

Coffee Weekly

A weekly examination of the fundamentals

January 8, 2009

Judith Ganes-Chase, President

914-232-1362

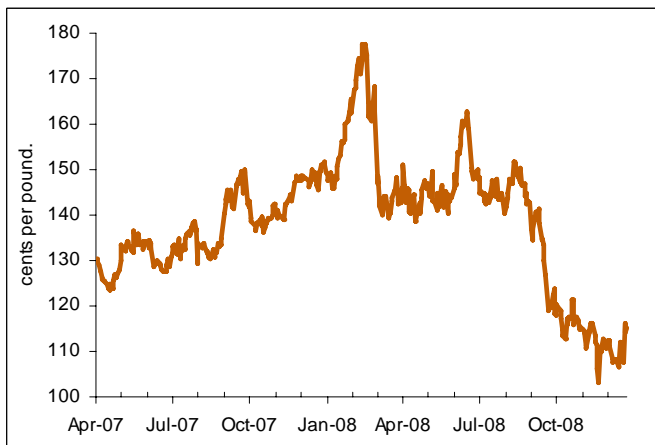
914-232-1364 fax

judyg@jganesconsulting.com

www.jganesconsulting.com

Coffee Outlook

Brazilian 2009-10 Crop Forecast Below Expectations



Source: FutureSource

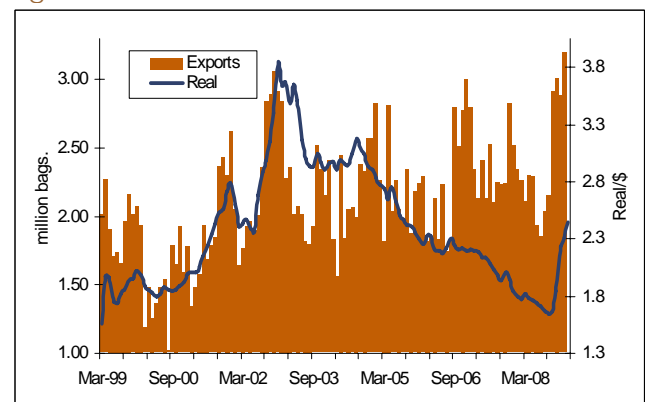
While most commodities are trading off the lows established last quarter, coffee was the market this week that led the charge out of the starting gate, posting a dramatic one day rise that took most by surprise. The market had been lulled into a sense of complacency last quarter, falling on widespread selling as funds de-leveraged and short term dollar strength. Supplies were believed to be ample with Brazil shipping aggressively and another large Vietnamese crop being harvested. Yet, when this window dressing is stripped away, the underlying structure of the market was shifting and better qualities Arabica coffees were becoming harder to come by. Differentials were firming reflecting this tightening market balance and should continue to hold steady as production is falling shy of expectations. High grown Central American coffees are trading anywhere from \$17-\$26 over the relevant "C" contract. Very few Centrals are trading at a discount to the Board any more.

As cautioned repeatedly, there is little excess supply at origin, with Brazil being the only question mark, and gaps in the supply chain could occur as a result. The sharply reduced Colombian crop is perhaps the largest hiccup but other problems exist compounding the situation. Too much rain has reduced output in a number of countries and yields are off slightly due to the reduced crop. While not a large problem individually, collectively the numbers

add up, especially because of the reduced supply from Colombia. High premiums for Mild Arabicas should keep coffee from being certified for delivery and certified stocks are likely to keep declining in the months ahead. I don't believe that roasters have been adequately covered for this. In addition to problems noted previously in Central America, India this past week also indicated that their Arabica output would fall short of expectations due to heavy rains and reduced crop care.

The market focus had been on the prospect of a potential shortfall in supplies much later in the year due to a smaller Brazilian 2009-10 harvest rather than on tightness developing sooner, especially since it seems apparent that the 2008-09 crop was at the upper end of expectations based on the volume of coffee being shipped the past several months. Brazilian coffee exports were at a record level in 2008 even though production was not. In December exports totaled just over 3.2 million bags (green plus roasted and soluble) compared to December 2007 shipments of 2.345 million bags. December exports were the highest single monthly total ever for Brazil to ship. For full year 2008, Brazil exported a total of close to 29 million bags. In the past four months, Brazil has had average exports topping 3.0 million bags. This frenzied pace of shipments won't be sustainable and should slow considerably after this month.

Brazilian Exports Surge as Dollar Strengthens Against Real



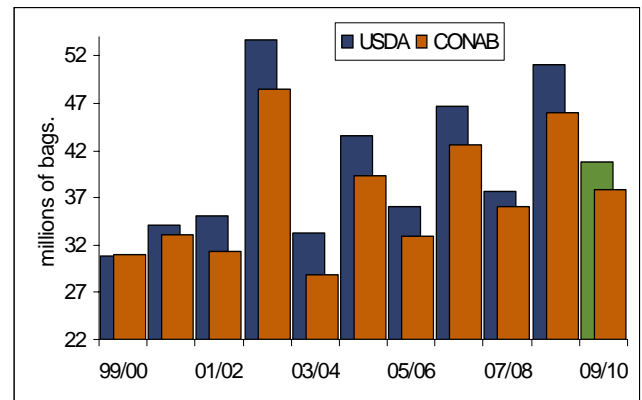
Source: Cecafe, X-rates.com

CONAB released its preliminary estimate on the new crop between 36.9-38.8 million bags, which was below trade views of a crop of 40-42 million bags. It's not surprising that CONAB sees the crop less than the trade, their estimates historically fall at the low end of the range. If CONAB is even close to being on the money in their view of the future Brazilian crop, then market supplies will become extraordinarily tight next year as opposed to just exceedingly tight, if one wants to compare superlatives. While I don't take the production figure, especially at this early date, in highest regard, what I do find as confirmation that troubles are brewing is the finding by CONAB that the area planted to coffee has declined marginally as farmers no longer find coffee as a viable investment and are looking to replace coffee with more lucrative crops. This is a result of the increased cost of inputs this past year but also due to higher labor rates. CONAB had made a minor adjustment up to the 2008-09 production estimate as well as to the area in production and the tree count, but the figures for 2009-10 fall below even the old data. According to CONAB, in 2009-10 there will be a total of 5.608 billion coffee trees down from 5.744 million in 2008-09. This will be the smallest amount since 2005-06. While the number of bearing trees usually drops in the down year of the production cycle due, the drop expected for 2009-10 is larger than in recent years.

In addition to the production figures, CONAB also released their balance sheet including stock data. The 2008-09 season is expected to end with stocks near unchanged at 12.529 million bags but then fall dramatically by end 2009-10 to only 3.284 million bags. The CONAB stock figure is based on an April-

March crop year basis. The stock figure for March 2008 is roughly two million bags higher than previously believed. There were no other changes to prior production figures. What the data shows is that Brazil will export record volumes in 2008-09 and not retain any coffee for making up the expected deficit in 2009-10 but instead stocks will be reduced by roughly nine million bags instead next year pushing private stocks to minimal levels. Government stocks have been already sold off to cover demand in recent years through regular auctions. This is one explanation as to why Brazil has been able to sustain exports despite CONAB's view that production was not nearly as large as the USDA or the trade has indicated.

CONAB Consistently Lower than USDA



Source: CONAB, USDA, 2009-10 J Ganes Consulting in green

Brazilian Coffee Area, Trees (millions), Output (thousands), Yields

	Area	Trees	Output	Yield per hectare	Yield per tree	Pounds
1997-98	1,788,320	3,260,640	18,860	10.55	0.0058	0.87
1998-99	1,788,320	3,260,640	34,547	19.32	0.0106	1.59
1999-00	1,870,400	3,437,000	27,170	14.53	0.0079	1.19
2000-01	1,980,300	4,110,000	31,100	15.70	0.0076	1.14
2001-02	2,077,300	4,496,130	28,137	13.54	0.0063	0.94
2002-03	2,310,770	4,990,330	48,480	20.98	0.0097	1.46
2003-04	2,201,550	4,835,620	28,820	13.09	0.0060	0.89
2004-05	2,212,870	5,355,350	39,272	17.75	0.0073	1.10
2005-06	2,217,666	5,324,482	32,944	14.86	0.0062	0.93
2006-07	2,152,397	5,365,948	42,512	19.75	0.0079	1.19
2007-08	2,073,092	5,615,248	33,740	16.28	0.0060	0.90
2008-09	2,169,795	5,744,768	45,992	21.20	0.0080	1.20
2009-10	2,122,613	5,608,953	37,848	17.83	0.0067	1.01

Source: CONAB