SUPPORTING FARMERS IN A VOLATILE COFFEE MARKET

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THE CONTEXT

The market price for coffee fluctuates daily – there are times when the price is 'up' but more often, times where the price is in a downward trend. Last year when coffee prices fell below $1.00 there was an outcry to 'do more' and of course, we agree. Unfortunately, this is not something new – coffee has a history of a boom and bust culture[1]. The C price, fluctuations in production in places like Brazil, Vietnam and Colombia, currency exchange rates and all the speculation related to the trade has wreaked havoc on farmers who are trying to keep their head above water in trying times. This constant uncertainty threatens the long-term supply of coffee as farmers begin to seek income alternatives. Given the current price crisis in coffee, many professionals are asking – What should we be doing to help farmers?

ACTIONS THAT CAN HELP FARMERS WEATHER THE CRISIS

This document provides professionals working in coffee sustainability or development an overview of important considerations when purchasing coffee. Our aim in releasing it is to stimulate more discussion within corporations on opportunities for enhancing the economic stability of coffee farmers in their supply chains.

So, where can you start? Here are a few ideas:

INCREASE YOUR KNOWLEDGE OF THE COSTS A FARMER INCURS TO PRODUCE COFFEE:

- ***Request cost of production data from supply chain partners*:** Understanding the average cost to produce coffee across different coffee sourcing regions enables the buyer to determine pricing based on actual costs rather than relying

[1] https://www.nytimes.com/roomfordebate/2011/03/09/coffee-the-new-shaky-commodity/a-boom-and-bust-culture

on the C market as the universal benchmark. When requesting this information make sure to understand the level of on-farm processing taking place across countries and the type of product delivered (i.e.: cherry, parchment, green). To best compare costs, the cost of production should be calculated to average cost per quintal, kilo, or pound of cherry, parchment or green. A starting point to understand cost of production across coffee origins is the Fair Trade USA "Cost of Sustainable Production" report and the Caravela article published in the Perfect Daily Grind.

UNDERSTAND THE ACTUAL PRICES PAID TO FARMERS WITHIN YOUR SUPPLY CHAIN:

- ***Request farm gate price data from supply chain partners:*** The price agreed in a contract between a buyer and seller (i.e.: roaster and cooperative) is not always the price that is paid to the farmer (i.e.: farm gate price). Requesting economic transparency on farm gate prices is important to ensure that fair prices reach the farmer and do not remain at the coop / trader level. Similar to when requesting cost of production, the unit being purchased (kg/lb of cherry, parchment or green) must be understood. Understanding the farm gate price can be a powerful tool when considering pricing across a supply chain.

- ***Check if there is a regulated farm gate price in countries where you source***: Some producing countries (ex: Rwanda) set a minimum price for coffee purchased from a farmer on an annual basis. This reduces the risk of unfair practices by increasing transparency of prices paid to farmers. Depending on the country, the price could be fixed or simply a suggested reference point.

- ***Check the living income reference price***: Fairtrade International is undertaking a living income analysis for multiple coffee origins that could be used by the industry as a reference point for coffee prices. The calculation takes into consideration 1) the cost of a nutritious low-cost diet, 2) cost of basic decent housing, 3) other essential expenses for education, health care, clothing and transportation, and 4) provision for unexpected events. Using such a benchmark removes the need to rely solely on the C-market for the starting point for pricing.

EXPLORE OPPORTUNITIES TO BETTER LEVERAGE MARKET MECHANISMS TO HELP STABILIZE FARMER INCOMES:

Coffee sourcing is complicated, particularly given that it can be bought on the exchange and/or though formal relationships built between a buyer and a farmer. Futures contracts, forward contracts, options, long-term pricing, minimums, etc. are mechanisms used to solidify relationships between the buyer and the farmer and may offer some opportunities for farmers (and other supply chain members) to mitigate risk. Here is a brief overview of how these tools can benefit farmers.

- ***Futures contracts*** allow farmers to lock in a future price (determined on the exchange) in advance of delivery, essentially hedging their risks based on speculation of the future price of coffee. When this trading instrument is used properly, it could limit losses and reduce volatility for farmers.

- ***Forward contracts*** are private agreements that enable the farmer to know the price they will receive for their coffee prior to delivery, which they may be able to leverage into credit.

- ***Long-term pricing*** enables the farmer to know the price they will receive for their coffee over a longer time frame and thereby better plan and re-invest in their farms.

- ***Premiums based on quality or environmental or social performance*** pay farmers prices that are above the market value based on performance, which can help buffer them against some market volatility.

To have a thoughtful and productive discussion on ways to improve purchasing practices that benefit a company and their supply chain, understanding basic market mechanisms is a must. You can check out more in the book "Dear Coffee Buyer" or by reading "The Coffee Guide" published online by the International Trade Centre.

INVEST IN BUILDING THE CAPACITY OF FARMERS TO UNDERSTAND AND LEVERAGE MARKET INSTRUMENTS:

Price risk management training teaches farmers and cooperative managers how to develop financial strategies that use market tools (i.e.: hedging strategies, contracts, etc.) to reduce price volatility. This sort of knowledge is key to empower farmers to have a voice in the market. Several organizations offer online and in-person training. For example, Oikocredit, Inter-American Development Bank and Fair Trade USA are offering price risk training management to farmers in 16 coops in Honduras, Guatemala, Nicaragua, Colombia and Peru. The World Bank also offers an online, self-paced coffee price risk management course open to the public.

These are simply a few mechanisms that can help you get started in developing a strategy that enables your business and the coffee farmers you rely on to weather market crises like the one we are currently in. Many Challenge partners are working to address this topic, and we encourage you to engage in and leverage the work of Fair Trade USA, Fairtrade International, the Specialty Coffee Association, the International Coffee Organization and others are working on. We also encourage you to share your experience to enable economic development through coffee in producing countries.

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SUSTAINABLE COFFEE CHALLENGE