



CBI cases on trade cost reducing initiatives

This paper provides an overview of cases that depict public, private and public-private initiatives aimed at reducing trade costs. These cases have been gathered by the Centre for the Promotion of Imports from developing countries (CBI) for the World Trade Organization (WTO) in preparation of its 5th Global Review on Aid for Trade.

Case 1. Food Compass: a Dutch private sector initiative to improve compliance with food safety standards and simultaneously reduce pesticide residue monitoring costs.

What is the issue?

Dutch companies that are trading or processing fresh fruits and vegetables have to comply with the European and Dutch Food Law. An important aspect of the food law is the testing of fresh produce for pesticide residues. Within the Dutch Code of Practice on Hygiene these tests are obligatory. Fresh fruits and vegetables have to comply with maximum residue limits (MRLs) in order to be allowed to be placed on the market. In addition to these legal requirements, test reports are also required by clients within the food chain and several European retailers have introduced private standards for pesticide residues on fresh produce that are more strict than the legal standards.

Which trade costs does this bring along?

Testing for pesticide residues is a costly affair for companies. In the Netherlands, a major trade hub for fresh fruits and vegetables, each year an approximate 100,000 tests on fresh fruits and vegetables are conducted. The vast majority of these tests are conducted on behalf of the businesses themselves and approximately 3,000 are conducted by the Dutch Food and Consumer Product Safety Authority (NVWA). The costs for sampling and analysis amount to an estimated 10 to 20 million euro annually.

Furthermore, since testing takes time -- ideally one or two days, but occasionally much longer if not properly managed -- it brings along market risks and costs as fruits and vegetables have a limited shelf life. Costs can also occur for the overseas supplier, as they may be faced with a batch that is rejected at the Dutch

or EU border due to pesticide residues that exceed the MRL. The latter costs are particularly relevant for SME suppliers of fresh fruits and vegetables in developing countries, who often lack proper residue testing facilities.

What is the solution?

[Food Compass](#) is an independent, Dutch non-profit organisation that provides a residue monitoring service to its associate members. Food Compass was established by the Fruits and Vegetables Trade Association of the Netherlands ([Frugi Venta](#)) and the Dutch Product Board for Horticulture with the aim of providing companies a cost-effective monitoring solution in compliance with the requirements of the Dutch Code of Practice on Hygiene. Food Compass receives advice from an expert panel that includes representatives of the NVWA.

Once a company has signed up to Food Compass, an independent (and certified) inspection body takes samples of its product range. Product sampling is based on a sector risk assessment and performed according to the European Directive that has set methods of sampling for the official control of pesticide residues in and on fresh produce. Analysis of these samples takes place at accredited laboratories. Both sample data and analysis results are entered in the Food Compass web portal. Participants automatically receive an e-mail once new results have been entered and released. From the portal they can download analysis reports as well as spreadsheets with their sample and analysis data. In case of a MRL-exceedance, Food Compass informs the participant in question about the actions that are to be taken. Through the Early Warning & Response System (EWRS) all participating companies are informed when a potential health risk is identified at one of the companies that could be of importance for the other companies. Also, participants have access to the EWRS-database that is updated with thousands of test results annually. All EWRS-information has been made anonymous to increase the willingness to share data and the potential to learn from it.

How does this reduce trade costs?

For Dutch importers of fresh fruits and vegetables, Food Compass reduces trade costs in multiple ways:

1) Reduced costs of sampling & analysis due to the collective, risk-based approach

Food Compass has based its sampling and testing on a sector risk assessment. This assessment looks into many aspects including the MRL-exceedances of the past two years and the consumption data of the different products. Because of the risk-based approach, far fewer test results are required for an improved risk management. This reduces pesticide monitoring costs while simultaneously improving compliance with food safety standards. About 50% of the MRL-

exceedances are found in 10% of the product groups. Further refinement is done using various specifications such as country of origin.

Food Compass has annually almost 2,000 samples taken for pesticide residue analysis. The number of test results that is required for risk management is therefore much lower than when all companies would only use their own test results, or when companies have samples tested without using a risk assessment at all.

As of 2015, almost 300 companies joined Food Compass, representing approximately 60% of Dutch produce and imports of fresh fruits and vegetables. Due to this collective approach, Food Compass is able to make a robust sector risk assessment. In addition, the economies of scale allow Food Compass to perform a large number of tests for various companies at the same time, reducing the average costs per test.

2) Efficient handling of samples & test results through standardization & automation

Food Compass collaborates with professional sampling officers and laboratories. Because procedures have been defined for taking and processing samples, it is clear how test results come about. Therefore, costs arising from ambiguous test results are greatly reduced.

Furthermore, Food Compass has a web portal in which company details, sample data and test results are entered in a well-structured manner. Associate members can view and download data once logged on. This standardization and automation has reduced the risk of delays and errors, and costs involved, when reporting test results.

3) Reduced costs of non-compliances through improved issue management & learning

In the case of an exceedance of the MRL, Food Compass conducts a further assessment to identify the potential food safety risk. In the case of a food safety risk, an anonymous alert is sent out to all participants. This alert describes what is going on (specification of the problem), what measures have been taken and are to be taken, and how Food Compass will adjust its monitoring accordingly. The affected company receives assistance from Food Compass on how to mitigate the risk.

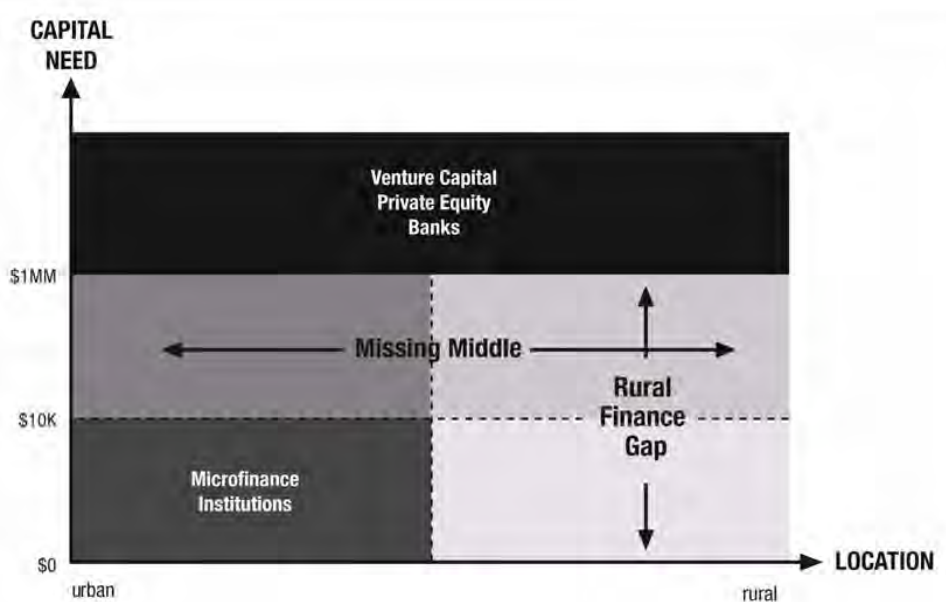
Food Compass shares the (anonymous) findings of all its tests, as well as the sector risk assessment, with its associated companies. This information helps companies to gain better insights into the potential risks of products and their countries of origin. This improved understanding on risks has a preventive cost reduction effect. When Food Compass test results from a specific product and/or country show multiple or serious defects, this can also be used by Frugi Venta to

engage in a problem-solving dialogue with public and private representatives from the producing country and sector. In this way, the problem may be solved at its origin in a well-informed manner.

Case 2. Council on Smallholder Agriculture Finance: targeting agricultural businesses in the “missing middle” in low- and middle-income countries

What is the issue?

The lack of access to finance for SMEs, a large sector not served by microfinance institutions and not effectively covered by commercial banking institutions, is commonly known as ‘the missing middle’. Estimates of the size of this credit gap are that about 45 to 55 percent of formal SMEs have no access to finance at all and 21 to 24 percent are underserved. The unmet credit needs of formal SMEs in the developing world account for an approximate \$850 billion.¹ If they are unable to obtain any or enough financial resources, they cannot grow into larger companies. This troublesome issue is particularly relevant for small-scale agricultural firms in the South.²



Source: Oxfam (2009)

Which trade costs does this bring along?

SME agricultural businesses in developing countries are often faced by limited access to (trade) finance, hampering their trade and growth potential.

¹ IFC (2013) IFC jobs study. Washington, DC: International Finance Corporation.

² Doran, A., McFadyen, N. and Vogel, N.C. (2009) The missing middle in agricultural finance – relieving the capital constraint on smallholder groups and other agricultural SMEs. Oxfam GB: Oxford.

Furthermore, when they do gain access, they are often charged high costs due to their perceived high risk profile. Financial institutions need higher returns to compensate for the higher transaction costs and risks in agriculture. Additionally the collateral requirements from the financial institutions are too high for many SME's and or not reflecting the needed amount (over collateralized) or the purpose of the loans (fixed assets as collateral for a short term loan).

What is the solution?

[Rabo Rural Fund](#)'s main objective is increasing access to finance in the agriculture sector in a sustainable way, supporting SME's in their future growth. Because of the extended knowledge and strong focus on the Agribusiness, Rabobank is able to assess the appropriate risks and as such structure adequate facilities suitable for the SME's active in the agriculture sector. Together with the [Council on Smallholder Agricultural Finance](#) (CSAF), an alliance of Belgian, Dutch, UK, US and Swiss social lending institutions (Alterfin, Oikocredit, Rabobank Rural Fund, responsAbility Investments AG, Root Capital, Shared Interest Society and Triodos Investment Management) Rabo Rural Fund is targeting agricultural businesses in the "missing middle" in low- and middle-income countries.

Social lenders participating in the council exchange lessons learned and work toward defining industry standards and best practices related to over-indebtedness, risk management, fair competition, transparent pricing, and social and environmental impact. For instance, council members shared and discussed one another's social and environmental due diligence tools and approaches, which facilitated improvements and increased harmonization.

How does this reduce trade costs?

CSAF members convene on a pre-competitive basis to exchange learning, identify best practices and develop industry standards across three areas:

1) Market growth

In 2013, the founding members of the council disbursed a combined \$362 million in loans to agricultural businesses. By 2016, council members target disbursements of \$500 million with growth in existing geographies and agricultural crops as well as to a wider range of geographies, crops and financing needs. This way, CSAF aims to meet a greater share of the vast financing need of the world's 450 million smallholder farmers. In order to support the growth of the middle missing, the members of CSAF work closely together in club deals and co-financing structures, reducing trade costs for the SME's.

2) *Responsible Lending Principles*

Council members have drafted a set of Responsible Lending Principles for impact-first agricultural lenders. These principles are promoting market growth that contributes to positive impact on agricultural businesses, the smallholder farmers they aggregate and long-term sustainability of the sector.

3) *Social & Environmental Impact*

Council members have identified a set of seven impact metrics that they all collect and will share on an annual basis. These metrics will form the basis for deeper impact analysis in the future. Individual organizations complement these impact metrics with more detailed case studies and evaluations.

Case 3. Standard contracts for global coffee trade

What is the issue?

As with other vulnerable agricultural commodities, an important aspect of the global trade in coffee revolves around making clear agreements between trading partners on their responsibilities regarding the coffee they are trading. For the buyer, it is important that he receives the proper amount of coffee with the right quality, at the right time and place for the right price. For the exporter of the coffee, it is important that he receives his payment on time and according to what he agreed upon with the buyer. For both actors, it has to be clear what the terms of delivery and notifications are and who is responsible for what. As such, transparent and reliable contracting is a key element in coffee trading.

Which costs does this bring along?

Setting up contracts can be a complicated and expensive exercise for companies, particularly SMEs who often lack the required legal knowledge and capacity to compose solid contracts that do not have any caveats. Furthermore, when trade takes place on the basis of poor or incomplete contracts, both exporters and buyers may incur costs when something goes wrong along the trading way and it is not clear whose responsibility this is. This may result in costly legal charges and claims.

What is the solution?

The trade in green coffee is facilitated if a shipment is bought and sold under the same conditions of sale. These define in a balanced way the responsibilities of seller and buyer in respect of – for instance – notification periods, insurance, force majeure and arbitration. The Contracts Committee of the [European Coffee Federation](#) (ECF) publishes and maintains four major standard coffee contracts that form the basis of the specific contract between buyer and seller. These contracts contain the most important and commonly used trade conditions and

notifications that come along with coffee trading. In order to create ownership and consensus on the design and content of the standard contracts, ECF consults both global purchasers of coffee as well as producing countries. The ECF standard contracts are widely used amongst coffee exporters and importers globally (except for US market, which has its own standard contracts), both small and large companies alike.

How does this reduce trade costs?

The standard contracts of ECF have various positive effects that reduce trade costs in the coffee sector:

- (1) Harmonisation and standardisation of legal terms in coffee trading, which creates predictability and enables coffee traders to draft 'simple' contracts of their own (they can refer to the ECF standard contract in their own contract, thus covering numerous practical implementation elements);
- (2) More transparency on trade conditions and notifications, as well as a common basis of understanding for coffee exporters and importers, which strengthens reliability;
- (3) No breach in trade conditions when coffee switches from one trader to the other;
- (4) In the end: lower legal costs for coffee exporters and importers.

Case 4. Import authorisation for organic products

What is the issue?

All produce from third countries labelled as organic must conform to strict rules which cover all stages of production and processing. The EU regulates both organic food and drink produced and/or processed within the EU and organic goods from elsewhere. These can readily be imported from so-called recognized third countries whose rules on organic production and control are equivalent to the EU's (i.e. Argentina, Australia, Canada, Costa Rica, India, Israel, Japan, New Zealand, Tunisia, Switzerland and the USA).

For all other third countries, including a large number of developing countries, importers need to have their organic products certified for import into the EU by independent private control bodies approved by the European Commission (Transaction Certificate or Certificate of Inspection).

Until July 1, 2014, it was also necessary for many organic products from non-recognized third countries that European importers were in the possession of an import authorisation for organic products, provided by their national competent authority. This authorisation needed to be in place well before goods are to be imported and was valid for a single year.

Which costs does this bring along?

The import authorisation required additional paperwork for many importers, who already provided costly third party evidence for the organic products they wanted to import into the EU from outside the EU (i.e. the Transaction Certificate). Furthermore, the issuance of an import authorisation by a competent authority often proved to be a lengthy procedure which needed to be in place before organic products were allowed to enter the EU market as officially approved and recognized organic products. If not in place on time, customs clearance of these organic products was not possible, meaning that the products could not be marketed on the EU market as organic products.

What is the solution?

As of July 1st 2014 it is no longer needed for EU importers to have an import authorisation additional to the Certificate of Inspection by a control body that is recognized by the EU for the product.

How does this reduce trade costs?

Apart from the costs of an additional import authorisation and the bureaucracy that comes along with this, the removal of the import authorisation also reduces the risk of organic goods getting stuck at the border due to a missing authorisation (which brings along a potential loss of products that can be sold on the European end market, especially for perishable goods).

Case 5. Ethiopian Commodity Exchange for trade in coffee and sesame seeds

What's the issue?

The Ethiopian Commodity Exchange (ECX) was set up in 2008 to serve as the link between farmers and exporters of two of Ethiopia's key export commodities: coffee and sesame seeds. The objective was primarily to enhance market access and values paid to farmers which were perceived as too low. Unfortunately the ECX was set up in a crude fashion for sesame seed with quality compromised by failure to classify and traceability lost by mixing or parcels. This has added high levels of cost to exporters although farmers have received higher values as a function of a higher market price.

What is the solution?

The Government of Ethiopia has realised the problem and recently introduced two initiatives to improve the ECX, mainly targeting the important role played by warehouses in this trading system. First of all, assisted by donor agencies such as USAID, it has started to develop a traceability procedure within the ECX warehouse system. An automated bag tagging system will be implemented this year that allows to trace back individual bags of coffee or sesame seeds at the washing or cleaning station. Furthermore, large producers of coffee and sesame will be allowed to tag their own produce at farm gate.

Secondly, a separate quality control system will be installed at all ECX-connected warehouses. This will be different from the current situation in which quality control and trading (exchange) are part of the same institution at the warehouses, which tends to emphasize its trading tasks over the quality control. With a separate quality control unit that is equipped with a newly installed warehouse inventory system, quality control will receive the much needed attention it deserves.

How does this reduce trade costs?

These two initiatives seem to be crucial steps for Ethiopian's export diversification strategy for coffee and sesame, aiming at high-end markets for their specialty coffees and seeds. At the same time, the automated warehouse systems and modern facilities will increase efficiency at warehouses and reduce handling costs. In the end, this should benefit Ethiopian coffee and sesame producers and exporters as well as international buyers (see figure below).

Who will Benefit from ECX Traceability Initiative?

Suppliers, Exporters, International Buyers and ECX

ECX Suppliers

- ▶ Can easily get product history/documentation
- ▶ Create better quality assurance, as it permits tracing back upstream
- ▶ Create transparency in ECX operation - sampling, grading etc.
- ▶ Build confidence in ECX system
- ▶ Safer coffee
- ▶ Creates opportunity to produce in better quality and quantity

ECX Exporters

- ▶ Opens up more opportunity
- ▶ Create confidence in ECX system
- ▶ Resolves coffee quality dispute
- ▶ Meet international market demand
- ▶ Easily access to a product's history
- ▶ Access to data and reports regarding products
- ▶ Guarantees the quality and safety of the product
- ▶ Get traceability certification

International Buyers

- Improves production inventory, quality management and control
- Gives better solution for conflicts related with quality certification
- Easily access to a product's history
- Better stock management – identifying average weight, moisture
- Gives transparency and better customer service
- Satisfies buyer desire for traceability
- Easily access to a product's history
- Gives opportunity for buyers to invest in this sector
- Gives better business opportunities
- Helps the product be sustainable

Source: ECX Traceability System Demonstration (2014)

Additional cases (we can further elaborate on these as well):

- Cashew nuts Warehouse Receipt System in Tanzania (in addition to Ethiopian ECX case);
- Strategic coordination between European Coffee Federation and major shipping lines to optimize logistics of global coffee trade;
- Aspire programme in Ethiopia:
http://www.snvworld.org/sites/www.snvworld.org/files/documents/eth_aspire.pdf