# The EU Banana Regime and the Caribbean Island Economies


### *Dr. Stephen J.H. Dearden*

**Manchester Metropolitan University**



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It might appear strange that bananas should have represented one of the last remaining threats to the successful conclusion of the GATT Uruguay Round. France sought to maintain the protection the EU had established for ACP (African, Caribbean and Pacific) suppliers, while Germany refused to accept the GATT accord in case it weakened its challenge to the existing EU banana regime that it was challenging in the European Court. These difficulties were a continuation of the internal conflict within the EU which had its origins in the EU's attempt to establish a new regime to regulate the import of bananas under the single market programme.

The EU accounts for approximately one-third of world imports of bananas, which in 1992 were worth ECU 20 bn. Prior to 1993 the EU banana market had been fragmented by national import controls. Half of the EU's member states operated such schemes covering 40% of EU imports and ensuring preference for their traditional `colonial' suppliers and overseas territories (DOMs - Departements d'Outre-Mer). Spain obtained most of its bananas from the Canary Islands; Portugal from Madeira; France from Martinique and Guadeloupe, the Cameroons and the Ivory Coast; the UK from the Windward Islands, Belize and Jamaica (See Table 1). By contrast Germany, the largest EU market for bananas, allowed tariff free imports and was supplied by the more efficient Central and South American producers, who with their large scale irrigated plantation based production obtain yields double those of the ACP producers. Except in Germany `dollar' banana producers faced a Common External Tariff of 20%, while ACP imports entered duty-free under the Lomé Conventions (see also Table 2).

The removal of the internal barriers to trade with the creation of the EUs single market required the elimination of these different national import controls. It is the evolution of a common EU import regime for bananas that will be reviewed in this article, together with an examination of the importance of this product for the economies of a number of Caribbean island economies.

## The Policy Options

Although the EU maintained a CET (Common External Tariff) of 20% on banana imports, with the exception of Germany, there was also considerable variation in national import controls. The UK offered duty-free access to ACP producers and in

addition dollar banana imports were controlled by import licensing. Dollar banana import licenses guaranteed access for a minimum of 30,000 tons annually, with additional licenses should traditional suppliers fail to meet domestic demand. Similarly sixty per cent of the French market was supplied by its Overseas Departments of Martinique and Guadeloupe, with further imports supplied by African Franc zone countries such as Cameroon. Dollar imports were subject to licensing which would only be granted if prices exceeded certain levels. Italy granted free access to ACP imports, with Somalia being offered preferential status, but restricted other imports to a global quota which in 1983 was 270,000 tons. Spain was supplied by the Canary Islands and Portugal by Madeira and both excluded supplies from other sources. The estimated welfare loss of this system of import controls ranged from ECU 425 m. (Read 1993) to ECU 1.3 bn. (Borrell & Yang 1990,1992).

Faced with the demands of establishing a single market a number of options presented themselves to the Community. The problem could have been circumvented by allowing derogations to some of the member states to continue their import controls. Although the perishable nature of the product and the dominance of the market by a limited number of importing companies might have made this possible, it offered no long-term solution. At the other extreme a free market could have been established following the German example.

The consequences for EU consumers, ACP suppliers and dollar producers of the various policy options has been evaluated Borrell and Yang (1990). Following the analysis of Noich (1985) they suggest that the overall effect of the existing policies of the EU had been to increase world prices, subsidise favoured supplying countries and consumers in Germany at the expense of non-favoured dollar producers and of consumers in the remaining EU member states who restrict access to their markets.

Borrell and Yang evaluated the impact of four policy options; the extension of free trade to the whole Community, the adoption of a CET of 20% on all imports, a system of deficiency payments and direct aid payments. The adoption of free trade in bananas was found to raise EU consumption by 9%. Dollar banana imports would increase by 12% but ACP suppliers would see their exports fall by 46%. Although EU consumers experience a gain in economic welfare of $386 m. (in 1987 dollars) annually and dollar exporters gain $61 m. from access to the EU market and higher world prices, ACP countries lose $209 m. each year. These loses are substantial when compared to the value of ACP banana exports to the EU which totalled $576 m. in 1987.

Turning to the extension of a CET of 20% to Germany, with continuing ACP duty-free access to the Community, German consumers experience a substantial welfare loss of $85 m. Alternatively the ACP tariff concessions could be abandoned. This produces a smaller global welfare lose than the previous case since a non-discriminatory tariff allows rationalisation of production between exporters. However such rationalisation will again be at the expense of the ACP producers who will experience substantial loses. To address this problem a deficiency payment system might be established financed by a CET. Such deficiency payments would be received by the ACPs to cover the difference between the world price they would receive and their current protected prices. Borrell and Yang calculate that a tariff of 16.7% would be required to finance such a scheme. Again German consumers would be the major losers of such an approach.

However Borrell and Young favoured direct aid payments financed by a CET of 16.1%. Deficiency payments would encourage production in the ACP exporters by artificially raising prices. By contrast direct aid minimises the distortion to world trade and allows the targeting of assistance to diversification of the ACP economies. They estimate that direct aid payments to ACP exporters would total $273 m. annually, an increase of $64 m. on the existing level of implicit benefit from discriminatory tariffs. However it would still result in the same 47% reduction in ACP banana exports as in the free trade scenario. The impact upon some ACP countries of such a dramatic structural transformation of their economies is not easily dismissed and is an issue to which I shall return when we examine the nature of some island economies.

Davenport and Page (1991) carried out a similar simulation of the alternative regimes that might be introduced. They examined three cases; removal of quantitative limits on imports with a CET, deficiency payments and a quota system. With only a CET restricting imports, without any ACP preference, prices would fall to those prevailing in those member states with unrestricted dollar banana imports - ie. Belgium, Denmark, Ireland and the Netherlands. This was approximately ECU 4.5 per kilo, compared with a price of ECU 7 for EC bananas, ECU 4.5 - 6 for African imports and ECU 6 for Windward Island bananas. The competitiveness of ACP bananas is such that their market share falls from 52% to 28%, reducing their export earnings by 75%. Were the ACP's to be compensated for these losses at a rate of ECU 165 per tonne, Davenport and Page estimate that the cost to the EU would total ECU 200 m. (based upon 1988 prices and volumes).

Deficiency payments, to supplement EU and ACP producers incomes from world prices in a free market, would still encourage these producers to become more efficient. However unless the deficiency payments differentiated between producing countries the least competitive (eg. the Windward Islands) would still lose market share. The cost of such a scheme could be high unless financed, as suggested by Borrell and Yang, from retaining a CET on dollar banana imports. Davenport and Page find that price guarantees at ECU 7 per kilo for EU producers and at ECU 5 per kilo for ACP suppliers, financed in part by a CET of 14%, would still result in a 16% fall in ACP exports and a decline in export earnings of 24%.

A quota system would involve establishing limits on EU imports of dollar bananas, with a lower CET. ACP bananas would continue their unrestricted duty-free entry into the EU market. The larger the initial size of the dollar banana quota and the greater its growth rate, the lower will be the Community's price of bananas but the smaller the ACP's share of the market. The price of bananas will also be lower if an overall dollar import quota is established within which producers had to compete, perhaps by auction, for licenses.

It was also possible to adopt a mixed scheme, eg. of deficiency payments and quotas. However any import regime would still have to reconcile the trade-off between the maintenance of ACPs market shares and the loss of EU consumer surplus from higher EU banana prices above the free-market world level.

Import Trends

In 1982 the EC10 imported 1.87 million metric tonnes of bananas, approximately one-third of world imports. Of this total 17.6% (0.33 m. tonnes) was imported from the ACP countries. Over the ten years to 1992 EC12 imports increased by 116% to 4.0m. tonnes, with ACP exports doubling to 0.7 m. tonnes, worth ECU 413 m. Over this period the ACP share of EU imports has been unstable (Fig.1), peaking at 25% in 1986 and declining to 15.4% by 1992. The decline in the ACP market share in 1991 and 1992 resulted from the dumping of surplus tonnages of dollar bananas and was regarded by some ACP producers as an attempt to to capture market share in anticipation of the SEM.

Germany represents one-third of the EU market for bananas, supplied exclusively by low priced dollar banana producers. Spain, Italy, France and the UK each account for 10%-14% of the total market. The UK imports 90% of its bananas from ACP countries, with 52% coming from the Windward Islands. France imports 59% of its bananas from the Overseas Territories of Guadeloupe and Martinique, while Spain imports all of its bananas from the Canary Islands. Except for its imports from Somalia (15%) Italy relies on dollar banana imports.

The distribution of bananas is dominated by three US Multi-national companies (MNC) - United Brands (formally the United Fruit Co.), Castle & Cooke (formally the Standard Fruit Co.) and the Del Monte Corporation. The latter entered the industry in 1967 through the purchase of the West Indies Fruit Co. These companies are principally concerned with supplying the US market from Central and South America, but through subsidiaries (eg. United Fruit's Elders & Fyffes) they also supply Europe. In 1980 63% of world exports of bananas were controlled by these MNCs (Read 1986). Their vertical integration had allowed them to resist new entrants. Nonetheless, in recent years they have withdrawn from the direct ownership of their specialist shipping and reduced their own plantation production. In 1974-76 United Fruit produced 75% of it's bananas from it's own plantations, but Standard Fruit relied on contracting independent producers for 53% of it's bananas and Del Monte for 57%. They have also faced a challenge from an inter-governmental owned banana company (Comunbana), the marketing arm of the Union de Paises Exportadores de Banano (UPEB). Formed in 1974 it is a producers association including all of the banana producing countries of Central America. Its principal market was the US, but it also exported to Greece and Italy. However in 1983 the company ceased trading, ending government attempts to gain a foothold in the international market.

The Caribbean Island Economies

Banana exports are important to a number of the islands of the Caribbean. Martinique and Guadeloupe are external territories of the EU and the volume of their exports is illustrated in Fig.2. In 1972 Guadeloupe was exporting 121,110 tonnes of bananas to France and Martinique 185,823 tonnes, by 1982 this was little changed for Guadeloupe at 120,921 tonnes, but Martinique's exports had fallen by 25,000 tonnes to 159,405 tonnes. Both islands experienced a substantial decline in the volume of banana exports from 1987 to 1989, followed by a recovery; however their share of the EU market actually increased over these years (Fig.3) reflecting the smaller decline in French imports ((31%) compared with the Community average (39%). For both islands bananas are an important source of foreign currency generating approximately 50% of their total merchandised export earnings. As high cost producers, especially as

both islands are covered by French minimum wage laws, their exports are confined to France.

Banana production in Jamaica began very early in 1901 and exports to the UK peaked at 300,000 tonnes. However in the 1970s the industry went into decline and by 1974 it was exporting only 66,800 tonnes. In 1981 a fundamental review of the industry took place, with the formation of BECO (the Banana Export Company) to help in restructuring production and marketing. Investment, funded by the Commonwealth Development Corporation (£11.8m.) and the International Finance Corporation (£3.8m.) has been concentrated in three large plantations and yields, as a consequence, are comparable to those of the Latin and Central American suppliers. By 1990 it produced 128,000 tonnes of bananas and exported 63,181 tonnes to the UK, its only EU market. As the volume of bananas exported to the EU has increased (Fig.4) it has taken an increasing share of Jamaica's total banana exports. In 1989 Jamaica exported 43,000 tonnes, but only 20,000 tonnes to the Community. By 1991 93% of its banana exports were to the EU and totalled 70,000 tonnes. Over the whole ten year period 1982-92 Jamaican banana exports to the EU tripled, the increase occurring in the years 1989-1992 and reflected in an increase in its EU market share (Fig.5). However Jamaica is a diversified economy and banana exports represented only 4% of its $1157m. of merchandised exports, although 34% of its $132 m. of non-fuel primary exports.

Jamaica was one of the earliest countries to attempt to break the control of the US MNCs. In 1929 the Jamaican Banana Exporters Association had been formed to offer a centralised export agency for the 6,000 small growers. It signed sales agreements with Standard Fruit, acquired part-ownership of some shipping and established a European marketing subsidiary. It was succeeded by the Jamaican Banana Board in 1947, which sells directly to wholesalers in the UK and through Elders & Fyffes. The Board has also been active in introducing new disease-resistant varieties and new packaging.

The Windward Islands

The Windward Islands of Dominica, Grenada, St.Vincent and St.Lucia are all independent countries and as such gain access to the EU under the Lomé trade concessions. Unlike Jamaica, bananas are of far greater significance to their economies. Bananas are one of the most labour intensive crops produced and account for between 23% and 34% of agricultural employment in these islands, itself one-third of all employment (Thomas 1989a). Banana production for export had expanded rapidly in the 1950s, encouraged by the UK government as a substitute for the declining sugar industry. First the large sugar estates diversified, to be followed by the smaller farmers. Production peaked in 1969 before the increase in costs following the 1972 oil price shock. Production was also adversely affected by hurricanes in 1979 and 1980. Estate production declined throughout the 1970s so that today bananas are principally produced by small and medium sized farmers (eg. 97% of production in Dominica is by farmers with less than 10 acres) (Thomas 1989a). It is estimated that banana production employs, directly and indirectly, 31% of the Windward Islands labour force (House of Commons, Agricultural Com. 1992). As with Jamaica each Island has a Producers' Association which has a statutory monopoly on the sale of

bananas. These Associations in turn had an exclusive marketing contracts with Geest, which controlled 45% of the UK market.

St.Lucia and St.Vincent only export to the EU and have shared a substantial increase in their exports, increasing by 200% and 170% respectively between 1982 and 1992 (Figs.4 & 5). Banana exports for St.Lucia in 1991 at $54.8 m. represented 54% of all export earnings, while for St.Vincent they were 50% of merchandised exports at $33 m. Banana production accounts for 36% of agricultural employment in St.Lucia and 21% in St.Vincent. Except for 1986 their share of the EU market has been steady at approximately 3% and 2% respectively.

Dominica has shared in the increase in its volume of exports to the EU, doubling from 26,438 tonnes in 1982 to 55,932 tonnes in 1992, with their share of the EU market averaging 2%. As with the other Windward Islands most of their exports went to the UK. In 1991 the value of these exports was $30 m., 59% of export earnings. Production absorbs 43% of the agricultural labour force.

By contrast Grenada has experienced a slight fall in its exports to the EU, down from 9,294 tonnes in 1982 to 6,015 tonnes in 1992, with a consequent fall in market share from 0.5% to 0.1%. Banana exports to the EU, its only market, earned $3.7 m. in 1991, 19% of merchandised exports. Unlike the other Windward Islands cocoa and nutmeg are more import export crops than bananas, and their production only involves 7% of the agricultural labour force.

The real wholesale price obtained in the UK rose by approximately 50% over the period 1966 to 1986 (Thomas), although in part this is affected by a change to the supply of higher cost higher quality produce. These trends contrast with the more volatile world free market price (Fig.6). Most of the fluctuation in Windward Island earnings from banana exports therefore arises from variability in the volume of exports, which as we have seen have been increasing.

Although bananas are of considerable significance to all of the Windward Island economies the industry has developed few forward or backward linkages. Inputs are imported and little processing is required before export. Farmers' earnings from banana production have not been channeled into alternative crops nor into tradeable manufactures. Dependence on banana production therefore remains high, except in Grenada. Although the Island governments have been attempting to improve their competitiveness with dollar bananas by increasing yields and reducing post-harvest loses, they have also been encouraging diversification of their agricultural sectors. In Dominica potato production has been encouraged to substitute for imports and in St.Lucia locally grown fresh vegetables to supply the tourist industry. To replace bananas as the dominant export crop Dominica and St.Lucia have promoted the production of mangos, grapefruits, avocados and oranges. However these attempts have met with only limited success. Bananas remain a far more attractive crop, with their labour-intensive capital-saving production and quick returns. Unlike the newly promoted crops, bananas are efficiently marketed through the Producers Associations and Geest. Further the high banana prices of recent years have undermined any attempt to encourage farmers to diversify (Thomas 1989b).

However these high prices have been dependent on the existence of their preferential access to the EU market. Davenport and Page (1991) have estimated that even with a quota on dollar bananas and with a CET of 14%, St.Lucia and St.Vincent would lose 25% of their export volume and 35% of their export earnings. While with only a CET of 14%, and no ACP preference, these two countries would lose about 55% of their exports and 70% of their earnings.

The EU Banana Regime

The Fourth Lomé Convention had committed the EU to ensuring that "no ACP state shall be placed as regards access to its traditional markets and its advantages on those markets in a less favourable position than in the past or at present." However in the negotiations of the Uruguay Round of the GATT the EU committed itself to the "fullest possible liberalisation of trade in tropical products." As these difficult negotiations continued they inevitably began to interact with the discussions taking place to establish a new Banana regime for the single European market. The threat existed of a challenge by the Latin American countries, under GATT procedures, to any adoption of quota system. Indeed the EU was already constrained by the existing GATT rules not to raise the average tariff on bananas. Thus the elimination of the German tariff-free quota on dollar bananas would require an offsetting reduction in any CET from 20% to 14%.

The Commission's response to the need for a Banana Protocol was not issued until August 1992 (COM 359/92). The new scheme was to be a combination of deficiency payments and import quotas. For the EU's own producers (Guadeloupe, Martinique, Canaries, Madeira and Crete) deficiency payments would be limited to 854,000 tonnes (cf. imports of 645,000 tonnes in 1990); ECU 1,000 per hectare would also be offered as compensation to any farmer who ceased production. ACP imports from the eleven traditional suppliers would continue to enter duty-free up to their 1990 level; but any greater volume of `non-traditional' ACP imports and all dollar bananas, would be subject to a basic quota of 2 m. tonnes. This would be increased if projected demand and supply conditions in the EU market suggested that a shortage might emerge. The proposal also introduced the `partnership principle' whereby 30% of import licenses would be reserved for importers who have established a partnership agreement with an ACP or Community supplier. As import licenses generate monopoly rents for importers, the Commission anticipated cross-subsidisation between the profits acquired from the import of dollar bananas and those from the import of EU and ACP fruit. It also provides some protection to ACP suppliers from predatory activities by `dollar' importers. However in the face of strong opposition from Germany and the Benelux countries and with the GATT negotiations seeking to remove non-tariff barriers to trade, the import quota proposal had to be abandoned.

The final version of the new banana regime (CEC 404/93) preserved duty-free access for ACP imports up to their traditional level. Traditional imports were initially limited to 622,000 tonnes, but the final figure is much more generous at 1.7 m. tonnes. This is now defined as the best ever import figure for each ACP state before 1991 and allows for existing expansion plans where appropriate (ie. Jamaica, 105,000 tonnes; St.Lucia 127,000 tonnes; St.Vincent 82,000 tonnes; Grenada 14,000 tonnes; Dominica 71,000 tonnes). This method of calculating the import limit will only constrain Jamaica in the short-run, but given the rising export trend for St.Lucia, St.Vincent and Dominica, it

must represent a serious constraint in the long term unless the EU concedes an upward revision.

For dollar banana imports and ACP imports in excess of their traditional level the EU adopted a tariff quota of 2 m. tonnes, subsequently revised to 2.2 m. tonnes for 1995-96. Within this limit imported dollar bananas will pay a duty of ECU 75 per. tonne, and `non-traditional' ACP bananas will continue to enter duty-free. Imports greater than 2.2 m. tonnes will be subject to a tariff of ECU 850 per.tonne (a rate of 170%) on dollar bananas and ECU 750 per. tonne on `non-traditional' ACP bananas. The overall quotas total 3.71 m. tonnes, compared with imports of 3.71 m. tonnes in 1991.

Even with a ECU 100 per tonne tariff advantage it would be unlikely that importers would substitute non-traditional ACP bananas for dollar fruit as part of their 2.2 m. tonne quota. Therefore to guarantee their market share the `partnership principle' is formally abandoned but replaced by the simple reservation of 30% of the licenses within the 2 m. tonne import quota for importers of `traditional' ACP and EU bananas. This will provide an incentive to ensure access to the EU market for ACP fruit in order for the importer to continue to retain their valuable license to import the more profitable dollar bananas. Nonetheless there remains the concern that the substantial profit margins likely to be made on quota dollar bananas may allow cross subsidisation for the import of non-quota dollar fruit and the capture of additional market share. Thus whether the proposed safeguards prove adequate remains to be seen. The remaining elements of the Regulation, which came into force on the 1st. July 1993, followed the original proposal.

The German government and Benelux importers attempted to challenged the legality of this Regulation before the European Court, but without success, although a second case may be presented. Also, as expected, the Latin American banana exporters initially requested the Protocols reference to the GATT panel. Only Guatemala pursued the objection and subsequently the GATT panel ruled against the regime. However in the face of opposition from the EU and ACP states the ruling could not be adopted by GATT; although it has thrown doubt upon the broader ACP preferences under Lomé and their future under the new World Trade Organisation.

At the same time as introducing a Banana Regime to control imports into the Community, the Commission has proposed additional assistance for those ACP countries that are likely to be adversely affected by the new regime (COM 465/92). Lomé IV had anticipated the problems for banana producers with the advent of the single market by offering financial assistance for diversification from its substantially increased ECU 1500 m. STABEX fund. This offers grants to compensate for destabilising reductions in export earnings from the sale of any of 49 products. For the island economies products will be eligible if they formed more than 1% of a States export earnings, which will be the case with bananas. However the Commission wished to go further in assisting the ACP countries to adjust to the new market conditions after 1993. They therefore proposed that financial assistance is made available to those ACP states that prepare programmes to improve the quality, marketing and competitiveness of their bananas. These funds will however be limited to ECU 30 m. to be allocated over a three year period to eleven eligible states. In addition they proposed that specific income support funds should be made available to these ACP countries should STABEX transfers be insufficient to compensate for the

loses experienced as banana prices fall. However it is intended that such assistance should only be temporary and continue only until stability returns to the banana market. Overall EU aid to the ACP producers is likely to total ECU 60 m. over a three year period, as compared with support of ECU 185 m. for EU producers. This special aid package was adopted in September 1994.

Conclusion

The changes to the EU banana market have been profound for a number of small and economically vulnerable ACP island economies. These changes have been driven by the demands of the establishment of the single European market but have also been influenced by the long drawn out negotiations of the Uruguay round of GATT. The problems of meeting competition from Latin American bananas is going to be severe for most of the Windward islands and yet the difficulties of attempting to diversify away from dependence upon this crop are equally problematic. The EU appears as unclear in the strategy that it wishes to encourage these islands to follow as are their own governments. It is prepared to fund programmes that improve the competitiveness of island bananas in the EU market while at the same time funding attempts at diversification. However it is clear from Thomas's studies that banana cultivation in the Windward islands will always be at a disadvantage compared with the plantation production of Latin America, while diversification will continue to be inhibited by the relative attractiveness of banana cultivation. For Guadeloupe and Martinique, their status as Overseas Territories of France will offer some protection; already as EU suppliers they will receive deficiency payments under the Banana Protocol. For Jamaica its larger economy may be able to absorb the adverse impact of a loss of EU market share. However for Dominica, St.Lucia and St.Vincent adjustment may prove much more difficult and their external status leaves them more vulnerable. As ACP mini-states their future may depend to a considerable degree upon the importance that the UK government attaches to their long term economic development.

Already there are signs of the difficulties that these islands may face. For Dominica banana exports in 1992 were 10% below expectations and grew only 2.7% to 55,500 tonnes in 1993. For St.Lucia and St.Vincent the situation has been even worse, with falls of 10% and 25% in banana exports between 1992 and 1993 to 120,129 tonnes and 58,771 tonnes respectively. These reductions were attributed to weak international demand. In September 1994 hurricane Debbie devastated the banana crops, reducing production by 40%. Although it strengthened prices it also reinforced the diversion of sourcing to `dollar' producers. For Geest the competition from dollar imports, with substantial price cutting, were unsustainable. In 1995 Geest sold it's banana interests to a joint venture between it's rival Fyffes and the Windward Islands Banana Development Company.

Meanwhile in the US legal action has been taken under Article 301 of the Omnibus Trade Act, which requires the US government to identify those countries undertaking unfair trading practices and authorises unilateral retaliatory trade restrictions if they continue. But the greatest challenge to the new Regime has been the complaint registered with the new World Trade Organisation by the United States and four Latin American countries. In March 1997 the Disputes Panel issued it's interim report which found that "fundamental elements" were inconsistent with WTO obligations.

Specifically it has ruled against the guarantee of 30% of the EU market for traditional ACP exporters and the differential treatment of banana exports from Colombia, Costa Rica, Nicaragua and Venezuela compared with the rest of Latin America. It also criticises the size of the ACP quotas as being well above their maximum exports in the past. However the report accepts the principle of preferential tariffs for ACP banana exports and supports the exemption of the Lomé Convention from the full force of WTO rules. Although unlike GATT decisions the EU is obliged to accept WTO rulings, further negotiations are likely, with the possiblity of an approach to the Appeals Tribunal.

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