

Banana policy: a European perspective[†]

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European Union banana policies do not make economic sense, and hence criticism of these policies is justified. Some facts should, though, be remembered. If the EU had chosen free trade in bananas when the Single Market was established, certain producers both inside and outside the EU would have lost income, and it proved politically impossible to choose direct financial compensation. Also, the quantitative implications of the new EU banana regime may be less than sometimes assumed, as trade has not been reduced very much. The WTO's role is not to judge the economic merits of these policies, but their legal justification.

1. Comment on Brent Borrell's article 'Policy-making in the EU'

Brent Borrell has engaged one more time in his well-known criticism of EU banana policies, and has done so very forcefully in this article. To comment on this article, as I have been asked to do, is not easy, for several reasons. First, Borrell is obviously right in the basic thrust of his criticism. EU banana policies do not make economic sense. For an economist with a liberal mind, it is simply impossible to defend those policies. Second, the type of quantitative analysis Borrell has presented over the years is fundamentally appropriate. One may disagree with some of the assumptions, parameters and statistics he uses, however, this does not undermine the overall message conveyed by Borrell's analysis. Third, the policy alternatives suggested by Borrell are definitely superior to current EU banana policies. From an economic perspective, free trade in bananas and the provision of direct and uncoupled support to EU and ACP banana producers are without any doubt preferable. Finally, as a German, a citizen of the EU country most negatively affected by, and most critical of, EU banana policies, I feel even less inclined to disagree with Borrell's conclusions. Moreover, for more than two decades in my professional life as an analyst of agricultural policies I have argued for trade liberalisation and uncoupled support. Indeed, on many occasions I

[†]I am grateful to Patrick Verissimo for his support in preparing this article.

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have strongly argued against quantitative trade restrictions, tariff quotas, licensing arrangements and market sharing agreements in agricultural trade. Why should I then contradict Borrell's point of view?

In this comment I shall, therefore, not defend EU banana policies. I shall, rather, make three points which may help to broaden the perspective. First, there was a political reason why the EU adopted its current policy. Second, the negative implications of this policy may be somewhat less pronounced than suggested by Borrell. Third, the role of the WTO in this story may be somewhat different from what Borrell appears to suggest.

2. Political reasons for EU current policy

Borrell rightly describes the origins of the current regime, starting with the different trade policies on bananas which the individual EU member states had before 1993. Clearly, these disparate policies could not be continued when the Single Market was established and required the abolition of border controls among EU member states. Of course, one option at the time would have been to adopt Germany's free trade regime for the whole of the EU. The large economic losses which then would have occurred for EU and ACP banana producers could have been compensated through direct payments, which ideally would have been made in an uncoupled fashion, very much like Borrell suggests. Two major political reasons argued against that option, and continue to argue against such a regime as an alternative to current policies. First, the EU budget is tight, and it is not easy to make the sums required available. Second, the producers concerned, in particular the ACP countries, did not want to be seen receiving these openly visible transfers. At the same time, the ACP countries concerned, and the respective banana-producing territories of the EU, feared that the consequent adjustments in their production structure, away from bananas, might be too socially disruptive.

In essence, these are the same arguments which farmers and agricultural policy-makers have always raised against proposals that agricultural price support should be replaced by uncoupled payments. We economists know these arguments, and we have counter-argued all the time. In domestic agricultural policies we have actually made some progress, and agricultural policy-makers around the world have now begun to embark on policies which go in this direction. Even farmers have begun to understand that such policies may not be altogether bad for them. However, EU and ACP banana producers have not yet moved to that point, and fail to be convinced that direct support might be better for them. They have strongly lobbied for price-related policies, and in those EU member states which feel politically responsible to these producers their arguments have won the day.

In this context it may be useful to remember the process through which the new banana regime was established in the EU. The first draft of the new regime was designed in the second half of 1992, when the United Kingdom had the presidency of the EU Council of Ministers. In the UK, political interests of the former Caribbean colonies and Latin American ACP countries joined forces with commercial interests of the three UK-based companies which benefited from the old licensing regime. In what is still seen by some British commentators as a black moment in the history of UK trade policies, these forces won the day. France, with similar interests, strongly backed the initial draft. Other EU member states were strongly opposed to the draft, but did not command a blocking minority. When, in the first half of 1993, the new regime was finally adopted under a Danish presidency, the blocking minority against it was missed by only one vote. Denmark, traditionally with a quota-free market, could have joined the opposition and then the new regime would not have been adopted. As the country holding the presidency, however, Denmark felt it needed to show 'European responsibility'. Also, Denmark was under heavy pressure from France and the UK, in relation to completely different political issues. In other words, the EU was not too far away from a better solution, but historical coincidences got in the way.

Borrell says, rightly, that EU banana policies are a test for policy transparency, and for the credibility of EU policies in general. One hopes that, one day, the EU will pass that test better than it has done so far. There is, however, also the issue of credibility *vis-à-vis* banana producers in EU territories and in ACP countries. From their subjective point of view, credibility of the EU required some form of maintenance of the previous status quo, through policies which did not diverge too much from the past. As time goes on, EU policy-makers may be able (if they are willing) to persuade those producers that there are alternative forms of maintaining credibility, with less economic waste involved. Yet, it appears that this stage has not yet been reached.

3. Less pronounced negative implications

In assessing the quantitative implications of the new EU regime, Borrell occasionally takes the situation in 1992 as a point of reference, for example when he says that availability to consumers declined by 11.5 per cent between 1992 and 1994. Comparison with the situation in 1992, though, may be somewhat misleading. In anticipation of the new regime to come, banana exporters from the dollar zone and respective trading companies began to increase shipments to the EU significantly in the years immediately preceding the policy change. As can be seen from figure 1,

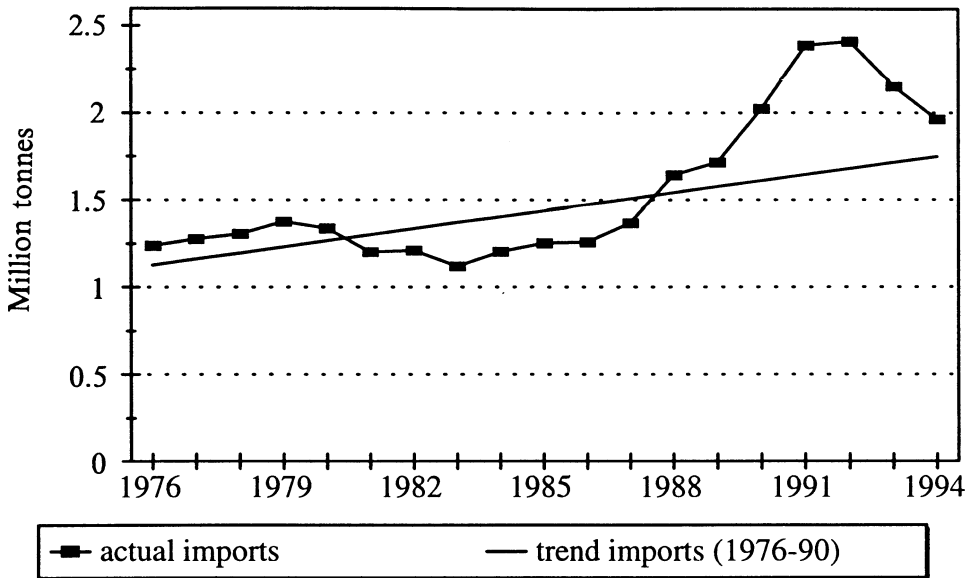


Figure 1 EU-12 imports of dollar bananas

Sources: EUROSTAT, EEC External Trade, CD ROM version, various issues and author's calculations

actual EU-12 imports of dollar bananas in 1992 and 1993 reached unprecedented high levels, before they were forced down again as a result of the new quota regime. If one extrapolates the trend of imports from 1976 to 1990 to the more recent years (also shown in the graph), it turns out that even the restricted imports in 1994 were above the longer-run trend. Of course, this is not to say that the new tariff quota regime does not effectively restrict imports. One also has to consider that 'accession' of East Germany to the EU in 1990 has increased the 'natural' volume of demand for bananas in the EU. Borrell's comparison with the particularly high levels of imports in 1992, however, provides a slightly misleading impression.

Another reason why effects of the new regime for exporters of dollar bananas are not quite as severe as it may appear at first glance is the fact that some modifications were made in 1994. The within-quota tariff was reduced by 25 per cent and the volume of the tariff quota was somewhat increased. Also, under the Framework Agreement negotiated during the Uruguay Round between the EU and four Latin American exporting countries, and in force since 1995, the exporting countries involved can

now issue export licences for 70 per cent of their country-specific quotas, thereby reaping part of the quota rent which otherwise would accrue to importing companies in the EU.

4. The role of the WTO

When considering the GATT/WTO disputes over EU banana policies one must avoid the impression that they deal with the economics of the case. The GATT is a purely legal affair, whether one likes it or not. The GATT has never prevented a country from wasting its economic resources. The purpose of GATT/WTO disputes is to make sure that countries stick to their legal obligations and commitments. Whether this is done in a least-cost manner is a moot issue in the GATT.

In its 1993 report, which still addressed the old regime, the first GATT Panel on EU banana policies mainly dealt with the national quantitative import restrictions maintained, under that regime, by some EU countries, and with the preferential treatment accorded to ACP countries. It found that the quantitative import restrictions were inconsistent with GATT Article XI:1 (elimination of quantitative restrictions), and were not justified by other GATT rules. Particularly important, because the whole policy of EU preferences for ACP countries was potentially affected, the Panel also found that EU preferences for ACP banana exporters violated Article I (most-favoured nation treatment). On this latter point, though, the Panel suggested that the EU might seek a GATT waiver which might allow it to provide such preferential treatment.

The second GATT Panel dealt with the new regime established in 1993. It had to consider a large number of complicated legal issues. It is important to note that, in its conclusions, the Panel did not find that the whole of the new EU banana regime was against GATT law, though some of its elements were found to be inconsistent with specific GATT obligations and commitments (as they stood before the conclusion of the Uruguay Round). In particular, the substitution of specific duties for the 20 per cent *ad valorem* tariffs which the EU had bound in its Schedule was found to be inconsistent with Article II (Schedules of concessions). The Panel also found that the particular scheme for allocating licences to trading companies used by the EU was inconsistent with both Article I, as it tends to discriminate between different countries of origin, and Article III (national treatment), as it discriminates against imported bananas in favour of domestically produced EU bananas. Finally, this Panel again found that preferential treatment of banana imports from ACP countries was inconsistent with Article I (as the EU had still not been granted a waiver by the contracting parties at the time).

Had the EU accepted these Panel findings, this would not have required it to do away completely with its new banana regime. It would have had to change some of its elements, and it would have had to seek a GATT waiver for continuing its preferential treatment (as it did, successfully, towards the end of 1994). However, it would be wrong to suggest that these findings would have forced the EU to adopt a fundamentally different regime. In particular, the policy alternative favoured by Borrell (and by myself) would not have been imposed upon the EU by the GATT.

At the time of writing, the third Panel on the EU banana regime has not yet come to a conclusion. It will be extremely interesting to see how it argues. Under the new WTO rules the EU will no longer be able to block adoption of the Panel report, as it did in the first two cases. However, this time the Panel will again judge exclusively on the basis of legal considerations, and not deal directly with the economic implications of the case. Contrary to Borrell's view, this WTO case will, therefore, not be 'a big test of . . . the capacity of the WTO to be drawn by analysis of the public interest' (at least not to the extent that this interest is defined in economic terms). Raising public awareness of the inefficiencies resulting from so many government policies will remain the job we economists have to do. Brent Borrell has made an important contribution to this process, and by the comments I have made here I do not wish to reduce the value of that contribution.