CHAPTER 1

INTRODUCTION

In India the agricultural sector has an important role to play in her overall economic growth. Firstly, it has to provide for the increasing demand for food and raw materials, secondly, agricultural commodities which account for a major share of total foreign exchange earnings of the country have to continue to earn more and more of foreign exchange for some more period of time. It is to be done in a situation of free market. But there have been occasions for the government to intervene when the structural bottlenecks of the market stifle its function of providing sufficient and just price signal. Intervention may be to strengthen the forces of demand and supply. One such case was the Indian Coffee market in the beginning of this century.

Lovers of good Coffee often wonder how Indian Coffee is distinctive, delicious and distinguishable. To comprehend fully the principal reasons for Indian Coffee being one of the world's finest coffees is, to understand pretty well a whole range of coffee facts and operations in the country.
Coffee Plantation in India

An introduction of coffee plant to India is one of the greatest plant introduction to India in the fifteenth century. It is believed that a Muslim saint name Baba Budan brought the seeds of this plant from Yemen (Arabia) in 1670 A.D. and planted them near the place of his worship on the hills near Chikmaglur in Karnataka. With this small beginning, the coffee plants gradually spread to the backyards and gardens of the neighbouring districts of Hassan and Coorg. It was only in 1870 when commercial plantations of coffee were raised by the British in the heavy rainfall of the hilly areas of the three southern states of Karnataka, Tamil Nadu and Kerala.

Area Under Coffee Production

Coffee cultivation in India covered an extent of 245,758 hectares in 1990-91. Of this 53 per cent was accounted by traditional areas viz., Karnataka followed by 27 per cent in Kerala and about 14 per cent in Tamil Nadu. The balance of 6 per cent came from non-traditional areas Andra Pradesh, Orissa, Assam etc. Arabica was grown in 123 thousand hectares with the remaining 109 thousand hectares coming under Robusta. Arabica is mainly cultivated in Karnataka, Tamil Nadu whereas Robusta is mostly grown in Kerala followed by Karnataka.
The area expansion in absolute terms during the three decades has been highest in Karnataka with over 60 thousand hectares, followed by 44 thousand hectares in Kerala and nearly 8 thousand hectares in Tamil Nadu. In respect of, holdings in the range of 2 to 10 hectares, the area under coffee has gone up by 63 per cent in Karnataka, 41 per cent in Tamil Nadu and 17 per cent in Kerala.

India is one among the small producers of coffee in the world. The total area under coffee in India was 245,758 hectares as against 9,414,545 hectares in the world. The share of India in area in the world is meagre of 2.61 per cent and it ranks 15th amongst the coffee producing countries of the world.

**Types of Coffee**

There are two types of coffee grown in the world: arabicas and robustas. Robustas can be grown in hot and humid climates. Arabicas require lower temperatures and are therefore grown at higher altitudes. Coffee is heavily damaged, however, when temperatures fall below the freezing point and this sets a limit to the area where coffee can be grown. There exist also two other types of coffee, liberica and excelsa, which are both grown in Western Africa, but they constitute less than 0.5 per cent of world production and exports.
In India, six commercially important varieties of Arabicas have been cultivated in succession. These are old chicks, coorgs, kents, S.228, S.795 and S.1934. Recently an another bumper coffee crop namely Cauvery has been introduced.

Arabica, a small tree with a grey to light brown bark, branches profusely with dark green leaves. The flowers are white and pentamoromous. The flower buds are produced in clusters in the axial of leaves during October to March. The flowers blossom in 9 to 10 days after the receipt of 'blossoms showers' in March-April. The fertilised ovary grows into a fruit in about 8 to 9 months. During this period, there is tremendous growth in the fruits, finally ripening into dark red berries which are round in shape. Each fruit usually produces two seeds. The freshly pulped beans, called parchment, are white. Sun drying and removal of 'silver skin' impart a bluish green tint to seed, which is considered as quality coffee.
Rebusta is a bigger tree than Arabica with broader and larger leaves. Leaves are pale green and flowers are white and fragrant. They are borne in large clusters than Arabica with smaller and roundish berries but high in number (varying from 40 to 60) per node. It is a low land coffee having a wider geographic distribution in Africa with high concentration in the Congo. It grows better under relatively open and humid conditions than Arabica.

The buds appear during late November to February, under the soil and climatic conditions of South India. The fruits mature in 10 to 11 months and are generally ready for harvest two months later than Arabica.

Coffee Production

Coffee is a tree crop and gets its first harvest in about 3 to 4 years after planting but it takes another two years to reach its normal yield. It is observed by planters that normally yield starts declining after 45 to 50 years of planting and is therefore, desirable to replace trees older than 50 years with
the new ones. Since 1960/61, India has been producing more than 65,000 tonnes of coffee annually. The average annual production during the first half of the sites has been around 1,35,000 tonnes. It was 1,57,000 tonnes in 1990/91.

Export Quality of Indian Coffee

Nature with its generous Indian climate and rich soil pampers coffee's growth, careful scientific cultivation of the coffee on hill slopes, programmed picking of the coffee fruits by deft human hands and the gentle, painstaking manner in which they are processed, unlock the full flavour latent in every bean. Rigid assessment of quality loads to the export of the finest beans accounting for the superiority and fine aroma of India's high grown, mild coffees. Indian coffee with different exportable grades, is amongst the best in the world and is used for blending with coffees of other origins. Indian coffee was exported to different destinations like the then USSR which is known as CIS at present and the East European countries viz., the
When World War II broke out, the economy of the Indian Coffee Industry was shattered. As India lost the continental markets for coffee and consumption within the country was not large enough to absorb the quantity that would have gone for export, the need to develop a strong domestic market was strongly felt. Thus the industry was suddenly facing a crisis. It was in this critical juncture, the Government of India issued an ordinance to exercise control on coffee through a Board. The ordinance was later replaced by an Act, 1942, by which the Coffee Board was established, with full responsibility for the collection, storage, curing and marketing of coffee both for internal consumption and export.

As envisaged in the Coffee Act, entire coffee produced in the country must be delivered to the Board.

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In turn, the Board has the statutory function to safeguard the interests of both the producers and the consumers. The Board releases Coffee under a 'Reserve Price Scheme' so as to ensure an economic return to the growers, particularly of small growers who constitute 98 per cent of the estates in India.

The area and production of Coffee in India have recorded an upward trend in the post-independent years. The present area of two lakh hectares is more than two and a half times the area that existed before independence. The actual production of Coffee has also shot up to 1.95 l.t. in 1993. The Coffee growing tract is mainly confined to three states viz., Karnataka, Tamilnadu and Kerala.

Production recorded a phenomenal increase during the four decades, rising from nearly 19,000t. in 1950-51 to as high as 1.95 l.t. in 1993. The expansion of production by more than 10 times has come, more from improvement in productivity than from the area.

expansion. The Coffee estates are an important source of employment. It is estimated that there are about 2.3 lakh daily workers engaged in 91,000 Coffee estates in India.

Coffee is not an important agricultural commodity in India areawise, productionwise and exportwise, but it is important as a major foreign exchange earner and as a source of revenue to the government. It ranks next only to tea among the plantation crops with an export earning of Rs.400 crores during 1992-93. In the World, more than 80 countries grow coffee. Brazil and Columbia account for nearly half of all the coffee produced in the world. India's share of global production is only 2.8 per cent. Therefore, India has to face a stiff competition in export of coffee.

Historically, the production of coffee grew, so did its exportable surplus because domestic consumption grew

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4 Coffee Board, Indian Coffee XLIII (a), 1979, p.254.

1 t - tonne = 1000kg. 1 l.t. = lakh tonnes.
at a much slower pace than that of production. However, the country was able to find export market for the whole of its exportable surplus of coffee in most of the years in the past. Only in the recent years, the sudden jump in production has resulted in accumulation of huge stocks and marketing of coffee has become a problem. The International Coffee Agreement (1976) provided a helping hand, but it collapsed in 1989.

The Coffee Board had a major role for the expansion of production and its efficient disposal, ensuring remunerative prices to the growers. The Board evolved and put to practice a scientific method of management and played its role successfully. But the latter half of the eighties and the beginnings of the nineties saw radical changes in the approach of many coffee growers and organisations towards coffee marketing aspects. The Board's failure to protect growers from the crisis caused by the crash in the international prices in July 1989, following the collapse of ICA, further aggravated the condition. The growers gave vent to their feelings openly by suggesting alternative system of marketing.5

The government responded to the demands with a presidential ordinance on August 20, 1993 allowing the growers to sell 30 per cent of their production under (free) Internal Sale Quota (ISQ). It was further changed into a system called Free Sale Quota (FSQ) by which farmers were allowed to sell 50 per cent of their production in combined open auctions for both domestic sales and export. Even this did not satisfy the growers. As Bhandari put it "the situation has put into a quandary everyone—the growers, the Coffee Board, the trade, both domestic and export and the curers." The farmers have demanded the FSQ to be 100 per cent. In other words it would mean optional pooling or depooling and the sale of coffee by the growers will be in a fully free market condition. Several signs of these possible developments were available from mid 1987 and the problems came into sharp focus consequent to the collapse of ICA. The role of the Coffee Board and even its need to exist were questioned since the mid-eighties. It is in this context, the present study found its rationale and scope.

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6 The Economic Times - February 8, 1994.
1.1 PROBLEM FOCUS:

Immediately the question arises as to why an institution that has stood the test of time is now losing the confidence of the coffee growers? With a large export market, is it not possible for the Board to bring satisfactory price to the growers especially when the Board has near monopoly in the trade? Is the recent problem of glut in the International market for coffee, a cause of this crisis? To answer these questions, the present study evaluates the performance of the Coffee Board vis-a-vis the role assigned to it more specifically its success in increasing production and efficient disposal of the produce to protect the interest of the growers and the domestic consumers of coffee and in inventory management.

1.2 OBJECTIVES:

Therefore the overall objective of the study is to evaluate the performance of the Coffee Board at a time when its very existence is questioned. More specifically the objectives are.

I) to evaluate the performance of the Coffee Board vis-a-vis its mandate to increase
production, export and consumption of coffee, with adequate protection to the interest of the growers;

II) to measure instability in production, export, domestic sales, and prices of coffee in export, retail sales and to the farmers;

III) to identify the major causes of instability; and,

IV) to suggest specific strategies for efficient management of increasing supply and consequent rise in stock holding.

1.3 HYPOTHESES:

The basic hypothesis of this study is that the instability in prices of Indian Coffee is large and needs to be narrowed down. The responsibility rests with the Coffee Board. Therefore, specific options available to the Board have to be identified and evaluated. This requires the empirical verification of the following hypotheses:

I) Significant expansion in the domestic market for coffee is essential to act as a cushion
against uncertainties in the international market.

II) growing size of the stock holding is a cause for instability in price of Coffee. Therefore inventory management needs better attention of the Coffee Board.

III) To protect the interests of large number of small growers, the Coffee Board has to promote export further and ensure remunerative prices to them.

IV) The collapse of International Coffee Agreement makes export more competitive and India with its tiny share in the world coffee market would suffer. So the revival of ICA will be to its advantage.

1.4 SCOPE OF THE STUDY:

The purpose of the study is to assess the performance of the Coffee Board with special attention to price instability and supply management in both domestic and international markets.

Considering the current scenario of the Coffee industry and the possible future directions the industry
should take, the study is of the opinion that there is a strong case for structural change in the industry. If the coffee industry is to grow and develop as a major industry in India in the long run, it has to maintain its comparative attractiveness vis-a-vis other plantation industries. At present Indian Coffee Industry is heavily dependent on the international market. Collapse of the International Coffee Agreement on quotas and the resultant competition in the international market would necessitate Indian Coffee Industry to adopt aggressive efforts in the international market to maintain and improve its share of the market and to better the price realisation. To examine these possibilities, the following steps are undertaken:

Firstly, an attempt is made to measure the instability in prices. This would help identify the factors responsible for trade performance of Indian Coffee.

Secondly, the stability pattern of the export prices of Indian Coffee is examined by developing an algebraic model incorporating various factors hypothesized to be important in the study will be
useful for policy formulation to achieve price stability and market equilibrium for Coffee in the future.

Finally, the findings of the study are summarised into a set of suggestions that would help the Coffee Board authorities in their policy formulations and even give policy alternatives.

However, resource and data constraints necessitate several simplifying assumptions. These assumptions and the limitations in applying the model to some other commodity, particularly for policy decisions, are indicated later.

1.5 PLAN OF THESIS:

CHAPTER 1 : INTRODUCTION

Problem setting, the objectives, hypotheses, scope of the study are discussed.

CHAPTER 2 : CONCEPTS AND REVIEW OF LITERATURE

A review of past work and concepts relevant to the study is done. This provides theoretical basis for model building.
CHAPTER 3: INDIAN COFFEE SCENARIO
Origin, growth, development of the Coffee Industry, marketing processes, price determination, rules and regulations of coffee marketing, International Coffee Agreement, importance of coffee industry are discussed.

CHAPTER 4: MODEL AND METHOD
Plan model and design of the study are described.

CHAPTER 5: RESULTS AND DISCUSSION
Major findings of the empirical analysis are presented and discussed.

CHAPTER 6: SUMMARY, CONCLUSIONS AND IMPLICATIONS
Summary of findings and conclusions together with policy and research implications are presented.