

# CONFIDENTIAL

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## STRICT LABOR REGULATIONS FOR COFFEE HARVESTING

The Ministry of Labor is duly enforcing legislation that regulates rural work in Brazil, coffee picking included: all workers must be formally employed; toilette and showers must be provided in the work site; eating areas must have food heating equipment, drinkable water, tables, chairs and a roof; the employer must provide and enforce the use of personal protection equipment; and workers must be transported by buses inspected by the states' Department of Transportation.

Source: O Estado de São Paulo (Agrícola)



## US\$ 1.7 BILLION CREDIT LINE FOR COFFEE CULTIVATION, HARVESTING AND PROCESSING EQUIPMENT

Coffee growers have gained access to the Moderfrota Program that finances tractors, implements, mechanical harvesters and post-harvesting processing equipment with an interest rate of 9.5% per year. The repayment period, which is 6 years on the average, reaches 8 years in the case of harvesting machinery. The funds, provided by the Brazilian Development Bank (BNDES), can be used to finance up to 90% of the equipment purchased.

Sources: Portal do Agronegócio and Cafépoint

## FIRST PEPRO AUCTION MAY HAPPEN IN SEPTEMBER

Representatives of all sectors involved in the coffee business are due to present their suggestions for the design of the 2008 Price Equalization Premium Paid to the Producer (PEPRO) Program until August 04. Final discussions will take place in the mid-August meeting of the Coffee Policy Council (CPDC) and the first auction is expected for September.

Source: Agência Estado

## NO DUTY ON FERTILIZER IMPORTS

The Ministry of Agriculture, Livestock and Food Supply (MAPA) is negotiating with other Ministries to lower or temporarily eliminate all duty on fertilizers and their components to compensate for escalating international prices. Negotiations are complicated by standing Mercosul tariff agreements. On another front, MAPA is moving to force mining at inactive concessions held by private companies.

Source: Valor Econômico

## MINAS GERAIS CREATES COFFEE CERTIFICATION SYSTEM

The largest producing state in Brazil has created the Program "Certifica Minas", available to all coffee growers but primarily directed at small farmers. It is a very low cost coffee certification system when compared with international ones because it makes use of existing state agencies, like its extension services, EMATER-MG, that coordinates the program, and the Agricultural and Livestock Institute (IMA) that will undertake auditing. Up to 380 growers are expected to be certified in 2008, with 800 planned for 2009.

Source: Cafépoint

## ROBUSTA GROWING IN SÃO PAULO HAS TECHNICAL, POLITICAL AND BUSINESS SUPPORT

A joint document released by the São Paulo Coffee Chamber (that comprises all actors involved in the state's coffee business), the Campinas Agronomy Institute (IAC) and the Agricultural Economics Institute (IEA) indicates that almost half of the land in the state has climate adequate to grow robusta coffee. It adds that the state may produce 3 million bags per year to supply its soluble industry, that accounts for 80% of the Brazilian production, not to say the state's own consumption, that corresponds to 48% of all coffee drunk in the country.

Sources: São Paulo State Secretariat of Agriculture and Food Supply

## DARK ASPHALT GROUNDS ACCELERATE SUN DRYING

The municipality of Poços de Caldas, a high altitude, quality producer in Minas Gerais, is providing incentives for coffee growers to make new drying grounds with black cold asphalt or to cover existing ones with a layer of the same material. The dark asphalt surface absorbs heat and shortens sun-drying time by 20 to 30%. Cold asphalt does not melt in hot days and does not contaminate the product. It costs only one-fourth of the price of conventional concrete for drying grounds.

Source: Gazeta Mercantil

## EXPANDING COFFEE MARKET ATTRACTS FOREIGN INVESTMENT

American fund TPG is negotiating to purchase a 25% participation in Strauss-Elite, an Israeli coffee company that in Brazil controls 50% of Santa Clara, the country's second largest roaster, and 100% of Três Corações, another leading roaster. Other foreign players active in the Brazilian roast and ground coffee market are Sara Lee, the current market leader, that triggered the sector's concentration in the 1990s with the acquisition of brands Pilão, Café do Ponto, União, Caboclo and Seletto, and the fourth largest roaster Melitta. Concentration in the sector continues even though the country still has 2,000 coffee brands offered by 1,200 roasters.

Source: Valor Econômico

## PRICES OF ROASTED COFFEE TO GO UP

Coffee prices to consumers have not grown in the past 14 months in spite of large increases in the costs of green coffee, packaging materials, labor and utilities. The average coffee prices paid by Brazilian consumers went up by only 34% whereas labor costs grew 641%, electric energy 461% and packaging materials 222% since 1994. Inflation in the period was 230%.

Source: Revista Cafeicultura

## NEW OPPORTUNITIES FOR COFFEE WITH PROHIBITION

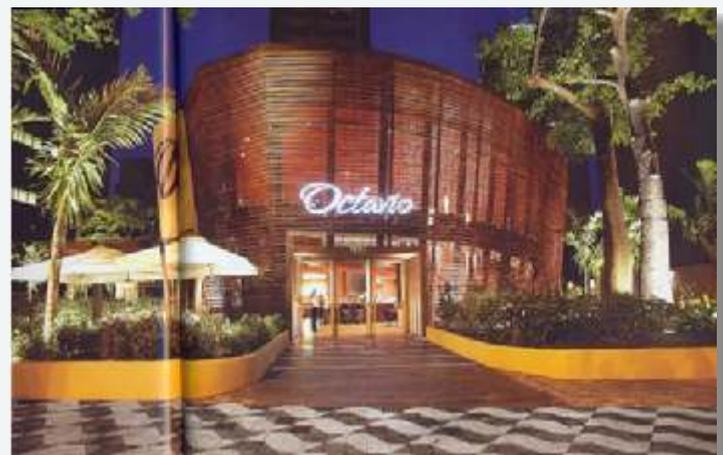
A researcher with the São Paulo Agricultural Economics Institute (IEA) has indicated that the new severe zero-tolerance drink-and-drive legislation enacted in Brazil opens up a series of opportunities to increase coffee consumption. The opportunities range from renewed interest in coffee beverages by all food outlets, specially those not specializing on coffee, to changes in drinking habits at home. The researcher predicts a great short-run interest for alternatives to alcoholic beverages, with the development of coffee menus, increased demand for baristas, and a greater interest in gourmet coffee beverages as a way to replace the glamour and social ambience usually associated with alcoholic drinks. On the other hand, he states that specific marketing actions will be required to consolidate the short-run tendencies and to make them lasting.

Source: Cafés do Brasil Network (Peabirus)

## OCTAVIO CAFÉ WINS DESIGN AWARD

Specialty coffee shop Octavio Café, located in a prime area of São Paulo City, was awarded the Brazilian edition of the International Design Excellence Award (IDEA), the most prestigious design award in the US. Octavio Café, opened in November 2007, serves coffees produced by its own Nossa Senhora Aparecida estate, in the Mogiana region of the state of São Paulo. The owner of Octavio Café bought American roaster Dallis Coffees last year and now plans to open a store in Manhattan with the same concept as the one in São Paulo, a city where specialty coffee sales are growing 15% per year.

Source: Diário do Comércio e Indústria



## CAFFEINE GOOD FOR CELLULITES AND REJUVENATION

A Brazilian beauty and plastic surgery clinic has launched the "Coffee System" line of products and treatments based on the application of coffee products, specially the extract of organic coffee, to the skin at several parts of the body. The clinic claims that caffeine and other compounds present in coffee are strong allies in the control of cellulites and skin aging. Their "Coffee System" acts on the skin, in combination with other products, to facilitate cleansing, hydration and other processes that help control fat build-up and other undesirable effects.

Source: Fator Magazine



## INTEGRITY OF PARCHMENT SKIN AND QUALITY OF WASHED COFFEE

I mentioned last month how much we learn when we visit clients abroad and when they visit us here. I have to return to the subject this month to acknowledge the visit and the teachings of a very experienced agronomist and consultant who worked in the past or is still working with coffee in areas as diverse as Congo, Panama, Hawaii, China, Mexico and Kenya.

I must report here the pleasure this agronomist experienced when we visited a farm here in Pinhal and he saw a sample of parchment coming out of the wet mill without a single defect or a single crack in the parchment skin. He asked me to hold the sample and took several pictures that he said he would use as an example to be shown to his clients. Smart as he is, the visitor then asked for a sample of dry parchment. The farmer duly brought it and the visitor said: perfect! He asked how the sample was dried and another session of photographs took place, again to be shown to his clients.

The visiting agronomist then went on to teach me something that, I must say, I have somehow overlooked in my almost 25 years in the coffee business: the importance of preserving the parchment skin intact in order to get first quality washed coffee.

As we know, washed coffee is stored involved by its parchment skin until immediately before it is exported or roasted in order to preserve its quality as much as possible. In other words, parchment coffee is only hulled shortly before shipment so that the washed coffee bean inside can benefit from the protective action of the parchment skin for as long as possible.

Our expert visitor and client was absolutely right when he got excited about the parchment samples he saw and when he made the statement that the parchment skin should always be intact, i.e, without pulper cuts, bruises, cracks, missing parts, etc, in order to ensure top quality for washed coffee. His important message was that damage to the parchment skin has irreversible and long lasting negative effects on the quality of the washed coffee bean inside it.

This quality loss happens, first and foremost, because openings in the parchment skin facilitate the entrance and attack by a series of micro-organisms that affect negatively the quality of the washed coffee bean during drying, storage and thereafter. A long list of such micro-organisms can be found in any good book about the subject. A second problem has to do with the color of the bean: cracks in the parchment skin cause the bean inside to loose color and fade with the final result that the lot will have uneven color, with dark green (undamaged parchment skin) and bleached or spotted (damaged parchment) beans. Third, the physical damage to parchment may go beyond the skin and reach the bean itself, thus originating pulper cuts, bruises and stains in the beans, and even broken beans.

The best way to avoid damage to parchment skin is to use post-harvesting processing equipment and procedures that handle parchment gently and avoid overheating, for example, immature cherry separator type pulpers, that are known to cause the least damage to parchment, last generation low friction mucilage removers, gentle revolving of coffee in drying grounds or racks, rotary driers, good temperature control and low impact transport equipment (elevators, conveyors, etc). If your parchment does not look like the photograph on the background and shows problems in the parchment skin, it is high time you consider improvements to your post-harvesting processing equipment and procedures.

### Brazilian prices

July 31, 2008 

#### Main Producing Regions / Farm Gate

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

Cerrado-MG fair average quality T.6	248,00
Mogiana-SP fair average quality T.6	242,00
South Minas fair average quality T.6	247,00

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

Cerrado-MG	260,00
South Minas	255,00

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

Vitória-ES fair average quality	210,00
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##### BM&F (US\$/ 60 kg)

Sep 2008	169,50
Dec 2008	170,30
Mar 2009	174,00

##### Dolar US\$/ Real R\$

July 31	1,56
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## ROTARY DRIERS SRE DRY FASTER, MORE UNIFORMLY AND WITHOUT DAMAGE TO COFFEE

The SRE line of rotary driers that Pinhalense offers today is the result of a development effort that started in the late 1970s and has been going on for nearly 30 years. It is no wonder that the SRE rotary machines have become the state-of-the-art driers, the equipment of choice for all quality and/or efficiency minded coffee growers and processors around the world.

Such development effort involved thermo-dynamic studies, ranging from fuel efficiency to hot-air and heat distribution in the drying drums, as well as studies of coffee motion inside the drum. The ultimate goals have been: (a) to ensure that each and every coffee bean, parchment or cherry, always receives the same amount of heat and therefore dries uniformly, (b) to make sure that coffee motion inside the drum is gentle enough to avoid physical damage, specially the cracking of parchment that often happens in other machines and on drying grounds, and (c) to enable optimum temperature control of air and, specially, coffee throughout the drying process.

These studies have been carried out not only by Pinhalense's own researchers, engineers and product development team but have also involved R&D partnerships with leading universities such as the Federal University of Lavras (UFLA) and the State University of Campinas (UNICAMP). Several patents have derived from this unique development effort in the field of coffee drying.

Regretfully, the success of the SRE driers has attracted copies that the lack of effective patent enforcement in many countries has failed to prevent. This unfair competition has forced Pinhalense to re-orient its development program in recent years. Instead of seeking the legal protection of patents, Pinhalense is now updating its driers continuously by means of manufacturing technology and specific constructive details that competitors are unable to use without the latest generation, computer controlled machines that Pinhalense has. The sophisticated materials and techniques that Pinhalense is increasingly using also require highly skilled labor and techniques that it has been developing internally for years.

The results of this new development policy are now being made evident by reports of clients who have switched, both in Brazil and abroad, from competing machines that "look like" Pinhalense rotary driers to actual Pinhalense SRE rotary driers. Such reports indicate that Pinhalense SRE rotary machines dry coffee 20 to 40% faster than the competitors' machines they had before. This means huge savings in fuel and labor in a world where all fuel prices are reaching record high prices and labor costs are increasing fast too. In addition, the clients' reports add, the uniformity of drying, the appearance and the physical integrity of parchment and cherry coffee dried in Pinhalense machines are superior, which ensure better product quality and, of course, higher prices. The lack of physical damage is specially important in the case of parchment, as mentioned in the preceding "Outlook" section. Cracked or hulled parchment exposes the coffee beans to the attack of micro-organisms with a great loss of quality. Physical damage to the parchment skin and to the coffee beans themselves may be caused by overheating due to poor heat distribution and/or by poor handling in both drying drums and in vertical driers and their recycling elevators where damage may be even more intense. Last but not least, it is always good to mention that there are Pinhalense rotary driers that have been working continuously for over 30 years!

The findings reported above have brought the demand for Pinhalense SRE rotary driers to extraordinary levels. Even though Pinhalense's factory makes 8 large SRE-150X driers every shift of 8 hours, i.e., an average of one large drier per hour, it is being forced to work overtime to meet the large number of orders from Brazil and abroad. More and more clients are making their "discounted cash flow" calculations and concluding that it is certainly worth paying somewhat more up front for a better drier rather than spending more on fuel, energy and labor and being penalized for quality faults for ever thereafter.

By the end of 2009 Pinhalense may reach the unique mark of 20,000 rotary coffee driers of all sizes and types sold in more than 50 countries around the world.

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