

CONFIDENTIAL

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

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☉ RANGE OF BRAZILIAN CROP ESTIMATES WIDENS

Based on an estimate of about 10 million bags harvested until the end of May and comparing this figure with percentages harvested in the same period of both 2014 and the last five years, a leading consulting company claims that the current Brazilian crop may reach 50 million bags. This echoes recent figures proposed by international traders, is 13% larger than Conab's figures just released and departs sharply from the Procafé estimate published last February. The range of estimates that seemed smaller than usual months ago has now moved in the opposite direction to become one of the largest in recent years.

Sources: Exame, Conab, CNC and P&A

☉ FUNCAFÉ INTEREST RATES TO GO UP

Funcafé credit lines, that provide financing to coffee growers in Brazil, will have higher interest rates starting in July. The new rates will vary between 8.75 and 10.5% per year, up from 6.5%, and total funds available will be R\$ 4.136 billion (US\$ 1.29 billion), 8% higher than in the previous crop year

Source: Valor Econômico

☉ MECHANICAL HARVESTING FOR MOUNTAINOUS AREAS

The Agricultural Research and Rural Extension Institute of Espírito Santo (Incaper), that has been working with other institutions to develop machines to harvest Conilon in flat areas, has recently started a new research project to develop machines capable of harvesting coffee, both Conilon and Arabica, in mountainous areas. Experiments will soon start in Brejetuba, a small municipality in Espírito Santo, using a machine already tested for Conilon harvesting in flat areas. Incaper plans to adapt this recently developed harvester that uses a long piece of canvas that is first spread out between two lines of trees and then rolled up to retrieve the coffee branches dropped on it. Mechanical harvesting in mountainous areas is one of the greatest challenges for Brazilian growers.

Source: CNC



☉ MINIMUM COFFEE PRICES RELEASED

The Brazilian government has recently published the minimum coffee prices for the period from April 2015 to March 2016. The Arabica price has been maintained at R\$ 307 (US\$ 96) per bag while the Conilon price was increased to R\$ 193.54 (US\$ 61) per bag, slightly higher than the previous R\$ 180.80 (US\$ 57). Unhappy with the guarantee price for government purchases of Arabica coffee, growers intend to continue to work closely with the Ministry of Agriculture, Livestock and Food Supply to analyze the actual production costs in the different coffee regions and reach a minimum price closer to reality.

Source: CNC

AMERICAN COFFEE ROASTERS TURN TO BRAZILIAN ROBUSTA

American roasters have started to gradually replace Robusta from Vietnam with Brazilian Conilon in their blends since price differentials for Brazilian Conilon are currently 3 to 5 cents per pound below Vietnamese Robusta prices. Conilons have been historically traded at a premium in relation to Robusta varieties from Asia with differentials reaching as much as 20 cents/lb above future prices. But Brazil’s offer of Conilon has been increasing: 3.8 million bags of Robusta were exported in 2014 compared to only 1.5 million the previous year according to the International Coffee Organization (ICO). Coffee exports from Vietnam have reached their lowest level in five years and growers hold stocks waiting for better market prices. Estimates of the Brazilian 2015 Conilon crop are widely spread in a range of 11.2 to 17.7 million bags.

Source: Reuters

4C AND CERTIFICA MINAS CAFÉ SIGN EQUIVALENCE AGREEMENT

During the 6th Forum and Coffee Dinner, promoted by CeCafé and held in São Paulo on May 18-19, the 4C Association and the Certifica Minas Café (CMC) Program announced the conclusion of the benchmarking process and signed the agreement that resulted from the technical comparison made between the two standards. Certifica Minas Café (CMC) growers will now be able to become 4C verified and sell their coffee as such without the need to go through additional verification. CMC certificate holders will gain a new gateway to the sustainable coffee market thus strengthening the international recognition and demand for CMC certified coffees without further costs. This project was supported and funded by the Sustainable Coffee Program (SCP), a global pre-competitive initiative coordinated by P&A in Brazil and powered by IDH.

Sources: 4C and IDH



From left to right, Robério Silva, Executive-director of ICO, Melanie Rutten-Suelz, Executive-director of 4C Association, João Cruz, Secretary of Agriculture of Minas Gerais, João Lian, Chairman of CeCafé’s Board of Directors, Jenny Kwan, Manager of Coffee Program at IDH, and Carlos Brando, Director of P&A

CECAFÉ AND IDH SIGN MOU TO DISSEMINATE COFFEE SUSTAINABILITY CURRICULUM

In the same event mentioned above, the Brazilian Coffee Exporters’ Association (CeCafé) and the Sustainable Trade Initiative (IDH) signed a Memorandum of Understanding to disseminate the Coffee Sustainability Curriculum using CeCafé’s Digital Inclusion Centers, whose 137 facilities are used by small growers and their children. The Coffee Sustainability Curriculum, developed by the Sustainable Coffee Program using Embrapa’s PI-Café standard as a basis, is meant to be used by government and private extension services to facilitate the adoption of sustainable coffee growing practices especially among small growers who are more difficult to reach.

Source: P&A

CAPSULE CONSUMPTION TO KEEP GROWING IN BRAZIL

According to a survey commissioned by the Brazilian Coffee Roasters’ Association (ABIC), 1.7% of the total domestic demand of 20.3 million coffee bags in 2014 was in capsules compared to only 1.1% the year before. Household penetration is also increasing, with capsules currently present in 1% of Brazilian homes, i.e., almost 500,000 households. Another survey, commissioned by roaster 3 Corações, indicates that the three largest players in the Brazilian single-serve coffee market are Dolce Gusto, Tres (3 Corações Group) and Nespresso, in this order. A typical Brazilian drinks an average of 81 liters of coffee per year, coffee is present in 98.7% of Brazilian homes and capsules sales grow 40% to 50% per year.

Source: Valor Econômico

BRAZILIAN CROP ESTIMATES: HOW (NOT) TO USE THEM – THE ULTIMATE GUIDE

This is not another Brazilian coffee crop estimate study or update. The coffee crop estimate season is in full swing as the harvesting season in Brazil is just starting. The several estimates released up to now have all reached one single conclusion: they are surely very different from their peers' estimates.

As estimates and new sources of data pop up, they reveal what we at P&A are calling the "coffee crop estimates volatility". We have not created an index for that yet, but since last year the volatility is high and this year is no different and even higher. High enough to a point that in the same day last May two important public institutions came forth with figures showing a 10 million bags deviation from each other. A difference that accounts for about 20% of the Brazilian crop (depending on which one you rely upon...).

Events like this draw the attention of the media and the coffee community but the lack of consensus among researchers and analysts is not new or recent. It only became more relevant (and harmful) to the market as Brazil's share of world coffee exports also became more significant.

It is worth to note that even for past crops the analysts do not reach a consensus which means that they are not only using different assumptions but also using different methodologies to reach their numbers. It also means that it is difficult to find some source to rely on when they do not even agree on things that were supposed to be a *fait accompli*.

Add to this the fact that studies to project coffee crops are scarce because they are difficult to be undertaken, costly and short lived. Imagine someone who tried to make a broad evaluation of the 2014 Brazilian crop performing a field study at the end of 2013. Firstly, this person would have to travel between coffee growing areas that are more than 1,000 km apart. Secondly, the researcher would need to survey as much as he/she could of the 2 million hectares of area under coffee because the productivity varies a lot from place to place within even the same farm! Lastly, after processing all the data in the beginning of 2014 the researcher would find out that all his/her work was in vain due to the severe drought that affected everything that he/she had surveyed a few weeks before...

Unreliable as they seem to be, coffee crop estimates cannot be ignored. But they just cannot be taken as given either. As paradoxical as it may seem, in my view the solution to the reliability of crop estimates is the release of more crop estimates from different sources.

In reality, everybody in the market has a crop estimate of his or her own. The Brazilian crop is so important for futures price formation that once a deal is settled in the futures market both parties are consciously or unconsciously betting on a given size for the Brazilian crop.

In other words it is not far-fetched to say that the international price of coffee carries implicitly an updated estimate for the Brazilian crop size. So why not invert this logic? If everybody is worried about how Brazil will affect the price of coffee, why don't we ask the price of coffee what it thinks of Brazil's next crop?

And how to manage this? Simply ask the people behind those prices. Since there are as many as thousands of daily deals let's just ask the opinion of market agents on the crop size of Brazil. The law of large numbers¹ will be behind us and it will help us build a market consensus around this subject.

¹ In probability theory, the law of large numbers (LLN) is a theorem that describes the result of performing the same experiment a large number of times. According to the law, the average of the results obtained from a large number of trials should be close to the expected value and will tend to become closer as more trials are performed.

Brazilian Prices

Main Producing Regions / Farm Gate

May 29, 2015

Arabica Naturals (R\$/ 60 kg bag)		Conilon / Robusta (R\$/ 60 kg bag)	
Cerrado MG	435,00 ↓	Colatina-ES fair average price	300,00 ↑
Mogiana	430,00 ↓		
South Minas	430,00 ↓		
Arabica Pulped Naturals (R\$/ 60 kg bag)		BM&F	
Cerrado MG	505,00 ↓	Jul 2015	155,70 ↓
South Minas	500,00 ↓	Sep 2015	158,00 ↓
		Dec 2015	159,20 ↓
		Real R\$ / Dolar US\$	
		May 2015	3,19 ↑

Source: www.qualificafex.com.br

EVER LARGER DRY COFFEE MILLS... FROM A SINGLE SUPPLIER - AN UPDATE*

The tendency toward larger and larger coffee export processing facilities has definitely consolidated with Pinhalense's supply in 2011 and 2012 of an Arabica mill with a capacity of 42 ton/hour and a Robusta one for 36 ton/hour. These mills can process more than 11,000 and 9,000 bags of 60kg per day in two shifts or about 4 and 3 million bags of coffee per year, respectively, with enough idle time to add a third shift and 50% of extra capacity. It is mind-boggling to think that such Arabica mill can process all the production of Mexico or Guatemala under one roof. The Robusta mill can in turn process all the production of Uganda or India. Amazing as these numbers are – these two mills are perhaps the largest of their type in the world – they represent the continuation of the trend for ever larger mills that started in the last decade and gained speed in this decade.

The design features that Pinhalense incorporated into these giant mills are stepped-up versions of the unique solutions that Pinhalense developed for the mills of all sizes shown in the table below, supplied to clients around the world in a few years before April 2012.

CAPACITY	ARABICA MILLS	ROBUSTA MILLS
2 to 6 ton/h	29	2
6 to 12 ton/h	13	8
12 to 18 ton/h	10	3
18 to 24 ton/h	3	4
24 to 30 ton/h	1	1
> 30 ton/h	1	1

The figures in the table have grown significantly since April 2012: four large Pinhalense dry mills started operation outside Brazil in the last 12 months alone: three in Southeast Asia, two with capacity of 28 ton/h expandable to 42 ton/h and one with 14 ton/h expandable to 21 ton/h, and one in Latin America, 12 ton/h. In addition, Pinhalense is currently manufacturing two large Arabica dry mills for Brazil, capacities 36 and 18 ton/h, one Robusta and Arabica mill for Africa, capacities 21 and 10 ton/h, respectively, and the expansion of another Arabica mill from 24 to 42 ton/h. And there is more in the pipeline.

Problems that are easy to solve in small projects are aggravated when the size of the mills increase, e. g., intermediate storage, mostly in big-bags now; flow and big-bag weighing; exchanging types of coffee to be processed; dust suction; and disposal of rejects. That is why Pinhalense has developed items like big-bag and flow scales specifically designed for coffee; bag - big bag - bulk interfaces and bulk handling of products and rejects; high-capacity, low-friction, self-cleaning elevators that address the problem of coffee damage and idle time to clean elevator feet; and dust suction systems and filters, to mention only a few features. These are some of the reasons why clients have been favoring complete Pinhalense mills, with machines, silos, conveyance equipment, etc. all manufactured by Pinhalense.

Pinhalense has always claimed that the success of a coffee mill depends equally on the performance of the equipment and the efficiency of the process flow. Pinhalense's computer aided design (CAD) facilities create an environment of permanent design improvement that benefits all clients. No matter how large a miller, exporter or multinational trader is, chances are that its engineers and technicians may have designed a few coffee mills only if any because their main task is operation and maintenance. This is to be compared with over 20,000 mills designed by Pinhalense, with a record of over three mills per day in the last two years. This is a reliable indicator of the technology that is transferred free of cost to clients who buy a complete Pinhalense coffee mill. It is therefore no wonder that clients prefer 100% Pinhalense mills today!

Besides the technological and efficiency benefits that clients enjoy when buying a complete Pinhalense mill, there are other tangible benefits too, for example, the responsibility for performance, maintenance services and spare parts lies on a single party, Pinhalense itself and its network of agents around the world. This can have a major impact on profitability considering that any coffee mill but specially large ones operate on a very tight contractual schedule.

The fact that the complete coffee mills listed above were supplied to leading international coffee traders and prominent local exporters in countries as diverse as Mexico, Honduras, Guatemala, Colombia and Peru, in Latin America, Kenya, Uganda, Ethiopia and the Ivory Coast in Africa, and India, Indonesia, Vietnam and Papua New Guinea in Asia and Oceania, besides Brazil, demonstrates that coffee millers are no longer willing to "blend" equipment from several makers and / or to buy separate pieces of equipment to be laid out by themselves. The bottom line may be that buyer and seller, equipment user and supplier, decided to stick to what each does better, trade coffee and design and supply coffee mills, respectively.

* The majority of the text above, that has now been updated, was published in Confidential No. 57 in April 2012.