

The International Political Economy of Coffee: From Juan Valdez to Yank's Diner. By Richard L. Lucier. New York: Praeger Publishers, 1988.

Coffee is of global importance, ranking second to petroleum in world commodity trade. Moreover, coffee is of particular importance as a major export commodity in many low-income countries in Latin America, Africa, and Asia. The primary purpose of *The International Political Economy of Coffee* is to integrate political science and economics in analyzing the five-fold increase in world coffee prices over an 18-month period in the mid-1970s. The effects of this price increase, resulting from a frost in Brazil in 1975, are traced from Yank's Diner in Scranton, Pennsylvania through the world coffee market (and the international coffee agreements) to several countries in which coffee is the major export and a prime determinant of the level of economic activity.¹ The effects of higher coffee prices on individual consumers in the United States and on coffee producers in Brazil, Columbia, and the Ivory Coast are analyzed. The individual coffee producer in Columbia is personified by "Juan Valdez," the Columbian coffee industry's fictional TV advertising spokesman. A stated concern of the book is to show how Juan Valdez and Yank's Diner are mutually dependent upon each other.

The book is divided into seven chapters. Chapter 1 describes the consumer outcry against higher coffee prices in the United States following the Brazilian frost, the resulting U.S. Congressional hearings, and General Accounting Office study of the world coffee system. The impact of this economic shock in the United States coffee market is the starting point of the inquiry into economic interdependence between countries producing coffee and countries consuming coffee. Chapter 3 describes the world coffee market, emphasizing the role of Brazil as a "dominant oligopolist" in coffee production. Coffee production and trade is considered in a broader political-economic context of economic growth and development of "Third World" countries.² Chapter 4 describes the history of the international coffee agreements. The issues raised in these agreements between countries producing and consuming coffee were the subject of negotiations in the call by less-developed countries for a New International Economic

¹ The information in the book about Yank's Diner was taken from an article in the *Wall Street Journal*.

Order (NIEO) during the 1970s. Chapters 5 and 6 focus on the role of coffee in economic development in Columbia and the Ivory Coast. The political economy of coffee in the 1980s is considered in the final chapter of the book, including a brief analysis of the effects of a Brazilian drought in late 1985.

This book presents a wealth of data about the international coffee industry. Trends in production and use of coffee, supply and demand, prices, exports and imports by various countries, the growth in production and consumption of soluble relative to roast coffee, market shares of leading firms in the coffee industry, and other aspects of coffee trade are clearly described and well documented. Thus, this book is a good data source about the world coffee market. Moreover, it clearly traces through the effects of the 1975 Brazilian frost on coffee consumers and producers. So long as the book is used as a source of data about the world coffee market, there is little room for criticism.

However, the book is not merely about the coffee industry. The broader objective is to analyze the relationship between coffee production and economic development in less developed countries. In doing so, the author focuses on "the highly charged issues of dependency, national sovereignty, and the forces that shape developing countries' political economies" (p. 19).

Lucier's aim is to integrate political science and economics into a single work on economic development by focusing on power relationships. He concludes, and properly so, that it is central to political-economic analysis that both power and markets be understood. However, the author fails to properly distinguish between power and market relationships.³ Market transactions are based on consensus whereas the governmental decision-making process inevitably involves power and coercion. A finding of "market failure" based on an oligopolistic view of coffee production leads the author to favor cartelistic solutions enacted and enforced through international agreements in regulating the production and consumption of coffee throughout the world.

²The Third World concept was forged after World War II, largely under United Nations auspices. The unifying characteristic of the Third World is that its constituents receive aid from Western governments. In economic development literature, the Third World was previously known as the underdeveloped world, the less-developed world, and now is often referred to as the South. See Peter T. Bauer and Basil S. Yamey, "The Third World and the West: An Economic Perspective," chap. 6 in *The Third World: Premises of U.S. Policy*, W. Scott Thompson, ed. (San Francisco: Institute for Contemporary Studies, 1978), pp. 118-20.

³Murray N. Rothbard, *Man, Economy, and State* (Los Angeles: Nash Publishing, 1970).

International Coffee Agreements

Coffee was one of the first commodities in which control over world trade was attempted. Brazil, producing from 75 to 90 percent of the world's coffee in the early 1900s, led Columbia and other Latin American countries to a series of producer-country agreements to control exports and raise world prices from 1902 until the first International Coffee Agreement was signed in 1962. This agreement represented a major change in the world coffee market since major coffee importing countries (including the United States) also became signatories. The 1962 Agreement, ending in 1968, was followed by similar international coffee agreements in 1968, 1976, and 1983. The agreements, based on a system of country-by-country export quotas, restrict marketing and raise coffee prices.⁴ As one might expect, however, the effectiveness of the cartels was eroded by competition as exporters shipped through third countries to cheat on the agreement.

Lucier is a firm proponent of international coffee agreements contending that free trade is a myth and that the real choice is between commodity agreements (including consumers as well as producers) and oligopolistic arrangements between producers only (pp. 163-65). Thus, the agreements, in his view, merely reflect the reality that governments are heavily involved in coffee markets in producing countries and coffee trade in highly developed countries is heavily concentrated in a few transnational firms. Further, Lucier argues that the agreements have been broadly beneficial because they both slowed the shift in production from low- to high cost producers and controlled production to balance world demand and supply. Lucier concludes that even coffee consuming countries benefit from these international agreements by having more leverage in marketing decisions. However, the latter conclusion is challenged by Law who found coffee prices under the agreements during the 1963-1972 period were *higher and less stable* than they had been in the preceding 10 years.⁵

The long term effects of commodity agreements are predictable from cartel theory. The post-World War II period has seen cartel-like international agreements in a number of other products including oil, wheat, and sugar. Despite the temporary success of the Organization of Petroleum Exporting Countries (OPEC) in restricting total sales, the effectiveness of cartels in raising prices is inevitably eroded over time.⁶

⁴A new coffee agreement is scheduled to begin October 1, 1989. In early 1989, the United States, objecting to inflexible quotas and sales to nations that are not members of the pact and at lower prices than members are required to pay, threatened not to join the agreement.

⁵Alton D. Law, *International Commodity Agreements* (Lexington, Mass.: D. C. Heath, 1975), p. 84.

⁶Peter H. Lindert, *International Economics*, 8th ed. (Homewood, Ill.: Irwin, 1986), p. 207.

There were some special factors contributing to OPEC's success in raising prices for a decade or so, but time has largely dissipated its power too. Thus, the typical results to be expected from restrictions on competition and higher prices arising from commodity agreements are: consumer resentment, a faster search for substitutes, cheating among signatories, an expansion of output outside the agreement, a constant struggle to keep total output or trade down and individual nations' shares up, and retardation of needed resource and production adjustments.⁷ The economic arguments against the various international coffee agreements and other commodity agreements are similar to those of other government cartels. Commodity agreements are more likely to inhibit productive resource allocation since quotas and prices are determined by political influence and past production and trading patterns rather than comparative advantage and market forces.⁸ Similarly, Bauer finds that commodity agreements tend to freeze the pattern of production, protect high-cost producers and restrict the growth of lower-cost supplies.⁹

Cartel theory suggests that arbitrarily raising product price will spur the development of substitutes. Thus, it is not surprising that Brazilian and Columbian coffee has faced increased competition as more and more countries began to produce and export coffee. Whereas only 14 percent of the world's coffee was grown outside of Central and South America in the late 1940s, non-American, chiefly African, coffee production has increased rapidly since that time and now constitutes about one-third of total world exports.¹⁰ There is little doubt, given the huge number of countries exporting coffee, that coffee consumers would be protected better by the market process than by world-wide cartel arrangements agreed upon by producing and consuming countries.¹¹

Economic Development and the New International Economic Order

The United Nations Conference on Trade and Development (UNCTAD) was convened in Geneva in 1964. The "Third World" countries

⁷Alton D. Law, *International Commodity Agreements*, pp. 77-78.

⁸*Ibid.*, p. 111.

⁹Peter T. Bauer, *Dissent on Development*, rev. ed. (Cambridge, Mass.: Harvard University Press, 1976), p. 263.

¹⁰U.S. Department of Agriculture, *Agricultural Statistics 1987* (Washington, D.C.: U.S. Department of Agriculture Printing Office, 1988), p. 238.

¹¹Nappi finds that past coffee agreements have defended a price floor above the long-term market price, frozen the industry structure through the allotment of export quotas, and not provided a mechanism to encourage reduction of high cost production capacity. See Carmine Nappi, *Commodity Market Controls* (Lexington, Mass.: D. C. Heath, 1979), p. 76.

succeeded in drawing attention to their view that the system of international trade and investments was established by the industrial high-income North at the expense of the low income South.¹² The oil shock of the mid-1970s galvanized the UNCTAD movement into a demand for a "New International Economic Order."¹³ This NIEO was to apply the OPEC cartelization approach to coffee and other primary products. One of the planks in the NIEO platform was to manipulate markets of primary products—as in international commodity agreements—so as to stabilize and raise commodity prices.¹⁴

Lucier appears sympathetic to the NIEO view that the system of international trade and finance benefits richer countries at less-developed countries expense. Two components of the NIEO were (1) stable and higher product prices, and (2) increased access for "developing country" exports to "developed"-country markets (p. 103). Thus, the international coffee agreements foreshadowed the active stance exemplified in the NIEO and coincides with the first component of the NIEO agenda.

The above discussion suggests that the economic results of cartelization of coffee markets are similar to those for other commodities. International commodity agreements are generally sold as measures to stabilize markets. However, stabilization schemes for cocoa, coffee, tin, and other products face the formidable incentive and information problems of correctly guessing what the long-run price trend will be, mustering sufficient resources to keep the price near that trend, and following through with the appropriate actions. After reviewing the experience with such schemes, Lindert concludes that price stabilization is "plausible in principle but unworkable in practice."¹⁵

Market stabilization schemes are interesting intellectual exercises but of little practical significance. Even if government officials could obtain the information necessary to increase price stability, the incentives of the political process are such that they are unlikely to do so. In this respect, international commodity agreements are similar to domestic government programs to stabilize markets. Neither theory nor historical experience provide reason to think that the political process will succeed in stabilizing markets where private action fails

¹²Bauer points out that the term Third World reflects a condescending attitude because we normally do not talk about the First or Second World. It is countries in Asia, Africa and Latin America that are lumped together by this term—as if they "were all much of a muchness." There is a great deal of ambiguity in distinctions made between developed and less developed countries but the term less developed is much less misleading than underdeveloped, developing, or Third World used as an adjective (Peter T. Bauer, *Dissent on Development*, p. 25).

¹³Peter H. Lindert, *International Economics*, p. 275.

¹⁴*Ibid.*, p. 276.

¹⁵*Ibid.*, p. 281.

to do so.¹⁶ For example, the International Coffee Agreement of 1976, advertised as a stabilization device, failed to prevent two years of high prices following the Brazilian frost in 1975.¹⁷ And, aside from the stabilization aspects of commodity agreements, there is no more justification for artificially raising prices through production and marketing controls (to assist producers) than there is for any other government redistribution program.¹⁸

The second component of the NIEO agenda, increased access (by more highly developed countries) for exports from less developed countries, warrants emphasis and support. The effort by Brazil in the late 1960s and mid-1970s to increase exports of soluble coffee to the United States, for example, was opposed by the National Coffee Association (the trade association representing United States coffee processors) and ultimately by the U.S. Congress (p. 142). This action is symptomatic of the schizophrenic nature of governmental policies in the United States and other economically advanced countries toward low income countries. On the one hand, various governmental economic development initiatives are launched at taxpayer expense to assist less developed countries, such as the Alliance for Progress and the Caribbean Initiative by the United States. At the same time, however, economic development is impeded by restricting imports of sugar, coffee, and so on, from these countries. The most effective way rich countries can help poor countries is to reduce trade barriers against their exports.¹⁹

¹⁶After more than 400 pages of formal analysis investigating the conditions under which government stabilization policies might be effective, Newbery and Stiglitz conclude: "In short ... we believe that the gains to be had from a commodity price stabilization programme are likely to be small, and that most of the benefits in risk reduction may be had by improving the workings of the market, for example, by making futures markets more readily accessible (directly or indirectly) to small producers," (David M. G. Newbery and Joseph E. Stiglitz, *The Theory of Commodity Price Stabilization: A Study in the Economics of Risk* [New York: Oxford University Press, 1981], p. 445). The authors acknowledge that their formal analysis is oversimplified by assuming away the formidable "empirical" problems in obtaining the information required to design and implement a price stabilization program to cope with "market failure" that arises due to the lack of perfect information and appropriate insurance markets to deal with risk. However, they completely ignore the incentive problems that predictably result in "government failure" as well as the policy implications of that failure. *Ibid.*, pp. 442-44.

¹⁷Bruce L. Gardner, *The Governing of Agriculture* (Lawrence, Kans.: The Regents Press of Kansas, 1981), p. 104.

¹⁸It is suggested by some people that the United States (and other industrial countries) should participate in international commodity agreements as a form of economic assistance to developing countries. However, no system of transferring income from the United States consumers of coffee and other products to foreign producers can be justified as increasing social utility. See David Osterfeld, "Social Utility and Government Transfers of Wealth: An Austrian Perspective," *The Review of Austrian Economics* 2 (1987): 79-99.

¹⁹Peter T. Bauer and Basil S. Yamey, "The Third World and the West," p. 115.

A thesis of Lucier's book is that "trade, focused on exports, is an undependable engine of growth and development" (p. 104). In this so-called classic dependence scenario, less developed countries are alleged to be dependent upon technically advanced countries as customers for their exports and as sources of the imports needed for economic growth and development. Furthermore, the development and wealth in the advanced countries and the lack of development and poverty in the poor countries are held to be a function of one another.²⁰ However, this dependency view has little relevance. When trade occurs, there is mutual dependence—interdependence—and all parties benefit from it. The fact that many less developed countries mainly export primary commodities in exchange for imports of manufacturing capital goods does not mean that such trade is harmful.

Development economists frequently assume that government planning is a central factor in economic development. In this view, there must be a "development policy" or "development strategy" with government activity regulating investment expenditure, imports and exports, and terms of trade. Lucier favors government planning in "developing countries" to direct investment and production and to protect "infant industries" from foreign competition as ways to promote economic and political development (pp. 97-98). However, there is a great deal of evidence that centralization and increased governmental power is "much more likely to obstruct economic progress than to advance it."²¹

Lucier draws a sharp distinction between economic growth and economic development. Economic growth is identified with increases in output and income while,

economic development is a process of change: in the composition of output, in production processes, in the distribution of income, in the production and diffusion of knowledge, and in the sophistication and modernization of the entire social system and its institutions [p. 93].

In this view, economic growth occurs without economic development when the outcome is not consistent with the "development goals." In the Ivory Coast following independence in 1960, for example, a high rate of economic growth was achieved with the assistance of foreign investment from France and other developed countries—but (according to Lucier) little economic development. The major beneficiaries of the economic growth were foreign-owned firms, and the Ivorian population did not receive "its share of economic benefits" (p. 303).

The "terms-of-trade" are held to be of critical importance if "exports are concentrated on a few primary commodities" (p. 95). Bauer

²⁰Anthony S. Smith, "The Case of Dependency Theory," chap. 11 in *The Third World: Premises of U. S. Policy*, p. 211.

²¹Bauer and Yamey, "The Third World and the West," p. 84.

in sharp contrast, finds that the discussion about terms of trade of less developed countries is misleading or incorrect and that "terms of trade are, in fact, unrelated to the prime causes of poverty in the underdeveloped world."²²

Much of the analysis in economic development involves a "nirvana approach"—comparing the present situation with an unattainable outcome.²³ In assessing the effects of trade, investment, and other factors contributing to the development of economic activity in any country, the relevant comparison is between the present situation and the condition that would exist in the absence of the factor(s) responsible for the change in economic conditions. For example, the fact that incomes in a poor country would be higher if a smaller proportion of the rewards were going to "foreign factors of production" (p. 303) or if terms of trade were more favorable are not relevant in assessing the effects of foreign investment, international trade, and so on.

In brief, Lucier's book is much more informative about the operation of the international coffee market than it is as a policy guide for ways to promote economic development in less developed countries. The objective of public policy should be to develop an institutional framework that provides maximum scope for individual choice. Only in this way can resources be used most effectively throughout the world and the interests of producers and consumers best be served. The recommended cartelization of the world coffee market in the form of international coffee agreements is not consistent with this objective.

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²²Ibid., p. 258.

²³Harold Demsetz, "Information and Efficiency: Another Viewpoint," *Journal of Law and Economics* 12 (1969): 1-22.