



Leveraging the Market for a Sustainable Coffee Economy

Opportunities for Renegotiation of the International Coffee Agreement

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1. Introduction

Sustainability in the coffee sector is threatened by a variety of market imperfections which manifest themselves as market volatility and declining terms of trade; systemic poverty; and environmental degradation. Attempts to improve the sector's sustainability to date have principally focused on: more efficient management of the international markets; and more efficient management of international supply chains. While complementary, these two approaches have, for the most part, been pursued independently without coordination of efforts and strategies. The natural interdependence between market and supply chain efficiency, however, suggests that systemic treatment of both aspects at a policy level is imperative to the effective implementation of sustainability in the sector at a global level.

The International Coffee Organization is the only dedicated forum for discussing coffee-related matters at the international level and, as such, provides the essential focal point for international cooperation in the development of a sustainable coffee economy. The negotiation of a new International Coffee Agreement, on the other hand, presents a rare opportunity to fortify the underlying spirit of participatory governance for sustainability embodied within the ICO to date. This brief outlines a series of concrete options for consideration by stakeholders within the context of the current ICA negotiating process.¹

2. Strategic planning, governance and information sharing

Participatory governance operates as one of the underlying pillars of sustainability under the Earth Summit process.² The ICO's high level of consumer and producer country membership, combined with its formal inclusion of the private sector through the Private Sector Consultative Board, renders it a model for implementing participatory governance in international relations. Renegotiation of the ICA

provides an opportunity to advance this spirit to enable more effective stakeholder participation in global governance of the coffee sector.

Revisiting the Structure of the Private Sector Consultative Board

Article 22 of the current ICA establishes the framework for the creation of the Private Sector Consultative Board (PSCB), made up of eight exporting and importing country representatives of the private sector respectively.³ Membership in the PSCB to date has been limited primarily to major coffee associations and institutions with little participation of smaller producer and trade organizations.

Under its current make-up, the PSCB provides a critical voice for major industry interests, but still risks excluding those with less developed communication structures from ICO discussions. In particular, there is a need for ensuring better representation of *smallholder producer groups* within the context of the PSCB. Filling this need could help improve and deepen communications within private sector supply chains, thus fulfilling the objectives of the PSCB more effectively.

Opportunity 1: *In an effort to expand the reach of the PSCB to smallholder producers, exporting country representation could be expanded from eight to 12 with the addition of a third exporting country representative to each coffee group reserved specifically for smallholder producer representatives.*

Consultative Board on Sustainability

Article 39 current ICA commits members to giving, "due consideration to the sustainable management of coffee resources and processing bearing in mind the principles and objectives on sustainable development contained in Agenda 21."⁴ The

past two decades has given rise to the development and expansion of a variety of multi-stakeholder, supply chain-oriented sustainability initiatives. These initiatives are distinguished by their inclusion of many voices in their development and implementation, as well as their attention to sustainability constraints at the micro (enterprise and supply chain) level. While it is recognized that such approaches are an essential part of a holistic approach to achieving sustainability, a lack of clarity on the appropriate relationship between government policy, the ICO and such initiatives, as well as limited information on their actual impacts, has prevented the development of proactive global strategies under the ICO.

This context, combined with Agenda 21's explicit recognition of the importance of widespread participation of major groups in the development of strategies for sustainability, suggests inherent value in the establishment of a dedicated multi-stakeholder forum on implementing sustainable practice in the coffee sector within the ICO. In September 2004, the Executive Board considered a proposal of the Sustainable Coffee Partnership for a "Sustainability Committee."⁵ A new ICA could secure a systemic place for multi-stakeholder "sustainability" activities through the establishment of a formal forum for discussion and strategic development within the ICO.

Opportunity 2: *In an effort to build shared understanding and approaches to sustainability in the coffee sector at the global level, the ICO could establish a "Consultative Board on Sustainability" using document WP Board 960/04 as a point of reference.*

Coffee Observatory

Accurate market information is a prerequisite to sound economic planning and development. One of the central objectives of the ICO is "to act as a centre for and promote the collection, dissemination and publication of economic and technical information, statistics and studies, as well as research and development, in coffee matters."⁶ To date, with some exceptions, the ICO has focused its regular statistical analysis on the four major coffee quality groups. However, as the coffee market becomes increasingly differentiated, the regular provision of up-to-date data on prices and production in *differentiated* coffee markets is becoming increasingly important to the development of "sustainable" production strategies for farmers and producer countries alike. Accurate pricing information on differentiated coffees is also a key to long-term strategies for ensuring that the costs of production are internalized within the market (see Opportunity 8 below).

Opportunity 3: *Following its mandate as the principal body for generating and disseminating global statistics for the coffee sector, the ICO could undertake measures to establish a Web-based "coffee observatory" which provides aggregate data of price levels for differentiated coffees on the basis of geographic "sustainability" and other quality-related conditions of production.*

3. Project development, supervision and financing

Many of the world's coffee producing regions remain underdeveloped and, as a result, are in dire need of technical assistance and infrastructural support in order to effectively participate in international markets. Through the liberalization and structural adjustment policies of the 1980s and 1990s, traditional support institutions at the local level have been dismantled, leaving deep gaps in meeting structural assistance needs for coffee farmers. At the same time, with markets being increasingly defined by quality, technical and sustainability requirements, farmers are experiencing a growing need for technical assistance on the ground. Based on the current context, technical support is particularly needed to help producers and producer countries move forward along five lines:

- the implementation of better management and marketing practices associated with quality, technical and sustainability requirements;
- the multiplication of opportunities for pursuing diversified livelihoods;⁷
- strengthening of producer organizations;⁸
- improving access to credit; and
- improving access to risk management tools.

While individual, country-based funding can provide more targeted and flexible funding based on rapidly changing market conditions, such efforts are vulnerable to inefficiencies created by duplication and inadequate information exchange across projects. The prospect of potential efficiency gains and economies of scale through the adoption of more "shared" strategies and learning in project development and implementation suggests the promise of collaboration in the provision of *timely* and *flexible* funding for coffee projects.

Clearing House for Technical Assistance Projects

Technical assistance and related projects are scattered among a multiplicity of donors, project executors and geographic regions. Many projects are necessarily designed to match specific geographic, climatic, social, political and economic conditions. Nevertheless, given the systemic and global nature of many of the problems facing coffee producers, there is also a clear potential for improved efficiency in the design and implementation of technical assistance projects through improved coordination and information sharing among project donors and developers at the global level. In its capacity as disseminator of information, the ICO is the appropriate forum for the implementation of a more proactive strategy towards shared project development and implementation.

Opportunity 4: *In order to leverage project learning, economies of scale and other efficiencies available from information sharing, the ICO could organize and manage a "clearing house" for technical assistance projects implemented in member countries.⁹*

Partnership Fund for Sustainability

Rapidly changing market conditions require timely, targeted and efficient technical assistance interventions. With the disappearance of locally-based institutions and resources for extension and other technical assistance, there is a growing need for the international community to formalize commitments for the provision of assistance specifically designed to fill the gaps left by existing funding and extension services across the five pillars outlined above. Following precedents established under the 1968 ICA (diversification fund); 1994 ICCA (environment fund); and 2005 ITTA (Bali Partnership Fund) and (Bilateral Funding Mechanism),¹⁰ ICO members have an opportunity to establish an efficient and coordinated approach to funding sustainable supply chain management through coordinated funding mechanisms.

Opportunity 5: *The ICO could establish a working group to conduct a feasibility and ex ante impact analysis on the establishment of a “Partnership Fund for Sustainability” or a bilateral funding mechanism dedicated to the implementation of better management and marketing practices, diversification and strengthening producer organization.*

Financial Services Information Access Point

The seasonal nature of coffee production combined with rapidly changing market conditions persistently requires coffee producers to invest savings and capital in the maintenance and development of their production systems. Identified areas where credit facilitation for producers and producer organizations is needed include: pre-harvest financing and seasonal working capital; infrastructure development; diversification; debt financing; and risk management.¹¹ The growth in the complexity and technical specificity associated with supplying differentiated markets has amplified the investment challenge facing producers. The freeing of access to credit *specifically* for producers committed to entering differentiated markets could stimulate the sector’s transition to differentiation and, with it, overall sustainability. Although a number of specialized credit institutions currently exist, infrastructure support for producers and local financial institutions in using them is lacking. A centralized information access point could help generate efficiencies both for producers and the financial markets serving them.

Opportunity 6: *The ICO could stimulate access to credit for small producers interested in accessing differentiated markets by facilitating access to existing credit services through a “financial services information access point” and through the promotion of cooperation among existing financial service providers serving differentiated markets.*

Risk Management Facility

One of the founding motivations for international cooperation within the coffee sector is a shared interest in long-term market stability and equilibrium. In light of the deep political and economic difficulties associated with strategies for controlling prices through supply management, the ICO should seek alternative market-based means for promoting stability. Roasters and traders in the private sector have long relied on a suite of risk management tools ranging from “put options” to hedges and other specialized trading instruments. Such instruments currently remain largely out of reach for most producers due to a lack of capital, technical assistance and appropriate infrastructures.¹² Technical assistance and training on the use of risk management tools through a “risk management facility” could offer a market-friendly approach for improving producer sustainability in the face of market volatility.

Opportunity 7: *The ICO could facilitate the establishment of a risk management facility dedicated to improving producer access to risk management instruments.*

4. Market efficiency and cost internalization of sustainable practices.

The primordial motivation for the establishment of the ICO has been to help facilitate the development and implementation of strategies for matching supply and demand. The principal outcome sought by ICO activities in this area, has been the maintenance of prices which are both “fair” to consumers and “remunerative” for producers.¹³ The coffee market suffers from deep and pervasive market imperfections arising from imperfect information, market concentration and externalities associated with the provision of public goods, all of which operate as obstacles to attaining the objective of “fair and remunerative pricing.” While it is clear that the ICO cannot be responsible for creating the conditions of a perfect market, it is also clear that the ICO’s mandate as focal point for international cooperation on coffee matters places it in a unique position to generate conditions conducive to improved market efficiency.

The ICO’s activities related to information collection, generation and dissemination on coffee markets help overcome the systemic challenges associated with imperfect information, while the ICO’s capacity for establishing equitable, representative and inclusive “global governance” of the coffee sector can have the effect of reducing the impacts of disparities in market power. To date, however, the ICO has not, on a broad scale, directly addressed issues related to externalities associated with social and environmental public goods provision. While the growth of supply chain-based monitoring and enforcement mechanisms has significantly enhanced the ability of markets to price the social and environmental costs of production, free rider problems still result in the undervaluation of such inputs in the absence of a proactive policy framework. The ICO is the appropriate forum for developing policies designed to internalize the costs of sustainable production as called for under Principle 16 of the Rio Declaration.

Opportunity 8: *The ICO could help the international coffee market internalize the economic, social and environmental costs of production by adopting policy level measures aimed at promoting sustainable production and consumption practices including, inter alia:*

- *preferential export conditions/tariffs for sustainable coffees;*
 - *preferential import conditions/tariffs for sustainable coffees;*
 - *preferential sales and services taxes for sustainable coffees;*
 - *income tax credits for business dealing in sustainable coffees; and*
 - *set premium schedules for recognized “sustainable” coffees (on commodity exchanges).*
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5. Moving Forward

While the negotiation of any agreement involving a large number of governmental members can be expected to be a slow and difficult process under any circumstances, the treatment of sustainability issues through shared strategies can be particularly difficult. Special care, of course, needs to be taken not to infringe on national sovereignty and to ensure that any commitments are backed by meaningful resources. Ultimately, though, the key to success will almost certainly turn on the degree to which real meaningful discussions on different strategies are possible among the different negotiating parties. With this in mind, and to help ensure that full advantage is taken of the opportunities presented by integrated supply chain approaches to sustainable development, ICO delegates could establish a “special negotiating group” to explore, develop and propose options for linking differentiated coffee markets and sustainable supply chain initiatives to overall ICO strategy within the context of the new ICA.

Opportunity 9: *The ICO could establish a “special negotiating group on differentiated markets and sustainable supply chain initiatives” to explore the above and additional options for enabling the strategic development of market-based sustainability initiatives within the context of the new ICA.*

Notes

- 1 These options are drawn from the longer document *Building a Global Strategy for a Sustainable Coffee Sector: Considerations on the Renegotiation of the International Coffee Agreement* originally presented by IISD to the steering committee of the Sustainable Coffee Partnership for its consideration in the context of the 2006 negotiations. Accessible at http://www.iisd.org/pdf/2006/coffee_global_strategy.pdf
- 2 Paragraphs 23.1 and 23.2 of Agenda 21 not only emphasize the need for participatory governance for ensuring sustainable development but also, “the need for new forms of participation.” UNCED, *Report of the United Nations Conference on Environment and Development, Annex II—Agenda 21 A/CONF.151/26* Aug. 12, 1992.
- 3 Art. 22, ICA 2001.
- 4 Art. 39, ICA 2001.
- 5 *Proposal for an ICO Sustainability Committee*, WP Board 960/04 (September 17, 2004).
- 6 Art. 1(5), ICA 2001. The ICO’s role as information generator and disseminator is also explicitly outlined in Art. 1(4) and Art. 29 of the Agreement.
- 7 Diversified livelihoods can be achieved through vertical diversification along the coffee supply chain and horizontal diversification, either alongside or out of coffee production.
- 8 Producer organizations can play a key role in providing not only market information and local technical assistance, but also in strengthening the bargaining position of producers in international markets.
- 9 A clearing house could take many different forms—ranging from a database to a “warm body” forum consisting of project promoters, executors and donors.
- 10 UNCTAD, *Preparation of a Successor Agreement to the International Tropical Timber Agreement*, 1994 TD/IMBER.3L.6 (October 5, 2005).
- 11 OXFAM, *The Crisis Continues* (OXFAM, 2005).
- 12 The International Taskforce on Commodity Risk Management, facilitated by the World Bank, has conducted several pilot projects with coffee producers with some success. The main barrier to more extensive uptake is inadequate training and infrastructure. Panos Varangis, Donald Larson, Jock Anderson, *Agricultural Markets and Risks: Management of the Latter, Not the Former* (WPS 2793) (World Bank: 2002) at 13 and 14.
- 13 Art. 1(2), ICA 2005, outlines the objective of providing, “a forum for intergovernmental consultations, and negotiations when appropriate, on coffee matters and on ways to achieve a reasonable balance between world supply and demand on a basis which will assure adequate supplies of coffee at fair prices to consumers and markets for coffee at remunerative prices to producers, and which will be conducive to long-term equilibrium between production and consumption.”