

Grinding Poverty?

Coffee and the Development Challenges for East Timor



Dry-processing coffee in Ermera, July 2001

by Ben Moxham
Student Number 37169
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Department of Political Science, University of Melbourne,
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Abbreviations

CCO	Cooperativa Cafe Organica
CCT	Cooperativa Cafe Timor
CNRT	National Council for Timorese Resistance
ETTA	East Timor Transitional Administration
FAO	Food and Agriculture Organisation
FRETILIN	Frente Revolucionario Timor Leste Nationale (Revolutionary Front for an Independent East Timor)
GCC	Global Commodity Chain
IMF	International Monetary Fund
NC	National Council
NCBA	National Cooperative Business Association
PUSKUD	Pusat Koperasi Unit Desa (East Timor Federation of Cooperatives)
SAPT	Sociedade Agricola Patria e Trabalho
TERADP	Timor Emergency Rehabilitation And Development Program
TNC	Transnational Corporation
UDT	Democratic Union of Timor
UNTAET	United Nations Transitional Administration in East Timor
USAID	United States Assistance in Development
ICO	International Coffee Organisation
ICA	International Coffee Agreement
UNCTAD	United Nations Commission of Trade and Development
NCBA	National Cooperative Business Association
NIEO	New International Economic Order
ACPC	Association of Coffee Producing Countries

NB: All currencies are in US Dollars unless otherwise referred to.

Introduction

East Timor's vote for independence during the August 30th, 1999 referendum marks a critical juncture in the nation's tumultuous history. It leaves behind a brutal 25 year Indonesian military occupation that it staunchly resisted under a national unity built on the demands of self-determination. The future presents a radically different challenge. As a small, underdeveloped and war-torn country in an era where national sovereignty is being rolled back by an increasingly integrated and dynamic global market, it must develop robust social, political and economic institutions to deliver on the promises of a post-independence articulation of self-determination. Specifically, this thesis examines and analyses the role the coffee industry will play in East Timor's development. As the country's principal export earner until the Timor gap oil comes on line, it is a crucial source of income for an estimated 44,000 farming families or 25% of the population and also employs thousands of seasonal workers.¹ It is therefore the central way many East Timorese have and will come into contact with an undiscerning global economy. How that contact should be mediated is the subject of this thesis.

East Timor's unique decolonisation process casts a shadow over any discussion of national development. From referendum to transitional administration to early independence, it has been almost entirely supervised by powerful international institutions. The United Nations Transitional Administration in East Timor

(UNTAET), the body overseeing the two-year transition to independence, effectively has the powers of a 'pre-constitutional monarch in a sovereign kingdom'.² Since the reconstruction period began, in the wake of the post-referendum militia led rampage, both the International Monetary Fund (IMF) and World Bank have the job of 'building the foundations of the fledgling country's economy', which 'will probably be designed and built by a clique of Washington-based economists and development planners'.³ Much of the macroeconomic infrastructure of the country has already been planned without any popular consultation. For the coffee industry, the entire body of primary research for this thesis was completed before the recent inaugural elections, yet among elites, a clear policy direction has already emerged.

According to Michael Casey from the *Asia Wall Street Journal*, 'This tiny devastated former Portuguese colony is to become an important testing ground for the World Bank, the IMF and a group of wealthy donor countries.'⁴ But a testing ground for what? It will be a testing ground for the policies of market liberalisation prescribed by the Bretton Woods institutions that have sparked off so much debate and protest in recent years. To grossly paraphrase the East Timorese NGO *La'õ Hamutuk*, East Timor may be a lab rat drip fed on neo-liberal management?⁵

¹Jacqueline Pomeroy, 'Coffee and the Economy in East Timor', in Hill, Hal and Saldanha, Joao, *East Timor: Development Challenges for the World's Newest Nation* Institute for Southeast Asian Studies, Singapore, 2001, p. 126

²Jarat Chopra, 'The UN's Kingdom of East Timor', *Survival*, Vol. 42 No. 3 Autumn 2000, p. 28

³Michael Casey, 'New Economy has Meaning in East Timor', *Asia Wall Street Journal*, 7 October 1999.

⁴*Ibid.*

⁵'The World Bank in East Timor', *The La'õ Hamutuk Bulletin*, Vol. 1, No. 4, 31 December 2000

Most of the development literature written on East Timor roughly fits into this mold. So much so that it worth considering the words of the US Academic, Fredric Jameson who considers the way proponents of corporate-led globalisation attempt to control the terms and rules of debate:

‘Discursive struggle (as opposed to outright ideological conflict) succeeds by way of discrediting its alternatives and rendering unmentionable a whole series of thematic topics. It appeals to trivialisation, naivete, material interest, ‘experience’, political fear and historical lesson, as the ‘grounds’ for decisively delegitimising such formerly serious possibilities as nationalisation, regulation, deficit spending, Keynesianism, planning, protection of national industries, the security net, and ultimately the welfare state itself.’⁶

Much of this struggle is achieved by labeling the debates in development as either of state vs market control or ‘inward-’ vs ‘outward-looking’ economies. Several authors have pointed out that Timor should adopt an ‘outward looking’ or free market perspective to mimic the development success of the four Asian ‘Tigers’. Hal Hill for example, presents Timor’s policy options as a choice between an outward-looking South East Asian model or an inward-looking South Pacific model.⁷ The former developed a robust economy, while the latter is a stagnant backwater. Similarly, Wolfgang Kasper suggests that Timor should avoid the history of corrupt African

⁶Jameson, Fredric, ‘Five Actually Existing Theses on Marxism’, in Hardt, Michael and Kathi Weeks *The Jameson Reader*, Blackwell Publishers, Oxford, 2000, p. 166.

⁷Hal Hill, ‘East Timor’s Future: South East Asian or South Pacific?’, *Southeast Asian Affairs 200,1* Institute for Southeast Asia Studies, Singapore, 2001, pp. 82-92;

regimes and their structuralist policies and, instead, follow the success of Singapore's open economy.⁸

The reality of East Asian development is far more complex and indeed, marks a blossoming of debate in development theory.⁹ The rise of the 'developmentalist state' – strategic state intervention that forced investment decisions to conform with national priorities – led many writers within the neoclassical tradition, for example, to admit that state interventions in East Asian economies were not merely 'market conforming' but rather 'market guiding', even deliberately 'market distorting'.¹⁰

Singapore for example, had much of its social and physical structure built as Britain developed it into a colonial metropole.¹¹ Its subsequent development strategy employed heavy state intervention in the economy; very selective financial instruments, trade policies, inward investment to support domestic industry and tight control over industrial relations to build an effective infrastructure that was then able to manage export orientated industries.¹²

The development of Export Processing Zones (EPZs) - industrial parks that supply cheap, disciplined labour and substantial tax breaks for foreign investors – was a key strategy in the Tiger's development¹³ but attempts to replicate EPZs elsewhere have

⁸Kasper, Wolfgang, 'A Recovery Plan for East Timor', *Policy*, Summer 1999/2000, p. 45-46

⁹For a comprehensive overview on the different theories of the developmental state that sprang up in the wake of the East Asian 'Tigers', see Ankie Hoogvelt, *Globalisation and the Postcolonial World: The New Political Economy of Development* Macmillan, London, 1997, Ch 10, pp. 201-216

¹⁰*Ibid.* p. 204, see for example New Trade Theory, Paul Krugman, *Strategic Trade Policy and the New International Economics* MIT Press, Cambridge, 1986

¹¹ Douglas Dowd, *Capitalism and its Economics*, Pluto Press, Annandale, 2000, p. 209

¹²Hoogvelt *op. cit.* p. 204

¹³Walden Bello, *Dragons in Distress: Asia's Miracle Economies in Crisis*, Penguin, London, 1990

had mixed results.¹⁴ The rush of nations setting up EPZs from Latin America, the Caribbean, Asia and Africa are competing in an increasingly globalised economy that has constrained host government attempts to convert fly-by-night direct investment into substantial national development. Writers like Walden Bello are critical of institutions such as the World Bank who promote EPZs as successful embodiments of free trade, ignoring their complex history.¹⁵ It remains to be seen what sort of investment will be attracted to the EPZ, the Investment Institute of the East Timorese Transitional Administration¹⁶ (ETTA) plans to develop.¹⁷

‘There is not a single example in history’, argues Professor Noam Chomsky, ‘of a developed society which has followed free market rules’.¹⁸ From British suppression of the Indian cotton trade in the 1800s¹⁹ to the \$361 billion that is spent annually to support OECD farmers²⁰: state and industry have always worked to secure economic development. Much of the literature on East Timor acknowledges that the state has a role to play but limits it to ‘correcting market failures in terms of distortions such as monopoly’,²¹ as two of East Timor’s leading economists, Joao Saldanha and Helder da Costa, note. For East Timor’s present situation, this does not appreciate the realities

¹⁴Weissman, Robert ‘Waiting to Export: Africa Embraces Export Processing Zones’, *Multinational Monitor* July/August, 1996, p. 12.

¹⁵*Ibid.*

¹⁶ETTA is the East Timorese wing of an administrative partnership with UNTAET

¹⁷Investment Institute, *East Timor: Building the First State of the New Millennium*, East Timor Transitional Administration, Dili, 2001, p. 7.

¹⁸Chomsky, Noam *Latin America: From Colonization to Globalization*, Ocean Press, Melbourne 1999, p. 83

¹⁹‘The state was the chief element in insuring that the infant and early developments of the cotton industry would be fully protected from competition’, Dowd *op. cit.* p. 25

²⁰Fowler, Penny, *Harnessing Trade for Development*, Oxfam Briefing Paper No 1, August 2001, p. 27

²¹Saldanha, Joao & da Costa, Helder, ‘Economic Viability of East Timor Revisited: Outlook for the 21st Century’, *East Timor Study Group Working Paper No. 1*, Australian National University, Canberra, July 1999, available at <<http://rspas.anu.edu.au/etsg>> p. 14

of reconstruction and recovery in post-conflict situations. A brief sample of the literature is clear - governments need to control the market, not be dominated by it.²² It is necessarily a balancing act between the demands of economic growth and those of social justice and welfare, but in all cases someone needs to do the balancing. Perhaps this role has been filled by various aid agencies and non-governmental actors, but as Benjamin Crosby stresses, one of the key roles of governments in such a period, is to get these powerful actors to agree with national post-conflict development priorities and strategies.²³

The other major point made in the literature is that East Timor should provide a strong legal framework for private enterprise to feel secure and flourish.²⁴ Sarah Cliffe from the World Bank argues that Timor's development will be endangered 'if it does not foster effective banking supervision, adequate bankruptcy laws, transparency and standards of financial accountability'.²⁵ Similarly, Joao Saldanha from the East Timor Study Group, cites Douglas North's argument that well defined institutions that were able to guarantee stability of property rights with consistent and transparent rules spearheaded economic development in the US and Britain.²⁶ This may be a warning to policy makers to avoid the cluster of deformed capitalisms in developing countries

²²See for example, Harris, Geoff and Lewis, Nerl, 'Economic Reconstruction and Recovery', in Harris Geoff (ed) *Recovery from Armed Conflict in Developing Countries: An Economic and Political Analysis*, Routledge, London, 1999 p. 53; Crosby, Benjamin, 'Central America' in Lake, A et al *After the Wars: Reconstruction in Afghanistan, Indochina, Central America, Southern Africa and the Horn of Africa*

²³Crosby *Ibid.* p. 133

²⁴Jose Ramos-Horta & Emilia Pires *loc. cit.*

²⁵Cliffe, CNRT address, p. 3

²⁶Saldanha, in Fox and Soares (eds), paraphrasing North, Douglas *Institutions, Institutional Change and Economic Performance*, Cambridge University Press, Cambridge, 1990.

that foster personal loyalties above economic demands.²⁷ Paul Hutchcroft for example, writes of a 'booty capitalism' in the Philippines that has constrained successful economic development to a large extent by the weaknesses of political development.²⁸ It is a classic post-colonial pitfall: An anglo-legal structure, developed over centuries of class and state interplay²⁹ is formally imposed on a different culture usually attempting to emerge from a stage of chronic underdevelopment. While legal consistency and transparency is important, without the concurrent development of the social, political and economic fabric of the nation it can be meaningless.

The second flaw in this argument is the equation of flourishing private enterprise with national development. Da Costa stretches this link, paraphrasing Kasper: 'Economic openness is a means of cultivating habits and rules of economic and political conduct that are essential to peaceful cooperation and reconciliation'.³⁰ It can also be a means of cultivating underdevelopment, alienation and starvation or, as Karl Polanyi's analysis of the tyranny of the 'self-regulating market' shows, two barbaric world wars.³¹ To manage the market on their terms, the East Timor need a clear articulation of national priorities and a nuanced understanding of their position in the global economy. The risk here is that East Timor's nationalist struggle - the vehicle that brought a group together to demand freedom from foreign domination and the realisation of self-determination - loses meaning once this very goal, the achievement

²⁷ Oskar Curer *The Political Foundations of Development Policies*, University Press of America, Lanham, 1997 p. 4

²⁸ Paul Hutchcroft, *Booty Capitalism: The Politics of Banking in the Philippines*, Cornell University, Ithaca, 1994 p. 2

²⁹ See for example, the development of modern corporations law in the United States in Humphrey McQueen, *The Essence of Capitalism* Sceptre, Sydney, 2001 pp. 21-32

of national, is realised. As Partha Chatterjee shows, a nationalist impulse must always be part of a larger politics or else it is without meaning.³²

Worryingly, Jose Ramos-Horta and Emilia Pires, two key figures in the transitional bureaucracy, argue that the nationalism that fought off a colonial dominator is perfectly compatible with a nationalism that encourages private investment:

‘A post-transition East Timor will welcome sound investments by firms that wish to operate in an environment free of artificial barriers to trade. We expect that all stakeholders in our society will embrace the values that have guided the East Timorese liberation struggle for the past twenty-five years: transparency, mutual respect, and equality of treatment.’³³

This subversion of the original national project is problematic. In the following examination of East Timor’s coffee industry, I argue that a nuanced understanding of international market dynamics is needed to guide the industry. Blanketly removing ‘artificial barriers to trade’ will expose a fragile industry to a savage commodity market, immiserate the much of the population and derail the nationalist project - a glue that has bound a people together through tremendous crises. In the words of Franz Fanon, indigenous elites like Ramos-Horta risk becoming, ‘the transmission line

³⁰Helder da Costa, ‘Linkages between Globalisation, Trade, Investment and the Environment’, *Sustainable Development in East Timor* Timor Aid, 2001 p. 50

³¹ Polanyi, Karl, *The Great Transformation*, Beacon Press, New York, 1944

³² Partha Chatterjee *Nationalist Thought in the Colonial World*, Zed Books, New Delhi 1985

³³ Jose Ramos-Horta & Emilia Pires *loc. cit.*

between the nation and a capitalism, rampant though camouflaged, which today puts on the masque of neo-colonialism'.³⁴

The structure of the thesis, like the source of Timor's development obstacles, is broad. Firstly, Chapter One applies the Global Commodity Chain (GCC) approach to map the transformations in the structure of the international coffee market over the last two decades, and examines the repercussions for developing countries such as East Timor, heavily reliant on coffee production. Chapter Two looks at the two stillborn colonial attempts to developing a function coffee plantation economy in East Timor. It then provides an overview of the present industry and discusses what problems have emerged as an independent East Timor integrates with a liberalised coffee market. Chapter Three looks at ways East Timor can capitalise on emerging possibilities but acknowledges that they are limited. I conclude by suggesting that East Timor could capitalise on the emerging Fair Trade movement as well as organising smallholder farmers cooperatively.

³⁴Fanon, Franz, *The Wretched of the Earth*, Penguin, Ringwood 1990, p. 133

Chapter One

The International Coffee Market

1.1 Global Commodity Chain Approach

The GCC approach disaggregates and analyses the international network of labour and production processes that produce a finished commodity. Conceptually, a commodity chain can be expressed as a series of nodes linked together in a network, where the commodity is transformed as it passes from each successive node. Gary Gereffi, the main theorist, outlines four features of any chain: input-output structure, geographical coverage, internal governance structures and the institutional framework.³⁵ The first two describe the physical configuration of the chain, while the latter two focus on the coordination and control exercised by various actors.

Like its political economy forebears, particularly from the Dependency³⁶ and World-Systems theory³⁷ schools, GCC is concerned with the international flows of surplus and how this restricts or improves national development prospects. While the 'dependentistas' argue that underdevelopment results from surplus being transferred

³⁵ Gary Gereffi, 'The Organization of Buyer-Driven Global Commodity Chains: How U.S. Retailers Shape Overseas Production Networks', in Gary Gereffi & Miguel Korzeniewicz (eds), *Commodity Chains and Global Capitalism*, Greenwood Press, London, 1994 p. 97, for an interesting overview see for example, Philip Philip et al, *Global Commodity Chain Analysis and the French Filiere Approach: Comparison and Critique* Centre for Development Research Working Paper 00.3 February 2000

³⁶ Tony Smith, 'The Underdevelopment of Development: The Case of Dependency Theory', *World Politics* Vol. 31 No. 2 pp. 247-288

³⁷ Immanuel Wallerstein, *The Politics of the World-Economy*, Cambridge University Press, Cambridge, 1994

from the 'periphery' or underdeveloped nations, via capitalist accumulation to the 'core' or developed nations, in GCC analysis, the distribution of wealth is an outcome of the relative intensity of competition within various nodes of a commodity chain.³⁸

In reality this has often meant that wealth has accumulated to core-like nodes rather than peripheral ones because enterprises and states in the core have effectively transferred competitive pressures to peripheral areas of the world-economy.³⁹

This approach has a nuanced understanding of the economic processes that have restructured the world economy in the last few decades (often termed post-Fordism). The rise of the formerly poor East Asian Tigers exposed the simplicity and rigidity of the dependency theorists' division of the world into effectively static 'core' and peripheral' regions. In response, the GCC approach is more of a methodological tool box than a grand theory of underdevelopment. It cuts across local, national and international levels to emphasise the heterogeneity of organisational arrangements of production and trade while still allowing for the analysis of common themes.⁴⁰ GCC shows that power is mainly associated with systems of coordination rather than with concentration of ownership. For example, technological advances in transport and communication have allowed transnational corporations (TNCs) to outsource labour intensive production processes to developing countries with cheap, disciplined pools

³⁸ Gary Gerrefi & Miguel Korzeniewicz (eds), *Commodity Chains and Global Capitalism*, Greenwood Press, London, 1994, p. 4

³⁹ *Ibid.* p. 2-3

⁴⁰ Stefano Ponte, 'The "Latte Revolution"? Winners and Losers in the Restructuring of the Global Coffee Marketing Chain', *Centre for Development Research Working Paper 01.3*, Copenhagen, June 2001 p. 2

of labour while maintaining managerial control in the North.⁴¹ This adds a political dimension lacking in most convention trade theories that instead for example, try to blame underdevelopment on the unproductive profit seeking activities of Third World nations.⁴²

Traditionally, Unequal Exchange and Dependency theorists argued that developing countries should 'delink' themselves from the world economy in order to re-create the preconditions for development enjoyed by the dominant developed countries.⁴³

Today, however, any attempt at economic isolation will mean only a more brutal kind of domination by the global system, a reduction to powerlessness and poverty. GCC analysis on the other hand attempts to look at opportunities for fragile industries to shelter and develop within the nooks and crannies of the world-system. This involves an analysis of the chain's governance structures. Often this is a tussle between a state in the South attempting to 'forward integrate' or gain control of nodes further up the chain while Transnational Corporations (TNCs) engage in the reverse process. For smaller countries heavily dependent on primary commodity exports, gaining control of processing of the commodities that link them to the world economy can be an important development strategy.⁴⁴

⁴¹ See for example, Mittelman, James H, "Rethinking the international division of labour in the context of globalisation", *Third World Quarterly*, Vol 16 No 2 1995, pp. 273-295

⁴² See for example, Bhagwati, Jagdish, "Directly Unproductive Profit-Seeking (DUP) Activities", *Journal of Political Economy* 90, 5:988-1002. For an application of this perspective to the present Timor situation, see Ron Duncan, 'Some Development issues for East Timor', *Bulletin of Indonesian Economic Studies* vol. 3 no. 2 1999 p. 40-45

⁴³ Samir Amin, *Accumulation on a World Scale*, Monthly Review Press, New York, 1974

1.2 The Coffee Commodity Chain

Analysis of the coffee commodity chain provides a stark insight into North-South economic relations. Over 90% of coffee production takes place in the South, while 70% of consumption occurs in the North.⁴⁵ Many developing countries rely on coffee for a high proportion of their export earnings and until recently, it was second only to oil as the most valuable traded commodity. More significantly, it exemplifies the effects of market liberalization on the structures of coordination and control in producing countries.

The physical structure of the coffee commodity chain is both simple and constant. The coffee cherry is usually semi-processed in the producing country and exported as a green bean to the consuming country where it is roasted, packaged, distributed, marketed and finally sold for consumption (see Appendix 2). Traditionally, the market has been volatile, following the classic economic cycles of boom and bust. This is due to the climatic sensitivity of crops and the difficulties faced by producers responding to shifts in market demand. Given that coffee trees take three to four years to mature, a crop planted to take advantage of high prices often causes a glut in the market when it finally comes on-line. Farmers are unlikely to respond to the consequent price decline by ripping up their trees.

⁴⁴Talbot, John, "The Struggle for Control of a Commodity Chain: Instant Coffee from Latin America", *Latin American Research Review* vol. 32, no. 2, 1997, p. 118

1.3 The Rise and Fall of the International Coffee Agreement

With roasted coffee going stale very quickly, it has been difficult for producers to export anything other than the green bean. Given these physical restraints on forward integration and the inherent volatility of the commodity, producers have instead tried to regulate supply of the semi-processed product to guarantee a strong, stable price. Since 1962, there have been a number of International Coffee Agreements (ICAs) between producing and consuming states which have, at times, imposed export quotas on producing countries.⁴⁶ Most econometric analyses of the world coffee market have concluded that this regulation of supply increased world market prices above market equilibrium levels.⁴⁷

Of all the post-war commodity agreements, the ICA was arguably the most successful.⁴⁸ It was formulated at a time of unprecedented Third World solidarity buoyed on by the success of many national liberation movements, high economic growth (from the early 50s until the late 70s) and their geopolitical positioning during the Cold War. This rising influence led to the call for a New International Economic Order (NIEO) - an agenda demanding an equitable distribution of global economic power. This led to the formation of bodies like the United Nations Commission on

⁴⁵Ibid, p. 119

⁴⁶ When a set price calculated by the International Coffee Organisation (ICO) rose over the set price, quotas were relaxed: when it fell below that price, quotas were tightened

⁴⁷ see for e.g. Akiyama, Tamassa and Panayotis, Varangis, "The Impact of the International Coffee Agreement on Producing Countries." World Bank Economic Review 4, 2 (May 1990 pp. 157-73; Akiyama, Tamassa, 'Coffee Market Liberalization since 1990', in *Commodity Market Reforms* World Bank, 2001 pp. 83- 120; Bates, Robert, *Open Economy Politics: The Political Economy of the World Coffee Trade* Princeton University Press, Princeton New Jersey 1999.

⁴⁸ Talbot, 'Where Does Your Coffee Dollar Go?: The Division of Income and Surplus Along the Coffee Commodity Chain' *op. cit.* p. 87

Trade and Development (UNCTAD), designed to assist in achieving fair commodity prices. TNCs from the core acquiesced to the collective action of the ICA largely because it provided a consistent supply of coffee and still allowed them to make a profit.⁴⁹

The erosion of economic strength and political unity in the South eventually derailed the NIEO. Walden Bello argues that this was an explicit US goal, largely achieved using the Bretton Woods institutions⁵⁰ to force a free market agenda on the South.⁵¹ The pressure of mounting debt and crippled domestic currencies in the South allowed international financial institutions like the IMF to impose austere Structural Adjustment Programs (SAPs) that liberalised economies as conditions for debt relief. State participation in the economy was severely limited, government enterprises passed into private hands, protectionist barriers to Northern imports were reduced and domestic economy were tightly integrated into the global in a neoliberal efficiency drive.⁵² Many Southern countries also actively endorsed such policies, especially in Latin America. This, along with the collapse of the Cold War, undermined the cooperation among producing states, and commodity price management was no longer a priority for industrialized countries, leading to the collapse of the ICA in 1989.

⁴⁹Talbot *op. cit.* 15 of 18

⁵⁰The post-World War 2 bodies were the IMF, World Bank and the ITO/GATT/WTO, originally designed to stabilise the global economy.

⁵¹Bello, Walden, *Dark Victories: The United States, Structural Adjustment and Global Poverty*, London, Pluto Press, 1994.

1.4 Market Liberalisation and the Shifting Governance Structures.

In 1985 only 15 out of the world's 51 major coffee-producing countries had private marketing systems. Twenty-five countries sold coffee through state-controlled monopolies, including marketing boards, stabilisation funds and institutions. Another 11 countries had mixed state and private sector marketing bodies.⁵³ Industry and state previously had a symbiotic relationship: Government could assist the development of industry, protect small holders and represent their concerns the international level while reciprocally, industry could provide an important source of taxation revenue. Many states, however, squandered the surplus or, through stagnant planning, reduced incentives to produce.

One recent study of coffee market liberalisation in India, Uganda and Togo concluded that the main benefits to the industry were the jump in producer prices, the quick payment of farmers and a dynamic and competitive private sector.⁵⁴ Prices increased because of the abolition of export taxation and price control mechanisms that forced sub-market prices onto growers. However, this advantage has turned to a disadvantage as prices have gone through the floor. Similarly, the ability of the private sector to provide the necessary inputs for industry development fades in sour times. In Tanzania, for example, lower farm gate prices, dropping infrastructural support and

⁵²For an overview of the whole process see for example, Chussodovsky, Michel *The Globalization of Poverty*, Zed Books, London 1999.

⁵³Akiyama, Takamasa "Coffee Market Liberalization since 1990", in *Commodity Market Reforms* World Bank, 2001, p. 83

⁵⁴Akiyama, *Ibid.* p. 99,

exploitative traders have led to lower quality coffee.⁵⁵ At the national level, liberalisation has produced mixed results for producing countries with well developed industries - the story has been bleak for those without.

Fading state control over industry largely led to the breakdown of international coordination among producers creating a 'tragedy of the commons' among coffee producing nations: individually it is in each country's interests to produce as much coffee as possible but, collectively, this oversupply has dragged the price down so far that total coffee export revenues are now lower than they were in 1980 (see Appendix 5). Although the price has fluctuated both up and down since 1989, largely due to frosts in Brazil, the long-term trend is a decline in prices.⁵⁶ In 1997 this was 3.85 USD per kilo but slumped to 1.43 USD by May 2001 - just 37% of its value.⁵⁷ Since then, the price had dropped to 1.137 USD with some industry commentators predicting it could go as low as 0.99 USD.⁵⁸

There are several reasons why coffee supply has grown at twice the rate of demand in the last decade.⁵⁹ Firstly, with hi-tech industries now driving the global economy, the value of primary commodities has declined by 50 per cent in the last decade.⁶⁰ While the unit value of manufactured products exported by Northern countries more than

⁵⁵Stefano, Ponte, 'The 'Latte Revolution?' Winners and Losers in the Restructuring of the Global Coffee Marketing Chain', *Centre for Development Research Working Paper 01.3*, Copenhagen, June, 2001, p. 25

⁵⁶Ponte *op. cit.* p. 12

⁵⁷Development Alternatives International Inc, *Sustainability Assessment of the National Cooperative Business Association East Timor Coffee Activity*, Draft, June 2001

⁵⁸Laird interview, also 'Coffee Prices Fall Sharply, Timor Lorosae Farmers Protest' *Suara Timor Lorosae*" 1 July, 2001

⁵⁹Celine Charveriat *Bitter Coffee: How the Poor are Paying for the Slump in Coffee Prices* Oxfam Great Britain, 16 May, 2001 available at <<http://www.oxfam.org.uk>> p. 5

doubled between 1975 and 1993, for the South, they are at their worst level since the 1929 depression.⁶¹ It is therefore more expensive for the Southern farmer to purchase imported agricultural inputs especially now without state assistance. Secondly, the pressure of debt has forced countries – with the assistance of the World Bank and other agencies - to expand exports in order to generate hard currency. It was with their assistance through project lending and wider macro-economic reforms over the last five years that Vietnam was transformed into the second largest producer of *Robusta*.⁶² Similarly, Uganda's coffee market reforms were a condition of the World Bank SAP begun in the late 1980s.⁶³

The governance structure of the chain has also shifted. TNCs' control over consumer markets has been accelerated by the collapse of the ICA so eight TNCs currently control between 55% to 60% of the world trade in coffee.⁶⁴ They force an estimated 20 million small holder households, who could previously negotiate collectively through the apparatus of the state, to compete with each other.⁶⁵ Market liberalisation in this sense, is the union busting of an entire commodity chain. The inequalities in the coffee commodity chain are a sad affirmation of Noam Chomsky's argument that 'really existing free-market policies' are thrust upon the poor, while corporations are protected.⁶⁶ Despite the lowest green bean prices ever,⁶⁷ coffee corporations have not

⁶⁰Belinds, Coote, *The Trade Trap: Poverty and the Global Commodity Markets*, (Second Edition with Additional information by Caroline Lequesna), An Oxfam Publication, London, 1995, p. 23

⁶¹UNCTAD *World Report* 1994

⁶²Chaveriat *op. cit.* p. 4

⁶³Akiyama, *op. cit.* p. 96

⁶⁴John Madeley, *Hungry for Trade: How the Poor Pay for Free Trade*, Pluto Press, Annandale, 2000 p. 91

⁶⁵Chaveriat *op. cit.* p. 2

⁶⁶See for example, 'Socioeconomic Sovereignty' in Noam Chomsky, *Rogue States: The Rule of Force in World Affairs* South End Press, Cambridge 2000 pp. 199-214.

passed on their savings to the consumer.⁶⁸ Between 1975 and 1993, the international price of coffee declined by 18 per cent on world markets yet the price paid by the consumer in the US increased 240 per cent.⁶⁹ Nestle's business documents reflect how 'trading profits increased... and margins improved thanks to favourable commodity prices'.⁷⁰ This is also the main reason Starbucks, the Seattle-based coffee chain, posted a 41% increase in profits in the first quarter of 2001.⁷¹

This in part explains why the private sector producing houses that have replaced state marketing boards have been unable resurrect an effective stock retention plan.⁷² By controlling but not owning the small holder, a higher node in the chain can simply pass on the poor price while retaining the surplus.

John Talbot has studied the general shifts in surplus and income between producing and consuming countries over the last three decades (see Appendix 3).⁷³ He estimates that in the 1970s, an average of 20% of total income was retained by producers, while the average proportion retained in consuming countries was almost 53%. The

⁶⁷In real terms, and taking inflation into account, prices are now at their lowest ever levels. Chaveriat *op. cit.* p. 1

⁶⁸J. Morisset, *Unfair Trade? Empirical Evidence in World Commodity Markets over the Past 25 Years*, World Bank (1997) There is little consumer pressure with many econometric studies illustrating that coffee demand is relatively inelastic – a modest increase in price will not reduce demand.

⁶⁹Chaveriat *op. cit.* p. 5

⁷⁰Chaveriat, *op. cit.* p. 2, Nestle was recently taken to court for anticompetitive practices but was acquitted largely on the grounds that other competitors had no issue with Nestle's pricing policy (they were no different to their own)

⁷¹*Ibid.* p. 6

⁷²Brown, *op. cit.* p. 5 Present stock retention plans seem to be piecemeal. The coffee retention plan developed by the newly formed Association of Coffee Producing Countries (ACPC) requires exporters to withhold 20 per cent of production from the market. Brazil, for example, is thought to have stored close to two million 60kg bags yet the quantities retained are too small to alter the price and compliance is patchy. The amount of coffee still in supply, including retained stocks, is still influencing the price especially when the amount of coffee in consuming countries stands at over one million tons.

remaining share consists of value added in producing countries, transport costs and weight loss. This balance was fairly consistent between 1981 to 1988, but the collapse of the ICA in 1989 changed this dramatically. Between 1989 and 1995 the proportion of total income received by growers slumped to 13%; the proportion retained in consuming countries rose to 78%. At present, with developing countries receiving less than \$8 billion of the \$50 billion in world coffee sales,⁷⁴ it would be safe to conclude that this surplus would have dropped further surplus now captured by producing countries would have collapsed - in many countries, turning into a deficit. Within producing countries, small farmers at the bottom of the supply chain receive less than ten per cent of the final retail price of coffee.⁷⁵

Given the increasing concentration of buyers and the huge diffuse number of small farmer-producers, the coffee commodity chain could be described as a 'buyer-driven commodity chain'. It is a term developed by Gereffi to describe organisational changes in the apparel and footwear commodity chains,⁷⁶ it has increasingly been applied to agricultural commodities.⁷⁷ They are characterized by large retailers, brand-name merchandisers and trading companies in industrialized countries being the key actors in setting up decentralized networks of trade in developing countries.⁷⁸

⁷³Talbot John M. "Where Does Your Coffee Dollar Go? The Division of Income and Surplus along the Coffee Commodity Chain", *Studies in Comparative International Development* 32(1) p 65-67

⁷⁴Taken from www.globalexchange.org on 28th September, 2001

⁷⁵Chaveriat, *op. cit.* p. 2

⁷⁶Garry Gereffi "The Organization of Buyer-Driven Global Commodity Chains: How U.S. Retailers Shape Overseas Production Networks' *loc. cit.*

⁷⁷Peter Gibbon, 'Upgrading Primary Production: A Global Commodity Chain Approach', *World Development* Vol. 29 No. 2 pp. 345-363;

⁷⁸Gereffi *Commodity Chains and Global Capitalism op. cit.* p. 7

There is also the emergence of two newer features in the coffee chain structure that are arguably linked to this post-Fordist reorganisation.⁷⁹ Firstly, hedging, or futures trading in commodities can provide a means of shielding farmers from price shocks as they sell their crop in advance. This requires access to Northern expertise that most smallholder growers lack. Ironically also, such speculations can add to price volatility.

The second feature is the rise of marketing as a barrier to controlling commodity chain nodes in the North. The post-war development of instant coffee, for example, provided peripheral capital with the opportunity to process coffee beyond the green bean stage for export and therefore achieve forward integration up the commodity chain. Currently, periphery producers still control the bulk of their domestic soluble coffee processing facilities, even in the face of increasing TNC share ownership, yet imports of soluble coffee into core markets only accounts for one fifth of coffee consumed there. Large advertising expenditures, brand names and distribution channels are dominated by TNCs squeezing out poorly networked peripheral capitalists.⁸⁰ However, marketing, along with maturing consumer tastes in the North is slowly leading to product differentiation among coffee brands. In this sense, the coffee commodity chain fragments into smaller chains that could be defined by country of origin, organic status and taste. to name a few. In this scenario, control of nodes would swing back to producing countries capable of effectively branding themselves and networking with select distributors and roasters in the North.

⁷⁹ Giovanni Arrighi argues that capitalism runs in historic cycles and is nearing an end of a cycle, marked by the rise in speculative capital See Arrighi, Giovanni *The Long Twentieth Century* Verso, London, 1994. Jameson takes his cue from Arrighi's cycles adding that the commodification of cultural forms is a symptom of a system running out of room to expand. He argues that this is the

Chapter 2

The History and Structure of East Timor's Coffee Industry

Both the Portuguese (1510-1974) and Indonesian (1975-1999) administrations in East Timor failed to establish a functioning plantation system that would incorporate the bulk of the population into a capitalist economy. The subsequent underdevelopment has left the industry largely in the hands of small holders who have resisted the clumsy modernising pressures of exploitative and centralised marketing boards, often backed by state terror. This section looks at the reasons for these historic failings, how those factors have shaped and inform discussions of the coffee industry today.

2.1 Portuguese Colonialism

Unlike most of the colonised tropics, the Portuguese administration was never able to establish an effective plantation economy in East Timor that would lead to the development of a money economy or, as one governor put it, 'the penetration of civilisation and the end to barbarism'.⁸¹ Itself largely peripheralised in Europe and lacking the capital and technology to lure its colonised peasants into wage labour,

reason for the rise in Postmodernism, Fredric Jameson, "Postmodernism, or, The Cultural Logic of Late Capitalism", *New Left Review*, 1990, p. 1-54

⁸⁰Talbot, 'Instant Coffee from Latin America' *op. cit.* p. 133

⁸¹Celestino da Silva quoted in Gunn, Geoffrey *Timor Loro Sae: 500 Years Livros Do Oriente*, Macau, 1999, p. 197

Portuguese colonialism, as Perry Anderson argues, had to use ‘undisguised coercion... to smash the subsistence sector’.⁸²

This is exemplified by the policies of Governor Celestino da Silva who, in 1894, attempted to lay the foundations of a functioning plantation system. A period of aggressive state planning followed, involving attempts to control land, labour and capital. The main instrument was the Sociedade Agricola Patria e Trabalho (SAPT), a powerful agri-business, which W.G. Clarence-Smith described as a ‘state within the state’.⁸³ Formed in 1897, under the governor’s leadership and using the apparatus of the state, it forcefully seized the most productive land in the Ermera district. This was followed by a program of forced coffee cultivation among small holders, where hundreds of thousands of coffee seedlings were planted under the gaze of the military. The administrative fervour for forced cultivation continued when Governor Camara forced the members of a defeated rebellion against a poll tax (1911-1912) to plant 600 coffee bushes each. Nearly eight million trees were planted in 1916 alone.⁸⁴ The attempt to establish a plantation system saw the rise of labour practices that included ‘forced cultivation of cash crops, forced and contract labour, illegal recruitment and starvation wages’.⁸⁵ Such methods were expensive, discouraged productivity, tended

⁸²Anderson, Perry, ‘Portugal and the End of Ultra-Colonialism: Part 2’, *New Left Review*, Vol. . 16, 1962 p. 98

⁸³W. G. Clarence Smith, ‘Planters and Smallholders in Portuguese Timor in the Nineteenth and Twentieth Centuries’ *Indonesia Circle* No. 57, Mar 92 p. 20

⁸⁴*Ibid.* p. 18

⁸⁵Gunn, *op. cit.* p. 197

to spark anti-colonial rebellion⁸⁶ and could hardly be sustained by a weak administration.⁸⁷

Colonial efforts were partially successful. Thought to have been introduced in 1815, coffee eventually became the economic salvation of the colony, accounting for 53% of exports by 1863.⁸⁸ Frequent booms like this were, however, probably attributable more to rising world prices and the entrepreneurial nous of Chinese traders than government attempts to rationalise the industry.⁸⁹ The further stagnation of Portugal's colonial rule into the twentieth century meant that they failed to provide the infrastructure necessary to capitalise on previous developments.⁹⁰ Instead, smallholders dominated export production, despite efforts to develop an estate sector and ill-adapted colonial directives imposed on smallholders.⁹¹

The bulk of the Timorese population continues to live in the traditional and subsistence part of what East Timorese economist Joao Saldanha describes as a 'dualistic economy'.⁹² Writing in 1970 on the Mambai people of Aileu, one of the coffee growing districts, the anthropologist Elizabeth Traube observed families in small hamlets of between two and five households who worked on their small coffee

⁸⁶Especially in the period from 1860-1912 when the administration was pushing ahead with its plantation policies. see *Ibid.* Ch 8 & 9

⁸⁷*Ibid.* p. 197

⁸⁸*Ibid.* p. 135

⁸⁹Should get the source from Clarence Smith

⁹⁰Jill Joliffe, *East Timor: Nationalism and Colonialism* University of Queensland Press, Queensland, 1978 p. 102

⁹¹W. G. Clarence Smith, *op. cit.* p. 15

⁹²Saldanha, Joao *The Political Economy of East Timor Development* Pustaka Sinar Harapan, Jakarta, 1994 page 63.

holdings cooperatively in kin groups to generate their main source of cash.⁹³ Unlike the profit-driven plantations, Timorese peasants typically generate an extremely low income from a few coffee bushes scattered over a wide terrain.⁹⁴

2.2 Indonesian Neo-colonialism

The 1975 Indonesian invasion brought with it a corporate infrastructure that would appropriate many Portuguese assets, serve the interests of a cadre of generals and provide the framework for economic control and exploitation. PT Denok Hernandes International, associated with Benny Murdani, the general leading the invasion, was 'the only company to land with the Marines'.⁹⁵ It seized SAPT assets to finance military expenditure, exporting over 1300 tons and earning \$3.1 million in the first year of occupation.⁹⁶ 9000 ha of plantation lands were later formally handed over to Denok by the Indonesian Governor in 1979, and all small holder land was declared government property.⁹⁷ Given a boom in coffee prices in the late 1970s, it has been estimated that Denok made a profit of \$20-25 million between 1976 and 1980.⁹⁸ East Timor 'was paying for its invasion in coffee'.⁹⁹

⁹³Traube, Elizabeth *Cosmology and Social Life: Ritual Exchange among the Mambai of East Timor* University of Chicago Press, Chicago p. 52-53

⁹⁴Helder Lain de Silva's 1956 study on the industry quoted in Gunn *op. cit.* p. 199

⁹⁵Wain, Barry, 'Military Seen Behind Firm Controlling Timor's Coffee', *Asian Wall Street Journal*, 16 June 1982

⁹⁶Geoffrey Gunn *A Critical View of Western Journalism and Scholarship on East Timor*, Journal of Asian Publishers, Manila, 1994 p. 221

⁹⁷Coffee - The Principal Beverage in the World NCBA document page 3

⁹⁸Robinson, Richard, *Indonesia: The Rise of Capital* Association of Southeast Asian /Allen and Unwin, Sydney, 1986 p 267-68

⁹⁹Budiarjo, Carmen and Liem Song *The War Against East Timor* Zed Books, 1984, p. 103

Denok monopolised the trade through tight military control of buying, selling and transporting of coffee. All trading had to be carried out through official Denok agents in each region, part of a government imposed network of village 'cooperatives' called PUSKUD (Pusat Koperasi Unit Desa). In mid 1982 for example, the fixed price farmers were forced to sell at was only a quarter of that offered under Portuguese rule.¹⁰⁰ Citing the previous nationalisation of land, Government officials justified the low price as simply a wage for 'labourers picking coffee that doesn't belong to them'.¹⁰¹ During harvest time, military check-points carried out intensive searches for stockpiled coffee. To compound restrictions on trade, Timorese were prevented from inter-regional movement, punishable through jail.¹⁰²

However, Indonesia did attempt to develop the territory. East Timor received more per capita from Jakarta than any other province although commentators are quick to point out that it was expensive to maintain a military that killed over one third of the population.¹⁰³ Given Portuguese neglect, it was also necessary to build infrastructure to exploit Timor's valuable natural resources. The first paved roads built in the region, for example, were for Denok trucks to transport coffee stocks from the mountains.¹⁰⁴ Jakarta attempted an almost Soviet-style centralised planning, funding a large civil service and subsidising many commodities such as fuels and food, but its deliberate

¹⁰⁰ *Ibid* p. 105

¹⁰¹ *Ibid.*

¹⁰² John G Taylor, *East Timor: The Price of Freedom* Pluto Press, Annandale, (2nd Edition) 2000. p. 125

¹⁰³ Gunn, *A Critical View of Western Journalism and Scholarship on East Timor op. cit.* p. 224

¹⁰⁴ Budiardjo *op. cit.* p. 104

policy of using the province just as a supply of natural resources led to its dependency and underdevelopment.¹⁰⁵

It prioritized the development of the coffee industry, but military ineptitude and abuse led one industry expert to label them ‘as bad as the Portuguese’.¹⁰⁶ The records are confused. Carmel Budiardjo notes that Indonesia attempted to expand the plantation economy by planting one million coffee seedlings by 1980 and claiming an additional 10,000 hectares for coffee.¹⁰⁷ Despite these initiatives, the Indonesian economist Hadi Soesastro notes that it was only in 1987 that the provincial government decided to provide ‘substantial financial resources’ to develop the industry.¹⁰⁸ Indonesian records from 1993 do not show this.¹⁰⁹

Richard Robinson, writing on the rise of capital in Indonesia, notes that military companies have been notorious for running down capital, despite having politically secured monopolies and concessions.¹¹⁰ PT Denok were bad managers trying to make fast money, but it is more accurate to conceptualise it as a particular brand of stagnant clientele capitalism.¹¹¹ In short, military resettlement programs in the coffee

¹⁰⁵ John G. Taylor, *East Timor: The Price of Freedom* Pluto Press, Annandale, 2000 (2nd Edition) p. 126-27; Geoffrey Gunn, *Gunn, A Critical View of Western Scholarship and Journalism on East Timor* Journal of Contemporary Asia Publishers Manila, 1994. pp. 207 - 236

¹⁰⁶ *The East Timor Rehabilitation and Development Project (TERADP): A Briefing Paper* National Cooperative Business Association, January 2001 p. 1

¹⁰⁷ Budiardjo, *op. cit.* p. 106

¹⁰⁸ Soesastro, Hadi, “East Timor: Questions of Economic Viability”, in Hill, Hal (ed) *Unity and Diversity: Development in Indonesia Since 1970* p. 225

¹⁰⁹ *East Timor Coffee Cultivation Project Profile* Regional Investment Board of East Timor 1993

¹¹⁰ Robinson *op. cit.* p. 268

¹¹¹ Curer *loc. cit.*

districts,¹¹² widespread human rights abuses and the semi-feudal exploitation of Timorese coffee farmers by a monopoly driving for quantity over quality, meant that over the last few decades, coffee exports have ‘declined drastically and farmer plantations have been neglected’.¹¹³

2.3 Present Industry Overview

The violence and destruction in September 1999 did not cripple the industry directly, but there has been significant broader ramifications. Despite some small scale looting most of the coffee stocks were safe and the bulk of the growing families were safe in the mountains.¹¹⁴ Nationally, there was a huge displacement of people, a plummeting dropping GDP interrupted agricultural output and the destruction of 70% of buildings.¹¹⁵ The coffee crop has recovered well with an anticipated harvest of 10,000 tons this year, worth \$13 million.¹¹⁶ There have been fewer traders operating due to supply networks with Indonesia being disrupted. Chinese traders still typically make up the majority of the market however it is the operations of the National Cooperative Business Association that dominate debate in Timor’s coffee industry. A quasi-international aid wing of its parent US company, NCBA began operating in Timor largely with the financial backing of USAID. They have developed an operation

¹¹² The relocation of the capital of Ermera from the mountain top town of Old Ermera to the Indonesia built town of Gleno sitting on an open plain had a clear surveillance function. Interview with Matues Tilman, KSI, 26th June 2001

¹¹³ TERADP *op. cit.* p. 1

¹¹⁴ Unsolicited Proposal

¹¹⁵ Hall Hil & Joao Saldanha, ‘The Key Issues’, in Hal Hill and Joao Saldanha *East Timor: Development Challenges for the World’s Newest Nation* Institute of South East Asian Studies, Singapore, 2001, p. 3

¹¹⁶ Sam Filiaci, quoted in ‘Mark Dodd, ‘Hard Grind: Weak Coffee Prices add to Fledgling Nation’s Woes’, Sydney Morning Herald 19-12-2000

which dominates the high quality end of the market, purchasing 35% of all coffee and generated \$4.1 million in export sales.¹¹⁷ NCBA is the single largest employer in East Timor, employing 300 full time staff and 3,900 seasonal workers in 2001. Exploring the NCBA project in detail offers a valuable insight into the overall industry in Timor.

The project was largely initiated by a visiting US senator who saw that the coffee trade was monopolised by Indonesian military interests.¹¹⁸ They were able to negotiate market access by entering into a temporary partnership with Suharto's daughter, 'Tutut' just after PT Denok's main founder, General Benny Murdani fell from grace in Jakarta's politics.¹¹⁹ They even received backing from Suharto himself.¹²⁰ NCBA utilised the existing PUSKUD network, effectively substituting the military's role and becoming the largest coffee purchaser. Calculating farm-gate prices from the open market, it used to pay better prices than in Indonesian times but many Timorese argue that it continues to wield quasi-monopolistic control over the industry.¹²¹

The organisational structures of NCBA have shifted from with their historical precedent. Following the September 1999 violence, the structure of the project was

¹¹⁷*Ibid.* p. 3

¹¹⁸It would not be in the realm of conspiracy to suggest that the US project had a surveillance function. It was initiated largely in the wake of the 1991 Santa Cruz massacre at a time when world interest in East Timor was renewed. Similarly, Lansell Taudevin, the coordinator for AusAid projects for much of the mid 90s and often the only consistent Australian presence, was 'asked to provide reports of "anything amiss"' to the Australian government as part of the funding agreement. see Lansell Taudevin, *Too Little Too Late*, Duffy and Snellgrove, 1999 p.76

¹¹⁹Lansell Taudevin, 'The Economic Viability of East Timor using Indonesian Achievements as a Benchmark', in Lansell Taudevin and Jefferson Lee (eds) *Making Amends: Analysing Australia's Role in Reconstructing East Timor*, Australia East Timor Association, Melbourne, 2000 p. 114

¹²⁰Cindy Shiner, 'East Timor's Coffee Growers Break the Military's Monopoly' *The Washington Post*, July 1998

reorganised with 16 Cooperativa Cafe Organic (CCO) groups set up in the districts, administered at the national level by the Cooperativa Cafe Timor (CCT). There are currently 18,830 members and the Co-op's membership is expected to reach about 25,000 members in 2002.¹²² Characterising the CCOs as collectives is problematic. They regulate who is one their books for both accounting and organic certification purposes and although have a 'democratically elected board of directors' seem to bow to the prerogative of the NCBA management in Dili.¹²³

Today, coffee is grown on about 50,000 hectares covering the higher altitude districts of Aileu, Ainaro, Ermera, Liquica and Manufahi (see Appendix 1). About 60% of this land is worked by an estimated 13,000 small holders on properties averaging 1-2 hectares.¹²⁴ Another 16,000 hectares is deserted plantation land, formerly run by PT Denok and its Portuguese predecessor SAPT, and picked by adjoining farmers.¹²⁵ The remaining land is large family plantations or *facendas* such as the 360 hectare property owned by the Carrascalao family in Ermera¹²⁶

About 80% of coffee grown in Timor is an *Arabica* hybrid called *Hybrido da Timor* that emerged at the turn of the century. It attracts a higher price than the *Robusta* variety that dominates production in Brazil and Vietnam and is used in soluble coffees. It grows at altitudes higher than 700 metres, is largely resistant to leaf rust, a

¹²¹Interview with Dr Lucas da Costa, ISEC Economist, Dili, 3 July, 2001; Interview with Jacinto Maia, Coffee Farmers Forum, Dili, 2 July, 2001, *inter alia*

¹²²Development Alternatives International *op. cit.* p. 3

¹²³*Ibid.* p. 16

¹²⁴NCBA *Discussion Notes - Coffee - East Timor*, April 14 2000, p. 2

¹²⁵*Ibid.*

common affliction of coffee plants, and is well suited to the shallow soils and frequent droughts in East Timor. The coffee is largely 'forest coffee', covered in shade by the giant Casuarina trees and free from any chemical inputs for at least the last 25 years.

Other than harvesting the coffee cherry from May to September, the farmers have little interaction with the trees. One industry report described them as 'subsistence farmers who made no serious investment of time or money to increase yields'.¹²⁷ The lack of pruning or planting of new trees has seen yields drop from roughly 600 kg in the 1950s to just 100 kg per hectare.¹²⁸ They have, however, traditionally 'dry-processed' the coffee. This involves removing the pulp around the bean, then drying this 'parchment' in the sun. Marcos Moreno, a coffee consultant employed by the ETTA, was highly critical of these poor production processes which produced a coffee of variable quality.¹²⁹ The subsequent erosion in quality forced the NCBA project to 'wet process' the cherry instead.¹³⁰ They now purchase the coffee cherry directly from the farmer and monitor all parts of the process. This includes early pulping, soaking, washing, hulling and drying to produce a coffee worth 40% to 100% more than dry processed coffee.¹³¹

¹²⁶ Aditjondro, 'An Official Language for a New East Timor?' Speech for seminar organised by Fundasaun Naroman, IMPETTU, 25 April, 2000 available at <<http://www.timoraid/timortoday>>

¹²⁷ Development Alternatives International, op cit. p. 12.

¹²⁸ From information provided by Mr. Cornelio Madeira Exposto, former SAPT plant manager in Fatubessi, quoted in Moreno, Marcos, *East Timor Coffee: An Industry Overview* p. 3

¹²⁹ *Ibid.* p. 6-7

¹³⁰ Interview with Alistair Laird, Technical Manager, NCBA, Dili 27 June, 2001

2.4 The Question of Competitiveness

Since NCBA's entry into the market in 1994, they have been selling to international buyers and roasters in the US and Europe such as Hollands, Royal, Dunkin' Donuts and the Seattle-based cafe chain, Starbucks who purchase two-thirds of the crop.¹³²

The industry is therefore very sensitive to prices set by the New York 'C' - the buying price for processed green bean delivered to the warehouses of the US - which in 2001 has been chronically low.

Such sensitivity to world prices means that all production costs must come in under the market price forcing growers and labourers to scramble over the pieces of a shrinking pie. They are engaged in a race to the bottom with the growers and labourers in other developing countries, many of which have plantation systems generating powerful economies of scale. This is a task made all the more difficult by the industry's historical underdevelopment and the devastation wrought in 1999 which has resulted in 'production and export costs that are among the highest in the world.'¹³³

The wages paid to the 3,600 seasonal workers employed by NCBA tripled from a pre-ballot level of Rp 7,500 per day to Rp. 20,000 per day.¹³⁴ Alistair Laird, the

¹³¹NCBA *TERADP op. cit.* p. 4.

¹³²Laird *loc. cit.*

¹³³Jacqueline Pomeroy, *Coffee and the Economy in East Timor*, Unpublished paper 21st May 2000.p. 4; Rui Nabiero from Delta Cafe explained to farmers when visiting Ermera that he pays 190 Escudos per kilo for 'the best quality coffee' without having to leave his office but NCBA were paying at 320 escudos (Rp. 18,000). Luciano Alvarez, 'No Agreement Yet on the Price (Among Other Things)', *Publico*, 29 Feb 2000

¹³⁴NCBA *discussion paper op cit.* p.4,

technical manager of NCBA who earned his stripes in the plantations of Papua New Guinea commented that, in comparison, workers there only receive \$1.20 per day.¹³⁵ NCBA have been critical of the 'lack of East Timorese labour to provide a full days work for what have now become very high rates of daily pay;'.¹³⁶ As a consequence, other coffee traders are sending parchment to Surabaya where it is processed with cheaper Indonesian labour.¹³⁷ Similarly, Laird has even installed machinery in NCBA's Dili factory, which has succeeded in cutting down staff in one production process from 75 in the previous season to just 12.¹³⁸ These 'rationalisations' are operating at a time when unemployment in Dili hovers around 80%.¹³⁹

Local wage increases can largely be attributed to inflation caused by the withdrawal of Indonesian subsidisation of basic consumer goods and purchasing power of the 15,000 highly paid international staff. In addition to their salaries, for example, UNTAET international staff are paid a daily living allowance of US\$109 per day, which has lined the pockets of those whom George Aditjondro has labeled 'cockroach capitalists' - foreign businessmen who run the expensive restaurants and supermarkets in Dili that ultimately force up prices in the local markets in Dili.¹⁴⁰ When a good local wage for a semi-skilled labourer is just Rp 600,000 per month (approximately \$60.), it is

¹³⁵Laird *loc. cit.*

¹³⁶NCBA *TERADP op. cit.* p. 3

¹³⁷ NCBA *TERADP op. cit.* p. 4; Hill notes that the daily wages of \$3 in some coffee plantations are two to three times higher than those in Indonesia Hill, Hal, 'East Timor's Future: Southeast Asia of South Pacific, *op. cit.* p. 90

¹³⁸Laird *loc. cit.*

¹³⁹ Celia Mather, *The Labour Situation and Workers' Support Groups in Timor Loro Sa'e*, Report of a research visit, 15-25 May 2000. p. 7

¹⁴⁰ George, Aditjondro, 'Self-Determination under Globalisation: Timor Loro Sa'e's transformation from Jakarta's colony to a global capitalist outpost', Department of Sociology and Anthropology, University of Newcastle, Australia, 2000 p. 12

unsurprising that striking and demonstrating workers cite rising prices as the main reason for demanding higher wages.¹⁴¹

Transportation costs have also sky-rocketed due to damaged roads and the loss of many trucks that were used for the Indonesian military's forcible removal of some 250,000 people.¹⁴² The subsequent shortage in supply and Dili's inflation has seen their rental prices quadruple from a pre-ballot Rp. 150,000 to Rp 600,000 in April 2000.¹⁴³ These pressures have also made transportation costs 2.5 to 3 times higher than comparable costs in other low-income countries.¹⁴⁴

Students and farmers raised these problems at a public meeting with UNTAET, asking them to 'weigh up the problems caused by the current costs of fuels, oils; the basic household essential commodities and the levels of basic salaries paid to staff and casual labour, against the costs of local production, especially coffee'.¹⁴⁵ However, there are no signs that UNTAET is considering either price controls or restructuring the pay system of its international staff to stem inflation, hoping instead that their imminent withdrawal will solve the problem.¹⁴⁶ This may improve East Timor's competitiveness but the chronic underdevelopment of the industry requires an actual policy solution.

¹⁴¹Mather *op. cit.* p. 17-18

¹⁴²Richard Tanter, 'East Timor and the Crisis of the Indonesian Intelligence State', in Richard Tanter et al (eds) *Bitter Flowers, Sweet Flowers: East Timor, Indonesia and the World Community* Pluto Press, Annandale, 2001 p. 193

¹⁴³Pomeroy *op. cit.* p. 2

¹⁴⁴FAO/WFP Crop and Food Supply Assessment Mission to East Timor, 19 April 2000, p. 13

¹⁴⁵Teixeira, Jose and Verniau, Serge, "Record of meeting held on June 12, 2001 at the Office of the Cabinet Member for Economic Affairs' June 15, 2001.

Professor Antonio de Serra suggests that UNTAET should implement anti-inflationary policies, such as capping profit margins on fly-by-night foreign operators.¹⁴⁷ However, the prevailing view is to leave the economy to the market and instead, ‘controlling aggregate demand’ as Luis Valdivieso, an IMF senior advisor suggests, through ‘reductions in wages and salaries’.¹⁴⁸ Does this mean cutting bloated UN salaries? For the coffee industry it means ‘rationalising labour laws and pay rates to be competitive in the world coffee industry’.¹⁴⁹ Joseph Hanlon writes that such a policy in UN administered Mozambique resulted in a ‘basic wage that was below the poverty line, forcing people to get a second job or engage in petty corruption’.¹⁵⁰

2.5 The Plight of Farmers

The alternative is to cut the price paid to the farmer but the 10 US cents per kilo for coffee cherry offered by NCBA is already crippling coffee growing districts.

Communities heavily reliant on income from coffee to buy food have suffered from general malnutrition, particularly in the Ermera, Lasuan region¹⁵¹ as per annum income has dropped to \$127.¹⁵² Although some of the malnutrition can be attributed to the September 1999 destruction most of it is due to the dependency on a coffee

¹⁴⁶Mather *op. cit.* p. 18; NCBA is anticipating as much noting, with high wages, that ‘after independence and the departure of the high wage UN-system it should not be so problematic.’ Development Alternatives International *op. cit.* p. 15

¹⁴⁷Serra, Antonio M. de Almeida, *Development Strategy and Policy for Timor Lorosa’e*, Faculty of Economics and Management, Lisboa, 2000, available at <<http://www.ish-lyon.cnrs.fr/iao/SENAS/A.deSerra.html>> p. 9

¹⁴⁸Hanlon, Joseph, “Can East Timor Survive the Aid Industry?: Some Questions from Mozambique”, *The L’ao Hamutuk Bulletin* Vol. 2, No. 3, June 2001, p. 5.

¹⁴⁹NCBA *Discussion Notes loc. cit.*; Pomeroy *op cit.* p. 4

¹⁵⁰Hanlon *op. cit.* p. 6

monoculture that is geographically vulnerable and financially volatile.¹⁵³ Due to the disastrous effects of El Nino, famines were widely reported in 1997.¹⁵⁴

Due to the price drop, Jacob Madeira, a farmer in Old Ermera, estimates his annual income is now between \$50-\$100 - not enough to send his eight children to school or purchase basic commodities such as rice, building materials and clothing.¹⁵⁵ During Indonesian rule he was getting twice this price: enough for a modest yet comfortable existence. Another farmer, Mauricio dos Reis Martins, supplements his income by teaching at the local school, earning \$155 per month.¹⁵⁶ However, the lack of money in the whole community reduces the viability of alternative sources of income. At a public meeting, Mauricio's school decided to drop the fees charged from the Dili price of 5-10 USD for each student per month to just \$2 to soften the effect of the price crash. Despite this accommodation, 117 students out of 267 still cannot afford to pay.¹⁵⁷ Although UNTAET is paying 11 of the 14 teachers wages, it is not feasible for the teaching staff to drop the price any further. For Evaristo da Silva, education gives his children the analytical skills to navigate life's problems: 'If the children can not go to the school in the future - if they are not educated - the violence will grow'.¹⁵⁸

¹⁵¹CDPM, *Agriculture, Rehabilitation and Development* ETO: AGR101, Lisbon, 2001 p. 2

¹⁵²Development Alternatives International *op. cit.* p. 29

¹⁵³CDPM *loc. cit.*

¹⁵⁴Pederson, Jon and Arneberg, Marie (eds) *Social and Economic Conditions in East Timor*, , International Conflict Resolution Program, School of International and Public Affairs, Columbia University, New York and Oslo, FAFO Institute of Applied Social Science, 1999, p. 25

¹⁵⁵Interview with Jacob Madeira , Coffee Farmer, Old Ermera, Ermera, 1 July, 2001

¹⁵⁶Interview with Mauricio dos Reis, Coffee Farmer and School Teacher, Old Ermera, Ermera, 1 July, 2001

¹⁵⁷dos Reis Martins *loc. cit.*

¹⁵⁸Interview with Evaristo dos Santos, Coffee Farmer 30 June, 2001.

With only one harvest each season, farmers have to carefully manage their earnings for the next year. This has led many farmers to stockpile coffee and sell it slowly to maintain a cash flow.¹⁵⁹ Given that the coffee cherry cannot be stored, farmers are dry process the coffee and sell to Chinese traders such as Acinku who offer Rp 6000 per kilo.¹⁶⁰ Farmers usually get their extended family or hired labour from Maubisse or Atambua to assist with the harvest. In they off season they plant vegetables.¹⁶¹

When asked why coffee prices were so low, farmers focused their criticism solely on chain node directly above them, citing either the corrupt practices of CCO staff or the monopoly status of the NCBA project.¹⁶² The high price of the final product on the supermarket shelves of Dili angered many farmers. Also, seeing many CCO staff driving recently purchased cars fueled concerns that they often cheat farmers, writing down the incorrect weight of coffee.¹⁶³ Without further research, it is impossible to know the extent of corrupt practices, but even if this were reformed (as it should be), the greater issue of market inequality persists.

A lack of knowledge about international coffee markets is part of the problem. When Rui Nabeiro from Delta Cafe first visited the district at the beginning of 2000, a reporter noted that he would have to be patient in his explanations: ‘stock exchange, quotations, markets and electronic machinery are words that are not yet in everyday

¹⁵⁹Dr Lucas da Costa *loc. cit.* commented that ‘in Lete Foho this morning I was told that they still have a stock of 3,000 tonnes. Maybe a double or triple figure could be in Liquisa or Ermera, so we still have a huge stock of coffee. Farmers are not willing to sell right now because of the price. Because NCBA is the sole enterprise it looks like farmers have no alternative.

¹⁶⁰It takes between four to seven kilos of coffee cherry to produce one kilo of parchment.

¹⁶¹Interview with some farmer

usage in the coffee plantations of TL'.¹⁶⁴ This may explain one of the main demands of farmers - to let more competitors into the market to break what they perceive to be the NCBA monopoly.¹⁶⁵ Although NCBA do have a tight grip on wet-processing facilities and have tight membership structures, it is hard to imagine another private investor arriving at a different purchasing price once production costs and market prices have been factored in. This is especially so given the \$8 million grant NCBA receives from USAID. Rui Nabeiro and Delta Cafe have acknowledged this much.¹⁶⁶

The best illustration of the broader dilemma facing both Timorese farmers and groups such as NCBA is the industry market chain table (see Appendix 2), taken from the Development Alternatives International report on the NCBA project. It looks at the income and profit derived by the grower¹⁶⁷ processor or cooperative, the importer and roaster or wholesaler calculated on a New York 'C' price of USD0.69/lb at the beginning of 2001.¹⁶⁸ Taking the first column as an example, as a proportion of the wholesale price, East Timor receives approximately 21% while the consuming countries net the remaining 79% of income. Significantly, this does not even take into account the share of final retail price. The picture is even bleaker if the surplus earned by each party is compared.¹⁶⁹ The NCBA project calculates that, after paying costs for depreciation, debt and a 30% tax on profits, they earn USD0.015/kg. If we assume

¹⁶²Interview with Julio Soares Madeira July 1st 2001; dos Reis Martins *loc. cit.*; Madeira *loc. cit.* July 2001; dos Santos *loc. cit.*

¹⁶³ Madeira *loc. cit.*

¹⁶⁴Luciano Alvarez, 'No Agreement Yet on the Price (Among Other Things)', *Publico* 29/2/2000,

¹⁶⁵Record of the Meeting held on June 12, 2001 at the Offices of the Cabinet, Member for Economic affairs. *loc. cit.*

¹⁶⁶Alvarex *loc. cit.*

¹⁶⁷Only the income for the grower can be estimated. To calculate profit would be to place value on abstract labour.

¹⁶⁸By the time a draft of the report was released, the price had fallen further to USD0.64/lb.

that the grower is acquiring no surplus - a fair assumption given the states of partial malnutrition existing in the districts - East Timor receives just under 1% of the surplus while the consuming countries are receiving 99%. This is not a promising picture for national development. Strategies for gaining economic surplus must either engage with nodes higher up in the chain or add value in the producing country.

¹⁶⁹Where surplus equals profit minus costs.

Chapter Three

Opportunities and Risks

3.1 Capturing Value along the Coffee Commodity Chain

Any attempt at increasing the share of income captured along the coffee chain should capitalise on the growing market for ‘conscious consumption’ where consumers are paying a premium for coffee that is high quality, shade grown, organic and ‘Fair Trade’ produced. Although this market is small - Fair Trade sales for example, are only 1% of the world market - it is the fastest growing sector.¹⁷⁰ Industry experts believe East Timor’s organic crop puts it three years ahead of the rest of industry.¹⁷¹ Well processed East Timorese organic coffee already attracts a 15-20% premium above the top specialty grades.¹⁷² Coffee roasters also use East Timor’s beans to smooth the acidic sharpness of their blends: as a result, local coffee is 40% more expensive than the benchmark *Arabica* sold in New York.¹⁷³ The demand for higher quality coffee has been spurred on by decades of bad soluble coffee saturating supermarket shelves. This represents a maturing of tastes in European, US and Japanese markets although some of the demand is arguably due to the rise of marketing to differentiate products. Indeed, Stefano Ponte argues that the rise may be more promising in the specialty area where marketing an image is essential to sales,

¹⁷⁰Ponte *op. cit.* p. 27

¹⁷¹Development Alternatives International *op. cit.* p. 33

¹⁷²*Ibid.* p. 21

¹⁷³Dan Murphy ‘Coffee Production: Ending Military Monopoly has Revitalized East Timor’s Coffee Industry’, *Far Eastern Economic Review*, 18 February, 1999, p. 2

rather than in the high quality sector.¹⁷⁴In pursuing either option, East Timor needs to produce a consistent, high quality product that is successfully branded. All of these factors point to having a well coordinated industry networked with all nodes of the chain. There are several models for this.

ETTA initiatives have focused on ensuring that all East Timorese coffee is certified and marketed as organic.¹⁷⁵ They plan to set up a regulatory regime and local organic associations under the umbrella of the 'Timor Organic Coffee Association' to govern export procedures, quality control and grading, all designed to ensure a distinguishable and uniform coffee.¹⁷⁶ NCBA already have their entire crop organically certified by the international body, Organic Crop Improvement Association who annually inspect and grant certification to the project's participants.¹⁷⁷ At the time of writing it is unclear what final form the regulations will take. Although the National Council, the East Timorese quasi-legislature set up by UNTAET, agreed to the plan in principle, they were still asking for further clarification.¹⁷⁸

It seems unlikely that the ETTA's role will extend beyond organic regulation. In the introduction to a report on coffee commissioned by UNTAET, Serge Verniau, the head of ETTA Agriculture stated that revitalisation of the industry will instead, be

¹⁷⁴Ponte, *op. cit.* p. 25

¹⁷⁵Interview with Serge Verniau, Head of Agriculture, East Timor Transitional Administration, 28 July 2001

¹⁷⁶Establishment of an Organic Product Regime in East Timor, UNTAET June 2001

¹⁷⁷NCBA *TERADP*, *op. cit.* p. 2.

¹⁷⁸Interview with Jose Teixeira, Finance and Investment, East Timor Transitional Administration, 2 July, 2001.

‘primarily industry driven’.¹⁷⁹ He accepted that government can have a role in providing policy and regulatory frameworks but should not be the primary player.

The inadequacies of this position frustrated many farmers and students in Gleno, Ermera who, organised what was a tense public meeting to demand a better price.¹⁸⁰ ETTA officials mediated an interim agreement between the farmers and NCBA, committing themselves to investigate the feasibility of a price control mechanism.¹⁸¹ However, both officials involved subsequently indicated that regulation of the coffee price was neither feasible nor desirable.¹⁸² To force private enterprise to foot the bill would be difficult, given the strategic clout of groups like NCBA¹⁸³ and the possible emergence of a black market transgressing Timor’s porous borders.¹⁸⁴ Mari Alkitiri, the then Economics Minister, acknowledged as much when he explained to farmers that no company would purchase coffee if he forced them to pay Rp 2,500 per kilo.¹⁸⁵ Internationally, Colombia was the last country to abandon set rates a couple of years ago.¹⁸⁶ Alternatively, the volatility of the market makes it impossible for the state to subsidise the farmers, especially during a fragile reconstruction period where assisting one industry involves the taxing another.¹⁸⁷ Even if regulation were

¹⁷⁹ Serge Verniau, Director, Division of Agricultural Affairs, introduction to Marcos Moreno, *East Timor Coffee: An Industry Overview*, Division of Agriculture, East Timor Transitional Administration, September 2000, p. 1

¹⁸⁰ Tilman *loc. cit.*

¹⁸¹ Jose, Teixeira & Serge Verniau, *loc. cit.*

¹⁸² Verniau *loc. cit.*; Teixeira *loc. cit.*

¹⁸³ Commenting on the uncertainty of the makeup of the future government in East Timor, Development Initiatives International report, ‘The Project is fairly well placed to get its positions heard by key decision makers’ Development Alternatives International *op. cit.* p. 36

¹⁸⁴ Maia *loc. cit.*

¹⁸⁵ Interview I had with either Jose T

¹⁸⁶ Interview with Julio Matinez, Agricultural Officer, ETTA, Gleno, Ermera, 29th June, 2001

¹⁸⁷ Hal Hill, ‘Tiny Poor and War-Torn: Development Policy Challenges for East Timor’, *World Development* Vol.29 No. 7, 2001 p. 1140; However, the possibility of large revenues from the Timor Gap oil fields could subsidise national development.

economically feasible the opposition to it is ideological as well as practical.¹⁸⁸ For Moreno, coffee boards 'simply do not work'.¹⁸⁹

The World Bank has been one of the only agencies to provide farmer support through their Pilot Agricultural Service Centre's (PASC).¹⁹⁰ Although, they will not provide a subsidised service, but require farmers to pay free market prices. This commitment is almost ideological. The Bank for example, sent a copy of *Farming Without Subsidies: New Zealand's Recent Experience*¹⁹¹ to an agricultural officer in Gleno not impressed that this principle was given a blanket application. For the Bank, things are simple: the role of government should be 'to create and implement a policy framework that rewards hard work'.¹⁹² With the present coffee prices however, nothing is being rewarded.

Another way to improve quality and consistency is to wet-process small holder coffee at central pulperies. NCBA has processing factories in Maubisse, Aifu, Liquisa and Estado and has indicated that it will expand this capacity allowing farmers to 'concentrate all their activities on harvesting and pruning'.¹⁹³ The problem is that the low price offered by the pulperies has encouraged farmers to dry-process instead - a significant example of market failure which is prevalent in producing countries.

¹⁸⁸See for example, Frances Ghesquierre, World Bank 27 June, 2001; Verniau *loc. cit.*; Moreno *op. cit.* p. 7 *inter alia*

¹⁸⁹Moreno *op. cit.* p. 12

¹⁹⁰'The World Bank in East Timor', *La'o Hamutuk Bulletin* Vol. 1, No. 4, 31st December 2000,

¹⁹¹Sandrey, R. and R. Reynolds, *Farming Without Subsidies: New Zealand's Recent Experience*, MAF Policy Services, New Zealand, 1990

¹⁹²'The World Bank in East Timor' *op. cit.* p. 5

¹⁹³NCBA *TERADP op. cit.* p. 4; There have been various complaints made against NCBA for pumping pollution out of these factories into nearby streams. 'NCBA Merugikan Petani Kopi?' *Talitikum* 11 June 2001 p 22-23

Assuming farmers do use NCBA's factories, this trend has led to better quality coffee and higher prices for the trader running the pulperies, but not necessarily for the farmers.¹⁹⁴ Therefore, the question underlying any discussion of upgrading is, to what extent do groups like NCBA represent the interests of smallholders, and national development generally?

The small surplus currently generated by the NCBA project is divided between staff bonuses, member dividends and capital works. There is also a substantial amount of money being put into projects to assist the coffee harvesting communities, in particular, the Clinic Cafe Timor project. In response to the almost total lack of health care facilities in rural areas, the NCBA set up five clinics that see over 25,000 patients a year for conditions such as upper respiratory infections (32%) and diarrhea (16%).¹⁹⁵ Although largely bankrolled by a USAID grant, NCBA hopes to make it financially sustainable, funding the estimated costs of \$194,566 by adjusting the cherry price and dividend paid to farmers and charging members who deliver less than 1000 kg of coffee.¹⁹⁶ The project also organises a network of retailers to supply consumer goods to farming communities to fill the vacuum left by the collapsed supply networks from Surabaya,¹⁹⁷ and has even repaired several rural roads.¹⁹⁸ Similarly, Delta Cafe is charging a levy on sales in Europe and especially Portugal to build several schools.¹⁹⁹

¹⁹⁴Ponte *op. cit.* p. 25

¹⁹⁵Development Alternatives International *op. cit.* p. 45

¹⁹⁶*Ibid.* p. 38

¹⁹⁷NCBA *Unsolicited Proposal op. cit.* p. 14

¹⁹⁸Pomeroy *op. cit.* p. 2

This corporate assumption of governmental function, while in many cases commendable, does entail a loss of democracy. A government aware of its polity's diverse needs is in a better position to allocate resources, than a company which may base its decisions on the loyalty or profitability of co-op members. Farmers have highlighted this problem: some were annoyed that access to the clinics, for example, was limited to co-op members, while others were critical that clinics are located in areas already serviced by the state.²⁰⁰ The trend of private welfare provision may be formalised. NCBA has already discussed the possibility of becoming a subcontractor to the government to provide health care in certain rural areas with the transitional Ministry of Health.²⁰¹ In the reconstruction and emergency phase of East Timor's development, these concerns are more philosophical than practical, given the dire need the population has for basic medical services. The long-term fear is if the project's needs conflict with the broader needs of the people, especially given the enormous political leverage it commands. One policy document notes, for example,

‘TERADP management will make concerted efforts to assist the future authorities of East Timor with the development of legislation and regulations that foster efficiency, competitiveness and economic growth’.²⁰²

One of the government's attempts to gain control of the surplus generated by industry was the imposition of a five per cent export tax, which came into effect on 1st March

¹⁹⁹ Interview with Abdul Khan, Delta Cafe, Dili, 27 June, 2001

²⁰⁰ Maderia *loc. cit.*

²⁰¹ Development Alternatives International *op. cit.* p. 38

²⁰² *Ibid.* p. 7

2001 at the insistence of the IMF. Despite near universal opposition from key Timorese leaders and industry players, Luis Mendoca, a senior economist with the IMF, argued that it would provide an important source of revenue and was a very low tax by international standards.²⁰³ He argued that the tax burden would fall on foreign companies like the US chain Starbucks and not on Timorese producers.²⁰⁴ However, the inability of both NCBA to pass these costs onto a TNC and the administration to regulate NCBA's balance sheet meant that the taxation burden was simply pushed onto the farmer. Cabinet decided to scrap the short lived tax on the 24th May 2001,²⁰⁵ perhaps buoyed on by NCBA's promise to increase the farmgate price for coffee cherry by one cent if they did so.²⁰⁶ Instead, several commentators have suggested a slow introduction of the tax only after the industry finds its feet.²⁰⁷

Several authors have expressed concerns that business interests will attempt to establish large-scale plantations for intensive coffee production that will alienate farmers from their land and turn them into landless labourers.²⁰⁸ Certainly this is a global trend with an extra one million hectares a year converted into plantations crops for export markets.²⁰⁹ The trend for coffee is less clear. Exporters who target specialty markets are increasingly relying upon estates either through vertical integration or long-term contracts to guarantee consistency of supply²¹⁰, yet for other parts of the

²⁰³Wilson da Silva, 'Timor Ire at Coffee Tax', *Associated Press*?

²⁰⁴*Ibid.*

²⁰⁵Verniau & Teixeira *loc. cit.*

²⁰⁶*Ibid.*

²⁰⁷The East Timorese economist Lucas da Costa argues that the industry could bear a small tax burden in three to four years. Jose Teixeira took a longer term view suggesting 10, 15 or even 20 years before the industry was healthy enough.

²⁰⁸Mather *op. cit.* p. 45; CDPM *op. cit.* p. 4

²⁰⁹Madeley, *op. cit.* p. 92

²¹⁰Ponte, *op. cit.* p. 25

market there is no strategic advantage for TNCs to own a node in a commodity chain that generates no surplus.²¹¹ In Timor it seems unlikely that agribusiness will carve up the land in the medium-term. According to Laird, the synergies of large-scale farming are not there: 'The land is too steep and the people don't want to work'.²¹²

What will be done with abandoned plantation land is unclear. The return of Banco Nacional Ultramarino (BNU), the old financial arm of Portuguese colonialism, has raised questions over Portuguese intentions for their plantations.²¹³ It seems more likely, however, that they will be divided up amongst the population generating a significant amount of employment. Mario Carrascalao, the leader of the Social Democratic Party (PSD) and a plantation owner believes that the government can facilitate this by compensating the former owners.²¹⁴ They presently make use of standard commodity market hedging techniques to protect coop members from downside market risk. Coop will most likely have to rely on expatriate professional managements over the long term.²¹⁵

3.2 Diversification Strategy

During the exit of the Portuguese administration in 1975, FRETILIN, the major independence party proclaimed, 'We are a country of peasants and farmers, but our

²¹¹Ponte *op. cit.* p. 18

²¹²Laird *loc. cit.*

²¹³Aditjondro, George, 'From Colony to Global Prize: Timor Loro Sa'e under a wave of Economic Transformation', *Arena Magazine* No. 47 June/July 2000 p. 31

²¹⁴*Ibid.*

²¹⁵Development Alternatives International *op. cit.* p. 19

people are hungry'.²¹⁶ They argued that the colonial regime orientated agriculture towards profit and not the people.²¹⁷ The current collapse in world coffee prices and consequent pockets of malnutrition in coffee growing areas is a stark reminder of the dangers of relying too heavily on a single crop. Diversification of crops is the obvious way to protect smallholders especially if subsistence crops are considered as an alternative to export crops. If the latter is pursued however, farmers are not in a position to invest nor do they know what is strategic to grow.²¹⁸ It requires coordination and support at the local, national and international levels, and there is the risk that diversification is not a corporate priority.²¹⁹

Occasionally it is profitable to diversify. Last year NCBA exported 400 kg of Vanilla; a crop that does not conflict with the cultivation demands of coffee and is presently worth a record \$10.00 per kg.²²⁰ The project managers have indicated however, that expanding the coffee industry is their priority.²²¹ NCBA intend to increase the number of participating families and expanding the operation to take in all coffee growing areas while enabling farmers to double their productivity.²²² Robert Randolph, the USAID Assistant Administrator for Asia, stated that the number of families under the project could more than double to 40,000.²²³

²¹⁶FRETILIN *The Struggle for East Timor*, Europe-Third World Research Centre, London, 1976, p. 12

²¹⁷Helen Hill, *Fretilin: The Origins, Ideologies and Strategies of a Nationalist Movement in East Timor*, MA Thesis, Monash University, Melbourne, 1978, p. 99; By the 1970s, the Portuguese administration acknowledged the territory's dependence on a 'highly vulnerable monoculture', but it was belated, Gunn, *Timor Lorsaie: 500 Years op. cit.* p. 256

²¹⁸Oliver Brown, Celine Charveriat & Dominic Eagleton *The Coffee Market: A Background Study*, Oxfam Great Britain, 2001, p. 18

²¹⁹CDPM *op. cit.* p. 1

²²⁰Development Alternatives International *op. cit.* p. 37

²²¹*Ibid.*

²²²NCBA *Unsolicited Proposal op. cit.* p. 12

²²³CDPM *op. cit.* p. 4

Effective export diversification requires a commodity which is more secure than coffee and unlikely to suffer from the same crisis of oversupply. The problem here is that even when prices decline, coffee production still might be more profitable than other commodities, especially given the expense of switching crops.²²⁴ It was countries such as Vietnam that originally diversified into coffee production which has exacerbated the present crisis.²²⁵ The problem of coffee oversupply is therefore intimately linked with the long-term decline of prices in most export crops in developing countries - inflamed by the continuing agricultural protectionism of Europe and the US.²²⁶ Talbot points out that no matter how well surplus has been managed in producing countries, income from coffee alone has never been sufficient to serve as an engine of national development.²²⁷

Given the systemic difficulties with export crops, a diversification strategy should include the growing of more staple crops and the development of nation markets. Some commentators have questioned the wisdom of pushing for outright self-sufficiency.²²⁸ However, it was only through Indonesian neglect that East Timor went from being self sufficient in staple food production three decades ago to being ranked at the bottom of Indonesian provinces in terms of food security and agricultural

²²⁴Brown, *loc. cit.* p. 18

²²⁵Chaveriat *op. cit.* p. 5

²²⁶Brown *op. cit.* p. 4; Similarly, Colombia and Bolivia are trying to get their farmers to grow coffee instead of cocaine - with US support. Although one year before President Bush announced his 'war on drugs', the US were the main party to place pressure on the international coffee agreement claiming it was a fair trade violation. Chomsky, Noam, "Plan Colombia" *Z Magazine*, June 2000

²²⁷Talbot, 'Where Does Your Coffee Dollar Go?: The Division of Income and Surplus Along the Coffee Commodity Chain' *op. cit.* p. 15

²²⁸Hal Hill, 'Tiny Poor and War-Torn: Development Policy Challenges for East Timor', *World Development* Vol.29 No. 7, 2001, p. 1142

productivity in 1997.²²⁹ Government can play a role in evaluating and managing land usage, the one policy tool that can limit the exposure of rural areas to an unforgiving market without being fiscally punished. There is support from local Timorese NGOs like the Coffee Farmers Forum and the People's Economic Development Centre (CDEP) for the development of national rice and coffee markets that were stilted under Indonesian rule.²³⁰

3.3 Fair Trade and the Grassroots

The increasing tyranny of the free market faced by producers of export commodities in the South led to the development of Fair Trade – a model of transnational cooperation where all nodes of a commodity chain cooperate to overcome the poverty of the grower.²³¹ Slowly rising in popularity since the 1970s, for coffee farmers, it can improve market access, strengthen producer organizations, pay a better price and importantly, raise awareness in the North about the inequalities of global trade.²³² Both through conscious consumers paying a premium and retail/wholesale outlets taking a cut in profit, Fair Trade is able to offer a capped price of \$2.77 p/kg to producing countries, more than double the New York C average of \$1.10 p/kg.²³³

In the language of GCC analysis, the success of a Fair Trade product depends on how effectively it can enter existing distribution and marketing channels or carve out its

²²⁹Jon Pederson & Marie Arneberg (eds) *op. cit.* p. 25

²³⁰Interview with Rui Castro, , People's Economic Development Centre (CDEP), Dili, 27 June, 2001; Maia *loc cit.*

²³¹Brown *op. cit.* p. 31

²³²*Ibid.*

own. Overcoming these barriers of entry either requires political and consumer pressure to get retailers to stock fair trade and/or the forging of transnational alliances between producers and Fair Trade organizations or NGOs. In both cases, effective marketing must create a distinct story of East Timorese coffee and the plight of its farmers. The often ahistorical and fragmentary nature of contemporary advertising poses several difficulties. Firstly, people may simply forget the message as consumer activism fatigue sets in, especially as East Timor slips from the public view. Secondly, like many political slogans, Fair Trade is a contested concept that the corporate imperative can easily appropriate and degrade.²³⁴ The marketing of East Timor has been exposed to such contestations. For example, companies such as Dili Coffee, replete with radical chic, sell coffee over the internet by telling East Timor's tragic story yet ethically, are indistinguishable from any other coffee seller.²³⁵

NCBA is interested in registering for Fair Trade although they note that the 'overlapping and joint land ownership in East Timor may not be compatible with the Fair Trade system'.²³⁶ There are more significant concerns with then getting this status. They have failed to carve out a niche in consuming countries, although originally they hoped they could.²³⁷ They are instead concentrating on 'getting a quality product out',²³⁸ but it would not be impossible for them to develop those networks. The larger problem is the cooperative structures employed by NCBA. At

²³³ Prices taken from www.globalexchange.org on 28th September, 2001

²³⁴ The classic example is the concept of 'sustainable development'. see for example, John Stauber & Sheldon Rampton *Toxic Sludge is Good for You!: Lies, Damn Lies and the Public Relations Industry*, Common Courage Press, Maine, 1995

²³⁵ see for example <www.dilicoffee.com>; Shiner *loc. cit.*; Murphy *loc. cit.*, *inter alia*

²³⁶ Development Alternatives International *op. cit.* p. 25

²³⁷ Shiner, *op. cit.*

present, they are little more than a roster of suppliers, albeit, paid a small annual dividend.

In contrast, the 5000 people strong Union of Indigenous Communities of the Isthmus Region in Oaxaca, Mexico is a far stronger example of local democracy.²³⁹ Through a Fair Trade alliance with an NGO in a consuming country, the community has gathered a valuable surplus from coffee crops. The results of their labor, shared by all of its members, include schools, health clinics, home visits by doctors, the training of nurses and dentists, and the strengthening of their indigenous culture. This coop has also helped create the region's only public busline; a hardware and farm supply center; healthcare services; cooperative corn mills; an agricultural extension and training program; accounting training; and the only secondary school in the region.

Such cooperation has been this has been the backbone for societies recovering from upheaval. Rebecca Spence, in analysing the findings of the 1993 UNRISD conference on rebuilding war-torn societies, found that many participants thought that reconstruction must be directed away from international and government orientated planning to grassroots organisation such as women's groups, elders and traders. It was felt, from experience, that these were the people who rebuilt society and should therefore be given a greater say in reconstruction planning.²⁴⁰

²³⁸ Laird, *loc. cit.*

²³⁹ available at <<http://www.globalexchange.org/economy/coffee/coffeeCooperatives.html>>

²⁴⁰ Rebecca Spence, 'The Centrality of Community-Led Recovery', in Geoff Haris (ed) *Recovery from Armed Conflict in Developing Countries: An Economic and Political Analysis*, Routledge, London, 1999, pp. 216-17

What a project could look like in East Timor is beyond this study, however examples, both historical and contemporary, can inform discussion. The most radical project was for FRETILIN in 1975, co-operatives of production, distribution and consumption were to be 'the base of economic and social life in East Timor'.²⁴¹ The program was inspired by their luso-marxist contemporaries leading the decolonisation struggle in Portuguese Africa and the need for them - an intellectual urban based party - to win over the largely peasant population.²⁴² Nicolau Lobato, the then leader of FRETILIN spearheaded the idea and describes an example:

'Bucoli people were planning a co-operative for next year's harvest. Villagers will pool their surplus crops (after deducting family needs) for sale in Dili for higher prices than they would get through Chinese middlemen. The receipts will be used as the villagers decide: to buy a truck perhaps or build a co-operative store, to buy wholesale basic necessities or to buy a small tractor'.²⁴³

According to Jose Ramos-Horta, it was FRETILIN's *trabalho de base* (grassroots work) that gave FRETILIN its popularity.²⁴⁴ This work included reaching out into the communities with literacy campaigns, teaching people to read and write in their own language, helping people build schools, health centres and implementing vaccination programs. It is easy to idealise such a program but John Taylor remarks that

²⁴¹FRETILIN *op. cit.* p. 16

²⁴²Helen Hill, *op. cit.* p. 98

²⁴³Freney, Denis, 'FRETILIN in a village, hope comes to Bucoli', *Tribune* 26 November 1974 quoted in Hill, Helen *FRETILIN: The Origins, Ideologies and Strategies of a Nationalist Movement in East Timor* MA Thesis, Monash University 1978. p. 103

²⁴⁴Ramos-Horta, Jose. *Funu: The Unfinished Saga of East Timor*, The Red Sea Press Inc, Lawrenceville NJ, 1987 p. 39

FRETILIN's programs were 'directly relevant, realisable and popular, emerging from specific forms of co-operation with the rural population'.²⁴⁵

It is unlikely that FRETILIN will resurrect such an ambitious collectivisation project given the radically different circumstances they find themselves in. Although, this philosophy is not alien to international organizations. The World Bank has set up the Community Empower Project (CEP) which intends to be a 'form of local governance and structures for a "bottom-up" approach to development'.²⁴⁶ Although they 'are not as legitimate and vibrant as socio-political structures that have emerged out of local, long-term processes', notes *La'o Hamutuk*.²⁴⁷ Also, As the 'Joint Donor' report noted, "At present the talent and energy at village level is more likely to be found around the chefe and the old clandestine structures within the council." It is such structures that the report contends, 'must be built upon if the country's urgent rural development problems are to be solved'.²⁴⁸

Two contemporary examples are pilot projects set up in Acabe and Liquica by the Timorese Socialist Party (PST). Their aim is to form cooperatives through which producers can defend their rights, particularly to sell coffee on the open market in Dili, and even to export.²⁴⁹ Like the FRETILIN project in 1975, it is unclear if this is a brand of crude structural communitarianism or a genuine socially cohesive unit.

²⁴⁵ John G. Taylor, *East Timor: The Price of Freedom*, Pluto Press, Annandale, p. 34

²⁴⁶ 'The World Bank in East Timor', *La'o Hamutuk Bulletin* Vol. 1 No. 4 31st December 2000, p. 6

²⁴⁷ *Ibid.*

²⁴⁸ *Ibid.* p. 7-8

²⁴⁹ Mather *op. cit.* p. 44

Conclusion

When the Philippines' economy was attempting to integrate with the international economy, similar to East Timor's, all it had to offer was commodity exports and cheap labour. According to Richard Falk, these terms were damning for national development:

‘the export compulsion capitalises agriculture at the expense of marginal peasants and domestic demand, while the investment compulsion both depresses real wages and the efforts of workers to resist’.²⁵⁰

Unlike a national identity forged through resisting a colonial power, this postcolonial power - that of the global economy – alienated and impoverished the people instead.

For East Timor to negotiate a different fate, it must capitalise on the few opportunities that exist in the international coffee market for increasing the price of their coffee, while pursuing sensible diversification strategies. One encouraging trend worth embracing is the growing Fair Trade movement. With the decline of state control in producing countries, Fair Trade compensates by constructing an artificial chain that ensures a fair exchange from local grower to consumer. To be effective, there needs to be strong alliance between NGOs willing to lobby and campaign for market access in consuming countries and a coordinated body of Timorese farmers providing a

high quality product. The success of Global Exchange, a US fair trade NGO, in forcing Starbucks to at least stock Fair Trade coffee in their US stores should give heart to campaigners in Australia. Given their slow sprawl over Australia and the 25% of East Timor's crop they purchase it may be the time to build alliances and launch a similar campaign. The Timorese half of that alliance needs to be organised under a better banner than the NCBA project. Cooperatives that are vibrant representative structures that respect and incorporate pre-existing forms of social cohesion are a powerful way of negotiating the market. They can also provide the social support that national governments increasingly cannot and regulate a modernising imperative that often loses sight of the people it is supposed to look after.

²⁵⁰Richard Falk, Foreword in Walden Bello, David Kinley and Elaine Elinson *Development Debacle: The World Bank in the Philippines*, Institute for Food and Development Policy, San Fransisco, 1982 p.3

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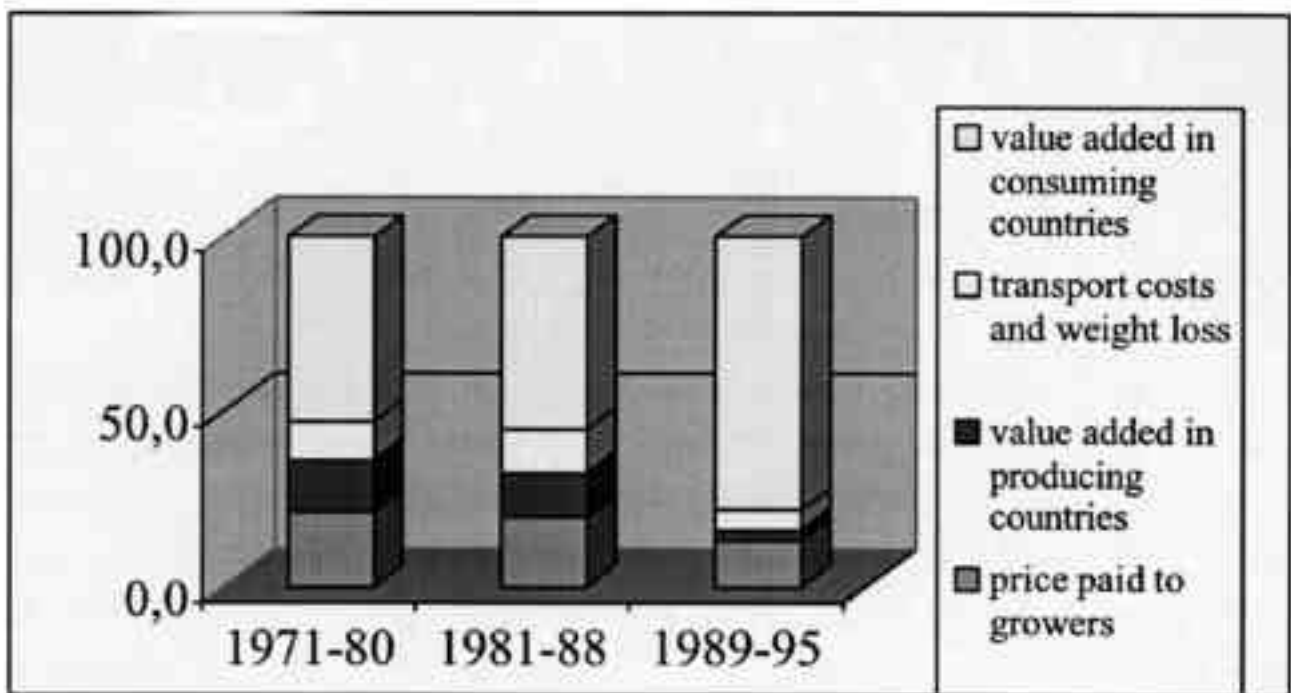
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Appendix Three

Distribution of Coffee Income along the Coffee Chain (1971-80 to 1989-95) (%)



Adapted from Talbot, John M. 'Where Does Your Coffee Dollar Go? The Division of Income and Surplus along the Coffee Commodity Chain', *Studies in Comparative International Development* Vol. 32 no. 1 pp 56-91 Taken from Ponte, Stefano, *The 'Latte Revolution'? Winners and Losers in the Restructuring of the Global Coffee Marketing Chain*, Centre for Development Research Working Paper 01.3, Copenhagen, June 2001, p. 15

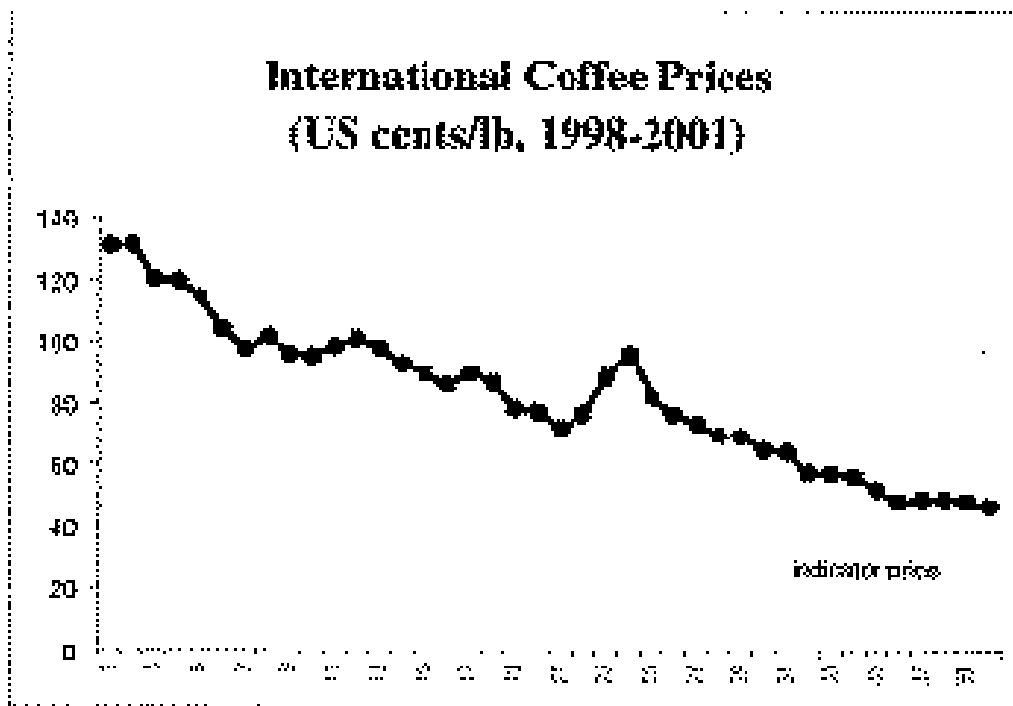
Appendix Four

NCBA Industry Market Chain Price Breakdown

Market Level	Non-Organic USD/kg	Non-Organic USD/kg	Non-Organic USD/kg	Organic USD/kg
I. Grower-Member				
Selling Price of Cherry	0.110	0.120	0.130	0.130
Variable Cost	0.005	0.005	0.005	0.005
Gross Sales Income	0.105	0.115	0.125	0.125
Dividend Remitted by Coop	0.009	0.014	0.019	0.014
Total Net Income	0.114	0.124	0.134	0.134
II. Processor - Cooperative				
Cherry to Green Bean Ratio (7:1)	7	7	7	7
Green Bean Selling Price, FOB Port Dili	1.520	1.618	1.708	2.011
Purchase Cherry	0.770	0.940	0.910	0.910
Other Variable Costs	0.533	0.533	0.533	0.533
Gross Margin on Variable Costs	0.217	0.245	0.263	0.568
Q&M, Depreciation and Debt*	0.195	0.195	0.195	0.195
Pre-tax Income	0.022	0.050	0.068	0.373
Tax on Profits 30.0%	0.007	0.015	0.020	0.112
After-tax Net Income	0.015	0.035	0.048	0.261
Distribution of After-tax Income				
Capital Reserve 30.0%	0.005	0.011	0.014	0.078
Staff Bonuses 30.0%	0.005	0.011	0.014	0.078
Dividend to Grower 40.0%	0.008	0.014	0.019	0.104
*assumes Q&M+Depreciation @ 65% of gross margin, included 1% export tax				
III. Importer				
Selling Price, FOB Warehouse US	1.949	2.047	2.135	2.440
Purchase Green Beans, FOB Port, Dili	1.520	1.618	1.708	2.011
Ship, Store & Sell	0.352	0.352	0.352	0.352
Pre-tax Net Income	0.077	0.077	0.077	0.077
IV. Roaster - Wholesaler				
Selling Price, Wholesale	7.310	7.520	7.790	8.130
Purchase Green Beans	1.949	2.047	2.135	2.440
Roast, Pack & Sell	4.000	4.000	4.000	4.000
Pre-tax Net Income	1.361	1.473	1.655	1.690

Source: NCBA East Timor and Royal Coffee Inc

Appendix Five



Source: ECO statistics, indicators composed of weighted-average prices of robusta and arabica.



Source: FAO statistics