THE PRICE OF

GREEN COFFEE

In this first installment of a three-part series on green coffee procurement, **RACHEL NORTHROP** *breaks down the various factors that add dollars to the cost of every container of specialty coffee.*

Understanding the price of green coffee requires accepting—for now—that the C market futures contract price is the benchmark. Most pricing is derived from it.

Like all economic and financial tools, agricultural futures markets have complex histories. Today, these markets remain liquid due to the mix of physical stakeholders, coffee exporters, importers, and roasters who deal in actual green coffee. Speculators also participate in the market out of financial interest alone.

If this sounds abstract, that's because it is. Global markets reflect global averages of supply, demand, currency exchange rates, and general sentiments. Coffee pricing can be closely tied to quality differentials based on origin and physical specifications, such as screen size and defect count, yet completely disconnected from the actual communities, people, and realities on the ground where coffee is grown.

Specialty coffee, however, is increasingly taking into consideration the local costs of production when determining price. This is true particularly in the segment of specialty coffee concerned less with cup score and more with purchasing coffee as a financially and ecologically sustainable investment. In this scenario, price is influenced by politics, government regulations, labor markets, climate conditions, and cost of all inputs required to produce coffee—from truck fuel to fertilizers—at origin.

Being connected to origin means the costs of doing business with individual farms and geographic regions will ultimately impact the price paid by specialty coffee and its consumers. This price still needs to account for the normal market factors of scarcity and perceived value, which will continue to drive negotiations between all vendors and sellers.

To see how pricing varies from origin to origin, let's take a look at two very different countries—Ethiopia and Nicaragua.

FACTORS AFFECTING PRICE: ETHIOPIA

"The price of Ethiopian specialty coffee can be affected by several factors," explains Adham Yonis, manager of **Testi Coffee**, a family-owned Ethiopian specialty coffee producer and exporter. "The main factors include weather, which includes droughts, insufficient rain, and not enough sunshine on time. When there are negative weather factors, the volume of coffee goes down, which makes the market go up locally."

Testi Coffee, established in 2009, owns a farm and several washing stations. The company participates in

PHOTOS COURTESY OF TESTI COFFEE

Coffee cherries travel from the farm to washing stations and drying beds at **TESTI COFFEE** a family-owned producer and exporter in Ethiopia.

the local market as a buyer of coffee and as a grower.

Changes in weather affect production levels, and fluctuations in production levels affect how much the washing stations in the local market will pay smallholders for the cherries they deliver.

"Another factor is unrealistic speculation at the washing station or farm level when purchasing red cherries to process," Yonis explains. Speculation is the anticipation of an outcome; how much coffee the region is expected to produce.

The third factor is disease. "When coffee trees are affected, it drastically reduces production volume," Yonis says. If cherry prices were low because the harvest was expected to be large, but ultimately was tiny, then producers could receive a low price for a reduced total harvest. It is not uncommon for the combination of speculation and disease to lead to lower total revenue.

Informed sourcing can sometimes correct for losses as a result of weather, speculation, or disease. But in the end, pricing is still very tightly linked to quality. At the Ethiopia Commodity Exchange (ECX), quality is expressed in both physical and sensorial terms.

"The ECX plays a big role in determining price, because the price that farmers are paid for their coffee is largely determined by grade, and that grade is determined by the ECX," explains Micah Sherer, green buyer with **Ally Coffee**.

"The exchange evaluates coffee based on color, physical defect, green aroma, screen size, moisture content, and cup score, then gives it a grade. When the coffee is sold on the exchange, it is paid for based on how it was graded. The ECX is supposed to ensure that farmers are paid a fair market price for their coffee based on its quality."

All specialty lots must be graded by the Ethiopia Commodity Exchange and then sold for at least that grade's price. In Nicaragua, however, there is no national system for assigning value based on quality outlined by standardized parameters.

FACTORS AFFECTING PRICE: NICARAGUA

Jorge Lagos Calix is a coffee farmer from Dipilto, Nicaragua. He outlines the differences between the costs of producing specialty and conventional coffee in a country where there is no guarantee what a given quality will be sold for. Unlike farmers in Ethiopia, Nicaraguan producers must carefully calculate their production costs to set sustainable prices when offering coffee to buyers.

"Even though the specialty coffee sector affords more opportunities to get higher prices than C contract »

NICARAGUA: Jorge Lagos Calix (left and center right) at Finca Santa Teresa in Dipilto, Nicaragua

pricing, we also face higher costs than conventional operations," Lagos explains. "To get quality to fit our customer's expectations, we have to manage less productive varieties. These varieties are also vulnerable to coffee leaf rust, which means we need to establish a program to control the disease. Conventional disease control is not as intensive as specialty."

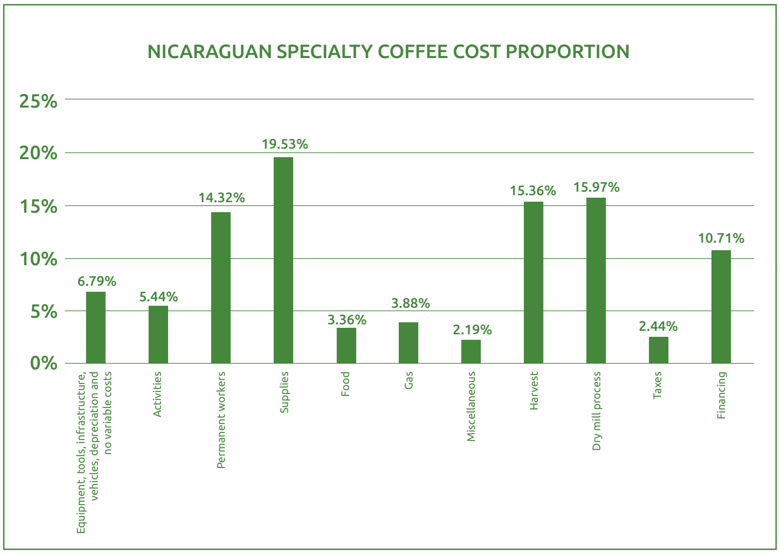
Factors influencing price begin with the trees and continue through processing. "Specialty coffee has a high cost of processing at the dry mill because of the pursuit of the perfect cup," Lagos notes. "To control, manage, and process coffees separately from conventional, we use specialized personnel and equipment, and we meet customer specifications."

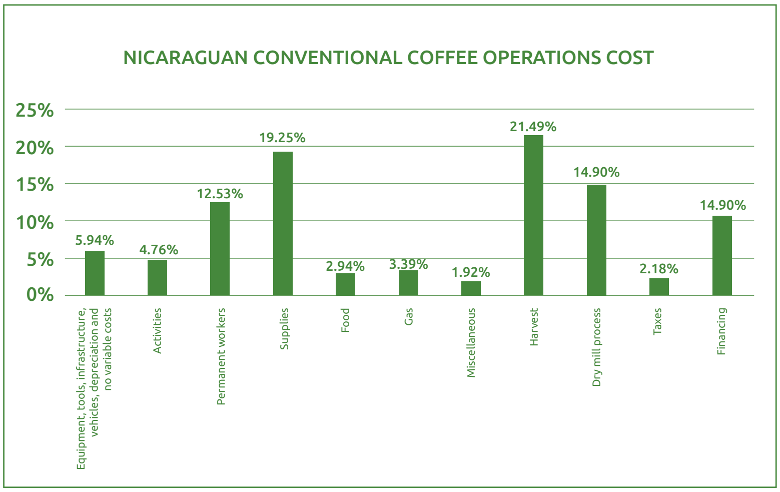
Paying skilled labor for selective manual picking adds yet another layer of costs. To better understand this difference in his community, Lagos conducted a survey of neighboring producers. He evaluated two cost scenarios for coffee operations: specialty versus conventional. (See graphic.)

Lagos gathered data from nine specialty operations in Dipilto and four conventional operations in Matagalpa and Jinotega. He calculated costs from the first day after finishing harvest to the last day of next year's harvest (April 2017–February 2018).

He found that to produce twice as much commercial coffee as specialty coffee results in only a 14 percent increase in costs. A bag of specialty coffee costs 74 percent more to produce than a bag of conventional coffee. Specialty coffee's pursuit of exceptional quality comes at almost double the cost. But the reality is that even if exceptional quality is not achieved, as reflected by high cupping scores and sensorial profiles, those initial costs still remain.

In both conventional and specialty coffee production, the *percentages* of cost categories are similar, but the *dollar amounts* across categories are increased threefold.





QUALITY VERSUS COST IN THE CUP

The coffee commodity market is driven by market pressures and, ultimately, what buyers are willing to pay for it. Whereas the specialty market is driven by the desire to procure the best quality possible, ideally for the lowest possible price.

But a new method for assigning value to green coffee is evolving. This method accounts for not only the costs of production—for instance, specialty coffee from a farm in Dipilto, Nicaragua—but also for the administrative and labor costs of keeping coffee separate during its international journey.

In this scenario, producers put in supreme effort to improve traceability, though higher prices are far from guaranteed. Not every lot that was expensive to produce will cup at 90 points.

Should producers who put in the extra effort be underpaid, often for reasons beyond their control, such as when roasters score their product too low to justify a higher price tag? The answer to that question will test specialty coffee's commitment to quality and to the people who help achieve it. FC

PART TWO of this series on green coffee procurement will outline ways in which roasters can ask themselves questions about how they determine worth and value—through cup profile alone or through a comprehensive review of production techniques—prior to sampling green coffee. When a coffee's price is easier to dissect and its decisive parameters are clear from the outset, each coffee can find a buyer who will pay its full price and pass its comprehensive value on to final consumers.

PHOTOS COURTESY OF JORGE LAGOS CALIX