Building a Global Strategy for a Sustainable Coffee Sector: Considerations on the Renegotiation of the International Coffee Agreement

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1.0 Executive Summary

Coffee producers and labourers account for an important segment of the world’s rural poor in developing countries. Market volatility and declining terms of trade along with inadequate access to infrastructure and market information, put sustainable livelihoods out of reach for millions of coffee farmers. Over the past two decades, both the public and private sectors have undertaken unprecedented efforts to improve the social, economic and environmental performance of the coffee sector through a variety of initiatives. To date, however, most initiatives have occurred along specific lines of cooperation with only limited levels of inter-initiative cooperation at the international level. Given the global and macro-economic nature of many of the challenges facing the coffee sector, there is a particular need and opportunity for building stronger information exchange and cooperation at the global level. The renegotiation of the International Coffee Agreement provides a rare opportunity to push such cooperation to a new level—particularly as it relates to voluntary private sector and multi-stakeholder initiative. On the basis of an overview of the background issues related to the development of a sustainable coffee economy, we offer the following list of opportunities for international cooperation as possible focal areas for sustainability related negotiations within the context of the renegotiation of the ICA:

**Opportunity 1:** In an effort to expand the reach of the PSCB to smallholder producers, total exporting country representation could be expanded from 8 to 12 with the addition of a third exporting country representative to each coffee group reserved specifically for smallholder producer representatives.

**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.

**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.

**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.

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

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.

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

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.

In order to ensure substantive consideration, investigation and discussion on the above and other issues related to the promotion of sustainable production and trading practices within the context of the new ICA, a dedicated negotiating forum on such matters needs to be established. We therefore recommend the establishment of a “special negotiating group on sustainability”:

Recommendation: The ICO should establish a “special negotiating group on sustainability” to explore the above and additional options for enabling the strategic development of market-based sustainability initiatives within the context of the new ICA.

2.0 Sustainability in the Coffee Sector

As one of the most important commodities in terms of value traded globally, coffee plays a crucial role in the livelihoods of millions of rural households across the developing world. In addition to the estimated 25 million small coffee farmers who depend directly upon coffee as their primary source of income, coffee contributes significantly to foreign exchange earnings and plays a leading role in determining opportunities for employment and infra-structure development in more than 50 developing countries. The breadth and intimacy of the relationship between coffee producers and a host of intermediary institutions along the coffee supply chain makes the sector of critical importance to sustainable development at the local, regional and global levels. The coffee sector faces significant challenges along each pillar of sustainable development in ways that highlight their interconnectedness.

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Unstable and long term declining prices are definitive characteristics of the coffee sector. Both attributes pose significant difficulties for small producers seeking to secure sustainable livelihoods. Since the 1980s, oversupply on international markets has resulted in a near 70% decline in nominal coffee prices. The damaging effects of long term declining terms of trade facing coffee producers are exacerbated by high price volatility. Over the past several decades, global export revenues from coffee have fluctuated between $5 and $14 billion per annum. Price volatility together with rigidities of production and the consequent distribution of costs make it extremely difficult for coffee producers and policy makers alike to determine optimal production strategies. Against the backdrop of market volatility and decreasing overall revenues, producer capacity to move into more lucrative markets are challenged by the systemic absence of access to infrastructural support for reasonable credit, risk management tools, market information and assistance in accessing value-added markets.

Although coffee production has the capacity to reinforce natural ecosystems when sustainably managed, the widespread introduction of mono-culture and related technified production systems has put many coffee producing regions at risk. There is, for example, documented evidence that public policy aimed at increasing productivity in Latin America, has led to substantial transition from traditional shade grown production to “sun” coffee or “mono-culture shade” coffee resulting in reduced biodiversity and capacities for carbon sequestration. Similarly, coffee production has been identified as having been a substantial cause of deforestation in the African context. The fact that more than 80% of the 11.8 million hectares devoted to coffee production around the world are planted in areas of former or current rainforest speaks highlights the global importance of the environmental impacts of coffee production. Given the high environmental sensitivity of coffee producing regions and the potential for eliminating negative environmental impacts of coffee production through the strategic adoption of better management techniques, it is clear that well planned and intentional strategies for the preservation of local, regional and global environmental integrity must be a high priority for the overall sustainability of the coffee sector.

The economic and environmental difficulties facing the coffee sector have direct impacts on the social well being of farmers, farm workers and their communities. Because coffee farmers typically depend upon coffee as their primary source of hard currency, volatile and declining coffee prices can have a direct impact on access to education, housing, food, medical services and other basic necessities. Hired labour serving coffee plantations and estates, on the other hand, are more susceptible to substandard wages and working conditions under uncertain and/or declining market conditions. Both conditions have been linked to migration and increased production of illicit crops giving rise to a vicious cycle of social instability at local and regional levels. Finally, the shift toward the use of synthetic chemicals associated with technified production systems poses direct health and safety risks for coffee workers and their communities.
The social, economic and environmental challenges facing the coffee sector are not, of course, new, but rather part of a long history resulting from inadequate infrastructure development, systemic supply chain inefficiencies and market imperfections. Despite the persistence of the difficulties facing the coffee sector, a new hope for improved sustainability and stability in the sector exists through a growing trend towards more transparent supply chain and market relations, market differentiation and the intentional adoption of “best practices” for sustainability.

Over the course of the past two decades the market for specialty coffees in the US, has grown at a pace of approximately 10% per annum giving rise to significant opportunities for producer diversification into value added markets based upon specific quality characteristics. Markets for certified “sustainable coffees” have grown at an even faster pace, with many sustainability labels displaying 20%+ growth per annum over the past several years. In addition to the potential for higher and more stable prices, participation in intentionally managed supply chains ultimately holds the promise of efficiency gains and market responsiveness—both core elements of building improved sustainability for the sector. A key priority for international cooperation over the course of the next decade must, therefore, include strategies for expanding and tapping into such private sector trends. The renegotiation of the ICA presents a unique opportunity for deepening multilateral cooperation among such initiatives as well as cooperation between public and private sector efforts to build sustainable supply chains.

### Principles for Sustainable Development of the Coffee Sector

<table>
<thead>
<tr>
<th>Principle</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>Principle 1:</td>
<td>Market imperfections should be reduced to enable a maximum amount of producers to be paid, at a minimum, a price/wage that covers basic production, living and environmental costs</td>
</tr>
<tr>
<td>Principle 2:</td>
<td>Employment relationships should be maintained in accordance with core ILO conventions and local law</td>
</tr>
<tr>
<td>Principle 3:</td>
<td>Production practices should be environmentally sustainable</td>
</tr>
<tr>
<td>Principle 4:</td>
<td>Producers should have enhanced access to credit and opportunities for diversification</td>
</tr>
<tr>
<td>Principle 5:</td>
<td>Producers should have enhanced access to trade information and trade channels</td>
</tr>
</tbody>
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### Salvador Coffee Declaration (Core Proposals)

| International Coffee Agreement (ICA): | We propose that the renegotiation of the ICA incorporate the issue of sustainability from the perspective of all actors involved in the coffee chain and sanction space for direct political representation by small scale farmers and rural workers organizations. |
| Support for Sustainable Development: | We propose that the ICO coordinates development projects for the coffee sector. Governments must allocate resources for the improvement of the coffee sector, principally in developing countries. These programs must ensure that family farmers are the direct recipients of the support. |
| Support by producer countries for coffee sector: | We propose that producer country governments commit themselves to implementing programs that target the coffee sector, specifically programs benefiting small scale farmers and rural workers that depend on public policy the most. It is crucial to guarantee debt refinancing, availability of affordable credit for working capital and long term capital investment, support of capacity building programs for small scale farmers and rural workers, access to market information, and promotion of small scale farmer access to markets. Governments should also ratify, publicize and effectively implement all relevant ILO Conventions, particularly Convention 184. Finally, we propose that producer countries engage in discussion and policy coordination that seek to establish the basis for fair trade between nations. |
3.0 The Role of Voluntary Private and Multi-stakeholder Approaches in Building a Sustainable Coffee Economy

Over the past two decades, the private sector, NGOs and consumers have responded to the sustainability challenges facing coffee producers through a variety of multi-stakeholder market based initiatives. Voluntary multi-stakeholder systems, such as Fair Trade, Organic, Utz Kapeh and Rainforest Alliance have consistently recorded growth which far exceeds that of the coffee market generally over the past several years. Although there has been little in the way of comprehensive research on the full impacts of such initiatives, there is anecdotal evidence that they have the potential to offer multiple benefits including improvements in:

- market information and communication along the supply chain
- overall supply chain efficiency and governance
- capacity building and infra-structure development for producers
- environmental conditions related to production
- working conditions for workers
- economic returns for producers
- farmer risk profile
- more equitable supply chain management

However, the growing diversity of initiatives and players involved has also given rise to new obstacles, costs and uncertainties which have restricted access to such initiatives by those most in need. Challenges to the effectiveness of supply chain initiatives as they move into mainstream markets include:

- Growing uncertainty of the full costs and benefits of individual initiatives
- Multiplication of transaction costs for producers
- Reduced access to markets for disadvantaged producers
- Competitive difficulties in markets which externalize social and environmental costs of production
- Lack of sufficient savings, capital and credit to make the transition to sustainable supply chains
- Insufficient infrastructures and resources to effectively participate in the development/management of initiatives and their corresponding administrative processes

Although the breadth and approach of voluntary initiatives varies considerably, they tend to share an emphasis on influencing individual and/or institutional decision making along...
the supply chain to promote, in varying degrees, social, economic and environmental sustainability. The focus of such initiatives on micro-economic decision making along supply chains, operates in clear contrast to the traditional macro-economic approaches to multi-lateral cooperation in the coffee sector under the ICO. The micro-focus of such initiatives enables enhanced efficiencies on the ground through more targeted mechanisms, but they lack the scope and reach to adjust the underlying framework of the market itself.

In principle, free markets, when operating under conditions of “perfect competition,” maximize total social welfare by compensating for all costs along the supply chain through the pricing mechanism. When externalities exist due to, inter alia, inadequate property rights in the face of public goods, imperfect information and/or anti-competitive behaviour, the market tends to produce sub-optimal social, economic and environmental outcomes. While supply chain initiatives can help significantly in improving the transmission of information across the market, and thus overall market efficiency, they have little power to address the problem facing the provision of public goods more generally. That is, although private sector initiatives can help identify public goods, they have little power to influence the willingness of consumers or others along the supply chain to pay for such goods. As a result, “sustainable products” which internalize costs along the supply chain put themselves at a competitive disadvantage compared with those which do not, giving rise to a replication of the public goods problem but with respect to the “sustainable products” themselves—namely, a sub-optimal willingness to pay for such products. Effective solutions to market imperfections associated with global markets, necessitate global cooperation among policy makers.

The difficulties such initiatives face in light of the larger macro-economic context arguably represents the single greatest challenge to widespread adoption of an integrated approach to sustainable development at the supply chain level. The ICO, through its dedicated attention to the macro-economic conditions of the global coffee market and corresponding instruments, offers precisely the tools needed to maximize the impacts of voluntary supply chain initiatives for sustainability.

4.0 The International Coffee Agreement: Leveraging Policy for Sustainable Development

Since the negotiation of the first International Coffee Agreement (ICA) in 1962, member countries have used the Agreement to facilitate price stability and price retention, principally through the management of supply and demand on international coffee markets. The use of export quotas in ICAs prior to 1989 as a means of controlling the supply (and thus price levels) on the international coffee market, provides the definitive, but not the only, example of the macro-economic approach that has distinguished the ICA approach to date.\textsuperscript{29} The ICA’s focus on the macro-economic conditions of the market, and its ability to credibly respond to such conditions through multi-lateral cooperation, makes it particularly well placed to deal with challenges faced by voluntary initiatives.
Indeed, international commodity agreements, as category of “international cooperation”, were originally motivated by, among other things, the desire, “to maintain and develop natural resources of the world and protect them from unnecessary exhaustion.” The 2001 International Coffee Agreement is no exception to this general rule. In addition to the general commitment under Art. 1(2) towards fair and remunerative prices, Art. 1(6) and Art. 39 of the ICA Agreement explicitly commit members to the promotion of a “sustainable coffee economy”. Art. 40, on the other hand, commits members to the promotion of labour conditions consistent with international conventions.

Over the course of the past several years the broad commitments to sustainability under the 2001 ICA have been implemented through a wide variety of ICO related activities. Within the context of strengthening international cooperation towards the implementation of an integrated approach to sustainable development it is worth considering the most recent activities and corresponding opportunities along three basic lines: 1. Strategic planning, governance and information sharing 2. Project development, supervision and financing 3. Market efficiency and cost internalization of sustainable practices. We consider these separately below.

4.1 Strategic Planning, Governance and Information Exchange

The ICO represents the only dedicated forum for discussing coffee related matters at the international level and, as such, should provide a focal point for international cooperation on the development of a sustainable coffee economy. The very fact that the ICO brings together consuming and producing governments for the development of shared global strategies, represents a major accomplishment towards the design and implementation of an equitable and participatory trading system and embodies the basic principles for sustainable governance as contained within Principles 3, 5, 6 and 7 of the Rio Declaration. With the coming into force of the 2001 ICA, member countries expanded the role of the ICO as a convening ground for cooperation at the global level to include the private sector through the establishment of the Private Sector Consultative Board (Art. 22). The provision of a formal forum for discussion, interaction and, ultimately, cooperation, both among the private sector and between the private sector and policy makers, not only introduces the potential for enhanced efficiency in the policy development process, but also improves the ability of the ICO to respond to key stakeholder needs, interests and perspectives through a shared governance process.

Both as a forum for producing and consuming countries to develop strategies for cooperation and information sharing together and as a forum for private sector players to provide input into the public decision-making process the ICO provides an important basis for sustainable governance of the sector. The negotiation of a new ICA presents a rare opportunity to fortify the underlying spirit of participatory governance embodied within the ICO to date. Below are a series of specific options for expanding the reach of the organization to non-governmental stakeholders as well as for developing specific strategies toward the development of sustainable supply chains at the international level.
4.1.1 Expanding Representation on the Private Sector Consultative Board

The PSCB currently provides the principal point of contact between the intergovernmental decision-making process and representatives of the private sector. As such, the PSCB provides a window for exchanging information, strategies and views on coffee matters between industry actors and their governmental counterparts. Art. 22(3) of the current ICA specifies that the PSCB shall be made up of 8 exporting country representatives of the private sector and 8 importing country representatives of the private sector (Box A lists current and alternate members). The 8 exporting country representatives are further divided into groups of two among the four major coffee groups: Colombian Milds; Other Milds; Brazilian and Natural Arabicas and Robustas. Under its current make-up, the PSCB provides a critical voice for major industry interests but nevertheless still risks leaving some of those with less developed communication structures, that is to say, those most in need of better communication channels, out of discussions at ICO level altogether. 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 ensure still better communication deeper within private sector supply chains and thus fulfill the objectives of the PSCB more effectively.

**Opportunity 1:** In an effort to expand the reach of the PSCB to smallholder producers, total exporting country representation could be expanded from 8 to 12 with the addition of a third exporting country representative to each coffee group reserved specifically for smallholder producer representatives.

<table>
<thead>
<tr>
<th>Exporting Members</th>
<th>Importing Members</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Colombian Milds</strong></td>
<td>All Japan Coffee Association (AJCA)</td>
</tr>
<tr>
<td>Asociación de Exportadores de Café de Colombia (ASOEXPORT)</td>
<td>Association des Fabricants de Café Soluble (AFCASOLE)</td>
</tr>
<tr>
<td>Sociedad Exportadora de Café de las Cooperativas de Caficultores (EXPOCAFE)</td>
<td>European Federation of Associations of Coffee Roasters (EUCA)</td>
</tr>
<tr>
<td>Federación Nacional de Caficultores de Colombia</td>
<td>Association des Fabricants de Café Soluble (AFCASOLE)</td>
</tr>
<tr>
<td>Eastern African Fine Coffees Association (EAFCA)</td>
<td>European Federation of Associations of Coffee Roasters (EUCA)</td>
</tr>
<tr>
<td><strong>Other Milds</strong></td>
<td>Committee of the European Coffee Associations (CECA)</td>
</tr>
<tr>
<td>Confederación Mexicana de Productores de Café (ORCECA)</td>
<td>European Coffee Federation (ECF)</td>
</tr>
<tr>
<td>Asociación Nacional del Café (ANACAFÉ)</td>
<td>European Coffee Federation (ECF)</td>
</tr>
<tr>
<td>Coffee Exporters Association of India</td>
<td>Institute for Scientific Information on Coffee (ISIC)</td>
</tr>
<tr>
<td><strong>Brazilian and other Natural Arabicas</strong></td>
<td>Committee of the European Coffee Associations (CECA)</td>
</tr>
<tr>
<td>Conselho de Exportadores de Café Verde do Brasil (CECAFÉ)</td>
<td>European Coffee Federation (ECF)</td>
</tr>
<tr>
<td>Associação Brasileira da Indústria de Café Solúvel (ABICS)</td>
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<tr>
<td>Conselho Nacional do Café (CNC)</td>
<td>European Coffee Federation (ECF)</td>
</tr>
<tr>
<td>Confederação da Agricultura e Pecuária do Brasil (CNA)</td>
<td>Institute for Scientific Information on Coffee (ISIC)</td>
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4.1.2 Establishment of a “Consultative Board for Sustainability”

Art. 39 of the 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.”

Over the past two years both the Executive Board and the Council of the ICO have dedicated an increasing amount of time to the discussion of ICO approaches to diverse sustainability initiatives. Over the course of these discussions the issues related to voluntary sustainability initiatives have proven to be both complex and controversial with the result that it has been difficult to establish concerted strategies for the advancement of shared approaches towards such initiatives. This context, combined with the evident need for strategic support and guidance for implementing sustainability at the international level and Agenda 21’s explicit recognition of the importance of including widespread participation of major groups in the development of strategies for sustainability, suggests an immediate need for the establishment of a dedicated multi-stakeholder forum on implementing sustainable practice throughout the sector.

In September 2004, the Executive Board considered the possibility of a Sustainability Committee.” Document WP Board 960/04 outlines a multi-stakeholder structure which both balances producer and consumer interests while providing mixed representation among all major stakeholder groups, including ICO delegates, small producer organizations, NGOs, and industry, with a view to fostering deeper collaboration among various actors across the sector. The key features of that proposal include:

Dedicated representation of:
- exporting and importing ICO countries
- exporting and importing private sector representatives
- small producer representatives
- civil society and intergovernmental representatives

Organization of a regular “Sustainable Coffee Forum” dedicated to:
- Information dissemination
- Capacity building
- Marketing and network building
- Selection of Non-ICO representatives to the committee

The uniquely participatory structure put forth under the proposal and its link to a Sustainable Coffee Forum, would further expand the reach of the ICO’s dialogue with...
non-governmental actors in the coffee sector while simultaneously enabling efficiency in the implementation of sustainable supply chain practices through public/private cooperation.

**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.

### 4.1.3 Establishment of a “Coffee Observatory”

According to Art. 1(5) of the ICA, 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”. To date, with the exception of specific, targeted studies, the ICO has focused its regular statistical analysis to the four major coffee quality groups. However, as the coffee market becomes increasingly differentiated, the provision of regular up-to-date statistics and trends in 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 key to long term strategies for ensuring that the costs of production are internalized within the market.

**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.

### 4.2 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 liberalization and structural adjustment policies of the 1980’s and 1990’s, 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 basic lines:

- The implementation of better management and marketing practices associated with quality, technical and sustainability requirements
- The multiplication of opportunities for pursuing diversified livelihoods
- Strengthening of producer organizations

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Improving access to credit
Improving access to risk management tools

The ICO has a mandate to develop technical assistance and policy related projects which seek to help producing countries receive increased returns over time. In addition to its role in developing projects on the basis of its one internal or self-generated resources, the ICO has the mandate for pre-selection and supervision of coffee related projects submitted to the Common Fund for Commodities (CFC). Through its project work, the ICO’s has provided critical input and direction for technical assistance activities aimed at improving sustainable development. Over the past few years, the ICO has been involved in the execution or supervision of several “sustainability” related projects including:

- Lifecycle Analysis of the Coffee Sector
- The State of Sustainable Coffee: An Analysis of 12 Major Markets
- Sustainable Coffee Growing in Africa
- Reconversion of Small Coffee Farms in Self Sustaining Agricultural Units
- The Clean Development Mechanism and the Coffee Sector

Despite the growth in the number of projects adopting an “integrated approach” to sustainable development, technical assistance for the development of sustainable supply chains has not kept up with the pace of demand and opportunity. Moreover, there are indications that the speed with which market demands for differentiated and sustainable coffees are developing, that the CFC in light of its limited resources, limited areas of activity and the length of project approval times, will not, on its own, be sufficient to meet supply chain needs in this area.

While individual country-based funding has the capacity to provide more targeted and flexible funding based on the rapidly changing market conditions of the coffee sector, 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.

4.2.1 Clearing House for Coffee Related Projects and Assistance

At present technical assistance and related projects committed to the coffee sector are scattered through a multiplicity of funders, 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

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information related to the coffee sector, 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.

4.2.2 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), ICO members have an opportunity to establish an efficient and coordinated approach to funding sustainable supply chain management through the establishment of a “Partnership Fund for Sustainability”. While the nature and management of any eventual fund would necessarily require careful consideration and planning, it is clear that, following the needs based approach to sustainable development called for under Agenda 21, it should, in general, entail the transfer of funds from consuming to producing countries. Whether or not any eventual funds for such an initiative should be raised through private sector contributions, public sector contributions, or a combination of the two, needs to be studied, along with whether or not such contributions should be determined individually or jointly.

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

4.2.3 Credit Facilitation

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: 1. pre harvest financing and seasonal working capital 2. infrastructure development 3. diversification 4. debt financing and 5. risk management. The growth in the complexity and technical specificity associated with supplying differentiated markets has amplified the investment challenge facing producers. As was demonstrated as recently as 2004, producers’ inability to access credit to move their coffee to market

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also jeopardizes the coffee industry’s access to uninterrupted supply of differentiated coffees. At the same time, investments designed to enable access to the highly organized supply chains associated with such markets, have the potential to generate increased returns and overall revenue stability for producers. The freeing of access to credit specifically for producers committed to entering differentiated markets would stimulate the sector’s transition to differentiation, and with it, overall sustainability. Although a number of specialized credit institutions currently exist, infrastructure support both 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.

### 4.3.4 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. Producer exposure to market volatility has grown with the elimination of state marketing boards and related institutions over the past two decades, intensifying producer vulnerability to market volatility and the need for compensatory instruments. 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 within the sector. Roasters and traders in the private sector have long relied on a suite of risk management mechanisms ranging from put options to hedges and other specialized trading instruments. Such instruments currently remain largely out of reach for most producers, particularly the smallest among them, due to the absence of capital, technical assistance and appropriate infrastructures. The ICO could play an important role in improving producer access to existing risk management instruments, as well as the development of more accessible instruments and overall improved stability for those most at risk, by establishing a risk management facility.

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

### 4.3 Market Efficiency and Cost Internalization

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 principle outcome sought by ICO activities in this area, has been the maintenance of
prices which are both “fair” to consumers and “remunerative” for producers. Economic theory predicts that the objective of “fair and remunerative pricing” is maximized under free markets operating under conditions of perfect competition. The coffee market suffers from deep and pervasive market imperfections related to imperfect information, market concentration and externalities associated with the provision of public goods. While it is clear that the ICO cannot be responsible for creating the “conditions of a perfect competition”, it is also clear that the ICO’s mandate as focal point for international cooperation on coffee matters, places it in a unique position for the generation of conditions conducive to improved market efficiency.

The ICO’s activities related to information collection, generation and dissemination on coffee markets helps 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.

While supply management is one possible tool for adjusting prices towards full cost internalization, deep seated political and economic obstacles to cooperation at this level suggest that softer tools aimed at adjusting the pricing mechanism are likely to be most appropriate in the given context. In addition to measures such as Resolution 420, research into the potential of using the Clean Development Mechanism and other efforts to promote the expansion of differentiated markets, the ICO should look into the potential for using preferential fiscal treatment of coffees associated with socially and environmentally preferable production practices. Following such an approach, the ICO could provide a forum for identifying appropriate national policies towards such fiscal differentiation including, but not limited to:

- 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
- Set premium schedules for recognized “sustainable” coffees (on commodity exchanges)

**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.**

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4.4 Moving Forward

The preceding overview of the challenges and opportunities to building a sustainable coffee sector, highlights the complexities of problems facing the sector. While the negotiation of any agreement involving a large number of governmental members, can be expected to 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 make sure 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 the different strategies is possible amongst the different negotiating parties. With this background 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 should, as part of the overall negotiation process of the ICA, establish a “special negotiating group” to explore, develop and propose options for linking sustainability initiatives with overall ICO strategy within the context of the new ICA.

Recommendation: The ICO should establish a “special negotiating group on sustainability” to explore the above and additional options for enabling the strategic development of market-based sustainability initiatives within the context of the new ICA.

5.0 Conclusion

The growth in the number, variety and depth of private sector sustainability related initiatives, combined with a growing consumer recognition for differentiated coffees, has put the coffee sector at a crossroads. New forms of organization along supply chains have the potential to improve the positions of small producers in international markets while new monitoring mechanisms for social and environmental practices can help ensure best practice across global supply chains. Although market failure still persists in the coffee sector, the growth of intentional systems to supply chain management provide a critical tool towards efforts to cost-internalization and thus have an important role to play in fulfilling the Johannesburg Earth Summit’s call for concrete mechanisms for implementing sustainability. The list of opportunities provided above is intended a constructive input into its efforts towards the fulfillment of this objective.

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3 Access to reasonable finance has long been recognized as a key element of sustainable production strategies for coffee producers. Finance can play a critical role in the stabilizing farmer cash flow as well as providing investment capital for diversification. See OXFAM, *The Crisis Continues* (2005) at p. 10-13.
Different forms of coffee production form a gradient between sun and shade grown systems. At least five general types of coffee production systems have been identified: traditional; traditional poly-culture; commercial poly-culture; shaded mono-culture and sun. The ‘traditional’ and ‘traditional poly-culture’ systems utilize the original forest canopy while the commercial and shade monoculture varieties utilize commercially introduced shade cover. See Merle D. Faminow and Eloise Ariza Rodriguez, Bio-diversity of Flora and Fauna in Shaded Coffee Systems. (CEC, 2001).

The average rate of conversion to shade monoculture and sun coffees for Northern Latin America as a whole has been estimated to be 40%. In Latin America a 50% reduction in avian bio-diversity has been observed under sun growing conditions. In addition to aggravating soil erosion, reduced forestation associated with sun and mono-culture production reduces overall carbon sequestration. The shift from “diverse shade” systems to “monoculture shade” systems has been estimated to have reduced carbon sequestration between 30% and 50% in Latin America. Rice, R. and J. Ward, Coffee, Conservation, and Commerce in the Western Hemisphere. (Natural Resources Defense Council and Smithsonian Migratory Bird Center. Washington, DC, 1996.) The difference in carbon sequestration capacities between monoculture shade grown coffee and forest shade grown coffee has been estimated to be more than two-fold. PROCAFE, Differentiating Salvadorian Coffee. Paper presented at the World Bank, October 2001 cited in Kristina Sorby, Background paper to World Bank Agricultural Technology Note 30, “Toward more sustainable coffee’ (World Bank, 2002).

Research commissioned by UNCTAD on the environmental effects of coffee production in the Ivory Coast concludes that coffee has played a major role in reducing the country’s forested land from 16 million to 3 million hectares. Denis Ouobole Seudieu, L’impact de la production et de la transformation du café, du cacao et du riz sur l’environnement en cote d’ivoire. (UNCTAD, 1993) UNCTAD/COM/24.


Although producer organizations can provide an important avenue for democratic, equitable representation and infra-structure development, the relative isolation of many small coffee farmers often places prohibitively high transaction costs on effective participation in such organizations.

A survey of coffee plantations in Guatemala, for example, revealed that none paid the country’s minimum wage and that a majority of them did not even pay half the minimum wage. Bart Ensing, ‘The viability of a code of conduct in the coffee sector in Guatemala’, Fair Trade Organizatie July 2000; The Guatemalan government regards minimum wage as being sufficient to cover on 40% of basic needs. Meanwhile, child labour is reported to be widely used on plantations in some countries. In Kenya, for example, it is estimated that 30% of the coffee pickers serving plantations are below the age of 15. See OXFAM, supra note 1 at 11-12. Housing conditions among such plantations have also been reported to be below national requirements. GTZ, Working and Living Conditions in Large Scale Coffee Production in Latin America accessed at http://www.die-gdi.de/DIE_Homepage.nsf/ViewAttach/51EFF03B641F9792C1256C2F0029A34E/$File/Summary-e2.pdf?OpenElement.

Under-regulated agrochemical use also threatens farmers and other rural residents with exposure to toxic substances in water supplies. In a 1987 case, more than 200 people became sick from drinking water contaminated with agricultural pesticides and fertilizers in the western Mexican state of Jalisco. Ivan Restrepo, 1992 Los Plaguicidas en México (México, D.F.:Comisión Nacional de Derechos Humanos), at 126-127, 130. Meanwhile, the use of nitrogen fertilizers in Costa Rica has been linked with unsafe levels of groundwater pollution. Levels in excess of World Health Organization acceptable levels have been documented in Costa Rica. Olman Segura B. and Jenny Reynolds, "Environmental Impact of Coffee Production and Processing in El Salvador and Costa Rica," (Geneva: UN Conference on Trade and Environment, UNCTAD/COM/20, August 27, 1993), at 15-16.


Many voluntary initiatives revolve around the development of new management structures both at the producer and supply chain levels which can have positive effects on efficiency.

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14 The Salvador Coffee Declaration was signed by the following organizations as part of a contribution to the Second World Coffee Conference held in Salvador, Brazil in September of 2005: CONTAG (Brazil), Karnataka Growers Federation (India), Oromia Cooperative Union (Ethiopia), Sidamo Cooperative Union (Ethiopia), Junta Nacional de Café (Peru), FEDECOCAGUA (Guatemala), Foro del Café (El Salvador), Frente Solidario (Central America), Global Alliance on Coffee and Commodities (GLACC), UIITA (Brazil), Koffie Coalitie (Netherlands), OXFAM International.

15 Giovannucci. Supra note 11 at 60-69.

16 A study commissioned by DFID on the impacts of Fair Trade concluded that one of the most important impacts of Fair Trade for producers was the role of the Fair Trade supply chain in providing up-to-date market information. See Oxford Policy Management, Fair Trade: Overview, Impacts, Challenges (2001) at 27.

17 Sustainability initiatives, through their traceability, monitoring and enforcement requirements require highly organized supply chains. The development of the necessary information structure can reduce supply chain inefficiencies.

18 On the one hand, the fact that producers require certain basic infrastructure in order to access “sustainable markets” operates as an incentive to organization. Recognizing this need, most sustainability initiatives complement their “administrative” with efforts to facilitate partnerships for providing technical assistance and infrastructure development. For example, The Green Development Foundation, Solidaridad and Sara Lee Foundation have formed the “Coffee Support Network” designed to support farmer adoption of Utz Kapeh guidelines.

19 Although environmental practices differ across initiatives, typical compliance requirements include: shade coverage, water conservation, forest conservation, rational use or elimination of synthetic chemicals.

20 Core ILO standards form the basis for many of the sustainability standards currently operational in the coffee sector.

21 The Centro de Investigacion des Mercados Sostenibles (CIMS) estimates that Latin American coffee producers received premiums between $.05 and $.60 per pound for coffees sold to sustainable markets. See Andres Villalobos, Prices and Premiums for Certified Coffees (CIMS, 2005). Actual premiums vary significantly between initiatives and market prices. Higher returns are also available through increased productive efficiency. See, for example, Nestle Project Report.

22 Some systems, such as Starbucks Café Practices, include options for “preferential supplier status” based on the adoption of preferred practices. Due to traceability and trust requirements for effective implementation, there is a stronger tendency for producers to deal directly with buyers and roasters through long term relationships. Socially and environmentally responsible practices also reduce social and environmental instability with concomitant impacts on economic stability.

23 Most initiatives are built on governance structures which operate independently of traditional supply chain decision making (eg. where key nodes drive supply chain activities) and, as such, can provide unique opportunities for economically disadvantaged actors to have more direct input in supply chain decision making. Accessing this opportunity is often difficult for producers who lack strong organizational representation and resources. (see below).

24 Market research indicates that industry players and consumers are confused about the impacts of different initiatives. At present there is very little objective research assessing the costs and benefits of applying different systems.

25 Each sustainability system entails certification and monitoring costs in addition to regular production costs. The fact that different systems have different administrative requirements leads can render multiple certification unaffordable for many producers.

26 Membership in a well organized producer group is a virtual prerequisite to participation in sustainable supply chain initiatives. Producers who are not organized may be systemically excluded from such systems.

Effective participation in both international markets and policy discussions for sustainability requires significant administrative resources which are not included in the price mechanism.

A more recent example of the ICO’s macro-economic approach is provided via Resolutions 407 and 420 which establish a quality standard for international export with the intent of reducing overall supply and improving demand, thus raising prices of coffee on the international market.

Chapter 14 of the Havana Charter in Restoration of World Trade, supra note 22 at 525. During the 1990s there was some explicit interest in the possibility of “International Commodity Related Environmental Agreements” (ICREAs) as a means of joining the macro-economic and micro-economic approaches to sustainable development. Following the integrated approach to sustainable development, it may be useful to conceptualize International Commodity Agreements as “Sustainable Commodity Agreements”—that is, agreements which take the Rio Principles and Declaration as the overall guide to international cooperation in a given commodity sector. This approach forms the context of our analysis below.

Art. 1(6) of the ICA 2005 specifies that one of the objectives of the agreement is, “to encourage members to develop a sustainable coffee economy”. Art. 39 of the ICA 2005 states that: “Members shall give 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 agreed at the United Nations Conference on Environment and Development, held in Rio de Janeiro in 1992.” ICA, 2005.

Principles 3, 5, 6 and 7 of the Rio Declaration emphasize the importance of equitable needs satisfaction of present and future generations (3), poverty eradication (5), priority to developing country interests (6), and global partnership with differentiated responsibilities (7). By bringing producing and consuming countries, developing and developed countries, together towards mutual cooperation, the ICO fundamentally embodies the spirit of the Rio Declaration.


Proposal for an ICO Sustainability Committee, WP Board 960/04 (September 17th, 2004)

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.

Diversified livelihoods can be achieved through vertical diversification along the coffee supply chain and horizontal diversification, either alongside or out of coffee production.

Producer organization 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.

A clearing house could take many different forms—ranging from a database to a “warm body” forum consisting of project promoters, executors and donors.

UNCTAD, Preparation of a Successor Agreement to the International Tropical Timber Agreement, 1994 TD/IMBER.3L.6 (October 5th, 2005)

It is important to note that discussions to date on the possibility of a “World Sustainable Coffee Fund” within the ICO (PSCB 58/04) have revolved around one particular model and framework for a coffee fund. This recommendation foresees the need to move beyond this specific proposal in the interest of achieving the principal objectives of: increased commitments; access, efficiency and flexibility for targeted technical
assistance. The performance of the “environment fund” under the 1994 International Cocoa Agreement as well as the Diversification fund of the 1968 International Coffee Agreement should form a basis of the proposed analysis.  

44 OXFAM, supra note 3.


46 Although the ICO is the logical forum for negotiating the establishment of such a facility, it may make more sense to actually house such a facility outside the ICO (perhaps within an international institution with specific financial expertise—for example, the World Bank or another development bank).

47 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.”

48 For example, The Gourmet Coffee Project.