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# Poverty Reduction and Trade:

## Fairtrade as a Vehicle to Combat Poverty

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## **Poverty Reduction and Trade: Fairtrade as a Vehicle to Combat Poverty**

Many farmers in developing countries, despite their hard work, live in poverty. When agricultural products are sold at low prices, farmers earn very little profit and can become stuck in a cycle of poverty, or poverty trap.<sup>i</sup> Unlike farmers in the developed world, there are no government or social safety nets to help them when market prices drop below production costs. Agricultural workers face similar challenges: low wages and difficult working conditions can lead to a cycle of poverty.

Fairtrade International believes agricultural production should be a sustainable and rewarding business for farmers in developing countries. It should allow farmers to cover the cost of sustainable production and generate a decent income for themselves and their families. Workers should have decent working conditions and earn fair wages for their labour.

Fairtrade International believes that poverty reduction is about the fulfilment of people's rights<sup>ii</sup> through their own empowerment and development. Given its' inclusive and participative approach, Fairtrade is a viable means for producers to combat poverty by strengthening their position and enabling them to take more control over their lives.

***Fairtrade is a means for vulnerable producers (farmers and workers) to combat poverty through their own empowerment and development.***

### Poverty in developing countries

According to the World Bank, approximately 21 percent of the world's population lived below the poverty line of US\$1.25 per day in 2005 – the great majority in developing countries.<sup>iii</sup> In sub-Saharan Africa, an estimated 50.9 percent of the population lives in poverty, while in South Asia 40.3 percent of people live in poverty. In East Asia and the Pacific, 16.8 percent of the population lives in poverty, and in Latin America 8.2 percent of people live in poverty. While this indicator is to a certain extent limited (factors beyond daily earnings are not considered), it illustrates the far reach of poverty in the developing world.

While these percentages are high, there are currently fewer people living in extreme poverty than there were in 1990 (the number has dropped from 1.8 billion to 1.4 billion).<sup>iv</sup> The most significant gains were made in East Asia, where the percentage of people living in poverty declined from 60 percent to 16 percent mainly due to economic growth and increased industrialisation. In the rest of the world, gains were relatively low. Poverty in the last 15 years in sub-Saharan African has decreased by only 7 percent, in South Asia by 10 percent and in Latin America by 3 percent.<sup>v</sup>

It is important to note that although poverty levels have decreased, the number of people at risk of falling below the US\$1.25 poverty line at any time is still substantial. For example, the World Bank estimates that an additional 64 million people were pushed into poverty worldwide in 2010 as a result of the economic crisis.<sup>vi</sup>

*Fairtrade farmers and workers are not necessarily living on less than \$US 1.25 per day, but many live in very limited and precarious conditions. Given their vulnerabilities, Fairtrade producers can easily fall into a poverty trap.*

### Why is Fairtrade needed?

Fairtrade responds to the gap between free trade rhetoric and actual trade practices. According to liberal trade theory, free trade is “the ability of people to undertake economic transactions with people in other countries free from any restraints imposed by governments or other regulators”.<sup>vii</sup> The World Trade Organization (WTO) indicates that liberal trade policies “allow the unrestricted flow of goods and services – sharpen competition, motivate innovation and breed success”.<sup>viii</sup> Nonetheless, while advocating for free trade, many countries support and protect their agricultural industries through subsidies and high import taxes.

The WTO also suggests that liberal trade policies “multiply the rewards that result from producing the best products, with the best design, at the best price”.<sup>ix</sup> However, not all players within the supply chain have the opportunities and capabilities to become highly competitive within international markets.

Producers have clear disadvantages in relation to others (middlemen, traders, companies, retailers), which limits them from realizing their market potential. Free trade does not address the vulnerability of some actors within the trade system, as it assumes that all actors can compete equally.



*Farmers and agricultural workers face the following vulnerabilities:*

#### *Vulnerability to international prices*

In the global trading system, prices for most commodities are set internationally, based on supply and demand or through trading markets. International prices have a direct effect on farmers from developing countries, as they must sell their products at prices that do not necessarily cover the costs of sustainable production or generate sufficient income for their families. Additionally, many farmers must sell their products to middlemen who negotiate an even lower price than the internationally set price, resulting in low returns for farmers.

#### *Vulnerability to price volatility*

Farmers are particularly vulnerable to market fluctuations and falling prices in an unregulated global market. As countries have further liberalized their trade policies and made them more export-oriented, agricultural prices have dropped, with harsh ramifications in developing countries. In its 2004 report on Least Developed Countries (LDCs), UNCTAD writes: “a particular problem for agricultural-commodity-exporting LDCs is that the widespread adoption of trade liberalization and export-oriented policies has been associated with falling world prices for agricultural commodities”.<sup>x</sup>

In recent years, prices of main exporting commodities have risen, but the risk remains that they could tumble once again. It is important to note that although the prices of products have risen, the price of agricultural inputs (such as seeds, fertilizer) has also increased.

#### *Competitiveness limitations*

Farmers from developing countries often lack access to vital information on international pricing, market options, adding value to products, product quality, etc. They also do not have the capital needed for agricultural inputs, such as equipment, technology and for infrastructure investments like storage and refrigeration. Access to both information and capital is essential for farmers to reach their full market potential. Farmers can also be constrained by limited organizational and management skills. Climate change also limits competitiveness, as temperature and precipitation variability and uncertainty, as well as an increase in extreme weather, require additional investments to avoid losing yields.

#### *Vulnerability to increasing food prices*

Farmers and agricultural workers also suffer from rising food costs. The Food Agriculture Organization (FAO) reports that in 2008 food prices rose to their highest level in 30 years, and continued to spike through 2011.<sup>xi</sup> Many farmers are doubly affected and vulnerable to fluctuations and lower returns for their cash crops, while still having to pay high costs for imported foodstuffs. Agricultural workers also frequently find themselves in jeopardy earning extremely low wages, but still subject to rising food prices, the increase of which can push them into poverty.

#### Fairtrade as a means to combat poverty

Fairtrade International believes that the global trading system is inherently unfair. Some actors within the supply chain are more vulnerable than others, namely small-scale farmers and workers. Fairtrade aims to promote a more just trading system by supporting livelihoods and empowering producers.



#### *Supporting livelihoods*

Fairtrade supports farmers and workers to combat poverty and strengthen their livelihoods by:

- Establishing a Minimum Price for as many Fairtrade products as possible – a price floor which aims to protect farmers from global price fluctuations and falling prices;
- Providing, on top of stable prices, the Fairtrade Premium – an extra payment that the producers decide collectively how to spend. It can be used for business development purposes to increase yield and quality, or for other types of development projects that will benefit producers, their families and their communities;
- Improving the terms of trade for farmers by providing access to information, clear contracts providing pre-payments, access to markets and financing;
- Promoting better living wages and working conditions for workers;

- Encouraging commitments from traders and retailers to ensure sustainable product demand and additional support for farmers.

A review of ten years of Fairtrade literature carried out by the Natural Resources Institute (NRI)<sup>xii</sup> studied a number of papers demonstrating the economic benefits of Fairtrade. The study indicated the following economic benefits, according to the papers examined:

<b>Benefit</b>	<b>Number of papers demonstrating benefit</b>
Guaranteed minimum price leads to improved income	29
Improved economic stability	27
Improved access to credit	11
Enables transition to organic	9
Enables diversification of income	7
Access to lower interest rates	3
Improvements to facilities and equipment (including being able to position themselves further up the value chain)	5
Quality improvement	4
Access to new export markets	9

*Table 1: Summary of the economic benefits of Fairtrade. Adapted from NRI (2009)<sup>xiii</sup>*

#### *Empowering producers*

The Fairtrade system also serves as a means of empowerment. Through Fairtrade, producers are enabled to:

- Develop stronger representative organizations;
- Improve their negotiation capacities which result in more balanced power relations within markets;
- Make decisions that have a direct impact on the sustainability of their livelihoods and communities;
- Decide where to allocate the Fairtrade Premium according to their rights and needs (housing, education, health).

The NRI study also points out the empowerment benefits of Fairtrade, according to a number of papers examined:

<b>Benefit</b>	<b>Approximate number of papers specifically identifying benefits in this aspect of empowerment</b>
Improved producer self-confidence	10
Improved market and export knowledge	13
Access to training and improvements in quality	14
Improved producer Fairtrade knowledge	2

*Table 2: Summary of the individual producer empowerment benefits of Fairtrade. Adapted from NRI (2009)<sup>xiv</sup>*

In the case of workers, Fairtrade encourages and supports freedom of association, collective bargaining and claiming of labour rights. It is very important to note that the Fairtrade system is, in itself, an empowerment mechanism that allows producers to be represented in its structure and have a say in the development of Fairtrade.

#### *Contributing to the Millennium Development Goals (MDGs)*

By supporting and empowering producers, Fairtrade contributes to reducing global poverty – Goal 1 of the MDGs.<sup>xv</sup> Fairtrade also helps achieve other development goals, as producers often invest the Fairtrade Premium in community development projects in health and education.<sup>xvi</sup> Given its nature as a multi-stakeholder movement to address poverty and foster development, Fairtrade also plays a key role in achieving Goal 8, a global partnership for development. Fairtrade is by definition a partnership model that links producers, traders, retailers and consumers, as well as funding agencies and development organizations.

#### Conclusion: combating poverty through empowerment and development

Fairtrade proposes a trading system that is fairer for farmers and workers in developing countries: a system that empowers them to combat poverty and improve their livelihoods.

By organizing into collectives or cooperatives, Fairtrade farmers become small business owners that are able to get the returns for their products that are rightfully theirs. Fairtrade workers, on the other hand, work within decent conditions and earn an income that sufficiently meets their needs.

Within the Fairtrade system, farmers become active agents of their own development. Independence from the conventional trading system allows them to make the best decisions for their own businesses. Fairtrade workers are also empowered: they are organized and therefore able to defend their rights and influence their work and employment conditions.

Combating poverty is not about addressing people's needs, but their rights through their own empowerment and development. Given its inclusive and participative approach, Fairtrade is a viable vehicle for producers to combat poverty, strengthen their position and take more control over their lives.

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<sup>i</sup> A poverty trap is "any self-reinforcing mechanism which causes poverty to persist". Costas Azariadis and John Stachurski, "Poverty Traps," *Handbook of Economic Growth*, 2005, 326

<sup>ii</sup> Both the Universal Declaration of Human Rights (Art. 25) and the International Covenant on Economic, Social, and Cultural Rights (Art. 11), indicate that every person has the right to an adequate standard of living (including food, clothing, housing, health and social services, etc.) and its improvement, thereafter. Although not a binding document, the Millennium Development Declaration reiterates that poverty needs to be reduced by half in the case of those living with less than one dollar per day (Goal 1). It also indicates that strong partnerships need to be developed to address poverty and foster development (Goal 8).

<sup>iii</sup> World population is currently around 6.47 billion. Poverty indicators from: The World Bank, *Poverty Data, World Bank Development Indicators*. For more information, see:

<http://data.worldbank.org/topic/poverty>

<sup>iv</sup> "Where do we stand" UN MDGs Fact sheet prepared for the UN Summit Sept. 2010

[http://un.org/millenniumgoals/pdf/MDG\\_FS\\_1\\_EN.pdf](http://un.org/millenniumgoals/pdf/MDG_FS_1_EN.pdf)

<sup>v</sup> United Nations, *MDG Report 2010 – Goal 1: Eradicate Extreme Poverty and Hunger*. For more information, see: <http://www.un.org/millenniumgoals/pdf/MDG%20Report%202010%20En%20r15%20-low%20res%2020100615%20-.pdf#page=8>

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- <sup>vi</sup> “Where do we stand” UN MDGs Fact sheet prepared for the UN Summit September 2010  
[http://un.org/millenniumgoals/pdf/MDG\\_FS\\_1\\_EN.pdf](http://un.org/millenniumgoals/pdf/MDG_FS_1_EN.pdf)
- <sup>vii</sup> The Economist, *Economics A-Z*. For more information, see:  
<http://www.economist.com/research/Economics/searchActionTerms.cfm?query=free+trade>
- <sup>viii</sup> WTO, *Understanding the WTO: The Case for Open Trade*. For more info, see:  
[http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/fact3\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact3_e.htm)
- <sup>ix</sup> *Ibid.*
- <sup>x</sup> UNCTAD (*United Nations Conference on Trade and Development*), *The Least Developed Countries Report – Linking International Trade with Poverty Reduction*, 2004. Document available online at:  
[http://www.unctad.org/en/docs/lcd2004\\_en.pdf](http://www.unctad.org/en/docs/lcd2004_en.pdf)
- <sup>xi</sup> FAO, *International Prices of agricultural commodities drop but high prices of non-cereal products still keep food import bills high, especially in developing countries*. For more information, see:  
<http://www.fao.org/news/story/en/item/42790/icode/>
- <sup>xii</sup> Natural Resources Institute, *The Last Ten Years: A Comprehensive Review of the Literature on the Impact of Fairtrade*. Document is available online at:  
[http://www.fairtrade.org.uk/includes/documents/cm\\_docs/2010/n/2\\_nri\\_full\\_literature\\_review\\_final\\_version.pdf](http://www.fairtrade.org.uk/includes/documents/cm_docs/2010/n/2_nri_full_literature_review_final_version.pdf)
- <sup>xiii</sup> *Ibid* p. 8
- <sup>xiv</sup> *Ibid* p. 22
- <sup>xv</sup> Goal 1 of the MDG is: *Eradicate Extreme Poverty and Hunger*. Target 1.A. is “to reduce by half the proportion of people living with less than a dollar a day”. Target 1.B. is “to achieve full and productive employment and decent work for all, including young people and women”. For more information on these goal and on the MDGs in general, see: <http://www.un.org/millenniumgoals/>
- <sup>xvi</sup> Fairtrade also contributes indirectly to other MDGs such as Goal 2 (Achieve universal primary education), Goal 3 (Promote Gender equality and empower women), and Goal 7 (Ensure environmental sustainability).