

Commodity Spotlight



Cotton Production Up, Demand Down

Cotton is experiencing greater weakness in world prices than grains and other crops. World cotton prices have fallen 39 percent from a year earlier as of October 2001, while comparable measures for wheat, corn, and soybeans range from a drop of 6 percent to a rise of 11 percent. Cotton prices, like other commodities, have suffered from global slackening of demand for commodities since the mid-1990s, but the current slowing of the world economy has coincided with rebounding world production, driving world cotton prices toward historic lows.

Demand Hurt by Economic Downturn

While a slowing world economy curbed expansion in global consumer demand for clothing, larger crops of cotton in the world's six major producing countries in 2001/02 resulted from favorable weather, government policies, and imperfectly integrated markets. Planted area in the Northern Hemisphere rose 9 percent from the year before, and with generally favorable weather contributing to yields, Northern Hemisphere production climbed 12 percent.

As cotton's problems have become apparent during this fall's Northern Hemisphere harvest, Southern Hemisphere farmers are now expected to cut cotton plantings by 11 percent in 2001/02. But since Southern Hemisphere countries account for little more than 10 percent of world production, their drop will not offset expansion in the North. Global cotton production is expected to rise 8.5 million bales in 2001/02, to its highest ever at 96.9 million bales. Meanwhile, consumption is forecast to decline slightly to 91.6 million bales, and world stocks outside China are expected to grow to their largest share of consumption since the mid-1980s.

A major source of cotton's current difficulty lies in the shifting world macro-economic outlook. During 1994-97, world GDP growth recovered from earlier weakness to range from 3.7 percent to 4.2 percent (International Monetary Fund estimates), and world cotton consumption resumed normal growth after a 6-year hiatus. The Asian financial crisis and its aftershocks in Brazil and Russia again deflected cotton consumption downward, but world economic growth only dipped to 2.8 percent in 1998. By 2000, world GDP growth had grown to nearly 5 percent as a surging U.S. economy played its traditional role as the global "locomotive." This role was particularly evident in cot-

ton consumption: 80 percent of the rise in world cotton consumption between 1995 and 1999 reflected increased purchases by U.S. consumers.

In part, expanding U.S. cotton consumption represented a long-term trend where a long-standing consumer and technical promotion program unique to the U.S. stimulated a growing preference for cotton. During the last 20 years, U.S. households were responsible for almost half of the 29-million-bale increase in world cotton consumption. There was also a short-term stimulus to U.S. consumption as U.S. economic expansion outpaced the rest of the world in the years leading up to 2000. In 2001, U.S. expansion has stalled, and U.S. end-use of cotton dropped for the first time since 1996. With no replacement for U.S. demand in a slowing world economy, world cotton consumption fell in 2000/01 and is expected to fall again in 2001/02.

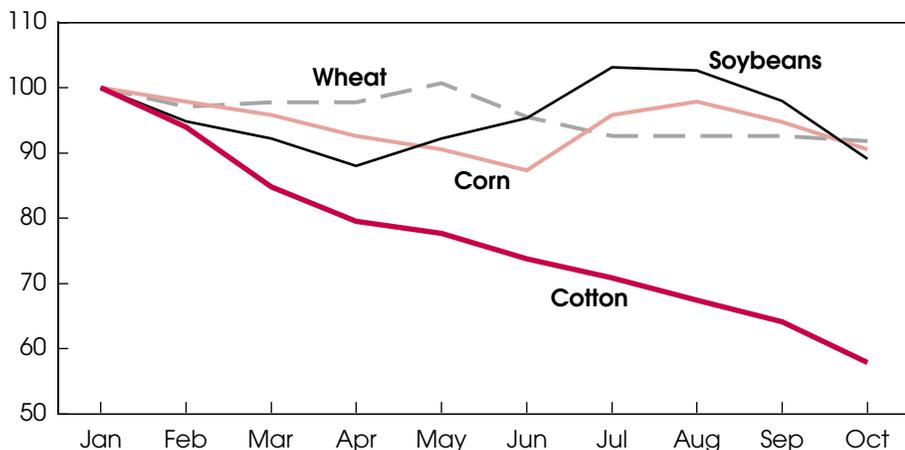
U.S. Cotton Production Jumps to New Record

Unfortunately for the world's cotton producers, the recent economic slowdown was largely unanticipated by economic forecasters. A year ago, prospects seemed relatively bright for cotton prices and production with another year of strong U.S. and world economic growth generally anticipated for 2001. Textile spinning capacity had been growing in recent years in China, Pakistan, India, Thailand, Brazil, and Central Asia, in some cases after a long hiatus, as textile exporters sought to capitalize on expanding demand. With these favorable prospects for cotton and with grain prices languishing well below their highs of a few years earlier, cotton production expanded in a number of countries in 2001/02.

Also, circumstances peculiar to the world's largest producers added to local incentives to produce cotton, with one of the largest gains, a 3-million-bale increase, occurring in the U.S. Although U.S. cotton prices were declining during planting time this spring, so were prices for other commodities, limiting the outlook for profitable alternatives. Furthermore, the U.S. marketing loan and crop insurance programs provided further incentives to plant cotton rather than other

World Cotton Prices Lose Ground in 2001

Index: Jan. 2001=100



Cotton price is Northern Europe. Other prices are U.S. Gulf Ports.
Economic Research Service, USDA

crops. As a result, U.S. cotton acreage in 2001 rose 4 percent to 16.2 million acres, the second highest in nearly 4 decades.

While drought occurred in parts of the Southwest in 2001, generally favorable growing conditions for other cotton producing regions likely provided a record U.S. cotton crop this season. The latest USDA production estimate is 20.2 million bales, 17 percent above 2000 and 3 percent above the previous record set in 1994.

During the last decade cotton production shifted back to the eastern half of the U.S. as boll-weevil eradication improved the profitability of growing cotton in the region. In 2001, the Delta and Southeast regions likely produced 60 percent of U.S. cotton, up from about 50 percent just 10 years ago. In fact, the Delta is expected to produce a 6.8-million-bale cotton crop this season, the second largest on record behind the region's 1994 crop of 6.9 million. Similarly in the Southeast, production is forecast to surpass 5 million bales for the first time since the 1937 season. In contrast, the Southwest (4.7 million bales) and the West (3.3 million bales) have been relatively stable over the past decade.

Foreign Cotton Production Also Up

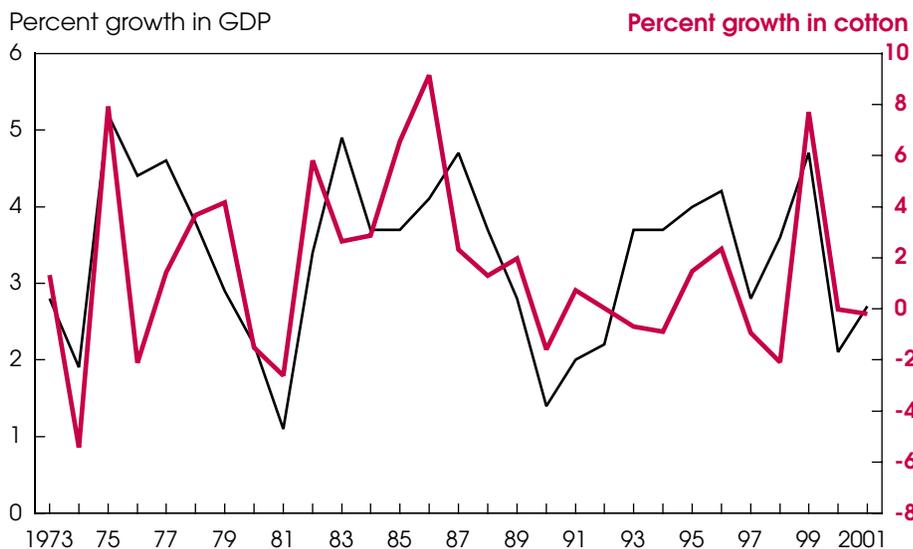
China, with the largest increase of any country in 2001/02, is expected to produce a 23.5-million-bale crop, up 3.2 million from a year earlier. Like the U.S., China is experiencing a return of cotton to the area (the eastern provinces) that domi-

nated its industry in earlier years. Factors contributing to this second-largest increase ever include:

- rebounding prices as China's cotton market reform passed through its initial shock,
- the introduction of Bt cotton to China's eastern provinces, and
- China's continued prohibition of imports combined with an effort to restrain grain output.

China's cotton area plummeted to a 37-year low in 1999/2000 as guaranteed government procurement was formally rescinded and an aggressive government effort to reduce textile capacity suggested continued sluggish demand. However, textile exports and cotton consumption began soaring in China during 1999/2000 and producers began receiving higher prices through both legal and illegal marketing channels. At the same time, the cost savings of Bt cotton were becoming apparent in eastern provinces like Shandong, Henan, and Hebei. In 2001/02, China's cotton area is estimated 29 percent higher than 2 years earlier, and with favorable weather, yields are forecast at their second highest ever.

World Cotton Consumption Tracks Global GDP Growth: Both Slow in 2001/02



2001 estimated.
Economic Research Service, USDA

Commodity Spotlight

India's cotton producers, in response to higher prices for cotton and price depressing supplies of Indian rice, planted 618,000-additional hectares to cotton. With the return this year of a favorable monsoon to Gujarat, the largest cotton producing state, yields are expected to be their highest since 1996/97, and India's production is expected to increase 1.3 million bales to 12.2 million.

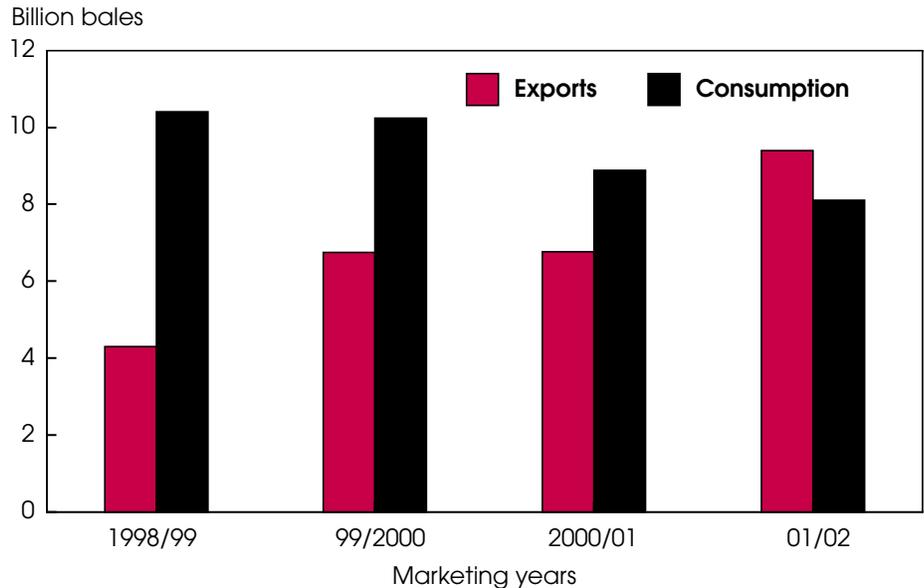
In **Pakistan**, although a prolonged drought has entered its third year, cotton production is expected to increase as planted area shifts from rice to cotton, a less water-intensive crop. An increase of only 100,000 bales from the year before is foreseen in Pakistan's cotton crop, to 8.3 million bales.

In **Central Asia**, yields appear to have increased in 2001/02 despite the continued drought. Last year Uzbekistan's westernmost districts suffered from poor irrigation supplies, so area shifted closer to irrigation sources in 2001/02, and output is forecast 300,000 bales higher at 4.7 million. Larger crops have also been realized in Kazakhstan, Tajikistan, and Turkmenistan. Cotton production in Central Asia has stabilized since 1996, following a 50-percent reduction over the preceding 8 years. Area has actually trended upward in the region despite the steady decline in world prices, as state monopolies determine producer payments independent of world events.

West Africa's Franc Zone has also seen increasing area since the mid-1990's, but largely because of a 1994 exchange rate correction. In 2001/02, area is estimated up 19 percent from the year before and record output is expected. Last year saw one of the sharpest declines in the region's output ever, in part due to poor weather, and in part due to a strike by producers in Mali, the largest Franc Zone producer. World prices rose slightly last year, and producers and marketing boards in the region pursued increased output.

Ironically, many of Mali's producers refused to plant cotton in 2000/01 due to low prices, but returned in force to the crop in 2001/02. Mali's area is estimated up 89 percent from the year before and, with favorable rains and yields, West Africa's largest cotton producer is expect-

U.S. Cotton Exports to Exceed Domestic Consumption in 2001/02



2001/02 forecast.

Economic Research Service, USDA

ed to harvest 620,000 bales, or 129 percent more than the year before. Overall, Africa's Franc Zone is expected to produce 1.2 million bales more cotton in 2001/02 than during the year before, and the region's exports are expected to overtake Uzbekistan's for the first time ever.

U.S. Cotton Mill Use Declines As Textile Imports Expand

The buildup of foreign cotton supplies and foreign textile capacity has come at a particularly inopportune time for the U.S. textile industry. Cotton mill use in the U.S. is expected to decrease 9 percent in 2001/02. While the U.S. spinning industry has declined in general over the last 4 years, the bulk of the reduction is attributable to cotton. In calendar year 2000, for example, cotton accounted for 29 percent of total fiber spun in the U.S., down from about 33 percent just 5 years earlier.

Increases during the last 5 years in domestic cotton consumption—which includes mill use plus the net trade of cotton products—have been satisfied mainly by imported products. U.S. cotton textile and apparel imports in calendar year 2000 rose for the 12th consecutive year to 7.5 billion pounds, a new record. On a per capita basis, imports amounted to over 27

pounds per person in 2000, double the level of just 7 years ago.

During the last several years, domestic mills have been under tremendous price pressure from imports as the U.S. dollar has reached heights not seen in over a decade. As a result of the dollar's strength, many U.S. mills have had to restructure their businesses by limiting their output, relocating their operations, or closing plants. In 2001 for example, an unprecedented number of textile industry participants shuttered their doors as financial losses mounted and improved prospects seemed limited.

While U.S. imports and exports of cotton products have been rising for over a decade, only part of the increase can be attributable to trade agreements—such as the Caribbean Basin Initiative and the North American Free Trade Agreement—which encourage extensive use of U.S. raw fiber or semi-processed products. About 80 percent of the U.S. trade deficit in textiles and apparel is with countries not covered by these agreements, and liberalization under the World Trade Organization (WTO) has expanded the access of these other countries in recent years.

Based on estimates by the International Textiles and Clothing Bureau, the U.S. has increased the size of its import quotas by about 35 percent since 1995 in order to meet its WTO obligations. However, imports from other countries increased more than 50 percent. With the strong U.S. economy, soaring value of the U.S. dollar on foreign exchange markets, and expansion of developing country exports into new products, calendar year 2000 was the first year in which net imports of cotton products exceeded U.S. mill use of cotton. In addition, preliminary 2001 data suggest that the gap between U.S. mill use and net imports will widen further.

Future Cotton Prospects Uncertain

Although U.S. mill use of cotton is trending lower, foreign mill use is expected to rise for the third consecutive year in 2001/02, albeit at a 0.7-percent rate com-

pared with the 1.7-percent rate of the preceding 25 years. Cotton consumption is expected to decline slightly in India, the world's second-largest industrial user, but higher mill use is expected in Pakistan and Southeast Asia. Brazil's consumption of cotton is expected to decline due to electricity rationing, and no change is foreseen for China, home of the world's largest textile industry.

As for further into the future, current low cotton prices could bode well for reduced world cotton output in 2002/03, although the magnitude may depend on the level of government support around the world. Similarly, low prices and forecasts for a rebounding global economy in 2002 and 2003 suggest world consumption could return to more normal growth, but considerable uncertainty remains about the economic outlook.

In the U.S., raw cotton exports will become increasingly more important if U.S. mill use continues its recent downward trend that has resulted in a buildup in U.S. stocks. With the U.S. holding a larger share of global stocks than at any time during the past decade, U.S. cotton exports could approach shipment levels attained in only a handful of prior years. And if the global economy rebounds in 2002/03 as forecast and world cotton mill use expands, the U.S. will be in a unique position to supply the growing need for cotton fiber around the globe. **AO**

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For more information:

www.ers.usda.gov/publications/agoutlook/dec2000/ao277c.pdf

www.ers.usda.gov/briefing/cotton

