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The Emergence of Fair Trade as a Development Channel

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Abstract: *Since the late 1980s, fair trade has emerged as a mechanism for supporting development initiatives in many countries. After reviewing economic arguments supporting fair trade, we draw upon arguments from Scholastic theology to argue that it should be understood as an economic mechanism for promoting the practice of justice rather than charity. JEL: B41, L4, O1. Keywords: fair trade, just price, economic development.*

From rudimentary beginnings in several European countries in the late 1980s, a global alliance of organizations has emerged, to promote the concept of fair trade as embodied in the standards for production set by FLO International (Fairtrade Labelling Organization International).[1] While the best known component of these standards is a price floor, the contractual terms covered by certification include labor conditions that are binding upon employers, the payment of a "Fairtrade premium" for use in social projects, the availability of project finance over the crop cycle, minimum contract lengths, and non-discrimination clauses that are binding on all producer organizations.[2]

In the UK, the largest single market for certified products, certified retail sales increased from £50.5m to £1,127m between 2001 and 2010. This average growth rate of 36.7 percent per annum has been sustained throughout this period, and is partly the result of growth of interest in

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certified products among consumers and retailers, and also of considerable product diversification from the original offering of tea, coffee, and chocolate (FLO, 2011; 2012; Fairtrade Foundation, 2011).[3] Worldwide, the 2010 retail value of certified sales was €4,361m (FLO, 2011).[4] From this, producers received €550m (approximately €478 for each of 1.15m individual producers and workers), and producers' organizations received a further €51.5m on account of social premia (approximately €56,900 for each of 905 producer organizations). Compared with leading businesses or even development charities, Fairtrade remains a relatively modest initiative. Nonetheless, especially in North West Europe, it confronts many consumers weekly because certified products are available so widely.

A specific category of "fair trade" is problematic for economists, not because economists support "unfair" trade, but because the adjective "fair" seems redundant; quite simply, in the context of economic theory, it is easy to argue that all trade should be fair. The category seems useful in arguments in other social sciences that purport to demonstrate that prices agreed by market participants are not "fair," or, introducing the term that we shall use later in this paper, "just." We consider an exchange to be just if the value received by each party for the resources that they give up is at least the "true" value. In particular, advocates of certification argue that without intervention of some kind, wage rates for labor or, for small producers, the commodity price, will be so low as to be unjust because neither offers a reasonable return to the total effort expended.

Economics quickly parts company from philosophy and other social sciences on this question, especially if "true" here suggests that there is some objective measure of value. Economists typically deny this, seeing value in terms of market based opportunity costs. In this framework, values are personal measures of the best alternative use of resources, and so are both largely subjective and created in the market. Adopting this understanding of the nature of value, it is usual to argue that if two parties agree to the terms of an exchange, then both must consider it to be in their interest to do so. In other words, taking part in the exchange must be at least as good for both parties as any alternative use of the resources. The opportunity cost of participation in an exchange is never negative.

For economists, it follows that in a world in which there are no transaction costs, and in which information flows freely so that everyone is perfectly informed, the allocation of resources resulting from market-based interactions will be efficient, in the sense that all resources end up being owned and applied in the way that creates most value. For this reason, economists often prefer to move the discussion away from ethical concepts such as the achievement of justice in exchange to relatively technical and seemingly morally neutral arguments about the ways in which outcomes might fail to be efficient, in their specialist, technical sense. Sources of economic inefficiency include market power, which in the case of fair trade, usually means the alleged monopsony power that a single, large buyer can exert over the many sellers of the good, or else blockages in the flow of information that prevent potential buyers from verifying the quality of the goods that they might purchase.

To bring together economic and other arguments supporting fair trade, we review arguments for justice in exchange that emerged during the thirteenth and fourteenth centuries. In this period, the teaching of economics in Western Europe was, as Langholm (1992) argues, largely confined to priestly formation, and much of the teaching that applied the concept of the just price was designed to enable priests to advise parties to a transaction as to what that price might be. As we shall see, the just price is not an alternative to the market price in this setting. Rather, it is a price that an independent expert considers to be reasonable in circumstances where there is no effective market, for example where the volume of trade is very small. We might also imagine an appeal being made to the just price doctrine where one party to a transaction has very little economic power, so that in a bargaining process, the other party is effectively able to extract all of the economic surplus from the transaction. The claim of just price theorists is that the share left to the weaker party is so small as to require a further transfer to be made. We can relate this to arguments in welfare economics that efficient outcomes need not be equitable, so that they might reasonably be supplemented by resource transfers. However, the argument from justice is that the stronger party to the transaction has a duty to recognize the undesirable features of the final outcome and so should anticipate them by refusing to utilize bargaining power to the fullest possible extent.

Bringing together the arguments from economics and philosophy, we note that both are effectively concerned with a co-ordination problem that can easily be resolved if all parties recognize the nature of their obligations to each other. Certification, we argue, has emerged because producers cannot credibly claim to pay their suppliers more than the market price for their labor without there being some external authority verifying the claims. This is very similar to the problem that churches must resolve to overcome free-riding, for example within the club good model (Iannaccone, 1992). We conclude that one reason for Fairtrade products viewed favorably from their inception by faith-based organizations is recognition that the mechanisms and objectives of Fairtrade are largely consistent both with churches' organization and also their historic teaching.

1 Certified Trade: Structure and Scale

The production process for certified goods involves producer organizations in the global South; processing, wholesale, and retail organizations, many of which, like the UK-based retailers that we describe below, are engaged in conventional production and distribution processes throughout the world; certifying organizations, such as the Fairtrade Foundation in the UK, most of them working under the FLO-International protocols; and consumers, who choose to purchase certified goods. As noted in the introduction, Fairtrade certifiers impose contractual arrangements, which affect the conduct of the small-scale primary producers participating in certified trade as well as the large-scale processors and retailers. For example, FLO-International contracts are long-term, offer project financing across the crop cycle, include a minimum price that is typically above the spot price for the commodity,[5] and provide for a fair trade premium, which is supposed to "help producers to improve the quality of their lives. It is paid on top of the agreed Fairtrade price, and producers decide democratically how to use it. Typically they invest it in education, healthcare, farm improvements, or processing facilities to increase income" (Fairtrade International, 2011).

The distinction between the price and the premium does not seem to have been exploited in the economics literature.[6] The economics literature also does not seem to have noted the anti-discrimination clauses of Fairtrade contracts, and the restrictions on production techniques, largely designed to meet European "organic" standards. These last conditions often enable retailers to sell certified products as premium brands. As we shall discuss towards the end of the paper, these characteristics of the certified trade give us good reason treat it as being designed to address problems of incentive compatibility.

1.1 The Emergence of Fairtrade in the UK

For many years, the UK has been the largest single market for certified goods, accounting for approximately thirty percent of global sales in 2010. An important feature of market in the UK has been the widespread adoption of certified products by supermarkets. Three national chains, Sainsbury's, Waitrose, and the Co-operative, have committed themselves to using certified produce in own label production, and have either established or use existing charitable trusts to provide additional development funding for producer organizations, partly funded from trading profits and partly from additional corporate donations.[7] Another large retailer, Marks & Spencer, has incorporated the sale of certified goods in its commitment to environmentally sustainable trading, "plan A." Thus, in the UK, certified products are no longer sold primarily by self-described ethical retailers, but have become an important element of the marketing mix of large corporations.

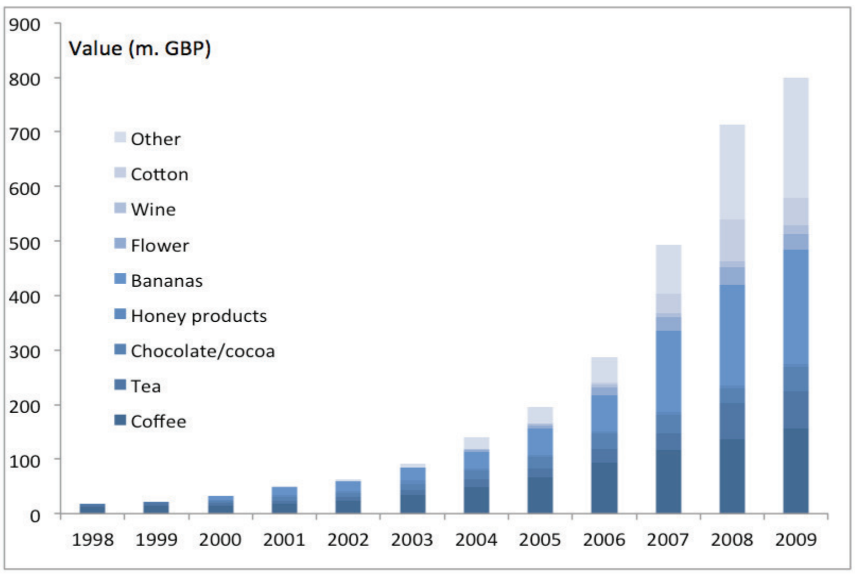

Figure 1: Sales of Certified Products in the UK, 1998-2009

Figure 1 illustrates the pattern of growth of certified products between 1998 and 2009. Beginning from a narrow range of coffee, tea, and chocolate, probably the important breakthrough was the promotion of certification as a means of supporting the UK's traditional banana suppliers in the Windward Islands (see Moberg, 2009). The nature of banana supply is such that only the largest retailers can contract to receive shipments, and the willingness firstly of the Cooperative and, soon after, of other leading supermarkets to do this rapidly widened the visibility of certified products in the UK.

2 Economic and Sociological Perspectives

The economic literature analyzing the working and effects of Fairtrade product certification is still quite rudimentary.[8] Much of the earliest work, for example Becchetti and Adriani (2002) and Hayes (2006) provides a largely positive account of the capacity of certification to reduce monopsony power among hirers of labor in rural areas of developing countries. In the context of large businesses buying directly from small producers, this approach claims that fair trade ensures a more equitable distribution of market power, and so, by reducing the market inefficiencies, it has the potential to be Pareto improving. It is not clear in these models how the presence of small producer co-operatives can affect monopsony substantially. An ethnographic account of coffee growing in Oaxaca state in Mexico, Jaffee (2007) recalls an encounter with a *coyote*, the local buyer for the spot market, who turned out to be almost as detached from the world markets as the growers. This suggests that the role of local co-operatives may perhaps be in dissemination of information, but also in monitoring behavior of growers, and other economic models have attempted to include these factors.

It is probably reasonable to claim that most economists are sceptical about the idea of certification. A forceful argument against it is found in Sidwell (2007), who notes the relatively small premium that is actually received by farmers.[9] In this reading, fair trade is essentially a method that allows retailers in the North to segment markets and benefit from price discrimination.[10] The paper also questions whether fair trade will be beneficial in terms of macroeconomic development, arguing that in the absence of monopsony, fair trade does not clearly benefit farmers, but instead land owners, and will also consolidate patterns of land holding and production, retarding diversification away from cash crops. This analysis receives little support in the sociological analysis that we review in the next section. Other concerns have been raised by Cameron (2004), who questions whether fair trade can benefit the urban poor, noting the importance of cities in generating economic growth. Lastly, Maseland and de Vaal (2002) have used trade models to compare fair trade with free trade and protectionist models, concluding that at a macroeconomic level, there is no decisive argument to be found in theory. This analysis seems to assume that fair trade is a much larger phenomenon than it actually is at present: as noted in the introduction, the global remittances associated with Fairtrade are less than the project funding of the UK's leading development charities.

2.1 An Industrial Organization Approach

The most recently developed economic models attempt to assess the value of certification in terms of the value of production. Two papers, Poret and Chambolle (2007) and Chambolle and Poret (2009), develop models that examine how certified products might come to be marketed within conventional distribution channels and how certification might benefit all farmers, not just those who are producing the certified good. A third paper, Reinstein and Song (2012), examines how certification might encourage an altruistic consumer to pay more for a unit of a good, which, accompanied by increased effort on the part of farmers, allows the certified producer to increase profits.

Poret and Chambolle (2007) begins from an assumption that consumers vary in their willingness to buy certified products. They assume the presence of a profit-maximising monopoly retailer (the processor in other models). The interesting outcome, where certified and uncertified products are sold, with price discrimination among consumers, depends upon the certifier, whose payoff is a function of both the quantity of the certified product sold and the margin above the uncertified price obtained for producers, placing a relatively low weight on the margin achieved compared with the weight on the volume sold. This recalls debate among proponents of fair trade relating to engagement with large businesses, which can on the one hand substantially increase the market penetration of certified products, but which are reluctant to provide a large margin to producers. Jaffee (2007) notes concerns about Transfair's certification of some of Starbucks' lines; Lyon and Moberg (2010) report criticism of certification of a single product marketed by Nestle; but Fridell (2007) argues that fair trade is necessarily a market- oriented intervention, with a relatively limited role.

A subsequent paper, Chambolle and Poret (2009), begins from an industry in which there is perfect competition among growers, oligopoly among processors, and a monopsonist retailer, who sells to final consumers. Given the form of consumer preferences, the monopsonist always increases profits by selling the widest variety of (horizontally differentiated) brands. A fair trade channel then opens, with the certifier's objective being to choose a guaranteed minimum price payable to farmers that is consistent with the monopsonist choosing to market the product. The presence of the fair trade product increases the price paid to all farmers firstly through market expansion (greater variety increases final demand), but also through a disintermediation effect, as the fair trade certifier purchases output that would otherwise pass through conventional channels. Given the relatively small scale of certified production, these effects seem likely to be interesting in theory, but of little practical importance.

While this work examines the creation of value throughout the production and distribution processes, Reinstein and Song (2012) analyze how the structure of payments in a Fairtrade contract can elicit additional effort from growers, with the fair trade premium and higher value output compensating manufacturers and distributors for their additional payments. Certification helps to resolve co-ordination problems that emerge from the structure of the industry. It seems reasonable that if a processor simply announces that it will pay the certified price without certification, it would obtain increased effort from producers, but not be able to sustain a higher retail price because its actions would not be verifiable.[11] Certification enables a credible claim to be made that the price received by the producer is just. Consumers are then willing to pay a premium for the certified product, which is treated as a bundle of the underlying commodity and a separate charitable donation because they consider this to be economically efficient. We shall argue below that this process satisfies useful criteria for ethical behavior.

2.2 Sociological Perspectives on Certification

If the economics literature is limited, the sociology literature often seems to be partisan,[12] with many contributors having worked with organizations to develop certified products. We lack competence in judging many of the competing claims, but the arguments of Jaffee (2007) in particular seem to translate well into economic terms. Reporting on the first ethnographic study to analyze the impact of certified trade on the members of a rural community, Jaffee demonstrates that members of the co-operative managing the certified production tended to have substantially higher gross incomes than their neighbors, but that they also tended to rely much more on hired labor. Indicators of well-being, such as reported health and nutritional information, ownership of consumer durables, and education levels, also tended to be higher for the families of co-operative members than for others. Yet, co-operative members seem more likely than others to receive remittances from family members living in cities. Analyzing the data, Jaffee (2007) exhibits a degree of ambivalence about the findings. They seem to suggest that certification provides access to opportunities that lead to migration from the rural community.[13]

Development economists (e.g., Bhattacharya, 1998) might regard this as evidence of certified trade enabling diversification of income and access to the formal sector. In contrast, Jaffee seems committed to the notion of certified trade as a mechanism for sustaining agricultural communities and to regard it as a revolutionary mechanism that might lead to a fundamental reconfiguration of trade relationships. Such an approach appears to preclude the use of conventional distribution channels, and reflects the debate in Raynolds, Murray, and Wilkinson (2007) and Lyon and Moberg (2010), relating to the difficulties that certifying organizations might have in deciding how to engage with large scale producers. Fridell (2007) has identified three strands within debates over the nature of fair trade: "alternative globalization," to which Jaffee (2007) and Raynolds *et al*. (2007) seem largely committed; "decommodification;" and "shaped advantage," which covers a range of processes through which some producers might obtain access to global markets on more favorable terms than would otherwise be possible, the understanding of fair trade presumed in most of the case studies in Lyons and Moberg (2010).

3 Justice in Exchange: A Scholastic Argument in Favor of Fair Trade

Historians of economic thought have not always been generous to the Schoolmen. For example, Schumpeter (1954) interpreted Scholastic doctrine as being important in being a prefiguration of later doctrines. Such an approach presumes that there are fundamental truths of economics waiting to be uncovered, and, as argued in Melitz (1971), may have led to a wilful rendering of the source texts to ensure that they conformed to such a project. An account such as Gray (1931), which treats the economic theories of the Middle Ages as being important and interesting in themselves is relatively rare.

As in previous work (Mochrie, 2006), the paper draws upon specialist histories of thought for its interpretation of the primary literature. Langholm (1992), a compendium of primary sources, is an excellent corrective to the general summaries like Blaug (1991), which reduce the development of economic teaching throughout Western Europe between 1100 and 1600 to Aquinas's interpretation of the just price and usury doctrines, and Oresme on money. Langholm (1982; 1984; 1996) has provided a framework for understanding the objects of economic inquiry in this period that is grounded in its value to society, demonstrating that it largely involved normative analysis of the desirability of certain courses of action, in which positive economic analysis was of secondary importance.

We have already noted the reference to the Schoolmen as "reluctant economists," Langholm (1992, p. 19), suggesting that they developed their theories in order to "take account of greed as a virtually unquenchable incentive, even though the purpose of their economic analyses was to guide the virtuous." For Wolter (2001) and Viner (1980), the role of economic analysis in Scholastic thought was also largely normative, and they emphasize the role of the Schools in priestly formation. As confessors, priests were required to provide advice on the liceity of certain commercial transactions.

Scholastic thought overturned the Church's previous conception of economic life. Pirenne (1935, p. 14) characterizes theology prior to the reception of Aristotle as tolerating a static, subsistence economy, in which "Poverty was of divine origin and ordained by Providence, but it behoved the rich to relieve it by charity." Such a conception of the world was consistent with the neo-Platonism of the Church Fathers, in which, as Viner (1980) demonstrates, rejection of the world was seen as meritorious. As Baumgarth and Regan (1988) have argued with respect to philosophy more generally after the reception of Aristotle in the thirteenth century, renewed engagement with the world followed on from acceptance of its reality, and this was as true in economics as in any other division of knowledge.

3.1 The Just Price Doctrine

The Schoolmen tended to argue, given the priority of spiritual, relative to temporal, good in their thinking, to treat acquisition of material wealth beyond that necessary for a "simple sufficiency" as covetous. Many authors therefore used the formula that property should be private in exchange, but common in use. This conclusion was typically derived from analysis in which goods were presumed to be held in common prior to the Fall, in accordance with natural law. During the thirteenth century, while there was general agreement that private property is a necessary institution in post-lapsarian society because the fallen nature of humanity means that powerful would exploit the weak (the argument from peace as developed by Albert the Great) there was considerable debate about the nature of property law. St. Thomas simply defined property rights as an addition to natural law, necessitated by the changes in the environment. John Duns Scotus, in a typically innovative argument, proposed that property rights are simply a part of positive law, and that one of the effects of the Fall has been to cancel the natural law in which goods were held in common. Effectively, Duns Scotus argued that property rights are entirely conventional, and, ranging across much that would now be considered political economy, argued at some length about how such rights might be legitimated through the institutions of civil society.

The formula "private in exchange, but common in use" may seem to be an unsatisfactory compromise, but is very important in understanding the Scholastic analysis of exchange. "Private in exchange" means that people have an absolute legal right to dispose of property as they see fit, or to engage in trade or manufacture. "Common in use" places restraints on the ability to use property. In his commentaries on the Gospels, Albert the Great used this formula together with the understanding of virtue as a means to argue that both excessive wealth and excessive poverty are barriers to spiritual perfection. Hence for Albert, it was right for someone to dispose of their superfluity to those in need.

Such sharing with the poor was not considered simply to be charity. In the *Summa Aurea*, William of Auxerre argued that it is a matter of justice to relieve the need of someone in need. The essence of the argument is that the needs of other people supervene in the exercise of property rights. This cannot be a matter of charity because that is a voluntary response to the needs of others, with no external compulsion to engage in it. Addressing the supervening needs of others is then a matter of justice; specifically distributive justice.[14]

Rendering the Scholastic understanding of distributive justice is difficult. Kaye (1998) makes heroic efforts, but the theory of income distribution that he develops seems to require that incomes should be related to some objective measure of position in a social hierarchy. Langholm (1992) takes a much more moderate position, that nothing in Scholastic teaching suggests that differences in social status should determine the operation of (commutative) justice in exchange. In recognising the needs of the other party to a transaction and going beyond the demands of commutative justice, we support distributively just outcomes.

3.2 Some Limitations on Market Based Transactions

It is a presumption of economics, at least since its development during the Enlightenment, that market exchange is anonymous. Scholastic economic thought did not recognize this veil of anonymity, and so placed a far heavier burden on parties to a transaction to take account of others' circumstances. As we have set out the just price doctrine here, it is simply a set of principles guiding behavior in situations where there is no clear market price, or where the unrestrained use of market power would exploit the need of the other party to a transaction.

In thirteenth century Scholastic thought, we find two major theoretical reasons for setting aside the market price in favor of the just price, together with several legalistic arguments. The first explanation that we consider is the concept of the mixed act, the belief that personal autonomy may be unjustly restricted by an external cause, which restricts the operation of an individual's will. Where Aristotle defined the concept of a mixed act, the Schoolmen preferred to define the problem as one of mixed will. For example, if the alternative is unemployment (without any social insurance), a worker in a developing country may accept a wage that is so low that it barely permits subsistence, potentially exhibiting mixed will. Here, we simply raise the possibility of mixed will as imposing an obligation on the counterparty in trade.

The other concept that supports an appeal to a just price is the *ius necessitatis*, perhaps best rendered as the law of survival. This was the claim that it is legitimate for a very poor person to take and to use such property as is required to sustain life. Note that this is entirely consistent with the understanding that property should be common in use: to sustain life is a primary duty of any animal, and it follows that a distribution that does not ensure the survival of all people cannot meet the requirements of distributive justice. There is perhaps some relation to the analysis of entitlement failure as a cause of famine (Sen, 1999), but with the suggestion that the appropriation of resources in the case of entitlement failure might be legitimate.

The situation considered in Scholastic thought that seems closest to certified trade is where, because of need, a seller reduces the asking price in order to achieve a quicker sale (or a buyer pays a very high price for some good to obtain it very quickly). Scholastic teaching on this matter is very clear: the circumstances of the counter-party in an exchange can never justify alteration in its terms, since, to use modern language, that would be an abuse of market power. It is important here to emphasize both the term "need," and that this is a limited deviation from acceptance of market prices.[15] Proximity to a subsistence boundary might then constitute need.

For Langholm (1992) St. Thomas's argument in the *Summa Theologiae* summarized very clearly the obligations implied by mixed will in a "double rule of just pricing." According to this, a seller might increase the price that he seeks to reflect the value that he places on it, so long as the buyer is willing to meet that price. However, the seller must not increase the price in a case where only the buyer values the good very highly. In the former case, he would be seeking compensation for loss; only in the latter would he be attempting to exploit another's need. Langholm (1992) and Mochrie (2006) note Duns Scotus's addition that in most transactions there will be surplus value and interpret his proposal for the division of that surplus to be similar to the Nash Bargaining outcome for a situation in which both parties have well defined outside options, so that there is equal division of the joint surplus.

The legalistic basis for an appeal to the just price doctrine follows from the much-used gloss, *res tantum valet quantum vendi potest*, which Langholm (1982) traces back to Accursius and the *Glossa Ordinaria* (c. 1224), indicating that the civilian schools in Bologna were very early adopters of it. In his second commentary on the *Ethics*, Albertus Magnus distinguishes between exchange where prices are set *ad pactum*, that is by mutual agreement, and those where prices are set *ad par*, that is with reference to some external valuation, necessary for example were restitution for loss to be made. Factors that determine the just price *ad par* can also be seen as the basis for identifying the situations in which prices set *ad pactum* might be set aside on the basis of the exploitation of the need of one of the parties to the transaction.

Taking mixed will to be the underlying cause of those situations where the imposition of a price *ad par* would be necessary, analysis centred on those circumstances where factors other than need might lead to imperfect consent. Henry of Ghent argued that it is not the price that a good might be sold for according to civil law that is just, but the price that it ought to be sold for in terms of natural law, where both parties to the transaction have full knowledge of the underlying nature of the good and there is no compulsion. He argued that in the legal maxim, *potest* was to be understood as "ought to be," and specified both need and ignorance as barriers to the achievement of the just price. Petrus Ioanneis Olivi shortly after added inexperience, fickleness (perhaps simplemindedness), impediments of the will and compulsion (by need or some other necessity).

These considerations do not appear to be onerous. They do not appear to go much beyond the standards of law of contract, and they confirm that the market price should typically be a good guide to the just price, but that it should be possible for either party to a transaction to appeal to some kind of arbitration if it seems that the other is preventing it being reached, either by exploiting need, or else by failing to act openly and in good faith. Advocates of fair trade argue that certification has this purpose.

3.3 Some Limitations of the Theory

The starting point of the discussion was the achievement of commutative justice in a single transaction. It has also touched on claims relating to the role of distributive justice and charity, which seem much more relevant to arguments in support of fair trade, where it is not necessarily single transactions, but the outcome of a set of transactions, that might be considered just. Two questions arise in this context.

Firstly, suppose that in a chain of exchanges, the first exchange (or some intermediate one) takes place at a price that exploits the need of the seller. The ultimate consumer appears to have been the beneficiary of an unjust act. What is the responsibility, if any, to make restitution? Secondly, the distribution of incomes across the value chain may be such that the poorest participants do not reach some (socially determined) minimum level—not a short run subsistence level, but a level at which poverty causes the early onset of chronic ill health and high morbidity. In those circumstances, where the Schoolmen would have argued that the requirements of distributive justice are not being met, what responsibility do other participants in the chain of transactions have to adjust prices to alleviate this situation?

In relation to the first question, it might appear that the ultimate purchaser has no responsibility to make restitution to the person who has suffered loss, although Duns Scotus is careful to insist that where the passage of time and distance from the person that has suffered loss make restitution difficult, alms should be given to the poor in Christ through the Church (Wolter, 2001). This suggests a channel for charitable giving as a means, however indirect, of correcting departures from justice in single transactions.

Turning to the second question, suppose that in an exchange economy, a person is given a very small endowment. Observing the requirements of commutative justice might lead to that person being unable to survive. Charitable giving provides one form of resolution and St. Thomas would rely on the *magnificentia* of the rich, who would undertake voluntary acts of charity to display not merely wealth, but virtue. A more general argument, following Aristotle, is that we should be concerned if the ultimate distribution in this economy prevents market participants from achieving full human flourishing. Fair trade is then an application of arguments about the achievement of distributive justice in such an economy. Rather than relying upon charity to adjust the final distribution, it may be possible to anticipate the likely outcome and adjust prices to eliminate the requirement for charity.

Given that the Schoolmen did not accept that it was possible to eliminate consideration of the needs of both parties to a transaction from determination of the just price, we conclude that the achievement of commutative and distributive justice were not distinct criteria. Where both parties recognize the needs of the counterparty fully, distributive justice would be achieved through exchange. This is our interpretation of the most recent economic models, in particular Reinstein and Song (2012). Their altruistic consumers are aware of the needs of other participants in the chain of transaction, and believe that if production is certified, then paying more for the goods that they wish to purchase will benefit those who seem to be being treated unjustly. Certification is not simply intended to facilitate such transfers, though. By placing obligations on producers, it requires them to increase effort, so that while they are being treated justly, it is not at the expense of the intermediaries between the primary producers and the final consumer. Rather than being altruists making a charitable donation, they are virtuous, and practice justice.

4 Conclusions

Fair trade has developed over the last twenty five years as an ethically-led trading initiative. Economists have been quite slow to analyze the mechanisms by which it might work, partly because the concept appears to support inefficiency in the allocation of resources. For certification to be effective as an economic institution, it seems that it must satisfy three conditions. Firstly, the technology for verification of both sides of contracts must exist, and the certifier must have the authority to exclude producers and processors. Secondly, there must be a market for the certified product, so that at given quality and price, it can retail profitably. This implies that there is a substantial group of consumers who are willing to accept that they have a duty to engage in ethical practice while making consumption choices. Thirdly, certified trade must be effective in promoting the ends of the certifier, which may seem obvious, but probably requires further research to determine whether the effort of certification generates benefits that other mechanisms for development support cannot. Economic analysis of certification is still quite limited, and it is only recently, specifically in the analysis of Reinstein and Song (2012), that a satisfactory account of how certification might improve efficiency has appeared. Yet even that account is incomplete, assigning almost no role to the certifier, unlike the earlier work of Poret and Chambolle (2007) and Chambolle and Poret (2009).

Economic and sociological analysis of fair trade now appears to be converging. To the dismay of many of its proponents, fair trade has developed into a market-oriented channel for development. It is straightforward to apply recent industrial organization models in this context. An alternative interpretation, which is also consistent with the rhetoric of Fairtrade certification and Scholastic theology, is that consumers consciously decide to acknowledge the economic power that they are implicitly exercising through being the final consumer of goods produced through a particular set of trading relationships in order to act justly.

Since its inception, Fairtrade certified goods have been promoted by both religious and secular development charities. These agencies might seem to be in competition with Fairtrade and its affiliates, especially if we accept the implication of the bundling argument in Reinstein and Song (2012), that consumers' willingness to pay a higher price for certified products reflects substitution away from charitable giving. Such organizations may however consider that there is substantial additivity to development support through purchases of Fairtrade goods, and so be willing to promote them. Specifically, much of the rhetoric supporting Fairtrade is built around the direct links between farmers and consumers, mediated through substantially shorter production chains than is usually the case. Such attempts to build communities, and to promote a sense of mutual obligation within them are typical of churches' behavior, especially as modelled using club theory (Iannaccone, 1992). In future research, it may be possible to understand better the role of the certifier if we treat fair trade as a method of resolving the problems of participation similar to those that arise in economic models of religious behavior.

Endnotes

1 We therefore restrict attention to the international movement that has developed since the Max Havelaar Foundation launched the first Fairtrade consumer guarantee label in 1988 on coffee sourced from Mexico. A fuller account would explore the emergence of the concept of fair trade shortly after World War II, where it referred to trade managed by networks, often affiliated to churches, that provided small scale craft producers with access to consumers, typically in North America or the UK. The precursor of the Mennonite charity in the USA, Ten Thousand Villages, appears to have been the first such organization.

2 We distinguish between the general concept of fair trade and certified trade conducted according to Fairtrade standards under the supervision of FLO-International and its affiliates.

3 In comparison, Charity Commission (2012) records the income of the four largest development charities in the UK for the year to March 2011 as: Oxfam (£367.5m), Save the Children (£291.5m), Christian Aid (£95.0m) and Tearfund (£63.9m).

4 The sales revenue of certified products is small when set against the

revenue of €90.8bn reported by the largest European food producer, Nestle SA (in 2010), but it is concentrated in a relatively small variety of product lines.

5 Much of the criticism of existing certification arrangements from proponents of fair trade is levelled at the process by which minimum prices are set. For example, the minimum washed coffee price of $1.25/lb was set in 1986, following the collapse of the International Coffee Agreement. This increased on 1 April 2011 to $1.40/lb, together with an increase in the Fairtrade premium from 10¢ to 20¢. While this would have been above the market price for most of the last 20 years, with the recent price spike in coffee, the new price floor is below the market price.

6 Reinstein and Song (2012) is the first paper in economics to note the presence of the premium, but it does not clearly state that even if the spot price is above the minimum price, producers still benefit from the premium.

7 See Sainsbury's (2012), Waitrose (2012), and The Co-operative (2012).

8 This contrasts with the very large literature in sociology. Interesting and useful recent surveys include Fridell (2007), Jaffee (2007), Lyon and Moberg (2010), and Raynolds, Murray, and Wilkinson (2007).

9 But see the response of Smith (2008).

10 Harford (2005), also raised this question in the context of the pricing strategy adopted by cafés, but noted that the price premium on certified products had quickly vanished.

11 This claim probably has more purchase in European markets than in North America. In Europe, where Fairtrade is part of the marketing mix of leading retailers, the certified product may well be of "standard" quality. In North America, there has been rather greater proliferation of certification schemes, with Fairtrade being simply one way in which specialty retailers can announce a commitment to quality.

12 Contributions such as Hayes (2006), Sidwell (2007), and Booth and Whetstone (2007) demonstrate that ideology also plays a substantial role in shaping economic analysis, particularly at the level of policy.

13 Moberg (2009) finds many similar results for banana farmers in the Windward Islands, where among participating farmers, certification is seen as involving the external imposition of standards, sweetened by the guarantee of higher prices and the social premium.

14 As with many elements of Scholastic economic theology, there is a counter-current. Arguments from natural law tended to support the social order as it existed, with substantial concentrations of power

and privilege. Following the argument of Aristotle in *Ethics* V, the Schoolmen tended to rely on the distinction between commutative and distributive justice to explain the necessity of potentates being able to display their wealth, claiming that certain behaviour is appropriate to a certain social position. Hence Albert the Great argued that necessaries for a king or a bishop are very substantial because of the obligations of their office, not because of their personal need. Similarly, St. Thomas emphasizes the importance of *magnificentia*, of the public display of virtue: a current example might be the work of the Gates Foundation, recalling as it does the role of public munificence in civic virtue during classical antiquity.

15 In this paper, I am concentrating on exchange. A fuller account would explore the theory of value, largely derived from Aristotle's *Ethics* V, in which insights into the role of cost of production, factor productivity, and relative scarcity of goods and factors emerged. The best account of this development is Langholm (1992), but see also Kaye (1998).

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