DJ Robusta Coffee at 19-Month High on Brazilian Drought Fears

By Katherine Dunn

LONDON--London-traded robusta coffee closed at a 19-month high on Tuesday, as concerns mounted that Brazil's robusta crop won't recover from last season's blistering drought.

The continuous robusta contract, which currently tracks the November contract, closed 1.25% higher at $1,943 per metric ton, its highest price since mid February 2015. The contract has risen 6.29% in the past month and more than 20% since the year began.

The robusta contract, which tracks the lower-quality variety typically used in instant coffee, has been climbing since February 2016, largely due to a severe drought in Brazil and a strengthening Brazilian real.

Brazil is the world's second-largest producer of the robusta variety, known domestically as conilon, after top producer Vietnam. But dry weather and a resulting irrigation ban in its key robusta region, Espirito Santo, cut back the crop by 22% in the 2015-16 season compared to the previous year, according to the U.S. Department of Agriculture. The Brazilian coffee season runs from July to June.

Meanwhile, the swift strengthening of the Brazilian real ahead of former president Dilma Rousseff's impeachment discouraged exports of coffee, pushing up prices in the larger and more liquid arabica market, where Brazil is the dominant producer. Typically, the New York-traded arabica market tends to lead the smaller London robusta market.

While traders had hoped the impact of the drought would be limited to Brazil, concerns are now rising that the weather in the region will remain dry, leaving exhausted trees unable to recover over the 2016-17 season.

"Apparently the consequences of the drought are going to be significant for the coming years," said a European coffee trader.

Coffee traders have responded by lowering their estimates for the current crop. In August, London brokerage Marex Spectron forecast a 1 million bag global coffee deficit for the 2016-17 season due to a crippled robusta crop, reversing a previous estimate of a global surplus.

That impact could be felt across the arabica market, according to traders. When supplies of robusta are low, lower-quality arabica coffee is typically used as a replacement bean in blends, which means that the arabica market could see more tightness despite expectations of ample supply.

The impact will be felt particularly hard on the domestic coffee market in Brazil, which must use arabica to make up the difference, said Rodrigo Costa, an analyst at Societe Generale in New York.

"It can get tricky as Brazil cannot import coffee therefore the impact, if things turn out bad, will be felt more on the arabica availability," said Mr. Costa.

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DJ ICE Coffee Chart Picture Weakens - Technical Analysis

By Kira Brecht

ICE December coffee futures erased intraday strength and tumbled into negative territory on Tuesday. The recent rally to $1.5570 a pound on Sept. 8 stalled just shy of major daily chart resistance at the July swing high at $1.5765. The action reveals hesitation on the part of the December coffee bulls near a major bullish chart objective. In the short-term, December coffee is vulnerable to bearish testing.

ICE December coffee recently traded down 115 points at $1.4975 a pound, off the intraday high at $1.5300.

Action in recent months has turned choppy and consolidative for December coffee futures and the contact has marked out a large intermediate term neutral trading range. The top of the range is bordered by major resistance at $1.5765 and the bottom of the range is seen at the late June and mid-August lows around $1.3760-$1.3785.

Short-term, December coffee is vulnerable to a test of Monday's low at $1.4845, which stands as short-term support. The 20-day moving average at $1.4721 stands as support just below there.

The recent failure from near the range top leaves coffee vulnerable to downside probing. If support at the 20-day moving average cracks in the days ahead it would open the door to a potential retest of the Aug. 24 low at $1.4225 and potentially the range bottom around $1.3700.

Daily momentum has turned bearish. The nine-day relative strength index recently turned down from an overbought 78% on Sept. 7 to Tuesday's reading at 53%. The momentum indicator is trending lower. The 50% line could act as a toggle point. If momentum stabilizes above the 50% line it could slow downside price probing. Conversely, a retreat under the 50% line would suggest the bears are gaining momentum.

On a multi-month basis, the trend remains bullish for December coffee. A bottom formation is seen on the daily chart off the late January and early March daily lows. December coffee has mounted a strong rally off the $1.1940 low hit on March 1. In the short-term, however, the recent hesitation to approach the July ceiling keeps December coffee stuck in its large June through September sideways range.

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