

**Southeast Asia
Centre of
Asia-Pacific Excellence**



The Perfect Blend

THAI COFFEE AND KIWI EXPERTISE

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EXECUTIVE SUMMARY

THE PERFECT BLEND THAI COFFEE AND KIWI EXPERTISE

The Perfect Blend is the name for a proposed New Zealand company based in Thailand. It would work to promote Thailand's coffee brand, bringing all company functions in house – marketing, creative services, R&D, distribution and administration and pushing Thai coffee into high value-added markets.

We believe that sustainability drives quality. Our goal is to enable Thai coffee growers to break into previously inaccessible international markets. We care about our coffee's journey from farm to cup, and about achieving excellence through expertise.

This report provides an analysis and evaluation of the current and prospective profitability of up-scaling Thai-grown coffee in the international market. The analysis covers Thailand's geo-political background, its growing speciality coffee industry, macro-trends, marketing strategy, initial costings and revenue.

We have developed four propositions to support relationship building between shareholders. These include:

- Working alongside New Zealand Trade and Enterprise for support and connections in the region.
- Partnering with New Zealand roasters and cafes to distribute Thai coffee beans.
- To gain credibility with shareholders, we would build up relationships by conducting fieldwork visits to regional coffee growers across Thailand, as well as business tours for local coffee growers/ owners.
- Offering an opt-out option at any time for growers/business owners to manage and market their products independently. This would attract more clients to work with us and will allow our organisation to develop trust faster.

INTRODUCTION

THAILAND: THE COUNTRY

Political history and economic overview

Thailand is the second largest economy in Southeast Asia and boasts an upper-middle income status, serving as an economic anchor for developing neighbour countries¹. It is the only country in Southeast Asia that has not been colonised by a foreign power and is ruled by a constitutional monarchy with a parliamentary system.

Despite this, democracy in Thailand is fragile. Until now, political turmoil has persisted, with periods of temporary rule by civilian political parties alternating with military coups. A military-led government seized power through a coup in May 2014. Despite political uncertainty, Thailand's economy has remained resilient and is expected to advance at a moderate pace into the foreseeable future.

Figure 1: Thailand at a Glance

Population	69.04 million
Total Land Area:	513,120 square kilometres
Capital:	Bangkok
Climate:	Tropical, mean annual temperature 28°C, high humidity.
Official Language:	Thai
Nominal GDP (billion USD):	455
GDP at PPP (billion USD):	1,234
GDP per Capita at PPP (USD):	15,682
GDP Growth:	3.9%

Source: International Monetary Fund – World Economic Outlook Database, October 2018

The agriculture sector in Thailand

Traditionally, the Thai economy is heavily based on agriculture. This sector contributes up to 8.2% of GDP and employs nearly 40% of the active population². Thailand is one of the world's leading producers and exporters of rice, but also produces other major crops: rubber, sugar, corn, jute, tobacco and coffee. Overall, agriculture's contribution to GDP is declining, while exports of goods and services have increased.

Thailand 4.0

In 2016, Thailand's military government unveiled its newest economic initiative, Thailand 4.0, a master plan to free Thailand from the middle-income trap, making it a high-income nation within five years³.

The government narrative describes Thailand 1.0 as the agrarian economy, which prevailed decades ago. This gave way to Thailand 2.0, the light industry, textiles, and food processing era. Thailand 3.0 describes the present economic era, with heavy industry and energy making up around 70% of Thailand's current GDP. In contrast, Thailand 4.0 is described as an economy driven by 'high-tech industries and innovation'. More specifically, the move to Thailand 4.0 aims at promoting, reinforcing and developing ten major industries, which will lead to the production of value-added products and services.

The ten significant industries include the First 5 S-Curve Industries where Thailand has existing strengths and capabilities. These are: the next generation automotive industry, intelligent electronics, advanced agriculture and biotechnology, food processing and tourism.

To supplement growth and development in these industries, the Thai government is also incorporating five new S-Curve growth industries that could complement and synergise the country's existing industrial base. These include: advanced robotics for industrial and domestic use, an integrated aviation industry, medical hub and healthcare services, biofuels and biochemicals, and digital technology industries.

Thailand within the global coffee industry

The global coffee industry is worth over \$100 billion, with \$20 billion being generated from exports. The majority of the world's coffee comes from developing countries in South America, Africa and Southeast Asia, or 'The Coffee Belt', which is an area between the Tropic of Cancer and the Tropic of Capricorn. In Southeast Asia, the largest coffee exporter is Vietnam, followed by Indonesia, Laos, and Thailand respectively.

Before 2003, Thailand would consistently rank as the third largest coffee exporter in Southeast Asia and experienced its highest exports in the 1990s. However, due to fluctuations in global prices at the turn of the millennium, Thai coffee producers have turned to other crops, causing coffee production to plummet over the past two decades⁴. Only 7% of Thailand's total coffee production is exported each year⁵.

Porter's 'five forces of the global coffee industry'

1. The threat of new entrants

Barriers to entering the global coffee exporting industry are high due to significant capital required for:

- establishing production
- building infrastructure and farmer relationships
- undertaking research and development in bean processing
- sourcing channels for selling and exporting.

Due to these significant entry requirements, new producers experience small economies of scale. Access to distribution channels is another barrier to entry as many countries have established well-structured relationships with their networks over decades.

At present, however, the threat of new entrants into the market is low, due to favourable

environmental and weather conditions along the global 'coffee belt'. However, with recent developments in food science and technology, this may not always remain the case.

2. The threat of substitutes

The threat of substitutes in the global coffee industry is influenced by the type of coffee product (i.e. instant coffee, whole bean coffee), and the type of bean (Arabica, Robusta, etc).

The main substitute product is tea, which comes from many different countries, with unique flavours and price points. Other substitute products include energy or soft drinks, which can be manufactured in countries that have no natural resources. However, these substitutes do not have the distinct flavour or cultural connection that coffee embodies. Thai coffee would face immense competition from larger-scale coffee producing countries.

3. The bargaining power of suppliers

Large numbers of international coffee suppliers already sell beans either to local companies or to offshore companies for processing into refined products. The global coffee industry is very mature, with trade and non-trade relationships between countries and companies lasting many years. These relationships are precious as they not only determine coffee prices and how competitive these are but also the quality of the coffee supplied.

However, it is likely that suppliers experience difficulty in differentiating their coffee beans from others on the market. Suppliers also experience difficulty in competing for good prices against other countries with better economies of scale. Hence, suppliers' bargaining power is moderate.

4. The bargaining power of buyers

Buyer bargaining power in the global coffee industry is moderately high as buyers tend to purchase large volumes. At a macro level, suppliers are relatively standard and easy to source. As buyer requirements become more niche, fewer suppliers tend to exist.

There are also few costs involved in switching coffee suppliers due to the high number in the market, though this may pose a risk to buyers, especially if they rely on a certain standard and grade of coffee. Information in the coffee industry is reasonably transparent, however, and buyers do have access to data on market prices and dynamics.

5. Industry rivalry

A high level of industry rivalry exists amongst competing sellers in the global coffee market. There are many competitors from different countries, each operating at vastly different scales while also aiming for market leadership. Due to this, a variety of competitive strategies can disrupt marketplace balance.

However, there are still countries with substantial economies of scale that push smaller countries out of the market due to their ability to export greater quantities at competitive prices. Some countries also maintain a level of brand reputation in the global market and consider their relationships to be of superior value. Saturation and maturity make the coffee market one of slow growth and high competition as companies can only grow by capturing market share from other competitors. The commodity nature of coffee also contributes to the competitive nature of the global industry.

Coffee production in Thailand

Thailand is Asia's fourth-largest coffee producer and produces two main types of coffee: Arabica in the north and Robusta in the south. While Arabica beans dominate the world market, in Thailand, Robusta beans are the major crop (99% of production). Arabica cultivation represents only 1% of production. Arabica coffee is the world's most popular coffee and is considered to be a profitable variety for all categories of farmers.

Robusta coffee is grown primarily in the southern provinces of Chumphon, Surat Thani, Nakhon Si Thammarat, Krabi, Phan Nga and Ranong. Robusta coffee is easier to cultivate, has greater crop yield and is less susceptible to disease. These characteristics make Robusta

beans cheaper to grow, and therefore a less expensive coffee variety. Robusta beans also produce a stronger, full-bodied coffee with a distinctive, earthy flavour. The variety boasts double the caffeine and antioxidants than Arabica, and is also significantly more bitter. However, when carefully processed and washed, Robusta can be both superior in quality and have a milder flavour than some lower quality Arabicas.

Thailand's speciality coffee scene and its farmers

The potential for Thai coffee is well recognised locally. This has resulted in a booming 'specialty coffee' scene in Thailand, where many farmers have adopted a 'farm-to-cup' philosophy, growing and roasting their beans and serving their coffee on a single estate.

In recent years, there have been continued efforts within the Thai coffee community, particularly by farmers, exporters and coffee shops, to promote Thailand within the specialty coffee landscape. For instance, many coffee roasters within Thailand have also shifted to roasting Thai-cultivated coffee exclusively in a bid to support the local industry. A change in international attitudes towards Robusta has incentivised Thai farmers to further invest in their production methods and help roasters achieve desirable taste profiles for their coffee blends.

A key example is the Indoi farm within the Doi Saket region in Chiang Mai, a coffee-growing province. The farm owners have successfully experimented with different processing methods, such as using black and yellow honey to create more sweetness and complex flavours, as well as washing beans thoroughly to enhance their flavour.

In addition, coffee farmers in regions such as Pangkhon have added interesting characteristics to their beans by developing their interpretation of Kenyan processing⁶. In particular, the farmers have extended the fermentation process after picking, as this creates more exciting flavours. Signs suggest that the industry will increasingly seek more scientific and innovative methods of fermentation.

Thai coffee production: the business problem

There is little brand awareness of Thai coffee in the global coffee industry or among neighbouring countries such as Vietnam, Laos and Indonesia. It is easy to hold its late market entry accountable. However, the main reason lies in its inability to perform well in the high value-added segments of the production chain, otherwise known as 'The Smiling Curve'.

High value-added segments include: conceptual research and design, branding, distribution, marketing and sales. Not engaging in high value-added activities can be traced to Thai coffee growers operating mostly on a small scale, thus not having the capacity, resources or skills to market or innovate their products effectively. Furthermore, the 'farm-to-cup' operations of many growers increase the challenge of communicating with other growers and gaining access to larger overseas markets.

There is a clear need for collaboration between Thai coffee growers and value-adding stakeholders (e.g. food technologists, market specialists) to share information and collaborate in building the image of Thailand's high-quality specialist coffee in the international market. This report proposes empowering coffee growers to achieve more international recognition for their product and encouraging co-operation between small-scale coffee farmers.

THE PERFECT BLEND: A BUSINESS PROPOSAL

The business model suggested is a New Zealand company (The Perfect Blend) based in Thailand working to bring all company functions in house – marketing, creative services, R&D, distribution and administration – in order to push Thai coffee into high value-added markets that have not previously been accessible.

Our idea is based on the success of the New Zealand Merino Company Limited. Through

marketing and differentiation, that organisation lifted New Zealand Merino out of the 'commodity basket' and raised the perceived market value of merino wool for farmers across the country. Coffee producers, like merino producers, face many challenges:

- Much of the value derived from coffee is added further down the supply chain, but does not flow back to growers.
- Farmers' marketing practices are often ineffective and poorly targeted.

THE PERFECT BLEND: A BUSINESS PLAN

A key role for The Perfect Blend would be to define a unique identity for Thai coffee as being different from other brands while commanding a premium but reasonable price compared with competitors.

The company would brand Thai coffee beans in a way that encapsulates the history and culture around Thai coffee beans, especially differentiating the flavourful and high-quality Robusta beans. Factors around improving Robusta coffee quality would include:

- selective picking
- careful and extensive washing and drying
- meticulous sorting and grading.

Applying these factors would make Thailand's speciality Robusta some of the cleanest, meldest coffee in the world. It would have none of the rubbery after-taste usually associated with Robusta beans. Consequently, it would fetch a good price in coffee markets.

The Perfect Blend would encourage best practice among Thai coffee growers, such as:

Proper planting: speciality beans owe their distinctive characteristics to being grown in suitable climates and varying soil types with little to no defects. Thailand grows coffee at high elevation (up to 1400 meters), and in the shade, which emphasises bean quality over plant yield.

Proper roasting: Becoming an expert roaster with an ability to 'read the beans' takes years of practice. The difference between perfectly roasted coffee beans and a ruined batch can be a matter of seconds. The Perfect Blend would provide incentives for roasters to bring out aromas and flavours locked inside green coffee beans.

Proper harvesting: Coffee beans grow inside coffee 'cherries', which resemble the red fruit. It is important for farmers to pick the cherries at just the right time when they are full and meaty. From there, to preserve flavour and quality they must be transported and milled in a timely fashion.

Environmental integrity: Any Thai coffee brands carrying The Perfect Blend Badge must be compliant with New Zealand's Resource Management, Biosecurity, and Conservation Acts. There would be fieldwork done with potential partners, such as Food Innopolis; during grower audits, growers would be asked questions regarding the sustainability of their practices.

Social responsibility: All farmers would need to comply with New Zealand's Occupational Safety and Health and Employment Relations Act. Compliance with these standards would be audited during farm inspections.

Traceability: Thai coffee beans must be traceable from the grower, through the supply chain, to the buyer, and back. This two-way traceability is unique in New Zealand agriculture and would result in long-term relationships, direct lines of communication, and a shared sense of pride between growers, brand partners, and their end markets.

As part of establishing traceability, The Perfect Blend would also accentuate the 'birthplace' of the coffee beans through its well-established key partners. This approach would appeal to a target market of sophisticated and conscious consumers.

To pursue a brand with these characteristics, The Perfect Blend would start with fieldwork visits to Northern Thailand and assess prospective client's products. Our team would establish relationships with growers and existing

brands by pitching to them the broader opportunities available on the international market. Moreover, we would use market research from New Zealand, Australia, the USA and other western countries to show farmers how to add value to their business.

Currently, without co-operation between farmers, it is not economical for overseas buyers to invest in Thai coffee. Instead, they purchase from more established markets. If **The Perfect Blend** could act on behalf of farmers, it could offer high-quality beans in larger quantities than previously available, thus allowing Thailand to compete internationally. If **The Perfect Blend** raises Thai coffee's perceived value internationally, it could fetch a higher price.

By acting as an intermediary, **The Perfect Blend** would also encourage communication between farmers who can learn from each others' practices. Essentially Kiwi expertise would bring Thai coffee farmers together into a collective brand. If they can co-ordinate their efforts to market their coffee as a premium product and offer a greater volume to the international market their operations will grow. **The Perfect Blend** business would oversee this process, helping connect farmers, build networks and market their product.

The Perfect Blend business plan would allow Thai coffee farmers to achieve higher prices for their coffee, to continue operating their businesses and grow, and to take up opportunities to develop their operations by increasing their access to technology and resources.

Market entry: Establishing and marketing the Thai coffee brand

The first step towards increasing the perceived value of Thai coffee would be to establish its identity. As previously discussed, Thai coffee is both rich in flavour and has a fantastic provenance story. However, internationally it is undervalued and exported in low volumes.

The Perfect Blend would work to establish its reputation, representing Thai coffee beans pro-

duced by a collective of small-scale farmers. A key part of this process would be the way of marketing Thai coffee beans on behalf of the farmers.

Thai coffee is well suited to entering the market via boutique coffee stores or via online specialist coffee suppliers, where it can generate higher margins. A well-targeted marketing campaign would also consider the use of accreditations such as 'Organic' and 'Fair Trade', which could resonate with consumers.

Currently, marketing practices are expensive and not feasible for small-scale farmers. However, bringing together many small-scale growers could allow them to advertise to a greater consumer base and spread the costs among themselves.

A suitable marketing scheme would focus on telling the story behind the beans. Thank you is a social enterprise using tracking ID on their personal care products, which consumers can scan in order to see where funds from their purchases are going and what work they support⁷. We propose a similar idea for Thai coffee beans. QR codes on the packaging would let consumers learn about the origin of the beans and what makes them unique.

Branding challenges

A challenge lies in building trusting relationships with Thai coffee growers. **The Perfect Blend** would minimise the time involved in developing trusting relationships by:

- working alongside New Zealand Trade and Enterprise whose support would facilitate establishing a network in the region.
- partnering with New Zealand roasters and cafes to distribute Thai coffee beans, explaining the value and provenance behind Thai coffee processes and how it is suited to boutique coffee shops and roasters in New Zealand.
- building relationships by undertaking field-work visits to regional coffee growers across Thailand, as well as arranging business tours for Thai coffee growers/business owners.

Key partners

Our partners would help to support Thai farmers on the ground. These partners include government agencies and stakeholders, distribution partners, marketing partners and boutique coffee shops.

Firstly, to gain credibility; The Perfect Blend would seek the support of New Zealand Trade and Enterprise. It could provide links with importers, exporters and government authorities to help us navigate the Thai commercial and regulatory environment.

To maximise our 'farm-to-cup' identity, we could partner with Sal Forest, a sustainable business accelerator, to run events and social impact assessments across Thailand to raise awareness of our business.

Thailand is also home to an increasing number of speciality coffee shops. Bangkok has many boutique cafés, which we believe would be interested in purchasing our high-quality Robusta beans. We have identified several we could partner with – Kaizen Coffee Co., Gallery Drip Coffee, Simple Coffee Simple Life, among others – as well as shops in New Zealand and other countries.

We would also engage world-class Kiwi expertise in animation and film to creatively convey the story of Thai coffee's provenance, its farm-to-cup journey and how its cultivation and roasting processes distinguish its taste and quality. The Perfect Blend would work alongside suitable marketing partners to effectively convey this story. A social media presence on Facebook and Instagram will also be necessary.

COSTING

Initial costs

The initial costs of setting up the operation will be high. It will take time and money to establish networks and build relationships with farmers until they are willing to pay The Perfect Blend for its expertise. Early stage set up and operation costs will be for staffing and transport to visit local farmers. In the long term, The Perfect Blend can recoup these costs and generate a profit.

Generating revenue

Our business model would be based on charging farmers roughly 8% of their gross income to represent and market their product, similar to the business model of New Zealand Merino. Once we demonstrate the value that partnering with The Perfect Blend creates, the benefits of our approach will spread through word-of-mouth.

In 2017 the average price of a kilogram of Arabica beans was USD 2.23. An 8% commission cut of this will generate NZD 15.84 on each 60kg bag sold through The Perfect Blend. This would allow us to operate and cover the costs of the operation. As we support Thai coffee farmers and their exports grow, so should our revenue.

Trust and long-term agreements: the risk

It takes time to build up trust in business in Thailand. Therefore we understand that farmers may not want to enter long-term agreements with The Perfect Blend, an unknown partnership. To counter this risk, farmers could opt out of the partnership at any time if they decide they would rather manage and market their coffee independently. This would reduce the risk for farmers and would be a way to develop trust faster.

CONCLUSION

This report highlights the potential for The Perfect Blend to enable Thai coffee growers to increase their presence in the international coffee market.

By drawing on expertise and support from key stakeholders, and facilitating knowledge sharing and innovation between coffee farmers, the Perfect Blend can increase brand awareness, quality and sales of Thai coffee in the global market.

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⁶ The Way to Coffee. (2018). Thailand's progress in producing specialty coffee. Retrieved from <https://www.thewaytocoffee.com/specialtycoffeeblog/specialty-coffee-in-thailand?fbclid=IwAR3P5CBhfKDq2oEJ8HSWj6YlPdUnHDGeBljWeLDxegz2lFrxB-scDgr2WCE>

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SOUTHEAST ASIA CENTRE OF ASIA-PACIFIC EXCELLENCE

The Southeast Asia Centre of Asia-Pacific Excellence (SEA CAPE) was established by the New Zealand government to enhance our engagement with the ten ASEAN member countries and Timor-Leste.

SEA CAPE is hosted by Victoria University of Wellington as part of a consortium of New Zealand universities that also includes the University of Auckland, the University of Waikato, and the University of Otago.

We work together with exporters, young New Zealanders, government agencies and others to improve understanding of these countries and build knowledge of their economies, languages, cultures and business protocols.

Through our Market Readiness and Market Insights Programmes, and mobility initiatives such as the Tertiary Market Immersion Programme and BizVenture, we show New Zealanders why and how to deepen our understanding of these valuable economies.

What we do

The Southeast Asia CAPE has four key objectives:

- To equip New Zealanders to engage and do business with the ASEAN countries and Timor Leste.
- To broaden and deepen New Zealanders' understanding of South-east Asian cultures, societies, languages, politics and economies.
- To excel nationally and internationally in the dissemination of knowledge and skills relating to Southeast Asia.
- To enhance New Zealand's economic, trade, political and cultural relationships within the region.

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 [linkedin.com/company/seacape](https://www.linkedin.com/company/seacape)

 seacape@vuw.ac.nz

 seacape.org.nz



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