update October 2012

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Informed Analysis, Expert Opinions

Executive brief

Cocoa sector

1. Background and key issues

The international cocoa trade currently has a global market value of over US$5 billion, with around 72% of global cocoa supplies originating in African, Caribbean and Pacific (ACP) group countries.

"Around 72% of global cocoa supplies originate in ACP group countries"

Cocoa is largely produced in West Africa although a considerable amount comes from Central Africa, with a focus on fine/flavoured cocoa in the Caribbean and the Pacific.

Beyond the ACP, Indonesia has a significant production of between 450,000 (2010/11) and 500,000 tonnes (2011/12). Although in the 1990s Brazil was a former major cocoa producer, disease outbreaks devastated production; however, Brazilian production is now on the rise. Meanwhile production in Ecuador faces problems. Nevertheless, cocoa will remain an essentially ACP export for some time to come.

Europe has the largest chocolate industry in the world and accounts for around 40% of global cocoa grindings.

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However, grinding operations are increasingly taking place in producing countries such as Côte d'Ivoire and Ghana. ACP countries supply close to 90% of the EU's cocoa beans, with Côte d'Ivoire and Ghana alone accounting for 60%. Trade largely takes place on a duty-free basis either under the Economic Partnership Agreement (EPA) or interim EPA (IEPA) arrangements. In the case of countries trading under IEPAs the current September 2011 EC proposal to amend market access regulation 1528/2007 is causing some concern, since, given the state of regional EPA negotiations in West and Central Africa, this could potentially threaten duty-free access to the EU market for processed cocoa products from 14 January 2014.

Three intermediate processors (Barry Callebaut, ADM Cocoa, and Blommer Chocolate) control roughly 55% of the world's industrial chocolate, whereas the retail level is dominated by six multinationals: Mars, Nestlé, Hershey, Philip Morris (Kraft-Jacobs-Suchard-Côte d'Or), Cadbury (part of Kraft Foods since 2010), and Ferrero.

> *"Three intermediate processors control roughly 55% of the world's industrial chocolate"*

With Asian demand for cocoa-based products growing strongly, how ACP cocoa-producing economies position themselves to capitalise on evolving global demand could carry important consequences for individual cocoa sectors, particularly in terms of the development of value-added processing activities.

Cocoa is traded on two world exchanges – London's Euronext.liffe in British pounds and New York's ICE Futures in US dollars. World prices can be highly volatile on a daily basis, subject to speculation and investment considerations, with currency movements at times compounding this volatility. Since 2000/2001 cocoa prices have increased by 86% in real terms, but input costs have also risen substantially. Managing price volatility to ensure stable farm-gate prices commensurate with increases in input costs is essential to provide a solid foundation for the further development of cocoa production to meet rising global demand.

Since 1973, the London-based International Cocoa Organization (ICCO) has coordinated and administered international cocoa agreements, with the aim of stabilising world prices at remunerative levels and promoting balanced market development. Since 1973 there have been seven agreements, and over time the agreements have moved away from price support measures, including export quotas and buffer stocks. The Sixth International Cocoa Agreement was negotiated in Geneva in 2001 and came into force provisionally on 1 October 2003. The Seventh International Cocoa Agreement, negotiated in 2010 in Geneva, is expected to come into force in October 2012. It seeks to:

- promote international cooperation in the world cocoa economy to strengthen national cocoa economies;
- secure fair prices and promote transparency;
- promote a sustainable cocoa economy;
- encourage the consumption of chocolate and cocoa-based products;
- enhance quality and encourage the elimination of trade barriers.

Within the global cocoa economy there has been an increasing focus on sustainability. This takes many forms, ranging from the growing trend towards fair-trade chocolate products, to a growing commitment to eliminating child labour from cocoa production processes.

2. Latest developments

Global production and demand trends 2011–12

The 2010/11 crop year (October/September) was exceptional owing to the favourable impact of the La Niña weather phenomenon on all West African growing regions for the second year in a row. Even though Indonesian production was affected by diseases and unfavourable weather, world production reached the record level of 4.3 million tonnes, an 18.5% increase over 2009/10. Despite the conflict which affected Côte d'Ivoire, in 2010/11 some 1.5 million tonnes of cocoa were produced while Ghanaian production reached over 1 million tonnes. This should have pushed down prices; however, the uncertainty generated by the conflict in Côte d'Ivoire and subsequent January 2011 trade embargo served to support prices for the first quarter of 2011. This was helped by rising Asian demand, which prompted prices to peak at £2,425 per tonne in March 2011 as industrial users replenished their stocks. Subsequently prices fell as the political situation in Côte d'Ivoire was resolved and the resultant surplus began to exert pressure on prices.

In 2010/11, the world cocoa surplus (seasonal production minus seasonal consumption) reached 347,000 tonnes, with 1.7 million tonnes in stock, giving a stocks-to-use ratio of 45.4%. The market effect of the high stocks-to-use ratio was compounded by declining European consumption linked to the ongoing financial crisis. (See Table 1 for 3-year production figures.)

Table 1: Annual production of cocoa beans from 2009–2012

	2009/10		2010/11 (estimate)		2011/12 (forecast)	
	('000 tonnes)	%	('000 tonnes)	%	('000 tonnes)	%
Africa	**2,483**	**68.4**	**3,223**	**74.9**	**2,839**	**71.7**
Cameroon	205		230		200	
Côte d'Ivoire	1,242		1,511		1,410	
Ghana	632		1,025		890	
Nigeria	235		240		210	
Others	168		217		109	
America	**516**	**14.2**	**544**	**12.7**	**529**	**13.4**
Brazil	161		200		180	
Ecuador	150		145		150	
Others	205		200		199	
Asia & Oceania	**633**	**17.4**	**537**	**12.5**	**593**	**15**
Indonesia	550		450		500	
Papua New Guinea	39		47		48	
Others	44		40		45	
World total	**3,632**	**100**	**4,304**	**100**	**3,990**	**100**

Source: ICCO Quarterly Bulletin of Cocoa Statistics, Vol. XXXVIII, No. 1, Cocoa year 2011/12

The 2011/12 crop year started off in October with high volumes in West Africa, but trailed off rapidly with a dry spell of over 4 months in Côte d'Ivoire and Ghana. Moreover, cocoa trees were on their 'off-year' after the exceptional 'on-year' crop of 2010/11, while farmers less intensively worked their trees in the light of much lower cocoa prices. On 15 December 2011, cocoa prices were quoted at £1,234 in London, the lowest level recorded in 2011. The scale of price declines in 2011 had not been seen in the cocoa sector since 1977. (See Table 2 for cocoa prices over 2008–2012.)

Indeed, 2011/12 will be a deficit production year, although this will not be as large as initially projected (under 43,000 tonnes compared to the earlier forecast of 71,000 tonnes). Estimates of output in Côte d'Ivoire were revised upwards by 5% and Brazil should also have better results than expected (+10,000 tonnes). However, figures for Nigeria were revised downwards. The US National Oceanic and Atmospheric Administration reported a 50% chance that El Niño conditions will develop during the second half of 2012. This could exacerbate the deficit in the coming 2012/13 season, causing prices to climb again. ICCO analysis suggest the El Niño phenomenon leads to an average drop of 2.4% in world cocoa output: 2.03% for Côte d'Ivoire, 1.72% in Ghana, 2.4% in Indonesia, with the Ecuadorian harvest shrinking by 6% on average.

Table 2: Cocoa monthly averages of daily prices (ICCO, US$ per tonne)

	2006	2007	2008	2009	2010	2011	2012
January	1,577.78	1,701.99	2,215.85	2,626.00	3,525.12	3,164.86	2,307.62
February	1,545.08	1,813.88	2,523.07	2,647.59	3,276.55	3,471.10	2,356.24
March	1,544.13	1,924.20	2,670.41	2,509.97	3,089.65	3,392.97	2,359.25
April	1,552.37	1,977.20	2,628.33	2,555.17	3,221.24	3,113.51	2,266.78
May	1,594.45	2,004.84	2,689.62	2,480.74	3,178.48	3,070.77	2,313.93
June	1,606.65	2,016.69	3,021.76	2,700.36	3,230.83	3,015.64	
July	1,676.65	2,152.65	2,953.68	2,791.35	3,229.55	3,167.18	
August	1,610.79	1,902.09	2,810.47	2,956.66	3,071.71	3,064.31	
September	1,567.42	1,938.08	2,678.96	3,142.86	2,874.93	2,873.88	
October	1,529.63	1,914.68	2,252.28	3,372.50	2,927.46	2,680.04	
November	1,581.18	1,966.84	2,067.72	3,384.13	2,910.31	2,527.43	
December	1,702.50	2,113.13	2,457.09	3,497.58	3,060.02	2,196.85	
Annual average	**1,590.72**	**1,952.19**	**2,580.77**	**2,888.74**	**3,132.99**	**2,978.21**	

Source: International Cocoa Organization

World cocoa grindings are increasing, despite economic and financial problems in OECD countries.

"World cocoa grindings are increasing, despite economic and financial problems in OECD countries"

This is linked to rising demand in Asia and other rapidly growing developing economies. However, the rate of growth in grindings is slower than the historical average.

While Europe remains the main grinder of cocoa and principal source of demand, growth in consumption in Asia is set to gradually transform patterns of global cocoa demand. Traditionally, grinding figures have been linked to regional consumption figures, but this is becoming less the case as Africa continues to increase its share of world grinding, reaching 18.1% in 2011/12 according to ICCO forecasts (see Table 3). A critical issue in the coming period will be how this expanded African grinding capacity will interact with growing demand for cocoa in Asian markets.

This needs to be seen against the background of the 5.7% increase in grindings in Asia (up to 157,000 tonnes) during the first quarter of 2012. This was faster than the increase in Brazilian cocoa grindings and in contrast to the trend in grindings in North America and Malaysia which dropped by 4.04% and 8.4% respectively (according to the National Confectioners Association).

Asia's growing appetite for chocolate is no surprise: two-thirds of the world's population live in Asia but only consume around 16% of global chocolate. Barry Callebaut expects double-digit growth in its sales to Asia in the foreseeable future.

Asia's growing appetite is largely for cocoa powder rather than cocoa butter, demand for which is on the decline as some candy manufacturers switch to lower-priced vegetable oils such as palm oil, shea butter etc.

"Asia's growing appetite is largely for cocoa powder rather than cocoa butter"

In June 2012, cocoa butter was priced at about US$2,470 per tonne against US$3,900 for cocoa powder. However, these cocoa butter price levels were still much higher than palm oil, a cocoa butter substitute, which was under US$1,000 a tonne at the end of June 2012.

Table 3: Annual grindings of cocoa beans 2009–2012

	2009/10		2010/11 (estimate)		2011/12 (forecast)	
	('000 tonnes)	%	('000 tonnes)	%	('000 tonnes)	%
Africa	**685**	**18.4**	**656**	**16.7**	**722**	**18.1**
Côte d'Ivoire	411		361		425	
Ghana	212		230		240	
Others	61		65		57	
Europe	**1,523**	**40.8**	**1,612**	**41.2**	**1,599**	**40.1**
Germany	361		439		450	
Netherlands	525		535		520	
Others	637		638		629	
America	**815**	**21.8**	**855**	**21.8**	**851**	**21.3**
Brazil	226		239		235	
USA	382		397		400	
Others	207		218		216	
Asia & Oceania	**708**	**19**	**792**	**20.2**	**820**	**20.5**
Indonesia	130		190		220	
Malaysia	298		305		300	
Others	280		297		300	
World total	**3,730**	**100**	**3,914**	**100**	**3,992**	**100**
Origin grindings	**1,527**	**40.9**	**1,594**	**40.7**	**1,680**	**42.1**

Source: ICCO Quarterly Bulletin of Cocoa Statistics, Vol. XXXVIII, No. 1, Cocoa year 2011/12

Emerging trends and issues in the cocoa sector

Issues linked to sustainability are of growing concern in the cocoa industry. Against this background, private companies are increasingly rolling out programmes to promote sustainable forms of cocoa production.

"Issues linked to sustainability are of growing concern in the cocoa industry"

This is in part linked to concerns over the need to secure cocoa bean supplies to meet rising Asian demand for cocoa-based products.

ICCO and others support the World Cocoa Foundation (WCF) created in 2000 by a group of companies such as ADM, Armajaro, Barry Callebaut, Nestlé and Cargill, chaired currently by Kraft Foods. The companies supporting the WCF between them account for more than 80% of the global cocoa market. The principal aim of the WCF is to promote and coordinate sustainable cocoa production and consumption. In 2011, WCF registered five new corporate members from Nigeria, the US and Indonesia.

During the Symposium on Global Agriculture and Food Security, which took place alongside the G8 Summit in Washington in May 2012, the WCF launched a US$4 million initiative to train and improve farming techniques of some 35,000 small-scale family farmers in Côte d'Ivoire, Nigeria and Cameroon. This will be carried out under the auspices of WCF's ongoing US$40 million Cocoa Livelihoods Program, which is co-funded by the Bill and Melinda Gates Foundation and 16 WCF members.

In addition to collective initiatives, individual companies have also launched their own. For example, Hershey has developed a text messaging service to support cocoa farmers in the field by providing critical information on fertiliser application, plant husbandry, harvesting techniques and other farming practices, as well as social messaging. Mars and other confectionery makers have committed themselves by 2020 only to use cocoa that has been certified as sustainably produced. Barry Callebaut (which accounts for 12–15% of the world's grindings) for its part is focusing on new areas suitable for sustainable cocoa production, and is also expanding its existing processing operations in Côte d'Ivoire, striking new outsourcing deals and expanding its gourmet business.

International institutions such as the World Bank are also involved in promoting sustainable cocoa, with the International Finance Corporation (IFC) investing US$55 million in Armajaro Trading in an initiative intended to meet the soaring demand for sustainably sourced cocoa.

In addition, under various development cooperation instruments, the EU continues to seek to improve the contribution of commodity production to poverty alleviation. In 2007, the EC launched its All-ACP Agricultural Commodities programme (AAACP). The AAACP website lists activities explicitly involving cocoa in Haiti and Cameroon, where four joint cocoa/coffee-sector-related initiatives are under implementation at a total cost of €250,000. The cocoa sector also benefits under this programme from cross-sector training and organisational development initiatives.

Closely linked to the question of sustainability is the emergence of fair-trade cocoa, which is meeting a growing share of demand. This potentially offers an area for joint ACP–EU action, particularly given the EC's growing policy interest in this area. Also important is the recognition of the relevance of policies on strengthening supply chains at the international level to promote more sustainable patterns of production, as noted in the February 2011 EC communication to the Council entitled 'Tackling the challenges in commodity markets and on raw materials' (see *Agritrade* article 'Agriculture speculation and the EC raw materials communication', 1 March 2011).

Another dimension of the sustainability issue of relevance to the ACP is the intensifying debate on the elimination of child labour throughout the cocoa supply chain. The November 2011 European Parliament report by Vital Moreira stressed the urgency of addressing child labour issues in cocoa supply chains. Indeed, on 14 March 2012, the European Parliament adopted a resolution calling for the EC 'to get tougher in negotiating trade agreements' on the child labour issue. Specifically the resolution called for the creation of 'accredited, third-party-audited traceability for the supply chain' and a labelling scheme for cocoa, so that consumers 'can vote with their wallets to end child labour'.

In the Caribbean, after many years of declining production, the prospect is emerging of a renaissance of Caribbean fine/flavoured cocoa production.

> *"After many years of declining production, a renaissance of Caribbean fine/flavoured cocoa production is emerging"*

Here the focus is increasingly on securing the price premiums associated with supplying manufacturers of quality-differentiated chocolate products. The new targeted marketing strategies being developed require both a consistency of products quality in line with end user requirements and an expansion of the volumes delivered (see *Agritrade* article 'Structural reorganisation and new strategy required for Caribbean cocoa sector', 20 August 2012). In some Caribbean countries, these developments are leading to a structural reorganisation of the sector, although the strategies being pursued differ markedly from country to country (see *Agritrade* article 'Caribbean looking to boost cocoa production', 10 June 2012). A common aspiration, however, is to promote local value-added processing of cocoa, to redefine the basis for the integration of the Caribbean fine/flavoured cocoa sector into global supply chains. The current challenges faced in the Caribbean can be seen as twofold:

- production and processing-related issues (disease, certification, cost of labour, mechanisation of operations);
- corporate issues related to the identification of strategic alliances with international chocolate companies capable of building up local value-added processing industries.

Similar aspirations exist among Pacific ACP cocoa producers, but with quality issues faced often being at a much more fundamental level (see *Agritrade* article 'Quality issues seen as critical in PNG cocoa sector', 9 August 2011).

The future basis for ACP–EU trade in cocoa products

Progress towards comprehensive regional EPAs between the EU and regional groupings of ACP states in West Africa and Central Africa has been slow. In 2007 to avert any loss of duty-free market access for (among other products) processed cocoa beans, Côte d'Ivoire, Ghana and Cameroon bilaterally initialled IEPAs with the EU.

On 30 September 2011, the EC adopted a proposal 'to amend the market access regulation … 1528/2007', which provides transitional duty-free access to ACP countries whose governments have initialled an IEPA. This proposal calls for the EC to be empowered to 'amend the list of countries that benefit from the preferences … by removing those which have still not taken the necessary steps towards ratification of an EPA'. The EC would be empowered to reinstate countries on the list where the governments concerned 'have since taken the necessary steps towards ratification of their respective agreements after removal from Annex I'.

Currently, given the state of regional EPA negotiations in both West and Central Africa, this could potentially affect exports of cocoa from Cameroon, Ghana and Côte d'Ivoire. Any reversion to the generalised system of preferences (GSP) treatment could hold back efforts to move up the cocoa value chain, bearing in mind the tariff escalation which is a feature of the cocoa sector under alternative trade schemes such as the EU's GSP scheme.

"Any reversion to GSP treatment could hold back efforts in West and Central Africa to move up the cocoa value chain"

This aside, the governments of the countries concerned are committed to concluding the negotiations process before the deadline of 1 January 2014 proposed by the EC. In this context there are no immediate concerns over the reimposition of import duties on cocoa product export, particularly following the vote in the European Parliament trade committee to move the proposed EC deadline to 1 January 2016. However, in the longer term, concluding region-wide EPAs in West Africa and Central Africa is likely to remain a challenge.

Developments in West and Central Africa

As stated earlier, West Africa is the largest cocoa-producing region in the world. According to the ICCO in 2011/12 (October/September), out of a forecast global production of 3,990,000 tonnes, Côte d'Ivoire will account for 1,410,000 tonnes (down from a record crop of 1,510,000 tonnes in 2010/11) and Ghana for 890,000 tonnes (compared to 1,025,000 tonnes in 2010/11). The 2010/11 crop year (October/September) was exceptional due to favourable weather conditions in all western African growing regions for the second year in a row. Less favourable weather conditions in 2011/12, coupled with lower market prices, account for the reduced production in the current season.

In 2011, given its importance as a global cocoa producer, the political crisis in Côte d'Ivoire and subsequent trade embargo influenced cocoa market sentiments; first supporting prices and subsequently, following the resolution of the crisis, seeing prices fall dramatically. These price declines were compounded in the latter part of 2011 by the introduction of cocoa sector reforms in Côte d'Ivoire, which restored state intervention in the sector. Starting in October 2012 (for the 2012/13 crop year), farm-gate prices in Côte d'Ivoire will once again be set by the state, rather than being left to the vagaries of volatile international prices.

These reforms prompted the introduction of forward auctioning of the new Ivorian cocoa crop in 2012. Indeed from January 2012 two Ivorian cocoa crops were being placed on the market in a single season. This served to contribute somewhat to a lowering of international prices.

In terms of the challenges faced in Côte d'Ivoire, full details of the envisaged reforms have not yet been announced; yet these reforms will need to be in place in a form acceptable to industry stakeholders by October 2012, the beginning of the new season. Major questions remain concerning pricing (guaranteed price for farmers, evaluating costs of getting cocoa from the bush to the ports, etc.) and quality assurance. European processors and chocolate makers have been stockpiling supplies of beans, fearing the London market could face a temporary supply crunch if Côte d'Ivoire were to delay exports at the start of the new 2012/13 season on 1 October as a result of shortcomings in the implementation of planned reforms (for more details see ***Agritrade*** special report 'Cocoa reform in Côte d'Ivoire', forthcoming 2012).

More generally, there are fears that a structural decline in production is imminent in Côte d'Ivoire due to ageing trees and a lack of investment during a decade of political upheaval.

"There are fears that a structural decline in production is imminent in Côte d'Ivoire"

However, some analysts dispute this view, pointing to the bumper 2010/2011 cocoa crop that occurred despite violent political conflict, with high prices encouraging a surprisingly high level of crop husbandry which, when combined with ideal weather, led to a record crop.

However, shortages of labour on cocoa farms, linked to competition from rubber plantations, appear to be threatening cocoa production, and have been compounded by conflict-related urban migration. This highlights another fundamental challenge facing the Ivorian cocoa sector, namely re-establishing security and political stability, which will need to address the difficult task of dismantling extortion rackets run by various bodies. All of these are cutting into the profits of growers and threatening to undermine the ongoing reforms.

Restoring security and stability would provide a basis for getting to grips with the backlog of investment in physical infrastructure, particularly roads, which currently serves to raise cocoa production costs.

Meanwhile, in Ghana – where farm-gate prices have always been state-controlled within moves towards privatisation of marketing of cocoa –the exceptional 2010/11 crop was, according to government officials, a result of the introduction of new farming techniques and good weather. In this season, the country produced 1,025,000 tonnes, compared to 632,000 tonnes in 2009/10. However, some analysts suggest that a reversal of smuggling flows, with Côte d'Ivoire representing more than 100,000 tonnes of the year-on-year change in volume, was also an important factor. The political crisis in Côte d'Ivoire strengthened existing, and opened up new, smuggling routes into Ghana from as far as the western Côte d'Ivoire towns of Daloa, Gagnoa and Bouafle in the heart of the Ivorian cocoa belt. Significantly, these routes could handle reversed trade flows should strong price differentials between the two countries emerge, favouring cocoa sales in Côte d'Ivoire. In this context it should be noted that in 2009/10, smuggling flows had gone the other way as cocoa prices were higher in Côte d'Ivoire than in Ghana. This suggests the need for closer policy coordination between the governments of Ghana and Côte d'Ivoire.

In 2011/12, Ghanaian cocoa production is expected to fall to 850,000 tonnes due to dry weather and price declines, which have led some producers to withhold some of their crop. Moreover, Cocobod, the Ghanaian Cocoa Board, has registered a shortfall of around 70,000 tonnes between official cocoa purchases and its inventory as some local licensed buying companies (LBCs) probably overstated purchases to gain advance funding. In May 2012 LBCs were warned that their licences to operate could be suspended if the discrepancy was not urgently addressed.

In 2012, the Ghanaian government began a US$10 million programme to distribute 20 million higher-yield seedlings to farmers in a bid to rehabilitate old plantations and boost output. This is considered necessary since ageing trees have reduced yields and/or are more sensitive to diseases like black pod and swollen shoot. In addition, depletion of nutrients in the soil on older plantations has also created a need for increased use of fertilisers, raising production costs.

The 2010/11 Cameroon production hit a record of 240,000 tonnes. The objective of the Cocoa Development Authority (Sodecao) was to attain 250,000 tonnes in 2011/12. However, in the first months of 2012, lack of maintenance on plantations, heavy rains hampering the drying of beans and damage to unpaved roads slowed down activities. Attacks by caterpillars and Black Pod Disease also delayed the start of the mid-crop harvest.

Although cocoa activities have been tax free for many years in Cameroon, the government is now drafting a proposal for a cocoa export tax of around 20 cents per kilo, which is intended to provide an incentive for local grinding and processing of cocoa. This legislation is scheduled to be tabled in Cameroon's parliament by November 2012.

Currently Cameroon's sole cocoa grinder, Sic-Cacaos, a subsidiary of Barry Callebaut, has a grinding capacity of 30,000 tonnes per year. However in 2010/11, it purchased a record 33,894 tonnes, with the excess tonnage being placed in storage. In May 2012 Morocco's leading chocolate-making company, Compagnie Chérifienne de Chocolaterie, announced that it will build a factory with a grinding capacity of 40,000 tonne per year, potentially providing a major boost to cocoa processing in Cameroon.

Reliable output figures are hard to come by for Nigeria. ICCO forecasts a crop of 210,000 tonnes in 2011/12, while the Cocoa Association of Nigeria puts it at 300,000–350,0000 tonnes, with estimates of a further increase of 10–15% in 2012/13 as plantations mature and farmers embrace new husbandry techniques.

Elsewhere in Africa, São Tome production declined by 8.1% in 2011 to 2,218 tonnes from 2,413 tonnes in 2010. Revenues also fell by 8%, even though organic fair-trade cocoa has been given a boost lately with production reaching 600 tonnes by mid 2010. As of last year in Liberia, a Food for Progress programme in partnership with the US Department of Agriculture, World Cocoa Foundation and others is establishing cocoa quality standards, an internationally recognised grading system, and is assisting legally registered farmers' associations in the direct sale of their cocoa to exporters.

Caribbean cocoa sector developments in 2011/12

The premium brand chocolate market is expanding at more than 10% per annum worldwide, with the EU and US markets being major contributors to this growth. However, only 5% of global cocoa production consists of fine/flavoured cocoa. In this context, small-scale producers in Jamaica, Guyana, Belize and Trinidad and Tobago are increasingly looking towards establishing direct marketing links with these high-value market niches. This often requires investments in improving the quality of cocoa produced, establishing recognisable quality standards and developing closer ties with end-users (e.g. high-end chocolate manufacturers).

Both the EU and US have extended support to the Jamaica Cocoa Farmers' Association (JCFA), which is seeking to play a greater role in marketing Jamaican cocoa, both through representation on the Cocoa Industry Board (CIB) and through its own marketing efforts. Considerable importance is attached to producers' organisations establishing direct relationships with end-user producers of quality-differentiated chocolate products.

In the Caribbean considerable importance is attached to establishing direct relationships with producers of quality-differentiated chocolate products

In 2011/12 JCFA has been consolidating direct commercial relations with Hershey in the USA and exploring similar relationships with buyers in Asia, Europe and North America.

This raises questions about the future role of the state-run CIB, which has been criticised for automatically renewing contracts without a careful review of evolving market opportunities. The role of the CIB is likely to be increasingly contested as the JCFA seeks to expand the volume of cocoa it markets to maximise short-term returns and promote greater local value-added processing.

However the CIB currently remains the major actor in the cocoa sector. Through the EU's Agro-processing Eco-tourism and Entrepreneurship Project (RECREATE), it is spending €350,000 from October 2011 to February 2013 to improve cocoa nursery infrastructure. Production should reach 1,200 tonnes in 2 years (in the mid 1990s, it averaged 3,500 tonnes).The USAID has also contributed US$15 million to rehabilitate another 1,000 acres of cocoa land in Jamaica.

The current production difficulties faced in Ecuador – which supplies about half of the world's fine cocoa beans favoured for high quality chocolate in Belgium, Switzerland, Italy and France – could present new market opportunities for fine cocoa producers across the ACP.

Pacific cocoa sector developments in 2011/12

Asia and Oceania account for 18% of the world's cocoa production, with Papua New Guinea (PNG) (48,000 tonnes), Solomon Islands (4,000 tonnes) and Vanuatu (1,200 tonnes) being the most significant suppliers. Single-origin, ethically traded, dark chocolate, certified cocoa, heath benefit niche markets and origin branding are sub-segments of a growing premium market that Pacific island growers are targeting, with an expected price premium of 10–20%. In addition these premium-priced markets are seen as being more resilient to economic downturns.

"Pacific island growers are targeting growing premium cocoa markets, which are seen as more resilient to economic downturns"

Smallholder production has increased in PNG by about 5% a year over the last 10 years. A major programme for replanting high-yield and more disease-resistant hybrids with a capacity to yield up to 2 t/ha is under way on cocoa estates. In May 2011, the commodity board responsible for dealing with cocoa called for far greater investment in combating Cocoa Pod Borer if production of high quality fine cocoa was to be maintained. A number of quality control and enhancement initiatives are underway, variously aimed at:

- enhancing fermentation and drier inspection;
- ensuring follow-up with non-compliant enterprises;
- strengthening licensing and registration procedures;
- promoting improvement of drier facility;
- launching a mini-project to improve cocoa quality;
- establishing a fermentation and production database;
- initiatives 'minimising the risk of smoke contamination and poly-aromatic hydrocarbon'.

The Adelbert Conservation Cooperative Society, a large coalition of farmers established in 2008 with the help of the NGO Nature Conservancy, has started producing fair-trade certified cocoa in New Guinea's Madang Province. In November 2011, Monpi, a local cocoa exporter, obtained its Fairtrade Chain-of-Custody Certification.

In Vanuatu, a programme was launched with donor assistance in 2011 to improve plant husbandry by removing diseased pods, increasing pruning, improving management and rat control. The French organic chocolate manufacturer Kaoka is looking to develop single origin cocoa products based on Vanuatu's organic cocoa production. To date, cocoa from Vanuatu is used in a blended 70% cocoa chocolate bar, which combines cocoa from Vanuatu, São Tome and Príncipe and Ecuador. In Solomon Islands, under the Cocoa Livelihoods Improvement Programme (CLIP), improved integrated pest and disease management are expected to contribute to the production of 6,000 tonnes of cocoa in 2011, while in Fiji, agricultural ministry officials favour an expansion of cocoa production over alternative crops such as coffee, since cocoa is seen as likely to enjoy stronger demand growth.

3. Implications for the ACP

Strengthening the functioning of supply chains to reduce the impact of price volatility

Different options are open to different ACP governments to strengthen the way that supply chains operate. In large, cocoa-producing countries such as Côte d'Ivoire and Ghana, state intervention through fixed farm-gate prices and forward selling on world markets appears to be the favoured option while, in Ghana, the focus is also on maintaining quality to ensure premium prices. In smaller ACP producing countries, which focus on fine/flavoured cocoa, the private sector will need to play a greater role, since continuous feedback from end-users is required to meet quality requirements of premium chocolate manufacturers. This is likely to require a redefinition of the role of CIBs where they still exist.

Capitalising on growing Asian demand for cocoa-based products

Growing Asian markets offer opportunities for the establishment of joint ventures that enable ACP cocoa producers to move up the value chain. In the longer term, however, this may require ACP producer bodies to become more involved in downstream businesses. By taking a financial stake in major multinationals involved in chocolate and sweets production, farmers' associations could help secure a greater share of the value added in meeting expanding Asian demand. This can be seen as the next stage, building on recent investments in value-added processing of cocoa in West Africa.

Coordinating policy in Côte d'Ivoire and Ghana

Competition between producing countries is getting tougher and no common policies have yet been worked on between Côte d'Ivoire and Ghana. However, stronger collaboration would give more transparency to the sector and ease smuggling. In this context 'aid for trade' support in establishing a common grading system for cocoa and harmonisation of pricing policy could help bring greater stability of producer incomes in West Africa, and strengthen local supply chains.

EU 'aid for trade' support could also usefully be deployed in developing particular quality-differentiated origin labelling schemes, given the EU's extensive policy experience in this area.

Getting to grips with eliminating child labour

Linking market access to the elimination of child labour does little to tackle the underlying causes of the problem, which lie in poverty levels in West Africa. Many cocoa farmers are seeing their profit margins squeezed and are barely keeping their heads above the poverty line. As Members of the European Parliament have pointed out, there is a need for Western companies which produce cocoa-based value-added products to look again at the way their cocoa supply chains operate, to ensure farmers 'a decent, predictable income for their cocoa', as an integral part of efforts to stamp out child labour. However, given the way the forward auction system operates, this could be difficult to implement in practice.

Scope for pan-ACP cooperation on fine/flavoured cocoa

From Jamaica to PNG to Cameroon, efforts are under way to enhance the quality and consistency of fine cocoa production, with a view to improving commercial returns to producers. There would appear to be potential for pan-ACP cooperation in drawing out best practices and lessons in defining marketing arrangements. This could build on such initiatives as in the September 2010, CTA/National Coffee and Cocoa Board of Cameroon (NCCB) consultation on the potentialities of geographical indications for the coffee and cocoa sectors of Cameroon, which allowed for exchanging experiences on the commercial possibilities of quality-based product differentiation.

Experience of strengthening farmers' organisations and improved linking producers to end-users could also usefully be shared. This is particularly the case given the volatility in cocoa prices and the need to ensure that producers fully benefit from the price premiums payable on quality-differentiated flavoured cocoa.

Possible effects of the EPA process on the cocoa sector

The EC proposal to modify Market Access Regulation 1528/2007 could possibly affect exports of value-added cocoa products from Cameroon, Ghana and Côte d'Ivoire, since higher tariffs are charged on value-added cocoa products under the alternative GSP scheme. Furthermore, uncertainty over future access of value-added cocoa products to the EU market could hamper efforts to attract investment in moving up the cocoa value chain. However, it could also provide a stimulus for developing strategies to trade value-added cocoa products directly into emerging Asian markets with rapidly growing demand for cocoa-based products.

Clear strategies for dealing with the consequences of delays in completing regional EPA negotiations will need to be developed if the adverse effects of uncertainty are to be avoided.

In addition, the implementation of EPA commitments may carry some limited negative implications in the cocoa sector by enhancing the price competitiveness of chocolate exports from the EU on national and regional markets that are being targeted by local chocolate manufacturers. Moreover, since EPAs have the objective of liberalising not only trade but also investments, local entrepreneurs in cocoa-producing ACP countries could be confronted with increased competition from both well-established and newly emerging chocolate-producing multinationals that are more technologically advanced and have greater marketing and promotion capacities.

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About this update

This brief was updated in October 2012 to reflect developments since July 2011.
The original executive brief was published in May 2008 and is available on request from agritrade-mail@cta.int
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