

CONFIDENTIAL

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

THIS ISSUE:

- MICRO LOTS AND THE FUTURE OF THE SMALL GROWER (PAGE 3)
- PROCESSING OF MICRO LOTS (PAGE 4)

UNCERTAIN PRODUCTION PUSHES COFFEE PRICES UP

A new crop estimate for Brazil released by a leading coffee trader in April helped to raise coffee prices once again; a recent study shows that prices are up by 63.94% in the first quarter of 2014. In response to good prices, growers in Minas Gerais have started to sell their coffee that was stored since last season. The impact of these sales is notorious in many cooperatives. In Varginha, for example, coffee stocks fell from 1 million to 400,000 bags. The price of the coffee bag in the Brazilian market reached R\$ 467 (US\$ 210) in late April compared to R\$ 279 (US\$ 125) in December 2013.

Sources: O Estado de S. Paulo, Globo Rural and Folha de SP

FUNCAFÉ CREDIT LINES DEFINED BY NATIONAL MONETARY COUNCIL

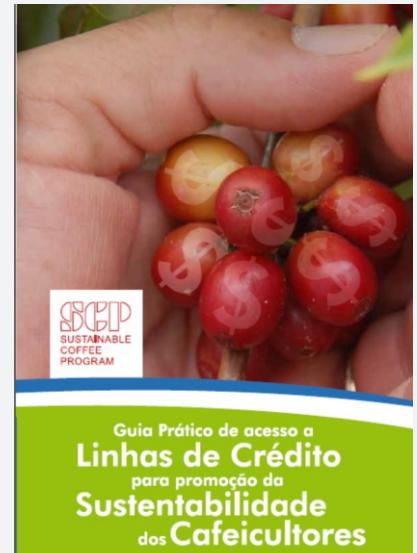
The National Monetary Council has defined the Brazilian Coffee Fund (Funcafé) credit lines for 2014. Coffee storage will receive the highest allocation of R\$1.3 billion (US\$ 585 mi); R\$845 million (US\$380 mi) will be reserved for husbandry; up to R\$750 million (US\$337 mi) for coffee purchasing; R\$20 million (US\$9 million) for the recovery of damaged crops and R\$10 million (US\$4.5 million) for operations in the futures market. Deadlines to renegotiate operations related to the Land Fund and Land Reform have also been extended.

Source: Cooxupé

SUSTAINABILITY AND ACCESS TO CREDIT LINES GUIDEBOOK

IDH's Sustainable Coffee Program (SCP), coordinated by P&A in Brazil, has released a Guidebook of Credit Lines to Increase the Sustainability of Coffee Growers. The 15-page booklet lists and describes credit lines made available by the federal government and the main coffee producing states. The wide scope of the 21 lines, that cover the different aspects of sustainability and favor small growers, gender equality and youth participation, helps understand why Brazil is already the largest source of sustainable coffee in the world and is preparing to grow even bigger in this sector.

Source: P&A



NEW MINIMUM PRICE FOR CONILON

Following demands from growers of Espírito Santo state and based on studies by Conab, the Brazilian Ministry of Agriculture decided to adjust the minimum price for Conilon (Robusta) coffee from R\$ 156.57 to R\$ 180.80 (from US\$ 70.50 to US\$ 81.50) per bag of 60kg, a 15.5% increase, that makes the minimum price equivalent to about US\$ 1,350 per ton.

Source: Ministry of Agriculture, Livestock and Food Supply (MAPA)

AREA IN MINAS GERAIS SHOWS POTENTIAL FOR CONILON

Extensive research on experimental farms in Matas de Minas started in 2003 shows a great potential for the region to become a producer of Conilon coffee that is more adapted than Arabica to the high temperatures that prevail in this part of Brazil. To promote Conilon production, Epamig (Agricultural Research Institute of Minas Gerais) is now distributing 10,000 seedlings of Conilon among selected growers as part of a pilot project; a second step will be to expand production to other municipalities of the region. The first Conilon harvest in Matas de Minas is expected in 2016.

Source: Diário do Comércio

CONILON THRIVES IN SOUTH BAHIA

After a long period of drought in the southern part of Bahia, abundant rain is helping to boost Conilon production. Growers in Eunápolis, for instance, hope that yields will reach 95 bags (5.7 tons)/hectare this season, 30% more than last year when the sector had one of its worst crises. Conilon output is expected to grow 11% in this part of Brazil in the current crop, reaching 800,000 bags.

Fonte: Globo.com



NEW BRAZILIAN ORIGINS MAP LAUNCHED

The new map of the Brazilian coffee origins, developed by the Brazil Specialty Coffee Association (BSCA) after research and support from state and federal organizations, was presented during the SCAA event in Seattle. The updated map presents the 20 main coffee producing areas of the country – 6 in the state of Minas Gerais, 4 in São Paulo, 1 in the border of Minas and São Paulo, 3 in Bahia, 2 in Espírito Santo, 2 in Paraná, 1 in Rondônia and 1 in Rio de Janeiro – and also includes the Alta Mogiana and Norte Pioneiro do Paraná Geographical Indications and the Denomination of Origin of the Cerrado. The map and specifications of each coffee region can be viewed at BSCA's website (www.bsca.com.br).

Sources: BSCA and Café Editora

ORIGIN DESIGNATION OF CERRADO PROMOTED AT SCAA

The designation of origin for the Cerrado region of Minas Gerais was promoted during the 26th SCAA event held in Seattle on April 24-27. The Cerrado region covers 55 municipalities and 4,500 coffee growers with an average output in excess of 5 million bags of coffee per year. To receive the certification, issued by the Cerrado Federation, the coffee grower must comply with a series of requirements including environmental and social practices, having his coffee stored at one of the Federation's warehouses and own Arabica plantations cultivated at a minimum altitude of 800 meters (2,600 feet).

Source: Globo.com



COFFEE SEED TRAFFICKING WORRIES SECTOR

Procafé Foundation and the National Coffee Council (CNC) note the increasing illegal exports of coffee seeds from Brazil to other producing countries. This illegal practice, that usually involves varieties that took years to be developed by Brazilian research institutes and present higher resistance to pests and/or higher yields, may constitute a phytosanitary threat. Procafé estimates that approximately 30 tons of coffee seeds were smuggled in 2013, the equivalent of 120 million seeds, enough volume to cultivate 30,000 hectares (74,000 acres) of land. A share of the illegal exports is credited to coffee representatives from other countries that visit Brazil, including a few that participate in cooperation programs. In the formal market, a kilogram of seed costs between R\$ 25 and R\$ 30 (US\$11.0 and US\$13.5)

Source: Valor Econômico



Pictures of the Month



MICRO LOTS AND THE FUTURE OF THE SMALL GROWER

Strong as the trend in the direction of micro-lots is, it makes one wonder if it is a solution for the plight of small growers whose children want to live in the city and whose profits from coffee are no longer compatible with rising living costs and aspirations. Micro-lots help but are far from being a definite solution.

The problems faced by small growers in a very competitive coffee business have to do with insufficient income; micro-lots may help but they are only a minute niche market. In addition, micro-lots do not necessarily help increase productivity considering that high prices in a niche market may be an excuse to avoid lowering costs.

Even micro-lots require some sort of scale. Depending on their size, they must come from a group of small growers. Micro-lots must be consolidated for shipment because they are smaller than a container load. Even direct trade requires some minimum scale and a guarantee of supply that cannot be secured with price premiums alone. What is the solution then?

The real challenge to ensure that small growers have a viable future is to create market instruments not subsidies that enable them to achieve scale and efficiency of production *without losing their identity*. The insistence on traditional production and processing systems and on labor-intensive practices as an indicator of quality no longer guarantees the sustainability of the business. Much to the contrary, they will condemn growers to poverty in a future that is closer than most believe. Let's not embrace a romantic view of a business that is increasingly professional and competitive and is becoming more concentrated at all levels, production included!

The most obvious way to bring growers together to gain scale in buying and selling and to transfer technology is cooperatives; they however have a mixed success record. They work very well in some countries, not so well in others and are nearly absent in still others. Even in large producing countries like Brazil cooperatives perform better in some regions than in others. Most countries have specific legislation for cooperatives with minimum requirements to qualify for benefits that are usually fiscal but not restricted to them.

The alternative to cooperatives is coffee growers associations, that have fewer requirements and benefits alike and are favored in some countries and regions. However they seem to be more used for marketing, promotion and lobbying than to seek economies of scale in production, processing and sales.

Institutional and fiscal instruments aside, the easiest way to attract growers to join hands and integrate activities is to share costs, specially fixed ones. The most common ways to integrate growers are buying together inputs – fertilizers, pesticides, etc. –, sharing equipment, and selling coffee together. Obvious as this seems, it is not easy to bring growers together to do it for reasons that range from lack of confidence in one another to fear of mismanagement to lack of a legal and fiscal framework to support the operations. Central processing facilities, e.g., a pulping / washing or drying unit may act as the seed and catalyst for the development of organized groups of coffee growers.

Central mills, that enable the sharing of investment and operating costs and are convenient for micro, specialty and commercial lots alike, are often the initial reason for growers to come together. This first collective activity may then be integrated either upward, with group purchase of inputs and sharing of other pieces of equipment, e.g., spraying or harvesting, or downward, with selling coffee together, or both. The latter is the most difficult to achieve, even if the identity of the lots is preserved by traceability systems. Even if joint processing does not trickle up or down into other collective actions, the sharing of this activity alone is justified by the large economies of scale that it enjoys. For example, the investment required to equip 1,000 growers with small pulpers may be 10 to 15 times larger than what is needed to build a central pulpery of equivalent capacity, i.e., to pulp the production of all 1,000 growers!

It is high time that governments, development agencies and even sustainability standards start to devote more attention to the grouping and/or integration of small coffee growers to avoid that they either disappear or become suppliers of labor to large corporate operations in the near future. Cooperatives, associations, central milling and group certification are all on the right path but institutional and financial support and innovative forms of association are also required to accelerate the process before it is too late.

More about this subject can be read in the Outlook section of Coffidential Nos. 64 and 67.

PROCESSING OF MICRO LOTS

Pinhalense offers equipment to process small coffee lots with full preservation of their quality features and origins in individual-grower or central-milling facilities.

The smallest model in the ecoflex line or pulpers – the ecoflex-1X – offers all the features of the large machines in the same family:

- unripe cherry separation,
- lack of damage to coffee,
- no loss of parchment with pulp,
- no pulp mixed with parchment, and
- minimum water consumption.

These pulpers may be preceded by the LSC-5PX mechanical siphon and followed by the mechanical mucilage remover DMPE-0X of equivalent capacity.

The new Pinhalense line of divided SRE rotary driers has been designed to process separately micro-lots of different sizes and characteristics. Details and sizes of these driers were presented in the last edition of this newsletter (April's Confidential No. 81).



SRE DIVIDED ROTARY DRIER

to process their micro-lots themselves and need small machines like the ones presented here, there are groups of small growers and mid-size and large farmers and exporters who want to install higher capacity lines to process micro-lots separately with full preservation of quality and origin. In this case Pinhalense recommends the pulpers ecoflex-2X and 4X along with the mechanical siphon LSC-10PX and the mucilage remover DMPE-3X. Larger *divided* SRE driers are also recommended, separately or in batteries, depending on the number and sizes of micro-lots that may also call for *whole* drum SRE driers.

Large estates and exporters of all sizes, whose dry milling lines usually start at 4 tons/hour and can be as large as 12 or even 18 tons/hour, are installing smaller separate Pinhalense lines to process both micro and certified lots. They use the hullers CON, the hullers-polishers DEPOS, the size graders PFA and the gravity separators MVF with capacities in the range of 0.5 to 2.0 tons/hour, depending on the number and sizes of the lots to be processed.



ecoflex-1X

The hulling and/or polishing and size grading of micro-lots of cherry and/or parchment coffee can be carried out by Pinhalense's C2DPRC, a single machine that hulls, polishes, repasses, and separates coffee by size. Although rather new, the C2DPRC has already become the machine of choice to take micro-lots from dry cherry or parchment form to export quality coffee in several countries.

In the same way that there are small growers who want



C2DPRC

Brazilian Prices

April 30, 2014

Main Producing Regions / Farm Gate

Arabica Naturals (R\$/ 60 kg bag)

Cerrado-MG fair average quality T.6	485,00	↑
Mogiana-SP fair average quality T.6	480,00	↑
South Minas fair average quality T.6	480,00	↑

+ 9.4%

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

Cerrado-MG	525,00	↑
South Minas	520,00	↑

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

Colatina-ES fair average quality	260,00	=
----------------------------------	--------	---

BM&F (US\$/ 60 kg)

May 2014	244,75	↑
Sep2014	252,30	↑
Dec 2014	256,05	↑

Real R\$/ Dolar US\$

April 30	2,23	↓
----------	------	---

Source: www.qualicafex.com.br