

China's Cotton Imports Rise Despite High Stocks

China's 1996/97 cotton production fell 11.9 percent to 4.2 million tons. However, ending stocks rose 16.7 percent as imports continued at a relatively high level and offtake was sluggish. China's central government-dictated cotton import plan reportedly called for little in the way of cotton imports this year in order to draw down growing stocks. However, lower priced imported cotton, primarily from the United States, attracted many joint-venture cotton yarn mills to import. Although difficult to verify, many non-joint-venture yarn mills reportedly were able to illegally obtain this lower priced imported cotton, increasing the financial pressure on the China Cotton and Jute Company, the government's official cotton marketing and warehousing body. Area and production in 1997/98 are expected to decline because of relatively low incentives for cotton farmers and increased area planted to wheat. Imports are expected to remain robust barring a change in the right of joint-venture yarn mills to import cotton. The structural problems within China's textile industry are not expected to improve dramatically in 1997/98 as the central government continues to give more weight to the social and political impacts of large layoffs and bankruptcies against the need to restructure the perpetually money-losing state-owned textile sector. [Hunter Colby (202) 219-0669]

Area sown to cotton in 1997/98 is expected to fall modestly because of poor returns to cotton relative to other competing crops. Despite the fact that free market grain prices declined in 1996, the rising opportunity cost associated with planting labor-intensive cotton, particularly in North and East China where alternative low-labor crops or nonagricultural employment opportunities are much greater, is expected to reduce cotton area. The majority of those reductions will likely occur in North, Central, and East China growing areas. Northwest China, notably Xinjiang Province, will probably continue to increase area sown to cotton, but not enough to completely make up for the reduction in other regions. Given the difficulty of forecasting future yields or relative crop prices, arguments for significant increases or decreases in yield are premature. Assuming average yields and a modest reduction in area, production in 1997/98 may fall below 4.0 million tons.

Estimates of China's imports in 1996/97 are now higher than initial forecasts because of surprisingly robust cotton purchases by joint-venture cotton yarn mills. A significant

but unknown share of these imports, however, are reported to be finding their way to non-joint-venture mills (in many cases via state mills establishing so-called "joint-ventures"). Robust imports during 1996/97 have been stimulated by China's high internal price relative to the world price.

Cotton imports in 1997/98 are contingent on a number of policy issues facing the central government—issues about which very little information is as yet available on what, if any, changes the government may make. If there are no changes in policy, imports will likely remain close to 1996/97 levels. This "no policy change" scenario for imports assume domestic prices remain above world prices (meaning the world price doesn't fall and the government doesn't lower the state-set domestic price); no government clamp down on the right of joint-venture yarn mills to import cotton outside the state quota system; and finally, no push by central authorities to eliminate or diminish state yarn mills from gaining access to out-of-quota cotton imports via under-the-table transfers from affiliated "joint-ventures" established by the state enterprise. However, if any of the government policies identified above changes, it has the potential to substantially reduce China's 1997/98 cotton imports relative to the current year. In the past, government cotton policy tended to be announced following the August or September National Cotton Work Meetings involving all the government institutions involved in the cotton sector. With an internal price above the world price, China's exports are likely to remain nominal through 1997/98.

Table 19--China's cotton supply and utilization

Item	1993/94	1994/95	1995/96	1996/97
	1,000 tons			
Production	3,745	4,333	4,768	4,202
Imports	176	884	663	544
Consumption	4,638	4,398	4,246	4,289
Exports	163	40	5	22
Ending stock	1,328	2,107	3,288	3,724
Percent stock/use	28.6	47.9	77.4	86.8

Source: USDA PS&D database.

Table 20--Monthly 1996 domestic cotton prices in China and the A index compared

US\$/ton	China's farm price	China's mill price 1/	A Index
		US\$/ton	
Jan	1,690	2,412	1,897
Feb	1,687		1,905
Mar	1,679		1,834
Apr	1,665		1,828
May	1,672		1,835
Jun	1,663		1,825
Jul	1,667	2,115	1,757
Aug	1,681	2,551	1,682
Sep	1,670	2,450	1,663
Oct	1,673		1,666
Nov	1,594		1,689
Dec	1,671		1,745

Sources: China's prices: China Ministry of Agriculture;
A Index: Cotton Outlook.
1/ Price paid by mills for cotton supplied by the state
(Supply and Marketing Cooperatives).

Supply and Marketing Cooperatives Struggle

In 1996, the central government restructured the government cotton procurement agency—the system of Supply and Marketing Cooperatives (SMC). The system of linked provincial, prefectural, county, and local SMCs was restructured, with a national level office formed to oversee all SMC operations. The national level office reports directly to the State Council, giving the central government leadership greater control over cotton purchasing operations and activities.

Over the last 3 years, estimates of China's cotton stocks have increased strongly. From an ending stock-to-use ratio of 29 percent in 1993/94, the ratio has risen to 42, 64, and finally, 76 percent in 1996/97. Although some stocks are held by the central government for strategic reserve purposes and some by mills, the majority of cotton stocks in China are held by provincial Supply and Marketing Cooperatives. As cotton supply has grown over the last 2 years, yarn mills have gradually decreased their cotton stocks from 2-3 months of consumption to a reported 1-2 months at most. All of this means growing financial outlays for the government procurement and marketing agency. With both the farm price and resale price to mills mandated by the government at a level above the price of imported cotton, the Supply and Marketing Cooperatives have little room to maneuver to avoid stock accumulation and an attendant increase in carrying costs. Illegal price reductions and longer credit periods are reportedly the response of Cooperatives as they attempt to attract yarn mills who can now attempt to bargain before they buy domestic cotton.

Bollworm infestation continues to be a problem in several of the major producing provinces, most notably Shandong, Henan, and Hebei. Despite continued problems with bollworms, national yields rose slightly in 1996/97

Table 21--Provincial cotton area and output

Province	1994		1995	
	Area	Output	Area	Output
		1,000 tons		
Xinjiang	750	882	743	994
Henan	967	628	1,000	770
Hubei	498	450	502	586
Jiangsu	535	457	565	562
Shandong	793	559	666	471
Anhui	443	258	443	301
Hebei	685	390	701	370
Hunan	209	238	185	224
Jiangxi	163	175	132	119
Shanxi	129	85	127	91
All others	356	219	358	280
Total	5,528	4,341	5,422	4,768

Source: China Statistical Yearbooks.

due to unusually good weather during harvesting. National average yield in 1997/98 is expected to fall because of a return to more normal weather and also because of reduced incentives to farmers to increase fertilizer, pesticide, or labor inputs relative to other more profitable crops. However, over the long term, China is expected to gradually increase yields through additional improvements in pest management techniques, better varieties, and improved input quality and farm management.

Modest Consumption Growth Forecast

Cotton consumption is expected to rise in 1997/98 from an estimated 4.4 million metric tons in 1996/97. On a marketing year (August/July) basis through April 1997 (the most recent data available), monthly yarn output (including cotton yarn, synthetic yarn, and blended yarn) rose 7.8 percent compared with the same period the previous year. Yarn production is rising due to higher cotton supplies, bolstered by significant imports and plentiful domestic production, and reports of increased pricing flexibility on the part of the Supply and Marketing Cooperatives. Reports indicate that some Cooperatives are now selling cotton to yarn mills on the basis of 30-90 day extension of credit (rather than payment on delivery or 30-day credit). Other reports indicate cases where Cooperatives sell cotton to yarn mills at a discount to the official sales price mandated by the central government. Although technically not allowed, Cooperatives may be making a financial decision that it is better to take a manageable loss in selling the cotton "below cost" rather than the indeterminate loss incurred in holding the cotton in stock.

In general, the textile industry in China continues to suffer from rising input prices, very large debts, high operating margins, and growing competition for international markets from other textile producing countries. The large state-owned textile enterprises in China are in the most difficult financial straits, though recent press reports have attempted to claim an improvement as money-losing state-owned textile enterprises declined from 59 percent in the first quarter of 1996 to only 56 percent in

the same period in 1997. All of the difficulties in the state sector notwithstanding, China's total textile exports rose to US\$8.7 billion in the first quarter of 1997, an increase of nearly 36 percent over the same period in 1996. The 1.0 percent increase in consumption in 1996/97 and the rise in export value in early 1997 may be attributable in part to the government finally beginning to make good on at least a portion of the 3 years of accumulated export tax rebates (9 percent in 1996) owed to textile exporters.

Long-Term Import Picture

China's long term cotton trade outlook is for continuing imports and consistent, but small, exports. Cotton production is expected to increase gradually; although yields in China still have room to grow, rising domestic input prices and high competing crop prices will limit yield increases. On the demand side, consumption is also expected to increase gradually, but the rate of growth will be limited by a rising share of synthetic fiber in yarn production. Accordingly, assuming normal weather, China is expected to be a consistent net cotton importer, though occasional years of net exports are not impossible if optimal weather and policy conditions coincide. China's cotton imports are expected to be at

least 500,000 metric tons by the year 2005. Exports are expected to be quite low, but relatively stable, at roughly 40-50,000 metric tons in the year 2005.

Textiles and apparel account for roughly 30 percent of China's total export earnings. Officials in China indicate that the importance of the textile sector to the national economy means that the government will likely maintain more control over cotton than other agricultural commodities. However, as indicated earlier, growing financial pressure on the Supply and Marketing Cooperatives may move the central government to initiate some as yet unspecified reforms for cotton—the last remaining commodity where the government maintains tight control over domestic purchases, marketing, and distribution.

References

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2. Textile Asia, various issues.
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