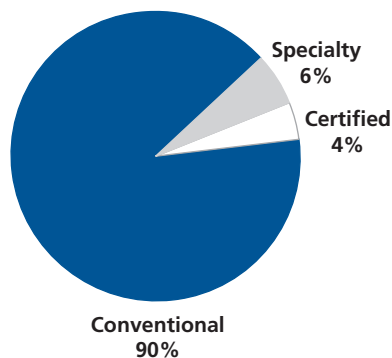


## CHAPTER 3: CERTIFIED COFFEE<sup>82</sup>

Coffee is one of the most important commodities on the world market. It is produced and exported by nearly 60 nations, ranks as one of the top cash crops in developing countries, and is critical to the economies of several of them<sup>83</sup>. According to the International Coffee Organization (ICO), world exports of green coffee amounted to 5.3 million metric tonnes in 2006, valued at approximately US\$10.85 billion. The value of exports is expected to exceed US\$12 billion in 2007 – a considerable rebound from the low of US\$5.5 billion that producing countries received in 2002 but still only about 17 percent of the US\$70 billion estimated global retail sales<sup>84</sup>.

Nevertheless, in some nations, producers received only US\$0.30 per pound of coffee when export prices are over three times higher. In one African nation, producers earn even less with an average of only US\$0.09 per pound of robusta<sup>85</sup>. For many, coffee is the only cash crop yet it can be a difficult way to earn a living. Low prices are only part of the challenge. World conventional coffee markets are highly competitive and typically cyclical with recurring patterns of oversupply that make prices volatile and producer incomes very insecure.

**Figure 11. World exports of certified coffees in relation to specialty and conventional coffees in 2006**



Source: D. Giovannucci estimates based on various data sources

Social and environmental certification has created a fast-growing niche market that offers an advantage to growers that can produce quality certified products. Certified coffees are commonly defined as those that include the three pillars of sustainability (economic, environmental and social) and are certified by independent third parties. This category has emerged from almost negligible quantities in the late 1990s to become a significant portion of today's coffee exports. In 2006, certified coffees amounted to approximately 4 percent of global green coffee exports or more than 220 000 metric tonnes (Figure 11)<sup>86</sup>.

<sup>82</sup>Please cite as: Giovannucci, D., Liu, P. and Byers, A., 2008 Adding Value: Certified Coffee Trade in North America. In Pascal Liu (Ed.) Value-adding Standards in the North American Food Market - Trade Opportunities in Certified Products for Developing Countries. FAO. Rome

<sup>83</sup>World Bank (Lewin, B., Giovannucci, D. and Varangis, P., 2004)

<sup>84</sup>ICO (2007)

<sup>85</sup>ICO (2007)

<sup>86</sup>Giovannucci, D (2008)

While the market penetration of certified coffee is still relatively modest, coffee is nevertheless the leading agricultural sector in terms of both the number and frequent use of such certifications. These certification initiatives are more responsive to public needs and have become important vehicles for managing or regulating sustainability in coffee<sup>87</sup>.

When coffee prices plummeted in the late 1990s and early 2000s, hundreds of thousands of farmers were forced out of business. Oxfam<sup>88</sup> and the Lewin *et al.* World Bank report (2004) note resulting hunger, dislocation, and even a number of deaths attributable to this collapse. Prices for certified coffee declined considerably less than those of conventional coffee during the crisis, providing some growers with a lifeline<sup>89</sup>.

## 1. OVERVIEW OF THE NORTH AMERICAN COFFEE MARKET

Nearly all coffee sold in North America is imported from developing country producers and exporters<sup>90</sup>. The North American coffee market accounts for over one quarter of global coffee imports in value (27 percent in 2005) and the United States is the world's largest single buyer of coffee. Its consumers are increasingly attentive to quality and origin, and have demonstrated a growing interest in the social, economic, and environmental aspects of coffee production. The expansion in the number of gourmet coffeehouses in the United States illustrates this rapid evolution. From approximately 450 in 1991 there are now nearly 24 000 in operation<sup>91</sup>. The unique development of such differentiated demand in the United States and Canada, especially over the last decade, has had a significant impact on the coffee industry and its producers. In recent years, the value of differentiation has increasingly concentrated in the intangible and downstream parts of the value chain as some retailers sell coffees at many multiples of their purchase price<sup>92</sup>. The demand for certified and higher quality gourmet coffees allows producers to capture a greater percentage of the final retail value for their crops in the form of price premiums<sup>93</sup>.

### *Volume, value and prices*

Approximately 1.42 million metric tonnes of conventional green coffee was imported into North America in 2006, with 1.28 million metric tonnes entering the United States<sup>94</sup> and 139 000 metric tonnes into Canada<sup>95</sup>. The FOB value in 2006 is estimated to exceed US\$3.6 billion<sup>96</sup>. The tariff levels are favourable to coffee imports: green and roasted coffees enters the United States and Canada duty free and for most other processed coffee products the tariff is either zero or very low. When measured by value, Colombia accounts for the largest share whereas Brazil supplies the largest quantity. Green arabica coffee accounted for about 53 percent of the total. The United States also exported significant quantities of coffee (68 percent of which was roasted) that in 2006 were valued at US\$451 million. Canada is the largest market for US exports and it also re-exports a modest amount of coffee.

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<sup>87</sup> Reynolds, L., Murray, D. and Heller, A. (2007)

<sup>88</sup> Oxfam (2003)

<sup>89</sup> Varangis, P., Siegel, P., Giovannucci, D. and Lewin, B. (2003)

<sup>90</sup> With the exception of production from Hawaii and Puerto Rico

<sup>91</sup> Sources: SCAA, Mintel, NCA elaborated in Giovannucci, D. (2008)

<sup>92</sup> Ponte, S. and Daviron, B. (2005)

<sup>93</sup> World Bank (Lewin, B., Giovannucci, D. and Varangis, P., 2004)

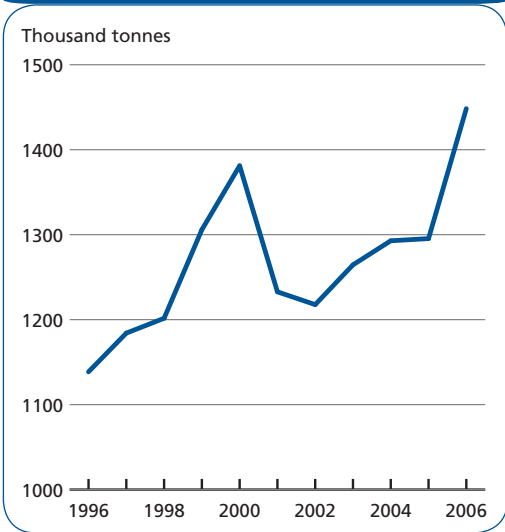
<sup>94</sup> USDA FAS (2007)

<sup>95</sup> Canadian Coffee Association (2007)

<sup>96</sup> USDA FAS (2007)

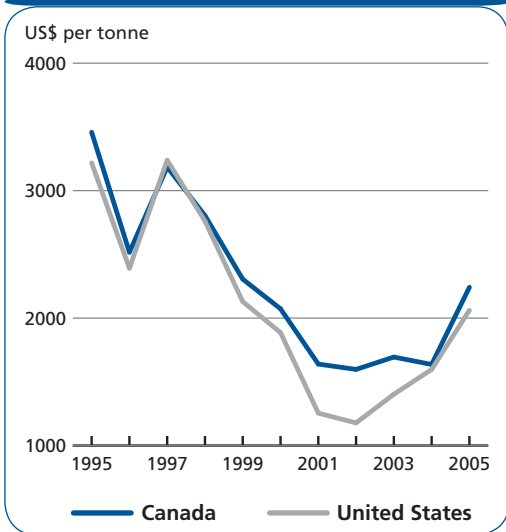
North American consumption has shown little overall growth in recent years. The quantity of green coffee imported into North America grew markedly in the 1990s and reached a peak in the year 2000. The volume declined in 2001 and 2002 and then showed only marginal average growth of approximately 1 percent per annum (Figure 12) until 2005. Disaggregating the different market segments uncovers that the sales of conventional coffees actually declined while growth has occurred in the differentiated or specialty coffees. Real prices for all coffees fell from the mid-1990s, reaching record-low levels in the early 2000s. This fall was reflected by declining unit values of imports in Canada and the United States as shown in Figure 13. The severe price declines appear to have had little or no impact on global consumption trends. The fall in prices however caused considerable hardship for all coffee producers. Import prices have partly recovered since 2002, but they are still below the nominal price levels of the early 1990s.

**Figure 12. Imports of green coffee into North America**



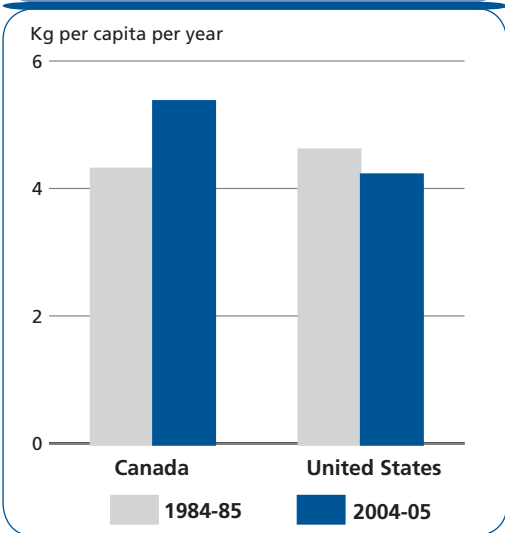
Source: FAOSTAT (ICCO for 2006)

**Figure 13. Unit value of United States and Canada green coffee imports**



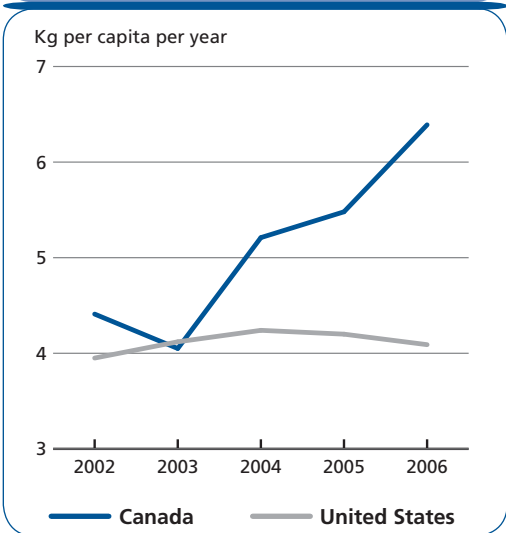
Source: FAOSTAT

**Figure 14. Change in coffee consumption across two decades, United States and Canada**



Source: International Coffee Organization (ICO) 2007

**Figure 15. Recent changes in coffee consumption in Canada and the United States**



Source: International Coffee Organization (ICO) 2007

In the United States, per capita consumption has been almost stagnant over the past five years, and is even below its level of the mid-1980s despite population growth. Conversely, it has expanded in Canada (Figures 14 and 15). Individual consumption in Canada reached 6.39 kg per capita in 2006 and is among the highest in the world, well above that of the European Union (4.95 kg), the United States (4.09 kg) and Japan (3.38). Higher consumption rates are only found in Scandinavian countries and some smaller European states (Benelux, Estonia and Switzerland).

## 2. CERTIFIED COFFEE

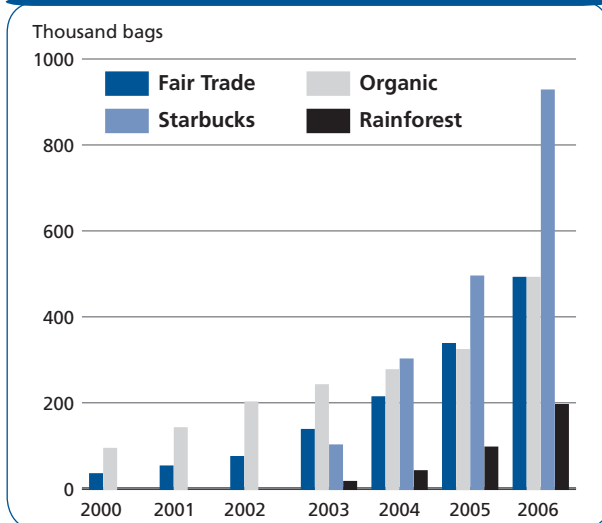
Calculating estimates of the quantities of certified coffees marketed in North America is made difficult by the fact that only a portion of the coffees that are certified under a sustainability programme are actually sold under a certified seal. Several factors contribute to this dynamic:

- A portion of a farm's output may not meet quality requirements of a buyer seeking certified coffees and must therefore be sold as conventional.
- Some coffees are purchased for their sustainability attributes and, for various reasons may be blended or marketed without the identity of a certification.
- A buyer may want to purchase only a portion of the coffee as certified and the rest as conventional, even though the entire farm may be certified.
- In some cases, buyers are not seeking a certification but will give preference to certified coffees even though they do not use the certification and may or may not pay a premium.

Unless otherwise specified, the figures provided in this section relate to the quantities actually purchased as certified. Total certified production volumes may be substantially higher.

Estimates for 2006 indicate that the imports of certified coffees rose to approximately 110 000 metric tonnes, accounting for nearly 8 percent of the market. These certified coffees include organic, Fairtrade, Rainforest Alliance, Bird Friendly, Utz Certified and Starbucks C.A.F.E. Practices and account for overlapping certifications (Table 11). This is a very substantial growth from the approximately 60 000 metric tonnes of certified coffee that were imported into North America in 2005, then accounting for approximately 5 percent of the green coffee imports. The export value (FOB) for these coffees was estimated at approximately US\$330 million in 2006<sup>97</sup>.

**Figure 16. Estimated growth of US certified coffee imports**



Sources: Giovannucci from own data and CIMS, TransFair, Rainforest Alliance, Starbucks

<sup>97</sup> Calculation by Root Capital and Giovannucci based on conservative estimates of average FOB prices

Many large North American retailers such as Starbucks, Dunkin Donuts and McDonalds, now offer organic and/or fair-trade coffee. Other coffees certified as sustainable are increasingly becoming popular as well (Figure 16). RA is now one of the fastest growing coffee certification schemes in North America, due in part to its partnership with industry giants like Kraft Foods. Utz Certified and Bird-Friendly (Smithsonian Migratory Bird Center) have smaller positions.

**Table 11. Estimated imports of certified green coffee into North America**

Type	Quantity (MT)
Organic	30 700
Fair-trade	32 100
Rainforest Alliance	11 600
Utz certified	1 800
Bird friendly	200
C.A.F.E. Practices (Starbucks)	58 000
<b>Total (*)</b>	<b>110 000</b>

(\*) Due to multiple certification, the total is less than the sum of the rows

## 2.1 Organic coffee

### Market situation

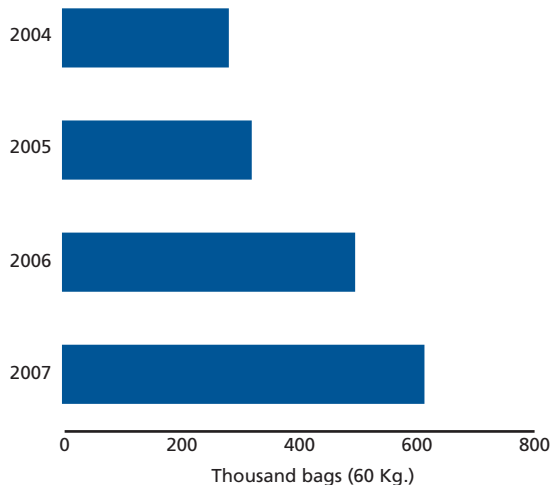
Based on a survey of importers and industry sources, Giovannucci estimates that world sales of certified organic coffee exceeded 67 000 metric tonnes in 2006, nearly half of which (30 700 metric tonnes) were consumed in North America. This is considerably more than the approximately 52 000 metric tonnes of organic coffee consumed worldwide in 2005<sup>98</sup>, when

**Table 12. Estimated imports of certified organic coffee (metric tonnes)**

Year	2003	2005	2006
World	42 000	52 000	67 000
North America	16 500 (2004)	19 000	30 700

Source: Giovannucci and Coffee Guide for 2005 and 2006; World Bank (2005) for 2003. Giovannucci and CIMS for 2004.

**Figure 17. US imports of organic coffee (past and industry projections)**



Source: Giovannucci and Villalobos, 2007. The State of Organic Coffee: 2007 US Update, CIMS: San José, Costa Rica

19 000 metric tonnes (37 percent) were consumed in North America (Table 12 and Figure 17). The share of North America in world organic coffee consumption has increased substantially.

This estimate indicates that organic coffee represents approximately 2 percent of the total North American coffee market in volume. The share in value is slightly higher since organic coffee usually fetches higher prices than conventional coffee.

### Market trends

Estimates for the growth rate of the organic coffee market differ across sources. Data collected by AC Nielsen<sup>99</sup> show that organic coffee sales in the United States increased by 54 percent during the period November 2004 - November 2005, while total coffee sales grew by only 8.5 percent in that period (covers only certain segments of the market). Data from the *Organic Trade Association's 2006*

<sup>98</sup> The Coffee Guide (2007)

<sup>99</sup> AC Nielsen quoted in Supermarket News, 19 December 2005 issue, United States

*Manufacturer Survey* point to a slightly slower growth for organic coffee of 40 percent over the period December 2004 - December 2005. Both surveys polled limited sources. As regards North American organic coffee imports, Giovannucci and Villalobos found in research conducted for CIMS covering US importers that the average growth rate between 2004 and 2005 was 23.5 percent<sup>100</sup>. Their more recent 2007 survey indicates that the average growth in 2006 was approximately 56 percent compared to 2005 imports of green organic coffee<sup>101</sup>. They estimate that growth will slow considerably in 2007.

### Suppliers

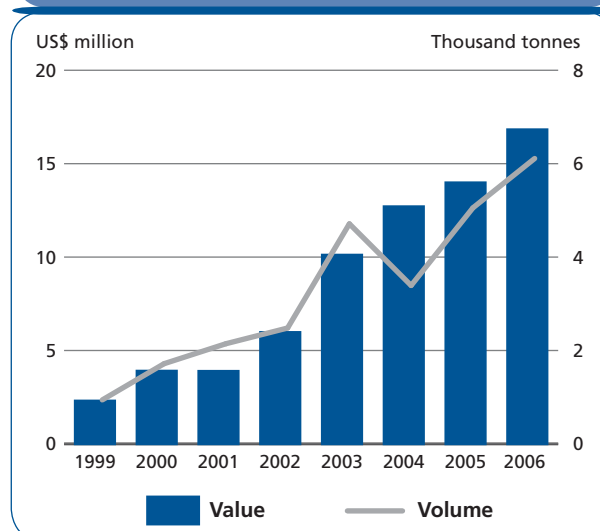
Certified organic coffee is exported from more than 30 countries (Table 13). Most of the global supply comes from Latin America where the largest exporter in 2006 was Peru (26 400 metric tonnes), followed by Central America, Brazil, Mexico and Colombia. Ethiopia is Africa's largest exporter followed by Uganda. In Asia, Papua New Guinea and Timor-Leste are the leading exporters followed by Indonesia and India.

Most organic coffee found in North America comes from Latin America, in particular from Peru, Mexico, Brazil, Bolivia, Colombia, Costa Rica, Guatemala and Nicaragua. Peru's exports to the United States have been rising steadily since 1999 and reached 6 100 metric tonnes in 2006 (Figure 18). Coffee accounts for over half of Peru's organic export earnings to the United States. There is strong interest in organic coffee from a wider range of countries<sup>102</sup>.

### Prices

Price premiums vary considerably due to several factors. In many cases, organic premiums are part of larger premiums based on quality, regional designation, reputation of the producer or additional certifications like fair-trade or bird friendly<sup>103</sup>. In recent decades tight relationship between supply and demand meant that nearly any certified organic coffee would receive a premium. In a study carried out

**Figure 18. Peru's exports of organic coffee to the United States (volume & value)**



Source: J. Fernandez, PromPeru 2007

**Table 13. Organic coffee suppliers**

Latin America and the Caribbean	Bolivia, Brazil, Colombia, Costa Rica, Cuba, Dominican Republic, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Mexico, Nicaragua, Panama, Peru, Trinidad and Tobago, Venezuela
Africa	Burundi, Cameroon, Ethiopia, Ghana, Kenya, Madagascar, Malawi, Rwanda, Togo, United Rep. Tanzania, Uganda, Zambia
Asia	China, Timor-Leste, India, Indonesia, Lao PDR, Nepal, Philippines, Sri Lanka, Thailand, Viet Nam

\* Some are occasional exporters

<sup>100</sup> Giovannucci, D. and Villalobos, A. (2006)

<sup>101</sup> Survey of US-based importers estimated to cover well over 90 percent of the North American market.

<sup>102</sup> ITC (2002)

<sup>103</sup> Giovannucci, D. and Villalobos, A. (2006)

in Northern Nicaragua during the 2000-2001 harvest, Bacon<sup>104</sup> found that the average price reported at the farm gate for organic coffee was US\$0.63 per pound, while that of conventional coffee was US\$0.41 per pound, i.e. a premium of 54 percent. While the actual amount paid has remained somewhat constant, the relative percentage is clearly greater during periods of low prices. Today the organic premium is much more correlated with quality. High-quality producers tend to receive a larger premium.

In the first half of the 2000s, the premiums for organic coffee showed a declining trend as new supply from many origins became available. However, the decline reversed in 2005 as demand firmed up in several channels, particularly among larger retailers. According to Giovannucci and Villalobos, price premiums averaged around US\$0.28 per pound (US\$0.62 per kg) in 2005 and many companies reported premiums between US\$0.15 and US\$0.80. For 2006, Giovannucci and Villalobos, cite that premiums paid by importers averaged US\$0.24 per pound with a tighter range of US\$0.10 to 0.60 per pound. This represents a general average premium of just over 20 percent. Some Latin American exporters reported premiums between 30 and 40 percent for 2005 and 2006<sup>105</sup>.

A premium paid by the buyer is not necessarily received by the producer. As certified coffees move further into mainstream distribution channels they become part of increasingly complex supply chains and, quite often, face less transparent transactions. It is difficult to determine how the premiums are distributed along the supply chain and how much reaches the farmer or cooperative. There is considerable variation in distribution and a number of North American importers are not aware of how the premiums they pay are distributed in the country of origin.

Importers that are aware of what price reaches their suppliers claim in a recent study that approximately 80 to 90 percent of the premium reaches the farmer or cooperative<sup>106</sup>. However, this is probably not representative of all certified coffees since it is likely that importers with a greater interest in knowing what their farmers receive may also stimulate higher payment levels to them.

## 2.2 Fair-trade coffee

### *Market situation*

Coffee is by far the most important fair-trade product and sales of fair-trade certified coffee have grown considerably in the last decade. FLO indicates that sales of certified fair-trade coffee worldwide reached 52 077 metric tonnes in 2006, up from 33 994 metric tonnes in 2005 (+53 percent). Nearly half of this volume was sold in North America.

According to TransFair USA<sup>107</sup>, 29 380 metric tonnes of fair-trade coffee were imported into the United States in 2006, up from 20 220 metric tonnes in 2005 (+45 percent). The fair-trade coffee market in the United States has grown dramatically in recent years (Figure 19), although preliminary estimates for 2007 indicate a marked deceleration due in part to some over-purchasing in 2006. Canada imported and sold an estimated 2 770 metric tonnes of green fair-trade coffee in 2006 growing by approximately 60 percent over 2005.

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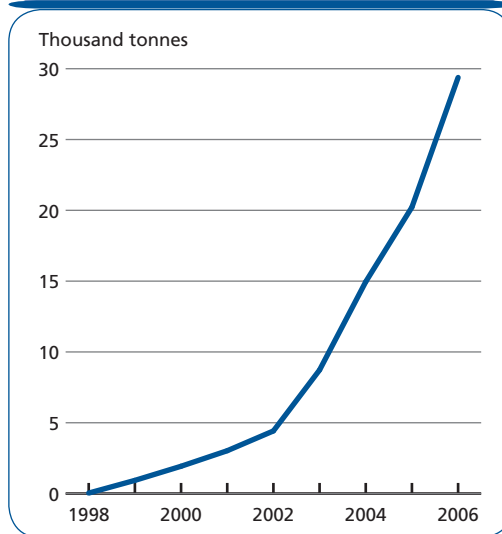
<sup>104</sup> Bacon, C. (2005)

<sup>105</sup> Daabon and Apex Brasil

<sup>106</sup> Giovannucci, D. and Villalobos, A. (2007)

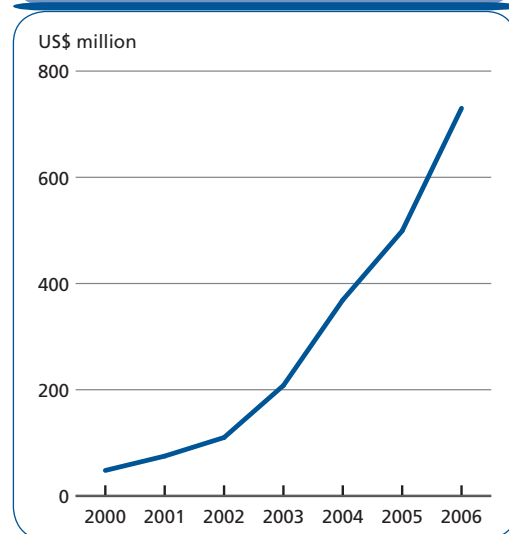
<sup>107</sup> TransFair USA (2007) Fairtrade Almanac 1998-2006

**Figure 19. Imports of FLO-certified coffee into the United States**



Source: TransFair USA (2007)

**Figure 20. Estimated retail sales value of fair-trade certified coffee in the United States**



Source: TransFair USA (2007)

Fair-trade certified coffee imports account for some 2 percent of the total US green coffee imports. TransFair USA estimates that the retail sales of fair-trade coffee in the United States reached US\$730 million in 2006 (Figure 20), up from US\$499 million in the previous year (+46 percent). It calculates that fair-trade coffee represents over 3 percent of the US retail market value. The number of firms (roasters and importers) licensed by TransFair in the United States has risen steadily since 1999 to 463 firms in 2006 (Table 14).

**Table 14. Number of firms licensed by TransFair USA**

No of licensees	Roasters	Importers	Total
2000	62	13	75
2006	395	68	463

Source: TransFair USA (2007)

There is considerable overlap of the organic and fair-trade coffee sectors. In 2006, approximately 78 percent of the fair-trade coffee sold in the United States was also certified organic while in Canada and the world this reached near 50 percent on average. This reflects a tendency toward double and even triple certifications; a trend with challenging implications for producers (see Section 3). The premium for fair-trade coffee that is also certified as organic rose in 2007 by US\$0.05 per pound to US\$0.20. The increase reflects the higher costs of organic production and compliance and also serves as an incentive for greater environmental sustainability.

### Suppliers

Fair-trade coffee was produced and exported by 26 countries in 2006 (Table 15). The five largest fair-trade suppliers to the North American market were Peru, Mexico, Nicaragua, Indonesia and Ethiopia, together accounting for two-thirds of US imports. Other important suppliers include Guatemala, Colombia and Brazil<sup>108</sup>.

<sup>108</sup> Transfair USA (2006)



**Table 15. Countries supplying FLO-certified fair-trade coffee to the United States in 2006**

Country	Exports to the USA (MT)
Peru	7 349
Mexico	3 581
Nicaragua	3 299
Indonesia	2 821
Ethiopia	2 584
Brazil	1 998
Guatemala	1 788
Colombia	1 520
Papua New Guinea	< 1 000
Costa Rica	<1 000
Dominican Republic	< 1 000
Haiti	< 1 000
Honduras	< 1 000
Timor-Leste	< 1 000
El Salvador	< 1 000
Rwanda	< 1 000
United Rep. Tanzania	< 1 000

Source: TransFair USA 2007

### Prices

The FLO system guarantees a Fairtrade Minimum or floor price that is based on the estimated cost of sustainable production. The minimum price ranges from US\$1.01 to US\$1.21 per pound depending on the type of coffee and the country of origin (Table 16). When market prices rise above the minimum, i.e. US\$1.21 for many washed arabicas, a small additional premium is paid<sup>109</sup>. For many years that additional premium was US\$0.05 per pound but in June 2007 it was raised to US\$0.10 per pound. The premium is intended for use by cooperatives for social and economic investments at the community and cooperative level. When the coffee is also certified organic, an extra premium of US\$0.20 per pound applies.

This system proved very beneficial during the recent price crisis. Although the fall in conventional coffee prices caused considerable hardship for small coffee growers across the developing world, the price obtained by fair-trade growers was often above the

**Table 16. FLO Minimum prices for coffee as of 2007 (US cents per pound FOB)**

Type of coffee	Central America, Africa, Asia	South America & Caribbean
Washed Arabica	121	119
Non-washed Arabica	115	115
Washed Robusta	105	105
Non-washed Robusta	101	101

Source: FLO 2007

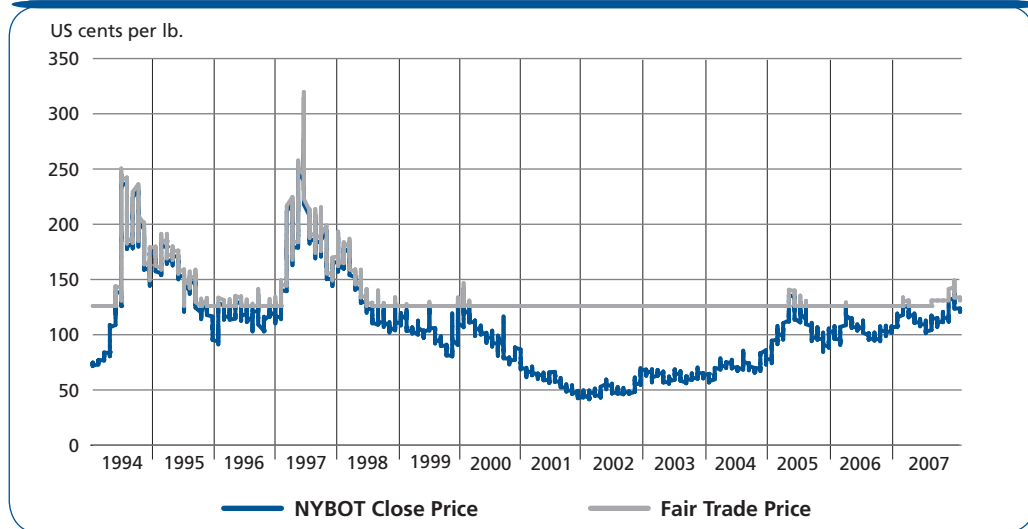
**Table 17 Countries and farmers supplying fair-trade coffee globally in 2006 (FLO-certified)**

Country	Farmers participating
1. Bolivia	3 666
2. Brazil	7 500
3. Cameroon	1 037
4. Colombia	19 502
5. Congo, D.R.	87
6. Costa Rica	14 555
7. Côte d'Ivoire	3 937
8. Dominican Rep.	5 745
9. Timor-Leste	17 576
10. Ecuador	1 249
11. El Salvador	1 257
12. Ethiopia	40 325
13. Guatemala	8 898
14. Haiti	28 968
15. Honduras	2 054
16. India	2 343
17. Indonesia	2 346
18. Kenya	8 811
19. Laos	517
20. Mexico	24 988
21. Nicaragua	7 174
22. Papua New Guinea	4 756
23. Peru	33 991
24. Rwanda	10 916
25. United Rep. Tanzania	3 321
26. Thailand	192
27. Uganda	2 950
28. Venezuela	677
29. Zambia	289
<b>TOTAL</b>	<b>259 627</b>

Source: FLO International and TransFair USA 2007

<sup>109</sup> For arabica coffees (representing the majority of fair-trade certification) the market price is determined by the price of the second position 'C' futures contract at the InterContinental Exchange (ICE).

Figure 21. Fair-trade price advantage in difficult years



international market price (Figure 21). In October 2001, when the market price fell to a record low of US\$0.45 per pound, the price of fair-trade coffee was 180 percent higher. Recently, as market prices have stayed above the US\$1.00 range, the relative premiums for fair-trade coffee have been more modest. As such there are questions about the extent to which producers want to continue with the certification when the price differential is small. For many that do continue there are likely to be two reasons: i) having a longer-term vision of the cyclical nature of commodity pricing, and ii) recognizing the other benefits of fair-trade (i.e. organizational strengthening, more stable relationship with buyers and community investment).

Over a quarter of a million farmer families directly benefited from the sales of fair-trade coffee in 2006 (Table 17). Most belonged to 241 organizations of coffee producers that were certified by FLO in 2006. FLO estimates that the fair-trade system earned farmers an extra income of some €41 million (US\$57.4 million) that year. This sum represents an average of more than US\$200 per farmer above what they would have earned selling on the conventional market. TransFair USA estimates that the quantities sold in the United States alone generated an additional income of US\$17 million for 106 farmer cooperatives in 23 countries.

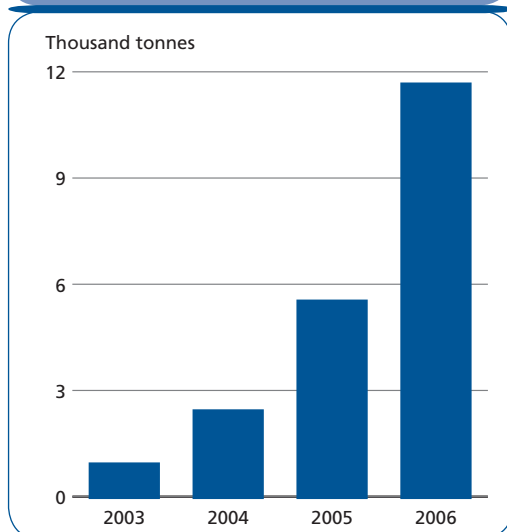
### 2.3 Rainforest Alliance coffee

RA emerged in the mid-1990s as a certifier of environmentally friendly coffees (originally called Eco-OK) that were then collectively called shade-grown. From early efforts in Central America, it has expanded to other parts of Latin America and more recently to Africa and Asia. In terms of coffee volume sold, it is currently the fastest growing. As of October 2007, RA had certified 16 838 farms and over 200 000 hectares of coffee.

According to RA, 11 631 metric tonnes of their certified coffee were imported into North America in 2006, up from approximately 5 500 metric tonnes in 2005. This represents slightly less than 1 percent of the total imports of green coffee into North America. Since 2003, North American imports of RA-certified coffee have grown by more than 100 percent annually (Figure 22).

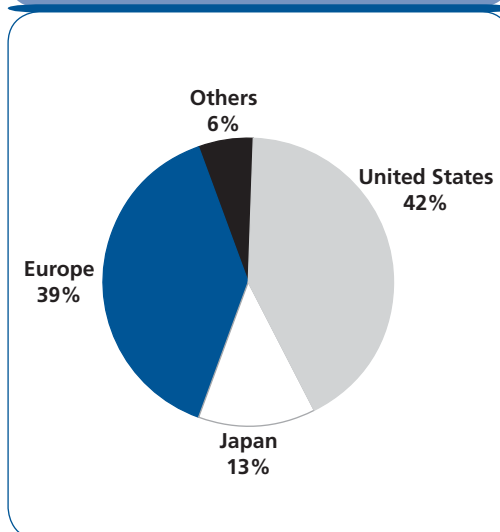
The international market for these coffees has also expanded considerably in recent years with more than 100 percent average annual growth in the last three years. In 2006, North America represented roughly 42 percent of all RA coffee sales (Figure 23) though this share is dropping. Sales are expanding rapidly in Europe and are also on the rise in several other markets including Japan, Australia and Brazil, though at a slower pace.

Figure 22. Imports of RA-certified coffee into North America



Source: Rainforest Alliance

Figure 23. Markets for Rainforest Alliance coffees (2006)



Source: Elaborated from Rainforest Alliance data

As with the organic and fair-trade certification schemes, RA has recently been adopted by some larger roasters and retailers such as Kraft Foods, Tchibo and Lavazza in Europe and Wal-Mart and Kraft in the United States. As with other certifications, their partnerships with major industry players are growing. For example, all of the nearly 1 200 McDonald's restaurants in the United Kingdom and Ireland now exclusively sell Kenco (Kraft Foods) coffee from RA-certified farms.

Brazil is the single largest supplier of certified RA coffees. Nearly all of the RA coffees before 2006 came from Latin America. Today Ethiopia, United Republic of Tanzania and Indonesia also participate (Table 18). Several new origins are in the process of certification.

Table 18. Exporters of Rainforest Alliance coffees (2007)

Country	No of farms
1. Brazil	34
2. Colombia	2 104
3. Costa Rica	2 023
4. El Salvador	210
5. Ethiopia	6 294
6. Guatemala	88
7. Honduras	309
8. Indonesia	539
9. Mexico	1 149
10. Nicaragua	17
11. Panama	4
12. Peru	4 065
13. United Rep. Tanzania	2

Source: Compiled from RA data

The price premiums for certified RA coffee range from US\$0.04 to US\$0.20 per pound with the average at US\$0.08 to US\$0.12. As with many other certification schemes, these premiums depend largely on the quality of the product and the relationship between the buyer and the producer.

## 2.4 Bird Friendly coffee

Bird Friendly® (BF) was one of the early environmentally-oriented certification schemes for coffee and helped to establish the standards now used by others. It emerged as a response to the dramatic decline in North American migratory bird species when this decline was strongly correlated to the reduction of the avian winter habitat areas of Latin America. The reduction of these forests often coincided with their conversion to agricultural land, including the conversion of naturally shade-grown coffee to more intensive methods that eliminated much of the tree cover. Studies in the 1990s demonstrated that shade coffee farms could both provide valuable habitat for avian biodiversity as well as remain profitable. To encourage such farmers, the Smithsonian Migratory Bird Center (SMBC) elaborated its BF certification. The BF programme focuses on natural biodiversity and a prerequisite

for its seal is organic certification, which, among other guidelines, prohibits the use of any synthetic fertilizers, pesticides, herbicides or fungicides.

While relatively small in terms of coffee sold, it supplies a significant North America niche. Over 3 600 metric tonnes of BF coffees were sold in 2006, all to Japan, Canada and the United States. Yet, according to the SMBC, less than 200 metric tonnes were sold with the BF label. The bulk of BF-certified coffee is grown in Mesoamerica, from southern Mexico through Central America (Table 19).

**Table 19. Number of bird-friendly certified farms by country of origin (2006)**

Country	No of certified farms
Mexico	11
Peru	10
Salvador	6
Guatemala	4
Bolivia	1
Venezuela	1

Source: Smithsonian Migratory Bird Center

Price premiums for BF coffee have ranged from US\$0.05 and US\$0.28 per pound with the average typically being between US\$0.05 and US\$0.10; that is in addition to the price premium for the organic certification. As with other certifications, the premiums vary according to the buyer and the quality of the coffee.

## 2.5 Utz Certified

The Utz Certified label currently has a relatively modest presence in North America, but is growing. This programme was founded in Guatemala as Utz Kapeh in 1997 by Dutch coffee roaster, Ahold Coffee Company and later became an independent globally-oriented foundation. It helped to develop a code of Good Agricultural & Business Practices that is now the Coffee Code of GlobalGAP (formerly EurepGAP). It also uses basic social criteria from the International Labour Organization Conventions. Producers and participating firms must meet the Chain of Custody requirements that ensure traceability.

Utz Certified coffee is exported from 18 producing countries and sold in 19. Utz is one of the few schemes that certify significant quantities of robusta coffee. Europe is, by far, its major market region. Global sales of Utz certified coffee reached 36 000 metric tonnes in 2006, representing 25 percent growth over the prior year. North American sales accounted for less than 5 percent or 1 800 metric tonnes<sup>110</sup>.

Products that use the Utz Certified logo may benefit from a suggested price premium but there is no mandate for this. In practice, producers have been receiving premiums that average US\$0.03 to US\$0.05 with a reported range of between US\$0.01 and US\$0.12 over the last three years<sup>111</sup>.

## 2.6 Private company standards for quality and sustainable coffee production

The standards and verification programmes set by companies are seldom included in sustainability discussions because of three reasons: i) they are under the private control of a company or group of firms that can at any time alter, dilute, or simply not fully use the standard or code as they see fit; ii) they may be designed more for corporate needs than for producer sustainability, for example, having questionably effective standards or not using independent third-party certification; and iii) they may not meet the economic needs of producers (one of the pillars of sustainability) by not providing adequate remuneration for sustainable production practices.

<sup>110</sup>Source Utz Certified

<sup>111</sup> Giovannucci personal communication with Utz Certified and field investigations to Central America, Mexico, Colombia in 2005-06.

Nevertheless, this report briefly considers two company certification schemes because of their large potential impacts due to the size of their purchasing and the perception that, for the most part, the above arguments may not apply to them. It should be noted that at the time of writing this report no independent study has been carried out on the costs and benefits of these schemes.

Starbucks is one of the world's leading coffee brands and one of the top retail food chains operating more than 14 000 outlets worldwide in 2007. Several years ago it developed its own private sourcing standard called Coffee and Farmer Equity Practices or C.A.F.E. Practices that incorporates a set of basic social and environmental standards with its private quality requirements.

In 2006, Starbucks purchased more than 145 000 metric tonnes of coffee and paid an FOB average price of US\$1.42 per pound (non-exporting growers may reportedly obtain 15-35 percent less depending on how many middlemen stand between them and the exporter). Nearly 77 000 metric tonnes were independently certified according to C.A.F.E. Practices<sup>112</sup> and approximately 56 000 metric tonnes were estimated to be sold in the United States. Global projections for 2007 indicate that the total will exceed 100 000 metric tonnes<sup>113</sup> Starbucks also purchased significant but smaller amounts of organic, fair-trade and other eco-friendly coffees.

Nespresso is one of Nestlé's fastest-growing subsidiaries providing espresso and brewing equipment on a membership basis to clients around the world. North America is one of its most important markets. Although it is not a certification scheme, it may be useful to mention Nespresso's AAA Sustainable Quality Program® due to the impacts it may have on coffee growers in the future. This programme was co-developed with RA, whose members also verify compliance with the standard. It features social and environmental practices and purchases coffees in Costa Rica, Colombia, Guatemala, Mexico, Brazil and Kenya. It was publicly introduced in 2005 and is still relatively new. In 2006 nearly 6 000 metric tonnes, or approximately one-third of Nespresso's purchasing, met its AAA standard<sup>114</sup>. According to Nespresso, producers typically receive well above the market price for a combination of quality and sustainability though Nespresso makes no distinction in terms of a premium for meeting the AAA standard.

## 3. COSTS AND BENEFITS TO DEVELOPING COUNTRY SUPPLIERS

### 3.1 The value of transparent price premiums

Many buyers believe that it makes good business sense to request that some higher standard of quality is met as part of sustainable practices. Indeed, the trend toward higher quality in certified coffees may well improve their desirability in the marketplace<sup>115</sup>. However, when buyers fail to distinguish the value they place on sustainable practices, they dilute its importance. Paying a high price for a certified coffee may simply mean that a buyer is purchasing a higher-quality coffee with preferred flavour characteristics. As such, when

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<sup>112</sup> Starbucks corporate records

<sup>113</sup> Estimate calculated from total global certification based on relative percentage of total store revenue earned in the United States.

<sup>114</sup> Personal communication November 2007 D. Giovannucci with Nespresso's Karsten Ranitzsch and GoodBrand & Company's Dean Sanders.

<sup>115</sup> Bacon (2005); CIMS (2003)

there is no correlation between the price and the recognition of a producer's sustainable practices, it becomes more difficult for a producer to justify the costs of sustainability. For sustainability to advance, producers need to have a clear signal from the market about sustainability and there is no signal clearer than a price premium.

The transparency of pricing — where buyer and seller clearly understand what is being paid for — facilitates transactions and improves market functions. In practice it may be difficult to achieve a rigid or exact distinction such that, for example, 37 cents is for the quality and 22 cents is for the certification. Nevertheless, some distinction is necessary. While the lack of transparency may create a temporary negotiation advantage for the buyer, this is a false economy since it is also more likely to reduce the number of interested participants or the number of certified products available. Furthermore, without clarity and transparency in these transactions, it becomes difficult for any buyer or firm to claim they are supporting sustainability. Without a clear correlation between price and sustainability practices, the buyer may simply be paying for any other characteristic such as rarity or taste.

Besides knowing what the premium is for, it is also important to know who receives it. Growers that are large enough to export directly tend to receive much, if not all, of the negotiated premium for certified coffees. However, most growers operate through middlemen or cooperatives that play a vital role in marketing their coffee. In some cases these can capture a substantial portion of the premium paid for certified products. Few buyers are willing to disclose the distribution of premiums along the value chains. Yet, if producers fail to receive a fair portion of the premium they may also fail to achieve sustainability. In accordance with fair labour practices, companies are increasingly insisting on transparency that assures them that their value chain is performing sustainably. Some, like Starbucks, want to know what the farmers who provide their coffees are actually paid. Recent examples illustrate the dangers faced by firms that are unaware of (or uninterested in) the pay or the conditions of their value chain<sup>116</sup>. Value chains can be both transparent and competitive as demonstrated by one of the fastest-growing certified coffee import firms in North America<sup>117</sup>. Transparency and sustainability are intertwined.

### 3.2 Assessing the costs and benefits of different certification schemes

Increasingly, producers have their coffee certified to two or three different standards. Roasters and major retailers in North America as well as Europe have shown an increasing trend toward multiple certifications for a single product<sup>118</sup>. Today, the majority of both organic and fair-trade coffees in the market carry at least one other certification. The implications of meeting multiple standards can be substantial for any producer. In addition to learning the individual requirements of the different standards, they may necessitate following somewhat different practices and also keeping separate sets of records. In some cases additional financial resources are required in order to invest in meeting the standards. The benefits they receive may be both tangible and intangible and can vary significantly between standards.

Several of the certification programmes, encourage and even require farmers to meet basic good management methods such as keeping records, adopting lower-cost integrated pest management, or resource and water conservation strategies. Though the evidence is only anecdotal, some certifiers note that this appears to provide some efficiency benefits at the farm level that can supplement an actual premium.

<sup>116</sup> US government resolution of child slavery in the cacao industry, Wal-Mart and JCPenney garment industry "sweatshop" scandals, Nike Inc.'s stock value decline resulting from consumer awareness of pay and working conditions in their contracted footwear factories. See also: Klein, N. (2000); Utting, P. (2005)

<sup>117</sup> Firm is ranked in Inc. Magazine's "Inc. 5000", that lists the fastest growing companies in America. See <http://sustainableharvest.com/mba>

<sup>118</sup> Busch, L. and Loconto, A. (2007); Giovannucci, D. and Koekoek, F.J. (2003); Busch, L. and Bain, C. (2004)

A recently launched effort under the auspices of 20 institutions<sup>119</sup> has developed a useful method for measuring, at the farm level, the costs and benefits of any sustainability initiatives. This work carried out by the Committee on Sustainability Assessment (COSA) is now being piloted in Africa and Latin America. For producers, it provides relevant information on the expected financial and time investments so they can both select and manage any sustainable practices they choose in a more cost-effective manner. Traders and the rest of the industry benefit since sustainable management can help to achieve stability and consistency in farm output. For policy-makers, COSA methods offer clear and objective information on how different sustainable practices actually impact producers and their communities. Even the sustainability initiatives or standards bodies themselves benefit since they need to understand the impacts of their methods at the farm level<sup>120</sup>.

## 4. MARKET PROSPECTS

In recent years, there has been strong growth in the demand for certified coffee. Some certification labels are gaining credibility, generating substantial revenues for producers, and rapidly entering the mainstream<sup>121</sup>. While the conventional coffee market shows little or no growth in North America, the market for certified coffees has been growing at double digit rates since the turn-of-the-century. Of course, the volumes are still smaller for certified coffees so large growth rates are slightly less significant. Nevertheless, an average for the three-year period 2004-2006 shows consistently higher growth for certified coffees than for either conventional or specialty and gourmet coffees (Table 20).

North America's growth pattern resembles tendencies in other developed markets including much of Europe and Japan. Giovannucci and Koekoek (2003) note that growth for certified coffees has historically occurred in either small-scale or alternative trade channels whose intrinsic reach would limit the expansion of certified products. Increasing consumer demand in recent years has stimulated most mainstream retailers to devote more space to sustainable products.

Today, highly visible retail food service chains (i.e. Starbucks and McDonald's) and mainstream supermarkets (i.e. Wal-Mart, Kroger, Safeway and Loblaws) are the twin drivers for the fast-growing consumption of certified sustainable products. These firms seek to both differentiate their offerings and meet emerging demand while improving their positioning as socially responsible corporations. These market channels have provided considerable opportunities for certified producers and yet could pose severe challenges as well.

**Table 20. Growth rate of distinct coffee industry segments**

	Global %	USA %
Conventional	1-2	0-1
Gourmet (specialty)	5-10	10-15
Organic	13-17	38
Fair-trade	46	41
Rainforest Alliance	106	120
Utz certified	31	+

Source: Giovannucci calculations based on USDA, SCAA, FLO, TransFair USA, Giovannucci, CIMS, Utz Certified, Rainforest Alliance

When large firms manage considerable proportions of the volume, even minor changes in their purchasing choices can have a significant impact on what is still a relatively small segment of the market. Certified markets are still relatively thin in terms of the number

<sup>119</sup> The Sustainable Coffee Partnership at: [www.iisd.org/markets/policy/scp.asp](http://www.iisd.org/markets/policy/scp.asp)

<sup>120</sup> [www.iisd.org/standards/cosa.asp](http://www.iisd.org/standards/cosa.asp)

<sup>121</sup> World Bank (2004). And also in Giovannucci, D. and Ponte, S. (2005)



of buyers and therefore can be volatile. This does not match well with the much longer timeframe of producers who typically have to work for one to three years to complete a certification process.

Industry projections for the North American market suggest continued but more modest growth in 2007 and 2008. Double-certified coffees such as organic + fair-trade are likely to continue their strong growth since they are widely accepted by consumers and broadly distributed. About three-fourths of fair-trade coffee in the United States and half in Canada and the rest of the world is also certified organic with this trend likely to continue or even increase. Similarly, a large proportion of organic coffee commonly also carries another certification with fair-trade being the most common. Imports of organic coffee into North America are forecast to reach about 35 000 metric tonnes in 2007<sup>122</sup>. The Coffee Guide forecasts global imports to range between 60 000 metric tonnes and 66 000 metric tonnes in 2007<sup>123</sup> while Giovannucci estimates over 70 000 metric tonnes. The growth of single-certified fair-trade coffee sales is also expected to slow somewhat from its pace in recent years. Sales of RA-certified coffee are projected to grow, though less quickly than in the past, with 2007 global estimates exceeding 2006 numbers by just over 50 percent and overall volume exceeding 40 000 metric tonnes. Utz Certified coffee, which has a relatively modest presence in North America, is expected to grow well in 2007 though on a small base as global sales reach approximately 50 000 metric tonnes.

Quality continues to be a key factor for growth in the North American market for certified organic, BF and fair-trade coffees. With the advent of much larger buyers, several certification schemes have attracted much larger producers as well. The less demanding standards can provide large volumes at lower costs for buyers, and are facilitating the creation of more mainstream commercial partnerships between producers, traders and large buyers. There are also company codes (not certification schemes) that intend to provide the most basic social and environmental standards to the industry, though none have yet been visible in North America<sup>124</sup>.

There are concerns for the consumer perception of different sustainability labels on products. Some of the concerns focus on the possible difficulty of making distinctions between them though currently few are advertised and no problem has yet emerged. Other concerns center around the potential advertising of a label when the product may contain only small quantities of sustainably-grown coffee. The organic label is the only one that is regulated in North America (this is pending in Canada) and requires a very high percentage (>95 percent) of certified organic product before the term can be used on the label.

Many growers are adapting their production methods in order to take advantage of these emerging market segments<sup>125</sup>. More than 20 million families rely on coffee for their livelihood and between one and two million farms participate in the different certified programmes. Many are small-scale family farms that produce over 70 percent of the world's coffee<sup>126</sup>.

Differentiated and value-based products offer a way for producer countries to participate in the highly competitive international coffee market. According to a World Bank report by

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<sup>122</sup> Projections from Giovannucci.

<sup>123</sup> World Market for Organic Coffee, *The Coffee Guide*, 03.02.11

<sup>124</sup> The Common Code for the Coffee Community (4C) is the most visible such code. It encourages basic good agricultural and management methods and includes minimum social and environmental standards.

<sup>125</sup> Bacon, C. (2005)

<sup>126</sup> Oxfam (2001)



Lewin, Giovannucci and Varangis, a competitive market position based on processes that are more difficult to duplicate, such as certified coffees, is potentially a more viable long-term strategy for coffee producers:

*Differentiation can present a feasible competitive platform, especially for countries lacking the necessary factors to be competitive as bulk raw material producers. Such process-oriented strategies lend themselves well to many of the poorer producing countries and present a rare opportunity for rural smallholders to participate in global markets while also safeguarding their natural resources<sup>127</sup>.*

Nevertheless, it is important to note that this segment of the market is also becoming increasingly competitive as it grows. Being certified is important for many growers but it is not enough. Success depends on also having good quality, consistency and effective marketing relationships.

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<sup>127</sup> World Bank (Lewin, B., Giovannucci, D. and Varangis, P., 2004. p.13)

## CHAPTER 4: CERTIFIED COCOA

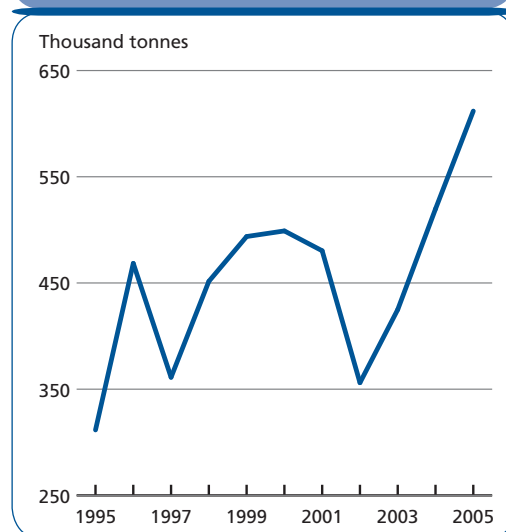
All cocoa sold in North America is imported and most cocoa is produced in developing countries, creating specific opportunities for developing country exporters. There is strong demand in North America for high quality products and, unlike coffee, the cocoa market is presently characterized by undersupply.

### 1. OVERVIEW OF THE NORTH AMERICAN COCOA MARKET

North America imported an annual average of 1.55 million metric tonnes of cocoa beans and processed products (including chocolate) over the period 2005-2006 for a value of some US\$3.5 billion, accounting for 16 percent of world imports in value. Imports of cocoa beans amounted to 552 000 metric tonnes (474 000 metric tonnes in the United States and 78 000 metric tonnes in Canada) valued at US\$846 million in 2006. Imports of chocolate account for over half of the import value (Table 21 ). According to a report released in 2007<sup>128</sup>, total sales of chocolate through all channels reached US\$16 billion in the United States in 2006.

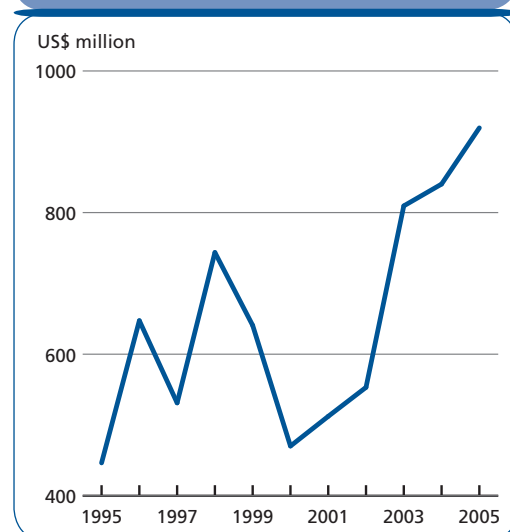
North American consumption grew by approximately 30 percent between 1990 and 2005. Imports of cocoa beans grew markedly from 2002, reaching a high of 632 000 metric tonnes in 2005 (Figure 24). In value, they rose from less than US\$500 million in 2000 to over 900 million in 2005 (Figure 25). They dropped in 2006, as more semi-

**Figure 24. Imports of cocoa beans into North America**



Source: FAOSTAT 2007

**Figure 25. Import value of cocoa beans into North America**



Source: FAOSTAT 2007

<sup>128</sup> Packaged Facts (2007)

Table 21. Imports of cocoa products into North America in 2006

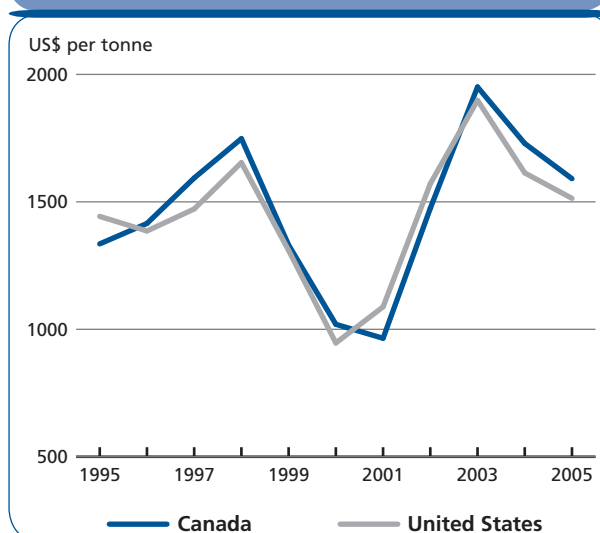
Products	Volume 2006 (MT)	Value 2006 (000 US\$)
Cocoa beans	551 759.9	846 008.7
Butter	120 255.0	491 560.5
Powder and cake	166 086.0	229 931.2
Paste/liquor	54 715.1	136 606.0
Chocolate	648 332.5	1 814 449.6
Total	1 541 148.5	3 518 555.9

Source: COMTRADE 2007

processed and processed products were imported. Nevertheless the total value of imported cocoa products (including chocolate) continues to increase (+3.4 percent between 2005 and 2006). The unit values of cocoa beans imported into the United States and Canada rose in the early 2000s, reflecting the strong increase in world cocoa prices (Figure 26).

## 2. CURRENT MARKET SITUATION FOR CERTIFIED COCOA

Figure 26. Unit values of cocoa bean imports into Canada and the United States



Source: FAOSTAT 2007

There are even fewer trade data for certified cocoa than for certified coffee or fresh produce. In the specific case of cocoa, the absence of official statistics is compounded by several factors: the quantities produced and marketed are extremely low; there are different forms of cocoa products (beans, liquor, powder, cake, butter, paste, chocolate) and the quantities imported may differ from those marketed due to stocks. The data are incomplete and very fragmented. Worse, the reliability of the few available estimates may be questioned. Therefore, readers should consider the data provided in this chapter as indicative estimates only and give more importance to the trends.

Several organizations and industry sources point to a marked expansion in the production and sales of certified cocoa and its processed products. According to a recent ITC report<sup>129</sup>, sales of organic chocolate and other cocoa products are on the rise and world demand for organic cocoa is growing. The International Cocoa Organization (ICCO) reckons that the market for certified organic chocolate has developed dramatically in recent years, with global sales of organic chocolate alone (not including other cocoa products) reaching US\$304 million in 2005, a 75-percent rise over its level of 2002<sup>130</sup>. It explains this increase by

<sup>129</sup> ITC (2006), p.46

<sup>130</sup> ICCO (2007)

consumer concerns about food safety and environmental issues and the growing demand for premium chocolate. In the United States, the share of premium chocolate grew from 13 percent of the total market in 2002 to almost 17 percent in 2006<sup>131</sup>. In response, organic cocoa production has increased significantly – farmers are attracted by higher prices and governments and development agencies are encouraging them to convert to organic production. While the North American certified cocoa market is growing fast, Europe is by far the largest importer of certified cocoa beans (especially organic) and the largest processor and manufacturer of certified cocoa and chocolate products. A portion of the certified cocoa processed and packaged in Europe is re-exported to the United States, Canada and Japan.

## 2.1 Organic cocoa

### *Market situation*

There is a critical lack of data on the quantities of organic cocoa marketed worldwide. More studies have been done at production level, but estimates differ widely across sources. ICCO estimates that production of organic cocoa worldwide exceeded 15 500 tonnes in 2005, while Willer and Yussefi<sup>132</sup> calculate a much larger figure exceeding 32 000 metric tonnes. However, these authors estimate exported volumes at 10 627 metric tonnes at least, due to data gaps for some exporters, i.e. only one-third of total output. This compares to an estimate of world production in 2000 of 11 700 metric tonnes made by the Swiss Import Promotion Programme (SIPPO) in a report released in 2002<sup>133</sup>. It could be that the ICCO figure relates to production for export only. Both the ICCO and Willer and Yussefi reports have significant data gaps and do not provide production volumes for substantial suppliers such as Colombia and Ecuador. Under this assumption it can be inferred that exported quantities ranged between 11 000 and 15 500 metric tonnes in 2005. It is certain that the organic market only represents a very small share of the global cocoa market, estimated by ICCO at less than 0.5 percent in 2006<sup>134</sup>.

It is difficult to determine what percentage of this quantity is sold in North America. Most estimates regarding North American organic cocoa imports date from 2000 and 2001, with approximately 70 metric tonnes imported in 2000 and 75 metric tonnes imported in 2001<sup>135</sup>. Although less than 1 percent of the North American cocoa market is organic, there has been a sharp rise in demand in recent years. According to the Nature Conservancy, organic chocolate sales have grown by approximately 70 percent per year since 2002. Even though current market penetration remains low, exporters, certifiers and industry experts agree that the potential of organic cocoa is high. However, there are many challenges on the supply side relating to quality, the cost of certification and producer access to and knowledge of organic supply channels. Trade channels will have to allow for increased volumes of organic cocoa, for example through the entry of bigger players in the market<sup>136</sup>. The development of direct trade channels and growth in the processing and manufacturing industry in North America should accelerate considerably the growth of the North American organic cocoa market.

### *Suppliers*

Beside the cocoa re-exported from Europe, the organic cocoa sold on the North American market originates mainly from Latin America and the Caribbean. According to ICCO

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<sup>131</sup> Packaged Facts (2007)

<sup>132</sup> IFOAM (2006)

<sup>133</sup> SIPPO (2002)

<sup>134</sup> ICCO (2007)

<sup>135</sup> ITC (2004) and SIPPO (2002)

<sup>136</sup> ICCO (2007)

and Willer and Yussefi, this region produces more than 70 percent of the world supply of organic cocoa (Table 22). The Dominican Republic is by far the largest supplier<sup>137</sup>, but estimates of its production and exports differ widely across sources. While ICCO estimates output at 5 000 metric tonnes in 2005, Garibay<sup>138</sup>, has a much higher figure of 14 350 metric tonnes. Estimates of its exports are displayed in Table 23. However, most of its exports are destined for Europe, although shipments to North America have been rising in the recent past.

Peru exported almost 1 000 metric tonnes of organic cocoa beans in 2006 for a value of US\$2 million<sup>139</sup> and its export promotion organization PromPex claims that it is the world's second largest supplier of organic cocoa. Most of its exports go to Europe, with North America accounting for less than 20 metric tonnes in 2006. However, CIMS ranks Colombia as the second leading supplier and estimates that together with the Dominican Republic this country produces 50 percent of the world's organic cocoa<sup>140</sup>. The uncertainty over Colombia's exports makes it difficult to estimate total world supply.

According to ICCO, Africa produced over 3 000 metric tonnes of organic cocoa in 2005, but most of it was exported to Europe. ICCO and Willer and Yussefi rank Madagascar, the United Republic of Tanzania and Uganda as the main producers of organic cocoa in Africa. There is evidence that organic cocoa production is increasing rapidly. Newcomers such as Cuba and Venezuela are reported to be expanding their cocoa areas under organic management.

### Prices

As for many other organic products, the market for organic cocoa has exhibited strong price fluctuations, which are mainly due to the small quantities, the lack of consistency in

**Table 22. Different estimates of organic cocoa production (in MT) in selected countries in 2005 according to two sources**

Countries	ICCO	Willer and Yussefi
Madagascar	1 500	1 500
United Rep. Tanzania and Uganda	1 500	1 400
Bolivia	400	300
Brazil	1 100	n.a.
Costa Rica	300	n.a.
Dominican Republic	5 000	14 350
Mexico	2 500	9 419
Panama	350	n.a.
Peru	1 850	4 500
Other Latin America and Caribbean	238	128
Sri Lanka	200	n.a.
Vanuatu	500	500
Other Asia and Pacific	62	50
<b>Total identified</b>	<b>15 500</b>	<b>&gt; 32 000</b>

Sources: ICCO Annual report 2005/06 and IFOAM (2006)  
n.a.: not available

**Table 23. Exports of organic cocoa beans from the Dominican Republic 2004-2006 (in MT)**

Exports	2004	2005	2006
To North America	121	355	454
Total	3 319	1 676*	4 002

Sources: CEI-RD, 2007

\* IFOAM (2006) estimate total Dominican Republic exports at 8 500 metric tonnes

<sup>137</sup> The National Confederation of Dominican Cocoa Cultivators (CONACADO) is the largest producer and exporter of organic cocoa in the world. See [www.cei-rd.gov.do](http://www.cei-rd.gov.do)

<sup>138</sup> Quoted in Willer and Yussefi (2006)

<sup>139</sup> PromPerú, August 2007

<sup>140</sup> CIMS/EM (2005)

Table 24. Unit values of cocoa bean exports to the United States in 2006

Country	Conventional cocoa beans (US\$/MT)	Organic cocoa beans (US\$/MT)	Price premium (US\$/MT)	Percentage premium (%)
Peru	2 354	5 684	3 331	142
Dominican Republic	1 394	1 590	195	14

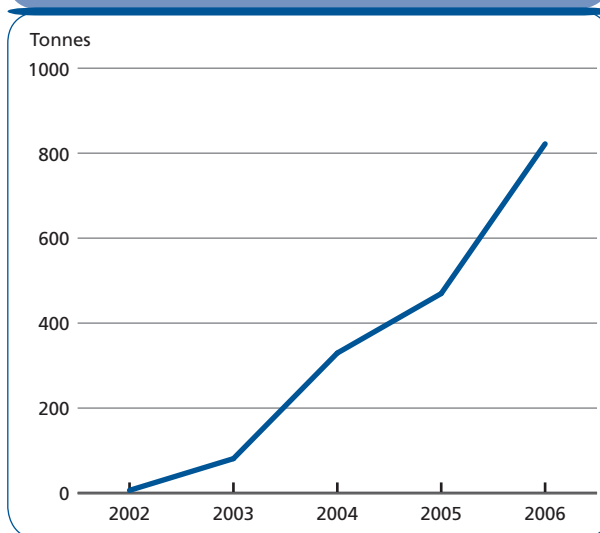
Sources: CEI-RD online and PromPeru 2007

quality and the irregular pattern of deliveries. ICCO estimates average price premiums at between US\$100 and US\$300 per metric tonne at production level, but the Colombian producing and exporting company Daabon indicates export price premiums of up to US\$1 600 per metric tonne for organic cocoa in 2006.

According to data from the Peruvian and Dominican statistical agencies, price premiums at export level varied considerably between the two countries in 2006 (Table 24). The FOB prices of Peru's organic cocoa exhibit wide variations depending on the destination. In 2006 it ranged between 1 958 (for Switzerland where 70 percent of the exports were directed) and 6 752 US dollars per metric tonne for the United Kingdom<sup>141</sup>.

The considerable range in organic premiums reflects the price variations mentioned above and is also due to the difficulties of estimating premiums along the supply chain, and variations in quality and supply chain relationships.

Figure 27. US imports of fair-trade certified cocoa



Source: TransFair USA 2007

## 2.2 Fair-trade cocoa

### Market situation

World imports of FLO-certified cocoa almost doubled in one year, reaching close to 11 000 metric tonnes in 2006. Imports into the United States rose to 820 tonnes. They have risen steadily since FLO-certified cocoa was introduced into the US market in 2002 (Figure 27). The growth rate reached 75 percent in 2006. Between 40 and 50 percent of the imported quantities were re-exported to Canada. According to TransFair USA, some 80 percent of the fair trade certified cocoa imported into North America between 2002 and 2006 was also certified organic (Table 25).

The number of TransFair cocoa licensees in the United States rose by 32 percent between 2005 and 2006, with a total of 45 licensees at the end of 2006.

<sup>141</sup> PromPeru, August 2007

**Table 25. Percentage of organics in imported fair-trade cocoa**

	2002	2003	2004	2005	2006
Imports (MT)	6.4	81	329.6	469.6	821.9
% also organic	51	97	85	72	80

Sources: TransFair USA 2007

### Suppliers

Overall, fair trade cocoa is produced in Peru (six producer groups), Côte d'Ivoire (two producer groups), the Dominican Republic (two producer groups), Belize, Bolivia, Cameroon, Costa Rica, Ecuador, Ghana, Haiti, Nicaragua and Panama (one producer group each). In 2006, eight farmer cooperatives in seven developing countries exported FLO-certified cocoa to North America. TransFair USA estimates that the 820 metric tonnes they exported earned farmers an additional income of almost US\$200 000 (Table 26).

**Table 26. Estimated additional income to farmers of fair-trade cocoa exports to the United States**

Year	Additional farmer income (US\$)	Number of cooperatives	Number of countries
2002	956	n.a.	n.a.
2003	12 171	n.a.	n.a.
2004	38 291	6	5
2005	130 323	10	8
2006	199 164	8	7

Sources: TransFair USA 2007

### Prices

As for coffee, the FLO pricing system consists of a guaranteed Fairtrade Minimum Price and a premium. FLO has set the Fairtrade Minimum Price (FOB) for certified standard-quality cocoa beans at US\$1 600 per metric tonne. In addition to the Fairtrade Minimum Price, buyers also pay a fair-trade premium set by FLO (US\$150 per metric tonne FOB). If the world market price for the specific origin or type of cocoa beans is higher than the Fairtrade Minimum Price, then the fair-trade price is the sum of the world market price

and the fair-trade premium. If the cocoa is also certified and labelled organic then there is an additional premium (on top of the Fairtrade Premium) of US\$200/MT. The Fairtrade Minimum Price for organic cocoa (including premiums) is US\$1 950/MT<sup>142</sup>.

There are also FLO prices for semi processed cocoa products such as cocoa liquor, butter and powder. These prices are calculated on the basis of the Fairtrade Minimum Price of the cocoa bean.

## 2.3 Rainforest Alliance certified cocoa

RA also certifies cocoa and, according to its own estimate<sup>143</sup>, approximately 4 000 metric tonnes were exported to North America in 2005. The quantities marketed under the RA label are unknown. RA-certified cocoa is grown in the Dominican Republic, Ecuador and other tropical countries as listed in Table 27. RA is optimistic about future expansion of RA-certified cocoa production and expects the market to grow considerably in the next

**Table 27. Areas of RA-certified cocoa in supplying countries (2006)**

Country	Certified cocoa area (ha)
Dominican Republic	3 998
Ecuador	3 845
Côte d'Ivoire	2 167
Brazil	268
Guatemala	90
Costa Rica	3

Source: Rainforest Alliance

<sup>142</sup> FLO (2007)<sup>143</sup> Based on a conservative average yield of 300 to 400 kg per hectare

few years. Some RA-certified cocoa is also certified organic and most of it is shade grown. According to RA, price premiums for single-certified RA cocoa are between 20 and 25 percent.

## 2.4 Bird Friendly

Although there is not yet certification for shade grown or bird friendly cocoa, RA-certified cocoa is generally shade grown and recent research shows that coffee shade growing methods have similar positive results when used in cocoa production. It is possible that the Smithsonian Migratory Bird Center will develop a bird friendly label for cocoa.

# 3. MARKET PROSPECTS FOR CERTIFIED COCOA

Cocoa and chocolate are not considered to be “traditional” organic or fair trade products, but certified cocoa consumption has shown considerable growth in recent years and is expected to become increasingly popular over the next decade, fuelled by the growth of the overall North American cocoa market<sup>144</sup>. According to ICCO, this market will grow by some 30 percent over the next decade. The report released by Packaged Facts<sup>145</sup> forecasts that total sales of chocolate through all channels in the United States will reach US\$18 billion by 2011.

One of the principal reasons for the rapid growth in demand is a dramatic change in chocolate consumption; more and more consumers are choosing high quality, differentiated cocoa products and cocoa is increasingly seen as an “ethical” product. Consumers are willing to pay more for chocolate because they see it more as a luxury and a delicacy. They are also starting to look for chocolate products with a higher percentage of cocoa mass, perhaps in part because of studies demonstrating the health benefits of dark chocolate. Recent research on the role of antioxidants in reducing cancer risks has raised attention on their presence in foods. The ORAC (Oxygen Radical Absorbency Capacity) index ranks foods according to their concentration of antioxidants. Dark chocolate has one of the highest ORAC indexes (Figure 28).

The recent acceptance of organic and fair trade standards for cocoa in the United States and the entry of US-based organic processors should reduce prices, increase supply and stimulate considerable market growth. Previously, all certified cocoa was shipped to Europe for processing and packaging, and then re-exported to North America. There is strong demand in North America for high quality product and the cocoa market is characterized by undersupply. A 2005 CIMS/Ecomercados study shows that the North American market for organic and fair trade cocoa presents a significant opportunity for developing country producers.

There is evidence that organic cocoa production is increasing rapidly. Although less than 1 percent of the North American cocoa market is organic, there has been a sharp rise in demand in the last few years and suppliers are scrambling to meet demand. According to the Nature Conservancy, organic chocolate sales have grown by approximately 70 percent per year since 2002 and the market value should reach about US\$35 million in the near future. In this survey, several producer groups and industry sources forecast that the market is likely to grow by at least 20 percent per year during the next decade. Colombia-based Daabon, one of the largest Latin American organic cocoa producers, plans on tripling its

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<sup>144</sup> CIMS/EM (2005)

<sup>145</sup> Packaged Facts (2007)



production before 2010 and establishing a processing facility. Much of Daabon's cocoa is double-certified organic and RA, and the company expects to have over 3 000 hectares planted by the end of 2007.

In addition, rising interest in good-quality Central American cocoa and the prospects for organic cocoa exports should lead to the expansion of organic cocoa production in Central America if the challenges associated with the cocoa pod disease, *Cocoa moniliasis*, can be overcome.

Some industry sources point out that organic cocoa faces considerable supply side challenges. The main ones relate to quality, the cost of certification and producer access to and knowledge of organic supply channels. On the other hand, these challenges, combined with consumer trends and cocoa's relatively late entry into organic production, mean that there may be more opportunity for growth in the cocoa market than there is for any other organic products. Growing interest from major manufacturers and retailers will likely foster demand for certified cocoa considerably in the next few years. Cooperation and partnerships between producers and North American importers, manufacturers and retail groups, is critical if the North American organic cocoa market is to reach a substantial size.

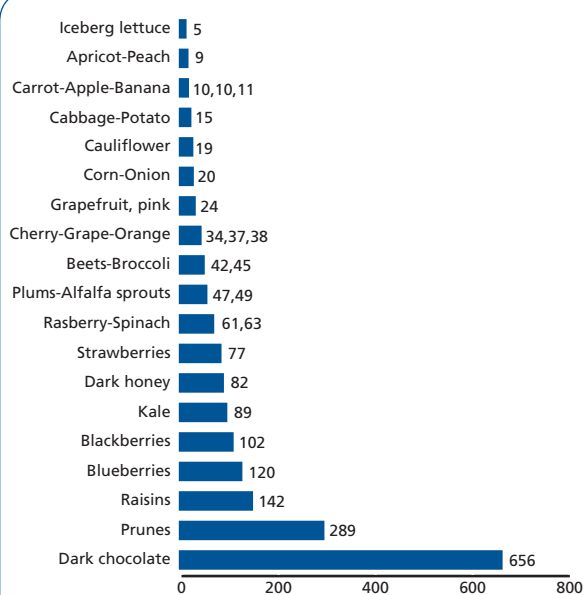
As for fair-trade certified cocoa, this market has grown very strongly since 2002 and industry experts predict that the expansion will continue over the next few years at least, with most fair trade cocoa also being certified organic. As with coffee and other certified products, there has been a sharp increase in double-certified cocoa, particularly organic and fair-trade. The rising number of cocoa processors and distributors licensed by TransFair USA is a sign that the market is taking off.

Developing countries seeking to add value to their certified cocoa may benefit from the increasing demand for processed products such as cocoa butter or chocolate. The type of cocoa products imported into North America has changed markedly over the past 10 year. While imported quantities have risen for all product types, the rise has been stronger

for chocolate than for cocoa beans (Figure 29). In value terms, in 1995-1996, cocoa beans accounted for one-third of imports while the share of chocolate was slightly below 40 percent. In 2005-2006, the latter was almost 50 percent while the former had fallen to one-quarter (Table 28). This change in the product mix has important implications for developing country producers and exporters.

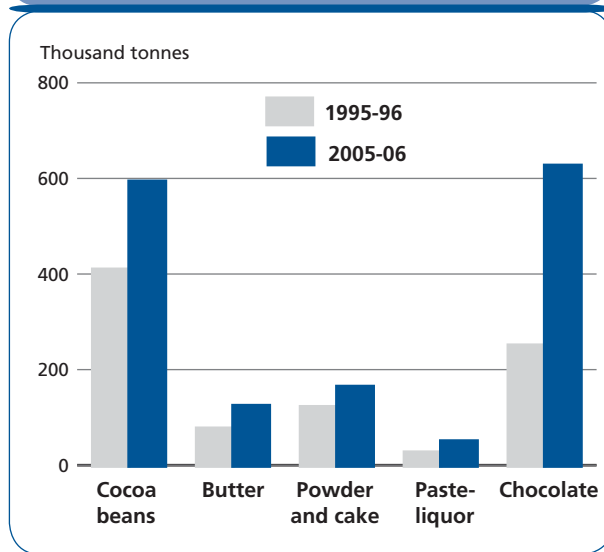
However, tariff escalation may be a challenge for developing countries aiming to add value to their certified cocoa by exporting processed products such as cocoa butter or chocolate to the United States. While this country allows duty-free imports of cocoa beans, it applies much higher tariffs on processed cocoa products. It should be noted,

**Figure 28. Ranking of selected foods according to their ORAC index**



Source: Fabrice Vaillant, CIRAD

**Figure 29. Change in the types of cocoa products imported into North America**



though, that countries that have the Most Favoured Nation (MFN) status benefit from much lower tariffs (Table 29). As for Canada, it grants duty-free entry to cocoa beans and applies low tariffs on processed cocoa products except chocolate ice cream mix and ice milk mix.

**Table 28 . Share of products in the total value of cocoa product imports**

	Average 1995-1995 (%)	Average 2005-2006 (%)
Cocoa beans	33.6	25.7
Butter	16.5	14.2
Powder and cake	7.4	6.8
Paste/liquor	3.3	3.5
Chocolate	39.2	49.8

**Table 29 . Import tariffs on cocoa beans and products in the United States**

Code	Product description	GEN tariff	MFN tariff
1801	Cocoa beans, whole or broken, raw or roasted	0%	0%
1803	Cocoa paste, whether or not defatted:		
1803.1	- Not defatted	6.6 cent/kg	0%
1803.2	- Defatted	6.6 cent/kg	0.2 cent/kg
1804	Cocoa butter, fat and oil	25% of FOB value	0%
1805	Cocoa powder, not containing added sugar or other sweetening matter	6.6 cent/kg	0.52 cent/kg
1806.1	Cocoa powder, containing added sugar or other sweetening matter:	from 20% to 40% of FOB value or from 25 to 39.5 US cents/kg depending on the product	from 0 to 10% of FOB value or from 21.7 to 33.6 US cents/kg depending on the product

# CONCLUSIONS

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The use of private standards and certification has been increasing rapidly in the North American food sector, resulting in further market segmentation and creating new opportunities for product differentiation. Admittedly, not all of these standards directly add value to products. In many instances, producers mainly adopt a business-to-business certification scheme more because it is demanded by their corporate customers than because they see a clear opportunity for value adding. In such cases the choice of certification is primarily a defensive strategy to avoid losing clients.

In contrast, some environmental and ethical certification schemes that target consumers with a recognizable on-product label tend to result in higher product prices and may provide farmers with new market opportunities. The markets for organic and fair-trade foods are of particular interest to small-scale farmers in developing countries, as they usually offer higher prices. Demand for organic foods in North America is forecast to continue expanding rapidly, mainly fuelled by consumer concerns about health and the environment. Other growth factors include the higher involvement of conventional and specialized supermarket chains in the marketing of organic foods and the development of organic product lines by conventional food manufacturers. In addition, North American food processors, distributors and retailers increasingly include corporate social responsibility into their management principles and public-relation strategies. Selling certified foods is a visible and credible means of showing their commitment to social responsibility.

Domestic production will not be able to cover all the expected growth in demand, thus leaving substantial room for imports. Developing countries are well positioned to supply a wide range of organic products such as fresh produce, cocoa, coffee, tea, herb teas, sugar, aromatic herbs and spices. Organic agriculture tends to be labour intensive, which may give developing country smallholders a comparative advantage. The increased per capita consumption of fresh fruit and vegetables, combined with renewed consumer interest in the health value of these products means that there is market demand for imported certified fresh produce in North America. In this category, the best export opportunities for developing countries are in tropical fruits, exotic vegetables and off-season temperate fruit and vegetables. Chapter 2 of this study has focused on the market potential of tropical fruits. Within this category, the outlook is good for organic pineapples and mangoes, which should benefit from the rapid expansion of the overall pineapple and mango markets. The expected growth should provide outlets for both established suppliers and new entrants. Imports of other tropical fruits such as papayas, litchis, rambutans, guava and passion fruits are also expected to rise, partly due to the growing ethnic markets and the demand of the foodstuff industry, but quantities should remain much lower than those of pineapples and mangoes.

Growth prospects are also good for organic bananas, but the large areas of banana land currently in transition to organic cultivation means that there will not be much room for new suppliers. Existing producers, in particular in Ecuador, Peru and Colombia, are expected to meet the future additional demand. In both the banana and pineapple sectors, the control exerted over the North American market by the large US fruit companies may be a constraint to market entry. On the other hand, forging trade partnerships with them may also be a valid strategy for some developing country exporters. Alternatively, exporters may approach specialized organic importers.

While North American imports of cocoa and its processed products have been rising steadily, the market share of organic cocoa is still extremely low. There is therefore considerable growth potential. World supply of organic cocoa is still low compared to the demand of the manufacturing industry, which leaves room for new suppliers. The fact that North American importers increasingly source their cocoa directly from producing countries provides producer organizations with new opportunities.

Although total coffee imports are growing very slowly in North America, consumption of specialty coffee has soared in the last decade. This trend is expected to continue and will benefit certified coffees, in particular organic coffee. The market for certified coffee is growing at approximately 20 times the rate of the conventional coffee market. For growers who can produce high quality coffee, certification is a strategy for adding value, accessing niche markets and securing buyers. The best prospects are seen in organic coffee that also bears fair-trade certification.

The North American market for certified fair-trade foods is also expected to expand substantially, although its size will remain well below that of the organic market. Fair-trade benefits specifically developing country farmers, in particular smallholders, and offers guaranteed minimum prices and premiums. Beside these direct advantages, certified producers may benefit from long-term trade relationships, pre-financing and support from the FLO network. However, the market penetration of fair-trade foods is still extremely low in North America for all products but coffee. There is a significant market potential for products such as cocoa, tea, herb teas, sugar and honey. The market for fair-trade cocoa is forecast to expand markedly. An increasing number of cocoa producers in Latin America is obtaining fair trade certification. Fair-trade cocoa which is also certified organic stands to benefit from strong market growth. Even for fair-trade coffee, whose imports are already sizeable, further growth potential exists, especially if it is also certified organic. The number of stores selling fair-trade coffee has soared in recent years, providing a basis for further expansion.

In contrast, the market for fair-trade fruits has not yet taken off in North America. The market control exerted by the large US fruit companies is seen as an obstacle to the development of fair-trade bananas and pineapples. The mango market being more fragmented, it may be easier for developing countries to export fair-trade mangoes than fair-trade bananas and pineapples. In any case, fair-trade organizations will need to undertake significant awareness raising and promotion campaigns if the fruit market is to reach a meaningful size. Forging partnerships with supermarket chains is necessary. In this respect, the example of the United Kingdom is telling. The decision of two leading retail chains that all bananas on their shelves should be fair-trade certified raised the share of this product from less than 5 percent to some 20 percent of the British market. Fair-trade avocados could become an interesting market, especially for Mexican farmer groups. In the medium term, fair-trade exotic fruits such as litchis and papayas may offer exports opportunities, in particular for Latin American and Caribbean countries, but only a limited number of suppliers will benefit, as these are likely to remain niche markets.

Beside organic agriculture and fair-trade, other types of certification labels targeting consumers in the North American market may provide developing countries with export opportunities, but they focus on a limited number of products. The Rainforest Alliance has a strong presence in the banana market and, to a lesser extent, in the coffee sector. In order to expand the volume it certifies, it has forged alliances with large US market players (e.g. Chiquita for bananas, Kraft for coffee). Imports of RA-certified coffee are growing rapidly. In the North American banana market, if Dole, which has recently obtained certification for one plantation in Costa Rica, decided to seek RA certification for all its Latin American

farms, the market share of RA-certified bananas would exceed 50 percent. However, the level of recognition of the RA label by consumers and the price premium for RA-certified bananas are unknown. Presently, virtually all the RA-certified banana farms are plantations. Whether this standard would meet the needs of small-scale growers and earn them a premium remains to be determined. RA is trying to expand in the cocoa and citrus markets, but the quantities marketed under the label have been very low so far.

The United States is an obvious destination for exporters due to the enormous size of its market and its role of entry point to the Canadian market. However, developing country exporters should not neglect Canada. Many Canadian traders and distributors also import at least part of their requirements directly from foreign suppliers other than the United States, and there is a growing interest in the organic industry to source more internationally and directly from the producing country. The increasing involvement of conventional supermarket chains is accelerating the growth of organic food sales. In the fair-trade sector, Canada may provide excellent market outlets in spite of its smaller population due to the high awareness of its consumers on social issues.

This study has focused on a few certification schemes that are thought to be the most advantageous and suitable to small-scale farmers in developing countries. Beyond these, farmers and exporters in these countries may find benefits in other schemes such as those aiming at good agricultural practices, good manufacturing practices and food safety (e.g. SQF, GlobalGAP, and ISO-22000), worker rights and welfare (SA-8000) and product quality. These schemes may be of particular interest to large-scale commercial farms, plantations and large food-processing firms. Because North American consumers have an increasing number of requirements on the foods they buy, multiple certification gives a market advantage. For small-scale producers the combination of organic and fair-trade, possibly with a food safety certification, may improve market access considerably. In any case, the choice of a standard should be based on a comprehensive *ex ante* cost-benefit analysis.

The North American market for certified products is characterized by volatility in demand and strong price fluctuations. Consequently, even though the bulk of demand for certified products is in developed countries, farmer organizations and trade associations in developing countries should strive to diversify markets. This includes developing their domestic market, which provides an alternative when prices fall in the export markets. It also offers an outlet for products that do not qualify for export. Further, sales of certified products need not be less profitable in the domestic market. Admittedly, prices are lower but so are marketing costs. Finally, domestic sales of organic and fair-trade goods are growing in developing countries and these markets are set to become an important part of the global market in the next decades, providing further sales points for producers.

#### Areas for further research

There is much evidence that voluntary standards and certification can improve incomes, working conditions, organisational capacity, social capital and environmental quality in developing countries. Yet, few studies have undertaken to quantify the overall benefits to these countries. The lack of data is a key constraint. While the industry can provide estimates for quantities, it is often reluctant to disclose price data, which are confidential by nature. This makes it difficult to estimate the price premiums for certified foods. Although several researchers have examined organic food prices in the United States, the studies tend to be too narrow in coverage. More systematic studies are needed, especially on the prices of foods certified to the organic and Rainforest Alliance standards. This is a complex field, as prices exhibit wide variations over time and space. Similarly, the distribution of the profits generated by certified food sales from retailers, through distributors, importers, exporters to producers has not been analysed in a systematic manner. Even in the fair-trade

sector, there is a scarcity of information, with most studies focussing on a specific farmer group. Case studies demonstrate that the benefits and costs of standards vary considerably depending on the type of farm, product and location. Further research is needed in this area.

Better knowledge of the costs and benefits and their distribution along the supply chain will help to clarify the debate and determine the extent to which standards and certification can be used as a tool for sustainable economic development. It is also important to consider the non-pecuniary effects of certification, such as organisational development or added social and human capital. This information is essential to farmers who are considering how to add value to their products, and to governments, aid agencies, NGOs or trade associations considering strategies for agricultural development and poverty alleviation.

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*In addition: numerous trade journals, papers, newsletters, web sites, etc. including those mentioned in the text.*

# LIST OF RESPONDENTS

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## CONSULTANTS AND RESEARCH ORGANIZATIONS

### **AgriSystems International**

Tom Harding, Director  
Tel.: +1 610 863-6700  
Fax: +1 610 863-4622  
Email: agrisys1@aol.com  
Website: [www.agrisystems.co.uk](http://www.agrisystems.co.uk)

### **Belrose, Inc.**

Desmond O'Rourke, President  
Tel: 509-332-1754  
Fax: 509-334-5209  
Email: belrose@pullman.com  
Website: [www.e-belrose.com](http://www.e-belrose.com)

### **CIMS (Centro de Inteligencia sobre Mercados Sostenibles)**

Andres Villalobos, Coffee Coordinator  
Costa Rica  
Tel.: +506 437.2294  
Fax: +506 433.9912  
Website: [www.cims-la.com](http://www.cims-la.com)

### **ECOLOGIA USA**

Randy Kritkauskay, President  
USA  
Tel./Fax: 1-802-623-8075  
Email: [ecologia@ecologia.org](mailto:ecologia@ecologia.org) or [rkritkauskay@ecologia.org](mailto:rkritkauskay@ecologia.org)  
Website: [www.ecologia.org](http://www.ecologia.org)

### **Daniele Giovannucci**

1006 South 9<sup>th</sup> Street  
Philadelphia, PA 19147  
USA  
Tel.: (215) 922-7518  
Fax: (215) 922-5723  
Email: [d@giovannucci.net](mailto:d@giovannucci.net)

### **Michele J.L. Martin**

Root Capital / EcoLogic Finance  
USA  
Email: [mmartin@rootcapital.org](mailto:mmartin@rootcapital.org)  
Website: [www.rootcapital.org](http://www.rootcapital.org) or [www.ecologicfinance.org](http://www.ecologicfinance.org)

### **Rudy Kortbech-Olesen**

Marketing Advisor/Consultant  
Email: [RKOrganics@voila.fr](mailto:RKOrganics@voila.fr)

## STANDARD SETTING AND CERTIFICATION ORGANIZATIONS

### **Associazione Italiana per l'Agricoltura Biologica (AIAB)**

Cristina Grandi, IFOAM Liaison Officer

Via Piave, 14

00187 Rome

Italy

Tel.: +39 06 86329403

Fax: +39 86385945

Email: [c.grandi@ifoam.org](mailto:c.grandi@ifoam.org)

Website: [www.aiab.it](http://www.aiab.it)

### **Bird Friendly Coffee Program, Smithsonian Migratory Bird Centre**

Robert Rice, Director

SMBC--National Zoo

Washington, DC

USA

Tel.: +1 202 633 4209

Email: [ricer@si.edu](mailto:ricer@si.edu)

Website: <http://nationalzoo.si.edu/ConservationAndScience/MigratoryBirds/Coffee/>

### **FLO International**

Verónica Pérez, Communications Officer

Bonner Talweg 177

53129 Bonn

Germany

Tel.: +49-228-949230

Fax: +49-228-2421713

Email: [v.perez@fairtrade.net](mailto:v.perez@fairtrade.net)

Website: [www.fairtrade.net](http://www.fairtrade.net)

### **Rainforest Alliance**

Marcel Clement

Chris Wille, Chief of Sustainable Agriculture

655 Broadway, Suite 500

New York, NY 10012

USA

Tel.: (212) 677-1900

Fax: (212) 677-2187

Email: [mclement@ra.org](mailto:mclement@ra.org) or [cwille@racsa.co.cr](mailto:cwille@racsa.co.cr)

Website: [www.rainforest-alliance.org](http://www.rainforest-alliance.org) or [www.eco-index.org](http://www.eco-index.org)

### **TransFair Canada**

Carolyn Whitby, Director

328 Somerset West

Ottawa ON K2P 0J9

Canada

Tel.: 613-563-3351

Fax: 613-563-1462

Toll-Free: 1-888-663-FAIR

Email: [Carolyn.whitby@transfair.ca](mailto:Carolyn.whitby@transfair.ca)

Website: [www.transfair.ca](http://www.transfair.ca)

**TransFair USA**

Hillary Miller-Wise, Director of Global Producer Services  
Oakland, CA USA  
Tel/Fax: +1 301 270 0866  
Email: hmillerwise@transfairusa.org  
Website: [www.transfairusa.org](http://www.transfairusa.org)

## CERTIFIERS AND INSPECTORS

**Independent Organic Inspectors Association**

Jim Riddle  
Route 3, Box 162C  
Winona, MN 55987  
USA  
Tel./fax: 507-454-8310  
Email: jriddle@luminet.net  
Website: [www.ioia.net](http://www.ioia.net)

**Quality Assurance International (QAI)**

Joe Smillie, Senior Vice President  
Kasey Moctezuma, International Account Coordinator  
12536 High Bluff Dr., Suite 300  
San Diego, CA 92130  
USA  
Tel.: +1-619-792-3531  
Fax: +1-619-792-8665  
Email: jsmillie@qai-inc.com or kasey@qai-inc.com  
Website: [www.qai-inc](http://www.qai-inc)

## INTERGOVERNMENTAL ORGANIZATIONS

**Instituto Interamericano de Cooperación para la Agricultura (IICA)**

Pedro Cussianovich, Especialista en Agricultura Orgánica  
Apdo Postal 4830  
Managua  
Nicaragua  
Tel.: +505 276-2754 Ext. 4107  
Fax: +505 278-2405  
Email: pcussian@iica.int.ni  
Website: [www.iica.int](http://www.iica.int)

**International Coffee Organization (ICO)**

Lilian Volcan, Projects and Sustainability  
Denis Seudieu  
22 Berners Street  
London, W1T 3DD  
UK  
Tel.: +44 (0)20 7612 0625  
Fax: +44 (0)20 7612 0630  
Email: Volcan@ico.org  
Website: [www.ico.org](http://www.ico.org)

**International Trade Centre (ITC)**

Alexander Kasterine, Senior Market Development Adviser  
Morten Scholer, Senior Market Development Adviser  
54-56 rue de Montbrillant  
CH-1202 Geneva  
Switzerland  
Tel.: +41 22 730 0378 / 0111  
Fax: +41 22 730 0446  
Email: [kasterine@intracen.org](mailto:kasterine@intracen.org) or [scholer@intracen.org](mailto:scholer@intracen.org)  
Website: [www.intracen.org](http://www.intracen.org)

**International Sugar Organization (ISO)**

Lindsay Jolly, Senior Economist  
1 Canada Square  
Canary Wharf  
London E14 5AA  
UK  
Tel: 00 44 (0)20 7513 1144  
Fax: 00 44 (0) 20 7513 1146  
Email: [lindsay@isosugar.org](mailto:lindsay@isosugar.org)  
Website: [www.isosugar.org](http://www.isosugar.org)

## GOVERNMENTAL ORGANIZATIONS

**State of Colorado Department of Agriculture**

Tim Larsen, Senior International Marketing Specialist  
700 Kipling St., Suite, 4000  
Lakewood, CO 80215  
USA  
Tel.: +1 303 239 4114/8  
Fax: +1 303 239 4125  
Email: [tim.larsen@ag.state.co.us](mailto:tim.larsen@ag.state.co.us)  
Website: <http://www.ag.state.co.us/>

**ProChile Export Promotion Bureau**

Ministry of Foreign Affairs  
Av. Bernardo O'Higgins 1315, 2<sup>nd</sup> floor  
RCH – Santiago  
Chile  
Tel.: +56 - 2-565900  
Fax: +56-2-6960639  
Email: [mhernan@prochile.cl](mailto:mhernan@prochile.cl)  
Website: [www.prochile.cl](http://www.prochile.cl)



**USDA Economic Research Service**

Catherine Greene  
1800 M Street NW  
Washington, DC  
20036-5831  
USA  
Tel.: +1 202-694-5541  
Fax: +1 202-694-5757  
Email: [cgreene@ers.usda.gov](mailto:cgreene@ers.usda.gov)  
Website: [www.ers.usda.gov/briefing/organic](http://www.ers.usda.gov/briefing/organic)

## INDUSTRY ORGANIZATIONS

**International Banana Association (IBA)**

Washington, DC  
Tel.: (540) 314-3214  
Fax: (202) 303-3433  
Website: [www.eatmorebananas.com](http://www.eatmorebananas.com)

**Organic Trade Association (OTA)**

Dan Pratt, Directory Coordinator  
Marissa Potter, Operations Manager  
PO Box 547  
Greenfield MA 01302  
USA  
Tel.: +1-413-774-7511  
Fax: +1-413-774-6432  
Email: [dpratt@ota.com](mailto:dpratt@ota.com) or [mpotter@ota.com](mailto:mpotter@ota.com)  
Website: [www.ota.com](http://www.ota.com)

**Organic Trade Association, Canadian Office**

Stephanie Wells, OTA's Canadian Liaison  
323 Chapel Street  
Ottawa, ON K1N 7Z2  
Canada  
Tel.: (613) 787-2003  
Fax: (613) 236-0743  
Email: [otacanada@ota.com](mailto:otacanada@ota.com)  
Website: [www.ota.com/pp/canada.html](http://www.ota.com/pp/canada.html)

## EXPORTERS, IMPORTERS AND DISTRIBUTORS

**Albert's Organics**

Melody Meyer, National Procurement Director  
2450 17th Avenue Suite 250  
Santa Cruz CA 95062  
USA  
Tel.: +1 800 625-5661 ext 62225  
Email: [mmeyer@albertsorganics.com](mailto:mmeyer@albertsorganics.com)  
Website: [www.albertsorganics.com](http://www.albertsorganics.com)

**Asociación de Exportadores de Banano del Ecuador-AEBE**

Raúl Villacres V., Sub-Director Ejecutivo  
Av. Francisco de Orellana y M.H. Alcivar  
Centro Empresarial "Las Cámaras" 3er piso Ofic 301  
Guayaquil  
Ecuador  
Tel.: +593-4 2681569  
Fax: +593-4 2683019  
Email: rvillacres@aebe.com.ec  
Website: [www.aebe.com.ec](http://www.aebe.com.ec)

**Beta Pure Foods**

Nate Morr, Vice President  
335 Spreckels Dr Ste D  
Aptos, CA 95003-3952  
USA  
Tel.: (831) 685-6565, ext. 326  
Fax: (831) 685-6569  
Email: nate@betapure.com  
Web site: [www.betapure.com](http://www.betapure.com)

**CF Fresh**

Luis Acuna, Director International Operations  
P.O. Box 665  
Sedro-Woolley, WA 98284-0665  
USA  
Tel.: (360) 855-3190  
Fax: (360) 855-2430  
Email: luis@rootabaga.com or luis@cffresh.com  
web site: [www.rootabaga.com](http://www.rootabaga.com)

**Chiquita Brands, L.L.C**

Michael Mitchell, Director, Corporate Communications  
250 E 5th St  
Cincinnati, OH 45202-4119  
USA  
Tel.: +1 513-784-8959  
Fax: +1 513 564-2705  
Email: mmitchell@chiquita.com  
Web site: [www.chiquita.com](http://www.chiquita.com)

**Chiquita Brands International, Inc.**

David McLaughlin, Senior Director, Environmental and Regulatory Affairs  
Edificio Numar, Calle 1Avenida 5a  
PO Box 10076-1000  
San Jose  
Costa Rica  
Tel.: +506 204 2135  
Fax: +506 233 22 96  
Email: dmclaughlin@chiquita.com  
Website: [www.enviro-chiquita.com](http://www.enviro-chiquita.com)

**Chiquita Fresh Europe**

George Jaksch , Director, Corporate Responsibility and Public Affairs  
Rijnkaai 37  
2000 Antwerp  
Belgium  
Tel.: +32.3.203.9135  
Fax: +32.3.203.0350  
Email: [gjaksch@chiquita.com](mailto:gjaksch@chiquita.com)  
Website: [http://www.chiquita.com/chiquitaCR01/BIinformation/bi\\_p41.asp](http://www.chiquita.com/chiquitaCR01/BIinformation/bi_p41.asp)

**Citrus Industries**

Jim Reed, President  
PO Box 835  
Three Rivers, CA 93271  
USA  
Tel.: +1 559-561-3391  
Fax: +1 559-561-4073  
Email: [jim@citrusindustries.com](mailto:jim@citrusindustries.com)  
Website: [www.citrusindustries.com](http://www.citrusindustries.com)

**Daabon Organic USA Inc.**

Caroline Warren-Newman, Sales Director  
131 B E Alderson St  
Bozeman, MT 59715-5290  
USA  
Tel.: +1 (406) 556-0330  
Fax: +1 (720) 528-7709  
Email: [cnewman@daabonusa.com](mailto:cnewman@daabonusa.com)  
Website: [www.daabonusa.com](http://www.daabonusa.com)

**Daabon Organic Japan Co. Ltd**

Juan Pablo Campos, President  
6F, 8-7-11 Nishi-Gotanda, Shinagawa-Ku  
Tokyo 141-0031  
Japan  
Tel.: +81 3 5719 2733  
Fax: +81 3 3495 0344  
Email: [campos@daabonorganic.com](mailto:campos@daabonorganic.com)  
Website: [www.daabonorganic.com](http://www.daabonorganic.com)

**Dole Fresh Fruit International, Ltd**

Frans Wielemaker, Director Organic Program  
PO Box 12  
Centro Colon 1007  
San Jose  
Costa Rica  
Tel.: +506 287-2170  
Fax: +506 287-2172  
Email: [FWielemaker@la.dole.com](mailto:FWielemaker@la.dole.com)  
Web site: [www.dole.com](http://www.dole.com)

**Fincapol**

Ricardo Martin, Director/CEO/General Manager  
Av Comodoro M  
Rivadavia 1681 6-A  
Buenos Aires C1429DBR  
Argentina  
Tel.: +54-11-47035693  
Fax: +54-11-47035693  
Email: r.martin@fincapol.com  
Website: [www.fincapol.com](http://www.fincapol.com)

**ForesTrade**

Sylvia Blanchet, Vice President  
41 Spring Tree Rd. Brattleboro, VT 05301  
USA  
Tel.: +1 802-257-9157  
Fax: +1 802-257-7619  
Email: sylvia@forestrade.com  
Website: [www.forestrade.com](http://www.forestrade.com)

**Global Organics, Ltd**

Dave Alexander, President  
PO Box 272  
Arlington, MA 02476-0003  
Tel.: +1 781 648-8844  
Fax: +1 781 648-0774  
Email: info@global-organics.com  
Web site: [www.global-organics.com](http://www.global-organics.com)

**InterNatural Marketing, Inc**

Dina and Chris Bell, Owners  
PO Box 1401  
Lake Worth, FL 33460-1401  
USA  
Tel.: +1 561 586-0048  
Fax: +1 561 586-2863  
Email: cbell@internaturalmarketing.com or dina@internaturalmarketing.com  
Web site: [www.internationalmarketing.com](http://www.internationalmarketing.com)

**New Harvest Organics, LLC**

Philip Ostrom  
4 Ojo Corte, Box 8, Rio Rico  
Nogales, AZ 151850  
USA  
Tel.: +1 520 281-0231  
Fax: +1 520 281-0237  
Email: philip@newharvestorganics.com  
Website: [www.newharvestorganics.com](http://www.newharvestorganics.com)

**Organic Valley**

Tripp Hughes, Category Manager  
CROPP Cooperative  
One Organic Way  
LaFarge, WI 54639  
USA  
Tel.: +1 970 472-1497  
Fax: +1 608-625-3025  
Email: [tripp.hughes@organicvalley.com](mailto:tripp.hughes@organicvalley.com)  
Website: [www.organicvalley.coop](http://www.organicvalley.coop)

**Pacific Organic Produce**

Steve Akagaki, General Manager  
1311 Sutter Street, Suite 203  
San Francisco, CA 94109-5415  
USA  
Tel.: +1 (415) 673-5555  
Fax: +1 (415) 673-5585  
Email: [treefruit@pacorg.com](mailto:treefruit@pacorg.com)  
web site: <http://www.pacorg.com>

**ProOrganics Inc.**

Debra Boyle, President/CEO  
#4 324 Horner Avenue  
Toronto, ON M8W 1Z3  
Canada  
Tel.: +1 (416) 252-3386, ext.16  
Fax: +1 (416) 252-3142  
Email: [dboyle@proorganics.com](mailto:dboyle@proorganics.com)  
Website: <http://www.proorganics.com>

**SunOpta**

Gunta Vitins, Vice President Marketing  
4523 Still Creek Ave.  
Burnaby, BC V5C 5W1  
Canada  
Tel.: +1 604-253-6549, x103  
Fax: +1 604-253-0439  
Email: [gunta.vitins@sunopta.com](mailto:gunta.vitins@sunopta.com)  
Website: [www.sunopta.com](http://www.sunopta.com)

**United Natural Foods Inc.**

Troy Emineth, Director of Purchasing, Eastern Region  
P.O. Box 999  
260 Lake Road  
Dayville CT 06241  
USA  
Tel.: +1 603 256-3000 ext. 42182  
Email: [temineth@unfi.com](mailto:temineth@unfi.com)  
Website: [www.unfi.com](http://www.unfi.com)

# Value-adding standards in the North American food market

## Trade opportunities in certified products for developing countries

This publication analyses the use of voluntary standards and certification schemes in the food markets of the United States of America and Canada. With its large population and its high individual purchasing power, North America provides considerable opportunities for exports of value-added agricultural products. Consumers are increasingly attentive to the social and environmental aspects of food production as evidenced by the significant expansion of certified food sales in both natural food stores and mainstream supermarket chains. North America ranks just behind Europe, the world's leading region in terms of certified food sales. The United States of America is the world's largest organic food market and accounts for over 40 percent of global sales.

The report assesses the market opportunities for developing countries aiming to export value-added certified foods to North America. After discussing the potential of various types of voluntary standards for adding value to agricultural products, it focuses on a few environmental and social certification schemes that use a registered on-product label targeting consumers. Special emphasis is put on organic and fair trade certified agricultural products due to their value-adding potential, their level of recognition by consumers and the strong and sustained growth of demand. The main product categories examined are tropical fruits, coffee and cocoa owing to their economic significance to many developing countries and their high market potential in North America.

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