



INTERNATIONAL COTTON ADVISORY COMMITTEE

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Memorandum 900

To: Delegates to the Standing Committee, Coordinating Agencies, members of the PSAP, SEEP and CSITC

From: Executive Director

Subject: Report from the Private Sector Advisory Panel (PSAP)

Date: June 7, 2011

The 57th Plenary Meeting in Santa Cruz de la Sierra, Bolivia in 1998 agreed to a proposal that had been forwarded by the Standing Committee to form a Private Sector Advisory Panel (PSAP). The PSAP was subsequently formed in 1999. According to the founding documents, the mandate of the Private Sector Advisory Panel is to foster communication between the private sector and member governments. Consultations between the PSAP and governments may cover, but are not limited to:

- Strategic issues critical to the long term growth of the cotton industry;
- Matters relating to the format and agenda for each Plenary meeting;
- Consideration of the mission of the ICAC and how it can foster the development of cotton; and
- Explore opportunities for financial support of the ICAC and its activities.

The PSAP has met 26 times since its founding, and reports have been delivered by the Chair of the PSAP at each plenary meeting. The membership on the PSAP includes representatives of producing and consuming countries, and representatives of developed and developing countries. Members represent all three major segments of the cotton value chain: producers, traders and spinners.

26th Meeting of the PSAP

Eight members of the PSAP met in Washington, DC on May 12, 2011 on the margins of the Annual Convention of the American Cotton Shippers Association. Nine private sector observers and three members of the Secretariat joined the PSAP members. Mr. Manfred Schiefer serves as Chair of the PSAP and Mr. Alois Schönberger serves as Vice Chair.

Members Present: Romano Bonadei, Filartex, Italy; Sebahattin Gazanfer, All Textiles and Raw Materials Exporters' Association of Turkey; Henning Hammer, Otto Stadlander, Germany; Adam Kay, Cotton Australia; Suresh Kotak, Kotak and Co., India; Manfred Schiefer, Schiefer Trading, USA; Alois Schönberger, Cottonex Anstalt, Poland; and Jorge Vartparonian, Camara Algodonera, Argentina.

Members Absent: Shiou-Chung Chen, Tah Tong Textile Company, Taiwan; Ahmed Elbosaty, Modern Nile Cotton Co., Egypt; Hamisi Kigwangalla, MSK Solutions Limited, Tanzania; and Joao Luiz Pessa, GFN Agricola, Brazil.

Observers: Ray Butler, ICA, UK; Jess Ennis, Cotton International, USA; Isidor Gilan, Primatex Fibre Company, Philippines; Neal Gillen, ICAC Representative to UNCITRAL; Kai Hughes, ICA, UK; Andrew Macdonald, Libero Commodities, Brazil; Buxton Midyette, Supima, USA; Peter Wakefield, Wakefield Inspection Services; and Phil Wakelyn, Cotton Council International, USA.

Secretariat: Andrie Guitchounts, Alejandro Plastina, and Terry Townsend.

Report of the 26th Meeting of the Private Sector Advisory Panel (PSAP)

Volatility in Cotton Prices

The PSAP noted the obvious, that cotton prices had been extremely volatile during the current season, resulting in numerous distortions and disruptions to trade. It was noted that there is no complete solution to the issue of price volatility, and that volatility is inherent to commodity markets. Nevertheless, the PSAP observed that improved statistics on cotton supply and use, particularly statistics on production, could reduce uncertainty and thus reduce volatility. It was observed that many countries rely on their private sectors to gather, compile and report data on cotton supply and use. The PSAP felt that because information is a public resource, information gathering is inherently a public responsibility, and the PSAP called on government officials to improve collection and reporting of cotton statistics. The PSAP acknowledged that industry must work with governments to ensure accuracy and consistency in collection and reporting of cotton statistics.

Recalling the report from the Seminar on Cotton Price Volatility organized by the Secretariat in cooperation with The World Bank in February 2011, the PSAP endorsed the conclusion of the seminar that universal adoption of metric measures and a standardized cotton season would improve transparency in the cotton industry.

It was noted that increased volatility leads to increased cost and damage to the entire cotton sector. It has a negative impact on the growth and further development of cotton and on the whole cotton chain itself. Erratic price movements in cotton are negative advertising to the cotton itself losing further market share towards man made fibre such as increased use of polyester which to same extent can be irreparable damage. The reason of volatility are internal as well as external, such as historic low stocks, aggressive speculative movements, sudden governmental intervention or restrictions such as import or export bans etc

The PSAP is supporting preventive measures to be taken by government and private sector alike to minimize the damage. To create stability and confidence in the cotton sector, sufficient stocks shall be hold to keep the price more stable, sustainable produced and marketed cotton shall further strengthen the cotton brand making the inherent cost of cotton production more transparent and the price less volatile.

It was noted that there is not a futures contract for cotton yarn, and defaults on contracts for cotton by spinners often result from the inability of spinners to hedge yarn prices. The PSAP asked the Secretariat to investigate the correlations and time lags between cotton and yarn prices so as to determine whether it might be feasible to hedge the prices of yarn using cotton futures. It was suggested that the cotton industry should approach the Intercontinental Exchange (ICE) where cotton futures are traded about developing a futures contract in cotton yarn.

The PSAP vehemently opposed the imposition of bans or limits on exports and imports of cotton, especially bans or limits applied retroactively. The PSAP noted that imports are the mirror image of exports, and policies to restrict one are intellectually and practically identical to restrictions on the other. It was observed that disruptions to trade during 2010/11 had contributed significantly to raise the average level of cotton prices and to raise the volatility of cotton prices.

The PSAP observed that disruptions to cotton marketing exacerbate problems of contract defaults and distort markets by channeling shipments to the advantage of some and the inherent disadvantage of others. Noting that such policies are rarely, if ever, imposed on chemical fiber trade, the PSAP observed that bans or limits on trade have negative long term impacts on the entire cotton value chain worldwide as spinners respond to such disruptions by reducing cotton use in favor of other fibers.

The PSAP reserved some of its harshest criticism for the private sector itself. It was noted that governments often intervene in trade matters in response to requests from segments of their own cotton value chains that are seeking economic advantage by shielding inefficiency behind government policies. Noting the improvements in the efficiency in trade in cotton textiles and clothing since the ending of the Multifibre Arrangement in 2005, the PSAP excoriated industry players and trade associations seeking to take the cotton value chain backward through requests to governments for trade protection. It was noted that some countries

having benefited the most from the elimination of MFA quotas were now among those involved in the most severe forms of trade disruption.

The PSAP is aware about the risk of increase in defaulting of contracts due to the negative impact of the volatility in the price. The PSAP urges the governments and associations on the private sector to take more efficient measures in honoring the awards by reducing any legal obstacles and simplifying the procedures as well as taking adequate measures to prevent defaulters from providing further business.

The PSAP also encourages the use of mediation on an international level like ICA as an efficient tool to avoid arbitration as the ultimate step to get the contract fulfilled. It is regarded as being mostly cheaper, more efficient and maintaining the business relationship between the market participants on an international level as already successfully implemented in several countries on a national level.

BCI

The PSAP received a report from the executive director of BCI. The report indicated that about 40,000 metric tons of BCI cotton had been produced in 2010, the first year in which the Initiative was active. The report indicated that BCI is currently in dialogue with the Joint Cotton Committee of the International Textile Manufacturers Federation (ITMF) to address the issue that the term "Better Cotton" is often understood to refer to better quality, whereas BCI means better practices at the farm level. The report indicated that a resolution is expected by September 2011. The report also indicated plans for expansion in 2011 and included a discussion of successes, such as investment of Euro 1.5 million in producer support by BCI members during 2010, and challenges, such as linking producers with ginners in the BCI supply chain.

Members of the PSAP appreciated the report from the executive director of BCI. However, there were concerns that, while BCI started out as a "wonderful idea" for improvement in mainstream production practices, **there is also a risk not to become another "marketing gimmick."**

Members of the PSAP noted that there is nothing inherently "better" about BCI cotton, and that millions of tons of cotton in many countries are produced responsibly using production practices that reach or even exceed BCI requirements.

The PSAP explicitly **pointed out that the "better" supposed to mean better cotton practices, not better cotton quality. Avoiding any inaccuracy or harm** to the cotton industry as a whole the use of the term "better" when applied to BCI cotton, the PSAP called on the managers of BCI to resolve this issue in consultation with the Joint Cotton Committee of ITMF.

Some members of the PSAP **raised their fear that** BCI is tending towards becoming another certification program that will fragment the cotton market. It was noted that initial plans for BCI called for the mainstreaming of production practices without certification or premiums, but that ginners participating in BCI in Pakistan and Brazil are charging premiums for BCI cotton. **BCI, however, confirmed that no certification program is planned which might lead to fragmentation of the market. Oppositely, BCI is rather promoting cooperation with local organization, fulfilling the sustainable criteria and bringing in first line a positive change on the farm level. As it is a non-profitable initiative it is not operating in competition with other organisations like Fairtrade or organic cotton producers, however, it enlarges its scope of application by integrating the use of biotech cotton in BCI production.** A member of the PSAP reported that the BCI secretariat appeared unwilling to engage with the cotton industries of some countries. It was noted further that the World Wildlife Fund, an initial sponsor of BCI, was working to restrict access to chemicals used in cotton production, an effort that undermines the competitiveness of cotton production.

The PSAP agreed that BCI recommendations for improved production practices are fine, provided that BCI does not encourage fragmentation of the cotton market.

It was also noted that the absences of standards defining responsible production practices provide opportunities for market exploitation, **particularly when based on self assessment.** It was noted that the development of metrics for the measurement of responsible production practices would be helpful, and the PSAP asked the Secretariat to investigate whether there is a role for the ICAC in developing such metrics for international application.

Harmonization of Phytosanitary Certificates and **Electronic Bill of Lading**

The PSAP thanked the Secretariat for raising awareness among governments of the existence of a model phytosanitary certificate that had been prepared by the Food and Agriculture Organization of the United Nations (FAO) **required by 35 countries**. The PSAP noted that documentation for cotton shipments tends to be highly complex in comparison with other commodity industries, and every effort to streamline procedures through standardization of requirements would help to improve the efficiency of cotton trade. The PSAP urged the Secretariat to continue to encourage governments to adopt the FAO model phytosanitary certificate.

Harmonization of Electronic Bill of Lading is regarded as a requirement to improve and simplify the documentation in order to accelerate the procedure in shipment of cotton in compliance with the technological progress. The Secretariat shall investigate the reason of the lack of implementation in the various countries concerned. The aim shall be a worldwide unified application to improve the documentary procedure and alleviate the shipment.

Debunking Myths about Cotton Production

Inaccurate information about cotton production is being promulgated by NGOs and advocates of organic cotton production in furtherance of marketing objectives. Common inaccuracies include the assertion that cotton production accounts for 25% of pesticide use in agriculture worldwide and that cotton accounts for a disproportionate share of water use. Actual pesticide use in cotton production is 7% of world pesticide use, and water consumption in cotton production is proportionate to cotton's share of world arable land use.

The PSAP encouraged the Secretariat to continue providing factual information about cotton production practices and its environmental and social impacts. The PSAP encouraged the Secretariat to cooperate with advocacy organizations to counter inaccurate information about the cotton sector.

Mr. **Schonberger** concluded the meeting by thanking the **Argentinian government** for their hospitality in facilitating the meeting of the PSAP. He thanked members of the PSAP and the observers for taking part in the meeting, and he thanked the Secretariat for its support.