



Brazil Arabica Review



Arabica production for the 2009 harvest is expected to fall 8.00 million bags to 31.8 million bags; this represents a decrease of 15%.

- Average on cycle arabica production has been growing at 10% per year.
- Average off cycle arabica production has been growing at 8% per year.
- Arabica production under current land under harvest can reach 44.0 to 47.0 million bags for the 2010 harvest; this would equate to a yield of 26 to 28 bags per HA.
- According to the USDA, bearing trees expanded from 2.106 thousand trees per HA to 2.662 thousand trees per HA.

Wide spread rains across the Arabica producing regions is expected:

- to have a negative impact on the current quality; reducing amount of fine cup and increasing the presence of Riada cups.
- to result in the lowering of the current production from 33.8 million bags to 31.8 million bags, as mentioned above.
- to have a very good impact on the 2010 harvest, which warrants watching during the next 4 to 6 weeks.

Arabica exports have been growing at an average of 6% per year.

- September – August 2009 exports total 26.95 million bags, a 5.62 million bag increase.
- Washed – Semi Washed arabica exports is estimated to reach 2.00 million bags plus.

Arabica stocks bottomed at 7.6 million bags during April 2009; and a larger super crop expected during 2010 has paved the way for some retention scheme.

Government plans to withhold coffee upto 10 million bags

- 3.0 million bags were sold through options program
- 300 million Brazil Reals is allocated for the purchase of coffee for public stocks. This is limited to 1,000 bags per producer for a minimum price of 261.69 Reals per bag. This represents 1.1 million bags.
- 697 million Reals has been approved to exchange debts for the 2008/09 coffee



Colombia Review

	06/07	07/08	08/09 Est.	09/10 Est.
Carry In Total Stocks				
Origin Carry Over	1,492,737	1,312,191	1,190,628	838,499
Certified Stocks	352,094	418,063	219,148	1,035
Total Carry In / (Deficit)	1,844,831	1,730,254	1,409,776	839,534
Production Estimate	12,187,000	12,515,000	9,202,900	10,307,248
Exports	(11,167,546)	(11,556,563)	(8,755,029)	(9,455,431)
Dom. Consumption	(1,200,000)	(1,200,000)	(1,200,000)	(1,200,000)
Imports	0	120,000	400,000	370,000
Ending Stocks	1,312,191	1,190,628	838,499	860,316
Ending Certified	418,063	219,148	1,035	1,035
Total Ending Stocks / (Deficit)	1,730,254	1,409,776	839,534	861,351
Change In Certified Stocks	65,969	(198,915)	(218,113)	0
Change in Total Stocks	(114,577)	(320,478)	(570,242)	21,817
Total Disappearance	(12,482,123)	(12,957,041)	(10,125,271)	(10,263,615)

Colombia's 2008/09 production was revised down 1.37 million bags to 9.2 million bags; this represents a reduction of 26%.

Primary reasons for the 2008/09 production were

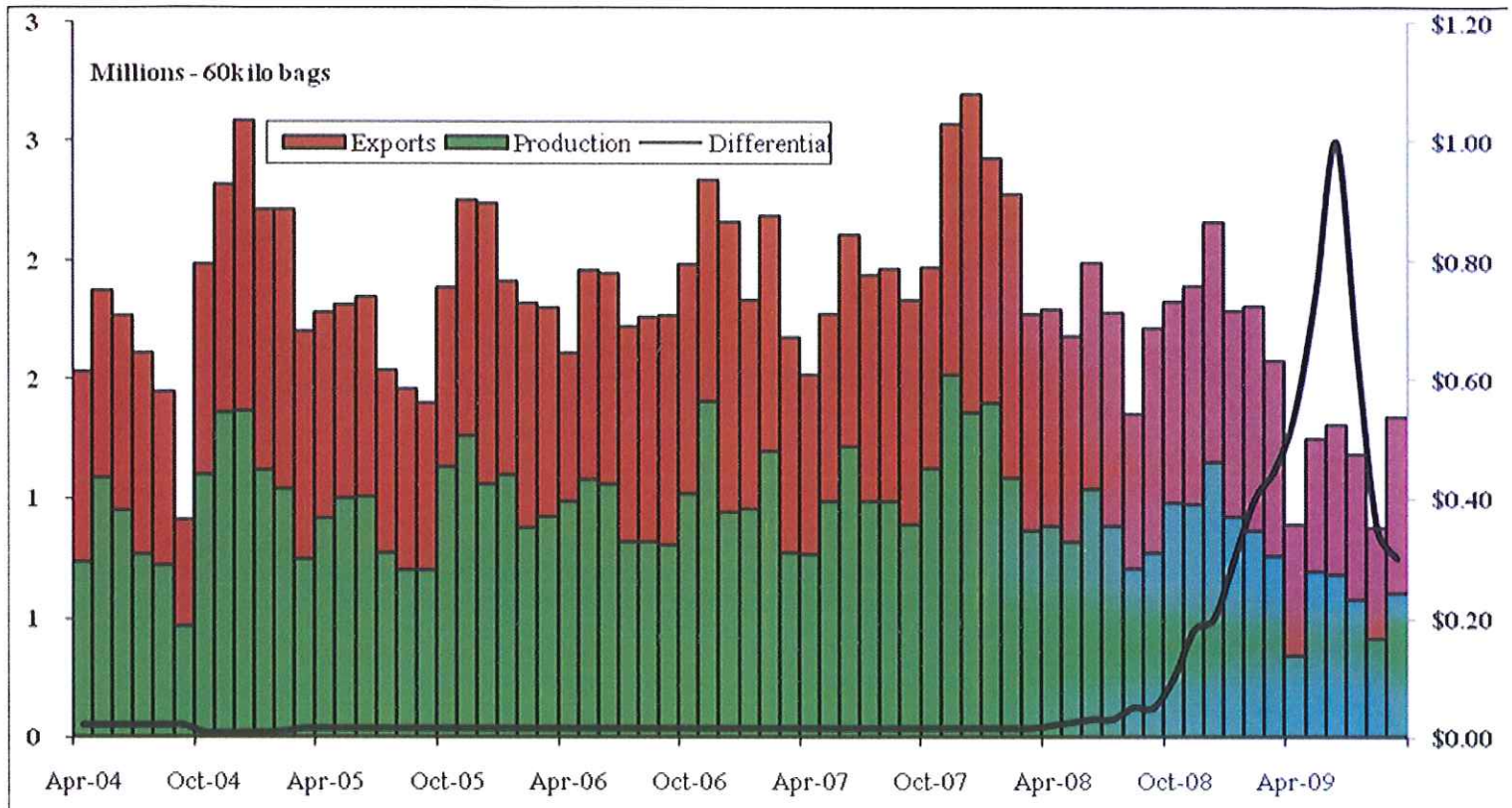
- Prolonged rains from October thru April 2009, a result of La Nina
- Tree Renovation Program

2009/10 production is forecast to increase 12% to 10.3 million bags:

- return of dry weather in May helped promote the flower setting, resulting in a late September harvest, however the risk of rust disease is present
- the main crop is expected to produce 58% of the crop this year, down from the 62% it has averaged during the last 12 years

The Tree Renovation Program which is aimed nationwide has set an ambitious goal to reach 17 million bags by 2014.

- It has targeted 211 thousand HA to date and is expected to continue through 2013/14 crop aiming to bring down the average age of the trees to 8 years.
- Will continue to target smaller, less productive family farms which has started two years ago.
- The Huila region and to a lesser extent the Nariño and Tolima areas have experienced production improvements because of the program as well as being a low cost producing region

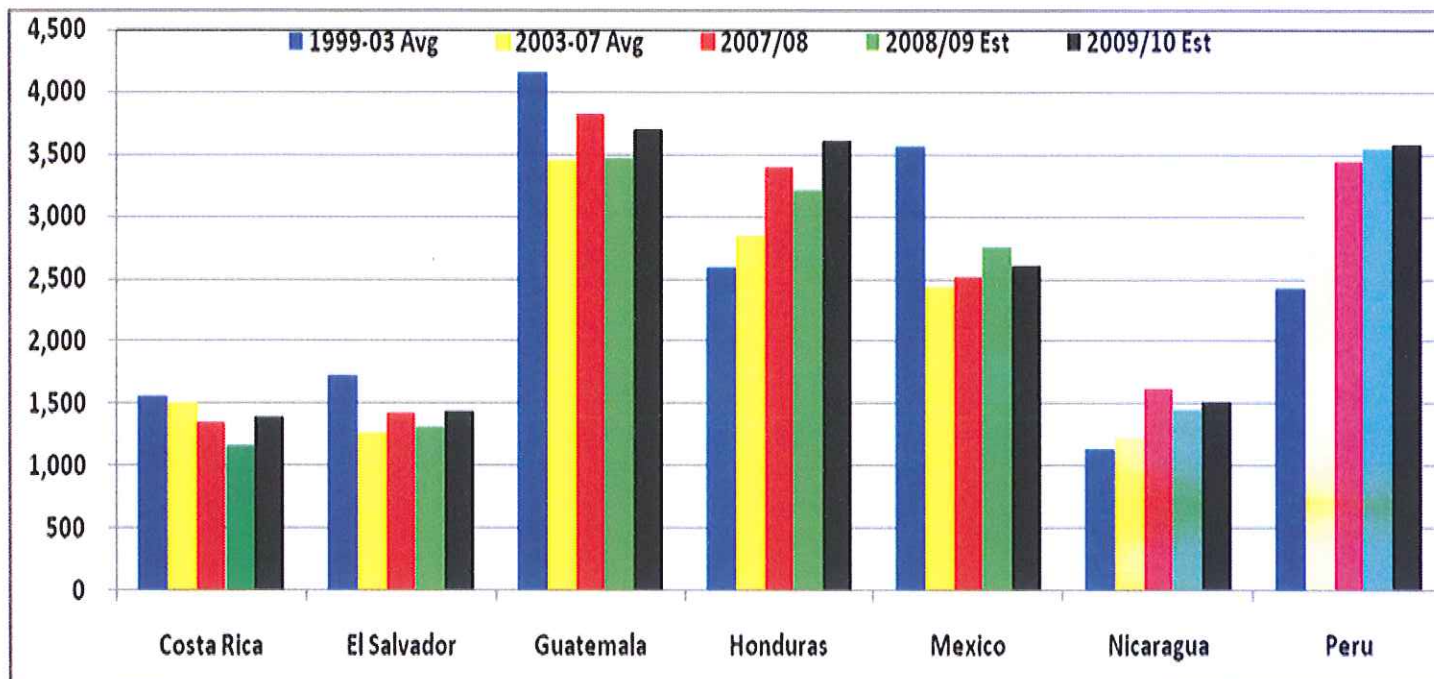


Exports for 2009/10 are expected to increase 0.70 million bags to 9.455 million bags.

- The 08/09 exports of 8.755 million bags, represents a decrease of 2.80 million bags from the previous year.
- The reduced availability of Colombians was bridged by:
 - 218 thousand bags of Colombian ICE Certified coffee, a majority of which was re-imported into North America
 - imports from Ecuador and Peru are rumored to have increased by 280 thousand bags into Colombia
 - Europe reverted to a greater percentage of African milds, while North America used more Central Arabicas as well as Brazilian washed / semi-washed coffees...the total substitution may have been as much as 3 million bags
- due to the volatility of differentials, Colombia's 2009/10 new crop sales are lower by 30% - 35% as of the end of August compared to the same period last 2008
- Industry has made provision's to substitute fourth quarter Colombians which is evidenced by:
 - the small accumulation of spot Colombians
 - the narrowing of nearby differentials vs. deferred differentials; at its widest, the nearby – deferred differential spread was 60 cents, while it has recently narrowed to 4 cent premium in favor of the nearby position



Latin American Arabica Exports



Central American production for the:

- 08/09 crop fell 8% down to 17.3 million bags, the result of normal production cycle downturn and La Nina induced dry weather last year.
- 09/10 crop is forecast to increase 5% to 18.1 million bags.
- Costa Rica's 09/10 production is under close watch because the dry weather has lasted longer than normal resulting some uncertainty for this year's Tarrazu region, while the other regions are not expected to be greatly impacted.
- The El Nino dry weather needs to be watched in Costa Rica as well as rest of Central America, as it may effect how fertilizer is absorbed and how the trees develop for the 2010/11 crop.
- Costa Rica, Guatemala, and Nicaragua are seeing the an earlier harvest indicating, while the rest of Central America is likely another 4 to 6 weeks away.
- While Costa Rica's quality has recently come under review due to the weather.
- Guatemala, Nicaragua, Honduras and El Salvador are all expecting to see an improved quality across the board compared to the 08/09 crop which saw better quailty in the low lying regions compared to the higher altitude coffees.

Central American exports are expected to increase to 700 thousand bags to 14.2 million bags.

- Mexico is the only country expected to see lower exports during the new season
- Honduras is forecast to increase exports 12% to 3.60 million bags, the most among Central America.



- Lower Colombian supply diverted approximately 1.0 million bags worth of North American demand to Central America; the pyramid below depicts the acidity hierarchy based on current blends.



- Costa Rica, Guatemala and Nicaragua experienced the earliest and largest price increase due to demand, while Mexico experienced the least increase demand and price increase.

Arabica consumption in consuming countries has steadily been growing, mostly in Asia and Eastern Europe.

In thousands (Oct-Sept)	2006/07	2007/08	2008/09	2009/10
Mild Arabica	30,800	33,300	31,700	31,700
Brazil Washed/Semi Washed	0	0	2,000	2,000
Brazil Naturals	24,800	22,400	22,900	22,900
Total Arabica Consumption	55,600	55,700	56,800	56,800

Export Market Share for Latin American Mild Arabica:

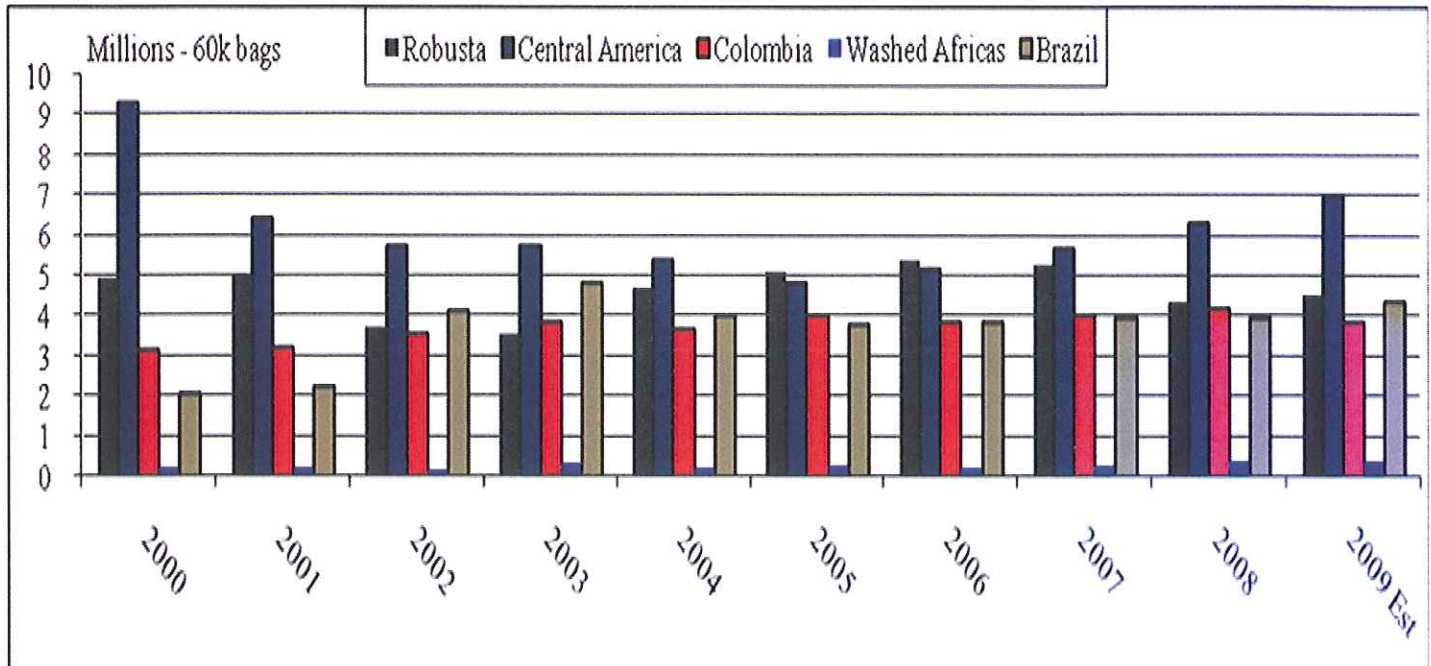
- Central America's share has fallen from 63% of total in 99/00 crop year to 53% in the 09/10 year.
- Peru's market share has increased from 7% to 12% for the same time period.

Clearly the US market has been replacing Central Mild Arabica with Colombians and we expect this to reverse in 2010

- US imports of Colombians are expected to decrease 344 thousand bags during 2009, concealing approximately 200 thousand bags of re-imported Colombians from Europe.
- Since 2000 the US Colombian imports increased 1.026 million bags, while Central imports decreased 3.012 million bags.
- US coverage for 2009 is complete and very little demand exists, we expect roasters to buy a larger share of Central Arabicas which are currently 2 to 10 cents cheaper than their Colombian counterpart.



US Import Review



ICE Certified Coffee:

- disappearance since October 2008 – August 2009 is 1.7million bags compared to 1.3 million bags the previous year due to the 2009 Mild supply constraints
- approximately 13% of the stocks at the end of August were less than 1 year old, however a majority of these coffees are regarded lots and have actually been sitting around closer to 2 years or more

Conclusion:

Brazil differentials will remain unchanged through the first quarter 2010 and make new lows before second half of 2010:

- Brazil's lower 2009 harvest is expected to be followed by a bumper 2010 crop.
- Industry and trade are well covered; the exporters are assumed to be the big short for next year.
- Government programs to withhold stocks, will impact the local market more than the international because of the coverage already taken
- There is a large surplus of unsold Brazilian Arabica in Europe and North America.
- The ICE Certified Arabica will keep Brazil differentials from getting too far out of line. The current average ICE Certified discount is 11 cents and is expected to fall to 13.25 cents by March 2010.



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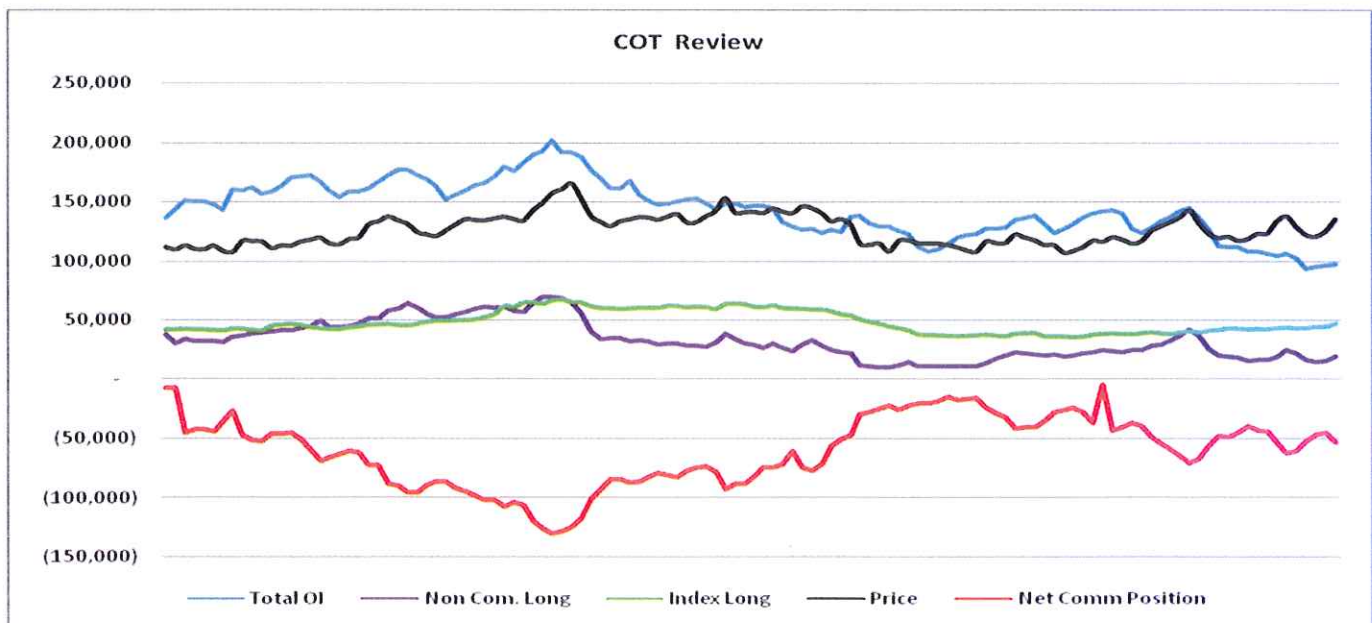
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Colombian differentials will continue to erode, probably faster than I can write about. The first half of 2010 the range will be + 18 to +10 c/lb FOB while the second half of 2010 differentials can be as low as + 8 FOB.

- Prompt shipment differentials compared to January forward differentials have eroded 15 cents in less than a week, which will further weigh on forward differentials as the crop comes in to very little demand.
- Farmers/exporters have very little sold beyond December shipments
- US and European roasters can be expected to substitute as much as 2.00 million bags of Colombians with Centrals and African/Asians, respectively.
- Lost market share ahead of a renovation program is expected to increase production of Colombians by 50% in two years.

With the Central American crop starting about a month early expectations are for differentials to come down to roasters' bids before the end of 2009 and make a low during the first quarter of 2010 before stabilizing.

- Very little of the crop has been committed forward.
- An early and slightly larger crop coming in and should weigh on the nearby differential.
- Expect a smaller percentage of the crop to be available in the second half of 2010.
- Approximately 87% of the ICE Certified stocks will fall into a Brazil category and not a fresh MILD Arabica.



Total open interest has been declining steadily since peaking at 201,843 lots back in February 2008:

- For 2008 the average open interest was 147,972 lots, ending the year at 122,856 lots.
- For 2009, the average open interest has averaged 123,065 lots, last tally was 96,285 lots.



Non-commercial OI averaged 18% and 21% of the total OI for 2009 and 2008, respectively.

- At it's peak, non-commercial OI represented 34% of the OI.
- As of September 15, it represented 20% of the total OI.

Index fund OI averaged 32% and 38% of the total OI for 2009 and 2008, respectively

- When market prices and OI were at their highest, Index Long represented only 33% of the total OI
- As of September 15th the index fund represented 48% of the total OI, a high mark!

Net Commercial Position averaged 35% and 48% (short side) for 2009 and 2008, respectively.

- As of September 15th, net short totaled 56% of the OI
- The commercial longs and shorts are both 10% points below there normal for this time of the year. A result of the lower volume of physical business committed for 2010.

Near Term Bearish argument for the futures market is:

- high percentage of Index Longs
- the misalignemnt of origin nearby selling against deferred industry buying.
- Bumper Brazil crop during the second half of the year.

Bullish argument for the futures market is:

- First half of 2010, should see more industry buying
- Low open interest leaves substantial room for the non-commercials to add to their position (I believe if they add to their position, it will be from the long side).
- Global economic improvement should mean higher commodity prices across the spectrum.