

# CONFIDENTIAL

**YOUR BEST SOURCE OF INFORMATION ABOUT THE BRAZILIAN COFFEE BUSINESS... AND MUCH MORE. THIS ISSUE:**

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- PROCESSING ONE HALF OF THE WORLD'S COFFEE? (PAGE 4)

## **DROUGHT PROBLEMS TO AFFECT NEXT CROP**

Minas Gerais is suffering from the strongest drought in four years. According to Brazilian coffee researchers and consultants, the lack of rain in the last four months and the high day temperatures caused intense water stress in many coffee areas of Minas Gerais with consequent delays in flowering and buds turning into branches instead of flowers. The roots are also being affected and despite the good nutritional situation of plantations, coffee production will be affected. However, it is still early to forecast the impacts on next year's crop. See Pictures of the Month session for more photographs.

Sources: EPTV, Rede Cafés do Brasil and P&A



## **HIGHEST COFFEE PRICES IN 50 YEARS**

The current low year of the Brazilian coffee crop cycle, record low worldwide stocks and the smaller Colombian production are factors that have contributed to the rise of green coffee prices in 2011. Prices of Brazilian coffee reached R\$ 520.00 per bag (around US\$ 305.00), the highest nominal prices in 50 years and twice the price registered in 2010. Known before as a supplier of quantity, Brazil has been gaining recognition as a producer of quality coffees with increasing yields. Brazilian coffees today have a participation of 50% in Starbucks blends.

Sources: Valor Econômico and P&A

## **ESPÍRITO SANTO BREAKS YIELD AND PRODUCTION RECORDS**

Coffee growers at Espírito Santo state broke two records this year: a record harvest and the highest yields in Brazil. The third official forecast for the 2011/2012 crop showed a total production of 11.57 million bags, 8.49 million Conilon/Robusta and 3.07 million Arabica. The average yield in the state reached 25.5 bags/hectare (1.5 tons/ha) to be compared with the average national yield of 22 bags/hectare (1.3 tons/ha).



Source: Revista Cafeicultura

Espírito Santo produces both Arabica and Conilon/Robusta

## **FERTILIZER DEMAND GROWS AT TWICE THE WORLD AVERAGE**

Brazil is the world's fourth largest consumer of fertilizers, after China, India and the USA, with a total of 24.6 million tons consumed in 2010 and a yearly growth of 6%, equivalent to two times the world average. Even though the country's average use of mineral inputs has increased from 69 kg/hectare in 1995 to 132 in 2009, around 60% of the agricultural properties, mostly small farms, still do not use any kind of fertilizer, indicating a huge potential market to be explored.

Source: Valor Econômico

## **RESEARCH, RURAL EXTENSION AND UNIVERSITY DEBATE SOIL FERTILITY AND FERTILIZATION METHODS**

The "Polo de Excelência do Café" (Coffee Excellence Center) held a meeting at the Federal University of Lavras (UFLA) to debate the latest topics on soil fertility and fertilization in coffee plantations. The objective was to find consensus among researchers, professors and rural extensionists on what to recommend to growers on topics like soil sampling, the use of lime, gypsum and phosphate, and leaf fertilizers at a time when husbandry is improving as a result of high coffee prices.

Source: Polo de Excelência do Café

**FAIRTRADE CERTIFICATION FOR SMALL CERRADO GROWERS**

The Minas Gerais Cerrado region is known for the high efficiency and professional profile of its coffee growers. What most people do not know is that the region is also home to small coffee growers. Now, the members of the Cerrado Association of Small Coffee Growers (APPCER) reached the important goal of being Fairtrade certified. It is expected that 2,000 bags of FT certified coffee will be exported in 2011; 27 out of the 39 APPCER members were certified.

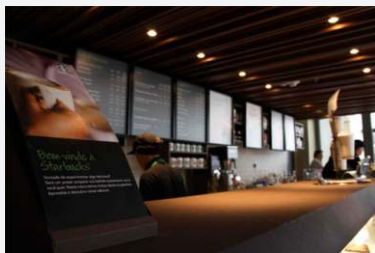
Source: SEBRAE

**INNOVATIVE PROGRAM AT 6th ESPAÇO CAFÉ BRASIL EVENT**

The 6th Espaço Café Brasil will be held in São Paulo on October 6th to 8th. The event expects more than 12,000 visitors among baristas, cuppers, roasters, exporters, growers and coffee lovers. This year's program offers specialized lectures, workshops, cupping labs and a barista competition, apart from the trade fair. The first meeting of the Brazilian branch of IWCA (International Women's Coffee Alliance) and the first Round Table between certified farms and certifying organizations are some of the attractions of this edition of the event.

Sources: Espaço Café Brasil and CNC

**STARBUCKS OPENS SHOP WITH EXCLUSIVE DESIGN INSIDE UNIVERSITY**



Starbucks opened its first store inside a Brazilian university in the city of São Paulo in September. The new shop was inspired in the 1930s modernist movement with a design specially created for the campus, with exposed steel beams, brick walls and windows that resemble and old factory. Around 60% of the materials used in the construction came from the previous structure that existed on the site. The new Starbucks store has 115 m<sup>2</sup> and offers community tables to enable students to study and work in groups.

Source: Exame

**BRAZIL'S ROBÉRIO SILVA IS THE NEW ICO EXECUTIVE DIRECTOR**

The International Coffee Council of the International Coffee Organization met in London from 26 to 30 September 2011 and decided by acclamation to appoint Mr. Robério Oliveira Silva as the new Executive Director of the ICO for a five-year term. Mr. Oliveira Silva is currently the Director of the Coffee Department and Chief of Staff of the Secretariat of Production and Agroenergy at the Ministry of Agriculture, Livestock and Food Supply of Brazil.

Source: ICO



**HIGHER DOLLAR COMPENSATES FOR FALLING COFFEE PRICES IN SEPTEMBER**

The recent appreciation of the American Dollar in relation to the Brazilian Real has allowed coffee growers and exporters to make up for the price drop of the commodity in international markets. The exchange rate, which reached R\$ 1.95 on September 22, has stabilized at R\$ 1.88 on September 30th. The Dollar gained 16% against the Real from the 1st to the 22nd of September.

Source: A Cidade – Ribeirão Preto



**Pictures of the Month**

**DROUGHT EFFECTS ON COFFEE PLANTATIONS**



Sources: EPTV and TVU

## THE FUTURE OF COFFEE CONSUMPTION

The table below shows how world coffee consumption behaved in the last decade according to the ICO and how it is likely to behave in the next 10 years according to our own forecast. A firm growth tendency is widely accepted by coffee experts, but what lies behind the annual growth rates expected? What is actually happening with coffee consumption to explain these projections?

	2000		2010		PAST ANNUAL GROWTH RATE (%)	P&A ESTIMATE 2020	
	THOUSAND BAGS	SHARE (%)	THOUSAND BAGS	SHARE (%)		THOUSAND BAGS	SHARE (%)
TRADITIONAL MARKETS	63.367	60,1%	70.837	52,9%	1,1	75,000	45.5%
PRODUCING COUNTRIES	26.385	25,0%	40.280	30,1%	4,3	58,000	35.2%
EMERGING MARKETS	15.750	14,9%	22.883	17,1%	3,8	32,000	19.3%
WORLD TOTAL	105.502	100,0%	134.000	100,0%	2,4	165.000	100,0%

SOURCES: ICO and P&A

definitely move from the North Atlantic basin eastward to Eastern Europe and Asia and southward to producing countries. What is behind this likely shift in the geographical distribution of worldwide coffee consumption?

Filter and soluble coffee will continue to account for the bulk of consumption but the drivers of consumption will change. In past decades consumption was driven by specialty coffee and coffee shops, primarily in traditional markets but in new markets too. Although the espresso preparation has a modest participation in total consumption numbers, it had an important role in attracting new consumers and making existing consumers to drink more coffee. Espresso coffee used the "stage" of coffee shops, our "temple" of coffee consumption, to make the barista movement grow and attract new consumers, a tendency that is likely to remain and increase in the near future.

If past consumption was driven by the specialty coffee and coffee shop "revolutions", the new revolution will be around the single-serve format either as individual coffee shots delivered by machines designed for home use or available in envelopes or sticks filled with soluble coffee.

The growth of machines for single-serve filtered coffee, like the Senseo in Europe and the Keurig in the US, is benefiting from the adverse economic situation that is shifting consumption back into homes in traditional markets. With over 15 million Philips-made machines sold, Sara Lee's Senseo has become a common household item in countries like Holland and France where about one-half of the houses have the gadget. Keurig, an open system available to different brands, whose K-cups offer over 200 different single-serve products, has recently signed an agreement with Starbucks that is due to start offering its coffees in K-cups before the end of the year.

Soluble, the beverage of choice to introduce coffee in tea-drinking emerging markets, also plays an important role in coffee consumption in most producing countries, with the major exception of Brazil. The single-serve 3-in-1 coffee mix, an envelope or stick with soluble coffee, non-dairy cream and sugar, flavored or not, usually served hot but also available for cold preparations in some markets, is becoming a major hit with young coffee consumers in Asia. Almost one-third of all coffee consumed in Indonesia today is sold in the 3-in-1 single-serve format. The offer of soluble coffee products is increasing beyond higher quality freeze-dried products to include organic, certified and single-origin coffees in order to appeal to more sophisticated consumers, including those who may be considering moving to roast-and-ground coffee.

Single-serve filter coffee is also starting to appear in coffee shops in North America where a battery of individual filters is being used to prepare different types of coffees for different clients. Another evolution in the coffee shop front has been the offer of coffee at and the addition of coffee outlets to fast-food chains, e.g., McDonald's McCafé, where coffee is usually sold at a lower price than at conventional coffee shops. These two tendencies are not only likely to stay but to develop further in coming years.

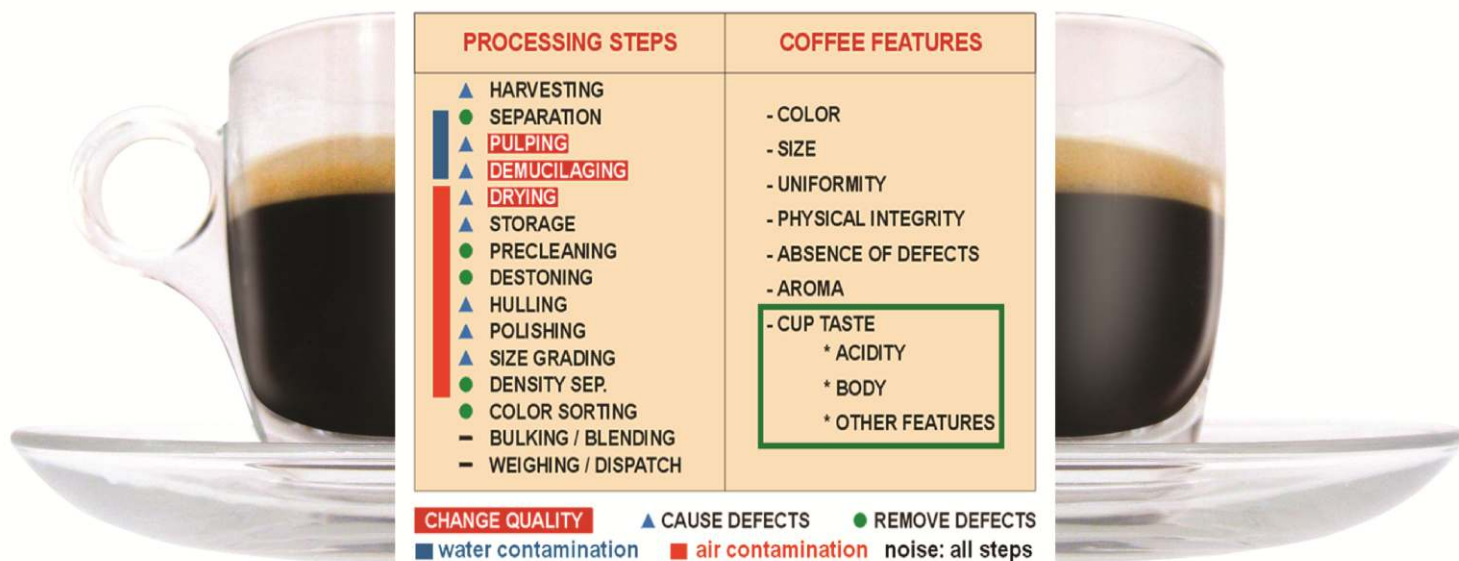
Innovation in coffee drinking will not be restricted to what is described above because the market is dynamic and ever changing. The power of innovation cannot be overstated. Even though innovation may only affect a niche market directly, e.g. Nespresso, or a small portion of the market, e.g. espresso itself, it may have a large impact on the consumption of the mainstream products – filter and soluble coffee – because innovation places coffee in the limelight, makes it fashionable, attracts new consumers and increases the intake by existing coffee drinkers.

If the forecast above is correct, consumption in "new" coffee consumers – producing countries and emerging markets – will overtake that in the "old" traditional markets of the US, EU and Japan before 2020; the BIIC countries, that have large populations and produce and consume coffee, – Brazil, Indonesia, India and China – are likely to account for one-fourth to one-third of world consumption in 10 to 15 years; and the dynamic growth poles of coffee consumption will



## PROCESSING ONE HALF OF THE WORLD'S COFFEE?

The table below lists the steps involved in coffee processing on the left-hand side and the coffee features that can be affected by processing on the right-hand side.



The challenge of coffee processing is to remove existing defects and to avoid the creation of new defects in order to enhance quality, that cannot be created by processing but can be modified and refined to suit clients' requirements. Modern coffee processing must also be sensitive to the environment where it is performed; water and air contamination as well as noise must be minimized or avoided.

The science and the art of coffee processing lie first on the design of the machines itself, second on how machines are combined to create an efficient flow, and third on how processing meets market requirements. Pinhalense excels on all three counts.

Pinhalense is well known for the development of new machines, processes and technologies, reason why it holds over 25 patents in the field of coffee processing alone.

Pinhalense has designed over 16,000 coffee mills - wet, drying and dry processing facilities - for clients in over 80 countries on the 5 continents. This bears witness to the company's unique ability to respond to any coffee processing challenge around the world, be it a single line for a micro grower or a full mill for a small, mid-size or large farmer or processor.

Pinhalense machines and mills deliver coffees that meet market requirements – moisture content, bean color, size distribution and aspect, and cup quality – because their development and manufacturing incorporate solid engineering knowledge **and** their performance is evaluated according to the features of the coffee that they deliver, quality included, as determined by professional coffee cuppers.

It is for the reasons above that Pinhalense estimates that the majority of the coffee drunk in the world today goes through at least one Pinhalense machine, more probably through a Pinhalense coffee mill. If that is not the case of your coffee yet, please contact the Pinhalense representative nearest you to check if you are indeed getting all that you can – aspect, quality and price – out of your coffee.

## Brazilian Prices

September 30, 2011

### Main Producing Regions / Farm Gate

Arabica Naturals (R\$/ 60 kg bag)		+ 11%	Conilon/ Robusta (R\$/ 60 kg bag)	
Cerrado-MG fair average quality T.6	505,00 ↓		Colatina-ES fair average quality	235,00 ↑
Mogiana-SP fair average quality T.6	500,00 ↓			
South Minas fair average quality T.6	500,00 ↓			
Arabica Pulped Naturals (R\$/ 60 kg bag)			BM&F (US\$/ 60 kg)	
Cerrado-MG	555,00 =		Dec 2011	307.45 ↓
South Minas	550,00 =		Mar 2012	308.00 ↓
			May 2012	296.20 ↓
			Real R\$/ Dolar US\$	
			September 30	1,88 ↑

Source: www.qualicafex.com.br