FMF-19
Brazil: The Importance of Coffee

Rio de Janeiro
26 October 1968

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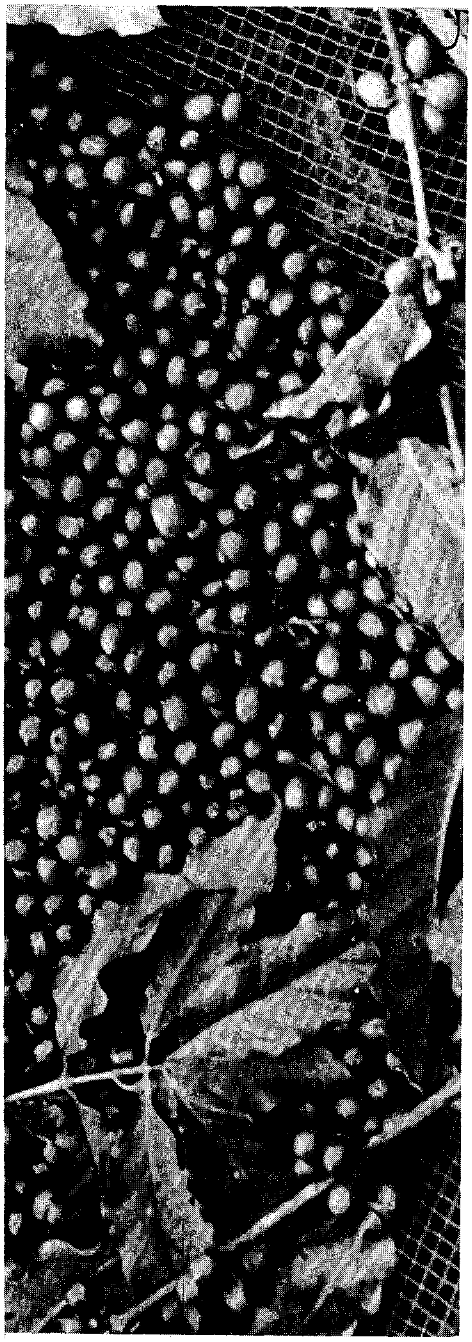


Dear Mr. Nolte:

I chose the wrong topic for this or any FMF newsletter. Coffee for breakfast starts the day right, but once I am started I am no longer interested in drinking the acrid black liquid. To gather the information for this report, I spent about six weeks in and around São Paulo and Rio, visiting such institutions as the Brazilian Institute of Coffee, the Agronomic Institute in Campinas, the Industrial Company of Soluble Coffee, etc. Never have I drunk so much coffee!

In smaller establishments it is the secretary---in larger it is a man, often in white jacket, whose sole function is to dispense and endless succession of little cups of coffee. He appears on an average of every quarter of an hour, his tin tray primed with a clutch of demitasses brim full of a thick brew already overly sweetened with sugar. One of my sessions at the Coffee Institute lasted three and a half hours. That's an awful lot of coffee.

It is an insult not to accept a cafezinho, but some means of self-protection must be adopted. Therefore, I came to risk being discourteous by refusing the cup proffered as I stood in line to get onto the elevator or as I sat in the waiting room. Once inside the innersanctum of an executive's office and in his view, such an act would be traitorous.

No matter how modest the office, clinic, store or factory, the cafezinho is ritual, a sacred institution of the Brazilian society. One day a ferocious lion escaped from the circus and hid in the offices of a large firm. Being hungry, he ate the typist the first day. On the second, the switchboard operator. On the third, the assistant manager. On the fourth, the company president. And so it went for 47 days until he committed a serious error: he ate the man who served the cafezinhos. Only then was his presence discovered.

Besides being an escape from ennui, a mid-morning fortifier, a dietary supplement, a social nicety, an excuse for a cigarette---the cafezinho is a mainstay of the national economy. The percapita consumption of coffee averages 13 lbs. per year, the Carioca chauvinistically downing over 22 lbs. transformed into the bitter Rio coffees disparaged by the Paulista who consumes some 18 lbs. of his milder São Paulo coffees per year. But the cafezinho's contribution to the national cause goes considerably beyond its support of the sacrosanct coffee crop; it likewise contributes significantly to the sugar industry. Subsidized by the Brazilian government, a cafezinho costs but a few cents---in addition, the sugar bowl is at hand on the counter, its contents available to all in whatever quantity for free. I have given many ragged cruzeiro notes to emaciated little boys who dash off to fool their stomachs with a hot cafezinho chock full of sugar.

A German watching a Brazilian fill his cup over halfway with sugar, asked him jokingly:

"Why don't you just fill it right up to the top once and for all?"

Seriously, the Brazilian replied:

"It's because, in fact, I like my coffee a little bitter."

So it is that a population of about 80 million people consumes some three million metric tons of sugar, about 80 lbs. per person annually.

Drinking a cafezinho is, therefore, one of the most patriotic acts a Brazilian can perform. Refusal suggests at least a hint of treason. But this internal market does not bring the all-important dollars into the national coffers. Over 50% of Brazil's export earnings come from coffee sales; without this income of hard currency the country would be primitive or bankrupt.

Brazil is the world's largest supplier, 38% of the market, and the United States the world's largest consumer, over 50% at a rate of 441 million cups per day. Therein lies a stormy love affair.

For a century coffee has been the green gold which has modified Brazil's landscape, politics, economic development, international relations, way of life. Throughout its history the country has been plagued by a one-product psychosis. First it was sugar in the Northeast which made Salvador a beautiful tropical capital filled with gold-laden churches and radiant mulattas. The caravels sailed into the large and protected Bay of All Saints bearing a cargo of enslaved Africans and returned to Europe with holds full of sugar. But in the 18th century the Dutch in the Caribbean broke the Brazilian monopoly of the market, and gold was discovered in the State of Minas Gerais. All attention turned to the new-found wealth, and Salvador was divested of the national government in favor of another port with a large bay, Rio de Janeiro, a focal point for transfer of the ore from New to Old World.

In the same century the coffee plant began its journey toward the red soils of São Paulo and Paraná, via the Caribbean, Surinam and Belém. From 1830 on it became Brazil's principal commercial crop. With edaphic and climatic conditions well-suited to the remunerative plant, the south of the country accumulated the wealth and power which until this day gives that region political and economic dominance. Though never crowned with the national capital, São Paulo became a potent rival of Rio in this century and now surpasses the latter on almost all significant counts. For several decades until the Revolution of 1930 two states controlled the nation's executive branch in what was called café com leite politics (coffee with milk): São Paulo was symbolized by café, Minas Gerais by leite, and they passed the presidency back and forth between them in a sort of gentleman's agreement between two tycoons.

With plenty of virgin land and labor, the fazendeiros covered the rolling terrain of São Paulo, Minas Gerais, Rio de Janeiro and Espíritu Santo with coffee trees; with sufficient control of the government, they created an artificial mechanism to assure a market when overproduction caught up with them at the turn of the century. By the Convention of Taubaté in 1906 the national government initiated a system of quotas by which it would buy and store any excess production so as to limit exports to the world demand and thus support the market price. The Brazilian Institute of Coffee (IBC) was created to execute this policy, Assured of a buyer and a favorable price, the growers had a heyday as annual production and governmental stockpiles soared.

In the words of the magazine Brazilian Business, "The cost to the government to buy and store all this coffee was astronomical. Warehouses had to be rented all along the coffee producing areas, jute sacking had to be purchased, new railway lines, highways and even airstrips had to be constructed in order to get the coffee out of the fields and into the warehouses. A complex monster of bureaucracy and graft built itself up over the years and each Brazilian president either made good use of its choice jobs for political friends or else ignored it completely. It became a 'sacred cow' so filled with so many 'untouchable' positions and operations that no one was willing to attempt reforms."

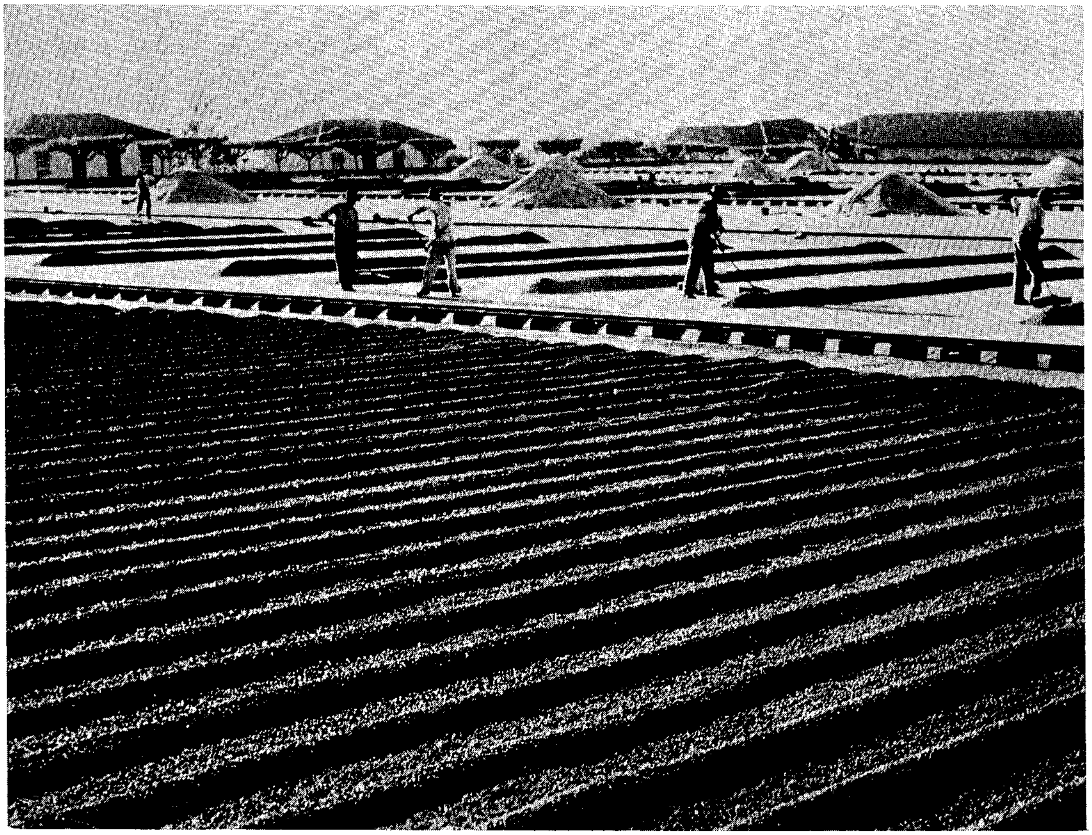
The value system of the society was predicated on land. To become a large coffee plantation owner was the ultimate achievement, and "high society" was a homogeneous agglomeration of fazendeiros. Children were sent to Europe for education. No Brazilian product was deigned worthy, and homes were extravagant museums of china, silver, crystal, silks and veneers from the Continent. Coffee exports made possible these luxury expenditures---in 1924, for instance, the crop earned 75.8% of Brazil's international receipts.

To this day, São Paulo families considered grã-fina (literally, the grand fine) have been or continue to be large landowners. One typical family of this clique, whom I know, continue to live in the large home, now almost consumed by the commercial center of the city; once seignorial the house is now musty, dark and malfunctioning. Its interior recalls the past with its marred Carrara floors, its uncomfortable rococo furniture, its threadbare Arraiolos carpets. The parents speak Portuguese, French and English fluently; she is related to Washington Luis, the last of the cafe com leite presidents and, therefore, lived in England as a child while her father was counsellor. The husband is a manqué attorney and dillettante poet; her hobby is binding in leather the books of Victor Hugo, Beaudelaire and Verlaine. Both are very conservative in their political views, refusing even to voice the names of certain liberals whom they consider Communists, participating actively in the planning of the 1964 "Revolution", and championing the cause of such U.S. politicians as Barry Goldwater.

Angling for an invitation to the fazenda, I learned that the manorhouse was so run down that it was no longer fit for guests; furthermore, the coffee crop was meager. Instead, I surmised, the profits have been siphoned from the country and put into São Paulo real estate. But there is no longer an income allowing new luxuries. The children go to the University of São Paulo, their cultural orientation toward the United States rather than England and France. Weekend outings are no longer to the fazenda, but as guests at a modern glass-walled, swimming-pooled country home of a banker-industrialist.

The first rude blow to the traditional coffee culture came with the depression. By 1929 Brazil's productive capacity was nearly double the amount being exported. With the crash, coffee consumption plunged, the price fell to eight cents a pound, the monocultural economy of Brazil was bankrupt, and a strongman from the State of Rio Grande do Sul brought an end to the Brazilian republic of café com leite politics. In the next 15 years bonfires consumed some 80 million sacks of coffee beans, but the policy of government support continues until this day and with it the constant dread of overproduction.

Talking with officials in the government's Coffee Institute (IBC), I found them lamenting that this year had not brought severe frosts to cut down the crop. Having visited the Agronomic Institute in Campinas and knowing of its good reputation, I asked about the applicability of its research on coffee cultivation. I learned that the findings of the Institute could greatly increase yields and modernize



ABOVE. Coffee drying in the sun. Beans are spread on concrete platforms, called terreiros, and are turned regularly to guarantee uniformity.

the coffee-growing industry. Thousands of hectares could be freed from what is now a low-yield extensive crop, and greater production could be realized by an intensive approach to the cultivation. But greater yields and production is just what the government does not want.

Today Brazil has almost 70 million bags stockpiled around the country, enough to meet the entire world demand for well over a year. In addition to the original cost of the coffee, paid to the producer, there are transport, warehouse and sacking costs (Coffee beans absorb moisture and swell up, making it necessary to enlarge the sacking in three different stages).

Brazil's biggest production area is no longer the red soil of São Paulo, so much a part of the coffee history of the country. The crop is a vagabond; over the century it has moved southwestward, now staking its claim in the northern and western parts of the State of Paraná.

Leading to the present-day location in Paraná is the wide swath of the coffee trail cutting across southern Brazil. Lands cultivated only for a few decades have been abandoned as the coffee planters moved on to find new and better soils for their crop. Once flourishing towns fell into decay, population and commerce surging on to the new frontier where life was a swirl of fast money, big losses, lawlessness and rootlessness; soils and men were abused and exploited in the race for the quick profit. Behind lay a land in devastation---the natural forest destroyed to make way for the coffee trees, planted on the slopes of the crystalline plateau now exposed to heavy erosion.

The first time I traveled through an area of the old coffee trail I was not aware of the crop's past and was misinformed by my Brazilian host as to the cause of the poverty-stricken area I was seeing. Leaving São Paulo, we headed northward on the Via Presidente Dutra, the four-lane highway to Rio de Janeiro. It follows the Valley of the Paraíba do Sul River between two massifs, the Serra do Mar to the southeast and Serra da Mantiqueira to the northwest. This riverine axis is now important for its chain of industries but a century ago was a belt of coffee; Volta Redonda, pride of Brazil for its steel mill, was erected as a new town upon the land of a decadent coffee farm. Closer in to São Paulo, the Japanese have put the floodplain to use for rice cultivation and truck farms.

Leaving the Paraíba basin near São José dos Campos, we followed a narrow road which twists along the cut of the tributary Paraibuna River where hillocks rise abruptly on each side of the stream. Galleries of eucalyptus follow the water course but, beyond, only occasional clumps of the tropical forest or secondary growth remain. The terrain rolls on and on, a savanna of coarse, inferior grass. Milk cans sit in front yards, and in the fields herds of criollo cattle are interspersed with better-quality Holsteins and Zebu.

Most impressive on the landscape are the termite anthills, ugly red pox sometimes the height of a man, erupting across the fields at intervals of 50 to 100 feet. The first explanation I was given for this campo sujo destitution was that the ants had staged a blitzkrieg, invading and devouring the vegetation. To wipe them out would be practically impossible, walking from one to the other of the thousands of anthills to drown them with a powerful insecticide.

I later learned that the ants were relative latecomers. Man had first stripped the land for its wood, the trees then finished off to make room for coffee. With its exodus the surface next suffered an overburden of cattle-raising. What I first interpreted as cattle paths around the hillsides I later found were the vestiges of the coffee era, regular alignments of depressions where the trees once stood. The conjuncture of blights attacking the area could only suggest to me that nature's next recourse would be desert.

Thus a coffee region grows old. In contrast, Paraná is now in full bloom, the coffee groves stretching as a sea to the horizon. Because of economic factors, the cultivation has even exceeded its natural boundaries in that state, pushing into soils and climates which often prejudice the crops.

Coffea arabica's native habitat is Ethiopia, and it flourishes in humid tropical climates ameliorated by altitude so that the average temperature fluctuates within the 60's. It is almost strictly confined within the Tropics of Cancer and Capricorn, and these boundaries are exceeded precariously only in the island of Taiwan, southern Mozambique and parts of Brazil's Paraná.

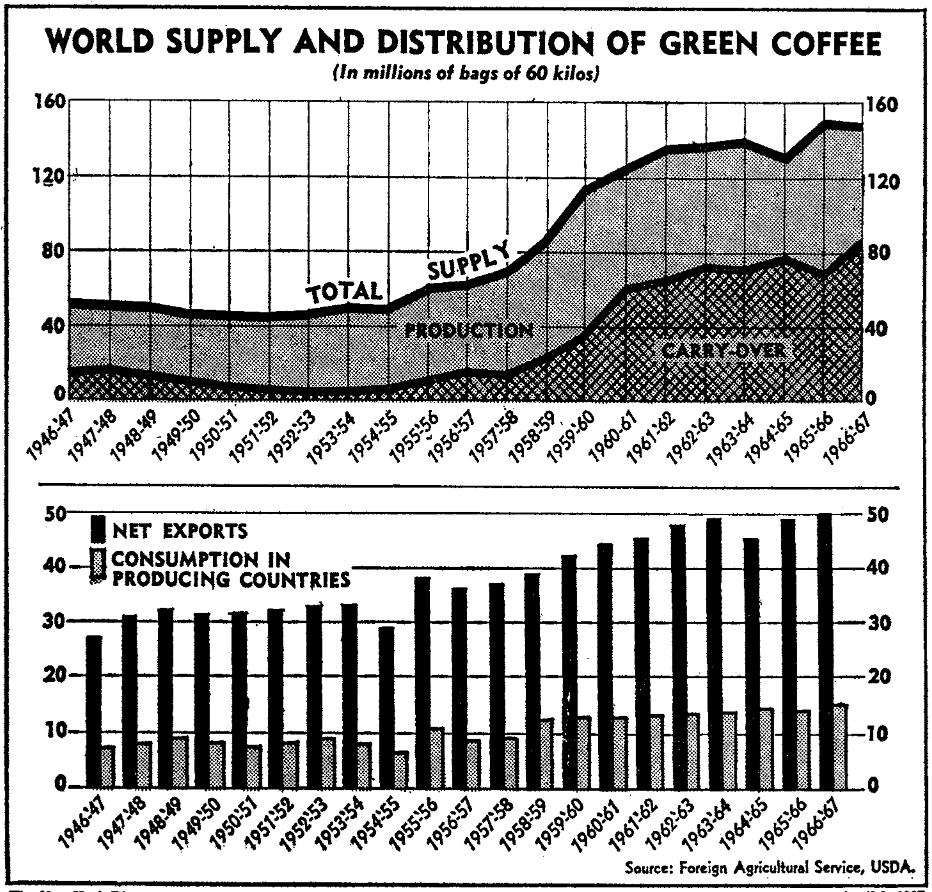
This southern state had long toyed with coffee cultivation but plunged into it only in the 1950's. In 1945-46 the state produced 674,000 bags (132 lbs. per bag); the crop 20 years later topped 21 million bags. This proliferation is the main cause of Brazil's current warehouse burden and of the peculiar market situation of the popular bean. The reason for the glut in production can be traced largely to world market prices in two years: 1950 and 1954.

When World War II practically shut off the international coffee market, the United States set export quotas to try to stabilize the situation and save certain coffee-producing countries from economic chaos. But both price and market were severely limited by wartime exigencies, and growers turned to other crops.

The renewed demand after 1945 was met by annual production supplemented by stocks on hand. Suddenly in 1949 these were not sufficient and, for the first time in a quarter of a century, there was a coffee shortage. The price jumped and held at about 54 cents for three years. The favorable quotation prompted a scurry of plantings, especially in the pioneer areas of Paraná. But since it is three to four years before a tree produces, the market did not immediately react to a new supply but, instead, in 1953 to rumors of serious frost damage to Brazil's crop. Another flurry and the price soared to $1.00, then settled at 78.7 cents for the year and 57 cents for the next two. The coffee fever spread across Paraná, even to sandy soils and the western decline of the plateau exposed to sporadic invasions of Antartic cold air masses which sweep across the pampa and up the Paraná basin. Response to the high prices likewise came in Africa which until the 50's posed no threat to Brazilian coffee.

The year of the high coffee price plus three more for tree maturation brought the predictable surplus: in 1957 Brazil stockpiled once more, and the market obeyed the dictates of supply and demand. In 1959-60 Brazil's crop topped 43 million sacks, exceeding the total world consumption. The commercial crop par excellence again suffered the vagaries of an inelastic demand and a highly elastic production.

The crisis affecting Brazil's major foreign currency earner came just at the time that President Juselino Kubitschek had geared the



The New York Times April 9, 1967

country into an ambitious development plan of infrastructure and industrialization. Hard cash for import of capital goods was critical. Unilaterally Brazil decided to restrain severely her coffee sales in order to maintain high prices. She also began to push for an international accord. No other country experienced the comparable excess in capacity; therefore, Brazil's role as residual supplier gave her a monopoly control of the market. One of the ironies of her policy, described as "opening and holding the umbrella", of withholding to assure a high price was that other countries, particularly African, chose to join the money-makers, planting vast areas and, as of the 50's, stealing parts of Brazil's market in Europe and the United States. At the time of World War I Africa produced 1.3% of the world's coffee crop; in 1964-65, 32.4% coming from 30 nations. In contrast, Brazil's share of the market has diminished from 80% at the beginning of the century, to 56% in the 1930's, to the current 38%.

One of the main causes for the soaring African sales was the soluble coffee industry which came into being after the war. Compared to Brazil's type of coffee, "unwashed arabic", the African "robust" type is hard, inferior but also cheaper. It serves well in blends, for instance with the Colombian "milds", and is, therefore, the principal coffee used in the U.S. instant coffee industry. From U.S. imports of 72,000 tons in 1952, African robust reached 280,000 tons in 1961, largely to the detriment of Brazilian coffee sales.

Brazil's dilemma was described in June 1958 by <u>The New York Times</u>:

"Since last July 1 (1957) Brazil has followed a strict 'coffee defense' policy under which the Government brought coffee from exporters and producers whenever prices on the New York Coffee and Sugar Exchange fell below the established minimum price. Because United States buyers could get cheaper African coffees, little Brazilian coffee was sold. The results were twofold. The country found itself with a highly unfavorable international balance of payments as the government deficit skyrocketed and the Government contributed further to inflation by buying some 11,000,000 bags of coffee.

"On top of this, Brazil entered into an agreement with other Latin-American coffee producers to keep off the export market 20 per cent of her exportable production in another effort to maintain prices. Other Latin-American producing countries were keeping back 10 per cent of their exportable production.

"This pact produced limited results because the African producers were not bound by it. Now, Brazilian growers, traders and exporters are against any renewal of what they call a unilateral arrangement.

" Senhor Lopes (Brazilian Finance Minister) evidently assumes that ...talks by the Coffee Study Group in Washington, in which the United States, all Latin-American and most African producers are participating, will produce a price guarantee or import quota formula that will stimulate exports and the nation's dollar income and at the same time cut down on the volume of unsold coffee the Government is committed to buy."

The tug of war to arrive at the 1st International Coffee Agreement in 1962 was prolonged. The United States, as major consumer, was not eager to enter into an agreement which committed it to support prices above their equilibrium levels. There exists a formidable array of arguments against commodity agreements in general: that they tend to maintain artificially high prices leading to overproduction, that the quota system built into such agreements freezes the production patterns so as to favor traditional producers and discourage enterprising producers, that the apparatus to supervise such agreements is inevitably so complex as to lead to imbalances and deviations, and that low-income consumers are forced to pay higher prices which in fact serve as subsidies advantaging rich landowners in the producing countries.

Spearheaded by the theories of Raúl Prebisch, the case presented by economists and negotiators of the lesser developed nations emphasizes the inexorable deterioration of trade terms since World War II: their primary products earning less in the international market while they must pay more for the manufactured goods they import. Causes for this weakening position of commodities are several, including overproduction, substitution by synthetic products, and protectionist policies in the developed countries. The thrust of the argument of the exporting countries is that commodity agreements contribute significantly to their economic development by assuring them a degree of stability and hard currency earnings, thus easing their dependence on foreign aid.

There is little doubt that Castro's rise to power in Cuba caused the United States to pay greater heed to the cry for a coffee agreement which would benefit not only Brazil but also Colombia, Mexico and several Central American countries. "Coffee is now politics, not economics" is a comment often heard. One English author observed, "The 1962 Agreement is admittedly a political move, and to a large extent a move in the cold war which for the Americas became so much more intensive as a result of the Cuban revolution..."

Coffee is one of the commodities most suited to control by a price-quota system. Production is widespread so that benefits accrue to a number of nations, but an excess is held in the hands of few, in this case Brazil and Colombia, so that supply control is concentrated in a manageable center. Brazil also offers two other qualities of interest to such an agreement: a system of "quotas of contribution" which channels the increased earnings into economic development rather than the fazendeiro's bank account, and a program of agricultural diversification aimed at reducing the coffee crop.

Besides stabilizing its international receipts, Brazil was also surely interested in restraining the upstart African nations from a burgeoning expansion in their coffee production. But, as is natural, the favorable guaranteed price has encouraged such proliferation, and through the six years of the first agreement, many abuses took place in the form of extra-quota exports via transhipments through non-member countries.

There are those who argue that the agreement is not to Brazil's advantage. Due to her preponderant control of the world's buffer stock, this one country can in effect manipulate the international market. One proposal is that the Brazilian Government should use political courage by reducing the price paid to the producers (all coffee to be exported is purchased by the IBC) so as to force out the inefficient growers and eliminate the obsolete capacity. Thus streamlined, Brazil, already a low-cost producer, could then underprice the African nations whose cultivation is more primitive and infrastructure less developed. It is also observed that Brazil, by dumping its huge stockpile, could shatter the world coffee market and pick up all the pieces for itself.

At least two major factors, however, seem to work against such drastic measures. One is the nature of coffee cultivation, the tree being a perennial which produces for 30 to 40 years; in addition, it is common to plant other crops——corn, cotton, beans, mandioca—— between the rows. Therefore, it is relatively easy to ride out a low-price cycle if the grower exerts a little patience. A sociological variable also comes into play---i.e., the difference in standards of living between the African and Brazilian producers. The first tends to be a small subsistence farmer whose survival is not dependent upon the coffee crop and whose way of life is simple and relatively free of the need of ready cash. In Brazil a significant part of the coffee is produced on fazendas and medium-sized farms, the owner accustomed to a degree of luxury consumption, and the workers dependent on the salaries earned from the coffee cultivation. Therefore, even though Brazil had the will and the way to underprice the rest of the world, it seems unlikely that such a donnybrook would serve her long-run purposes.

The 2nd International Coffee Agreement was negotiated for 18 months and came into effect on the 1st of this month, October 1968, for five years until 30 September 1973. Sixty-seven members represent both the consumer (25) and producer (42) countries and, naturally, there was a great deal of squabbling and compromising among them. Brazil's major demands included a price structure more favorable to her "non-washed arabics", a tighter control to forestall extra-quota shipments, a program to foster diversification in all producing countries, and removal of protective tariffs prejudicing sales of Latin American coffees.

To a considerable degree she was successful in the first three of these. In the price-quota system established by the agreement, four types of coffees compose the world supply, set at 47.8 million sacks. The largest quota goes to the "non-washed arabics" giving Brazil a market share of 20.9 million sacks, down 1% from last year's quota; African robusts are the next largest group giving the African nations 23.4% of the world market; "other milds" contribute 20.9%, largely from El Salvador, Guatemala and Mexico; and Colombian "milds" were granted 15.5% of the total. Each of these four has its own world market quotation based on 37.40 cents per lb., "robusts" being the cheapest and Colombian "milds" the most expensive.

When the indicator price of any one of the four types of coffee exceeds the IAC-established quotation and maintains this level for 15 days or more, the countries supplying this coffee type are granted an increase in their quota. This system of selectivity based upon a quality/price competition brought increased quotas for both Colombian and African coffees last year, whereas Brazil won no such increase. Therefore, with the negotiations for the commercial year 1968/69 Brazil demanded that the price for "non-washed arabic" be more competitive with the other three types. The final price structure was favorable to Brazil, raising the robusts to a level nearer the arabics which, since the latter are of a higher quality give them a significant edge; likewise, the milds suffered a price hike, again giving the cheaper Brazilian beans an advantage. A new president taking charge of the IBC has launched an aggressive sales campaign, so it can be expected that Brazil may succeed in obtaining an increase in her world market quota due to revived demand.

Several steps have been taken to eliminate evasion of export quotas. Importing nations, with the United States as prime example, take precautions to ascertain the legitimacy of source of all incoming coffee. Certificates of origin and re-export are now required, and exporting members cannot ship coffee unless the export documents bear a stamp obtained from the Coffee Council, executive body of the International Coffee Agreement.

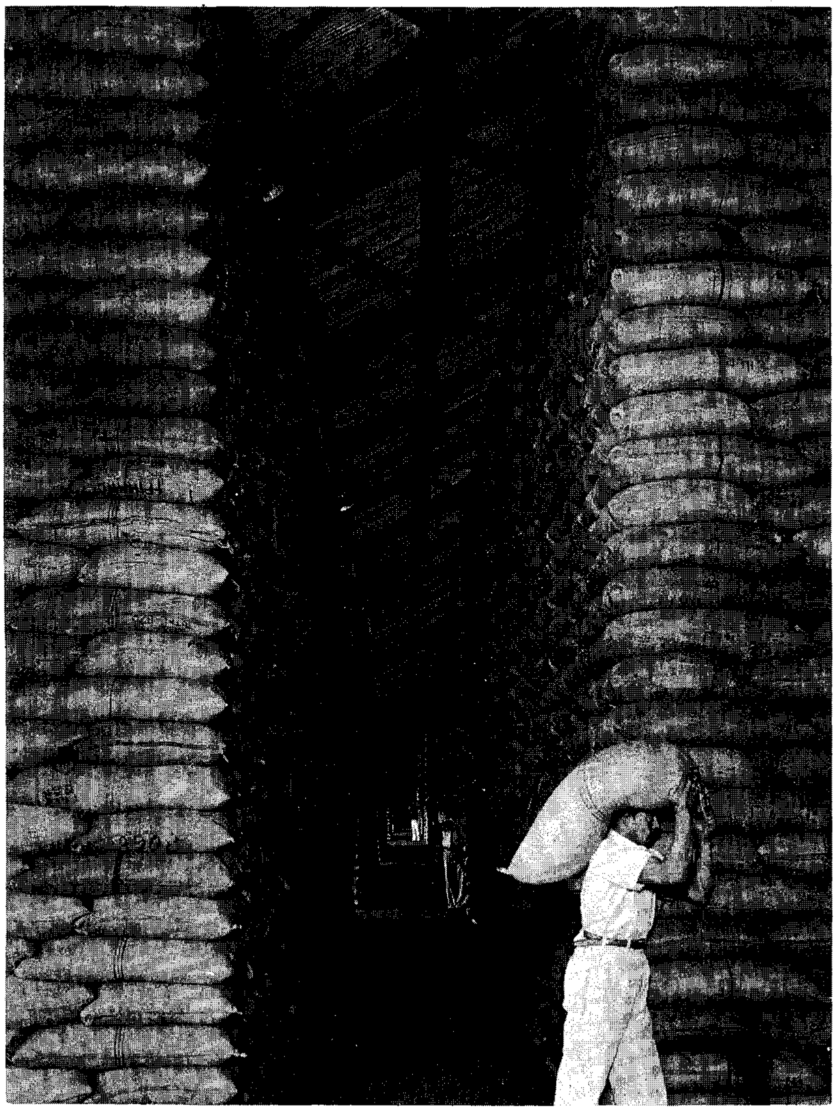
Measures have, therefore, been taken to control "touristic coffee", i.e. that going round-about in order to escape ICA surveillance. Ironically, it seems, however, that Brazil is herself now initiating so-called "special deals" which at best are on the borderline of ICA regulations. One such "operacão especial" comprised 5.4 million sacks destined for five U.S. importers at a sale price two cents under the indicator price set by the IAC controls. Another maneuver, called "paired" or "married coffee" ("café casado") involves coffee shipped abroad to IBC warehouses in such non-IAC-member countries as Yugoslavia, Lebanon and Hong Kong. This coffee is then counted as if sold to fulfill the Brazilian quota and is often used as counterpart sales at reduced prices.

Brazil in 1961 initiated and financed her own diversification program aimed at reducing coffee production. The intention was that such a lead should be followed by other nations, and with the new agreement of this month a diversification fund is established to which all producing members must contribute. This money shall go for programs or projects approved by the Fund with the "objectives of limiting the production of coffee in order to bring supply into reasonable balance with world demand."

Although Article 47 of the Agreement deals with "Removal of Obstacles to Consumption", Brazil did not succeed in eliminating the discrimination of the European Common Market against all non-African coffees. Instead the effete article recognizes "that there are presently in effect measures which may to a greater or lesser extent hinder the increase in consumption", but no meaningful measure to rectify the situation is proposed.

Hashing out an accord on the above-mentioned items was, however, but child's play in comparison with the one major battle which threatened to destroy the whole international agreement. The two titans representing the largest consumer and the largest producer drew swords on the issue of soluble coffee, and it took months of recrimination and obduracy before Brazil finally backed down before the superior force of the United States.

Brazil's sin was to have a better, cheaper instant coffee which was beating U.S. firms at their own game in their own market. The powdered brew represents 20% of the U.S. coffee consumption and, since the early 60's, had been largely supplied by such giants as General Foods, Standard Brands and Tenco (a subsidiary of Coca-Cola) from their



ABOVE. A view of a small part of Brazil's stockpile.

plants in the U.S. Africa, Mexico and Central America. The usual soluble product is composed chiefly of the cheapest African beans of scant aroma and indifferent flavor; it is bolstered by an admixture of high quality "milds". In contrast the pure Brazilian arabic bean makes a tasty coffee superior on all scores to the half-breed. Of this I am sure, having had many cafezinhos of Brazilian soluble during talks with executives in that industry.

Certain U.S. food distributors, such as Hills Bros., turned to the better product: in 1965 Brazilian solubles had 1% of the U.S. market; 3.5% in 1965; 14% in 1967; and the direction was up, up, up in 1968, although the real amount, about $35 million, was but a pittance of the total coffee market. Due to the lobbying action of the food giants, the U.S. Congress had not imposed a tariff on soluble coffee as it would hurt American firms with plants abroad. Now, some other recourse should be found to cut off the alien flow, and it was at hand with the renegotiation of the International Coffee Agreement.

Brazil's long-established policy of upholding the world price combined with her low cost production has allowed the Government to exact what is officially referred to as a "contribution quota" and unofficially as a "confiscatory exchange tax". In fact, it amounts to an export tax. Foreign currency earned by coffee sales goes to the Bank of Brazil which in turn pays the exporters and, therefore, the producers in cruzeiros at a government-decreed exchange rate, artificial and always lower than the official rate. A reasonable but not excessive profit is allowed. Inflation is thus curbed and Brazil assures that cheap coffee does not enter and upset the world market. The government's income from this maneuver benefits the coffee sector with agricultural research, sales promotion, a diversification program, administration of the Coffee Institute, etc. In addition, a significant amount is diverted to the general program of economic development.

The contribution quota is exacted only on exports of the raw product. Within the country the IBC sells at cost, even subsidizing coffee beans for regular domestic consumption. Much of the Brazilian surplus is composed of broken beans, not saleable abroad but usable for soluble coffee manufacture. Therefore, the five Brazilian instant coffee plants were able to obtain their raw product at a low cost; four of these plants were wholly-Brazilian enterprises.

The instant coffee industry here was a happy fulfillment of The Declaration of American Presidents signed by President Johnson at Punta del Este in April 1967. Among other things, it states:

"The Government of the United States intends to make efforts for the purpose of liberalizing the conditions affecting exports of basic products of special interest to Latin American nations...(and pledges itself) to provide incentives and financial resources for the industrialization of agricultural products, especially by small and medium-sized industries and by the promotion of the exportation of these industrialized agricultural products."

In the light of such official pledges the U.S. Agency for International Development channelled funds through a government development corporation for its program to aid the embryonic instant coffee industry. Acting in good faith, the agency was soon caught up in the maelstrom of conflicting interests. AID officials now deny or sidle off from their involvement in the affair.

In the chain of command Big Food in the U.S. brought pressure to bear on Congress which advised the State Department of its concern for the competition posed by the foreign upstart: the Brazilian Government must be convinced to impose a tax on the raw product used by its own industry so that the cost was comparable to that paid by U.S. firms for the Brazilian export.

The U.S. line hardened and for all Brazil's pleas to negotiate the matter bilaterally, outside of the 67-member council of the International Coffee Agreement, there was no concession. The others watched and waited through the long months of negotiation as the two giants made war. Though there are hints that other items such as U.S. foreign aid to Brazil were at stake, it seems that the cudgel wielded by the U.S. was the threat to withhold support of the International Agreement.

Brazilian newspapers through 1967 and early January 1968 editorialized "we will never give in to this high-handed blackmail.":

"This same (President) Johnson who attacks us with his 'frontmen' of the State Department is called upon to honor his signature solemnly inscribed upon a document which commits him to support the industrialization of agricultural production---that is, coffee---and to promote the exportation of industrialized agricultural products---that is, soluble coffee. It is from this commitment that the hero of Viet Nam intends to flee. He orders or permits (which is in fact the same thing) that his emissaries call us 'immoral' because the Brazilian soluble coffee industry would compete 'disloyally' with the U.S. industry. Where is free enterprise? Where is free competition? And 'continental solidarity'?"

Other press attacks were more vitriolic. The Brazilian people were aroused and, though the issue was settled in February, it still simmers under the surface. With no amplification needed, the two words "café solúvel" are used, just as are "República Dominicana", to synthesize cynicisms and disillusionments with U.S. foreign policy.

There were, of course, strong arguments on the U.S. side---the injustice of the artificially high price imposed upon the U.S. firms, the absence of an import tariff in the U.S., the contribution of the U.S. to the Brazilian coffee industry via the agreement, etc. But these never convinced the local populace.

Within both countries vested interests were pitted against each other. Those U.S. coffee distributors relying upon and profiting from the Brazilian product were opposed to the General Foods bloc---but the former were smaller and weaker. In Brazil the instant coffee industrialists were opposed to the green coffee exporters who feared they would lose the international agreement---but the former were smaller and weaker. In January Sr. Horacio Coimbra "resigned" as president of the Brazilian Coffee Institute. His firm, Companhia Cacique de Café Solúvel, is Brazil's largest instant coffee processor, comprising an industrial complex in Londrina, Paraná, which employs about 400 workers. Under the pressures of the green coffee producers and the U.S., the Brazilian Government no longer found Sr. Coimbra a convenient negotiating chief. A Brazilian journalist observed that his resignation indicated "the weakening of the Brazilian position in the dispute with the United States." Alluding to a facetious national saying, the article closes:

"Although with no real optimism, I am going to make a promise---to whom I don't yet know---to find out if God is really Brazilian or if he has decided to become the knight-errant of General Foods."

By late January editorials were referring to the "immeasurable risk" posed by the U.S.-Brazil impasse which threatened "the Agreement, the stability of the market, the income of the coffee-producing nations, and all the immense effort since 1957 to eliminate the dangerous fluctuations in the product's price."

The U.S. mobilized the overt support of other importing countries. Frightened by the possible consequences of the Brazilian intransigence, the producing countries began to pressure for a conciliation. A U.S. negotiator's caveat that Brazil would have to accept the U.S. terms caused a Brazilian to retort: "When are you going to send your gunboats?"

On February 19, the International Coffee Agreement was approved. Article 44 incorporated Brazil's defeat. In essence it stipulates that: 1) Brazil or any other exporting country is prohibited from selling soluble coffee under conditions more favorable than green coffee. This means that the Government will have to tax their exports of soluble coffee comparably to green coffee or eliminate the "contribution quota" on the latter; 2) The United States has the right to present a formal grievance to the Executive Director of the Coffee Council whenever it judges itself prejudiced by irregularities in the exportation of soluble coffee; 3) After 40 days, if the two litigants have not resolved the question bilaterally, the Executive-Director of the Coffee Council will create an arbitration board composed of three impartial parties; 4) If the board decides in favor of the United States, Brazil (or other violating country) will have 30 days to remedy the irregularity and, if the United States does not consider the matter corrected, it may take retaliatory action aimed specifically at the Brazilian imports.

When I asked the opinion of a high official of the Brazilian Coffee Institute regarding the soluble coffee settlement he said:

"I have two things to say---one official and one private. As an employee of the Government, I have 'no comment'. As a citizen, I think it was a crime on both the side of Brazil and the U.S. Though economically a small matter, it has done immeasurable harm to the U.S. image---it was a great victory for the Left and a major contribution to the cynicism of the average citizen regarding the sincerity of pretty phrases which the U.S. voices and supports with its signature. We know that the U.S. Government itself did not wish to force Article 44, but we see how the Government's good intentions are squelched by the economic powers within the U.S."

Article 44 has not yet made its full impact felt upon the Brazilian soluble industry. For one thing, it is aggressively hunting new markets, especially in the "non-traditional"(i.e., non-IAC member) countries of Eastern Europe and Asia. Companhia Cacique, for instance, was originally dependent on the U.S. market but now some 18 other countries take more than half of its production; Horacio Coimbra was recently in Hungary trying to expand sales.

Then, it is predicted that the Brazilian Government will exercise <u>jeito</u> to dilute and delay the application of the measure. As a first concession it has leveled a 15% tax on the export of soluble coffee, a token not likely to satisfy the U.S. firms. There may follow a series of protests met with insufficient redresses. And the Brazilian businessman is no doubt capable of various shenanigans to get around the restrictions. So, it may be that, in the long run, the damaged party will be more the U.S. image than the Brazilian soluble coffee industry.

Sincerely yours,

Frances M. Foland

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Photos: Brazilian Business

Received in New York November 4, 1968.