



OXFORD FARMING CONFERENCE 2017
The Frank Parkinson Trust Lecture

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Profiting from Sustainability – The Coffee Case Study
Konrad Brits – CEO Falcon Coffees Limited

Good morning.

Thank you Will and thank you, the OFC, for inviting me to speak with you this morning. My thanks also to the Frank Parkinson trust who sponsored this talk.

My name is Konrad. I am a businessman, I am also a husband and father and as you can probably tell by my accent, a South African.

I am the founder and CEO of Falcon Coffees. We are a green coffee trading company. This means we buy raw coffee beans from farmers in developing countries and sell the beans to coffee roasting companies in developed countries. We also undertake the logistics of moving the coffees from its place of origin to its place of final destination. This can be from the Congo in central Africa to Tokyo or Toronto.

Last year we spent \$95m buying around 24000 metric tons of coffee from farmers in 18 countries and then sold and shipped this coffee to 400 clients in 23 countries around the world.

The place that I occupy is the unseen middle. We act as the conduit, the bridge between coffee farmers and the companies that buy their coffees.

Before joining Falcon I worked in a small group of companies involved in coffee for a period of fifteen years. In 2008 I decided to break away and form my own business. I wanted to build a company with a dual purpose and that purpose was to make profit, but also to have a social impact agenda. This idea/decision was a very personal one that came out of a realization that dawned on me somewhere in my thirties.

As a white South African born in the sixties, I benefited from the system of Apartheid because of the color of my skin, at the oppression of my fellow South Africans, because of the color of their skin. I was conscripted into the South African army in my late teens and became an infantry officer, deployed on northern Namibia on the southern Angolan border, where a civil war raged for 27 years. Another proxy war of the Cold War era. It was through this experience that I came to recognize the gross social injustice that was taking place in my country. In subsequent years it has been difficult for me to reconcile why it took me so long to notice. It was as if my moral compass was broken.

I reached a point in my coffee career where I realised that I made my money trading with some very poor people and that if I did not take some responsibility as to their plight, I could find myself guilty of the same thing twice. Apathy and indifference in the face of other people's suffering. This time through poverty. The dual purpose of Falcon means that I have tended to approach my work with a different perspective, affording me a different view. It has had a big influence on my life, personally and professionally. At times, it has been disastrous, but it has also been very rewarding and I think that is one of the reasons I am speaking with you today.

In the last twenty-four years, coffee has taken me to 42 countries around the world. I have met a broad range of people from different cultures and different backgrounds. What I have come to realize is that we share in the same hopes and aspirations - the same needs for security, dignity, justice and belonging. But what we don't share in is equal access to resources. We don't share equal access to healthcare, education and credit. In commercial relationships, when people are negotiating with one another, your resource pool heavily influences the shape of that negotiation. This is particularly true in agricultural supply chains.

Powerful retailers, in pursuit of market share and profit, may seek to drive down costs by putting price pressure on front line suppliers. Those suppliers turn around and apply the pressure back down the supply chain. Eventually the pressure arrives at the person who provides the raw material: the farmer. Those farmers are often very far away, they are not very visible and they have the least amount of resource and negotiating ability. So the unintended consequence can be that they are forced to engage in socially and environmentally damaging practices to absorb this cost pressure and keep their heads above water.

There appears to be a strong disconnect between retail market forces and the real costs of ethical and sustainable farming. This is easy to see for smallholder farmers in developing countries. It is sometimes harder to grasp when you have a supply chain which is domiciled inside a developed market economy, like the UK, where even subtle shift in interest rates, energy prices or exchange rates can take a farm from viable to loss-making in a very short period of time.

While coffee farming as a tropical crop and may seem far away from British farming, there is relevance and perhaps lessons to share as we all face the growing tension of economic austerity, diminishing resources and the pressure to constantly raise standards.

There is a conversation currently taking place in the global coffee industry about defining and acting on sustainable future. As the evidence grows that we all will need to change the way we acquire, consume and discard, it is a conversation that every single industry will need to have at some point in the future.

So, what is coffee's story? Why does the coffee industry feel ahead in this conversation? How is the conversation playing out in the market place and in the supply chains to farmer level?

To answer these questions, I would like to share a sequence of events in my coffee career that have influenced and shaped my conviction of what Falcon, as a business, needs to look like and do to capitalize on the opportunities that come with enormous upheaval of the old ways and an unclear path to the future. What we need to do to survive and thrive.

I began my coffee career in the early nineties, living and working in Africa. The company I worked for at the time was focused almost exclusively in Zimbabwe, which had a small but thriving coffee community and we, at one point, handled over 90% of their coffee crop production. Then, in 1999, Robert Mugabe, having lost a referendum, began confiscating white-owned farms. Zimbabwe's economy was predominantly agriculture and tourism and, within that, 95% of agriculture production came from white-owned farms. The economy imploded and with it coffee imploded. In 2 years, we lost our main income source. We packed up and left.

Seeing the writing on the wall, I began working in Zambia, a land-locked country with a small, but thriving coffee community. Zambia is, in terms of resource, an incredibly rich country - it has a vast amount of arable land, around 7% under cultivation and it is copper-rich with one of the largest copper veins in the world. But after beginning work in the coffee community there, a number of things took place

simultaneously. During the commodities super-cycle in the early 2000's, copper prices recovered and rose to levels not seen since the Vietnam War when copper was in demand for ammunition. At the same time the Zambian Kwacha valued against the dollar, oil prices drove up transport and agri-chemicals costs and then the Zambian government increased the minimum wage by 30%. This all came at a time when the world price of coffee was extremely low. In a very short space of time, this perfect storm drove coffee farmers to uproot their labour intensive, price volatile coffee trees for annual cash-crops that they could mechanize. So for the second time, my supply base again disappeared so we packed up and left.

USAID invited me to work on a program to rejuvenate the coffee industry in Angola in south west Africa. Angola was oil-rich in the North so very much a single tier economy. 50% of the population had moved into slums in the capital city and aid organizations wanted to disperse these communities back into the countryside to get them growing food and hard currency exports. Until the early seventies, Angola was one of the world's largest coffee producing countries. The 27-year civil war that I had played a small part in had abruptly ended that.

After building a small export operation over a period of two years, we soon realized the overhead costs were atrocious. As a country with infrastructure that had been utterly ravaged by war, a country that manufactures and produces nothing and is a net importer of all things, and when the only economic activity is in the oil industry, the cost of running a startup operation was incredibly high. With a burdensome overhead and a very limited export volume of coffee as a start-up, coupled with a world-price of coffee that capped the ceiling that we could sell this coffee for, the only way we could pay for those overheads, on that low volume of coffee, was to place downward pressure on the farmer. We had to drive down prices to the farmers to below sustainable levels, so really the point of the business was self-defeating. The point had been social impact through a for-profit business, but we were actually gauging the farmers in order to pay our bills. We shut the operation down.

While in Angola, I received an invitation to set up a coffee operation in western Democratic Republic of Congo. In hindsight, I realize that sometimes optimism and stupidity run side by side.

The Congo is famous for its eastern side; for the gorillas, the war, the volcanoes and all the mineral wealth – the metal, Coltan, makes your mobile phones. I was working in the western Congo, near the Congo River mouth, which had not seen any foreign direct investment since the sixties. This area was an indigenous home to the coffee shrub and we were urged to invest by local government and business people, working in collusion. Over two years we bought land, built a warehouse, a coffee mill and imported machinery from Brazil. I took some of my Zimbabwe farmers that had lost their farms and put them into the Congo to run the operation and bring their skills and experience. We were selling, we were exporting and we had revenue, but once we had invested and invested and invested, suddenly the noose begun to tighten. A conspiracy materialized by everybody Congolese – from the government, to the export department, to my own staff. Suddenly it became impossible to get our hard currency out. The government stamps we needed to export our coffee begun to get more and more expensive, our staff started stealing our coffee through the back door and running around to the front door to sell it back to us. Eventually, we took all our tools, our 250 kVA generators and Mercedes Benz trucks, and locked them away in that warehouse (I am still a land owner in the Congo) and left, shutting down that operation with a loss of \$1.3m.

These repeated failures took me to a very dark place. I was questioning this idea of social impact side-by-side with a for-profit business as well as my own skills as a businessperson. What I learned through all this was that good intentions and a moral high ground are not enough to see you through. You still need to chop wood and carry water. While you dream big, you really need to work small.

Then I read a book by the economist Paul Collier, called the Bottom Billion, published in 2007. In this book, Mr. Collier suggests that the 6 billion of us rising out of poverty are responsible for the 1 billion falling into the abyss of worsening poverty. He puts forward the idea that when you remove people's hope and dignity, the moral fabric of society begins to decay, leading to extremism, radicalization and you give birth to rogue states, citing Somalia as an example. We can probably think of a few more to add to that list today.

The piece that caught my attention was his list of the four poverty traps that identify the states where the bottom billion reside.

1. Poor governance – this is self explanatory
2. In conflict / post conflict – the impact of war, or war in recent past.
3. Land-locked with poor neighbors – the idea being that you do not have a sea port meaning your trade partners are your immediate neighbors. If your neighbors are poor, you are going to struggle to build your economy.
4. The Mineral Wealth Trap – this may seem counter intuitive, but the idea being that, when you have a country with mineral wealth, it tends to be controlled by very few, and not with the greater good of the general population. The economy does not diversify and very often conflict comes in close behind the pursuit of that wealth.

All four of my operating countries fell into at least two of these traps. What I realised was that, although I'd certainly done some things wrong and made some bad decisions, there was something bigger playing out here. None of us exist in a bubble of existence; you don't operate in your sphere of influence anymore. We are all buffeted by world events and circumstances beyond your control and your ability to survive and to continue is going to be about anticipating those, being willing to change and sometimes being willing to abandon what you're doing and walk away, as hard as that may be.

I then took a further step back and looked at these four poverty traps in the light of the world map of coffee-producing countries.

I started with Peru and the Shining Path, Colombia and the FARC, Bolivia has had nearly 200 coups in its 200 years of independence, nearly one per year. Civil war in Nicaragua, El Salvador, Honduras and Guatemala. Narco trafficking in Mexico. Over to Africa. Genocide in Rwanda, the Derg in Ethiopia, ethnic cleansing in Kenya, Idi Amin in Uganda, war in Congo, Angola and Zimbabwe. Over to Asia and again conflict and poor governance in Laos, Vietnam, Cambodia, Indonesia and Thailand.

The majority of countries that house the coffee farmers fall into these poverty traps. When taking a closer look at the socio-economic profile of the coffee farmers themselves, between 50-70% of the world's coffee is produced by 30 million smallholder farmers across 50 of the world's poorest countries. 21 of these countries feature in the bottom 30 of the World Bank's list of countries by economic wealth (by purchase parity and GDP). Of the IMF's list of 40 Highly Indebted Poor Countries - countries with low levels of development, high levels of poverty, high levels of debt - 25 produce coffee. What this means is the base of the matrix that makes up my industry relies upon tens of millions of farmers, who are highly vulnerable through lack of personal security, food security, lack of education, access to healthcare and to markets.

On the flipside is our \$100 billion retail coffee industry that has a compound growth rate of 2% every year. The coffee industry is thriving - take Asia, populous with areas of very low per capita consumption and decades and decades of growth ahead. We have shrugged off the recession of 2008 - everybody here will be aware of the success of the high-street coffee shop. With decades of growth and developing markets ahead of us, the burning question being contemplated in our industry is, "Where will the raw material come from to feed this growth?"

The result of this question being asked by more and more people, is the creation of a paradigm shift. This shift being that altruism, the caring for the welfare of others, (in this case smallholder coffee farmers), is not about philanthropy; not about social justice. It is about the bottom line. And the bottom line is the universal language that every single business speaks. As a coffee industry, we recognize that we have to invest in the quality of life of the millions of people that we rely on for our industry today and tomorrow. We need to provide hope and dignity for those people. Hope that coffee and farming is a means to improve the quality of their lives, and the dignity to know that we, the people who engage with them, will treat them as equals. This is an enormous problem when you think of the numbers and the geography.

So how do you eat this whale? The way you eat any whale. One bite at a time. We have taken a few nibbles, but recently a bigger bite was taken. The credit doesn't belong to Falcon, but to our sister company, Rwanda Trading Company. Rwanda, the pearl of Africa, is a tiny, land-locked east African country, which has no mineral wealth and is the most densely populated country on the continent next to Malawi. 20% of the largely subsistence farming population are directly involved in coffee production.

Rwanda Trading Company, based in Kigali, buys coffee from around 60,000 subsistence farmers across the country, grades it and exports it. In an effort to improve the lives and economic prosperity of its farmer partners, Rwanda Trading Company has designed and deployed an agribusiness-training program. They looked at their farmers and thought about how they could improve their productivity and efficiency. The philosophy behind the program is that your farm is your business, there are usually two business owners – husband and wife – and they are probably the labor force as well. The program was focused on agronomy training, so increasing yield and efficiency, as well as financial literacy – how do you use that little resource you have and deploy it to best effect your business. It is a 20 module, two-year training program for both the husband and wife to attend. The initial pilot was with 6000 farmers. After completing the program, we tracked the data using fairly basic technology and found the annual average yield increase was 155%. We didn't measure their food crops, but the agronomy training will have most likely played into food security of other crops too. The household income (average across all households) from coffee was up 61%, despite this being the year that the global coffee market lost 15% of its value. Currently, the program has extended to enroll 24,000 farmers across Rwanda and Tanzania and we are moving the program to western Uganda in the Ruwenzori Mountains on the Congo border. The exciting part is that the increase in yield meant an increase in volume, which meant an increase in revenue and profitability. By year three, the initial costs related to the training of those 6000 farmers were recovered. This is Zero Cost Sustainability.

Other initiatives we are involved with include working with farmers in the Bill and Melinda Gates Foundation in Ethiopia. World Coffee Research, which is a non-profit seeking to breed climate change resistant varieties without turning to GMO. We are seed funders of the Program for Gender Equity. 46% of the labour force in smallholder agriculture in developing countries are women. To not address gender inequality, is to exclude half the people involved. We are involved in a Bio Char project in Peru and are building community supply chains in Nicaragua. In Congo, we work alongside Ben Afleck's East Congo Initiative and Starbucks, tripling the income of 4200 households in one of the most war-torn regions on earth.

These are great banners to fly and great stories to tell, but it is tough going. There are a lot of companies out there who profess to embrace sustainability, but are unwilling to make the initial investment or struggle to change their culture and remain focused purely on price. There is still a lot of box ticking and green washing going on out there. It is not easy – I sometimes feel like Sisyphus pushing my rock up the hill only for it to fall back down again. We still have to pay the bills. We still have to buy and sell coffee and make a margin in between.

The winds of change are beginning to blow in our favour. We see a market coming towards us as more and more roasting companies adopt ethical sourcing standards and look to companies like ours to help them figure out credible sourcing policies that protect them legally, meet their clients demands, are cost competitive and feed their brand equity.

We are working hard to become better communicators. Using social media to tell our story, build our brand and to place us in communities with shared values. Inside and outside of coffee. Story telling about who we are, what we do, why we do it and who with, is a vital part of educating our clients and their clients; the consumers. We can say to our clients 'if you buy your coffee through us, then you become part of this supply chain, the impact of these programs become yours'.

This paradigm shift of altruism moving to the bottom line has really changed the culture inside Falcon. We have come to realize that our story is the story of our farmers. The threats and challenges to our farmers are our threats. We have to be collaborators. The only way for our supply chain to survive is if everybody in those supply chains is profitable.

What is driving this cultural revolution is what I call the very first building block of all ethical and sustainable initiatives. The one common thing. Traceability. In order to undertake any ethical, sustainable initiative, you must be able to trace the origins of your product.

When you roll back supply chains and get rid of the smoke and mirrors, you eventually come across people. Communities. When you connect your products to the people that produce them, you de-commoditise that product. This is actually quite profound, as its journey to you becomes a very human story. That influences its intrinsic value.

This plays into the rising groundswell of community, local produce, local economies. People want to source locally and want to feel that the choices they make as consumers support ethical behavior. This represents both a moral obligation and a marketing opportunity. These conversations are springing up in communities all over the world.

My personal experience as a UK consumer is in stark contrast to this. I went down to my local superstore where I purchase my family food and I bought products under a British farm label. I was pleased, because I am keen to reduce my carbon footprint and support British farmers. Some weeks later I heard that the farm names were made up. Fictitious. Created in the marketing department. In fact, the products inside most likely were not even British.

I felt duped and foolish. Had. They pitched right into that sweet spot of my conscience, for their own financial gain. I felt that they had intentionally stopped me from supporting British farmers, pocketing the difference I trusted them to pass back to you. My response was to vote with my wallet. I began to shop elsewhere.

Millennials, the generation that live very comfortably in the world of social media and digital space, that control a growing percentage of disposable income, are less gullible than me. If you don't walk your talk and do what you claim to do, you will be sniffed out, uncovered and vilified in the very public arena of social media and no company is likely to survive that.

The movement towards ethical sourcing and sustainability is not going to stop or turn. It is only going to intensify and grow in momentum. To avoid participating, to refuse to build it into the DNA of your business, is to commit a form of delayed commercial suicide.

Do I believe we in coffee have cracked the code to sustainability? No. We are not even close. While I am excited about all that is happening in coffee, and believe we are advanced in recognizing the size of the problem, I am not sure our industry will survive in its current healthy state. So when people ask me where I see the growth of Falcon, I answer, with diversification. We need to mitigate risk by diversifying our skills into other crops. We are under pressure from urbanization, climate change, a very old farming population and food crop pressure. I am unsure of the future of coffee. I like what we are doing, I am excited about it, I am bought in and I will definitely participate, but I believe we will have to diversify to survive.

While much of the global discussion around ethics and sustainability is centered on action, what is key is a change in culture. We are in a free market economy, everybody has to fend for themselves, they have to cover their patch and make what they can. But when you have two people at the negotiating table and one of them has a significantly different resource pool, the relationship becomes quite predatory; it is not a fair fight. We need to move from a highly competitive buy low / sell high business model to one more nurturing. One where we recognize the people behind the commodity and the need for everyone in the supply chain to be viable - socially, environmentally and economically.

At the beginning of my talk, I mentioned that I was a husband and a father. The reason I did this was because I feel that when we sometimes step into our business persona, we abandon some of our softer values that we have in our relationships, with our families and friends, and in our communities. I believe we need to bring these softer values back into the work place.

My wife and I frequently discuss the world we will leave behind for our children. The outlook is bleak. The news and statistics that permeate our lives feel almost biblical in their foretelling of doom. Melting ice caps, acidifying oceans, the extinction and extraction of raw materials and poor leadership. At times, I have felt despondent. Our twenty something-year-olds are angry, angry about the legacy that they can see, and our nine-year-old is anxious. She looks on YouTube for nature programs and finds stories of the ecocide being perpetrated on our fauna and flora. I have decided that I have an obligation to remain optimistic, come what may, to give them hope. Despondency and despair lead to inertia in a time where we need change. The greatest place that I, as a global citizen, can enact change is through my work. Business is the greatest extractor of natural resources, the greatest consumer of energy for manufacture and distribution and the greatest generator of waste. It therefore stands to reason that business holds the key to building a sustainable future.

If we recognize that farmers around the world are stewards of the land, of our natural resources, then through our relationship with them, as business people and consumers, we share the responsibility of that stewardship.

Thank you.

Konrad Brits

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