Statement by
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to the ICO World Coffee Conference

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AS PREPARED FOR DELIVERY

Mr. President,
Excellencies,
Ladies and Gentlemen,

Permit me at the outset to thank you, Mr. President, for your invitation to participate in this Conference, which brings together the widest possible range of stakeholders working with and in the coffee industry.

I will be talking mainly about the impact of commodities, and in particular coffee, on the economic and social development of poorer developing countries. This should be the goal of all economic activity: to achieve a level of development that is socially beneficial, environmentally harmless and economically sustainable. In addition, I will highlight several areas where the current economic crisis is having a transformational effect on the commodity economy.

Commodities like coffee provide many economic opportunities for developing countries, but also expose them to several risks. Historically, the terms of trade for commodities compared to those for manufactured goods have been in decline, a trend that coffee growers and exporters can confirm. For many commodities, there are fewer opportunities for productivity gains than in manufacturing, and for many exporters it has been relatively more difficult to add value to their primary product and move up the value chain. Although there are examples of where this is changing, in many cases countries have not reaped the full potential from their commodity endowments and have been dependent on rising demand in importing countries to maintain their earnings and the terms of trade.

For developing-country commodity exporters in general, reliance on external markets increases their vulnerability to fluctuations in international prices. In the coffee industry this is less so for the biggest exporters – Brazil, Viet Nam, Colombia – where coffee represents a relatively small share of overall exports. But for producers such as Ethiopia, where coffee represents close to 40% of exports, the country is potentially more vulnerable to price shocks and balance-of-payments problems. Even for the larger exporters, there are still important questions to be asked about the diversification and development of both products and markets – in particular, the growth of the domestic market and the capturing of higher-value processes and coffee products.

The development of domestic markets for all exporters has been brought into focus since the start of the current global economic crisis, which has caused the most precipitous fall in international demand since the Second World War. On top of that, it has also undermined policies oriented towards export-led growth. This is particularly relevant to developing countries, which often have a large share of exports in their GDP, and it is even more relevant to commodity producers that are dependent on foreign demand. For countries dependent on export markets for their growth, the crisis has been an incentive to look at developing domestic markets, as well as markets within the region. For coffee, global consumption rates are much lower in producer countries, suggesting there is great potential to develop domestic consumption in these countries.

The economic crisis has also exposed the vulnerability of commodity exporters to speculative activities. In the second half of 2008, as the sub-prime market collapsed, speculators looked for new investment opportunities in different asset classes. Commodities became the next target, and a series of price spikes in agricultural and energy commodities were fuelled in part by speculative positions in several derivative markets. More recently, we have seen sugar become the target of speculative activity; and in the past, coffee has experienced similar pressures. The problem of speculation for producers is that it creates false price signals and expectations about future production which ultimately destabilize supply and can lead to a price collapse.

Whilst many financial and market-based hedging products can help producers shed some of the risks of production and price volatility, they can also be distorted by excessive speculation. It is questionable whether these excesses – which can have such disastrous consequences for the livelihoods of farmers – should be permitted to continue. This is especially pertinent for the coffee industry, which in many producing countries is characterized by smallholder production.

Over the past 30 years, the deregulation and lack of transparency in the financial and commodities markets has contributed to increasing volatility in commodity prices. It is important that the monitoring and regulation of speculative activities now be tightened in the wake of both the economic crisis and the recent erratic movements in agricultural and energy prices. The proposals currently being put forward for the international control of speculative activities, mainly in currencies and financial products, are welcome. However, they need to be coordinated across countries and sectors to ensure that speculators cannot exploit opportunities for arbitrage, either between asset classes or between countries and regions.

Such an agreement, targeting the distortional effects of large-scale speculation in different areas, is absolutely crucial for stability in commodities markets, and for creating a wider framework for globalization that has the potential to deliver rising living standards for all.

In addition to changes in product and market orientation, and speculation, another feature of the current global economic crisis that could have a far-reaching impact on commodity production is greater recognition of the State's role in supporting economic activity. We have recently seen the State come to the rescue of the banking and manufacturing sectors as well as provide countercyclical fiscal stimulus to shore up demand in many countries. But the State's role should extend beyond the provision of safety nets for markets, industry and employment.

There was, unfortunately, a rolling-back of the State in the agricultural sector and in agricultural marketing in particular, in most coffee-producing countries within the context of macro-economic policy reforms of the past three decades. In the wake of the current crisis, this trend needs to be addressed. Technical support is particularly needed to help producers and producing countries move forward in such areas as the implementation of better management and marketing practices associated with quality; technical and sustainability requirements; enhancing opportunities for pursuing diversified livelihoods; the strengthening of producer organizations; improving access to credit; and, improving access to risk management tools.

Rapidly changing market conditions require timely and targeted technical assistance interventions. With the removal of locally based institutions and resources, there is a growing need for the international community to formalize commitments for the provision of assistance to fill the gaps left by existing funding and extension services in the areas outlined above. While individual, country-based resources can provide more targeted and flexible funding, these efforts are vulnerable to such inefficiencies as duplication and inadequate information exchange across projects. Given the systemic and global nature of many of the problems facing coffee producers, there is also potential for improved efficiency in the design and implementation of technical assistance projects among project donors and developers at the global level. We believe that this is an area in which both the ICO and the Common Fund for Commodities could assist.

A further aspect of the global economic crisis that has had an impact on commodities and that I would like to address is the contraction and higher costs of credit. The seasonal nature of coffee production makes access to credit a necessary feature of production, as it is for many agricultural commodities. Credit facilitation for producers and producer organizations is required in several areas, including: pre-harvest financing and seasonal working capital; infrastructure development; diversification; debt financing; and risk management. Improving access to credit, particularly for producers attempting to enter new and differentiated markets, could stimulate product and export market diversification in the coffee sector and, with it, overall sustainability. Although a number of specialized credit institutions currently exist, support for producers and local financial institutions for utilizing them is limited. A centralized information portal for financial services could help generate efficiencies both for producers and for the financial markets that serve them.

One of the major incentives for international cooperation in the coffee sector is a shared interest in long-term market stability. Given the deep political and economic challenges identified with controlling prices through supply management, alternative market-based means for promoting stability should be sought. Roasters and traders in the private sector have long depended on risk management tools and other specialized trading instruments. Yet such instruments remain largely out of reach for most producers, due to lack of capital, knowledge and technical infrastructure. Assistance and training in the use of risk management tools through a special risk management facility could offer a market-friendly approach for improving the sustainability of production in the face of market volatility.

The last feature of the current economic crisis that I would like to highlight as it affects the commodity economy is the precipitous decline in foreign direct investment by transnational corporations (TNCs). FDI flows fell across all regions, from their $2-trillion high in 2007 to the less-than-$1.2 trillion projected for 2009. Yet, between 1990 and 2007, FDI flows in agricultural production tripled from $1- to-$3 billion a year. Although these flows are quite small in proportion to overall FDI flows, they represent a huge source of finance for many low-income countries where agriculture accounts for a relatively high share of FDI inflows. Moreover, FDI in the entire agricultural value chain – from the farm to the supermarket shelf – is much higher, with food and beverages alone accounting for more than $40 billion in annual flows, from 2005 to 2007.

TNC participation in agriculture can have both positive and negative effects in developing countries. On the negative side, governments should address, in particular, environmental and social concerns associated with TNC involvement, such as the crowding-out of small farmers which might create job losses, land grab, dispossession of indigenous peoples and overdependence on TNCs.

On the positive side, TNC involvement can result in the transfer of technology, standards and skills, as well as jobs and market access, all of which could improve the productivity of the industry and of the economy as a whole. TNCs can exploit potential economies of scale that can make agricultural commodities more affordable, and they also bring knowledge of standards and markets. All of these factors depend, however, on host countries adopting the right policies that will maximize benefits and minimize the costs of TNC participation.

Ladies and Gentlemen,

The commodity economy has helped many countries attain economic growth and support poverty reduction efforts. At the same time, the current crisis has highlighted the continuing vulnerability of commodity-dependent countries on external demand and price fluctuations. To ensure the sustainability of commodities production and export – such as coffee – countries must find ways of diversifying both their markets and products, and learn how to benefit from technological and business knowledge. There may be ways to profit from the positive aspects of TNC involvement in production, exports and marketing. At the international level, governments and international organizations alike could now, in the light of the economic crisis, do more to monitor and regulate the commodity economy and financial markets. Price volatility in commodities is impairing the ability of developing countries to build up their capital base and diversify into other sectors, keeping many countries in a state of commodity dependence. Additionally, price volatility disproportionately affects those at the bottom of the value chain because they have the least bargaining power: primary producers therefore tend to absorb most of a price decline and yet benefit the least from price rises, especially in poorer developing countries. Finding ways to help countries move up the value chain may therefore help them respond better to price volatility, and promote the sustainability of commodities for developing countries.

It is my hope that the outcome of this Conference will provide coffee stakeholders – farmers, governments, and the private sector – with some helpful guidelines on attaining the future sustainability of the world coffee sector.

Thank you.

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