

OMD: 200: SUBJECT FILES: COFFEE

BOX: 11 FILE: 160
#4588

DEC 6 1955

Dear Mr. Uribe:

This is in reply to your letter of November 28, 1955, asking that a study on coffee prepared by a member of the Fund staff be made available to the Subcommittee of the Special Committee on Coffee of the Inter-American Economic and Social Council for use and possible quotation in the Subcommittee's report to member governments.

The study to which you refer is entitled "Prospective Price Developments for Coffee and Their Effect on the Payments Position of Exporting Countries", by Miss Gertrud Lovasy, and dated October 24, 1955. We are pleased to make this paper available to your Subcommittee. If you feel it useful to refer to the paper, or to attach it to your report, we would appreciate it if you would bear in mind, and convey to your readers, the fact that the paper does not attempt to forecast the price of coffee, but merely tries to evaluate the likely behavior of coffee prices under certain assumptions, among them the assumption that there would be no concerted governmental action in the international coffee market.

Three copies of the study are enclosed. We will be glad to send you additional copies if you wish.

Very truly yours,

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Ivar Roeth
Managing Director

Mr. Andres Uribe
Chairman, Subcommittee of the
Special Committee on Coffee
Organization of American States
Pan American Union
Washington 6, D.C.

cc: Mg. Dir.
Dep. Mg. Dir.
WHD
UN Rep.
RES
ERD
SEC
Miss Stark

INFORMATION COPY

To : Mr. I. Rookh

Fr : E. Elmholt

Subject : G. Lorange's paper on coffee

The remark that "it appears that prices would have to be lowered to some 30-40 percent below the 1953 level in order to "clear the market" seems well documented on pp. 7-10. The table on p. 14 gives the effects on Latin American Coffee Reporter's foreign exchange receipts, and page 16 an estimate of the effect on Ethiopia is made. On p. 17-18 the present international schemes for stabilizing the coffee market are reviewed. The paper, I found very good and in spite of the technicalities of the method well tempered with common sense.

In addition to the long gestation period and subsequent lifetime of the tree which prevent an early adjustment of production, output is subject to short-run variations resulting from exhaustion of the tree after each large crop which is then followed by a poor one in the following year. A regular two year cycle arising from this property of the tree would not, as such, create market disturbances. It is, however, frequently upset by weather conditions; frost damage has occasionally caused a series of poor crops and favorable weather has raised the yield in consecutive "high crop" years. These irregular fluctuations, rather than sudden changes in demand, have been responsible for the sharp year-to-year changes in coffee prices observed in the past.

Demand for coffee primarily determined by established habits has been steadily growing with rising population in the major consuming countries; short-run changes are minor as the response to income and price changes is, as is shown below, rather feeble.

Data for the last 63 years show that -- with the exception of the war periods -- a decline of consumption by more than 4 per cent occurred only three times -- in 1899, in the early thirties and again in 1954, but in none of these periods did the reduction exceed 10 per cent (see Diagram 1). Price fluctuations -- short-run as well as long-run -- were almost exclusively due to the factors on the supply side mentioned above. Coffee prices during the 63 years starting in 1892/93 when deflated by a general wholesale price index show three cycles, each consisting of a short period (2-6 years) of very high prices followed by a 10-20 years stretch of continuously low prices. During the last six years prices have again been high (see Diagram 2). There have been considerable year-to-year fluctuations within each of the high and low price periods, but in no year either of the high or low price periods did prices decline or rise respectively to the average level for the 63 years period as a whole.

As shown in Diagram 3 the four high price periods were associated, sometimes after a time lag, with a narrowing of the margin between potential supply (i.e. annual exportable production plus carryover stocks in producing countries)^{1/} and consumption in importing countries^{2/}. The subsequent widening of this margin initiated the periods of low prices. In the first period shown the downward reaction (1895/96) was quick and sharp. The steep but brief upturn starting in 1910/11 came after a comparatively minor decline in supply relative to demand. At that time support operations by the State of Sao Paulo had already started and part of the stocks were held by the State. The sharp downturn after the shortlived boom was no doubt

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- ^{1/} The term production or output and all the data on production used in diagrams, tables and in the text refer, throughout this paper, to "Exportable production", i.e. total production reduced by the quantities retained for domestic consumption (largely of inferior quality) and, in the case of Brazil, also excluding port consumption. The stock figures used to compute total supply are total carryover stocks in the producing countries; no allowance was made for stocks temporarily withheld from the market; they are included in the stock figures used. Data on segregated stocks are available for Brazil only, and only for a limited period. It therefore seemed preferable to use total stocks in producing countries throughout
- ^{2/} The term "demand" or consumption and data on consumption used in diagrams, tables or in the text refer throughout this paper to demand or consumption in importing countries.

precipitated by the war. The sharp upturn in prices in the mid-twenties was again associated with a narrowing in the margin; the failure of prices to react to the rapid rise in output and widening of the margin in the late twenties resulted mainly from support operations by the Brazilian Government which delayed, but could not prevent, the collapse of prices after 1929. The coincidence of rapidly rising production with the depression of the thirties enhanced the steep rise in the spread between supply and demand; the persistently high level of that spread throughout the thirties -- in spite of destruction of large quantities of coffee in Brazil^{1/} -- left coffee prices depressed throughout the thirties. Low prices coupled with strict prohibition of planting in Brazil resulted in a sharp decline of Brazilian output, only partly offset by expansion in other areas; thus, by the end of World War II production had fallen by about one fifth^{2/}; stocks were rapidly used up and the supply-consumption margin narrowed down rapidly. Prices reacted with a sharp rise; their high level for the last five years, however, has stimulated new planting in Brazil and elsewhere; from the late fifties on output is expected to rise at a sharply increasing rate and the widening of the margin between supply and demand, which has already begun will rapidly proceed.

2. Market developments in recent years. The current statistical position indicates a considerable excess of supplies over demand (see Table 1).

Table 1. Developments in Supply and Consumption of Green Coffee (million bags)

	1953/54	1954/55	1955/56
<u>Exporting countries:</u>			
Carryover	6.0	6.0	10.3 ✓
Production	<u>33.5</u>	<u>32.3</u>	<u>37.0</u> ✓
	39.5	38.3	47.3
Exportable supply ^{1/}	<u>35.5</u>	<u>34.3</u>	43.0
<u>Importing countries:</u>			
Total net imports ^{2/}	33.5	28.0	
United States: net imports	20.5	15.2	
drawing on stocks ^{3/}	<u>-1.3</u>	<u>2.4</u>	
apparent consumption	19.2	17.6	
Other importers' approximate consumption	13.0	12.8	
Total consumption in importing countries	<u>32.2</u>	<u>30.4</u>	

Sources: Based on U.S. Department of Agriculture, Foreign Agricultural Circulars; George Paton and Co., "Coffee Intelligence", Pan American Coffee Bureau Coffee Statistics.

1/ Exportable production for the year plus carryover deducting 4 million bags as working stocks.

2/ Estimate based on net exports.

3/ Minus sign indicates stock accumulation.

1/ Destruction over a period of 10 years has been estimated at some 70 million bags. 2/ Output in the early postwar years compared to the average of the thirties.

*In all countries
not only Brazil*

DIAGRAM I

EXPORTABLE PRODUCTION AND CONSUMPTION OF COFFEE 1892/93-1955/56

MILLION BAGS

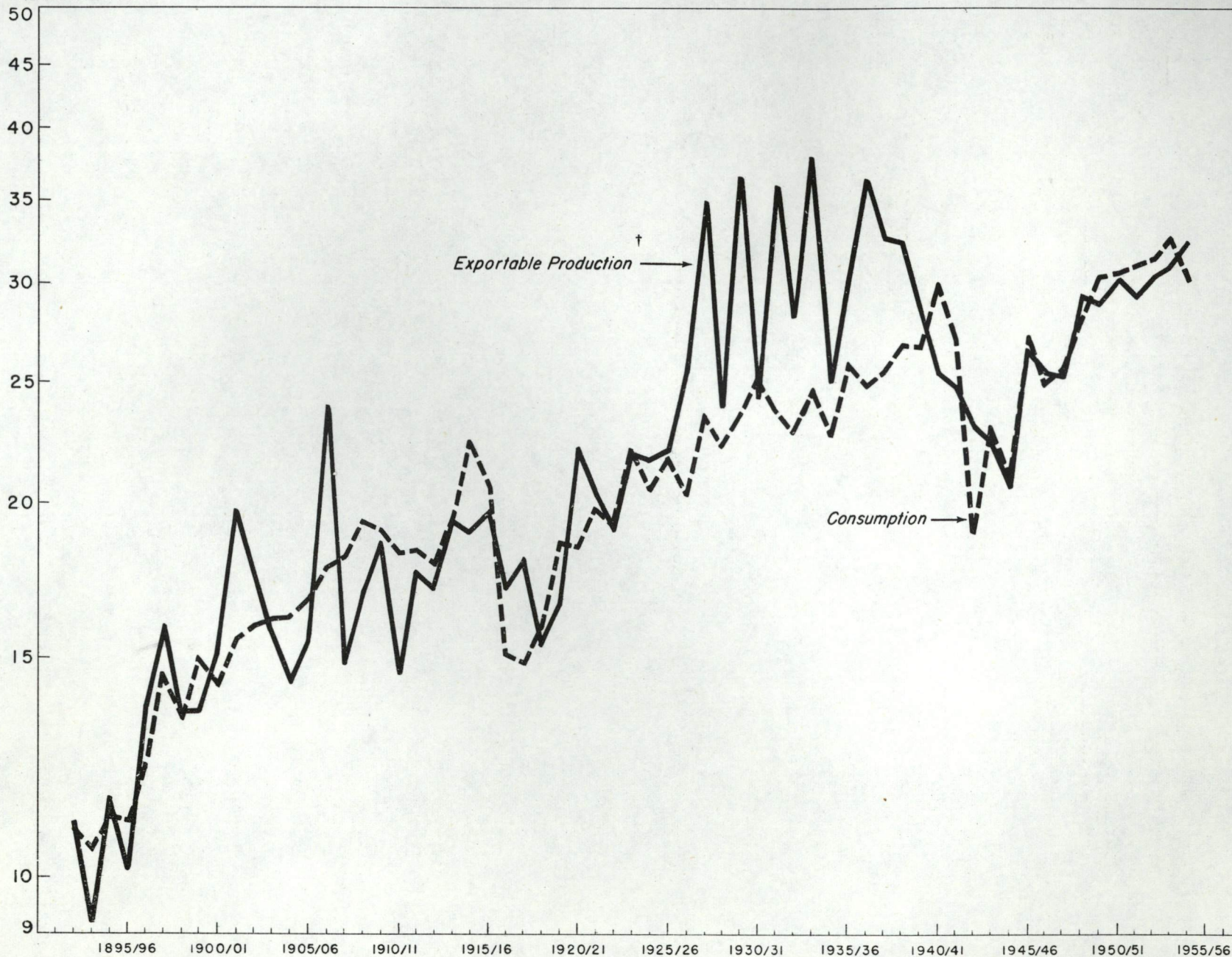
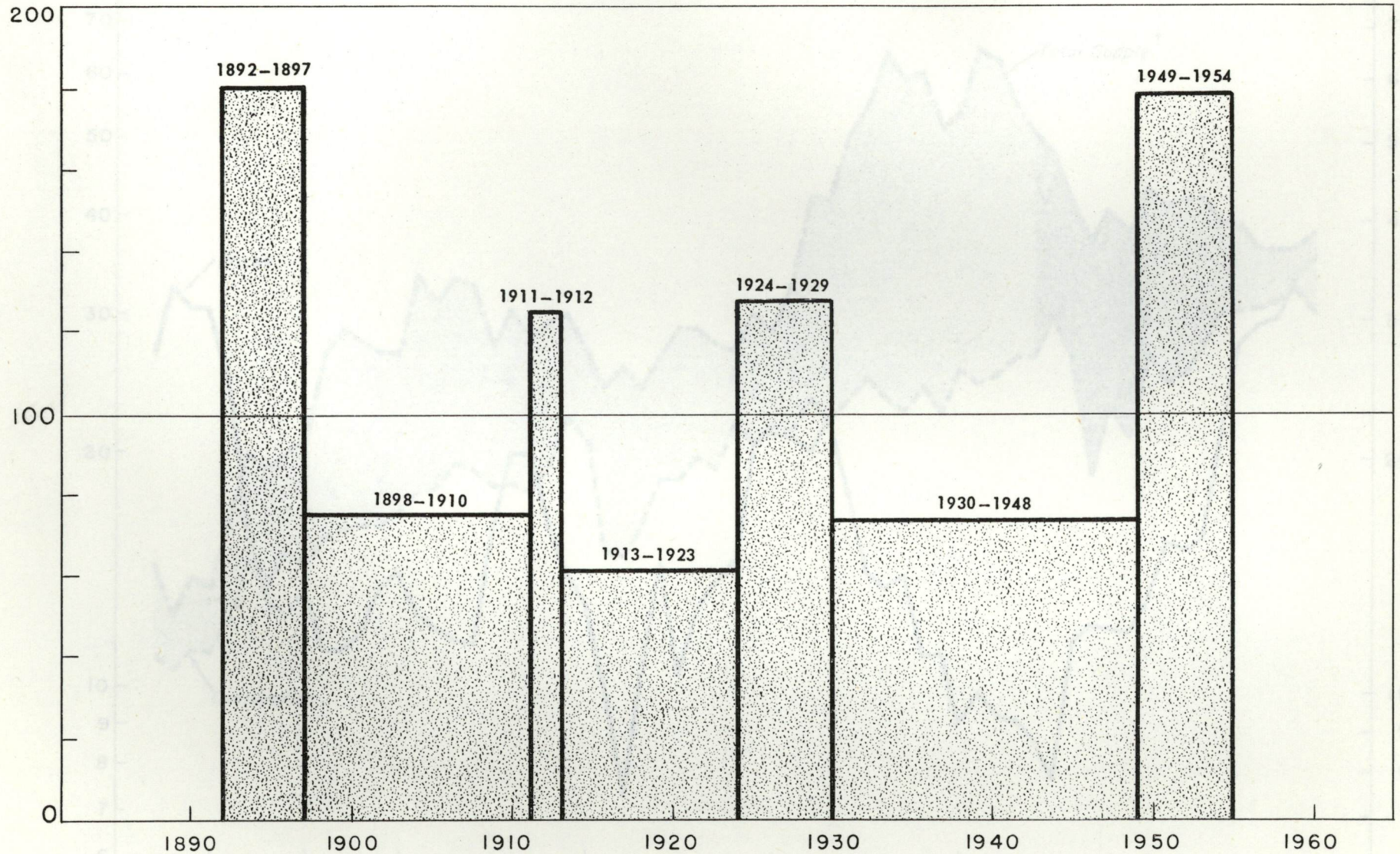


DIAGRAM 2
 †
 COFFEE PRICES: CYCLICAL MOVEMENTS 1892-1954



† Unit value of U.S. coffee imports deflated by U.S. general wholesale price index, averaged for sub-periods shown, and expressed as percentage of the average for the whole period 1892-1954.

Any figures for each country? yes p

Exportable supplies in producing countries in the 1955/56 marketing season (i.e. annual output plus carryover, allowing for domestic consumption and working stocks) may be put at roughly 43 million bags. This compares with consumption in importing countries, presently estimated at a rate of about 32-33 million bags. Exportable production in 1955/56 is expected to amount to 37 million bags, about 10 per cent above the postwar peak reached in 1953/54. In that year exportable production had finally caught up with import demand and, for the first time in six years, did not have to be supplemented by drawing on stocks. The frost in Brazil of July 1953 caused some production setback in the following season; the current crop, however, fully reflects the effect of extensive planting during the period following the price boost late in 1949. Output in 1956/57 will again be affected by frost damage in Parana. It is believed, however, that production gains in other parts of Brazil and elsewhere will at least offset the short-fall in Parana and world production in 1956/57 is expected to equal or even to exceed current levels. For subsequent seasons considerably higher and rising crops are anticipated. Demand for coffee, on the other hand, cannot be expected to rise at a similar rate; it therefore would appear that the international coffee market is about to enter another phase of high production and declining prices.

3. Price developments on the New York Market. In view of the large share of the United States in total coffee imports -- some 60 per cent of total coffee trade is absorbed by that country -- price developments on the New York market may be considered as a fair indication for the strength or weakness of the coffee market. The behavior of futures quotations on the New York Coffee Exchange, their relation to spot prices and the spread between quotations for the nearest and most distant contracts indicate the changing outlook with respect to market developments.

Table 2. Development of Spot and Futures Prices for Coffee in New York cts. per lb., 1951-55

	<u>1951</u> June	<u>1952</u> June	<u>1953</u> June Dec.		<u>1954</u> June Sept. Dec.			<u>1955</u> June	<u>1955</u> Sept.
Spot, Santos 4 <u>1/</u>	53.6	53.0	56.0	61.3	87.0	71.8	68.5	57.0	
Futures 2/									
Nearest month	52.1	52.5	56.3	<u>65.7</u>	89.0	61.6	62.7	51.3	<u>48.9</u>
Furthest month	48.0	49.8	51.2	<u>65.0</u>	<u>86.0</u>	51.9	48.8	36.0	<u>40.0</u>
Spread as % of									
nearest month 3/	8	5	9	1	3	16	22	<u>29</u>	18

Sources: George Paton and Co., "Coffee Intelligence"; Journal of Commerce.

1/ Average of month indicated.

2/ Closing quotations. June 1952 and 1953: all other end of month.

3/ Spread between nearest and most distant futures: for June quotations 12 months; for September and December quotations 10 months.

From 1951 to the beginning of 1953, spot prices were subject to an official price ceiling. During that period and up to the middle of 1953 spot prices and futures for the nearest month remained very close and the spread between the nearest and most distant futures varied within fairly narrow limits -- 3 to 12 per cent. No major price change was anticipated during that period. Late in 1953, however, when, on account of frost damage in Parana, expectations for the 1954/55 crop were most pessimistic and a sharp rise in prices was anticipated, futures rose considerably above the spot level and the spread between nearest and most distant futures virtually disappeared (see Table 2). By mid 1954, however, it had become obvious that the anticipated shortage would not materialize; crop prospects had improved and consumption had declined in response to the sharp price rise. Moreover, the time drew nearer when the output of the new trees planted after the price rise in 1949 would make for more plentiful supplies. The gradual price decline through the second half of 1954 and up to the summer of 1955 was accompanied by a widening margin between spot and futures prices, the latter falling faster than spot quotations. Moreover, the spread between nearest and most distant futures widened; in the summer of 1955 it reached and occasionally even exceeded 30 per cent.

4. Future prospects. Current supply and prospective output of coffee over the next years in relation to demand strongly suggest that, if nothing were done to prevent it, there would, in the near future be a sharp decline in coffee prices. The history of the coffee market as well as the course of futures prices on the New York Coffee Exchange point in the same direction.

Taking it for granted, however, that the market is in danger of a serious break leaves us with a number of open questions: when would the downturn tend to come, what would be the extent of the price decline and how would it affect exchange earnings and incomes in exporting countries: Finally it might be asked what, if anything, is being done to avert or mitigate the expected break of the market. The question with respect to timing can be answered in very broad terms only; the weakening of prices might well tend to start towards the end of the year when Central American crops reach the market, but both the date of the downturn and the speed of the process would depend on other factors. Apart from unforeseen hazards which may change this or next year's supply prospects, support policies in major exporting countries may have a delaying effect. The comparatively low level of inventories in the United States and the possibility that importers may wish to replenish stocks to their customary size, which is roughly one million bags higher than the present level, also may retard the price decline. But such purchases for inventory could raise demand only temporarily; moreover, it would only narrow down and not close the gap at present prices between prospective supply and prospective demand at prevailing prices. It therefore would appear that in the absence of weather hazards or effective intervention, prices would be likely to come down within the current crop year.

at what time are the different crops coming to the market

What is that

II. Price Reduction Required to Raise Demand to Current Supply

In what follows a rough indication will be provided of the level to which the price for green coffee would have to fall in 1955/56 in order to raise consumption in importing countries to the level of prospective exportable supplies. It is assumed as a starting point that prospective current consumption in 1955/56 at 1953 prices would be the same as current consumption in 1953, viz., 33 million bags. 1953 prices are approximately the same as present prices and 1953 consumption would appear to be not too different from the present rate of consumption. It should be noted, however, that 1955/56 level of total consumption equal to the 1953 level implies a rate of per capita consumption somewhat lower than in 1953. Data on the per capita number of cups consumed in the United States compared with per capita consumption in terms of green coffee suggest an increasingly better utilization, partly on account of rising use of solubles, which is still further increasing. Appraisal of the decline in demand to be expected on that account is difficult and no allowance has been made for the use of solubles. It would be unrealistic, however, to expect, under these conditions, a rise in per capita consumption at present prices.^{1/}

It has been assumed for the purpose of estimating exportable supplies in 1955/56 that carryover stocks accumulated in producing countries will not be put on the market in addition to current exportable production; this assumption is not unrealistic since excess stocks^{2/} are largely being held by the Governments of Brazil and Colombia with the purpose of supporting prices. For the current crop, however, Brazil has discontinued stockpiling operations, and current output is expected to be offered on the market. Moreover, in estimating consumption no allowance has been made for purchases by U.S. importers to replenish inventories in the United States; as already mentioned, such purchases would be of a passing character; they could only temporarily make for a stronger response of demand to a price reduction and thus permit prices to remain somewhat above the level required in the absence of these purchases. Since, however, the high level of current production is expected to continue and to rise further it seems justified to neglect the possibility of a temporary addition to demand.

Taking 33 million bags as the rate of current consumption and 36.6 million as supply for 1955/56, demand at current prices would fall short, by roughly 10 per cent, of supply. The price reduction required to raise demand by 10 per cent depends mainly on the response of consumption in the major importing areas, the United States accounting for some 60 per cent of imports and Western Europe roughly 30 per cent.

- 1/ The U.S. Department of Agriculture expects U.S. per capita consumption for 1955 at no more than 15.4 lb against 16.7 lb in 1953 and 14.7 lb in 1954.
- 2/ I.e., stocks in excess of working stocks.

In this realistic

Does Col. this hold stocks?

not likely if shipping is accepted

I know that S.L. does not believe in an increase in consumption in Russia

not clear to the reader

A number of studies have been made on the response of coffee consumption in the United States to price and income changes. The results, referring to per capita consumption and to changes in retail prices for roasted coffee, agree in so far as they all show a very feeble reaction to changing prices. The numerical results for the price elasticity of demand, however -- all of them referring to short-run responses -- vary with different methods. The equation used by the Federal Trade Commission Study gives a price elasticity of roughly -0.5. The somewhat different approach by the FAO authors, yields a range of price elasticities from -0.2 to -0.3, varying for different income levels; at the present per capita income the price elasticity is roughly -0.27². An earlier study, based mainly on prewar data, yielded a price elasticity of only -0.2³.

Similar studies on European demand are lacking; except for one relating to Belgium only. Based on prewar data it arrived at a price elasticity of Belgian demand for coffee of around -0.54. Since Belgium with a share of less than 10 per cent in total European consumption cannot be considered as representative, demand elasticities for the three major importing countries -- France, Germany and Italy -- have been computed. In view of the fact that postwar data for these countries are distorted by rationing in the early years the computations have had to be based on the interwar period. Inspection of the data for recent years suggests, however, that the demand reaction to price changes would by and large follow the prewar pattern. The elasticity of French demand is found to be very low, -0.26; the corresponding figure for both Germany and Italy, on the other hand, is quite high -1.3. The striking difference may be explained by differences in the per capita income level and coffee prices in relation to income in the three countries. In France with the highest level of income the price for 1 kilogram of coffee in the late thirties was roughly 0.2 per cent of per capita income; the corresponding ratio for Germany was 0.5 per cent and for Italy as much as 1 per cent. In all three countries roughly 1 per cent of per capita income was spent on coffee: in France about 9 lb per head was bought, in Germany less than 6 lb and in Italy as little as 2 lb. These figures indicate that coffee is much more of a luxury in Germany and Italy than in France and a much higher demand elasticity is to be expected in these two countries.

*2 B
mid 21*

- 1/ Federal Trade Commission: Economic Report on the Investigation of Coffee Prices, July 30, 1954, p. 37 ff and Annex A; A. Szarf and I. Pigualosa: Factors Affecting United States Coffee Consumption, FAO Monthly Bulletin, October 1954; M. Holzman: The U.S. Demand for Imports of Certain Individual Commodities in the Interwar Period, IMF, RD 811, February 1949 (not published).
- 2/ The range for the corresponding income elasticity is 0.54 to 0.56.
- 3/ It should be noted, in this connection, that the equation yielding a price elasticity of -0.5 indicates a low income elasticity (0.2) while the equation used by Szarf and Pigualosa gives an income elasticity of around 0.5.
- 4/ Ch. Baré: Note sur l'élasticité de la demande de certain produits, Bulletin de l'Institut des Recherches Econ. et Soc., February 1953, p. 39.

In computing the overall elasticity of demand for coffee the data for the United States and for the four European countries, France, Italy, Germany and Belgium, accounting together for over 80 per cent of consumption in all importing areas have been used. In view of the large spread in the findings for the demand elasticity in the United States two alternative computations have been made, one based on the Federal Trade Commission's figure of -0.5 , the other on the figure of -0.27 found by the FAO authors^{1/}

The figures for both the United States and Europe refer to the response of demand to changes in retail prices; for our purpose the corresponding elasticity with respect to changes of the wholesale price for green coffee, f.o.b. exporting country has to be derived. The margins between the wholesale price for green coffee and the retail price for roasted coffee in the importing countries are largely determined by the cost of transportation, processing and distribution, and, where applicable, by duties and taxes. They appear to be fairly rigid in absolute amounts; except for short periods due to some time lag in adjusting retail prices they do not vary with changing wholesale prices. Consequently the decline in the retail price which follows a price reduction for green coffee is proportionately smaller than the change in the green coffee price; thus the demand elasticity with respect to the latter is less than with respect to the retail price.

In computing the elasticity of "world" demand on the wholesale price the demand elasticities of the five countries have been combined in the ratio of their shares in total coffee imports in 1953 and 1954. The retail prices used were the average prices as they prevailed in 1953; roughly equal to those in the summer of 1955. For Germany where a considerable tax reduction in August of 1953 made for a sharp decline in retail prices the reduced price has been used. The wholesale price for green coffee is the average price for Brazilian Santos 4, f.o.b. Santos, in 1953, i.e., 53 cents per lb., roughly equal to the average price in the first six months of 1955. Details of the calculation are shown in Annex Table 1.

The short-run elasticity of "world demand" for coffee with respect to the wholesale price on the basis of the data described was found to be slightly under -0.2 (using the U.S. retail price elasticity of -0.27) and just under -0.3 (using the U.S. figure of -0.5). This implies that in order to raise world demand by 10 per cent, the f.o.b. price for green coffee would have to be lowered by 28 per cent (if the elasticity is -0.3) or by 40 per cent (elasticity -0.2). On that basis the f.o.b. price for Santos 4 would have to be reduced to 38 or to 32 cents.

Before examining the effect of a decline of coffee prices to 38 cents per lb or less on the earnings of coffee exporters it should be emphasized that it is not the purpose of this paper to forecast the prospective level

This is a rough calculation with forecast

^{1/} No allowance was made for the increasing use of solubles which reduces the amount of green coffee used in preparing one cup of coffee and therefore tends to reduce per capita consumption of green coffee.

of prices at any given time. The intention is rather to indicate the price level which would "clear the market" ~~taking current consumption and output and rely~~ solely on the price mechanism to equate supply and demand. The accuracy of our result hinges primarily on how close to reality are the data on demand elasticity and there can be little doubt that they fall within the range chosen.

III. Effect of Price Cuts on Export Earnings of Coffee Exporters

a) Latin American Exporters. Of the ten Latin American countries which together supply some 80 per cent of world coffee trade, five depend for more than two-thirds of their export earnings on coffee; for the other five coffee accounts for 12-50 per cent of their export receipts. A decline of coffee prices to 30-40 per cent below the 1953 level would seriously cut the earnings of most of these countries.

Table 3 compares the value of this season's exportable production at prices reduced to the level at which, according to our computations, import demand would be raised to the level of expected output, with actual receipts for coffee in each of the years 1951-1954 and shows that the total export value for the ten countries together would be 15-30 per cent below actual receipts in the year 1951, the lowest in the four year period.

Table 3. Main Latin American Exporters: Coffee Exports 1951-54 and Computed Value of 1955/56 Production at Prices Reduced by 28 and 40 per cent from 1953 Average Level (Million U.S. dollars)

	1951	1952	1953	1954	1955/56 Exportable Production at Prices Reduced from 1953 Average	
					by 28%	by 40%
Brazil	1,051	1,038	1,088	948	860	722
Colombia	360	380	492	550	345	286
El Salvador	76	78	77	92	48	40
Guatemala	59	72	68	74	47	39
Haiti	26	34	25	43	23	19
Nicaragua	19	22	21	25	14	12
Costa Rica	22	24	34	35	16	13
Dominican Rep.	18	27	25	31	23	20
Ecuador	16	20	19	27	14	11
Mexico	51	47	91	109	56	47
Total	1,697	1,741	1,939	1,935	1,446	1,209
Average price						
U.S. cents per lb.	50	52	53	67	(38)	(32)

Source: International Financial Statistics, Pan American Coffee Bureau, Annual Statistics.

Note: Totals added before rounding. The prices used to compute the value of 1955/56 exportable production for the individual countries were derived by reducing each country's average price (unit value) for coffee exports in 1953 by 28 and, alternatively, 40 per cent. For the average of all exporters and incidentally also for Brazil, the export price in 1953 was 53 cents per lb; the reduction by 28 and 40 per cent on that price gives 38 and 32 cents per lb, respectively. The corresponding prices for the other countries used to compute the value of 1955/56 output are shown in Annex Table 1.

Let me have a list of 1955 (or 1954) bal p. deficits of these countries

*exportable
excluding stocks
that surplus
How much would consumption rise if prices reduced.*

As already indicated earlier the 1955 frost in Parana is expected to retard only temporarily the expansion of output anticipated for future seasons: production in 1956/57, according to a tentative forecast, may not exceed this season's level but a considerable rise is expected for 1957/58. *Total?* Exportable production in that year may reach or even exceed 40 million bags; the natural rise of demand taking population and income growth into account, may by then have raised demand (at 1953 prices) to some 34-34.5 million bags; thus by that time the gap will have risen to 5-6 million bags or some 15 per cent and a price decline considerably beyond the 28-40 per cent necessary to absorb the output expected for 1955/56 would be needed to absorb that expected for 1957/58.

Table 4. Estimated Exportable Production
1955/56 and 1957/58 by Main Regions
(million bags)

	Brazil	Colombia	Other Western Hemisphere	Rest of World	Total
1955/56	17.2	6.5	6.0	6.9	36.6
1957/58	18 - 20	7.0	6.5	7.5-8	39-41

Sources: 1955/56 Foreign Agricultural Circular, July 28 and August 16, 1955, supplemented by later information from USDA: 1957/58, estimate based mainly on total production forecast by Federal Trade Commission, Economic Report on the Investigation of Coffee Prices, July 30, 1954.

The forecasts for 1957/58, particularly for individual countries and regions, though indicating the future trend of coffee production to be expected, are yet too tentative to be used as a basis for further projections of price developments; this paper confines itself to give a rough indication on prospective earnings for the current (1955/56) exportable crop if prices would be allowed to find their level *if consumption will increase as calculated.*

It is not intended here to analyze the balance of payments implications of a reduction of coffee prices on the balance of payments of major exporting countries but a summary indication may be provided by relating the hypothetical decline in coffee earnings to total export receipts of the countries affected by the decline.

Since export earnings in 1954, the latest available full year, were exceptionally high for most of the countries, primarily as a result of the high coffee price in that year, it appeared unsuitable as a basis for these comparisons. We have therefore chosen the preceding two years -- 1952 and 1953; the computed values of exportable production in 1955/56 (see Table 3) have been deducted from actual average receipts in these two years; the "decline" was then compared with total earnings from all exports in these two years.

Taking average earnings for 1952 and 1953 has the advantage of ironing out year-to-year fluctuations in the value of coffee exports due to the two-year crop cycle which is quite pronounced in some countries. It also tends to reduce the effect of random fluctuations in earnings on both coffee and other exports. Moreover, for the group of countries as a whole exports over the two years probably came fairly close both in volume and in value to the present rate of consumption and exports. This makes the two years selected particularly suitable as a standard of comparison.

Export earnings on commodities other than coffee, for most countries, did not appear particularly high or low on the 1952/53 average.^{1/}

Table 5. Coffee Exports, Volume and Value, 1952-53 Average and Estimated 1955/56 ^{1/}
Main Latin American Exporters

Did these countries have hold more stocks than necessary for regular shipping?

	Exports 1952-53 Average (thousand bags)	Export-able Output 1955/56	Value of Exports 1952/53 Average	Value of 1955/56 Output at Prices Reduced from 1953 Average by 28% 40%		Decline from 1952-53 value: Col.(3) minus Col.(4) Col.(5)	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Brazil	15,691	17,200	1,063	860	722	203	341
Colombia	5,832	6,500	436	345	286	91	150
El Salvador	1,106	955	77	48	40	29	37
Guatemala	980	900	70	47	39	23	31
Haiti	457	480	30	23	19	7	11
Nicaragua	314	290	22	14	12	8	10
Costa Rica	411	300	29	16	13	13	16
Dominican Rep.	386	444	26	23	20	3	6
Ecuador	322	307	20	14	11	6	9
Mexico	1,138	1,200	68	56	47	12	21
Total	26,637	28,576	1,841	1,446	1,209	395	632

Sources: U.S. Department of Agriculture, Foreign Agricultural Circulars, July 26 and August 16, 1955; International Financial Statistics.

Note: Prices used in Col. 4 and Col. 5 taken from Table 3.

^{1/} Export data refer to average of calendar years 1952 and 1953, exportable output refers to crop year 1955/56.

^{1/} The only notable exception is the figures for Brazil. The almost complete cessation of cotton exports during 1952 and part of 1953 kept earnings for non-coffee exports in that period unusually low. This tends to exaggerate the effect of a decline in earnings from coffee measured against the total export value in these years. It appeared, however, that adjustment of that figure to correct for the low level of non-coffee exports (see Table 6, footnote 2 below) hardly changes the result based on the unadjusted data.

✓ effect on other countries of changes in rates in office
 Br + Col.

The sizable decline in the computed values compared to 1952-53 earnings (Cols. 6 and 7 of Table 5) reflect volume as well as price changes; as can be seen from Cols. 1 and 2 for five countries the decline in values is to some extent mitigated by a rise in volume; for five countries, however -- El Salvador, Guatemala, Nicaragua, Costa Rica and Ecuador, the value decline is accentuated by the lower volume of 1955/56 output. This is partly due to the fact that 1955/56 is the lower year in the two-year cycle; in addition Costa Rican production has been severely affected by drought and Guatemalan output has not yet recovered from the serious neglect of plantations in recent years. In order to exclude the effect of a temporary reduction in volume on estimated earnings the value at assumed 1955/56 prices for the five countries with lower 1955/56 output has been recomputed on the basis of their average export volume in 1952 and 1953 (Table 5, col. 1). For all further comparisons these values, shown in Table 5a have been used.

Table 5a. Value of Coffee Exports at Reduced Prices Based on 1952-53 Average Export Volume Compared with Actual 1952-53 Average Value (Million U.S. dollars)

	El Salvador	Guatemala	Nicaragua	Costa Rica	Ecuador
Value of exports					
1952-53 average	77	70	22	29	20
Value at prices reduced					
by 28%	55	51	15	21	14
by 40%	46	42	13	17	12
Decline from 1952-53 Value					
Row (1) - row (2)	22	19	7	8	6
Row (1) - row (3)	31	27	9	12	8

The reduction in earnings from coffee to a level ranging, for individual countries, between 20-40 per cent of the 1952-53 level, would obviously entail hardships to individual producers in all countries. For countries, however, which derive a major proportion of their total export receipts from coffee, a decline in the value of coffee exports to such a level would have serious effects on their entire economy. As shown in Table 6 which compares the decline in export receipts on coffee between 1952-53 average and 1955/56 with the 1952-53 value of total exports of the ten Latin American countries dependent for 10 to 87 per cent of their earnings on coffee exports, a decline in the latter by 20-40 per cent would tend to reduce total export receipts for the group as a whole by as much as 12-20 per cent, assuming that non-coffee receipts remained unchanged from 1952-53 average to 1955/56.

For which would it not

1/ Or, alternatively in countries where producers receive compensations under some equalization scheme, might cause a serious burden on the budget.

Table 6. Estimated Decline in Value of Coffee Exports Compared with Value of Total Exports (1952-53 Ave.) of Main Latin American Coffee Exporters

	Value of Total Exports 1952-53 Ave. million \$	Coffee as % of Total Exports in 1952-53 Average	Decline in Value ^{1/} of Coffee Exports		Decline as % of Value of Total Exports, 1952-53 Ave.	
			A	B	A	B
Brazil ^{2/}	1,474	71	203	341	14	23
Colombia	538	83	91	150	17	28
El Salvador	88	87	22	31	25	35
Guatemala	88	80	19	27	22	30
Haiti	45	66	7	11	16	20
Nicaragua	44	50	7	9	16	20
Costa Rica	76	38	8	12	10	16
Dominican Rep.	110	24	3	6	3	5
Ecuador	98	21	6	8	6	8
Mexico	558	10	12	21	2	4
	3,114	59	378	616	12	20

Sources: First two columns: International Financial Statistics, next two taken from Tables 5 and 5a.

- ^{1/} Columns A and B show decline in export value on the basis of prices 28% and 40%, respectively, below the 1953 level, see Columns 6 and 7 of Table 5 and last two rows of Table 5a.
- ^{2/} If in the case of Brazil, the value of 1952-53 average exports were raised to \$1,600 million so as to correct for the relatively low level of "other exports" in these two years, the per cent decline on account of reduced coffee prices would be 13 and 21.5 per cent instead of 14 and 23 per cent.

The five countries depending for two thirds or more of their foreign exchange earnings on coffee exports, would obviously suffer the heaviest loss. The decline in their coffee earnings between 1952-53 and 1955/56 would tend to reduce their total earnings by 14-25 per cent on assumption A as to 1955/56 prices, and by one fourth to one third on assumption B. For Brazil and Colombia and, to a lesser extent, for Haiti, the rise in the volume of coffee exports between 1952-53 and 1955/56 moderates the decline in export receipts; for Guatemala and El Salvador where no rise in the export volume over the 1952-53 average is expected and where the share of coffee in total exports amounts to four fifths or more, earnings would fall, on assumption B, by as much as 30-35 per cent.^{1/}

- ^{1/} Production estimates for 1957/58 based on the numbers and new plantings (see Federal Trade Commission, op. cit. p. 76) anticipate a moderate rise in Guatemalan and no change in El Salvador's output. It therefore would appear that these two countries will continue to bear the full brunt of any price decline for coffee with little or no offset through an increased volume of exports.

For two of the remaining five countries, Nicaragua and Costa Rica, with a fairly high dependence on coffee and no rise in coffee production assumed between 1952-53 and 1955/56, the decline in total export receipts would also be substantial. In the Dominican Republic, where coffee output has been rapidly increasing in recent years, the reduction in the country's total export receipts would be slight. The effect of the assumed 1955/56 prices on Ecuador's and, to a much higher degree, on Mexican total earnings, is mitigated by the lesser importance of coffee in the two countries' export trade.

Considering that none of the countries discussed above were in significant balance of payments surplus in the 1952-53 period, that the rise in coffee earnings since that time has induced most of them to raise their price levels and expand their imports, and that a normal expansion of import requirements on grounds of growth in population and output may in any case be assumed to have taken place between 1952-53 and 1955/56, it is clear that declines of export earnings of the order discussed above would be bound to create serious payments difficulties for most of the countries in question and to force them to curtail imports severely.

Practically all the countries concerned are engaged in development programs, some with the very purpose of diversifying their trade and reducing their dependence on one single crop. A large share of imports is devoted to the carrying out of these programs and the need to cut imports would seriously interfere with development activities and retard economic progress. These considerations should suffice to make clear the serious consequences of a sharp drop in earnings from coffee exports on the majority of producing countries.

b) Exporters outside the Western Hemisphere. Some 20 per cent of total coffee exports originate in areas outside the Western Hemisphere, largely Africa and to a lesser extent the Far East. For none of the Far Eastern coffee exporters -- Indonesia being the main source of supply in that region -- does coffee provide a major share of total export receipts; thus a decline in prices and earnings from coffee would not cause a significant decline of their total earnings. Most of Africa's coffee is produced by French, British, Portuguese and Belgian dependencies.

The only independent country outside the Western Hemisphere for which coffee provides a major source of export income -- 54 per cent of the 1952-53 average^{2/} -- is Ethiopia. Conditions in the country -- climate, altitude and soil -- have been found suitable for growing high quality coffee; planting has been encouraged and output has increased in recent years.

and coffee
1/ See Annex Table 2.

2/ All data for Ethiopia -- export as well as output -- refer to years ending September 10.

In 1952 and 1953 coffee exports, on the average, yielded U.S.\$28 million; the volume was 500,000 bags. The same volume is expected as exportable production for 1955/56, which, for Ethiopia is the low year of the cycle. If exported at prices reduced by 28 or 40 per cent, export receipts would amount to \$20 and \$16 million, respectively -- \$8-12 million less than earnings on coffee in 1952-53. The value of Ethiopia's total exports in that period came to \$52 million; the decline in earnings from coffee would entail a reduction of total 1952-53 export receipts by 15-24 per cent. The conclusions with respect to the future are similar to those for Latin American exporters -- a reduction in earnings from coffee of the magnitude indicated would seriously impair Ethiopia's payments position and income.

IV. Action to Achieve Greater Stability

Reduction of the dependence on coffee and greater diversification of the economies through the development of additional and, to some extent, alternative resources would obviously mitigate the ill effect of unstable coffee prices on the exchange income of exporting countries. Development programs which would further that end are under way in several countries; but diversification is a slow process and might be hampered if falling coffee prices reduce the ability to continue these programs. Even under the most favorable conditions, however, diversification can only be achieved in the longer run and cannot be considered as a solution for the pressing problem ahead.

Stabilization policies by individual countries aimed at maintaining both export prices and incomes of domestic producers have been pursued by Brazil for many decades; they have involved stockpiling by the Government over long periods, destruction of large quantities of coffee, export and planting controls, but their success -- at least as far as export prices are concerned -- was very short lived. In the late twenties prices were maintained for some time in spite of growing surpluses, but none of Brazil's efforts during the thirties could prevent the collapse and prolonged depression of prices. While output in Brazil gradually contracted under severe planting restrictions, production in other areas was expanded. Recent experiences -- the unsuccessful attempt to peg prices in the summer of 1954 which was followed by a sharp reduction in the country's exports -- were even less encouraging. The failure of Brazil's action was precipitated, no doubt, by her attempt to peg prices at their peak level. But quite apart from that mistake, individual action by a single country can never succeed as long as competing exporters expand their trade at its expense. This, however, is bound to happen unless all major producers take similar action.

1/ The long history of Brazilian coffee support schemes, carried out by the State of Sao Paulo and by the Brazilian Government has often been described. See e.g., Federal Trade Commission: Economic Report of the Investigation of Coffee Prices, 1954, p. 94 ff. For a more detailed description see Wickizer: The World Coffee Economy with Special Reference to Control Schemes, Food Research Institute, Stanford, 1943.

Problems solved temporarily by W.W.I and W.W.II

Various national price support schemes have also been in operation in other coffee exporting countries, primarily intended to reduce the impact of price fluctuations on the international market on domestic producers. With the exception of Colombia, however, each individual country has too small a share in total supply to appreciably affect, through national action, prices on the world market.

International action to stabilize coffee prices has been under consideration for some time. The Inter-American Economic and Social Council, at its conference in Rio de Janeiro late in 1954 has requested its Special Committee on Coffee to undertake a detailed study of the world coffee market and the prospects for the future, with special regard to the possibility of stabilizing the market through concerted action. A special subcommittee set up by the Coffee Committee has been charged with the preparation of that study; the study is under way but has not yet been completed.

In the late spring of 1955 the members of FEDECAME (Federation of Central American, Mexican and Caribbean Coffee Producers) in cooperation with Brazil and Colombia established the International Coffee Bureau with the task of devising, as a first step, a control scheme among Latin American producers; it should be open for later participation of African producers (and importing countries). The Coffee Bureau started by framing a regional agreement, based on export quotas. On the basis of estimated requirements for 1955/56 of 33 million bags provisional quotas were worked out; establishment of reserve stocks in the amount of some 3 million bags to be held by the Bureau would absorb excess supplies. Export quotas and contributions to the reserve stock were proposed as follows: (thousand bags)

	Brazil	Colombia	FEDECAME ^{1/}	Total Members	Not Allocated	World Total
Quotas 1955/56	15,350	5,650	5,250	26,250	6,750	33,000
Stock contribution	650	850	1,650	3,150	--	--
	16,000	6,500	6,900	29,400	--	--

The non-allocated quantity was left for non-Western Hemisphere exporters and should form the basis for their future quotas. The Bureau also suggested adoption of a price range and recommended immediate implementation of the scheme. It met, however, with opposition, particularly from Brazil; that country objected to the stock provision which made no allowance for the stocks accumulated in Brazil under the 1954/55 support program; it also did not favor minimum prices. Developments during the summer which lent temporary strength to the market were not conducive to changing Brazil's attitude; taking into account, in addition, the negative attitude of the United States the prospects of arriving at a regional control scheme did not appear favorable.^{2/} Discussions within the Coffee Bureau, however, were continued and the framework of a quota agreement is being worked out in considerable detail.

1/ Quotas for the individual FEDECAME members were not published.

2/ A recent statement by U.S. Assistant Secretary of State, H.F. Holland, to the effect that the United States could agree, in principle, with plans for an international coffee agreement has however, given encouragement to producing countries attempting to set up market controls. (New York Times, October 11, 1955).

*who should finance the Bureau
and contribute less than Colombia*

Meanwhile African producers met in Brussels on September 12 with the objective of setting up a Federation of African Producers which would facilitate cooperation with Latin America. Although the meeting ended without having achieved its goal, considerable progress was reported and it is hoped that establishment of a federation will be possible in the near future.

The meeting was held in Brussels on September 12, 1957. It was attended by representatives of African and Latin American producer organizations. The main objective of the meeting was to discuss the possibility of forming a Federation of African Producers which would facilitate cooperation with Latin America. The meeting ended without having achieved its goal, but considerable progress was reported. It is hoped that establishment of a federation will be possible in the near future.

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Item	Quantity	Value	Percentage
Wheat	100,000	10,000,000	10%
Cotton	50,000	5,000,000	5%
Other	50,000	5,000,000	5%
Total	200,000	20,000,000	20%

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ANNEX 1

Computation of world demand elasticity for coffee with respect to wholesale price, f.o.b. for green coffee.

Equation for E_p on average wholesale price, for green coffee, f.o.b.

$$E_p = \frac{e_1 \cdot q_1 + e_2 \cdot q_2 \cdot \frac{P_1}{P_2} + \dots + e_5 \cdot q_5 \cdot \frac{P_1}{P_5}}{q_1 + q_2 + \dots + q_5} \cdot \frac{P}{P_1}$$

- e_1 elasticity of U.S. demand with respect to retail price
- e_{2-e} elasticity of demand of European countries demand with respect to retail price
- P_1 U.S. retail price
- P_2 European retail prices
- q_1 quantity consumed in the United States
- q_2 quantities consumed (imported) by European countries
- P green coffee price; Santos No. 4 in Santos
- E_p "world" elasticity with respect to green coffee price (f.o.b.)

The data used in the two alternative computations, based on different elasticity assumption in the United States, are shown below:

	Elasticities:	Retail prices ^{1/} U.S. \$ per lb.	% of total imports ^{2/} used as weights
U.S.	e_1 -0.5, -0.27	P_1 0.89	q_1 62.0
France	e_2 -0.26	P_2 1.22	q_2 8.4
Germany	e_3 -1.3	P_3 2.00	q_3 4.8
Italy	e_4 -1.3	P_4 1.34	q_4 3.3
Belgium	e_5 -0.5	P_5 1.10	q_5 2.6
			81.1

The elasticities on the wholesale price derived from the two alternative computations are -0.287 (using $e_1 = -0.5$) and -0.183 (using $e_1 = -0.27$). On the basis of these elasticities the reduction of green coffee prices f.o.b. required to bring about a 10 per cent rise in consumption would have to be 28 or 40 per cent from the 1953 level.

^{1/} Average retail prices in 1953 except for Germany where the reduced price after the tax cut in August 1953 has been used.
^{2/} Based on imports in 1953 or 1954.

Annex Table 1. Computation of Coffee Prices
Reduced by 28 and 40 per cent from 1953 Level

	Exports of Coffee in 1953				Reduction by			
	Value	Volume	Unit Value		28%	40%	28%	40%
	Million \$	Thousand bags	\$ per bag	cents per lb.	\$ per bag		cents per lb.	
Brazil	1,088	15,562	70	53	50	42	38	32
Colombia	492	6,632	74	56	53	44	40	34
El Salvador	76.6	1,098	70	53	50	42	38	32
Guatemala	68.2	944	72	54.5	52	43	39	33
Haiti	25.0	372	67	50.5	48	40	36	30
Nicaragua	21.3	313	68	51	49	41	37	31
Costa Rica	33.6	469	71.5	54	52	43	39	32
Dominican Rep.	24.6	335	73	55	52.5	44	40	33
Ecuador	18.9	304	62	47	45	37	34	28
Mexico	91.2	1,406	65	49	47	39	35	29
	1,939.4	27,435	70	53	50	42	38	32
Ethiopia	33.2	617	54	41	39	32	30	25

The data used in the two alternative computations, based on different elasticity assumptions in the United States, are shown below:

U.S. \$ per lb. U.S. \$ per lb. U.S. \$ per lb.

U.S. France Germany Italy Belgium

The elasticities on the wholesale price derived from the two alternative computations are 0.287 (elasticity of -0.27). On the basis of these elasticities the reduction of green coffee prices is computed to bring about a 10 per cent rise in consumption would have to be 28 or 40 per cent from the 1953 level.

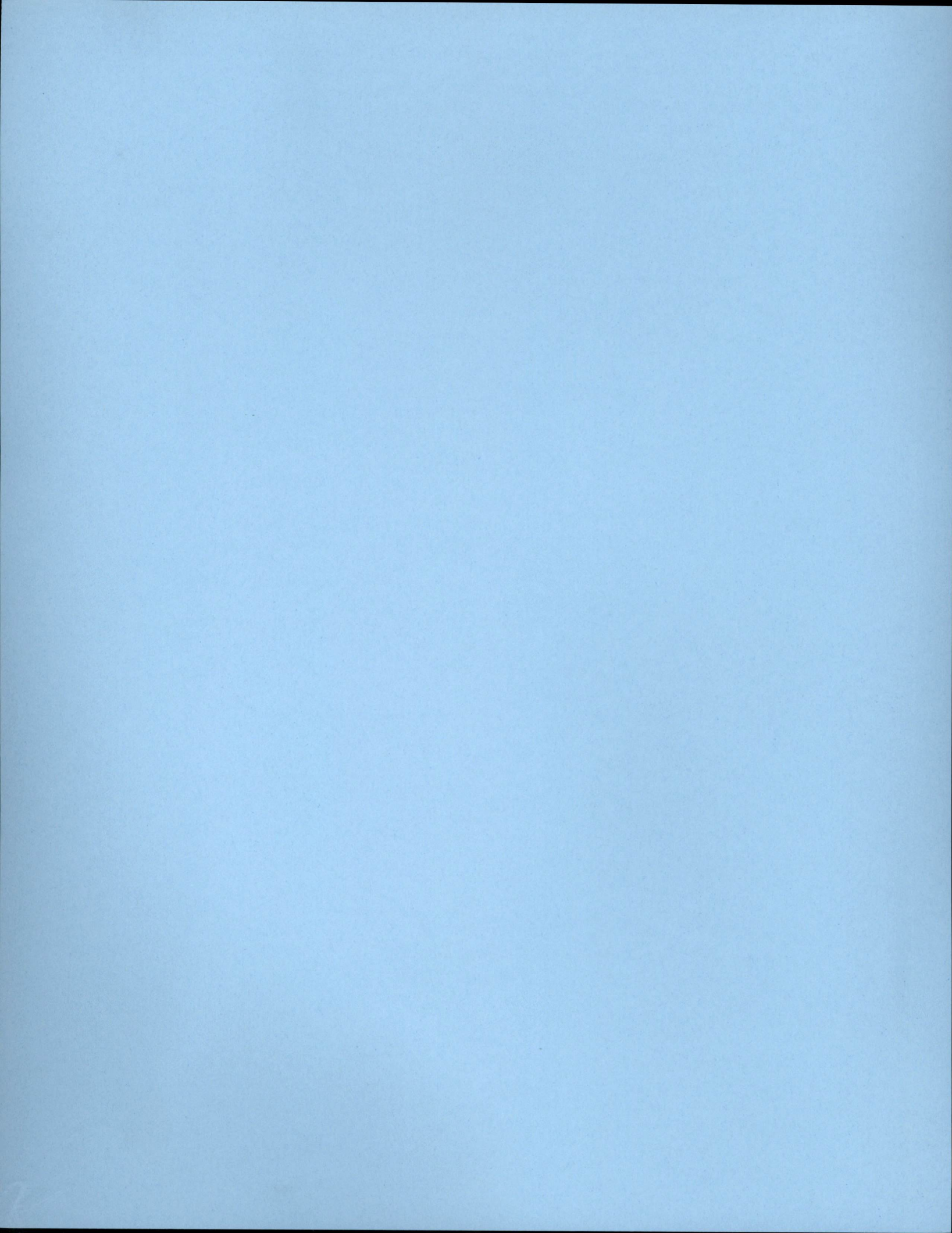
U.S. retail prices in 1953 except for Germany where the reduced price after the tax cut in 1954 has been used.

Based on imports in 1953 or 1954.

Annex Table 2
 Total Exports and Imports of Latin American Coffee Exporters
 Exports f.o.b., Imports c.i.f.
 (Million U.S. dollars)

	Brazil	Colombia	El Salvador	Guatemala	Haiti	Nicaragua	Costa Rica	Dominican Republic	Ecuador	Mexico
1951: Exports	1,757	463	85	84	51	37	63	119	71	573
Imports	2,011	419	63	81	44	35	56	86	62	822
Balance	<u>-254</u>	<u>+44</u>	<u>+22</u>	<u>+3</u>	<u>+7</u>	<u>+2</u>	<u>+7</u>	<u>+33</u>	<u>+9</u>	<u>-249</u>
1952: Exports	1,409	473	87	95	52	42	73	115	101	581
Imports	2,010	415	69	76	53	47	68	111	70	808
Balance	<u>-601</u>	<u>+58</u>	<u>+18</u>	<u>+19</u>	<u>-1</u>	<u>-5</u>	<u>+5</u>	<u>+4</u>	<u>+31</u>	<u>-227</u>
1953: Exports	1,539	596	88	108	38	46	80	105	88	536
Imports	1,319	547	72	80	44	51	74	99	76	807
Balance	<u>+220</u>	<u>-49</u>	<u>+16</u>	<u>+28</u>	<u>-6</u>	<u>-5</u>	<u>+6</u>	<u>+6</u>	<u>+12</u>	<u>-271</u>
1954: Exports	1,562	657	105	115	55	55	81	120	116	564
Imports	1,634	672	87	86	48	68	81	94	103	800
Balance	<u>-72</u>	<u>-15</u>	<u>+18</u>	<u>+29</u>	<u>+7</u>	<u>-13</u>	<u>--</u>	<u>+26</u>	<u>+13</u>	<u>-236</u>

Source: International Financial Statistics.



Reformed Criminals Aid Youth Give Advice to First Offenders

By Judith Crist

A novel experiment in having reformed criminals assist in the rehabilitation of first offenders is described in the annual report of Chief Justice Irving Ben Cooper of the Court of Special Sessions, made public yesterday.

Eight men and women once convicted of criminal charges, put on probation and now "responsible, well established and prosperous members of their several communities," met with twenty-seven teen-age offenders to tell them of their reactions and experiences from the time of their arrest until their probation ended, in all cases five years ago and to answer their questions. The session, arranged and conducted by Justice Cooper, was so successful that similar "classes," he said, will be held every three months.

His report is entitled "Generalized Irresponsibility," a malady from which, he said, the eight men and women suffered and which afflicts the "several thousand" youths who appear annually in Special Sessions. But the experiences of the eight, recounted by themselves and recorded in his report, show, he believes, that the court's probation is a valid instrument of

bation service, Justice Cooper noted, is caused by the "doubts, suspicions, antagonisms, moral insensibility and inertia" of new probationers. In an effort to overcome these, he invited the assistance of "satisfied consum-



Mr. Ivar Rooth

Room 935

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DM/55/21

INTERNATIONAL MONETARY FUND

Research and Statistics Department

Prospective Price Developments for Coffee
and Their Effect on the

Payments Position of Exporting Countries

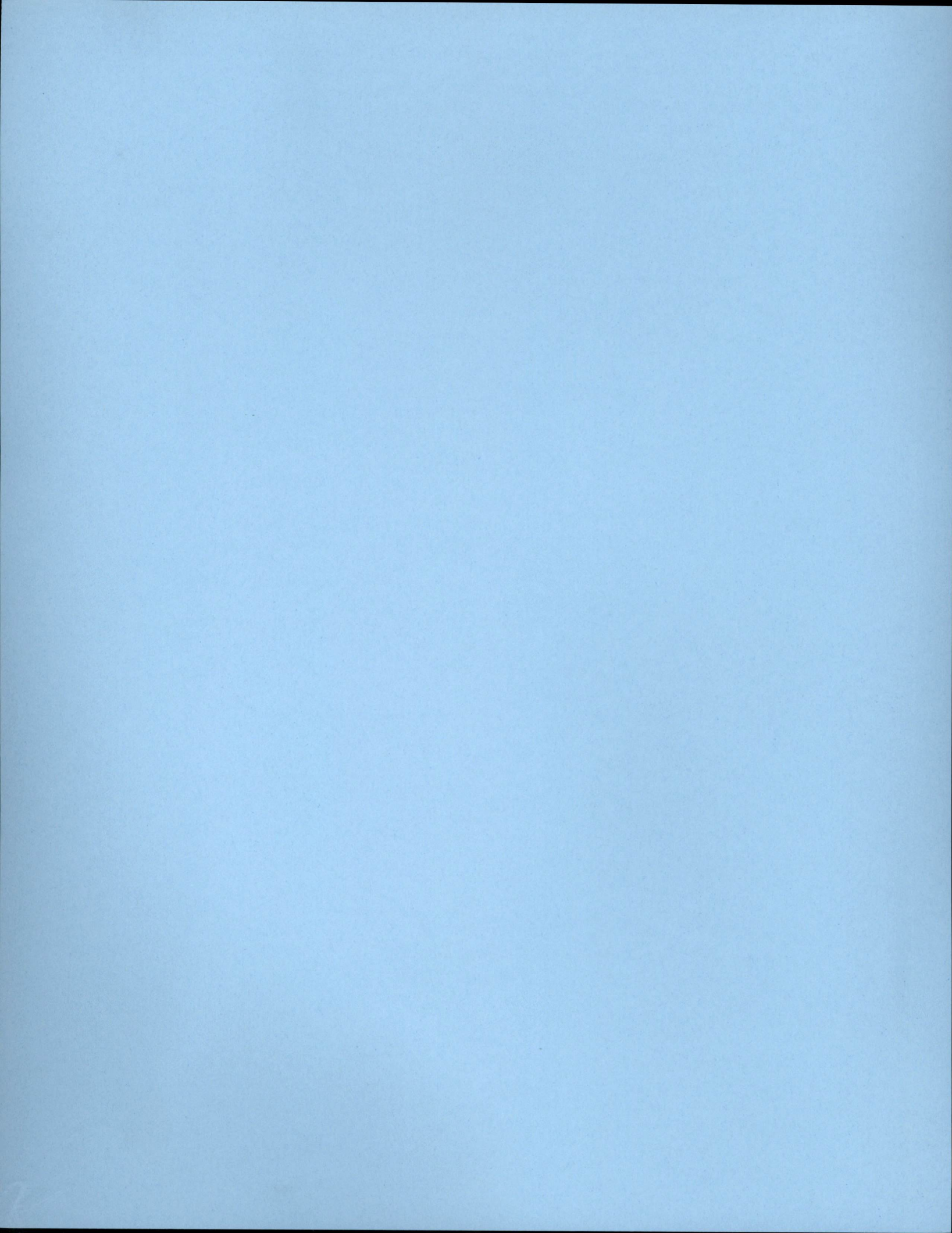
Prepared by: Gertrud Lovasy

Approved by: J. Marcus Fleming

October 24, 1955

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Mr. Ivar Rooth

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Annex 1

Annex Tables 1 and 2

Summary and Conclusions

The international coffee market, though displaying temporary strength appears likely to enter a protracted phase in which expanded production threatens to depress prices and earnings of coffee exporters. Prolonged periods of high supply and low prices after spells of very low supply and high prices have been familiar on the coffee market for many decades; they stem from the nature of the crop which prevents speedy adjustment of output to demand.

This paper, after briefly surveying past and present developments, attempts to estimate the level to which prices would have to fall in the near future in order to raise current demand to the level of current output. Based on output and consumption estimates for 1955/56 and taking account of the very feeble response of demand to price changes, it appears that prices would have to be lowered to some 30-40 per cent below the 1953 level in order to "clear the market". Prospects for the farther future imply still deeper declines in the price at which demand would balance output. In view of the large share of coffee in total export trade of many countries, mainly in Latin America, such a price decline would result in a serious deterioration in the export earnings and indeed in the total incomes of these countries. Concerted action to control the market is now under consideration with a view to avoiding such developments.

I. Developments on the International Coffee Market

1. Market developments in the past. Alternation of a few years of high prices and low supply followed by an extended period of high output and depressed prices has been a familiar phenomenon on the coffee market. This sequence is caused mainly by the slow reaction of production to price changes which, in turn, stems from the growing conditions of the coffee tree. It takes 4-5 years before a newly planted tree comes into bearing; during this period the possibility of expanding output in response to a price rise is limited to more intense utilization of existing trees and drawing on stocks. This, however, will frequently do no more than to alleviate a relative shortage and prices tend to remain high. Persistence of high prices for a period of 4-5 years, however, is almost bound to stimulate new planting beyond future demand. The lifetime of trees after they come into bearing is some 30-40 years, with output declining in the later part of the period. Thus excessive planting during the high price period will tend to result in high output for a decade or more, the length of the period depending largely on the age distribution of existing trees. Reduced care and abandonment of older plantations while prices decline or remain depressed, though reducing surplus production have not proved sufficient in the past, to bring production into line with demand. Market supply, as distinct from output, has frequently been reduced by stockpiling in producing areas, primarily Brazil, and during the thirties, by destruction of coffee.

1/ Relatively high or low prices: relative to long-run average, see Diagram 2.



Office Memorandum

file: Coffee

TO : Mr. Ivar Rooth
FROM : Jorge Del Canto *JSDC*
SUBJECT : Coffee and Latin America

DATE: June 29, 1955

At a meeting with Mr. Polak yesterday, I learned through Miss Lovasy of your interest on the effects of changes in coffee prices in the Latin American coffee countries and, accordingly, I am sending you a set of various country studies undertaken in our Department.

In October 1954--being aware of the significance of changes in the coffee situation upon our Latin American members--we set up a project in our Department attempting to measure the impact of these changes in Latin America. As a prelude to a commodity study, which we expected would be undertaken by the Research Department, I encouraged our staff to proceed with preliminary country analyses. This explains the country pieces I am attaching to this memo.

I understand the Research Department has been burdened with other assignments, and it is only now--at yesterday's meeting with Mr. Polak--that the Research Department will put Miss Lovasy to undertake the commodity study. Once such a study is completed we will undertake to rework our country pieces. I am afraid, however, that this 8-month delay in the commodity study might make the study obsolete, to the extent the Coffee Committee of the Pan American Union--with the aid of outside consultants--is about ready to release the study requested at the Rio Meeting of Ministers of Finance.

I thought you might be interested to know that we have been preoccupied with the seriousness of the changed coffee situation in Latin America all along.

Attachments



Office Memorandum

R

TO : Mr. J. Del Canto

DATE: 5/26/55

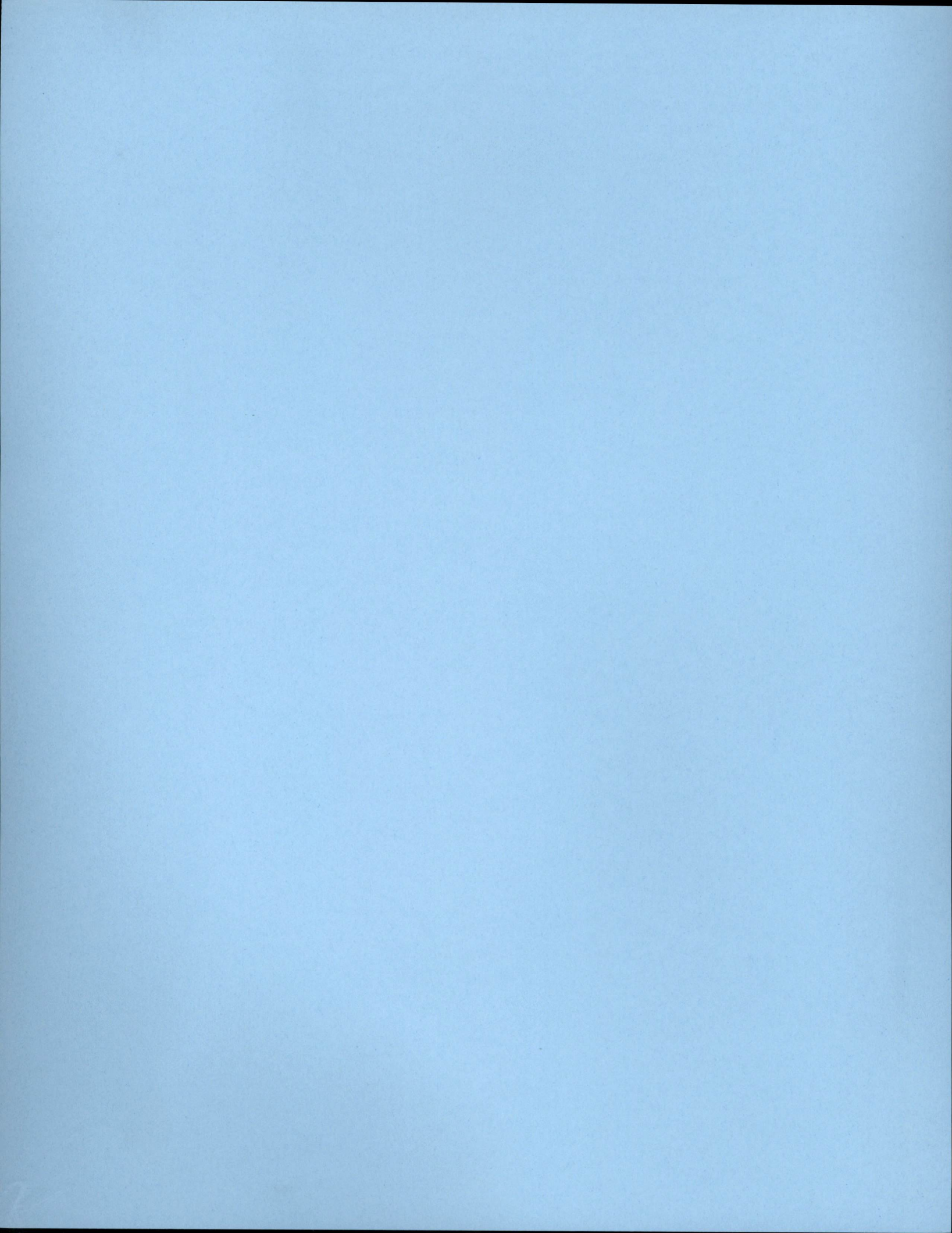
FROM : A. Foz *A. Foz*

SUBJECT : Volume of coffee exports and prevailing prices

In compliance with your request, the following is the latest information available on the volume of coffee exports and the prevailing prices.

During the period January 1, 1955-May 14, 1955, total coffee shipments amounted to 3,602 thousand bags, about one million bags less than during the same period in 1954, when 4,657 thousand bags were exported. However, it appears that lately coffee exports have been somewhat higher than in 1954. During the first two weeks of May Brazil exported a total of 328 thousand bags of coffee, of which 148 thousand bags were shipped to the United States. In the same period of 1954, 279 thousand bags were exported, of which 141 thousand were shipped to the United States.

Both spot and future coffee prices continued to decline during the second and third weeks of May. On May 19, 1955, spot prices for Santos 4's in New York were 53.50 cents per pound--a drop of 1.50 cents from the May 12 quotation and 15.5 cents lower than the 1955 high of 69.0 cents per pound price on February 7. On futures, March 56's were being quoted at 36.30 and May 56's at 35.45 cents per pound. These prices represent a drop of 85 cents from the prices prevailing on May 12.





Office Memorandum

R

TO : Mr. Del Canto

DATE: May 6, 1955

FROM : A. Foz and J. J. Thackara

SUBJECT: Brazil--Coffee measures, and the cotton and cocoa depreciation

Finance Minister Whitaker's order to the Coffee Institute to stop buying coffee of the present crop (1954-55 year ending June 30, 1955) is an important development in coffee policy. It is a step in the direction of eliminating the effective minimum price for coffee.

Up to now the exporter has had at least three alternatives in disposing of his coffee:

- (1) To sell it to the Coffee Institute on the basis of the minimum price of Cr\$20.32 per pound.
- (2) To carry his coffee under special credit facilities extended to them by Bank of Brazil, which was for 100 per cent of the value of the coffee, the Bank of Brazil agreeing to take the coffee in repayment of the loan. (The exporter absorbed the carrying charges.)
- (3) To sell his coffee abroad at the market price.

Big stocks at Santos

It appears that there never was a minimum surrender as such. The effectiveness of the internal minimum of Cr\$20.32 per pound was achieved by the Coffee Institute standing ready to buy at that minimum, and the Bank of Brazil standing ready to finance the entire value of the coffee.

What the next move will be is unknown. The Minister has the following alternatives, aimed at stimulating coffee exports:

- (1) To depreciate the coffee export rate. This would lower the dollar equivalent of the domestic minimum price.
- (2) To instruct the Bank of Brazil to give no further loans to coffee exporters on this year's crop. The price of coffee would then fluctuate freely since the effectiveness of the minimum would be eliminated.

At the present effective export rate for coffee of Cr\$37.06 per dollar the Brazilian minimum price of Cr\$20.32 per pound is the equivalent of 54.7 U.S. cents. The basic equation in the calculation of the U.S. dollar equivalent is the following:

$$\text{Cr}\$20.32 \text{ per pound} + \text{Cr}\$37.06 \text{ (exchange rate)} = 54.7 \text{ U.S. cents.}$$

Fairfax Parchment

Thus, if the exchange rate is depreciated, the dollar equivalent falls.

There are indications of possible exchange rate changes. The Journal of Commerce of May 5 published an A.P. cable from Brazil under the headline: "Devalue Brazil Cotton Export Cruzeiro." This report and an editorial in the same paper advises that cotton and cocoa exports were shifted from second to third categories. This shifting increases the export bonuses (which are paid in addition to the official Cr\$18.36 buying rate) from Cr\$18.70 and Cr\$17.19 to Cr\$24.70 and Cr\$22.95 for convertible or inconvertible currencies, respectively. It amounts to a depreciation of about 16 per cent.

This decision of the Brazilian authorities may perhaps be an isolated measure taken because of the very great political pressure of cotton and cocoa interests that has been developing since coffee was shifted into that category of exports. On the other hand, it may be the first of a series of important adjustments that the authorities feel compelled to undertake, as previously noted by the staff.

On April 28 the Minister of Finance, as reported by the press, ordered a "temporary" halt in the purchases of coffee by the Brazilian Coffee Institute. The details are still unknown. The Broadcast Bulletin of the Brazilian Embassy on May 2 transcribed excerpts from a speech on the subject by Deputy Herbert Levy before the Brazilian House of Representatives. The following points made by Mr. Levy in this speech were:

- (a) The Finance Minister, in order to avoid the need for new currency issues, had suspended the purchases of coffee by the Institute.
- (b) The Minister had instructed the Banco do Brasil that all the coffee of the present crop as well as of the future crop should continue to be financed on the same basis as at present, i.e., Cr\$2,000 per bag. (80 per cent of the minimum of Cr\$20.32 per bag. This is the financing primarily for producers as distinct from the special financing for exporters on a 100 per cent basis.) *to this continued*
- (c) That the Institute had purchased a total of 3.1 million bags of coffee, which represented the "excess over consumption" of the present crop, and that this amount, withdrawn from the market, was considered sufficient to re-establish the "statistical equilibrium" and to normalize the market.

When 20% for prod. or more for exports

58

From the data available, the situation would appear to be the following:

1. As previously mentioned, the purchase of coffee by the Institute, at the cruzeiro equivalent of 87 cents per pound (Cr\$20.32) was the factor that transformed the minimum price into an effective minimum export price. The halting of such purchases is, therefore, in the direction of abolishing the minimum export price.

2. Coffee exporters who in the past had decided to sell to the Institute instead of exporting because the international price, converted into cruzeiros, was lower than the Cr\$20.32 per pound which the Institute was ready to pay, are now faced with the prospect of either exporting, accumulating stocks, or delivering their coffee to the Bank of Brazil.

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3. Previous reports indicate that the Banco do Brasil was financing coffee up to "100 per cent,"^{1/} which would appear to mean an amount equal to the amount the Institute was ready to buy. Such financing would have been approximately Cr\$2,680.00 per bag (Cr\$20.32 x 132 pounds). Thus, coffee exporters who had decided not to export and who had chosen to hold their stocks for speculative purposes rather than sell to the Institute, made use of this special credit. The cost of holding those stocks--in the form of storage charges and interest--may have appeared rather small, compared with the cruzeiro profit that could be made either by a reaction of coffee prices or a devaluation of the coffee rate.

4. The coffee that has been financed in this way by now must have an "effective cost" which is much higher than the minimum of Cr\$20.32, due to the accumulated interest and storage expenses, and the cruzeiro equivalent of the present international price at the present effective export rate may not be enough to cover that "effective cost." This may be another reason why exporters continue to hold their stocks.

5. It seems that the coffee exporters' knowledge of the tremendous dollar shortage faced by Brazil and of their own great political power are factors which have contributed to encourage their hopes of forcing the Government to again depreciate the coffee rate or grant a moratorium in their indebtedness to the Banco do Brasil.

6. While it is not clear, it may be that the Minister's statement with regard to the continuation of the Cr\$2,000 financing (80 per cent of the minimum) portends the elimination of the special financing of exporters on a 100 per cent basis. If this were to occur then in fact the effectiveness of the minimum price disappears, in the sense of an export minimum.

7. On the other hand, it may be that very few exporters in Brazil still have coffee that has not yet been financed, or, in other words, the quantity of coffee of the present crop that would otherwise have been available to receive financing is rather small.

8. As for the new crop, the results would therefore be different if both measures are maintained.

9. In its drive to encourage coffee exports, the Government may have adopted these measures as preliminary steps. Since the only apparent result has been a further weakening of the international price, it seems that pressures to grant coffee a more favorable exchange rate must have increased. But it would have been almost impossible to grant coffee a rate of exchange more depreciated than the one granted for cotton and cocoa.

^{1/} This "100 per cent" financing appears to be a special treatment that was temporarily given to coffee exporters. The law of June 3, 1954, that established 87 U.S. cents as the basic price for financing and purchase by the Institute, provides for a financing (primarily for producers) up to 80 per cent of that minimum price, or about Cr\$2,060.00 per bag.

10. The experiment of having coffee, cotton, and cocoa in the same export category seems to have proven unsatisfactory. Furthermore, the authorities may have decided not to give coffee the full differential between the second and third categories, either because it would not be necessary in order to create a stimulus, or because of the possibility of too sharp a drop in the international price.

11. If the above assumptions (items 9 and 10) are correct, it would have been necessary to first adjust the cotton and cocoa position before making any change in the coffee rate.

In summary, the recent shifting of cotton and cocoa from second to third export category may have accomplished two purposes: First, it satisfied the requests of the cotton and cocoa interests; second, it paved the road for a possible adjustment in the coffee rate.

In the last two weeks coffee prices have tended to decline. There was an official report last week in Brazil that the carryover on June 30, 1955, would be 5.3 million bags and that the crop for the marketing year 1955-56 would be between 16 million and 17 million bags. This was followed the next day, on April 28, by the announcement that the Coffee Institute would stop buying coffee. Forward Brazilians continue at a heavy discount and the usually large premium on Colombians has continued.

Coffee Prices in the New York Market

(In U.S. cents per pound)

	Santos 4's		Colombians	Comments
	Spot	March 1956's		
1955				
April 25	57.75	41.99	63.50	
April 26	57.75	42.25	64.75	
April 27	57.25	40.25	63.50	Carryover of 5.3 in Brazil announced by Institute and a crop of 16-17 million bags next marketing year
April 28	57.25	38.50	63.00	Purchases of coffee halted in Brazil by Institute
April 29	56.75	37.14	61.50	
May 2	56.25	39.14	61.50	
May 3	56.00	39.85	63.00	
May 4	55.50	39.85	62.00	
May 5	55.00	37.85	61.50	

Shipments from Brazil increased during April as shown in the following table. Given the low level of stocks in the United States, the reduction in U.S. imports in the second half of 1954 and the availabilities in Brazil, a higher volume could have been expected.

Coffee Exports, 1955

(In thousands of bags)

Month	Week Ending	Total	To United States	To Europe	Other Countries	Total 1954
January	1/8/55	255	130	55	70	326
	1/15/55	205	79	124	2	250
	1/22/55	160	77	71	12	379
	1/29/55	<u>244</u>	<u>113</u>	<u>120</u>	<u>11</u>	<u>154</u>
		864	399	370	95	1,109
February	2/5/55	171	86	80	5	245
	2/12/55	104	46	37	21	147
	2/19/55	148	53	90	5	212
	2/26/55	<u>114</u>	<u>44</u>	<u>57</u>	<u>13</u>	<u>312</u>
		537	229	264	44	916
March	3/5/55	135	64	60	11	200 ^{1/}
	3/12/55	137	108	20	9	254
	3/19/55	268	116	144	18	332
	3/26/55	<u>162</u>	<u>78</u>	<u>72</u>	<u>12</u>	<u>321</u>
		702	366	296	40	1,107
April	4/2/55	230	140	80	10	327
	4/9/55	159	120	25	14	277
	4/16/55	306	187	117	2	220
	4/23/55	237	157	65	15	213
	4/30/55	<u>239</u>	<u>146</u>	<u>86</u>	<u>7</u>	<u>209</u>
		1,171	750	373	48	1,246
Total--January-April		3,274	1,744	1,303	227	4,378

^{1/} Estimated.

Source: Pan-American Coffee Bureau, New York, Coffee Market.

10 mill = 800 per month

about 1,000

808

818

11/5-55

I was expected to be

Coffee Prices, New York
(Cents per pound)

	<u>Brazilian</u> Santos 4	<u>Colombia</u> Manizales
1949 Jan/June	26.8	32.4
July/Dec.	36.7 x	42.5 x)
1950 Jan/June	47.8	49.3
July/Dec.	53.2	57.3
1951 Jan/June)	54.3	58.9
July/Dec)		
1952 Jan/June	54.1	56.9
July/Dec.	54.1	57.6
1953 Jan/June	55.6	56.5
July/Dec.	60.2 x)	63.1 x)
1954 I	78.1	80.8
II	86.5	85.9
III	78.5	79.3
IV	70.2	74.2
1955 Jan.	67.0	70.9
Feb.	58.2	60.5
March	58.0	59.3
April	••	••
May 4	55.5	62.0

I have been

Increase in last quarter of 1949 when accumulated bag. stocks sold and coffee in short supply for some 5 years. The higher prices stimulated production outside Brazil.

) At the end of 1953 believed that frost in Parana would keep quantity down for a couple of years

Average Prices Paid for Green Coffee by U.S. Importers at Foreign Ports and in the U. S. (cents per pound)

	1952				1953			
	I	II	III	IV	I	II	III	IV
At Foreign Ports	52.41	50.94	51.74	51.92	52.79	53.44	55.34	56.43
In the U.S.	52.94	51.03	52.43	53.37	53.61	54.51	56.93	59.63

Production for next few years will probably be much above consumption.

May 11, 1955

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2. At the end of 1953 it was believed that the frost in Parana would keep quantity down for a couple of years.
3. Production for next few years will probably be much above consumption.

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Exports of Green Coffee (Million bags)

	<u>1945/49</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>
Brazil	16.3	15.8	15.6	10.9
Colombia	5.4	5.0	6.6	5.8
Other Latin America	<u>4.3</u>	<u>5.7</u>	<u>6.5</u>	<u>5.6</u>
Total Latin America	26.0	26.5	28.7	22.3
Rest of world	<u>4.4</u>	<u>5.8</u>	<u>6.3</u>	<u>7.0</u>
Total	30.4	32.3	35.0	29.3

Dependence of Latin American Republics on Coffee Exports as Indicated by the Share of Coffee in their Total Exports: 1953

L.A.	Brazil	Colombia	Costa Rica	Dom. Rep.	Ecuador	El Salvador	Guatemala	Haiti	Mexico
25	68	83	42	24	21	86	82	66	12

Nicaragua

May 11, 1955

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