countries and lower EU imports from ACP countries (Figure 4).

(Insert Figure 4)

A five-year dynamic simulation incorporating time shifters in supply (productivity changes) and demand (per capita consumption trends) shows that it would be necessary to set the tariff at a higher level (about 250 euros per tonne) in order to maintain in 2008 the CIF import average price that prevails in 2003 in the EU. In other words, applying a tariff of 227 euros par tonne on dollar bananas over the five-year period 2003-2007 would lead to a decrease in the EU CIF import price (from 603 euros per tonne in 2003 to 582 euros per tonne in 2008) and to an increase in EU consumption (from 4,62 million tonnes in 2003 to 5,08 million tonnes in 2008, i.e., + 10.1 %). This consumption increase

would benefit to both the dollar zone and West African countries. With respect to 2003 levels, their exports to the EU would increase by 327,000 tonnes and 96,700 tonnes, respectively. In percentage terms, the export increase would be higher for the two West African countries (Cameroon and Ivory Coast) than for the countries of the dollar zone (+ 24.1 % versus + 9.9 %). By contrast, EU imports from Caribbean countries would decrease by about 5,700 tonnes (- 3.3 %) as compared to 2003.

Table 1 also indicates that a relatively low tariff (say 100 euros per tonne) would severely affect the banana industry in the Windward Islands and Jamaica. With respect to the situation that prevails in 2003, their exports to the EU would decline from 157,200 tonnes to less than 100,000 tonnes, i.e., a cut of 37 %. A relatively high tariff (say 300 euros per tonnes) would allow the group of ACP countries to expand their exports to the EU by 276,300 tonnes, from 642,400 tonnes in 2003 to 918,700 tonnes in 2008. This increase would essentially benefit to Cameroon and Ivory Coast in so far as exports of Caribbean countries to the EU would rise only by 18,800 tonnes.

(Insert Table 1)

## **5. Concluding comments: What future for the Caribbean banana industry?**

Nature and geography make it very difficult for the Caribbean banana producing states to compete on equal terms with LA countries (see, for example, Myers, 2004). This point is well known and explains, to a large extent, the banana trade war briefly described in the first section of this paper. But natural conditions make it also very difficult for the Caribbean states to compete with West African countries although both types of countries are included in a single group in current negotiations on the move to the tariff-only regime. If the tariff were to be set at a relatively high level, say more than 300 euros per tonnes according to our simulation results, the main beneficiaries would be Cameroon and Ivory Coast, not Caribbean countries. In that context, the question to be addressed is the future of the Caribbean banana industry, particularly if the EU is not able to resist to pressures from low-cost LA producing countries and sets the tariff at a relatively low level (100 euros par tonne or less, according to our simulation results). Different options, not exclusive, can be envisaged to assist the Caribbean banana industry. They include income support, as well as aids directed to competitiveness and/or quality improvement, product differentiation (organic and/or fair trade bananas), diversification and restructuring. Among the possibilities, a EU trade regime involving differentiated tariffs for dollar bananas on the one hand and West African bananas on the other hand, Caribbean bananas entering the EU duty free, should be carefully examined.

From a more general perspective, the specific case of the EU banana trade policy illustrates the issue of the ending of EU trade preferences. In that perspective, our analysis illustrates the need to consider

each ACP country individually and not ACP as a single group. EU trade preference schemes can be criticised on several grounds, but any reform of these schemes should take into account the fact that beneficiary countries are not homogeneous and that the reform process should be country-differentiated. It should also be gradual, i.e., spread over several years.

### **Further Reading**

Borrell, B., Bauer, M. (2004), *EU Banana Drama: Not Over Yet. New Distortions from a High Tariff-Only Policy*, Centre for International Economics (CIE), Australia, Canberra and Sydney.

European Commission (2004), *Banana Imports: Commission Proposes to Open Tariff-Only Negotiations*, IP/04/707, Reported in European Union in the US, News Releases n° 90/04, June 2, 2004 (<http://www.eurunion.org/news/press/2004/20040090.htm>).

FAO (2003), *Banana Projections to 2010*, Committee on Commodity Problems, Intergovernmental Group on Bananas and on Tropical Fruits, Third Session, Puerto de la Cruz, Spain, 11-15 December 2003.

Guyomard, H., Laroche, C., Le Mouël, C. (1999a), Impacts of the Common Market Organisation for Bananas on European Markets, International Trade and Welfare, *Journal of Policy Modeling*, 21(5), 619-631.

Guyomard, H., Laroche, C., Le Mouël, C. (1999b), An Economic Assessment of the Common Market Organisation for Bananas in the European Union. *Agricultural Economics*, 20, 105-120.

Guyomard, H., Le Mouël, C. (2003), *The New Banana Import Regime in the European Union: A Quantitative Assessment*, The Estey Centre Journal of International Law and Trade Policy, 4(2), 143-161.

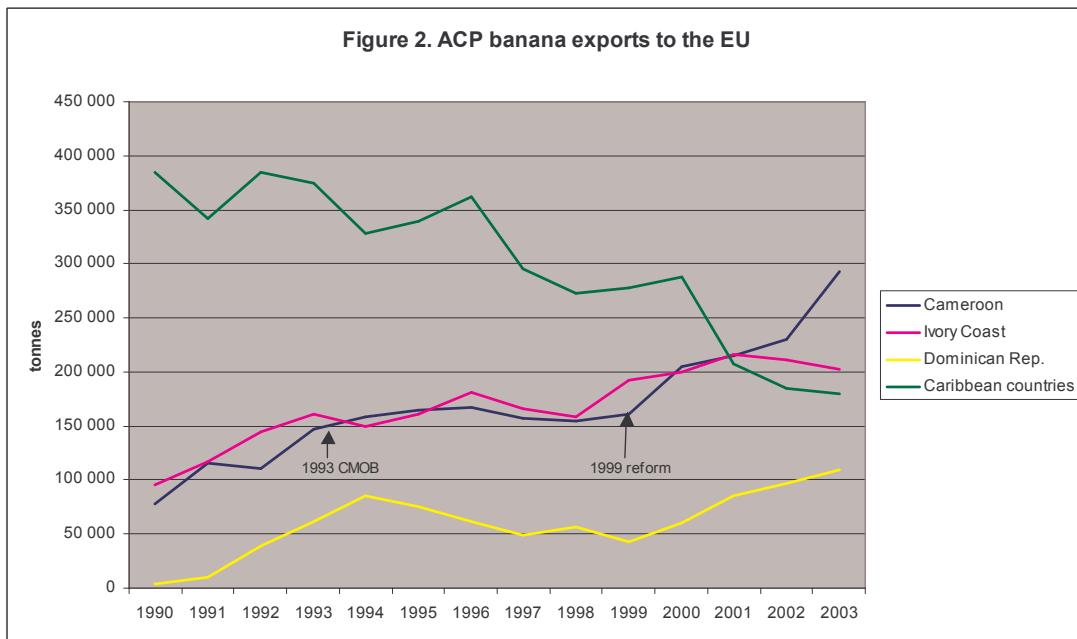
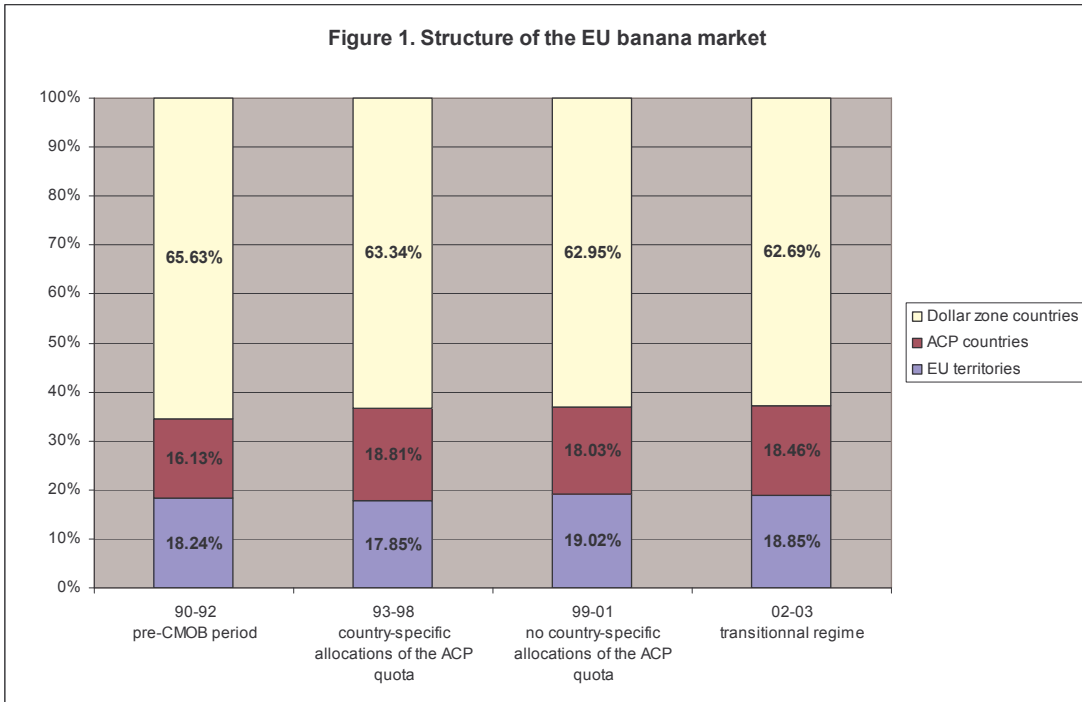
Kersten, L. (2003), Zur Revision der EU Bananenmarktordnung, <http://www.ma.fal.de/dokumente/kerstenpersonbanane1.pdf>.

Myers, G. (2004), *Banana Wars: The Price of Free Trade*, Zed Books, London.

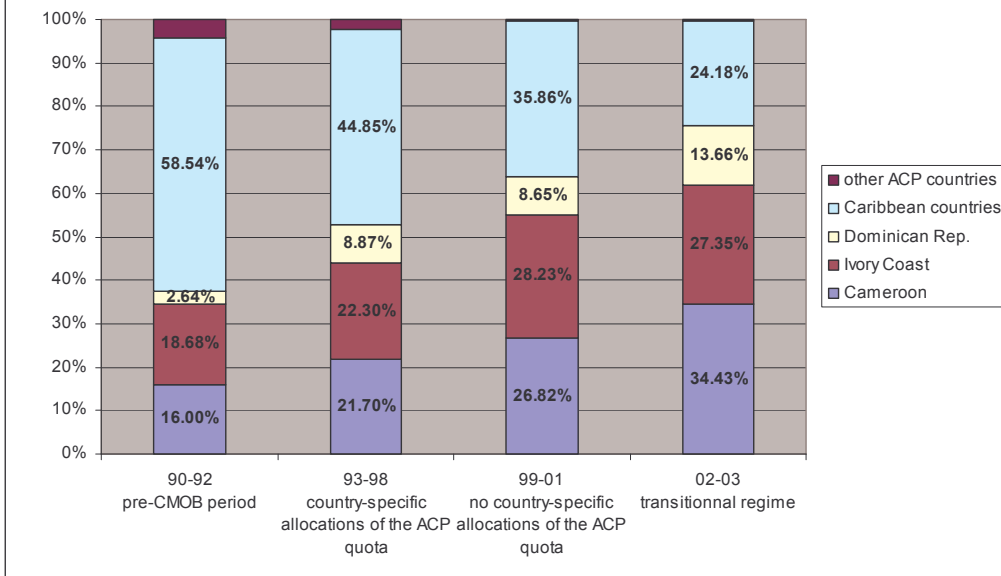
NERA and OPM (2004), *Addressing the Impact of Preference Erosion in Bananas on Caribbean Countries*, Report to DFID, NERA and OPM, London, August 2004.

Raboy, D. (2004), *Calculating the Tariff Equivalent to the EU Banana Regime*, Unpublished Document.

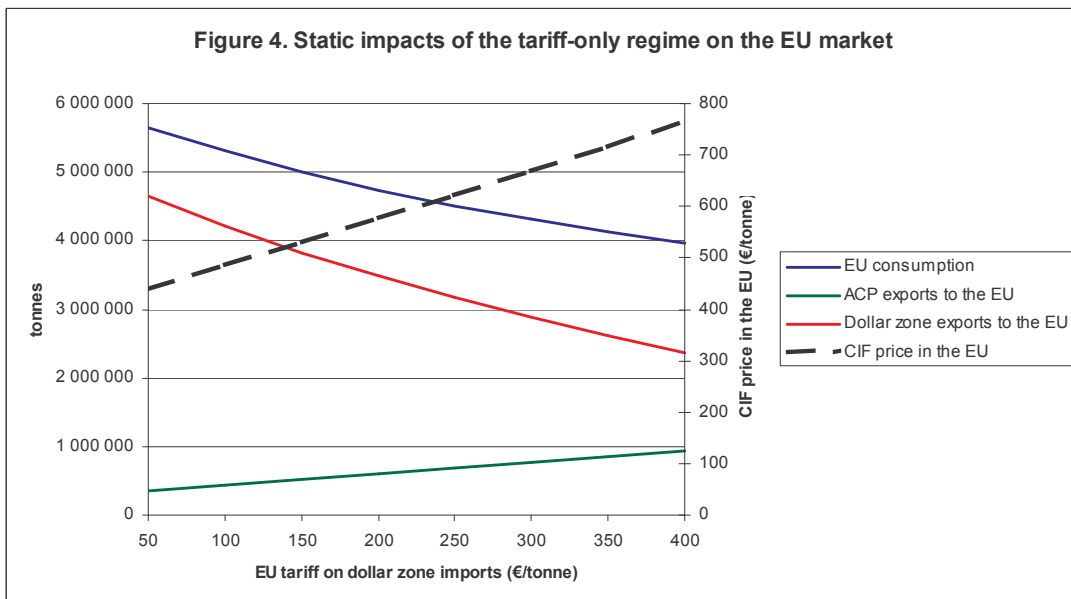




**Figure 3. Shares of the different ACP countries in total ACP banana exports to the EU**



**Figure 4. Static impacts of the tariff-only regime on the EU market**



**Table 1. Impacts of the tariff-only regime on the EU banana import structure: Comparison of static and dynamic effects (tariffs and prices in euros per tonne; quantities in tonnes)**

Tariff level	Static simulation			Dynamic simulation		
	100	227	300	100	227	300
CIF average price in the EU	486	603	671	464	582	650
EU consumption	5,305,205	4,615,272	4,311,845	5,871,496	5,079,894	4,735,654
EU imports from the dollar zone	4,214,074	3,310,010	2,881,938	4,725,287	3,636,976	3,116,575
EU imports from ACP countries, including:	428,236	642,367	767,013	445,834	742,542	918,704
- Cameroon	125,257	205,238	251,795	136,410	249,042	319,916
- Ivory Coast	124,025	195,144	237,018	142,394	248,019	314,432
- Caribbean countries	115,474	157,173	180,865	99,094	151,981	175,985

Note: The dynamic simulation corresponds to a five-year 2003-2008 projection of the tariff-only regime incorporating time shifters in supply (export) and demand (import) functions. The static simulation analyses the “instantaneous” impact, i.e., in 2003, of the tariff-only regime.

Will the banana trade war ever end?

Hervé Guyomard, Chantal Le Mouël, Fabrice Levert, INRA and CEPII, F

Jahir Lombana, University of Göttingen, G

### Summary

The current banana import regime in the European Union is a two-step process towards a tariff-only regime that should enter into force 1 January 2006. What should change at that date is the import regime, not the level of support and protection offered to European producers and African, Caribbean and Pacific countries. Two approaches can be used to calculate the tariff equivalent to the current tariff-rate quota system, the price-gap method and the simulation method. Both suffer from drawbacks which are discussed. A new evaluation of the tariff-only regime for the EU-25 is provided based on a multi-country partial equilibrium model of the world banana market using years 2000 to 2002 as base years. The static tariff equivalent which would maintain the EU import price at its base period level should be set at around 227 euros per tonne. A higher tariff should be applied (around 250 euros per tonne) in order to maintain this price level over the five-year period 2003-2008.

Hervé Guyomard (Director of research),

Chantal Le Mouël (Director of research)

Fabrice Levert (Assistant)

INRA, Department of social sciences

4 allée Adolphe Bobierre, CS 61103

35011 Rennes cedex

France

[Hervé.Guyomard@roazhon.inra.fr](mailto:Hervé.Guyomard@roazhon.inra.fr) (33 2 23 48 53 87)

[Chantal.LeMouël@roazhon.inra.fr](mailto:Chantal.LeMouël@roazhon.inra.fr) (33 2 23 48 53 86)

[Fabrice.Lever@roazhon.inra.fr](mailto:Fabrice.Lever@roazhon.inra.fr)

Jahir Enrique Lombana Coy (Ph.D. student)

Universität Göttingen

Oeconomicum, Ibero-Amerika Institut

Raum II-35

Platz der Göttinger Sieben 3

37073 Göttingen

Germany

[jahirl@terra.com.co](mailto:jahirl@terra.com.co)

