Memo to Political Busybodies: There Is No Value Addition in Processing Coffee. It Is a Cockroach Idea

Paul Krugman, 2008 economics Nobel Laureate and prolific *New York Times* columnist narrates how as a young man he went to work for Government and an old hand, presumably a senior government economist, explained to him that their job was mostly about fighting bad ideas. The bad ideas, the old hand went on to explain, are like cockroaches, "No matter how many times you flushed them down the toilet, they keep coming back."

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One such cockroach idea is that we are losing money by selling our coffee raw, and we could add a whole lot of value by processing it domestically. I first wrote an Op-Ed on this idea fifteen years ago, I read sometime back that a venturesome cooperative in either Nyeri or Kirinyaga had set up a coffee processing operation but couldn't sell the product. Someone forgot to tell them that it is at the business end – market entry, product launch marketing, distribution and all that – that the rubber hits the road. Still, hope springs eternal. I have learned that Moses Kuria, the mouthy MP for Gatundu South, has drafted a bill intended to make domestic processing of coffee mandatory.

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The idea of value addition is closely related to the concept of agricultural value chains. But many people who talk very forcefully about value addition do not actually understand what a value chain is. If they did, they would not be so cocky. More often than not, they are talking about a supply chain. A value chain captures the production-to-market linkages that generate value for the customer. A supply chain captures the processes that transform raw materials or commodities into products.

A supply chain analysis starts with the procurement of raw materials and ends with the delivery of the product to the shelf where the final consumer picks it from. A value chain starts at the other end – with the value proposition to the customer – and traces how and where that value is created along the chain all the way back to the raw material. Value proposition means the characteristics that a consumer likes or prefers about a particular product that makes them choose that product, and even pay a premium over similar or competing products. The value proposition can be price, taste, appearance, durability, convenience, image, or all of these attributes and more.

Consider sneakers. A supply chain view of sneakers will seek to understand the sourcing of raw materials that go into manufacturing sneakers, the logistics of getting these materials to the sweatshops in Asia and elsewhere, volumes, sizes, styles and colours, production cycles, inventory, distribution channels and such like. A value chain analysis will start with why customers are willing to pay three or four times more for their Air Jordans than for generic products or cheaper brands, and work through the chain to see how and where the value is created.

The most expensive coffee in the world is an Indonesian coffee called Kopi Luwak, also known as Cat Poop Coffee. Kopi is coffee, Luwak is the local name for the Asian civet cat. Kopi Luwak is retrieved from the poop of the civets, which eat the cherry but do not digest the beans. A cup of this coffee will set you back anything from $35 to $100 (Sh3,500 to Sh10,000) and $200 to $1,200 (Sh20,000 to Sh120,000) per kilo of beans, about 20 times the price of other premium coffees. If exactly the same coffee bean was processed by human beings as opposed to being pooped by a civet, it would not fetch more than $40 a kilo. In effect, at least 80 per cent of the value of Kopi Luwak is generated by civets.

The Espresso & Coffee Guide lists its top ten coffees of 2019 – in no particular order – as Tanzania Peaberry, Hawaii Kona, Nicaraguan coffee, Sumatra Mandheling, Sulawesi Toraja, Mocha Java, Ethiopian Harrar, Ethiopian Yirgacheffe, Guatemalan Antigua and Kenya AA. Jamaica Blue Mountain gets an honorable mention and Kopi Luwak a dishonorable one. Most other coffee reviews have more or less the same list. The reason that Jamaica Blue Mountain does not make the list is because it is expensive, costing according to the website, double the price of Kona and four times the price of Kenya AA. But the review does acknowledge that Jamaica Blue Mountain is consistently rated as the best coffee in the world. Kopi Luwak gets a thumbs down for the ridiculous price, lack of traceability (i.e. authenticity certification) and animal cruelty reputation issues.

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Homegrounds.co – a coffee e-commerce website whose top ten coffees also overlap with those on the Espresso & Coffee Guide – has Jamaica Blue Mountain as the most expensive, with several offerings retailing at between $50 and $100 a pound (Sh11,000 – Sh22,000 a kilo) and a Central American Geisha from Costa Rica and Panama in the same range at $70 a pound (Sh15,400 a kilo). All the rest, are priced between $18 and $24 (Sh4,000 and Sh5,300) a kilo. Kenya AA is priced at US$20 a pound (Sh4,400 a kilo)

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What these price differentials are not about is processing. There is no amount of domestic processing of Kenyan coffee that can increase its value from $20 to $50 a pound. Beans and ground coffee generally cost the same. A decent kitchen grinder costs Sh3,000 at the supermarket, cheap ones half that. Moreover, roasting brings shelf life issues into play; raw beans will last well over a year, although they begin deteriorating after six months. Once roasted, coffee is best consumed within 24 hours. Once ground, it loses its freshness within half an hour. Discerning coffee drinkers don't want stale coffee, and will pay more for coffee roasted as they wait, or for green beans for that delectable treat of serving your dinner guests fresh coffee, roasted right before their eyes. It is of course possible to preserve some freshness by vacuum packing, but supermarket coffee buyers are price not value customers. The import of Moses Kuria's "value addition" bill is to lock Kenyan coffee out of the value market.

We are then left with the question that, if Kenyan coffee can fetch well over Sh4,000 a kilo, how much of that is the farmer getting? The February 2019 market report from the Nairobi auction – the most recent on the Nairobi Coffee Exchange website – gives prices of $70 and $320 for the low "T" grade and the top grade AA, respectively, and an average of $220 per 50 kg bag. These prices translate respectively to $1.40 (Sh. 140), $6.40 (Sh640) and $4.40 (Sh440) per kilo of clean coffee, meaning that the farmer is getting no more than 10 per cent of the shelf price. It is of course the case that not all Kenyan coffee ends up in the premium market; some ends up in supermarket roast and ground blends – but that does not mean that it is of less value.

I cannot emphasise enough that there is no value addition to speak of that happens between the Kenyan AA bought at the auction at Sh640 a kilo and the Sh4,400 shelf price in the destination market. But even locally, the retail price is on average three times the auction price, The coffee trade has all manner of commercial and technical explanations, but it is hard to see them as anything but self-serving seeing as it is the trade itself that appropriates the premium. The simple answer is: middlemen – a powerful ruthless global cartel politely known as "the trade" ("the craft" would be more apt).

Let's start with the national brand Kenya AA. You will have noticed that most coffees are named for their geographical origin. Jamaica Blue Mountain is grown on the Blue Mountains range that dominates the Jamaican landscape. Ethiopia has two coffees in our top ten list, Yirgacheffe and Harrar and Indonesia has three: Sumatra, Sulawesi and Java.

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So, why Kenya AA and not Mt. Kenya Peaberry or Aberdare Ruiru 11? AA refers to bean size, known as screen size. AA are the largest beans.The next size is AB, which in the February market report averaged $4.40 (Sh450) a kilo. In effect, coffee from the same bush can end up having a 30 per cent price difference on account of a one millimeter difference in the size of the bean. The reason for sorting out coffee beans by screen size is roast evenness, that is, to ensure that when beans are roasted, some are not undercooked and others overcooked. Once roasted, the AA beans and the AB beans sold at a discount can be re-mixed, packaged and sold as Kenya AA. These are the "trade secrets."

But the crux of the problem is the fact that the law denies farmers control over their product. Converting coffee cherries (the ripe fruit that farmers pick) to coffee beans that you can roast at home is a simple process that can be done on the farm manually, even on a small scale. Yet farmers are compelled by law to sell their coffee through the auction, or to appoint members of the trade as marketing agents. Cooperative members lose control of their coffee as soon as they deliver the cherry to their local pulping factory, while those with their own pulping plants lose control after milling (milling entails removing the beans from the husk, and is not very different from hulling maize).

The $100-a-pound Jamaica Blue Mountain offerings come with names like Wallenford, Clifton Mount Estate and such like. These are coffee growers, and such coffees are known as single origin coffees. This is how value is added to coffee – by market segmentation, and positioning single origin brands in different niche markets. Jamaica produces only 8,000 tonnes, and sells 80-90 per cent of it to Japan. Kopi Luwak production is between 500 and 1,000 tonnes a year. The more distinct the coffee and more niche the market, the higher value. The difference between the price of green and roasted beans of a certified single origin Blue Mountain coffee is immaterial.

Fifteen years ago, my colleague Githuku Mwangi, myself and the late Julius Mimano (the man at the helm of Kenya Railways when trains ran on time) who was then chairperson of the Kenya Coffee Growers Association – and coffee farmer par excellence – developed a plan to give control of coffee to the farmers so as to enable them to sell single origin coffees. We did all the homework, including mapping all the growing regions, developing a brand book, and securing the support of the Specialty Coffee Association to implement the specialty coffee certification system. We got many stakeholders behind the initiative but the trade cartel wore us down. A decade and a half later, so called coffee reforms are still going round in circles.

These reforms would have enabled the coffees from the different growing regions to distinguish themselves and find the consumers who have the taste and are willing to pay good money for their coffee. Mt. Kenya coffee might make a name for itself in California, Kisii Highlands coffee in Sweden or somewhere else. If the farmers were to get 70 per cent of the consumer price, the additional cost and risk of roasting, packing and marketing would not be worth taking. On the other hand, as long as the middlemen are in control, processing coffee locally makes no difference for the farmer. Whatever benefits might accrue will still end up with the middleman.

At the peak in the late 80s Kenya produced 130,000 tonnes of coffee. By 2003 when we got involved, production was down to 50,000 tonnes. With our reforms, we estimated we could get it back up to 80,000 in three years, and to 150,000 in a decade, averaging $10 a kilo, which at $1.5 billion in export earnings (Sh150 billion) would have catapulted coffee back to the country’s top foreign exchange earner. We are now down to 40,000 tonnes, earning about 15 per cent of that (Ksh. 23 billion last year).

As long as cartels and cockroach ideas rule the roost, coffee farmers will continue to vote with their feet. Because farmers owe themselves an income, be it from bananas or avocados, it does not matter. They do not owe trade cartels or the Government coffee.