KONA KAI FARMS POSITION PAPER
THE STATUS OF THE KONA COFFEE INDUSTRY

November 7, 1991

On Friday, November 1, *West Hawaii Today* ran an editorial entitled "Trouble Brewing for Kona Coffee" which declared "The Kona coffee industry is in trouble and those who make up the industry are most to blame." It went on to detail the problems of today's low prices, competition from coffee on other islands, problems of protecting the name "Kona" and the "Kona Blend" situation, and the lack of a cohesive voice speaking for the industry as a whole. It concluded that the "secret" of Kona coffee "will die with the Kona coffee industry itself."

Although we might argue that some of Reed Flickinger's charges are not justified as to our company, we agree with the sentiments expressed in the editorial. The industry has been in a state of crisis for over one year, and we have yet to see any basis for improvement. The farm price for coffee cherry stands today at 50 cents per pound from Kona Kai Farms and 40 to 45 cents from other Kona processors, down from 55 to 65 cents last year, and over 90 cents during the 1989-90 harvest year. Since most farmers agree that they need to receive at least 70 cents per pound to make coffee a worthwhile venture, the long-term implications of low coffee prices are obvious and indeed do threaten the existence of the industry. It is incumbent upon Kona Kai Farms to respond to the pessemistic outlook voiced in *West Hawaii Today*, and to give our best assessment of the realistic situation facing Kona coffee farmers today.

WHAT KONA KAI FARMS HAS BEEN DOING

If Kona coffee farmers go out of business, then we go out of business. Besides farming 30 acres of coffee, Kona Kai Farms depends on coffee supplied by over 300 farmers for the raw materials necessary for our business: the sale of Kona coffee in all its forms--green, roasted, and by the cup. We have a tremendous investment in land, plant, equipment, and human resources that is at risk if farmers were to quit farming coffee. As a consequence, we have put a lot of effort into reversing the current downward price/supply spiral.

It is obvious that we cannot rely on any one large outside marketer to provide stability for either our own company or the Kona coffee industry in general. When push comes to shove, any such company is too removed from the situation to respond quickly and effectively to changes in the Kona coffee market. Any large coffee marketer, whether it be Superior Coffee, UCC, or C. Brewer, only relies on Kona coffee for a tiny percentage of its sales. Conversely, local processing companies are almost totally dependent on Kona coffee for their business, so they cannot have a profitable business without a healthy industry--they have the incentive to keep the farm prices at a tolerable "floor" so their suppliers don't go out of business.

What the industry needs is for local companies to develop the capability of marketing large amounts of Kona coffee directly to retailers. Sales of Kona coffee that merely replace one brand of coffee for another do not increase demand; instead they exert downward pressure by providing more sellers for the same commodity. Sales which substitute pure Kona for blend, or introduce new packaging or new markets, add to demand.

The reason local companies have not moved into the market in this way up to this point is the tremendous investment it takes in creating state-of-the-art packaging and promotional materials, and in establishing a distribution network to get the product to a national, or even a statewide market. Although every processing company sells roasted coffee in Kona and there are dozens of small "estate" coffee brands for sale here, no local company has been able to reach either a statewide or national market. The minimum investment for such an effort, including product inventory, is in the neighborhood of $250,000. Besides such an investment, it is necessary to find a good partner to roast, package and distribute the coffee--the plant and equipment necessary to produce this packaging is more than half a million dollars.

When the price of Kona coffee crashed last August, Kona Kai Farms made what we thought was a serious effort to increase our marketing of pure Kona coffee in Kona--we took out newspaper advertisements, made sales calls on all the hotels and restaurants, and sent out printed material. It was ineffective, because we didn't have the packaging and depth of sales support that these customers needed. We were so discouraged about our results in Kona that we didn't even bother going to Honolulu. However, in the following year we have learned from this experience.

Kona Kai Farms now has the product line, the packaging, and the the distribution network necessary to sell large quantities of roasted Kona coffee to a national market. This includes:

* 8 ounce valve packages of both whole bean and ground pure Kona;
* 2 ounce vacuum packages of ground pure Kona;
* 10 pound bulk packages of whole bean pure Kona;

All of the above come in regular, decaf, mac nut flavored, and chocolate mac nut flavored varieties.

* A gift pack of four two ounce packages--one each of all four varieties.

All of the 8 ounce and 2 ounce packaging is attractive, state-of-the-art, pre-printed bags. Each variety is a different color: black, teal, pink, and purple. We will be following this up within a year with additional varieties: Peaberry, Dark Roast, Extra Fancy, and Coconut Flavored "Kona Colada". We have a separate brand name to sell our "Prime" Kona coffee at a reduced price. We have a national distributor who has already placed the product in stores such as Macy's, Bloomingdale's, Disney World and Williams Sonoma on the mainland. Our Honolulu distributor has gotten accounts such as Hilo Hattie's and Liberty House. Our own sales division has placed the 8 ounce product in all of the supermarkets on the Big Island, and is having success in the smaller gift stores. We now have four retail outlets in Kona, and should have a store in operation in Waikiki by next spring.

From the results of our marketing up to this point, we are projecting that our roasted coffee will use up an additional 1,500 bags of green coffee *this harvest year*. This makes our roasted division our biggest single customer for green coffee in its first year of serious operation--well on the way to reaching our goal of 50% sales roasted and 50% green. This additional use is enough to raise the farm price of Kona coffee, and is why Kona Kai Farms is now paying at least five cents above the price paid by any other commercial Kona processor. We are confident enough in the success of our program to predict that it will raise the demand and price of Kona coffee, no matter what happens with Brewer's inventories, the "Kona Blend" legislation, or the success or failure of other marketing ventures.

In concentrating on the packaged roasted coffee business, we have not neglected green coffee sales, which will continue to be a large portion of our revenues for the forseeable future. At the current value of the dollar, new overseas sales are increasing, especially in Western Europe and Asia. Last month we had a booth at the ANUGA food show in Cologne, Germany and were very pleased with our sales and contacts. Next spring we will have a similar booth in Tokyo at the 1992 Great American Food Show. We now have green sales in Australia, Spain, France, Hong Kong, Italy and England as well as continuing sales in Japan. We have sent representatives to franchise holders meetings of Gloria Jean's and Coffee Beanery, two of our large retail chain customers with promotional gifts of Hawaiian flowers. And, this year's Cupping Competition, which Kona Kai Farms produces and funds, will feature five distinguished international judges and over $3,200 in prizes.

The cost of this effort has been considerable. We stretched our resources to the breaking point, and had to delay payments for coffee delivered last February and March until September and October. We apologize to our farmers and suppliers for the hardship or inconvenience caused by paying our bills late. We believe that we are now in a position to take the industry back to a position of strength which will provide stability many years into the future. We cannot predict at this point that the industry will be able to expand in the face of production on other islands (see *infra*), but we think that demand will be enough to maintain our current acreage and production.

RECENT HISTORY

Note: The following discussion relies heavily on several articles previously published by Kona Kai Farms and others:

The Re-Emergence of the Kona Coffee Industry (William Dyke, 1984, 1989)
Kona Blend Position Paper (Robert Regli and Michael Norton, 1990)
An Overview of Proposed "Kona Blend" Coffee Regulation (Roger Coggburn, 1990)
Kona Kai Farms Coffee Farmer Newsletter, Number 13 (1990)
The Makings of the Crisis in the Kona Coffee Industry (1990)
The Markets and Marketing Issues of the Kona Coffee Industry (Stuart Nakamoto and John Halloran, University of Hawaii, 1989)

Coffee has been a commercial crop in Kona since the 1830's, and has traditionally experienced periods of boom and bust. In the Post-World War II era, coffee acreage rose from 3,500 in 1946 to over 6,000 in 1959, the year Hawaii became a state. Between 1959 and 1982 Kona coffee acreage went steadily downhill to around 1,800 acres in 1982. At that point, the average farm price for coffee cherry (the red berries picked from the trees) was just under 50 cents per pound. The reason for the decline was the inability of Kona coffee to command premium prices enough to justify the higher land and labor costs associated with statehood. Although the Kona Farmers Co-operative did succeed in forging a marketing agreement with Superior Coffee of Chicago in the '60's establishing a premium for their crop, it was not enough to stem the tide, and farm acreage continued to decline.

The rise of the specialty coffee industry, beginning in the late 1970's, created new demand for Kona coffee from the dozens of specialty roasters which had sprung up all over the United States. Companies such as United Coffee of San Francisco, First Colony Coffee & Tea of Norfolk, Virginia, Fairwinds Coffee in Concord, New Hampshire, and Starbucks Coffee in Seattle dramatically expanded their businesses, reaching all over the United States via UPS, Federal Express, and other rapid delivery services. Retail outlets such as Peet's Coffee & Tea in Berkeley, California and The Coffee Connection in Boston began to roast their own beans. Supermarkets saw a gradual increase of whole bean coffee in their coffee sections, and equipment dealers experienced a huge increase in the demand for home grinders, electric coffee brewers, and espresso machines.

Between 1982 and 1989, Kona coffee experienced this rising demand, flat supply growth (little increase in acreage), and as a consequence, consistent increases in farm prices. At the beginning of the 1989-90 season, the cherry price had steadlily risen to 85 cents per pound, and acreage had expanded to about 2,200 acres in Kona. In 1982, United Coffee opened a processing outlet in Kona and began buying coffee cherry directly from farmers. They were soon followed by locally-based processors such as Kona Kai Farms, Bong Brothers, Rooster Farms, and Captain Cook Coffee Company. As 1989 began, there were at least a dozen companies or individuals buying and processing Kona coffee in Kona. The market share of Kona Farmers Co-op/Pacific Coffee Co-op, 100% in 1980, was under 25% in 1989. Superior Coffee, nervous about their supply, negotiated agreements with Kona Kai Farms and Bay View Farms for additional coffee. The large Japanese coffee company, UCC, was a growing market force. They also started to purchase from other processors. The outlook was described as very optimistic by all concerned.

1989-90 CROP SEASON

The 1989-90 season was a landmark for the Kona coffee industry. A series of events pushed the farm price for cherry to $1.00 per pound. Roasters worried about supplies purchased over 20,000 bags of Kona coffee at prices averaging more than $6 per pound for green beans (Kona bags weigh 100 pounds each). Foremost among them was Superior Coffee, which bought more than 10,000 bags. A new Honolulu roasting company, Hawaiian Isles (whose parent company is one of the top 100 corporations in the state according to *Hawaii Business* magazine), bought several thousand bags directly from Kona farmers. Coffee farmers never had it so good.

After the season, Hawaiian Isles' purchasing arm, "Sunrise Farms," suddenly pulled up stakes and left Kona, with no public explanation. Of even more significance, Superior Coffee (acquired earlier as a division of Sara Lee) put its Hawaii operations up for sale. The three interested potential buyers were General Foods, UCC, and C. Brewer, a 164-year old Hawaii "Big Five" company which dominated macadamia nut production and marketing under their "Mauna Loa" brand. On May 24, 1990 it was announce that Brewer was the winning bidder, paying over $20 million for the Hawaii business, including the rights to the "Royal Kona" brand name.

In the stores, the results of the high prices started to make themselves felt. At the new price levels, retail prices for packaged roasted coffee rose to $15 to $20 per pound (up from $12 to $15 at the previous year's prices). Sales of pure Kona coffee slowed considerably.

Back at C. Brewer & Company, Alan Kugle, the executive in charge of the Superior Coffee acquisition, suddenly realized that the more than 7,000 bags of Kona inventory included in the purchase would constitute over a two year supply the way sales were going. At book value of around $6.25 per pound, that coffee was worth around $4.5 million of the purchase price of Superior, but the actual market value of that coffee in the summer of 1990 was closer to $2.5 million. Carrying charges alone on the book value of the coffee would be over $50,000 a month, and Brewer was about to go through a belt tightening freeze on executive bonuses.

Why Brewer did not more fully investigate the industry they were buying into is a question for serious consideration. Although Superior had a large contract from Kona Kai Farms, as well as other agreements with Kona Farmers Co-op, Pacific Coffee Co-op and Bay View Farms, they never made any inquiries of Kona Kai during their "due diligence" negotiations. If they had, they would have found out that Kona Kai owners Robert Regli and Michael Norton, had pleaded with Superior not to support the $6 per pound price of green coffee in 1989.

In March, 1990, Kona Kai's Farmer Newsletter stated that "prices over $6 per pound are impossible to support for a large volume of coffee. At this point, we cannot market two million pounds of coffee at those prices." By that time it was also apparent that Hawaiian Isles had several years' supply of Kona coffee and would not be coming back into the market soon or with strength. News also came that United Coffee had filed bankruptcy papers in San Francisco, ending their purchases of Kona coffee indefinitely (they owed green coffee brokers close to a million dollars). After the season had peaked, farm prices had edged down to 85 cents, which Kona Kai believed "is still an excellent price level for Kona coffee, and one that we will be fortunate to maintain if next season's harvest is significantly greater than the 1989-90 crop."

THE 1990-91 CROP SEASON

In August of 1990, Alan Kugle delivered a certified letter to Kona Kai Farms (and, we assume, to the four processors with which Superior Coffee had purchasing agreements), exercising the "economic hardship" clause in the contract, and stating that Brewer could not at this time commit to buying any coffee during the 1990-91 season. Privately, Kugle told processors that they expected to purchase some coffee, but at this point they had to be conservative until their marketing strategies started showing some success. Overnight, the farm price of cherry dropped to 60 cents per pound and stayed there throughout the season.

The "crisis" brought about by Brewer's actions caused a great deal of turmoil in Kona. Meetings were held with farmers, government officials, processors, and roasters discussing the situation. The Department of Agriculture sponsored an emergency mailing, urging Hawaii residents to buy Kona coffee and Hawaii macadamia nuts for Christmas presents (the nuts were experiencing even bigger problems than Kona coffee). A new "Kona Blend" bill was introduced in the state legislature, which eventually was signed in 1991 and required Hawaii roasters to put the percentage of Kona coffee in their blends on the label of the package, and that it be a minimum of 10%. Kona Farmers Co-op effectively merged with Pacific Farmers Co-op.

Both Brewer and UCC ended up purchasing coffee from KFC/PCC, and Brewer purchased a good deal of coffee from Bay View Farms. They criticized Kona Kai as "uncooperative" for complaining about the cancellation of their contract and purchased no coffee from Kona Kai Farms. They accused Kona Kai's "panic" publication of the status of the industry in their public statements as depressing the price of green coffee for potential foreign sales.

Processors and farmers scrambled for cover. Kona Kai Farms stopped taking customers for their farm management program, and discontinued their fertilizer incentive program for farmers. Payments for coffee delivered in February were delayed until September, and the price for cherry fell to 50 cents per pound by the beginning of the 1991-92 season with 90 day terms. Prices from other processors were 40 to 45 cents per pound, less than half of what they had been only 18 months before. Farmers quit fertilizing, stopped replanting, and expansion of farm acreage screeched to a halt. In Kona today, coffee farmers are shaking their heads and hoping the situation will improve, but they lack any concrete reasons for optimism. Old timers believe that "what goes up must come down" and vice versa, but it is little encouragement to new farmers with mortgage payments to make and coffee pickers that must be paid.

THE KONA COFFEE COUNCIL

Much of Reed Flickinger's editorial was directed against the lack of an effective industry voice:

> The Kona Coffee Council is splintered, ineffective, and practically mute. . . . The personalities and their conflicts have overwhelmed an obvious but obviously overlooked common bond, the need to ensure the integrity and prosperity of the Kona coffee industry. . . . without a voice, who will speak for Kona coffee? Certainly the major buyers and processors have not. And we have heard not a peep from the farmers, some of whom must regard this as simply another lean time that should pass.

The Kona Coffee Council is composed of six processor representatives and six farmer representatives. Divisive conflicts have led to the resignations of several processors, and others were dropped for lack of interest. Today, only about half of the processors are represented on the Board of Directors (Kona Kai Farms, Captain Cook Coffee, Rooster Farms, and Sugai Products are the largest). Representatives from KFC/PCC regularly attend meetings. Of the major processors, only Bong Brothers and Bay View Farms do not attend at all.

Kona Kai Farms has been a continuous member of the Council since it was started in 1984, and for what they are worth, we offer our observations on the subject. The Council was re-organized by Tom Kerr, a retired San Francisco law professor who had moved to Kona and developed an interest in coffee farming. He was the one uniting force in the industry who everyone respected--astute, yet conservative enough to belong to the Co-op and be comfortable with the "good old boys." Although the Council did not boast of any great accomplishments during his presidency (our one major piece of legislation, the 1986 "Kona Blend" law, was vetoed by Governor Ariyoshi--see generally the article in the June 1986 issue of *Tea & Coffee Trade Journal*). When Tom became too ill to continue as President of the Council, the cohesive bond was lost, and no one was able to command unified support for their point of view.

During the period after Tom Kerr left, the major issues dividing the Council put the customers of Superior Coffee (the co-ops) on one side, and everyone else on the other. In retrospect, it was unrealistic to expect the co-ops to "bite the hand that feeds them." As the dominance of Superior became less and more small processors and estate farmers began to speak out, there were so many opinions on every issue that consensus was very difficult. From our standpoint, Kona Kai Farms felt that its opinion on issues such as what was the correct percentage of blend for the new law, was more relevant than a farmer who sold 100 bags of cherry per year and had no marketing experience.

Since August of 1990, the major issue facing the Council has been the blend legislation which was eventually passed by the legislature and goes into effect on January 1, 1992. A similar issue is now before the FDA which could affect the other 49 states. Perhaps a review of what happened with these issues illustrates some of the problems of building a consensus around a specific program.

In the Winter of 1990, two legislators introduced similar "Kona Blend" bills. It is a measure of the lack of communication with the industry that the bills were introduced on their own, without any direct consultation with the Kona Coffee Council, which had no paid staff or even a telephone. Kona Representative Virginia Isbell and Hawaii Kai (Oahu) Senator Donna Ikeda both introduced "truth in labeling" type legislation which would have required marketers in Hawaii to put the percentage of Kona coffee in their blends on the front label of their package. When the Coffee Council found out about the bills, most members felt that in addition to the labeling (which received unanimous support), there should be a certain minimum that any "Kona Blend" should contain.

The exact nature of this minimum blend caused fierce debate. Kona Kai Farms felt that the institutional market would never go for 51% and wanted a 20% blend for the hotels and restaurants. Most of the farmers were adamant that any Kona blend contain at least 51%. Kona Kai produced a seven page "Position Paper" and one of the farmer members of the Board of Directors compiled a 60-page booklet detailing the pros and cons of the various positions. One member of the Board justified the 51% as an initial bargaining position that could be negotiated later on.

The roasters were for the status quo. Lion Coffee would put more Kona in their blends (they stated they currently used 10%), but didn't want to have to put additional labeling information on their package. Brewer didn't want any minimum or any labels, and stated in public for the first time that "some of their blends" were indeed below 10%. They didn't want to compete for mainland sales against mainland roasters who didn't have to follow Hawaii rules.

Just before a crucial hearing in the legislature, the Department of Agriculture called a meeting of Lion, Brewer, and two members of the Kona Coffee Council (not Kona Kai Farms). The meeting reached a "consensus" that the new law be amended to require 10% but to delete any labeling requirement. The Council members later stated they hadn't wanted the 10% but had been forced to agree by the Department of Agriculture and the roasters saying that nothing else was possible.

Kona Kai Farms was really upset that the truth in labeling requirement had been deleted from the bill. We went on a letter writing blitz, and went to the next meeting of the Senate Agriculture Committee chaired by Donna Ikeda to testify. Probably for her own reasons, Senator Ikeda put the labeling requirement back into the bill, and from there it went smoothly through the House and was signed by Governor Waihee. In Kona, no one is happy with the 10%--everyone agrees that it is too low a percentage. Kona Kai Farms said that it proves that 51% was unrealistic and a bad negotiating position. Other Council members felt Kona Kai Farms' stance against the 51% had destroyed the chances for it to become law.

We believe that the Council should have united around a consensus figure which would have raised the actual use of Kona coffee, rather than have had a divisive position for the 51% (as we remember, the vote was something like 6-4). We felt the 51% was an emotional desire without any basis in the marketplace. Interestingly enough, this logic appears to have been accepted around similar FDA legislation, where the Council finally appears to have voted to drop the 51% rule and urge merely a truth in labeling requirement.

Another perennial problem facing the Coffee Council is that they have no legal right to tap into coffee industry for funding--unlike commodity groups with federal marketing orders such as the Papaya Administrative Committee. As a consequence, the organization depends on the goodwill of its processor and large farmer members for funding which is then spent on projects which will supposedly benefit the industry as a whole. Processors who contribute are understandably upset that their competitors who contribute nothing stand to benefit from these promotional ventures. For example, Kona Kai Farms, which markets more than 1/3 of the crop, has only one vote out of 12 on the Council Board of Directors, yet is asked to contribute nearly half of the funds raised by processors.

It is reasonable to believe that the Coffee Council will continue to be divided over the specifics of various ways to strengthen the industry, while at the same time being united on many important concepts, such as promoting the pure Kona product against the "Kona Blends". Without a marketing order or a figure like Tom Kerr to provide leadership, the industry voice will not be as strong as it could be. However, it is illusory to think that anything the Council does would have a dramatic effect in the marketplace. The marketing and promotion of Kona coffee is much more in the hands of the private companies which sell it as a brand name product. Nothing the industry does can force them to promote Kona coffee if it is otherwise not in their interest to do so. And, there is no guarantee that even a united group of growers and processors can force dramatic changes which are vigorously opposed by the principle marketers.

WHERE THE SITUATION STANDS TODAY

By most estimates, Brewer's inventory of green Kona coffee is no less today than it was in August of 1990. Purchases from Kona Farmers Co-op, PCC and Bay View Farms have probably exceeded sales since that date, especially since the Gulf War and the recession have dramatically reduced sales of all Hawaii-based companies over the last ten months. Brewer is offering green coffee for sale, both directly and through brokers (including one public relations company, Active Media Services of New York), at under $4.00 per pound. Alan Kugle and Mauna Loa Mac Nuts are being sued for price fixing by two former MacFarms employees, and he is no longer in charge of coffee for C. Brewer (a former executive of competitor Hawaiian Isles was hired to run Superior Coffee). Less than a month ago, Kona Farmers Co-op was full of approximately 5,000 bags (500,000 pounds) of Brewer's inventory.

High priced inventories of most other roasters have finally been sold off, and they are starting to purchase new crop coffee at this year's prices. Most processors have reduced their green prices to match Brewer's, and are accordingly paying farmers between 40 to 50 cents per pound for cherry that costs 25 to 35 cents per pound to pick. Farmers agree that around 70 cents per pound for cherry is a price that justifies the effort of farming.

Hawaii roasters are still selling low percentage "Kona Blend," as the new 10% law doesn't go into effect until January 1. The FDA is reviewing a petition by the Kona Coffee Council to require "truth in labeling" for all Kona coffee sold in the other 49 states.

UCC coffee has not stepped in to take over the void left by Superior, as their purchases of Kona coffee have not increased significantly. With no other potential "white knight" on the horizon, and competition looming from other islands, the Kona coffee industry is struggling just to tread water.

WHERE DO WE GO FROM HERE?

Today the Kona coffee industry faces problems not unlike it faced in 1959, also a year of big declines in farm prices. We have listed many of the problems facing the industry, and stated our belief that Kona Kai Farms' roasted coffee program by itself will raise demand significantly. What other factors do we have going for us that might be used to pull Kona coffee out of the doldrums?

(1) Increased marketing visibility on all levels. High inventories lead to promotional activities as everyone struggles to turn inventory into cash. Kona Kai Farms is not the only company with new products and marketing strategies. For example, Brewer has introduced a pure Kona "portion pack" for the institutuional market in Hawaii. Lower prices make Kona coffee more affordable, especially in the Hawaii tourist market. As the price rises, some of these customers will drop out, but some will hang on to be good customers at prices which can support coffee farming.

(2) Consumer awareness of the "pure" versus "blend" Kona coffee products. All the publicity around the new law has heightened awareness of the difference between pure and blended Kona coffee. Given an informed choice, a much higher percentage of visitor customers in Hawaii will choose pure over the blend. We are seeing this now in our retail stores.

(3) Increased use of institutional customers because of the 10% rule. We estimate that the increase in Brewer's blend to 10% will use up an extra 2,000 bags of Kona coffee per year if total consumption remains the same.

(4) Low value of the dollar makes foreign sales easier. With the yen around 130 to the dollar, Kona coffee is not nearly as expensive for Japanese roasters. Right now, Japan is the hottest market for foreign sales, with Europe not far behind.

(5) Increased marketing in Kona and the Island of Hawaii. There are dozens of small coffee marketers now in Kona, mostly farmers selling their own coffee in roasted form. Estate coffee and organic coffee are two new niches which provide increased sales for Kona coffee.

(6) Continued rise of market share of specialty coffee industry. The specialty industry, with cheap coffee resulting from the lack of ICO quotas, continues to take sales away from American mass consumption coffee products. Industry experts estimate that it will hit 20% of all coffee sales in the '90's.

(7) Lack of significant increase in farm harvests. Because of the low farm prices, farm production will not increase significantly over the next few years unless the weather is exceptional. Farmers thinking of abandoning coffee have no other viable alternatives at this point, and the supply of agricultural workers is increasing as large hotels lay off workers and Mexican nationals migrate to Kona to harvest coffee.

COFFEE ON OTHER ISLANDS

The one other significant negative factor facing the Kona coffee industry is the increased competition soon to be felt from coffee grown on other islands. Under normal circumstances, growing thousands of acres of coffee in Hawaii, picked by mechanical harvesters, competing with already dismally low-priced coffee grown in third world countries, seems like abject folly. However, these are not normal times for the Hawaiian sugar industry. Every sugar company is desperate for a crop to replace their doomed sugar cane acreage, which is comparable to a hospital patient with tubes sticking out of every vein. One day, the U.S. Congress will pull out the "tube" of price supports from the domestic sugar industry, and Hawaiian sugar will be gone overnight. Until then, a combination of the federal subsidy, low interest state loans, and the sale of agricultural lands for residential and tourist development, along with efficient production and side businesses like cattle feed lots and electrical generation keeps the industry alive. But the sugar companies know the end is coming, and they have several contingency plans to replace sugar with other crops. Incredibly, coffee is one of the most promising--not because of its own success, but because all the others have failed worse.

The first company out of the block in the race to grow coffee on other islands wasn't a sugar company at all, but a private venture on Molokai called "Coffees of Hawaii." Despite an impressive prospectus, the venture ran short of funds, and was easily passed by the McBryde Sugar Company, a wholly owned subsidiary of Alexander & Baldwin, another "Big Five" company which besides its agriculture and development holdings, owns Matson Shipping Company. McBryde's plantation on Kauai is 13,000 acres, and they have slated about half of that for coffee production. They are now harvesting 600 acres and are said to have another

4,000 acres planted. Under a joint venture marketing arrangement with Hills Brothers, the coffee will be sold under the "Hawaii Makana" brand name ("Gift from Hawaii'). McBryde's venture is a serious one--they know large scale farming and Hills Brothers (now owned by Nestle) has one of the strongest coffee marketing organizations in the world. Although the coffee is not likely to make inroads on the specialty green coffee market, it should do very well as a tourist gift item in Hawaii, priced somewhere between "Kona Blend" and pure Kona coffee.

Coffees of Hawaii is now back, with several million dollars of capital infusion from John Magoon, who recently sold most of his share of Hawaiian Airlines. Magoon recently took over as Chief Operating Officer from the company's original founder, John Hayes. Although Coffees of Hawaii has been able to finally plant 400 acres with Magoon's investment, their future is far more speculative than McBryde's. Amfac's Pioneer Mill in Lahaina, Maui, is currently watching a test planting of one hundred acres of coffee, and there are test plots in several locations on all of the other islands run by the Hawaii Sugar Planters Association. All of these companies have the agricultural expertise necessary to grow coffee, and the land is essentially free. Coffee was grown on all the islands of Hawaii--in 1898 there were 13,000 total acres with only half on the Big Island. There is a huge question of the effectiveness of mechanical pickers in Hawaii, and past that, the question of the marketplace.

The economics of coffee on other islands have not been well thought out. There is, in fact, no market for the coffee at prices comparable to coffee grown in the Third World. In 1986, Superior Coffee signed an agreement with Coffees of Hawaii to purchase all of the coffee grown on Molokai at a price 20 cents above the world price of coffee on the commodities exchange, or $1.50, whichever was higher. At the time, the ICO supported price was around $1.25; today it is 82 cents. Hills Brothers is trying to sell small quantities of green Kauai coffee for around $3.00 per pound with little success. Production costs were also sadly mistaken--predictions used to lure investors and justify capital expenditures have a habit of being far lower than reality. Sugar companies have been dazzeled by the success of Kona coffee and the abject failure of macadamia nuts, cocoa, papayas, or any other alternative. Like a drowning sailor thrashing for a life preserver, the sugar companies are grasping at coffee. Their chances of success are not high, but the consequences of failure reach out past their own interests to Kona. The effect of other Hawaiian coffee in supermarket shelves and gift stores in Hawaii will undoubtedly be to cut in-state sales of Kona coffee at a time the industry needs to increase every market it has.

CONCLUSIONS

It is too early to play taps for the Kona coffee industry, which has shown remarkable resiliance over its long history. Increased marketing efforts on many levels have put the name "Kona coffee" in front of consumers as never before, at a time when farm supplies will not be increasing. Although there are some serious negative factors such as competition from coffee on Kauai and other islands, Brewer's current inventory, and the disappointing 10% "Kona Blend" law--there are many other positive factors which will increase demand. By focusing on the accelerated development of our sales of Kona Kai Farms roasted Kona coffee, we believe we are making the most dramatic possible positive impact on demand and passing that increase directly to farmers. Kona Kai Farms expects that the price of cherry coffee will rise towards the 60 cent mark between now and the end of the 1991-92 coffee season (normally in February), and is fully capable of hitting 70 cents a year from today, depending on the volume and timing of the 1992-93 harvest. Coffee farming in Kona has never been a lucrative occupation, but its viability during the rest of the '90's should not require farmers to suffer the losses they have taken during the last two seasons (they made good money in 1989-90).

Five years ago Kona Kai Farms put out a position paper on "Kona Blend" for a meeting of the Kona Coffee Council on *November 5, 1986.* We think it is instructive to reprint some of it here to show that the problems we are dealing with now were predicted five years ago with telling accuracy:

We believe that the recent growth of the Kona coffee industry has experienced is now threatened unless the distribution and sale of "Kona Blend" coffee, starting with coffee sold in Hawaii, can be sensibly regulated .... We do not need a taste test... we need an economic test to tell us how we can sell increasing supplies of Kona coffee at prices that will support a healthy industry.

Look at the facts: Superior and Kona Farmers Co-op are now trying to sell green Kona coffee to the mainland market. Instead of increasing their roasted coffee business with increasing supplies of Kona coffee, they are adding to supplies which must be consumed by mainland roasters. Sales of roasted Kona coffee in Hawaii are either remaining level or DECREASING. All the processors in Kona are struggling to keep their prices the same as last year, after years of steady increase. And this is only the beginning of what are projected to be steadily increasing levels of supply....

Kona Kai Farms has proposed adopting regulations which allow a 20% "Kona Blend" to be sold to restaurants and other institutional users and a 50% "Kona Blend" for retail sales.... Ours is not the only possible plan for regulating the blends and using up supplies, but we are the only ones proposing anything but the status quo. The industry needs to unite around a plan of action and make that our top political priority. The active and vocal support of the farming community is necessary to force the roasters to either come up with a workable plan or have one imposed by state law.

Kona Kai Farms has consistently been called some version of "troublemaker" for merely stating accurate facts concerning the Kona coffee industry. When we complained that the Kona Coffee Festival was focused on a beauty contest and had nothing to do with coffee, we were ignored by the Coffee Festival Committee, and had to develop the Cupping Competition on our own. Now the Festival wants to take it away for themselves. When we first started complaining about the fact that "Kona Blend" didn't contain much Kona coffee, it was as if we were the hapless jester who noticed that "the Emperor has no clothes." Now everyone in Kona realizes what happens when you sell the sizzle but don't pay for the steak. When we told Brewer last August that their coffee was worth $3.50 a pound, not $6.00, they said we were panicking. Now their two-year old coffee is on the market for about that price. Not all of what we have written or predicted has been proven accurate, but we have always tried to give a true and realistic picture of events as we have seen them. And, we are the only ones in Kona who have consistently put forth our views in public position papers, newsletters, and other public documents which have always been open to scrutiny.

We invite others to comment on this assessment of the industry. We are always eager to hear other points of view. At this point, the industry doesn't have much to lose by "going public" with its problems. The *West Hawaii Today* editorial was a good step in that regard.

Robert Regli and Michael Norton
Kona Kai Farms