THE EMERGENCE OF THE WORLD TRADE ORGANIZATION (WTO): IMPLICATIONS FOR CARIBBEAN TRADE - THE CASE OF BANANAS

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SECTION 1: INTRODUCTION

The conclusion of the Uruguay round of negotiations on reforms to the General Agreement on Trade and Tariffs (GATT) has stimulated much discussion, analysis and interest with regard to the expected impact of changes. While analysts differ on the impact of this agreement, contending that some countries will win and others will lose, this line of thought is not supported by international trade theory which supports the thesis that countries can overcome limitations of size of the market through trade.

International trade theory, beginning with the Ricardian theory [Ricardo, 1948] of comparative advantage and including recent trade theories advanced as part of the "new growth theory" paradigm, has expounded the virtues of trade liberalization en route to free trade. Some might argue that a country can be made worse by trade liberalization, but this thesis is often centered on using the theory of individual firm's analysis arguments that in trade, "one firm's gain is another firm's loss."

For countries, trade is not a zero sum game. It is for this reason that the removal of barriers to trade (trade liberalization) is regarded by most trade theorists to be a desired principle in world trade. Free trade or the removal of all trade barriers is seen as necessary to create the optimal environment in which goods and services may be exchanged between and within countries for the benefit of all.

Other benefits claimed by free traders include increased competition which forces firms to cut waste, keep prices down and raise quality.

New trade theory argues for benefits such as
(1) the augmentation of human and physical capital resources;
(2) the sharing and transfer of technology; and
(3) increase in learning by doing opportunities.

While theoretical argument on the virtues of free trade is almost unanimous, there are those who suggest that trade among developed countries, at least in part, is due to reasons quite different from comparative advantage. Bela Balassa (1962), Herbert Grubel and Peter Lloyd (1975) among others have suggested that the rapid expansion of trade among developing countries has not taken the form of increased specialization, as comparative advantage would lead one to expect but rather, of a simultaneous increase of the exports by all countries. These arguments for free and open trade (the cornerstone of the GATT) also emanate from the theory of comparative advantage which argues that successful multilateral trade liberalization resulting in goods being provided at their lowest relative cost will enhance the returns to all countries. Developing countries, however, have in the past been concerned that the theoretical benefits of trade liberalization are often not translated into real gains from trade which has led to some skepticism about the Uruguay Round and its potential benefits for developing countries.

As such, this paper addresses the likely impact of the World Trade Organization (WTO) on the future of Caribbean trade. More specifically, it addresses concerns generated by members of the Caribbean Community and Common Market (CARICOM) trading partners in respect to recent rulings by the WTO regarding the export of bananas to the European Union. The paper further considers options open to the Caribbean countries as they seek to adjust their economies in the face of the changing realities.

Methodology

The paper analyzes the impact of the rulings by the WTO with respect to the export of bananas from the CARICOM. For these CARICOM countries trade figures are compared and analyzed. The study comprises three sections. In addition to Section I entitled Introduction, Section 2 provides a general discussion and brief history of GATT and identifies the general provisions of the Uruguay Round. This section also presents a demographic description of the CARICOM region and a profile of the region's trade pattern as it relates to its most important trading partners. A graphical model is offered in the third section to explain the pending changes. A description of the Rely effects follows with recommendations as to possible responses.

SECTION II: THE URUGUAY ROUND - THE GATT

Main Provisions of the Uruguay Round

The conclusion of the Uruguay Round (UR) of GAIT negotiations may be described as the most significant event to come out of the agreement since its inception in 1947. The UR made advances in world trade rules by broadening its coverage to areas that previously were not subject to multilateral discipline. It will lower tariffs; tighten existing rules regarding agriculture, textiles and clothing; strengthen dispute procedures; establish a new overall administrative structure, the World Trade Organization (WTO). These rules relate to trade in services, intellectual property rights, and investment measures. The General Agreement on Trade in Services (GATS) establishes procedures to reduce and eliminate barriers to trade in world services estimated at about US$1 trillion. The agreement on trade-related aspects of intellectual property rights (TRIPS) represents important progress in areas such as patents, trademarks, copyrights, and trade secrets.

These new provisions aside, probably, the most significant development of the UR was the establishment of a new permanent (international) multilateral institution, the World Trade Organization (WTO). The establishment of WTO, and accompanying procedures for the multilateral settlement of disputes contained in the Dispute Settlement Understanding (DSU), consolidates the results, understandings and agreements of previous trade negotiations under a common framework and reinforces the Trade Policy Review Mechanism (TPRM).

Included in this agreement are a list of tariff reductions and the removal of export subsidies mainly on agricultural products. Previous rounds had already brought average industrial country tariffs (AICT) down to 6.40 percent and the expected 39% reduction associated with the current round will lower the AICT to only 4.0 percent. The agreement also calls for the complete elimination of tariffs in a number of sectors such as steel, pharmaceuticals, construction equipment, agricultural equipment, medical equipment, semiconductors and computers. All of these commitments reflect a growing belief in the potential benefits of trade liberalization and is consistent with trade promotion efforts.

THE WORLD TRADE ORGANIZATION (WTO)

An outgrowth of the Uruguay Round (UR) is the formation of institutions and venues to administer the trade obligations contained in the UR agreements. The two primary instruments established are the World Trade Organization (WTO) and the dispute settlement procedures set forth in the Dispute Settlements Understanding (DSU).

The agreement establishing the WTO includes two basic components:

1. It creates a formal institutional structure for conducting trade relations among countries covered by UR agreements, and
2. It makes acceptance of all UR multilateral trade agreements a condition of WTO membership.

Essentially, the WTO agreement retains and recognizes the existing institutions and practices that have developed over some 45 years to implement the GATT, a wide ranging multilateral trade agreement which now has over 100 participants. The agreement expressly states that unless otherwise provided, "the WTO shall be guided by the decisions, procedures and customary practices followed by the CONTRACTING PARTIES TO GATT 1947, and the bodies established in the framework of GATT 1947" (ART XVI: 1).

Membership in WTO is open to any country or customs union that is not currently a contracting party to GATT after first negotiating an accession agreement approved by two-thirds of WTO members (ART XII).

Least developed countries (LDC's), as recognized by the United Nations, will be required to undertake commitments and concessions only to the extent consistent with development, financial or trade needs, or institutional capabilities (ART XI: 2). Additionally, LDC's may also be accorded special and differential treatment in other UR agreements. The WTO agreement provides the mechanism to be followed in bringing an amendment before WTO members for a vote as well as establishing a variety of super majority requirements for particular types of amendments.

THE CARIBBEAN COMMUNITY (CARICOM), DEMOGRAPHICS AND TRADE FEATURES

CARICOM was established, July 1973, with the objective of promoting economic integration and stimulating trade in the Caribbean region. The membership of thirteen countries encompasses nearly six million people and covers an area of some 271,000 square kilometers of territory (Table I).

TABLE I - CARICOM: Selected Indicators 1995

Countries	Area Km2	Population ,000	Population Growth %	% of CARICOM	Unemployment % * ** ***
Antigua-Barbuda	440	64.3	0.1	1.1	5*
Bahamas	13942	275	1.5	4.73	NA
Barbados	432	264.4	0.2	4.55	19.7***
Belize	22960	216.5	2	3.73	12.5***
Dominica	750	74.2	1.1	1.28	10*
Grenada	345	97.4	0.5	1.68	25*
Guyana	214970	760.4	2.1	13.1	35*
Jamaica	11424	2486.5	1	42.8	16.2***
Montserrat	102	10.4	0.7	0.18	8.3**
St. Kitts-Nevis	269	42.8	0.8	0.74	15*
St. Lucia	616	145.3	1.7	2.5	15.9***
St. Vincent	388	109.9	0.3	1.90	30*
Trinidad-Tobago	5128	1261.9	0.6	21.71	17.2***
TOTAL	271,766	5809.00	NA	100.00	NA

Source: Caribbean Development Bank, Annual Reports, 1996
*1990 Data, **1994 Data, ***1995 Data

Often described as "mini-states," their population ranges from just over 10,000 in Montserrat to some 2 million in Jamaica. Population growth rate in 1995, ranges from 0.7 percent in Montserrat to 2.1 percent in Guyana, reflecting somewhat a slowing of population growth among these countries. The larger countries of Belize, Barbados, Jamaica, and Trinidad & Tobago had total population growth of 2.0, 0.2, 1.0 and 0.6 percent, respectively. (Table 1). The fact is, however, these countries as described by William Demas [1986: pg. 14] " are either small or very small." As he continues, "the two great barriers to the escape from dependence and underdevelopment in the West Indies [Caribbean] are the small size of the countries and the legacy of a long history of massive external dependence."

Profile of CARICOM Trade

Bauxite and petroleum are important resources in three of the countries. In 1990, Guyana exported 68.2 thousand tons of bauxite while Jamaica exported 103.1 thousand tons of bauxite and 584 thousand tons of alumina, respectively. Six of the member countries produce and export sugar ranging from 9.1 thousand long tons from St Kitts/ Nevis in 1990 to some 85.8 thousand long tons from Jamaica, while Banana exports ranged from 3.9 thousand tons from Grenada to 69.5 thousand tons from St. Lucia over the same period.

With respect to GDP, Barbados, Jamaica and Trinidad and Tobago accounted for over 50 percent of the GDP of CARICOM countries in 1995. Of these countries, Belize had the highest GDP growth rate of 3.7 percent. Jamaica's growth was less than one percent (0.5) and Trinidad & Tobago had an increase of 1.9 percent. St Vincent was the country with the fastest GDP growth rate of 7.4 percent, followed by Guyana (5.1 percent) and St. Lucia (4.1 percent) clearly aided by positive effects of the Economic Recovery Program. (See Table II).

TABLE II-CARICOM: Gross Domestic Product GDP per capita for Selected Years

Countries	GDP at current market prices ($ million)			GDP per capita current prices			Real Rate of Growth in GDP (%)
Years	1987	1991	1995	1987	1991	1995	1995
Antigua-Barbuda	275.7	421.9	494.5	3,399	6,591	7,690	(4.4)
Bahamas	2,730.0	2,810.8	3,420.0	11,447	7,426	12,436	NA
Barbados	1,456.9	1,696.3	1,854.5	5,747	6,572	7,015	2.7
Belize	NA	395.6	583.6	NA	2,089	2,696	3.7
Dominica	125.9	177.3	215.3	1,550	2,491	2,901	1.8
Grenada	139.1	210.1	265.0	1,346	2,319	272	2.8
Guyana	344.1	342.4	630.8	455	454	830	5.1
Jamaica	2,864.6	3,496.8	5,202.0	1,219	1,442	2,092	0.5
Montserrat	48	59.3	NA	3,997	5,387	NA	(2.9)
St. Kitts-Nevis	98.6	170.9	228.1	2,119	3,974	5,331	3.4
St. Lucia	199.4	421.4	556.72	1,400	2,730	3,832	4.1
St. Vincent	136	237.4	276.6	1,210	2,630	2,517	7.4
Trinidad-Tobago	4,603.2	5,278.7	5,175.2	3,782	4,266	4,101	1.9
TOTAL/countries	1085	1209	1574	2898	3721	4309	2.175

Source: Caribbean Development Bank, Annual Reports 1989, 1992, and 1996

Economic performance in most of the CARICOM countries has been sluggish during the 90s. Low growth rates have been the result of the fiscal and monetary policies which most of these countries have been forced to introduce to stem their balance of payment difficulties. The general weak regional performance has in turn contributed to mounting unemployment with several of the larger countries reporting unemployment rates in excess of 15 percent (Table 1).

Three major occurrences have dominated regional discussions in the 90s. First, there was the implementation of the CARICOM COMMON EXTERNAL TARIFF (CET) in 1992; second, there was the implementation of the European Single Market in 1993 and third, was the signing of the Uruguay Round under GATT in 1994. Each of these occurrences had major importance for regional development. In the former, Caribbean leaders agreed to a phased implementation of the CET with import tariffs (excluding agricultural products) to be reduced to 20 percent by 1998. In the latter, an agreement was reached with the EC Ministers of agriculture on measures which should ensure for some time continued preferential access of CARICOM members' bananas to the United Kingdom under the single market arrangement.

REGIONAL TRADING PATTERNS

The level of trade relative to GDP reflects the importance of international trade in an economy (See for example, de Alonso, pgs. 13 - 23).

TABLE III CARICOM: Exports of Goods and Services for selected years

Countries	Exports ($ million)			Imports ($ million)			Balance of Trade ($ million		
	1987	1991	1994	1987	1991	1994	1987	1991	1994
Antigua-Barbuda	209.7	345.7	440.8	28,101	403.1	433	-71.4	-57.4	7.8
Bahamas	1,662.5	174.7	1,789	1,824.8	1,947.9	1,974.6	-162.3	-1,773.2	-185
Barbados	714.3	857.9	1,003.4	774.5	936.7	866.6	-60.2	-78.8	136.8
Belize	NA	248.1	292.9	NA	312.4	346.2	NA	-64.3	-53.3
Dominica	49.6	99.1	95.6	73.7	147.2	131.7	-24.1	-48.1	-36.1
Grenada	68.5	103.5	127.7	103.7	168.4	168.0	-35.2	-64.9	-40.3
Guyana	248.3	239	526.4	296	222	NA	-47.7	17.0	NA
Jamaica	1,570.7	2,380.9	2,453.8	1562.6	2,785.2	2,791.9	8.1	-4,043	-338.1
Montserrat	5.3	20.5	30.1	27.9	46.2	44.3	-22.6	-25.7	-14.2
St. Kitts-Nevis	60.4	100.1	120.2	91.9	139.7	143.8	-31.5	-39.6	-23.6
St. Lucia	132.6	306.9	336.9	171.8	396.4	369.5	-39.2	-89.5	-32.6
St. Vincent	71.4	118.6	93.7	109.1	173.4	157.7	-37.7	-54.8	-6.4
Trinidad-Tobago	1,648.5	2,228.4	2,011.8	1,965.3	2,235.4	1,247.6	-316.8	-70.0	764.2
Regional Total	6,441.8	7,223.4	9,322.3	9,811.4	9,914	8,674.9	-3,369.6	-2,690.6	647.4

Source: Caribbean Development Bank, Annual Reports 1988, 1992, and 1995

As such, Table III provides information on the level of trade, Exports and Imports for the thirteen CARICOM member countries. For the years 1987, 1991 and 1994 all countries except Jamaica (1987), Guyana (1991) and Antigua, Barbados and Trinidad and Tobago (1994) had a negative trade balance. The significance of this to the new GATT provisions is that it will be quite difficult for these countries to erase their present status in the face of the removal of preferential prices. A ratio of the volume of Exports and Imports as a proportion of GDP is provided in Table IV for members of the CARICOM region. For the region as a whole, the ratio was 1.248, 1.090 and 1.048 for the periods 1987, 1991 and 1994, respectively, reflecting an increasing level of openness on the part of the CARICOM trading bloc.

TABLE IV CARICOM: Ratio of Exports and Imports of Goods and Services to GDP by Country for selected years)

Countries	1987	1991	1994
Antigua-Barbuda	1.78	1.774	1.767
Bahamas	1.28	0.755	1.157
Barbados	1.021	1.057	1.076
Belize	NA	1.416	1.157
Dominica	0.979	1.389	1.094
Grenada	1.237	1.294	1.086
Guyana	1.581	1.346	NA
Jamaica	1.093	1.477	1.237
Montserrat	0.691	1.124	1.224
St. Kitts-Nevis	1.544	1.403	1.261
St. Lucia	1.526	1.668	1.377
St. Vincent	1.327	1.229	0.979
Trinidad-Tobago	0.785	0.845	0.674
Regional Index	1.248	1.090	1.048

Source: 1987 and 1991 calculated from Tables II and III

Naturally, the level of openness on the part of the individual countries differed. In 1987 the ratios of all countries except Dominica, Montserrat and Trinidad and Tobago's were above one. In the case of these countries, the results for 1991 and 1994 reflect an even greater level of openness with Barbados having values of 1.057 and 1.076, Grenada 1.294 and 1.086; Jamaica 1.477 and 1.237 respectively, and only Trinidad and Tobago with ratios of 0.785 and 0.845 for the years 1987 and 1991, probably reflecting its strong domestic petroleum base.

The strength of these values seem to lend credence to the ideas of those who see small, open economies as having no alternative to trade. The idea of trade in itself is arguably not bad, but it lends itself to second-guessing when trade, especially imports, is growing faster than domestic production; hence the level of vulnerability with respect to world prices and world supplies become greater.

Direction of trade

CARICOM countries in the 1980's received substantial trade preferences from their three major trading partners (U.S., Canada and the EEC including the UK). These trade preferences provided special treatment of the region's export's under the U.S.

Caribbean Basin Initiative (CBI), the EC's African, Caribbean and Pacific Countries (ACP) and the Lome Convention, and Canada's Preferential Trade Scheme for the Commonwealth Caribbean (CARIBCAN).

Table VI provides information derived from CDB reports relative to the direction of trade on the part of the members of CARICOM. For the region as a whole, the United States, and Europe (EC and UK) in 1994 were the major destination of export followed by CARICOM with 13.9 percent on the other hand, 21.23 percent of export was to "other countries".

TABLE V: Direction of Trade in 1994 (Imports) for selected CARICOM countries

Countries	CARICOM	USA	Canada	UK	EU	Other	Total Imports
Barbados	119.5	237.5	34.9	56.4	39.6	126.4	614.3
Belize	11.2	138.1	6.0	18.9	10.9	74.9	259.9
Grenada	33.9	41.4	3.0	14.2	7.5	19.4	119.4
Guyana	149.1	1,145.1	82.9	96.2	100.9	603.0	2,177.2
Jamaica	6.9	12.7	0.7	4.6	0.8	5.3	30.9
Montserrat	6.9	12.7	0.7	4.6	0.8	5.3	30.9
St. Lucia	63.9	112.1	11.8	40.4	16.5	56.9	301.7
St. Vincent	34.2	45.6	2.9	16.6	15.5	15.2	130.0
Trinidad-Tobago	60.3	620.2	75.1	109.0	93.0	345.2	1,302.7
All countries (Tot/Av.)	59.28	280.2	26.14	43.7	34.19	160.99	-
% of total	9.8	46.36	4.32	7.23	5.66	26.63	-

Source: Caribbean Development Bank Annual Report 1995

In 1994, the United States (46.36 percent) was the primary single source country for CARICOM imports. Some 26.63 percent was from "other countries" with the rest of the region accounting for nearly 10 percent (Table V).

TABLE VI: Direction of Trade in 1994 (Exports) for selected CARICOM countries

Countries	Export ($ millions)						
	CARICOM	USA	Canada	UK	EU	Other	Total Exports
Barbados	61.2	32.6	7.7	33.8	3.7	41.6	180.6
Belize	5	63.1	10.2	43.4	7.1	14	142.9
Jamaica	58	439.7	147.7	164.4	122.1	287.5	1,219.5
Montserrat	0.6	1.1	0.0	0.1	1	0.1	2.9
St. Lucia	14.6	26.3	0.3	49.9	1.8	1.9	94.9
St. Vincent	28	407	0.1	15.2	0.8	2.1	51.0
Trinidad-Tobago	436	976.6	85.4	42	128.8	573.4	2,242.2
All countries (Tot. /Av.)	67.04	216.27	27.9	38.75	29.48	102.29	
% of total	13.91	44.9	5.8	8.04	6.12	21.23	

Source: Caribbean Development Bank Annual Report 1995

In terms of value, the level of intra-regional trade engaged in by these countries are well below the level which would make a real contribution to the growth and the development of these countries. Barbados, Jamaica, Trinidad and Tobago, Antigua and St. Lucia were the countries that had transactions (I or E) with every other member of the bloc. Belize, on the other hand, had the least number of transactions with the other countries. The significance of this lends support to those who minimize the importance of regional trading blocs serving as an "engine of growth" of their economies.

Importance of Bananas for Caribbean Community Members

The importance of bananas to the members of CARICOM Countries is succinctly expressed in the report, US and CHIQUITA at the WTO, which states:

> The banana industry is central to the economic well being of the Caribbean and while it can certainly benefit from reform to reduce costs and increase productivity, no other legal crop or industry can be developed to replace it in the foreseeable future.

That study further elaborates on the industry's significance as it explains that the banana industry accounts for in more than fifty percent of the total export earnings of Dominica and St. Lucia and is second only to sugar as an agricultural export earner for Jamaica. Further, it is directly or indirectly the major single employer of the work force of Dominica and St Lucia and is important to Jamaica as an agricultural employer.

The Prime Ministers of the Windward Island countries further strengthened this importance in statements when they met President Bill Clinton at the Caribbean Summit. The Prime Minister of Dominica, Mr. Edison James stated:

> What we have seen, and are seeing now in my part of the world, is a dismantling of confidence among those of our people who grow bananas and who earn their living from bananas. Many banana fields have already been abandoned, and this is so because of the WTO challenge led by the USA.

The Honorable Vaughn Lewis, former Prime Minister of St Lucia elaborated on this statement as follows:

> The banana industry in the Caribbean is a strategic industry. It accounts for fifty percent of the visible export earnings of the Windward Islands (Dominica, Grenada, St Lucia and St Vincent and the Grenadines). In the particular case of Dominica, it represents over 70 percent of export earnings. For the four islands it accounts for 15 percent of Gross National Product, 27 percent to 40 percent of government revenue and employs 25 percent of the work force of these islands.

What is common in the expressions of all of these statements is that banana production and export is critical to each of the countries of the region. The industry is the single most important commodity to these economies contributing to foreign exchange earnings, employment generation, savings and government revenues. As such, they have been nurtured on a regime of relatively stable prices under the protective umbrella provided by commodity or trade agreement provided by the African, Caribbean and Pacific Countries/ Europe Economic Committee (ACP/EEC) accord.

There is, therefore, a critical urging for the countries of the region for the governments to develop and promote alternative crops and/or commodities that could make use of existing shipping and infrastructure mechanisms which are in place in the various communities within the region.

SECTION III: A GRAPHICAL MODEL OF POSSIBLE WTO COMPLIANT TRADE LIBERALIZATION EFFECTS ON CARIBBEAN TRADE IN BANANAS

Like any other epoch making change in international trading agreements, the establishment of the WTO is bound to have both positive and negative effects on trade between countries and regions. Will the CARICOM countries be among the winners or losers as a result of the establishment of the WTO? An objective response to this question requires an in depth analysis of the group of countries which make up CARICOM.

This paper utilizes a sectoral approach to look at the impact of the establishment of the WTO and its impact on Caribbean trade in bananas. This particular methodology demonstrates the use of a graphical trade model to illustrate the likely effects of changes in the terms and conditions of Caribbean banana exports as the EU contemplates WTO compliant trade liberalization measures. This approach has the advantage of providing a clear visual picture to Caribbean officials and policy makers of the trade implications of a number of liberalization scenarios.

The banana sector was chosen for this study because of its importance to a number of the smaller and vulnerable Caribbean countries, such as the Windward Islands, which continue to rely heavily on trade in bananas, particularly under the LOME preferential trading arrangement with the EU. For these countries, the decisions made with respect to the timing and magnitude of the changes to the current trading arrangements will determine their ability to survive as stable and fairly democratic nations. As the EU and the ACP country representatives prepare to discuss and negotiate inevitable changes to LOME IV, Caribbean trade representatives and negotiators must be fully aware of the consequences of actions proposed by the EU based on various scenarios. The possible impact of these trade liberalization decisions can be studied and evaluated. In the following section, an attempt is made using graphical tools to provide such an analysis for the banana sector.

Assumptions

The model is based on the following three basic assumptions:

1. That the EU will, in the medium to long term, lower the preferential prices and quotas offered to ACP countries under the current LOME IV. This will result in lower prices paid for Caribbean bananas.
2. That Caribbean banana producers are currently not operating at the lowest point of their short run average cost curve and as a result are capable of reducing their costs of producing bananas and improving the quality of production in the short to medium term by moving down towards the lowest point of their existing cost curves. Also, that Caribbean banana production is capable of achieving technological efficiencies to the extent of shifting the average cost curve downwards in the longer term.
3. That the EU will provide a compensatory aid and investment package to the ACP countries to help them to adjust to changes in the preferential content of trade that they enjoyed under LOME.

Description of Possible Effects

Figures 1A, 1B and 1C illustrate the movement in prices and quantities of Caribbean banana exports to the EU based on the above assumptions. Figure IA shows the demand and supply curves in the world market for bananas. The equilibrium price for bananas sold on the world market is P_w and the equilibrium quantity is Q_w. Figure 1B shows demand and supply curves for Caribbean bananas in the current EU market and some possible effects of expected changes in preferential prices and quotas. Figure 1C illustrates some possibilities for the short-term and long-term average cost position for Caribbean banana producers.

We begin by observing that the current situation with regard to the export of Caribbean bananas is represented by two possibilities as shown in Figures 1A and 1B. Apart from the inter-regional exports of banana, within the Caribbean common market area, Caribbean Exporters can either sell their produce, up to the amount represented by their quotas (depicted by Q_p 1 in Figure 1B), to the EU under the LOME arrangement for a preferential price (shown as P_p 1 in Figure 1B) which is normally significantly above the world market equilibrium price (shown as P_w in Figure 1A) or alternatively sell their bananas on the world market at the world market price,

As profit maximizers, the Caribbean producers would obviously sell as much bananas as they can produce up to their quotas to the EU and only sell to the world market that amount which is produced in excess of their quotas and domestic consumption. The rectangular area bounded by a-b-Q_p I-O_p in Figure 1B represents the total revenue received by Caribbean banana exporters under the current Lome arrangement. It is a reasonable assumption that there is some variation in the efficiency of Caribbean banana producers. Some producers are likely to produce at point A on their short run average cost curve as shown in Figure 1C, where they operate at or close to, breakeven point. Other, more efficient producers make a profit and are assumed to produce at a point on the average cost curve such as B in Figure IC. If the average Caribbean producer is at point B on the short run average cost curve (SRAC) in Figure IC, then the profit that goes to these Caribbean exporters currently is represented by the bounded area a-b-c-d in Figure 1B.

Given assumption 1, it is projected, that the preferential price for Caribbean bananas under Lome will be gradually reduced and brought closer to the world market price for bananas. It is also anticipated that though the EU is expected to retain the quota system that is currently used to regulate the amount of Caribbean and other ACP goods entering the union, that the quotas allocated for Caribbean exports, including bananas, will be substantially reduced over time. For the purposes of this paper, it is assumed that the period of adjustment will not exceed ten years. If this scenario plays, the Caribbean banana industry must be prepared to compete successfully on the world market for selling bananas by the year 2008 or the banana industry will cease to exist as a viable mainstay of some Caribbean countries such as the Windward Islands. Therefore, as the EU preferential price decreases and as Caribbean banana quotas are reduced as shown in the shift of the demand curve from DC, to DC2 along the fixed short run supply curve, S_c1 in Figure 1B, equilibrium demand and supply moves to E_p2 and the respective prices and quantities are P_p2 and Q_p2.

The reduction of both prices and export quantities will lead to a fall in total revenues and as a result profit levels will fall. As profits are driven to zero, Caribbean exporters must find ways to reduce their production costs while at the same time improving the quality of the product. Caribbean banana producers may be able to increase their total revenues by exporting more bananas to other markets (including the world market). However, they will only be able to regain levels of profitability if average costs are reduced in the short to medium term.

If the Caribbean producers are able to get close to the lowest point on the short run, average cost curve at C (see Figure 1C) and prices remain at P_p2 for a period then they will experience profits as represented by the area bounded by d-c'-e-f in Figure 1B. Even if this is achieved, there is expected to be further preferential price and quota adjustments downward and closer to the world market price level P_w. At this price, providing that Caribbean producers are able to openly compete in the quality of bananas offered for international consumption, they will be indifferent to selling to the EU or to the world market.

However, at P_w, Caribbean producers will again be selling at a loss, if they are unable to get to the absolute lowest point of their short run average cost curve at C in Figure 1C. Even if on average they are operating at C and are unable to obtain prices above the world market price, P_w, the less efficient producers will experience a loss. At this point, the only way for Caribbean producers to return to profitability in the industry is through its ability to shift the average cost curve downwards. Caribbean producers will have to enjoy changes in certain conditions of production such as increase the average yield per acre of banana plantations and a reduction in cost of production inputs such as labor and transportation costs. If Caribbean banana producers are able to achieve these efficiencies and also improve the overall quality of the bananas produced, they will be able to compete successfully on the world market. It is therefore anticipated that Caribbean banana producers will expand their supply of bananas exported, thereby shifting the supply curve out to S_c2 as shown in Figure 1B.

The combination of a reduction in the average costs of production as depicted by point D on the LRAC in Figure 1C, and an increase in banana exports depicted by Q_p1 in Figure 1B, will restore profitability to the Caribbean banana industry, based not on the largest of the EU but on the international competitiveness of Caribbean producers.

Discussion

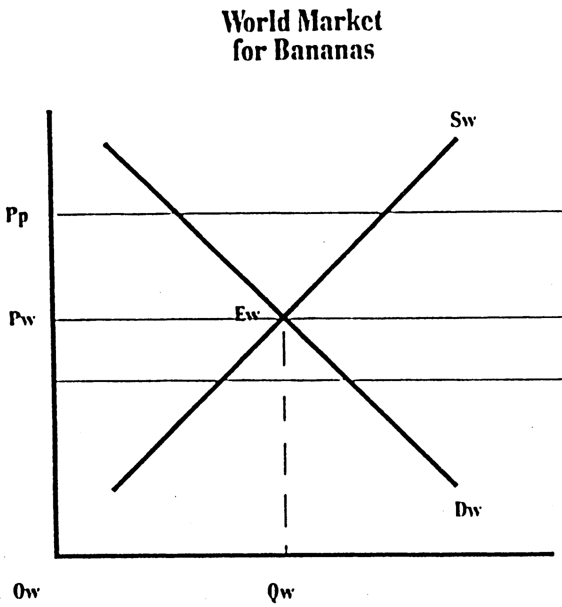
This graphic model illustrates some of the expected effects of WTO rulings on Caribbean banana exports. The preceding illustration of the possible or expected effects of EU trade liberalization efforts on banana exports and earnings point to three major concerns.

The first major concern is for the outcome of forthcoming discussions and negotiations with the EU with regard to the timing and magnitude of changes to Lome IV. It is critical that Caribbean trade representatives are able to convince the EU trade authorities that despite proposed changes in the letter of Lome IV that the spirit of Lome should remain intact.

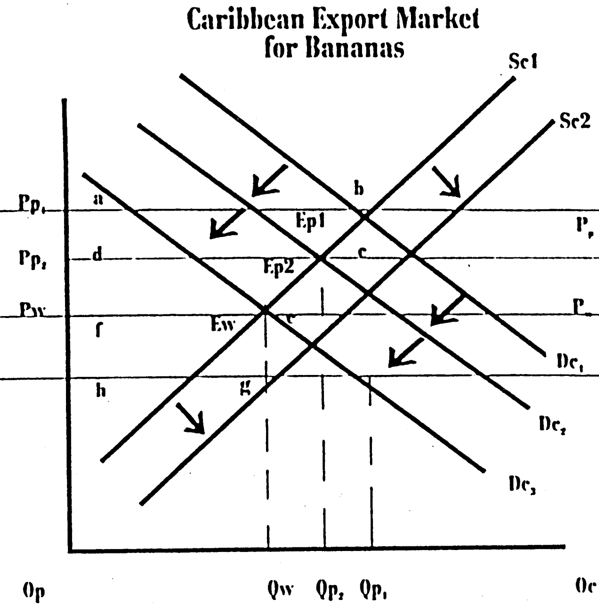
As a result, the EU should at least maintain current levels of effort with regard to trade and development aid concessions to the ACP group. These one way preferences have a basis in a joint decision of GATT member countries known as "the enabling clause."[1]

An important objective for the Caribbean representatives in these negotiations is the establishment of a "Compensatory Trade Adjustment and Development Fund" (CTADF) hereafter referred to as the Compensatory Fund (CF) for short. This fund should be set up by the EU to assist ACP countries to make the adjustment and transition needed to compete successfully in the world market for certain exports like bananas. The CF would be used mainly for the development of appropriate technologies to make the Caribbean producers more

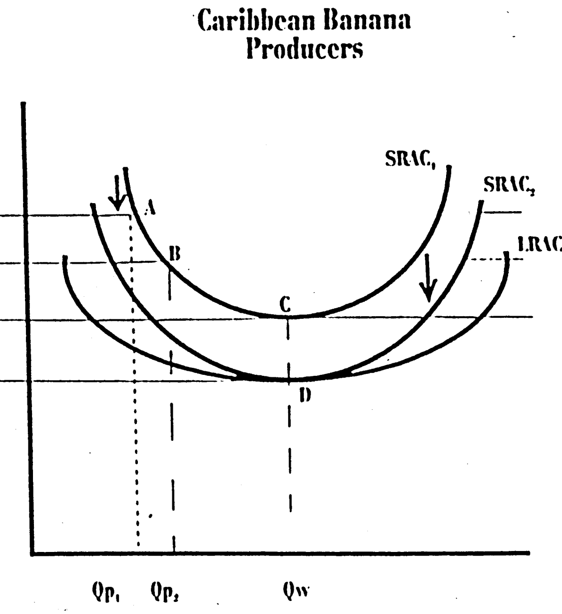
[1] In 1965, GATT Parties added Part IV to the General Agreement, an amendmant that recognises the special economic needs of developing countries, and asserts the priciple of non-reciprocity. Under this priciple, developed countries forgo the receipt of reciprocal benefits for their negotiated comitments to reduce or eliminate tariffs and restrictions on the trade of less developed contracting parties. Because granting preferential tariff rates to selected countries would violate the MFN obligation, GATT parties in 1971 adopted a waiver to Article I for the Generalized Sytem of Prefernces (GSP) which allowed developed contracting parties to accord more favourable treatment to the products of developing countries for 10 years. Developing countries were able to secure adoption of the Enabling Clause at the end of the Tokyo Round of GATT in 1979 as a permanent deviation from the MFN by joint decision.



(1A)



(1B)



(1C)

Definition of Terms in Figures 1A, 1B and 1C

Pw - World market price of bananas

Qw - Quantity of bananas supplied to the world market

Dw - The demand for bananas on the world market

Sw - The supply of bananas on the world market

Ew - Equilibrium in the world market

Pp - Preferential price offered to Caribbean exporters by EU

Qp_1 - Quotas of banana allowed to Caribbean exporters by EU

Ep_1 - Equilibrium in EU market at current preferential prices and quotas

Ep_2 - Equilbrium in EU market assuming future reduction in preferential prices and quotas

Qp_2 - Potential change in EU quotas for Caribbean bananas

Dc_1 - Quantity of bananas demanded from Caribbean producers Under current Lome agreement

Dc_2 - Quantity of bananas demanded from Caribbean producers assuring future reduction in quotas

Dc_3 - Quantity of bananas demanded from Caribbean producers at current world market prices

Sc_1 - Quantity of bananas supplied by Caribbean producers under current Lome agreement

Sc_2 - Quantity of bananas supplied by Caribbean producers assuming larger volumes of diversified exports

Ow, Op and Oc are the various points of origins displayed.

a, b, c, d, e, f, g, and h are points depicting the profit components of total revenues assuring different levels of average cost to Caribbean producers.

$SRAC_1$ - Initial short run average cost curve of Caribbean producers

$SRAC_2$ - Potential short term average cost curve of more efficient Caribbean producers

LRAC - Potential long term average cost curve of Caribbean Producers efficient producers, and for the improvement of quality through innovations in packaging, storing and transporting techniques and facilities. The size of the fund should be determined after careful studies and evaluations of the required effort for Caribbean producers to achieve international competitiveness in key trade sectors.

The second major concern is to allow enough time for Caribbean producers and exporters to make the adjustment to a more efficient and diversified export base. The Uruguay Round of GATT provides that, save for exceptional cases, "the phase-in period for interim agreements should not exceed ten years". It is assumed that this is a reasonable period of time for Caribbean exporters under Lome to make the necessary adjustments to become more internationally competitive, given the creation of the compensatory fund. The first five years should be spent introducing better production and marketing techniques to enable Caribbean producers to move close to the lowest point of their current average cost curves.

The second five years should be spent on efforts to shift the average cost curves downwards for the major Caribbean producers affected by the proposed changes. This process will be difficult and would involve changes in scales of production, including increases in the average size of banana farms and the achievement of economies of scale in the banana industry.

In 1965, GATT Parties added Part IV to the General Agreement, an amendment that recognizes the special economic needs of developing countries, and asserts the principle of non-reciprocity. Under this principle, developed countries forgo the receipt of reciprocal benefits for their negotiated commitments to reduce or eliminate tariffs and restrictions on the trade of less developed contracting parties. Because granting preferential tariff rates to selected countries would violate the MFN obligation, GATT parties in 1971 adopted a waiver to Article I for the Generalized System of Preferences (GSP) which allowed developed contracting parties to accord more favorable treatment to the products of developing countries for 10 years. Developing countries were able to secure adoption of the Enabling Clause at the end of the Tokyo Round of GATT in 1979 as a permanent deviation from the MFN by joint decision.

In this second five-year period the benefits of human capital investments, which should occur at the very beginning of the first five-year period, should start to yield returns in increased productivity. At this stage R&D investments, which would also have occurred at the beginning of the first five-year period, should begin to payoff. Concomitant with these efforts, is a need for more effective and aggressive marketing of Caribbean exportables utilizing new technological opportunities such as those created through the Internet. Aggressive marketing is needed if Caribbean exports are to penetrate non-traditional markets as it seeks to increase its volume of exports to levels where the economies of scale are significant.

The third major concern is that the very survival of some Caribbean countries such as the Windward Islands will depend on the success of the adjustment plan. This factor is so important that it should not be left to chance. It is proposed that the entire ten year period be broken down into "very reasonable" six month program and performance measure periods for the implementation of the adjustment plan and that disbursements from the compensatory fund be made contingent on the achievement of these program and performance measures.

At issue would be the selection of an appropriate mechanism for monitoring this activity. Whether some Caribbean Institutions, such as the Caribbean Development Bank, should be charged with this monitoring and disbursement responsibility, or whether this authority should remain with the EU should be worked out. If this responsibility is given to the CDB, it is recommended that a special monitoring committee of experts, outside of the CDB, be established to examine the performance of producers and exporters and to determine the extent to which the performance measures are satisfied, before recommending disbursement of funds, subject to the banks own accountability criteria.

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