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COMMODITIES CORNER

Coffee Keeps on Percolating

By LISA KALLAL

Strong demand still seen for arabica beans,

ENJOYING A CUP OF JOE remains a strong consumer habit, even amid current economic worries. In fact, global consumption continues to rise by 1.7% to 2% annually. Combine this with a delicately balanced supply, and a long-term coffee rally seems to be brewing.

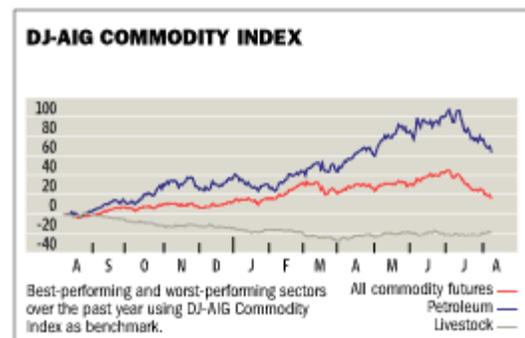
"I have not seen any indication or reduction of consumption," says Nestor Osario, executive director of the International Coffee Organization. He adds that, even if visits to the local coffee shop decline, the home and office are where the bulk of the world's java is consumed. Even in Great Britain's traditional tea-drinking society, purchases of coffee for home use were up 4% year-over-year in terms of volume and 5% in value through mid-July, according to TNS Worldpanel, a retail researcher.

Eugen Weinberg, a commodity analyst for Commerzbank, says that coffee will write "a very bullish story" over the next two to three years, as consumption growth stays constant and as production fluctuates greatly. Coffee trees produce more every other year, creating output cycles.

Because 2008-09 is an "on year" in Brazil, the world's largest producer, global output is forecast to be 128 million 60-kilogram bags, 8.5% higher than the previous year's total, the International Coffee Organization predicts. This is just above projected consumption of 125 million bags, keeping supplies finely balanced.

"There will be less of a surplus in 2008-09, followed by a deficit in 2009-10," says Andrea Thompson, an analyst for CoffeeNetwork. While the market has already largely factored in the reduced two-year cycle of supplies, Thompson says that the impact of weather will be greater, because the market is so "precariously" balanced.

ICE Futures U.S. arabica coffee (the higher-quality beans) settled Friday in New York at \$1.3580 a pound, marking a drop of 3.1% on the week but a 14.6% rise since Aug. 8, 2007. The London-traded Liffe robusta



price settled at \$2,325 a ton, down 4.3% on the week, but 27% stronger than it was this time last year. A pickup in the U.S. dollar and some options-expiries accounted for the short-term action in New York, which was mirrored in London.

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DJ-AIG Commodity Indexes

| DJ-AIG Indexes | 8/8 | 8/1 | YTD |
|-------------------|---------|---------|-----|
| Commodity Futures | 189.299 | 204.346 | 2% |
| Total Return | 377.918 | 407.819 | 4% |
| Energy | 301.814 | 332.658 | 13% |
| Petroleum | 568.746 | 616.514 | 19% |
| Livestock | 53.768 | 53.293 | -7% |
| Grains | 65.321 | 73.196 | -6% |
| Industrial Metals | 189.533 | 199.366 | 0% |
| Precious Metals | 132.520 | 143.515 | 0% |
| Softs | 57.246 | 59.418 | -5% |

Dow Jones/AIG International

Shawn Hackett, publisher of the Hackett Money Flow Report newsletter, calls coffee his favorite commodity to own right now. He expects the ICE December contract coffee to surpass \$2.50 a pound by next summer. "Brazil will need every bag of extra coffee production in 2008 just to get reserves back up to minimum buffer levels," he says.

The year-on-year rise in coffee futures has yet to spark increased plantings, as the dollar's weakness against currencies of producing countries largely negates higher coffee prices denominated in greenbacks. Input costs, especially for fertilizer, also have skyrocketed.

Growers aren't abandoning coffee plantations, but there are no economic incentives to plant more trees, says the International Coffee Organization's Osario. Trees need several years of growing time before they can produce. And, Osario adds, finding labor to pick the coffee is becoming a problem in Brazil and in Vietnam, the world's second-largest producer. As more of Vietnam's population moves to the cities, annual output there is expected to be capped near the current level of about 18 million to 20 million bags.

CRUDE-OIL PRICES AGAIN HELD huge sway over markets. For more, see [Follow-Up](#).

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