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file

Coffee Agreement
Decision

Mike Duval-F41

I believe I
sent this to you
last week

Bud

Call
BRUCE

NATIONAL SECURITY COUNCIL

May 10, 1976

NOTE FOR: Bud McFarlane

FROM: Malcolm Butler *mb*

There is an additional political argument which I did not put in the memo: So far coffee prices are not a political issue. Making a public statement would be one way to make it a political issue, however, and it would be one which would offer the President nothing. He would be admitting that he had taken a decision which was no longer in the country's interest, and he would be creating expectations he could not fulfill -- he can do nothing to put more coffee on the world market, and that is the problem.



NATIONAL SECURITY COUNCIL

INFORMATION
May 10, 1976

MEMORANDUM FOR: BRENT SCOWCROFT
FROM: MALCOLM BUTLER *MB*
SUBJECT: Coffee Prices and International
Coffee Agreement

Bud asked me this morning to prepare a fact sheet on the relationship--or, more accurately, non-relationship--of recent coffee price increases to the International Coffee Agreement now pending before the Senate.

Attached (Tab A) is such a fact sheet, which summarizes arguments suggesting that there is no connection between higher prices and US participation in the Agreement. The thrust of these points is that coffee production has fallen off markedly as a result of various factors, most importantly the disastrous frost in Brazil, and that scarcity of supply explains recent price increases. To the extent that the market is nervous, any extraordinary expression of concern would only aggravate the situation, and probably lead to additional increases.

Treasury as well as State would agree with the substance of these comments.



Coffee Prices and International Coffee Agreement

Although coffee prices have continued to rise rapidly since the new International Coffee Agreement was signed on February 27, this appears to be the result of market forces rather than supply manipulation by producers. Any move to back away from the International Coffee Agreement now pending before the Senate would be likely to increase any speculation which may be stimulating price increases, driving them up still further.

- The price increases are the result of a sharp reduction in world coffee supplies brought about by a major crop disaster in Brazil, the world's largest producer, where frost destroyed millions of coffee trees and cut production by two-thirds. Bad weather in Colombia, and the disruption caused by the war in Angola and the earthquake in Guatemala, have also adversely affected supplies. (Congressional hearings in March reached the same conclusion.)
- Coffee exports to the US are 13% above exports for the same period last year. If producers are withholding coffee now for shipment later in the year, the total increase for this year compared to last would be even greater.
- There is no hard evidence to support a connection between current high prices and the new Agreement. (Under the Agreement, prices would have to fall 45-59 cents per pound before export restrictions could be put in place.) On the contrary, the Agreement gives producers the security they need to restore production through investments in massive replanting programs which will help assure adequate supplies at fair prices in future years.
- We are investigating reports that three small producers in Central America -- Honduras, El Salvador, and Costa Rica -- are tinkering with export restrictions. Our initial view is that these reports represent confusion with long-existing regulations limiting exports slightly in order to keep domestic prices down.
- We have expressed our concern to the President of the Brazilian Coffee Institute, who points out that Brazilian consumers have faced drastic coffee price increases themselves. (Secretary Simon will also discuss this problem during his visit.)



- Private traders may be withholding some coffee from the market, but this is in line with normal commercial practices and is not related to the International Coffee Agreement. US stocks of green coffee have risen 40% since the frost, and 15% in March alone.

- Given the present nervous market, we must expect some speculation. Focusing more attention on coffee prices by withdrawing the Agreement or issuing a Presidential statement would tend to increase this nervousness and the resulting speculation, leading to still higher prices. No action we can take will put more coffee on the market.

- Both the President and Secretary Kissinger have frequently mentioned the US participation in the International Coffee Agreement as a concrete example of the willingness of the United States to participate in international commodity agreements which are practical solutions utilizing market forces to dampen cyclical fluctuations. Appearing to renege the Agreement would undermine our strategy in the North-South dialogue.



COFFEE PRICES

1. Natural market forces moved green coffee prices after the freeze in Brazil from 60¢ to the mid-80¢ range, reflecting an anticipated drawdown of excess world stocks. Prices stabilized at this level for 3-1/2 months. Nothing has occurred to affect anticipated world supply since the Brazil freeze.
2. The subsequent green coffee market move from mid-80¢ price range to \$1.30+ is a direct reflection of:
 - a. U. S. approval of the draft International Coffee Agreement in London in early December. Under ICA, the producing countries' shares will be importantly based on shipments after October 1976. Producing countries, therefore, are withholding stocks to release this fall. There is clear evidence of this. (NOTE: One can be misled by the fact that January-March 1976 U. S. green coffee imports were 13% ahead of the same period year ago; actually, the year-ago quarter was atypically low. Versus the previous four-year average, imports are down 3%, this during a period of heavy roaster demand reflecting large retail trade purchases of coffee in the face of major list price increases.)
 - b. Producing countries belief (based on statements in House Committee hearings of 3/17 and 3/19, and President's Message to Senate of 4/5) that the U. S. Government is not unduly concerned about consumer coffee prices at \$2.00+/pound level that will result from current green coffee prices.
3. The roasters' list prices have been raised to within 2-3¢ of current green coffee prices. Retail prices still lag. The retail price was \$1.23/pound before the Brazil freeze. It is currently \$1.57/pound. It will be \$2.07/pound about July 1. Roasters will start shipping current list price coffee by 6/1. After that, there will be no way to avoid \$2.00+ coffee at retail. If green coffee prices come down significantly before the end of May, the roasters could avoid shipping coffee at the current list prices.
4. Green coffee prices probably will be reduced significantly by fall as the producing countries release stocks to gain shares under ICA. But U. S. consumers will face \$2.00+ coffee from July through September or October -- in the very heat of the Presidential campaign.
5. The only realistic way to bring green coffee prices down by the end of May is for the U. S. to announce a delay in considering the ratification



of ICA, thereby encouraging the release of stocks now being held for fall shipment. There is no need for ICA at this time to encourage the production of coffee. Price will do this. Green coffee prices in absence of ICA will probably remain in excess of 80¢ until 1979 when world excess stocks begin to build.

6. If coffee gets to \$2.00+/pound, a highly controversial consumer issue is certain to erupt -- and as certainly will be aired and exploited by political adversaries of this Administration.



THE WHITE HOUSE
WASHINGTON

May 13, 1976

MEMORANDUM FOR: BILL GOROG
FROM: MIKE DUVAL *Mike*
SUBJECT: COFFEE PRICES

By way of follow up to my previous memo to you on the coffee price problem, the following is some additional information which may be of help as you prepare the decision memo.

I'm advised that the price of green coffee rose from the mid-eighty cent range to \$1.30 as a result of U.S. approval of the draft International Coffee Agreement last December. According to my information, this occurred because under ICA, the producing countries will have a share of the U.S. market based on their shipments after October of this year. In order to increase that share, the producing countries are withholding stock with the intention of releasing them this fall, and this, of course, is causing the price to rise dramatically here in the United States.

I understand that it is entirely possible that retail prices are likely to rise by mid-summer to the \$2.00 plus range per pound. This is in comparison with the current \$1.57 per pound which is the current average price.

Although there is some question as to the cause of all this (apparently imports are up this year compared to a year ago, but that reflects the fact that last year was an all-time low), it is nevertheless generally accepted throughout industry that the dramatic increase in retail price is due to the Coffee Agreement. Therefore, we're faced once again with the allegation that government action is hurting the consumer.

I'm advised that one way to force the price down to competitive market levels for the consumer is to announce a delay in Senate



ratification of the Agreement. This might make some sense in light of the fact that there probably should be an Administration review of the current prices to determine whether or not the Agreement is causing the dramatic increase.

I think it's important that the President focus on this before there's any major outcry in Congress, so that if corrective action is warranted, he can take it within the Administration, and not pursuant to Congressional and public pressure.

