

Monday, February 26, 2007

BUY ▲

A POTENTIAL 60% RISE IN THE OFFING

COFFEE happens to be one of most traded agriculture commodities derivatives all over the world. We believe coffee has just begun a bullish rise which may potentially increase the prices by over 60% this year from the present levels. This year 2007 may turn out to be one of the most positive years in the long history of Coffee futures trading

This note contains the fundamental reasons for this expected movement in coffee prices. We have also technically justified the idea as the charts look to be set for a tremendous rise.

FUNDAMENTAL SNAPSHOT

The following fundamental points support the triangle breakout pattern which shows a bullish outlook for Coffee in the year 2007.

DEMAND FACTORS:

- ☞ *Coffee's demand is expected to grow at a faster pace globally. Roughly 75% of the total consumption is from the developed world. However, the developing world is expected to show a significant contribution to the consumption.*
- ☞ *Although most of the developing countries are primarily seen as tea consuming countries, emergence of coffee shop culture, growing per capita income and a favorable shift in demographics are expected to support demand from developing countries.*
- ☞ *For example an increase in number of Starbucks stores in China and surrounding area from less than 100 to nearly 450 in 2006, has increased the company's positive growth outlook for the region.*
- ☞ *The 2008 Olympics is also seen as one event that will help increase the demand potential in the region. Major International brands are expected to showcase western coffee products and consuming habits assertively to develop a significant demand pool.*
- ☞ *Traditionally the focus of coffee producing countries like India and Vietnam had been to promote the variety of domestic brands in the International markets. However, Governments in these countries are taking measures to increase domestic demand for a healthier and stable market conditions.*
- ☞ *Since a peak in 1940s, per capita coffee consumption in developed nations like US showed a continued fall. Then again, nearly two third of the global consumption is centered in developed nations and has shown a consistent growth of 0.5% a year from 1995. This rate is expected to sustain or increase in the coming period.*

SUPPLY FACTORS

- ☞ *Due to sustained lower prices in the past, producers had shifted towards 'Commoditization' of coffee by producing lower qualities to cut down productions costs. However with the evolution of coffee culture consumers in Developed countries are more informed and their preferences seem to have moved towards higher quality coffees. In this scenario, producers are shifting production to higher qualities to take advantage of better margins.*
- ☞ *If this trend in production sustains then it could weigh on the yield growth as higher qualities yield much less per hectare than the lower ones. This could affect the supply in a way to keep prices on a higher side.*

TECHNICAL OUTLOOK



Over a period of last 3 years coffee futures have formed an almost picture perfect classic symmetric triangle pattern and has broken out of it. During December 2006, prices broke out of the triangle pattern at 115 levels and saw some follow through buying. However buying receded and the price snapped back to the upper line of the triangle and held there. This week the prices have held exactly above the breakout line and have shown a steep rise with the prices running away higher during the last two days by over US cents 8 per pound.

The price breaking out of triangle and snapping back towards the breakout line and subsequently holding above the line confirms the classic breakout action.

RSI hovers well below the over sold region as the momentum has begun to pick up only during the last few days. RSI at 55 indicates a lot of room on upside and provide ample scope for price action to intensify North-wards.

Based on the technical and fundamental analysis, the snapshot of which is given above we believe Coffee futures on NYBOT (near month) may be set for a rise towards \$1.95 per pound from the present levels of \$1.19. **We suggest buying COFFEE futures (NYBOT MAR contract) near \$1.19 levels for a target of \$1.55 and \$1.90 with a stop-loss below \$ 1.10.**

The call requires the contract to be rolled forward and the roll-over premium, if any may add to the cost.



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