Glut of coffee beans on market

By Alexandra Wexler and Leslie Josephs, Wall Street Journal

When coffee prices climbed to multi-year highs in 2011 on a scarcity of high-quality beans, farmers revved up investments in their plants, adding fertilizer, pruning trees and planting more productive varieties.

But the buzz didn't last long. The result was a glut of beans that has sent prices to the lowest level in nearly four years.

Welcome to the coffee bust.

Cycles of boom and bust have long defined the coffee market, with Brazil, which at present supplies one-third of the world's beans, at the epicenter.

When coffee prices plunged during the Great Depression, Brazilians burned it on land and threw some of it out to sea.

"They tried to make roads out of coffee beans, make it into asphalt," said Mark Pendergrast, author of Uncommon Grounds: The History of Coffee and How It Transformed Our World, referring to other coffee busts. Brazilians even "tried to make plastic out of it."

While prices for other agricultural commodities like corn and cotton also rise and fall based on supply and demand, arabica-coffee trees take at least three years to grow, so the production response to high prices is often more gradual.

The last coffee bust was in 2001, when prices dropped to almost 40 cents a pound, about a third of the current price. It was so bad that it is still known in the coffee world as "The Crisis." Farmers ripped trees out of the ground and skipped applications of pesticides and fertilizer on those

left standing.

But this time, the coffee bust has come in the wake of rapid economic growth in Latin America, where most of the world's arabica beans are grown. That has proved both a blessing and a curse for farmers.

Much of that decade-long growth was fueled by rising global demand from China for the region's rich mineral and agricultural resources. The inflow of cash has enabled big coffee-growing countries in Latin America, like Brazil and Colombia, to support farmers when prices are low and control supplies that hit international markets.

"The (Colombian) government has never had the revenue it has had today," said Mauricio Galindo, head of research at the International Coffee Organization.

But economic growth has also spurred inflation, and the cost of production has climbed as well.

"It's worse than ever," said Christian Wolthers, president of Fort Lauderdale, Fla.-based coffee importer Wolthers America. Wolthers started his career in Brazilian coffee four decades ago. "It becomes worse because you have inflation and you have increased prices for all coffee management tools and products," including fertilizer, he said.

But prices may soon find a low point, investors and analysts say.

"While harvest pressure will likely weigh on prices in the short term, we continue to expect a rebound in the space in the second half of 2013," Chris Narayanan, head of agricultural commodities research at Societe Generale GLE.FR +1.08%, said in a note. He sees expectations for lower supplies in the coming season boosting the price of arabica coffee to $1.57 a pound in the fourth quarter of the year.