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A Climate Policy Blind Spot

The EUDR's Effect on
Ethiopia's Coffee Sector



© Pete Lewis, Department for International Development

Introduction

This May, the European Parliament [will decide](#) whether to simplify the EU Deforestation Regulation (EUDR). This decision follows a postponement last November of the implementation of the law. The postponement was welcomed in Ethiopia, as the sector was [unprepared to comply](#) with the legislation, originally announced in 2022. Without changes to make compliance to the EUDR easier, Ethiopia's coffee sector and its economy as a whole could be negatively impacted, as could

broader EU trade relations with Ethiopia. This would disrupt local livelihoods - [25% of the population](#) derives a significant portion of its income from the coffee sector - and economic stability, which means the EUDR also risks increasing political unrest. To mitigate the risks outlined above, the European Parliament must make compliance feasible for smallholder farmers and the supply chain at large, and foster collaboration with nonprofits and Ethiopian agencies that are modernizing the coffee sector.

Coffee: backbone of the Ethiopian economy

The impact of the EUDR on Ethiopia is potentially significant given the enormous role the coffee sector plays in the economy. Coffee was the largest export product in 2024 and is farmed by approximately [four million smallholder farmers](#). The supply chain for coffee is scattered across cooperatives, processors and exporters, making it difficult to implement new regulations quickly. Especially at local levels where [understanding of the EUDR](#) is still limited, replacing paper-based traceability systems with the right digital alternatives will be a [massive undertaking](#).

Ethiopia has long faced foreign-exchange shortages and high inflation, which also makes the EUDR relevant from a macroeconomic perspective. Foreign currency is hard to come by due to Ethiopia's [negative balance of payments](#), and thus coffee export is one of the few available methods to acquire foreign currency, which the country depends on for the import of manufactured goods and cereals. Additionally, this system serves as a source of foreign currency for Ethiopia's banks, since exporters are [required to exchange 50%](#) of their incoming foreign currency into Birr within a month.

While half of Ethiopia's coffee production is [consumed domestically](#), the export of coffee is vital to Ethiopia's economic stability and therefore [tightly regulated](#) by the government. A weekly [minimum export price](#) is set by the Ethiopian Coffee and Tea Authority in order to maximize foreign currency flows. Coffee prices within Ethiopia are higher than this price, so exported beans are sold at a loss, sometimes as [high as 50%](#). Exporters recover these losses through a complex system, in which [sister companies](#) use the foreign currency earned through coffee export to import cereals and manufactured goods sold domestically at high margins.

The EUDR could negatively impact this entire system, since the EU is Ethiopia's largest trading partner in coffee, with [30% of Ethiopia's coffee](#) export going there. This includes the highest

quality beans with certifications like Fairtrade and Rainforest Alliance. [ODI has estimated](#) that if export to the EU suddenly became impossible, Ethiopia's total exports would drop by 18.4%, resulting in a 5.8% fall in imports due to forex constraints, with a likely ripple effect of wage decreases and lower government revenue.

Consequences of the EUDR

The EUDR requires due diligence statements to show that imported products like coffee do not originate from areas deforested after 2020.¹ It was introduced after years of [fruitless encouragement](#) of voluntary initiatives to prevent deforestation. The EUDR works by comparing GPS data from farms with satellite imagery of forest canopies. Micro and small operators need to comply with this system by June 2027, larger operators need to do so six months earlier. Because coffee grows well in the shade, it is [uncommon](#) to cut down forests for plantation-style coffee farms, and deforestation has been regulated by customary [land ownership laws](#) for centuries.² Typical Ethiopian coffee farms are small, not formally registered and spread throughout the country, making it expensive and time-consuming to register GPS data. Beans are often processed in large batches, which means that if one of the supplying farms is non-EUDR compliant, the entire batch cannot be exported to the EU.

Since smallholder farmers have trouble meeting the requirements in time, they are at risk of not being able to sell to the EU. Export will likely shift towards markets in the Middle East and China, with buyers less willing to pay [high prices for specialty coffee](#) from sustainable origins.³ This means farmers and exporters alike will profit less from coffee production, leading to income

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- 1 This is required of the first entity that puts coffee beans on the European market, which will need to trace its coffee beans back to the farm of origin.
 - 2 A risk assessment by Enveritas commissioned by the Ethiopian government found only 20 plots showing signs of deforestation since 2020. While the real number is likely higher, forest-based coffee farming is [considered less vulnerable](#) to deforestation than plantation-based coffee.
 - 3 Interviews with an Ethiopian coffee roaster and exporter.

reduction which can encourage unsustainable farming practices to reduce production costs.

Nationally, potential fallout from the EUDR risks exacerbating political tensions and inequality within Ethiopia. For example, land registration schemes have been used in the past by local elites to [capture land](#), leading to regional conflicts. An uneven distribution of information will make marginalised communities more vulnerable to similar forms of exploitation. [Some predict](#) that if the cost of exports to the EU were to rise by 10%, total exports would fall by 9.5%. Such a scenario would lead to shortages in essential sectors and high inflation, increasing the likelihood of political unrest in a country that is already dealing with high poverty rates and facing [severe regional conflicts](#). In such a fragile context, with the potential for tensions to escalate rapidly, significant changes in one of the most important sectors of the country can undermine stability.

Internationally, the EUDR risks weakening the trade relations between the EU and Ethiopia in a time where alternative markets are growing in importance. Several European specialty coffee processors have already withdrawn from Ethiopia due to fears of not being able to become EUDR compliant in time.⁴ Concurrently, the Ethiopian government is actively trying to [attract Chinese coffee importers](#); and this strategy is working. China rose from the [33rd largest importer](#) of Ethiopian coffee to the 4th largest, within a five-year period. Europe risks giving up its important position in the Ethiopian coffee market. This will limit the effectiveness of the EUDR and can impact EU-Ethiopia trade in other sectors. Since an increase in coffee exports to China will lead to an influx of Yuan, it is likely that Ethiopian importing companies will shift to importing from China.

In principle, the EU's political relations with Ethiopia are [centred on stabilisation](#) and combatting inequality, as a means to prevent the escalation of various regional conflicts. But

4 Interview with an Ethiopian coffee roaster and exporter.

the EUDR, in its current form, undermines this broader policy by risking a reduction in trade between the EU and Ethiopia, driving up inflation and impacting livelihoods, especially those of marginalised groups.

Despite these downsides, a successful implementation of the EUDR may lead to several benefits. Besides preventing deforestation, the EUDR is creating a push towards the [digitisation](#) of the coffee value chain, by registering farm locations and tracing the origin of coffee beans through the value chain. This would not only make the sector more transparent, but it would also make it easier for farmers to obtain certificates addressing human rights protection and environmental practices. There are many farmers who produce organic coffee who are either unaware that they are already in compliance or face high costs to get their certificates in order.⁵ However, the degree of digitisation required for the EUDR's implementation could also be achieved through projects that require a lower administrative burden on Ethiopia's value chain.⁶

Recommendations

There are several steps the EU and its member states can take to prevent or mitigate the risks highlighted above. Most importantly, the European Commission will publish a report at the end of April to evaluate the administrative burden of the EUDR. After this, the European Parliament will have the [opportunity to vote](#) on easier implementation, especially for smallholder farms. While the contents of the report and the proposed legislation are still unknown, several ideas could make implementation in Ethiopia easier and quicker. Three are particularly compelling:

- 1) Allowing for a [territorial approach](#) for the registration of coffee beans could enable those who bring coffee on the market to list a region as the source of their products, instead

5 Interview with an Ethiopian coffee importer.

6 For example, through European importers who are able to offer digital services to the farmers they buy coffee from.

of individual farms. Insofar as deforestation could be sufficiently monitored at a regional level, this would greatly decrease the number of registrations necessary, lowering administration costs (particularly for smallholder farmers) and time necessary for implementation.⁷

- 2) Allowing for [subnational risk benchmarking](#), whereby specific regions where coffee is gathered from naturally growing coffee trees in forests could be marked as medium or low risk, if there are no additional signs of deforestation. Currently all of Ethiopia is classified as medium risk for deforestation for all products, which increases the due diligence requirements, regardless of their applicability in particular sectors or regions.
- 3) Scaling up programmes already in force that combine existing certifications, like [Rainforest Alliance](#), with EUDR compliance. While these programs currently are too small and too underfunded to reach large portions of Ethiopia's farmers, with extra support from the EU they could ease EUDR compliance at scale and create an incentive to adhere to other production standards, like the prevention of child labour.





Furthermore, the EU can commit to setting realistic timelines when future regulations are proposed, which reduces [uncertainty about deadlines](#) and specific requirements. While EUDR has been postponed for one year, the challenges of becoming EUDR-compliant in time have not disappeared. If improved, the EUDR can make good on its potential to prevent deforestation and contribute to sustainable economic growth in Ethiopia. A feasible, well-supported implementation process will ensure the EU remains an attractive business partner. The report by the European Commission, expected in April, will offer ample opportunities towards that goal.

7 This would also prevent to a certain extent that farmers lose out on premium European prices because one non-compliant farmer in the neighborhood has made an entire shipment of coffee unsuitable for the European market.

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