

CURRENT STATUS AND PROSPECTS FOR COFFEE INDUSTRY IN THE NEW MILLENIUM

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BACKGROUND

1.1 Coffee in Agriculture and the Economy

Between 1992 and 1998, earnings from coffee accounted for over 41 percent of total agricultural export earnings (Figure 1), 12% of total exports including minerals, and 5% of PNG's Gross Domestic Product (GDP).

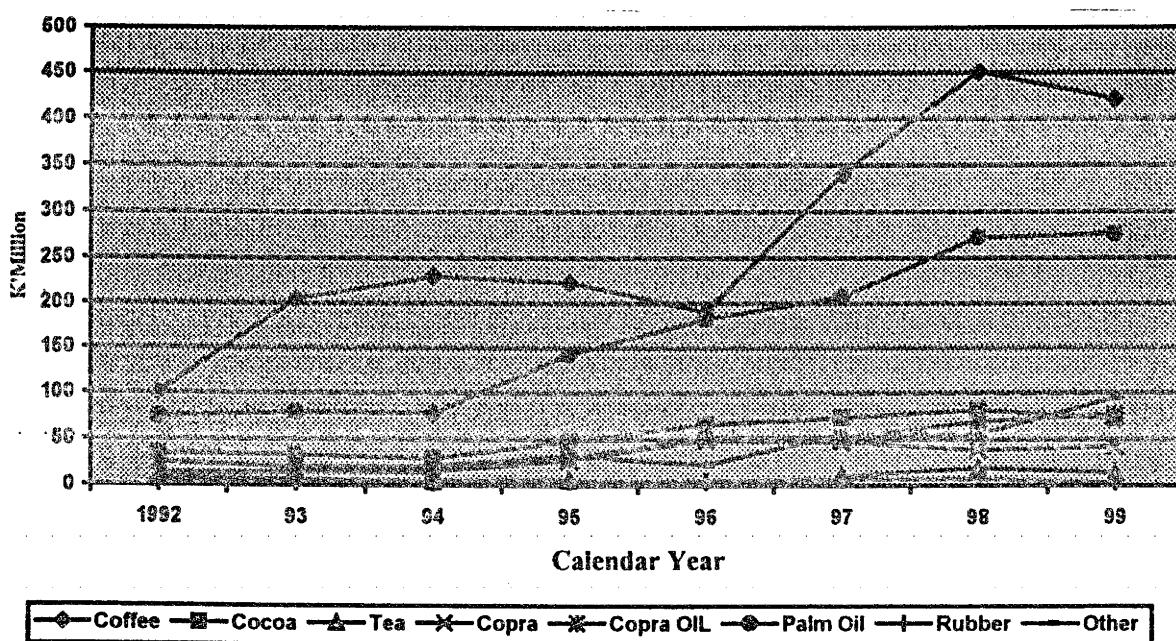
About 2.0 million people (i.e. half of PNG's population) depended on coffee as their major source of cash income, and an important part of PNG

culture and business, particularly in major producing provinces. The industry has important linkages with other sectors of the economy and is also a net foreign exchange earner.

Over 85 percent of coffee exported every year is produced by smallholders who use very little cash inputs. It is unquestionably, the major agricultural export earner, a main source of cash income and creates employment for a significant number of people.

Coffee is a renewable resource. It was here well

Figure 1. Total PNG agricultural export earnings between 1992 & 1998.



Source: Bank of PNG and CIC

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before the mineral and oil boom, and will be here when mineral and oils are gone together with their proceeds.

1.2 Coffee Industry Corporation

The industry regulatory body was first established as a Coffee Marketing Board in 1964, and later Coffee Industry Board (CIB). With the amalgamation of Research and Extension, Coffee Industry Corporation was established in 1992 under the company's Act and comprised of four divisions;

1. Industry Affairs
2. Corporate Services
3. Coffee Research Institute, and
4. Extension Services Division.

The Industry Affairs takes over the function of the CIB and is mainly involved in market promotion, economic studies, export and quality control, monitoring of prices and marketing margins, export and processing licensing. Corporate Services is responsible for the efficient and effective management of the Corporation's finance and personnel administration, while Research and Extension takes over the functions of conducting applied coffee research and providing extension services respectively.

1.2.1 Mission Statements of the Corporation are;

- Maximise financial returns to all coffee producers, and
- Contribute to the Government's economic and social goals

As a member of PNG Chapter of Transparency International and its determination to ensure profits by all from lessons of past, the CIC's standard watch words governing its operations are;

- Prudence in the Spending of Resources
- Transparency in all undertakings
- Objectivity in all plans and strategies

1.2.2 Main Objectives

The objectives of the Corporation's Corporate Plan 1998 - 2002 are to;

1. Enhance the size and quality of coffee
2. Enhance the efficiency and sustainability of Coffee Industry
3. Minimize incidence of pests and diseases
4. Represent PNG in World Coffee Trade to ensure the legality, fairness and positive relationship rules at all times
5. Promote interest in coffee growing as part of a secure and a rewarding activity, particularly amongst women and youths
6. Enhance the financial returns to growers by encouraging competition and seeking new market opportunities
7. Facilitate the effective involvement of all industry sectors in the management and control of the industry.

2. CURRENT TRENDS AND DEVELOPMENT

2.1 Production and Exports

Over 95% of production is washed mild arabica coffee while the remaining 5% is washed robusta produced mainly in the East Sepik and Madang provinces. Arabica is high altitude crop while robusta grows well on lowland areas.

Smallholder sector is the industry's "back-bone", accounting for about 70% of annual production, followed by Plantations (20%) and Blocks (10%). They are also the most efficient producers in terms of cash cost (estimated at about K127/tonne in 1993). Yields are estimated at 700 kilograms green bean/hectare. This is considered high when due to the fact that maintenance is minimal and application of fertilizer and other yield-enhancing inputs is nil or negligible.

Plantations and Blocks are high-cost producers and responsible for the PNG's reputation as producer of high quality mild arabica coffee. Their costs in 1997 were around at K3,411/tonne, which can only be profitable at prices above costs. Trend in production and export are depicted in Figure 2. Smallholder production is increasing while largeholder production is either stagnant or declining.

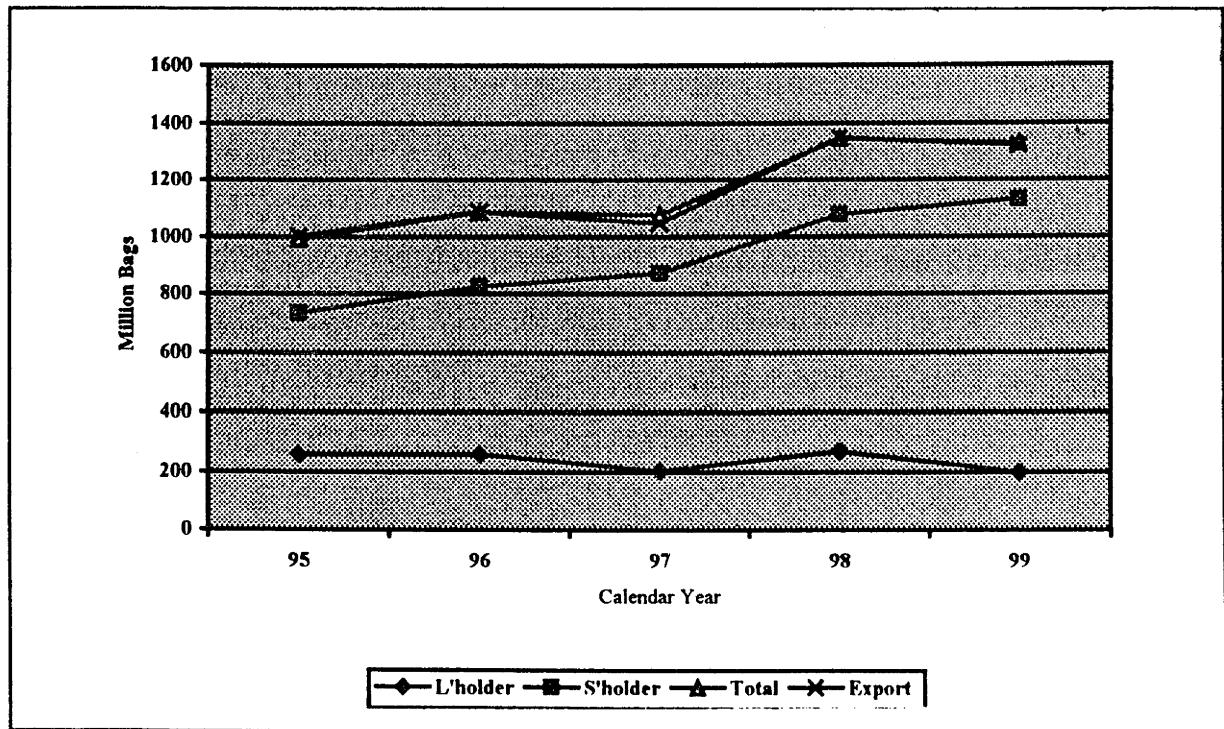


Figure 2. Production & Exports: 1995 - 1999

2.2 Volume & Value of Exports

Coffee exported from PNG averaged 1,050,000 bags (63,000 tonnes) over the past 8 years. Export earnings have averaged K138 million during the same period. In 1998, exports of 1.3 million bags earning over K451 million. In 1999 total green bean coffee exported is 1,320,000 bags valued at K421 million. Figure 3. Shows the value of export earnings from coffee over last six years. From a low of K190 million in 1996, it has increased significantly to over K451 million in 1998, and declined to K421 million in 1999. The decline in value is a result of declining production.

2.3 Prices

Free-on-board prices of green bean coffee over the last 11 years have shown that from 1989, price started declining and reached all time low of about K1,000/tonne in 1992. Since then, prices improved and reached K3,700/tonne in 1995 but fell again in 1996 to K2900/tonne. From

1997, prices improved significantly to reach a record high of K5,582/tonne in 1998.

Two main explanations for the significant increase are: depreciation of the kina following the floating of kina, and increase in international prices.

2.4 Stabilization Fund.

Following the depressed world market prices for extended period, the Government stepped in with Price Support Scheme. Total loan reached K140.7 million of which a significant component was repaid to the Government. The remaining balance of K52,416,671 from Stabex fund was converted to grant in February 1999.

The Board re-established the fund and it totalled K20.5 million at the end of January 2000.

2.5 Expansion Programme - MOA with Provincial Governments

In its efforts to increase production and expand

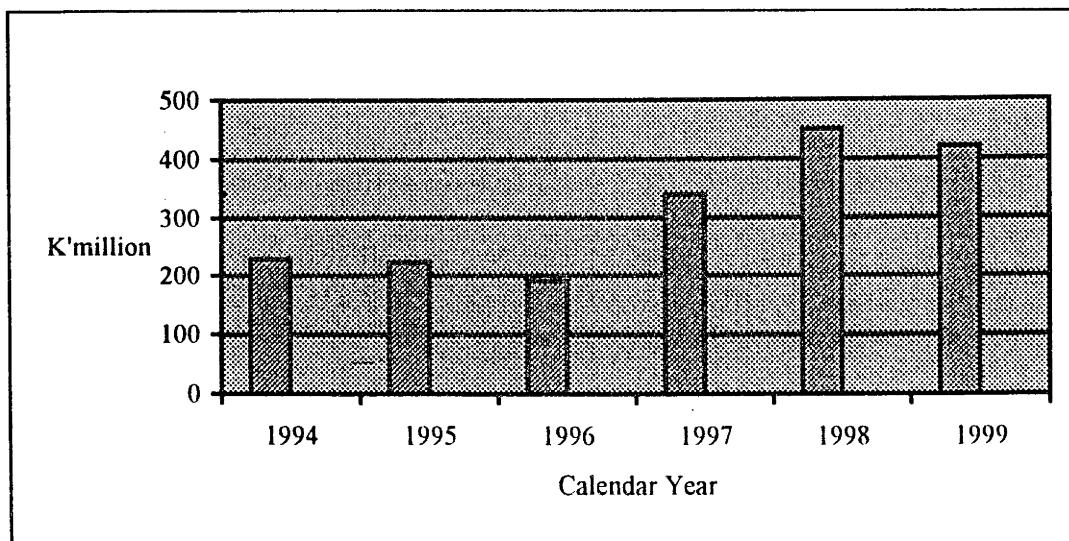


Figure 3. Value of Coffee Exports (K'million); 1994 - 1999

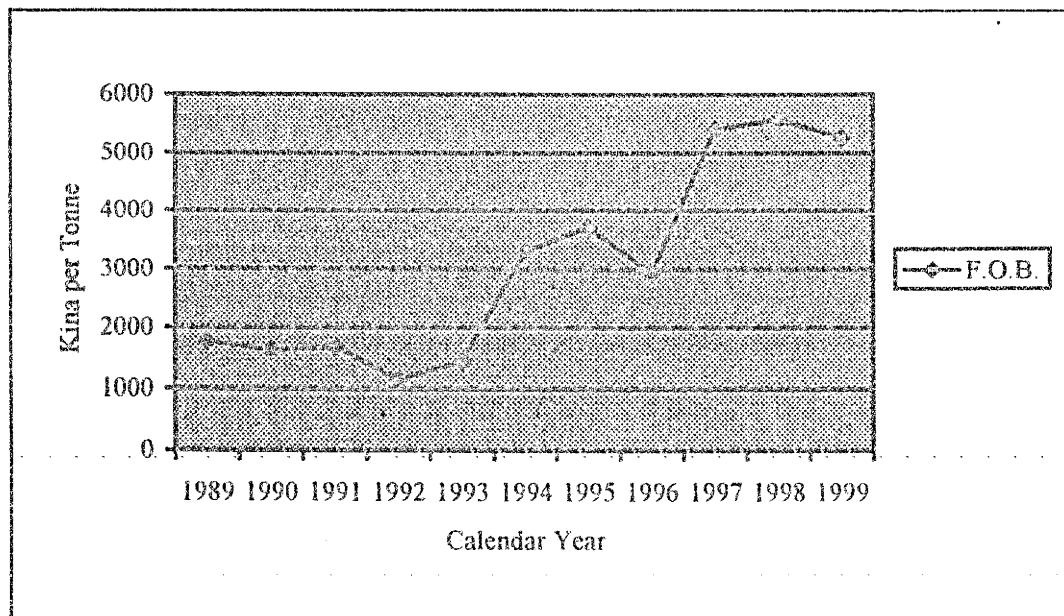


Figure 4. F.O.B. Coffee Prices; 1989 - 1999

coffee growing into regions and provinces with potential, the Corporation signed a number of MOAs with Provincial Governors and individual MPs. Those already signed include: Southern Highlands, Enga, New Ireland, East New Britain, Milne Bay, and Member for Komo Magarima for his electorate.

2.6 Coffee Nursery

The Corporation establishes coffee nurseries in central locations around the country to supply planting materials to farmers. These planting materials are subsidized by the Corporation to assist growers to have easy access to planting materials at reduced prices.

2.7 Coffee Credit Scheme

A total of K1,176,593 was approved and funded for over 1,491.07 hectares of coffee - mainly for smallholder rehabilitation and wet factories. Total repayment is K223,752.57 and this goes back into the revolving fund for further lending.

2.8 Freight Subsidy Scheme

Freight subsidy is an initiative of CIC with initial funding of K400,000 in 1999. Up to 40% of the cost of air freight is paid for by the CIC, while the remaining 60% is paid for by the growers.

Preliminary estimates shows that from K250,000 spent on freight subsidy in 1999, the industry earned more than K1.3 million. Given this success, K400,000 is being budgeted for 2000.

2.9 Promotion

Papua New Guinea Chairs the ICO Committee on promotion, particularly in Russia, Japan, China, and other Asian Countries. Our promotional activities in the last two years were undertaken with funding from the European Union. **Promotion of PNG Niugini Village Premium Coffee (NVPC)** was well received in Japan following successful trade show in late 1999. Already a container of NVPC coffee was exported to one of the big roasters in Japan.

3. STRATEGIES FOR SUSTAINABLE COFFEE DEVELOPMENT

From the year 2000 to 2004, the Corporation will give high priority to the following strategies;

- Establish strong linkges between farmer/extension/research and to remove competition for scarce resources;
- Continue with its restructure an rationalization programme to make the Corporation leaner, efficient, productive and cost effective;
- Improve smallholder coffee production and quality through the provision of subsidized pulpers, mini-credits and freight subsidies;
- Approach the government to review import duties on all agricultural inputs. There are practical problems associated with implementing VAT at the smallholder producer's level. Tax credit in terms of coffee pricing will have difficulty in implementing;
- Improve quality of PNG coffee to obtain premium prices;
- Strengthen traditional markets and aggressively promote into new markets for PNG coffee;
- Closely monitor price and marketing margins to ensure that growers receive a fair price.
- Develop central Coffee Marketing Depots (CMD) in more remote coffee growing areas.

The long term objective is to sustain production, quality, and ultimately growers income. The future of coffee industry rests with increased productivity, sustaining production and quality - not necessarily increased production.

To counter the highly volatile international prices, growers must be efficient to be competitive in the global markets.

4. PROSPECTS AND CONSTRAINTS

4.1 Prospects

- Generally, prospects of coffee industry continued to remain bright. This is clearly shown by trends in production over the years as discussed earlier. Potential for further development is in the smallholder sub-sector based on family units or individuals.

- As long as constraints impeding growth are removed and incentives provided, there is potential to increase production to double the present level to over 3 million bags. This also means income will double to over one billion kina - almost half the national Governments annual budget.

- Plantations and Blocks produces some of the best quality coffee in the world. Their profitability is reduced and costs increases as a result of a combination of factors including coffee theft, and law and order related problems. There is also lack of new investments in plantations.

4.2 Main Constraints

4.2.1 Budget Constraints. It was a general understanding between the National Government and Commodity Boards including then Coffee Industry Board (now CIC) when Corporatising, that level of funding will shift according to movements in international prices. When the prices are high, the industry Boards/Corporations will bear most of the operational funding component for research and extension. When prices fall, the government will bear most of the funding component.

Prices have fallen since last year, and continued into the first 7 months of year 2000. The international coffee market is currently saturated and it is expected that prices will remain low for some years to come unless bad weather hits major producing countries like Brazil.

The Corporation would require Government support for its research and extension services during this low coffee prices. Administration levy of 8 toea per kilogram is insufficient to fund the entire operation. To further add to funding shortfalls, production has declined this year as a result of bad weather. It is illogical to impose additional levy on the growers because they are already being hit by the current low prices.

The only option now available is for the Government to step in at this critical time. An estimated funding requirement from the government for the remainder of this year is K3 million, and K6 million per year from year 2001 onwards until prices improve.

4.2.2 The Coffee Industry Corporation fully endorses and supports all the recommendations made by the National Development Forum. Some of these include (but not limited to);

- Opposing the FAO proposal for Agriculture Reform, particularly relating to the Coffee Industry Corporation Act
- Poor infrastructure (roads, bridges, wharves)
- General Law & Order related problems and lack of community support
- Weak farmer/extension/research linkages as a result of very high extension/farmer ratio
- Inadequate marketing services for inaccessible areas
- High transport costs
- Inadequate private sector investment
- Volatile international prices
- Inadequate resources to support research and extension

- Limited access to credits
- VAT at the smallholder producer's level. Tax credit in terms of coffee pricing will have difficulty in implementation.

5. CONCLUSION

To conclude, I would like to re-emphasize the importance of coffee in the national economy and household income to growers. The industry was here before the oil and mineral boom, and will be here when they are gone. Any reforms to commodity boards should be based on CIC as a model.

I would also like to commend the Government for their continuous support over the years, through various assistance programmes. These include, price support, conversion of remaining price support loan to grant, and continuous funding for research and extension until 1999. I would also like to acknowledge, financial and technical assistance from international agencies including, AusAid and the European Union. The CIC will continue to look forward to assistance from the Government and International Agencies.