The World Cotton Market

By Michael Edwards, Cotton Outlook

Sentiment was already shifting firmly to the bull side when we last contributed to *The Australian Cottongrower* in mid-September. Since then, a sustained import demand from China has seen prices strengthen with remarkable speed.

The Cotlook A Index has risen by over 12 cents, or 19 per cent, in two months. During the same period, New York futures have also risen strongly. Although futures prices have recently fluctuated in a particularly volatile fashion, this has not fundamentally undermined the firmness of price sentiment, at least as regards the next few months.

TIGHT GLOBAL SUPPLY

With the A Index already close to 80 cents per lb, much conjecture centres on the extent to which prices can rise further. Based on current estimates, the global supply position is certainly tight, with the 2003–04 season's projected endstocks of comparable proportions to those recorded in the mid-1990's — a period of exceptionally high prices. In April 1995, the A Index rose to its all-time high of 119.40 cents per lb, shortly before its temporary withdrawal, owing simply to the dearth of offers in the market.

Whether or not such reminiscences offer a clue to the likely course of the present bull market is of course open to question. But there can be little doubt that developments in China will be of paramount significance. What then do we know (or think we know) of the statistical situation in that country?

Based on current assessments, there would appear to be scope for additional Chinese purchasing of some magnitude. Figures presented to the China Cotton Conference in October suggested that stocks on September 1, 2003 totalled 870,000 tonnes — equivalent to well under two months of consumption.

Cotton Outlook's current forecasts suggest production of 4,800,000 tonnes, consumption of 6,600,000, and thus an apparent shortfall of 1,800,000 tonnes, if one assumes that stocks will not be allowed to dwindle further by the end of the season. The recent wave of Chinese demand has seen purchases that many private estimates suggest may amount to close to 1,000,000 tonnes (by November 6, sales amounting to roughly 580,000 tonnes of US cotton alone had been confirmed by USDA). Although USDA has a higher stock figure for China, even on Washington's projection, a substantial volume of imports apparently remains to be covered.

CHINESE PUZZLE

However, such calculations are predicated on figures that may themselves be subject to revision. China's National Bureau of Statistics customarily does not release its definitive crop estimate until around the end of the year. Although the agency has already indicated that the crop would be 'barely changed' from 2002–03, when 4,920,000 tonnes were produced, recent history reminds us that a surprise in the year-end figure cannot be discounted.

On the consumption side, too, there may be room for adjustment. The escalation of raw cotton replacement costs has, by all accounts, reached a point at which some Chinese spinners have been obliged to idle spindles, or to shift to polyester. Yarn production during October was weaker than in any month since May, when the impact of the SARS crisis was most strongly felt. China's capacity to produce polyester staple fibre has been growing strongly of late, and the country is expected, before long, to have achieved self-sufficiency in the commodity.

Those less committed to the bullish cause also note that the volume of imports secured thus far, together with the availability of the domestic crop, should be sufficient to feed Chinese mills for some time to come. If import purchasing were to remain relatively slow until the later stages of the season, the focus of attention might by then be on the production outlook from the 2004–05 crop, which may see a price-driven increase in cotton plantings in some countries, and perhaps further expansion in China herself.

Beyond the current season, therefore, considerable uncertainty reigns. Such indicators as are available point to a retreat of prices in 2004–05. At the time of writing, the October 2004 contract in New York is trading at a discount of over 12 cents, relative to July 2004.

The International Cotton Advisory Committee suggested at the beginning of November that the average of the A Index during 2004–05 will be 10 cents below the Committee's latest estimate for the current season. The manifest lack of confidence in the outlook for world prices beyond the end of this season contrasts sharply with the current strength of the global balance sheet.