

Building a Competitive Coffee Industry in Tanzania

BACKGROUND – Coffee is one of Tanzania's major exports, generating more than \$60 million a year. Tanzania has the climate and altitude to produce specialty *Arabica* coffee that attracts premium world market prices. Almost all of Tanzania's coffee is grown by 400,000 poor smallholder farmers, each owning less than five acres of land. The traditional commodity pricing system, which rarely rewarded quality, trapped them in a vicious cycle of declining quality and productivity, exacerbated by declining world prices.

Tanzania's coffee exports and income began to steadily fall in the mid-1990s due to a number of reasons. Trees were old (up to 70 years old) and yields were among the lowest in the world. Although the intrinsic quality was high, poor processing resulted in poor quality coffee that ended up being sold in the highly volatile "blended" coffee market. Until regulations were changed recently, smallholder farmers sold their coffee only to the state-run auction through cooperative unions or private buyers, but neither system rewarded quality.

ASSISTANCE – Over the past eight years, with funding from USAID, USDA, the Swiss State Secretariat for Economic Affairs and private donors, TechnoServe helped the industry stakeholders to develop and implement a plan to transform Tanzania into one of the world's premium specialty-coffee producing nations. Targeting the entire supply chain, TechnoServe created a unique "farmer business group" model that helps small-scale growers improve quality, obtain financing, establish contracts with overseas buyers, and ultimately increase profits. TechnoServe also helped establish a farmer-owned trade association and encouraged government policy reform to lower farm-gate taxation and authorize premium coffee producers to sell directly to foreign buyers.

In 2001, TechnoServe mobilized 11 farmer business groups to form the Association of Kilimanjaro Specialty Coffee Growers (KILICAFE), a farmer-owned company that specializes in providing services to member coffee business groups. TechnoServe provided technical assistance on coffee production, post-harvest handling, group formation, business planning, credit acquisition, marketing and business management. Member groups improved their coffee quality and had better access to finance and markets. KILICAFE now supports 93 groups representing more than 9,000 smallholder farmers.

With support from McKinsey & Company, TechnoServe conducted a ground-breaking analysis of Tanzania's coffee taxation policies to determine their effects on the overall industry. The study revealed that Tanzania had high taxes on coffee compared to five "peer" coffee-producing nations (Costa Rica, Ethiopia, Guatemala, Kenya and Uganda). Countries such as Costa Rica and Uganda have significantly reduced tax levels to alleviate the effect of major price drops on coffee growers and to make their industries more competitive.

TechnoServe, KILICAFE, the Tanzania Coffee Board (TCB) and key industry stakeholders presented these findings to the Tanzanian government. In June 2003, the Minister of Finance, Basil Mramba, pledged the government would harmonize and rationalize its taxes and levies to boost rural productivity, and that measures would be taken to reduce local licenses and permit fees. These reforms would significantly reduce the number of "nuisance taxes" that plagued smallholder farmers, amounting to tax levels of up to 21% on coffee.



In October 2003, the TCB enacted new regulations advocated by TechnoServe, KILICAFE and others to allow high-quality coffee growers to sell directly to specialty buyers and bypass the national auction system. TechnoServe helped the TCB and the government draft new regulations so specialty coffee growers could receive premium prices through direct negotiations with roasters. KILICAFE became the first organization to export specialty coffee directly to overseas buyers. TCB's new licensing procedure removed a significant barrier between Tanzanian specialty coffee producers and international buyers willing to pay premium prices.

POLICY IMPLICATIONS – The TechnoServe work helped to catalyze regulatory changes and tax reforms that are projected to boost Tanzanian farmers' incomes by US\$20 million over the next 10 years. The successful regulatory changes in Tanzania have also launched debates in several other coffee-growing countries, such as Kenya, that are expected to introduce direct export policies.

IMPACT/LESSONS LEARNED – With TechnoServe's assistance, KILICAFE groups improved their coffee quality from "Class 9" to "Class 5." This quality improvement, combined with a better marketing system, allowed farmers to get a 70% price premium. In the three coffee-growing regions where KILICAFE operates, it has consistently obtained higher prices for its farmers' coffee than other sellers.

In March 2004, a specialty coffee roaster with an international reputation for high-quality coffee – Peet's Coffee & Tea – purchased more than 23,000 pounds of washed *Arabica* from five KILICAFE groups representing 645 smallholder farmers. This was the first direct grower-to-roaster transaction in Tanzania under the new regulations. The farmers received premium prices 150% higher than other coffee growers. With the coffee Peets purchased from KILICAFE, they created a special

Tanzania "Kilimanjaro" limited edition coffee. KILICAFE has sold to Peet's, Starbucks and other international specialty buyers in the past three years, with direct export sales exceeding US\$500,000 annually.

TechnoServe has drawn several lessons from this work, including: (1) assistance should be targeted to specific competitiveness drivers that unlock additional industry value; (2) continuity and flexibility of donor support is critical, requiring a multi-year phased approach to promote industry growth and competitiveness, and (3) exposing industry stakeholders – from farmers to policy makers – to global best practices and working in partnership with them is the best way to create desirable change.

REPLICATION/SCALING UP – Having gained experience in areas that include coffee finance, coffee quality improvement and business strategy for producer organizations, TechnoServe has been asked to replicate its coffee competitiveness initiative. In 2006, plans are underway to increase the number of central pulperies from 29 to more than 50 and to support KILICAFE to produce best-practice guidelines to help member farmers increase farm productivity. Discussions are underway to replicate the approach in several other countries in Africa and Latin America.

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