CF 10/13
17 December 2013
Original: English

E

3rd Consultative Forum on Coffee Sector Finance
10 September 2013
Belo Horizonte, Brazil

Summary report of the 3rd Consultative Forum on Coffee Sector Finance

Background

1. The 3rd Consultative Forum on Coffee Sector Finance took place during the 111th Session of the International Coffee Council in Belo Horizonte, Brazil in September 2013. In March 2013, the Core Group on the Consultative Forum agreed that the topic for the 3rd Forum would be aggregation. Furthermore, the Core Group decided to establish a small working group comprising Brazil, Colombia, Guatemala, Mexico, the USA, Core Group experts and the Chairperson of the Forum who would work intersessionally on the preparations for the 3rd Forum, including participants and financing.

2. The 3rd Forum was facilitated by Mr Robert Nelson, Chief Executive Officer of the National Coffee Association of USA (NCA) and received sponsorship from the All Japan Coffee Association (AJCA) and the World Bank.

REPORT ON THE 3RD CONSULTATIVE FORUM ON COFFEE SECTOR FINANCE

Executive Summary

1. The Consultative Forum on Coffee Sector Finance is an initiative by the International Coffee Organization to facilitate consultations on topics related to finance and risk management in the coffee sector. It has a particular focus on the needs and wellbeing of small and medium-scale producers and local communities in coffee-producing areas.

2. The Forum met for the third time in Belo Horizonte, Brazil, on 10 September 2013 during the 111th session of the International Coffee Council. This was an all-day event, with over 100 participants. A core nucleus of 22 experts was also created in order to facilitate the discussions. The topic of the event had previously been selected as 'farmer aggregation' to identify best practices through which access to finance and risk management could be achieved more effectively.

3. In the morning session, participants discussed seven case studies, providing examples of cooperatives at various stages of development. This process helped to set the context of farmer aggregation and the challenges faced by cooperatives.

4. The afternoon session was composed of a structured brainstorming session, using the force-field problem-solving model, in order to identify environmental forces which are conducive to farmer aggregation and those which create barriers. As a result of this exercise, participants identified three priority 'driving forces' and four priority 'restraining forces' which were considered key to creating an enabling environment. These forces were finalized as follows:

i. Driving Forces:

(1) Market incentives for farmers to organise
(2) Examples of successful cooperatives
(3) Management and leadership skills

ii. Restraining Forces:

(1) Lack of female participation
(2) Lack of education about cooperatives
(3) Poor legal framework and corruption
(4) Risk aversion and risk management

5. Each priority force was then considered in depth to put together implementation strategies which are to form a roadmap for the future work of the Core Group of the International Coffee Council.

INTRODUCTION

1. The 3rd Consultative Forum on Coffee Sector Finance was held on 10 September 2013 in Belo Horizonte, Brazil, during the 111th session of the International Coffee Council. Over 100 participants took part, including a core nucleus of 22 experts specifically identified by the organisers. There was broad representation among participants from exporting and importing countries, as well as from various institutional backgrounds, including public, private and non-profit sectors.

2. The objective of the event was to identify best practices and disseminate information to Members about farmer aggregation as a platform through which access to finance and risk management could be achieved more effectively. The topic of farmer aggregation was agreed in March 2013 by the International Coffee Council, in order to show how successful, well-organised farmer groups could be a vehicle for managing risk and access to finance, as well as delivering other benefits to farmers, such as training, education and information dissemination.

3. The Consultative Forum was set up by the International Coffee Agreement 2007 to facilitate consultation on topics related to finance and risk management in the coffee sector, with a particular emphasis on the needs of small and medium scale producers. The first Consultative Forum took place in September 2011 and focused on existing and future risk management tools associated with green coffee price volatility. The second was held in March 2012 and discussed the role of producer associations, governments and other entities in making risk management and financing tools more accessible to small and medium size producers.

PRESENTATIONS

Dan Zook, Dalberg: Farmer Aggregation and Access to Finance

4. Mr Zook gave an overview of the topic of farmer aggregation, focusing on the potential opportunities created and why they were not always realised. He described the agricultural sector in developing countries, which was growing rapidly and how demand for certified agricultural products was now exceeding supply. Smallholder farmers were therefore becoming an essential component for buyers to ensure supply chain consistency and traceability. Aggregation could help smallholder farmers to increase production through five channels, namely: access to finance; improved production and processing; decreased transaction costs and increased economies of scale; access to markets; and policy advocacy. Furthermore, as producer groups become more mature and obtain firm contracts from buyers, banks are more willing to step in and provide lending, which helps producers to increase their yields.

5. However, smallholder lending is still very small in comparison to other commercial funding, and does not come close to covering demand. The question was therefore asked: why are more farmers not involved in producer organisations? Various historic reasons for this lack of participation were offered, including previous state intervention; low internal capacity; exclusion of women; weak governance and leadership; and insufficient access to resources. However, these barriers could be countered by supporting donors, public agencies and corporations to partner more effectively with farmer organisations, enabling them to better meet the market-oriented needs of their members. Ensuring feedback mechanisms to identify the best practices and incorporating the views of farmers, as well as integrating incentives for farmer organisations to incorporate women and smallholders, can also promote their development. Finally, an enabling environment is crucial to creating effective organisations, so it is necessary to remove regulatory hurdles and ensure effective oversight.

Alex Serrano, NCBA Clusa: Farmer Organization and Aggregation

6. NCBA Clusa is the largest trade organisation in the United States, with over $650 billion in annual sales and $3 trillion in assets. It is also an international development agency with experience working in over 80 countries in Africa, Asia and Latin America. Mr Serrano presented three models of farmer organisation outreach: firstly, Community-Based Solution Providers (CBSPs), which are more informal farmer groups where extension services are provided to farmers and any fee is based on a commission from sales. Secondly, midsize farmer organisations usually contain a few hundred farmers, aggregating around 1,000 tonnes of output, who are provided with financing, bulking and technical services. Finally, large cooperatives serve thousands of farmers, offering a wide range of business solutions, including agricultural processing, technology and service clustering. Large cooperatives are managed by professionals who are accountable to a Board, and usually focus on a single commodity.

7. Mr Serrano outlined seven ‘Cooperative Principles’, which could be interpreted as either a strength or as a liability, depending on how they are implemented:

a) **Voluntary & Open Membership:** Cooperatives are voluntary organisations, open to all people able to use its services and willing to accept the responsibilities of membership, without gender, racial, political or religious discrimination.

b) **Democratic Member Control:** Cooperatives are democratic organisations controlled by their Members who actively participate in setting their policies and making decisions.

c) **Member Economic Participation:** Members contribute to the capital rather than outside investors. Members benefit in proportion to the business they conduct with the cooperative rather than on the capital invested.

d) **Autonomy & Independence:** Cooperatives are autonomous, self-help organisations controlled by their members. If the cooperative enters into agreements with other organisations or raises capital from external sources, it is done so based on terms that ensure democratic control by the members and maintains the cooperative's autonomy.

e) **Education, Training and Information:** Cooperatives provide education and training for members, elected representatives, managers and employees so they can contribute effectively to the development of their cooperative. Members also inform the general public about the nature and benefits of cooperatives.

f) **Cooperation among Cooperatives:** Cooperatives serve their members most effectively and strengthen the cooperative sector by working together through local, national, regional and international structures. Cooperatives often lack necessary resources to meet all the needs of their members, and can achieve greater economies of scale by working with other coops.

g) **Concern for Community:** While focusing on member needs, cooperatives work for the sustainable development of communities through policies and programmes accepted by the members.

He finished by noting that the secret to a successful cooperative is to be pragmatic, rather than dogmatic.

Lakshmi Venkatachalam, Asian Development Bank:
Emerging Sustainable Commodity Value Chains in Asia

8. The Asian Development Bank (ADB) is committed to inclusive and sustainable growth in the Asia-Pacific region, with food security in particular accounting for a major aspect of this work. Future food demand is projected to increase by 60% by 2050 as the world population increases to nine billion. As a result, food productivity needs to be doubled by addressing inefficiencies in the supply chain. This applies to more than just agricultural productivity, as 60-70% of the cost of food comes from post-harvest activities.

9. This is leading to a paradigm shift in global supply chains, as increasing demand prospects and supply sustainability concerns realign global sourcing strategies. Many companies have therefore started sourcing through aggregation, i.e. farmer groups, in order to secure a stable supply of quality raw materials. Integrating smallholder farmers into commodity supply chains benefits both long-term corporate sourcing strategies and food

security. Vertical integration at the global and regional level can increase productivity and encourage sustainable agricultural practices, while income gains at the household level directly enhance the food security of the rural poor. Emerging private-public partnerships for agricultural commodities offer new financing and aggregation opportunities.

10. The main challenge of this model will be scaling up to reach a transformational level, which will require a favourable regulatory framework. The public sector will play a crucial role by investing in infrastructure and creating the enabling policy environment in order to support the private sector. The ADB already directly invests in agribusiness and supports agricultural commodity value chain development through its trade finance and supply chain finance programmes.

CASE STUDIES

11. Seven case studies, giving examples of cooperatives at various stages of development, put together by the World Bank and NCBA Clusa, were distributed to participants in advance of the Forum. Participants were then split into groups, aiming for geographical and expertise diversity, to discuss a specific case study, along with guiding questions. Each group subsequently presented the study and questions to the rest of the Forum for discussion. The seven case studies were as follows:

a. The pre-cooperative phase: The first step in farmer organizations
b. The emerging phase: Registration as a legal entity
c. The growth phase (I): Reaching critical mass
d. The growth phase (II): Meeting the never-ending challenges
e. The emerging cooperative phase: Deciding to stay together
f. The established and growing phase: How should we grow
g. Mature cooperative phase: Growing and consolidating a coffee relationship

12. In the discussions resulting from this scenario exercise, several recurring themes were found, offering guidelines for best practices in the sector, and what main concerns were encountered in the development of successful cooperatives. These recurring themes include governance, capacity, quantity versus quality, sustainability and risk management.

i. Governance and management

13. The most consistent issue coming out of the discussions was the need for strong and competent leadership, free from political bias and government intervention. Farmers need to trust their Board, and this must be done through increased transparency, improved

communication channels and involving farmers in the decision-making process. Limited engagement with farmers results in autocratic management; a successful cooperative needs to engage with its members and encourage feedback from farmers. Increasing grassroots democracy and participation will benefit member loyalty and commitment to the cooperative. Furthermore, improving the internal processes of the cooperative will hold management accountable and thus improve governance. This can be achieved through a firm legal framework, which gives the cooperative the power to act relatively autonomously, while maintaining checks and balances on the management structure.

ii. Capacity and training

14. A lack of technical knowledge was frequently cited as a major challenge to successful cooperatives. This applies to both the technical capacity of farmers and also the competence of the cooperative itself. Encouraging the development of human resources, through extension services or donor programmes, can bring multiple benefits. The degree or type of training will vary according to the size and maturity of the cooperative; for example, small emerging cooperatives might benefit from basic administrative training whereas midsize organisations could require education on the use of more advanced financial instruments such as supplier credit or forward contracts.

iii. Quality versus Quantity

15. A consistent challenge of cooperatives at all stages of development was the conflict between quantity and quality of production. Coffee importers require a certain consistency of supply which the cooperative needs to meet. It is therefore the cooperative's task to communicate these business requirements to its members. The push towards quality comes with risks and costs, such as the price of inputs or the cost and responsibilities of certification. The cooperative needs to make the case to its farmers of the benefits of increased quality, for example through obtaining a premium price in the specialty market.

iv. Sustainability

16. The question of sustainability was predominantly an issue of balancing short-term against long-term priorities. For example, in some cases this was a matter of short-term food security rather than long-term economic security. For a cooperative to remain competitive over time, it needs to maintain good agricultural practices and ensure a relatively consistent supply. This is not always possible in the short term due to competing priorities. The cooperative needs to build up its reputation in order to remain financially stable, as well as maintaining good business practices. It was considered that it can be easier

to establish a cooperative than it is to maintain one, particularly when attempting to expand and grow the organisation. Finally, a concern was expressed regarding the role of donor organisations, who occasionally were looking for quick fixes rather than long-term progress.

v. Risk management and price volatility

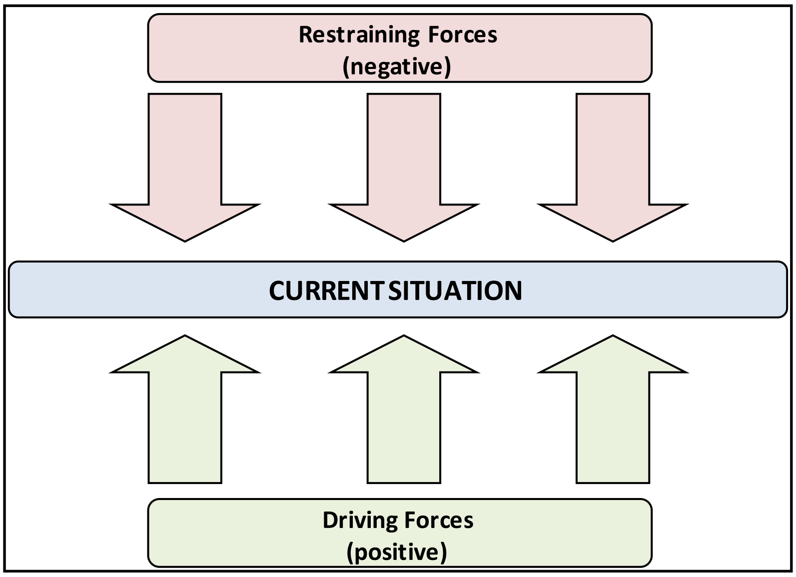
17. Several of the case studies highlighted how farmer organisations can help with risk management, through multiple channels. Firstly, by aggregating producers and production, cooperatives have increased access to sources of finance, whether through public grants, subsidies loans or specialised credit lines. Similarly, a cooperative can undertake diversification programmes away from coffee to offset some degree of risk, which would not be feasible for individual farmers. Furthermore, a cooperative has the potential to protect against falling prices by accessing certification programmes that pay a premium over the market prices. However, these potential strategies are dependent on the institutional framework of the cooperative, which might require all members to agree on a certain course of action. Finally, there were some concerns expressed over the inherent risks associated with being dependent on a single buyer, which cooperatives might want to take into consideration.

18. Clearly, there is a certain degree of overlap between these issues, with many cutting across more than one specific theme. For example, the need to increase the quality of coffee production can be approached through capacity-building, and will likely also require strong leadership and clear communication channels. This is not meant to be an exclusive list of relevant issues, but rather a highlight of recurring themes to set the context for further discussion.

FORCE FIELD PROBLEM-SOLVING EXERCISE

19. The Forum used a ‘force field problem-solving model’ to identify current environmental factors which are supportive to farmer aggregation (‘driving forces’), and those that create barriers to aggregation (‘restraining forces’). During this exercise participants were encouraged to suggest ideas without judgement; to emphasise the quantity of ideas rather than their quality, and to focus on creative thinking.

Figure 1: Force field problem-solving model



20. During the brainstorming session that followed, the Forum identified 105 driving forces which facilitate aggregation, and 82 restraining forces that inhibit it. A full list of both forces is available in the Annex. Subsequently, the Forum undertook a process of prioritisation, narrowing down the full list to three or four priority forces; the ones that would be implemented in an ideal world.

21. The next step was to evaluate each priority force individually and identify specific actions and strategies to facilitate the establishment of farmer organisations. These strategies could then be used as a springboard for the ICO to develop in future meetings.

i. Driving Forces

22. There was a wide-ranging discussion on the merits and feasibility of the 106 driving forces which had been identified during the brainstorming session. The overall goal was to identify specific actions which could help facilitate the main motivating factors. There were certain forces which, though considered important, had no corresponding actions to undertake. The priority driving forces and their respective implementing strategies as identified by the Forum were as follows.

a) **Market incentives:** how to use market forces and economic incentives to encourage farmer aggregation and create an enabling environment for producer organisations. For example, identifying a common buyer for a group of producers can help to ensure that there is adequate demand for output and thereby encourage aggregated production. Market incentives can also be used to promote sustainable coffee production and provide more income security for farmers.

Implementing Strategies:

- Identify buyers and encourage them to purchase from organisations which meet certain standards.
- Buyers can also bring financial institutions to the table, identifying potential beneficiaries for both sides. Financial institutions are more likely to provide finance if a buyer is already in place.
- Certification agencies can communicate with potential lenders on where the demand for finance is most pressing. There is no shortage of demand for finance, but lenders need information on credit-worthiness.
- Create market incentives for farmers to produce in quantity, as this will encourage aggregation.

b) **Examples of successful cooperatives:** how to create a sense of excitement around the concept of farmer aggregation. By finding and disseminating success stories of how producer organisations can provide multiple benefits, and showing how these benefits are passed on to farmers, other producers might be more inclined to participate. Although it was emphasised that organisation might not be the optimal strategy for every producer, information on the potential benefits should be well documented and more easily available.

Implementing Strategies:

- Prepare case studies of successful cooperatives to identify what they did right and the potential benefits to achieve.
- In addition, identify failures in order to show what not to do, and mistakes to avoid in order to improve.
- Establish a competition for the best cooperative in order to encourage participation. Alternatively, establish a competition for donors or other institutions to identify and work with the best case study.
- Create an exchange programme between successful and less successful cooperatives, or between cooperatives in different geographic regions, so that farmers, particularly leaders, can learn from one another.

c) **Management and leadership skills:** how to enhance the administrative capacity of farmer organisations. The success of well-run cooperatives is often attributed to the capacity of their management. By increasing the institutional capacity of the relevant leaders, producer organisations will be more likely to succeed and therefore bring benefits to their members.

Implementing Strategies:

- Identify young powerful leaders, for example through exchange programmes.
- Find management development programmes and disseminate this information to farming communities.
- Human resource development for all levels of management, particularly in administrative skills such as accounting or auditing.

ii. *Restraining Forces*

a) **Lack of female participation:** The disenfranchisement of women from engaging in the running and composition of cooperatives was considered a major obstacle to future development. It is therefore essential that female participation in such organisations be enhanced.

Implementing Strategies:

- Remove legal constraints to registering women, particularly with respect to property rights.
- Develop policy advice to governments on gender integration.
- Encourage buyers or financial institutions to require a minimum percentage of female participation, or devise special financing facilities for female cooperatives.
- The cooperative itself could mandate a minimum percentage of women members in its regulatory framework.

b) **Lack of education about cooperatives:** This issue has two aspects. Firstly, members of a cooperative can be uninformed about its benefits and details; secondly, there can be a lack of awareness outside the organisation about how it works and how to work with them.

Implementing Strategies:

- Introduce the fundamentals of farmer organisations into the curriculum in primary schools.
- Train farmers' children on the basics of various management skills necessary for successful cooperatives, for example accounting or agronomy.
- Provide training on the rights, responsibilities and obligations of cooperative membership.

- Train farmers on aspects of the coffee trade beyond farming, such as financial management.
- Educate bankers and buyers about cooperatives and farmer organisations.

c) **Poor legal framework and corruption:** This issue is intertwined with the local political situation in many countries. Although considered one of the most important impediments to successful aggregation, there is a limit to the extent of potential actions. Any programmes in this area need to be well targeted with tenable objectives.

Implementing Strategies:

- Develop a transparency scorecard system, along the lines of those used by certification standards.
- Provide governance training that includes elements such as oversight and fiduciary responsibility.
- Undertake a review of best practices, including current laws, regulations and policies which are conducive to farmer organisation. Identify which countries thrive and why, and disseminate such information to governments, cooperative members and the private sector.
- Develop a code of ethics or conduct which cooperatives could implement.

d) **Risk aversion and risk management:** The element of risk contains two main factors. Farmers may be risk averse and therefore unwilling to join a cooperative. There is also the element of price risk management which affects coffee farmers across the spectrum, not just in cooperatives.

Implementing Strategies:

- Educate farmers on how to appear less risky to financial institutions, for example by diversifying beyond just coffee production.
- Promote both vertical and horizontal diversification, that is, the production of crops other than coffee, but also into other areas of the coffee value chain.
- Inform non-members about the potential benefits of organisation, such as access to finance and reduced exposure to risk.
- Identify potential mechanisms to provide finance to cooperatives, to develop appropriate risk management techniques.

NEXT STEPS/ROADMAP

The contents of this document are intended to serve as a roadmap for the ICO going forward. The outcomes of the Forum will be used to identify and implement strategies for risk management and finance solutions. It is also expected that the priorities and strategies identified by the 3rd Forum will form the basis of Core Group discussions and future Forum activities.

FULL LIST OF DRIVING FORCES

1. A significant event
2. Ability to apply complex tools
3. Access for women
4. Access to finance
5. Access to information
6. Adaptation to climate change
7. Agricultural insurance
8. Asset ownership
9. Banks looking for clients
10. Bargaining power
11. Basic research
12. Certainty of income stream
13. Cheap financing
14. Common buyer
15. Common cuisine
16. Common ethnicity
17. Common political party
18. Common religion
19. Common threats
20. Community activism
21. Consumer interest
22. Corruption
23. Credibility
24. Culture
25. Demand
26. Demand for certification
27. Demand for common services
28. Demand for quality
29. Demand for quantity
30. Demand for sustainable coffee
31. Demand for traceability
32. Democratic culture
33. Desire for higher prices
34. Desperation
35. Difficulty competing against firms
36. Dissatisfaction with current system
37. Distribution of agricultural inputs
38. Donor and NGO programmes
39. Economies of scale
40. Efficiencies
41. Environmental pressures
42. Examples of successful groups
43. Farmer problems
44. Farmers' voice in policymaking
45. Follow up of statistics by regulatory bodies
46. Global trade
47. Good examples/ success stories
48. Greater accountability
49. Higher primary and secondary education rates
50. Higher profitability
51. History of organisation
52. Homogenous groups
53. Increased development of rural infrastructure
54. Information Technology
55. Infrastructure
56. Internal trust development
57. Internet
58. Lack of competition
59. Land title
60. Leadership
61. Literacy
62. Logistics
63. Long-term planning
64. Low coffee prices
65. Loyalty
66. Management skills
67. Market access
68. Market intransparency
69. Market needs of retail brands
70. Need for better product
71. Need for finance
72. Need for higher prices at farm gate
73. Need for improved leadership
74. Need for inputs
75. Obtaining critical mass for downstream processing
76. Open mindedness
77. Optimism
78. Organised market systems
79. Peace and stability
80. Peer pressure
81. Power base for politics
82. Pre and post natal care
83. Presence of a leader
84. Presence of catalyst
85. Promotion
86. Reduced cost of collecting data
87. Reduced transaction costs
88. Regional economic development
89. Regular supply of basic needs
90. Regulatory environment
91. Respect for rule of law
92. Security for farmers and their assets
93. Self respect and confidence
94. Social and community services
95. Storage
96. Strong church groups
97. Strong cooperative movement
98. Strong extension services (public or private)
99. Supply of basic needs at a fair price
100. Taxation
101. The next generation
102. Transparency communication
103. Trust
104. Vision
105. Withdrawal of governments

ANNEX II

FULL LIST OF RESTRAINING FORCES

1. Absence of expected results
2. Adverse regulation
3. Age
4. Aversion to change
5. Aversion to rules
6. Bad experiences
7. Bureaucracy
8. Conflict
9. Conservative thinking
10. Corrupt leadership
11. Corruption
12. Cost
13. Coyotes
14. Discrimination
15. Egos
16. Exploitation by monopolies
17. Fear of change
18. Financial sector suspicion of cooperatives
19. Forced organisations
20. Forced resettlement
21. Geographical location
22. Hunger
23. Ignorance
24. Impact of climate change
25. Increased cost of borrowing
26. Inflexible cooperative models
27. Insecurity
28. Institutional resistance
29. Interference by Boards
30. Interference of local government
31. Isolated farmers
32. Isolation
33. Lack of competition in banking sector
34. Lack of education about cooperatives
35. Lack of female participation
36. Lack of good management
37. Lack of government capacity for cooperative development
38. Lack of information
39. Lack of leadership
40. Lack of motivation
41. Lack of resources
42. Lack of support from NGOs etc
43. Lack of time
44. Lack of trust
45. Lack of understanding in banking sector about coops
46. Lack of vision
47. Lack of young members
48. Little capacity to increase education levels
49. Mentality of dependency
50. Misconceptions
51. Mistrust
52. Monopolies
53. No payment
54. No recognition of female role
55. Non-transparency
56. Not enough good leaders or managers
57. Ownership status
58. Paternalism
59. Perceptions about cooperatives
60. Personal conflicts
61. Perverse incentives
62. Politics
63. Poor communication
64. Poor information dissemination
65. Poor infrastructure
66. Poor legal frameworks
67. Poor member participation
68. Poor prior experiences
69. Poor support of financial institutions
70. Price volatility
71. Profitable for some
72. Rebel threats
73. Risk adverse
74. Selfishness
75. Short-term thinking
76. Tax liability
77. The law
78. Under educated population
79. Unfair competition
80. Urgent and basic needs
81. Very transparent and efficient market system
82. Vested interests