COMMODITY RESEARCH

Coffee Fact Sheet

Working Document

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This working document has been prepared by Wageningen UR Centre for Development Innovation for the "From the Islands of Success to Seas of Change" WHAT WORKS WHEN SCALING INCLUSIVE AGRI-FOOD MARKETS? event held on April 11-13, 2012 in The Hague, The Netherlands. The event was organized and supported by the following partner organizations:

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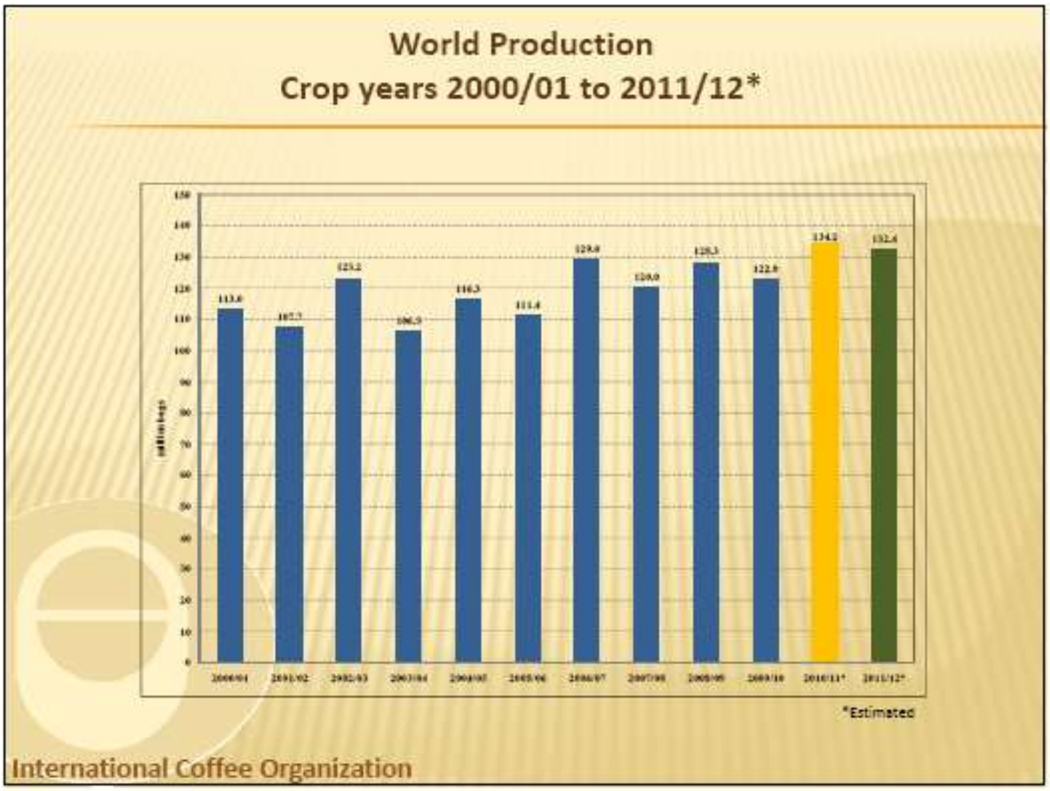
Key Highlights:

- Coffee ranks high among the most important agricultural commodities traded in international markets, in terms of both volume and value.
- A vast majority of the world's 25 million coffee producers are smallholder farmers, who are directly dependent on coffee for their livelihoods.
- Demand outstrips supply. Production has remained below demand due to under-investment, poor production practices, adverse climatic conditions, lack of interest from the next generation of coffee growers, and aging coffee trees.
- The production of sustainable coffee accounted for about 16 per cent (21 million bags) of the global production in 2010/11. The sales of sustainable coffee have grown to 12 million bags, or 9 per cent of total consumption.
- The Dutch coffee sector has collectively expressed the intent to increase the share of sustainably produced coffee to three quarters by 2015.
- Most companies are increasingly involved in certification schemes: but its true impact on farmers' livelihood is not clear.
- Scaling up sustainable production requires the effective implementation of standards, improving access to finance for farmers, increase production, yields and export availability of sustainably grown coffee and mitigating the effects of climate change.

1. Main highlights of coffee production, trade and consumption: Which are the potential and challenges of the sector?

- **Coffee ranks high among the most important agricultural commodities traded in international markets, in terms of both volume and value.** Clearly, coffee growing and processing has proven itself to be a lucrative industry. Yearly, about 120 to 134 million 60-kg bags of green coffee beans are produced in 80 countries in Central and South America, Africa and Asia.[1]
- **Who are the coffee farmers?** Over 100 million people are engaged in producing and processing coffee. A vast majority of the world's 25 million coffee producers are smallholder farmers, who are directly dependent on coffee for their livelihoods. **African countries account for 13 per cent of global coffee production. Ethiopia is the largest coffee producing country in Africa, with 90% of coffee produced on smallholder farms.** Other producing countries where coffee growing is an important livelihood strategy for smallholders include Uganda, Cote d'Ivoire, Tanzania, Kenya, and Rwanda.
- **Global coffee consumption continues to grow at a steady pace, particularly in emerging markets.** Consumption in 2010 is estimated at 135 million bags, an increase of 2.4% compared to 2009. During the last ten years world consumption increased at an average rate of 2.5% per annum.[2] Growth is fastest in emerging markets, such as those in Eastern Europe and Asia, and in the coffee producing countries themselves. In Europe and the United States, consumers are increasingly attentive to quality and origin, and show a growing interest in the economic, social and environmental aspects of coffee production.[3]
- **At the same time production struggles to keep up with demand increase** (in the 2010/11 crop season, total production is estimated at 134 million bags, while for 2011/12 is it is projected at 132.4 bags. Production has remained below demand due to under-investment, poor production practices, adverse climatic conditions, lack of interest from the next generation of coffee growers, and aging coffee trees.
- **The world coffee market is dominated by three very large transnationals - Nestlé, Kraft Foods and Sara Lee**, and a few big coffee roasters like Smucker's, Strauss, Starbucks and Tchibo. The decisions these companies make impact significantly on the overall demand for sustainable coffee. More than half of the top ten roasters are members of the 4C Association. The largest roasters tend to rely heavily upon traders for their supply of coffee rather than dealing directly with producers or producer groups. Trading companies are large players and include Neumann Gruppe (Germany), Volcafé (Switzerland) and ECOM (Switzerland). These three companies together trade 50% of the world's green coffee beans. In recent years, international traders have strengthened their supply network especially, to guarantee a minimum amount of certified coffee to their major clients. Traders are the closest to the farmer and have to secure quality production and volume. These companies have established sourcing guidelines for sustainable coffee procurement.

[1] Tropical Commodity Coalition, Coffee Barometer 2012
[2] International Coffee Organisation, www.ICO.org
[3] Tropical Commodity Coalition, Coffee Barometer 2012



Main challenges of the sector:

- Price fluctuations
- Exchange rate fluctuations
- Access to finance
- Poor extension services
- Poor research/development in the sector
- Poor organization of farmers
- Poor marketing systems
- Poor infrastructure
- Increasing poverty in rural areas
- Increasing costs of production
- Low productivity
- Climate change
- Crops irrigation

The key problem for African producing countries is decreasing production and productivity. There is a urgent need to increase yields. While Brazil will expand its coffee production and Vietnam will remain quite stable, many African countries are reducing their production. There are very few origins in Africa to source from. In Cameroon, for instance, over the past 25 years, production of coffee declined dramatically - From a peak of 120,000Mt in the mid-eighties, the country currently produces only 34,000Mt per year. The reasons for the decline in volume are multiple. In some cases this is due to diseases of coffee berries, in other cases issues reside at governmental level and are hard to address by a single project, others are easier to influence, such as lack of access to services by farmers.[4]

Production: 10 leading producers
(Volume in 000 bags - % of world production)

	2010/11	2011/12*	% change
Brazil	48 095	43 480	-9.6
Vietnam	19 467	18 500	-5.0
Ethiopia	7 500	9 804	+30.7
Indonesia	9 129	8 750	-4.2
Colombia	8 523	8 500	-0.3
India	5 033	5 370	+6.7
Peru	3 976	5 000	+25.7
Mexico	4 850	4 500	-7.2
Honduras	4 326	4 300	-0.6
Guatemala	3 950	3 450	-12.7

*Estimated

International Coffee Organization

2. How is inclusiveness tackled? Which approaches and models are demonstrating (elements of) success? What are key incentives in the approaches that drive that success?

In the face of these challenges many initiatives have been launched to build inclusiveness in the coffee sector for instance by:

- Reinforcing farmer organisations through which farmers have better access to local markets (see box 1)
- Providing services such as technical advice and credit
- Promoting and supporting activities generating complementary earnings
- Supporting extension services to promote good agricultural practices
- Support research/development
- Improving the marketing systems
- Support programs for the development of domestic market
- Facilitating farmers' access to finance
- Improving conditions for use of price risk management tools

[4] Interview to Don Jansen, Program Manager Douwe Egberts Foundation

Box 1. Strengthening farmers' organisations

Since 2002, Sara Lee is the main sponsor of the Douwe Egberts (DE) Foundation, which has a budget of 1.2 million euro to improve the living and working conditions of small coffee and tea farmers in countries of origin. The main objective of the DE projects is to get producers organized and implement sustainable farming and processing practices. If successful, producers will improve the yield and quality of their product, have access to certification and therefore can command better prices. Producers benefitting of the support of the DE foundation do not have obligations to sell to Sara Lee but they can take advantage of different market options. The DE foundation aims in fact to identify areas with greater potential, support farmers to gain better access to market while leaving them their independence to sell to the best buyer. DE programs have a business orientation- overall, they seek to help farmers professionalise their operations.

An interesting example in this respect is offered by the first project supported by the DE foundation, called: "Better quality, more efficiency, certification and direct market access for small-scale coffee producers in Luwero, Uganda". Small-scale farmers, particularly in Uganda, produce and sell such low volumes of coffee that individually they have very little influence on how their coffee is traded. Addressing the matter of small volumes is crucial for improvement to happen in places such as Luwero. In the absence of competition from larger traders, the village-based traders have a captured supply and can afford to offer low prices or charge high interest rates if they buy coffee in advance of the harvest. Addressing the issue of low volumes was done in 2 ways: Improving productivity and form so-called farmer-owned and managed Depot Committees (DCs) where producers sell their coffee through a group. The second step was crucial as it opened up local markets to competition. With aggregated volumes Depot Committees suddenly became very interesting business partners to various traders. As a result, participating producers obtain around 20% higher prices than non-participating producers because of better quality coffee, certification and lower transaction costs because of bulking their coffee. Project farmers realize on average 30% higher coffee yields per hectare. Training has been carried out for DCs to take a pro-active role in the certification process. A third phase is now being initiated. In partnership with Ibero, the EU and the Bill and Melinda Gates Foundation, DE foundation aims to assist the 24 DCs that were formed in the previous phase to become part of a larger farmer-owned and eventually farmer-managed company called the Uganda Coffee Farmers Alliance (UCFA).

Another interesting example is the one of the Cooperative Agraria Cafetalera Sostenible Valle de Ubiriki (CACSVU). There the two successful ingredients for building inclusiveness were: **Building confidence** and **Transferring of knowledge/expertise to increase productivity and provide market linkages.** This was achieved by coupling the work of the DE foundation which knew needs at producers' level with the commercial interest of Sara Lee. New cooperatives generally have difficulty to enter the market. Without an established reputation importing companies are hesitant to do business with new sellers in general and, for various reasons, cooperatives in particular. From 2005 to 2007 Decotrade AG, the buying company of Sara Lee, provided a pivotal role by buying significant volumes of CACSVU coffee. The year 2008 marked a turning point. Coffee volumes more than doubled from 4,000 bags in 2007 to 10,000 bags and CACSVU sold large volumes to the higher end of the market, with companies such as Starbucks and Panamerican Coffee. All together CACSVU sells regularly to 8 different EU and US-based coffee companies. All CACSVU coffee is certified. Price differentials have changed significantly during project implementation. In 2003 coffee from the area was trading at 66USD/Mt below NY-C (the world market indicator price for Arabica coffee), in 2008 the cooperative coffee was trading at 661USD/Mt over. Three main reasons explain this vast improvement: Quality improvement, better access to the higher end of the market and lastly certification premiums.

Source: Interview to Stefanie Miltenburg, Director International Corporate Social Responsibility, Sara Lee International b.v. and to Don Jansen, Program Manager Douwe Egberts Foundation.

Many companies started engaging in sustainability efforts to react to consumers' pressure blaming big companies of paying very low coffee prices to farmers in origin countries. However, according to some experts "the intrinsic motivation that the sector itself needs to transform to go to mainstream sustainability is not fully there yet. Some supply chain parties seem to expect sustainability programs to do it for them rather than with them. Here, the cocoa sector gives a good example: many initiatives are taken up in order to help farmers make the move to more sustainable farming." [5] Indeed in cocoa there is a strong business case for sustainability to go mainstream, given the current shortage of supply, in turn a series of companies (e.g. Cargill, Mars) are making important efforts. As in the words of UTZ CERTIFIED, the "coffee sector has always been a leading sector and cannot benefit from the learning curve of others".

3. What is the scale of impact that is being achieved, how does that compare with what is needed, where could it go?

The world market share of sustainable coffee has grown rapidly in the past few years, in fact, at a much faster rate than conventional coffees. The production of sustainable coffee is now reaching significant levels of market penetration, accounting for about 16 per cent (21 million bags) of the global production in 2010/11. The sales of sustainable coffee have grown to 12 million bags, or 9 per cent of total consumption.[6]

In recent years, major coffee roasters have made serious commitments to increase their purchasing of sustainable coffee. The Dutch coffee sector has collectively expressed the intent to increase the share of sustainably produced coffee to three quarters by 2015.

In August 2010, **Nestlé** launched the Nescafé Plan which contains a set of objectives which will help the company to further optimize its coffee supply chain. In addition to the CHF 200 million invested over the past ten years, Nestlé will invest CHF 500 million in coffee projects by 2020. By 2015, Nestlé has committed to double the amount of Nescafé coffee bought directly from farmers and their associations, eventually purchasing 180,000 tonnes of coffee from around 170,000 farmers every year. With the support of the Rainforest Alliance and the 4C Association, all directly purchased green coffee will meet the internationally-recognized 4C sustainability standards by 2015. In addition, 90,000 tonnes of Nescafé coffee will be sourced according to the Rainforest Alliance and Sustainable Agriculture Network (SAN) principles by 2020.

For the 2010-2015 timeframe, **Kraft Foods** has set some ambitious goals around transportation and agricultural commodities. One of them is to increase sustainable sourcing of agricultural commodities by 25 per cent, including the commitment that all of the company's European coffee brands will sustainably source 100% of their coffee by 2015. The company will meet its agricultural goal through third-party certification groups like Fairtrade, Rainforest Alliance and 4C. In 2010, the company

[5] Interview to Han de Groot and Daan de Vries, UTZ certified
[6] Tropical Commodity Coalition, Coffee Barometer 2012

purchased nearly 50,000 metric tons of Rainforest Alliance Certified coffee, more than half of which went to their EU coffee business.[7]

In early 2011, **Sara Lee** announced a new five-year initiative to boost its sustainable commodity program. In the past five years Sara Lee has become the world's largest buyer of UTZ CERTIFIED coffee thanks to cumulative purchases of more than 110 million kilos of the commodity. The company has committed to more than triple that amount in the next five years and purchase at least 350 million kilos across all its markets and product segments. The aim is to have more than 20% of its entire annual coffee volume certified sustainable. The company estimates its sustainability investments can deliver to coffee farmers, their associations and representatives up to $100 million of income over and above what they would have earned by selling uncertified coffee beans in the open market.

However, despite these serious commitments to increase their purchasing of sustainable coffee, **the key question for the future is whether the actual volume of sustainable coffee produced in origin countries will meet the commitments.** The lack of substantial volume of sustainable coffee is an important issue. The situation of course varies depending on the countries: Vietnam for instance is progressing at a much higher speed than Uganda in producing sustainable coffee.

Which is the impact of standards? Conformance to a coffee production standards system can give participating producers opportunities, for example, training in Good Agricultural Practices, access to new markets, and enhanced efficiency and revenues. However, the business case for certification only applies to farmers who already have a basic level of organization and education. As indicated earlier, only 9 per cent of coffee produced worldwide is certified. Certification so far has helped mostly those farmers that have relative smaller distance to the sustainability codes, they may be better organized, have good access to training or have fewer environmental challenges to deal with, etc. The greatest challenge now is for certification to reach the less advanced ones and to make intrinsic benefits of certification more visible for farmers.[8]

In order to provide less advanced farmers with a solid basis to engage further in certification, the 4C Association has defined the 4C Code of Conduct, the baseline standard for sustainability in the coffee sector. The Code comprises 28 social, environmental and economic principles for the sustainable production, processing and trading of green coffee. Differing from certification systems which are comprehensive in their nature, 4C Units start at a simple baseline level and are expected to continuously improve social, economic and environmental practices over time to reach desired sustainable conduct. 4C allows the verification of farmers to identify what it takes for them to be certified. It is crucial however that Business does not see 4C verification as an end it itself but more as an improvement process. That is why the 4C Association works with independent third-party verifiers to make sure that its members have implemented mechanisms to both measure their improvement process and to assure that they meet a baseline level of sustainability.

[7] Tropical Commodity Coalition, Coffee Barometer 2012
[8] Interview to UTZ CERTIFIED

In general, some actors in the sector are concerned regarding the lack of information on the actual impact of certification on farmers' livelihood. **Indeed their true impact – especially on famers' incomes and transfer of skills is not clear yet**. According to the 2012 TCC Coffee Barometer, a review of the scope of main standards reveals some general trends and commonalities. Most economic criteria revolve around product quality and minimum wage requirements. Living wages[9], price premiums (only explicitly included in Fairtrade standards) and written contract requirements are rare. At the moment it is easier to check for things that farmers do not do rather than establishing specific criteria on productivity and income (e.g. does the farmer receive the right percentage of coffee price?). As one standards system after another has to scale up rapidly to meet the demands of mainstream market channels, understanding their actual impact becomes more important. Recent impact research highlights the limited number of studies able to clearly demonstrate positive or negative impacts of coffee production standards on the coffee smallholders. COSA's Preliminary Cost Benefit Analysis of Sustainable Practices in Coffee[10] summarizes its main findings as follows: Certified farms generally appear to be better off economically (assessed by net income) than their conventional counterparts, but the gap seems to be small. Many of the environmental parameters measured (such as biodiversity and shade coverage), show little evidence that certification had a significant effect on the environment over the first two years of certification - possibly due to the lag time between implementation of practices and environmental impact (e.g., planting of shade trees or constructing erosion barriers). Certified farms appear to have distinctly better occupational health and safety practices, employee relations and labour rights performance[11].

4. What are the roles and responsibilities of business, government, civil society and knowledge institutions in the scaling efforts?

Upscaling and resolving the structural deficiencies in the sector requires an active and coordinated action from all relevant stakeholders. The Sustainable Agriculture Initiative Platform (SAI Platform) established in 2002, by Unilever in collaboration with Nestlé and Danone is an example of a safe space where companies can share experiences and concerns on sustainability. However, according to some key coffee players interviewed, traders left quite soon the SAI platform given that they are very competitive in their activities at farm level, therefore at the moment there are mainly roasters involved in SAI, with each of them having different strategies. Some invest more in certification (Sara Lee), others like Nestlé have their own factories (more supply chain oriented), Kraft Food does not engage in co-investment with partners to set up projects but focuses on its own supply chain. Today, the activity of the SAI Working Group that sees all its partners involved is the issue of carbon footprint associated with green coffee production.

[9] Minimum wages tend to be low for agricultural workers. Many casual, temporary or seasonal coffee plantation workers are paid at least in part on a piecework basis, for instance, per kilo of crop picked, row-length weeded, or hectare sprayed. If rates are low, this can lead to people working very long hours to earn a subsistence income. Coffee standards initiatives all require at least the legal minimum wage and remunerated overtime, but in many cases one worker's wage does not stretch to meet the family living needs.

[10] Giovannucci, D. And Alia (2008) Seeking Sustainability: COSA preliminary analysis of sustainability initiatives in the coffee sector. COSA.

[11] Tropical Commodity Coalition, Coffee Barometer 2012

In general, some interviewees lament that as for now there is not yet a strategic thinking at industry level for what concerns the responses to big challenges that the coffee sector need to face. In addition, many of the problems in the coffee sector today lie in government's hand in countries of origin. This means, in turn, that the private sector will not be able to transform the coffee sector by itself. There is a need of co-investment (local governments should invest in improving infrastructure and providing extension services for instance).

While in Africa government's commitment is limited, in other context, there are much more supportive government's policies and strategies. In Vietnam, for instance, there is a national coffee strategy since 2005. In Colombia, the government delegated all responsibilities related to agricultural research, production promotion, and export market development to the Colombian Coffee Growers Federation (FNC). The FNC currently represents more than 550,000 producers, most of whom are small family owned farms, their participation in the cooperative allows them to enjoy higher prices for their coffee. The government set up, already in 1934, a levy on exports, to be administered jointly by the national government and the producer association. Revenues from this levy are used to promote production, through credit, to build marketing and export infrastructure, and to finance a coffee research station.

There is an increasing recognition by key players to move beyond the use of standards and labels and to create an overarching, holistic strategy needed to transform the coffee sector. Along this line, IDH and a series of partners in the coffee industry and standard setting organizations are currently designing a coffee program to further increase sustainable coffee production in a pre-competitive manner and make coffee farmers more resilient in coffee volatile market. Four main hurdles have been identified for the sector: mitigating the effects of climate change, improving access to finance for farmers, implementing effectively standards embedded at local level, increasing production, yields and export availability of sustainably grown coffee.

5. What are the constraints and opportunities to further upscaling?

As designed in the IDH coffee program, scaling up sustainable production requires the effective implementation of standards, improving access to finance for farmers, increase production, yields and export availability of sustainably grown coffee **and mitigating the effects of climate change** (see box 2).Some useful lessons are emerging from successful inclusive business models implemented by various actors.

Box 2. New initiatives to respond to climate change challenges have improved coffee farmers' productivity and income: lessons learned for scaling them up.

Coffee production depends on stable climatic and environmental conditions. Rising temperatures are impacting negatively on coffee quality and are triggering, for example, more and new pest and disease incidents. Changes in rainfall patterns are disrupting flowering cycles and erratic rains are impeding maturation of coffee berries affecting quality and quantity. As stated by the International Centre for Tropical Agriculture, climate change is affecting all coffee actors along the supply chain and needs cooperation and joint efforts to find effective responses. This was the rationale behind a project assisting coffee producers in adapting to climate change: Climate Change Adaptation and Mitigation in the Kenyan Coffee Sector (Sangana PPP). The project was launched by several partners, including Sangana Commodities Ltd, the Kenyan subsidiary, of the ECOM Group, GIZ, World Bank and the 4C Association, a multi-stakeholder organization of actors committed to addressing the sustainability issues of the coffee sector in a pre-competitive manner. The project started in 2008, targets 16000 coffee farmers and provides training to producer organizations on climate change issues and on good agricultural practises (efficient fertiliser's use, soil management, coffee picking, coffee processing, integrated pest management). The evaluation carried out at the end of the project in 2011, shows very positive impacts in terms of productivity, quality, and livelihoods. Overall production has increased by 15 per cent, some farmers have doubled/ tripled their yields. Due to increased quality coffee, prices paid to farmers have improved from 35 Kenya Shilling in 2009 to 68 Kenya Shilling in 2010, and 116.5 Kenya Shilling per kg cherry in 2011. In turn, farmers who had abandoned their coffee farms have started to take it up again. The youth is gaining interest in farming again. Sangana Commodities Ltd is thinking about rolling out the approach to other East African countries and maybe even trialing it in the cocoa sector. Some key lessons learned emerged from this project which should be taken in consideration when scaling it up in the region or in other commodities: Producers have their own coping mechanisms and have to be involved in finding solutions, i.e. adaptation options. Adaptation has to be a mix of scientific and participatory approaches. Local, regional and national networks are necessary for successful adaptation. Funding for adaptation is one of the biggest challenges.

Source: Climate Change Adaptation and Mitigation in the Kenyan Coffee Sector (September 2011)- Guide Book - Sangana PPP - http://www.4c-coffeeassociation.org/

Effective implementation of standards: The differing existing standards confuse producers, they are not aligned, are sometimes inefficient and very costly to comply with. Efforts are underway to promote the harmonisation/alignment of standards. In particular, it is important to organise joint auditing (e.g. so that farmers that are multi-certified can do one audit). In 2011, the market demand is driving cooperation among standards. 4C has changed its business model towards a demand-driven approach, matching market demand with a new base of suppliers. Rainforest Alliance and UTZ CERTIFIED intensify cooperation with FLO, because they need to include more smallholder cooperatives in their supplier base to be able to grow rapidly.[12]

The opportunities for scaling up lie also in finding new sources of production. As of now the supply of sustainable coffee remains highly concentrated among a small number of countries, with two-thirds of the supply coming from the more organized and developed Latin American producers, while African countries produce very limited quantities of certified coffee. Next to including more smallholder cooperatives, standards systems must find ways and means to pull in more coffee producers in Africa and Asia.[13]

To respond to the enormous financial needs of the coffee sector, there has been seen a surge of inclusive financial models: In Ethiopia, IFC provided a $10 million risk-sharing facility to local Nib International Bank to encourage the bank to lend to coffee cooperatives that receive training on better production and processing practices by the U.S. nongovernmental organization Technoserve. IFC's guarantee enabled financing to 45,000 small coffee farmers to purchase milling equipment that has led to significant improvements in the quality of coffee and 50 per cent higher prices. IFC will replicate this approach in other countries and for other commodities that suffer from lack of financing due to perceived high lending risk by local banks (see box 3). Other examples of financing mechanisms

[12] Tropical Commodity Coalition, Coffee Barometer 2012
[13] Interview to Ahold Coffee Company and Tropical Commodity Coalition, Coffee Barometer 2012

which had a successful uptake and can provide useful lessons learned for other commodities and countries include: Trade finance to local coffee cooperatives in Kenya and Uganda by Rabobank and warehouse receipt finance to coffee growers in Tanzania. Warehouse receipt finance is a form of secured lending to owners (farmers, traders, processors) of non-perishable commodities such as grains and coffee that are stored in a warehouse and that have been assigned to a bank through warehouse receipts. Warehouse receipts give the bank the security of the goods until they have been sold and the proceeds collected. With the support of Rabo Development, warehouse receipt financing has been successfully developed in the coffee sectors in Tanzania in partnership with the National Microfinance Bank (NMB). NMB is looking to extend WHR financing to other sectors (e.g. SF seeds). It is crucial to integrate these financial tools with innovative risk management tools (e.g. futures contract, combining warehouse receipt financing with put options)

Box 3. NIB's inclusive Business Model

Drivers of inclusiveness for NIB: - Underserved but significant business opportunity in lending to the Ethiopian coffee sector, - NIB's commitment to support small farmers and promote sustainable growth in the coffee sector, - Need to mitigate risk in lending to the agriculture sector in Ethiopia.

NIB is one of Ethiopia's fastest-growing private banks and is the market leader of the private banking sector in lending to agriculture. To maintain and grow this position, the Bank aims to expand its reach into rural areas and to continue to strengthen its risk management practices. In support of these goals, NIB is providing access to finance for cooperatives of smallholder coffee farmers as part of the **Coffee Initiative in East Africa**. The Coffee Initiative is a $47 million program funded by the Bill and Melinda Gates Foundation and managed by the US-based non-governmental organization TechnoServe. Its goal is to increase the incomes of coffee farmers in Ethiopia, Kenya, Rwanda, and Tanzania by increasing the quality and quantity of coffee they produce. In Ethiopia, participating cooperatives range from 300 to 500 smallholder farmers who average approximately three-quarters of a hectare of land each. Nearly 40% of NIB's bank branches are outside of Addis Ababa, providing a foundation on which to reach these farmers. Beyond physical access, **the Bank's inclusive business model hinges upon partnerships for financial risk-sharing and farmer capacity-building**. For financial risk-sharing, NIB entered into an agreement with IFC establishing a three-year, up to $10 million facility to provide working capital loans to cooperatives working with TechnoServe. The facility offers up to $250,000 per cooperative, disbursed against cash flow requirements and collateralized by coffee stocks. The program is designed such that cooperatives should be able to repay their working capital loans within one year entirely through the sales of their coffee. However, IFC will cover up to 75% of any credit losses NIB incurs. In order to qualify for the working capital loans, cooperatives must have **the capacity to produce high-quality washed coffee** that earns a premium in the market—the product of using the wet milling process to remove the skin and pulp from coffee cherries, and then wash and dry the coffee beans. During the coffee harvest, the cooperatives use the working capital from NIB to purchase farmers' fresh coffee cherries and process them through the wet mills. Farmers benefit by receiving a competitive price from the cooperative at the time of sale and then a second payment, or dividend, out of the cooperative's net profit (calculated after all exports and debt payments are complete). Combining the first and second payments, farmers typically receive a share of two-thirds of their cooperative's gross revenues. Gross revenues for the 2010 harvest averaged $100,000 but in some cases exceeded $300,000 per cooperative. **TechnoServe's role is to help the cooperatives make effective use of the wet milling process to produce higher value-added coffee**. TechnoServe provides technical assistance in operating and managing the wet mills, as well as close collaboration in the business development and governance of the cooperatives. For instance, it helps them organize and register formally, provides their leaders and farmers with training and technical support, and creates linkages with other players along the coffee value chain. One TechnoServe business advisor works closely with two to three cooperatives at a time, and coordinates local specialists that can provide additional training and agronomy services. In addition, TechnoServe helps the cooperatives negotiate and export their coffee directly to buyers instead of working through intermediaries. Over the life of the risk-sharing facility, the volume of coffee processed by borrowing cooperatives is projected to increase to 4,000 metric tons with an increasing share sold as high-quality—a strong indication that they will be able to repay the loans they take out. Furthermore, TechnoServe's capacity-building is designed to help build cooperatives that are sustainable after the organization phases out its assistance, representing potential repeat business for NIB. In 2010, NIB made working capital loans to 62 cooperatives made up of 45,000 smallholder coffee farmers. With TechnoServe's support for the wet mill model, the cooperatives produced and sold high-quality, washed coffee directly to 12 international buyers in Europe and the United States. They received on average 40% ($0.75 per pound) more than they previously received for low-quality, unwashed coffee, translating into a total of $1.5 million in added revenues. Over 1,500 full- and part-time wet mill jobs were created. About 63 washing stations have been created. Given the good result so far the Bill and Melinda gates foundation has renewed funding for an additional 4 years. Lessons learned: need for competition (Farmers can sell coffee to the cooperative or to a trader), Ownership (farmers can buy equipment with 20 per cent equity contribution -they should take a loan not a grant). Transparency (Technoserve helps creating more transparency in the market, in supporting the negotiations with the buyers).

Source: IFC (2011) Inclusive Business Models — Guide to the Inclusive Business Models in IFC's Portfolio and interview to Carl Cervone (Technoserve)

Box 4: ECOM'S INCLUSIVE BUSINESS MODEL

DRIVERS FOR ECOM'S INCLUSIVE BUSINESS MODEL: • Need to ensure stability and security of coffee supplies, • Market demand for high-quality, certified coffees and related sales premiums and • Company vision to scale up its certified coffee trade. On the financing side, ECOM is providing seasonal credits to its coffee suppliers in Mexico, Guatemala, Nicaragua, Honduras, and Costa Rica. These pre-payments finance the farmer throughout the production cycle, supporting the purchase of inputs like fertilizer, the maintenance of the coffee plants, and harvesting. On the technical assistance side, ECOM works with rainforest Alliance and CIRAD in a partnership facilitated by IFC to improve farmer productivity, sustainability, and eligibility for certification through training of trainers and farmer workshops. In addition to the financing-technical assistance combination described above, the participation of a high-value coffee buyer like Nestlé Group's Nespresso is critical to ECOM's inclusive business model in Central America. Nespresso's participation includes money to co-finance, with IFC, the roles of rainforest Alliance and CIRAD. This sends a strong signal to farmers about the company's intention to purchase high-quality, sustainable coffee at premium prices and allows ECOM to work with its farmers to plan in advance the quantities that are required. This signalling is important as farmers decide whether or not to invest in the improvement programs they need to meet Nespresso's strict quality and sustainability criteria. Depending on market conditions, premiums paid for certified coffee can be significant to the growers. As of 2008, 20% of ECOM's coffee was sold as certified. The company aims to increase this figure to 50-80% over time. This will be possible only if the smallholder farmers in its supply chain can consistently produce certified varieties in the necessary quantities, making the availability of smallholder financing and technical assistance key to the company's long-term vision. **The business and development results of ECOM's inclusive business model are intimately linked. As smallholder farmers are reached with financing and technical assistance, they enjoy greater productivity, security, and earning potential. Meanwhile, ECOM strengthens and secures its supply chain, expands its access to high-quality, certified coffees, and captures the premiums they bring.** By June 2009, ECOM had purchased 481,606 bags of certified coffee in the three years since the model was established, representing a premium of $3,692,000 paid to smallholder farmers in Central America. This has been made possible through $17.4 million in seasonal financing to 14,149 smallholder farmers and technical assistance that has enabled 10,145 farmers to work toward the certification and quality standards of Nespresso AAA, FLO-Fairtrade, and Nestec 4C. An additional 3,282 farmers have improved their productivity through training in management, pruning techniques, and the benefits of hybrid plants. **These results are encouraging and point**

to a greater impact potential as ECOM estimates it works with about 125,000 growers in Central America.

Source: IFC (2011) Inclusive Business Models — Guide to the Inclusive Business Models in IFC's Portfolio and interview to Carl Cervone (Technoserve)

Author: Lucia Wegner, Sr Development Economist, Associate consultant, Wageningen UR Centre for Development Innovation, email: lucia.wegner@wur.nl, March 2012

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- Carl Cervone, TechnoServe/Ethiopia - Coffee Initiative
- Han de Groot, Executive Director UTZ Certified
- Daan de Vries, Field Director, UTZ Certified
- Margo Zuurveld van Oosterom, Manager Buying and Sourcing, Ahold Coffee Company
- Stefanie Miltenburg, Director International Corporate Social Responsibility, Sara Lee International b.v
- Don Jansen, Program Manager Douwe Egberts Foundation