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Chain governance, sector policies and economic sustainability in cocoa

A comparative analysis of Ghana, Côte d'Ivoire, and Ecuador

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Chain governance, sector policies and economic sustainability in cocoa: a comparative analysis of Ghana, Côte d'Ivoire, and Ecuador

Giel Ton, Geoffrey Hagelaar, Anna Laven, and Sietze Vellema

1. Introduction*

Sustainability in cocoa has received a lot of attention in the recent years. Various media, advocacy groups and alternative trade organizations address the social aspects of workers and producers in the cocoa sector. Certification organizations are in the process of developing and implementing codes of practice with the purpose to define and audit sustainability performance. Several processing and food manufacturing companies are involved in reviewing their sourcing strategies and they make efforts to include sustainability criteria an element of trading. Public and private partners meet at round tables or international conferences to exchange views on how to achieve sustainability in the cocoa sector. Enhancing sustainability performance is subject of discussion within the intergovernmental International Cocoa Organisation (ICCO), where producing and consuming countries meet to identify policies beneficial to the sector and to the numerous smallholder producers in particular. Projects financed by the intergovernmental Common Fund for Commodities (CFC) increasingly try to combine market-led development and poverty alleviation in commodity dependent countries. The Commodity Action Plan of the European Commission specifically addresses the poverty problems in commodity dependent countries. Even within the World Trade Organisation, governments are discussing the particular problematic situation of commodity dependent countries. These public and private endeavours set the context for working towards enhanced sustainability performance in cocoa. They are, however, confronted with volatile and whimsical economic realities in the international commodity markets as well as with, by times, uneven distribution of margins throughout the cocoa chain, which may slow or even hinder investments in and progress towards sustainability. An important question therefore is what kind of policy or strategy is able to shape the right economic conditions for sustainable development in the cocoa sector.

The task of the paper is to examine modes of economic governance and policy measures that may alter the economic playing field for sustainability and social equality in the cocoa sector. The paper will not define or measure sustainability in cocoa. It has a strong focus on the economic dimensions of the desired transition process towards sustainability, and, in the context of cocoa, emphasises the relevance of predictability and stability in the market for poor cocoa producers. The paper adopts a comparative framework to describe the evolution of public-private interaction in economic governance in the cocoa sector development. The case studies examine the involvement of national governments with managing and governing the economic realities in cocoa in two major West-African

* In 2005, the intergovernmental International Cocoa Organization (ICCO) designated a Consultative Board to work on the World Cocoa Economy, and to foster sustainability of the sector considering the three pillars of sustainability: economic, environmental and social sustainability. In 2008, this became formalized in a public-private partnership (PPP), named the Working Group on Round Table for Sustainable Cocoa (RTSC). The Working Group will consist of governments of producing and consuming countries, the European Commission, selected NGOs and trade and industry associations, the ICCO Spokespersons for Producers and Consumers and the Chairman of the ICCO Consultative Board on the World Cocoa Economy. The present report is geared to the policy advisors involved in these discussions, and wants to highlight some dynamic and historic elements related with the governance of the cocoa value chain.

producing countries, Ghana and Côte d'Ivoire, and one Latin American country producing a specific quality cocoa, Ecuador. The paper further focuses on the policy instruments used to in the governance system in these countries that are related with the economic sustainability of the sector. First, the paper introduces the issue of public-private interaction in the field of economic governance.

2. Public and private interaction in cocoa

In the past three decades, the role of public interventions in the economic realm has been modified and scrutinised. Formerly, intergovernmental commodity agreements, such as the International Cocoa Agreement, contributed to a certain level of stabilization and rule setting in commodity markets and thereby to a more robust business climate for producers, traders, and processors. Currently, the scope of the commodity agreements moved away from direct interventions in the markets to finding other measures. Direct government involvement in supply management and price stabilization has decreased, partly due to the choices fundamental to, for example, the structural adjustments policies of the World Bank, the lending policies of the International Monetary Fund, and the trade policies negotiated in the World Trade Organisation.

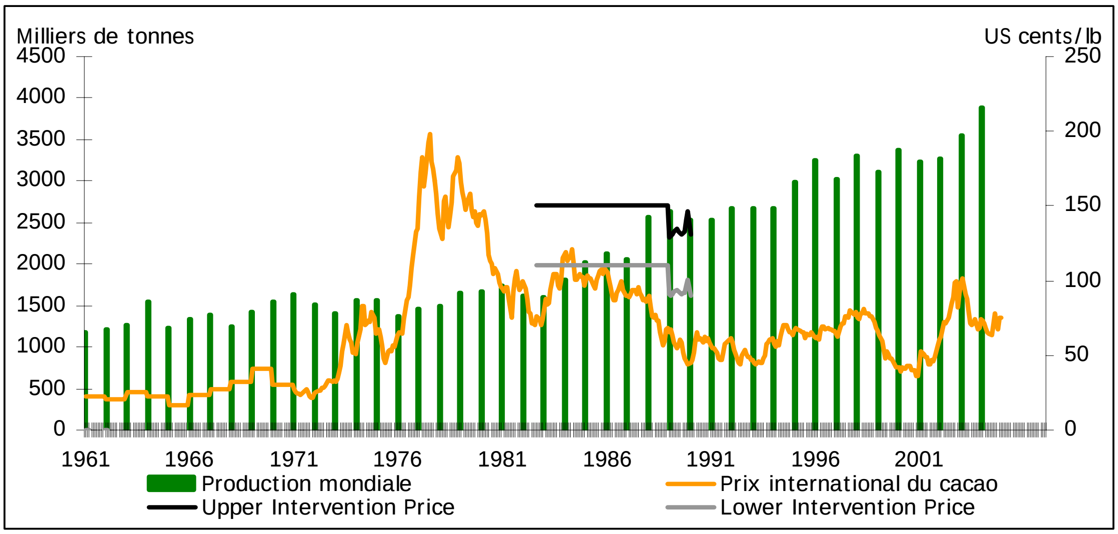
More recently, however, the general interest in sustainable development evoked a discussion on economic governance for ensuring public goals, such as sustainable development or poverty alleviation. Therefore, it seems worthwhile to investigate how existing policy frameworks contribute to equity and economic sustainability in cross-border and complex commodity chains. In the case of the cocoa commodity chain, the intergovernmental commodity agreement exists and specifically addresses sustainability. Likewise, in producing countries, national policies and public organisations, such as marketing boards, still strongly shape the dynamics in the cocoa chains, and, consequently, the conditions for enhancing sustainability. Although this public interference with market realities may be more limited in scope than in the 1970s and 1980s, it still seems important to discover how these institutions and agreements relate to on-going market-led initiatives and how they set conditions for the improvement process towards sustainability in cocoa.

In the case of commodity chains, the public sector has a role to play in creating the right economic conditions for the desired improvement process due to the involvement of large numbers of poor and relatively unorganised smallholder producers. This may be beyond the capacity of individual market-led initiatives that works towards sustainability in the cocoa sector. In a discussion on sustainability, the International Cocoa Organisation proposes "…that the economic pillar takes priority and precedence over the other two pillars. The main reason for that is that for the smallholder cocoa farmers, economic considerations override both environmental and social concerns. (..) In other words, the first priority in activities towards a sustainable world cocoa economy is to improve the revenues and incomes of the cocoa farmers" (ICCO, 2007). Hence, it seems likely that the growing interest in sustainability has to address the issue of how public policies and regulations affect both the economic playing field and the nature of commercial transactions in such a way that it sets the conditions for sustainability (Vellema et at, 2007).

The issue of creating the right conditions for sustainable development in cocoa is becoming even more complicated because developments of the global value chain of cocoa tend towards concentration of production in a small number of countries and a process of vertical integration of upstream activities by a handful of international cocoa processing firms (Daviron and Gibbon, 2002; Losch, 2002; Abbot, Wilcox and Muir 2005). This two-fold process of economic concentration affects bargaining power and price setting between the different chain actors. These concentration processes also determine, together with the taxes and levies applied on various transactions within the chain, the farm-gate price and thus the economic perspectives for the producers. Therefore, it is important to look into the attributes of a chain configuration that are most intimately related with the 'economic sustainability' of the sector: the stability of internal price levels and the share of the producer price relative as a percentage of the export price.

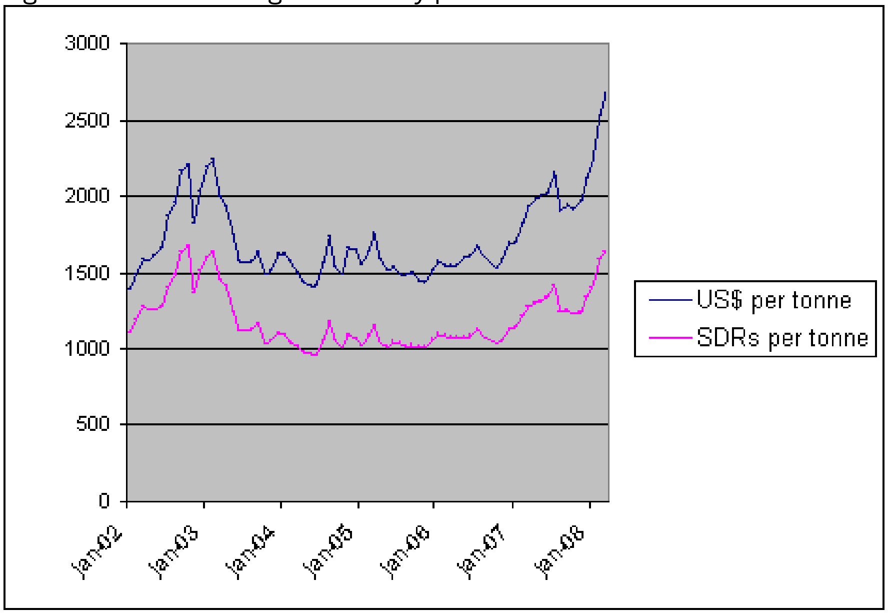
Price levels in international commodity trade are generally independent of the volume increases in production of individual countries, but respond to global stock levels. There is a wide fluctuation of prices between years. Figure 1 gives an impression of the steady increase in cocoa production and the irregular pattern of world cocoa prices.

Figure 1: World cocoa production and cocoa world prices (1961-2006)



Source: (Gouin 2007)

Figure 2: ICCO - Averages of weekly prices 2002-2008



Source: ICCO, http://www.fao.org/es/esc/prices

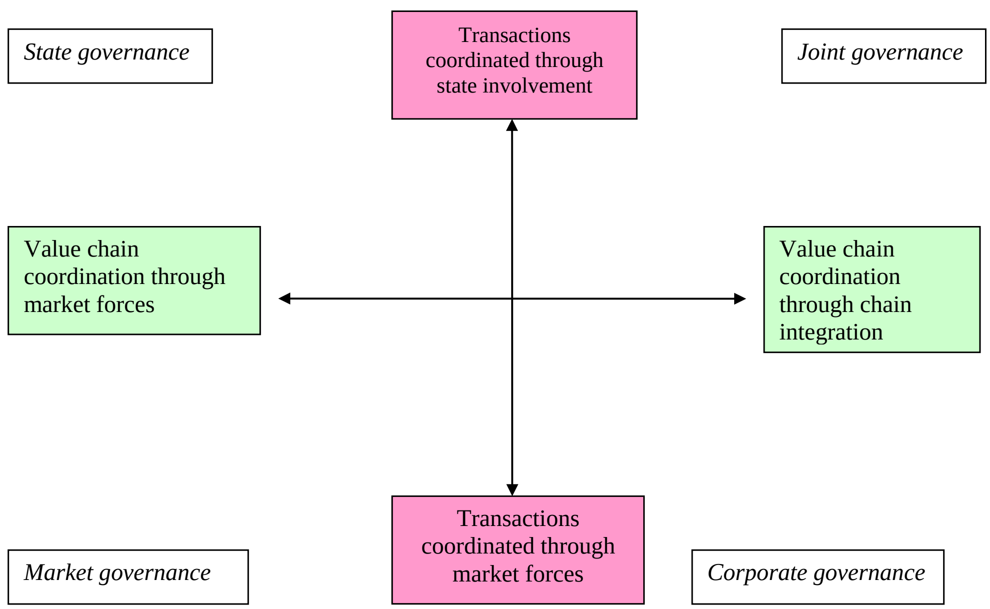
For chain actors price levels are a very important incentive to produce, but also the predictability of the price during the year is an important issue that influences entrepreneurial decision making, by farmers, traders, exporters, and even for government financial policy. Cocoa is characterized by a very instable world market price during the year, varying between weeks and months without any seasonality. Figure 2 indicates this fluctuation of the cocoa price in the (depreciating) US$ and in terms of a (stable) virtual international currency, using the IMF Standard Drawings Right (SDR). This price volatility increases risks and transaction costs for all chain players. To lower these transaction costs for themselves, private business (including smallholder farmers) tries to find ways to reduce them. This can be done collectively through chain coordination, but also by using the government to define 'rules of the game' that lead to more transparent and stable domestic prices.

Most cocoa producing countries have developed institutional arrangements to translate the international cocoa prices to (indicative) domestic prices for cocoa beans in the place of processing or place of shipment to international markets. Some countries have mechanisms to fix and stabilize these prices during specific periods, and some countries have developed institutional arrangements in the value chain to target specific qualities with higher than average prices on the world market. The following case studies illustrate the historical process that has lead to country-specific institutional arrangements that are key in economic governance of the domestic cocoa sector, and that are the result of the economic interests of and power relations between producers, domestic intermediary traders, governments and international processing companies

The case studies examine how the interactions between governments, intermediary organisations, international authorities and firms shape economic governance in the cocoa sector and define margins and price setting in transactions. These case studies label several periods in each country's cocoa sector history according to the dominant 'mode of governance' during that period and have an interest in the specific socio-political factors that influence the functioning and possible transition of modes of governance. To describe this economic governance system, the paper uses a conceptual framework in the description of the cocoa case-studies developed by Griffiths and Zammuto (2005). The framework directs our attention to the steering of a commodity sector through the interaction between public and private actors to coordinate economic activity and decision making.

The comparative framework (Figure 3) includes two fairly independent dimensions that influence economic governance and decision making defining the conditions within economic transactions within a sector: (1) the fragmentation or integration of the value chain (McGahan and Porter, 1997).; and (2) the level of state involvement versus coordination through market mechanisms (North, 1981; Hall and Soskice, 2001). Countries and socially embedded commodity chains are inherently complex and not comparatively measurable on a scale: therefore not the absolute position in each country-specific graph of the institutional governance system, but the direction of change in time of this system is important.

Figure 3: Comparative framework for labelling public-private interaction in a commodity chain



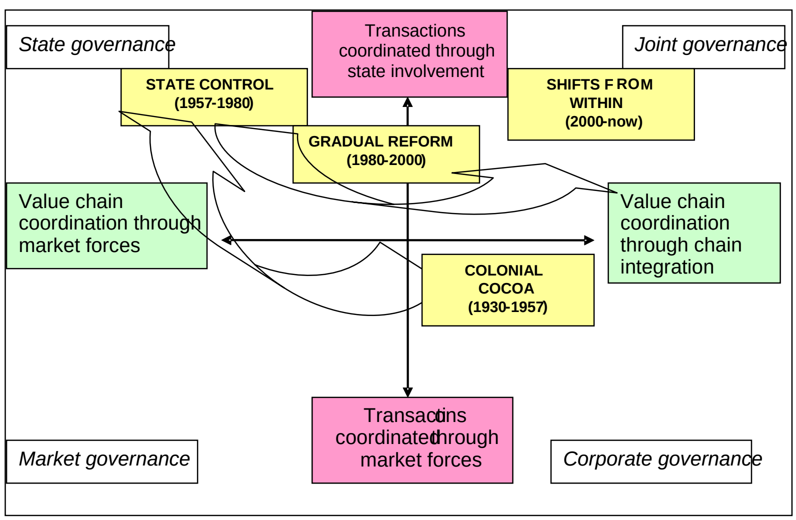
Source: Authors, based on (Griffiths and Zammuto 2005)

3. Ghana*

In Sum

Ghana started already before World War II with coordinated action to stabilize prices. This was done in direct negotiation between import companies (buyers), exporters and organized producers. This resulted in corporate governance systems to govern transaction in the cocoa sector (the 'cocoa buying agreement'), but after the war transactions and price setting was increasingly regulated by the state with a decreasing chain integration. The recent periods of gradual reform during the 1990s and the current re-affirmation of the state control in the cocoa chain, make that Ghana is stays in the upper level of the graph (high influence of the state in governing transactions) and gradually moving tot the right, influenced by the growing chain integration within the transnational cocoa processing industries and/or certification schemes (fair trade, organic, etc.). In Ghana there is an alliance between international buyers and the government, sharing an interest in maintaining the current system, as it guarantees a consistent supply of premium quality beans (Fold, 2001); a kind of joint governance system with an active role of the state and a passive role of global buyers.

Changing Institutional Governance Systems in Ghanaian Cocoa



Introduction

Ghana is the world's second largest producer of cocoa, responsible for producing around 20 per cent of the world's cocoa in 2005-06 (ICCO, 2006). Cocoa is a very important source of income and foreign exchange earnings for Ghana. Around 6.3 million Ghanaians depend on cocoa for their living, representing around 30 per cent of the total population. Cocoa is Ghana's dominant cash crop and single most important export product. In 2006, exports of cocoa butter, powder, beans, paste, and waste totalled US$1,241 million, equivalent to more than 33% of Ghana's merchandise exports. The contribution of cocoa

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production and marketing to GDP was 8.5% in 2006, up from 4.9% in 1998. The EC is the main export destination for cocoa produced in Ghana (IMF 2007).

Cocoa is cultivated on some 1.6 million hectares in Southern and Central Ghana. About three quarters of output is produced by some 700,000 small-scale farms. The product life-cycle of cocoa (increasing and later decreasing cocoa yield after establishing a plantation) and more intensified methods of cocoa cultivation, stimulated by the government and private extension providers, have been key factors in boosting cocoa production, leading to record outputs in 2003/04 and 2005/06 (Ruf, 2007). Smuggling from Côte d'Ivoire (and the end of smuggling from Ghana to neighbouring countries) also contributed to the increase in volume of cocoa beans exported.

The Ghanaian government has always been actively involved with the development of the cocoa sector. During colonial times, public involvement was initially combined with private efforts to stimulate cocoa production and to improve its quality. From the late 1940s onward, a system of state governance was put in place, which was consolidated during the early years of independence.

With the introduction of structural adjustment programs (SAPs) in the late 1980s, governance processes in other cocoa-producing countries shifted from state to forms of corporate and joint governance. In Ghana, however, state governance remained the dominant system. The introduction of gradual reforms nevertheless led to other actors entering the sector and taking over some of the previous state responsibilities.

A distinction can be made between three time periods. The first period (1920-1980) deals with the shifts from a fairly corporate governance system around Worlds War II, as part of the colonial economy, to a state-controlled economy after Independence in 1957. The second period (1980-2000) describes the gradual introduction of reforms and the consolidation of the strong position of the state, domestically as well as internationally. The third period (2000-present) discusses the responses of other actors to the system of state governance, and its current dynamics.

Ghanaian cocoa sector policies in motion

Period 1 1920-1957 Colonial governance

As a result of the colonization process, cocoa was introduced to Africa in the late nineteenth century. Once established in Ghana, cocoa production expanded rapidly and Africa became the main producer by the mid-1920s. Cocoa has dominated the political economy of Ghana (formerly Gold Coast) since 1920. Between 1923 and 1932, cocoa accounted for an average of around 77 per cent of Ghana's total exports (Department of Cooperatives, 1990, 11). In the cocoa season 1920-21, Ghana became the world's largest producer, reaching its peak with a total production of around 560,000 tons, and it kept this leading position for more than 55 years, until in 1977-78 Côte d'Ivoire took over this position. In the early years, cocoa production was concentrated in the Eastern region (Ministry of Finance, 1999, 6). In the mid 1940s the centre of production shifted to the Ashanti and Brong Ahafo regions, where cocoa was produced on virgin forest land. This is partly attributed to the outbreak of Cocoa Swollen Shoot Virus disease (CSSVD), which had to be 'cured' by cutting down the trees. However, the willingness of many small farmers to migrate to new cocoa production regions was a *sine qua non* for the expansion of the cocoa sector (COCOBOD, 2000; Hill, 1963).

During the colonial period, the cocoa sector initially operated under a free market system. European companies controlled both local buying and exporting, with Cadbury as the leading British cocoa manufacturer. Public interventions took place through the involvement of the (colonial) Department of Agriculture, which encouraged the establishment of cooperative enterprise in Ghana's cocoa industry. Organizing farmers into cooperatives was seen as a way to ensure the production of good quality cocoa for export. Moreover, by means of combined sales, cooperative members could demand higher prices. Around the same time, cocoa societies became involved in the provision of credit, farmer inputs (e.g. chemicals) and consumer goods. Many European traders were hostile to the promotion of cooperatives with government backing, because they worried that this would eventually eliminate them from the cocoa trade (Department of Cooperatives, 1990, 9-16).

The strength of the cooperative movement became clear at the time of the first cocoa hold-up in 1930-31. The action achieved its goal: both the supply and the price steadily increased (Milborn, 1970, 59). In 1937 a second cocoa hold-up was organized in response to a fall in the world price of cocoa and the concomitant introduction of the 'cocoa buying agreement', which introduced the idea of paying a uniform price to all farmers. Farmers and brokers, who had not been consulted by the foreign buyers, initially rejected this agreement. Both internal and external marketing of cocoa stagnated, until in March 1938 a 'truce' was signed between the two parties and sales restarted, though in a context of 20 per cent declined world market prices (Milborn, 1970).

In response to the hold-up, a royal assignment called for a 'commission' to report on the conditions of the cocoa economy in West Africa. The commission's recommendation was: public support for cocoa marketing operations (Graue, 1950, 259). Consequently, the West African Cocoa Control Board was established in 1940, and replaced in 1942 by the wider West African Produce Control Board (WAPCB). In 1947, the Cocoa Marketing Board (COCOBOD) was installed and it was decided that the British Ministry of Food was to be the only seller of the Ghanaian cocoa, using the COCOBOD channel. The existing (mainly expatriate) cocoa buying companies were appointed agents of the WAPCB and they continued to have responsibility for buying (Anin, 2003, 15).

Cadbury's position was in its support for the argument that West African cocoa economies should be rehabilitated and in its 'general acceptance of the marketing boards' a reality in the Colonial cocoa commodity chain (Beckman 1976, 43).

Period 2 1957-1980 State-controlled cocoa economy

In 1953, the United Ghana Farmers Cooperative Council was founded as 'a general farmers' organization with political objectives'. It became the so-called farmers' wing of the Convention People's Party (CPP) led by President Nkrumah (Beckman, 1976, 11). The Farmers' Council was given sole responsibility for cooperative development and it became the head of the cooperative movement, which in itself became an economic and political force to reckon with. In 1961, four years after the country's independence, the Farmers' Council capitalized on the Colonial heritage of the cocoa marketing boards and took over the cocoa trade and became the monopoly buyer of Ghana's cocoa. Doing so, it put an end to the direct involvement of foreign buyers in cocoa marketing. In the same year, the Cocoa Marketing Company (CMC) Ghana was set up as a commission agent of COCOBOD. CMC Ghana became responsible for registering buyers, appointing local (Ghanaian) buying agents to facilitate foreign buyers' operations in Accra, marketing of cocoa, recording of cocoa sales and shipping of cocoa, including involved payments (Amoah, 1998: 78-104). From being governed by fairly liberal economic policies, the cocoa sector was transformed into a predominantly state-controlled system, which moreover was now independent from colonial ties.

The state also invested in processing capacity, furthering state-led chain integration. In 1963, two cocoa processing factories were built, both owned by COCOBOD, and falling under the mandate of the Ministry of Finance. They were operated by one of COCOBOD's subsidiaries, the Cocoa Processing Company limited (CPC) (Ministry of Finance, 1999, 71-2). In 1982, COCOBOD took over a third factory, the formerly British processing company West African Mills (WAM) at Takoradi.

The state governance continued after a short disruption between 1966 and 1977. When in 1966 the Nkrumah Government was overthrown by a military coup, the Farmers' Council was dissolved and banned (Beckman, 1976, 11-7). During the following decade, characterized by political instability and mismanagement, cocoa prices fell and cocoa production was halved. Competition among local buyers was re-introduced, but this did not last long due to problems with delayed payments. A single buying system was reintroduced and from 1977 onward, the Produce Buying Company (PBC), a subsidiary of COCOBOD, was in control of internal marketing. In this period, different subsidiaries of COCOBOD provided support and services to the farmers. The Cocoa Services Division (CSD) had the monopoly on the procurement and distribution of inputs. In addition to its role as input provider, the CSD used to be responsible for cocoa extension services, which consisted of advising farmers in cocoa and coffee production, the production and distribution of planting materials and the control of pests and diseases (Amezah, 2003, 1). The Quality Control Division (QCD) was responsible for a strict control on the quality of cocoa. The Cocoa Research Institute Ghana (CRIG) was the national centre of excellence for the study and cultivation of cocoa.

By the early 1980s, Ghana's economy and political system was in an advanced state of collapse. In 1981, Lieutenant Rawlings came to power and he had to face the complexity of the economic crisis. When a severe drought in 1983 worsened the situation, his government accepted the intervention of international donor organizations. The Economic Recovery Program (ERP) was set up, resulting in the introduction of reforms in the cocoa sector through its Cocoa Rehabilitation Project (CRP) and the Agricultural Sector Adjustment Programme (ASAP) (Ministry of Finance, 1999; Fold, 2002).

Period 3 1980-2000 Gradual reform

The reforms were meant to have the effect of increasing producer prices by reducing the costs of inefficient marketing and pricing systems as well as by improving efficiency of related cocoa activities (Akiyama, 2001). All major West African cocoa-producing countries introduced at least some reforms since the late 1980s. While Cameroon and Nigeria initiated drastic reforms, Côte d'Ivoire and Ghana chose a more gradual approach to liberalization, thus resisting some of the pressures of international donor organizations.

Wanting to avoid the generally negative experiences of cocoa producing countries that liberalized over-night, such as Nigeria, the Ghanaian government opted for a gradual introduction of reforms. These have so far included the liberalization of internal marketing, privatization of input distribution, reform of extension services, reorganization of processing activities and a drastic reduction in COCOBOD's staff-level. In the early 1980s there were approximately 120,000 people employed by COCOBOD while in 2006 this number was only 5,500 (IMF 2007) Many former employers of COCOBOD are still involved in the cocoa sector, as private consultants, providers of extension services and/or as buyers of cocoa..

COCOBOD continued to control external marketing. The QCD remained responsible for the final quality checks of cocoa beans and Ghana continued to deliver consistent supplies of relatively good quality cocoa, for which it received a premium on the world market. Through a system of forward sales, COCOBOD managed to pre-finance the cocoa while price stabilization has remained intact (Ministry of Finance, 1999; Laven, 2007a).

The liberalization of internal marketing started in 1992 with the introduction of private Licensed Buying Companies (LBCs) as competitors to the state-owned monopoly in buying cocoa from farmers. During 1996-97, sixteen LBCs obtained the permission to buy cocoa alongside the PBC, and four received provisional licenses (Ministry of Finance, 1999, 45). The number of buyers fluctuated, as did their active involvement in buying cocoa. The majority of LBCs were Ghanaian, only two were foreign-owned (Olam and Armajaro). One LBC was farmer-owned (Kuapa Kokoo Union) and was set up with the support of international NGOs. PBC remained the largest buyer by far.

Not only marketing reforms took place in this period, which was also characterized by institutional reforms. COCOBOD reformed the organization of its processing activities, as a way of expanding its low processing base. In 1993, this resulted in a joint venture with a German processor. COCOBOD moreover merged the extension component of its services division with that of the Ministry of Food and Agriculture (MoFA), providing unified extension services. The division's non-extension functions were organized on the basis of project and private sector participation (Ministry of Finance, 1999, 23-4). With these changes, CSD's monopoly on the procurement and distribution of inputs ended. In 1995, the Ghana Cocoa, Coffee and Sheanut Farmers Association (GCCSFA) took over this responsibility. The objective of this privatization of input supply was to increase competition, which would – so it was hoped - lead to the availability of the right quantity of inputs at the right time, and moreover effect a reduction in the price paid for the inputs.

Period 4 2000-present Shifts from within

In response to the reforms and the reduced role of COCOBOD and its subsidiaries, other actors and partnerships entered the cocoa sector, ready to fill the vacuum left by the (partly) retreating public sector. PBC is still the major buying company (buying almost 33 per cent of the cocoa in 2005-06), although its buyers' share is declining. Recently PBC itself was partly privatized and its shares are traded on the stock market, with COCOBOD being the company's major shareholder. In this period, no new foreign buyers have entered the stage. One new (still small) farmer-owned LBC, Ghana Sompa Kokoo, was recently set up by the Kuapa Kokoo Union.

The introduction of competition in internal marketing did not result in price-differentiation. In the absence of competition through prices, LBCs generally found (other) ways to ensure that farmers sell (only) to them. They invest in building trust as well as in building social capital.

LBCs receive a yearly fixed 'buyers-margin' set by the government. In 2002-03 this margin was set at 9 per cent of the FoB price; in 2004-05 it got somewhat reduced. From this margin LBCs pay their Purchasing Clerks (PCs) on commission basis, thus encouraging them to buy as much cocoa as possible from the farmers in their communities. As a result of the gradual pace of the reforms LBCs are locked into a system with few incentives for high performance, and little financial scope for establishing strong relations with farmers.

Following liberalization of internal marketing of cocoa, the government decided to allow qualified LBCs to export part of their cocoa purchases, with effect from October 2000. Officially LBCs were allowed to export 30 per cent of their domestic purchases, as long as they meet the conditions set by the Ghanaian Ministry of Finance. The idea behind the gradual pace of the reforms was that this transition period would allow LBCs to become familiar with and acquire the necessary skills for effective external marketing (Ministry of Finance, 1999). In 2007 this partial liberalization has been discontinued (IMF 2007). Government officials argue that the current system works and that LBCs are unwilling or not yet ready to enter into direct exporting. Some of the larger LBCs contest this view, arguing that Cocobod obstructs their involvement in external marketing. LBCs do not openly complain about the practices of Cocobod. After all, the relationship between LBCs and COCOBOD remains a hierarchical one, as they depend on COCOBOD for their license to operate. Also, many of the LBCs, especially the smaller ones, benefit from the current system; they can take advantage of the marketing expertise and ability to borrow offshore when financing local purchases of the CMC. To global buyers of cocoa the partially liberalized system in Ghana is also beneficial. Thanks to the reliability of the marketing system, Ghana enjoys a high reputation for contract and quality fulfillment.

Currently, world's largest cocoa processing companies Cargill, ADM are in the process of outsourcing part of their processing facilities to Ghana. Barry Callebaut, world's third largest processing company, already has a processing factory running with a capacity of 75.000 tons. Although physically international traders did move 'closer' to the farmers, their grinding operations in Ghana has not resulted in direct contract relations between buyers and cocoa farmers International buyers have limited their activities in Ghana to initiating/supporting small-scale programs aiming mainly at the use of more environmentally friendly practices, addressing the problem of child labor and community development, individually or for example through involvement in public-private-civil partnerships like the Sustainable Tree Crop Program-STCP.

For the Ghanaian government and COCOBOD there are strategic reasons why the cocoa sector is not fully liberalized The Ghana Cocoa Board, COCOBOD, a semi-autonomous institution under the Ministry of Finance and Economic Planning, has still a huge staff of some 5,500 (IMF 2007). Table 1 shows the composition of the net FOB price during the 2002/2003 season. There is a significant margin between the FOB price ('free on board' price) and the CIF price of exported cocoa (placed in Europe harbor, incorporating the 'costs, insurance and freight' from West-Africa) equalling around 35 per cent in 2002/03. As export is organized by COCOBOD, there might be an significant additional flow of resources generated by their state-led export transactions.

Table 1: The composition of the Net FoB price in 2002-03

COMPONENT	MAINSTREAM COCOA USD/TONNE 1 = 8700 CEDIS	DISTRIBUTION IN % NET FOB
Producer price	976	68,11
Buyers' Margin	128	8,93
Domestic transport costs	32,2	2,26
Storage and shipping	18,4	1,27
Disinfectation costs	9,66	0,67
Crop finance costs	33,3	2,3
Government taxes and levies	236	16,44
FOB price	1433,56	99,98 %
CIF price (to Europe)	*± 2200*	

Source: COCOBOD, 2003 (white cells) and personal communication industry (dark cell), 2003.

It is clear that for the Ghanaian government, cocoa is an important source of income and foreign exchange earnings; consequently, the government has a stake in retaining control over cocoa exports. Cocoa exports are subject to taxes and repatriation of export revenue and its conversion into local currency. The tax rate on exports of cocoa beans is determined annually by the Minster of Finance and Economic Planning; for the crop year 2007/08, it is 11.1 per cent of the FOB price. The effective tax rate has varied strongly over the recent years (IMF, 2007).

The producer price is adjusted to the real price on the market through a yearly review of prices and margins. A bonus is paid for cocoa supplied by farmers through the LBCs. The producer bonus is calculated by using the policy defined percentage of the FOB price: 70% in 2007. The calculation of the bonus and the distribution of the bonus to the cocoa farmers is perhaps the most innovative institutional arrangement to influence price stability and fairness within the cocoa chain. The Ministry of Finance states that farmers are protected from price falls, and only positive adjustments in the producer price are possible.

> 'Since producer prices are announced prior to the actual purchase or export of cocoa, a situation may arise where ex-post payments could exceed 70% of FOB price. This could arise from differences between the ex-ante projected exchange rates and world market prices and the actual ones. In such a situation, the over-payment to the farmer should be borne by other stakeholders, other than the farmer. However, in a situation where exchange rate and the world market price exceed their projected values, the surplus arising there from should be shared between the government and the farmer as "bonus" or "compensation" to bring producer price to the programmed FOB percentage" (Ministry of Finance, 1999:85)

Characterizing interventions and their effects

This section describes which policy-instruments are implemented to reach sustainable agricultural development of cocoa in Ghana. For the sake of clarity, a distinction has been made between the four periods as discussed in the previous section.

The first and second period: from colonial policies to a more state-controlled economy

This period is characterized by two shifts, firstly, a gradual shift from a market type of governance to (colonial) state governance, and secondly, from colonial control to independent state governance. Especially in the years prior to independence there is a clear alliance between private and public actors. After independence foreign buyers return to their core business and operate more on the side than being active players within Ghana. Foreign buyers were interested in control of price fluctuation. In 1937 international buyers introduced a 'cocoa buying agreement', as a first attempt. Later, the Ghanaian government established the Pan-Territorial Fixed Price Policy. On the one hand, this pricing system guaranteed farmers a reliable income and assured the government in obtaining revenue from cocoa (as the price is determined before the crop is harvested) (Ministry of Finance, 1999, 82). But, on the other hand, this guaranteed price was substantial lower than the world market price. This low producer-price was the result of high taxes and marketing costs. The government compensated farmers by providing them with subsidies on inputs and services. Also the government undertook several attempts to channel rural credit to farmers.

Product-quality has always been an important attribute of Ghanaian cocoa. Initially, the organization of farmers in cooperative societies was regarded as a way to ensure good quality performance. When the cooperative movement collapsed, the Ghanaian government introduced a quality control system, ensuring the export of good quality cocoa, for which it received a premium on the world market. The strong emphasis on quality performance, both by public and private actors, has contributed to the still exceptional position of Ghana; the only cocoa beans still consistently separated by national origin for grinding purposes are those from Ghana (Gibbon and Ponte, 2005, 135-6).

Research and training have always been regarded as important ways of increasing volumes of cocoa production and dealing with pests and diseases. In the late 1970s, COCOBOD established a special division, bringing knowledge and new technologies to the farmers.

The third period: Gradual reform

Liberalization was enforced onto Ghana by international donor organizations, but Ghana managed to resist their pressure and chose for the gradual introduction of reforms. In this period Ghana's government remained the dominant coordinator of the supply chain, though reforms altered some of its functions. The objective of liberalization of internal marketing was to improve the operational and financial performance of Ghana's marketing system, in order to enable higher producer prices and stop Ghana's declining production trend (Ministry of Finance, 1999; Fold, 2002). The aim was to reduce the government tax and marketing margins on cocoa gradually. In 1998-99 the producer-price was set at 56 per cent of the net f.o.b. price ('free on board'), the margin reserved for marketing/COCOBOD operations was set at 18.2 per cent and Government tax at 25.8 per cent. Within six years the producer-price had to increase up to 70 per cent and both its operational costs and taxes had to decrease, equaling both 15 per cent of the net FoB (Ministry of Finance, 1999, 90). In this period, the system of price-stabilization continued to protect farmers from price-fluctuations in the world market. In this period also producer-bonuses were introduced.

The introduction of gradual reforms has stimulated a recovery of the sector. For Ghana as a whole it is estimated that the area harvested from season 1990-91 till 1997-98 increased with 73 per cent (from 707,000 ha to 1,220,000 ha). But production only increased with 37 per cent, indicating a reduction in productivity with 21 per cent; the increase in cocoa production was ‘almost entirely due to the traditional method of expanding output by means of additional land’ (Teal and Vigneri, 2004: 8-12). With the introduction of reforms, COCOBOD allowed the entering of local buyers of cocoa, providing them with licenses to trade cocoa domestically. COCOBOD remained control on the external marketing of cocoa. The quality control system of Ghana remained in place, contributing to the production of premium quality cocoa in Ghana.

Also the reforms contributed to a gradual increase in producer-price; however, this did not automatically resulted in an increase in remunerative farmer income, which also depends on the costs of cocoa production, productivity and on diversification of income. Prior to the reforms, inputs were generally free or heavily subsidized, but privatization of input distribution led to enormous price increases (Haque, 2004; Ministry of Finance, 1999). Haque suggests that in Ghana production costs have tripled between 1989 and 1995-1999. It is argued that the increases in production-costs have led to ‘self-exploitation’ among farmers. Farmers worked longer hours themselves, mobilized family members, and increased labour exchange groups (Blowfield, 2003). For many farmers currently, productivity is low and cocoa production is not economically sustainable (Mehra and Weise, 2007).

<u>The fourth period: Shifts from within</u>

In this recent period the dynamics of the partial liberalized system become clearer. Besides public interventions, private actors and NGOs increased their activities in Ghana, sometimes in partnership.

Still COCOBOD continues to intervene in the sector, using partly the same instruments as in the period between 1980 and the year 2000. In its interventions the state clearly prioritizes the production of good quality cocoa and high quantities of cocoa beans. LBCs are still not allowed to become involved in external marketing of cocoa. LBCs receive little incentives to invest in their network and to contribute to good quality performance. The monopoly on external marketing has also obstructed attempts of NGOs to open up alternative marketing channels (e.g. organic cocoa) next to conventional cocoa. International buyers, under pressure of media, NGOs and consumer organizations, have become involved in the development of national certification schemes, with a focus on labour practices and sustainable sourcing**.**

In terms of increasing producer-prices and reducing margins and taxes, reforms in Ghana turned out to be successful. Already for some years farmers receive around 70 per cent of the net f.o.b., equalling around 995 USD/ton in 2006-07. Despite this increase in price, COCOBOD’s share of the export value remained high. Reinvestments in the sector have been various, but there is a lack of clarity on the exact value of these investments and the extent to which they benefit farmers equally. The higher producer price did, as intended, contribute to a recovery of cocoa production. The recent increase in volume is mainly attributed to the product life-cycle of cocoa and state interventions aiming at increased productivity, rehabilitation of old cocoa farms and the planting of new varieties (hybrid trees). Smuggling also contributed to the increase in volume of cocoa beans. Surprisingly, productivity in Ghana did not increase. The expansion of output was accompanied by a large increase in num-ber of person-days on the farm, what suggest that the cocoa boom therefore seems to have fueled investments in education and in employment opportunities in other sectors (Teal, Zeitlin and Maamah, 2006).

Although QCD remained responsible for the final quality checks, in this period some problems with quality performance occurred. It is likely that the introduction of competition among local buyers based on volume (instead of prices or quality) reduced the incentive for LBCs and their Purchasing Clerks (PCs), buying cocoa at the community level, to be very strict about quality control and it induced PCs to cheat farmers with wrongly adjusted scales used for weighing cocoa (Laven and Baud, forthcoming). COCOBOD declared in 2005 all bags of cocoa with more than 25 per cent 'purple beans' as sub-standard, and paid local buyers only half of the producer-price. This constrained LBCs financial performance and seriously affected the livelihood of many farmers; not being able to sell (or store) their cocoa they loss their main source of income (Laven, 2007b). Despite these (temporary) problems, due to quality losses in neighbouring countries, Ghana continues to receive a premium for its cocoa beans. Farmers in general appreciate the liberalization of internal marketing, and claim that 'it saved them from a lot of hardship', as their payments are now made on time.

To stimulate cocoa production farmers have been receiving 'free spraying' on their farms. Also public and private pilots have started to provide farmers with fertilizer on credit. The cocoa output increase is a combined result of 'input intensification' in the Ashanti and Brong Ahafo Region, and 'extensive expansion' in the Western Region (Teal, Zeitlin and Maamah, 2006 The poor quality of public extension services has been reason for the private sector and for NGOs to initiate public-private-civil partnerships, supporting farmer-driven extension programmes. International manufacturers and processors, driven by risks of supplier failure, also started to invest increasingly in research (with a focus on pests and diseases and the development of new varieties) and became involved in community development and international certification schemes.

Surprisingly, the introduction of competition did not result in farmers negotiating with local buyers in selling their produce collectively or negotiating for extra services as a group (for example through contract farming). They prefer selling to someone from their social network, and lack the institutional arrangements to support their negotiating power; a major legacy of the former state-marketing system.

Additional to the facilitation of inputs and knowledge to the farmers, COCOBOD developed a unique institutional arrangement to support the access of producers to rising cocoa prices. COCOBOD reinvests part of its margin back in the cocoa sector, giving farmers incentives to remain involved in cocoa production and increase their volume of production. This bonus is an outcome of the yearly recalculation of margins and prices by COCOBOD. This bonus is distributed by the COCOBOD through the LBC's and its Purchasing Clerks. Access to this bonus is not without costs as some administrative regulations have to be fulfilled, less feasible in more remote areas. Furthermore, the bonus is not for all farmers, e.g. it excludes sharecroppers as eligible for the bonus.

Total bonus payments to farmers 2000-2006

Season	Amount in Cedis	Amount in US$
2000/2001	¢70.1 billion	6.79 million
2001/2002	¢41.5 billion	4.12 million
2002/2003	¢157.9 billion	15.30 million
2003/2004	¢161.2 billion	15.62 million
2004/2005	None	17.26 million
2005/2006	¢178.2 billion	58.99 million
Total	¢608.9 billion	6.79 million

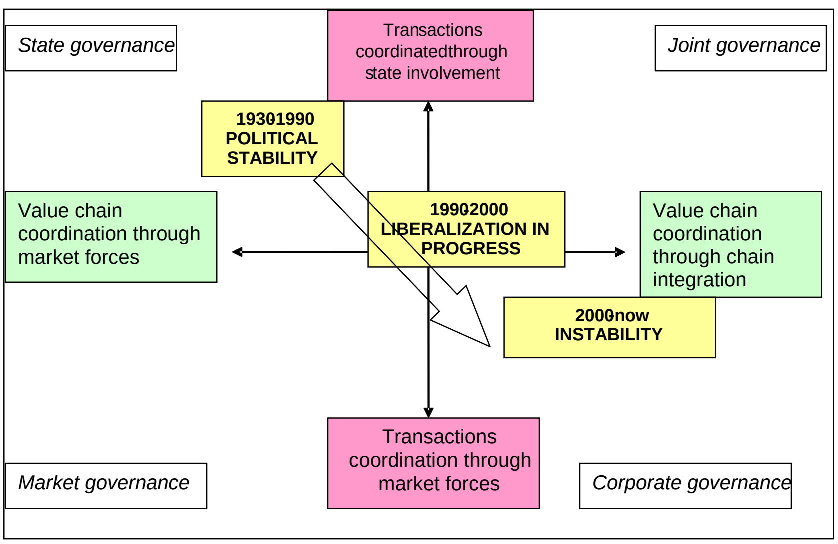
Source: Ministry of Finance, 2007. http://www.ghana.gov.gh/ghana/speech_deputy_finance_minister_prof_gyan_baffour.jsp

4. Côte d'Ivoire[*]

In sum

Côte d'Ivoire had a similar start as Ghana, but its state-controlled governance system, where credit, pricing and export licensing where intimately linked has always had more private partners. Till 1990 the government had major control of the cocoa sector. The farmers are dependent for the export and the domestic market on governmental controlled institutions. After the 1990s a more market-based corporate governance system is in place. After the breakdown of its institutions following the failed cocoa hold up and increased structural adjustment pressures from World Bank and IMF after the debt crisis, the market became again the major mechanism for price negotiation. Foreign companies used the room given for investments in the country and increased 'in-company' chain integration. However, due to the civil war, this process is heavily influenced by pressures to generate 'cash for arms' instead of possibilities to invest and upgrade chain activities.

Changing Institutional Governance Systems in Côte d'Ivoire Cocoa



Introduction

The economy of Côte d'Ivoire is primarily dependent on its agriculture: traditional export crops, particularly cocoa and coffee, other export crops such as palm oil, hevea, pineapple, sugar cane, cotton, bananas, etc. and food crops such as plantains, yams, and cassava. Cocoa accounted for one-third of all exports in 2004 (OECD, 2006, 232-237). Thus, the cocoa-sector in Cote d'Ivoire became an economic power domestically, but also internationally. Cote d'Ivoire is one of the leading producers of cocoa beans. They effectuated this position by an exceptional growth which reached in the midst 1990s 40-45 per cent of world supply and almost 50 per cent of internationally traded cocoa (Losch,

[*] Research Geoffrey Hagelaar and Giel Ton, Wageningen UR

2002, 206). In the following decade the institutional environment and sector policies that facilitated this economic 'Miracle', changed profoundly.
Ivorian cocoa policies going in motion

Period 1 1930-1980 Institutional stability with growth

The specialization of Cote d'Ivoire on cocoa started with colonial rule. The French used the country to generate a strong cluster of tropical agro-export crops. Unless in other countries in West-Africa, a significant proportion of the cocoa export where generated by French planters. The African cocoa growers united in 1944 in the trade union of African cocoa farmers, lead by Felix Houphouët-Boigny. He became the first African minister in a European country, and was the 'founding father' of the independence form French colonial rule. He was elected first time president of the country in 1960 and stayed in power till 1993. He supported the influx of migrants form Europe and neighbouring countries to boost agricultural production. This period can be characterized by a mixture of public ad private efforts with the effect of stimulating, amongst others, the cocoa production and export of Cote d'Ivoire. Production, collection, storage, conditioning and shipping was in private hands. The Ivorian marketing board, lead by the Ivorian government, had the task to license private buying agents and export firms, setting producer prices, rate of remuneration, and commission for traders; and giving final approval to sales contracts with overseas buyers of cocoa but also in the case of coffee (Hecht, 1983, 34).The boost in market demand of cocoa facilitated this strong increase in production. After independence (1960), a continuity of existing institutions and deepening relationships with (foreign) firms in the cocoa business can be witnessed.

At the export level, the originally French colonial trading societies (CFAO, SCOA, CFCI) were progressively replaced by new specialized exporters of foreign origin (SIFCA, JAG, SHAG, DAFCI). These gradually sold shares to local interests transferred to private capital (mainly the *Comafrique* society). The stabilization system created by the French colonial authorities allowed private exporters to remain in business under the centralized management of the marketing board called the *Caisse de stabilization*, abbreviated to *Caisse* or *Caisstab*. This set up continued after independence when the gradually increased powers of the *Caisstab* did not displace private exporters, though it strongly regulated their activity through a system of buying quotas. This system of strong vertical coordination was arena of strong political pressures. It led to the appearance of fictitious exporters, benefiting from political protection to profit in the market or for quotas, which sold their quotas to actual exporters, who undertook the physical management of the product. At the export level the marketing board gained via taxes 38 per cent of the export earnings from cocoa (Hecht, 1983, 30).

At the level of domestic marketing – called *traite* – coordination between agents (farmers, farm-gate buyers, wholesalers (called *traitants*) and exporters) rested on commercial channels based on longstanding 'gentlemen's agreements' and a system of redeemable cash loans (*mandates*) granted by exporters using bank credit. This vertical coordination was built up and strengthened by the stabilization system through an administrative scheme called the *barème* (scale). This involved the *Caisstab* fixing the cocoa prices annually for each stage of the marketing chain (farm-gate, collection centre, exporter warehouse, port warehouse, f.o.b., c.i.f.). Product quality was dealt with by exporters (entailing complementary drying, cleaning and calibration) under final control of the *Caisse de stabilization*.

Also on the international level, cocoa was coordinated by centralized public systems in producing countries (boards, offices, 'caisses', and institutes). These international institutions established crop quality standards. These quality standards served to determine premiums and discounts on quoted prices at the moment of exports. However, the country also used a stabilization system that offered producers a guaranteed price and outlet that did not take into account the quality of the product upstream in the chain (Losch, 2002, 208). According to the principle of the *Caisse de stabilization,* private exporters were the owners of the cocoa but needed authorization from the *Caisse* in order to export it. At the end of the 1970s, however, the *Caisstab* had developed so-called 'direct' sales, in which it negotiated contracts itself and demanded that private exporters implement them. This practice had become very important by the end of the 1980's, covering up to 80 per cent of the harvest.

Like many other producing countries, Cote d'Ivoire invested in a cocoa bean grinding industry from the early 1960s, for two reasons. One was specific to cocoa marketing and aimed to improve performance and revenues by adding value to poor quality beans through processing, hence improving the quality of the exported raw product. The other reason was a more general promotion of industry in the governments program of economic development. Three industrial cocoa grinding companies were created and benefited from public participation, subsidies and preferential tax regimes. The first was (SACO) created by a French industrial enterprise (Cocoa Barry) in 1962. The other two (API and PROCACI) were formed as parastatals in 1968 and 1977, with private management contracts then transferred respectively to SACO and a new Ivorian company (UNICAO) (Losch, 2006, 209).

Production is largely in the hands of smallholders farms. In 1975 for instance there were 450.000 peasant farmers which were growing cocoa and coffee on an average 5.4 hectares a household. This small-scale production is export –oriented and based on the combination of family and wage labour. The wage labourers are mainly a migrant workforce stemming from Guinea, Mali and Burkina Faso (Hecht, 1983, 36-37). The boost of the production of cocoa was mainly caused by the increase in the overall expansion of area under cultivation caused by the increase in the number of smallholder farms. The production of cocoa was not lifted by improving the yield per hectare or intensifying the production otherwise (Hecht, 1983, 42). Collection, storage and export firms were dominantly foreign. For instance, in 1980 Lebanese buying agents and transporters dominated collection and storage while French firms controlled the international marketing and shipping (Hecht, 1983, 34).

Globalization of the cocoa market received its form through an international agreement (1972). This agreement united producer and consumer countries and installed a pricing system and an institutional buffer stock After international price booms from 1977 to 1979, prices fell and the international agreement could do very little about it. Cote d'Ivoire pulled out of the international agreement. Cote d'Ivoire tried to revive the in 1962 founded Cocoa producers' Alliance and it attempted some unilateral action, deluded by its position as the leading world supplier of cocoa. Actions were to pull out cocoa beans from the market, increase its grinding capacity and inaugurated the practice of block dealing (Losch, 2002, 211). Prominent in this struggle for improving price levels, has been the historic cocoa strike. Between July 1987 and October 1989, the government of Cote d'Ivoire blocked all shipments and tried to organize stocks in Europe. However, these endeavours were a total failure because the market could wait until Ivorian beans were again released. The entry barriers for competitors in the cocoa sector were underestimated by Cote d'Ivoire.

Period 2 1990-2000 Liberalization in progress

The domestic consequences were disastrous: the cocoa strike lead to the implosion of the guaranteed prices system, non-payment to producers, and a stricken and bankrupt economy. Due to the virtual bankruptcy of all institutions that had been involved in paying higher-than-world-market-prices, the banking system could not give advance loans to the farmers any more. The institutions that embodied the system of vertical coordination collapsed, and left many chain actors unprepared for doing business in uncontrolled markets.

In line with the political winds after the collapse of the socialist stated in Eastern Europe, the international donors were keen to formally impose liberalization on the cocoa sector and the wider economy and limit the role of the state in economic activities. From 1990 on a privatization program was put in place; the state should withdraw from production activities and certain services. The process of liberalization was forced upon Côte d'Ivoire by donor organizations. The strategic importance of the cocoa sector and the governmental control on the cocoa sector via the *Caisse de stabilisation* were the reasons for the government to resist for ten years the international donor organizations over their liberalization plans (Losch, 2002, 213).

In the early stages of liberalization, different attempts can be identified to control buying networks. One was the organization of a central purchasing pool (the ACCACI company) by seven small exporters which ensured product collection. The collecting company worked with traditional intermediaries as well as with cooperative organizations. Another newly developed organization was the association of producer groups. This system included technical support and equipment and a system of cash loans based on guaranteed payment at the official price. A third attempt was the approach of vertical integration by a trader. This encompassed integrated chain producing quality cocoa with two parts; direct production and product preparation (post-harvest fermenting and drying of beans). The latter experiment still lasts, the other two schemes extinguished. The running costs of such systems were too high to be able to compete effectively in the price competition instigated by liberalization. Growers became more sensitive for the buyers' price bids than to the availability of infrastructure and technical support (Losch, 2002, 221, 222).

The effect of this liberalization and deregulation was that small local exporters were no longer able to obtain finance without the guarantees of the stabilization system. This liberalization process occurred in a period that there was an increasing concentration in the sector globally: the number of grinders and manufacturers reduced to each three-four big international corporations. A division of labor between those conglomerates evolves. A small group of international grinders try to capture the primary production whilst the manufacturers concentrate on marketing the end-product. Priority seems to lie with producing cheap cocoa butter. Transaction is embedded in chains and these chains are now more or less internal to the major global companies/groups. By 2000, 85 per cent of all Ivorian exports were in the hands of foreign firms.

In 1999 the key-player in the old system, the so-called *Caisse de Stabilization,* was dismantled. With that, the guaranteed price of cocoa for producers was not offered anymore. The system developed in this stage, and still existing, is subjected to the logic of the farm gate-buyer. This buyer tries to maximize purchases and proposes prices based on the directions given by partner exporters. Firms compete by securing the loyalty of their middlemen rather than of producers, as well as on liquidity (no guarantees from cocoa institutions) and their capacity to adjust rapidly to price movements (Losch, 2002, 222).

Liberalization is imposed by international donors. The next quote is taken from the Memorandum of understanding (IMF, 2002) between the IMF and the government of Cote d'Ivoire:

> 'In the coffee/cocoa sector, the government will consolidate the liberalization of the sector and continue building an institutional framework that (i) eliminates any direct government intervention and any direct or indirect financial support in the marketing of major commodities; (ii) ensures that international price changes are adequately passed on to producers; and (iii) guarantees free and fair competition at all levels, while preventing monopolistic practices or a return to a system of export quotas.'

The shift away from domestic price stabilization, to the policy to reflect international price changes directly to producers, has led to a situation where prices of cocoa are volatile throughout the cropping season and also differ between regions in the cocoa zone (Losch, 2002, 223). The guaranty price still exists, but is only indicative now, not enforceable. Instead a new institutional context for the cocoa chain was introduced. Instead of the *Caisse,* new managing bodies in the sector were built, such as;

- the coffee and cocoa regulation authority, *Autorité de regulation du café et du cacao* [ARCC]; for regulatory issues
- the coffee and cocoa exchange, *Bourse du café et du cacao* [BCC], for price discovery and price risk management
- the regulatory fund, Fonds de régulation et de contrôle [FRC]; for export credits
- the coffee and cocoa producers' development fund, *Fonds de dévelopment des activités des producteurs de café et cacao* [FDPCC], for financing producer-sponsored rural development initiatives (Worldbank, 2003).

Period 3 2000-present Political instability

These new institutions emerged in a period of increased political instability, including a military coup in 1999, followed by an army rebellion in September 2002, and postponement of several presidential elections in 2005, 2006 and 2007. The on-going conflict between the northern and southern part of Côte d'Ivoire crippled the role of the state. However, despite the geographical separation and political instability, Cote d'Ivoire still accounts for 40 per cent of the world's production of cocoa in 2006.

Cocoa is the main economic resource of the country, representing on average 35 per cent of the total value of the Ivorian exports, worth around 750 bn CFA. An estimated 10 per cent of the country's cocoa is grown in the rebel-controlled zone in the north, the rest of the cocoa is grown in the government-controlled south. In both zones, specific system of levies and taxes are implemented. The national government and especially Laurent Gbagbo, the country's president who came to power in 2001, succeeded to retain control of the national cocoa and financial institutions. The Ivorian government reinstated some sort of minimum producer price and tries to regulate competition to limit market concentration. This initiative was taken as a result of the pressure of and leaders of local companies.

Civil society organisations, and in particular Global Witness, report on the relationship between financial flows in cocoa and the on-going conflict in the country. Global Witness refers to a speech by the president thanking cocoa farmers for their gifts; there has been a discussion among the different cocoa bodies about the appropriateness of using the money for the purchase of weaponry. The cocoa bodies agreed a consensus on this point and mentioned the importance of protecting of farmers' lives and possessions (Global Witness, 2007: 24, 25). Global Witness estimates that a comparable amount (about 15.1bn CFA -US$30m- per year) of money is generated in the rebel-hold northern part of the country to fuel the rebel army (Global Witness, 2007: 37-41). A cocoa blockade prevented northern cocoa transiting to the south, which secured revenues from the cocoa trade for the ones controlling the northern region. Much of the cocoa of the northern zone is exported via Ghana, Burkina Faso and Togo. Companies buying cocoa in Togo are in fact buying Ivorian cocoa.

Characterizing interventions and their effects

<u>The first period: Institutional stability</u>

The interventions in the cocoa sector in this period exemplify the conditions of state governance. Although there is private ownership (grinding companies, exporters, farmers) and there is cooperation between the public and private sector at a first glance, centralization of the state becomes evident when studying the implementation and effect of policy instruments. The Ivorian government influenced directly all actors involved. The tasks and responsibilities of the *Caisse* give this organization a powerful position: the *Caisse* is in control of the chain.

The guaranteed prices meant for the small farmers a guaranteed income. The guaranteed price was about ¼ of the world market price. Although not always, but the trend was of a gradually increasing price through the years. Besides a guaranteed price, farmers could receive a bonus when adopting certain production techniques (new variety, spacing, spraying). The area of cultivated land expanded because of new, mainly immigrant farmers who had access to credit to start cultivation. This had as an effect that average farm size stayed small (5-20 hectares) and the number of farmers exploded to up to 800.000 farmers. By imposing export quotas the state influenced the amount of tonnes of cocoa and influenced with such measures the market. The taxes on export rose to 38-40 percent. A part was re-invested in the cocoa sector for instance to set up grinding companies. The greater part fell to a small elite mainly within the government and industry in Côte d'Ivoire (Hecht, 1983, 31-42)

By controlling the amounts to export and which company is able to export, the Ivorian government influenced the growth and size of the export companies. The state arranged that the exporting companies were and stayed small. There were 50-60 exporting companies which were eventually in private hands, but because of the already mentioned state interventions the exporting companies were very dependent on the government. This meant certainty for farmers, and combined with the Ivorian land policy, this stimulated the growth of the cocoa production. The price which the producer received however was not enough to invest in the expansion of the farming activities. Therefore, the farmers stayed small. As the collection of the cocoa beans was done by intermediaries, there did not develop farmer cooperatives to produce and market the cocoa by themselves. As long as the production and marketing functions are executed by governmental controlled institutions and exporters and within a system of guarantees, farmers have a certain level of livelihood. The farmers were satisfied but did not receive the resources to develop and expand their farm. However, when the power balance within the cocoa chain changes from the Ivorian government to multinational grinders and roasters, the volatility of the market starts to influence the cocoa prices and in line with that the livelihood of the producers. The farmers are then a vulnerable part of the cocoa chain. The group of farmers was not prepared for a change of power within the cocoa chain.

The second period: Liberalization in progress

Liberalization is enforced on to Cote d'Ivoire by donor organizations like the IMF. This means as described above, that market forces become the overall governance mechanism. Decisions on the supply and processing of cocoa beans become 'chain internal' decisions which are made along the supply chain. Taking control of the supply chain has become the task of the few big grinders which are left in the world. The Ivorian government tries to fight this 'take-over', but is compelled by donor organizations to liberalize the cocoa market. One way of trying to keep control on the export revenues of coffee, after the breakdown of the *Caisse de Stabilisation*, is the installation of several new institutions based on World Bank suggestions. To fund these institutions the government raised taxes. The Droit Unique de Sortie (DUS) export tax levied by the state of Côte d'Ivoire provides the latter with a significant source of revenue. Taxes on cocoa, the bulwark of the Ivorian economy, are currently nearly 40 per cent of the export price. Through the DUS, 20 per cent of these go to the state, and 20 per cent to the various managing bodies of the sector (PRSP, 2002). World Bank is pressing for lowering these taxes and para-taxes, to improve the price share for producers, but the IMF is ambivalent, as the cocoa revenues are crucial for Ivorian debt service.

The important changes in Ivorian trade policy began in 1994. By making imports more costly, the change in the parity of the CFA franc allowed a series of measures to liberalize imports and domestic and foreign trade to be implemented. The State's control over production, domestic marketing and export prices often makes it fully responsible for any price risk, whether for agricultural or energy products. The effect of such a system has been that price fluctuations on global markets, especially for coffee and cocoa, have had a much greater impact on the State's finances than on the private sector (WTO, 1995).

As administered prices disappeared form 1999 onwards, prices for cocoa become volatile and more vulnerable for changes in market prices during this period. The implementation of these instruments directed at liberalization of the market coincided with a trend of concentration of the downstream parties of the cocoa chain. The grinding parties and the chocolate producing companies concentrated both into 3-5 conglomerate multi-nationals. By opening up the cocoa market by abolishing quotas and guaranteed prices and the trend in concentration of downstream companies, it becomes apparent that companies are setting the prices for cocoa for farmers as well.

Quality has shown a downward trend over the years 1997-2000 (Losch, 2002, 222). The liberalization reforms introduced in the cocoa sector (as well as in the coffee sector) in October 2002 had three goals: to end direct government intervention and all direct or indirect financial support of the cocoa trade; to obtain adequacy between world prices and producer prices and; to secure the efficiency of competition. The current organization of the cocoa sector, however, lacks clarity, due notably to the overlapping of the various competent institutions. In addition, producer co-operatives suffer from both lack of resources and the inability to obtain a larger share of the market, the minimum price having become a mere guiding price (AfDB/OECD 2006, 232-233).

The institutional system remains geared to collecting taxes which has a strong influence on the difference between the world prices and the price that farmers get for their product. The dismantling of the administered marketing system increased uncertainty and risk. The livelihood of farmers has become vulnerable and they are dependent on the intermediaries who buy their cocoa at the farm gate. Also for national and foreign processing firms uncertainty increased about volumes qualities delivered, and how the farmers and initial buying agents would be financed following stricter conditions of bank credit. In 2000, new institutions related to the Coffee and Cocoa Regulation Authority (Autorité de Régulation du Café et du Cacao – ARCC) were, with World Bank support, organised to provide some form of price predictability and stability in the market. These used two major mechanisms:

- The Regulation Fund (Fonds de Régulation et de Contrôle du Café et Cacao – FRC)
- The Coffee and Cocoa Auction (Bourse du Café et Cacao- (BCC)

The BCC registers prices of all cocoa procurement and shipping in Côte d'Ivoire, and makes these prices publicly available. Based on a cost structure of the activities in the chain it calculates an indicative producer price. If the ARCC decides that this price is too low, it can instruct the FRC to intervene in cocoa markets procuring at a higher price. However, in practice this active role of the FRC to stabilize prices in the market has been absent in the first years of its existence.

<u>The third period: Political instability</u>

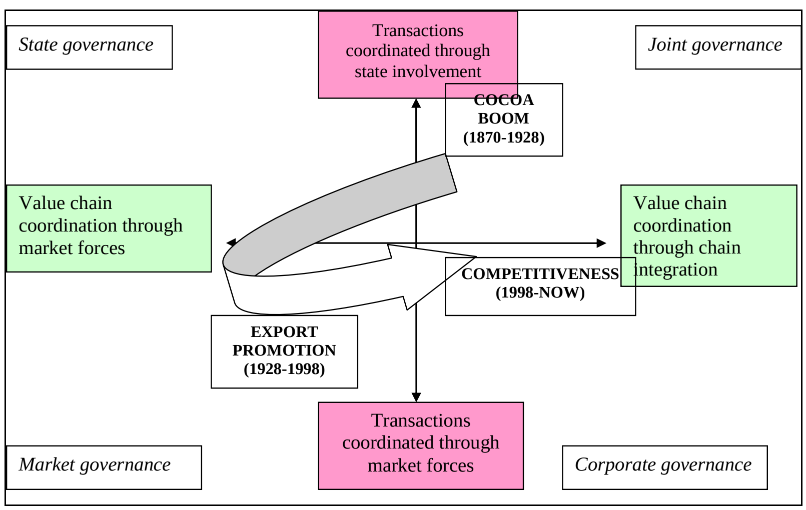
In this period of political turbulence and civil warfare, the Ivorian government implement these new institutions. The intention is clearly oriented at damping the turbulence for the farmers, and also by imposing taxes, to generate the necessary funds for non-cocoa related expenses, including the resolution of the civil war. The tax pressure on cocoa is high, partly due to the collapse of some sectors of the economy and the closure of many small and medium-sized companies that have made the government to depend primarily on the tax levies on cocoa (OECD, 2007). Global Witness (2007) also observed that parastatal agencies responsible for economic conditions in the cocoa sector used large amounts from levies on cocoa transactions for non-cocoa related purposes. During this episode, characterised by a complex intertwining of private and government (or rebel-government) governance of the sector, financial transparency of the institutions controlling the cocoa sector was reduced. This eroded the effort to stabilise prices in the cocoa value chain. However, farmer pressure for an effective minimum producer price is strong and, with the civil war waning, the government policy is expected to be increasingly geared to make the 'indicative' producer price defined by ARCC as the effective minimum price to farmers by a more targeted use of the FRC funds. Some pilot experiments with risk management instruments like 'hedging' are started with support of the CFC and ICCO.

5. Ecuador*

In sum

Ecuador started cocoa production with an institutional governance system where private interest where intimately related between producers (plantations), exporters, bankers and policy makers. The existing vertical integration has been broken after the 1925 coup d'état and the subsequent period of market deepening and globalization of production and consumption. Vertical integration has been replaced by a more facilitating role of the government, and an atomization of production due to changes in land tenure, replacing the plantation model with the smallholder model of production as dominant feature of cocoa production in Ecuador. The current emphasis of the Ecuadorian government in developing public-private chain platforms makes that this 'relatively' market-based governance system is heading to a corporate or even (incipient) joint governance system.

Changing Institutional Governance Systems in Ecuadorian Cocoa



Source: Authors, based on (Griffiths and Zammuto 2005)

Introduction

Ecuador is a major player in the world cocoa economy. Not because of its volume of cocoa, but because of the quality of the beans. The market share of fine and flavour cocoa (FF cocoa) has fallen dramatically over the last century, due to new processing technology, bulk cocoa beans proof to be good or even preferred by some chocolate manufacturers. However, especially in Europe the demand for this type of specialty cocoa is growing and easily capable to absorb production increases. International demand of FF cocoa outweighs supplies, which creates a very attractive niche for cocoa chain development. The quality of Ecuadorian cocoa has been a product of nature, without much additional quality policies, until the end of the twentieth century, when quality policies have been introduced to shape its distinctiveness with other varieties on the Ecuadorian market.

* Research Giel Ton, Wageningen UR

Ecuadorian cocoa sector policies in motion

Period 1 1900–1925 Cocoa Boom and Private Banking

Ecuador has been the major producer country of cocoa during the late 19th and beginnings of the 20th century. By the turn of the century, it provided 20-25 per cent of world production. High cocoa prices, coupled with abundant supplies of cheap labour and an infrastructure of rivers that connected the production areas with global export markets, gave rise to booming business. A powerful oligarchy, made up of large producers, exporter, importers and bankers, developed in the coastal areas of Guayaquil. Backward and forward linkages of the cocoa sector with the rest of the Ecuadorian economy were limited (De Janvry, 1981; Henderson, 1997). The rivers formed a cheap and efficient form of transport for cocoa shipping and this generated few incentives to use cocoa revenues for road or rail construction. Though cocoa exports provided the main source of currency for imports and fiscal income for the state, little of this hard currency was spent on productive infrastructure or invested in domestic manufacturing. The Ecuadorian cocoa boom created a class of very rich families, many of them living abroad, that concentrated state power and enjoyed a life-style based on imported luxuries (Larrea and North, 1997).

The direct intertwining between these private family interests and the government during this period manifested itself in the development of the so-called 'baquete de estado' (the state's banquet) around the agricultural bank – BCA (Banco Comercial y Agrícola) – based in Guayaquíl. Henderson (1997) gives a careful and precise description of this:

> 'In order to sustain politically necessary expenditure (..), liberal governments, dependent on fluctuating income from customs revenues and largely denied access to foreign loans, a consequence of Ecuador's poor history of debt servicing, increasingly resorted to borrowing from domestic banks. The steadily mounting internal public debt was for the most part funded by two Guayaquil banks, the Banco de1 Ecuador and the Banco Comercial y Agricola. At the turn of the century roughly half of the debt was owed to these two institutions and the proportion continued to rise in subsequent years, with the BCA assuming the dominant role in 1911. (..)Another organization that became key in fostering the dominance of BCA was through the Association of Agriculturists -, the Asociación de Agricultores, which was established in 1912 by prominent cocoa exporters to control the price of Ecuadorian cocoa on the world market. In 1914 the Asociación began buying cocoa from producers by paying them half in cash and half in vales (i.0.u.s). Speculating on a price rise, it then exported the cocoa on consignment. By 1916 the Asociación was responsible for purchasing 77 per cent of Ecuador's cocoa. (..) In purchasing an ever increasing proportion of the country's cocoa, the Asociación was forced to borrow in order to finance its operations, the costs of which far exceeded the revenue obtained from the export tax. (..) As a guarantee for the loans the export tax was pledged to the Bank. Furthermore, as the Asociación's financial situation deteriorated, the foreign drafts that it received for its cocoa were also handed over to the BCA, which thereby came to control a substantial share of the country's foreign trade' (Henderson, 1997: 179).

By this, the BCA, a private bank, controlled virtually all aspects related with cocoa exports. It almost broke down in 1921 due to low post-First World War commodity prices and serious cocoa plant diseases (Witches' Broom and Monilia Pod Rot). Faced with the prospect of a major banking collapse and no doubt pressed by the BCA Congressional bloc, the government was forced to intervene, and rescued the bank by admitting 'free' monetary emissions by the BCA, based on the banks property of state bonds. The result proved a 'solution' for the financial problems of a private bank and its cocoa plantation owners, by shifting the burden to other sectors, creating an inflationary process that affected the entire economy. In 1925, a coup d'état, attacked this intimate 'steering' of state policies in the interest of a class of very rich private families. One of their first actions when assuming power was to restructure the omnipotence of the BCA.

Period 2 1925-1998 From Rent Seeking to Export Promotion

The 1925 coup d'état indeed managed to break the financial-political oligarchy. They dismantled the BCA and re-engineered the monetary institutions to prevent a similar banking crisis as with BCA (Drake, 1989). However, the Great Depression and World War II made it difficult to attract investments in a more national, broad based, development. The dependence of the Ecuadorian state on agro-export taxes made it dependant of the political power of the plantations. Next to the cocoa and coffee exports, the banana plantations began to spur. As these plantations are mostly located in the lowlands, it re-affirmed the dependency of the state (in the capital Quito) of the second main city Guayaquil. This relation induced CEPAL (UN Economic Commission for Latin America and the Caribbean) to call the development of Ecuador 'bi-centralista', with two centres. The flow of economic rents form the periphery to these centres left the rest of the country disarticulated from the benefits of economic circulation and growth, resulting in extreme poverty. The post-war booming banana sector reproduced the situation that few incentives were there to start a process of 'import substituting industrialisation', the economic policy recommended by CEPAL during the 50-70s, During the 1960s and 1970 petrol became Ecuador's most important export product replacing the agro-export sector as the major source of fiscal income.

The upward spiral in oil prices during the 1970s and the boost to public sector revenues derived from oil exports freed the Ecuadorian government from persistent balance of payments deficits and from reliance on domestic taxation to fund expenditure, enabling the state to embark upon an ambitious programme of industrial development, infrastructure expenditure and social investment). (..)The new oil wealth gave a further stimulus to a process of industrial development already aided by preferential treatment and favoured status under the provisions of the Andean Pact. The manufacturing sector was able to appropriate for itself a substantial share of the new oil wealth in the form of subsidies and protection for new industries, tax concessions and the formation of joint ventures involving the state, national and multinational capital. As a result manufacturing industry grew at an annual average rate of 10 per cent between 1972 and 1981, so that by the end of the decade manufactured goods comprised 25 per cent of total exports (Corkill 1985). Also the state bureaucracy increased sharply. Quito developed in a large part as a result of increasing public servants employment. Ecuador registered one of the highest average annual growth rates in public sector employment in the developing world (in excess of 10 per cent for 1976-80), with the capital city benefiting disproportionately (Corkill, 1985).

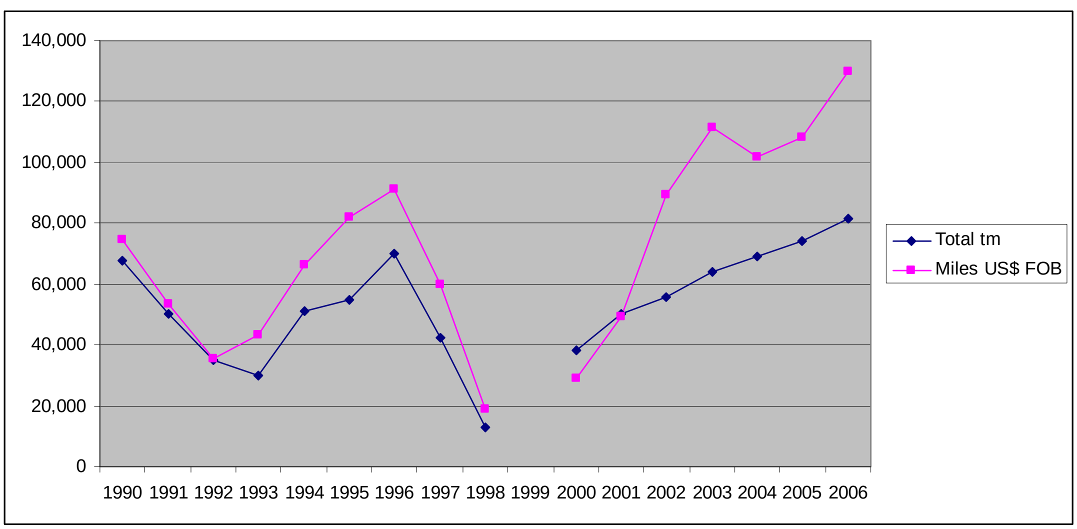
This petrol 'bonanza' created the conditions for structural deficits in public finance. Revenues from petrol exploitation made Ecuador a preferred client of international lenders. At the turn of the century this had resulted in one of the most indebted countries in Latin America. The scarcity of hard currency and the balancing of the fiscal deficit were coped with by monetary politics of money creation and associated devaluation the local currency. This depreciation of the local currency, made domestic costs relatively cheap and resulted in high revenues from exports. This obviously favoured the cocoa sector, and partially offset negative impacts of the falling cocoa prices during the 1980-90s.

Period 3 1998-2007 The 'Dollarized Economy' and Competitiveness

The Ecuadorian cocoa economy collapsed in the 1995-1998 period due major political and economic turbulence. The chart above illustrated the productive an economic decline during the 1990s. As world cocoa production has increased greatly, and also the specialty cocoa markets found a major producer in Indonesia, the volume of Ecuadorian cocoa has stagnated on to the pre 1995 level. In contrast, export earnings have risen sharply due to rising commodity prices (Figure 4). Productivity of Ecuadorian trees is relatively low, though marketing costs are reported to be lower than in competing countries (Collinson and Leon, 2000).

Political turmoil resulted in several short-lived presidencies: the populist president Buckaram, elected in 1997, was declared 'mentally ill' by the political opposition, reacting especially on allegations of corruption and economic mismanagement during his short rule, and replaced in a sequence of presidents with little control over the country and alleges by charges of corruption and economic mismanagement. The situation of hyperinflation resulted in a sequence of popular uprising that culminated in January 21 2000 when President Mahuad fled the country after the popular movement took the National Assemblee by force. Vice-president Noboa took office and implemented a shock therapy in which Ecuador tuned to a dollarized economy: the US dollar became the official national currency. This dollarization dramatically changed the possibilities for the Ecuadorian government to use the devaluation of the currency as means to offset production inefficiencies and falling prices. The "dollarization" of the economy forced companies to be more efficient in order to compete in the international market.

Figure 4 Ecuador cocoa beans export (1990-2006)



Source: http://www.sica.gov.ec)

The emphasis of the Ecuador government agricultural policy is therefore on an increased facilitation of chain partnerships and chain development efforts. The importance of coordinated chain action is especially important in the Ecuador cocoa sector that depends to a significant degree on its quality of produce (FF cocoa). Creating an enabling environment for the marketing of the Ecuador specialty cocoa has become a top priority in Ecuador cocoa sector policy.

This enabling policy for chain development became manifest in the regulation of quality in the cocoa chain that led to a specific policy to steer the impacts of the introduction and marketing of a new cocoa variety: CCN51. National cocoa trees ('Arriba') are low yielding and are mostly restricted to small and medium sized farms. CCN51 by contrast is a relatively new, high yielding variety and is mostly produced on large-scale plantations. Ecuador's local cocoa processing and chocolate manufacturing industries prefer CCN51 because it has high cocoa butter fat content and suffers no mould problems, but most cocoa exporters are in favour of national cocoa and its associated quality premiums. Exporters' profitability relies heavily on this price differential (around 15 per cent). Under the responsibility of the Ecuadorian National Council for Reactivation of Production and Competitiveness - CNRPC (Consejo Nacional para la Reactivación de la Producción y la Competitividad) the sector concentrated on a limited number of value chains. A key one is the value chain of specialty cocoa. CNRPC supports the Consultative Council of the Agroindustrial Chain of Cocoa and Derivates (Consejo Consultivo de la Cadena Agroindustrial Cacao y Elaborados). Supported by funding of the European Union and GTZ, this council aims to recover/defend the special position of Ecuador cocoa on the world market. Major result of this chain coordination is the decree of July 2005 that defines that specialty coffee ('Arriba') has to be marketed separately form the new CCN51 variety.

Another milestone in cocoa chain development has been the 2004 National Forum of the Cocoa Chain, which gave rise to a shared vision and action plan. Follow-up is given by two entities: the Steering Committee composed of chain actors (active in production); and a Support Group, composed of supporting stakeholders (NGOs and donors). Their activities continue with BID donor support. The shared vision is to double cocoa production within 5 years. The cocoa sector strategy focus is on 4 objectives (http://www.ecuadorcocoaarriba.com/):

- renovate and improve existing plantations to increase yields;
- align product quality to market demands;
- further positioning of the Ecuador's fine and aromatic cocoa ("cacao fino y de aroma de Ecuador") in the national and international markets
- the nation wide organisation and entrepreneurial skills of the small scale cocoa producers is strengthened and they are more efficiently linked in the chain

Characterizing interventions and their effects

<u>The first period: Cocoa Boom and Private Banking</u>

The first period in Ecuadorian cocoa sector policies can be characterized as a combination rather strong vertical coordination of the cocoa chain through the Guayaquil oligarchy. They manifested itself in two organizations: the BCA (the private Commercial and Agricultural Bank) and the Association of Agriculturalists that in the early twentieth century managed to control most of the cocoa production, trade and exports. There was very intense personal intertwining between cocoa associated private interests and the Ecuadorian state. The strong chain coordination could translate itself in very favourable, though in the end unsustainable, public policies that generated culminated in 1921 with a bankruptcy and a monetary emission when the tree pests devastated the Ecuador cocoa production from 40.000 TM in 1915 to 15.000 TM in 1930 (Cabrera, 2005). During this period the fiscal needs of the state have been negotiated intimately with the private interest of the oligarchy. The governance structure of the cocoa chain in this period can be placed in the utmost corner of the Joint Governance quadrant of the matrix.

The second period: From Rent Seeking to Export Promotion

During the second period the vertical integration in the cocoa chain was significantly reduced. Smallholders entered and replaced the plantations as prime production sector. The state tried to break with the oligarchy and increasingly depended on support of other sectors in the economy. Meanwhile, the oligarchy diversified its activities to other sectors in the economy, especially in bananas. In the 1970s petrol became the key sector for the generation of fiscal revenues. We may place the governance structure that characterizes this period between state governance and market governance. Compared with the previous period the coordination in the value chain became less hierarchic and more market based, and state involvement was important though not decisive in shaping sector policies.

As monetary and trade policies, were characterized by protection of the emerging manufacture sector and 'cheap food for the cities', the price level of domestic costs structurally lagged behind the value of 'hard currency' generated by exports. The cocoa sector policy became integrated with wider macro-economic policies of export promotion and import substitution that generated conditions for the development of local processing facilities. In line with the dominant paradigms about an import substituting industrial policy (ECLA-CEPAL) and the generating a fair and better predictable world price (UNCTAD), Ecuador participated in the international cocoa agreement that tried to influence world market prices.

The third period: The 'Dollarized Economy' and Competitiveness

The value of the domestic currency becomes replaced by the value of the US dollar. Current macro-economic policy room is limited to the managing of fiscal and trade balances, but it is impossible for the Ecuadorian government to use the instrument of money creation as it has prevailed in the past. Likewise, the influence of state policies in the cocoa chain has been strongly reduced as a result of the dollarization of the economy. The role of the state is explicitly limited and focussed on the creation of 'strategic alliances' between chain actors. The state plays a pivotal role in generating the national organisations and consultative councils through which this corporate governance is effectively institutionalized. The government plays an active role in fostering chain coordination between all involved chain actors. A key activity of the Consejo Consultivo de la Cadena Agroindustrial Cacao y Elaborados, is to recover/defend the special position of Ecuador cocoa on the world market. Major result of this chain coordination is the decree of July 2005 that defines that specialty coffee ('Arriba') has to be marketed separately form the new CCN51.

6. Conclusions

This paper shows that the specific economic conditions for sustainability in producing countries are an outcome of the interplay between market coordination and state governance. Chain actors, e.g. farmers, processors, traders, are constrained and/or enabled by the national economic policies, the rules in the market place and political economic power relations in creating competitiveness in global markets. Crucial aspects influencing the performance of the cocoa value chain, like production volumes, product quality and distribution of value between chain actors, are to a large extent a result of the changing institutional governance systems and its 'enabling environment'. Accordingly, the paper suggests that policy and strategy targeting sustainability in a complex and layered commodity chain may be more effective when they build on existing governance structures and policy measures instead of replacing them with an entire new organisational architecture, with a drastically changed division of labour between public and private domains. Subsequently, the recommendation is that before replicating or transposing organisational frameworks and public sector roles from one context to another, it is important to identify the main 'rationale' and driving forces behind the historically evolved and currently prevailing market regulatory functions and patterns of public sector involvement (Joosten and Eaton, 2006). As a result of such an approach, it is better possible to outline the main functions for public policy in achieving sustainability (Vellema et al, 2007).

In this paper the prime focus is on mechanism and arrangements that create (or have created) the capacity to increase predictability of prices and stability in transactions in the cocoa chain, which may lead to inclusive and sustainable development for the large numbers of smallholder producers engaged in cocoa. The case studies point at existing institutional arrangements generated in the historical development process of a specific sector that serve these purposes. This observation draws attention to the existence of, and suggests a revaluation of, sector specific policies ('industrial policies'). From the study it is obvious that cocoa has sector and country specific problems, e.g. low quality or low economies of scale, which have been addressed by specific rather than generic policies. Industrial or sector policies have shown to be dynamic and are responding to new challenges from their specific historical preconditions, market dynamics and development paths. Not all policies are responding in a satisfactory way to all challenges. Instead of exploring a 'best for all' policy recommendation, the challenge lies in finding appropriate and effective institutional arrangements that respond to context specific sector policies and that are based on transparent public-private configurations. This may imply the need for change in focus by policy makers and a shift in interest from macro policies to policies filling the void at meso level when targeting sector or commodity specific measures for sustainability.

In all three countries we see that at a certain point of time a transition has been made from an institutional governance system with strong state involvement in price setting and international trade to a system where transactions are more market based. The extent to which the state keeps a leading role differs. In Côte d'Ivoire, the public private interaction governing the cocoa sector changed dramatically. While Ghana maintained a stronger state involvement in defining prices and contract conditions. In Ecuador we see that the role of the state in cocoa taxation is far less than in the West African countries. In both Ghana and Côte d'Ivoire, the cocoa sector is still the major agricultural export crop and therefore crucial in generating funds for the state bureaucracy and for national economic development. Taxation of the cocoa sector through state control on transactions is higher than for other agricultural sectors. Specific (para)fiscal taxation arrangements are created to transfer resources to the state. This is reflected in the relative lower producer price: the farm-gate price as a percentage of the reference world commodity price for cocoa. This producer price as a percentage of the FOB price, is lower in Côte d'Ivoire than in Ghana, and both are lower than in Ecuador.

However, perhaps more than with relative producer *price levels*, the success of cocoa sector policies seem to be related to service provision and policy measures in the cocoa chain that increase the *'stability' in the prices* in both input and output markets. Before the eighties, state credit was elementary to facilitating access to inputs and the state-led pricing system facilitated the predictability and stability of output markets. In all countries processes of liberalization and privatization, induced by IMF and World Bank conditionalities, affected the possibilities for such an enabling environment. Generally the cocoa liberalisation reforms increasingly confronted producers and traders with risks within value chain transactions. This increased 'instability' in the cocoa value chain has been mediated in three case studies with the unfolding of new or adjusted institutional arrangements between private chain partners and the state. As a response, private actors and NGOs have become increasingly involved in providing some of these services to producers.

In Ghana, the state has still a major role to play in the cocoa sector. The Ghanaian state continued with the state-control on internal prices, which materialized in the yearly review of cocoa prices, margins and bonus system. Their interventions, and their outcomes, have eased the responsibilities of other actors to become involved in the sector. For example, NGOs play only a marginal role in the cocoa sector. NGOs have also been constrained in attempt to introduce organic cocoa in Ghana, providing farmers with a new marketing channel for niche markets. It seems that interventions in the cocoa sector in Ghana require consent and involvement of the state. Policies aiming at Ghana as a sustainable sourcing country are likely to be more successful than the introduction of separate marketing channels for sustainable cocoa.

In 2000, the government of Côte d'Ivoire ended state control through the system of administered prices, but retained some influence through several new institutional arrangements to enhance price predictability and stability in the market. The arrangements aim to increase transparency of prices and cost structures and calculate 'reasonable' producer prices. The government is entitled to intervene in the cocoa market if prices decrease too much. In recent years the government took some policy measures to respond to price turbulence in the market. However, the cocoa sector was also central in the generation of public funds through taxation. The latter outweighed the importance of the policy to increase farm-gate prices. More than the new cocoa sector policies, the maturing of the new cocoa plantations established during the 1990s turned Côte d'Ivoire into the main producing country replacing Ghana as the world leader in cocoa exports. Côte d'Ivoire has the international cocoa grinders as the major export companies in the country. This concentration of 40% of world cocoa production in Côte d'Ivoire is compensating partly for the worsening of the political and business environment and facilitated investments of international cocoa grinders in the country. Service provisioning by the state is weak; the poor extension services led to the entering of some NGOs and public-private partnerships, but on the whole they provide limited alternative services to farmers.

In Ecuador the international buyers dominate the cocoa value chain. Some domestic cocoa processing takes place, but most of the special quality cocoa that Ecuador produces is processed in Europe by a wide array of specialized chocolate factories. The government mainly sees its role in facilitating chain alliances, which can enforce the special position of Ecuador's quality cocoa in the world market. Quality regulations and public private partnerships play an important role in vitalizing this 'high price niche market' strategy. The Ecuadorian government mainly contributes to institutionalising chain governance and coordination. The government's main influence on the enabling environment for price setting within the chain is through quality enhancing policies, especially through the separation of modern high yielding lower quality CCN51 cocoa from the traditional low yielding higher quality Arriba cocoa. As smallholder grow predominantly Arriba cocoa that has a significant price premium on the international market, this policy of chain segmentation fosters the economic sustainability of smallholder cocoa production.

	Ghana	*Côte d'Ivoire*	*Ecuador*
Typification of the institutional governance system	Joint Governance	*Corporate Governance*	*Corporate Governance*
Direction of change of public-private configuration	Increasing state control on transactions and private sector investments in chain integration	Corporate Governance by the private sector, with decreasing state involvement linked to the civil war	Corporate Governance on a pathway to Joint Governance with a facilitating role of the state
Key policy measures affecting predictability of prices and stability in transactions in the cocoa chain	Administered prices and fixed margins Producer Price Bonus	Cocoa and Coffee Auction Regulatory and Control Fund - FRC	Consultative Group on Cocoa and Derivates
Outlook => direction of change	International buyers are increasingly concentrating investments in Ghana, as the cocoa sector policies create a stable environment for sourcing bulk cocoa. The system gives ample incentives for improving cocoa yields and producer prices. Incentives for chain segmentation and niche marketing based on quality differentiation is low.	The state fails to create incentives for further investments in cocoa quantity and quality by farmers. Service provisioning to farmers has been severely affected by the drain of resources due to the civil war. Economic sustainability of smallholder production will be contingent on the use of the new cocoa institutions for increasing the relative producer price.	The state plays a facilitating role, only marginally draining resources away from the sector. Improvements in quality and quantity will be centred on 'brokerage' of private – private partnerships in the cocoa chain. The state is in the process of re-inventing sector specific policies for increasing economic sustainability.

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Author: Otto Hospes

paper #11
Understanding institutional arrangements: Fresh Fruit and Vegetable value chains in East Africa
Authors: Derek Eaton, Gerdien Meijerink and Jos Bijman

Editors of this series:
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