

CONFIDENTIAL

5th

Anniversary
Issue

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

- FIVE YEARS OF CONFIDENTIAL NEWSLETTER / CONSULTING AT P&A (PAGES 3 AND 4)
- MACHINE (DECISION) OF THE MONTH: BROWN FIELD OR GREEN FIELD? (PAGE 5)

EXCESSIVE RAINS DURING HARVESTING MAY AFFECT COFFEE QUALITY

Frequent rains in the Cerrado, South Minas and Mogiana regions in the first weeks of June have delayed harvesting and may affect coffee quality and prices. The unexpected rains dropped part of the cherries on the ground; drying on patios has also been seriously affected. Other problems are cherries with different degrees of ripeness and cherries changing quickly from unripe to over-ripe which curtails the ability to pulp and produce washed coffees.

Sources: Canal Rural and P&A



LABOR COSTS CONTINUE INCREASING ABOVE INFLATION

The 14% growth of the minimum salary in Brazil was the main factor behind the increase in the direct costs of coffee production this year. Direct costs rose 9.55% in farms that use manual labor and 5.19% in farms that are mechanized. The share of coffee production required to cover total direct costs reached 68% in March 2012, against 65% in October of last year.

Source: Boletim Ativos do Café (National Agriculture Federation, CNA)

INTERNATIONAL CONFERENCE ON COFFEA CANEPHORA IN ESPÍRITO SANTO

An International Conference was held in Vitória, capital of Espírito Santo, on June 11 to 15, to celebrate the 100th anniversary of the introduction of Conilon coffee in the state. Over 500 people from 22 countries attended the event including government representatives, the executive director of the ICO and industry experts from producing countries Vietnam, Indonesia, India, Uganda and the Ivory Coast. The conference focused on research, innovation, quality and market opportunities for Robusta/Conilon coffee in Brazil and abroad. Conilon production in Espírito Santo increased from 400,000 bags in the 1970s to over 9 million bags in 2012 due mainly to investments in research and transfer of technology to small holders.

Source: Portal of the Government of Espírito Santo

RISING SHARE OF ROBUSTA IN BRAZILIAN BLENDS

Industry representatives estimate that Robusta/Conilon may already represent one half of the "average" roast and ground blend in Brazil. According to CeCafé (the Brazilian Coffee Exporters' Association), the share of Robusta in the national blend has grown to 50% from only 20% a decade ago and now accounts for almost 10 million bags of coffee per year. The use of more Robusta started because of lower prices but quality improvements have also played an important role. Although Brazil is investing to increase the quality of its Conilon production, last year the country exported only 197,000 bags of gourmet Conilon but 2.47 million bags of average quality Conilon.

Source: Valor Econômico



SALES OF HAND-HELD HARVESTERS ESCALATING

The market for hand-held harvesters has been expanding rapidly in Brazil this harvesting season. The equipment, priced between R\$ 1,500 and 1,800 (US\$ 750 and 900) on average, is being adopted not only by small and medium-sized coffee growers, but also by big producers. A leading manufacturer reported sales growth of 55% in the hand-held harvester segment from January to June 2012 compared to the same period last year; another company plans to expand its business to other producing countries in Latin America. This type of machine can increase the volume of coffee harvested per person by 3 to 4 times and costs can be lowered by 40% when compared to the traditional manual picking of cherries.

Source: Agência Estado



Source: Ipanema Coffees

NEW IT TOOL TO SELL COFFEE AT COOXUPÉ

Cooxupé, Brazil's largest coffee growers' cooperative, is now offering to its members a new system of online operations called "Café Online". Among other services, the new tool allows growers to quote products and to sell their coffee from their own computers avoiding the need to go to the cooperative offices. Cooxupé is also implementing a digital inclusion program to train growers on computer skills and access to the Internet.

Source: Notícias Agrícolas

US\$ 100 MILLION IN BUSINESS DEALS AT EXPOCAFÉ 2012



The 15th edition of the largest Brazilian coffee trade fair held annually in the municipality of Três Pontas, Minas Gerais, generated US\$ 100 million in sales by exhibitors. Pinhalense broke its past-year sales record in spite of lower coffee prices now. Besides equipment and machinery for coffee, Expocafé also had a conference track featuring scenarios and trends for the coffee

business in Brazil and abroad including exports opportunities presented by the Brazilian Specialty Coffee Association (BSCA) and the Brazilian Trade and Investment Promotion Agency (APEX). P&A's Carlos Brando presented on strategic opportunities for the Brazilian coffee business at a special strategy meeting of the National Coffee Council (CNC) held during the event.

Sources: ASCOM and P&A

IAPAR LAUNCHES NEW NEMATODE-RESISTANT VARIETY

The Paraná Agronomy Institute (IAPAR) released coffee cultivar "IPR 100" that is resistant to the nematode "*M. paranaenses*" without grafting. The new variety is part of IAPAR's efforts to develop non-chemical techniques to control nematode infestation in the state of Paraná. In another project, researchers reduced nematode infestation by 88% using fungi control with mycorrhizae and nematode eaters.

Source: IAPAR

125 YEARS OF IAC: PIONEERING ROLE IN BRAZILIAN COFFEE HISTORY

The Campinas Agronomy Institute (IAC) became 125 years old on June 27th. Brazil's position as the largest coffee producer and exporter owes much to IAC's pioneer research on soil, genetics and mechanization, among others. Coffee varieties developed by IAC represent 90% of all Arabica coffee planted in Brazil.

Source: Embrapa Café



BRAZILIAN GOVERNMENT TO INCREASE SUSTAINABLE PURCHASES

In preparation for the Rio+20 Conference, the Brazilian government issued measures to reinforce the "Sustainable Public Contracting" program created in 2010 to stimulate the "green economy". The list of sustainable products that should be acquired in public tenders was extended to 700 items and include recyclable ink cartridge for printers, air conditioning equipment, recyclable paper, among others.

Source: Valor Econômico

FIVE YEARS OF COFFIDENTIAL NEWSLETTER

We have reached issue number 60 of our Coffidential newsletter: five years reporting what happens in the Brazilian coffee business, presenting our opinions and those of guest writers in the Outlook session and educating readers about coffee processing. We are grateful for our readers' attention and the comments and suggestions they have sent over the years. Coffidential is today published in English and Spanish, translated into Chinese and Bahasa Indonesian, and sent to almost 5,000 readers in 107 countries. We are proud to have you in our readership.

This is a good time to introduce the persons who are behind the Coffidential newsletter. It started with Paulo Henrique (PH) Leme and myself and for a time we had the support of Rodrigo Pasquini who moved to P&A machinery trading division. Maria Fernanda Brando joined the team later as did Larissa Menegatto who is charged with production.



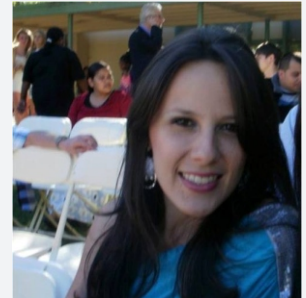
Paulo Henrique Leme (PH)



Carlos Brando



Maria Fernanda Brando



Larissa Menegatto

Content is created by PH, Maria Fernanda and myself. Both PH and Maria Fernanda are active in the consulting division of P&A addressing promotion of consumption, sustainability, geographical indication (GI) and strategy and structure issues, to mention only a few areas. They have both attended graduate school since they joined P&A. PH, an agronomist, did his masters in agribusiness with a dissertation on consumers' preferences and is currently working on his PhD. Maria Fernanda, with a background in communications and the hospitality industry, did her MBA with concentration on marketing and today oversees content development at P&A including the many presentations we make in Brazil and abroad every year.

Our "editorial board", if we may say so, also includes the P&A traders who are active selling Pinhalense machinery around the world: João Staut (who is a coffee cupper and quality expert and runs our specialty coffee operations), Joaquim Brando (Latin America), João Brando (Asia) and Rodrigo Pasquini (Africa). Joaquim and João Henrique are agronomists, the former with a master degree in agribusiness management and both with extensive experience in coffee growing and processing in several areas of Brazil and abroad.



Joaquim Brando



João Staut and Rodrigo Pasquini



João Brando

Coffidental receives coffee prices and market intelligence information from the group's specialty coffee company Qualicafex. Our advertising agency GSB2 is in charge of Coffidental's graphic design, art work and images. Pascoal Brando manages the mailing list.

P&A CONSULTING IN BRAZIL AND ABROAD

The reader may be wondering what all these highly trained and experienced professionals do at P&A besides machinery trading. P&A actively consults for leading coffee business clients in Brazil and abroad ranging from national and regional governments and institutions to companies, cooperatives and growers of all sizes including leaders in their market segments in all coffee producing states of Brazil and countries as diverse as India, Indonesia, Vietnam, East Africa, Mexico, Central America, the United States and Europe. P&A has also consulted for the World Bank, the International Coffee Organization (ICO), the IDH Coffee Program and multinational corporations that supply inputs and equipment to the coffee business.

P&A has recently decided to expand its consulting activities abroad in response to increasing demand for projects and as a result of the recent signing of a Memorandum of Understanding between the ICO and the Brazilian Cooperation Agency (ABC) to assist coffee producing nations with Brazilian technology and expertise. P&A has hired new senior professionals, is entering into agreements with other consulting companies that complement its portfolio of services and retained experts in areas that require the intervention of highly specialized professionals (e. g.: genetics and biotechnology, diffusion of technology and rural extension, and climatology). P&A has a network of representatives and associates in 34 countries that cover nearly all coffee producing areas of the world and are well connected with business and government.

The project areas that P&A is and will continue addressing include but are not restricted to sustainability, yield management, organization of the production chain, strategy, communications, marketing and promotion of consumption. Even though this scope of work may seem wide at first sight, all components fall under the umbrella of creating a sustainable coffee business that adds value to products, is socially and environmentally responsible and provides fair returns to growers and labor.

We will elaborate further on consulting at P&A at a coming issue of Coffidental.



Brazilian Prices

June 29, 2012

Main Producing Regions / Farm Gate

Arabica Naturals (R\$/ 60 kg bag)

Cerrado-MG fair average quality T.6	390,00	↓
Mogiana-SP fair average quality T.6	385,00	↓
South Minas fair average quality T.6	385,00	↓

Arabica Pulped Naturals (R\$/ 60 kg bag)

Cerrado-MG	405,00	↓
South Minas	400,00	↓

+ 5,2%

Conilon/ Robusta (R\$/ 60 kg bag)

Colatina-ES fair average quality	275,00	↑
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BM&F (US\$/ 60 kg)

Jul 2012	210,90	↑
Sep 2012	216,55	↑
Dec 2012	219,40	↑

Real R\$/ Dolar US\$

June 29	1,98	↓
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Source: www.qualicafex.com.br

BROWN FIELD OR GREEN FIELD?

Coffee companies and processors faced with the need to expand capacity often have the option to buy existing equipment or mills ("brown field") or to go for brand new machinery and solutions that are designed to respond to their specific needs ("green field"). Actual cases and experience indicate that brown-field opportunities that seem attractive in the first place often turn out to be far from ideal and lose, sometimes badly, for green-field alternatives. Let's look at the reasoning behind this statement.

The first question to be asked when buying existing machinery or mills is why they are being sold. Even if they pass the first test – they are not old technology, poorly maintained or laid out in an inefficient manner – they may have been designed for coffee growing and marketing conditions that no longer apply. For example, countries that had no berry borer before but now do usually require substantially different milling solutions and equipment. At the other end of the processing flow, the outgoing finished product may call for different processing features and require different machines and layouts if for instance coffee buyers demands changed from commercial to differentiated coffees or from ungraded to size-graded coffee. The way coffee is harvested – the chances of receiving a mixed maturation product are ever increasing – may drastically affect the way a wet mill is designed and mechanical driers are selected. Climate change itself can alter the thickness of both the pulp and the dry cherry shell as well as the size and shape distribution of coffee beans with important implications for pulping, hulling, size grading and defect separation. In summary, there is always a risk of buying a good mill that has good technology but is outdated and no longer responds to current processing requirements!

The potential problems with brown-field solutions do not stop here. Old machinery tends to require more power, water and labor than modern Pinhalense equipment. Even if an existing mill is ready to restart operation under new ownership it may have to be changed not only to cope with the quality and processing requirements of the incoming raw-material and outgoing finished product to be supplied, as described in the previous paragraph, but also to align energy, labor and water consumption with current industry standards.

The price of the brown-field acquisition plus the costs of updating the machinery and flow often exceed the price of a new green-field mill that will have the further advantage of being designed and manufactured to respond to all client specifications. The short delivery times practiced by Pinhalense today, even for large mills, invalidate the possible ready-to-run advantage of a brown-field solution, specially considering that it is almost always unavoidable to repair, maintain, change and upgrade equipment and to customize flows in a recently acquired second-hand mill.

The high cost of electricity in coffee producing countries and its growing impact on coffee processing costs definitely favor green-field solutions with modern energy saving equipment, specially when the machinery supplier is Pinhalense. Finally, today's dust aspiration and worker safety requirements render existing mills quite difficult and costly to adapt with the extreme cases of having to disassemble everything and to assemble again according to a new layout and with new pieces of equipments added. Relocation of machinery and reorganization of warehouse space may also be called for by the trend to move from standard-sized jute bags to big bags and bulk handling.

Think twice before you favor a brown-field coffee milling solution because, last but not least, the success of a coffee mill depends 50% on the machines themselves and 50% on the process flow. The latter is most likely not to be what you need even if you buy a second-hand Pinhalense mill that has obviously not been designed for you. On the other hand, you are always welcome to rely (at no cost) on Pinhalense's engineering and design departments for your tailor-made green-field projects that today must include not only machinery but also automation, warehouse layout and product logistics. With so many changes going on in all stages of coffee processing and storage it is unlikely that brown-field solutions will be attractive at all.

