

Fairtrade coffee



1. The Global Coffee Industry in Brief

Coffee is the world's second largest traded commodity after crude oil. It is grown in more than 50 countries in a band around the equator and provides a living for more than 20 million farmers. Up to 100 million people worldwide are involved in the growing, processing, trading and retail of coffee. According to the International Coffee Organisation (ICO) some 125m people are dependant on coffee in the developing world and if you add those in the developed world, including people working in transporting, selling and financing coffee, about 500m people are involved.

For most farmers there is no guarantee when they plant their crop that they will be able to sell it for a decent price come harvest time. They frequently have to borrow money at exorbitant interest rates before the harvest to invest in production and take care of their families. The moneylenders are sometimes also the local coffee dealers, known as 'coyotes' in Latin America; they are often the only source of information about the current coffee price, which, like many commodities, is dictated by the fluctuations of futures and commodity exchanges, most importantly in New York and London.

At harvest time, farmers are forced to sell their crop to local dealers for whatever price they can get, and even if the market price drops below the cost of production, they still have to sell in order to pay back their loans. This means that after working so hard to produce their crop, farmers can still end up with no profit, or even with huge debts. Farmers throughout the world have had to give up their land in order to pay off their debts, and during slumps in the price of coffee, many have been forced to migrate to the cities in search of work, joining the growing number of urban slum dwellers.

Most conventional coffee is traded through the world commodity markets, so the buyer and seller never meet. This means that buyers do not know who the growers are, or how much they receive for their beans. Nor is it possible for buyers to know what conditions the producers work in. When coffee is traded in this way, it is impossible for international buyers to influence the price paid to the farmers.

Coffee is a 'boom and bust' industry characterised by highly volatile prices: arabica coffee prices rocketed to US\$2.73 per pound on the New York market in 1997 when the Brazilian crop was hit by drought but plummeted to 30-year lows of around 45 cents in 2001 when the market was oversupplied. But the world price does not reflect the amount the farmers actually receive from coffee dealers - depending on their position in the supply chain, the growers may receive considerably less than this.

Global production fluctuates according to various factors such as the affects of adverse or beneficial weather conditions and the price received by farmers determines how much they invest in their crop. In 1990 production stood at 5.6m tonnes; in 1997 at 6m tonnes; in 2000 at 6.9m tonnes; in 2003 at 6.2m tonnes; and in 2006 at 7.3m tonnes.

2. Fairtrade Coffee

Price and Benefits

Fairtrade guarantees a minimum price that covers the cost of sustainable production and allows for investment. The knowledge that they will receive a stable price for their crop gives farmers a degree of security that allows them to plan for the future.

The guaranteed Fairtrade price paid to farmers' associations and co-operatives is US\$1.31/lb for arabica coffee. This comprises the Fairtrade minimum price of 131 cents/lb plus the additional Fairtrade premium of 10 cents/lb to be used for social and commercial development projects agreed on by the farmers. When the world price is higher the Fairtrade price is always 10cents per pound more.

Direct trade

The direct nature of the Fairtrade commercial relationship is at least as important as the price. Bypassing the international commodity market and buying direct from farmers' organisations means that farmers get a greater share of the rewards of their labour. Fairtrade terms mean longer-term contracts and up to 60% pre-financing if required.

Fairtrade returns a better deal to farmers than 'conventional' coffee because:

- all Fairtrade coffee must be bought direct from organisations of small growers
- these organisations must be democratically structured and genuinely representative of their members
- the coffee must be bought at a price which meets the cost of production, plus a margin for social investment
- the availability of advance payments ensures that the grower organisations can finance their activities.

Fairtrade coffees are independently audited and are guaranteed to meet these criteria.

The security of selling on Fairtrade terms means that farmers:

- have been able to strengthen their organisational and commercial capacity
- have been able to survive one of the worst price slumps in living memory
- have been able to afford medical treatment for themselves and their families
- have been able to send their children to school.

3. Fairtrade and Oromia Coffee Co-operative, Ethiopia

Oromia Coffee Farmers' Co-operative Union was founded in 1999 by 35 small certified organic co-operatives. Its members are indigenous farmers located in the vast Oromia State of southern and southwest Ethiopia which produces 65% of the country's coffee. The farms are located in mountainous, rainforest areas at altitudes of 1,500 to 2,000 metres where electricity and running water are rare.

Eleven of Oromia's member co-operatives, all organic, have been Fairtrade certified since May 2000. They represent almost 9,000 farmers and produce around 3,000 tonnes of organic coffee a year. In 2003, they sold 950 tonnes to Fairtrade markets in Europe and the US.

The co-operatives receive a guaranteed minimum price of \$1.51 a pound for Fairtrade sales. This includes a 20 cents organic premium and the 10 cents Fairtrade premium reserved for education, health and credit programmes that their communities desperately need.

"Our members have greatly benefited from the profits Fairtrade has generated. On top of that, we are now getting technical and financial support that enables us to continue our tradition of excellence. Therefore, Fairtrade membership is very important to our organization and its members." Tadesse Meskela.

Use of the Fairtrade premium

• **Social development.** Under a quarter of Ethiopian children complete primary education¹. As Tadesse Meskela points out: "The farmers cannot afford to buy [school] uniforms for children, cannot afford to pay even a small amount of contribution to the schools, they cannot afford to pay for food for when they stay in school, because it is 10 to 20 kilometres from their house." Recognising the essential role of education in the fight against poverty, Oromia is in the process of building four primary schools to help farmers keep their children in school.

Two clinics and two clean water pumps have also been built or are under construction (2004) and farmers have used the extra income to build or repair houses and purchase livestock.

The Homa Co-operative in Yirgacheffe has 967 members, all Fairtrade and organic certified. Fairtrade premiums are funding the construction of two schools as well as a clinic built from traditional teff grass bales. It will serve more than 2,000 people, with treatment under the supervision of a trained health expert provided by the government².

• **Equipment and repairs.** Seven coffee washing stations have been completed or are under construction. A fund has been developed for the repair of de-pulping machines to safeguard the organization's capacity to produce high quality,

¹ 24.1% in 1999, World Bank Development Data.

² Extract from Ethiopia Trip Report by Higher Grounds Coffee Co at <http://www.javaforjustice.com/ethiopiafairtradecoffee.asp>

washed Arabica coffee.

- **Food security.** Members have reduced their dependence on imported food by intercropping coffee plants with fruit and vegetables.

- **A commitment to organic production.** The cooperative provides technical assistance to its members, including workshops on composting the by-products of coffee production and utilizing shade trees and natural fertilizers to enrich the soil.

- **Future plans.** The premium has been earmarked for the construction of a processing plant and warehouse and 50 more coffee washing stations. Quality improvement programmes are planned and money will be invested in promotional and marketing work to expand sales in Europe, Japan and the US.

"To me, Fairtrade means a buying and selling process in which humanitarianism has a big part. It is creating a family relationship between peoples who live on this planet." Tadesse Meskela, Oromia General Manager, January 2005.

"With the extra income from the coffee sales we have built a school and given a dividend to our members who are now able to pay school fees for their children"

Dulecha Gobena - Chairman, Kilenso Resa Cooperative, Yirgachefe.

4. International Coffee Crisis 1998-2005

The International Coffee Agreement was relatively successful in stabilising prices until 1989 when political manoeuvring led to the removal of its price maintenance and export quota clauses. Prices immediately slumped and have remained low apart from two short-lived booms in 1994 and 1997 that saw arabica prices rocket above 240 cents/lb when frost then drought hit Brazilian production. The slump deepened into a crisis, with arabica prices tumbling to around 45 cents/lb in October 2001, the lowest-ever level in real terms. Prices remain at around 30-year lows, or 100-year lows if adjusted for inflation. Production costs vary from country to country, 45 cents in Vietnam, for example, but \$1/pound could be considered an average figure.

The collapse was caused by the oversupply of coffee driven largely by the rapid expansion of production in Vietnam and new plantations in Brazil. Brazil's increased supply is a direct result of the deregulation, private investment and technical innovation in the sector, while its high labour costs are mitigated by the use of improved mechanical harvesting and a consequent reduced need for labour. Vietnam's supply surge was driven by the government policy of increasing earnings from agricultural exports and was supported by government subsidies, institutional funding and very low labour costs.

Social & Economic Impact

The collapse in international prices has had severe economic and social consequences for producing countries and has devastated the livelihoods of millions of coffee farmers and plantation workers. Prices did not even cover the costs of production for most growers, seriously affecting farmers' ability to provide for their families, pay medical bills and keep their children in school. Thousands abandoned their land and migrated to city slums in search of work or made the treacherous journey to the US. In Nicaragua, at least fourteen malnourished and sick adults and children died as unemployed coffee pickers marched to the capital, desperate for work and the promise of land.

"The price paid for coffee is now at a thirty-year low and small farmers are unable to cover the costs of production. They cannot earn the income necessary to feed their families, send their children to school, buy essential medicines and stay on their land. The coffee crisis is affecting 25 million producers in large parts of Africa, Asia and Latin America. Coffee is the nucleus of the Ethiopian economy. Coffee accounts for more than 50% of Ethiopia's exports, 95% of which is grown by small farmers. About 700,000 households are dependant on coffee and another 15 million are partly dependant on coffee for their livelihoods." Tadesse Meskela, General Manager Oromia Coffee Co-operative, Ethiopia, May 2003.

The impact of the coffee crisis on the economies of producing countries is demonstrated by the fact that at the depth of the crisis the value of coffee exports fell by more than half from \$11.43b in 1998 to an estimated \$5.64b in 2003. This is in spite of export volumes increasing from 79.92m bags to 84.87m in the same period.

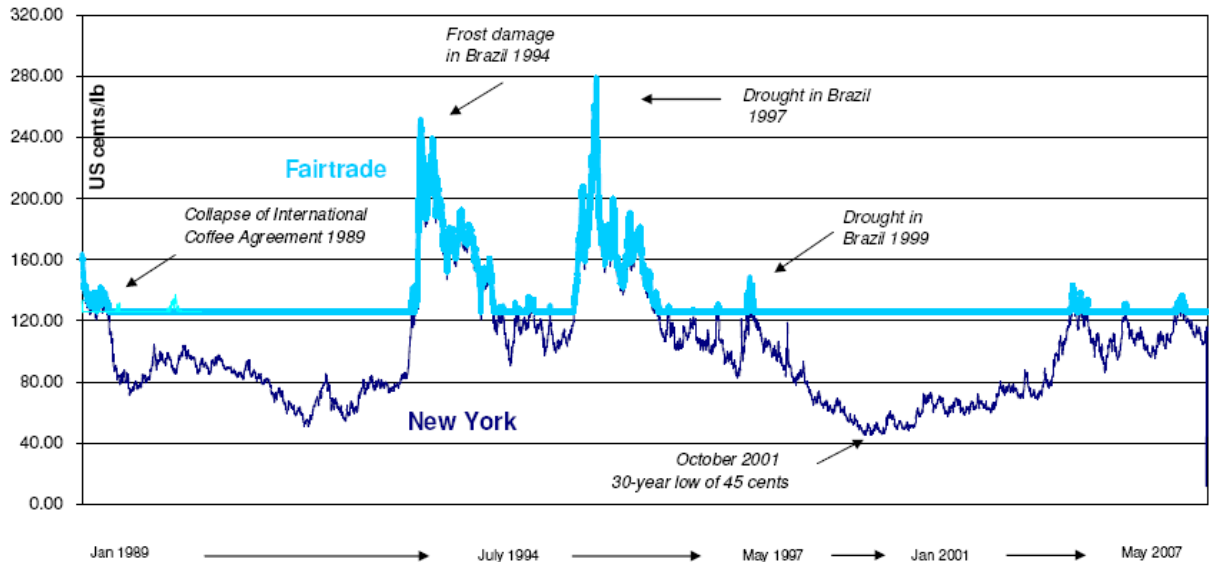
"The collapse of coffee prices that has resulted in the loss of revenue for Ethiopia is obviously very serious. Despite the improvement of the quantity and quality of coffee production in the last six years, Ethiopia lost nearly \$900 million over that period." H E Mr Fisseha Adugna, Ambassador of Ethiopia, November 2004.

5. The Coffee Market Today

Prices have recovered since 2005 and supply and demand in the market is now relatively balanced. In fact, there is currently a small supply shortfall caused by a reduction in production as growers responded to the lengthy period of low prices. But this can all change if production is affected by adverse weather or a bumper crop in Brazil.



The Arabica Coffee Market 1989-2007: Comparison of Fairtrade and New York Prices



NB Fairtrade price = Fairtrade minimum price of 121 cents/lb + 10 cents/lb premium*

When the New York price is 121 cents or above, the Fairtrade price = New York price + 10 cents

* Premium was increased from 5 cents/lb on 1 June 2007

The NY price is the daily closing price of the second position Coffee 'C' futures contract at the NY Board of Trade

© Fairtrade Foundation