

Each year, the "Marketplace Insight" provided by Billy Dunavant is a highlight of the US Beltwide Cotton Conference. His ability to summarise market influences and predict market trends is legendary. His 2005 address to the Beltwide will be his last and so it has some historic significance. This article is a summary of that address.

Marketplace insights

By William B. Dunavant Jr., Chairman, Dunavant Enterprises

The Beltwide is always the highlight of my annual speaking and it is exciting to make this presentation. This will be my last Beltwide speech because I am stepping down, in June 2005, from being Dunavant's active chief executive officer, but I will remain chairman of the board forever. I have been speaking at the Beltwide for 19 years, and it has been truly an honour.

As most of you know I have supported the entire cotton industry during my career but I must reflect my extreme disappointment in the working of our existing farm bill.

It seems the chances of maintaining a good step two program is in jeopardy, and it is very necessary for our domestic textile industry, and for making US cotton competitive in the world market. I am also disappointed that a cotton producer potentially makes more money when prices are low than when prices are high. There is nothing about that situation that makes any economic sense to me.

I do not blame the West Africans, the Brazilians, and Australians, for raising hell about our farm program.

I sincerely want the American cotton producer to survive, and survive well, but not based on the farm program that we have today.

I am certainly happy this is not last season because everything I believed then was incorrect, and did not come true. It was the first loss our company had suffered in nearly 70 years.

In looking back, the primary reason was China not meeting my expectations. This past spring they had a severe credit crunch, and we suffered many defaults from Chinese textile mills. The worldwide cotton industry also suffered many defaults but that did not help our company. We are still working trying to get some of the problems resolved.

This year we are back on track and will have a good year even though cotton prices are cheap. The demand is very good and the US and world will produce record crops.

When I spoke last year I talked about the sad demise of the US textile industry. Last season we consumed 6,489,000 bales and conditions seemed to have stabilised. This season's consumption will be approximately 6,250,000 bales. Many people are talking about US cotton consumption dropping below five million bales, but I do not see that as a reality in the next three years.

But I do not see US cotton consumption going back to 7.5 million bales in the future. The American cotton producer will be looking to the export markets of the world — particularly China — for his future.

I am very worried about the level of the US carryover at the end of this season. I think it can threaten, and will threaten, the farm program. We at Dunavant are projecting a US carryover of 7.9 million bales.

If the government takes over three to four million bales and catalogues it to sell in competition with the next season's crop then the whole program is in serious trouble. I think the taxpayers are not going to put up with this in the future and I do not blame them.

China, as I have said for years, is the future as their cotton consumption continues to grow.

US SUPPLY-DEMAND SITUATION

Now let me slightly change pace and talk about the US and world supply-demand as we at Dunavant view it today.

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Believe it or not the final US crop will be about 22.8 million bales — a record for us. The US and world turned to cotton this season. Domestic consumption will be 6,250,000 bales, as I have already stated, and our exports will be 12.2 million bales for total offtake of 18,450,000 bales.

We have currently registered for export 8.75 million bales so China really needs to be a player this year and I think they will be.

Looking at my numbers, the US carryover goes from last season's 3.5 million bales to a whopping 7.9 million bales — too much.

Every region in the US produced a huge crop. Texas is going to produce 7.45 million bales, and if they had not had a seige of bad weather in the fall, the final US crop would have been over 23 million bales.

For next season we think US production will be 19.5 million bales, with domestic consumption of six million bales, exports growing to 14 million bales, and our carryover dropping slightly to 7.44 million bales — still too much.

I think weather, improved technology, and improved seed varieties created our monster crop this season. It could happen again because Texas has a huge amount of subsoil moisture to draw from next season.

WORLD SITUATION

Now let's talk about the world because it is also unbelievable. World production will reach 115.5 million bales, and world consumption will be 104.0 million bales — a new record.

Our numbers say the world carryover will rise from

35.5 million bales to 46.9 million bales or about an 11.3 million bale increase in one year.

It is truly hard for me to believe how dramatically the US and world numbers have changed in 12 months.

For 2005–2006 we see world production shrinking to 103.4 million bales, world consumption rising to 106 million bales, with the world carryover dropping to 44.2 million bales — still a big number.

Now, let me be more specific with where these numbers have come from. We think China's production will be 29 million bales this season, and their consumption will be at least 36.5 million bales, leaving them a carryover of 8.4 million bales at the end of this marketing year. We think they will import at least 8.2 million bales. Currently, we think they have bought for import only 1.7 to two million bales this season. So China still has a lot of cotton to buy after the Chinese New Year.

Last season China produced 22.3 million bales, and consumed 32 million bales. They have increased production by nearly seven million bales, and consumption by 4.5 million bales in one marketing year.

India and Pakistan are both producing huge crops. India will produce at least 15.1 million bales versus 13.8 million bales last season, while Pakistan will produce 11.5 million bales versus 7.8 million bales last season.

Basically, every cotton producing country in the world is enjoying substantial increases.

I mentioned last year the emergence of Brazil as a major cotton producer because of the huge increase in cotton acreage in Mato Grosso and Bahia. They produced 5,850,000 bales this season, and I project even with prices down they will produce 5,250,000 bales in 2005–06.

Uzbekistan has increased its production to five million bales versus 4.1 million last season.

As you scan the globe this season we have major increases in the world in production and consumption, but production has grown much faster, and world production will definitely decline next season primarily because of price.

The West African countries have really struggled because prices are way below their cost of production and they are further penalised with the strength of the euro.

PRICE OUTLOOK

Now, I will attempt to discuss my views on price. I only hope what I say today has more validity than what I said a year ago. I never dreamed a year ago that December cotton would trade at 84.80 in the fall, and then in the months following, cotton prices would drop dramatically with a tight statistical situation.

Our US carryover dropped to 3.5 million bales, and prices went down for October cotton to 43.50 cents per pound. Today, March cotton is trading at 45.30 in the face of huge US and world supplies.

Two factors that have held cotton prices at today's level have been the weakness of the US dollar and the strength of the euro. World prices of competing growths have not plunged as many of us thought they would.



Maybe world prices will drop in relationship to New York futures, but it has not happened yet to a major degree. It can happen but only time will tell.

China can help to stabilise prices in the future if they start an aggressive buying campaign. Our people in Asia do not think they will be aggressive until after the Chinese New Year, which comes after February 9, 2005.

Today, I see no reason for prices to go substantially higher because you run into a wave of selling by merchants and cooperatives. Certainly, we can get a rally of two to three cents if the commodity funds who are short decide to cover their position, but a major rally, in my opinion, is not on the cards with world production at this season's record level.

If the world price declines sharply in the future, then of course New York futures can also decline, and will decline.

As I have said, first we must see weakness in world price to a major degree, and it has not happened yet.

With the US carryover at 7.9 million bales, if I was a producer, then I would sell at any equity because somebody is going to be left holding the bag come summertime. The loan, as you know, is a 10 month loan, and cotton loans will start expiring in late July, and then escalate each month going forward.

We need for China to purchase much more in the world than my projected 8.2 million bales of imports. It can happen if the Chinese government decides to build Chinese stocks in the future, but I am certainly not predicting that to happen.

More potential for price fall

There is certainly more potential for world prices to decline than escalate with a world carryover growing by more than 11.3 million bales.

We see China reducing production next season by 2.25 million bales from 29 million bales to 26.75 million bales, and we see Chinese consumption continuing to escalate going from 36.5 million bales to potentially 38 million bales.

Chinese imports may increase from 8.2 million bales this season to 10,750,000 bales next season. That is certainly a bright spot for demand for the future.

When I spoke last year I said that we would have a substantial increase in world production this year from 93.1 million bales to 102.3 million, and we will end up producing 115.5 million bales in the world.

Nobody, and I mean nobody, would have predicted that kind of production. World consumption has gone up also from 98.4 million

bales to 104.0 million bales — a nice increase, but nothing compared to the production number.

I have stated that I am not a supporter of our current farm program as it is today, but I am only a small voice in the crowd. I do know that you as a producer and ginner must support the National Cotton Council if you are going to have a chance for the future. I certainly support it though I don't agree with current farm policy. The Council has been good to me, and our company, for many years, and has on the whole, created a lot of good for the US cotton industry.

Thank you for the opportunity of serving you for the past 19 years! 