2.2 Boosting Investment in the Coffee Value Chain

Section 1: Market signals and their impact on the coffee supply trends in 2011

Global coffee production in 2011 is estimated to have been 135m 60kg bags. The year 2011 was characterised by a steady rise in prices of both Robusta and Arabica coffees, above those realized in 2010 in Uganda. The average Kampala FoT prices for Robusta FAQ and Arabica ordinary parchment were UShs 4,600 and UShs 8,000 respectively, compared to UShs 3,600 and UShs 5,900 for the respective varieties in 2010. Throughout the year there was a high level of effectiveness in dissemination of market information for coffee. This helped to fairly distribute the margins between the value chain actors, with the farmers continuing to receive the highest share of these margins.

The Uganda Coffee Development Authority (UCDA) continued to monitor market trends and to post indicative daily coffee prices (for all varieties and grades) for both export and

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1 Author: Asaph Besigye, Consultant under contract to aBi Trust
2 Source: United States Dept. of Agriculture.
3 For example farmers engaging in Robusta coffee production received 70% of the Kampala FoT price with the balance shared between the other actors in the chain.
local transactions on its website. This service by the UCDA greatly boosted access to important market information.

Indeed, 2011 saw a tremendous improvement in the dissemination of market signals. This is attributed to the sustained high level of competition in the coffee sector, the continued shortening of the value chain with many farmers’ organisations directly selling to exporters, and increased market transparency by the leading coffee exporters including their regular direct dissemination of price information to producer organisations and traders, as was the case with Ibero Coffee. In addition, robust access to market information via mobile phone SMS, web mails and websites of several market information providers was maintained. Furthermore, actors providing grading services were a valuable channel for market information access as they had a constant data flow, through commercial linkages, on prices for the different coffee grades. Therefore, coffee value chain actors had rich sources of timely and reliable market information that informed their supply response decisions.

Because of the big boost in access to market information and the clear positive market signals, producer and trader confidence to engage in the market increased. This was reflected in the increased volume of coffee exports of 3.17 million 60 kg bags worth US$ 456 million in 2011 up from 2.8 million bags in 2010\(^4\), an indication of supply response by producers and traders in anticipation of higher returns and margins. From the available data, it was also ascertained that there was increased volume of farmer bulk-marketed coffee. For example the volume of bulk-marketed FAQ through Kaweri Coffee Farmers Alliance Support Project in Mityana/Mubende increased by 45% from 701 mt in 2010 to 1,021 mt in 2011 and this has been attributed to the good margins realized by the farmers. These ranged between UShs 400 and UShs 800 per kg.

**Section 2: Investment trends within the coffee value chain**

The favourable trend in the market during the year countered, to some extent, the continued global uncertainty and the harsh domestic economic situation occasioned by the high inflationary pressure during the second half of the year. Indeed, there were noticeable investment flows into the coffee value chain as reported by both aBi partners and collaborating entities that were supporting this value chain.

Production level investments in acreage expansion and rehabilitation of the existing shambas, including replacement of old coffee trees, stumping, pruning and gap-filling were highly visible. There was excess demand for planting materials, leading to countrywide shortages of quality seedlings from the nurseries.

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\(^4\) Source: UCDA monthly reports for 2011.
Beyond investment in quality seedlings, producers stepped up investments in other yield enhancing technologies such as manure, inorganic fertiliser, mulch materials and soil conservation. There were also increases in investments targeting quality improvement for premium prices as reflected by the steady increase in the demand for drying tarpaulins and increase in the number of farmers adopting better drying technologies such as raised platforms for washed Arabica coffee to minimize dust, moulds and other foreign matter.

At the processing level there was a noticeable increase in investments targeting higher and better value addition. This was indicated by the increase in the number of wet coffee washing stations, additional coffee grading operations, increased number of farmers and farmer groups acquiring and using hand pulpers and increased investment in quality hullers and hulling equipment refurbishment. The investment in rural-based coffee hulling facilities was also propelled by the rapid shift by the farmers from selling Kiboko coffee to selling FAQ which provided an increased demand for hulling hire services. In addition, there was a noticeable increase in domestic coffee roasting for both local consumption and export.

A further development in the domestic coffee roasting initiatives was the shift from roasting poor grade coffee to roasting good quality coffee for better cupping quality. In addition, there was a dramatic increase in the number of coffee bars, especially at shopping malls and supermarkets and at busy filling stations, with Ugandan coffee constituting the major raw material ingredient.

Besides investment in capital assets in the respective coffee value chain points triggered by the good market, investment in increased working capital, precipitated by the increase in prices during the year, was inevitable. Buyers had to dig deeper into their pockets for the same volume previously purchased. Also, the vibrant market ought to have had a direct ripple effect on investment in coffee trading infrastructure such as storage and haulage. This effect is difficult to accurately qualify for this article, especially due to the non-specific and multi-commodity usage of these assets.

**Section 3: Interventions by the aBi Trust to boost investments in the coffee value chain**

The aBi Trust adopted a holistic approach to support coffee value chain actors, aimed at improving their operational efficiency and market competitiveness - keys to stimulating investment in the sector. This was accomplished through targeted technical and financial support to implementing partners such as farmer organizations, SMEs engaging in processing and marketing, women and youth groups and input supply stakeholders’ associations, and also through collaboration with other development partners and public sector actors. Primarily, aBi interventions, as summarized in the next paragraphs, aimed
at increasing productivity, quality, access to finance and markets, and greater gender integration in the entire value chain.

i. Producer level productivity enhancement support targeted technology transfer mechanisms through demonstration of best agronomic practices such as: use of improved inputs, water conservation, stumping, pruning and pest and disease control. Related support was provided for demonstration of quality management through better harvest and postharvest handling practices such as picking ripe coffee cherries, proper drying using appropriate facilities. The value chain. Partnering with UNADA and UCDA, input dealers have been trained in key aspects that enhance efficiency at this level of the value chain. Support was also provided for input supply linkages, especially with farmer organizations.

iii. Though aBi has not yet provided substantial support for the processing and marketing level of the coffee value chain, it has an enriched menu for it in the short and medium term. Indeed, aBi highly rates the role of value addition through processing to impact the coffee value chain through backward and forward linkages. Its strategy supports BDS for

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aBi Trust considers producers as anchors of the value chain and thus puts greater emphasis on interventions at the primary production level. Also aBi emphasized producer-led initiatives at this level of the value chain for maximum ownership and the eventual sustainability of the interventions. For standardization of technology dissemination messages, aBi worked with MAAIF and UCDA to produce standard coffee productivity and quality improvement dissemination manuals.

ii. At the inputs supply level, aBi support targeted increasing availability, accessibility and affordability of quality inputs through support for development of an efficiently functioning inputs procurement and distribution network, where the actors therein understand the relevance of quality inputs in the entire business plan development, processing technology identification and sourcing and management systems development. The aBi Trust also supported a number of exporters and NOGAMU to step up efforts to meet organic and other certification requirements for the conventional coffee market.

iv. On the financial services development side, aBi supported a number of financial institutions to improve their efficiencies in providing financial services to agribusinesses, including the coffee sector. Improving agribusiness lending skills and developing appropriate financing mechanisms and products amongst partner financial institutions, and supporting the value chain actors to effectively link with financial institutions underpinned aBi’s strategy in this dimension. aBi Trust also supported
efforts aiming at increasing outreach for financial services through branch network expansion and branchless mechanisms. Some of this support targeted coffee growing areas such as Kyenjojo with Opportunity Bank. Lines of credit from aBi and the aBi agribusiness credit risk sharing scheme for financial institutions also benefited the coffee value chain actors, as was reported by the partner financial institutions.

One example of aBi’s support for financial services that is impacting the coffee value chain is the support to Opportunity Bank. In June 2011 Opportunity accessed a line of credit from aBi for on-lending to agribusiness actors, especially smallholder farmers.

Linking with the Uganda Coffee Farmers Alliance, Opportunity Bank applied part of the funds from aBi to lend to coffee farmers, through their farmer groups in Mityana and Mubende, for inputs such as herbicides, pesticides and tarpaulins. Lending was through a low risk and low cost structured trade mechanism under which disbursement of loans was directly to the input supplier and recovery was through the producer groups, from the proceeds of coffee delivered by the borrowers. Though still at pilot level, by the end of the year Opportunity had disbursed UShs 15.5 million to 27 coffee farmers belonging to one farmer group. Applications from other farmers were in the final stages of being appraised, with the expectation that a reasonable amount of credit will be disbursed during the first season of 2012. Opportunity intends to replicate this innovation in other areas and with other commodities. It also leveraged from the USAID DCA guarantee, through the USAID/LEAD Project, for its agribusiness lending including to the coffee sector, and intends to enlist on the aBi risk sharing facility as its utilization of the DCA facility is about to be exhausted.

Though aBi’s interventions have emphasised innovation, this lies more in the new combinations of techniques, rather than new stand-alone systems of supporting investment. Thus aBi support draws heavily on existing researched and documented good practices, replicating successful cases, sharing knowledge and experiences and leveraging expertise resources as long as these are able to stimulate efficiency within the value chain. The support puts greater emphasis on certainty of the market and existence of market linkages.

Section 4: Support services for the coffee value chain

Support services are of critical importance, given the nature of the coffee value chain. It is dominated by over one million smallholder producers, who face production-related problems such as coffee wilt and black twig borer diseases. Other pertinent characteristics include: a large number of small middleperson traders, a few major exporters and the high quality standards demanded by the terminal market. The effectiveness of overall support services for the coffee value chain during 2011 was mixed, with some cases being highly satisfactory and others critically inadequate.

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5 Please see Article 4.1 below in this Yearbook.
6 As detailed in Article 2.1 in this Yearbook, on the maize value chain.
The extension support for enhanced productivity and quality and for sensitization on how to combat pests and diseases, for the coffee sector, takes two dimensions. The public sector supported and supplied extension services (including NAADS and local government agricultural extension staff) has gaps in regard to outreach effectiveness, quick responsiveness and entire value chain coverage. The key constraint in this respect is the inadequate resources (human, physical and financial). For example, one extension staff in a sub-county for all crops is inevitably overwhelmed and cannot be effective. As a result most coffee exporters, in some cases collaborating with donor programs, continued to invest in own-managed private coffee-specific extension services. These have been very effective because they are based on a farmer-led approach.

Related to extension is the support for organic certification and traceability of origin in organic and fair-trade marketed coffee. This is twinned with quality inspection and certification at the exporter level. The service providers in these areas are efficient, though their costs are still high and largely out of reach for small actors. It is also foreseeable that as demand for these services increases in response to increased market opportunities, the supply will be overburdened as currently there are few service providers.
Similarly, private initiatives in market information provision and market linkages, and linkages to financial services providers (especially for farmer groups) registered a remarkable positive impact during 2011. However, though inspection at inputs supply level is vested in UCDA and MAAIF for both coffee nurseries and quality crop protection pesticides, the continued occurrence of counterfeit inputs and substandard seedlings are indicators of a service support gap. Thus, generally the private based support services continue to outperform the public sector based services, a clear indication of the benefit of the liberalized coffee sector.

During the year there was a noticeable increase in the provision of commercial finance to the coffee value chain, especially in cases where market linkages were positively functioning, thus enabling development of structured trade financing mechanisms such as those operating for the farmers and farmer groups supported by the Uganda Coffee Farmers Alliance in the Mityana/Mubende area.

As highlighted earlier in this article, aBi interventions in the coffee value chain are expected to tackle these gaps in the geographical areas where it operates and hopefully these initiatives can be replicated elsewhere by others.

In summary, aBi’s support to partners and its collaboration with other entities and stakeholders are of a nature that targets increasing production, productivity and quality, and increasing access to financial services. In addition, some of the interventions directly target addressing the constraints emanating from the support services gaps.

These include meeting the costs of certification, market information dissemination and direct linkages for financial services.

Section 5: The coffee sector policy environment and issues – Ten points for attention

As mentioned earlier, during 2011 Opportunity Bank’s involvement with the coffee value chain was stepped up; Centenary Bank also became more involved. However, lack of insurance products to mitigate production and market risk continued to constrain access to finance. Also, limited innovation in payments and remittance mechanisms for producers, producer groups and small traders remained an issue to be tackled, as buyers and sellers continued to shoulder the risk of carrying huge amounts of cash.

Given the historical and current importance the coffee sector commands in the national economy and national development strategies (a major traditional cash crop, major source of export earnings, significant role on increasing household incomes and in poverty reduction, important contributor to rural employment and carrying enormous potential for value addition) it has benefited from a good share of enabling policy and legislative attention. The sector’s policy environment continues to be anchored in UCDA and MAAIF.
However, there are identified gaps that ought to be of relevance for policy formulation and implementation, as summarized in the Ten Points below.

1) The slow pace of approval of the draft National Coffee Policy, that is expected to plug a number of gaps in the 1994 UCDA (Amendment) Statute, is of serious concern to many stakeholders in the sector. While the existing statute focuses on the upstream activities from the processing level, the draft policy is expected to address, and thus steer the efficient functioning of the entire coffee value chain.

2) The downgrading of the former Coffee Research Institute in Mukono to a Research Center is perceived as a blow to the much needed research initiatives. This is contrary to the direction in the sister East African states of Kenya and Tanzania where there has been upgrading of research institutes to research foundations, with the stakeholders (especially farmers) having a say in the research initiatives, with resulting highly visible impacts.

3) There is a need to step up research and release of research results on high yielding and disease-resistant varieties, increase disease surveillance through effective phytosanitary controls and, intensify interventions to combat the menacing coffee wilt and twig borer diseases.

4) On taxes, there should be a review of withholding tax on the sale of seedlings and other inputs, and review of taxes and licence fees for processors, which are currently considered to be very high.

5) There is also a need to provide standard guidelines and specifications for processors on milling out-turn, quality-enhancing equipment.

6) Urgent attention is needed to tighten control measures to eliminate counterfeit inputs, especially pesticides.

7) The structure of the roles and relationships between UCDA, COREC and NAADS needs to be reviewed to align them with the dynamics of the industry, and ensure that UCDA support services effectively trickle down to local government level, so as to deepen their impact.

8) Industry stakeholders strongly believe that they should be allowed to actively engage in determining the utilization of the Coffee Cess funds both to improve the relevance of this instrument and to positively underscore the need to step up the rate from the current 1% cess, once its benefit has been broadly internalized. This has been done in Kenya and Tanzania.

9) Furthermore, efforts and deliberate incentives to step up value addition and to increase domestic consumption need to be pursued.

10) The highly successful coffee value chain development model supported by the NKG Alliance Trust should be replicated in other locations, especially through public private partnerships. The aBi has been and is expected to continue supporting this replication.