

FAIRTRADE COFFEE AND DEVELOPMENT

A FIELD STUDY IN ETHIOPIA

by

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Fairtrade Coffee and Development

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Abstract

Coffee is one of the world's most traded goods, but as the commodity price has plunged in recent years it is increasingly hard for coffee farmers to survive on their crops. Fairtrade is a trading initiative based on equity that claims to contribute to development by increasing farmers' profits and empowerment in communities. Few academic studies have examined Fairtrade development claims. This thesis discusses how much truth lies in these statements. A field study in Ethiopia has been used for the purpose. Ethiopia has grown coffee for a thousand years, is heavily dependant on export of coffee beans, and has recently started to export Fairtrade certified coffee. A qualitative research approach has been used in interviews with coffee farmers, importers, and managers. My conclusion is that Fairtrade does bring economic benefits to farmers. The price of coffee is higher than that of conventional coffee, farmers receive a premium that is to be invested in the community, and they have good working conditions. But lack of education and participation of farmers obstructs economic development.

Keywords: Fairtrade, Coffee, Ethiopia, Cooperatives, Development Theory

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Conversions

10 Birr = 6.85 SEK = 0.73 EURO = 1.07 USD
6 kg red cherries = 1 kg clean exportable coffee beans
1 libra = 327,45 grams

Abbreviations

AFN	African Fairtrade Network
EFTA	European Fair Trade Associations
FINE	FLO IFAT NEWS! EFTA
FLO	Fairtrade Labelling Organizations International
FOB	Free On Board
GNI	Gross National Income
HDI	Human Development Index
ICA	International Coffee Agreement
ICO	International Coffee Organization
IFAT	International Fair Trade Association
NEWS!	Network of European Worldshops
OCFCU	Oromia Coffee Farmers Societies Union
PPP	Purchasing Power Parity
USAID	United States Agency for International Development
YCFCU	Yirgacheffe Coffee Farmers Societies Union

1. Introduction

According to a legend, Ethiopia is the country where coffee was first discovered and spread to the world. The crop plays an important role in the country's economy even today. It is heavily exported and it is estimated that 25 % of the population depend directly or indirectly on coffee for their livelihood.¹ Ethiopian coffee farmers' dependency on international prices along with a stagnation of the rural economy puts farmers in a vulnerable and exposed position. The rural poverty level is 45%², and the country is ranked 169 of 177 on HDI.³

Most of the coffee is consumed in the northern part of the world, while 90 % of the production takes place in the South.⁴ It is in fact one of the most important primary export commodities of developing countries and the fifth most internationally traded good. Coffee is big business globally, but local Ethiopian small-scale farmers receive only a fraction of the retail price and continue to engage in subsistence farming. In the early 1990s coffee producing countries earned 10-12 billion USD and retail sales were 30 billion USD; by 2002 the earnings of producing countries were 5.5 billion USD and sales had increased to 70 billion USD.⁵

Fair trade was created in order to regulate the market and bring more advantages to the coffee producers in exporting countries. The organization aims to create an equitable and stable trading system by establishing a fair price for goods and direct market access for farmers. It guarantees prices to cover the coffee producers' costs of production, which in turn enables improvement of their livelihood: the overall aim being social and economic development of the community.

1.1 Aim of the Thesis

Ethiopia is one of Africa's largest countries with a population of about 70 million people of which about 25 % have their income connected to coffee.⁶ The production takes place in rural areas where the poverty rate is 45 %.⁷ The country receives substantial foreign aid every year and there is a large presence of NGOs.⁸ Despite attempts to markedly raise the average

¹ Ethiopia Cradle of the Wonder Bean p. 9

² FAOSTAT (2006) Food Security Statistics

³ Human Development Report 2007

⁴ Ponte (2001) p. 2

⁵ Osorio (2002) p. 1

⁶ Ethiopia Cradle of the Wonder Bean p. 9

⁷ FAOSTAT (2006) Food Security Statistics

⁸ Foreign aid accounted for almost 18% of GDP in 2005 with an amount of 1,937 USD (SIDA)

income level over a long period of time, Ethiopia remains one of the least developed countries in Africa with a GNI per capita of 180 USD.⁹

Trade is widely recognized as a means to alleviate poverty and Fairtrade claims to make a significant contribution as it brings economic benefits to the poor. The Swedish company Ljöfbergs Lila recently launched their Fairtrade coffee with the slogan “Eradicate poverty in your coffee break”.¹⁰ The Fairtrade Foundation in the UK aims to shift public and consumer lifestyles in the future to make Fairtrade coffee the norm in order to make a greater impact on coffee producers’ lives.¹¹ The development claims of Fairtrade are not modest and deserve to be investigated.

The aim of this thesis is to examine Fairtrade’s contribution to economic development by focusing on two coffee farmers’ cooperative unions in Ethiopia. The underlying question is whether, and to what extent, Fair Trade is a sustainable approach to lift poor producers out of poverty.

1.2 Outline of the Study

The study begins with a presentation of the methodology used, the coffee market in Ethiopia and the main stakeholders, followed by a description of the characteristics of the world coffee market in order to contextualize the presence of fair trade. The functioning of Fairtrade are presented together with claims on impact and previous research. Then is a discussion on the impact on the unions participating, with an analysis focused on financial impact as well as organizational development, both being important from the viewpoint of economic development. Lastly there is a conclusion with comments on the future of Fairtrade in Ethiopia.

1.3 Method

Field studies in Ethiopia are used to investigate the impact of fair trade on development. Interviewed subjects are general managers of cooperatives and unions, local managers, farmers, and importers involved in coffee production and trade. All data are secondary data. Most interviews are recorded.

1.3.1 Selection of Coffee Farmers Unions

The study focuses on two cooperatives unions. A reason is that I wanted to see if there was any difference in the view of Fairtrade between the unions. Participating in the study were

⁹ World Development Indicators, World Bank statistics from 2006

¹⁰ “Utrota fattigdomen på din kafferast” www.lofbergslila.se

¹¹ The Fairtrade Foundation Vision for 2008-2012 available at www.fairtrade.org.uk

Yirgacheffe Coffee Farmers Cooperatives Union (YCFCU) and Oromia Coffee Farmers Cooperatives Societies Union (OCFCU). The reason for this choice is that these two cooperatives showed most interest in my study.

1.3.2 Limitations of the Study

Due to the fact that some of my interviewees did not speak English, employees of the Unions translated into English. There is always a risk of the meaning being slightly altered when having an unprofessional as a translator.

YCFCU was at the time of my study not allowed to sell their coffee in the Fair trade market because they failed to meet the Fairtrade standards at the last inspection. Their work was focused on changes in accordance to 7 corrections given by FLO-CERT¹².

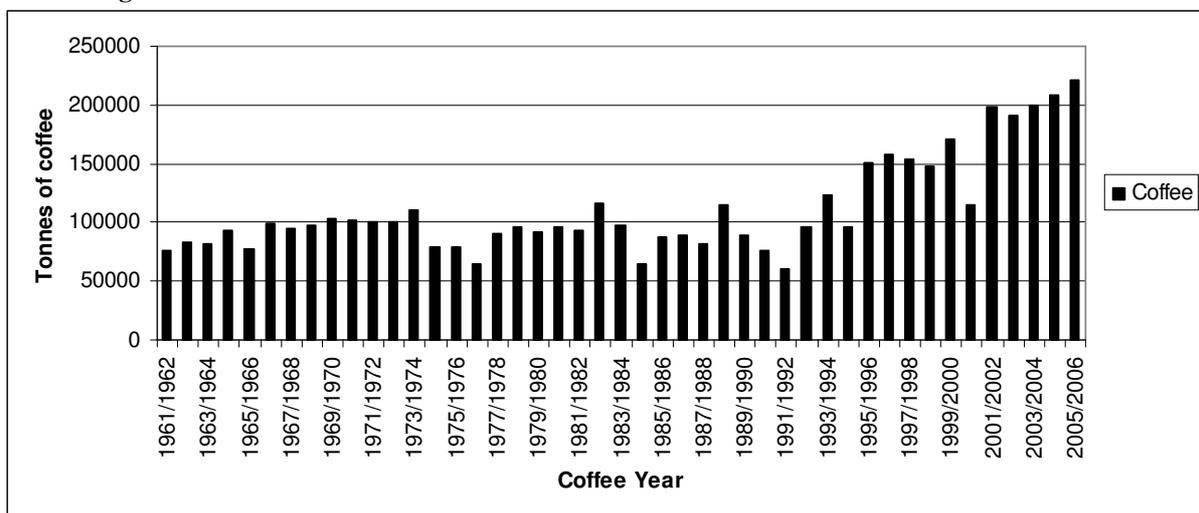
Results from this study can not be generalized to other cooperatives, although I suspect that the results could apply to most cooperatives.

¹² FLO-CERT GmbH is an independent International Certification Company offering Fairtrade Certification services to clients in more than 70 countries

2. Coffee in Ethiopia

Settled agriculture began in Ethiopia some 2000 years ago, and as long as anyone can remember Coffee Arabica has been grown in the wild forests of the south-western massive highlands in the district of Kaffa. Coffee is said to have taken the name of Kaffa, the region where it was first discovered. Export began to Yemen, and was from there introduced to Indonesia, India, The Netherlands, Colombia and Brazil. Coffee in Ethiopia is not only an important export good but it is a part of the culture; about 50 % of the produced coffee is consumed domestically and there is even a cultural ceremony connected to it.¹³ Total production of washed and unwashed coffee is increasing every year, shown in figure 1 below.

Figure 1 Washed and un-washed coffee at auction centres in Addis Ababa and Dire Dawa



Source: Ethiopian Coffee and Tea Authority

Note: Coffee year is October-September

Conventional coffee is collected from the individual farmers, processed and shipped to the auction in Addis Ababa or Dire Dawa, and exported through the port in Djibouti. Fairtrade coffee has received permission from the Ethiopian Coffee and Tea Authority to bypass the auction and be directly exported through Djibouti, with the benefit of avoiding middlemen to get a higher FOB-price. The coffee sector has 215 exporters, who exported 176,390 tonnes of coffee, accounting for some 36 % of the total export value of Ethiopia in the fiscal year 2006/2007.¹⁴

¹³ “Coffee, The Gift of Ethiopia to the World” p. 21

¹⁴ The Fortune, 2007-11-04

The potential for coffee production in Ethiopia is very high considering the country's suitable altitude, rainfall, temperatures and fertile soil. The production is traditionally organic and the soil remains fertile by recycling. The total area covered by coffee is about 400,000 hectares with a production of 200,000 MT of clean coffee per year. 95 % of the farmers are small scale and 5 % are big plantations owned by the government. The four systems of production are forest coffee in the traditional way, semi-forest coffee, garden coffee and plantation coffee owned by the state.¹⁵

Millions of farmers in Ethiopia were badly hurt by the coffee crisis because coffee-export earnings dropped from \$330 million (70 % of GDP) to \$165 million (30 % of GDP) between 1999 and 2004.¹⁶ There was one group partially shielded from the economic devastation: those participating in a differentiated market with attributes such as shade-grown, fair trade, or organic, could earn their living.¹⁷ Fair Trade was introduced in Ethiopia by Oxfam International in 2002. There are four Fairtrade certified unions in Ethiopia¹⁸:

- Kaffa Forest Coffee Farmers Cooperative Union
- Sidama Coffee Farmers Cooperative Union
- Oromia Coffee Farmers Societies Cooperative Union

One union has its membership on hold until the next inspection:

- Yirgacheffe Coffee Farmers Cooperative Union

Two of the unions, YCFCU and OCFCU, took part in this study. Unions represent cooperatives in dealing with importers and roasters, and try to create and develop long term business relationships. Their role is to search for new export markets, and they perform quality controls and store the coffee while it is waiting to be exported.

2.1 The Farmer Profile

The typical Ethiopian farmer grows his/her crops in the backyard of the house. Besides coffee, the farmer generally grows staple food such as enset (false banana), corn and cabbage for family consumption. The costs of production differ from farm to farm depending on the use of pulping machines, hired workers etcetera. Agriculture is traditionally organic and no

¹⁵ "Coffee, the Gift of Ethiopia to the World" p. 7ff

¹⁶ Oxfam America (2003) Press release

¹⁷ Messekerem Tekema 2007-11-23

¹⁸ www.flo-cert.net

chemical fertilizers or pesticides are used. Average productivity on the coffee farm is 500 kg/ha, which is low in an international perspective.¹⁹

2.2 Presentation on Objects of Study

I worked with two unions in Ethiopia to carry out this study: Yirgacheffe Coffee Farmers Cooperative Union (YCFCU) and Oromia Coffee Farmers Societies Cooperative Union (OCFCU)

2.2.1 YCFCU

YCFCU was established in June 2002 and represents 44,189 farmers in its 23 member cooperatives. It is located in the Gedeo zone in southern Ethiopia. Production potential is 39,308 MT. 5 cooperatives are Fairtrade certified and 3 have both a Fairtrade and an organic certification. The 5 cooperatives have exported Fairtrade coffee worldwide since 2004. The certification took place after the suggestion and economic aid from Oxfam America and FINTRAC, a US based contractor working for USAID. The overall aim of the union is poverty reduction.

2.2.2 OCFCU

Oromia Union was the first established fair trade certified union in Ethiopia, with a registration dated June 1999. It is the largest union today. Until last year 11 cooperatives were fair trade certified but the applications for 17 more cooperatives to get access to the fair trade market were recently granted. All of them have an organic certification as well as Fairtrade. The production potential of the union is 230,209 MT. They participated in the film Black Gold which got much international attention and provided good business opportunities for the Union. OCFCU are using the slogan of Oxfam International: “We will make poverty history”.

¹⁹ Abayneh Alemu 2007-12-07

3. Coffee and Price Fluctuations

Coffee producers live in rural areas and often in developing countries. It is common that the only cultivated crop in the rural area is coffee. There are two types of coffee produced in the world: Arabica and Robusta. Arabica is vulnerable to attacks by pests and diseases and is best grown in the highlands of tropical zones. Robusta is more resistant and preferably cultivated at altitudes between sea level and 800 meters. The coffee price is set on the stock exchange in London (for Robusta coffee) and New York (for Arabica coffee). Farmers pick red cherries from the coffee tree, pulp them to separate the green bean, and sell the beans at the local market to a middleman who processes it either by washing or sun-drying. Middlemen in turn sell it to an intermediary for export. Importers in the coffee consuming country buy their coffee from an established exporter or a large plantation owner and sell it in small amounts to the roasters. The roasted and packaged coffee is then sold in retail stores, ready for consumption.²⁰ Coffee is processed by using two methods. The wet method includes pulping of ripe cherries, fermentation and washing, followed by drying, peeling and polishing. When using the dry method ripe cherries are harvested, dried and hulled. Washed coffee prices are higher than unwashed, but the processing is more complicated and the risk of damaging the beans is greater.

The coffee trade was highly regulated during 1962-1989. The International Coffee Organization (ICO) set a target price for each year and allocated quotas to its member countries in order to control the supply of coffee on the world market through International Coffee Agreements (ICAs). Both producer and consumer countries signed the agreements which contributed to stable prices on the world market and higher than free market prices.²¹ When the system was abolished in 1989 it affected the bargaining power in favor of the operators in the consuming countries, followed by a change in distribution of income.²² The imperfect markets in producing countries made it possible for a few companies to gain large market shares and keep low coffee prices at FOB-level²³. Today's coffee market is dominated by four multinational companies: Kraft, Nestlé, Sara Lee, and Proctor&Gamble.²⁴ Production has rapidly expanded as quotas have vanished, and has resulted in a world wide oversupply of

²⁰ Fitter and Kaplinsky (2001) p. 4f

²¹ Bohman and Jarvis (1990) p. 100f

²² Talbot (1997) p. 9

²³ Free On Board. The price received at the port of export, including goods plus the service of loading those onto the ship at the location

²⁴ Black Gold Movie

coffee.²⁵ Coffee prices are consequently lower and more volatile, and a higher share of the profit is retained in the consuming countries.²⁶

Production requires little machinery or other long term investment and is not characterized by economies of scale, which is why the production units are often very small, and consequently vulnerable. 70 % of coffee is grown on farms of less than 5 hectares.²⁷ After planting, a coffee tree takes three years before the first harvest can take place. Production can then continue for 20 years, followed by 20 years of declining yields. In the case of a sudden increase in demand, production does not respond quickly, so the only way to increase production in the short term is to hire more workers and use more fertilizers and pesticides. It makes the price elasticity of supply relatively inelastic, and the produced quantity tends to be stable while coffee prices fluctuate.

The price elasticity of demand is also low because the demand of coffee is relatively stable and does not covariate much with price.²⁸ This could be because the commodity cost represents a small portion of the end retail price to consumers. Lindsey estimates that the cost of coffee is only 5-7 % of the price at Starbucks.²⁹ When supplied quantities vary, the effect on demand is little if any, and the price mechanism takes the economy back to equilibrium. Price fluctuations of the raw material on the world market are therefore big.

²⁵ Ponte (2001) p. 12

²⁶ Ponte (2001) p. 11

²⁷ Fitter and Kaplinsky (2001), p. 14

²⁸ Ponte 2001, p. 7

²⁹ Lindsey (2004) in Nicholls and Opal (2005) p. 45

Figure 2 Effect on price of a supply shock

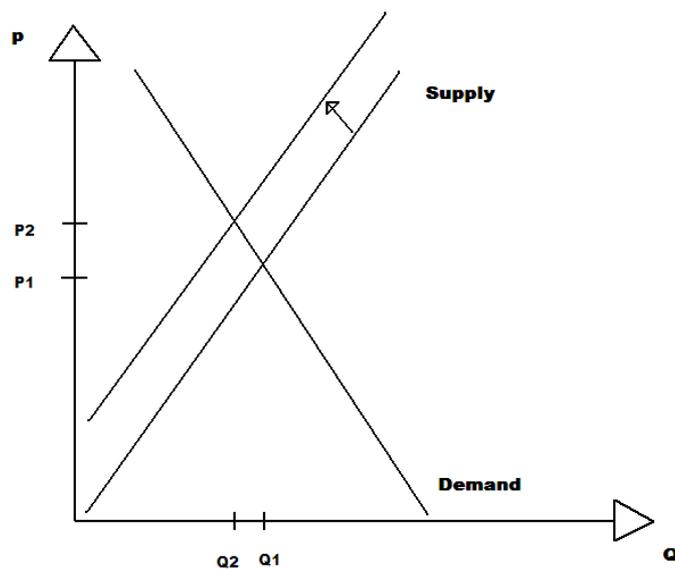
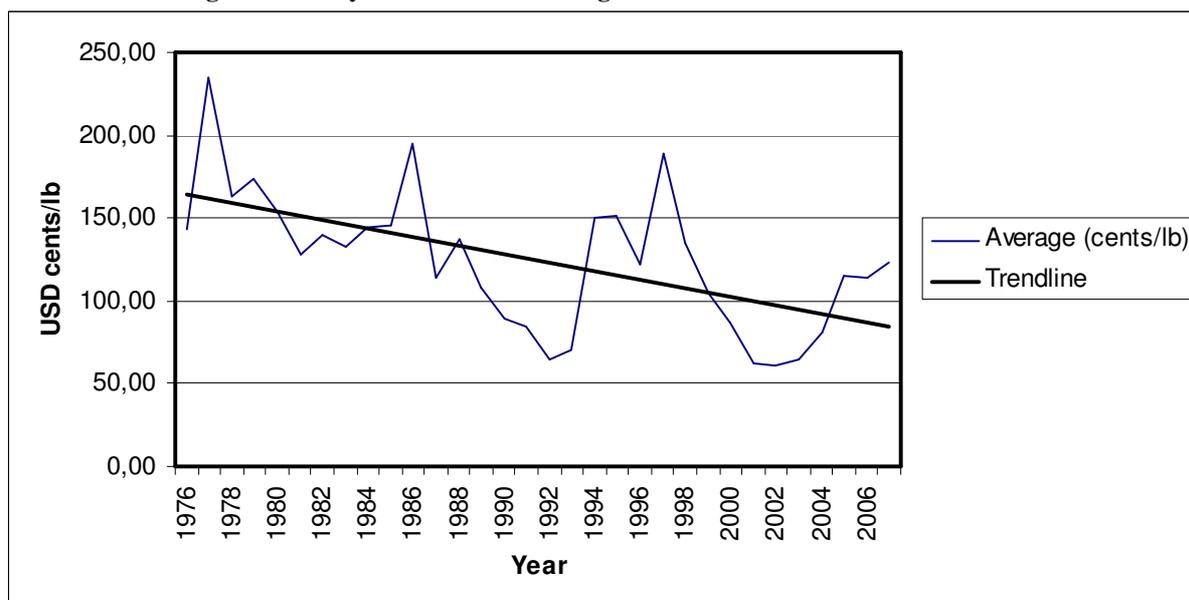


Figure 2 shows a rapid decrease in supply and the subsequent increase in price. Unexpected drought or diseases are quite common and can destroy large quantities of harvest. Prices can increase rapidly without any significant change in the quantity consumed. The response on the supply side is usually quick as more farmers will plant the coffee trees when they see the chance for profit. After a few years when their trees are ready for harvest the price stabilizes, but excess supply on the world market causes further changes towards a lower price. The response is now the opposite; farmers harvest their coffee as long as it covers its marginal cost. A lower price forces them to abandon coffee farms. Decreased supply causes the coffee price to increase and so the cycle continues. A recent and important example of price fluctuations on the world market is the so called coffee crisis. It started in 1997 with a decrease in coffee prices and hit a low in 2001 as can be understood by figure 3. The price of 2001 was the lowest in real terms for over 100 years according to the ICO.³⁰ Figure 3 shows a trend of decreasing prices.

³⁰ Osorio (2002) p. 1

Figure 3 Yearly world market averages for Mild Arabica coffee 1976-2007



Source: ICO

The price decline did not affect countries all over the world in similar ways because the national production and economic structures differ, but it had a big impact on all coffee producing countries and continents. ICO estimates that over 125 million people worldwide depend on coffee for their livelihood.³¹ In Brazil where production costs are relatively low and exchange rates are favourable farmers could still make a living but unemployment rose.³² Where coffee is a cash crop, as in Ethiopia, farmers could not afford basic necessities like medicines and school fees. Unemployment rose and there were abandonment of farms which caused migration to urban areas and swelling urban underemployment.³³

3.1 Market Imperfections

As many developing economies have moved towards a market economy in recent years, it has become apparent that the success of an economy without state intervention depends on prerequisites that facilitate trade. These are institutional, cultural, social and legal.³⁴ Coffee producers live often in rural areas where these fundamentals are either weak or absent. Ethiopia is not a liberal economy, and all the premises of traditional economic models are not met in this market.

In Ethiopia land is owned by the government but leased to farmers. Farmers' property rights are weak and discourage investment in land specific business. A poorly developed

³¹ Milford (2004) p. 4

³² Osorio (2002) p. 2

³³ "Coffee, the Gift of Ethiopia to the World" p. 26

³⁴ Todaro and Smith (2003) p. 698

insurance market, where land is the preferred collateral, prevents people without collateral from getting access to credit, and leaves farmers vulnerable when facing, for example, droughts and diseases on coffee trees. It also prevents farmers from affording the investment required for diversification of farming income. Diversification refers to having more animals and growing more fruit and vegetables to sell. A high dependence on one cash crop is associated with the risk of income loss from crop failure and high exposure to market price variability over time, and diversification reduces that risk.

Coffee farmers are many and in tough competition with each other because start up costs and fixed costs related to growing coffee are low. They sell their crops to the highest bid in the local market to a middleman who in turn sells to processors and exporters. There are normally few processors and exporters operating because of high entry barriers in the form of cash guarantees and storage facilities. The rural position of the farmers and their low knowledge of market functions prevent them from searching and accessing markets, informing themselves about prices and getting technical assistance.

The chain from producers to retail stores consists of many middlemen who all need to make a profit. The price volatility has made it necessary to engage in hedging for most international traders. It reduces the risk taken by the trader who is facing a possibility of loss if the prices unexpectedly would decrease. Its implication is that only some buyers can engage in trade on top of the value chain where there is little competition, being able to make a profit even though the market price is low. The profit left for the producer at the end of the chain is small and sometimes, depending on the price at the time, not enough to make a living on. According to Oxfam the farm-gate price, the price of the product available at the farm excluding transport or delivery charge, was below production cost while Nestlé had an estimated profit margin of 26 %.³⁵ This implies a market failure.

3.2 Consumption patterns

An important characteristic of the coffee market is how the consumption of coffee tends to increase with the level of income per capita. The increase declines and consumption stabilizes when reaching high levels. This is why there is a widespread opinion of an oversupply of coffee in the world market, suggesting that coffee farmers should cultivate other crops that are demanded on the world market. When looking at the European countries and the USA (table 1) it is clear that per capita consumption is relatively stable in all countries, pointing at a saturated market. Norway is decreasing its consumption per capita. Japan shows a different

³⁵ Oxfam (2002) p. 2

trend with increasing coffee consumption. There is a trend for roasters and retailers to increasingly invest in Asia to boost demand in China, Russia and Japan. Interest in the differentiated coffee market, a niche market within the coffee industry, where the value added of the coffee is higher, is growing.³⁶

Table 1: Average per capita consumption in high income countries

	Averages in kilogram's						
	1965-2003	1965-1969	1970-1979	1980-1989	1990-1999	1990-1993	2000-2003
TOTAL	4.47	4.14	4.30	4.52	4.70	4.80	4.58
USA	5.00	6.76	5.71	4.59	4.22	4.42	4.06
European Community	4.92	3.68	4.40	5.23	5.58	5.68	5.37
Austria	6.45	2.76	4.34	7.93	8.82	9.91	6.71
Belgium/Luxembourg	6.92	7.02	7.12	7.45	5.76	5.15	7.90
Denmark	10.82	11.26	12.05	11.01	9.94	10.53	8.92
Finland	11.88	10.66	12.32	12.64	11.57	12.51	11.22
France	5.40	4.59	5.24	5.73	5.62	5.74	5.46
Germany	6.16	4.21	5.00	6.80	7.44	7.67	6.71
Greece	2.57	1.35	1.81	2.77	2.88	2.83	2.00
Ireland	1.29	0.43	0.81	1.43	1.79	1.83	2.00
Italy	4.18	2.69	3.51	4.32	4.93	4.77	5.47
Netherlands	8.19	6.65	7.72	9.34	8.91	9.90	6.67
Portugal	2.68	1.87	1.90	1.97	3.38	3.06	4.30
Spain	3.21	1.68	2.37	3.10	4.46	4.29	2.37
Sweden	9.82	9.23	9.75	10.29	10.00	11.37	8.20
UK	2.23	1.53	2.13	2.41	2.48	2.52	2.26
Other importing countries							
Japan	1.93	0.44	1.09	2.10	2.84	2.71	3.24
Norway	11.29	12.94	12.69	11.65	9.95	10.21	9.09

Source: "Price-elasticity of demand and coffee consumption in importing countries", ICO

³⁶ Coffee such as organic, shade-grown, eco-friendly, and fair trade coffee

4. Fairtrade in Function

Fair Trade has existed since the fifties when the first initiatives were taken to give third-world producers a bigger share of the profits. It started as a partnership between non-profit importers in the North and producers in the South. The alternative trade organizations grew in numbers and spread internationally. The movement came to be coordinated by the transnational Fairtrade Labelling Organization (FLO). FLO is an umbrella organization with members in 21 countries in the Northern part of the world representing Fairtrade Certified Producer Organizations in Central and South America, Asia and Africa. The four main fair trade networks³⁷ agreed on a definition of fair trade in 2001:

“Fairtrade is a trading partnership, based on dialogue, transparency and respect, which seeks greater equity in international trade. It contributes to development by offering better trading conditions to, and securing the rights of disadvantaged producers and workers – especially in the South. Fair Trade organizations (backed by consumers) are actively engaged in supporting producers in awareness raising and in campaigning for changes in the rules and practices of conventional international trade.”³⁸

The trading partnership is meant to be long-term. A relationship between buyers and sellers of a product secures the income of the farmers as it becomes predictable, and allows farmers to get market information. Another aim is to cut the chain from producer to consumer by selling coffee directly to an international trader or a roasting company based in a consumer country. A shorter commodity chain leaves a higher profit for the farmer. Fairtrade also requires pre-payment up to 60% of the estimated contract value on the request of the seller. Through pre-financing the producer organizations have access to the liquid assets needed to buy coffee from their members.

4.1 Cooperative Structure

Fairtrade does not work with small-scale farmers, so in order for them to join they must form organizations to represent them. A number of coffee farmers get together and start co-operatives. “A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise” according to the International Co-operative

³⁷ FLO, IFAT, NEWS!, EFTA

³⁸ FINE, October 2001 www.flo.org

Alliance³⁹. A cooperative tackles market failures, and by pooling resources the position on the local market is stronger than that of the individual farmer.

The co-operatives that live up to Fairtrade Standards get a Fairtrade Certification. It guarantees a fair price of the coffee and a Fairtrade Premium. Fairtrade Standards require that the producer organization is democratic, transparent, and brings social rights and security to its workers. FLO expects the cooperatives to improve working conditions, increase environmental sustainability and invest in developmental projects for workers and farmers. This is to help them move from a marginalized position to economic self-sufficiency and to empower them to actively improve their working and living conditions.

The cooperatives need to meet certain standards to be associated with Fairtrade, and inspections to guarantee this are made by FLO-CERT. Connected to the membership application and standards inspection is a cost. Depending on the number of members of the cooperative there is an initial certification cost of 1400-3400€, together with the application fee of 250€. They are charged an additional cost for inspection of any joint processing equipment.⁴⁰

4.2 Minimum Price

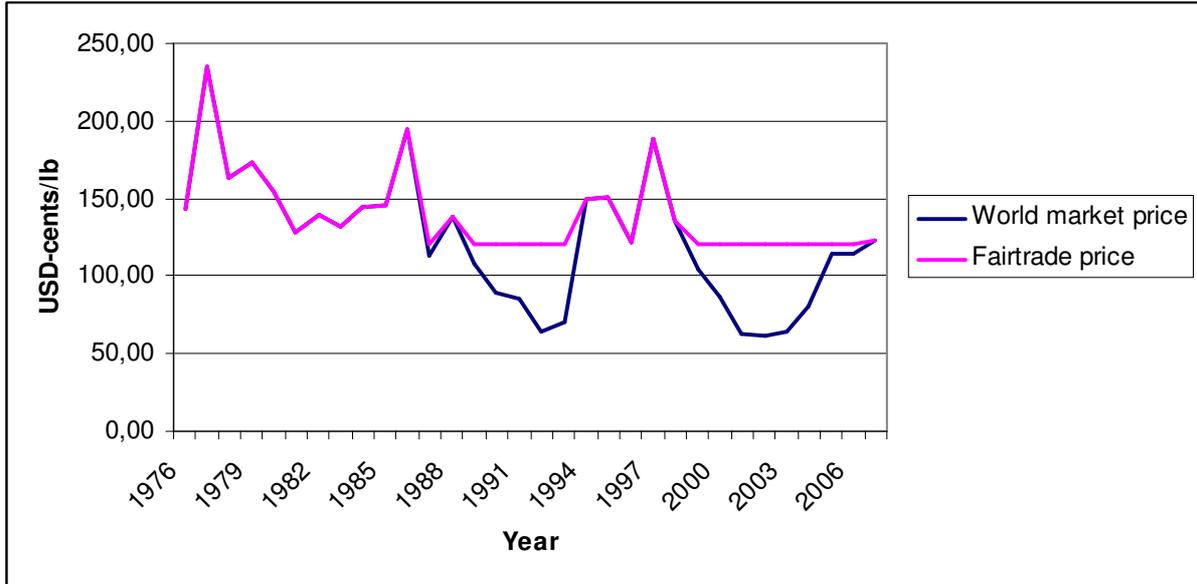
FLO standards require that Fairtrade producers be paid a minimum price, regardless of the market price at the time of trade, which is roughly calculated to cover the production costs. Small-scale coffee farmers get 1.21 USD for each pound of washed Arabica coffee and 1.15 USD for un-washed Arabica coffee.⁴¹ The price of organic coffee is higher. As shown in figure 4, the minimum price creates a price-floor on the Fairtrade coffee market. When world market prices, based on the New York “C” contract, are above the agreed price floor, Fairtrade products are traded for the higher price.

³⁹ www.ica.coop

⁴⁰ FLO-CERT Producer Certification Initial Fees – Small Farmers http://www.flo-cert.net/flo-cert/_admin/userfiles/file/Fees/PC%20Initial%20FeeSystemSF%20IS%2019en%20_2_.pdf

⁴¹ Prices will be raised from 1 June 2008 to 1.25 and 1.20 USD respectively www.flo-cert.net

Figure 4 Average coffee prices for Mild Arabica washed coffee and the Fairtrade price 1976-2007



Source: ICO, FLO

The minimum price is calculated according to this formula:⁴²

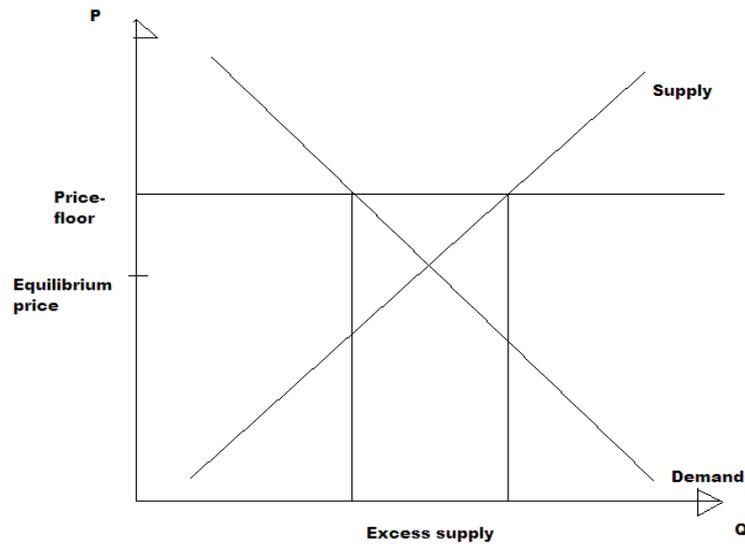
$$\text{Fair Trade price floor} = \text{cost of production} + \text{cost of living} + \text{cost of complying with Fair Trade standards}$$

This ensures a decent standard of living and food security for coffee farmers. It is an income security that enables farmers to plan for the future. However the price floor can cause disturbances on the world market. If the price is kept artificially high it induces an increased supply with more farmers producing coffee. Demand at the prevailing price level will be lower than supply and there will be an excess supply of coffee on the world market. This is illustrated in figure 5. Prices are kept higher than consumers are willing to pay for the coffee which leaves a large quantity unsold. Figure 4 show that the minimum price has constituted the Fairtrade price every year since 1999. The current world excess supply is estimated to be 8 %.⁴³

⁴² Nicholls and Opal (2005) p. 41

⁴³ Oxfam (2002)

Figure 5 The effect of a price floor on supplied and demanded quantities



An assumption made in this diagram is that the market initially is at equilibrium where supply equals demand. This might not have been the case because ICAs were in use. The discussion is valid though, even from different starting points. Critics of fair trade claim that the overproduction is a signal for producers to switch from coffee to other crops. Paying the guaranteed price prevents the signal from getting through and, by raising the average price for coffee, encourages more producers to enter the market, increasing supply even more.⁴⁴

4.3 Fairtrade Premium

Producers connected to Fairtrade receive extra money in the form of a premium, which is a part of every export contract and is paid by the buyer. The amount of 10 USD-cents/pound is earmarked for social and economic development in the local communities.⁴⁵ The producers decide themselves democratically how these funds are to be used, and are accountable to FLO-CERT for the spending of the money. FLO encourages the money to be used for training and education, infrastructure, productivity increases, environmental protection, and revolving funds⁴⁶ for loans and micro-credits, but decisions must be taken jointly by all members after a thorough discussion on what is needed in the community. The community could mean just the

⁴⁴ Read “Grounds for Complaint” by Lindsey (2004) for an explanation

⁴⁵ Fairtrade Standards for Coffee for Small Farmers Organisations §4.4, Generic Fairtrade Standards for Small Farmers Organisations §2.1.1.1

⁴⁶ A fund which is intended to be refilled so it can be loaned or spent repeatedly

producers or the producers and their families, or the larger community where the producers live.⁴⁷

4.4 Consuming Fairtrade

Fair trade, as a system of exchange⁴⁸, is dependent on the willingness of consumers in developed countries to pay a price premium for the purchased product. According to a study by Basu and Hicks⁴⁹ this is subject to two opposing effects. The willingness increases with the credibility of the poverty aversion claims but decreases with the fear of relative deprivation of the poor producers not included in the fair trade program. Market restrictions on the consumption side is one of the problems that fair trade face, but business is nevertheless going well and sales from Fairtrade coffee are increasing in the world market (for example from 33.994 Metric Tonnes (MT) in 2005 to 52.077 MT in 2006).⁵⁰ A high increase in sales is shown in the latest annual report by FLO in table 2. It is a part of the strategy 2008-2012 for the British Fairtrade Foundation to make Fairtrade the norm of all consumption in the UK.⁵¹ There is no such outspoken attempt from FLO but the controversial decision to let the certification mark be used by multinational companies shows an attempt to penetrate the conventional coffee market. McDonalds and Starbucks serve Fairtrade coffee at their stores, and Nestlé have recently launched a Fairtrade certified coffee with their name.⁵²

⁴⁷ Explanatory document for Generic Fairtrade Standard for Small Farmers' Organisations, Appendix 1

⁴⁸ Including brands like Fairtrade, Rainforest Alliance, UTZ Certified and many more

⁴⁹ Arnab K. Basu and Robert L. Hicks (2007)

⁵⁰ Fairtrade Annual report 2006/2007

⁵¹ The Fairtrade Foundation Vision

⁵² O'Nions (2006) p. 1

Table 2 Estimated Fairtrade retail value in consuming countries. Numbers concern all certified goods.

Country	2005	2006	Increase
Austria	25.6	41.7	63%
Belgium	15.0	28.0	86%
Canada	34.8	53.8	54%
Denmark	14.0	21.5	54%
Finland	13.0	22.5	73%
France	109.1	160.0	47%
Germany	70.9	110.0	55%
Ireland	6.6	11.6	77%
Italy	28.0	34.5	23%
Japan	3.4	4.1	23%
Luxembourg	2.3	2.8	23%
Netherlands	36.5	41.0	12%
Norway	6.7	8.6	28%
Sweden	9.3	16.0	73%
Switzerland	133.8	135.3	1%
UK	276.8	409.5	48%
USA	344.1	499.0	45%
Australia/New Zealand	2.5	7.2	191%
Spain	0.0	1.9	6233%
Total	1132.4	1609.0	42%

Values in million Euros and %

Source: Fairtrade Annual Report (2006/2007)

4.5 Fairtrade claims on impact

The idea of economic development has altered many times. It has gone from a measure of purely economic growth to a concept that is multidimensional because it encompasses all that affects quality of life. The World Bank defines development like this:

“The challenge of development, in the broadest sense, is to improve the quality of life. Especially in the world’s poor countries, a better quality of life generally calls for higher incomes – but it involves much more. It encompasses as ends in themselves better education, higher standards of health and nutrition, less poverty, a cleaner environment, more equality of opportunity, greater individual freedom, and a richer cultural life.”⁵³

Wealth and income are seen as an instrument to obtain a better life but are not ends in themselves, and human values are in focus. The contribution to development of Fairtrade is more than monetary, according to FLO.⁵⁴ Many of the impact areas presented below are

⁵³ World Bank (1991), p. 4

⁵⁴ www.fairtrade.net

particularly difficult to quantify, and it is a challenge to find causality between benefits and participation in Fairtrade. Nevertheless, Fairtrade estimates it benefits five million producers worldwide in the following way.⁵⁵

Better living conditions: Fairtrade creates better living conditions for the workers and their families as well as for the society because of the premium that creates positive externalities.

Environmental sustainability: Farmers are encouraged to engage in sustainable forms of production with respect for the environment, and avoid toxic pesticides.

Access to international markets: Farmers get access to international traders who are usually suspicious of any unknown trading partner. They provide producers with contacts and mobilize them to get a better understanding of, and status on, international markets.

Empowerment of women: There is an example of a women's cooperative in India where the women own their own plots of land and thereby strengthen their income and position in the family.

Long-term investments: Examples are investment in pension schemes, life insurance, income diversification and more.

Anti-discrimination: The aim is to promote equal rights amongst ethnical groups. All the cooperatives are democratically ruled.

Community solidarity: There are often spill over effects to other farmers in the area and solidarity for disadvantaged farmers can increase.

Ensuring labour rights: Workers take an active role in their workplace; they are more involved when doing business, they are aware of their rights and some are members of a trade union.

Stronger business: Fairtrade enables stronger business organizations to develop, ensuring quality products and better access to international markets.

⁵⁵ O'Nions (2006) p. 1

5. Impact of fair trade on development

“Fairtrade should make a difference in development for certified producers” - FLO⁵⁶

As Ronchi (2002) also realizes, the fact that it is mandatory for all small-scale producers to be organized in cooperatives to receive the Fairtrade certification reflects a conviction of co-operatives as development agents.⁵⁷ Fairtrade is therefore affecting the society through two channels: in a monetary way through higher prices and premium money and through producer organizations with societal effects. My impact analysis is structured correspondingly.

5.1 Previous Research on Fairtrade

The claimed impact from Fairtrade seen in chapter 4 seems extensive as not only the individual farmers will benefit but also the community. Since the start of fair trade there has been some research conducted on its impact and contribution to development. The conclusions are both positive and negative.

Booth and Whetstone’s opinion is that fair trade is a good small scale system but it cannot be sustainable in the long run. It only encompasses a minority of producers and a regulated system with a price floor cannot hold forever. The gains from a total de-regulation of all trade, in northern and southern countries, would be much greater than Fairtrade can ever be. Countries need to trade but they also need an institutional framework which facilitates business creation and growth. Coffee is an income inelastic product so poverty alleviation cannot come only from coffee production.⁵⁸

Lorraine Ronchi conducted research on a coffee cooperative in Costa Rica in 2002. She found that Fair Trade had accomplished its goal of improving the returns to small-scale producers and positively affecting their quality of life. After the coffee crisis in the 1990s, which heavily affected the farmers, the cooperative organizations were rebuilt thanks to Fairtrade and could represent them effectively locally and nationally again.⁵⁹

⁵⁶ Generic Fairtrade Standards for Small Farmers’ Organisations §1.1

⁵⁷ “Small farmers can join Fairtrade if they have formed organisations (in co-operatives, associations or other organisational forms)” - Fairtrade Generic Standards for Small Farmers Organisations p. 3

⁵⁸ Booth and Whetstone (2007)

⁵⁹ Ronchi (2002)

5.2 Financial Impact

At the time of my study the coffee prices in Ethiopia were uncommonly high. During the coffee crisis farmers got less than 1 Birr per kilo red cherries, but they got 5-6 Birr in late 2007, which was higher than the actual world market price. It is not ultimately established what pushed the prices so high. The necessity of Fairtrade as a means to get higher prices seemed absent. However, the situation was the complete opposite five years ago and the consequences are still noticeable: Out of the 23 cooperatives of YCFCU only five are financially sustainable. The union helps the others to survive by providing credit and pre-payment of goods.⁶⁰ Both unions have managed to put farmers in a better financial situation by substantially increasing exports the past five years, but growth is highly variable (table 3).

Table 3 Export volumes and growth rates for OCFCU and YCFCU

	Export volumes (ton)		Annual increase	
	YCFCU	OCFCU	YCFCU	OCFCU
2003	437.0	967.2		
2004	850.0	2 431.5	94.51%	151.40%
2005	1 036.0	2 690.5	21.88%	10.65%
2006	1 172.0	3 182.3	13.13%	18.28%
2007*	861.9	4 446.6	-26.46%	39.73%

Source: YCFCU annual report, OCFCU annual report

*The amount for OCFCU of year 2007 is an estimation based on information from the first 7 months of that year.

Additional income to sales of coffee can be derived from working at the cooperative's washing stations where all cherries are weighed and pulped and finally washed or sun-dried. Both men and women are hired as workers and payment is 10-12 Birr per day and 20 Birr per night. This extra income can be crucial for the survival of many families in harsh times. The income is not specific to Fairtrade; the cooperatives in this study operated before they engaged themselves in fair trade (but some of them are still in business solely because of their Fairtrade certification).

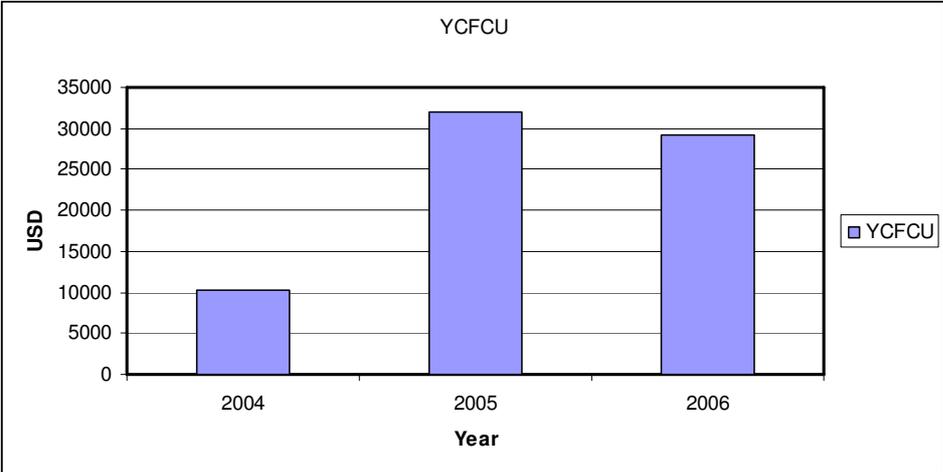
The extra income earned by farmers through Fairtrade sales are calculated in the following way by FLO:

$$(\text{Fairtrade Price Floor} - \text{Market Price for Coffee}) * \text{Volumes Traded}$$

⁶⁰ Messekerem Tessema 2007-11-23

The formula is applicable only when the market price is lower than the Fairtrade minimum price. This was not the case in 2007 and the year is therefore not included in my calculation. The result for YCFCU (figure 6), shows that Fairtrade has brought economic benefits to farmers. Income benefits are estimated to decrease in the immediate future as the world market coffee price was high in 2007 and started off high in 2008. As the price goes up cooperatives increasingly question the importance of fair trade. YCFCU, which is facing exclusion from the fair trade market, has started to look for another certification to get premium prices. Their opinion is that fair trade is not the only solution, and premium prices may easily be attained with other certifications. A higher income to the cooperatives benefits farmers and is a step towards the overall aim of both unions: poverty alleviation.

Figure 6 Extra income earned by farmers through Fairtrade sales



Source: ICO, YCFCU annual report

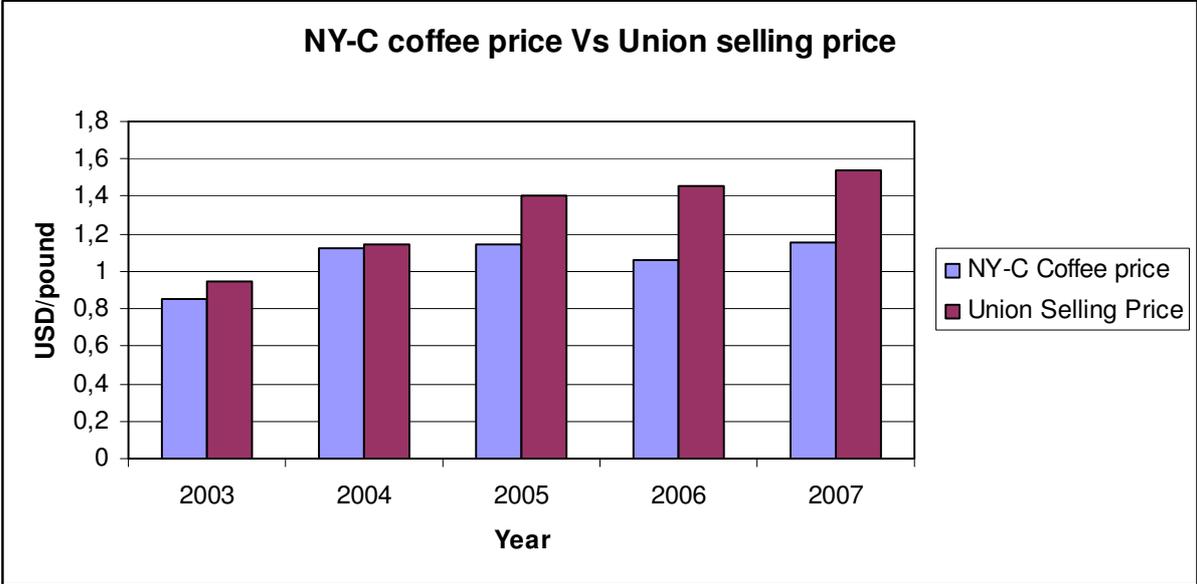
The distribution of extra income is proportional to the amount of coffee that members deliver to their respective cooperative. Higher income to a part of the population affects the community through a dispersion effect. It increases consumption, creates job opportunities, and augments tax revenues. An opposite effect is derived from the overall higher coffee price that affects the community as a decrease in purchasing power of coffee. 50 % of coffee production is consumed domestically; coffee is an everyday drink for all Ethiopians.⁶¹ The outcome depends on which effect is stronger.

Being part of a big organization and therefore meeting foreign inspectors and buyers at their own cooperative enhances the self-esteem of farmers and encourages them to seek new markets. Support in terms of information and technical assistance from the union enables

⁶¹ “Coffee, The Gift of Ethiopia to the World” p. 21

them to access new markets, such as the one for specialty coffee where prices are higher. The change in production from conventional coffee to the differentiated coffee of fair trade has increased the profits of the unions, see figure 7.

Figure 7 New York stock exchange coffee price versus YCFCU selling price 2003-2007



Source: YCFCU financial report 2007

While YCFCU, which is a smaller union, sells all its Fairtrade coffee on the specialty market, OCFUCU only sells a fraction of its produced fair trade coffee with that label. The 28 certified cooperatives have a production possibility of 30,535 metric tons of coffee, but only 8 % is sold on the fair trade market.⁶² More cooperatives are interested in getting the certification but the union’s advice is to wait. High demands on standards, the cost to get the certification, and the limited fair trade market, prevent more farmers from entering fair trade. YCFCU is also interested in certifying more cooperatives and will do so if accepted at the next inspection. The problem of deficient demand is addressed by the African Fairtrade Network (AFN). It is an umbrella organization of Fairtrade certified producers with a mission to expand the market by increasing awareness of fair trade in Africa.⁶³

5.2.1 Premium Investments

The Fairtrade premium is extra payment from the buyer that supports the improvement of business, community and environment. It can be used by the cooperative as funding for projects or training, and how it is used is decided democratically in the General Assembly of

⁶² Dessalegn Jena 2007-11-15
⁶³ www.fairtrade.net

the cooperative where all members have a right to take part and to vote. After the decision a proposal is written by the board of the cooperative. When the union has evaluated and approved the proposal the cooperative is responsible for the realization of the project. The amounts from the last three years are stated below in table 4.

Table 4 Premiums paid for washed and un-washed coffee and the investments for Fairtrade certified cooperatives of YCFCU and OCFCU (Birr)

	OCFCU	YCFCU
2004	884 332,00	110 221,71
2005	1 673 812,00	361 140,82
2006	2 722 422,00	192 333,86
Total	5 280 566,00	663 696,39

Source: YCFCU annual report, Ayidefer Gemeshu 2007-12-20; OCFCU book-keeping, Dessalegn Jena 2007-12-21

Money from YCFCU was invested in improvement of:

- 1 school facility
- 1 annex of a school
- 2 electricity extensions to the more remote areas of the Gedeo zone
- 2 flour mills to help women in their work.

Premium money from the first year of the Fairtrade membership was not invested in fixed assets as they were supposed to. It was discovered by the Fairtrade inspector, and recently corrected. What caused the matter is unclear, and there were three explanations: a misunderstanding, lack of information about the regulations, and a “coup” at the start of the union.^{64,65} The fluctuating amount of premium money is co-varying with the export quantity.

OCFCU used their money to build:

- 1 annex to a school
- improvement of 4 schools
- 4 new schools
- 4 health clinics
- 3 potable water stations
- 1 bridge

⁶⁴ Ayidefer Gemeshu 2007-12-20

⁶⁵ Messekerem Tessema 2007-11-23

The increase in the amount of the premium of OCFCU from 2004 to the next years is substantial. The reasons are that the quantity exported as Fairtrade from each cooperative increased and that Fairtrade certified cooperatives increased from eight to eleven in 2005.

The probability that the projects would have been realized without Fairtrade money is low because of the overall bad financial status of the cooperatives. Although Fairtrade by its structure excludes non-fair trade farmers from its financial benefits, the investments made by the Fairtrade premiums are beneficial to all community members. Cooperatives use locals to realize the projects, which gives employment opportunities for the community.

The schools will help increase the average ability to read and write in the community, since only 6/10 children attend elementary school.⁶⁶ Education is an important mean to facilitate development because social returns are much higher than social costs at the primary and secondary educational level. Productivity increases markedly when people get basic education such as reading and mathematics because education is a necessity for a country to efficiently use modern technology and to increase productivity, capacity and growth.⁶⁷ Without education it will be difficult for farmers to leave subsistence farming as the main income and create a more dynamic and diversified production. Rural poverty was 45 % at the turn of the millennium.⁶⁸ Tadesse Meskela, General Manager of OCFCU said “I want to see all kids go to school; I want most of them to leave the farms, so that only a few people take care of the coffee and the rest get an education. This is my vision.”⁶⁹

It is important to create schools for children without access, but at the Negel Gorbitu cooperative of OCFCU, where a new and bigger annex was built, the initial school was old but perfectly functioning. The quality of the teaching was not affected by the investments since they are provided by the government, and there was a notorious lack of pens and paper. At the same cooperative the road to reach it was hardly accessible, a tiny winding road made of earth and filled with potholes. To find the way to the cooperative is difficult and to transport the beans from there is a problem.

Health clinics make health services more accessible, which will decrease child mortality rate and increase life expectancy. The potable water stations will increase child

⁶⁶ Landguiden, Utrikespolitiska Institutet

⁶⁷ Todaro and Smith (2006) p. 383f

⁶⁸ Landguiden, Utrikespolitiska Institutet

⁶⁹ Tadesse Meskela 2007-12-11

survival (17 % of child deaths are caused by diarrhoeal diseases, bacteria usually coming from dirty water⁷⁰). Both will raise the overall quality of life of the citizens.

5.2.2 Finance and Investments

In order for an economy to grow it must regularly save and invest to increase the capital stock, according to the Harrod-Domar growth model. Low savings rates, on the other hand, decrease levels of investments and create a dependency on loans and aid.⁷¹ The culture of saving is weak, so farmers lack resources to upgrade production techniques or for emergency funds when subject to crop failure. It is important for farmers to be able to borrow money but it is not always possible because farmers lack collateral or the interest rates are too high. Most times access to credit is not provided for at all in the rural areas. For this purpose, OCFCU have established the Oromia Cooperative Bank with services for their members. It was established in 2004 with capital raised by members, and has opened branch offices in seven other districts. An aim of the YCFCU, as presented in the activity performance report, is poverty reduction by establishing rural saving and credit finance. When asked, it seemed not to be a high priority at the moment. Savings institutions should be provided by the government, and although they wanted to they had no resources to allocate to such a project.⁷² Both YCFCU and OCFCU offer credit to their cooperative organizations.

The cooperatives have the option to provide credit services for their members and it is jointly decided at the General Assembly if the service is wanted or not. Hafursa, belonging to YCFCU, is a cooperative which, at the time of my visit, did not give loans to members. Manager Getachew Ararso explains: “We had this service but since the coffee price is so high now it is not necessary. The problem before was that many farmers could not repay the loans, which created conflicts.”⁷³ The cooperative recently used 1000-2000 Birr to finance the schooling of ten children, it was a rare happening but the parents of the children had good knowledge of money and were therefore trusted. Lending money to its members can be a source of conflict if it is difficult to get repayments in time. Because farmers have no or little education they may not understand the functioning of interest rates and repayments, and lack lacking cost-consciousness. Instructions on lending mechanisms, repayment schemes and incentives for repayment can reduce and in successful cases eliminate the problem of re-

⁷⁰ Under-5 mortality is 166 per 1000 live births. Life expectancy is 50 years in Ethiopia. Data is available at WHO homepage (Mortality Country Fact Sheet 2006)

⁷¹ Todaro and Smith (2003) p. 113

⁷² Ayidefer Gemeshu 2007-12-20

⁷³ Getachew Ararso, Manager at Hafursa Cooperative, 2007-11-30

payment. Micro-loan institutions have already shown that it is possible for credit services to function when customers are uneducated.

Fairtrade guarantees a minimum price for the coffee delivered, which means that farmers get a stable income and they have the opportunity to plan ahead. People make better investment decisions when they have more information accessible. But the information farmers have on fair trade is very limited, and the vast majority do not know what it is. A recent study in the district of Yirgachefe estimated that only 1 % of coffee farmers know about the fair trade market.⁷⁴ The majority feel that since the unions came into place prices and revenues are higher, but the reason behind is not understood. Poor people in developing countries are the most risk-averse because they have no access to safety nets, and a small loss of income can have severe consequences when living on the margin. Members are cautious when trying to predict the future, scarred as they are by the past. Investments in coffee production will not happen if they are in doubt about future incomes.

Costs are reduced as cooperatives jointly use processing equipment and storage facilities. This should lead to higher productivity and quality, increased economies of scale, and as a consequence higher incomes and living standards. Prevailing average productivity is only 500 kg/ha, so an upgrade from low-yield and low-cost production techniques is well-needed. Increased productivity can outweigh a decline in price. Coffee quality is highly variable, and ranges from one to four on the coffee grading scale⁷⁵. If Ethiopian coffee production is not internationally competitive, other countries will increase their market shares. Ethiopian farmers do not spend much time maintaining their trees and soil, which if they did would raise their annual yield and quality of the beans. Farmers are advised on how to handle their coffee by the Fairtrade Liaison Officer and the cooperative Expansion Agency, which is a governmental organization.⁷⁶ Training is provided yearly and contains how to handle the picked cherries, how to prune the trees, and the reason for mulching. The training must be continuous to maintain the knowledge of the used practices, but insufficient resources are a big constraint. Farmers take little responsibility for their own knowledge and personal development.

Institutional structures also affect farmers' decisions, and how they look at the future. Most farmers do not own their land but they lease it from the government, which is a legacy

⁷⁴ Tsegewin Woubetu Tsegaye (2007), case study in YCFCU Fairtrade and organic certified cooperatives. Numbers concern both farmers who grow fair trade coffee and farmers who do not.

⁷⁵ Scale ranges from 1-5 where 1=high quality with very few defects

⁷⁶ Chala Erko, FLO Liaison Officer of Ethiopia, travels regularly to Fairtrade cooperatives in Ethiopia to educate people in efficient agricultural practices

from the communistic regime in 1974-1991. The governmental policy of Ethiopia today is that coffee should be produced in small units, preferably organized in cooperatives. But how much are they willing to invest in their land when they do not own it? When asked, farmers talked mostly about improving their living conditions. They wanted to build a better house for their family, expand the farm and diversify. They did not see coffee as the best way to earn their living in the future, but they would rather spread their risks to decrease their dependency on coffee. The farmers had been members of cooperatives for from six to more than 20 years and their plot was inherited from their parents who also were members.⁷⁷

Another precondition for future incomes is sustainable production. Fairtrade is putting focus on sustainability by encouraging all farmers to engage in eco-friendly farming. Agriculture is using and misusing natural resources, and has had bad effects on the environment all over the world. Farming in Ethiopia is by tradition organic in the meaning that they reject all chemical products such as fertilizers and pest controllers. Thanks to this the earth still has high fertility. But far from all cooperatives are certified for organic farming, because they do not fulfil the requirements. The washing technique uses large amounts of water to process the coffee beans, leading to water depletion and pollution of the earth. There are installations available in the market to reduce the use of water and clean it before being let out in the nature, but they are costly and very few cooperatives are able to afford them.

5.3 Impact through Cooperative

One reason for the farmers' exposed situation is the lack of infrastructure in their society. They have little information about buyers and prices and difficulties transporting their goods because roads are in bad shape and women's backs are hurting from many years of carrying heavy loads. This causes a supply constraint and gives opportunities for private buyers to individually collect the beans. Buyers come to the farmers' house, either before cherries are ripe offering pre-payment for a future purchase at a low price, or when they are harvested to buy them directly. Ethiopian cooperatives give farmers an alternative market and consequently the possibility of choosing buyers. Their presence is a counterbalance to private buyers that stabilizes the market. Farm-gate prices are therefore less volatile, and they are higher because of the competition.⁷⁸

It can be difficult to trace the coffee back to its producers when it is collected or handed in to private buyers because a reliable record on what production is organic and what is not, or

⁷⁷ Konshori Figa, Hailo Bariso, Matchale Wako, Habtamo Kaleab, Getachew Ararso

⁷⁸ Dessalegn Jena 2007-11-15

what kind of bean is produced where, is not always kept. Prices of different beans can induce “coffee-tourism”, like selling Sidamu coffee as Yirgacheffe (Yirgacheffe is valued higher). Fairtrade standards demand a strict separation between different types of beans, and cooperatives are obliged to keep records of all production. By facilitating traceability of the beans, the reputation of Ethiopian coffee is raised in the world market and thereby easier to export.

Private buyers constitute a challenge for Ethiopian cooperatives, especially when the world market price is above the fair trade minimum price. In this situation middlemen are able to pay the same price as cooperatives, and sometimes more. Cooperatives often struggle with financial difficulties which force them to make delayed payments. Farmers’ temptation for fast cash from middlemen creates a member retention problem. The inability to commit the members to the cooperative creates a view of the membership as unconditional and temporary, in sharp contrast to the aim of Fairtrade of long-term commitments and sustainability.

YCFCU has shown difficulties complying with Fairtrade standards. All certified cooperatives have received warnings regarding delayed or defaulted payments of premiums, overlapping of numbers in the bookkeeping, inaccuracy in registered farmers and overestimation of yields. Mismanagement has detrimental effects in several ways. It harms the reputation of the union (nationally and internationally) with negative effects on membership and sales. The financial standing of the union deteriorates, which ultimately worsens farmers’ social and economic situation.

The support from YCFCU and OCFCU is extremely important for cooperatives. They do not only facilitate international business-making, but their work is oriented towards poverty alleviation. OCFCU runs several projects to achieve a better living standard for members. One of them involves production of cashew nuts for export, another encourages farmers to plant beans around their coffee trees. The beans reduce weed, bring nourishment to the soil, and give food security to farmers.

Many cooperatives would have gone bankrupt without the support of Fairtrade. In the case of bankruptcy farmers would have been forced to get income from other agricultural crops or other economic sectors. It is possible that Fairtrade helped reduce urbanization. When migrating to Addis Ababa people are often forced to live in slum areas with high unemployment and underemployment⁷⁹, where the possibility of making a decent living often

⁷⁹ Having less than full-time, regular or adequate employment

is equal to urban areas. No other cash crop gives as high income as coffee in the Ethiopian market. Fairtrade cooperatives are retaining farmers in the coffee industry and the implication is a continued dependence on coffee.

5.3.1 Strength of Producer Organization

The coffee cooperatives, as emphasized by Fairtrade standards, are democratic organizations. They are important institutions considering many of the effects on the quality of life of producers are felt through them. The farmers are both members and owners, as they own a share of the organization proportional to the amount of products they deliver to the cooperative. The principle of one member – one vote applies, and everyone has therefore the same incentive to participate and take responsibility. As Milford points out, it is the benefits and costs that affect how valuable a membership is and how much effort members put into the organization.⁸⁰ Benefits are for example a higher coffee price, right to vote, and labour rights. Costs are membership fees and delayed payments. The coffee price alone therefore does not determine membership. The membership in turn, affects how strong the organizations are and therefore its impact.

Empowerment⁸¹ of the farmer is important in order to transform farmers from price-takers to business-farmers that take conscious production decisions. Producer organizations could be an effective organ that empowers farmers to improve their living conditions. Generally one of the successes of cooperatives is the development of human resources so that all members can contribute to the cooperative activities. It is easier to make use of existing know-how about production and processing techniques and create a vast knowledge spread to other members when working in cooperatives. According to Fairtrade standards cooperatives must meet once a year for the General Assembly where the annual report is presented, current issues are discussed, and it is decided how to invest the Fairtrade premium. Some cooperatives meet more than once a year. Attendance at this meeting is always high, and members enjoy talking and discussing possible improvements of their situation. “Members of the cooperatives understand that common effort gives common benefit. Those who are not ready mentally are not members because they cannot invest mind, money, knowledge” says Mr. Ararso, one of the professional managers.⁸² But while some members invest time in their cooperative, which they feel ownership of, many members are not involved at all. Indeed

⁸⁰ Milford (2004) p. 53 ff

⁸¹ World Bank definition: Empowerment is the expansion of assets and capabilities of poor people to participate in, negotiate with, influence, control, and hold accountable institutions that affect their lives. World Bank Prem (2002)

⁸² Manager of Hafursa Cooperative of YCFUCU

most coffee farmers sell their cherries wherever they get the highest immediate profit; to their cooperative or to private buyers. Unions have different approaches to this. YCFCU do not consider it a big problem because an estimated 90 % of their farmers are loyal to their cooperatives.⁸³ OCFCU worries about the problem of delivery, because if farmers do not sell to the cooperatives as much as expected the union cannot deliver on signed contracts.⁸⁴ Besides the General Assembly once a year, farmers do not maintain a dialogue. The general explanation of the disinterest of farmers is that it is a consequence of the previous regime. From 1974-1991 it was mandatory for farmers to be organized into cooperatives whose leaders were commonly engaged in power abuse. The spin-off is low faith in the leaders of today. In addition to the theory by Milford, I would argue that an equally important reason is the top-down communication. Farmers are positive towards fair trade because they get higher prices: that is a tangible effect. But there are several “fluffy” goals of cooperatives set by FLO and the unions that poorly educated farmers can not see the direct benefit of.

A strong organization can be a powerful voice of farmers, but a heavy bureaucratic structure causes inefficiency. How they are managed are therefore of big importance. One of Fairtrade’s requirements is that the position as manager of the cooperative is occupied by a professional. This is not the case in all cooperatives, neither OCFCU nor YCFCU can fill all their manager positions with professionals, and in YCFCU the rate is as low as 1/5. The explanation is practical; the remote areas and low salaries make the jobs unattractive for graduates. Poor management is the reason why YCFCU could not keep the Fairtrade standards.

All Fairtrade cooperatives in Ethiopia are represented by a union which handles all contacts with buyers in export countries. Cooperatives are generally too small to create and develop these contacts themselves, a reason why the unions play an important role. However, the centralized system makes knowledge and decision-making components necessary for empowerment, to by-pass farmers. The overall result is that producer organizations are weak in Ethiopia, and members are disconnected from their cooperative.

5.3.2 Gender equality

One aim of Fairtrade is to bring more gender equality into the society through the empowerment of women. Studies have found that the position of the woman is stronger in a family where the income of the woman is relatively high. Furthermore, when household

⁸³ Ayidefer Gemeshu 2007-12-20

⁸⁴ Tadesse Meskela 2007-12-11

income is low women allocate virtually 100 % of their income towards nutrition, a significantly higher percentage than men.⁸⁵ There is no criteria concerning women in the Fairtrade standards other than non-discrimination by gender, and the unions do not have any specific policy regarding the matter. Coffee is a cash crop, and cash is generally controlled by male household members. Land is by tradition passed on to males in Ethiopia, and most members of the cooperatives are male. Numbers in table 5 are from the Oromia Union.

Table 5 Member status by gender in OCFCU

OCFCU				
Year	Farmer Members			% female members
	Male	Female	Total	
2000/2001	21 342	1 161	22 503	5,16%
2001/2002	21 589	1 232	22 821	5,40%
2002/2003	21 793	1 250	23 043	5,42%
2003/2004	22 336	1 257	23 593	5,33%
2004/2005	22 336	1 257	23 593	5,33%
2005/2006	45 237	2 675	47 912	5,58%
2006/2007	70 816	3 909	74 795	5,23%
2007	97 639	5 311	102 950	5,16%

Source: Status of OCFCU 2007

Most female members are widows. Being a member of a Fairtrade cooperative gives them a better chance to survive because of the higher income. Another possibility is to work on the board of a cooperative. The elected get training in their respective area, and attend meetings at the union level. I did not see or hear about any female general manager of a cooperative, but what I found was that it is not rare that a board member is female.⁸⁶ Having the right to occupy a higher position in a cooperative is positive, but it is not clear if the women who did participate would have done so if the cooperative had not been Fairtrade certified.

⁸⁵ Todaro and Smith (2006) p. 229

⁸⁶ The accountant of Negele Gorbitu cooperative of OCFCU and a member of the control committee, Nenko Yimamu, of the Voca cooperative of YCFCU are examples of women occupying higher positions in cooperatives

6. Conclusion

Economic development is a process that changes the society in economic, social and political ways. People that have very little endowments alter their lives fundamentally with higher living standards, and in turn push societal transformation. I have been looking at the factors that are the triggers. Overall, Fairtrade in Oromia and Yirgacheffe Cooperatives has achieved what it is aiming to do according to the definition presented in chapter 4. It is a trading partnership, which proved to be stronger in OCFCU than in YCFCU. It contributes to development by seeking greater equity in international trade (increasing absolute and relative profits of farmers) and securing the rights of producers (good working conditions). Fairtrade supports producers in awareness raising (education about coffee prices and practises), but does not inform about fair trade or the rules and practises of conventional trade.

Small-scale farmers engaged in coffee production live in rural areas where poverty is widespread. Coffee prices are extremely volatile, which puts farmers in a vulnerable position. Fairtrade gives the opportunity to unprivileged farmers to get a stable income that often is higher than for conventional coffee. The impact of Fairtrade is clear in times of low coffee prices on the world market, when cooperatives operate at a loss and Fairtrade successfully protects farmers from bankruptcy and extreme poverty. There is no guarantee that a certain percentage of consumer prices go directly to the farmer, but the minimum price helps farmers to plan ahead, which enables them to take conscious business decisions that positively affects their future (it may be to invest in their childrens' education or to diversify into value added coffee). There is an emphasis on sustainability in terms of environment, production, and economic growth, which has a noticeable influence on the work of the cooperatives. The Fairtrade premium that is invested for social development is strengthening the society and provides services that would otherwise not be accessible. Overall quality of life is expected to increase as the investments from premium money come into place. Unions give training to raise coffee farmers' knowledge of prices and quality, which increases their bargaining position in the local market, and allows for access to new markets that increases exports. The cooperatives presence in the Ethiopian rural areas increases competition and enables them to get a higher price for their coffee. The economic benefit from Fairtrade is visible. However there are several weak points that obstruct success and should be highlighted.

The biggest problems unions and cooperatives face are lack of finances which prevents them from providing education and supporting the work at the farmer level. The technical assistance aimed at decreasing the environmental impact of production and increasing

productivity is not given regularly. Beans are year after year of mixed quality and productivity is continuously low. Low membership participation is creating a free-riding problem and cooperatives continue to be weak. Mismanagement inhibits economic growth. Farmers' low knowledge of money and finance creates obstacles for the cooperatives and individuals and prohibits them from enjoying the full advantages of fair trade.

The work of YCFCU focuses on economic profits, while OCFCU drives developmental projects on the side of coffee, many concerning crop diversification. The platform of Fairtrade facilitates initiatives such as the Oromia Bank, a successful attempt to build a new institution to provide for something that society does not provide. The cooperative could be an engine for development of itself, depending on its organization. The present cooperatives have a democratic organizational structure but participation of members is low. The problem is persistent, and if there is no involvement there is little empowerment and socio-economic change. Likewise, cooperatives provide formal equality of opportunity to all its members, but it is not enforced on a practical basis and there is therefore a long road to achieving gender equality. Therefore, in the light of Fairtrade rhetoric, there is more to wish for.

6.1 Fairtrade in the Future

Fairtrade in Ethiopia started as a top-down implementation, and initiatives are still coming from the top. This is ironic because the initial idea of Fairtrade is a grass-root driven system. It cannot be required that uneducated impoverished farmers to know about Fairtrade's role in the market when not even westerners, who have access to the information, understand it. But the possibilities for development within the frames of fair trade are big and it would be a success if they were used. If they are democratic, transparent and participation is high they could contribute to social capital, a cornerstone for any democracy.

It seems to be that the development aim of Fairtrade is more important to consumers than to producers. The meaning of Fairtrade is stressed to consuming countries as a marketing strategy to raise the willingness to pay, but Fairtrade means often nothing more to farmers than a higher income. Consumers, who, by buying Fairtrade goods invest in cooperatives, want to see sustainable growth and development. Producers get most value from cash for the moment and this causes a wedge between the vision of Fairtrade and the reality at the farms. YCFCU, which is facing the possibility of being left outside the profitable specialty market, is prepared to get another certification if the last inspection fails, reflecting the view that Fairtrade is only one possibility of getting better income amongst other alternatives and not

necessarily the best. Fairtrade must effectively communicate its vision towards both consumers and producers if it is to be a long lasting and continuous way to alleviate poverty.

Fairtrade in Ethiopia is a recent phenomenon and as a new actor on the market it faces a number of challenges, as discussed above. However, these problems can most likely be eliminated in time with good managerial competencies. In the meantime Ethiopia is facing a boosting Brazilian coffee production and Vietnam as a new export country, as well as the competition from neighbouring African countries. The strategy to add value to the green bean before export must be complementary to quality improvements to raise the reputation of the coffee unions, and it requires good marketing as well as better products. The Fairtrade market is an excellent way to go about it because of the positive image of the brand, and the market share is expanding every year.

It is a problem that the market is not big enough for all fair trade produced coffee. This restriction means that some farmers can sell all their production as Fairtrade and enjoy its benefits, while some can sell parts of it, and others are fully excluded from the market and its benefits. Consumption of Fairtrade certified goods are sky-rocketing in many countries, which is making the future look bright for the brand, but the question is if it is because of a genuine interest or because of temporary fair trade hype. Cowe and Williams (2000) found in a survey that 30 % of the population is particularly motivated to buy ethical goods and services, but that such products only account for 3 % of their markets.⁸⁷ It seems like there is a growing awareness amongst consumers of the “unfairness” of the global trading system, but the success of the mainstreaming strategy of Fairtrade will depend on whether it can make consumers choose the “right” product in the shop.

A few privileged farmers that have access to the profitable fair trade market enjoy a higher quality of life, which to a large extent is derived from higher incomes. As the present system works, with entrance barriers in the form of certification fees and demand restrictions on Fairtrade products, not all farmers can join. Marginalized producers will still be marginalized unless a change comes about in the domestic setting. Institutional changes are needed to give all farmers access to information and equal opportunities to do business. An example is the middlemen in rural markets. Fairtrade identifies middlemen as a problem of the imperfect market – competition is too low – and its policy is to by-pass them. Rightly, it is generally known in Ethiopia that private coffee exporters have high profit margins. As long as

⁸⁷ Cowe and Williams (2000) p 1

these kinds of problems remain there will be a need for producer organizations, and a need for fair trade.

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