Sustainable Coffee Survey of the North American Specialty Coffee Industry

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Conducted for
The Summit Foundation
The Nature Conservancy
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Specialty Coffee Association of America
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Acknowledgments

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Executive Summary

As the coffee industry experiences some of the lowest green bean prices of the past hundred years (in real terms), high-quality and niche coffees are among the few receiving a more substantial remuneration. Organic, Shade, and Fair Trade coffees—collectively known as sustainable coffees—fill a market niche that is often rewarded with a premium price and can provide superior environmental, economic and social benefits to producers.

This survey, the largest of its kind, studies the characteristics and trend estimates of sustainable coffees across the full range of actors—from importers to retailers—in the North American specialty coffee market. Because data for these coffees is often sketchy and incomplete, additional research has considerably supplemented the baseline survey conducted in early 2001. This supplementary research is integrated into this document.

The marketplace is very much aware of these particular specialty coffees and a majority of firms surveyed carry at least one type. Substantial price premiums are currently earned for these coffees and most companies believe that these will continue in the near future.

In 2000 most firms experienced similar or increased sales of sustainable coffees compared to 1999 and approximately half expect these to increase over the next two years. Almost none project decreases. Among those who project increased sales, estimates of growth are approximately 27% over the next two years. The estimated North American market for *certified* sustainable coffees is approximately $152 million at retail. Total sustainable market value, including non-certified coffees that are marketed as sustainable i.e. bird-friendly, ranges to a rough estimation of about $188 million[1]. Global market estimations are approximately $565 million at retail.

Coffee quality rather than price, customer demand, or convenience of supply was found to be the overwhelming criterion for industry purchasing decisions. Consistency of supply ranked second in importance - understandable, given the costs and risks of sourcing from new suppliers.

Although each of these coffees has very specific criteria, as defined by their respective certifying agencies, the definitions and distinctions were often unclear to the firms surveyed. There is doubt whether some of the coffees termed sustainable in the marketplace truly are so because they lack third-party certification.

[1] The market estimations and retail values should only be taken as approximations because of statistical inference and cross calculations from various sources as well as the absence of empirical data.

Executive Summary continued…

More than two-thirds of the specialty coffee industry believes that certification of sustainable coffees will be important to their business in the future. Similarly, about two-thirds were in favor of a simpler way of communicating sustainability in the marketplace, in effect a super seal incorporating criteria from Organic, Shade, and Fair Trade coffees.

What are the main inferences that can be drawn from this study?

- The sustainable coffee segment is growing very fast.
- Industry is already benefiting, in terms of increasing sales and higher prices, from the product differentiation, improved quality and price premiums of sustainable coffees.
- The specialty coffee industry appears to understand that their future is intimately linked with the sustainability and quality of their supply.
- If industry is unclear over definitions, so are consumers. Providing education and information will be critical factors in expanding these market niches.
- Standardized terminology and consumer-friendly certification can help prevent confusion and erosion of support for this market segment.
- The industry is optimistic about the future of sustainable coffee.

Methodology

The survey was based on a list of more than 9000 coffee related firms supplied by the **Specialty Coffee Association of America** and the **Coffee Association of Canada**. More than 27,000 phone calls yielded a random sample of 2098. Statistically, the study presents a 95% confidence level that the margin of error is +/-2% for most questions. For some questions, where the sample size was necessarily smaller, the margin of error ranges +/-4%.

The survey included *(sample is greater than 2098 due to multiple answers):*

- 1558 retailers
- 570 roasters
- 312 wholesalers
- 120 distributors, and
- 94 importers

The survey response was balanced. Importers accounted for 4.7% of the total survey response (66% of the entire industry). Roaster wholesalers accounted for 15.5% of the response (66% of the industry). Roaster retailers were 12.9% of the survey (23% of the industry). Retailers were the largest group accounting for 64.9% of the survey (24% of the industry).

Most firms surveyed sell better quality coffees or niche market coffees commonly known as specialty coffees. Only respondents who were aware of one or more types of the specialty coffees defined as sustainable coffees (Organic, Fair Trade, and Shade) were included in the survey. The final sample was therefore reduced by 4.9% to eliminate those who had never heard of any of the sustainable coffees. The sample size for all charts and tables is between 1400 and 2089 firms.

Small businesses, with 2000 gross sales of less than $100,000 per year, comprised 23.2% of this survey. 14% of firms had gross sales in excess of $1 million. The median gross sales of respondents' companies as a whole were $326,400. Slightly less than one-half of those interviewed (45.6%) are members of the Specialty Coffee Association of America, and 2.7% are members of the Coffee Association of Canada. Most (70.5%) would like to be informed about new sources of sustainable coffees.

Those interviewed were located throughout every state and several territories of the United States and every province in Canada with the largest number being from California, Washington, Oregon, and New York. The survey was conducted between February 8, 2001 and April 6, 2001, individuals were interviewed from Research USA, Inc.'s facilities in Illinois.

Introduction

The specialty coffee market in brief

The U.S. handles about 1/4 of global coffee imports (2.45 billion pounds). Canada imports nearly 400 million pounds. The U.S. specialty coffee industry is responsible for only approximately 17% of the total U.S. green coffee imports mentioned above but its $7.8 billion sales represent approximately 40% of the $18.5 billion U.S. coffee market[2].

Total U.S. retail sales of specialty coffee beverages were $5.3 billion in 2000 while retail sales of specialty coffee beans reached $2.5 billion. It is the only segment of the coffee industry that has shown consistent and notable growth[3] and is the largest specialty coffee market in the world. According to the International Coffee Organization (ICO) and the SCAA, most potential specialty coffee markets are far from saturated. Specialty coffee sales continue to expand by 5% to 10% per year according to conservative estimates[4].

The North American specialty market therefore represents one of the largest and most vibrant coffee markets in the world. Its ability to develop strong new trends and influence global consumption is well documented. These reasons and its historic role as a market for many of the producing countries that are at the forefront of developing certifiably sustainable coffee production, make it the ideal target for the first large-scale industry survey of sustainable coffees.

Definition of sustainable coffees: Organic, Fair Trade, Shade

There is mounting evidence that much of the global coffee industry does not consistently meet two basic tests of sustainability: protection of the environment and social fairness. Nevertheless, a growing number of coffee producers, coffee companies and consumers are pioneering efforts to encourage the coffee industry to move toward more environmentally friendly practices and toward more economic and social benefits for producers. Three categories of coffees attempt to meet some or all of these criteria; they are Organic, Shade Grown and Fair Trade coffees. For the purposes of this survey, these are collectively termed "**sustainable coffees**".

The following terms served as brief and very basic definitions for the survey:

- *Organic coffee* is produced with methods that preserve the soil and prohibits the use of synthetic chemicals.

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[2] Specialty or gourmet coffees are distinct from average supermarket brands. SCAA Coffee Market Size 2000. SCAA 1999 Coffee Market Summary. ICO Production Statistics 2000/2001. ICO US market estimates do not take into account retail value and volume of coffee beverages in the food service segment.
[3] National Coffee Association (NCA) estimates average annual growth of about 30% in last five years.
[4] Specialty Coffee Assn. Estimates (T.Lingle). Annual Coffee Report 1998. 1999 International Coffee Organization (ICO). May 2000 ICO updates.

Introduction continued…

- *Fair Trade coffee* is purchased directly from cooperatives of small farmers that are guaranteed a minimum contract price.
- *Shade coffee* is grown in shaded forest settings and is good for biodiversity and birds.

Although each of these coffees has defined its own market channels and its own criteria, in practice many of these categories actually overlap, causing considerable confusion. For example, Fair Trade coffee is often but not necessarily Organic and Organic coffee is sometimes but not always grown under shade. For the purposes of this survey, we chose to make clear distinctions in order to distinguish the markets and accurately capture data.

Lack of information limits investments

Although interest in sustainable coffee is garnering increasing attention from consumers, trade organizations and producers, little reliable data exists about its markets and trends.

Lack of information significantly limits the willingness to invest in the long-term processes necessary to support sustainable coffee. The small farmers who risk venturing into this field, with or without the help of NGOs or publicly funded projects, are unable to assess the size, nature and composition of matching market channels. Conversely, downstream the importers, distributors, roasters and retailers who are interested, or potentially interested, in such coffee are less able to source it consistently and possibly less willing to invest in expanding what appears to be a not well-defined market. Industry is already benefiting from the product differentiation, improved quality and price premiums of sustainable coffees but the real success of sustainable coffee markets will rest on sustainable growers being fairly rewarded so that there is a continued synergy between them and the markets.

Survey goals

In order to ascertain both the supply of sustainable coffee to consumers and the constraints to its availability we surveyed key actors in the North American specialty coffee business (importers, distributors, roasters and retailers) to determine:

- the demand, including volume and pricing information
- the source of the demand
- bottlenecks to the demand and to its fulfillment
- market trends
- how the market can be developed by better understanding its characteristics

A. Awareness of Sustainable Coffee

We chose to make clear distinctions between the three types of sustainable coffee in order to more accurately capture data. For example, Shade coffee – the least well-defined in the marketplace – was used to mean coffee that not only uses the term, but is primarily and distinctly marketed as Shade coffee or bird-friendly coffee. There was, however, a noticeable tendency among respondents to blur or disregard these distinctions, despite the clear definitions. This and other evidence throughout the survey indicates that there is confusion about the three (3) different types of coffees and what each represents.

95.1% of the firms contacted were *aware* of at least one or more types of sustainable coffee:

- 98.7% were aware of Organic coffee
- 82.5% were aware of Fair Trade coffee
- 76.4% were aware of Shade coffee

B. Availability of Sustainable Coffee

When asked what types of sustainable coffees their suppliers offered, respondents replied that many offered at least one type of Organic coffee. Fair Trade and Shade coffee responses were strong but less definitive. Typically roasters and wholesalers (as opposed to retailers, importers, and distributors) tended to register a more ready supply of these three sustainable coffees. The importers noted reasonable but not universal access to these coffees, indicating a facile market opportunity for producers given that there are only approximately 100 substantial specialty coffee importers. Of these, 78.7% have Organic suppliers, 61.7% have Fair Trade suppliers, and 67% have suppliers who offer Shade coffee. Most suppliers who offer one type also tend to offer at least one of the others (86.2%). Table B.1 shows the entire industry average for each type of coffee.

Sustainable coffee type	**% of suppliers offering**	**% of suppliers <u>not</u> offering**
Organic Coffee	78.6	17.8
Fair Trade coffee	54.0	34.7
Shade coffee	51.8	35.0

Table B.1

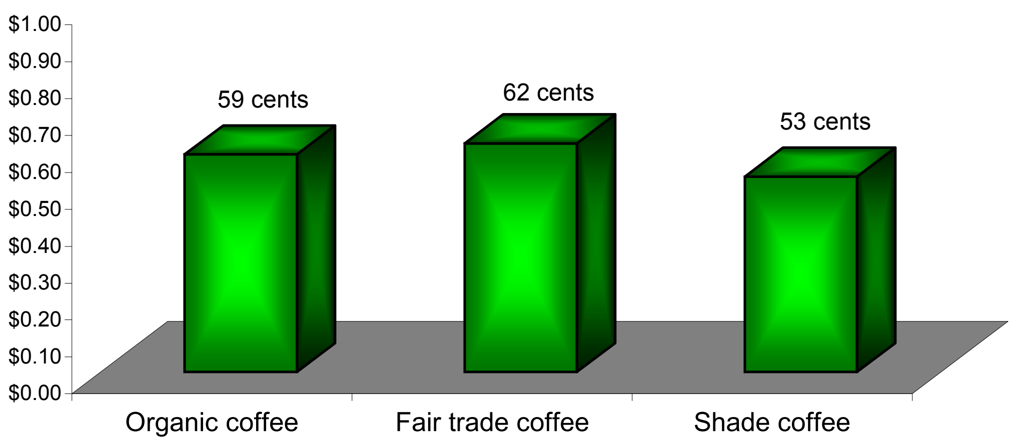
C. Price premiums

When asked "How much of a premium (in U.S. cents per pound) do your suppliers charge for Organic, Fair Trade, Shade coffees?" the respondents showed a remarkable range with statistically significant responses beginning as low as $.10 cents per pound and ranging in excess of $1.50. The industry average was between $0.53 and $0.62.

> Approximately 3/4 of firms feel that price premiums are reasonable and nearly 9 out of 10 firms expect them to continue.

Fair Trade fetched slightly higher premiums than Organic and Shade; this is likely due to the substantial difference between the Fair Trade floor price ($1.26) and the New York "C" market price over the past year. This is particularly notable in the considerably higher price paid by importers. This premium seems to smooth out somewhat as coffee passes down to the retail channels. Shade coffee commands only slightly lower (10% on average) premiums than Organic. Retailers typically pay higher premiums than other industry channels.

Average Amount of Premium Charged per Pound for Sustainable Coffees



C. Price premiums, continued

Premiums Paid for Sustainable Coffees			
	Organic	**Fair Trade**	**Shade**
Retailers	$.64	$.65	$.60
Roasters	.46	.51	.41
Wholesalers	.50	.58	.49
Distributors	.47	.48	.44
Importers	.36	.74	.35
Industry average	***.59***	***.62***	***.53***

Table C.1

Interestingly, for all three coffees, between 34.4% and 37.4% did not know the amount of the premium or gave no answer.

When asked if they feel that price premiums for sustainable coffees are reasonable, approximately 3/4 of the respondents answered "yes."

% of Firms That Feel Price Premiums Are Reasonable		
	Yes	**No**
Organic coffee	76.9%	16.8%
Fair Trade coffee	73.6	18.0
Shade coffee	73.7	18.0

Table C.2

When asked if they expect price premiums to continue for at least a few years, between 86% and 90% answered "yes" for all three types of coffees.

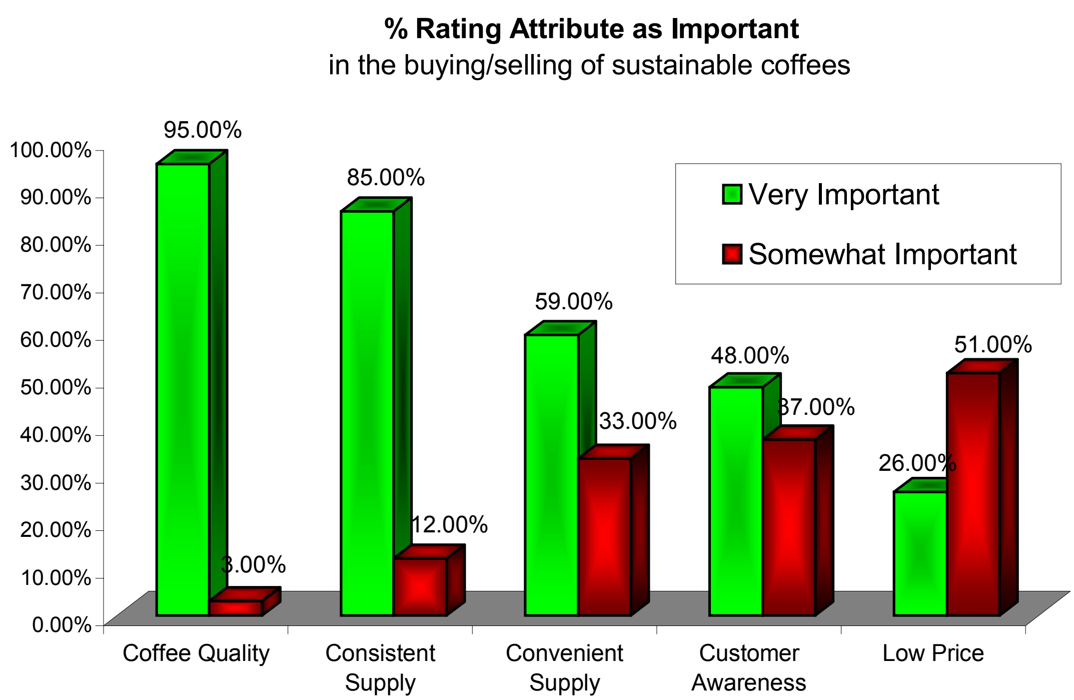
% of Firms That Expect Price Premiums to Continue		
	Yes	**No**
Organic coffee	90.0%	5.0%
Fair Trade coffee	87.9	6.6
Shade coffee	86.1	6.3

Table C.3

D. Important attributes for buying and selling sustainable coffee

Businesses were asked to rate how important (very, somewhat, not very, not at all) are the effects of five distinct factors to their buying or selling choices for sustainable coffee. Results for at least one factor concur with recent consumer surveys that found coffee quality to be a primary criterion for purchasing decisions[5]. Consistency of supply ranked second in importance and underscores the industry's typical preference for steady and predictable quality given the costs and risks of sourcing from new suppliers.

Next to last in importance is consumer awareness. This is an interesting indication that consumer demand may not currently be the primary driving force behind the sustainable coffee market. There are indications that the industry itself has played the key role in developing sustainable coffee markets by first providing the supply. It is clear that consumers have responded favorably when considering the growth trends for these coffees. Organics show approximately 20% growth over the last several years; Fair Trade has grown considerably, albeit from a very small base; Shade coffee, practically unknown to the market in 1997, is now marketed by a number of companies and growing strongly.



[5] Commission for Environmental Cooperation. 1999. Measuring Consumer Interest in Mexican Shade-Grown Coffee: An Assessment of the Canadian Mexican and U.S. Markets. CEC Secretariat. Page 10. Rice, P. McLean, J. 1999. Sustainable Coffee at the Crossroads. Consumer's Choice Council. Pps. 29 & 34.

E. Which sustainable coffees firms sell

Organic coffees are more frequently sold than either of the other sustainable coffees. Approximately 70% of enterprises surveyed sell one or more types. Taken in aggregate, from retailers to importers, 56.1% of the enterprises surveyed claim to sell Organic coffee while 36.8% claim to sell Fair Trade coffee and 34.4% Shade coffee. When these figures are cross-tabulated to extract only those enterprises that sell exclusively100% certified coffees, these numbers drop dramatically: 27% sell 100% certified Organic, 14% sell certified Fair Trade, 12% sell certified Shade coffee.

Third party certification or verification of coffees provides reasonable assurance that they are indeed sustainable coffees and truly meet internationally accepted standards for Organic, Fair Trade or Shade coffees. The absence of certification does not necessarily mean that coffees do not meet the standards or are not sustainable but it can raise doubts. More than two-thirds of the businesses surveyed felt that certification was somewhat or very important to their business.

A number of respondents assumed these three types of coffees were similar and sometimes interchangeable. Hence, for example, Shade coffee was sometimes considered the same as Organic coffee. In fact, many firms indicate or believe they are selling sustainable coffee although they lack independent certification or verification.

> There is considerable confusion about what the three terms Organic, Fair Trade and Shade actually mean. Failure to promote or educate about standardized terminology will very likely lead to the deterioration of terms such as "Shade coffee" until they are as meaningless to a consumer as the word "natural".

While many reputable firms prefer to support certification as a means of clearly confirming and conveying their adherence to the relevant certification principles, the data suggests that many more may be either ill-informed or taking advantage of the sustainable coffee terms like "Shade-grown" or "bird friendly". Some firms feel justified in using these terms even when there are only a few trees or a single species of tree on coffees farms and regardless of the clear scientific agreement on this criteria for Shade or

E. Which sustainable coffees firms sell, continued

bird-friendly coffees[6] and the existence of two recognized international certifiers. The obvious quandary here is that consumers will not know which terms to trust and which are merely green-washing or empty advertising. The indications of industry confusion or free-riding are supported by other survey questions. For example, a number of respondents claimed that Shade or Fair Trade certification was conducted by agencies that actually do not certify these and approximately half did not know who their certifier was.

Failure to clearly define and support certification will very likely lead to the erosion of terms such as “Shade coffee” until they are meaningless to a consumer. On the other hand, consumer education and industry support for standardized terminology and certification can enable truly sustainable growers to benefit from their efforts by being fairly rewarded in the marketplace. Such clear market signals will likely also encourage growers to continue producing reliable and high-quality coffees.

F. U.S. and Canadian primary markets for sustainable coffee

About two-fifths of respondents named the West Coast of the United States (41.9%) and the Midwest, Mountain, and Southwest (40.9%) as a primary market for their sales of sustainable coffee. Other regions of the U.S. named as primary markets were the Northeast (28.2%), South (22.6%), and Mid-Atlantic (19.4%).

In Canada, the West Coast was the leading region named as a primary market (by 9.6%) for sustainable coffee. Ontario (7.2%) and Quebec (5.7%) were the only other regions claimed as a primary market by more than 5% of respondents.

Among Canadian companies selling to the U.S. market, more sold to the Northeast and mid-Atlantic areas than anywhere else. In the Canadian domestic market, Ontario and the West Coast were the most popular primary markets.

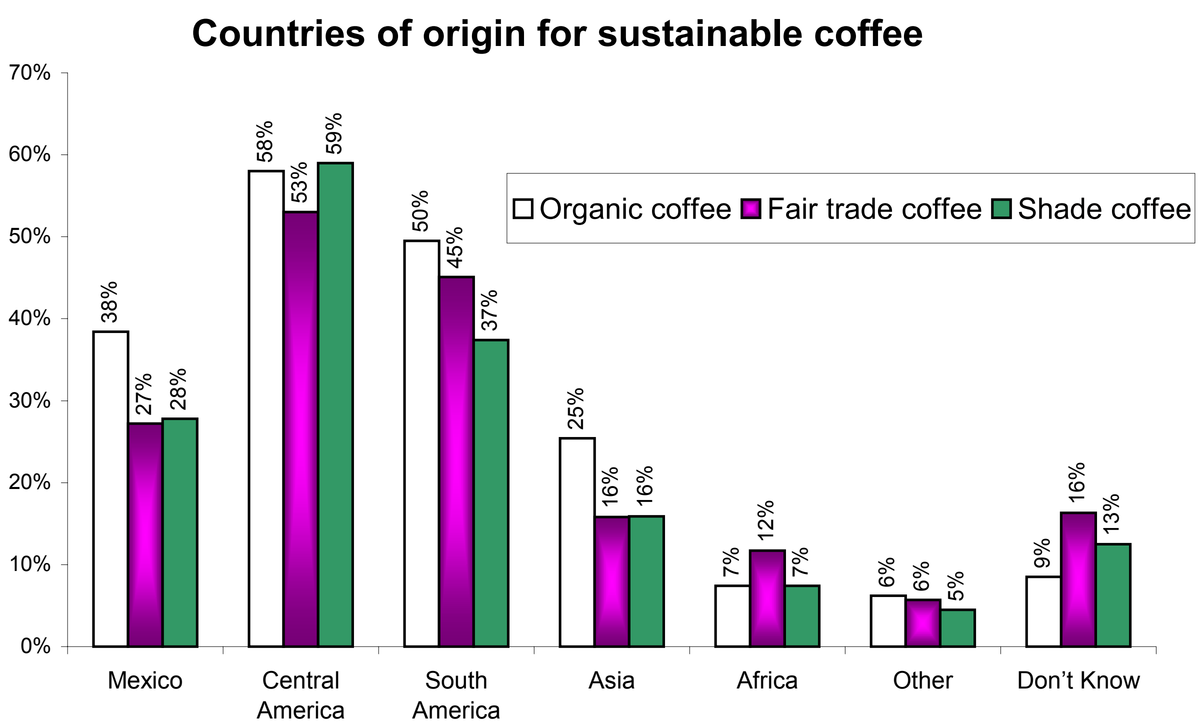
[6] Smithsonian Migratory Bird Center (SMBC) guidelines are the standard for certification and used by SMBC and Eco-OK as well as the CCC mediated Conservation Principles for Coffee Production and the forthcoming sustainable coffee certification in Mexico by Certimex and OCIA. These include a minimum of 10 native species and a minimum Shade coverage of 40% of the land.

G. Source countries for sustainable coffee

Latin America is, by far, the leading supplier of sustainable coffees.

Central America is the region that supplies more sustainable coffees than any other. South America is also a strong supplier, although much less so for Shade.

For Organic coffee Colombia, Costa Rica, Guatemala, Indonesia, Mexico, and Peru are claimed as the leading suppliers. For Fair Trade coffee responses indicate that Colombia, Costa Rica, Guatemala, and Mexico are the leading suppliers. Shade coffee responses also put Colombia, Costa Rica, Guatemala, and Mexico as the leading suppliers. Considerably more respondents did not know the country of origin for their Shade (12.5%) or Fair Trade (16.3%) coffees than did for their Organic coffees (8.5%).



G. Source countries for sustainable coffee, continued

Countries of origin for sustainable coffee			
	Organic	**Fair Trade**	**Shade**
Mexico	**38.4%**	**27.2%**	**27.8%**
Central America	**58.0**	**53.0**	**59.4**
Costa Rica	31.4	30.4	32.0
El Salvador	8.1	8.3	8.7
Guatemala	41.1	33.7	39.6
Nicaragua	14.4	13.9	16.4
Other Central America	3.3	3.7	5.7
South America	**49.5**	**45.1**	**37.4**
Brazil	10.8	14.1	8.0
Colombia	22.2	27.2	20.7
Peru	29.3	17.4	16.4
Other South America	4.1	4.3	3.3
Asia	**25.4**	**15.8**	**15.9**
Indonesia	24.0	15.4	14.7
Other Asia	1.9	.7	1.6
Africa	**7.4**	**11.7**	**7.4**
Other countries	6.2	5.7	4.5
Don't know/no answer	8.5	16.3	12.5

Table G.1

H. Factors that make sustainable coffee valuable to business

Coffee quality is more important than any other factor.

When asked how important each of the following 7 factors is in making sustainable coffee valuable to their business, the quality issue was confirmed as primary by 91.9% of the respondents who believe it is a v*ery important factor*.

1. Specialty quality or taste
2. Opportunity for differentiation
3. Customers are asking for it
4. Better profit margins
5. Personal beliefs about chemical-free agriculture
6. Personal beliefs about biodiversity or the environment
7. Personal ethics about fair trade for the growers

Surprisingly, customer requests, while important, are not seen as the most important factor. Only 50.9% rated these as *very important* and 29.3% as *somewhat important*. Customer demand is usually the primary driver for business, especially socially responsible business[7]. Given that its current growth, according to this survey, does not appear to have yet been solely because of consumer demand there could be considerable opportunities for market expansion.

The respondent firms' personal beliefs and ethics - numbers 5, 6, and 7 - appear to be approximately as valuable as customer demand with about half rating these as *very important* and about a third rating them as *somewhat important*. This indicates that addressing the coffee trade's beliefs and ethics with ongoing sustainable coffee information and education initiatives could be an efficient and cost-effective means of further developing the sustainable coffee markets.

Sustainable coffee rated as *somewhat important* to 44.6% of businesses as an opportunity for differentiation, that is, distinguishing oneself in the marketplace by providing a unique or different product line. Another 37.6% claimed this was *very important*. Earning better profit margins ranked lowest of the factors making sustainable coffee valuable to a firm.

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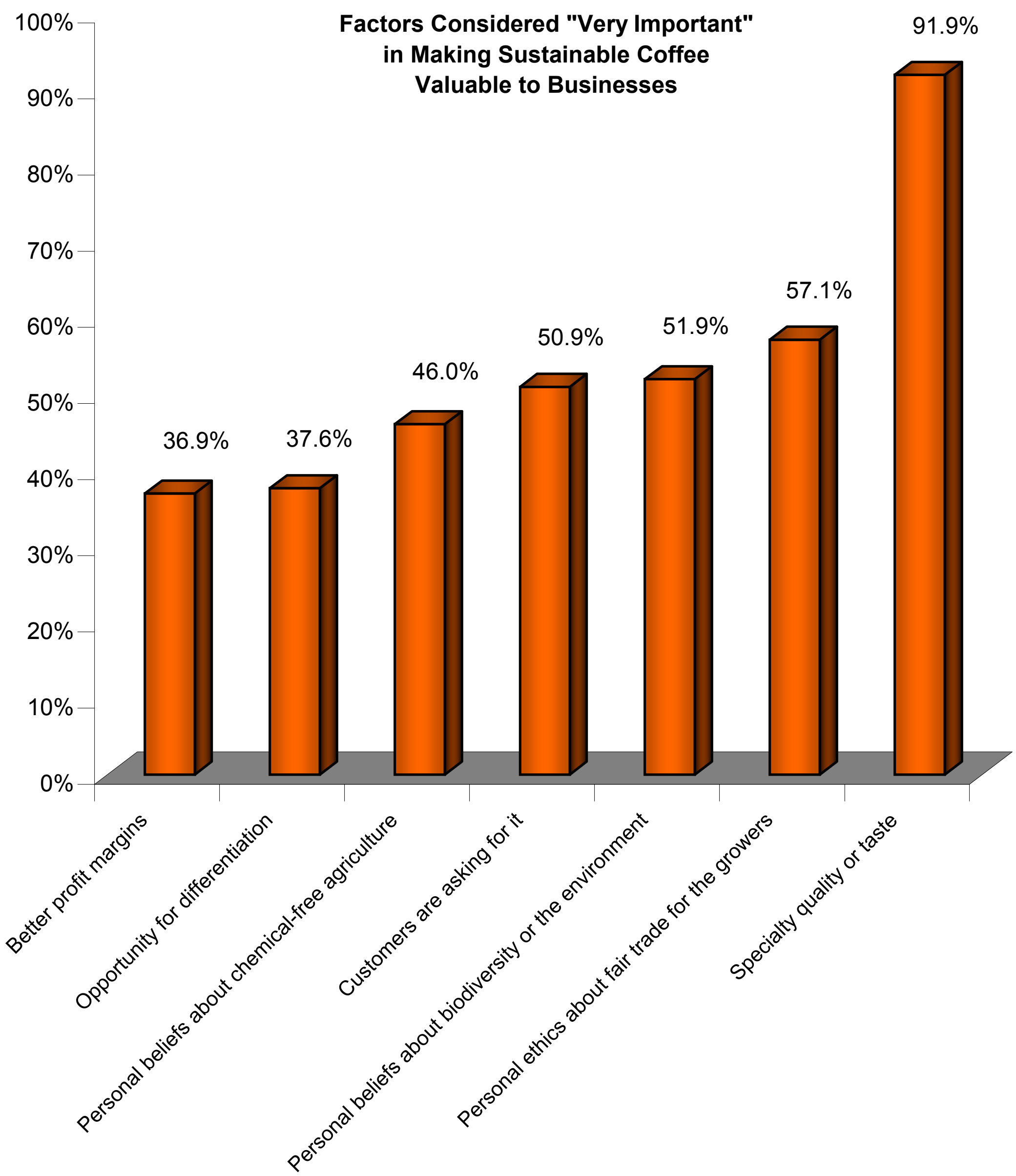
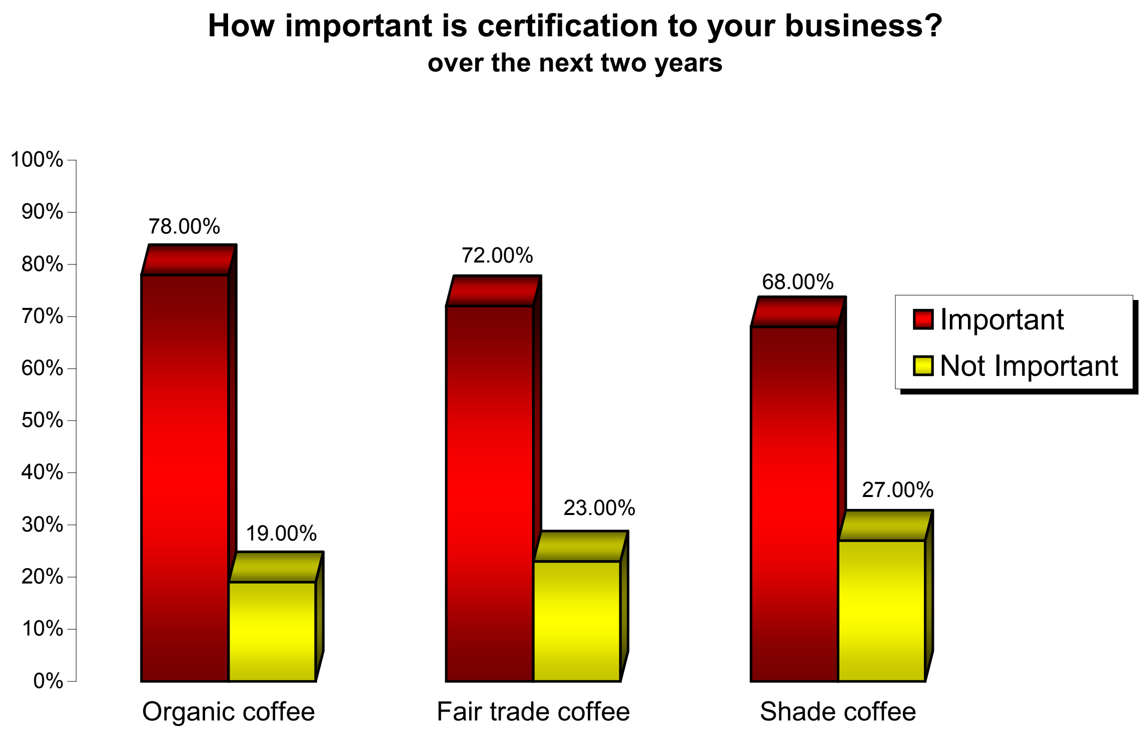
[7] Blowfield, M.2000. Fundamentals of Ethical Trading. In D.Giovannucci (Editor), The Guide to Developing Agricultural Markets and Agro-enterprises. The World Bank.

H. Factors that make sustainable coffee valuable to business, continued



I. Certification

A considerable majority of the businesses interviewed indicated that certification is *somewhat or very important* for their sustainable coffee business over the next two years. Approximately 68% to 78% affirm that certification would be somewhat or very important while between 19% and 27% believe that certification will be either not very important or not at all important.



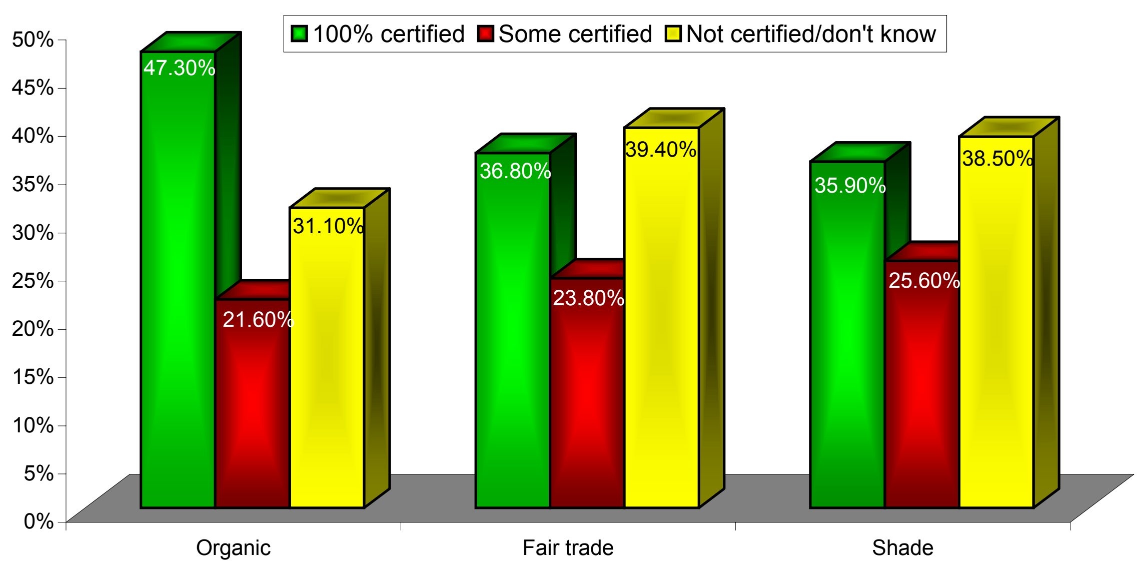
A surprisingly large number of firms did not know or did not answer which organization certifies their coffee. For Organic coffee respondents, 34.3% did not know or did not answer. This figure rose to more than 50% and 45% respectively for Fair Trade and Shade respondents. This lack of sureness or clarity about certification correlates to earlier findings that there is considerable weakness in terms of an accepted common terminology and clear definitions of these coffees.

OCIA was noted as the leading certifier of Organic coffees followed by QAI and Oregon Tilth. TransFair was noted as the leading certifier for Fair Trade. Smithsonian Migratory Bird Center and Eco-OK are the two certifiers for Shade coffee. It is worth noting that an earlier and open-ended version of this question yielded a considerable number of different certifiers who did not in fact provide such certification. This implies a measure of confusion within the coffee trade, particularly about Shade coffee certification.

I. Certification, continued

When asked what percentage of the sustainable coffee they sell is third party certified or independently verified, a considerable number did not know or gave no answer (22% Organic, 23% Shade, 29% Fair Trade). When combining those who don't know with those who claimed that none of their coffee is certified, these numbers represent considerable proportions for all enterprises, retailers to importers: 31% for Organic, 39% for Fair Trade, and 39% for Shade coffee. It could be that respondents are unaware of their certifications since many do not personally handle these, but the substantial responses could indicate a deeper concern for the industry: fraudulent coffee claims. As in the need to ensure accurate coffee origin, it will be critical to ensure that coffee marked as Organic, Fair Trade, or Shade, actually is so.

Percentage of coffee that is third-party certified or independently verified



Organic certification is more widely recognized and available than either Fair Trade or Shade. It is evident however, that certification in general still has a long way to go in terms of broad market visibility and acceptance. It is considered important for at least three reasons:

- It provides marketplace credibility and consistency of characteristics and claims
- It captures demand and price incentives of niche markets
- It “glues” participants to multiple objectives: commerce, conservation, and/or social justice by linking economic success to monitored certification principles

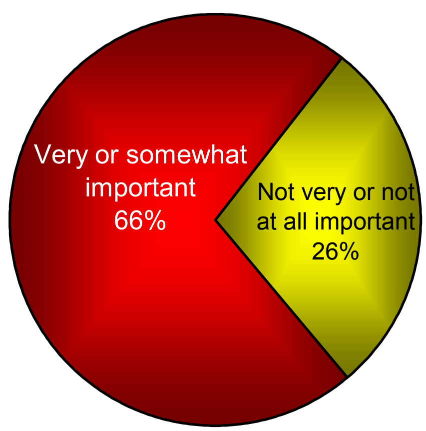
I. Certification, continued

Since there is no single definition for sustainable coffee and the three major types covered in this study all have different criteria, the result can be confusing. If members of the coffee industry are somewhat confused about the differences, then it is very likely to be even more difficult for consumers to understand sustainable coffee and make an informed decision. A simpler, all-encompassing certification or super seal has been proposed. Earlier studies showed limited demand for such a seal[8] but industry response is now clearly in favor.

> Most businesses claim that certification will be important for sustainable coffees. Two-thirds feel that a super seal, combining the criteria for the three sustainable coffees, is important for their business.

When asked, "How important to your business is a **super seal** that combines most, but not all, criteria for these sustainable coffees?" 66.1% considered it somewhat or very important while 26.1% considered it not very or not at all important.

Importance of Super Seal for sustainable coffees



[8] Rice, P. McLean, J. 1999. Sustainable Coffee at the Crossroads. The Consumer's Choice Council. Page 8. Also discussion and vote among group of about 300, at the SCAA Annual Conference April 2000, regarding a unified labeling system (super label) that could include Fair Trade, Shade and Organic aspects where a majority of those present were not in favor (49% against, 38 % in favor, 13% undecided).

J. Sustainable coffee volume and sales

Nearly 9 out of 10 companies report that sustainable coffee sales either increased or remained the same last year. Hardly any reported reduced sales. Most expect this positive trend to continue over the next two years.

The North American specialty coffee industry has grown considerably in the last 20 years. When divided into four major functional categories, there are approximately 150 importers, 500 roaster wholesalers, 1200 roaster retailers, and 6800 retailers. The market estimations and following retail market values should only be taken as approximations because of statistical inference and cross calculations.

Compared to 1999, gross sales of sustainable coffees for 2000 either remained the same or increased for nearly 87% of the respondents. Increases were reported by 30.5 percent of the respondents selling Shade coffee, 32.5% of those selling Fair Trade and 49.5% of those selling Organic. Decreases in the sustainable coffee business were reported by only 3.4% of the Organic sellers and 2.6% of the Fair Trade and Shade sellers.

Small businesses, with year 2000 gross sales of less than $100,000 per year, comprised 23.2% of this survey. Approximately 63% of firms registered gross sales between $100,000 and $1 million. 14% had gross sales in excess of $1 million. All of the data listed for firms assumes the entire company, which may be a single unit or multiple units.

There is no apparent correlation between the size of a business and whether it is inclined to carry Fair Trade coffee. However, small businesses are four times less likely than large ones to carry Organic coffees. Small businesses are only about 50% less likely to carry Shade coffee than large ones.

J. Sustainable coffee volume and sales, continued

> Total global retail market value for sustainable coffees is approximately US$ 565 million

Organic coffee

For the year 2000 importers that sold Organic coffees each claimed to sell on average approximately $184,000 worth of Organic green coffee. Extrapolating survey data one can estimate that North American specialty coffee importers sold approximately 4.9 million pounds. According to the Organic Trade Association (OTA), the majority of Organic coffees are sold through distribution channels other than specialty coffee retailers and cafes. The majority of these coffees are sold through grocery channels (health food stores) rather than through specialty coffee stores. Independent industry sources when accounting for the remaining channels (grocery, supermarket, health food), estimate the total North American market to be about 9 million certified pounds[9]. A very rough estimation of approximately 20% more of non-certified coffee may have been sold as Organic for a total of 11.8 million pounds.

A rough estimation of total North American *certified* Organic coffee market, assuming both importer data and estimates of other channels is $122 million at retail. Including uncertified Organic coffee estimations would push this figure even higher to a rough estimate of $146 million. Currently, there is no reliable transactional or empirical data on the amount of certified Organic coffee sold in North America. Discussions are underway to determine the most efficient manner to capture accurate data for this segment in the future. OCIA, the largest certifier is considering this. According to Griff McClellan of Quality Assurance International (QAI), currently do not track it.

Global certified Organic coffee exports were approximately 15-18 million pounds for the 1999/2000 year[10]. Non-certified traded Organic coffees could swell this figure significantly. The US$ retail value of this *certified* total is approximately $223 million. Including non-certified[11] puts the global approximation at 21.2 million pounds with an estimated retail value of $286 million. Industry experts estimate a 15%-18% increase for the 2000/2001 season. These are all approximations since empirical data is not available.

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[9] Field surveys and calculations based on the tabulations of various industry sources (primarily leading importers) and confirmed by the Organic Coffee Association.

[10] Calculations same as footnote 9

[11] 11.8 million pounds N.A. plus 9.4 million pounds estimation in other major markets.

J. Sustainable coffee volume and sales, continued

Fair Trade

In the survey 22 importers claimed 100% certified sales of 1.4 million pounds. The North American Fair Trade certification agencies (Transfair) registered considerably higher figures for the year 2000: 4.7 million pounds; 4.3 million pounds in the U.S. and 420,000 pounds in Canada. Transfair estimates that there is little if any Fair Trade coffee sold in North America that is not certified by them. Using the latter certification figure, total year 2000 North American Fair Trade sales were approximately $64.4 million at retail; U.S. Fair Trade sales were $58.1 million and Canadian sales were $6.3 million. Approximately 79% of these coffees are also certified as Organic.

Confirming the confusion that exists around sustainable coffees, the extrapolation of retailer survey data indicates more than 2500 retail firms (Transfair claims only approximately 2000) selling a total of more than 7 million pounds a number which experts agree is incorrect. Average sales for a retail firm were $23,000 in 2000. All importers (including those selling 100% certified) averaged $71,000 each in annual sales.

Globally, Fair Trade certification agencies estimate total production capacity of approximately 165 million pounds from 255 cooperatives in 22 countries. Approximately 29.1 million pounds are actually sold as Fair Trade for a retail value of approximately $393 million[12]. On average in 2000 Fair Trade growers received 74.9 cents per pound over the London "LCE" Market rate for Robusta and 43.2 cents per pound over the New York "C" Market rate for Arabica. Organic certification is steadily growing in popularity among Fair Trade coffees moving from 1% of total sales in 1996 to 36% in 2000.

Shade coffee

By extrapolating survey data to include the entire N. A. specialty market for the year 2000, there are 72 importers selling approximately 2.1 million pounds of Shade coffee. That is nearly 30,000 pounds each annually. The retail value of this market estimation is $28.4 million.

As with the other sustainable coffees, retailers claim to sell considerably more than importers claim. In this case they claimed to average over $16,000 in sales in 2000 for a retail market estimation of $37.9 million. This data clearly reflects confusion about what is actually considered Shade coffee. The importer data is likely to be a more accurate representation of the total market while the certifiers' data below represents the value of

[12] Fair Trade Labeling Organization (FLO) June 2001 data for year 2000. Personal communication.

J. Sustainable coffee volume and sales, continued

Shade coffee market that is certified to the generally accepted international standards set by the Smithsonian Migratory Bird Center (SMBC).

Globally more than 6.6 million pounds of Shade coffee were certified in 2000-2001, the bulk of this is in Guatemala and El Salvador. According to the two certifiers, SMBC and Eco-OK, after only two years of certification activity, sales have jumped significantly but rely on a relatively small number of buyers ranging from high-end specialty firms to select supermarkets and even a mass merchant. Estimates for year 2000 sales of certified Shade grown coffee are approximately 1.2 million pounds (most to N.A., 5% to Japan, less to EU). Retail value of this certified Shade coffee is just under $16.2 million.

Total size and retail value of the sustainable market

Using the above approximations for *certified* Organic, Fair Trade, and Shade the estimated total quantity of these sustainable coffees for the North American market is 11.2 million pounds, with a retail value of approximately $152 million. Including sales of non-certified coffees, the North American market size is approximately 15 million pounds with a value of more than $188 million. These sales estimates represent less than 1% of the total North American market ($20.7 billion) and approximately 2% of the North American specialty coffee market. This figure would be considerably higher if it incorporated sales of those coffees that used the word "Shade" on their packaging or marketing materials.

A rough estimate of global sales of these three *certified* sustainable coffees is 36 million pounds valued at $490 million[13]. Total market for both certified and non-certified coffee that is sold with a sustainable "label" is 42 million pounds with an approximate value of $565 million[14]. Although considerable, this still only represents less than 1% of global coffee sales.

[13] Calculation includes certified Organic $223 million + 64% (non-organic portion) of $393 million certified Fair Trade sales + Certified Shade coffee $16 million.

[14] Calculation includes certified Organic and estimation of non-certified ($286 million) + 64% of $393 (non-organic) certified Fair Trade sales ($252 million) + Shade coffee that was sold at a premium ($28 million).

K. Canadian variations

Canadian coffee firms are more aware of sustainable coffees than their U.S. counterparts and more confident of growth in Fair Trade and Shade coffees.

In general terms, the Canadian specialty coffee industry is more similar than dissimilar to its U.S. counterpart. Nevertheless, some differences can be noted. Canadian respondents are typically even more aware of sustainable coffees than U.S. counterparts. Compared to the U.S., a similar percentage have access to Organic coffees but a larger percentage have access to Fair Trade and Shade. Premiums for these coffees are much more likely to exist but tend to be lower. Although a smaller percentage of Canadians feel that premiums are reasonable, more than 90% believe they will continue.

Customer awareness was considered a somewhat more important attribute in their buying and selling decisions than it was for US companies.

Like U.S. firms, Canadians are much more likely to source sustainable coffees from Latin America but their individual country choices differ. Canadian firms had a markedly higher propensity than Americans to import organic coffees from Mexico, Guatemala, Peru and Nicaragua; Fair Trade coffees from Mexico, Peru and Nicaragua; Shade coffees from Guatemala, Mexico, and Peru.

Canadian coffee companies concur that the single most important factor that makes sustainable coffee valuable to their business is specialty quality or taste. However, their personal beliefs about chemical free agriculture and biodiversity or the environment were ranked very important by a larger number as was the opportunity that these provided for differentiation in the marketplace.

Although a similar percentage experienced Organic coffee growth between 1999 and 2000, approximately 30% more Canadian firms showed increases in Fair Trade and Shade coffees. Canadians were slightly more optimistic about growth in this category over the next two years, particularly for Shade coffee, and none expect a decrease in business. They predict a slightly lower rate of increase for Organic and Shade (although still over 20%) and a somewhat greater rate of growth for Fair Trade.

Considerably more Canadian firms feel that certification will be *very important* to their business over the next two years. For Organic 66% vs. 49% of U.S. firms; for Fair Trade 64% vs. 41%; and for Shade 50% vs. 36%. Regarding the idea of a super seal certification covering all three types of sustainable coffees, Canadians and their U.S. counterparts had similar views in favor.

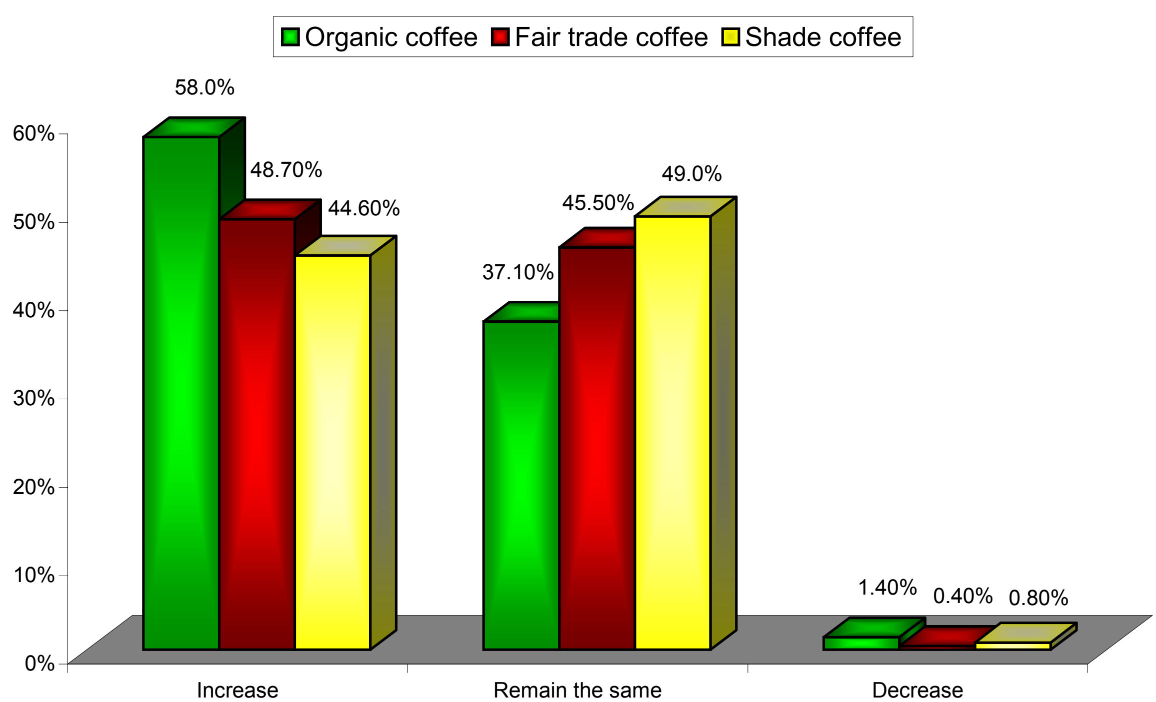
L. Future trends

In the next two years less than 2% expect any decreases and nearly 95% expect sales to either remain the same or increase.

The survey indicates that coffee *quality and consistency of supply* are the two most important attributes in the specialty coffee trade. Producers who seek to be competitive must consider how well they can fulfill these two expectations in the future.

Approximately half of the respondents expect an increase in sustainable coffee business over the next two years led by Organic coffee (58%). Very few (less than 2%) expect to experience decreases in any category.

Industry Expectations for Sustainable Coffee



For those businesses selling sustainable coffees, year 2000 sales have either remained the same or increased from 1999 sales for more than 85% of respondents. Less than 4% registered decreases. In recent years sustainable coffees have grown even more strongly than the specialty coffee market. Organic coffee has demonstrated steady 20% annual

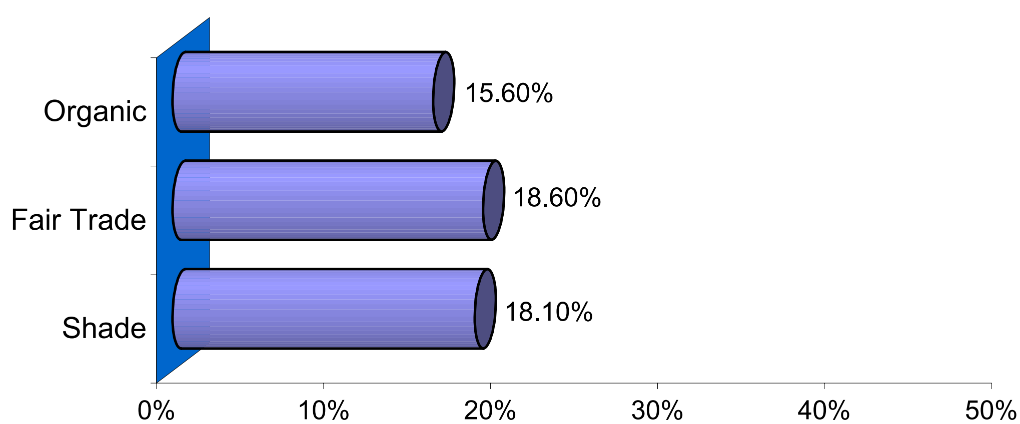
L. Future trends, continued

growth rates. Although Fair Trade and Shade coffees have a shorter history and start from a very small base, these have shown remarkable growth as well with Fair Trade registering 115% over last year and Shade, although not measured last year, showing strong indicators of increasing certification (approximately 7 million pounds available for 2001) and sales. While this growth is notable, caution should be exercised in consideration of the relatively small size of the sustainable segment that represents only about 2% of the North American specialty market.

Those respondents who believe that their sustainable coffee business will grow, project all three sustainable coffees to grow by an average of 26.5% over the next two years. Less than 1% intend to drop these categories altogether. Organic coffee leads the others in recognition and acceptance reflecting its considerably longer history in the marketplace. Nevertheless, if the current growth rates continue for the other sustainable coffees they could surpass organic coffee sales within a few years.

A number of respondents not currently selling at least one of the sustainable coffees expect to begin selling one or more types (*see chart below)*. Not surprisingly, some of North America's largest retailers are exploring these markets as well. In this case, first mover advantage could be considerable given the currently limited supplies from producer countries. This represents a considerable opportunity for new business.

Percentages of firms planning to enter sustainable coffee market



L. Future trends, continued

Certification will be important to a large majority of the industry over the next two years, this is particularly true for Organic coffees (78.3%). As more firms support third party certification, they will help promote accuracy in labeling and further educate the marketplace with consistent and common terminology. If the industry fails to achieve this, it will not only risk a downturn in one of its more successful niche markets but also a collateral erosion of confidence and credibility in related markets such as single origin coffees.

Although it is not clear to what extent the support for a unifying super seal is a surrogate for the desire to have simpler sourcing criteria and/or clearer marketing messages rather than the complex issue of combined certification criteria. In either case, the market's interest in having clear and concise certification appears clear.

The vast majority of respondents to this survey (86% - 90%) expect that *price premiums* for all three sustainable coffees will continue for at least a few years. Only 5% - 6% expect that they will not. This indicates that the market perceives a measure of extra value in these coffees. This extra value can be useful to promote a more sustainable industry, but only if a fair share reaches the producer. Currently, the average economics of the supply chain for a pound of coffee leaves the producer with a disproportionately small share. Of the $50 billion global coffee business only approximately $5 billion stays with the producers.

As production technology reaches even small farmers, enabling them to produce sustainably at international output levels[15], one of the main stumbling blocks to widespread farmer adoption of sustainable principles, high productivity, will be removed. As productivity reaches levels of conventional coffee (agro-chemically supported mono-crops) the advantages of lower input costs and improved soil quality could dramatically swell the ranks of sustainable coffee growers and push increasing supplies onto a market that may not then continue to provide the same significant premiums. It is unlikely that this will occur in the near term of 3-5 years.

The projected 10.5 million bag global surplus in 2001 (estimated exports relative to consumption) will likely mean continued downward pressure on prices for the near future. Most industry sources in both producing and importing countries do not see significant price improvements in the short or mid-term. With current prices already close to the cost of production in many countries, sustainable coffees and the premiums they fetch in the marketplace are one of the few bright spots in an otherwise dismal socio-economic situation for producers.

[15] Mexican Coffee Council data demonstrating internationally competitive output levels for Shade coffee.

M. Constraints and opportunities for sustainable coffees

Sustainable coffees fill a specific niche as part of the specialty coffee market, a segment that, unlike most of the coffee industry, has experienced notable growth in recent years. While it is true that these markets are particularly strong and growing in North America there are also ample opportunities in the EU and Japanese markets. In the EU, Fair Trade markets are considerably larger than those in the U.S., Organics are strong and Shade is still relatively novel. In Japan Organics are well-known, Shade has made some very modest inroads (primarily a large coffee beverage manufacturer) and Fair Trade is relatively novel. Possibilities also exist for consumption in the domestic markets of some producer countries. Mexico, Jamaica, and Brazil, among others, are already successfully demonstrating this with higher quality domestic sales. Consumers, sellers and farmers have distinct but interrelated opportunities and constraints.

Coffee Consumers

Various studies show that consumers are indeed interested in at least one or another of these sustainable coffees and are willing to pay a modest premium[16]. Much has been made of the customer profile of a sustainable coffee drinker: affluent, educated, cause-friendly, as an excellent target market.

Combining this profile with the natural affinity groups for this product (bird watchers, organic gardeners, environmental groups) whose North American members run into the tens of millions, makes simple marketing sense. Yet, this natural audience has not yet significantly embraced sustainable coffees. This and other studies have demonstrated that quality (taste) is the number one factor in coffee purchasing decisions. Until recent years some sustainable coffees were inconsistent due primarily to rustic post-harvest and processing methods. Since many of these coffees now consistently meet high quality and taste criteria, the two most plausible reasons that remain for the less than expected market response are product availability and education.

Many consumers prefer one-stop shopping for their food needs (supermarkets) and availability implies both convenience and visibility. Many North American supermarkets either do not stock sustainable coffees or present only one, often as a single origin or blend, and usually Organic. Although considerable quantities of Organic coffee are sold through the grocery and supermarket channel, their ready availability is limited mostly to the West Coast and select urban areas. This dynamic appears to be on the verge of changing as supermarkets and mass marketers show an interest in these coffees and vie

[16] a) Commission for Environmental Cooperation. 1999. Measuring Consumer Interest in Mexican Shade-Grown Coffee: An Assessment of the Canadian Mexican and U.S. Markets.CEC Secretariat.
b) Rice, P. McLean, J. 1999. Sustainable Coffee at the Crossroads. CCC.
c) David Griswold 1999 survey for the El Salvador Shade Coffee project.

M. Constraints and opportunities for sustainable coffees, continued

for competitive positions with differentiated and higher-quality products as conventional product margins continue to slip and conventional coffee sales stagnate.

According to the National Coffee Association (U.S.), in 2001 13% of daily and weekly specialty or gourmet coffee drinkers (8 million people) say they purchased organic coffee at least once. Among those who drink regular coffee daily and weekly, 3% (2 million people) say they purchased organic coffee at least once. For Fair Trade about 4% of specialty / gourmet drinkers purchased it at least once and 1% of regular coffee drinkers purchased it. Shade coffee showed similar responses with 3% of specialty / gourmet drinkers purchasing and 1% of regular coffee drinkers. This relatively new market appears to have considerable room for growth but consumer trends are difficult to capture since most data collection has only started in the last 1-2 years.

This Sustainable Coffee Survey in particular indicates a lack of clarity in the industry about what each of the sustainable coffees actually represents and certainly there is confusion concerning the distinctions between these coffees. If this is true among members of the industry itself, it is safe to assume that consumers are also confused and perhaps more so. Although the North American Specialty Coffee Association has provided strong leadership in this arena for its members, the industry itself has not yet managed to reach a broad consumer audience with information/education about sustainable coffees.

Another and perhaps more viable alternative for improved consumer education is the considerable reach and impact of the environmental groups and NGOs whose missions often coincide with the tenets of sustainable coffee. Through their regular mailings, magazine articles, and events, the sustainable coffee message can be easily conveyed to a vast and interested audience at little or no additional cost. Many opportunities exist for cross merchandising and cause related marketing that few are exploiting.

Coffee Sellers

The North American coffee market is dominated by three multinational companies that have to date not ventured into sustainable coffees. There are industry indications that this could soon change as they search for growth opportunities in a stagnant market. Meanwhile, surprising new channels may soon open as market savvy companies, including two of the world's largest retailers, are actively exploring this market. More supermarket chains, including large ones such as Safeway, Kroger's, and Albertson's are expanding or adding new sustainable coffees to their offerings.

For the moment there appears to be adequate supply of these coffees to the industry although the entry of large players into the field could temporarily tax the ability of

M. Constraints and opportunities for sustainable coffees, continued

suppliers to provide consistent and high-quality coffees. Any significant new entry into this market would have to partner with producer organizations or at least exporters or middlemen to ensure the rapid assimilation of quality standards and the provision of consistent supplies. A number of Non-Governmental Organizations (NGOs) and even the donor community are piloting an effective interface with producers[17].

The temptation to vastly increase this business too rapidly could come at a considerable price. Two areas are worthy of cautious consideration. First, if in the rush for new business, quality and consistency are not maintained then consumers will reject sustainable coffees, perhaps permanently. Second, a few in the industry are already free riding on the reputation of sustainable coffees, particularly Organic and Shade coffees while either not complying with the scientifically accepted definition of these terms nor or not choosing certification. This approach opens the door to green-washing and a dilution of these terms that could lead to consumer rejection.

Coffee Producers

A recent study, endorsed by the Mexican Coffee Council, notes that production levels for sustainable coffees can reach the international standards of conventional coffees. A number of earlier studies have demonstrated the economic viability of sustainable coffees for small producers. Perhaps equally valuable is the emerging understanding that coffees varieties that are grown naturally under shade can have a superior taste profile.

Sustainable coffees also provide smallholders with useful risk management strategies. Diversification of production (multi-cropping) on a sustainable coffee farm offers several advantages to a farmer. Coffee certification can be an excellent hedge against market price downturns since most certifications can provide premiums although there are no guarantees. Shade and some Organics also offer some benefits when facing natural stresses such as drought. Reducing or eliminating the use of purchased inputs limits the farmer's expenses and therefore his subsequent market exposure.

For many producers, conversion time, preparation, and certification are costly and sometimes difficult. Achieving and maintaining more than one is beyond the economic capacity of most. Furthermore, no one certification deals with all of the aspects necessary for a grower to sustainably produce coffee (Eco-OK comes close). Ideally, growers should abide by the basic principles of all three – Organic, Fair Trade and Shade - in order to be more truly sustainable.

[17] Global Environment Facility (GEF) in Mexico, El Salvador, and Uganda. USAID in Peru and Nicaragua. Rainforest Alliance in El Salvador and Guatemala. Conservation International in Mexico and Colombia.