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China - Peoples Republic of

Cotton and Products Update

November Update

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Report Highlights:

Due to weather impacts which lowered yields in major production regions, Post's MY13/14 cotton production forecast is lowered to 6.7 million tons. MY13/14 imports are forecast down significantly at 2.2 million tons as massive state stocks, import constraints and slowing consumption influence demand. On the other hand, low prices and open market access are influencing a growth trend in yarn imports that may reach 2 million tons in 2013. As of late-November, total state stocks are estimated at more than 10 million tons. A modification of the government cotton support policy is currently under consideration and may be announced in 2014.

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Executive Summary:

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MY13/14 cotton production forecast at 6.7 million tons

Based on a recent survey by China's National Cotton Market Monitoring Network (cncotton.com), MY13/14 domestic cotton production is estimated at 6.67 million tons (down 12.3 percent over the previous year) on 4.72 million planted hectares. Average yield is forecast down 9.3 percent to 1,415 Kg per hectare due to unfavorable weather impacts.

An October survey by MOA's Rural Economy Research Center (RERC) of 133 major cotton-producing counties reflected total production of 6.79 million tons. A China Cotton Association (CCA)'s household survey result indicated MY13/14 production at 6.93 million tons, down 10.4 percent over the previous year.

Information by various provincial statistics bureaus also indicates a smaller production as follows:

| | Xinjiang | Hebei | Shandong | Hubei* | Anhui** |
|--------------------------|----------|-------|----------|--------|---------|
| Area (million Ha) | 1.73 | 0.48 | 0.63 | NA | NA |
| Production(million tons) | 3.1-3.38 | 0.5 | 0.65 | 0.47 | 0.24 |

*Hubei Cotton Association; **National Cotton Market Monitoring Network

Based on strong profits in MY12/13, Post forecasts that the Xinjiang planted area (if including marginal land) will equal or have exceeded that of MY12/13. Optimal production in the northwest region, however, was curtailed by weather conditions during the growing season. Drought across Xinjiang, as well as rain and early frost in September and October in northern Xinjiang, reduced overall yields. One PCC farm close to Shihezi City reported that the average yield fell 25 percent over the previous year. Xinjiang production is estimated at 4.08 million tons (down 8.3 percent over the previous year) based on yield averaging 1,415 Kg per hectare (down 12.5 percent).

In the Yellow River region, production is estimated at 1.54 million tons, down 16.1 percent over the previous year, based on a 5.3 percent drop in average yield year to year to 1,065 Kg per hectare. Compared to cotton from other production regions, the Yellow River region cotton quality was better

than last year.

In the Yangtze River Region, production is estimated at 1.02 million tons based on average yield of 945 Kg per hectare, both down 23 percent and 17.6 percent, respectively, over the previous year. Hot and dry weather in July and August, followed by long wet days in September, caused a reduction in both production volume and overall crop quality.

| | The Yellow River Region | | The Yangtze River region | | The Northwest Region | | Nation | |
|--------------------------|-------------------------|---------------------|--------------------------|---------------------|----------------------|---------------------|---------|---------------------|
| | MY13/14 | Change over MY12/13 | MY13/14 | Change over MY12/13 | MY13/14 | Change over MY12/13 | MY13/14 | Change over MY12/13 |
| Area (million Ha) | | | | | | | 4.72 | |
| Yield(kg/Ha) | 1,065 | -5.3% | 945 | -17.6% | 1,895 | -12.5% | 1,415 | -9.3% |
| Production(million tons) | 1.54 | -16.1% | 1.02 | -23% | 4.08 | -8.3% | 6.68 | -12.3% |

Cotton classification and cotton purchase for reserve

As of November 21, the state reserved had purchased 2.46 million tons of MY13/14 cotton, 6.9 percent lower than the previous year. The state reserve imposed new quality conditions this year which are believed a strong factor in reducing the volume of eligible cotton for state purchase. Of the total purchased to date, 78 percent was Xinjiang cotton. The total purchased volume from the Yangtze River and Yellow River regions was 550,770 tons, down by 24 percent over the previous year.

As of November 24, classified cotton had reached 3.82 million tons. Xinjiang cotton accounted for 77 percent of classified cotton at 2.93 million tons.

Cotton import TRQ and release of reserve

As previously reported, industry sources estimate the government has issued an additional 1.2 million tons of tariff rate quota (TRQ) (over its WTO commitment) subject to sliding duty based on a total auctioned cotton reserve at about 3.7 million tons (based on a 3:1 ratio whereby the government allocates 1 ton of import TRQ per 3 tons of cotton reserve purchased).

China's textile sector has called for an additional release of state cotton reserve at an affordable price (from RMB17,500 to 18,000/ton) to meet demand. An official decision on the industry's request has not been announced.

Stocks remain high

According to industry sources, as of late-November, total state stocks were estimated at 10 million tons. This volume is expected to grow as the state continues to purchase MY13/14 crop under its price support program.

Consumption

The MY13/14 forecast for cotton consumption of 8.4 million tons is lower than the 8.7 million tons in the previous report as increasing yarn imports reduce the use of cotton by China's mills. Nevertheless, China's growing yarn production and textile and apparel exports support a moderate growth of cotton use in MY13/14 from the 8 million tons in the previous year.

According to China's Textile Industry Association, in the first three quarters of 2013, yarn production was 25.76 million tons and fabric production topped 494 million square meters, both up 7.45 and 7.12 percent over the previous year. Total textile and apparel export value rose to \$215.3 billion, up 11.7 percent over the previous year. Exports to southeast Asian countries spiked to \$25.1 billion, up 43 percent over the previous year. This positive performance supported a 17.4 percent rise over last year in the sector's profit margins. Industry insiders are optimistic that textile and apparel exports will grow 10 percent in 2013.

Imports

--Cotton

MY13/14 import demand is forecast significantly lower than the 4.43 million tons in MY12/13. Huge domestic stocks, TRQ constraints, state reserve stock releases and softening consumption are factors which continue to influence import demand. First quarter MY13/14 cotton imports fell by 26.4 percent to 618,340 tons, of which 108,439 tons were US origin.

-Yarn

Yarn's low price and lack of import quota attracts China's traders as a means to fill mill demands for raw material. So long as China's domestic cotton price remains above world price, yarn imports are expected to remain a strong sourcing alternative.

As indicated in the following table, yarn imports in the first ten months of 2013 climbed 46 percent over the previous year while the average price stood at \$3,212 per ton (compared to the \$3,344/ton floor price for domestic cotton). This is a net increase of 1 million tons of yarn imports as compared to the volume in 2011. Total yarn imports in 2013 are likely to reach 2 million tons.

| Partner Country | Quantity | | | % Change |
|-----------------|----------|-----------|-----------|-----------|
| | 2011 | 2012 | 2013 | 2013/2012 |
| World | 634,206 | 1,122,017 | 1,640,964 | 46 |
| India | 97,218 | 240,872 | 512,185 | 113 |
| Pakistan | 230,939 | 438,775 | 507,648 | 16 |
| Vietnam | 73,029 | 125,546 | 191,763 | 53 |
| \$/Ton | 3,804 | 3,205 | 3,212 | |

A set of new cotton production support policy is in pipeline

The recent China's Communist Party's communiqué for new economic reform emphasized a stronger role for the market to play in the allocation of resources. For agriculture, limited land resources and a crop's comparative advantage will play a major role in any economic changes in agriculture-related policies. In a recent industry seminar, a government official suggested that China may reposition cotton in its economy due to its lack of comparative advantage, compared to other crops, and the availability of international cotton resources to meet China's textile industry demands. A new policy is expected to be announced in 2014.

Current policy options reportedly under discussion include financial support for new varieties/high quality seed development to upgrade productivity, allocation of direct support to farmers by region, enhanced crop insurance and modifications of purchase programs toward a target price.

China's industry is responding by calling for more sales of state stocks at a lower price to meet the textile industry demands, and suggesting that the cotton TRQ be distributed in open auctions based on a more market-oriented bidding price.

(Exchange rate \$1=RMB6.1)

PSD (in 1,000 Bales and 1,000 Ha)

| Cotton China | 2011/2012 | | 2012/1013 | | 2013/1014 | |
|----------------------|--------------------------------|-------------|--------------------------------|-------------|--------------------------------|-------------|
| | Market Year Begin: Aug 2011 | | Market Year Begin: Aug 2012 | | Market Year Begin: Aug 2013 | |
| | USDA Official | New Post | USDA Official | New Post | USDA Official | New Post |
| Area Planted | | 5,380 | | 5,275 | | 4,720 |
| Area Harvested | 5,500 | 5,380 | 5,300 | 5,275 | 5,100 | 4,720 |
| Beginning Stocks | 10,603 | 10,603 | 31,081 | 30,181 | 50,333 | 47,956 |
| Production | 34,000 | 33,100 | 35,000 | 34,900 | 33,000 | 30,770 |
| Imports | 24,533 | 24,533 | 20,327 | 19,750 | 11,000 | 10,100 |
| MY Imports from U.S. | 0 | | 0 | | 0 | |
| Total Supply | 69,136 | 68,236 | 86,408 | 84,831 | 94,333 | 88,826 |
| Exports | 55 | 55 | 75 | 75 | 75 | 75 |
| Use | 38,000 | 38,000 | 36,000 | 36,800 | 36,000 | 38,600 |
| Loss | 0 | 0 | 0 | 0 | 0 | 0 |
| Total Dom. Cons. | 38,000 | 38,000 | 36,000 | 36,800 | 36,000 | 38,600 |
| Ending Stocks | 31,081 | 30,181 | 50,333 | 47,956 | 58,258 | 50,151 |
| Total Distribution | 69,136 | 68,236 | 86,408 | 84,831 | 94,333 | 88,826 |
| Stock to Use % | 82 | 79 | 140 | 130 | 161 | 130 |
| Yield | 1,346. | 1,340. | 1,438. | 1,441. | 1,409. | 1,415. |