

Briefing Note: Soft Commodities– Tea and Coffee

Tea

Kenya is Sub-Saharan Africa’s largest tea exporter

Kenya is Sub-Saharan Africa’s leading tea exporter in addition to being among the world’s largest black tea producers. Within East Africa, Kenya is the key producer, accounting for 59.6% of total production in Africa on average over the past six years (2008-2013), well above its competitors, Uganda (8.7%), Tanzania (5.1%), Rwanda (3.6%) and Burundi (1.2%).

There has been noteworthy growth in tea output, attributable to good weather as well as increase in total tea acreage, over the past decade recording a 6.3% 3 year CAGR. Total output has grown 37.2% over the past decade, from 324.0m Kgs in 2004 to 444.8m Kgs in 2014. In 2014, total tea acreage stood at 203,000 Ha (+2.2% y/y), with small holder farms at 128,600ha (+1.0% y/y) and estate farms accounting for 74,400ha (+4.3% y/y).

In Kenya, tea is among the largest foreign exchange earners, accounting for 20.0% of the value of exports in 2014 equivalent to KES 94.0bn.

The sector is largely made up of small holder farms, which account for more than 50.0% of tea produced in the country each year. Production goes on all year round with two main peak seasons: March to June and October to December which coincide with the rainy seasons. Kenya boasts of tea produce that is free of agrochemicals with the environment in which the tea is grown acting as a natural deterrent to pests’ infestation and diseases attack.

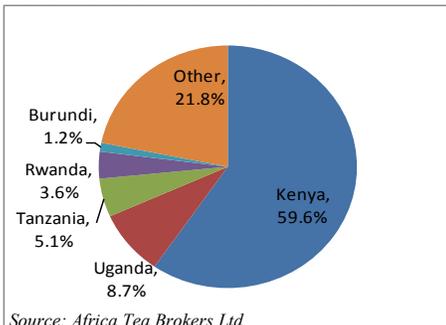
Research Analysts

Kestrel Research

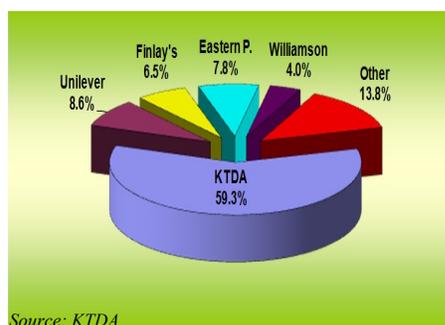
research@kestrelcapital.com

www.kestrelcapital.com

Share of Africa’s Total Production



Tea Production– Key Players



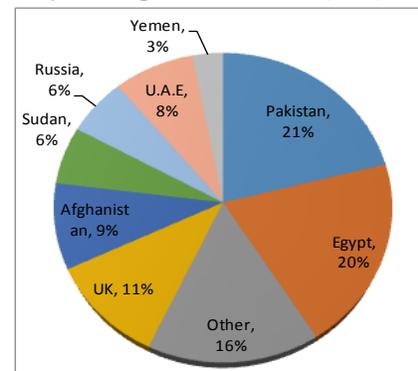
The Mombasa Tea Auction has transformed tea marketing

The Mombasa Tea Auction has undergone major transformation in the recent past, to emerge as the world’s largest CTC (cut tear and curl) auction centre.

- Live auction data feed (September 2014): The system incorporates instantaneous data visualization and analysis, automated data warehousing, quick and efficient post-auction reconciliation and world-class auction floor operations. The live streaming of auctions was developed as a means of ensuring transparency, ideally attracting international traders ahead of the implementation of electronic trading slotted for 2015.

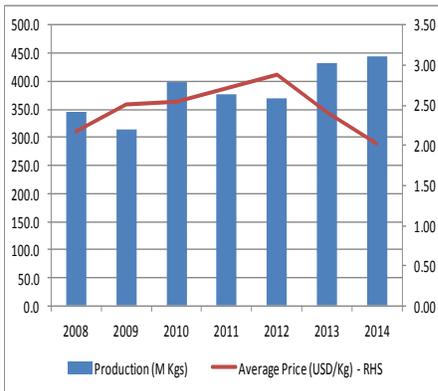
Approximately 60.0% of Kenyan tea is exported to several countries among them: Pakistan, Egypt, Britain and Afghanistan . The Tea Board of Kenya is seeking to attract more export destinations and we expect that the strides taken towards modernizing the auction system will play a critical role in ensuring the success of the plan.

Key Tea Export Destinations (2014)



Increased production continues to put pressure on tea prices

Production and average annual price (2014)



Source: KTB, Africa Tea Brokers Ltd

In 2014, Kenya's tea production was at an all time high of 444.8m Kgs. Rising production has largely been attributed to an increase in tea acreage coupled with good weather especially in 2013 and 2014. As a result, tea prices at the Mombasa Tea Auction averaged at USD 2.03/ Kg in 2014, the lowest price in 7yrs (-15.8% y/y, 2008: USD 2.18/Kg).

Depressed rainfall in 1Q15 saw the supply glut recorded in 2014 decline marginally. As a result, tea prices edged up to a January to April average price of USD 2.36/ 1 Kg (+6.8% y/y). With the onset of the long rains towards the end of April, output is expected to resume the upbeat momentum registered in 2014. The Kenya Meteorological Service estimates that rainfall in tea producing regions will be near normal with a tendency towards enhanced rainfall. Being that Kenya is a major world exporter, the increased output could see average prices remain depressed in 2015, especially in the May to June peak season.

The venture into lucrative specialty segment faces challenges

Although Kenya is known for the production of high quality black tea, producers are looking into farming of orthodox specialty tea varieties as a diversification strategy. The value of Kenyan black tea exports has been prone to fluctuation as a result of volatility in prices, a trend that has resulted in low income for farmers. Some have resulted to uprooting the crop in favor of other fast growing high yield crops, while others have chosen to plant other tea varieties among them, purple tea, white tea and green tea in the hopes of deriving better value from the crops. Specialty teas fetch a higher price in world markets owing to their scarcity as well as their appeal to herbal tea lovers owing to their medicinal properties.

The major challenge specialty teas farmers are faced with however, is the lack of processing capacity in most tea factories. In fact, the only factory with the infrastructure necessary to process these varieties is Kiangati Tea factory located in Kerugoya, Kirinyaga County, with its location sidelining producers in distant production zones.

We however note that, the Kenya Tea Development Agency (KTDA) is looking to establish cottage tea processing industries for specialty teas. The extent of the development of these plans is yet to be disclosed, however, we expect that once fully established, more farmers will look to produce the specialty teas.

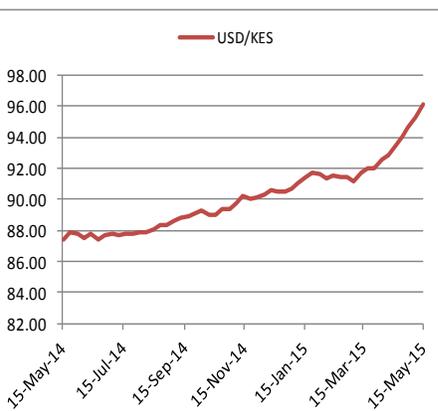
A look at 2015

Kenya's tea farming still holds a lot of potential. Strides towards attracting and venturing into new markets as well as diversification of output are expected to aid in seeing the segment remaining among Kenya's largest hard currency earners in the medium term. However, the weakening of the Kenyan Shilling against the dollar in 2015 (-5.8% ytd to KES 96.15*) is expected to see the cost of inputs (especially fertilizer) increase, exerting pressure on farmers' margins. This coupled with the decline in tea prices could result in slower growth in 2015.

We note that the civil unrest in Egypt and Pakistan in 2013 and 2014 contributed to the drop in tea prices at the Mombasa Tea Auction as the demand in the countries declined over that period. Since the unrest in Egypt has been quelled, demand in the country is expected to grow providing support from the depressed prices owing to increase in supply.

* Price as at May 15, 2015

USD/KES trend



Source: CBK

Coffee

Coffee ranks among Kenya’s top foreign exchange earners, raking in USD 226.5m* (KES 19.9bn) in foreign exchange in 2014 (~4.3% of the value of exports). In Africa, Kenya ranks second after Ethiopia in quantity of Arabica coffee exported, accounting for 0.9% of total global exports of Arabica coffee on average in the past 10 years. Coffee production has seen notable growth which we believe can be attributed to incentives from the Coffee Board of Kenya (CBK), among them, the training of farmers on better crop husbandry practices. Total output during the crop year 2014/2015 was at 51.0m Kgs (5.8% 5yrs CAGR). However, we note that land under coffee is constantly under pressure mainly from the mushrooming real estate developments. Total Coffee acreage expanded a marginal 0.2% y/y in 2014 to 110,000ha from 109,800ha in 2013 and 2012.

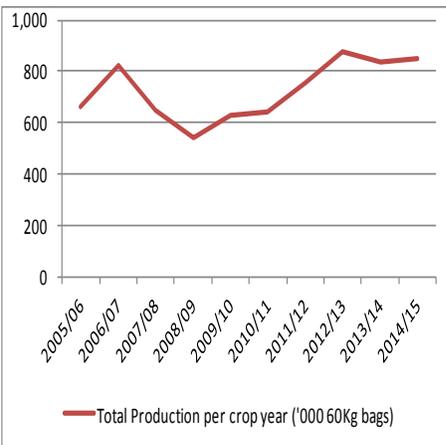
Western Europe countries (mainly Germany, Belgium and Sweden) and USA are the main importers of Kenyan coffee. There has been a general upward trend in the quantity of coffee imported in these countries with USA recording the highest 5 yr CAGR at 2.8% followed by Germany at 1.7%. Average annual growth rate in global coffee consumption since 2011 has been at 2.3%, a rate that we expect will be maintained in the near term with the biggest potential being in several markets among them, Algeria, Australia, Russia, South Korea and Turkey.

Coffee prices recorded a rebound in 2014, from a decline in 2012 and 2013. The drought experienced in Brazil was cited as the major reason behind the increase in prices. We note that Kenyan Coffee in general, trades at a premium relative to other brands owing to its higher quality. As at 2014, Kenyan Coffee traded at 9.6% and 39.6% premium relative to other Colombian Milds and the ICO Composite Indicator respectively. With regard to 2015, we expect increased supply, especially from Brazil, to exert pressure on prices seeing them decline relative to 2014. As at 1Q15, the International Coffee Organization (ICO) composite indicator recorded a general decline in coffee prices averaging at USD 139.7 Cents per pound, 34.0% lower than the USD 210.3 Cents per pound peak average price in 2011.

On the marketing front, Kenya has launched a coffee branding initiative designed to boost the country’s reputation for producing high quality beans and help the industry regain its position as a top foreign exchange earner. The initiative involves the introduction of the mark of origin which is expected to increase visibility of the Kenyan brand in both domestic and foreign markets.

* Figure based on a USD/KES exchange rate of KES 87.91

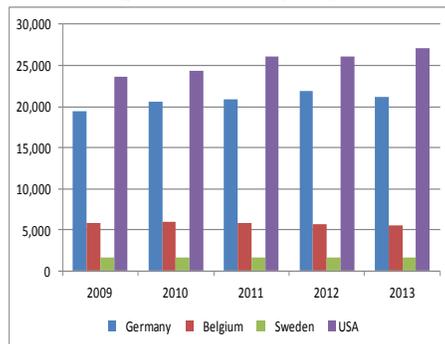
Kenya: Coffee Production



Source: ICO

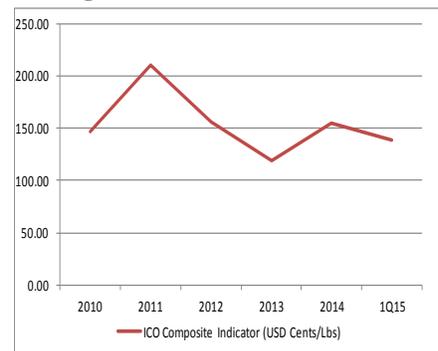
	2014 Average Price (USD Cents/Lbs)
Kenyan Coffee	216.71
Other Milds	200.39
Colombian Milds	197.95
Brazilian Naturals	171.59
ICO Composite Indicator	155.26
Robusta	100.43

Coffee Imports in M 60Kg Bags



Source: ICO

Average Annual Coffee Prices



Source: ICO

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