



Market Report IHGC DHWV - Paris 21.04.2006

Reliable crop and yield figures of the various hop growing countries for the year 2005 are now available. The 2005 world hop crop is approximately 92.500 tons, corresponding to roughly 8.000 tons of alpha immediately post-harvest, or 7.200 tons of alpha of hop products for the brewing industry.

Based on worldwide beer production of 1.65 billion hectoliters at a hopping rate of 4.3 g. alpha / hl, the crop 2005 alpha acid demand of the brewing industry for use during the 2006 brewing year is estimated at 7.100 tons . Using a calculation based primarily on estimates, we expect there to be a balanced market.

These were the assumptions we made when marketing of the 2005 crop started, and consequently expected normal market conditions.

This year, however, quite clearly shows that the hop industry should not base its market expectations and consequent decisions solely on the available figures. There are many factors other than crop statistics which can influence the market.

Shortly after the 2005 harvest, breweries made their usual spot purchases, either for their full year's requirement or topping up any existing forward contracts. Nevertheless, as we already reported in November, the market was relatively slow, a phenomenon which has continued until now. There have been some sales of high alpha hops during the last few weeks, although these sales have been made at prices significantly lower than the purchase costs.

The important markets for high alpha hops and standard aroma varieties like Perle, Tradition or Select are determined by Germany. American aroma hops were almost fully forward contracted. Due to this year's above-average hectare yields for special aroma varieties from Germany, France and the Czech Republic, some quantities remain unsold, especially in the Czech Republic. As a result of the small crop in the U.S.A. means there has been literally no spot market for high alpha varieties. This market segment has been compensated by the above average yields of high alpha hops in Germany. However, high

alpha hops have been sold at prices lower than the € 2.50 / kg paid to the growers. Even the € 2.30 / kg paid for pool hops was not always low enough to achieve a sale profit.

Taking into account the figures for supply and demand, how can we determine why the market is not moving in the direction one would expect?

The data used to calculate the industry's requirements are produced with the utmost care and are backed up by analyses of the bitter units in a wide cross-section of international beers. There is still a major degree of uncertainty about the hop production and beer sales figures supplied by China, which has become the world's biggest beer producer. The most doubtful statistic from that country is the claimed alpha dosage per hectoliter of beer. Based on the figures China has provided, there are insufficient quantities of home-grown hops to supply the Chinese market. In order to cover this shortage, China would need to import substantial quantities of hops. This, however, is not reflected by currently available statistics. One might assume that China has actually reduced the alpha used in its mass-produced beers in order to manage with the hops available on its own market. This would result in a readjustment of world alpha requirements of approximately 100 tons or more. This assumption would have an effect on the statistics for international alpha-acid usage, reducing the figure down to 4.3 g/hl, maybe even as far as 4.2 g/ hl. This would mean a reduction in worldwide demand down to 6.900 tons of alpha.

Another factor which has not been sufficiently accounted for when calculating the supply and demand position is the strategic stock held by breweries worldwide. My definition of a strategic inventory is the amount of alpha-acid already purchased by the brewing industry, and being physically held in stock, either in the brewery or by the supplier. This quantity would allow the international brewing industry to brew beer for a certain number of months, even if there were to be a complete crop failure. It is quite impossible to quantify this inventory position.

How could this strategic inventory influence our evaluation of the market?

In the past there have always been and there still are breweries which keep considerable stocks of hop products. On the other hand there are breweries which tend more towards keeping inventories as low as possible. The strategic inventory to which we refer is an average of the assumed figures for all breweries.

Although these breweries still retain their varying stock positions, the mergers of the past years mean that the information pertaining to these stock situations has been centralised

into a handful of corporate headquarters. It has therefore become much easier to adjust the different stock positions of the individual breweries to achieve a balanced situation within the groups. This can be done without having to make new hop purchases. It is true that this reduces the strategic inventory of the breweries worldwide, but at a time of overproduction and interchangeability of high alpha products this is quite justifiable. By reducing strategic inventory by just one month's requirements, the theoretical demand for alpha-acids would drop by 600 tons. This quantity might explain the very slow market. We believe that we are confronted by exactly such a situation right now.

This means that despite a previously calculated equilibrium of supply and demand of crop 2005 alpha-acids, we actually could have a significant oversupply, accompanied by all the associated consequences.

Market equilibrium can only exist if strategic inventories in the breweries are significantly reduced. As long as strategic stocks are held, the breweries can use them to influence market movement. The greater the respective inventories the greater the influence in creating a weak market place.

Strategic inventory can only be reduced, if there is a shortage of supply for a sustained period of time.

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