# Current situation of the coffee industry

1Coffee is one of the world's most valuable assets and at least 25 million people around the world base their livelihood on their production. Most of these producers are small-scale farmers in the developing world, despite the extent of coffee consumption takes place in the United States and Europe

Over the last twenty five years of the last century, developing countries have been incited to follow export-oriented economy models as a way to increase living standards of their citizens. With this model, countries have opened their economies globally, boosting international trade and investments, and expanding their exports with the objective of earning foreign exchange. These strategies try to substitute older models based on import-replacement, which proposed that developing countries should impose protectionism measures in order to protect their domestic economies by controlling investments and external trade.

At face value, specializing in exporting coffee seems to be a good strategy for developing countries, knowing that they have the perfect conditions to grow coffee crops and taking the advantage that richer countries are not competitive in this field, but they are very interested in purchasing the product as they earn considerable profits of its distribution and consumption. However, the global coffee industry has become a nightmare as the world prices have dampened, which have an important impact on livelihoods of those countries.

Why has this happened, and how is affecting developing countries?

# CURRENT SITUATION

2The current crisis is the latest and most dramatic in a long history of industry ups and downs. Coffee prices have plummeted to 30-years lows. (See appendix 2)

Coffee, which is produced in over 50 developing countries, is one of the s

world's most important commodities exports. It makes an important contribution to development socioeconomic and poverty alleviation as well as its economic importance is based on exportation, some of represent more than the

half of their export earnings. Moreover, a cup of coffee in any neighborhood in New York or Paris can reach the $ 3. 60 price. That same cup of coffee, a coffee farmer in the Andes of South America or Southeast Asia receives only 24 cents, a paltry 7% which, of course, does not even cover the cost of production or the basic needs of collectors. This are the most direct consequences of a crisis in the last two years which has sunk into poverty over 25 million people, while the coffee trade of the four big multinationals (Nestle, Kraft Foods, Procter & Gamble and Sara Lee) has curbed their economic growth.

Therefore, it is not a trivial matter; it is actually the major source of foreign exchange for several countries. The current crisis is directly affecting some 20 million families living in the area where the center of all growing and production, between the Tropics of Cancer and Capricorn, and depend on grain as their main source of income. Moreover, the United Nations World Food Program launched an emergency operation to assist 155, 000 people in

Guatemala, where a severe drought that killed subsistence crops coincided with low coffee prices.

# CAUSES

Coffee prices are at the alarming and the specialty coffee industry is in a crisis. In addition, most industry experts predict that will not improve in the near future. At the root of the current crisis is an oversupply of coffee on world markets. Since 1990, coffee production worldwide has increased by 15 percent, exceeding consumption by two folds. This increase was precipitated by new producers entering the market, most notably Vietnam (see appendix 3). Keep in mind that coffee production in Vietnam is not really traditional, in 1987. The Vietnamese were at the beginning just consumers. But the access to the position of largest producer of " robusta" type of coffee is actually the result of a political will, encouraged by the World Bank. As one of the most disadvantage countries in Asia, Vietnam saw in the business the chance to expand its economy and as a way to gain valuable foreign exchange. Furthermore, it provided an opportunity to encourage economic expansion in relatively disadvantage areas. However, coffee production has surged in other countries as well. The reason for this relate to some complex technical, economic and political factors.

In addition, during the last decade productivity of coffee trees increased because of enhanced agricultural practice. Moreover, many countries increased their lands in order to specialize in coffee production. 2The reasons for this is different from country to country, liberalization of trade in coffee, improving better transportation and communication on production data, prices and inventories

increase security of supply World; domestic food markets were deregulated, which encouraged a general shift to export production; and land previously reserved for non-agricultural production, for example forest areas, was brought into agricultural use through privatization and non regulation.

Going a little bit further, the beginning of the crisis dates back to 1989 when the International Coffee Agreement collapsed, contributing greatly to the problem of oversupply. The agreement had been responsible for the restrictions on exports of coffee, without it, many producing countries sought to increase export earnings through increased production. Unfortunately, its success in increasing it led to a surplus that, actually, decreased revenues. Moreover, severe frosts in Brazil during the middle 1990’s showed a temporary rise in coffee prices, before the basic trend kept on increasing until the present days (appendix 3).

But all of these effects are not just based simply one of supply and demand. The connections between the links of the supply chains that connect producers with consumers have also changed. Nowadays, coffee farmers receive less than 7% of the retail price of coffee in developed world markets; the rest of the percentage until 100%, 93% is paid to importers, packaging firms, roaster and retailers. In part this reflects a structural disparity of commercial power in the global coffee system, whereby six international trading companies control over half of the world coffee exports. In these contexts, developing country coffee growers are in a very weak bargaining position.

## CONSEQUENCES

This downward pricing spiral is affecting infrastructures in coffee-producing countries where they are collapsing. There is no money to fix or repair roads, the cost of trucks is out of reach and distributing the merchandise is definitely a hard task. When small agricultural producers are dependent on some buyer to sale their crops for a large amount of money, slumping prices have dramatic repercussions for those poorest countries who everyday fight against hunger and social vulnerability. In recent years aid agencies have struggled to bring awareness about these human repercussions trying to call the attention of policy-makers. These human-scale dimensions of the crisis should flow into national and regional economies. For a significant number of tropical countries, coffee is the major source of export-earning. The collapse of coffee prices, then, has destabilized the systems of whole national economies. Many of these countries are also seriously in debt to international organizations, and have had to renegotiate or even suspend the repayments of loans. In turn, the resultant debt crisis of developing countries is a major source of financial instability in the world.

As always, the poorest countries are most affected, the business profit is becoming some of the poorest and most vulnerable of the world into extreme poverty, livelihoods of small farmers are being destroyed by international markets beyond their control.

But not everyone is losing in the current scenario. While the cost of the raw material comes in a slump, some companies, particularly multinational companies along with several large coffee retailers, continue earning and being profitable. Their market powers allow them essentially to dictate to their suppliers and take advantage of the lower prices. As always, poorest countries are the most affected, corporate gain is turning over some of the world's poorest and most weak people to extreme poverty: the livelihoods of smaller producers are being destroyed by international markets that are beyond their control.

# SOLUTIONS

It seems clear that one of the solutions to the coffee crisis passes to limit grain production to raise prices in international trade. This would be the theory in the context of the market economy. In practice, it has been tried it last year and received the denial of the Asian countries and Brazil. in oil.

Experts agree that the coffee industry is undergoing major changes in order to recover the price-crisis prices. The entry of Vietnam into the coffee trade had important consequences: the way to produce cheaper.

Alternatives to the coffee crisis are in what some NGOs have called fair trade. If producing countries such as Vietnam has grown 400% in the last decade is because their culture has focused on the logical contribution of new technologies. It is a commitment to diversified organic coffee, coffee quality associated with sustainable development and fair trade outside intermediaries, to improve the price paid to farmers and reducing the supply with further restructuring of the field. An idea that is far from being realized because of the illiquidity of the farmer .

4″The costs of producing differ from country to country, perhaps from 60 to 90 cents for

The worst hits are Latin American countries with relatively high production costs. These countries may try to find ways to cut costs or find niche markets that command premium prices, such as organic or shade-grown coffee that provides ecological habitats. But those options do not help everyone. Many farmers ultimately have to move to other more lucrative products.

In the fall of the current prices, farmers enough eventually be driven out of business, which will produce increased coffee prices again. That means another potential shortage threat in the future, especially for higher quality coffees are more expensive to produce. And this shortage can lead high enough to encourage overproduction, once again.

It is not clear when this damaging cycle will repeat again, or even if it is going to finish. What is clear is that new and better solutions are needed to help the poorest countries that are affected by it.

# CONCLUSION AND RECOMMENDATIONS

In conclusion, the existing circumstances of the world coffee industry represent a crisis of huge human cost. The low prices being received by coffee farmers not only put in danger the livelihoods of people and communities, but add significantly to global inequality and its correlated to financial and political implications.

For another point of view, the crisis also unveils the failures of export-oriented models which curiously most developing countries follow. What it can be learned at this point: what is true for some countries may not be true for anothers. When one country increments its coffee exports, it benefits. But if all countries do the same, then the effects are to produce an over-supply of commodities and to cause prices to fall.

The lives of smallholder farmers become vulnerable by depending on the conditions imposed those who dominate commodity markets, which in any case are structured in ways that concentrated power in a small number of transnational companies.

And at least, some recommendations can be given: Correcting the imbalance between supply and demand by increasing consumer in particular by: improving quality in the world market and promoting diversification to reduce dependency. It is recognized that to ensure market access for products alternative, there must be a substantial reduction of tariffs and subsidies to those who are now protected agriculture in industrialized countries. In addition, support a broad-based rural development to enhance the capacity of local processing and producer associations, and also measures to

improve access to credit and risk management.

Beyond these suggestions, the coffee industry should participate in programs designed to help reducing the effects of price shocks at the farm level. These efforts should include locking roasters in contracts with farmers for the coming years, as a way to motivate farmers to keep on producing coffee, for example, paying more for certain quality coffees. Simultaneously with the efforts of importers, roasters and retailers to create mutually beneficial relationships with farmers, producers have taken steps toward understanding what the market demand for its coffee.

APPENDIX 1

APPENDIX 2

Prices of the coffee market (2003)

APPENDIX 3