

Pepper

MONDAY, JULY 21, 2008

OVERVIEW

NCDEX	
RTRS code	NPE:
Bloomberg Code	M3

Current Market Price	
Spot Garbled	14600
Spot Un-Garbled	14000
NCDEX Aug	14705
NCDEX Sep	15050
Vietnam (FOB)	\$3450

INSIDE THIS ISSUE:

GLOBAL SCENARIO	2
SUPPLY	3
DEMAND	8
ENDING STOCKS	10
CONCLUSION	11
ANNEXURE & DATA	12

"Black Gold" (Black Pepper) has performed exceptionally well during first two quarters of 2008. India has always been first to commence pepper harvest, but this year it got delayed by almost a month due to unseasoned rains. This created ripples in the global pepper market which was already riling under supply crunch. As a result of which prices spiralled in domestic market by almost 9% (i.e.) from Rs.13,500 during December'07 to Rs.14,700 in March'08, with prices making high of Rs.15,400 during February'08 and at present quoting at Rs.14,500.

On the international front Indonesia has entered its pepper harvest, whereas in case of Brazil harvesting activity has been delayed by almost a month. Normally small picking in Brazil starts in the month of July, but due to unseasoned rains during June it has been delayed and would start from mid August.

In case of Vietnam, pepper harvest got completed during the previous month (June) which started after Tet holiday's (March). And as per Vietnam Pepper Association total crop is expected to be between 85,000-87,000 tone, due to pests and diseases affecting plantations. Even we downgrade our crop estimates for Vietnam by 10% from 1,00,000 tones to 90,000 tone. But more

than figures present by Vietnam Pepper Association.

During 2005-06 we have seen international pepper prices being suppressed as Vietnam harvest sets in, reason being farmers use to offload it stocks as and when it was harvested. But since last year due to lucrative Coffee prices farmers are yet to release their pepper stocks as their financial needs are taken care off and they are in no hurry to release them. Average export price for Vietnam's Robusta Coffee during (Oct'07/June'08) was \$2,041/MT (FOB), this is almost 35% higher as compared to same period during previous year. And in keeping track with higher export prices even local prices rose by 37% from 23,366DONG to 32,022DONG during the period mentioned above.

Due to which pepper exports up to April 2008 were reported to be at 23,722 tones (21,350 tones of black and 2,372 tones of white pepper), down by 18.8% compared to same period last year. Reason being expectation of better prices since Vietnamese pepper fetched an average price of \$3,520 a tonne during the first four months, or 31% higher than the average for the same period in 2007.

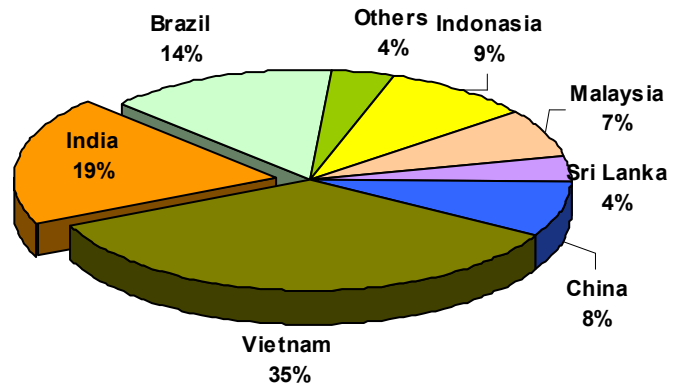
GLOBAL SCENARIO

In our previous pepper update we estimated global output for the current season (i.e.) 2008 at 2,63,000 tones down by almost 3% as compared to 2007 in which it was reported at 2,71,000 tones. We downgrade the production figures to 2,60,000 tones down by 1% compared to previous estimates and down by 4% as compared to 2007. Reason being Indonesian crop is expected to be tad lower at 22,000-23,000 tones from 25,000 tones due to floods during the start of the year.

Lower production is expected to keep demand-supply disparity intact as global pepper consumption has been increasing because of western countries experiencing a consumer trend that favors greater consumption of spicy foods. Furthermore because of fast paced life consumers are obliged to eat out of home due to lack of time. In European Nations 50% pepper is used for preserving meats. Out of remaining 40% goes towards household consumption and the remaining 10% is divided amongst medicines, perfumes, and health & beauty products.

Demand by consuming nations leaving aside the producing nations is estimated to be at 18,750mt per month and consumption by producing nations is estimated to be at 6,500mt per month. If we sum up the demand annu-

Production Contribution Countrywise 2008 e

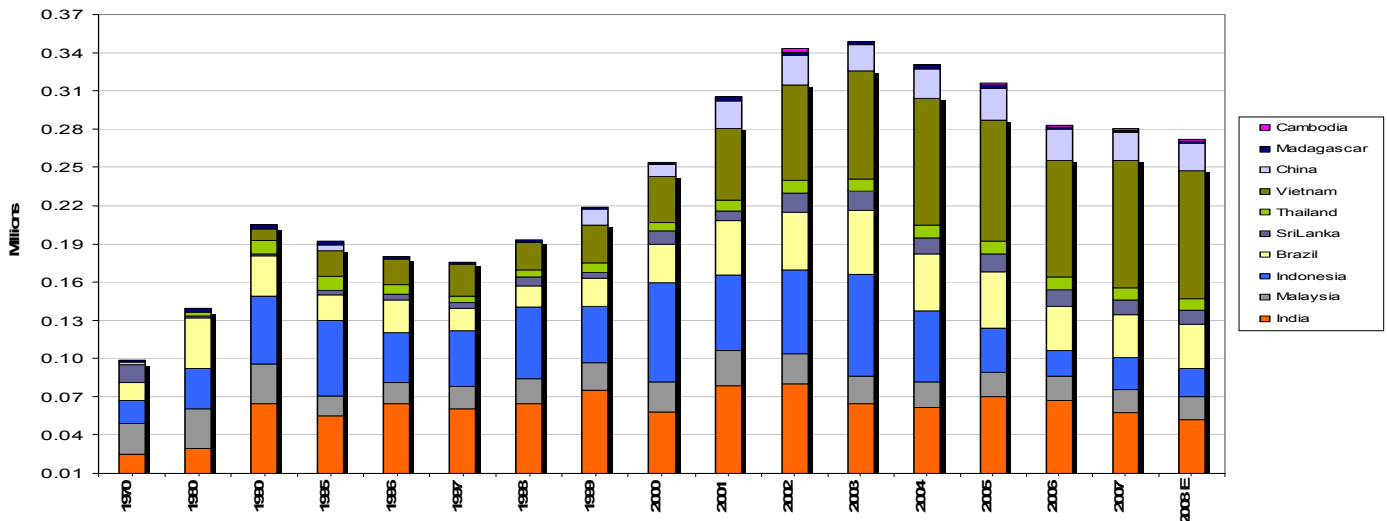


Source: ARG Research

ally than total consumption stands at 3,03,000 tones.p.a. Whereas total production for the current year is estimated to be at 2,60,000 tones.

As a result of which globally prices spiraled as evident from IPC Composite Price for the period (Jan-Apr) 2008. Black pepper composite prices rose by 26% as compared to previous year for the period mentioned above and White pepper composite prices rose by 41%. Hence, current uptrend is very much justifiable and is expected to continue until demand-supply gap gets narrowed.

Country Wise Pepper Production



SUPPLY

Harvest Schedule of Pepper for 2007-08

	DEC	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV
VIETNAM												
INDIA												
BRAZIL												
INDONESIA												
MALAYSIA												
SRI LANKA												

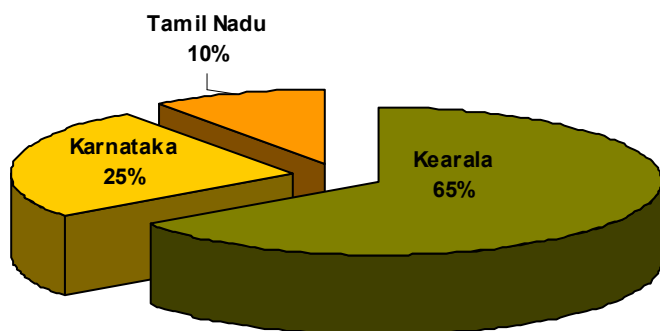
Small Arrivals

Peak Arrivals

INDIA

India completed its pepper harvest in March and production is expected to be in the range of 51,000-52,000 tones. With major contribution coming from three important regions mentioned below.

Production Contribution Statewise India (2008)



Source: Spices Board

During the initial stages of harvest there were general consensus that this year crop would be around 45,000-47,000 tones reason being unwanted rains during the month of October, which delayed harvest by almost a month. Furthermore it lead to severe dropping of berries especially in Coorg district whereas in case of Wayanad plantations were hit by wilt disease. But then climatic conditions became conducive and as a result production estimates also improved, even then it is down by almost 10% as compared to previous year. Since India is the first to conclude its harvest among all the other origins and for that reason looking at

Indian Pepper Crop Estimates (Jan-May) 2008

(Source: Spices Board & ARG Research)

State	District	Production (Mt)	
Kerala	Idukki	16,575	
	Wayanad	8,951	
	Others	7,624	33,150
Karnataka	Coorg	8,925	
	Chickmagalore	1,530	
	Others	2,295	12,750
Tamil Nadu			5,100
Total			51,000

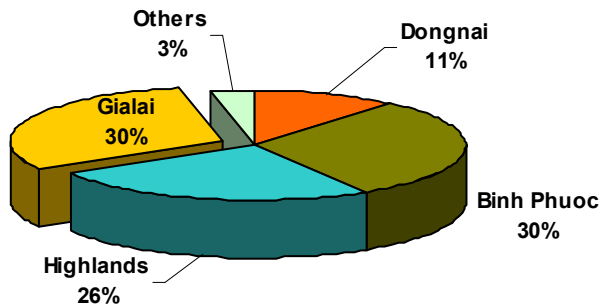
the gains made during the previous year farmers were reluctant to part with their stocks on expectation of better prices.

As a result of which arrivals during the month of January was reported to be at 10-15 metric tones on daily basis as compared to average arrivals of 30-35 metric tones during previous years. But gradually arrivals increased and during the month of February to 150 metric tones because Vietnamese markets were closed for Tet holiday's and India was the only source of supply. As a result of which good overseas demand shifted to India, export figures released recently for the period April-May'08 were reported to be at 5,750 tones. This is up by 17% compared to same period during the previous year.

VIETNAM

Normally Pepper crop is harvested after Tet holiday's and so was the case this year, it started in the month of March but due to unseasoned rains the pace of arrivals was very slow. Furthermore, situation of pests and diseases such as Slow Wilt and Quick Wilt was reported in some provinces such Binh Phuoc and Dong Nai. As a result of which Viet-

Production Contribution Provincewise Vietnam (2008 e)



Source: ARG Research

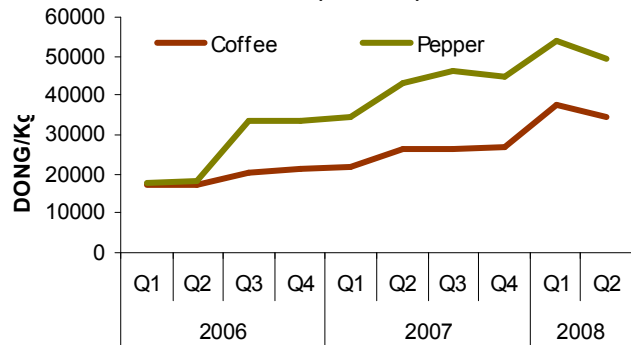
nam Pepper Association downgraded its final crop estimates to 85,000-87,000 tones from 90,000 tones previously. On the back of which even we downgrade our crop estimated by 10% from 1,00,000 tones to 90,000 tones due to above mentioned reason.

According to Vietnam Pepper Association Gia Lai province Chu Se district this year is reported to have a bumper pepper crop. Yield on an average was reported to be at 15 tones per hectare, the highest ever yield in Vietnam as well as in the world. Reason being good spacing between plantations as a result crops gained the most sunshine and pestilent insects could be avoided.

Until 2005-06 global pepper prices were suppressed as and when Vietnam started its harvest and Vietnamese farmers were not able to reap benefit out of higher prices. But form 2006-07 with the urge from Vietnam Pepper Association farmers have started holding back its pepper crop and farmers are in no hurry to offload their stocks.

This was reflected in export figures up to April 2008, total export from Vietnam was 23,722 tones (21,350 tones of

Vietnam Quarterly Pepper & Coffee Prices (2006-08)



Source: ARG Research, Reuters & Bloomberg

black and 2,372 tones of white pepper), down by 18.8% compared to same period last year. Reason being farmers holding back their produce to benefit out of price rise during later part of the year. As their financial conditions (holding capacity) have improved a lot due to lucrative Coffee prices.

Local coffee prices during (Jan-June) 2008 rose by 36% as compared to yearly average prices of 2007 and by 43% when compared to Jan-June during the previous year. Whereas pepper prices during the same period rose by just 11% compared to 2007 yearly average prices and 15% during the period Jan-June. Such a phenomenal rise in coffee prices was due to good export demand as globally crop conditions were bad. Even than pepper export shoed some recovery and total export for first six months of 2008 stood at 47,000 tone (41,930 tones black pepper and 5,070 tones white pepper)

Total pepper supply is expected to be at 1,00,000 tones in which carried over from 2007 is 10,000 tones. Out of this total exportable quantity is expected to be at 87,000 tones.

Vietnam Pepper Crop Estimates 2008 (Source: ARG Research & Trade Sources)	
Provinces	Production (Mt)
Dongnai	10,000
Binh Phuoc	27,000
Highlands	23,000
Gialai	27,000
Other	3,000
Total	90,000

INDONESIA

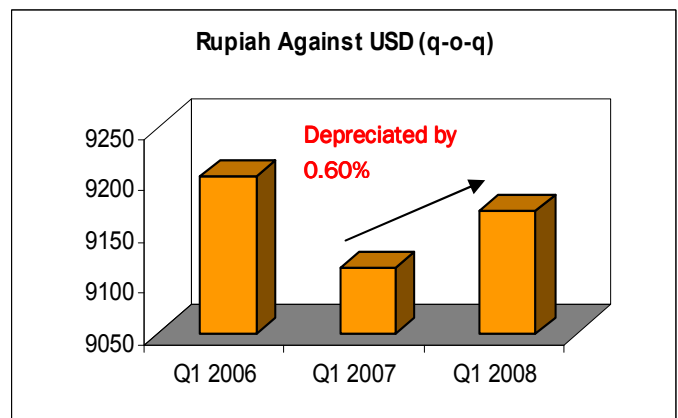
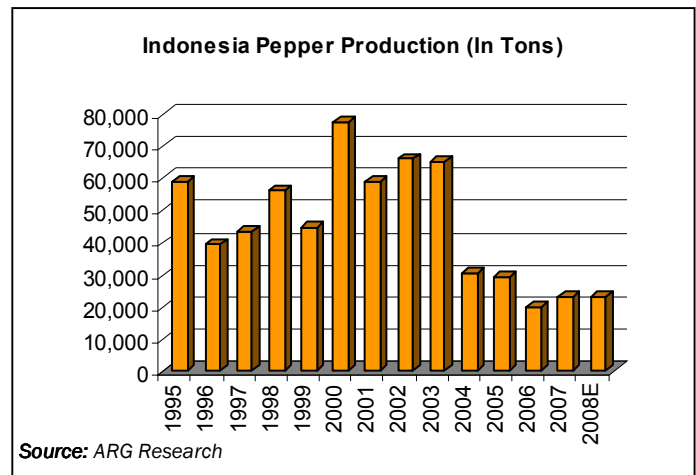
Vietnamese pepper harvest got over in the month of June and Indonesian pepper harvest has started from July onwards which will continue until September. In our previous update we had estimated Indonesian pepper crop to be at 25,000 tones, but we downgrade our target by 12% to 22,000-22,500 tones. Reason being floods which had hit the country during the start of this year, as a result of which productivity is expected to plunge.

Indonesian crop does influence the prices in the global market, because after Vietnam it is the cheapest source of pepper. And whenever its harvest sets in global prices have dipped as evident from IPC Composite Prices during 2007. Composite Black Pepper prices declined by almost 8% during the month of August'07 from July'07.

But this year impact on prices is expected to be minimal as Indonesia pepper stocks are already exhausted. As it has already shipped out bulk of its stocks to US as evident from the graph. Import to USA from Indonesia during the period Jan-March'08 increased by 374% as compared to same period during 2007 (i.e.) from 1,590 tones to 7,534 tones. This is highest ever in last five years, reason being Indonesia currency (Rupiah) depreciated against USD by 0.60% as compared to same period in previous quarter. This made Indonesian Pepper cheapest against all the other origins especially Brazil and India where currency appreciated against USD by 18% and 10% respectively.

Furthermore, Indonesian pepper market is controlled by three big traders from Indonesia who have a strong hold due to money power and drives the market as they want. And these people released their stocks looking at the price trend and global supply situation. Hence, to take advantage of recent prices surge it seems that they have offloaded most of their stocks.

Total supply is expected to be at 29,000 tones in which carried over from 2007 is 6,000 tones. Out of this exportable quantity is expected to be at 18,000 tones.

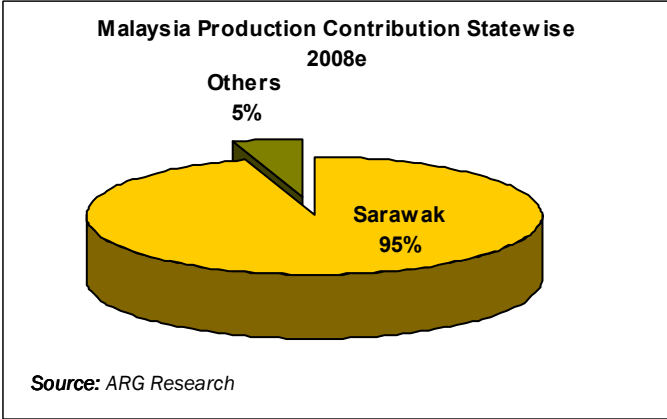


MALAYSIA & SRI LANKA

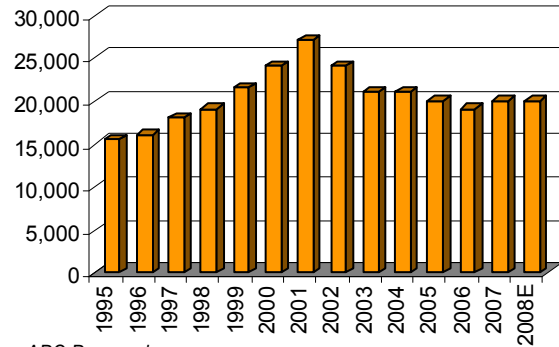
Both the countries have their own significance in the world pepper market. Production hover between 20,000-25,000 tons for Malaysia and 10,000-15,000 tons in case of Sri Lanka. Sri Lankan pepper does not influence world pepper prices directly as major portion of its produce is exported to India and which has repercussion on world prices. Whereas in the case of Malaysia major portion of it goes into white pepper conversion for that reason its importance to influence the prices is reduced.

Malaysia started its pepper harvest in the month of June which will be extend up to July-August. Almost countries 95 % of countries pepper production comes from the state of Sarawak . Growing area concentrated in the Kuching, Sri Aman, Sibiu, Sarikei and Bintulu divisions. For the current year production is expected to be in same line as estimated in our previous update (i.e.) in the range of 18,000-20,000 tones. Total supply is expected to be at 44,700 tones in which carried over from 2007 is 24,700 tones. Out of this exportable quantity is expected to be at 20,000-21,000 tones.

Whereas in case of Sri Lanka harvest got completed in June. Production for 2008 is expected to be in same line as estimated in our previous update in the range of 14,500-15,000 tones. Total supply is expected to be at 16,300 tones in which carried over from 2007 is 1,300 tones. Out of this exportable quantity is expected to be at 9,000-9,500 tones.

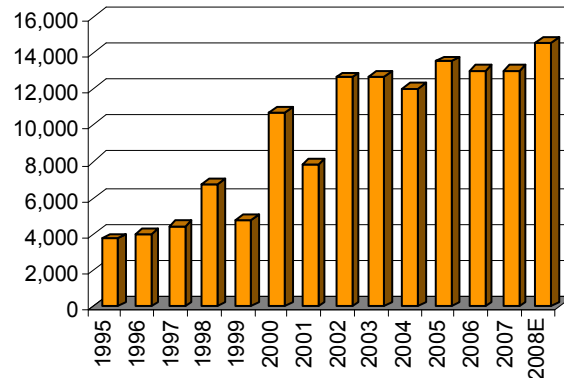


Malaysia Pepper Production(In Tons)



Source: ARG Research

Srilanka Pepper Production (In Tons)



Source: ARG Research

BRAZIL

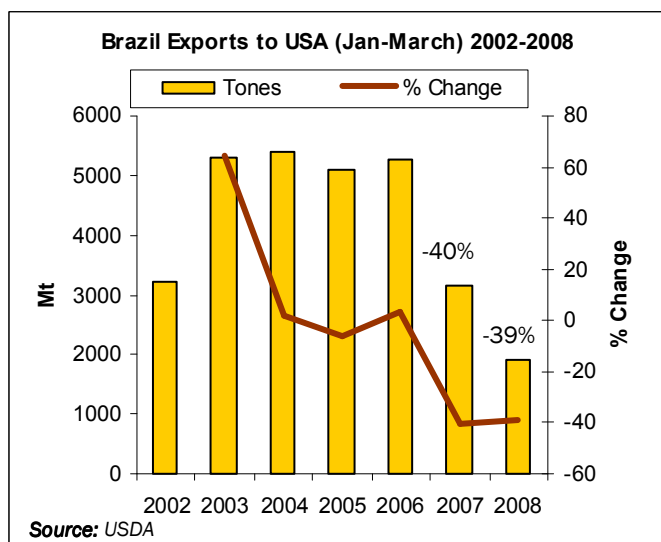
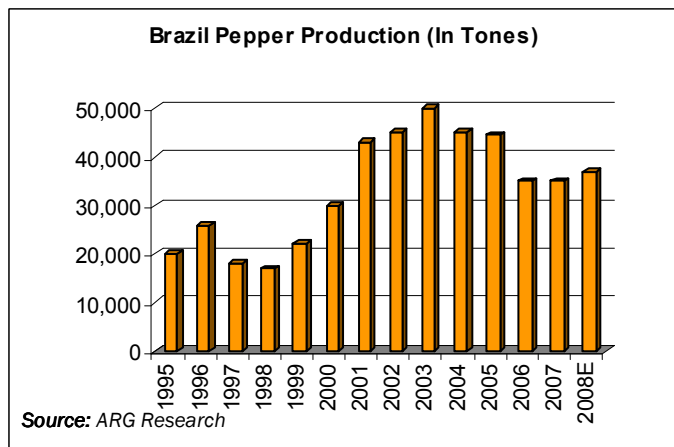
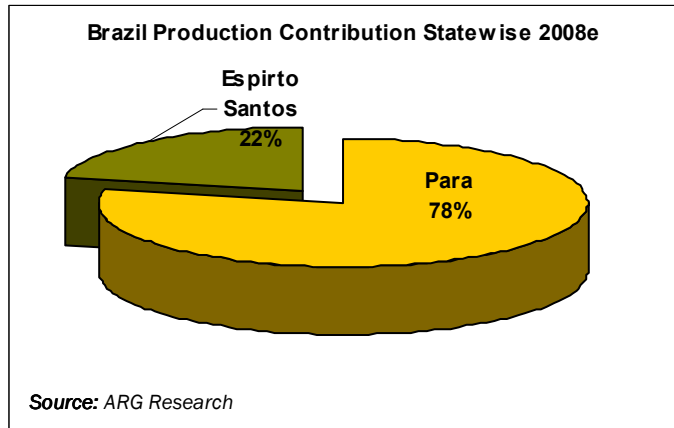
After Indonesia and Malaysia pepper harvest Brazilian pepper harvest sets in. Normally small picking in Brazil starts in the month of July, but due to unseasoned rains during June it has been delayed. It would start from mid August and get extended up to November/December. Global pepper harvest gets concluded after Brazil harvest, as it is the last country to harvest its pepper crop. For 2008 season Brazil production is estimated to be in the range of 36,000-37,000 tons.

Brazil pepper production is primarily concentrated in the region of Espirito Santo (South Brazil) and Para (North Brazil). In Espirito Santo there are two crops stages, first stage is from May/June and the second stage Sept/Oct/Nov/Dec. Very minimal crop is harvested in the first stage and the maximum of produce is harvested during second stage. During the previous year Brazil crop was heavily impacted as Espirito Santos and Para both had reported a crop damage in second stage due to dry climatic condition.

Due to geographical convenience it is the largest supplier to USA pepper needs. And globally prices have always been suppressed as an when Brazil harvest sets in. This is very much evident from IPC Composite Prices during 2007. Composite Black Pepper prices declined by almost 5 percent during the month of September'07 from August'07. Reason being USA buyers cover their need from Brazil itself.

But since last year during the period January to March Brazilian Pepper exports to USA have dipped by almost 40% as compared to same period during 2006. And for the year 2008 exports to USA have dipped by almost 39% in comparison to 2007. Reason being appreciating Brazilian currency (Real) against USD, which rose by of 3% in 2007 and by 18percent in 2008 (graph on page 12). That made Brazilian pepper costlier. As a result of which USA bought heavily from Indonesia which was the cheapest source. This means Brazil will be having ample crop and we could see global prices being suppressed as when its full harvest sets in (.i.e.) mid September.

For the year (2008) country's total supply is expected to be at 50,000 tons including stock carried over from 2007 at



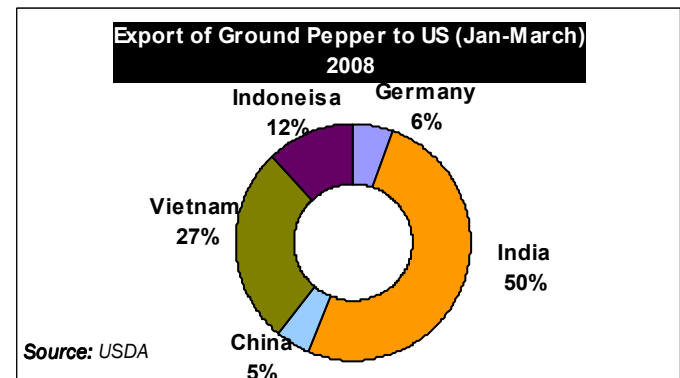
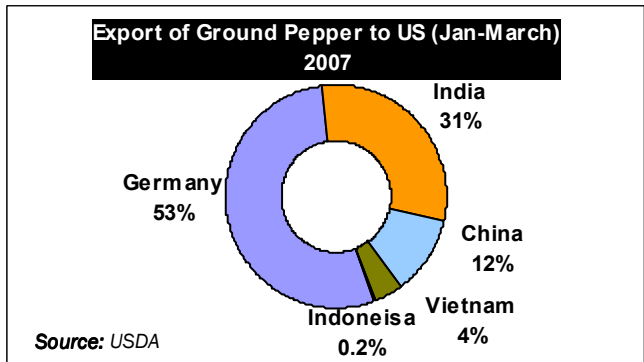
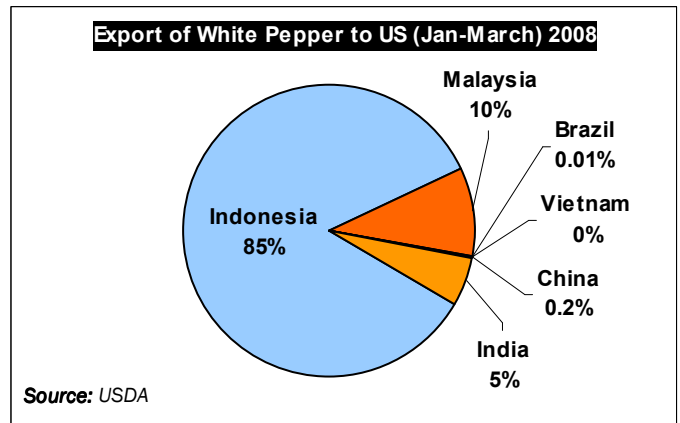
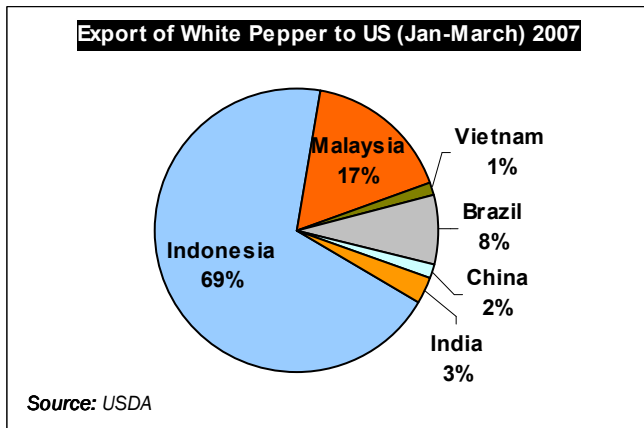
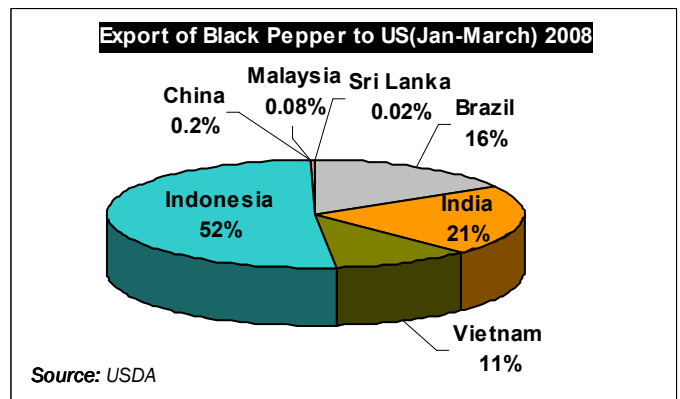
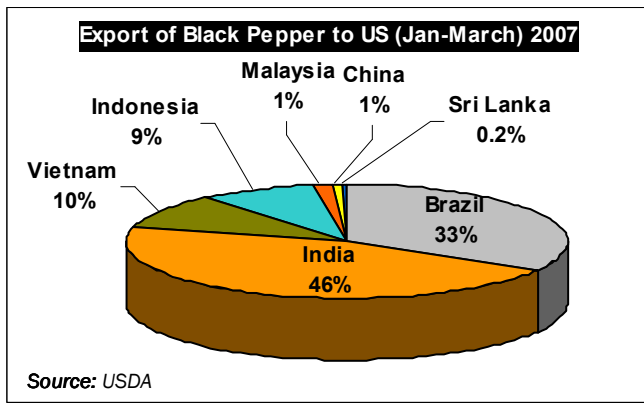
13,000 tons. Out of which total exportable quantity is expected to be at 35,000-36,000 tones.

DEMAND

During the end of first quarter there were general consensus that US imported less pepper reason being deteriorating economic conditions have restricted consumer demand. But actual scenario is totally opposite if we analyze figures for US pepper imports provided by USDA. Pepper imports during the first quarter of 2008 was reported to be at 14,494 tones, which as compared to same period during

the previous month its up by almost 20%.

US is the leading importer and consumer and it has always procured Black Pepper heavily from its neighboring countries especially Brazil as it geographically closer. But during first quarter 2008 Indonesia dominated the supply pack not only in White pepper but also in Black and Ground pep-



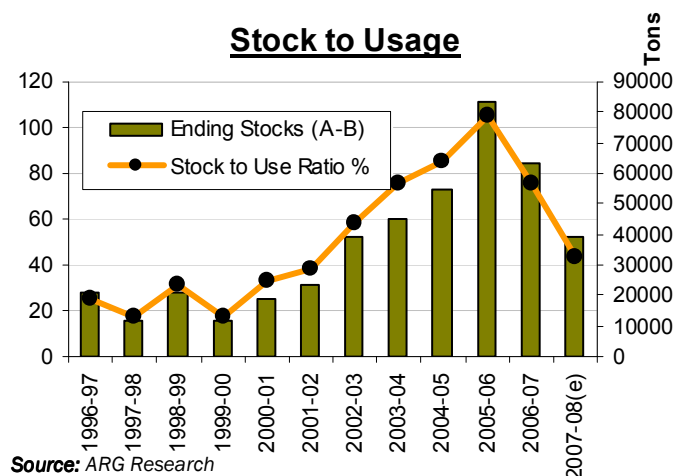
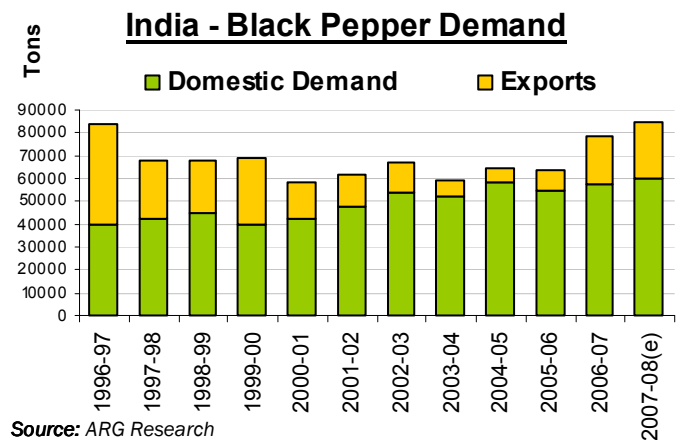
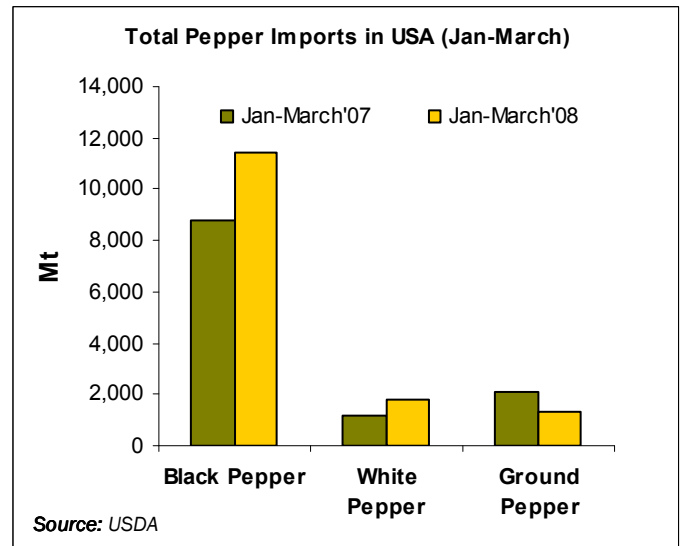
per. it also took over Germany which was largest exporter of ground pepper during the same period in 2007. This is because of depreciating Rupiah against USD whereas other currency appreciated during the same period. The graph on the previous page gives the comparative view of the countries pepper exports to US.

Despite the rupee appreciation (graph on page 12) and other negative global economic factors, India could regain its past glory in the global pepper trade. The short supply in the global market and limited selling by major producing countries like Vietnam has pushed up the pepper prices in the international markets. The average spot prices of Black Pepper in US market have gone up from US\$ 2.62 per kg in 2006-07 to US\$ 4.05 per kg in 2007-08.

During 2007-08, Indian pepper exports stood at 35,000 tones valued Rs.519.50 crores, which is higher by 22% in quantity and 70% in value as compared to the last year's exports of 28,750 tones valued Rs.306.20 crores. This is the highest export of Pepper made by India, both in volume and value in the new millennium. The average fob unit value has increased to Rs.148.43 per kg from Rs.106.50 per kg of last year. The major buyers of Indian pepper are USA, UK, Italy, Germany and Canada.

Domestic demand is expected to rise this year from 57,000 tons to 60,000 tons. As a result of which there is increase in overall demand from 83,377 to 90,000 tons tons. This has resulted in the decrease of ending stocks and fall in stocks to usage ratio, a key fundamental indicator which helps to find the direction of the prices. if we analyze stock to use ratio which has declined to 43% from 76% during previous year 2006-07. Which clearly indicates that demand is outpacing supply and trend for last three years. In 2005-06 we had the highest ratio of 132%, this was reduced to almost half in 2006, as the lower prices in global markets and abrupt weather conditions reduced the output.

For the current year stocks to usage ratio is estimated to be at 43% on the back of good demand from domestic as well as overseas market. (Indian Pepper B/S refer to pg 13)



ENDING STOCKS

World Pepper production has been very volatile but at the same time demand have been quiet steady as seen from the graph given below. Total consumption is approximately around 3,03,000 tones, out of which 2,25,000 tones is from consuming countries and 80,000 tones from producing countries. On the monthly basis consuming countries demand 18,750 tone per month and in case of producing countries it is 6,500 tones per month. If we were to analyze the trend for last 10 years than it clearly shows until 2003 global supply of pepper has always outpaced global demand and for that reason ending stocks have been accumulating.

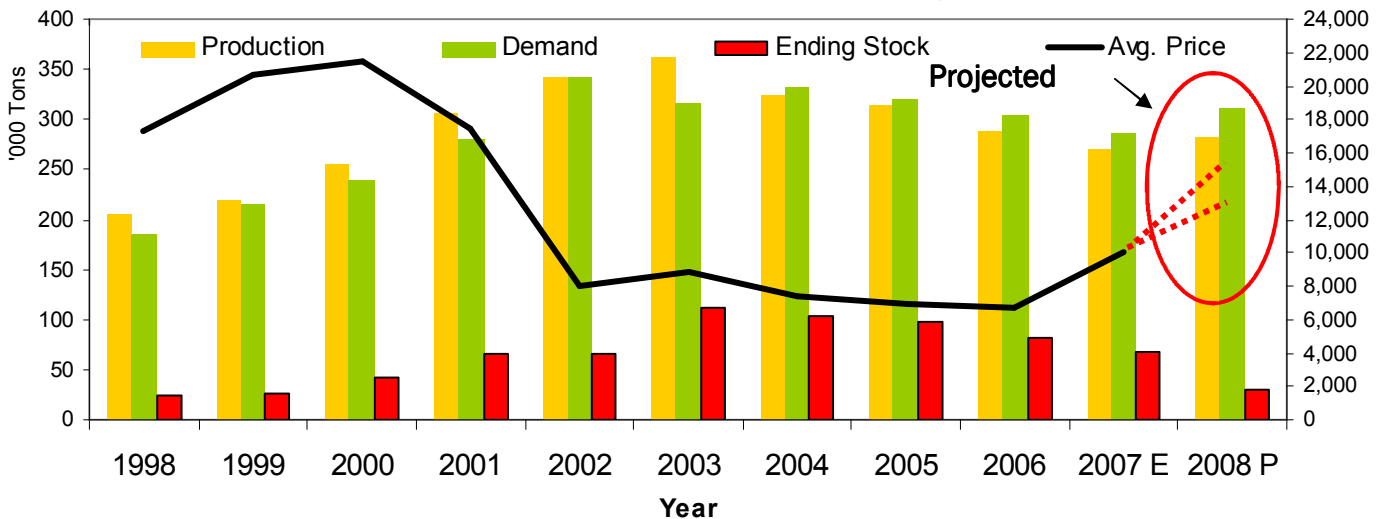
During 2003 ending stocks were reported to be highest almost at 1,00,000 tons. But from 2004 onwards supply has slowed down and demand have been quiet steady, but due to good carry over stock it has been able to suffice the demand. Hence, this has resulted decline in ending stocks, in next year (2005) supply showed some recovery but at the same time demand stood at same levels due to which ending stock saw some upside as compared to 2004 and were reported to be at 77,000 tons. Year 2006 and 2007 has seen drastic change in global pepper market, wherein supply pace has slowed down but demand have been on the steady note. This was due to erratic weather conditions which disrupted supply. But due to ample stock accumu-

lated during previous years demand was meet it has resulted in declining carry over stocks. For the year 2007 ending stocks are estimated to be at 68,000 tons.

Furthermore there is something called as iron stocks which is kept by farmers themselves and does not get accounted when the official figures are released. But as and when the price increase these stocks enter the market as farmers look to en-cash and benefit from the higher prices and this was witnessed this year, which is quiet evident if we analyze actual produce vis-à-vis the exports country wise:

During 2007 even though the production was reported to be lower at all the producing centers as compared to previous year, but at the same time exports has been meagerly hit. This is primarily because demand was well sufficed by the so called “iron stocks” at all the producing regions and especially in case of India, wherein its exports have risen drastically from 26,377 tons during 2006 to 30,000 in 2007. Even in case of Brazil exports have surpassed actual produce in 2007 but well below its exports figure reported during last year. But in case of Vietnam 2007 exports is estimated to have reduced to 83,000 tons from 1,16,670 tons during 2006. Reason being lower crop and farmers unwillingness to part with their stocks on expectation of better prices.

Black Pepper Global Scenario with Indian Price Projection for 2008



CONCLUSION

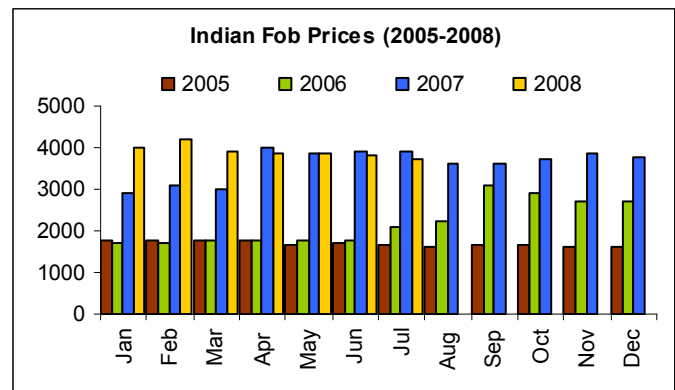
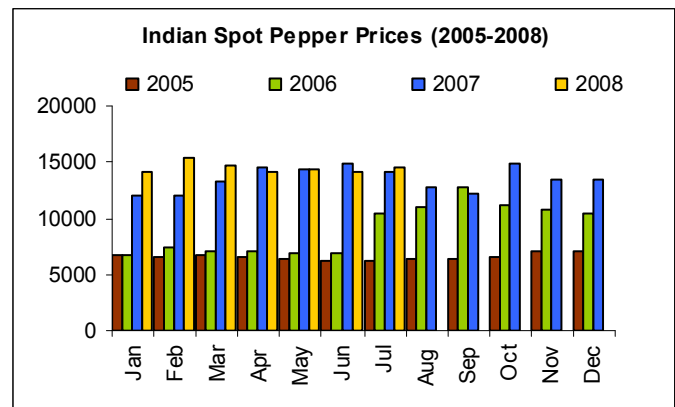
Pepper prices ten year cycle is very much underway as evident from the price rise during previous quarters on the back of tight supply position. Average price during first two quarters 2008 in the domestic market was reported to be at Rs.14,500 which is up by almost 7% as compared to yearly average of 2007. And even in comparison to same period (Jan-June) 2007 prices rose by almost 7%. Whereas Fob prices rose by almost 8% in comparison to 2007 average, it stood at \$3,900. And in comparison to same period (Jan-June) in 2007 it rose by 11%, which was supported by appreciating rupee.

Our target for Q1 2008 of Rs.13,400 in spot was almost achieved as prices touched Rs.13,600 and after which it spiked. But in the futures counter our target of Rs.13,700 was very well met. Whereas, our target for Q2 2008 of Rs.14,500 in spot and Rs.14,900 in futures were very well achieved.

In our previous update we had mentioned our Q3 2008 target of Rs.17,500 in spot front and Rs.18,000 in futures counter. We downgrade our targets to Rs.16,500 in spot front and 17,000-17,500 in futures counter. This is because we expect Brazil would suppress Indian prices as an when its full harvest sets in place.

But looking global ending stocks which are at all time low, where as US imports are increasing. Indian exports have been recorded a historical high and domestic consumption exceeding production putting huge pressure on the inventories. The stocks to usage ratio of the domestic markets is not yet reached all time low, but still is very much in danger zone, from 76% it slipped to 43% and will continue to fall through 2008. Even, weakening rupee will make Indian pepper lucrative in global markets.

Furthermore, there is sharp drop in rainfall during this monsoon and it is a matter of grave concern for farmers. Comparing to the same period last year, there is more than 60% drop in rainfall this year. Last year, the rainfall was 769.8mm from May to July 14 against 272.4mm this year. Pepper vines blossomed early this year owing to the untimely summer rain, but the continuous showers essential for pollination and emergence of berries have not material-

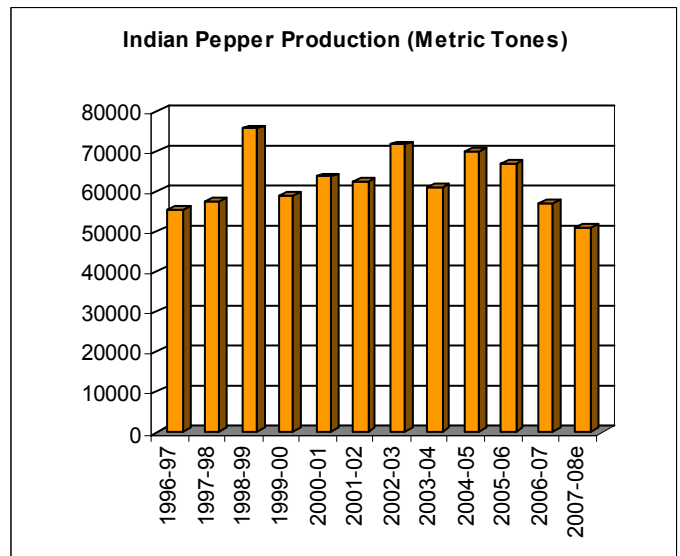
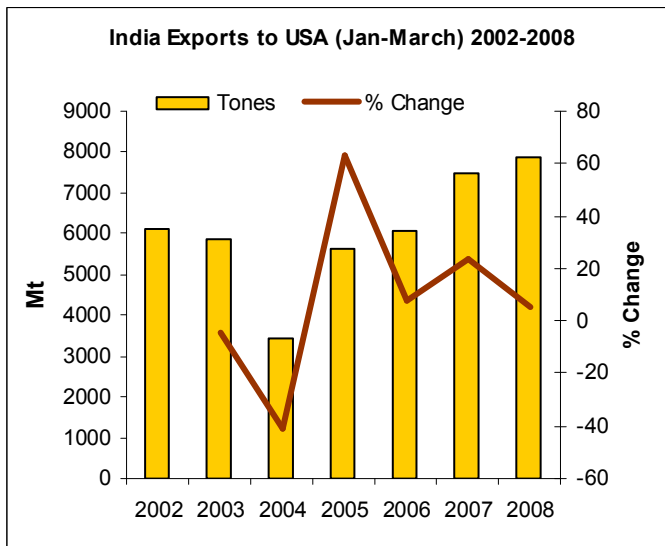
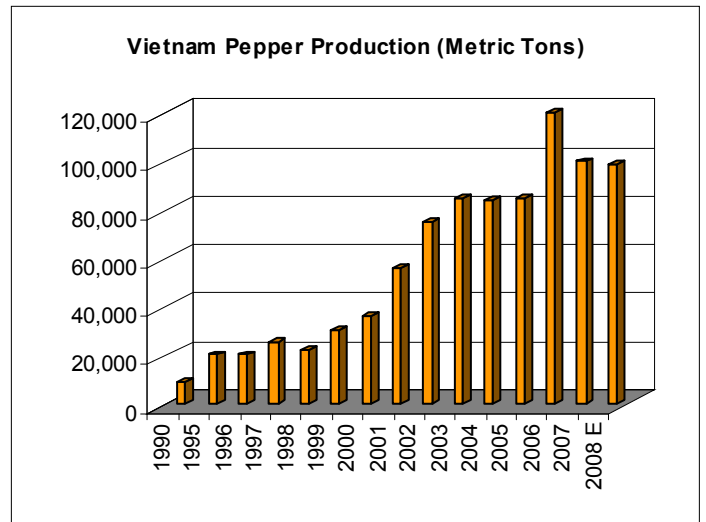
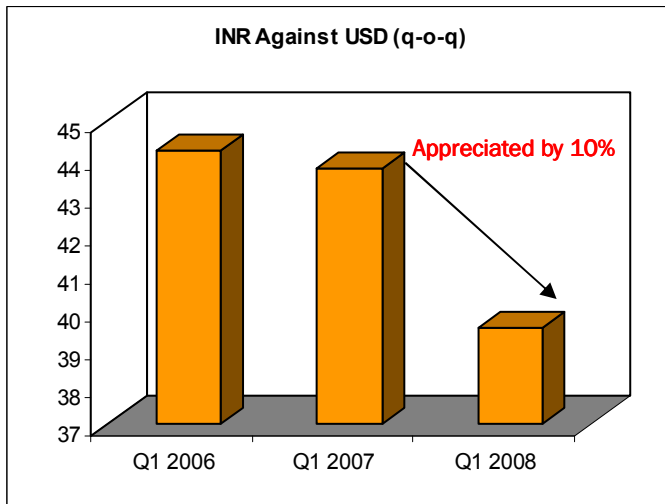
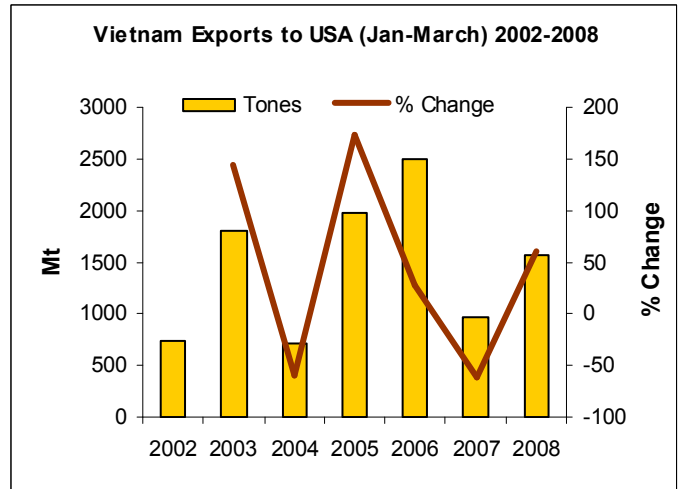
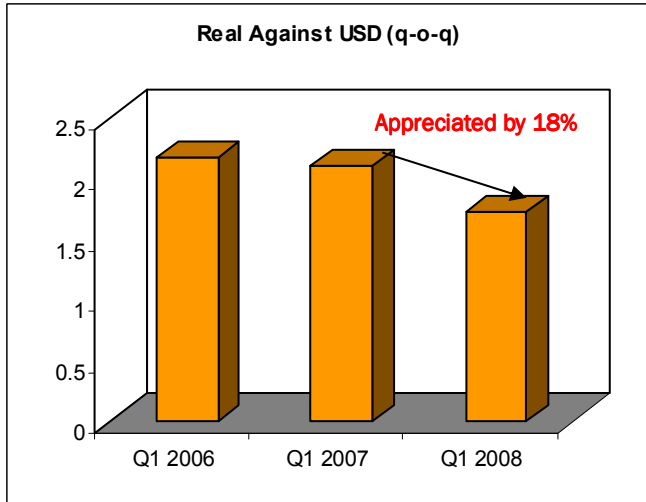


ized.

On the global front Indonesian selling pressure during harvest would be minimal as they have already parted with their stocks. As a result of which overseas demand would shift to India. Furthermore China's total produce is 20,000 tones of which it consumes major portion of it and since Olympics is underway in August more spices would be in demand and especially pepper. This would be supportive for prices.

But the only hindering factor is Vietnamese farmers have huge pile of pepper stocks and coffee prices have been falling they would part with pepper stock to benefit from prices rise, which would suppress Indian pepper prices.

We expect FOB prices will touch \$4200 levels by mid August -2008 and at the same time domestic prices are expected to touch Rs16,500 levels, prices could average around Rs14800 for entire 2008.

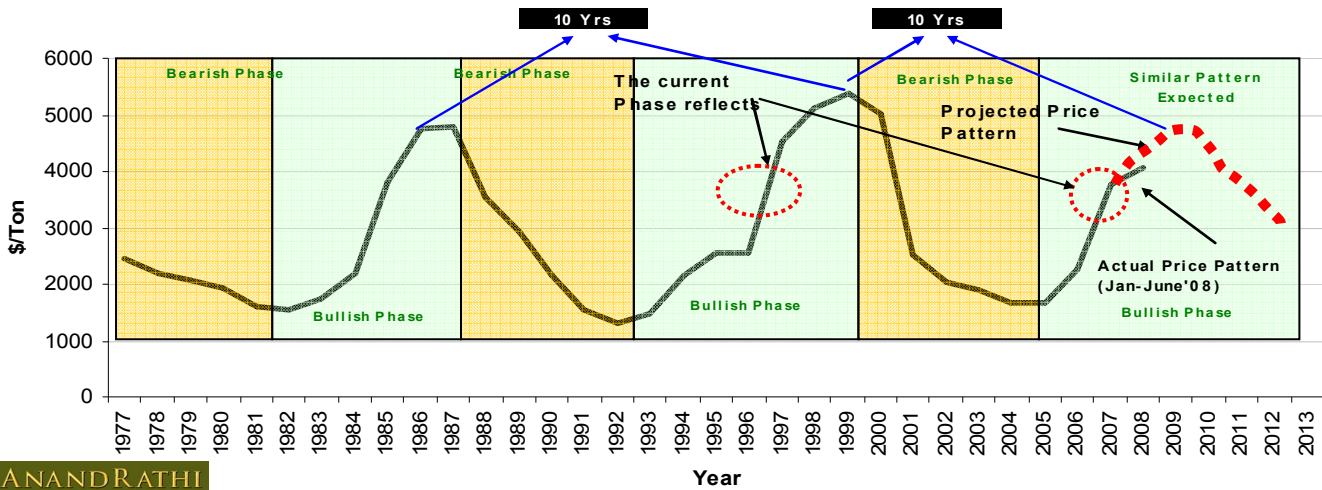


KEY FORECASTS & DATA

AnandRathi Price Forecast				
	End Q1 2008	End Q2 2008	End Q3 2008	Average 2008
India Spot	Rs13,400	Rs14,500	Rs16,500	Rs14,800
1st Month Futures	Rs13,700	Rs14,900	Rs17,000-17,500	Rs14,500
Vietnam (FOB)	\$3300	\$3000	\$3500	\$3200

	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08 (e)
Opening Stock	48000	20904	11435	20752	11881	19170	23601	39107	45018	54942	83768	63094
(Add) Production	55590	57300	75700	59000	63700	62400	71700	61200	70000	67000	57000	51000
(Add) Imports	908	1489	1163	1182	1584	3432	11128	3930	4425	25498	5703	15000
Total Supply (A)	104498	79693	88298	80934	77165	85002	106429	104237	119443	147440	146471	129094
(Less) Domestic Demand	40000	42000	45000	40000	42000	48000	54000	52000	58000	55000	57000	60000
(Less) Exports	43594	26258	22546	29053	15995	13401	13322	7219	6501	8672	26377	30000
Total Demand (B)	83594	68258	67546	69053	57995	61401	67322	59219	64501	63672	83377	90000
Ending Stocks (A-B)	20904	11435	20752	11881	19170	23601	39107	45018	54942	83768	63094	39094
Stock to Use Ratio %	25	17	31	17	33	38	58	76	85	132	76	43

New York Pepper Average Prices with Trend Projections



ANANDRATHI

ANAND RATHI

behind every successful investor

11th Floor ,Times Tower,, Kamala City,
Senapati Bapat Marg, Lower Parel,
Mumbai - 400 013, India

Phone: +91-022-4047 7000

Fax: +91-022-4047 7080

Kishore Name

kishorename@rathi.com

Vice President

Head - Commodity Research

Alimhammad Lakdawala

alimhd@rathi.com

Analyst - Spices



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* All the data in this report is being sourced from reputed sources like Reuters, Bloomberg, Malaysian Pepper Board, International Pepper Community (IPC), Indian Spices Board, Brazil Export Association, Ministry of Agriculture, Govt. of India. We do not guarantee its authenticity.