
Fiji and the Sugar Protocol: A Case for Trade-Based Development Co-operation

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Development co-operation can take several forms. One important form is concessional aid, namely, a transfer from a donor to a recipient. Multilateral and bilateral donors and national governments all agree that, from the standpoint of the recipient, this form of development co-operation is the pre-eminent way to acquire foreign exchange. Moreover, from the point of view of the donor, concessional aid may be a superior form of development co-operation because it can be better targeted in line with donor priorities such as poverty alleviation or private sector development. Concessional aid is thus the usually preferred form of development co-operation: it is a cost-effective way of easing foreign-exchange and savings gaps.

This article takes a contrary position. It argues that, in the specific case of Fiji, trade is a more effective form of development co-operation. Indeed, in the specific case of Fiji's sugar sector, it argues that the social efficiency gains fostered by trade can be used to sustain a case for preferential market access. Admittedly, trade and aid should be seen as complementary forms of development co-operation. However, this does not mean that both forms are equally effective in all circumstances. It is therefore of interest to investigate the circumstances under which trade may be comparatively more effective. The article is organised as follows. After outlining the role of sugar in the Fiji economy, the Sugar Protocol, under which a substantial portion of Fiji's sugar is traded, is introduced and its economic and social impacts are considered. The comparative merits of trade and aid as complementary yet contrasting forms of development co-operation for the Fiji economy are then examined, and it is argued that the Sugar Protocol is an appropriate means by which trade-based development co-operation can be channelled to Fiji. In the light of the previous discussion, the strategic issues confronting Fiji's sugar sector in the medium and long term and the prospects for trade-led restructuring in the sector are then discussed.

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Sugar in Fiji's Economy

The sugar sector

Fiji is one of the largest Pacific island countries. With a per capita GNP in 1993 of US\$2,130, it is classified by the World Bank as a lower-middle-income developing country. Further, with an average life expectancy of 71 years, infant mortality of approximately 22 per thousand, and an 89% adult literacy rate, Fiji has a high level of social development (UNICEF, 1996). For most of the period since its independence in 1970 Fiji has pursued an employment-oriented development strategy focused on the continued exploitation of its natural resources. As a consequence, agriculture has been and continues to be a major area of economic activity.

Table 1
Fiji agrarian indicators, 1980–92

<i>Year</i>	<i>GNP per capita</i> (US\$)	<i>GDP growth per year</i> (%)	<i>Trade deficit in GDP</i> (%)	<i>Agri-culture in GDP</i> (%)	<i>Sugar in GDP</i> (%)	<i>Sugar in exports</i> (%)
1980	1,750	-2	15	20	n/a	81
1985	1,650	-3	20	16	12	59
1986	1,740	8	14	19	16	55
1987	1,620	-7	4	21	13	56
1988	1,620	1	9	18	12	44
1989	1,780	14	12	17	13	41
1990	1,860	5	21	20	11	37
1991	1,920	1	15	20	11	40
1992	2,010	3	14	20	11	41

Note: GDP growth per year is in constant prices.

Source: World Bank, 1995a; Fiji Bureau of Statistics, various issues; Reserve Bank of Fiji, various issues.

Table 1 provides some indicators of the role of agricultural production in the Fiji economy. It demonstrates that agriculture has provided around a fifth of GDP. In addition, agriculture remains a major employer: more than 75% of all

households work on a full- or part-time basis in crop production, livestock, forestry and fisheries (World Bank, 1995b). Since its introduction in the 1880s sugarcane farming and processing has dominated commercial agricultural activity. Although the significance of sugarcane farming has declined somewhat in recent years, the sugar industry as a whole was worth approximately F\$320m. in 1995 — more than 12% of GDP. Sugarcane farming accounted for more than 40% of the total agricultural sector in 1995. Moreover, sugarcane processing accounted for almost 30% of the total manufacturing sector in 1995 (Fiji Bureau of Statistics, various issues: Table 3.3). At the same time, sugarcane farming and processing remains the largest single source of employment in Fiji. Sugar provides direct employment for more than 25% of the economically active population. Moreover, while it is no longer the country's largest foreign-exchange earner, it provided some 40% of exports by value in 1992 and as such made a major contribution to easing the trade constraint that Fiji's small open economy faces. In sum, sugarcane farming and processing remains the most important component of the Fiji economy. Admittedly, garment manufacturing and tourism have been of increasing importance in recent years. However, the long-term outlook for the garment industry is problematic (Akram-Lodhi, 1992a), while tourism has been subject to significant cyclical oscillations (Akram-Lodhi, 1996).

In 1993 sugarcane farming in Fiji was carried out on 23,454 registered farms. According to the World Bank (1995b), the average size of a sugarcane farm was 4.2 hectares. The average area harvested was 3.11 ha, the average cane yield was 48 tonnes per ha, and the average gross revenue received was F\$8,314. Most sugarcane farms are thus small production units. Operating for most of the year with only household labour, 61% of sugarcane farms produce on average less than 150 tonnes of cane per year. Moreover, 24% of sugarcane farms have operational holdings of 1 ha or less and produce on average 50 tonnes or less of cane a year.

Sugarcane farming is subject to long production cycles, inflexible allocation of resources and the uncertainty of the weather. In Fiji, production uses self-provided seed cane, animal draught power and limited quantities of agro-chemical fertilisers. In addition to family labour, hired labour is used during the harvesting season. Cane harvesting is performed manually under a complex gang system which involves farmers working alongside some 13,500 seasonal harvesters, many of whom are landless migrants. Cane harvesters receive an average rate of F\$7.50 for every tonne of cane cut, which translates into an average daily wage of approximately F\$8.50, almost 40% below the mean average for all industries. However, in addition to wage costs the farmer hiring the harvesters often bears the cost of providing housing and meals for the temporary labour.

Sugarcane is processed into raw sugar at mills owned by the Fiji Sugar Corporation (FSC), a publicly listed company in which the government owns

70% of the shares. Four mills are capable of producing 500,000 tonnes of sugar a year. The FSC also possesses storage and handling facilities. The earnings which accrue to farmers and the FSC from processing are based on an average price earned from sugar sales in all markets, after some deductions for certain costs. Farmers receive an average of 72% of the processing proceeds in four payments; the remaining 28% goes to the mill.

Sugar marketing is performed by the Fiji Sugar Marketing Company, a government-owned company funded by a commission on the export sales of sugar. With only 1% of domestic production being consumed locally, almost all production is exported, the most important buyer being the UK transnational corporation, Tate & Lyle. Almost half (45%) of exports go to the European Union via the UK. Other significant markets include Malaysia, Japan, Singapore, South Korea, Canada and the United States.

Current issues in the sugar sector

The most important issue facing the sugar industry is that of access to land. Although only 260,000 ha are used for agricultural production, most of the land used for sugarcane is not owned by the farmers who work it, but is rented on long-term transferable leases of 30 years' duration, leases which define the way in which the land can be used. Indeed, some 83% of land in Fiji is communally owned by the indigenous Fijian population, which comprises just over half the population of the country. The foundation of communal ownership is that this land cannot be sold (Akram-Lodhi, 1997). By way of contrast, 70% of sugarcane farmers come from the Indo-Fijian community, descendants of the indentured labour brought to the archipelago by the British during the first third of the colonial period. Only 30% of sugarcane farmers come from the indigenous Fijian community. Thus, with the ownership of land residing within one community and the production of sugar largely within another, access to the land needed for sugar production has a complex ethnic dimension. This ethnic dimension is also found in other parts of the sugar industry. Cane cutters come from both the indigenous and the Indo-Fijian communities, while a majority of FSC employees come from the indigenous Fijian community.

Ethnic relationships have had a major impact on the country's economic development, particularly since independence. In seeking to exploit the country's natural resources, the government pursued a labour-intensive development strategy designed both to sustain economic opportunities and, more particularly, to maintain communal relations between the two communities. Indeed, the limited amount of economic diversification prior to the 1980s can be explained in part by the desire to maintain communal stability. However, in the early 1980s Fiji underwent a 'multidimensional crisis' (Cameron, 1994: 420) consisting of drought, cyclones, the 1979 oil price rise and an unusual degree of turbulence in the international sugar price. Economic crisis generated conflict

within Fiji society, conflict which often assumed an emotional ethnic dimension (Akram-Lodhi, 1992b). This in turn paved the way for two military coups in 1987, which polarised communities and in so doing led to a deterioration in ethnic relations. This deterioration was deeply felt within the sugar sector and has especially marked the issue of access to land.

There are currently some 30,000 leases administered by the Native Land Trust Board (NLTB) on behalf of the indigenous Fijian landowners. The rents paid by leasehold farmers are not determined by a land market, but are regulated by the Agricultural Landlord and Tenant Act (ALTA), which sets rents equal to 6% of the unimproved capital value of the land and then transfers the rents to the NLTB, whose operating expenses are covered by a deduction from the rents and a grant from the government. The unimproved capital value of the land is in theory determined every five years. Rents as a proportion of crop value vary tremendously. Conflicting data from the World Bank (1995b) and our own research (Prasad, 1995) suggest that rents for sugarcane land may vary from a low of F\$50 to a high of F\$350 per ha.

Leases under the ALTA framework began to expire in 1997. While only a small number actually expired in that year, farmers with leases expiring thereafter have found it very difficult to borrow against the remainder of their leases for two reasons. First, it is likely that rents will rise substantially in the near future. Secondly, the NLTB is currently following a practice of closely assessing the land requirements of the landowning units prior to considering renegotiation with tenants. This uncertainty about the extension of their tenure has made it difficult for some farmers to maintain production and more particularly productivity-enhancing farm investment. Given the importance of the agricultural sector in the overall pattern of economic activity, the inability to maintain efficiency-enhancing farm investment is a major concern.

There is an urgent need to enhance the efficiency of sugarcane farming and processing in Fiji. Ethnic relations within the sugar sector have undoubtedly held back restructuring and diversification in the past and contributed to an inability to sustain a competitive advantage. At the same time, the industry expanded rapidly in the 1970s and 1980s. Some of this expansion occurred outside the traditional sugarcane-growing areas. Such expansion into productive land was constrained by higher transportation costs, while expansion into less suitable land witnessed decreases in average yields and increases in the variability of production. In both cases, efficiency declined — a problem which was worsened by three interrelated factors. First, payment systems are based on the quantity rather than the quality of the cane produced. Secondly, payment systems do not preclude the burning of the cane fields, which, despite reducing the sugar content of the cane, is commonplace: in the period 1991–6 some 30% of the total tonnage processed was burnt. Thirdly, as a consequence of transport, mechanical and scheduling problems, Fiji has high cut-to-crush times; some 40% of cane takes more than 24 hours to crush (World Bank, 1995b). This

reduces the sugar content of the cane. However, it has minimal impact on the payment received by the farmer, which is based on quantity. As a consequence of these three factors, insufficient regard is given to the quality of the cane produced, which in turn acts as a disincentive vis-à-vis the modernisation of production and processing facilities.

Other problems compound this lack of attention to quality. The use of unimproved planting material rapidly diminishes productivity on sugarcane farms. The limited use of agro-chemical fertilisers hampers productivity gains. The research and extension system is weaker than it should be because of a loss of skilled labour and a decline in investment since the early 1980s. The cost of labour in sugarcane harvesting and processing is a comparatively high proportion of total costs, especially in the later stages of processing. The freight and insurance costs faced by Fiji are especially high, because of the country's comparative isolation from major markets. In addition, the relatively modest size of Fiji's sugar production and its limited domestic market for goods mean that the size of shipping serving Fiji is small and there is less two-way shipment, both of which serve to increase costs.

In 1997 a fragile constitutional and political settlement was reached by the leaders of the two main communities in Fiji. Such a settlement could have a positive impact on the sugar sector if confidence within the industry increases. Nonetheless, challenges remain. Undoubtedly the second most important issue facing the sugar sector, after that of access to land, is the prices received for its product. The mechanics of sugar pricing cannot be discussed without considering the Sugar Protocol.

The Sugar Protocol

The Sugar Protocol replaced the Commonwealth Sugar Agreement (CSA) of 1950. The CSA was a preferential agreement between the United Kingdom and Commonwealth countries whereby the UK guaranteed to purchase specified quantities of sugar for a negotiated price which in the period 1951–73 exceeded the world market price by an average 165% (cited in Herrmann and Weiss, 1995).

The CSA was incompatible with the foreign trade regulations of the then European Community (EC). Therefore, when the UK was negotiating its terms of accession it sought, in conjunction with pressure from the Africa, Caribbean and Pacific (ACP) states and Tate & Lyle, to have a new Community-wide preferential agreement for sugar agreed. The Sugar Protocol agreed between the EC and the ACP countries came into force in 1975 under the auspices of Protocol 3 of the Lomé Convention. Formally, the Sugar Protocol is independent of the Convention, with an unlimited duration. However, it can be denounced by its signatories if two years' notification is given.

Under Article 1 of the Protocol the EC agreed to import 'at guaranteed prices, specific quantities of cane sugar, raw or white, which originate in the ACP States and which these countries undertake to deliver to it'. Under Article 5 the price paid for this sugar is negotiated annually and is agreed to equal the price range obtained within the Community. Thus, subject to certain provisions, it can be stated that, as a consequence of the Protocol, the European Union (EU) applies to ACP sugar exporters its internal sugar regime, which determines production quotas, producer price guarantees and export subsidies. Article 3 of the Protocol stipulated the quota amount of sugar the EC agreed to import from specific ACP countries. Finally, under Article 7 any failure to deliver the agreed quantities of sugar results in a loss of quota equivalent to the shortfall. Any shortfall is then divided among the remaining ACP producers. The total preferential quota set for all the signatories was quantified in 1975 as being equivalent to 1.3 million tons of white sugar. This figure has not been changed as a consequence of sugar production exceeding consumption within the EU. It has, however, been periodically reallocated among the signatories to the Protocol.

The Sugar Protocol thus commits Fiji to deliver specific quantities of sugar to the EU at prices which are guaranteed and which are based on the price of sugar set annually under the CAP. In 1975 Fiji was allocated 163,600 metric tons, equivalent to 13.4% of the total preferential quota. Currently, it has a preferential quota of 165,348 tons, equivalent to 12.7% of the total quota. For the period 1990–2 Fiji's quota allocation amounted to an average 42% of its total sugar production and 46.6% of its total sugar exports. Fiji received a price averaging between 2.5 and 3 times the world market price for these exports.

EC enlargement to include Portugal resulted in supplementary preferential access for sugar to the European market which started in 1995 under the Special Preferential Sugars (SPS) agreement, designed to fulfil the EU refiners' deficit. Under the SPS the EU determines an additional annual preferential import quota based upon raw beet production in Portugal, production levels in the French Overseas Departments, and refiners' needs. The increased quota is first allocated among four countries which traditionally exported to Portugal: Côte d'Ivoire, Malawi, Swaziland and Zimbabwe. The balance is then shared on a pro-rata basis among the signatories of the Sugar Protocol.

The SPS price has been fixed for a 6-year period and is subject to renegotiation prior to its expiry. It is set at between 83 and 85% of the price ACP countries receive under the Sugar Protocol. Deducted from the price is a refiner's margin and a special reduced tariff which together amount to 8.1% of the price. This deduction is designed to assist the EU in complying with its international obligations under the Uruguay Round Agreement to reduce its levels of subsidy. The SPS is thus consistent with the EU's World Trade Organization (WTO) obligations.

In the first year of operation supplementary preferential access to the EU market under the SPS agreement amounted to 334,100 metric tons; under the pro-rata stipulations of the agreement Fiji exported 48,045 tons. The SPS thus provides Fiji with a further incentive to direct sales towards preferential markets.

In addition to the preferential prices it receives under the Sugar Protocol and the SPS, Fiji also has a small amount of quota access to the United States under the Generalized System of Preferences. This sugar is sold at preferential prices averaging between 1.5 and 2 times the world market price. However, US sugar imports have been declining over time and Fiji receives only 0.9% of the US quota. Thus, as long ago as 1988 Fiji's quota was only 9,000 tons. Fiji's remaining production is sold on the world market at the prevailing price, although the country has entered into long-term delivery agreements with Malaysia, Japan and Singapore.

The economic impact of the Sugar Protocol

The primary benefit for Fiji of the preferential quota arrangement under the Sugar Protocol has been twofold. First, the Common Agricultural Policy is designed to stabilise the living standards of Europe's farmers by providing support for agricultural production, distribution and marketing; European sugar production quotas are therefore agreed and European internal sugar prices stabilised. As the Sugar Protocol guarantees that its signatories receive the EU internal sugar price, Fiji obtains a price for its sugar which is usually in excess of the world market price. In the early 1990s the EU's price was roughly double the world market price. Secondly, as a major purpose of the CAP is to stabilise prices Fiji is subject to less fluctuation in the price it receives for the sugar it exports to the EU. Whereas in the period 1975–91 the world price varied year by year around its average to the order of 41%, the EU price varied by only 8.7%. The Sugar Protocol thus significantly reduced the variability of export earnings that a reliance on world market prices would have produced, by just under an estimated 40% (Herrmann and Weiss, 1995). Thus, the Sugar Protocol has been an important source of both price stability and sales security, factors which are of major importance to a country like Fiji which produces only a small percentage of the world's sugar.

These benefits to the Fiji economy can be seen in a range of areas: increased production, increased employment in the farm and mill sector, increased incomes for landowners, growers and millers, and the attendant impact that such increases in income have had on living standards in the sugar community. Such benefits arise as a consequence of the fact that the Sugar Protocol has been responsible for a transfer of income from the EU to Fiji. In aggregate, during the 1980s the transfer received by Fiji from the price subsidy implicit in the

Sugar Protocol has been estimated as being worth 3.72% of GDP (McDonald, 1996). In 1992 it was estimated to be worth F\$90 m. Such levels have been sustained over the life of the Protocol. Thus, over the period 1975–91 the average annual transfer to Fiji arising from the Sugar Protocol has been estimated at ECU 26.5 m, equivalent to an annual per capita transfer of some ECU 37.75 (Herrmann and Weiss, 1995). It is instructive to compare this transfer with the official development assistance received by Fiji between 1975 and 1995 from the European Development Fund — ECU 8.87 m per year, equivalent to an annual per capita assistance of some ECU 12. Thus, the Sugar Protocol generates transfers from the EU to Fiji some three times greater than that supplied under official development assistance.

The Sugar Protocol also has an economic impact in Europe. Unlike the sugar regime of the CAP, imports under the Sugar Protocol and the SPS are not self-financing. They fall within the export refund budget and thus have a cost beyond those transfers from consumers to producers which are a consequence of price support schemes. However, despite this cost the Sugar Protocol and the SPS have been of net benefit to European sugar producers and refiners. For producers, imports under the Sugar Protocol and the SPS affect European production levels agreed under the CAP. The amount imported under the Protocol and the SPS is currently equal to approximately 1.6 million tonnes. Under the terms of the CAP an equivalent amount of European production can be exported, with producers receiving a subsidy equal to the difference between the world and the European internal support prices. As a result of the Uruguay Round Agreement on Agriculture the value of subsidised exports must fall by 36% by the year 2000, using 1986–90 as a reference period for the value of subsidised exports. Further, the quantity of subsidised exports must fall by 21% by 2000. However, the 1.6 million tonnes exported by European producers as a consequence of ACP imports is exempted from the commitment to cut export subsidies. European producers are thus able to maintain exports of 1.6 million tonnes of sugar at a price higher than that for their remaining sugar exports. Since the conclusion of the Uruguay Round European producers have been better-off as a consequence of the Sugar Protocol.

For European refiners, the import of ACP sugar allows the refining sector to maintain its capacity utilisation, and in so doing reduces the per unit cost of refining.

The social impact of the Sugar Protocol in Fiji

The social benefits of the Sugar Protocol have been widely distributed across Fiji. This has helped moderate the level of poverty in rural areas and contributed to social stability throughout the country.

The nature of land arrangements in Fiji have in the past discouraged resource accumulation on the basis of land. The NLTB has a preference for lessees with single holdings. The consent of the NLTB and the Ministry of Lands is required for the transfer of land ownership. As a result, holdings remain largely fixed in size. Much of the expansion of farm acreage in the 1970s and 1980s was not so much a consequence of land reallocation but rather a result of the opening up of new, less productive lands in the existing sugar regions.

It would thus appear difficult for farmers to increase their wealth through resource accumulation. The World Bank has recently (1995b) suggested that 600 tons of cane generated an average annual net income of F\$13,000 in 1994. However, it would appear that only 250 farmers produced on average more than this amount of cane. The Bank has also suggested that growers producing less than 200 tons of cane are likely to be in poverty. Indeed, it appeared that in 1995 one in three rural households could be classed as living below the poverty line. Preferential prices have thus not been to the exclusive benefit of large farmers. Admittedly, they will have received a disproportionate share of the transfers generated by the Sugar Protocol. However, there are not that many large farmers. It can therefore be argued that the key beneficiaries of preferential prices have been smallholders. The remunerative prices provided by the Sugar Protocol have maintained social efficiency by promoting production and employment amongst the far more numerous smallholder farmers who would otherwise most probably have been unable to sustain the livelihood security of their households. Therefore, it is possible that the Sugar Protocol has acted as an employment-generating safety net for the one in three rural households living below the poverty line.

Moreover, for those growers on comparatively low incomes the long-term arrangements of the Sugar Protocol have allowed commercial borrowing, using crop liens to finance efficiency-enhancing capital improvements in agriculture. Indeed, long-term resource flows have been generated amongst the comparatively poor which facilitate the provision of education, health and housing needs. Admittedly, farmers have accumulated debt. For example, a 1992 Sugar Cane Growers Council study noted that sugar farmers had an average outstanding debt burden of F\$11,500 (Prasad, 1995). However, the social benefits generated by such loans mean that the primary negative impact of the debt should be seen as the constraint it creates upon the ability of farmers to take the risks associated with diversification.

Farmers have not been the only group to benefit from the Protocol. Wages for 13,500 seasonal cane harvesters depend in large part upon the ability of Fiji to sell its sugar to the EU under the Protocol. The World Bank (1995b) has argued that rural wage labour is one of the most impoverished groups in the country. The ability of this group to sell their main productive asset — their capacity to work — depends upon the Sugar Protocol. Similarly, in the milling sector high union densities and a well established industrial relations framework

have ensured that factory and field employees of the FSC have benefitted from both the preferential prices and the sales security guaranteed by the Protocol.

At the same time, the benefits have not been focused upon one community. Indigenous Fijian landowning groups have also benefitted. Higher prices for crops drive up the capital value of the land farmed, and will thus eventually drive up the rents paid. Any decline in sugar prices could affect land rentals and indigenous landowning groups. Moreover, sugar provides an important channel through which greater numbers of indigenous Fijians are being incorporated into the farming and milling sectors. The increase in the number of growers from 15,000 in 1975 to more than 23,000 in 1996 came not only from a restructuring of existing holdings but also from large numbers of indigenous Fijians utilising their traditional lands in existing sugar regions to enter the sector. The proportion of indigenous Fijians in sugarcane farming increased steadily after independence to more than 30% by the end of 1995. The Sugar Protocol has facilitated social and economic stability by its impact on farmers in the indigenous Fijian community, thus deepening the equity outcomes of preferential trade. A sharp decline in sugar prices would seriously affect this trend. Perhaps more importantly, it would also have an effect on relationships between the two main communities.

Overall, sugar income has been distributed across the sugar regions of the economy; while some have benefitted more than others, it can be argued that no one group in the countryside has benefitted disproportionately. In addition, the indirect contribution of sugar proceeds to such fields as education and health will have had benefits well outside the sugar region. The aggregate multiplier effects of the economic activity generated by the Sugar Protocol will have been spread outside the sugar region and across the country: the jobs and income generated will have facilitated increases in the effective demand for goods and services produced outside the sugar sector. Finally, and importantly, transfers which operate through transparent prices offer less scope for rent-seeking activity. Any decline in sugar incomes would therefore extend well beyond production, exports and employment in the sugar sector. It would affect the level of social development in the economy as a whole, and in so doing adversely impact upon the level of social efficiency in the Fiji economy.

Trade and aid

Fiji engages in international economic relations in order to increase national income. These relationships have the effect of increasing the level of foreign exchange available to the economy. This allows Fiji to overcome the problem of insufficient domestic savings, and to facilitate the domestic investment which enhances growth. By easing foreign-exchange scarcity, international economic relations increase Fiji's ability to purchase the investment and consumer goods

and services which the country requires but does not produce. In so doing, increases in welfare are promoted.

In Fiji, increasing inflows of foreign direct investment (FDI) have been significant in recent years (Akram-Lodhi, 1992a). However, in evaluating the efficacy of the Sugar Protocol it is helpful to set FDI to one side and to focus upon the other two general and complementary forms of international economic relationships. The first is official development assistance from bilateral and multilateral agencies; the second is international trade. Like FDI, both have the effect of easing the foreign-exchange and savings gaps which hinder the country's economic development. However, despite their complementary character it is a matter of some debate as to which of the two is the more effective form of international economic relationship for an economy such as Fiji.

At the most general level, if concessional aid is simply a free transfer from a donor then the value to Fiji of the foreign exchange received in this form will always exceed that of an equivalent amount of foreign exchange received from exports (Thirwall, 1976). This is because exports have additional associated costs which concessional aid does not: namely, the costs of transforming domestic resources into goods and services capable of being sold on world markets. Moreover, from the point of view of the donor, as already noted, concessional aid is a superior form of development co-operation because it can be better targeted in line with donor priorities. It is for this reason that many in the EU would like to transform the transfers Fiji currently receives under the Sugar Protocol into formal bilateral concessional aid.

However, in the case of Fiji concessional aid may be a less efficient means of transferring income as compared with trade. Yassin (1982) makes the point that in assessing the relative merits of trade and aid it is important to consider what Thirwall (1976: 40) called 'secondary repercussions'. The main secondary repercussions to be considered are in terms of the impact on savings and on productivity. The argument that aid cuts domestic savings was originally made by Griffin (1970). Subsequent work has dismissed it on both theoretical and empirical grounds (White, 1992). As regards the comparative impact on productivity, little work has been done. However, there may be reasons to believe that in the case of Fiji the productivity implications of exports may exceed those of concessional aid. The basis for such an argument is that, even though Fiji's exports remain dominated by a primary commodity, such exports nonetheless bring dynamic benefits that concessional aid does not.

In terms of the dynamic efficiency gains brought about by trade, there is the possibility of the country benefiting from economies of scale as the total market available to producers increases; this is certainly true in the sugar industry. Moreover, economies of scale have in the past facilitated growth-enhancing investment. Other dynamic gains from trade include the recognition that Fiji must produce internationally competitive goods. This acts as a discipline on

domestic producers to improve efficiency. It is certainly true that the Fiji sugar industry is aware of the importance of the international market for its growth and development. Another dynamic gain is the acquisition and dissemination of technical knowledge which permits efficiency improvements to flow from investment. Those in the Fiji sugar industry recognise that efficiency improvements necessitate the industry's modernisation, and that this in turn requires having access to productivity-enhancing international knowledge. Finally, trade-oriented economies demonstrate greater adaptability to changes in economic circumstances. Enhanced ability to be flexible is an important benefit of international trade. Thus, in terms of its respective merits, trade may enhance productivity, investment and growth in Fiji in a way which exceeds that to be obtained from an increase in its comparatively low levels of concessional aid.

In order to reap these gains Fiji needs market access. However, while many developed market economies seek to foster free trade in developing economies, they concurrently maintain restrictions on market access. Thus, free trade as such does not exist. Rather, arrangements for the movements of goods exist. Such arrangements can enhance the vulnerability of countries like Fiji, which produce primary commodities. They may be unable to sell their products freely and to garner the resources needed to fund diversification into more valuable processed goods. This constraint is compounded in the case of the European Union by the fact that the EU is the world's largest sugar exporter. While not as important as they once were, European sugar exports have had an impact on the world market price of sugar in the past and have thus acted to constrain the ability of Fiji farmers to compete. This has weakened Fiji's capacity to diversify.

Fiji needs to reduce its dependence on sugar by expanding into new agricultural products, and new sugar by-products, and by diversifying its manufacturing base. Admittedly, it could be argued that the impact of the Sugar Protocol in Fiji has been to block diversification by fostering a variant of 'Dutch disease'. Dutch disease occurs when increased inflows of external resources result in the price of non-tradeables rising in relation to the price of tradeables, with the effect of generating a rise in the real effective exchange rate, a decline in export competitiveness, and the possible onset of stagnation. It could be argued that the income transfers resulting from the Sugar Protocol might result in the operation of similar mechanisms. However, it is not clear whether Dutch disease is an appropriate analysis for Fiji. Theoretically, models of the impact of Dutch disease require full employment of resources (Karshenas, 1990). Such an assumption does not hold in the case of Fiji, where there is a large degree of slack in the labour market, particularly outside the sugarcane harvesting season. Moreover, the key variable in managing the transition process arising from the inflow of external resources in circumstances of a lack of full employment is that of the quality and timing of policy interventions. Policy interventions should seek to avoid the possibility of crowding out arising as a

result of the inflow of external resources. While not done for this particular reason, Fiji's devaluation of the nominal exchange rate in the late 1980s served to reduce the real effective exchange rate by almost 46% (Akram-Lodhi, 1996). The upward drift in the real effective exchange rate during the 1990s has been modest and has not negated the initial devaluation. This has served to limit the potential of the Sugar Protocol to foster Dutch disease during the 1990s. Indeed, there appears to be little pressure for further devaluation in those sectors which might benefit, particularly garments and tourism. Dutch disease is thus something of a non-issue; what is an issue is the continuing need of Fiji's farmers to generate the resources to diversify. Farmers must be able to sell their products and governments must assist in the diversification process. What is required is market access which gives Fiji's producers the resources capable of funding diversification and efficiency improvements, together with the time needed to adjust by restricting third-party competition. This is precisely what the Sugar Protocol currently accomplishes for Fiji. The Protocol is a form of trade-based official development assistance linked to a commercial agreement. In order for it to be able to continue to perform this role, there is a need to maintain preferential access to the European market.

The future of the sugar sector in Fiji

As we have seen, the Sugar Protocol has been an important source of price stability and sales security for Fiji. However, it is being argued by some in Fiji that the benefits of the Protocol for Fiji are likely to erode. Five reasons are commonly given. Scarce budgetary resources within the EU have led to pressures on the CAP sugar subsidy. Moreover, some people have argued that the EU's internal sugar price will start to fall in the wake of the Uruguay Round Agreement. In addition, it is possible that more US pressure will be exerted on the EU to cut subsidies further. At the same time, special market access arrangements such as those under the Sugar Protocol are now vulnerable to third-party complaints under the WTO. Finally, short-term expectations are that world sugar prices will fall by between 5 and 10% over the next 10 years. The Fiji sugar industry is therefore facing a period of significant challenges. The strategic external challenges confronting the industry operate in two time frames: the medium and the long term.

The medium term

It is becoming widely accepted in Fiji that over the remainder of the 1990s there will be a reduction in national welfare originating in changes in the sugar industry. The main source of this is believed to come from the loss of the transfers received from the Sugar Protocol. As already noted, under the terms

of the Uruguay Round Agreement the EU has agreed to reduce both the tariff protection and the volume of export subsidies received by European farmers. As a result, some people have argued that the EU's internal sugar price will fall, leading to a fall in the price paid for Fiji's quota exports to Europe. A widely-quoted figure is that the latter will fall by as much as 15% by 2000 (Akram-Lodhi, 1996). It has been estimated that under such a scenario the impact of Uruguay Round agricultural trade liberalisation would mean a net welfare loss to Fiji equivalent to some 2.52% of GDP (McDonald, 1996).

This scenario is unlikely to occur. Barring an unforeseen shock, the EU should be able to meet its Uruguay Round commitments while simultaneously maintaining the level of internal support prices. Moreover, it can cut internal sugar quotas in an effort to sustain the internal support price. Thus, it is probable that for the rest of the 1990s this price will remain broadly stable, which means that Fiji will continue to receive a comparable level of transfers from the Sugar Protocol.

As for the world sugar price, it is likely that the world market is entering a period of reduced volatility. It is true that some price erosion is likely to occur. However, the Uruguay Round Agreement will have only a limited effect on the world sugar price. The impact of the reduction in the EU's export subsidy on the world sugar price remains speculative. It is worth stressing, however, that the EU now has a less important role in determining the world sugar price than was previously the case because of the growing importance of Brazil, India and Indonesia. While World Bank estimates of a gradual fall in world sugar prices of between 5 and 10% up to 2005 appear to us to be optimistic, such an estimate does seem appropriate for the early years of the next decade.

The long term

The long-term position of Fiji's sugar industry is affected by two factors. First, the current Lomé Convention expires in 2000. It is highly likely that a follow-up convention will be negotiated. Admittedly, for the Fiji sugar sector a follow-up convention may appear unimportant; the Sugar Protocol is formally independent of Lomé. However, both the possibility of a follow-up convention and the Fiji sugar industry itself will be directly affected by the second factor: that, as a consequence of the Uruguay Round Agreement, agriculture now falls within the purview of the WTO.

It is not widely recognised that the Uruguay Round Agreement has already been highly significant for Fiji. Under the Agreement on Agriculture, tariff quota access to the EU for sugar was locked into tariff schedules inspected and agreed by all signatories to the agreement and subsequently all members of the WTO. Moreover, the amount of tariff quota access agreed was identical to that contained within the Sugar Protocol. The beneficiaries of tariff quota access to the EU sugar market are explicitly recognised as being the ACP group of

countries. Thus, the Uruguay Round Agreement established ACP access to the EU sugar market which is consistent with the WTO. The locking in of market access under agreed tariff schedules means that, barring a major economic shock, that access will under no circumstances be reduced; it can only be enlarged. Thus, ACP market access to the EU sugar market is now independent of the Sugar Protocol itself. It is possible, of course, that this could be subjected to a legal challenge in the WTO. If this were to happen, it is unclear whether the oligopolistic market-makers which structure sugar distribution channels — tncs such as Tate & Lyle — would be robust in resisting the challenge. However, a challenge remains unlikely at the present time. It is important, though, to issue a caveat: the locking in of tariff quota access applies to the ACP states as a whole and not to Fiji in particular. There is no provision concerning the allocation of tariff quota access to specific countries. In the light of this, the current importance of the Sugar Protocol to Fiji rests in two areas: its allocation of quotas among individual ACP countries and its pricing regime.

That having been stated, the inclusion of agriculture within the WTO poses two significant challenges for the Fiji sugar industry. Under the Agreement on Agriculture, the next round of WTO-initiated multilateral trade negotiations in agricultural products will begin in 1999. These negotiations 'will set in train a more powerful impetus to change than may at first sight seem obvious' (Roberts, 1996: 6). Negotiations

can be expected to broadly follow the lines of the Uruguay Round: further reductions of support, increases in market access (eg. through further reduction of tariffs and tariff equivalents) and further reduction in export subsidies and subsidized export quantities (*ibid.*: 5).

Moreover, it is likely that the EU will face some pressure to make commodity-specific agreements. These could have a major impact on the EU sugar regime as negotiations pursue cuts in tariffs, in export subsidies and in the support directed towards European sugar production. At the same time, pressures on the EU sugar regime are likely to be intensified by those European industries that use sugar as an input in the production of higher value-added commodities. Producers of such commodities, which form an increasingly important share of EU exports to non-EU members, may become reluctant to pay the comparatively high internal sugar price; they are likely to prefer procuring sugar at the world price. In sum, there is likely to be sustained internal and external pressure upon the internal sugar price. Indeed, it is quite possible that the EU will begin a process of shifting towards world market prices in the sugar sector. This would substantially erode if not eliminate the benefits Fiji receives from preferential access to the EU sugar market.

Pressure on the sugar price may be accentuated by difficulties involved in negotiating a follow-up convention to Lomé IV. Despite the fact that non-discriminatory non-reciprocal trading arrangements such as Lomé are

permissible under the WTO, the WTO has already expressed doubts about the general benefits of non-reciprocal trading arrangements, arguing that they provide limited economic gains and foster protectionism (WTO, 1995). Formally, the WTO will only support regional trading arrangements if they are consistent with Article XXIV of the General Agreement on Tariffs and Trade, which means that they must have as an explicit objective a movement towards reciprocal free trade between the contracting parties over a 10-year transition period, with free trade being defined as trade subject to zero import duty. In some exceptional cases, the transition period may be extended to 12 years. Moreover, regional trading arrangements which violate WTO rules can be subject to legal action. Admittedly, the application of Article XXIV has been haphazard in the past. However, following the Uruguay Round Agreement the EU and the ACP did feel it necessary to obtain a temporary waiver of Article XXIV in order to prevent third-party complaints about the special market access arrangements.

It is possible that doubts about the benefits of non-reciprocal regional trading arrangements may lead to attempts to apply more strictly the rules of the WTO, and Article XXIV in particular. At the same time, it is unclear whether the EU would agree to seek another waiver for a subsequent convention. If it did not do so, participants in a post-Lomé agreement would not only have to act on behalf of their own producers and consumers, they would also have to consider the impact of the agreement on the freedom of world trading relationships. As a consequence, a follow-up convention would have to constitute a reciprocal agreement encompassing a dismantling of trade barriers in an effort to move towards free trade between the contracting parties over a 10-year period. It could be argued that the European Commission's Green Paper on future relations between the EU and the ACP is an attempt to facilitate the negotiation of a post-Lomé agreement which is WTO-consistent (European Commission, 1997). In addition, support from the WTO for regional trading arrangements requires that they exclude no significant economic sector. If Article XXIV were to be rigorously enforced, the inability of a post-Lomé agreement to exclude significant sectors would mean that the Sugar Protocol would at the very least have to be made consistent with a follow-up convention, which implies significant movement towards a reformulation of the Sugar Protocol. A reformulated Sugar Protocol would have to make significant progress towards free trade in sugar between the contracting parties by 2010. This implies an end to quotas for specific countries. Moreover, the locking in of tariff quota access for ACP sugar exports to the European market means that the market access provisions of the Sugar Protocol are now redundant. With redundant market access provisions, a need to move towards free trade by 2010, and pressures within the EU itself to reduce substantially its support to the sugar sector, a more realistic scenario would be the termination of the Sugar Protocol.

If Article XXIV were to be more rigorously enforced, freer trade in sugar would mean that European producers would face competition from ACP countries not at the internal support price but at the much lower world market price. This would reinforce any trends within the EU towards a reduction in the internal support price arising out of post-1999 negotiations on multilateral agricultural trade liberalisation.

Therefore, to sum up: the long-term outlook for the Sugar Protocol to continue to provide benefits to Fiji is problematic. The market access arrangements of the Protocol now exist independently, but make no specific provision in favour of Fiji. This means that the main continued benefit of the Protocol lies in its quota allocations and the price it offers for Fiji's sugar. However, after 1999 there is likely to be major downward pressure on the EU's internal sugar price, and thus the price received by all ACP producers. This pressure will only be reinforced if Article XXIV comes to be more strictly interpreted, as, in order for a Protocol to survive, it must become consistent with the free trade objectives of a follow-up convention subject to the approval of the WTO.

Fiji faces the possibility of losing both sizeable transfers from the EU and its clearly specified preferential access to the EU market. Clearly, in the long term its sugar industry faces a major challenge. It has recently been estimated that full trade liberalisation will result in a loss to Fiji of US\$41m. a year at 1985 prices (McDonald, 1996). Such a loss would represent a major shock to such a small economy. Fiji will have to adjust.

Trade-led restructuring in Fiji's sugar sector

Sugar has been a source of social stability in Fiji. However, it would appear that the Sugar Protocol is unlikely to survive in its present form beyond 2010. Indeed, Fiji seems likely to face the need to undergo restructuring in the sugar sector, in order to become competitive at the world market price. A transition to an environment ruled by free market prices could result in severe dislocations. Moreover, production, harvesting and transportation costs in the sugar sector are already rising, reducing the returns to growers and millers. At a time when Fiji's economic system is challenged by so many other problems, including the impending cessation of preferential market access for its non-sugar manufacturing sectors, a highly uncertain future awaits the sugar sector and indeed the economy as a whole (Akram-Lodhi, 1996). Much will therefore depend on how well Fiji's sugar sector is able to respond to these challenges.

Fiji policy-makers have long recognised that in the longer term the country will have to develop an internationally competitive sugar industry. However, attempts at restructuring have been burdened by the problems of ethnic relations and a complex system of land ownership and distribution, by distance from

markets, and by the escalating freight and insurance costs. A rapid transition to free trade will not solve these problems. Moreover, it will severely undermine social equity and probably increase social conflict. It is therefore imperative that Fiji manage the transition in its sugar sector. A longer-term approach will be essential if the structural reforms needed in the sugar sector are to take account of the potentially serious social costs involved in the reform process.

Already, at the industry level preferential prices have created an environment in which major initiatives aimed at efficiency improvements in both the milling and farming sectors have been undertaken. These efforts need time and support to translate into improvements in productivity. In the light of this, preferential trading arrangements have an important part to play in managing the transition that must occur in Fiji's sugar sector. Over their remaining life it is important that the preferential arrangements embodied in the Sugar Protocol are used to prepare Fiji's sugar industry for open competition in world markets by increasing supply capacity, overcoming supply constraints, and cutting costs. The challenge is a major one: we estimate that the farming and milling sectors have to seek to boost productivity by at least 25%. This will require investment of more than F\$80m. in the milling and transportation sectors and more than F\$50m. in the harvesting sector (Sugar Commission of Fiji, 1997).

Experience elsewhere demonstrates that restructuring at the farm level is likely to result in a gradual concentration of farm enterprises into larger working units as they seek to generate productivity gains. It also demonstrates that further productivity improvements on larger-scale farms may be secured through a transition to semi-mechanised harvesting. However, these processes would have major social consequences. The 65% of growers producing less than 350 tonnes per year are likely to be seriously exposed to poverty as price supports are reduced to world market levels. Moreover, rural cane cutters would also face deepening economic hardship. Displacement out of sugar-producing regions is a distinct possibility. In an economy which has created no more than 900 new wage and salaried jobs a year over the last five years, such displacement might not only have an impact on equity. It might also undermine the fragile constitutional and political settlement reached in 1997 between the leaders of the indigenous Fijian and Indo-Fijian communities.

We do not welcome this outcome. It is therefore necessary to formulate policies which can assist in maintaining the security of those threatened by the transition to free market prices. For smallholder farmers, five policies might assist in enhancing their productivity and thus their security during uncertain times. First, a lasting settlement of land lease questions could make a major contribution to stabilising the transition process. Secondly, renewed efforts at encouraging crop diversification are going to be needed. Thirdly, decades of accumulated experience in plant breeding and improved husbandry measures should be reinvigorated in order to seek to boost productivity. Fourthly, substantial infrastructural investments targeted at improving transport and

increasing the efficiency of cane crushing and milling could assist in fostering productivity improvements. Fifthly, there must be some movement towards a system of payments based on the quality of cane rather than its quantity. All five issues cannot be solved overnight, however; a medium- to long-term timeframe is required.

While the need for productivity gains has been stressed, Fiji also needs to use preferential trade to begin to develop a range of sugar by-products which have a higher value-added component and which can be produced locally. Moreover, it will be necessary to try to develop niche export markets for such products. The development of such products will be an important means whereby the economy can seek to deal with the employment issues created by the transition to a more open trading environment for sugar. Such policies will be of major importance to both those farmers who lose their livelihoods and to those rural cane cutters displaced by trends towards mechanisation.

These policies involve resource costs. The challenge will be to target some portion of the preferential price currently received under the Sugar Protocol towards sustaining efforts designed to foster productivity improvements in the farming, harvesting and milling sectors. An increase in export taxes may be inevitable. Resources will also be required to accommodate the social equity implications of restructuring. If social disruption is to be avoided, research, industry-level support and central co-ordination will be required. Moreover, it is vital that the EU should be engaged in this process and that future EU-ACP trade agreements sustain a preferential trade-based institutional framework during the transition period. Inevitably, successor trade-based institutional arrangements to the Lomé Convention and the Sugar Protocol will need to accept that these frameworks have worked in favour of Fiji's economy in the past. The last thing Fiji needs is a replacement of trade-based institutional arrangements with new concessional aid regimes.

Conclusion

The Sugar Protocol has contributed enormously to Fiji's social and economic development. By providing price stability and market access, it has helped sustain productivity improvements in the sugar industry and provided the main source of income for almost a quarter of the country's economically active population. While the EU's international commitments over the remainder of the 1990s will not seriously affect the industry, any further price falls in the following decade arising from multilateral negotiations will expose the industry to global competition without the prerequisite competitive strength. International competitiveness in the sugar industry must be the long-term goal. However, in order to move towards international competitiveness it is vital that the market security and price stability provided by the Protocol be retained as long as

possible so as to sustain the conditions necessary for productivity improvements and agricultural and non-agricultural diversification. In the absence of an orderly process of change, social stability and Fiji's economic well-being are likely to be seriously harmed.

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