The world cotton market

By Matt Robinson, Cotton Outlook

The Cotlook A Index has continued to lose ground during the period under review, declining decisively below 50.00 cents per pound and reaching its lowest point since July 2002. New York futures have also eased, particularly in the deferred months — the nearby December contract has traded at a premium over the March 2005 during the past few weeks. The weakness of prices can be attributed in the main to a global balance sheet, which portends a significant addition to world ending stocks by July 31, 2005.

Cotlook's forecasts at present suggest a supply surplus of over two million tonnes during the running season — more than twice the deficit estimated for 2003–04, with almost all of that net addition to stocks occurring outside of China. Confidence in the attainment of bumper crops from many of the Northern Hemisphere's major producing countries has been well maintained during the period under review. Cotlook's world production estimate has increased by no less than 766,000 tonnes during the past two months.

The Northern Hemisphere harvests have been expedited by largely benign conditions. The concern that existed when we last contributed to the *The Australian Cottongrower*, over the potential impact of wet weather in eastern China, and most notably the damage caused to the US crop by an active hurricane season, has generally faded.

In the former country, a lint output comfortably in excess of six million tonnes has become more assured, while in the latter, the USDA has increased its domestic crop forecast by no less than 1,640,000 bales (480 pounds) since its September report, and now foresees a record production of 22.54 million bales.

Record crops have also remained in prospect in Pakistan and India, as figures showing heavier seed cotton arrivals than a year earlier have emerged. Final official harvest data from many of Central Asia's producing states point to a higher output than last season.

Moreover, the weakness of international prices appears to have had only a modest impact on planting intentions in the Southern Hemisphere. As readers of the Cottongrower will be well aware,

48 ▷

◁ 47…WORLD COTTON MARKET

the arrival of spring rainfall in some parts of the Australian cotton belt has underpinned a planted area of around 300,000 hectares, compared to the 185,000 hectares dedicated to the drought-stricken 2003–04 crop.

Although some estimates in Brazil have predicted a further expansion in production next season, the general opinion is that a similar output to 2003–04 is foreseeable. A significant recovery in outturn from Argentina is deemed likely and, while a combination of the pessimistic price outlook and unfavourable weather has dented prospects in Paraguay, early predictions in Zimbabwe suggest plantings for 2004–05 will be about maintained on last season's 360,000 hectares.

In view of the foregoing, one might have expected a still sharper downturn in international offering rates. But several mitigating circumstances have been discernible, not least the unwillingness of farmers to sell cotton at the prevailing prices, which has in turn hindered the smooth flow of supplies into the normal marketing channels. A soft US dollar exchange rate has exacerbated the unattractiveness of offering rates in many parts of the world, but especially in the African Franc Zone countries, which are especially vulnerable to adverse price fluctuations.

GOVERNMENTS INTERVENE

Several governments have felt obliged to intervene in domestic raw cotton markets. State trading enterprises in India and Pakistan have launched procurement campaigns and have started to hold export tenders (though little interest has thus far been generated).

The China National Cotton Reserve Corporation, having absorbed over 100,000 tonnes of 2003–04 crop into the state reserve, was instructed at the beginning of November to commence the take-up of new crop supplies into the reserve. An initial target volume of 300,000 tonnes was set, but thus far only 500 tonnes have been purchased and so little impact on spot market price levels has been observed.

In Brazil, an initial 'PEP' auction has been announced, by which the government provides incentive payments to facilitate the marketing of cotton in an endeavour to restore prices to at least the official minimum support level.

A paradoxical tightness of supply has been created in the US by farmers preferring to place cotton into the Commodity Credit Corporation Loan, on price grounds, rather than sell on the open market. Cotton in the loan is only expected to become available to US shippers in volume when the differential between futures and world prices widens sufficiently to allow entitlement to pass to merchants on payment of a premium considered profitable by farmers. A further consideration for shippers of US California Acala SJV descriptions has been a scarcity of higher grades following unwelcome rainfall in late October/early November. Most have subsequently proved reluctant to offer better qualities.

DIFFICULT MARKETING DECISIONS

The restricted flow of cotton from origin has presented the international trade with some difficult marketing decisions. A desire to conclude new crop sales has been tempered by mounting exposure to an upward movement in prices, as 'short' positions have been accumulated at levels that have often been well below current replacement costs at origin.

But some sellers of 'outside' growths have been anxious to take advantage of the hiatus in US competitive pressures to add to their new crop commitments and have offered growths such as West African aggressively. A reasonably brisk import demand has been evident in some of the major South East Asian markets, but only when prices have declined sufficiently to spur buying interest. Any firming in offering rates has been followed by a swift withdrawal of enquiry.

Price sentiment in trade circles at the time of writing remains inclined to the bear side, based on fundamental considerations. But the caveat has frequently been given that current price levels are already well below the long-term average and for that reason further downside potential may be limited.

The direction prices will take moving into the New Year could once again depend heavily on developments in China. Estimates continue to show a significant import requirement in China during the current season, and though an upturn in enquiry has been discernible from that market in recent weeks, a substantial expansion in purchasing will be necessary sooner, rather than later, if current forecasts of imports are to prove accurate.

If such an expansion is not forthcoming, the already substantial ending stocks predicted for the current season (particularly in the US), may yet prove conservative.