

## TRADING OUT OF POVERTY IN LATIN AMERICA

### Project Series

In partnership with the Institute for the Study of the Americas (ISA), the Foreign Policy Centre (FPC) hosted a seminar entitled *“Trading Out of Poverty in Latin America.”* This was the first event in a series of roundtable discussions organised by the FPC in collaboration with universities and institutes of higher education across the United Kingdom.

**“Tackling poverty is an issue in which NGO and business agendas have increasingly found more common ground.”**

*Hilary Parson, Nestlé*

The aim of the seminar series is to engage with future global leaders, policymakers as well as policy advocates in wider civil society to explore the role played by business in international development. The forums hope to identify constructive ways in which civil society together with the private sector can forge more effective links. We hope to exchange ideas and share best practice relating to poverty alleviation and achieving sustainable development and economic growth. The event series has been sponsored by Nestlé.

### Reinforcing why trade matters

**“Trade matters but context matters too.”**

*Graham Symons,*

*Department for International Development (DfID)*

Exploring the challenges and opportunities presented by Fairtrade in Latin America provided five important discussion points during the seminar.

Firstly, the largest number of Fairtrade producers are concentrated in Latin America. Understanding the impact of Fairtrade on poverty in the region provides useful insight for the potential of Fairtrade in other regions of the world.

Secondly, discussing the impact of Fairtrade in the region provided an opportune reminder of the significance of Latin America in the international development debate. In recent years the region has received relatively little attention, compared to Africa and South Asia, in spite of its many development challenges. DFID’s recent approach to the region has been one of trying to leverage impact by working with significant multilateral institutions, such as the World Bank and the Inter-American Development Bank.

Thirdly, developing export markets is important for economic growth. From 1990 to 2004, exports in Latin America grew by nine per cent. In spite of the impressive expansion of exports, economic growth rates were low and income inequality remained high in the region. Part of the problem was that economic policies were primarily focused on trade and foreign direct investment and assumed that they would both automatically lead to economic growth and sustainable development. In fact, policies that promote trade and foreign investment need to be accompanied by complementary policies which tackle structural impediments to growth and development. Prioritising structural issues such as land reform, improving labour productivity, developing local markets, promoting institutional reform, encouraging the creation of small and medium sized enterprises, pursuing a good governance agenda (which prioritises gender equality and female empowerment) should also be important aspects of a successful development policy.

One of DfID’s global priorities on trade is to increase its spend on *aid for trade* initiatives by 50 percent to \$750 million by 2010 (with support for complementary infrastructure). These schemes provide assistance to developing countries to help implement economic reforms and promote trade liberalisation.

Fourthly, the current global trade regime prioritises increased market openness at the expense of systematically failing the global poor. As such, there needs to be greater

political commitment (particularly by industrialised economies) globally to implement policy interventions that better regulates global markets to ensure those most in need benefit from trade.

Finally, in light of the indefinite suspension of the Doha Development round (despite optimism that negotiations could be resumed), there were very real concerns about accelerated regional integration in Latin America. This is particularly in light of the disproportionate dominance of the US, in these trading blocs (North American Free Trade Agreement - NAFTA and Central American Free Trade Agreement - CAFTA), at the expense of smaller economies.

By way of illustration, when NAFTA was created in 1994, Mexico had three million corn farmers (one-fifth of the population). However, the opening up of the Mexican corn market led to an influx of US corn imports, production of which was subsidised by the US government. By 2002, the domestic price for corn had fallen by 70 per cent and families who once relied on income from corn production suffered adverse effects with respect to food security, health and education provision, as farmers' incomes fell to less than 30 per cent of its pre-NAFTA levels.

### Making a difference in the lives of ordinary people

**“Fairtrade maximises the positive effects of political and social globalisation by building formal and informal links between producers, developing countries and consumers in developed countries.”**

*Dr. Diego Sánchez-Ancochea, ISA*

Fairtrade and other crop certification initiatives are designed to give farmers increased ownership of the goods they produce by securing greater incomes, as well as acquiring more of a share in the profits and benefits from directly marketing their products. In addition, Fairtrade promotes sustainable agricultural trade through improving social and environmental standards and practice which are more beneficial to people and their environments.

Fairtrade also represents efforts to link ethical consumers in industrialised countries with producers in the developing world. It provides a mechanism to raise consumer awareness about the very local impact (on producers' lives and livelihoods) of price volatility and commodity demand shocks in the international trading system. While recently the world has witnessed a surge in commodity prices such as oil and raw materials, due to unprecedented growth rates in emerging economies such as China and India, in real terms many traditional agricultural commodity prices have declined. In the case of cocoa and coffee this plummet has exceeded 50% since the early 1980s.

Fairtrade has promoted debate about ethical trade as a profitable business model (opposed to simply being philanthropy) which provides real returns for producer, suppliers and consumers.

As well as Fairtrade boosting growing consumer support, DfID has provided over £1 million to the Fairtrade Foundation (responsible for awarding the Fairtrade mark in the UK). DfID has also helped support Fairtrade initiatives such as the Kuapa Kokoo cocoa growers in Ghana.

### The dilemmas facing Fairtrade

1. Fair trade is only part of the solution

**“Fairtrade market share is small but growth is strong.”**

*Professor Brigitte Granville,  
Queen Mary, University of London*

Global Fairtrade sales reached €1.1 billion in 2005, an increase of a staggering 37% compared to 2004. Growth is expected to rise further as the popularity of ethical trading gains increasing mass market appeal. However, Fairtrade accounts for a mere 0.1 percent of global trade. Coffee represents approximately 30% of all Fairtrade sales in Europe and North America, however, the market share for Fairtrade coffee is only 3.4% in its largest global market, Denmark.

Given the relatively limited penetration of Fairtrade products in the retail market, it is important that the private sector makes a

more active commitment to promoting economic development. Nestlé provides an interesting example in this regard.

Nestlé has operated in Latin America since the early 1920s. Approximately 25% of the 320,000 farmers in its supply chain are milk producers. In partnership with farmers in milk districts in Brazil, Chile, Colombia and Mexico, Nestlé has worked to enhance labour competitiveness. By sharing knowledge about improved animal nutrition and developing business skills, farmers have experienced better yields and higher farming incomes.

2. Increasing the participation of more small-scale farmers and farm workers

Fairtrade pays significantly more compared to conventional market commodity prices and as such provides a critical lifeline to ensure a minimum quality of life for producers at the sharp end of poverty. This is particularly important during commodity crisis when the cost of production can often exceed the world market price for commodities. However, it is specialty producers concentrated in niche markets that are most likely to participate and benefit from Fairtrade activity. For many small-scale farmers and poor farm workers who are unable or unsuccessful in acquiring Fairtrade certification, they are left with very few options to mitigate against the effects of low commodity prices. In addition, even Fairtrade producers themselves continue to market a significant proportion of their produce through traditional markets systems. Therefore while growth is strong, Fairtrade has yet to convert a significant proportion of the global marketplace.

For some, Fairtrade is regarded as a form of protectionism because by guaranteeing a minimum price, producer incentives are distorted (without necessarily improving the producer's competitiveness eg. quality). Some would argue that this may represent an economically inefficient means by which to transfer income from consumers to producers (a direct transfer might be seen as more efficient).

Currently Fairtrade focuses on a limited number of export commodities and hand-crafts. There are many other commodities such as palm oil, wheat, soybeans and corn which could benefit from operating under Fairtrade principles. Furthermore, there may be demand for trading commodities at the luxury end of the market (silk, gold, jersey etc.).

While targeting Fairtrade markets does enable vulnerable producers, it is not an integrated export strategy as it has very little impact on growth.

**“Fairtrade’s impact on the dynamics on the international trading system is limited (in the absence of regulation) as it is mainly focused on niche markets.”**

*Claire McGuigan, ChristianAid*

The nature of the global trading systems means that Fairtrade can only provide limited support to a shift into higher value added sectors. Such a move could promote much needed industrialisation in poor economies. Approximately two-thirds of Fairtrade value is accredited to Europe. Tariff barriers and import taxes mean that it is increasingly difficult for processed goods from developing country regions to penetrate EU and US markets. For example, an EU import tax on raw pineapple is eight percent however processed pineapple attracts a tax of 46%.

3. What about accountability and governance?

**“As the market for Fairtrade products expands [...], clearly established rules and legal foundations for Fairtrade objectives are required or they may be very easily undermined.”**

*Professor Janet Dine,  
Queen Mary, University of London*

The growth in Fairtrade and other ethical trading movements has led to mounting concerns about the absence of research analysing the organisational and governance structure of these movements (and their supply chains), how they operate and the relationships between their different

networks. Ultimately, is the lack of Fairtrade certification necessarily a bad thing?

Queen Mary, University of London have recently won a research grant from the Art and Humanities Research Council to assess whether a legal framework is needed to prevent fraudulent use (or ‘capture’) of the movement by large retailers and manufacturers who may seek to co-opt the movements’ principles, undermining its original objectives.

Exploring the important issue of legal accountability and enforceability may help better evaluate the extent to which Fairtrade succeeds in strengthening the capabilities of disadvantaged producer groups. Thus does Fairtrade empower producers or is it simply a development trap? Does assessing the cost of certification exclude vulnerable producers who could benefit from Fairtrade membership? Is Fairtrade commodity pricing accurate in covering the full cost of production?

### Concluding remarks

This opening seminar has acted as an important platform for developing more exchange around the complexity of ethical trade and the dilemmas of trade liberalisation. In addition, it perhaps challenges both civil society and the private sector about ways in which they can jointly engage with the public sector to promote industrial policies which look beyond exports markets as a strategy for economic growth and development.