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**Sustainable Markets are Growing  
– Is Sustainability Keeping Pace?**  
A Perspective on Sustainable Coffee Markets

*Jason Potts and Mark Sanctuary*

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## ABOUT THE AUTHORS



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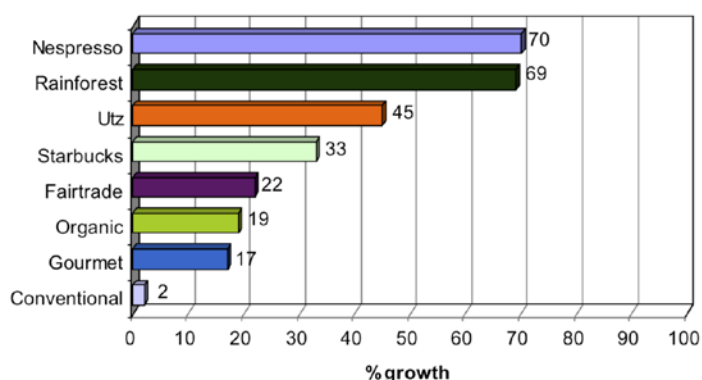
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# Sustainable Markets are Growing – Is Sustainability Keeping Pace?

## A Perspective on Sustainable Coffee Markets

By Jason Potts and Mark Sanctuary



**Figure 1: Average Annual Growth Rates of Major Coffee Sustainability Initiatives Over the Past Four Years Compared with Growth in Conventional Coffee Markets.** (Source: Daniele Giovannucci, 2010)

Globally, sustainable development for agricultural producers is now at the forefront of concern. We are experiencing a first wave of market initiatives for “sustainability” that are promising but still limited in their reach and uncertain about their real impacts. What are the next steps?

This ENTWINED Issue Brief examines the main constraints to sustainable-coffee markets and identifies three concrete opportunities that can leverage development in this field. This next phase must begin with a better understanding of farmer-level impacts, while focusing technical assistance on improved access for traditionally marginalized producers in international markets.

### INTRODUCTION AND OVERVIEW

As one of the most important globally traded commodities, coffee plays a crucial role in the livelihoods of millions of rural households across the developing world. In addition to the estimated 20 million small coffee farmers who depend directly upon coffee as their primary source of income, coffee contributes significantly to foreign exchange earnings and plays a leading role in determining opportunities for employment and infrastructure development in more than 50 developing countries. At the same time, coffee consumers are mostly found in the developed economies, with the Nordic countries showing some of the highest per capita consumption. Sweden, for example, is among the world’s top coffee consuming nations, with an annual per capita consumption of around 9 kg of coffee beans equivalent, or about 3.4 cups of coffee per person per day.<sup>1</sup> Coffee

markets link producers and consumers in developed and developing countries and is an important vehicle for sustainable development.

Recognizing this, consumers, NGOs, the private sector and donor agencies have taken a growing interest in promoting sustainable production and trading practices along coffee supply chains. Increasingly, these have taken the form of sustainability labels (such as Fairtrade and Organic), business-to-business standards and other certification initiatives, and Voluntary Sustainability Initiatives (VSI) that provide assurances to consumers and other supply-chain stakeholders that production is in accordance with sustainable development objectives. This Issue Brief documents the current state of markets for sustainable coffee, globally and within Sweden, as well as the drivers behind such markets, and highlights key opportunities for further improving the sustainability of global coffee markets.

### GLOBAL AND SWEDISH SUSTAINABLE COFFEE MARKETS

Certified sustainable coffees have existed for more than 20 years. While global production and sales have experienced uninterrupted growth over this period, the past half-decade has given rise to a massive expansion in the acceptance and use of a variety of sustainability labels, even amongst mainstream corporations engaged in the coffee market.<sup>2</sup> Over the past four years, the average annual growth rate of the major sustainability initiatives operating in the coffee sector has been between 19% and 70% (Figure 1), significantly outperforming the annual growth of conventional coffees in both the specialty and mainstream sectors. By 2009, an estimated 480,000 MT, or 7.9% of global coffee sales, was sold as sustainable coffee to commercial or consumer markets. Over the same year, an estimated 1.2 million MT (16% of global production) of coffee was actually produced in accordance with the criteria associated with one or more major sustainability initiatives.<sup>3</sup> Although sustainable coffees still account for a small share of global production and trade, the rapid entry into mainstream supply chains suggests that sustainable coffees will become an increasingly important determinant of access to international markets and of living/working conditions in coffee-producing regions.

The sustainable coffee market in Sweden, although less developed than markets for sustainable coffee found in many other developed countries, reflects these global trends. The vast majority of sustainable coffee sales in Sweden are made under the Fairtrade (Rättvisemärkt) and Organic (Krav) labels. Figure 2 illustrates the market trends of these two sustainability labels over the last three years in Sweden. Sales of Fairtrade coffee in Sweden in 2009 were

worth about 332 MSEK – a 29% increase over 2008 – and currently account for 4% of the Swedish coffee market.<sup>4</sup> Sales of Organic Coffee in 2009, on the other hand, were worth about 210 MSEK – an 11% increase over 2008 – and account for an estimated 2.5% of the Swedish coffee market.<sup>5</sup> The development of price over the sample period for Fairtrade and Organic retail coffee is shown in Figure 3. In recent years, both Fairtrade and Organic coffees have commanded a fairly significant and consistent price premium, and offer the potential to generate increased economic returns for producers further up the supply chain. Although Swedish consumers have less choice in the variety and quantity of certified sustainable products relative to the global average, growth remains significantly higher than for conventional coffees, suggesting that market trends are likely to follow global trends toward more significant mainstream acceptance.

*Key message: The global market for sustainable coffee is expanding rapidly and has reached a significant market share. Sweden's sustainable coffee market is also growing rapidly but has not yet reached the level of penetration seen in other developed economies. Price premiums for sustainable coffee can be substantial, and represent an important opportunity for catalyzing social, economic and environmental benefits across the developing world.*

## TRADE FLOW

Many stakeholders, particularly those in developing country markets, have expressed concerns that standards stemming from voluntary sustainability initiatives may function as technical barriers to trade.<sup>6</sup> Although there is no systematic evidence that such initiatives are intentionally designed to favour specific regions or interests,<sup>7</sup> anecdotal evidence suggests that the cost of compliance may be higher for less-developed producers. One study found that the cost associated with compliance for small producers in Africa can be up to 3.5 times higher by volume than that for small producers in Brazil.<sup>8</sup> This observation appears to be vindicated by the fact that current production patterns show a clear concentration of sustainable production across historically more organized coffee-producing regions. More than 70% of sustainable coffee on global markets is currently supplied in Colombia, Brazil, Peru and Vietnam. By contrast, these four countries account for 57% of conventional supply. Similarly, 76% of sustainable coffee comes from Latin America,<sup>9</sup> while only 59% of conventional coffee comes from Latin America.

Higher rates of concentration of production for sustainable coffee markets across the more organized regions of Latin America suggests that barriers to market access for less-developed producers may be significant. As the global market presence of voluntary sustainability initiatives grows, the significance of the potential trade effects of sustainability requirements is likely to become increasingly important. The geographic concentration of supply of sustainable coffees points toward a need for investment in enabling marginalized producers in attaining access to markets for sustainable coffee.

*Key message: Access to sustainable coffee markets represents an important trade concern for many producing countries. Current market trends reveal that supply to sustainable coffee markets is concentrated across more organized producing regions. A dedicated effort is needed to ensure that sustainable markets deliver benefits to those most in need.*

## SUSTAINABILITY IMPACTS OF VOLUNTARY SUSTAINABILITY INITIATIVES

Although voluntary sustainability initiatives verify compliance with their standards, there is very little research verifying improved sustainable-development outcomes at the farmer or field levels. In a survey of existing literature on the field-level impacts of sustainable-coffee initiatives, only six studies were found to have applied counterfactual analysis capable of reporting on impacts associated with participation in a sustainability initiative.<sup>10</sup> The findings associated with many studies are inconclusive:

- Arnould, Palestina and Ball (2009) found that Fairtrade certification is positively correlated with coffee volume sold and price obtained, but less consistently correlated with indicators of educational and health status.
- Fort and Ruben (2008) found that Fairtrade farmers have lower incomes and productivity but higher levels of some assets and investments than conventional farmers.
- Sáenz Segura and Zúñiga-Arias (2008) found that Fairtrade farmers have lower incomes, profits, and household expenditures and worse perceptions of the functioning of their cooperatives than conventional farmers.
- Blackman and Naranjo (2010) found that organic certification improves coffee growers' environmental performance. It significantly reduces chemical input use and increases the adoption of environmentally-friendly management practices.
- Lyngbaek et al. (2001) found that net income for organic farmers was significantly lower than for conventional farmers.
- Bolwig et al. (2009) found that organic certification boosts net coffee revenue by 75% on average.<sup>11</sup>

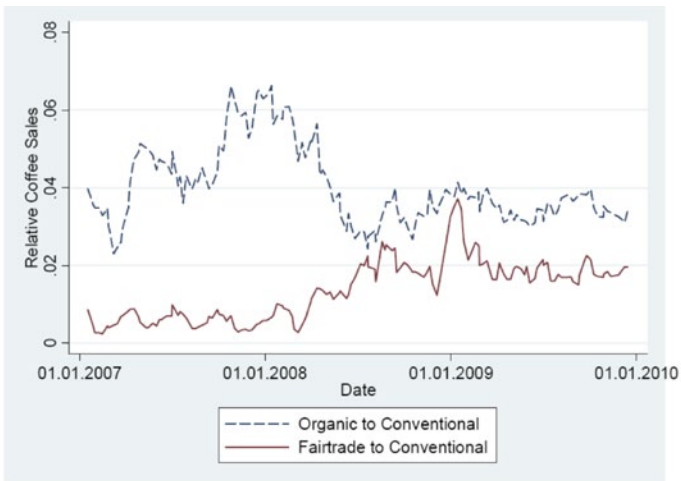
More importantly perhaps than the conclusions themselves is the lack of coherence and coverage of the different assessment processes applied across the studies. An analysis of the methodologies adopted shows considerable inconsistencies across approaches, leaving the results themselves subject to considerable question. Meanwhile, the limited focus of such studies on Organics and Fairtrade systems, suggests that a major fraction of voluntary sustainability initiatives is missing from current impacts research.

*Key message: Existing impact research on voluntary sustainability initiatives in the coffee sector is scarce and incomplete. The few existing counterfactual studies on the impacts of such initiatives do not provide representative coverage, and reach uncertain conclusions. More representative counterfactually-based research is needed. In order to ensure maximum usefulness, special effort is needed to ensure that impact research is coordinated and comparable.*

## THE LINKS BETWEEN MARKET POWER AND VOLUNTARY SUSTAINABILITY INITIATIVES

The continued viability of the Voluntary Sustainability Initiatives coffee market relies on the choices consumers make as they shop.

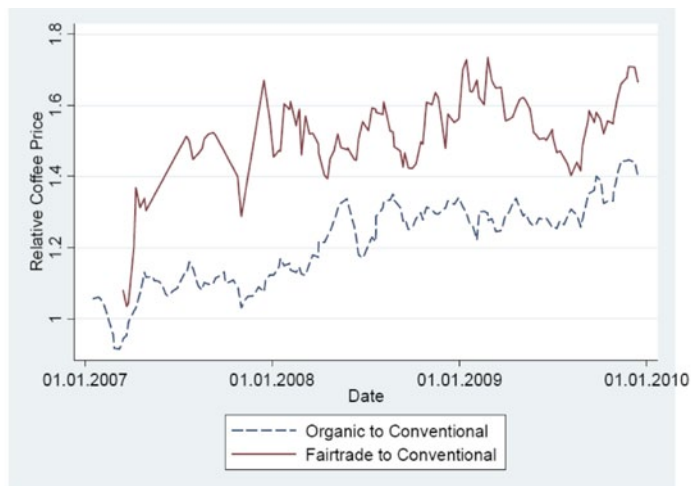




**Figure 2: Share of Organic and Fairtrade Coffee in Total Sales.**

(Source: Friberg, Richard and Sanctuary, Mark. 2010.

"A test of epsilon truthfulness" Forthcoming working paper.)



**Figure 3: Relative Price on Organic and Fairtrade Coffee to Conventional Coffee.**

(Source: Friberg, Richard and Sanctuary, Mark. 2010.

"A test of epsilon truthfulness" Forthcoming working paper.)



VSI-labeled coffee provides an opportunity for participants along the supply chain to shift to more sustainable practices to, for example, increase profits or gain a larger market share. For this to happen, consumers must, one way or another, change the way they shop. However, attracting the attention of consumers is a challenge for advertisers when there are so many competing labels.<sup>12</sup> Understanding how consumers respond to Voluntary Sustainability Initiative is critical to identifying the potential of sustainable coffee to deliver sustainable-development opportunities to producers, and has implications not only for private-sector stakeholders but also for the formulation of public policy.

For producers, understanding the consumer has obvious implications for targeted advertising efforts. One question is, "who is buying which VSI label on their sustainable coffee?" Is it a well-defined consumer profile or is there broad uptake across demographic groups. Friberg and Sanctuary (2010) find that many consumers in Sweden buy both organic and Fairtrade coffee. They also find that Fairtrade

coffee is more preferred by younger households with university-level education. In addition, Figures 2 & 3 (see above) indicate that the market share for organic coffee dropped while Fairtrade's market share grew, even though both labels were becoming more expensive relative to other brands. This suggests competition between organic and Fairtrade coffee and is a relevant issue for policymakers seeking to encourage competition in the marketplace on the one hand, and provide public financing to a particular sustainability label on the other.

At the same time, competition along the supply chain has a direct impact on how the benefits (mark-ups for example) are distributed along the sustainable coffee supply chain. There is a host of research, old and new, indicating that some actors in a supply chain are able to use their market power when they bargain with suppliers and buyers to increase their share of any benefits. In the context of sustainable coffee, this means that if the market power of retailers or coffee roasters, for example, is strong enough, that the sizeable markups (that





we see in for example Figure 3 above) would not translate to a corresponding markup for coffee growers. Rather, much of the benefit might remain with the retailer or the coffee roaster. Understanding the nature of competition and market power along the supply chain can help to clarify how the benefits of sustainability labels are distributed. While there is no research to date on this particular aspect of the sustainable coffee market, it is an issue that is relevant not only for policymakers but for consumers and producers as well.

*Key message: Understanding the competitive setting of the sustainable coffee market is critical for determining how public policy can be used to support such initiatives and ensure that stated objectives are met.*

### THE ROLE OF PUBLIC POLICY

The success and growth of sustainable-coffee markets to date has relied heavily on the support of external foundations and donor agencies. Of the five most well-known voluntary sustainability initiatives in the coffee sector, four rely upon grants for 45% or more of their annual revenues. The Swedish context reflects this general trend, with Fairtrade Sweden (comprised of a corporate entity and

an association) receiving significant donations from EuropeAid and Sweden's labor union association (LO-TCO) to aid operations.<sup>13</sup>

To the extent that sustainable-coffee initiatives offer public social and environmental goods, a prima facie argument can be made for such support. However, the relevance and appropriateness of such support is directly dependent on the ability of such initiatives to actually deliver positive sustainable development outcomes. This is not currently clear, particularly in light of uneven access to sustainable markets and the virtual absence of credible evidence (i.e. comparable, time-series, counterfactual) regarding the impacts of such initiatives. This, in effect, represents a major obstacle to the acceptance and effective use of voluntary sustainability initiatives as catalysts for a sustainable-coffee sector.

### INVESTING IN SUSTAINABILITY

Policymakers and other stakeholders seeking to invest in voluntary sustainability initiatives as a vehicle for promoting sustainability in the coffee sector need to ensure that such initiatives are being applied in a manner that improves the livelihoods and sustainability

of those most in need. With this in mind we propose prioritizing the following three investment opportunities:

*Investment Opportunity 1: Global Framework for Impact Assessment of Voluntary Sustainability Initiatives:* The conditions and varieties of sustainability initiatives are rapidly growing. Within this context there is a need for a common impact-assessment framework that provides an objective basis for generating comparable information on the impacts of different initiatives across countries. This framework needs to be backed by adequate resources to carry out counterfactual-based field-level research.

*Investment Opportunity 2: Regular Reporting on Market Trends of Voluntary Sustainability Initiatives:* There is a growing need to understand market presence and trends at the global and local levels. Information on market structure and growth are critical to ensuring that stakeholders can invest strategically in initiatives, as well as ensuring that the benefits of Voluntary Sustainable Initiatives are equitably distributed throughout the supply chain.

*Investment Opportunity 3: Generic Technical Assistance Platform:* Current research suggests that poorer producers may be at a disadvantage with regard to access to sustainable markets. Investments in sustainable production should focus on reaching much larger groups, rather than being initiative-specific. A generic, multi-stakeholder platform will enable better production and management practices that facilitate the entry of marginalized producers into any of the wide range of sustainable product lines. Such a common platform will not only improve practices for more producers, it will also streamline small-producer access to sustainable markets.

*Investment Opportunity 4: Multilateral Platform for North-South Dialogue:* The development and implementation of voluntary sustainability initiatives in the coffee sector has been led by stakeholders on the consumption side of the supply chain. Many developing country stakeholders remain skeptical of the value of such initiatives. In order to ensure that such initiatives are implemented in a manner that reflects the needs and interests of both consumers and producers, while promoting sustainable development, there is a need for a neutral, multilateral forum for dialogue and strategic development of sustainable coffee markets. ■

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<sup>1</sup> <http://www.kaffeinformation.se/templates/FullPage.aspx?id=811>

<sup>2</sup> Dunkin Donuts, Kraft, Sara Lee, Nestle, Ahold and Starbucks have all made public commitments to sourcing from sustainable sources over the past several years.

<sup>3</sup> Pay, E. (2009), "The Market for Organic and Fair-Trade Coffee." Study prepared in the framework of FAO project GCP/RAF/404/GER. Giovanucci, D and Pierrot, J (2010) "Is Coffee the Most Popular Organic Crop?" in Global Survey on Organic Agriculture 2010. Bonn: IFOAM and FIBL. p 62. FLO Annual Reports 2004-2009; --, 2009. "The Rainforest Alliance's Impact Grows Even in Economic downturn." Rainforest Alliance Press Release, April 8, 2009; UTZ Certified Annual Report 2004-2009; 4C Association Annual Reports 2008-2009. International Coffee Organization Statistics 2009, and personal communications with standards bodies, 2009. The total includes estimates of 2008 sales of the following programs: Fair Trade Labelling Organizations International, UTZ Certified, Rainforest Alliance, 4C Association, Organic certified, Starbucks CAFE Practices and Nespresso Triple A Quality. Note that not all coffee that is produced according to sustainability requirements is actually sold on the marketplace as "sustainable," hence the differences in production and sales figures.

<sup>4</sup> Data provided by Fairtrade Sweden.

<sup>5</sup> Not accounting for potential double certification.

<sup>6</sup> The TBT code of Good Practice sets forth basic transparency and accountability parameters designed to allow all members of the global trading system to participate in standards development and implementation. However, the degree to which WTO members are expected to ensure that private voluntary standards comply with the TBT Code of Good Practice remains unclear.

<sup>7</sup> On the contrary, one of the trends associated with most voluntary sustainability standards is an opening of supply chain decision-making to include a wider array of supply chain stakeholders in the decision-making process through multi-stakeholder governance structures.

<sup>8</sup> See Potts, Jason; Michael Opitz and Chris Wunderlich, "Closing the Gaps in GAPS: A Preliminary Appraisal of the Measures and Costs Associated with Adopting Commonly Recognized 'Good Agricultural Practices' in Three Coffee Growing Regions," IISD, 2007.

<sup>9</sup> Op cit, note 3.

<sup>10</sup> Blackman, Allen and Rivera, Jorge E., The Evidence Base for Environmental and Socioeconomic Impacts of 'Sustainable' Certification (March 26, 2010). Available at SSRN: <http://ssrn.com/abstract=1579083>

<sup>11</sup> However, they argue that this revenue effect is not principally due to price premiums offered to certified farmers. Rather, it is an anomaly of the "contract farming" organic marketing system in the markets they studied, which requires participants to process their coffee before selling it, thereby increasing its value.

<sup>12</sup> For example, a medium-sized supermarket in Sweden carries upwards of 60 different types of roasted and ground coffee alone.

<sup>13</sup> In 2009, Fairtrade Sweden collected over 7.3 MSEK in donations from these two organizations alone. Likewise, Organic in Sweden received donations in 2009 from Jordbruksverket (the Swedish Government's agricultural agency).

The research programme ENTWINED – Environment and Trade in a World of Interdependence – examines the interplay between the global trade regime and environmental policies promulgated by governments and private entities with a particular focus on the treatment of transboundary problems. ENTWINED is actively engaged with policy makers and other stakeholders to the Trade and Environment Debate. The team

includes researchers specializing in environmental and natural resource economics, international economics and trade law. The programme has its focus in Sweden, but engages leading experts in other locations, including Geneva, New York, Washington and Montreal. The ENTWINED programme is funded by the Swedish Foundation for Strategic Environmental Research, Mistra, see [www.entwined.se](http://www.entwined.se)