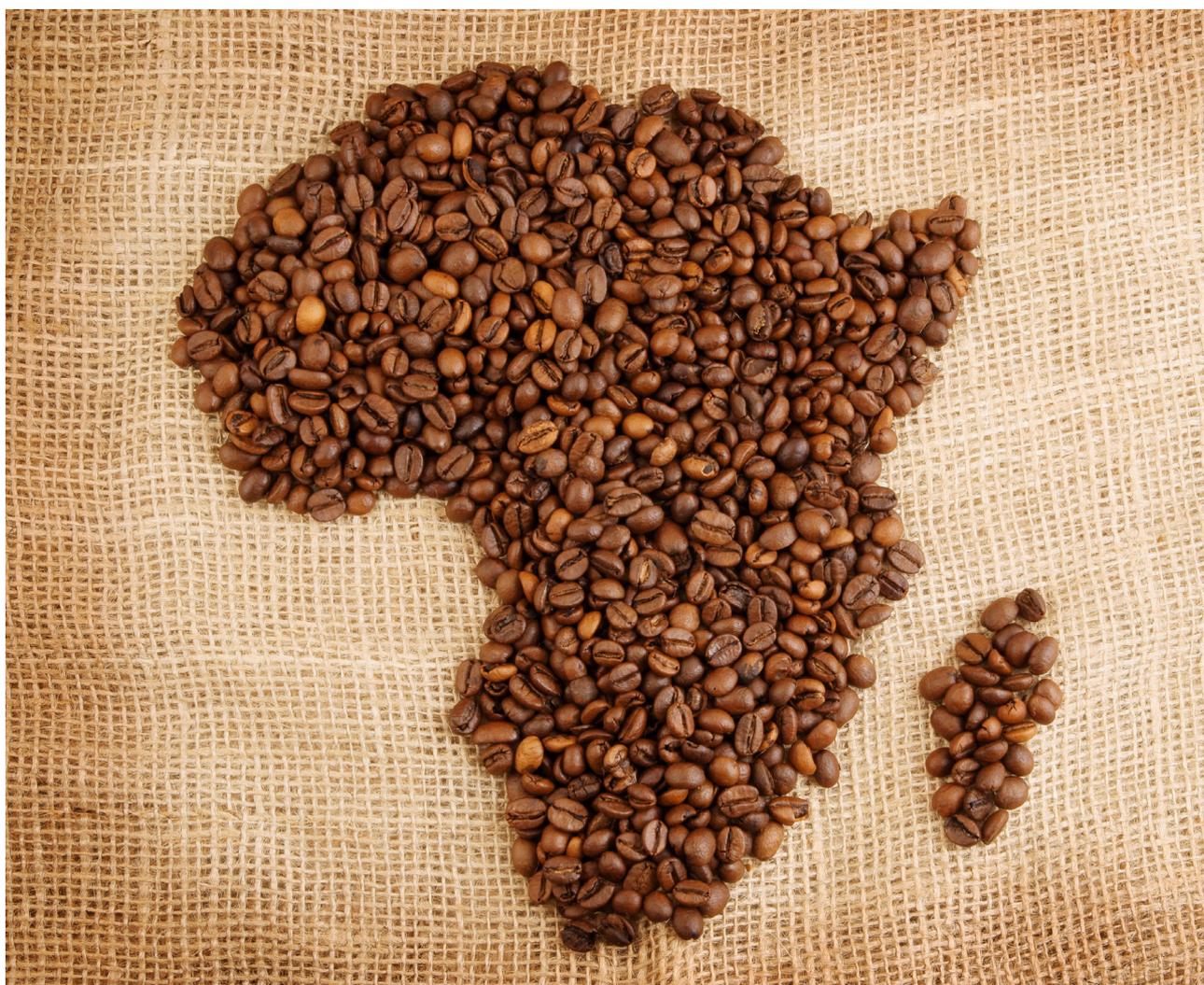


MORE FROM THE CUP

BETTER RETURNS FOR EAST AFRICAN COFFEE PRODUCERS



More from the cup

Better returns for East African coffee producers

About the paper

East Africa produces some of the world's most valuable specialty coffees, yet only a small share of profits go to coffee producers. Using case studies from Africa and beyond, the report explores how to get better prices for green coffee beans, learn about branding and develop business partnerships in international markets.

Direct trade from origin, also feasible through e-auctions, can result in better average prices for green beans. Roasted coffee offers significantly higher margins, but may not be practical to export. New alternatives exist for contract roasting, packaging and outsourced marketing, to transform green beans into branded coffee close to the customer.

Comments to this paper are welcome. Conclusions will be part of a forthcoming new edition of the ITC Coffee Guide.

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Foreword

Coffee is one of the world's most popular beverages. More than 2.6 billion cups of coffee are consumed every day and over 120 million people live off the coffee value chain worldwide. From fields to factories, from beans to baristas – coffee has moved from a simple commodity to a movement.

The dark side of the coffee business however, is that some of those farmers who grow the crop, the women who harvest the beans and those who pack the more than 140 million bags of coffee produced each year, are not benefiting from the large profits generated at the top of the value chain.

Coffee commodity prices reached new lows in 2019 (before recovering slightly) and the pain was felt in the low prices paid to producers. The cost-efficient producing countries of South-East Asia or South America, which focus on bulk production, absorbed the drop in prices to some degree. But in East Africa, a region renowned for the variety and quality of its specialty coffees, smaller-scale production and higher costs meant that low commodity prices resulted in losses or unsustainably low earnings for farmers.

Looking at the international value chain that delivers the '\$5 cup of coffee', less than 1% of the price remains in the hands of the men and women who cultivated the crop. Almost all value is created after the farm gate. Even allowing for the expected returns of the retailer, enough value should be generated to allow farmers a greater share of the global earnings.

Fair trade initiatives seek to do this by taking into account the cost of production and establishing generous benchmarks for the purchase price of raw coffee. But what if groups of farmers could be supported in adding value to their crop – not just selling the 'green beans', but by roasting and packaging their coffee, even selling it under their own brands? This is a priority for policymakers in East Africa who are working on initiatives to promote roasting facilities and encourage local coffee consumption.

This report examines these initiatives and seeks to go further. Can we learn lessons from farmer-owned coffees marketed internationally? Is it possible to contract with foreign partners to transform the product and market it on behalf of the farmers? Does the changing nature of coffee consumption and new service models and distribution channels open up new potential for coffee producers to earn more money for their work, escape poverty and eventually thrive from higher value added?

Historically, East Africa has had very few convincing success stories of farmer groups integrating into developed country consumer-level retail; Central and South America are only now beginning to show some success with these models. This publication recommends reimagining the experience of East African farmers and illustrating the profit potential of retail sales in developed countries, while highlighting the risks and need for long-term strategy and investment.



Dorothy Tembo

Acting Executive Director
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Contents

| | |
|--|-----------|
| About the paper | ii |
| Foreword | iii |
| Acknowledgements | iv |
| Acronyms | vii |
| Executive summary | viii |
| CHAPTER 1 WORLD COFFEE MARKET | 1 |
| World coffee trade: Concentrating market power among multinationals | 2 |
| The coffee value chain: A small share for producers | 4 |
| Changing preferences: Specialty coffee has high growth potential | 5 |
| Consumption in producing countries starts to generate demand | 7 |
| Coffee farmers face a variety of challenges | 7 |
| CHAPTER 2 SPECIALTY COFFEE MARKET | 10 |
| The sector is just starting to invest in sustainability | 10 |
| Specialty coffees are positioned on stories and values tied to their origins | 11 |
| Higher value chain models for green and roasted specialty coffee | 12 |
| Direct trade | 12 |
| Coffee auctions | 12 |
| Contract farming | 12 |
| E-commerce platforms | 12 |
| CHAPTER 3 EAST AFRICAN COFFEE MARKET | 13 |
| Challenges of productivity and profitability in East Africa | 13 |
| 'Premiumization' of African coffee | 14 |
| Country-by-country overview | 15 |
| Ethiopia | 15 |
| Kenya | 15 |
| United Republic of Tanzania | 15 |
| Rwanda | 16 |
| Uganda | 16 |
| Burundi | 17 |
| CHAPTER 4 BUSINESS MODELS FOR FUTURE SUCCESS | 18 |
| Direct trade models – green coffee | 18 |
| E-commerce models – e-auctions and online sales | 18 |

| | |
|---|-----------|
| Online sales of green coffee | 18 |
| E-auctions for green coffee | 19 |
| Online sales of roasted coffee | 19 |
| Value addition model 1 – selling roasted coffee locally and in coffee shops | 20 |
| Value addition model 2 – selling roasted coffee from origin | 21 |
| Value addition model 3 – selling coffee that the consuming country roasts | 23 |
| CHAPTER 5 CASE STUDIES | 24 |
| Direct trade from origin | 24 |
| The Coffee Collective | 24 |
| Ndaroini Cooperative Society | 25 |
| Muchomba Coffee Farm | 25 |
| Stean's Beans | 26 |
| E-commerce | 27 |
| E-auctions | 27 |
| E-commerce for roasted coffee | 28 |
| Roasting in origin and selling domestically | 28 |
| Ya Coffee | 28 |
| Question Coffee | 29 |
| Roasting in origin and selling internationally | 29 |
| Eva's Coffee | 29 |
| Rwanda Farmers Coffee Company | 30 |
| CaféRwa | 30 |
| Rwashoscco and Angelique's Finest | 30 |
| Roasting and selling coffee in a consuming country | 32 |
| Topeca Coffee Roasters | 32 |
| Pachamama Coffee Cooperative | 33 |
| The profit potential of outsourced coffee value addition in target markets | 34 |
| CHAPTER 6 THE WAY FORWARD | 36 |
| Showing how the process could work in East Africa: A pilot project | 36 |
| Ways to add value | 36 |
| APPENDICES | 38 |
| REFERENCES | 39 |

Figures and tables

| | | |
|----------|---|----|
| Figure 1 | Top 10 producing origins | 1 |
| Figure 2 | Top 10 consuming markets | 2 |
| Figure 3 | Market consolidation in 2012–2018 | 3 |
| Figure 4 | Cost breakdown of a cup of coffee | 5 |
| Figure 5 | Value of five major European coffee markets | 6 |
| Figure 6 | Growth of global coffee markets, 1965–2016 | 6 |
| Figure 7 | Coffee sustainability – a drop in the ocean? | 11 |
| Table 1 | Coffee production 1990–2018: Today’s top 3 versus East African origins | 13 |
| Table 2 | Monthly profitability per mid-size grower | 14 |
| Table 3 | Selection of Cup of Excellence auction results in 2019 | 27 |
| Table 4 | Revenue increase for farmers through value addition | 34 |
| Table 5 | Viability of roasting and selling coffee using value addition service providers | 35 |
| Table 6 | A comparison of routes to higher value in coffee | 38 |

Acronyms

Unless otherwise specified, all references to dollars (\$) are to United States dollars, and all references to tons are to metric tons.

| | |
|-----|-----------------------------------|
| FOB | Free on board |
| ICO | International Coffee Organization |
| ITC | International Trade Centre |
| KG | Kilogram |
| LB | Pound |

Executive summary

More than 90% of coffee is exported as a raw product, with most of the added value transformation taking place in developed countries. Only a fraction of global earnings, estimated as less than 1%, remains in the hands of coffee farmers.

This paper examines how coffee farmers, and groups representing them, can add and retain more value in local and international markets. We study recent developments in the sale of specialty coffee and identify which initiatives have successfully increased the earnings of farmers. The focus lies on East Africa, which has been hit particularly hard by recent low prices for coffee, even though the region has some of the most prestigious varieties in the world. The paper concludes that new opportunities exist to set up direct-to-market sales channels and innovative relationships to roast and package coffee in international and local markets.

Global coffee production climbed 65% since 1990, and the growth in consumption has followed at a steady pace. It would be natural to assume that the future of the industry is bright. Yet, throughout most of 2019, the international benchmark price for coffee sat under \$1 a pound. This is 30% below the 10-year average and, for most producing countries, less than the cost of production. The industry as a whole has been forced to consider its economic sustainability – and whether the estimated 12.5 million farms¹ that depend on the crop for their livelihood can make decent earnings.

The coffee value chain is long, with many stakeholders in both producing and consuming countries. Consumption, considered mature in Europe, the United States and Japan, is still growing in most of the Far East and in developing economies, including many producing countries. Innovations in mature markets – such as the marketing of specialty coffees and convenience products including single-serve pods or capsules, ready-to-drink options, cold brew and nitro brew – continue to add value.

Over the last 20 years, the sector has undergone considerable consolidation at the consumption end of the chain. Giant coffee groups are now active across the industry, investing in specialty businesses where they see the most potential for growth.

Paradoxically, while consumption is booming, many origin countries that rely on coffee for their foreign exchange earnings are facing not only a crisis in prices, but also a longer-term challenge of sustainability. Without mitigating solutions, climate change threatens to destroy large growing areas. Other problems include high production costs, low yields, urbanization, ageing farming populations and lack of access to finance.

Driven by competitive pressure, global production has consolidated among fewer origins: more than 70% of supply is now sourced from five countries. African production has dropped 18% since 1990 and only Ethiopia and Uganda figure in the top 10 global ranking. African origins must consider how to improve productivity to remain competitive in global markets, but they also need to consider value addition to earn a higher share of what they produce.

Growing coffee is a lengthy process and is often the only source of income for farmers. Many farming families, with limited capacity to invest, cannot afford long periods for a return on investment. Consequently, driven by a need to generate cash, they continue to sell at or near the farm gate.

Initiatives to help farmers sell raw (also known as green) coffee at higher prices could kickstart a cycle of investment. Through a selection of case studies, we show that direct trade offers a good opportunity for farmers to establish linkages to markets and can benefit both buyers and sellers. E-commerce platforms have helped to improve market access and visibility to a much larger audience, and e-auctions, generally for specialty coffees, show the very best qualities.

¹ <https://scanews.coffee/podcast/64/reco-podcast-david-browning-on-using-technology-to-help-smallholder-farmers-s2-ep-5/>

Selling roasted coffee requires a different set of skills than those of the farmer; marketing and customer service are disciplines that must be learned. One possibility is for producers to market their coffee locally, as markets in East Africa remain largely untapped. Only Ethiopia enjoys a traditional coffee culture, with half of production supplying the domestic market. The rest of the region requires national and government support to promote an increase in consumption significant enough to improve the livelihoods of farmers.

A more challenging route to value addition is to export the roasted product. Coffee can be roasted in and sold from origin. Some farmers in East Africa are already doing this, albeit on a relatively small scale. Exporting roasted coffee involves various hurdles, including delivering a fresh product and covering the costs of its packaging, transport and storage.

Some attempts have been made to sell through e-commerce channels, including third-party marketplaces such as Alibaba, Amazon and eBay. An alternative model is for farmers to export green coffee and have it roasted and packaged in the consuming country. While this ensures that a fresher product reaches the marketplace, it requires a greater degree of complexity in managing service relationships.

For farmers to embark on the route of value addition, careful research and sound business planning are vital. Knowing the specifics of the destination market and its consumer preferences are prerequisites for success. Some form of representation in the consuming market is essential; this could be a local company, partner or agent. Third-party service providers, experts in their functional area, could be used to navigate the value chain and remove the need for initial capital investment. A key challenge for producers, remote from the consuming market, is to find trusted partners and to build and manage these business relationships.

This study suggests that groups of producers, supported and working together, could earn significantly higher margins by transforming their green beans into branded coffee in international markets. The costs and risks are high, however, as the financial cycle is much longer than receiving payment at the farm gate, and generating market awareness and repeat sales is expensive and uncertain. We recommend a series of pilot projects to evaluate the risks and returns with farmer groups, and then sharing the lessons learned with a wider group and initiating a long-term cycle of investment. Technical support would be necessary to structure these routes to value addition and new markets, along with sources of finance.

The coffee industry recognizes the need for change. Governments in East Africa have long supported the goal of increased local value addition. With the growing interest of consumers in the origin of coffees and new routes to market them, the time is right to examine how producers can navigate a path to higher earnings.

Overview of the paper

The current state of the global coffee industry, with prices sinking to 12-year lows in 2019, has alarmed the whole value chain and given rise to a plethora of reactions and initiatives designed to redress the balance and enable coffee farmers to enjoy a sustainable livelihood. An example, which conjures up a disaster management picture, is the Specialty Coffee Association's Coffee Price Crisis Response Initiative.² The initiative states: 'Chronically low prices, and pricing volatility, combined with the embedded systems that work to deter actors from responding to low prices with a more equitable distribution of value, contribute to unsustainable livelihoods for coffee farming communities and the specialty sector as a whole.'³

Coffee consumption has grown steadily over the last 30 years and the habits of coffee drinkers have changed dramatically. Production must be able to keep up with this increased demand. But while stakeholders across the value chain mull ways for coffee farmers to improve their earnings and production levels, the time may also be right for farmers to consider broadening their horizons beyond their farms.

This paper identifies the main value addition models available to farmers and explores the requirements for success. Through a selection of examples and case studies, we aim to equip the reader with an overview of tried and tested value-addition models. The route to higher earnings for coffee farmers does not necessarily

² For more information, see www.sca.coffee/pricecrisis or e-mail pricecrisis@sca.coffee

³ Presentation by Ric Rhinehart at Sintercafe. November 2019, Los Sueños, Costa Rica.

mean selling roasted coffee. Before considering this option, the paper examines whether farmers can earn more money by exporting their green coffee.

It further assesses the current global coffee market before examining value addition in detail. It takes a closer look at the specialty coffee market, showing how it differs from other types of coffee markets and how it benefited as coffee consumption increased over the last three decades.

The attention then turns to the coffee industry in East Africa, with a brief profile of each origin country. The paper weighs the different value addition models for both green and roasted coffee, and presents case studies – taken from the region as far as possible – to explain different approaches and experiences.

This study concludes with calculations that show the potential costs and benefits to support producers from the region, and evaluates the risks for producers in pursuing value addition in export markets. Explore this potential through a pilot group and ensure that the results are shared with a wider community of stakeholders.

Further comments are welcome on this paper, which is a work in progress.

CHAPTER 1 WORLD COFFEE MARKET

Coffee is one of the most popular beverages on the planet, with an estimated three billion cups consumed every day.⁴ The coffee world is largely split in two: consuming countries, which tend to be the most economically developed, and producing countries, found geographically near the equator and which are (in many cases) also the least developed economies in the world.

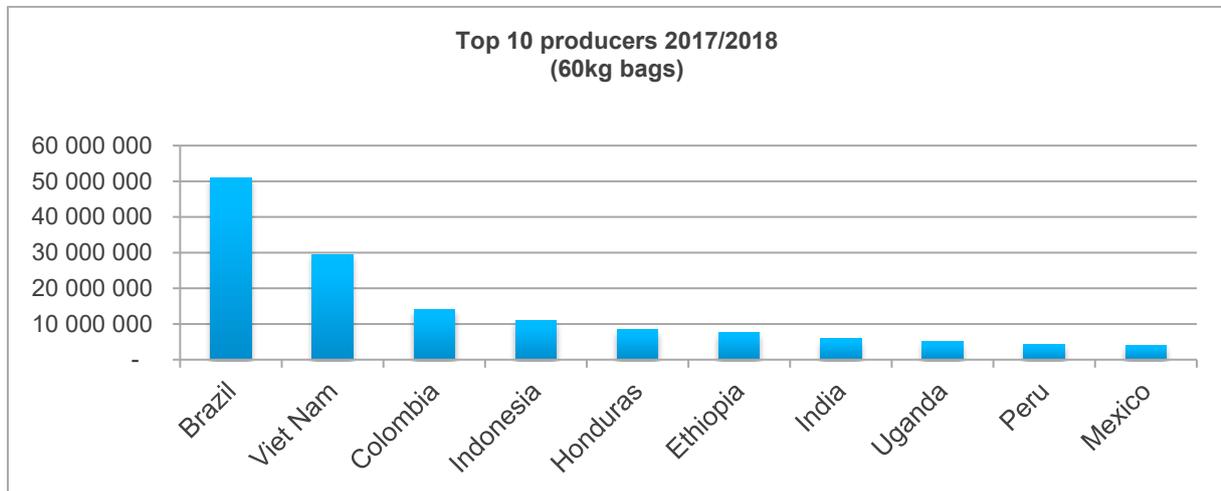
From 125 known wild species, only 60 have been developed for coffee production, and just two are produced for consumption – Robusta and Arabica.⁵ The former is grown at lower altitudes and is hardier, but it yields lower quality, much of which is used to produce instant coffee. Arabica is used to make the world’s finest-tasting coffees, often sold as single-origin or estate products, or in high-quality premium blends. It is also used in the average-quality coffee that is found in commercial, often loss leader, blended products on supermarket shelves around the world.

Specialty coffee is generally differentiated in some way, either by its superior quality or its uniqueness, through which it commands a premium price. There is little agreement in the industry about what percentage of total global volume fits into this category.

The International Coffee Organization (ICO) estimates that 25 million farming families produce coffee across the globe and that 100 million people – most of whom fall into the category of smallholder⁶ – rely on the crop for their livelihood. Since 1990, the market share of the top five producers has grown from 57% to 70%.⁷ More often than not, the countries that cultivate coffee are not traditional coffee-drinking nations, and producing countries account for less than 31% of global consumption.

This leaves them vulnerable when it comes to price negotiation, as their sales depend entirely on international demand. There are some notable exceptions to this – including Brazil, Indonesia and Ethiopia, which are the third-, fifth- and eighth-largest coffee consumers in the world (Table 2).

Figure 1 Top 10 producing origins



Source: ICO.

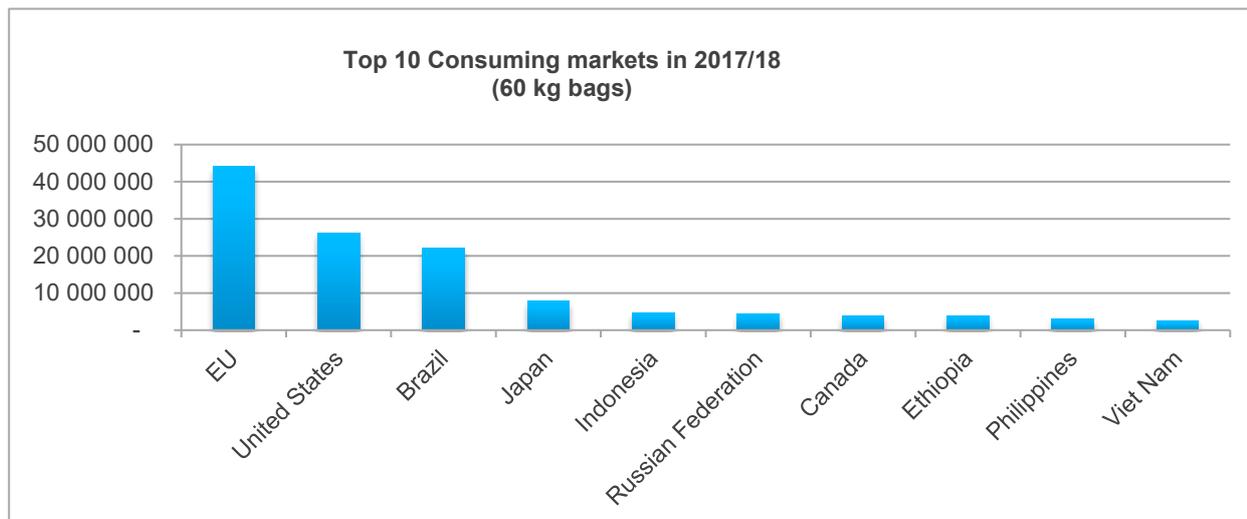
⁴ International Coffee Organization, 2019. Coffee Development Report (2019). *Growing for Prosperity: Economic viability as the catalyst for a sustainable coffee sector.*

⁵ World Coffee Research, 2018 Annual Report.

⁶ ICO, Coffee Development Report, *op. cit.*

⁷ ICO statistics.

Figure 2 Top 10 consuming markets



Source: ICO.

Consolidation has also occurred at the consuming end of the value over the last 20 or so years in the trade, roasting, supermarket and coffee shop sectors. According to Coffee Barometer 2018, ‘Billions are spent on countless acquisitions and mergers, positioning famous coffee brands in new markets. As the global coffee industry consolidates, it cuts cost to optimize profits, which causes additional downward pressure in the value chain which is increasingly felt by the producers at the farm level.’⁸

Some major roasters are investing in more specialty businesses to expand their specialty offer. On the flip side, they see a general decline in instant coffee (with the exception of three-in-one coffee mixes).

World coffee trade: Concentrating market power among multinationals

As Figure 3 shows, the top 10 roasters control more than 35% of all coffee sales. Nestlé and JAB Holdings have been investing, entering new markets and acquiring knowledge across the sector, buying into well-established and well-known specialty brands. This is a sign of recognition that the specialty end of the market is likely to continue to grow steadily.

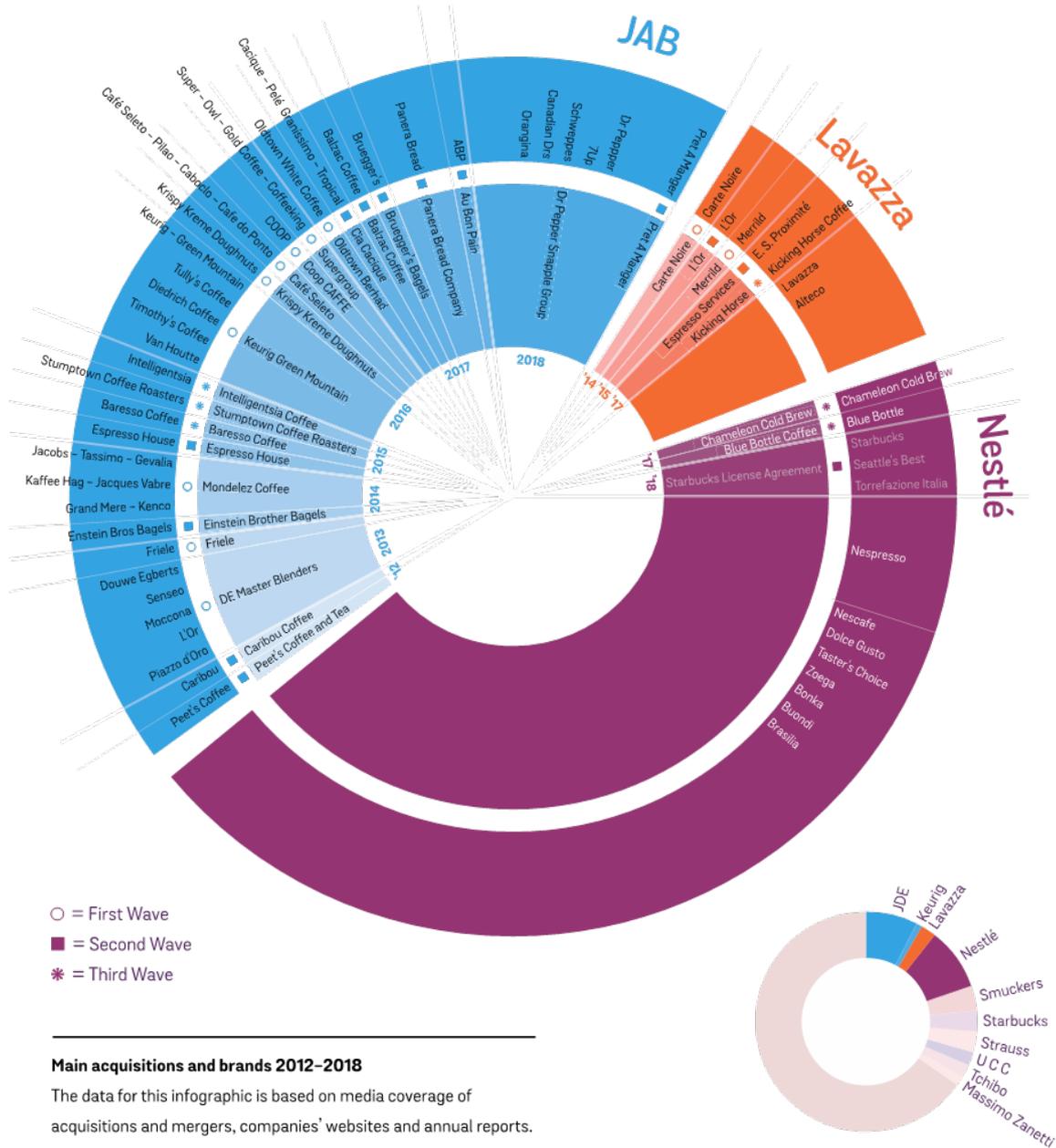
Industry experts describe the evolution of the coffee market in waves. The first wave occurred after World War Two, when new technology led to commoditization and cut-price goods that allowed large roasters to make coffee the beverage of choice for the masses. During the second wave, which started in the 1970s, differentiation began and coffee shop chains evolved, bringing higher quality and more variety to the market.

The third wave brought about the independent coffee shop. The new-generation café owner, coffee buyer and qualified professional barista have changed the focus to the origin of the coffee, its intrinsic qualities and the stories that surround its provenance, to the extent that ‘worldwide coffee culture is almost a cult’.⁹ This has been accompanied by increased attention to the brewing methods and the overall experience of coffee consumption. Consumers, influenced by the third-wave movement, are now demanding details about coffee origin, blend and sourcing practices. This focus on how coffee moves through the value chain – and the challenge to traditional processing, roasting and brewing methods – is already being referred to as the fourth wave.

⁸ Panhuysen, S. and Pierrot, J. (2018). Coffee Barometer 2018.

⁹ Pendergrast, M. (2010). *Uncommon Grounds: The History of Coffee and How it transformed our World* (revised edition), New York.

Figure 3 Market consolidation in 2012–2018



- = First Wave
- = Second Wave
- * = Third Wave

Main acquisitions and brands 2012–2018

The data for this infographic is based on media coverage of acquisitions and mergers, companies' websites and annual reports.

First Wave: Brands focusing on standardisation and volume, for at-home consumption (large roasters and grocery retailers).

Second Wave: Brands focusing on coffee origins and roasting styles, differentiation based on higher quality and out-of-home consumption (coffee chains).

Third Wave: Independent coffee shops focusing on consumer interaction with high quality coffee and a variety of brewing techniques.

Top ten roasters = 35% of world's coffee

Global volume of coffee 2016/2017: 157,7 million bags

Green coffee conversion

1 bag = 60 kilogram

1,0 tonne = 1,000 kilogram = 16,67 bags

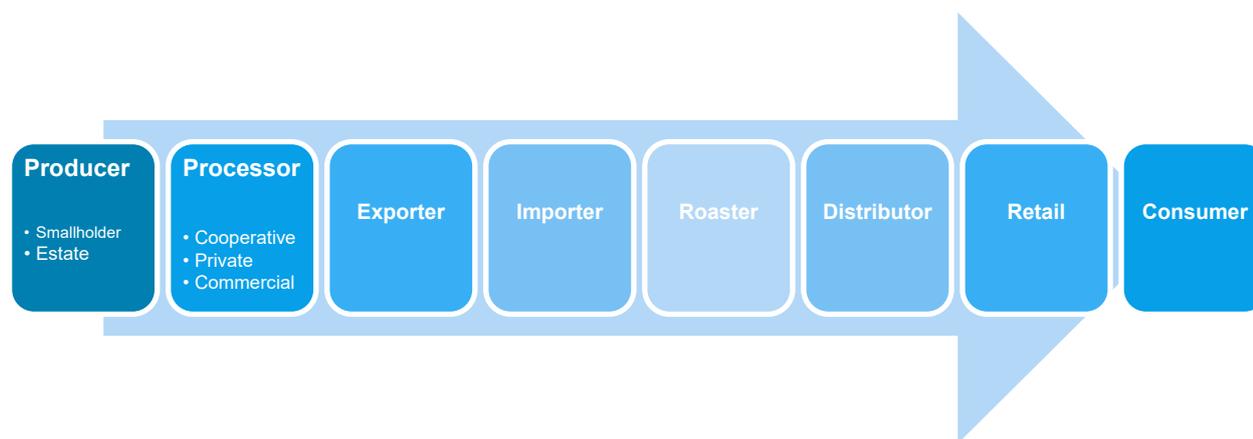
Attribution-NonCommercial-ShareAlike 4.0 International (CC BY-NC-SA) 4.0

Source: Panhuysen, S. and Pierrot, J. (2018). Coffee Barometer 2018.

The coffee value chain: A small share for producers

The coffee value chain is complex, because the beans must undergo multiple stages of processing before they end up in a cappuccino at our favourite coffee shop. From the time it leaves the grower's farm, the coffee will change ownership several times and pass through the hands of many service providers. At origin these will include local buyers, warehouse, exporters, transporters, shipping companies, customs and inspection agents. At the consuming end, the coffee will pass through importers, roasters, wholesalers, distributors and retail outlets before it reaches the consumer.

Figure 4 Coffee value chain



Source: International Trade Centre (ITC).

Unlike runner beans, strawberries or flowers, coffee cannot be simply packed for almost immediate sale and consumption, either domestically or internationally. Once harvested, there are various methods of primary processing¹⁰ that involve removing the outer layers of skin and pulp from the coffee cherry and drying the two beans it contains. Once dry, the outer skin of the bean, known as parchment, is removed mechanically and the beans will be sorted according to various criteria, but chiefly size and density. They may be processed further for export to remove defective beans (due to insects or disease, for example).

At this point, the coffee is ready to be roasted and packed – either ground or as whole bean for onward sale, ultimately, to the final consumer. However, producers roast and sell very little coffee for export. Most is shipped as raw (known in the trade as ‘green’) beans to the consuming countries, where it is roasted, packed, marketed and distributed for sale mainly through supermarkets, coffee shops and, increasingly, various e-commerce platforms.

It is important to understand that the coffee itself represents just a very small percentage of the value of the final product. Despite estimates that 10% of the \$200 billion coffee retail market is retained in the country of export,¹¹ Figure 5 shows that the value of the coffee in one cup, retained in origin, is probably as little as 1%. A study commissioned by the British Coffee Association reveals that the United Kingdom retains 76% of the value of every cup of coffee consumed in the country.¹²

¹⁰ The most common processing methods are water-assisted and wet-processed to produce fully or semi-washed coffee. Dry processing is used for naturals. Mechanical drying is common, but most coffee is sun-dried on raised beds or on drying patios. Recent advances in processing have given rise to coffees that are a combination of processes, such as pulped naturals or honey processed, which produces a washed coffee with a fruitier character.

¹¹ Panhuysen, S. and Pierrot, J., *op. cit.*

¹² Coffee facts from www.britishcoffeeassociation.org

Figure 4 Cost breakdown of a cup of coffee

**FARMERS' SHARE OF YOUR COFFEE CUP:
THEY TYPICALLY EARN A FRACTION OF 1%!**



Source: ITC.

Changing preferences: Specialty coffee has high growth potential

ICO reported in September 2019 that global production for the coffee year 2018/19 amounted to 168.7 million bags, up 3.7% from the previous year, while global consumption rose 2.1% to 164.82 million bags. Excess production is just one reason for the prevailing low prices, with the ICO composite indicator falling just under \$0.98 a pound in September 2019.¹³

A large proportion of production covers the demand for commercial coffee, which is mainly mass-produced, average-quality coffee either for roasted and ground products or instant coffee. Much of this is Robusta coffee. Although specialty coffees comprise just a small percentage of total market volume, this sector has the most growth potential because of changing consumer habits including demand for more beverage variety, a better experience or more ethically sourced products.

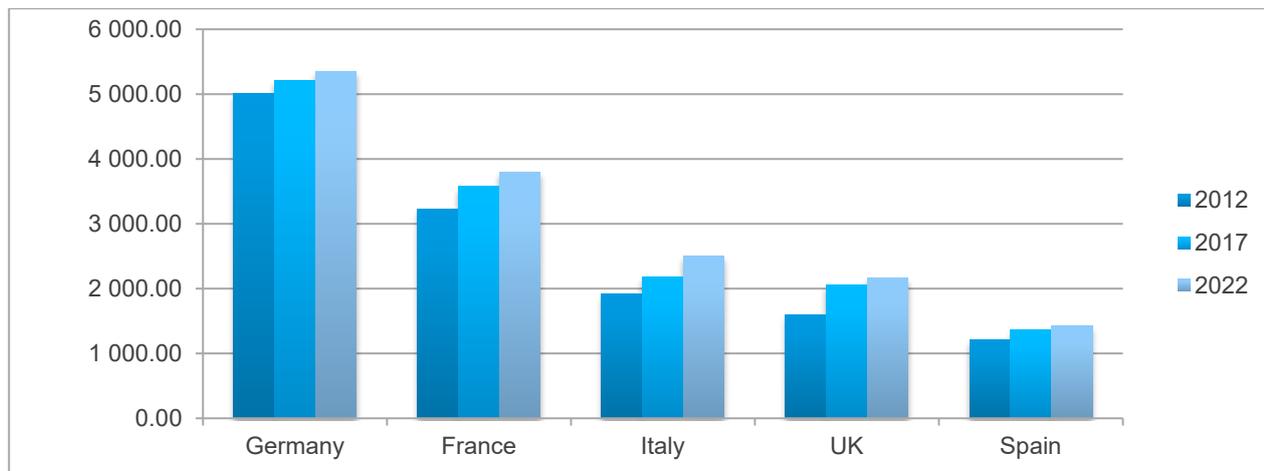
The traditional coffee-drinking markets are described as having reached maturity, and overall growth has declined. The compound annual growth rate in Western Europe, the largest and most mature market in the world, was just 1% in 2012–2017 and a similar level of growth is expected in 2017–2022.¹⁴ The Italian market is predicted to expand the most, driven by the single-serve pod, and the other European markets will register around 1% growth over the period.

Euromonitor forecasts that the value of the coffee market in the United States will grow 2.9% in 2018–2023, though volume will decline 1% over this period. Figure 6 shows the growth of the five biggest coffee markets in the European Union in terms of value in 2012–2022.

¹³ A global benchmark price of major origins and types recorded and published monthly by ICO since 1947. The indicator fell to 97.74 cents in September 2019.

¹⁴ Euromonitor International (March 2018). Passport Hot Drinks: Coffee in Western Europe.

Figure 5 Value of five major European coffee markets



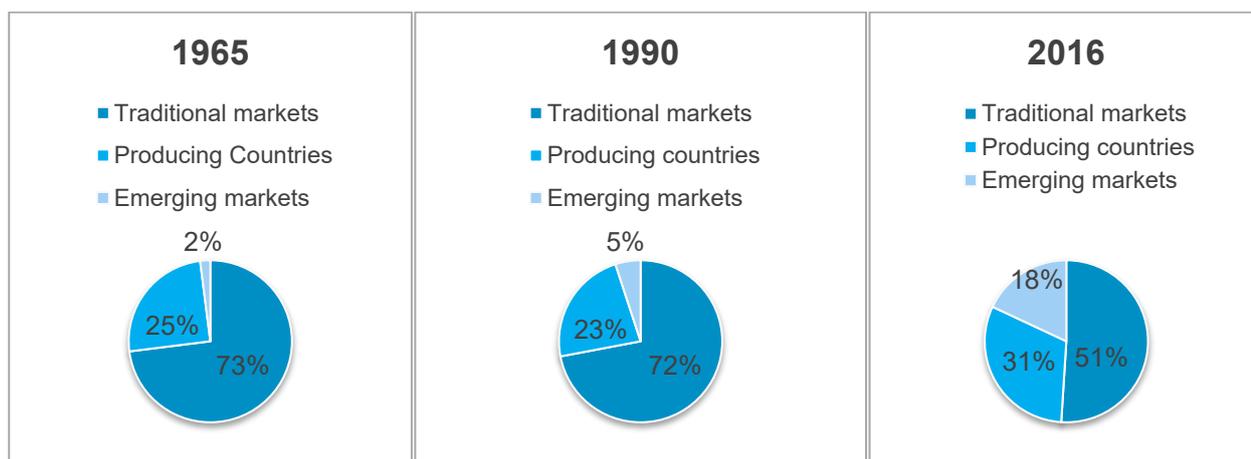
Note: Value is in \$ millions.

Source: Euromonitor, Passport Hot Drinks: Coffee in Western Europe, March 2018.

The value of the global coffee market was estimated at \$200 billion to \$250 billion in 2019.¹⁵ Most growth in 1990–2016 occurred in coffee-producing countries and emerging markets (Figure 7), where expansion has been rapid, although per capita consumption is still low.

China has seen annual increases of 15%. Indonesia is No. 1 in the South Asian market, though much of the growth is in three-in-one products (coffee, sugar, milk mixes). The situation is similar in Viet Nam, where consumption of instant coffee has increased, indicating that convenience is driving growth more than quality.

Figure 6 Growth of global coffee markets, 1965–2016



Source: P&A Marketing.

¹⁵ Sachs, Jeffrey, Cordes Kaitlin Y., Rising, James, Toledano, Perrine, and Maennling, Nicolas (October 2019). 'Ensuring Economic Viability and Sustainability of Coffee Production,' Columbia Center on Sustainable Investment.

Consumption in producing countries starts to generate demand

Coffee consumption has also increased significantly in the producing countries. Brazil has led the way, with a multimillion-dollar campaign that began in the late 1980s to boost domestic consumption. This involved taking coffee into the schools and the countryside, creating another generation of both drinkers and farmers. A marketing campaign took Brazil from a consumption of 6.5 million bags in 1985 to 22 million bags in 2018, with a corresponding per capita rise in consumption from 2.27 kilograms (kg) a year to 6.02 kg a year.¹⁶

Another success story took place in Indonesia, where the two main roasters are each turning over a million 60 kg bags, mainly in the manufacture of three-in-one products.¹⁷ The coffee shop has become the preferred hangout place in this predominantly Muslim country. For the coffee farmer, the biggest benefit of stable domestic consumption is the guarantee of an outlet and reduced exposure to global price volatility.

Global coffee consumption continues to increase steadily, with demand predicted at 300 million bags by 2050.¹⁸ But the industry faces some systemic and ecological threats that must be tackled to ensure that production keeps pace.

Coffee farmers face a variety of challenges

Fluctuating coffee prices

Although international demand rises about 2% a year, most smallholder coffee farmers are fighting for their livelihood and living in poverty. The lack of food security in these communities is accompanied by limited access to healthcare, water, education and basic human needs – all of which are concerns relevant to achieving the 2030 Sustainable Development Goals of the United Nations.

A coffee futures market principally traded on exchanges in New York and London governs world coffee prices. For Arabica coffee, the 'C' market (as it is referred to within the industry) provides price risk management tools for some stakeholders. Contracts are bought and sold, and although delivery of the actual coffee is possible, these are paper trades are chiefly aimed at protecting players against price volatility.

The prevailing prices take into account some fundamental factors, such as crop size, weather phenomena and stocks in consuming countries, and it is two years of production outpacing demand that has led to lower prices. There is also a considerable amount of speculative trading which dramatically influences prices. As price takers, farmers have little protection against unexpected price shocks.

It is thought that 25%–50% of high-cost origins are unable to cover their full production costs.¹⁹ Consequently, there is now a strong industry movement to tackle the price crisis and find ways to delink coffee pricing from the commodity benchmark and protect farmers so they can have a sustainable livelihood.

Coffee stakeholders came together in September 2019 in London during the 125th Session of the International Coffee Council. With farmer prices 32% below their 10-year average in 2019, 22 major private sector stakeholders including roasters, traders and retailers signed the London Declaration, agreeing in the 'spirit of shared responsibility' to find long-term solutions to 'price levels, price volatility and the long-term sustainability of the coffee sector'.²⁰ They pledged to promote sustainable and equitable market growth, increase market transparency and stimulate demand for sustainably produced coffee.

¹⁶ Brazilian Coffee Industry Association statistics, www.abic.com

¹⁷ Industry trade source.

¹⁸ Panhuysen, S. and Pierrot, J., *op. cit.*

¹⁹ ICO, Coffee Development Report, *op. cit.*

²⁰ London Declaration on price levels, price volatility and long-term sustainability of the coffee sector, Private Sector Consultative Board, ICO, 23 September 2019.

In its Coffee Development Report 2019,²¹ ICO proposes a range of measures to address some of the pricing challenges confronting farmers. These include delinking market prices from the futures price in favour of other price-setting mechanisms, such as cost-plus, or income benchmarks, such as the poverty line or living income index.

ICO also promotes better trading practices including forward contracts, long-term commitments and prompt invoice settlement. ICO Executive Director José Sette said in an interview for the November 2019 edition of Coffee & Cocoa International magazine: 'A key message of the report is that the sustainable and inclusive development of the coffee sector requires sector-led cooperation based on shared values and responsibilities and an alignment of actions, funding and schemes through pre-competitive action, public-private partnerships and investment.'²²

The 2019 Specialty Coffee Transaction Guide,²³ which uses data from 57 global specialty coffee businesses including producers, exporters, importers and roasters, aims to give coffee stakeholders alternatives and comparative pricing information. The guide uses data from 38,000 transactions over three crop-year periods (2016–2019) with total volume exceeding 4.7 million 60-kg bags and value topping \$1.4 billion. It reveals a median free-on-board (FOB) price of 2.8 dollars per pound. Further analysis shows that the higher the price, the better the quality. Similarly, the smaller the contract volume, the higher the price.

This is especially true in Kenya, which had the highest median price (\$4.48 per pound), while recording the highest median quality score but one of lowest median lot sizes.²⁴ This underscores that producers can retain more value by separating special lots of high-quality coffees from their average or lower qualities, and that specialty buyers are willing to pay more for smaller, unique and handcrafted microlots (multiple bags of 60 kg up to a few hundred kilograms). At the other end of the quality scale, volumes tend to be larger. Although these coffees still make the specialty category, their pricing is more closely correlated to commodity coffees.

Aside from pricing, coffee growers face several major hurdles that must be resolved if production is to keep up with demand over the next 50 years.

Climate change

Climate change is the biggest single threat to coffee production, with changing weather patterns affecting both crop cycles and volumes. While frost in Brazil was the biggest climatic threat to volumes and prices in the previous century, a lack of rainfall, too much rainfall or unseasonal rainfall patterns are more likely to affect production levels today.²⁵

Many early sustainability programmes and private sector initiatives focused on the economic and social plight of smallholder farmers. More recently, however, responses to climate change and climate mitigation solutions have been central to field-level programmes.

World Coffee Research²⁶ was set up in 2012 to seek ways to drive production development and genetic resilience. Its partners include private companies, government organizations and research bodies. The research stage of coffee genetics aims to create new high-yielding and disease-resistant varieties. The study has now moved on to trials around the world, to determine the most effective – and profitable – new varieties. World Coffee Research warns that 'fewer farmers, less origin diversity – that is the likely future that coffee producers face without significant innovation and investments to support coffee producers ... to remain profitable and continue farming'.²⁷

²¹ ICO, Coffee Development Report, *op. cit.*

²² Coffee & Cocoa International, November 2019, Volume 46, No. 5.

²³ 2019 Specialty Coffee Transaction Guide, Version 2.0, December 2019. See <http://www.transactionguide.coffee> for more information.

²⁴ *Ibid.*: 13.

²⁵ ITC research.

²⁶ www.worldcoffeeresearch.org

²⁷ World Coffee Research, *op. cit.*: 8

Besides seeking ways to boost quality and productivity, climate-change solutions also promote reforestation and shade tree provision.

Ageing farmers

Many coffee farmers are ageing and there is little incentive for younger people to remain on farms. Youth engagement will only succeed if sustainable business models are found to encourage them to stay in the business. There are many initiatives to promote women and youth in coffee production, but most of the focus is on women.

A secondary problem is inadequate capacity at the farmer level. Smallholder farmers lack knowledge about modern farming techniques and good agricultural practices. With ageing trees, soils that lack nutrients, a high risk of insect and disease damage, and poor infrastructure hindering post-harvest processing, farmers face both quality inconsistencies and high production costs.

Urbanization

As populations move towards cities in search of employment, better education, infrastructure, housing and social services, rural populations dwindle and demand for land around the cities rises. Selling coffee land for real estate is often the best financial option. As urbanization swallows coffee-farming land, there is a greater need to look for higher yields from the remaining trees or to find land that has less pressure for other uses.

Access to finance

Most individual smallholder farmers are unable to access microfinance to aid them during the growing and harvesting period. Well-organized, well-managed cooperatives can usually obtain money from either licensed lending institutions or industry partners against warehouse receipts or forward contracts. Farmers are generally cash poor, however, totally lacking in the wherewithal to break the vicious circle of low productivity and low returns.

Some financial assistance, such as the recent IDH Sustainable Trade Initiative named Farmfit Fund,²⁸ has been made available to farmers. With largely Dutch industry support, this initiative seeks to show that smallholder funding is possible, making €100 million available with a Rabobank/United States Agency for International Development guarantee facility. This is one of only a handful of attempts at farmer financing, with all its inherent risks.

In 2019, economist Jeffrey Sachs²⁹ proposed the creation of a multibillion-dollar industry fund to tackle some immediate low-price issues. He suggested a pre-competitive funding initiative³⁰ that would support newly developed national coffee sustainability plans and country coffee platforms to be set up in producing countries. Sachs said \$10 billion was needed annually for any meaningful impact in creating a sustainable future for coffee production and a better standard of living for farmers.

Lack of value addition retention

As mentioned earlier, farmers are often price takers, unable to dictate when and at what price they sell their coffee. Very little coffee is sold as roasted coffee – less than 0.5% is exported as a finished roasted and ground product.³¹ Although some producing countries have a healthy domestic market, many (e.g. Brazil and Colombia) have required high-level government intervention to promote local coffee drinking.

²⁸ <https://idhsustainabletrade.com/farmfit-fund/>

²⁹ Sachs et al., *op cit*.

³⁰ A type of funding available across the industry, to the benefit all

³¹ ICO statistics.

CHAPTER 2 SPECIALTY COFFEE MARKET

The label 'specialty coffee' is used to describe a product that differentiates itself. It sets itself apart from other products in the marketplace, generally referred to as the commercial sector (comprising average-quality roast, ground blends and instant coffee). Over the past 20 years, small independent roasters and coffee shops or chains of coffee shops have sprung up across the globe, known as the third wave, following the trend set by Starbucks, the market pioneer and leader of the second wave.

There are premium coffee shop chains all over the world today, and this trend is continuing. Some 34.5 million people visited at least one of Costa Coffee's 2,422 outlets in the United Kingdom in 2018. In the emerging Chinese coffee market, Luckin Coffee (established in 2017) has already opened 4,500 stores.³²

The specialty sector has grown over the past 40 years to include a range of products and qualities. These range from popular espresso-based drinks, single-origin products, sustainably produced coffees, and Fairtrade and organic coffees to the more recent introduction of single-serve capsules or pods and cold or nitro brews.

From a quality perspective, specialty coffee must score at least 80 points out of 100, judged on characteristics and a scoring mechanism popularized by the Coffee Quality Institute and Specialty Coffee Association of America.³³ The definition of the specialty market is qualitative, but it is thought not to exceed 5%–10% of the global coffee market.³⁴

The sector is just starting to invest in sustainability

Many business model drivers are based not only on coffee quality, but also on some form of direct trade, sustainability and farmer partnerships. Early sustainability efforts, introduced via different certification and verification standards, were known as voluntary sustainability standards. They were the first steps in the mainstream and specialty sectors of the industry to see improvements in social, economic and environmental conditions at farmer and origin level.

The major standard bodies – 4C, Fairtrade, Rainforest and UTZ – sought to set and improve baseline standards. Roasters signed up to the standard that best suited their values and markets. Some adopted their own proprietary standard, as in the case of Starbucks Café Practices and Nespresso's AAA Programme.

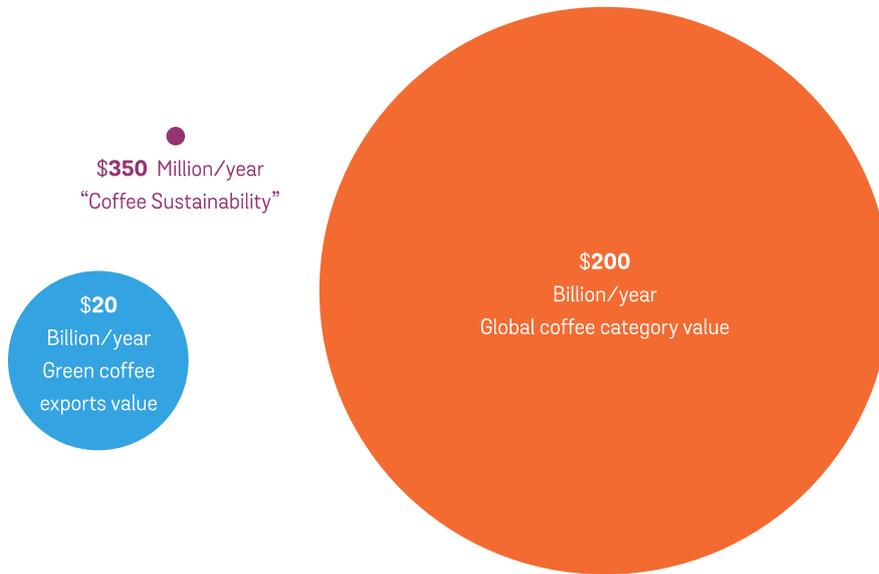
Over the past 20 years, huge investments and commitments have been made to ensure sustainability. Yet inequality along the value chain persists, as illustrated in Figure 8.

³² www.statista.com

³³ <https://sca.coffee/research/protocols-best-practices>

³⁴ ITC source.

Figure 7 Coffee sustainability – a drop in the ocean?



Source: Coffee Barometer.

Specialty coffees are positioned on stories and values tied to their origins

Specialty coffee is differentiated from commercial coffee primarily on quality. But associated values linked to their origin and the culture of coffee growing also play a role. Akin to the wine trade concept of ‘terroir’ single origin, the estate or factory/washing station is often sold by name or geographical location. It may undergo special primary processing, e.g. honey-processed coffee.³⁵

More often than not, this coffee will be taken to the marketplace after extensive visits to the producing countries, with buyers sometimes assisting with the growing or harvesting of the coffee they will buy. Unlike much of the world’s coffee, which is traded as a commodity, often as part of a long-term supply agreement between an exporter/trader and an importer/roaster, specialty coffee is typically sourced through close farmer/buyer relationships with transparency and traceability of pricing. Buyers of specialty coffees are often able to support their business model by investing in infrastructure or social projects to benefit the whole community.

The marketing and promotion of this coffee hinges on the storytelling and the experience. This is a key area of opportunity for producers to ensure that they remain differentiated, by finding a niche space and delivering a high-quality and distinctive product.

Most major international trading houses recognize the need to have a company that is focused exclusively on specialty coffee, moving away from large-volume, small-margin business to a small microlot, highly curated business with a corresponding high margin. To this end, the Neumann Group has InterAmerican Coffee (www.interamericancoffee.com), Sucafina has 32Cup (www.32cup.com) and Volcafe has Volcafe Specialty (www.volcafespecialty.com),

³⁵ This is a process in which the skin and pulp are removed, but the coffee is dried with mucilage remaining, resulting in a sweeter and heavier-bodied coffee. Different types of honey process (yellow, red, black) are so named according to the amount of mucilage remaining as well as the amount of light and heat during drying.

Higher value chain models for green and roasted specialty coffee

Direct trade

The term 'direct trade' is used when buyers are in direct contact with the source of their product. Such an arrangement is usually aimed at eliminating the middlemen from the value chain at the point of source. However, while some countries are fully liberalized when it comes to the coffee trade, there is considerable government regulation and oversight in others. From an economy-of-scale perspective, the small volumes involved per farmer/farmer group or roaster often necessitate some involvement of exporters and importers at both ends of the chain.

Coffee auctions

Kenya, Tanzania and Ethiopia are the only East African countries that sell coffee at auction or via a national commodity exchange. This form of selling dominates the marketplace in these countries, where regional auctions or sales are held daily or weekly to attract the best price. Industry experts say this is the best price discovery mechanism, as buyers from around the globe are represented by their local agents or exporters and auctions depend heavily on supply and demand on the day of sale.

Buyers say these systems need greater transparency and traceability. Coffee farmers tend to view auctions with suspicion and often accuse the system of falling victim to cartels and price collusion.

Some specialise auctions have been developed to show coffees to the world. Examples include Cup of Excellence and Best of Panama. Although these events can attract serious buyers and coffee can sell for extremely high prices, the point of such auctions is to sell very small amounts of high-quality coffee for the purpose of promoting and marketing a particular single-estate/cooperative coffee or a single-origin coffee.

Contract farming

Contract farming is a model where long-term contracts are in place for farmers to produce fixed volumes at a price that is pre-determined or periodically reviewed or set. This requires a direct relationship between the buyer and seller, with contract terms that will cover volumes, quality and frequency of delivery. This type of arrangement is typically for larger volumes – that is, container loads of consistent quality replicated year after year – rather than highly differentiated, small-lot coffees. Contract farming is not common in East Africa.

E-commerce platforms

Over the past few years, e-commerce has become mainstream. This presents a new opportunity for coffee farmers to extract more revenue from the value chain, as it provides an avenue for more direct contact with both roasters and consumers. Green coffee is marketed through industry sites such as Cropster (www.cropster.com) and Algrano (www.algrano.com), and farmers can offer coffee for shipment from origin just as easily as importing companies can post their inventory for sale.

The most popular major e-commerce platforms, such as Amazon and eBay, can be an option for roasted coffee. Online grocery shopping sites also provide a marketplace for roasted coffee. With more and more business being conducted online, there is a good argument for producers to have their own website, which gives them control of the content and intellectual property as well as direct contact with their buyers.

CHAPTER 3 EAST AFRICAN COFFEE MARKET

Since coffee was discovered in Africa, the continent has a long history and affinity to the product. Yet today, it accounts for less than 10% of global production in terms of both volume and value.³⁶ African coffee producers have seen their crops stagnate or dwindle, in some cases to almost nothing, as Table 1 illustrates.

Meanwhile, the world's three largest producers account for 65% of global production, with Brazil doubling its production since 1990 and Viet Nam growing from practically nothing to the world's No. 2 in the same period.

Table 1 Coffee production 1990–2018: Today's top 3 versus East African origins

| Origin | 1990/1991 crop year 60 kg bags | 2017/2018 crop year 60 kg bags |
|------------------------------------|-----------------------------------|-----------------------------------|
| Brazil | 29,090,000 | 60,000,000 |
| Colombia | 14,268,000 | 14,000,000 |
| Viet Nam | 1,310,000 | 29,500,000 |
| Ethiopia | 2,909,000 | 7,650,000 |
| Uganda | 1,955,000 | 5,100,000 |
| Kenya | 1,485,000 | 790,000 |
| United Republic of Tanzania | 932,000 | 750,000 |
| Rwanda | 535,000 | 245,000 |
| Burundi | 487,000 | 200,000 |

Source: ICO statistics.

Challenges of productivity and profitability in East Africa

High production costs in the region have led to generally higher prices for East African coffees. With the ongoing consolidation of coffee roasters and retailers at the consuming end of the value chain, buyers are seeking alternative origin coffees to reduce their production costs and remain competitive. Sudden changes in regulation, poor infrastructure and slow transit times have all damaged the reputation of these origins of production.

When commodity prices are low, the underperforming origins suffer the most. The saving grace for much of East African production is its quality, differentiation factor or story, will be discussed later for each individual origin.

Nonetheless, many problems have prevented serious production growth over the last 30 years. Small crops, due mainly to poor yields, urbanization, climate change, dwindling farmer numbers, poor infrastructure and highly regulated industries, threaten to marginalize Africa even further, with just two countries – Ethiopia and Uganda – producing more than 85% of the region's coffee.³⁷ Many international buyers have reduced their reliance on one or more of these coffees, usually because they became too expensive. An example of this is Kenya: many large commercial roasters have all but stopped using Kenyan coffee in favour of cheaper alternatives that have been accepted, over time, by their consumers.

In a recent presentation, Brazilian coffee consultancy P&A Marketing compared the cost of production and profitability in Brazil and Colombia with Kenya (Table 2). Although coffee from these two origins cannot be compared with Kenyan coffee in terms of quality, it is clear that Brazilian farmers can survive and return a

³⁶ ICO statistics.

³⁷ *Ibid.*

healthy profit, even faced with prices at 12-year lows. This is due to high yields, low production costs, larger landholding and higher percentage retention of the FOB value.

In the case of Kenya, where the average sales price of its benchmark coffee is more than double that of all the Brazilian examples, high production costs, low yields, a lower percentage of FOB price and small farms all amount to poor profitability for the farmer. These are the same reasons that Kenyan farmers are only fractionally better off than Colombian farmers in terms of the monthly profit per grower.

Table 2 Monthly profitability per mid-size grower

| Origin | Price \$/lb | Cost \$/lb | Yield bags/ha | Gross profit \$/ha/year | Farm gate/FOB % | Average landholding ha | Profit per grower \$/month |
|------------------------|----------------|---------------|------------------|----------------------------|-----------------------|------------------------------|----------------------------------|
| Brazil Fine Cup | 0.84 | 0.75 | 25 | 628 | 85 | 7 | 445 |
| Brazil Good Cup | 0.81 | 0.70 | 25 | 562 | 85 | 7 | 398 |
| Kenya | 2.25 | 1.00 | 5 | 893 | 50 | 0.5 | 37 |
| Colombia | 1.15 | 1.00 | 15 | 179 | 85 | 1.5 | 32 |

Note: This table uses the following abbreviations: pound (lb) and hectare (ha).

Source: P&A Marketing.

To differentiate, farmers have turned to certification and verification and worked to develop stronger relationships with their buyers to ensure their market. Although the North America market favours origins that are closer geographically, the European market prefers many African coffees, chiefly due to the historical relationship between the two continents.

Ethiopia, considered the birthplace of coffee, consumes half of its production and traditional coffee culture remains strong. Tea, introduced by European settlers, is the drink of preference for most of the region. Establishing homegrown domestic demand and a strong local coffee culture will require major national promotional campaigns.

‘Premiumization’ of African coffee

All East African origins sell part of their coffee as specialty, because of its intrinsic high quality. While a greater proportion of the fully washed and bolder bean coffees from Ethiopia, Kenya and Rwanda fit into this category, some Arabica coffees from Uganda, the United Republic of Tanzania and Burundi can also command huge premiums over the prevailing benchmark indicator prices.

The ‘premiumization’ of much of African coffee is highlighted in the 2019 Specialty Coffee Transaction Guide, which puts the median FOB price at \$3.23/pound (lb), far above the 2018 average ICO composite indicator benchmark price of \$1.09/lb.³⁸

³⁸ *Ibid.*

Country-by-country overview

Ethiopia

Ethiopia is the largest producer in East Africa, with total volume of more than 7.5 million bags split between washed and unwashed Arabica. Many coffee buyers around the world identify fully washed Ethiopian coffee as their favourite.

The main producing areas are Yirgachefe, Sidama, Limu and Harrar, which grow all the highest-quality, competition-winning coffees with 'intense floral aromatics and citrus fruit quality', according to Klaus Thomsen, co-founder and partner at the Coffee Collective in Copenhagen.

Ethiopian coffee farmers are among the poorest in the world. Coffee is sold mainly through a commodity exchange active on a daily basis in the capital, Addis Ababa.

This has always been an open outcry trading platform, attended by local Ethiopian exporters who bought coffee after inspecting samples, in highly regulated and price-controlled conditions. They would then prepare the coffee for export and sell to international trading companies and roasters who often had representative offices in Addis Ababa to oversee the adherence to quality and performance of their chosen exporter.

The Ethiopian Coffee Exchange was set up in 2008 to streamline the process, but it removed transparency and sustainability, which were rapidly becoming the backbone of coffee purchasing requirements. Although cooperatives were still able to sell their coffee directly, much of the production lost its identity and fell back into the 'commodity' category. Some modifications have been made to the system since 2017 to allow for traceability. Certification and sustainable production are on the rise, with some farmers now able to participate successfully in direct trade agreements.

Kenya

Kenya is the other country in the region that provides buyers with their favourite coffees. These coffees, primarily grown in the foothills of Mount Kenya, are world renowned for their sweetness, bright acidity, and blackberry and citric flavours. At the height of production in 1987/88, Kenya achieved a crop of over 120,000 tons of green coffee, but production has since decreased to 40,000 tons in 2018/19.³⁹

This is mainly due to the underperformance of the cooperative sector, which accounts for about 65% of total volume. Cooperative societies in Kenya are often poorly managed, lacking both technical and business capacity. Some are also prone to corruption, to the extent that the Cooperative Ministry carried out a nationwide audit in 2018 to assess the financial viability of coffee cooperatives.

Coffee can be sold in two ways in Kenya. One way is through the national auction platform, the Nairobi Coffee Exchange, whereby sellers provide samples in advance so local exporters can assess quality and then buy at the weekly auction. The other way is for farmers to sell coffee directly to overseas buyers – a system that was set up to cut out the middleman and obtain higher prices for farmers.

Despite the many challenges to the sector, Kenyan coffee is in high demand among roasters. They use it as both a single-origin offering and as a blender to add to coffees from other origins that might be considerably less expensive, but lack adequate quality.

United Republic of Tanzania

The United Republic of Tanzania has four main producing areas: in the north around Mount Kilimanjaro, near the northern towns of Arusha and Moshi, in the two Southern Highland areas of Mbinga and Mbeya, and in the Bukoba and Kagera areas bordering Lake Victoria, which produce mainly Robusta coffee.

³⁹ *Ibid.*

There have been many upheavals in the Tanzanian coffee industry over the past 30 years, but none as severe as in 2019, when the whole system to sell coffee was altered to allow for regional auctions. This change means that instead of one centralized weekly auction, multiple auctions take place every week. The change created serious problems for exporting companies, which had to change their modus operandi almost overnight.

ICO classifies Tanzanian coffee as an 'other mild'. In many ways, it is quite similar to coffee from Colombia and other South American countries against which it is benchmarked and for which it is sometimes used as a substitute (as was the case in 2010, when poor weather adversely affected the size of the Colombian crop). Tanzanian coffee is also a favourite of Japan; it's one of four main origins, along with Brazil, Colombia and Ethiopia.

Many industry experts say Tanzanian coffee used to be the best in the region. However, radical regime changes, corruption, mismanagement and the demise of the cooperative system have all contributed to quality deterioration. This has only been addressed in the past 10 years, with private/public cooperation to address poor agricultural practices and a national programme to introduce better-yielding varieties as well as replanting and new planting.

One of the changes made by the current Government of President John Magafuli was to channel all coffee through existing and/or newly formed cooperative societies and farmer groups. Although this has sidelined the larger local operators, which had been buying coffee cherry and parchment⁴⁰ since the industry was liberalized, this decision was designed to enable farmers to retain more of the value of their crop. Changing the system to rebuild cooperatives was expected to allow for better economies of scale, and training and capacity building for farmers. The biggest challenge to this has been the cooperatives' limited access to finance and the resulting lack of liquidity in the market.

Rwanda

The Rwandan coffee industry, practically wiped out during the civil war in the early 1990s, became the focus of international development agencies as of 2000. Business development has occurred rapidly, in large part due to the priority accorded the sector under the Government of President Paul Kagame, and production of fully washed coffee has risen to 50% of volume over the past 20 years.⁴¹

Rwandan coffee faces a serious quality problem that has also been the focus of much international attention: the emergence of a strong potato flavour. This has prevented Rwandan coffee from becoming mainstream, as many roasters avoid the origin because of the higher risk of defective coffee.⁴²

Nonetheless, Rwandan coffee is a staple for specialty third wave and bigger commercial roasters. It is also the regional 'darling' of both private and development sector when it comes to implementing coffee improvement programmes. Many coffee farmers in Rwanda are women, and here more than anywhere else in the region, one can find a proliferation of women's groups producing coffee.

Uganda

Uganda is the second-largest producer in the region, with more than 1.5 million smallholder families dependent on coffee for their livelihoods.⁴³ Most of Ugandan production is Robusta, due to generally lower altitudes, but there is also a belt of high-quality Arabica from the Bugisu and Mount Elgon regions.

⁴⁰ Cherry refers to the harvested coffee. Parchment is the naturally occurring, papery substance that surrounds the coffee bean.

⁴¹ C. Dormans Rwanda production statistics.

⁴² It is thought that this defective cup quality is caused by the Antestia insect that attacks and feeds on coffee plants.

⁴³ Uganda Coffee Development Authority statistics.

Ugandan coffee is channelled through middlemen and exporters who buy the coffee directly from the farmers for cash, using a network of buying stations and aggregators dotted around the countryside, and who take it to their premises for processing or sell it to the larger exporting companies based in and around Kampala.

The Uganda Coffee Development Authority was created in 1991 to oversee and regulate the industry and to promote the country's coffee overseas. A new National Coffee Policy that says 'value addition shall be pursued at all levels of the value chain for the benefit of all stakeholders' came into effect in 2012.⁴⁴ This bold programme, managed by the authority, aims for the country to produce 20 million bags a year by 2030 by improving yields threefold to fourfold, expanding the amount of land farmed for coffee by 20%, empowering farmers and providing service and delivery.⁴⁵

In addition to field extension programmes and coffee research, a promotional campaign targeted increased domestic consumption. This new policy gave the Ugandan coffee industry the boost it needed: production exceeded five million bags in 2017/18 and domestic consumption accounted for almost 245,000 60 kg bags.⁴⁶

Burundi

Burundi has suffered many years of political and civil turbulence. From the early 2000s, however, the Burundi coffee industry has made some progress in re-establishing itself as a differentiated coffee origin. Annual production is around 200,000 bags, of which 70% is fully washed and passes through one of around 200 washing stations mainly in the north and north-east of the country.⁴⁷

In 2008, the Government exited its state-run enterprise and created the Regulatory Authority of the Coffee Sector and Intercafe Burundi, a privatized body that was to be responsible for providing extension services and promoting and branding Burundi coffee. Although agriculture in Burundi accounts for 60% of export earnings, 90% is subsistence farming and the country is still relatively underdeveloped, especially compared to its neighbour Rwanda.⁴⁸ There are roughly 600,000 coffee farmers and the average smallholdings have 250–300 trees, mainly of the Bourbon variety.

Burundi coffee can also suffer from potato taste defect. However, much of the production ends up being small lot size because yields are low, so this coffee, which 20 years ago was shipped in bulk and used in value blends, has become increasingly popular among third wave buyers looking for 'weighty florals and dense fruit with great elegance'⁴⁹ in the cup.

⁴⁴ For more information, see www.ugandacoffee.go.ug

⁴⁵ *Ibid.*

⁴⁶ *Ibid.*

⁴⁷ www.cafeimports.com and www.nordicapproach.no

⁴⁸ *Ibid.*

⁴⁹ www.nordicapproach.no

CHAPTER 4 BUSINESS MODELS FOR FUTURE SUCCESS

Direct trade models – green coffee

The new generation of sustainable business models focuses on buying coffee through the most direct trade route possible. Buyers want to know their suppliers and be able to tell a unique story – whether the coffee is from a single farmer or cooperative, a group of cooperatives, a women’s group or a particular voluntary sustainability standard certification. In the best cases, the final product will be branded as a single-origin coffee (including the name of the farmer and the farm), providing the farmer with good international visibility.

In this model, often called ‘relationship coffee’ in specialty trade circles, buyers and producers work together to establish a long-term trading partnership that may be exclusive or semi-exclusive. The trading process is transparent; farmers gain bargaining power through knowledge and receive a fair price for their green coffee that is not vulnerable to commodity market fluctuations.

The buyer usually invests in the farming business, typically by providing funds for the purchase or rehabilitation of capital assets or capacity-building training. Buyers may also support the community by sponsoring social projects – for example, improving school facilities or providing running water.

This relationship benefits both parties, but especially the farmer, who gets a quick return on investment. For such a relationship to succeed, the farmer must respect timeliness, logistics, transport and distribution – all essential to maintain supplier reputation and customer loyalty.

‘Scaling up this model may both increase overall value and shift more of that value to producers,’ according to ‘The powerful role of intangibles in the coffee value chain’.⁵⁰ ‘This can provide significant opportunities for farmer-owned brands and geographical indications to conquer new segments and create a measure of consumer-level recognition for notable origins and farmers, enhancing prospects for upstream actors to capture consumer loyalty and appropriate value.’

Buyers are eager to differentiate themselves from mainstream coffees by being ‘origin-specific’. They look for the highest quality of coffee at a fair, and often significant, premium price. This is why AA grade coffees in Kenya fetched \$12-\$14 per kilogram in 2019, more than double the prevailing auction average of \$5.10 per kg.⁵¹

E-commerce models – e-auctions and online sales

Both green and roasted coffee can be marketed and sold via online platforms. Coffee trading, importing and roasting companies must have an informative, interactive and up-to-date website through which they can channel sales activity and provide all essential information about the coffees they are offering.

Farmers who want to sell their coffee online would need to have access to technology as well as good marketing and social media skills.

Online sales of green coffee

Green coffee, whether in microlots or container loads, is sold on the basis of spot destination or FOB origin with a known forward delivery date. Specialty green coffee importers, including Café Imports, Nordic Approach and Crop to Cup, market most of their coffees via their own websites and social media feeds.

⁵⁰ Samper Luis F., Giovannucci, Daniele, and Luciana Marques Vieira (2017). The powerful role of intangibles in the coffee value chain. Economic Research Working Paper No. 39, p. 4.

⁵¹ ITC research and Nairobi Coffee Exchange statistics.

There are also 'communal' platforms such as Cropster (<http://cropster.com>) and the Korean C2C platform (<http://c2cplatform.com>) that carry a 'catalogue' of coffees for sale.

E-auctions for green coffee

Green coffee auctions, introduced more than 20 years ago, have been used extensively – both commercially and as a marketing tool to draw attention to individual origins, regions or even single estates.

When the world-renowned Cup of Excellence, organized by the Alliance for Coffee Excellence, held its first competition and auction in 1999 in Brazil, the highest bid was \$2.60/lb.⁵² At the Brazilian Cup of Excellence winners' auction in November 2019, the top bid reached \$60.10/lb for a lot of yellow⁵³ natural coffee. Such high prices are a function of the uniqueness of the variety and the labour-intensive bean-processing technique, which together result in higher quality and consequently a higher cupping score.

Online sales of roasted coffee

Selling to importers, roasters or even end-consumers has never been easier than it is today, thanks to ever-evolving e-commerce platforms. E-commerce is central to many government trade discussions and bilateral agreements are being signed to strengthen this trading route. Rwanda is a member of the Electronic World Trade Platform, run by the Chinese group Alibaba. Under this programme, three Rwandan coffee brands (Gorilla's, West Hills and 1000 Hills) have been exported to China and are listed on the domestic Tmall platform, owned by Alibaba.

The challenge for producers is to have a highly visible website or listing that attracts more than a token amount of sales. The costs of development, ongoing site management and regular linked social media feeds will need to be part of any business plan. The alternative is to use a global e-commerce sales platform such as Amazon, eBay or Alibaba, where products are categorized and then reviewed and rated by customers. Technical investment to ensure that the website or product heads the search engine listings will also be key.

Farmers can access online sales models easily, but they will need support and local market knowledge for current and targeted marketing. Careful attention must also be paid to logistics, to contain costs and reduce the risk of non-competitiveness. E-commerce orders for roasted coffee are often small and need to be sent by airfreight or courier. Both are expensive ways to move goods, and shipping can exceed the value of the product.

There have been some initiatives to reduce transport costs, such as the SheTrades market linkage programme (www.SheTrades.com), an ITC initiative to empower three million women entrepreneurs by 2021. SheTrades is active in East Africa, where an agreement was reached with DHL to discount the costs of sending goods overseas.

The alternative would be to hold inventory in the consuming country. Larger shipments could then be considered to reduce transportation costs, but this would add new management complexities and risks. A local partner would be required to manage inventory and stock rotation.

Wholesalers usually carry a large range of products and work on a consignment basis. Although it is in their interest to turn over their stocks quickly to earn their commission, the onus on marketing and promotion, as well as the payment risk, remain with the seller or the seller's representative. Typically, wholesalers and distribution companies will earn a 15%–30% commission on the sales value of the product.⁵⁴

Subscription coffee has become popular in consuming countries, with roasters offering a weekly or monthly selection that introduces both choice and variety. Companies such as Pact Coffee in the United Kingdom

⁵² Alliance for Coffee Excellence statistics.

⁵³ Yellow coffee results from a distinctive drying process in which the beans are partially washed. For more details, see <https://www.perfectdailygrind.com/2017/02/yellow-red-black-honey-processed-coffees-whats-difference/>

⁵⁴ Industry sources.

and Trade Coffee in the United States provide such services. Pact offers 13 coffees from at least eight origins and says on its website that every farmer gets 25%-125% more than the Fairtrade base price, as well as 'training and investment'.⁵⁵

This sales model makes it easier for producers to manage the regular dispatch of pre-ordered amounts and allows for product rotation to retain buyer interest. However, Klaus Thomsen of the Coffee Collective fears that buyers may be tempted to rotate not only the coffee, but also the supplier, so they can sample a greater variety of coffees.

Value addition model 1 – selling roasted coffee locally and in coffee shops

One way to capture higher value for coffee is to roast and sell it locally, in the country of origin.

Domestic consumption in producing countries has grown slowly and has proven difficult to develop. However, the rapid growth of a middle class and a millennial generation that has the disposable income to spend on more consumer goods provides a well-timed opportunity to add value.

Most growth in the number of coffee shops is likely in developing countries, where they are still seen as a status symbol, according to Euromonitor. Several producing countries have reduced their reliance on the green coffee export price by creating or expanding their internal markets. Colombia's highly successful Toma Café campaign reversed a negative trend of several decades and spurred a 36% increase in domestic consumption over 2009–2016.⁵⁶

As mentioned in Chapter 3, Ethiopia is the only producing country that consumes a significant part of its own coffee. Kenya and Uganda, on the other hand, have a traditional tea-drinking culture. Changing taste preferences will require a generational solution.

To sustain these successes, a well-structured national strategy is required, as well as government support and investment in marketing and promotion. With large numbers of farmers involved in coffee production (1.7 million in Uganda and 500,000 in Kenya), national campaigns to 'drink your own grown coffee' could go a long way to kickstart domestic consumption. Indeed, it is alarming that many farmers have never tasted their own coffee and know little about what happens to their coffee after it leaves their farms.

Companies such as Vava Coffee (www.vavacoffeeinc.com) run programmes to educate coffee farmers. This social enterprise aims to link Kenyan farmers and sellers, bringing the two ends of the value chain together, building relationships, training farmers and teaching them to taste coffee. Through its Gente Del Futuro (people of the future) programme,⁵⁷ run by organizations in the United Republic of Tanzania, Kenya, Colombia and the United States, Vava Coffee aim to empower youth people to be involved in coffee in a profitable and sustainable way. When raising funds for Gente Del Futuro,⁵⁸ Vava Coffee said:

Through a more inclusive and equitable purchasing model, and extensive practical training programme geared towards the younger generation, we hope to not only improve incomes for producers while establishing a scalable and sustainable premium coffee business training programme, but create wider impact by generating a new generation of leaders within the coffee sector who have hands-on expertise to steer change and create more job opportunities within these coffee communities.

Overcapacity is a serious problem at roasting facilities in most East African countries, even though the number of local roasters is growing. This means that start-up roasters should be able to provide toll-roasting services⁵⁹ for reasonable prices. In Kenya, the most sophisticated market in the region, many companies

⁵⁵ <https://www.pactcoffee.com>

⁵⁶ <http://www.ico.org/documents/cy2014-15/Presentations/115-council-colombia-toma-cafe.pdf>

⁵⁷ <https://www.baristamagazine.com/gente-del-futuro/>

⁵⁸ <https://ifundwomen.com/projects/gente-del-futuro>

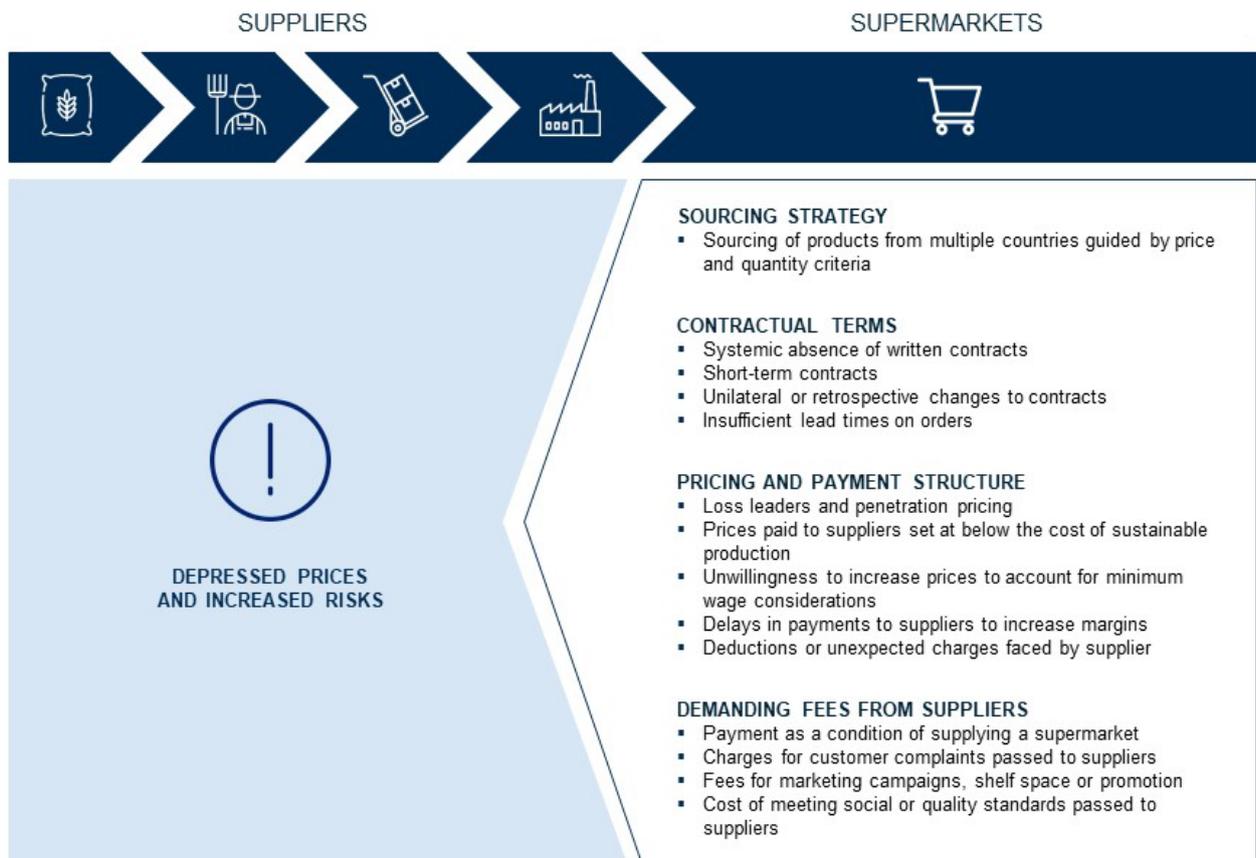
⁵⁹ The process of custom-roasting green coffee beans and then packaging them to specific specifications.

could provide these professional toll-roasting services – C. Dormans Coffee, African Coffee Roasters and Kenya Coffee Cooperative, to name just a few.

Value addition model 2 – selling roasted coffee from origin

Selling roasted coffee directly from the origin into export markets is another way to increase value capture, though it is more demanding. The following illustration clearly shows a ‘David and Goliath’ scenario, but it identifies many of the factors that farmers must consider to successfully launch a product in a foreign supermarket. Indeed, targeting specialty coffee distributors and small coffee shops might be more effective than trying to gain sell to larger grocery stores or supermarket chains.

Figure 9 The vast power of supermarkets



Source: Oxfam.

Andrew Rugasira provides many insights into the complexity and difficulties of exporting his Ugandan brand, Good African roasted coffee, in his book, *A Good African Story: How a Small Company Built a Global Coffee Brand*.⁶⁰ He cites barriers to trade in Africa from ‘the poor state of infrastructure and the high logistical costs of getting goods across the continent and overseas’⁶¹ to ‘accessing affordable and patient capital’.⁶²

⁶⁰ Rugasira, Andrew (2013). *A Good African Story: How a Small Company Built a Global Coffee Brand*. Published by Vintage in 2014. This book is an inspiring, if cautionary, story. For anyone aspiring to enter the roasted coffee business, it is a worthy read that clearly defines the challenges as well as the efforts and patience required to establish a brand overseas.

⁶¹ *Ibid.*: 59.

⁶² *Ibid.*: 111.

Rugasira, a champion of 'trade, not aid', describes problems finding distributors willing to take on goods that are not yet well known in the marketplace. He also stresses the need for support and says 'social and commercial networks' are critical to help forge trade links and gain access to new markets.

From small beginnings in the early 2000s, Rugasira had successfully rebranded as Good African and launched in Waitrose supermarkets in the United Kingdom by June 2005. A year later, his products could be found in 200 branches of Sainsburys. Before the Kampala-based roasting and packing plant was established in 2009, Good African coffee that was destined for the British market was roasted and packed in Ireland. This eliminated many of the concerns that the supermarket chains had about 'poor quality, lack of consistency [and] reliability issues with supply'⁶³ that made them reluctant to take African imports.

Difficulties with cash flow and access to capital impeded his progress. The strong brand presence of Good African masked an 'internal fragility' where Rugasira continually struggled to service and refinance loans. Initially, his sales revenue amounted to just half of what his farmer field operations and outreach cost. It has proven difficult to find information about his business today. Good African coffee cannot be easily found on overseas supermarket shelves, though it is still sold in the rapidly expanding Ugandan market.

This value addition model is challenging in terms of timely logistics and delivery – both from a cost perspective and due to the (often poor) infrastructure and efficiency in the origin country. Manufacturing and export/import regulations are strict, particularly in relation to health and safety compliance.

East African manufacturing facilities would benefit from conforming to certain globally accepted production standards, such as International Organization for Standardization and Hazard Analysis and Critical Control Points. Some of the established and more sophisticated roasting plants in the region have already achieved these manufacturing standards.

Considerable research, a sound business plan and, most importantly, adequate capital funding are essential to sell roasted coffee successfully in the international marketplace. Farmers would likely struggle to understand the local market well – not only consumer coffee preferences, but what packaging would appeal and where the goods should be placed for maximum retail impact.

Finding an overseas partner could be the key for this business model to be successful and sustainable, as will be shown through our case study of Angelique's Finest of Rwanda in Chapter 5. The farm end of the value chain handles the product and pays costs to the point of FOB, and the importing arm of the partnership then takes over title and the responsibility for importation, distribution, promotion and sales.

While it could be argued that having a partner means the farmer loses potential increased revenue from the value chain, it has the benefit of reducing the risks, finance costs and longer wait for a return on investment. As the coffee moves down the chain to the final consumer, the farmer can concentrate on growing the next crop, leaving the partner to manage the onward sales. The partner would also manage in-country inventory and branding and handle after-sales service, customer complaints and product replacement when required. This would protect the reputation of and loyalty to the product in the marketplace.

⁶³ *Ibid.*: 103.

Value addition model 3 – selling coffee that the consuming country roasts

The final and most advanced way to outsource the value-addition steps, but still capture the value, is to arrange for the coffee to be roasted and packed in the consuming country. The objective here is that the coffee is labelled with the producer's brand or at least origin, identified in association with a partner's brand.

The main benefit of this sales model is the shorter lead-time, which means a fresher product reaches the end user. However, it also requires considerably more investment and involves a slower return on investment, as title to the product is not transferred at the point of export.

As already noted in the discussion on value addition model 2, farmers will be disadvantaged by their lack of local knowledge and brand inequity, and supermarket entry may be impossible. Similarly, for value addition model 3 to succeed, the producer will need an adviser or partner with good local knowledge.

The case studies in Chapter 5 show that this is often someone with the same nationality as the coffee farmer who lives in the consuming country. It could also be an independent third party. This partner could be vested in the business or simply offer a value addition service such as importing, warehousing, roasting, distributing, branding or marketing.

As relationship coffee sales volumes grow amid the third wave push, this model may offer the greatest opportunities for producers.

CHAPTER 5 CASE STUDIES

Coffee companies in East Africa and elsewhere have successfully developed higher value channels. The following case studies illustrate the challenges and lessons learned by those that have been profitable. All the information in the case studies was gathered in the second half of 2019 through interviews, telephone conversations and e-mail exchanges with the companies themselves. Some supplementary information was obtained from press articles and desk research.

Direct trade from origin

We have taken several examples of successful direct trade in East Africa to demonstrate how this model can best serve the interests of the farmer. Buyers, not farmers, typically initiate these relationships.

The first case involves a smallholder cooperative factory from Kenya's top-quality producing area of Nyeri that has been selling its AA coffee to a Danish specialty roaster for the last nine years. We will then examine the case of a Dutch importer that committed in 2019 to buy 100% of the production of another Nyeri cooperative at a premium price. We also explore how a small estate from Meru linked up with a British specialty roaster and coffee shop business. Finally, we look at a small start-up roasting business in Amsterdam that buys all its coffee from a single washing station, called Liza, located on the edge of Lake Kivu in Rwanda.

The Coffee Collective

The Coffee Collective is a well-known Danish specialty business whose coffee-sourcing model hinges on direct trade and transparency. Its Sustainability Report, available on the Coffee Collective website (www.coffeecollective.dk) clearly sets out the goals and achievements of the company in this regard, as well as the prices paid to global suppliers.

The Coffee Collective signed the Pledge,⁶⁴ a voluntary code of best practices to support pricing transparency on green coffee purchases. Specialty roasting coffee companies from across the globe support this code. Klaus Thomsen says the 'C' (commodities) index does not influence the prices that the Coffee Collective pays and that the company prefers to set stable offers to farmers when possible.

The Kieni cooperative factory in Nyeri has sold its coffee to the Coffee Collective for nine years. Kieni received the second-highest price per kilo paid to farmers in the 2018/19 Kenyan coffee season.⁶⁵ This is a textbook example of relationship coffee that is working well for both seller and buyer.

One of the business challenges that Coffee Collective faces is that farmers have no idea what happens after they deliver cherry to the washing station. The company has tried to explain the value chain from seed to cup so farmers can appreciate how value is added. It even designed a farmer poster in the hope that visual communication 'would greatly improve their understanding and appreciation of all the steps, and avoid mistrust'.⁶⁶ Coffee Collective brought two cooperative officials to Copenhagen in September 2019 in a bid to improve farmers' understanding of the whole value chain.

⁶⁴ <https://www.transparency.coffee>

⁶⁵ Figures obtained from Coffee Management Services Ltd, one of the largest marketing and milling agents in Kenya.

⁶⁶ ITC interview with Klaus Thomsen, October 2019.

Ndaroini Cooperative Society

The best-paid farmers in Kenya in 2019 were members of another Nyeri-based cooperative called Ndaroini.⁶⁷ In this case, the buyer was Dutch specialty coffee importer Trabocca BV (www.trabocca.com).

Farmers in Kenya are paid months after they deliver their goods to the processing facility. Furthermore, they often receive far less money than they expect because of unexplained deductions by the processor. Seeing how poor returns reduced the quality of Kenyan coffee, Trabocca jumped at the opportunity to secure the high-quality coffee its customers desired and at the same time guarantee farmers a top price for every bean they produced.

The company contracted to buy all the coffee produced by Ndaroini farmers – irrespective of quality and bean size – for 100 Kenyan shillings (\$1) per kilo of cherry, which is roughly \$6/kg green equivalent. By establishing a farmer ledger, Trabocca was able to ensure traceability of payment to each farmer. The buyer also paid the cooperative's full costs for operations and overhead. This meant that farmers were aware of, and received up front, a net price, rather than the normal gross price, from which the management committee would deduct the cooperative's running costs.

This was a huge and sudden departure from traditional Kenyan value chain practices, and it was not without upheaval. The cooperative factory was one of three owned by a farmer association. While Trabocca agreed to buy the total volume of one factory, it could not purchase all the coffee produced by the society. This caused considerable internal friction.

People who had been acting as sales agents rejected this model, as did other local players who feared a ripple effect. Farmers held public protests and demanded the right to sell to their buyer of choice⁶⁸. The local press described the situation as similar to the 'coffee wars' that occurred more than a decade earlier.⁶⁹

Menno Simmons, the founder and owner of Trabocca, says this bold move to pay a fair price and practice open-book pricing and transparency has paid off, with much of the coffee sold before or upon its arrival in Europe and the United States. Ndaroini management and farmers have broken away from the parent cooperative and formed their own legal entity, a clear indication that this new model of buying has been well received by the farmers.

Muchomba Coffee Farm

Muchomba farm, in Meru region, is just one of several hundred small estates in Kenya. Since 2017, the farm has sold all of its main-grade coffee to Paddy and Scotts (www.paddyandscotts.co.uk), a roaster and coffee shop business based in East Anglia, the United Kingdom.

While buyers have worked with Kenyan cooperatives and farmers and invested in their infrastructure for the past 20 years, the entrepreneurial genius in this example was associating consumers directly with the source, inviting them to be partners in the initiative by buying a tree on the farm. This investment enables consumers to be part of the story, to visit the farm and see first-hand how their coffee is grown. The partnership has also financed the rehabilitation of a local school, a benefit to the whole community.

As in the two previous case studies, Paddy and Scotts pays the equivalent of \$6/kg plus a premium. This is substantially higher than the 2018/19 average main-grade price of \$4.70/kg published by the Nairobi Coffee Exchange.

Scott Russell, the founder and chief executive of Paddy and Scotts, says of his Kenyan supplier: 'Working directly with the Muchomba family has allowed us to build a partnership and relationship that we are very

⁶⁷ Coffee Management Services data.

⁶⁸ <https://mobile.nation.co.ke/counties/nyeri/3112264-4935716-wxmudf/index.html>

⁶⁹ The 'coffee wars' of the early 2000s were sparked by outrage over corruption and mismanagement of the cooperative sector. Some farmers died fighting for the right to break off into more manageable cooperative units. Farmers also sought to eliminate powerful forces that used the coffee industry for their own financial gain.

proud of. Trading coffee directly with the Muchomba family allows us to reduce the supply chain and support the farm and local community directly.'

Paddy and Scotts customers 'can enjoy real engagement with the farm and know that drinking our coffee is making a positive difference in Meru', Russell added. The company invests heavily in the Muchomba farm's infrastructure and agronomy as well as the local school 'to ensure that coffee is being used as a vehicle for social impact. We are committed to pay above market price for our crop and enjoy an agreement that guarantees the coffee produced by George and his team will go to a good home'.⁷⁰

Stean's Beans

Stean's Beans (www.steansbeans.com) is a start-up roasting business based in Amsterdam. Founder and owner Stean Fasol roasts about 500 kg a month and sells the coffee online or to local offices. His three blends (Tatu, Mbili and Moja) sell for €19–€25 (\$21–\$27.50) per 500g pack.

The company only uses Rwandan coffee from a single washing station, Liza, owned by Jean-Paul Tunda. Although volumes have quadrupled since Stean's Beans was founded in 2016, they are still small, at about 100 bags a year. For economy of scale as well as finance, Fasol uses an exporter in Rwanda to ship the coffee in a consolidated container and a local company to import, store and finance the coffee once it arrives in the Netherlands.

Stean's Beans roasts the beans using what might be described as a roaster cooperative, a company that offers co-roasting and working space along with cupping, brewing and storage facilities (<http://amsterdam-roasters.nl>). Roasting costs €1.65/kg plus a 20% value-added tax for a minimum of 250 kg per month.

This kind of facility is not common. But for any newcomer to the business, it provides good resources and collaboration to overcome initial technical challenges, reduce initial investment and manage overheads in relation to volume. Stean's Beans own-branded packaging costs 0.80 euro cents per pack. Fasol's other main expense, €800 a year, covers the graphic design and marketing needed to support his social media and website activities.

This business model includes regular visits to Rwanda to meet with the smallholder producers who deliver their coffee to Liza. The buying strategy hinges on 'more possibility for the sustainable relationship going forward to improve the quality of the coffee and the amounts being transferred back to the coffee farmers', Fasol said.⁷¹

He pays a fair price of \$5.50/kg to the washing station owner for the coffee on a Free on Truck⁷² Kigali basis, as well as \$0.33/kg at the end of the season. Fasol believes the washing station owner benefits the most from this arrangement, as farmers are apparently being paid the same amount as in the past, even though he is paying a premium.

Fasol favours a system where payments are split between the cherry price and costs related to processing. He is researching a new system that he hopes will enable payments to go directly to the farmers via a mobile phone banking platform.

The washing station owner has visited Stean's Beans operations in Amsterdam to learn more about the whole value chain. But Fasol says the farmers who supply the beans 'have no idea where the coffee goes or what consumers are paying for the coffee. They also have little idea of what is expected by the roaster in terms of quality. Lastly, the majority of farmers have never tasted their own coffee'.⁷³

⁷⁰ Interview with Scott Russell.

⁷¹ Interview with Stean Fasol.

⁷² FOT – is an INCOTERM that leaves the costs of transport by truck up to the buyer

⁷³ *Ibid.*

E-commerce

E-auctions

Sensible Development (www.sensibledevelopment.com) operates the online platform that is responsible for Cup of Excellence auctions. This enterprise, which has held online coffee auctions for eight years, hosted 25 events in 2019. It has 1,200 active buyers from 70 countries, with 39% coming from the Republic of Korea, Chinese Taipei, China, Hong Kong SAR and Japan.

Before the auction, Sensible Development handles the sample dispatch. Through active online marketing and social media, Sensible Development publishes full farm details per lot on offer, with producer stories, maps, videos, locations, etc. It encourages sellers to tell their own stories to help buyers visualize better and induce them to buy.

The auction works on a countdown basis. A three-minute clock starts once bids are made on all lots. The clock is reset every time a new bid is placed. This continues until bidding ceases and the clock hits zero.

Sensible Development uses different fee structures, but the main two are a fixed fee per event and a commission basis per lot. Table 3 shows the origin focus that can be achieved by selling small bag counts at auction.

Table 3 Selection of Cup of Excellence auction results in 2019

| | Variety/process | Highest price \$/lb | Average price \$/lb |
|-------------------------|-----------------|---------------------|---------------------|
| Colombia (north) | Geisha/natural | 35.60 | 14.31 |
| El Salvador | Pacamara/honey | 63.40 | 13.60 |
| Honduras | Geisha/natural | 120.10 | 13.67 |
| Burundi | Bourbon/natural | 21.10 | 6.76 |

Source: <http://auction.allianceforcoffeexcellence.org>

There are other successful auction models as well, including the Specialty Coffee Association of Panama's Best of Panama. At this auction, the La Esmeralda estate saw the price of its famous Geisha variety coffee rise from \$130/lb in 2007 to \$601/lb in 2017. In July 2019, two bags of Elida Estate Natural Geisha sold for a record \$1,029/lb.⁷⁴

During a June 2019 auction, 35 lots of special reserve coffees grown by Guatemalan estate Finca El Injerto fetched \$12.50/lb–\$95.75/lb.⁷⁵ These were sold in lots as small as two to four bags. Hacienda La Esmeralda held its own auction for similar quantities the same month and saw a price range of \$51/lb–\$163/lb.⁷⁶ Although this specialist auctions involve only limited volumes, the marketing and reputational impact for these two private estates is invaluable.

Auctions could be a useful platform for East Africa to offer microlots, especially to create value in the developing markets of Asia and the Middle East. Holding competitions, followed by an auction a month or so later, is a way to attract buyers and bring publicity to top-quality origins. Full transparency of farmer remuneration helps to generate interest from buyers with a social responsibility mandate.

⁷⁴ <http://scap-panama.com/auctions2001-2017/>

⁷⁵ <https://auction.fincaelinjerto.com/en/>

⁷⁶ <https://viewauction.haciendaesmeralda.com>

E-commerce for roasted coffee

There is scant information and data about the success East African producers have had with this model. China's TMall (www.TMall.com), which reaches 700 million consumers, lists the Rwanda Farmers Coffee Company's Gorilla's Coffee for sale at the equivalent of \$17/500g pack and latest figures indicate 138 units are sold each month. TMall also prints a guarantee that it is a 'a genuine, directly supplied overseas product'.

ICO reports that only 3% of coffee from origin is roasted before it is sold, so we can deduce that product visibility and placement on the site present the greatest challenges. Even a cursory Google search for 'roasted coffee products' generates 89 million results, so it is not difficult to see the importance of branding and placement for any measure of success using this sales model.

Roasting in origin and selling domestically

A number of East African roasting businesses focus either exclusively or primarily on the domestic market. Few are owned and managed by coffee producers, however. The skills required to grow coffee differ markedly from those needed to transform the beans into a finished product. Most smallholder farmers learned how to cultivate coffee from their elders and some may have studied at an agricultural college, but few will have any concept of manufacturing, sales and marketing. With demand growing strongly at home, African farmers have the potential to earn better incomes and learn about demand by selling their roasted coffee locally.

The following are examples of more recently established roasting businesses that are farmer-focused. Their unique selling point aims to be sustainability and better returns for farmers.

Ya Coffee

YA Coffee was established 2012, but the prevailing Ethiopian coffee regulations, which restricted traceability, transparency and sustainability, made it very difficult for the company to engage in a value-addition business, promoting specialty coffee internationally. The Ethiopian Government relaxed the rules in 2017 and permitted locally roasted coffee of export standard. Before this, only low-grade coffees could be roasted to maximize exports and foreign exchange earnings.

These changes enabled YA Coffee to source good-quality coffee from cooperatives or women's groups for its four 100% Ethiopian four blends: a house blend, a natural coffee, a single origin and a coffee sourced exclusively from the United Nations Educational, Scientific and Cultural Organization designated biosphere reserves. These are sold almost exclusively through artisan shops in Ethiopia.

Although Ethiopia drinks half of what it produces, YA Coffee founder and co-owner Sara Yirga says that the coffee beverages available on the domestic market are low quality due to 'almost non-existent knowledge of coffee value addition and coffee skills, untrained baristas and coffee vendors'.

This problem of poorly roasted or prepared coffee is common throughout East Africa. Yirga identifies 'professionalism in communication and ... the way of doing business, knowledge of the sector and how the global coffee market functions, understanding cultural differences and commitment to quality as well as integrity'⁷⁷ as prerequisites for success. YA Coffee relies on its website and strong social media presence for marketing and has organized coffee talks and catering events for further promotion.

Company representatives have travelled to international trade fairs, exhibitions and conferences to broaden their knowledge. They believe that, given the international reputation of Ethiopian coffee, a huge market remains untapped. Although they have made many contacts, overseas sales have been slow to follow. YA Coffee's first export business only materialized in 2019, with a consignment to a café in Somalia that will serve and retail their coffee.

⁷⁷ Interview with Sara Yirga.

Question Coffee

Bloomberg Philanthropies and United States-based Sustainable Harvest Coffee Importers, both committed to rural and social development, joined forces in 2013 to form the Relationship Coffee Institute (www.relationshipcoffeeinstitute.org).⁷⁸ This institute sought to train women farmers about good agricultural and business practices so they could increase productivity and improve quality. It also aimed to facilitate market access by creating a specialty coffee brand that could be sold on Rwandan market.

Question Coffee, a café and wholesale business in Kigali that focuses exclusively on the domestic market, was founded in 2016. During its first year of operation, Question Coffee (www.questioncoffee.com) amassed an impressive portfolio of retail and commercial clients including the Marriott, Radisson and Serena hotels and RwanAir. All proceeds from Question Coffee are used to train farmers. A roaster training school was opened in 2018 to complement the services it offers.

Question Coffee has annual sales of about 20 tons of green equivalent. Sales grew fourfold in its first three years of operation, proving the benefits of having a retail presence. Farmers who supply green coffee for the roasting plant receive the same price that Sustainable Harvest Coffee Importers pays for the large volume of coffee that it exports to roasters around the world. This enables farmers to extract more value for coffees that would be tough to sell on the global market, typically the lower screen-size coffees or small volume lots.

One of the side benefits of the Question Coffee initiative is that it exposes farmers to the international market. Many green coffee buyers visit Rwanda every year to source their annual requirements, and they often check out the local coffee scene. The café and school have become a valuable marketing tool to showcase the coffee cooperatives and improve their marketing awareness.

Exporting roasted coffee has been challenging, says Adam McLean, social enterprise director at the Relationship Coffee Institute. It has been difficult to find a competitive model after factoring in import taxes and shipping the coffee by air – necessary to guarantee freshness. The institute has a web store for online orders and subscription coffee that is roasted to order in the United States, but volumes have been very small to date.

Roasting in origin and selling internationally

Over the last decade, East African governments have stepped up pressure on farmers to regard value addition as a panacea to their problems. Indeed, in March 2019, a Kenyan lawmaker proposed amending the Coffee Act to limit exports exclusively to roasted coffee.⁷⁹ Selling roasted coffee to the local market is logical, but selling overseas is far more demanding as it requires mastery of international logistics and marketing.

We examine several examples, all very different in terms of size, levels of success and potential for growth, to help determine whether this is a viable way to add value.

Eva's Coffee

Eva's Coffee (www.evascoffee.co.ke) is an example of a small-scale local entrepreneur seeking to market coffee in international markets. The experiences of founder Eva Muthuuri and the challenges she has faced are not atypical among small entrepreneurs attempting to operate independently.

Muthuuri, a Kenyan national, has spent most of her adult life working in the development world. After the the United Nations Sustainable Development Goals were announced, she decided to further social development by championing sustainability in agribusiness. Together with her husband, an expert in creative design and brand development, she established her company and became a licensed coffee dealer in Kenya in 2016. She intended to work with coffee-farming families on a commercial basis to improve income and smallholder

⁷⁸ <http://www.relationshipcoffeeinstitute.org/about/our-mission>

⁷⁹ <https://www.the-star.co.ke/counties/central/2019-04-20-kuria-urges-support-for-coffee-bill/>

livelihoods, while also continuing her other development work, such of improving access to healthcare and gender equity.

Today, Muthuuri works with five Meru-based cooperative societies and some individual farmers who have their own wet mills. She sells about 100 kilograms a month for \$10–\$20/kg, depending on the order size. Most of these sales are in branded packaging, positioned as ‘Traceable Women’s Coffee from Kenya’. Muthuuri uses various channels to sell her coffee, including:

- ‘Suitcase’ salespeople, usually overseas students, who buy a certain number of packets for sale to friends and family and which provide ‘pocket money’ to cover some of their living expenses.
- Summer markets in Europe.
- Sales to the Republic of Korea via a contact who takes second-hand clothes to Kenya and uses the container to carry back African products, including Muthuuri’s coffee.
- Selling via local Kenyan institutions such as the Kenya Police Service, the local branch of Interpol and the Kenya Medical Association. She has regular contracts to deliver gift packs for their visitors or for officials to take gifts when travelling overseas.

Financial advisers say Muthuuri should get a bank loan to expand her business, but she does not want to take this risk. If Eva’s Coffee is to grow or innovate, however, it will need to increase its financing and management capacities.

Rwanda Farmers Coffee Company

A larger example is Rwanda Farmers Coffee Company, which was established with government assistance and today represents the interests of six cooperatives and more than 4,300 farmers, of which 36% are women. The roasting plant has an annual capacity of 1,500 tons, but it operates at just 10%–13%.

Despite efforts to penetrate international markets and Government support for some marketing trips, 70% of sales of Gorilla’s Coffee – its farmers’ branded coffee – are sold locally. Apart from some pockets of online-based selling, targeted at the African diaspora (www.mykibo.com), and to China via the Alibaba platform, overseas sales have proven difficult to grow.

Rwanda Farmers Coffee Company has not managed to compete with big brands in international markets. Sales and marketing manager Benjamin Nkurunziza says the cost of supermarket entry is prohibitively high. The average retail price of Gorilla’s Coffee in the European Union and the United States is about \$30/kg. The company tries ship to countries served by RwandAir as the favourable freight rate of less than \$2/kg means the arrival cost at destination is around \$11/kg, according to Nkurunziza. On top of this, importation, warehousing, transport or distribution might add to the costs of bringing the coffee to the final consumer.

CaféRwa

CaféRwa (www.caferwa.com), the roaster behind the Kivu Noir brand, represents a group of five Rwandan washing stations. This umbrella organization, which has a constituency of 7,000 farmers, sells approximately 700 tons of green coffee a year. CaféRwa also has a range of roasted products, most of which are exported to the United States with the help of a partner in Los Angeles that handles website sales and social media.

CaféRwa sold three tons green equivalent at \$15/kg in the first six months of 2019. This coffee has an online retail price of \$36/kg. The company’s 2019 budget target is 2% of its annual volume at 12 tons. In 2019, farmers received \$7/kg free on truck green equivalent selling their coffee as a roasted product. This is a healthy premium over the \$4/kg they received for most of their green coffee sales.

Rwashoscco and Angelique’s Finest

Rwashoscco comprises five cooperatives and a privately owned farm based in Rwanda, and it represents almost 14,000 farmers, many of whom are women. In 2007, Rwashoscco set up a roaster and established

a brand called Café de Maraba. Its main goal was to promote a coffee-drinking culture in Rwanda and to educate food and beverage outlets and consumers about coffee.

Rwashoscco moved into roasted coffee to create another revenue stream. As an umbrella organization representing the interests and marketing the coffee of its farmer members, it needed to remain sustainable. Selling roasted coffee generates income to help cover overhead and reduce the costs associated with exporting green coffee.

The company formed a partnership with a German social start-up company (www.kaffee.kooperative.de) in 2016 to sell roasted coffee overseas. This venture faced many barriers, from matching the desired quality profile and finding the right marketable story to overcoming a lack of local marketing expertise.

In 2017, Rwashoscco Managing Director Angelique Karekezi connected with the International Women's Coffee Alliance. Together, they developed marketing materials about the many women farmer members, widows of the war, and the strong messaging needed to sell the roasted product. Rwashoscco then began to separate production and persuaded its German partner to use coffee delivered by a group of 1,500 women, part of Dukunde Kawa cooperative.

Around the same time, a non-governmental organization called Terres des Femmes offered support for the development of a logo and packaging. The brand name Angelique's Finest was born. Marketing and storytelling to promote this coffee have been key to the success of the model.

With the assistance of the German Ministry of Economic Development, eight journalists including the editor of *Brigitte*, Germany's biggest women's magazine, were flown to Kigali in 2018. The magazine subsequently featured Angelique's Finest, giving it much-needed visibility in the German market.⁸⁰ A promotion that year enabled readers of the magazine to buy a pack of the coffee for €5.50 via a crowdfunding page that raised almost €33,000.⁸¹

A German television documentary and newspaper articles have also maximized exposure in the country.⁸² One of the German investors is actively involved in the business and its strategy planning, and spends part of the year in Kigali. Angelique's Finest is now looking for private equity investors and the right timing to convert its cooperative status to a limited company.

Annual sales of Angelique's Finest reached 11 tons green equivalent in 2018 while sales of Café de Maraba, Rwashoscco's original brand, languished at two tons. This demonstrates either the appeal of a coffee produced solely by women among German consumers and/or the greater appeal of European-designed and manufactured packaging and branding.

In 2019, Angelique's Finest was targeting sales of 30 tons and its German partner was pitching for a new client – health-shop chain DM, which has more than 2,000 stores across Germany. DM sponsored a competition in 2018 for new and innovative products, for which the prize was market access. The top three products were given in-store shelf space and 4th place, won by Angelique's Finest, saw its coffee launched on the DM online shop, where a kilogram of its roasted beans are selling for €27.90.

The sale of some of their coffee as a roasted product provides a stable market for farmers and income at an improved price. At the same time, the organization gains professional standing and international reputation. It also means that farmers get consumer feedback, which is usually absent along the farmer-to-consumer value chain.

⁸⁰ 'Kaffee ist Freiheit' (Coffee is Freedom), *Brigitte* magazine, 20/2018.

⁸¹ See <http://www.startnext.com/angeliques-finest-strong-women>

⁸² <https://www.zdf.de/gesellschaft/plan-b/plan-b-gut-gebrueht-102.html>

In 2019, when the farmers were selling their coffee locally, they earned \$3.50/kg green. But when they sold it as roasted coffee for export, they made \$4.80/kg and were paid when the order was confirmed. Roasted coffee sales averaged \$7.50/kg green equivalent in 2019.

Roasting and selling coffee in a consuming country

Few producer businesses roast and sell coffee in a consuming country on a fully commercial scale. When they do occur, it is often the result of migration, and they are created to offer other local expatriates a 'taste of back home'. The Ethiopian Coffee Company (www.theethiopiancoffeecompany.co.uk) in London is one example of this.

There are a few success stories out of Central and South America. The following two examples provide valuable insight as to what is possible with hard work and determination.

Topeca Coffee Roasters

The coffee industry in El Salvador has fallen victim to the fate of many producing countries of collapsing volumes in the face of tough, low-cost competition; production fell from almost five million bags in 1980 to fewer than 500,000 in 2018. The Government has continued to control and regulate without any investment or incentive for farmers to continue cultivating crops.

Emilio Lopez Diaz is a seventh-generation coffee farmer from El Salvador. In 2000, as he finished his undergraduate studies in Oregon, the United States, his parents were on the verge of being forced to sell their failing coffee business after realizing that the only way to expand and add value was to invest in milling and roasting.

He asked his father to send 150 lbs of roasted coffee and overnight, he became a 'suitcase' salesman, knocking on doors to see who would buy his coffee. Very quickly, Lopez learned that without equipment such as brewing machinery, cups and other accessories, he would not be able to penetrate the Oregon market.

After much perseverance, monthly sales reached 2,000 lbs in 2002 and Lopez invested in roasting machinery in El Salvador. Initially, his biggest hurdles were consistency and diversity. To tackle the first, Lopez joined the US Roasters Guild to learn about roasting. He repeatedly returned to the United States to improve his skills and knowledge. He was so committed that he became chairman of the guild in 2017.

The second problem required long-term investment. After returning to El Salvador, Lopez researched where he could buy affordable, small-scale equipment not only to roast, but also to depulp, hull and mill. Brazilian machinery manufacturer Pinhalense S/A (www.pinhalense.com.br) provided the solutions. The next years were spent experimenting with different processing methods – washed coffees, naturals, honey-processed – and fermentation to obtain the required diversity of coffee to enhance his blends.

Lopez saw his fledgling roasted sales market languish after his return to El Salvador. He teamed up with his sister and brother-in-law, based in Oklahoma, to establish and expand the roasted coffee business in the United States (www.topecacoffee.com). At first, the products were roasted and shipped from El Salvador and sold mainly to Latin American businesses based in the United States. In 2007, oil prices rose to \$2.50 a barrel and his 2008 courier bill reached \$75,000, which made the decision easier to invest in roasting equipment in United States.

Today, Topeca's roasting business and café in the United States sell more than six containers of green coffee equivalent every year. The company says it is one of only a handful with a 'fully vertically integrated seed to cup model'.

'We have our hands in every step of the process, from planting the coffee plant to hand-picking the ripest cherries to roasting it here in Tulsa, Oklahoma, and serving it in our own shops in downtown Tulsa,' Topeca says on its website.

Topeca sells four containers of coffee to the local El Salvador market. The company does not have any cafés in the country, but sells both retail and wholesale and to outlets of multinational food chains and hotels.

Lopez also exports green coffee to more than 40 destinations, which accounts for the balance of his 30 plus containers of coffee production. He has won the El Salvador Cup of Excellence, and his coffees have been used by barista competitors around the world.

Several lessons can be learned from this 'rags to riches' coffee story. Lopez says the best business plan is to start small and only invest after a market has been created. Coffee expertise and knowledge of the market are critical.

While consumers like the vertical integration story, competition in the consuming markets is fierce. Any partnership must be based on coffee knowledge and expertise. The biggest challenge to roasting in origin is freshness of the product. This is not an issue when starting small and airfreighting products to their destination. But once the business reaches container-load size, it must be shipped by sea. It can take two months to reach store shelves, by which time competitiveness in terms of freshness is lost.

In his first harvest, Lopez produced just 100 bags. He subsequently increased his landholding from the original 25 hectares to more than 250 hectares by buying out property owned by other family members (he has 21 first cousins). He realizes the necessity of aggregation to reach greater economies of scale and recently joined forces with a partner, adding another 250 hectares of coffee-growing land.

This case study underscores that diversity and passion are the secrets to success. Lopez says that 'I have a lot of options. I don't sell a single bean to someone I don't know. I have personally visited almost every single roastery, know the machine, the roaster, and have been to the coffee shops and met the baristas. We don't roast all of our coffee, and we have many other customers who buy our green coffee. Diversifying risk is the main thing I've accomplished by being so spread out'.⁸³

Pachamama Coffee Cooperative

The sole example we found of a farmer cooperative roasting and selling coffee to end-users is Pachamama Coffee Cooperative (www.pachamamacoffee.com), which is based in Sacramento, California, in the United States. It comprises five cooperative societies from Peru, Nicaragua, Mexico, Guatemala and Ethiopia.⁸⁴ The board of this cooperative consists only of farmer members and represents more than 100,000 farmers and their families.

The two co-founders, Thaleon Tremain and Raúl del Águila, along with representatives of the other groups, needed five years to establish the business and set up the cooperative structure. They started by outsourcing the roasting and selling out of a garage in 2006. It was not until 2012 that they were ready to move into commercial space, and 2015 before they were able to invest in their own roasting plant.

All Pachamama products are organic, an array of blends and single-estate coffees from each origin. Most of the coffee is sold to United States-based wholesale and retail customers, often also part of the cooperative movement. The cooperative also sells coffee at its café in Sacramento and via its online shop, which offers consumers a 'Coffee of the Month' subscription service. Members decide whether to pay dividends or retain profits.

The business also champions a Community Supported Agriculture programme. Its website lets consumers see the individual farmers who produced their coffee, send them tips to support their livelihood and pay to plant a tree in one of the five origins.

Communications manager Lauren Taber says Pachamama promotes global equity. 'We stand for radical changes to the way the everyday consumer thinks about business. That is why we are a farmer-owned

⁸³ <https://www.beanscenemag.com.au/emilio-lopez-diaz-on-coffee-from-seed-to-cup/>, 9 September 2019.

⁸⁴ The member cooperatives of Pachamama are Raul del Aguila from COCLA in Peru, PRODECOOP of Nicaragua, Manos Campesinos of Guatemala, La Union Regional de Huatusca of Mexico and Oromia Coffee Farmers Cooperative Union of Ethiopia.

cooperative – we believe that capitalism can be used to empower those that have traditionally been left behind by the bottom line of business: profit.¹⁸⁵

The following table, published by Pachamama in 2019, illustrates the historical share of earnings for farmers from the cooperative’s sales model. Although the ‘farmer share of value chain’ is shown as 76%, farmers would have a higher share of profits, as it can be assumed that they would also make money from the production of green coffee.

Table 4 Revenue increase for farmers through value addition

| Price breakdown | \$/lb | % |
|-----------------------------|-------|------|
| Average sales price | 12.69 | |
| Farmer green coffee price | 2.95 | 23.2 |
| Total variable costs | 3.01 | 23.7 |
| Gross profit | 6.73 | 53.0 |
| Farmer share of value chain | 9.68 | 76.2 |

Source: Pachamama Coffee Cooperative. <https://www.pacha.coop/why-pachamama/financial-transparency/>

The profit potential of outsourced coffee value addition in target markets

It is difficult to quantify the profit potential of selling roasted coffee directly to end-consumers using service providers, given the number of variables and limited amount of factual data available to support the exercise.

Based on information gathered from stakeholders during this study and making realistic assumptions from our own experience, we have created the following table, to estimate where breakeven would be possible. We used a typical price of \$5/kg for the farm gate sale of the green coffee, in line with examples we looked at earlier.

The achieved consumer sales price is key to the success of the model. At a sales price of \$25/kg, which should be attainable for high-quality specialty coffee, a fledgling venture should return a small profit. This would require the coffee to be positioned in a high-end segment.

It is important to recognize that while an additional \$2 per kilogram of profit for the farmer is less than 10% of the sales price, it could be a huge increase in their retained profit – which may only be tens of cents a kilogram for green coffee sold at the farm gate.

The downside is that should the coffee bring in a lower price – say, \$20 per kilogram – there may be a net loss. Add to this the risk that all the coffee may not be sold, and it is clear that most producers would not have the means to insure themselves against the potential losses.

This is where an intermediary can play a role: a non-profit partner or public body willing to underwrite the initial phases of development of such a specialty branded coffee business. The assumption would be that, after an initial phase of subsidizing the coffee transformation and marketing, costs and prices would be better understood, risks managed and more efficient practices implemented, and the farmer groups and private sector partners could take over the operations on a profit-making basis.

⁸⁵ <https://www.pacha.coop/blog/pachamama-coffee-celebrates-international-day-of-cooperatives/>

Our case studies also indicate the need for patience and commitment on the part of coffee producers. Investment, time, financing and the development of 'social connections' mentioned in *The Good African Story* are all required to build brand equity. The Rwashoscco case study shows that success often requires the support of a local partner in the target market (Germany, in this case) and the savvy use of promotion.

Most of the businesses we studied have needed five to 10 years to become fully established, and all have relied on a diversified set of market channels to expand their business. Initial sales in international markets can be small while the costs are large, and patience towards a long-term objective of establishing a market presence is required.

Table 5 Viability of roasting and selling coffee using value addition service providers

| Description of cost | \$ cost per kilogram | Comments | |
|--|----------------------|--|--|
| Cost of coffee | 5.00 | Achievable sales price of \$250/50kg | |
| Warehouse costs for export preparation | 0.18 | | |
| Movement to port, port expenses | 0.09 | | |
| Freight | 0.09 | Based on \$1,500 per 20-foot container | |
| Insurance at 0.5% | 0.03 | | |
| Landing and importing | 0.08 | | |
| Delivery to roasting plant | 0.13 | Will vary on distance from warehouse | |
| Roasting and packing | 2.00 | | |
| Roasting loss (17%) | 1.36 | Different roast profiles will yield higher or lower roasting loss. | |
| Packaging and labelling | 2.00 | | |
| Finance @10% for 180 days | 0.26 | | |
| Total cost | 11.73 | | |

| Per kilo | Sales price 1 (\$) | Sales price 2 (\$) | Sales price 3 (\$) |
|------------------------------------|--------------------|--------------------|--------------------|
| Cost of product | 11.73 | 11.73 | 11.73 |
| Sales price | 15.00 | 20.00 | 25.00 |
| Distribution cost @ 30% | 4.50 | 6.00 | 7.50 |
| Branding/Marketing @15% | 2.25 | 3.00 | 3.75 |
| Net sales margin | -3.48 | -0.73 | 2.02 |
| Total gross profit and loss | -17,330.00 | -3,645.40 | 10,059.60 |

Assumptions:

1. Input – 100 bags of green coffee at green coffee price of \$250/50kg ex Kigali, Nairobi or Moshi/Mbeya/Mbinga.
2. Coffee being shipped to Europe in consolidated container. If 100 bags were shipped alone, the costs would triple from \$0.19/kg to \$0.57/kg.
3. Coffee being roasted, branded, packed, sold and distributed by value addition service providers assuming minimum roast batch of 30kg.
4. Finance for six months from bill of lading date.
5. Coffee packed and sold in 500g.
6. Distribution costs range from 15%–30% of the sales price. For the purpose of this guideline, we are using 30%.
7. A brand agency may carry out branding and marketing. It will typically charge 15% of sales revenue.
8. Gross sales price per kg \$15, \$20 and \$25.
9. We have not taken into account any trade tariffs or import duties that may apply.

CHAPTER 6 THE WAY FORWARD

Showing how the process could work in East Africa: A pilot project

This study was undertaken to determine whether farmers can successfully sell roasted coffee to Europe, the United States and Asia.

Coffee producers may be able to earn much higher returns by transforming their product close to the end-consumer, outsourcing this transformation and promotion to well-established partners in the local market. The approach comes with risks and requires access to financing. This study has not been able to identify any East African examples that could serve as an ideal role model. Those that managed to achieve some presence for their roasted coffee in Europe appear to be exceptional cases.

This paper proposes to undertake a pilot project with at least one East African farmer group to demonstrate how the process could work, determine a realistic set of costs and establish a mechanism that other coffee producers could replicate.

Europe is a particularly suitable target market, given existing cultural and commercial relationships with East Africa. Within Europe, the United Kingdom stands out as a market that has a growing and sophisticated consumption of specialty coffees and is particularly open to innovation.

The proposal is to source the necessary value chain partners to cover the different functions of bringing a selection of coffees from origin to the country of destination and follow their path from farm gate to final consumer, via either a retail café outlet or a retail outlet for home consumption. First-hand experience will enable the farmers to appreciate the challenges involved, better understand the whole value chain and gain valuable insights into how to capture a significantly higher share of the total value added.

Ways to add value

Changes in the way coffee is consumed are leading to higher average retail prices around the world. Yet little of this value is finding its way to farmers. Increased demand for coffee may be coming largely from developing countries; elsewhere, the trend is towards 'premiumization'. The millennial generation, in its desire for experiential products, is a major source of demand for premium coffees – and the trend is set to continue.

However, while the revenues of coffee roasters have continued to grow, the international price for green coffee has not kept pace. As a result, the percentage of value of the global market retained at origin has dropped from 30% in 1991 to only 10% in 2018. This decline can be partially attributed to higher production costs. But it is also the result of a lack of transparency in transactions and the weak negotiating power on the part of farmers, who are usually price takers rather than price setters.

The production side also needs sustainable solutions to many problems, such as adapting to climate change, urbanization, low yields, ageing farmers and access to finance. All of these challenges are overshadowed by the current low prices, which are often below the price of production and prevent the farmer from enjoying a sustainable livelihood.

There is a new opportunity for farmers to sell a differentiated product; one that has been 'decommoditized' and can achieve a significant premium by virtue of its specialty characteristics. The substantial premiums attained in Cup of Excellence auctions and the price levels highlighted in the Specialty Coffee Transaction guide are both proof of this.

While diversification of farming and income could provide some relief, value addition solutions – which can be achieved in various ways – could provide a source of increased revenue for farmers. Producers can look to upsell their green produce, by creating specialty coffees using new varieties and new processing methods. With a superior quality and a marketable story, they can pursue the direct trade route and attract buyers who will commit to a long-term relationship for their coffee. Selling specialty coffees on an online coffee marketplace platform or using an auction system are other ways to attract both buyer interest and a premium.

Coffee consumption is increasing in many of the countries that grow the crop. Developing a domestic market has been key to the success of many producing countries over the past 30 years. Farmers who have ventured into roasting and selling on the domestic market create an alternative – and potentially lucrative – market for their coffee, shielding them from fluctuations in international prices. Developing a coffee-drinking culture requires a significant commitment to marketing and promotion. This can be driven by the private sector, but in most successful cases, governments have provided backing to the campaign.

More than 90% of coffee is exported in its raw form, and most of the remaining 10% is exports of instant coffee. That leaves just 1% of global coffee production exported as a finished roast and ground product from its country of origin. This low share of value-added coffee in trade is not surprising, given the logistical and commercial challenges highlighted in this report. Exporting roasted coffee implies additional costs, challenges to keep the product fresh and a need to understand consumer tastes in target markets.

An alternative approach becomes a real possibility in this age of outsourcing and global trade. Instead of selling the coffee in its raw or roasted form, growers can use the services of partners in target markets to roast, package and promote their coffee, under contract. In the cases we found where this had been done, the essential ingredient was a motivated and knowledgeable partner in the target market: either a family member or a trusted organization.

There is potential to question the status quo, identify suitable partners in international markets that can be contracted to support African producer groups, and demonstrate new, higher value routes to market.

APPENDICES

Table 6 A comparison of routes to higher value in coffee

| Route to value addition for producers | Opportunity | Challenge |
|--|---|---|
| Direct trade relationship with buyer, green coffee sold in origin | Buyers looking for new products Microlots, naturals, fermentation, differentiation Long-term commitment Price stability and premium E-auction E-sales platforms Partner investment in farm infrastructure Marketing and marketing exposure | Market linkage Consistency Higher cost of production Often small-volume business |
| Direct trade relationship with overseas buyer, green coffee sold in consuming country | Marketing Market access to more clients via importer Name becomes known Reputational spread | Coffee must be financed longer Seller retains product and quality risk on arrival Not as direct, importer margin |
| E-commerce for roasted products | Control of content and social media feed More and more people shopping on line Can roast small batches to order Pitch to multimarkets Direct content Control of product placement Customer reviews can attract more visibility and sales Growing trend of subscription coffee, | Lack of media expertise High cost of development Dedicated manpower to manage feed and content, which is expensive to outsource Requires marketing and communication resources. Lack of knowledge of target markets for content Lack of brand equity in target markets Possibly requires local inventory and management for speedy delivery |
| Coffee roasted in origin and sold on domestic market | Tap into growing markets Value addition East African excess roasting capacity Outlet for lower grades – smaller screen size and lower quality Less investment required Packaging marketing requirements less sophisticated Easier possibility of retail presence | Specialty coffee too expensive for consumers. Need retail space for exposure, requires bigger investment Lack of coffee drinking culture Lack of roasting manufacturing skills |
| Coffee roasted in origin and sold for export | Niche markets Direct purchasing is trending Consumers ready to try new products Consumers want variety and a good story. Farmers can provide the experience Growth in and popularity of e-commerce | Internal logistics Importation regulations and cost Freshness of product, longer shelf life Knowledge of market and consumer preference Branding expertise Distribution requirements Aftersales service |
| Green coffee shipped to consuming country and roasted, branded and marketed using value-addition service providers | ALL OF THE ABOVE PLUS: Coffee fresh to market Roasted and ground for the market of sale Packaging and branding for market Marketing and promotion suited to market | Finding the right service providers Brand support Ownership, financial and legal requirements |

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