

## **Fair Trade in the Brazilian Economy:**

### **Potential Implications of and the Role of Government**

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#### **Abstract**

The objective of this paper is to analyze the implications of Fair Trade (FT) in the Brazilian economy – especially the agricultural sector. As a result, it was found that FT certification would most directly impact and benefit producers' and workers' lives by changing processes and routines and providing better living conditions and possibilities of market participation. The research shows that if FT can be maintained by private efforts, then the government does not need to get directly involved. Thus, the role of government would be related to regulatory concerns about economic, social and environmental processes.

**Key words:** 1. Fair Trade; 2. Brazilian Economy; 3. Government.

#### **Introduction**

The Fair Trade (FT) movement emerged from the civil society, which began in the 50's, due to the creation of partnerships between non-profit importers, located in the Northern Hemisphere – notably the Netherlands – and small scale producers located in the Southern Hemisphere. The movement was based on the idea of allowing market access for small producers from the South, while excluding middlemen, not devaluing production and reducing negative economic externalities. Among the efforts to consolidate the Fair Trade premises, shops for specific products and the first label that would distinguish the products were created.

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In Brazil, the FT initiatives have occurred since the 80's, but the movement nationwide only started from in the last decade. The effort to disseminate and implement FT has been the result of public-private partnerships, the efforts are directed towards producers, consumers and distributors. The movement happens mostly in parallel with the movement of Solidarity Economy, which altogether reaches 23,000 enterprises - related either to Fair Trade, the Solidarity Economy<sup>2</sup> or to both -, generating 2 million jobs, and present in 51% of Brazilian municipalities, moving approximately U\$ 5 billion per year.

The objective of this paper is to analyze the implications of Fair Trade for the Brazilian economy – especially the agricultural sector. It is the intention to answer the following questions: 1. Is Fair Trade really a good policy for the Brazilian economy? 2. Should government have to get involved with the Fair Trade certification?

The structure of the paper is divided in five topics: 1. Fair Trade; 2. Relevant concepts and theories about international economy and trade; 3. Fair Trade in Brazil- Brazilian economy, the role of agricultural sector, FT the efforts and a case; 4. The potential pros and cons of Fair Trade in the Brazilian economy; 5. Final remarks relating the understanding about what could be the implications of Fair Trade for the Brazilian economy and about the type of involvement that the government could have related to this certification.

## **1. The Fair Trade**

Fair Trade was created to question traditional practices of international trade based on principles such as profit maximization and concentration – either on companies' owners or middlemen -, workers being paid less – not necessarily enough for maintenance of living

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<sup>2</sup> Proposal for economy marked by democratization process and greater influence for workers in labor relations, whit organizations predominantly characterized by associative and cooperative processes.

conditions -, among generating other economic externalities. So, as fair trade is a term that has meant various things at various times, recently, the concept of fair trade has begun to focus more specifically on whether production processes adhere to certain labor, environmental, and human rights standards (Ehrlich, 2010). According to Fair Trade Labeling Organization (FLO), the term "fairer trade" refers to the creation of a different commercial environment, which reinforces the idea that producers and traders are trading partners, relying on a business concept that has an adequate price-performance ratio for goods and commodities produced by developing countries.

The principles of Fair Trade were inspired by ideas of generate market access for small producers, differentiated prices for goods, fair and sustainable negotiations and trade relations, capacity building, environment protection and consumer awareness. The market access for small producers would be facilitated by the creation of specific networks of trade. Prices paid for goods should reflect the costs of production, ensuring a level of income sufficient to meet the basic needs of producers and workers - allowing a decent life. Fair and sustainable negotiation and trade relations should be a consequence of including social concerns in negotiations and long term conditions in contracts. Capacity building efforts would be the result of training producers and workers on specific skills, in order to increase and improve productivity. The environment protection consequent of the change of production processes – on the agriculture by the introduction of organic practices. The consumer awareness would result from the effort of explaining and teaching consumers about the importance of buying products that result from socially and environmentally friendly practices.

The growth of Fair Trade happened between 1980 and 1990, when different networks of Fair Trade were created, bringing together producers, traders and investors. The main networks were the Network of European World Shops (NEWS), the International Federation

for Alternative Trade (IFAT), the European Fair Trade Association (European Fair Trade Association - EFTA) and the International Organization of Certified Fairtrade (Fairtrade Labeling Organizations International - FLO) (FLO, 2006). So, since the 90's, Fair Trade became not exclusively a social movement aiming to impact the international market, but became a certification of compliance of practices and processes.

Conceptually, the Fair Trade (FT) networks differ from traditional networks of international trade by presenting at their core the activity focused on cooperation, long term business partnerships, elimination of middlemen and concern about externalities. Therefore, the proposed structure is composed of several actors that fulfill functions of maintaining and strengthening conceptual networks in terms of market and society. Among the FT networks are the actors located in the developed and developing countries - or production and consumption countries (Vieira and Maia, 2009). Part of the structure of the so called developing world – or lower to medium income countries - are the producers which in addition to their work coordinate FT agencies at each productive sector and also support, research, and regulate them. The developed world is composed of retailers and consumers.

Producers compose the group of interest for whom the FT system was created, as it aims to promote a fairer trading system, in which they are the main beneficiaries. The main prerequisite for certifying a producer is to be in accordance with minimum standards, capacity to export, and democratic decision-making. The certification ensures that the producing organization meets social, environmental and employment requirements in the production process. As a result, the certification of FT products benefits and guarantees to the producer a minimum price for its goods, a FT premium and access to a pre-financing of up to 60% by its buyers.

The FT certifications are composed by two different productive sectors: agriculture and handicraft – the first being the most representative in volumes of trade. For the

agricultural sector the principles of FT, when in practice, are supposed to impact activities that traditionally labor intensive and dependent on the environment. Labor intensive activities traditionally in the developing countries use to have very low wages, many times lower than that necessary to maintain living conditions. As an activity dependent on the environment it is especially important to preserve the conditions of places where production happens. For producers and businesses, FT certification works also as a brand, and as a way to increase recognitions and reduce risks of brand damage - especially those related to social and environmental issues (Conroy, 2007).

From the demand side, nowadays, the biggest market for FT products, companies and foundations are located in Europe. In 2009 Fair Trade certified sales amounted to approximately \$ 4.6 billion worldwide, produced by over 1.2 million producers and workers (Mohan, 2010). According to the biggest certifier the Fair Trade Labeling Organization International (FLO) in 2009, in Brazil, the direct sales to consumer increase to up to US\$ 4.17 billion. Apart from be a way to contribute for development, it seems to be a growing market niche. Today, in the food sector has greater relevance - being the most significant products in terms of quantity are the bananas, cocoa, coffee, fresh fruit, juices, honey, rice, spices and herbs, wine, sugar and tea.

## **2. Some Concepts and Theories about International Economy and Trade**

On trade, the central difference among traditional international trade (IT) – free trade - and Fair Trade practices is based in the differentiation on the way products are produced – and thus the consequent externalities. By the Marrakesh Agreement, signed by the World

Trade Organization (WTO) members in 1994, countries are prohibited to use production and process methods as a basis for banning imports of a product (Conroy, 2007). Fair Trade tries to solve problems that usually IT does not, giving consumers the chance to choose based on their preferences and values for either quality, prices or production processes criteria<sup>3</sup>.

Also, on the micro level of economy, the opening of markets has led to greater integration and trade between countries, regardless of their development levels. The liberalization has offered benefits for both sides on trade relations – producers and consumers. However on the trade environment there is the existence of disparities among transnational corporations and small producers in acquiring access to resources, knowledge and markets. In business, it is clear that the traditional model of international trade benefits large corporations and "intra-firm" trade – as pointed out by Cowling and Tomlinson (2005). Thus, smaller firms are relegated to lower priority - as generally they are excluded from the context related to support the acquisition of knowledge or markets access and usually have less access to resources, capabilities and market power in relation to the traditional multinationals, resulting in greater challenges with regard to the complexity of international operations. The main fact might be due to the current process of globalization, as well as the concentration of corporate power, that coupled with the efforts of these corporations to suppress the dilution of power, have contributed to a series of strategic market failures of world economy, affecting the interests of global community (Cowling and Tomlinson, 2005).

At the report entitled "Free or fair trade?" (Shafaeddin, 2000), published at the United Nations Conference on Trade and Development (UNCTAD), it is suggested that free trade targets the benefit of all countries, regardless of their level of development, industrial capacity, technological capabilities and other structural features. The principle is based on the existence of homogeneity among countries, so that, for all industries and products there

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<sup>3</sup> However, some people believe that Fair Trade only brings more complexity to the international trade arena.

should be same level of fares, as supposedly every economy should have reached the same development level. However, due to the existence of disparities in development between nations, there is an implied division, in which developing countries specialize in production and export labor intensive products and other agricultural commodities. In practice, free trade might accentuate disparities, as a competition "apparently" equal across markets is exercised, price pressures rise and so social and environmental matters might be left behind.

Also, for small producers, some barriers such as access to resources for financing production and information about market and transport allow the introduction of middlemen on trade relations. So due to the low or inexistent profits there is an increase of informal jobs. According to the document named "*Trading away our rights*" women are increasingly among the worst paid hard workers – working more and receiving less (OXFAM, 2008). Some data may explain the context of agriculture in traditional practices of international trade (FLO, 2010): During the coffee crisis, prices fell significantly, even though this is one of the primary products of relatively higher value in international trade; Developing countries have increased the market share of fresh fruits, however, not all received the benefit of the profits of business, or improvements in working conditions and job security; Many producers have to sell most of its production to a few buyers, and in many cases for lower values than its costs; The international food market is often marked by protectionist practices, which impede the profitable trade or even the transaction; Workers and producers in developing countries, in many cases, live below average standards of living conditions – due to working conditions, wages and other factors; With the increase of liberalization and competition between small and large producers, many of those who have lower access to resources are obligated to get out from market – and quit their basic source of income.

Thus, the international trade market consists in a number of factors such as actors, goods, capital, technologies and logics that result in different integration levels. There are

several interactions between actors to acquire goods over the possession of certain resources, and their regulatory dynamics. The production and export food systems creates barriers to market entry and pressures for price reductions, but from the other side, some consumers demand the adoption of codes of conduct and product quality. This creates conflict between economic interests, regulatory policies, demand for quality and behavior standards (from different ethics and perspectives), reducing the possibilities for small producers to enter in the international trade arena. The intersection of the aforementioned factors impacts the production systems, trade arena and the countries' public policies formation.

### **3. Fair Trade in Brazil**

To understand the importance of certifications related to agriculture in Brazil, it is important first to understand the relevance of this sector for the country. Brazil is one of the largest countries in the world, considered a middle income - or developing - country, whose economy historically was based on agricultural activities. Nowadays, the main public policies are based in the aim to reach macroeconomic stabilization, solid financial environment and reduce poverty. Agriculture is included in the public policies – especially those related to poverty reduction due to its large proportion in the overall volume of production and social inclusion (MDIC, 2010).

In contextual terms, Brazil occupies the 24th position on the world exports, and it has a positive balance of payments. The main Brazilian exporting countries - China, United States, Argentina, Netherlands and Germany - are also some of the main exporting countries in the world – with the exception of Argentina. In average 20% of exports are of semi-manufactured goods, 40% basic and 44% of manufactured goods.



Agriculture, as previously mentioned is still the most important economic sector and some of relevant data about Brazilian agriculture are the following (INFOSECEX, 2010): Agriculture is the most representative exporting sector for the Brazilian economy, responsible \$ 35 million - 17% of total exporting. Sugar cane, soy, corn, manioc and orange are the most produced and exported agricultural goods – from traditional and organic agriculture; From the agriculture goods, soy is exported in the most volume, representing in the organic segment an average of 74% of total volume; The number of farms with hired workers is considered to be on the level of no more than 10%, and family farms represent in average 64% of total exporting; 20% of the working population is on the agricultural sector and women are 10% of workers in this productive activity.

The Fair Trade movement in Brazil has developed along the last decade, and the last five years were the most relevant. The work of Brazilian public and private institutions involved with FT has been to take social and environmental concerns for the small producer - farmers and artisans. Basically, its insertion is directly connected to the production of organic food and its regulation, with the following chronological insert provision. In 1999 the first Brazilian organic regulation was established and in 2001 the discussion about FT started at the local.

In the year of 2002, a pilot project was implemented in Brazil by ISEAL Alliance<sup>4</sup>, to promote and develop criteria for measuring compliance involving organic and FT markets. In 2003 there was the publication of the Law for Organic Food and creation of the National Bureau of Economic Solidarity, which gave more power for the movement as these were the

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<sup>4</sup> As on their website, it is a global association for social and environmental standards, which works with established and emerging voluntary standard, develops guidance and helps strengthen the effectiveness and impact of these standards (ISEAL, 2010).

engines for changes in production. The Law for Organic food established criteria about food organic producing and retailing, covering issues from the rural the urban retailer. The creation of the National Bureau of Economic Solidarity was and still related to the Ministry of Labor and Employment and "...aims to facilitate and coordinate activities in support of the Solidarity Economy throughout the country, aiming at generating employment and income, social inclusion and the promotion of fair and equitable development" (MTE, 2010).

From 2004 the discussion about the Brazilian FT system certification began. As a consequence of changes in production, for organic, the first economic sector to be included was the agricultural – basically in coffee, cocoa and orange juice. Due to the FT growth, two years later, the Brazilian Fair Trade Work Group was instated, composed by government entities and civil society entities, aimed to develop a proposal to create a national Fair Trade system. From those efforts the National System of Solidary and Fair Trade – or Sistema Nacional de Comércio Justo e Solidário (SCJS) – was officially created in 2008, aiming to regulate and guide the "production of basic justice and solidarity."

In 2010 the National Bureau of Economic Solidarity found that in Brazil there are about 23,000 enterprises related either to Fair Trade or Solidarity Economy or to both. These enterprises generate 2 million jobs, present in 51% of Brazilian municipalities, moving approximately \$ 5 billion per year. As proposed, the National Fair Trade System (SCJS) should be a planning system of parameters that define trade, rules and the participants of Fair Trade system in Brazil. In addition it provides a national identity to the concept and the possibility to identify products and disseminate processes that meet minimum standards (MTE, 2010). Also, according to Rosemary Gomes, state secretary of Rio de Janeiro Solidarity Economy, it is the role of State to "...regulate, supervise and create public policies fostering solidarity economy" (SEBRAE, 2010).

More recently, in November 2010, it was established within the Ministry of Labor, the National System of Fair Trade, which is in charge of coordinating the Federal Government's actions to the recognition of Fair Trade practices and its promotion. Under the proposal states, municipalities and Federal District, economic enterprises, accreditation bodies may join the system voluntarily. Among the objectives are: 1. To strengthen the national identity of Fair Trade; 2. To encourage the practice of fair pricing; 3. To publicize activities of organizations that respect the norms of the system; 4. To subsidize enterprises and organizations through the national information base; 5. To contribute to promotional efforts of public and private actions; 6. To encourage economic cooperation between enterprises in solidarity, and support processes of consumer education. The Committee shall be composed of a representative of three ministries - Labor, Agricultural Development and Social Development and Hunger - plus members representatives of civil society. They may attend meetings of the Committee, and representatives are invited from other agencies and governmental entities, institutions of international cooperation, individuals and representatives of legal entities. The expenses necessary to conduct the activities of the Committee, as well as those resulting from projects implementation will come from budgetary allocations themselves consigned annually in the budgets of the ministries that comprise it.

It is also important to highlight the efforts of the Forum of Joint Articulation for Ethic and Solidarity Brazilian Trade (Faces of Brazil), which brings together networks of small producers, non-governmental organizations and public and private organizations and supports productive initiatives such as SEBRAE (Brazilian Agency for Entrepreneurship and Small Business) (FATOR, 2008). SEBRAE, besides its conventional activities of supporting entrepreneurs in training and market research has selected organizations with the greatest potential to adapt to the proposal, to support and monitor the projects certification on projects

that can be legalized in the form of cooperatives, associations or solidarity companies – in a parallel movement to the Solidarity Economy.

Another important topic is the initiative led by the Instituto Faces do Brasil<sup>5</sup>, which sent a project to the Brazilian Ministry of Labor, proposing the recognition and support from the government for the sale of certified products inside Brazil – in this case the country would be the first to legitimize FT as a national policy (Sobral, 2009). Therefore, the Brazilian agricultural and handicraft certified goods could be recognized inside the country through incentive of public policies, and outside the country by the FT movement's efforts.

### **3.1 A Case Related to FT in the Brazilian Agriculture: The Guarana**

In the Amazon, in the municipality of Urucará, producers of guarana<sup>6</sup> used to produce in isolated efforts. Then, in 2001, they opted to form the cooperative AGROFRUT. Instead of commercializing and delivering products separately, producers changed to a collective decision process and shared commercial and administrative costs.

Soon the better results started as the market and orders grew, and so the requirements for product improvement and quality. As an answer to the market the producers started to look for alternative ways of reaching higher level of productivity and quality. The European

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<sup>5</sup> Institute founded in 2001, by an articulation of public and private Brazilian organizations, historically contextualized in promoting the production based on solidarity principles, which believed the concept of Fair Trade to be a real possibility for expansion and improvement of trade relations based on solidarity.( [www.facesdobrasil.org.br/conhecaafaces.html](http://www.facesdobrasil.org.br/conhecaafaces.html))

<sup>6</sup> A Brazilian seed which mostly grow in the Amazon region. It is usually sold in different conditions as raw, powder, syrup and soda. In Brazil it is one of the most sold soda's flavor.

market<sup>7</sup> started to demand organic products, which resulted in changing production processes and, in 2005, culminated to the change for the organic production. Thus, AGROFRUT converted its production process and gradually began to develop activities focused on maintaining two segments: organic and non-organic – organic being the mostly exported and the surplus sold in the domestic market. Among the changes, the certification for organics demanded a series of adjustments and efforts focused on training and seeking for new and better ways to produce in smaller spaces. Due to the previous efforts, in 2007 they were certified as in accordance to Fair Trade.

Currently from the total volume produced - 40 tons -, only 2.5% is directed to the FT market. In comparison to the conventional or not certified products, the expectation is that in short-term returns of the FT are more visible in the social and environmental, as the financial return should be the result of increasing effective demand in the long term. The board of the cooperative believes that "a good project is the one that puts money in the hands of producer," i.e., the one that pays an amount equivalent to the work.

An important fact from the cooperative's learning is aided in its director's assertion that "there is no point for saying that something is Fair Trade if the money does not reach the hand of producer." So there is awareness about the need that all are benefited by the cooperative's productive activities. However, Fair Trade for this association is understood as "one more label", as the processes demanded as already part of daily association, independent from external demand for FT. The biggest change occurred due the suitability for organic production. Thus, there is the understanding that the most relevant label is organic and Fair Trade is a market.

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<sup>7</sup> Specially in Italy and France.

Among the main consequences related to FT, the organization did reach the external market and raised the price of guarana<sup>8</sup> and, also began to develop social projects<sup>9</sup>, raised the awareness about manufacturing methods and environment<sup>10</sup>, started providing financial worksheets to clients including data about non-felling of forests and use of space, and others<sup>11</sup>. Among the innovations that were developed were spreadsheets of the breakdown of costs, efforts to change the requirements for bank financing and plans for economic activity diversification.

The spreadsheets with costs of production decomposition were created as tools to develop transparency in negotiation between producer and traders. They consist of total costs – production, taxes, packing, maintenance of cooperative, transportation and others – and leading to a tripartite agreement – combining costs of production, marketing costs and prices paid by the consumer.

Bank funding efforts were made by changing the current practices in the country's largest bank: Banco do Brasil (BB). As reported, BB used to replicate models of projects, spreadsheets and cost allocation that were successful in other regions - mainly in South and Southeast - without regard to regionalism and adaptations to the needs from Amazonas. So the producers were forced to buy inputs unnecessary or inappropriate to their needs. During

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<sup>8</sup> Before, the production used to be sold after the harvest – for US\$ 4,7 per kilo – and in the past two years the production price is stable by a higher value – ranging from US\$ 11 and US\$15 per kilo. Nowadays, before there is a meeting to set the value of production – which is compared to market prices and production costs - granting of financing and setting of minimum prices. The final figure depends on negotiations, which is accompanied by the producers in a participatory manner.

<sup>9</sup> Such as inclusion of women on toasting of guarana and production of handicrafts, training of young leaderships for the creation of new cooperatives, sustainable production techniques, and others.

<sup>10</sup> As quoted by the representatives of this cooperative: “There is no point in producing organics if your neighbor does not... It will contaminate your production, water and soil.”

<sup>11</sup> As spillovers from theft on this cooperative, the surrounding producers, not certified, also forced middlemen to higher the price paid for production.

the certification process it was observed that many producers were stocking inputs - such as insecticides - with the final product and did not use them - wasting resources and risking contaminate of the product. So, from 2003 the cooperative suspended requests for financing, to pressure the banks to adjust the sheets. During a period of five years there has been a restructuring process in granting loans to farmers. Thus, from 2008 loans started to be carried out in accordance with the actual needs of producers of guarana which no longer included requirements to buy chemical pesticides, and thus targeting the production of organic and recovery of already degraded areas.

With improvements and market consolidation, projects for diversification of economic activity were developed, but not yet implemented - with production of guarana intercropped with other crops, such as fishing in captivity and plantation and processing of fruit's pulp. Thereunto, efforts are being developed to suit the producer's conditions and infrastructure – aiming producing and processing - to market needs, balancing the use of opportunities - such credit offered by the National Bank for Development (BNDES) <sup>12</sup>.

In trade context, the most notable change was that before the biggest client, AMBEV – the biggest beverage producer in Brazil - dominated the market dictating the price. Nowadays, with the new price for products derived from guarana there is still a great force from large enterprises, but the price is no longer determined by them, as there is the possibility of either negotiate for margins that are favorable to both parties or to direct the product to different segments. Likewise, the relationship between the cooperative and the company was improved, emerging in proposals to develop work and techniques such as farming and organic

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<sup>12</sup> In this case, there is a curious fact related to the need on the municipal level, but the council has no resources and the cooperative has no intention of become dependent of changes in public management policies variation – fact which leads to an understanding of an existing of lack of credibility on government.

production and financing of the harvest. Before, the cooperative would need to ask AMBEV for financial support in addition to pay the costs of product distribution. Today, the cooperative is self-sufficient in financial terms and the situation is the opposite, as the purchasing manager goes to the cooperative, by boat (only mode of transport in the region) to negotiate amounts and pay for the transportation of products.

Another important aspect is the awareness on the part of small producers about the need for interaction with domestic and external markets. With the European market crisis it was necessary to adjust behavior, targeting surplus to the domestic market, but with a higher price that suits the needs of short run capital and to avoid price swings.

Also, as consequence of certification, some conflicts arose, such as consumer resistance to understand and accept FT, diversity in certifications, saturated markets, costs of certification, size of market, role of distributor, costs of transportation – which follow in a brief description:

- a) The consumer is the person who has the power to put pressure on retailers to offer specific products to the public. However, many consumers who previously supported FT stopped buying this kind of product as they understood that FT has become a fuzzy concept, used mostly as a marketing tool and they were being charged a higher price, but without the actual benefit for the producing communities.
- b) Due to the possibility of establishing several organizations named as FT, some companies created their own certifications and certified themselves, so rules can be circumvented and the FT concept undermined.
- c) The market saturation, for instance can be seen in the French market where given the existence of many FT certifiers, there is the difficulty of differentiating the seals and their practices.



- d) The cost of certification is high for small producers, restricting the access of farmers and turning FT into a market and marketing tool.
- e) The label allows the existence of a differentiated market niche, representing higher sales, but still not significant in volume.
- f) There is the elimination of the middleman, but it follows the necessity of the distributor, which has less impact on the profits, but which in practice often leads to distortion of the FT concept.
- g) Cost of product's transportation is a big concern as there is a restriction in terms of structural characteristics of the region, such as "in the Amazon the distance is not measured in miles, but in hours of travel" – as reported by the cooperative's director. Thus, the product takes about a month to arrive to France.

Among the pros and cons, in general, there is the belief in the cooperative that the greatest deficiency is that FT is still a limited market and has a small demand, but which the results and prospects are better than the general market. "The pros are bigger than the cons", as there is the benefit the cooperative members together can be powerful - to reduce costs, negotiate prices, exclude the middlemen - and customers can indirectly contribute for the improvement of life in rural areas – as quoted by the director of this cooperative.

#### **4. The Potential Pros and Cons of Fair Trade in Brazilian Economy**

From the conjunction between theoretical background and empirical practice in the guarana case, this section begins to analyze the potential pros and cons of Fair Trade in the Brazilian economy. The analysis is based on the division and separated consideration about

different groups of actors such as producers, workers, consumers, government and the nation overall<sup>13</sup>.

**a) Producers**

As mentioned earlier, producers are the beneficiary group for which Fair Trade is created. Thus, it is expected that this group is the one to have more benefits effects than other groups. Among the main pros to be listed on this group are the opportunities to sell for higher and standardized minimum prices, elimination of middlemen, capacity building, higher market differentiation, new consumer perceptions about products and consumer's willingness to pay higher prices due to compliance to either social or environmental standards. Among the cons are the uses of FT certification as an excuse to charge higher prices without further social environmental benefits, unfair division of profits, differentiated forms of control over producers, new entry barriers for specific markets, *fairwashing* practices, small size of market and incentives to cheat on FT principles.

By definition, the FT price has to be equivalent to a minimum price that is sufficient to cover at least production cost and that does not float along the production season. So FT allows producers to reach a market in which the price is usually higher than the autarky, due to the FT premium price. Therefore, price becomes a good argument for producers to engage in this certification, as proposed the production costs are covered either by the minimum price or by the pre-financing of up to 60% from the buyers. However, FT may also become an argument for entering a new market only seeking for higher profits, rather than social or environmental concerns.

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<sup>13</sup> Workers are here considered as a specific group, which not necessarily the producers, as they will not always be the owners of production resources.

Another financial benefit is due to the elimination of the middleman, as normally this person would keep a representative portion of the profits from commercial activities. Now the profits are directly transferred to producers. However, as pointed out in the case of guarana, sometimes even though a higher price is charged fair profit division may not happen – in that case competitors would transfer only 20% of final price to the producers<sup>14</sup>.

Capacity building, in Brazilian FT, allows small producers to improve production techniques, reach higher efficiency levels and learn about management skills. Thus, due to the progressive increasing of FT productive standards, capacity building allows producers to learn new issues, reach minimum standards and to get more conscious about production management. From this perspective there is no con, even though some people believe that capacity building is an opportunity to impose control throughout behaviors and beliefs.

Certifications, as FT, allow companies and producers to reach a higher market differentiation and become more competitive as they are proofs of accordance with distinguishable practices. As quoted by Conroy (2007: 292) certifications are incentives “...for companies through the demonstration that higher social and environmental standards are economically possible in the regulatory structure; and they then have an incentive to see regulatory standards raised, rather than find themselves undercut by less responsible competitors.” In the meantime, Friedman (2002: 148-149) believes that it “... almost inevitably becomes a tool in the hands of a special producer group to obtain a monopoly position at the expense of the rest of the public. The result is invariably control over entry by members of the occupation itself and hence the establishment of a monopoly position.” Thus,

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<sup>14</sup> Mohan (2010: 30) points out that “...The Fair Trade model proposes trade that is as direct as possible, eliminating unnecessary ‘middlemen’ between importers and producers. But the capacity of Fair Trade to reduce the number of intermediaries is questionable. Local intermediaries have been the traditional means of access for most small producers, and for many Fair Trade producers these have been replaced by producer organizations.”

the aim for differentiation may lead to the use of certifications as ways to guarantee lower access to differentiated market niches and so monopoly positions.

Certifications that focus on social and environmental concerns have the potential to add a value that is hardly measurable. In the FT segment a fetish is created around the buying process to make potential customers not just understand FT products as a commodities, but as something with differentiated value (Hudson and Hudson, 2003). Standards reduce transaction costs, confusion and complications in the domestic and international trade, enabling the strategy shift from competition based on price (Hendrickson et al, 2008), so for large companies FT has turned to a market opportunity. However, the relationship with large enterprises suggests that due to the negotiation of sales in large volumes, the price reduction occurs, generating incentives for cheating<sup>15</sup> and the so called *fairwashing* practices<sup>16</sup>. Therefore, in medium or long term the relationship with between FT producers and FT consumers - who until then consumed them due to the concept of justice – might be affected (RENARD, 2005). Another point is due to the fact that certifications may require changes in productive processes that would neglect cultural aspects and particular social and economical characteristics of localities.

The final point is that FT market is pretty much dependent on consumers willingness to pay higher prices due to compliance to either social or environmental standards – or both. At the same time that there is a propensity to reach higher prices, there is still the possibility to reach a smaller volume of consumers and the need for higher efforts to make as potential consciousness about FT. Therefore, whether market size is not big enough to afford producers

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<sup>15</sup> As advised by Suranovic (2007) in order to reach FT compliance to standards and profit maximization is not compatible to FT practices as the main objective for FT is to raise the wages of workers.

<sup>16</sup> Use of FT label as a marketing tool, but without real compliance to FT practices.

needs of selling or the costs of advertising are too high, then the FT objectives may be threatened by traditional practices of trade.

#### **b) Workers**

Even though in small producer's units, most of the time workers or their relatives are also the owners of productive resources - when production is a consequence of familiar agriculture -. However, it is important to consider them as a different group, as they may not be part of one of the mentioned classifications – and so be dependent on producers decisions. Among the benefits for workers are the higher wages, formal jobs, safety issues and working conditions, fair gender inclusion and exclusion of infant work. Among the cons in FT for workers are the payments of wages for other workers in the FT certification system, dependency on the government's ability to turn social security into a real benefit, higher productive costs in the short run, conflicts with local culture and the aim for present incomes rather than future improvements.

In the FT thesis, workers should also be the beneficiaries of FT, as among the objectives are the raising of workers' wages. The payment of higher wages should allow workers to live in at least the minimum acceptable standards of living conditions, generating social benefits and spillovers. However, Suranovic (2007) points out that if FT needs to be costly advertised, then the money that supposedly should go to production workers wages will be used to pay the salaries of other socially conscious activists involved in the promotion of these products. Then, the benefits from the premium that should be delivered to FT workers could go to the payment of other actors also involved within the certification system.

As FT requires that businesses and workers are legally registered, it gives to workers the opportunity of being introduced in to formal jobs. The fact that workers are registered allow them to have access to social security, and thus to have theoretically better social opportunities in the future. However, social security is pretty much dependent on the government's ability to turn it in to a real future benefit for contributors.

Certifications include standards of safety which in many cases requires adaptations from producers in order to reach them and so better working conditions. These requirements may lead to change in productive practices and technologies, which in the short term would represent an increase in productive costs.

Also, throughout the requirement of equal treatment among genders, women are gradually included in economic activities – which sometimes are basically created in order to reach the requirement for inclusion. However, due to local cultural practices the real inclusion and equal treatment may not be a total reality as there is not such a requirement to include women into the decision boards.

The requirement for excluding children from work and productivity activities is also a plus derived from the FT certification, as children cannot be part of the workforce and then are supposed to go to school and increase opportunities for a better future. In this case, families may not understand it as a benefit as they might aim for present incomes rather than future uncertain improvements in living conditions.

**c) Consumers**

If we consider that FT aims to be a contribution for producers to reach international markets, then consumers would not be affected by FT practices. However, it is important to consider that FT products, in Brazil, are produced aiming to reach to both domestic and international markets. Therefore, Brazilian consumers would just be impacted if FT in fact becomes a domestic practice<sup>17</sup> and, as a market oriented movement, that only is possible to be maintained if consumers agree to pay for it. The redistribution effect would be dependent on the consumers decision.

For consumers the main benefit would be the opportunity of choosing products that comply with their personal beliefs, quality standards and also in accordance to consumer's willingness to pay. Below follows a brief explanation:

“We can think of consumer preferences in two ways. First, we might imagine that consumers, especially those in wealthier developed countries, have an underlying, and unsatisfied, desire to purchase products knowing that their production did not exploit workers. In other words, consumers may have always had demand for socially just products, but in the past they were never able to identify them. In this case fair trade agencies need do little more than get the word out. Their task is merely to communicate, to spread information, about the availability of these products so that consumers can quench their unrequited desires... however, if the fair trade wage level, determined by the fair trade organizations is too generous it may exceed consumers' willingness to pay.” (SURANOVIC, 2007)

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<sup>1717</sup> Brazilian producers aim also to sell FT products in the domestic market. However, the demand size for socially and environmentally responsible practices and consumer's propensity to pay higher prices are still too small.

However, due to the possible information asymmetry, as justice is an attribute that consumers may not be able to check. Thus, as consumers may not get all the information they would like about production processes, sometimes they may feel that they are being cheated. In this case, consumers would feel hurt as they would pay higher prices without feel that they got an equivalent benefit from this buying.

#### **d) Government**

For the government there will be more pros than cons derived from FT's depending on the level of involvement it decides to have. Among the main pros are the higher level of taxes collected and the higher inclusion of workers in the social security. From the cons, as mentioned, are the needs for regulatory efforts depending on the level of direct involvement with FT.

As a requirement of FT certification's businesses and workers have to be included in the formal system. From this inclusion government has the possibility of increasing the number of tax payers and so the tax revenue – even if applying differentiated and lower rates for small producers and their workers. More people will be working formally and paying taxes, even if at lower rates. Also, if FT proposes that the redistribution effect would be dependent on the consumer's decision, and then there would be the possibility of need fewer subsidies from the government would be required and so there could be a change in the use of money from tax payers.

Due to the increase of requirements, then formalized businesses and jobs would lead to the similar need of more strict practices from government. Then making as business's practices keep sticking to regulatory standards. To fight against cheating will require



additional resources to clarify the legitimate labels or government intervention to enforce and regulate the system (SURANOVIC, 2007). Thus, the government should measure the potential benefits and limits of getting involved with FT – and so the consequent benefits for the overall population.

**e) Overall – welfare effect**

For the overall nation the adoption of FT, from the economic perspective, would mostly be derived from the generation of positive externalities on social and environmental issues, such as more sustainable production techniques and redistribution of wealth.

The first contribution is due to the fact that giving incentives to turn economic activities in to formal jobs and business, FT then helps governments to solve some of the “Five mysteries of capital” quoted by De Soto (2000), such as missing information, capital, political awareness and legal failure<sup>18</sup>. As pointed out by the author, the missing information is a consequence that in developing countries it is very difficult to businesses to become and stay legal, and so the undercapitalized economy turns into the greater part of wealth of these societies – about 80%. Another problem is that capital is born in formal property, capturing, organizing and controlling all the relevant information to conceptualize the potential value descriptions and allows stimulating businesses strategies. The legal system allows entrepreneurs to cooperate and produce large amounts of surplus value in an expanded market, inviting both the creation of larger networks and the collection of the missing data about extralegal system – the networks that normally are ruled by established social contracts.

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<sup>18</sup> The fifth mystery is related to the missing lesson of U.S history.

The exclusion of infant work can be a contribution to the improvement of the nation's future, as then children can turn their time and efforts to learning and their own development. However, it only can be possible if their families have ways to afford a new reality in which children no longer contribute economically and in addition require resources for the desired development – such as schools close to their homes.

The contribution from environmental concerns is mainly a consequence of the introduction of organic production. Turning production into organic reduces the possibilities of polluting - water, soil and air – and also the possibilities of workers and producers contract sickness - as those derived from contamination by pesticides. The con on this situation is that the effectiveness of organic production is dependent on producer's neighborhood's adoption of organic production too.

As a market niche FT can be a possibility of advocacy-based certification systems that "... fill a governance need beyond what local and national regulation can achieve, especially under the current rules of the World Trade Organization (Conroy, 2007: 292)". Thus, consumers would be able to choose which companies are closer to their interests. In theory, the market growth would provide a critical gap for the promotion of human rights (LYON, 2007).

However, by just leaving the entire power on consumer's hands could also lead to the lowering of standards, if consumers are not aware enough about social and environmental problems and more concerned about prices. In this case FT would not be any effective. Then, to get positive results from FT could only be reached if in conjunction of efforts from different actors, as "... neither governments nor corporations acting alone are likely to protect, much less build our global commons. (Conroy, 2007: 41) ”

## 5. Final remarks

The objective of this paper was to analyze the implications of Fair Trade in the Brazilian economy – especially the agricultural sector – by focusing on two basic questions: 1. Is Fair Trade really a good policy for the Brazilian economy? 2. Should the government have to get involved directly with the Fair Trade certification? To reach the conclusion, the methodology included theoretical and empirical data<sup>19</sup>.

Answering the first question, it seems that FT certification would most directly impact and benefit producers' and workers' lives by changing processes and routines and providing better living conditions and possibilities of participation on markets. The benefits are mostly a consequence of the fact that cooperatives, together with FT networks, can help to solve problems due to the fact that perfect information is not a reality. Thus, FT provides to producers different alternatives and sources for sales. FT solves a market problem related to lack of information from the small producers' side, giving higher power and better conditions for small producers to negotiate and help to end the middlemen's monopsony of power. The power goes to cooperatives by higher access to information and networks. The government would also be benefited, because by giving incentives to bring businesses and workers to the formal sector it would also increase the government's revenues. To the society FT may contribute in long the term by allowing a better maintenance of social and environmental standards.

The second question is a little more complex to answer. Today FT is organized and regulated by civil society and producers. So, if FT can be maintained by private efforts, then the government does not need to get directly involved. If the government gets directly involved with the FT's regulatory process, then it is no longer a voluntary process. Thus, the

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<sup>19</sup> Interviews with members of private and public sectors and secondary data – mostly from those available at the internet.

government's role would be related to caring about regulatory concerns related to economic, social and environmental processes.

In the economic arena the main concern is related to the suggestion of De Soto (2000), about the need for recognition of property rights as a political necessity, an ingredient of macroeconomic and market reform programs. So, government should provide producers with adequate tools to have formal property universally accessible. Besides that, the government should make real efforts to create a tax system more adequate to the reality of small and medium producers; to offer training to workers and producers; to provide micro and small producers with higher, better and adequate access to credit; give to producer's families that children do not have to work; provide rural areas with better infrastructure, transportation conditions, communication and access to information; provide producers - and society - with complete and updated information about trade and notably about FT – separate from the Solidarity Economy.

In the social area the government should adapt laws to the needs of the country, by creating laws that are compatible to the needs of producers and workers. By, giving producers incentives to formalize workers, then gives to the workers the opportunity to get access to social security. Also, it should be the role of government to enforce laws related to underage workers and create the respect of formal jobs and the provision of reasonable working conditions.

In the environmental area the government should give incentives to increase organic and sustainable production, and also to develop environmental awareness through education – to both consumer and producers -, and as consequence to promote the reduction of pollution.

Apart from the above aspects, it should also be the government's concern to make sure that FT does not become another legal barrier for small producers, trade and exports. So this

certification should not be a tool for exclusion, as it is the objective of FT to include small producers in the market that is traditionally dominated by transnationals. Otherwise, FT instead of giving contributions for trade promotion, could create limitations for exports somehow. As quoted by Mohan (2010: 54) “The impact of Fair Trade is limited not only by the movement’s size but also by its narrow scope. The costs and other difficulties in becoming Fair Trade certified are constraints on the expansion of the Fair Trade market and its ability to target the poorest”. So, if FT becomes a barrier, then it does not accomplish its goal – neither does the country.

Also, by analyzing the pros and cons of FT, the preliminary conclusion is that, if it becomes related to domestic policies there is a possibility of diminishing the need for trade policies. When you give to the consumers the choice to pay the extra cost, then it reduces the need for subsidies. However, FT only will contribute to the producer and overall society welfare if the size and market demand are large enough. In these way, government interventions on trade policies are necessary and the FT is less effective.

It is important to highlight the explanation of one of the interviewees who points out that FT should add value to production and not costs. If FT aggregates costs, then it may place limits access to markets and also to redistribute wealth. But, if it is shown to be a viable trade that creates jobs, adds value, and gives incentives to the industry, then there is a reason for FT to be promoted and become part of public policies - since it helps national development. Today, the concern of Brazilian the government is to make the country maintain its level of industrialization, not remaining as an exporter of commodities. If FT contributes to this policy, there will be government interest – especially considering that agriculture is historically the biggest economic sector within the country. Another topic raised by interviewee B is that if the country gives incentives to FT then there is the possibility that the country connects its image to the social benefits. So, if the government decides to approach

FT proposals – as it did -, then it should make efforts to not allow coordination failures (Hausmann, Bailey and Wagner, 2008) and to end the vicious cycles of underdevelopment (Todaro and Smith, 2009).

After addressing the previous questions, some other questions for further research had been raised: 1. Should FT and economic solidarity be considered the same thing? 2. How effective can a policy be, if it is imposed by external agents that make small producers change their cultural and productive realities? 3. What are the possibilities that small producers´ have to track products and finance the productive processes? 4. How can standards of fairness and justice be set in a way that “one size fits all”?

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