

International Trade, Institutional Quality and Economic Development

PhD Thesis

Elisabeth Nindl

FIW Conference, 3. - 4.12.2015

December 3, 2015

Outline

1. Overview of the thesis

- ▶ Motivation
- ▶ Realization
- ▶ Contribution

2. Short presentation of the research paper on Fairtrade

Motivation

- ▶ Inconclusive findings on the nexus natural resources – economic growth.
 - ▶ Measurement issues.
 - ▶ Growth rate vs. level of GDP.
- ▶ Impact of natural resources is determined by the institutional setting.
 - ▶ Positive and negative effects.
- ▶ Natural resources affect the institutional environment.
 - ▶ Positive and negative effects, or even a spurious effect?
- ▶ Generalization: “Institutional content” affects the impact of trade on development.
 - ▶ Product certification (ideally) a means to identify the institutional content.

...and its realization

1. *In Quest of the Resource Curse: Natural Resources and Economic Development*
 - ▶ Literature review.
 - ▶ Empirical testing with focus on i) resource abundance vs. dependence and ii) growth rate vs. level of GDP.
2. *Globalization and Corruption, Revisited (co-authored with Harald Badinger)*
 - ▶ Empirical analysis of the effect of trade and financial openness on corruption levels.
 - ▶ Role of income inequality in determining the impact of globalization on corruption.
3. *An Empirical Assessment of Fairtrade: A Perspective for Low- and Middle-Income Countries?*
 - ▶ Identification of the determinants of participating in Fairtrade.
 - ▶ Analysis of the effect of Fairtrade on agricultural growth.

Part II

An empirical assessment of Fairtrade: Determinants and Growth Effects

Emergence of Private Voluntary Standards

- ▶ Criticism of the conventional agro-food system.
 - ▶ Degradation of human and environmental resources.
 - ▶ Multinational companies vs. small producers.
 - ▶ Health and product safety.
- ▶ Alternative trade concepts (fair trade, organic etc.)
 - ▶ Commodity circuits within ecological and social relations.
 - ▶ Against conventional price relations in guiding production and trade conditions.
 - ▶ Closer producer/consumer linkages.
 - ▶ Monitoring of the value chain.
 - ▶ Awareness raising.
- ▶ Social regulation
 - ▶ “Transnational private governance”: consumer pressure on private companies (Raynolds, 2012).

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- A set of small navigation icons typically found in Beamer presentations, including symbols for back, forward, search, and other slide controls.

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Research Question

Benefits of Fairtrade certification

1. Price Channel

- ▶ Fixed minimum price.
- ▶ Price premium per unit sold to a Fairtrade customer.

2. Cooperative Channel

- ▶ Market access, long term contracts.
- ▶ Technical assistance, training, education.
- ▶ Prefinancing, credit services.
- ▶ Environmental programs.



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Does the export of Fairtrade certified products reduce poverty of smallholders and agricultural workers in low- and middle-income countries?

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Certification Requirements

Producers

- ▶ Smallholders, hired labor and contract production schemes from low- and middle-income countries.
- ▶ Democratic organization in cooperatives (precondition).
- ▶ (Annual) Audits and payment of a certification fee.
- ▶ ILO labor standards (ILO conventions 87, 98, 100).
- ▶ Environmental requirements (e.g. no genetically modified organisms).
- ▶ Label per product.

Importers

- ▶ Minimum price, price premium + prefinancing of the purchase price (up to 60%)
- ▶ Per unit license fee to Fairtrade International.

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Facts and Figures

2012 Figures

- ▶ Sales €4.8 billion in 125 countries (av. annual growth 2003-2012 25.72%).
- ▶ Price premium €80 million.
- ▶ 1149 certified producers (224 (2001), av. annual growth rate 16%).
- ▶ 1.35 million farmers and agricultural workers in 70 countries.
- ▶ Share of organic: bananas 31%, green coffee beans 44%, cocoa 11% etc.

Issues

- ▶ Data is hardly available and inconsistent.
- ▶ Aggregation on *continent* level.
- ▶ No data on export or employment figures.

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Impact Studies

Coffee producers in Mexico

- ▶ Barham et al. (2011): US \$150-\$360 for organic Fairtrade producers.
 - ▶ 5-10% increase in av. household income.
 - ▶ Yields drive results, not prices.
- ▶ Weber (2011): US \$130 annual net income gain per household (5%).
 - ▶ Cooperative members receive on av. US \$0.12/lb (OLS, Heckman model).
 - ▶ No endogeneity/self selection into organic Fairtrade cooperatives.
- ▶ de Janvry et al. (2014): No monetary benefits in the long run.
 - ▶ Market entry reduces the quantity sold per producer.
 - ▶ In equilibrium, benefits from the floor price equal certification costs.
 - ▶ Av. price premium in 1997-2009 only US \$0.2/lb (US \$-0.13/lb for 2005-2009).
- ▶ Benefits through premium financed social projects, more stable revenues, reduction of externalities etc. rather than price premia.

Critique

Inefficient transfer (Yanchus and de Vanssay, 2003; Sidwell, 2008; de Janvry et al., 2014)

- ▶ The Economist (2007): only 10% of the higher price reaches producers.
 - ▶ Standard price discrimination strategy.
 - ▶ Administrative costs.
- ▶ Market entry.

Market distortions (Yanchus and de Vanssay, 2003; Mann, 2008)

- ▶ Welfare loss from oversupply
 - ▶ A coop. sells on av. 20% to Fairtrade customers.
 - ▶ Market share is very small.

Lock-in effect (Mann, 2008; Sidwell, 2008).

- ▶ Rewarding unproductive activities as a disincentive for modernization and change.
 - ▶ Technical assistance and training to improve productivity and product quality.
 - ▶ What are other *real* options?

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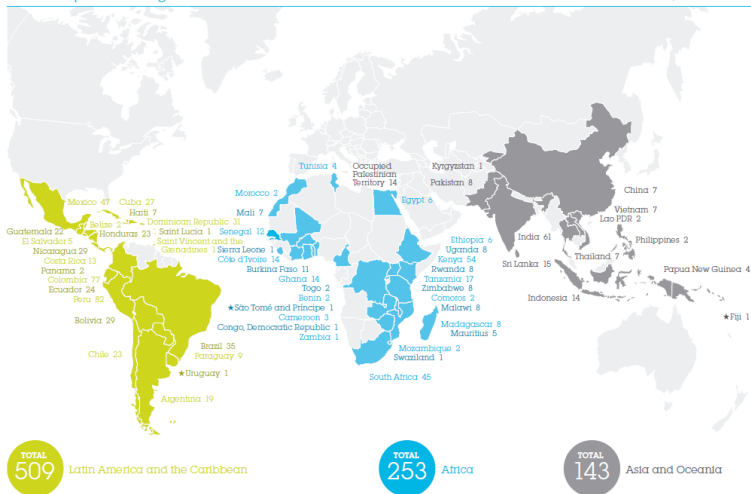
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Fairtrade producer organizations per country

FIGURE 4.2

Fairtrade producer organizations worldwide 2010

★ Indicates new producer countries



What determines whether a country has FTPOs and if yes, what drives the count?

- ▶ Why are there 45 FTPOs in South Africa, but none in neighboring Namibia?
 - ▶ Producers from 143 low- and middle-income countries can participate.
 - ▶ 63 countries have positive FTPO count, 80 countries have a zero count.
- ▶ Two-stage problem with count data and a non-negligible share of zeros.
 - ▶ Zero-inflated negative binomial model (ZINB).
 - ▶ Probit selection/participation equation.
 - ▶ Neg. bin. model on the observations with a positive participation probability.
 - ▶ ZINB assumes conditional independence of selection and outcome equation; focus on actual outcomes.

The Model

$$FTPO_{i,t} = \mathbf{x}'_{i,t}\beta + \mathbf{z}'_{i,t-1}\delta + \eta_r + \xi_t + \varepsilon_{i,t}.$$

- ▶ FTPO: number of Fairtrade certified producer organizations per country (2006, 2007, and 2010).
 - ▶ $FTPO \in \{0, 1, \dots, 82\}$
 - ▶ FTPOs for 2008 and 2009 were imputed.
- ▶ Explanatory variables: rural population density, arable land in total land area, population, GDP growth per capita, initial GDP (squared), trade, resource rents, Christian dummy, official development assistance, region and year dummies.
- ▶ 119 countries, 61 out of 63 with a positive count.
- ▶ 309 out of 556 observations have a zero count (52%).

Zero Inflated Negative Binomial Model

- Probability of observing $FTPO_{i,t} = 0$:

$$\Pr(FTPO_{i,t} = 0 | \mathbf{x}_{i,t}, \mathbf{z}_{i,t-1}) = \psi_{i,t} + (1 - \psi_{i,t}) \left(\frac{\alpha^{-1}}{\alpha^{-1} + \mu_{i,t}} \right)^{\alpha^{-1}}$$

- Probability of observing $FTPO_{i,t} = 1, 2, \dots$:

$$\Pr(FTPO_{i,t} | \mathbf{x}_{i,t}, \mathbf{z}_{i,t-1}) = (1 - \psi_{i,t}) \frac{\Gamma(FTPO_{i,t} + \alpha^{-1})}{FTPO_{i,t}! \Gamma(\alpha^{-1})} \times \left(\frac{\alpha^{-1}}{\alpha^{-1} + \mu_{i,t}} \right)^{\alpha^{-1}} \left(\frac{\mu_{i,t}}{\alpha^{-1} + \mu_{i,t}} \right)^{FTPO_{i,t}}$$

- with $\mu_{i,t} = \exp(\mathbf{x}'_{i,t}\beta + \mathbf{z}'_{i,t-1}\delta + \eta_r + \xi_t)$.
- and $\psi_{i,t} = \Phi(-\mu_{i,t})$ is the proportion of zeros (standard normal).

Determinants of Participation in Fairtrade

	Full sample		Short sample		Short sample ¹	
	Neg.Bin	Probit	Neg.Bin	Probit	Neg.Bin	Probit
log(GDP p.c. 2006)	6.1040*** (1.1635)	-0.4602** (0.1991)	6.3973*** (1.1542)	-0.4282** (0.1974)	4.3295*** (1.0705)	-0.8115*** (0.1429)
log(GDP p.c. 2006) ²	-0.3925*** (0.0777)	0.0554*** (0.0167)	-0.4166*** (0.0777)	0.0538*** (0.0148)	-0.2843*** (0.0736)	0.0769*** (0.0119)
GDP growth p.c. $t-1$	0.4529 (1.5605)	0.0491 (0.2176)	2.4146 (2.0162)	-0.2850 (0.5038)	-1.4555 (1.3233)	-0.3504*** (0.1322)
log(ODA/GDP) $_{t-1}$	0.3221* (0.1894)	0.0843** (0.0404)	0.2955* (0.1790)	0.0898* (0.0497)	0.3266** (0.1623)	0.0283* (0.0155)
log(Trade/GDP) $_{t-1}$	0.1824 (0.2885)	0.0422 (0.0756)	0.2003 (0.3025)	0.0549 (0.0766)	0.0219 (0.2492)	-0.1844*** (0.0474)
log(Res. r./GDP) $_{t-1}$	0.1857 (0.1520)	0.2612*** (0.0536)	0.1367 (0.1582)	0.2543*** (0.0401)	0.3816** (0.1590)	0.2775*** (0.0392)
Rule of Law	0.0657 (0.2137)	-0.2271*** (0.0738)	0.0966 (0.2066)	-0.2740*** (0.0878)	0.2802 (0.2720)	-0.2826*** (0.0572)
log(Pop.)	0.7962*** (0.1337)	-0.1176*** (0.0184)	0.8165*** (0.1479)	-0.1159*** (0.0252)	0.5375*** (0.0915)	-0.1689*** (0.0288)
log(Arable land)	0.2292* (0.1336)	0.0407* (0.0237)	0.2017 (0.1320)	0.0390* (0.0227)	0.3228*** (0.1099)	0.0494*** (0.0103)
log(rur. pop. den) $_{t-1}$	0.3283*** (0.0978)	0.1040*** (0.0298)	0.2896*** (0.1015)	0.0952*** (0.0273)	0.3174*** (0.1098)	0.1357*** (0.0234)
Christian	-0.0483 (0.3377)	-0.2306*** (0.0432)	-0.0697 (0.3186)	-0.2635*** (0.0533)	-0.0700 (0.2709)	-0.2177*** (0.0357)
Ethn. frac.					0.5596 (0.5283)	0.4670*** (0.0885)
No. of coups					-0.0113 (0.0193)	-0.0070*** (0.0019)
Political Freedom					-0.0392 (0.1715)	-0.1604*** (0.0343)
Overdispersion α	-1.1311*** (0.2493)		-1.1226*** (0.2347)		-1.1399*** (0.3465)	
N	586		351		566	
N zero	309		182		309	

Estimation results

- ▶ Participation equation: Fairtrade certification . . .
 - ▶ is most likely in large, resource-poor, Christian lower middle-income countries with a strong rule of law and a low number of coups d'etat.
 - ▶ is less likely in countries with a high rural population density and a large share of arable land in total land area (low capital intensity).
- ▶ Outcome equation: The number of FTPOs . . .
 - ▶ increases with rural population density and population size, arable land in total land area, and development assistance.
 - ▶ is largest in lower middle-income countries with labor intensive agriculture.

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Fairtrade and growth in the agricultural sector

Does the export of Fairtrade certified goods increase the growth rate of per capita value added in agriculture?

$$y_{i,t}^a = ftpo_{i,t-1}\beta + \mathbf{x}_{i,t}'\gamma + \mathbf{z}_{i,t-1}'\delta + \eta_r + \xi_t + \varepsilon_{i,t}.$$

1. Effect of FTPO on agricultural growth

- Functional form: $ftpo$, $ftpo^2$, $ftpo_{t-1}$, $ftpo_{t-1}^2$ (Clemens et al., 2011).

2. How to compare the number of FTPOs across countries?

- 300 members on average per cooperative but this varies widely.
- $ftpo_{i,t} \equiv \log \frac{(\text{FTPO}_{i,t} + 1)}{\text{rural pop}_{i,t}}$

3. Control variables from the ZINB model.

	RE				FE	BB
$\log(\text{agri. GDP p.c. 2006})$	-0.0064 (0.0114)	-0.0089 (0.0113)	-0.0068 (0.0113)	-0.0097 (0.0112)		-0.0106 (0.0110)
ODA (GDP)_{t-1}	0.0813*** (0.0297)	0.0822*** (0.0301)	0.0805*** (0.0295)	0.0812*** (0.0299)	-0.0337 (0.0585)	0.0649** (0.0294)
Trade_{t-1}	0.0156 (0.0170)	0.0185 (0.0170)	0.0161 (0.0170)	0.0195 (0.0170)	0.0294 (0.0765)	0.0201 (0.0170)
$\text{Resource rents}_{t-1}$	0.0441 (0.0346)	0.0446 (0.0330)	0.0444 (0.0342)	0.0454 (0.0325)	0.1264 (0.0921)	0.0511* (0.0298)
Rule of Law	0.0050 (0.0094)	0.0035 (0.0095)	0.0048 (0.0094)	0.0029 (0.0094)	-0.0310 (0.0441)	0.0015 (0.0090)
$\log(\text{Pop.})$	0.0102** (0.0044)	0.0113** (0.0045)	0.0113** (0.0045)	0.0126*** (0.0047)	0.0720 (0.5373)	0.0131*** (0.0047)
Arab. land	0.0884* (0.0491)	0.0804* (0.0480)	0.0898* (0.0494)	0.0820* (0.0480)	1.5250* (0.8939)	0.0879* (0.0460)
$\log(\text{Rur. pop. den.})_{t-1}$	0.0021 (0.0042)	0.0004 (0.0042)	0.0024 (0.0042)	0.0006 (0.0042)	0.0964 (0.0902)	0.0010 (0.0042)
Christian	-0.0210 (0.0156)	-0.0196 (0.0154)	-0.0222 (0.0157)	-0.0206 (0.0155)		-0.0206 (0.0152)
$\text{ftpo}_{i,t}$	0.0102 (0.0064)	0.0618** (0.0301)				
$\text{ftpo}_{i,t}^2$		0.0018* (0.0009)				
$\text{ftpo}_{i,t-1}$			0.0118* (0.0065)	0.0694** (0.0297)	0.2954 (0.2345)	0.0730** (0.0301)
$\text{ftpo}_{i,t}^2$				0.0020** (0.0009)	0.0083 (0.0070)	0.0020** (0.0009)
N	373	373	373	373	373	373
No. of Instruments						23
AIC	-675.194	-674.868	-675.801	-675.915	-794.204	

Interpretation of the results

- ▶ Evidence for a positive effect of Fairtrade on agricultural growth.
 - ▶ One additional FTPO (for a constant rural population) raises y^a by 0.44 percentage points (elasticity of 3) (column 6).
- ▶ Results resemble the findings of the aid-growth literature.
 - ▶ Impact only with a time lag.
 - ▶ Non-linear effect.
 - ▶ Evidence for a significant impact is only weak.
- ▶ Blundell Bond-estimation (Column (6)) as our preferred model:
 - ▶ Removes endogeneity from serial correlation and heterogeneity.
 - ▶ Sargan/Hansen-Test does not indicate weak instruments.
 - ▶ Lagged effect of $ftpo$ is theoretically more plausible.
 - ▶ $ftpo$ and $ftpo^2$ are jointly different from zero.
 - ▶ Increasing marginal returns: supports evidence for spill-over effects and spatial externalities.

	Low	Lower middle	Upper middle
$ftpo_{t-1}$	0.1808 (0.1411)	0.0691* (0.0384)	0.1368*** (0.0498)
$ftpo_{t-1}^2$	0.0058 (0.0047)	0.0021* (0.0013)	0.0037** (0.0017)
$\log(\text{agri. GDP p.c. 2006})$	0.0215 (0.0372)	0.0090 (0.0150)	-0.0399** (0.0174)
ODA (GDP)_{t-1}	0.0288 (0.0558)	0.0763 (0.1088)	-0.7069 (0.6795)
Trade_{t-1}	0.0733* (0.0397)	0.0000 (0.0212)	0.0027 (0.0278)
$\text{Resource rent}_{t-1}$	0.0517 (0.0554)	0.0990** (0.0388)	0.0279 (0.0461)
Rule of Law	0.0758*** (0.0153)	0.0024 (0.0138)	-0.0212 (0.0132)
$\log(\text{Pop.})$	0.0061 (0.0145)	0.0003 (0.0063)	0.0084 (0.0085)
Arab. land	0.0210 (0.0615)	0.1354** (0.0540)	0.0024 (0.0697)
$\log(\text{rur. pop. den.})_{t-1}$	-0.0152 (0.0181)	0.0082 (0.0101)	-0.0005 (0.0069)
Christian	-0.0005 (0.0289)	-0.0023 (0.0148)	-0.1146** (0.0559)
N	77	138	142
p-value (Hansen)	0.341	0.735	1.000
p-value AR(2)	0.211	0.813	0.608
No. of instruments	19	23	23

Notes: Dep. var. y^a (in logs). *, **, *** indicate significance at the 10, 5, and 1 percent level.

Conclusions

- ▶ Mismatch in the conception of Fairtrade
 - ▶ Largest impact in middle-income countries.
 - ▶ Implied effect on poverty rather small as agriculture is more effective in reducing poverty in low-income countries (Christiaensen et al., 2011).
- ▶ Problems
 - ▶ Focus on smallholders excludes landless workers.
 - ▶ High costs of certification exclude poor smallholders.
 - ▶ Encourages formation of very large cooperatives (e.g. cocoa in Ghana).
 - ▶ Fairtrade requires well developed production structures.
 - ▶ Not a viable development strategy for the poorest countries.
- ▶ Impact is economically (yet) irrelevant (1.35 million farmers participate globally).

References I

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