



**PRODUCTION AND
TRADE POLICIES
AFFECTING THE
COTTON INDUSTRY**

INTERNATIONAL
COTTON
ADVISORY
COMMITTEE

September 2006

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A report by the
Secretariat of the
International Cotton Advisory Committee



Washington DC USA

GOVERNMENT SUPPORT TO THE COTTON INDUSTRY

Average international cotton prices, as measured by the Cotlook A Index, were 4 cents higher in 2005/06 than in the previous crop year. As a consequence, subsidies provided in most countries declined. Nonetheless because of a widening of the gap between Chinese domestic prices and international prices, estimated government assistance in China (Mainland) almost doubled, despite reduced production. Direct government assistance provided to the cotton sector worldwide is estimated to have increased from US\$4.7 billion in 2004/05 to US\$5 billion in 2005/06.

Eight countries offered direct income and price support in 2004/05 ranging from \$2.4 billion in the USA to \$21 million in Mexico. Direct support in 2005/06, offered in seven countries, is estimated to be in a range from \$2 billion in China (Mainland) to \$17 million in Mexico.

USA

The 2002 farm bill in the USA channels direct support through three mechanisms: a direct payment (DP), a counter-cyclical payment (CP) and a loan deficiency payment (LDP). DPs, which are independent of market prices and based on historical planted area and yield, are set at 6.67 cents per pound. CP's, which are also based on historical planted area and yield, are paid when the effective price is below the target price. The effective price is the DP plus the higher of the national average market price paid to producers or the loan rate. The target price is set at 72.4 cent per pound and the loan rate is set at 52 cent per pound. The LDP is paid when market prices are below the loan rate.

In 2004/05, LDP's amounted to \$382 million, payments due to CP's were \$1.4 billion, and DP's amounted to \$608 million. In 2005/06, LDP's are estimated at \$356 million, payments due to CP's are estimated at \$1 billion, and DP's are estimated at \$562 million.

Total U.S. net outlays to upland cotton are estimated to decline from \$4.2 billion in 2004/05 to \$3.1 billion in 2005/06. Direct U.S. support to upland cotton declined from \$2.4 billion in 2004/05 to \$1.9 billion in 2005/06. In Addition to DPs, CPs, and LDPs, which comprise U.S. direct support, total U.S. net outlays to upland cotton include emergency payments, subsidies to exporters and consumers through the Step 2 program, export credit guarantees, and other programs. The cost of the U.S subsidy program for Pima cotton was \$199 million in 2004/05 and is estimated at \$11 million for 2005/06.

European Union

Payments under the current EU Common Agricultural Policy (CAP) are based on estimated seedcotton production for a maximum of 782,000 tons in Greece and 249,000 tons in Spain. Payments include penalties for excess production, but there is a combined CAP floor payment of \$770 million euros. EU income support amounted to US\$1.1 billion in 2004/05 and is expected to be \$900 million in 2005/06. Changes in EU CAP policies effective January 1, 2006 and applicable to the 2006/07 crop year, converted 65% of the production-linked payments to EU cotton farmers into decoupled farm income support.

China (Mainland)

Policies enacted in 1999 introduced market forces to the cotton sector in China (Mainland). However, the Chinese government still covers the cost of ginning, storage, and transportation of cotton through the financing of operations of procurement agencies. A recent study by FAO (Shangnan Shui, Policies toward the Chinese Cotton Industry: the Commodity Chain Analysis Approach, FAO, 2005) suggests that since 2002 the government finances only 20% of the procurement agencies in the country. As a result of this financing, and of policies designed to prevent the free importation of cotton into the country, domestic prices in China (Mainland) adjusted for location have consistently been above international prices. However, an additional policy designed

to reduce domestic stocks has resulted in a reduction of the difference between domestic cotton prices and prices of Chinese cotton offered in international markets. As there is no source of government expenditures in support of the cotton market in China (Mainland), the Secretariat uses the difference between domestic and international prices (as reported by Cotlook Limited) as an estimate of support, plus 10 U.S. cents per pound on 20% of production to account for ginning, storage and transportation costs.

The price differential between the CC index (an index of mill delivered cotton in China) and the Cotlook A Index (adjusted to include import duties, value added tax, and transportation to mills) increased from 5.8 U.S. cents per pound in 2004/05 to 14 U.S. cents in 2005/06. As a result, the estimate of benefits from border policies increased from \$800 million in 2004/05 to \$1.8 billion in 2005/06. Financing of the activities of procurement agencies is estimated at \$279 million in 2004/05 and \$254 million in 2005/06. The total estimate of support of the cotton market in China (Mainland) increased from \$1.1 billion in 2004/05 to \$2 billion in 2005/06.

Other Countries

Price increases in 2005/06 reduced the level of assistance to cotton producing farmers in developing countries. In Mexico, a support price mechanism with a target price of 67 U.S. cents per pound resulted in a payment of 8 U.S. cents per pound, or \$24 million, in 2004/05 and is expected to result in payments of 5 U.S. cents per pound, or \$17 million, in 2005/06. In Turkey, a premium of 6 U.S. cents per pound was offered in 2004/05 (equivalent to \$115 million), and in 2005/06 the premium declined to 4 U.S. cents per pound (equivalent to \$69 million).

In Colombia, as a result of increased imports of subsidized cotton and rapid revaluation against the US dollar, the government paid an average of 1 million pesos per ton of lint (18 U.S. cents per pound) in 2004/05, and 1.1 million pesos per ton (21 U.S. cents per pound) in 2005/06.

In Benin, government support amounting to \$34 million was paid in 2004/05 to help growers cope with declining prices, but support was not offered in 2005/06, and production in the country declined drastically. In Côte d'Ivoire, the government pledged to provide \$14 million in emergency assistance to cotton growers in 2004/05. However, as in the past few seasons, support was not distributed.

Level of Direct Assistance Provided by Governments to the Cotton Sector Through Production Programs *

Country	2004/05			2005/06 **		
	Production	Average Assistance per Pound Produced	Assistance to Production	Production	Average Assistance per Pound Produced	Assistance to Production
	1,000 tons	US cents	US\$ Millions	1,000 tons	US cents	US\$ Millions
China (Mainland)	6,324	8	1,087	5,770	16	2,039
USA	5,062	22	2,411	5,204	17	1,947
Greece	390	96	822	430	75	712
Spain	110	93	226	110	81	196
Turkey	900	6	115	800	4	69
Colombia	55	18	21	45	21	21
Mexico	138	8	24	138	5	17
Benin	171	9	34			
All Countries	13,150	16	4,741	12,497	18	5,000

* Income and price support programs only. Credit and other assistance not included. ** Preliminary.

Despite export and production subsidies amounting to a combined \$11 million in 2003/04, the Government of Egypt did not make any direct subsidy payment in 2004/05 or 2005/06. The government has rather increased imports of lower price cotton in order to maintain the profitability of textile mills, and since 2004/05 the Alexandria Cotton Exporters Association (ALCOTEXA) no longer sets export prices.

In Brazil, given the low domestic prices in 2004/05, the government acquired 474,000 tons of seed cotton in the first half of 2005 in an effort to create upward pressure on prices and avoid government payments due to minimum price regulations. As prices increased later in the year, cotton was sold at a profit.

Direct Assistance to Exports

The government of India made payments equivalent to \$7 million to compensate cotton exporters for higher transportation costs in 2004/05.

Assistance in the USA is provided through the Step 2 program offered to both exporters and domestic consumers of raw cotton. In 2004/05, the U.S. government disbursed \$250 million to exporters, and 2005/06 payments are estimated to have declined to \$186 million. The Step 2 program covers upland cotton, and exports of U.S. Pima are covered by a separate program, through which \$199 million were paid to exporters in 2004/05 and \$11 million are estimated to be paid in 2005/06. Following the conclusions of a special panel of the WTO, the U.S. Government decided to end the Step 2 program as of July 31 2006.

Level of Direct Assistance Provided by Governments to the Cotton Sector Through Export Programs

Country	2004/05			2005/06 **		
	Exports	Average Assistance per Pound Exported	Assistance to Exports	Exports	Average Assistance per Pound Exported	Assistance to Exports
	1,000 tons	US cents	US\$ Millions	1,000 tons	US cents	US\$ Millions
USA	3,137	6	449	3,701	2	197
Upland cotton	2,965	4	250	3,576	2	186
Pima	172	53	199	125	4	11
India	175	2	7			
Total	3,312	6	456	3,701	2	197

* Preliminary.

Cotton: World Statistics

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2005/06 SUPPLY AND USE OF COTTON BY COUNTRY										
	AREA	YIELD	PROD	BEG STKS	IMPORTS	CONS	EXPORTS	END STKS	S/U *	
	000 Ha	Kg/Ha	000 Metric Tons							Ratio
CANADA				10	42	45		7	0.17	
CUBA	4	269	1	5	9	10		5	0.50	
DOM. REP.				2	2				0.31	
MEXICO	127	1,088	138	264	320	432	45	244	0.51	
USA	5,545	938	5,204	1,230	7	1,306	3,701	1,433	0.29	
Sub total	5,681	941	5,343	1,510	379	1,796	3,746	1,690	0.30	
EL SALVADOR				5	21	21		5	0.25	
GUATEMALA				8	21	21		8	0.38	
HONDURAS				1	3	3		1	0.20	
NICARAGUA	2	538	1	0	1	1		0	0.18	
Sub total	2	538	1	14	46	47		14	0.31	
ARGENTINA	311	421	131	89	39	137	30	92	0.55	
BOLIVIA	10	653	7	7	11	11	7	7	0.39	
BRAZIL	851	1,247	1,061	954	35	870	460	719	0.54	
CHILE				3	14	14		3	0.22	
COLOMBIA	58	782	45	34	59	105		34	0.33	
ECUADOR	1	436	1	9	16	17		9	0.53	
PARAGUAY	259	270	70	26		5	65	26	0.37	
PERU	85	828	70	65	22	90	2	65	0.71	
URUGUAY				1	4	4		1	0.15	
VENEZUELA	15	340	5	14	18	21	2	14	0.60	
Sub total	1,591	874	1,390	1,200	218	1,273	566	970	0.53	
ALGERIA	0	560	0	5	22	22		5	0.24	
EGYPT	274	733	201	100	101	210	110	82	0.26	
MOROCCO	2	515	1	10	41	42		10	0.25	
SUDAN	169	496	84	57	2	2	82	57	0.68	
TUNISIA				6	16	16		6	0.35	
Sub total	446	642	286	179	181	293	192	161	0.33	
BENIN	200	415	83	103		3	116	68	0.57	
BURKINA FASO	641	465	298	144		2	283	156	0.55	
CAMEROON	230	465	100	78		1	116	61	0.53	
CENT. AFR. REP.	8	250	2	2			3	1	0.23	
CHAD	315	248	78	41		1	82	37	0.44	
COTE D'IVOIRE	243	444	108	17		10	78	38	0.43	
GUINEA	14	222	3	1			3	1	0.40	
MADAGASCAR	23	425	10	3		5	5	3	0.33	
MALI	552	417	230	118		4	241	104	0.42	
NIGER	5	413	2	0		1			0.18	
SENEGAL	48	373	18	10		1	21	5	0.24	
TOGO	140	229	32	43			48	28	0.58	
Sub total	2,418	399	964	563		28	996	502	0.49	
ANGOLA	2	286	1	0		1		0	0.12	
ETHIOPIA	83	265	22	5		20	2	5	0.24	
GHANA	26	301	8	5		3	5	5	0.61	
KENYA	50	112	6	4	17	22		5	0.22	
MOZAMBIQUE	225	111	25	16		2	24	15	0.58	
NIGERIA	330	253	84	40	15	47	40	52	0.59	
SOUTH AFRICA	28	750	21	21	27	46	7	16	0.30	
TANZANIA	434	165	72	118		16	103	71	0.60	
UGANDA	125	148	19	28		3	34	10	0.28	
CONGO, DR	10	281	3	2	6		9	2	0.25	
ZAMBIA	275	236	79	57		12	80	43	0.47	
ZIMBABWE	380	303	115	54		26	86	58	0.52	
Sub total	2,039	233	475	366	84	231	396	297	0.47	
BULGARIA	9	257	2	9	17	19	1	8	0.42	
CZECH REP.				25	38	40	1	23	0.55	
SLOVAK REP.				4	10	10		3	0.32	
HUNGARY				4	10	11		4	0.37	
POLAND				13	35	37		11	0.31	
ROMANIA				5	17	17		4	0.26	
FORMER YUGOSLAVIA				6	13	13		6	0.43	
Sub total	9	257	2	67	143	150	2	60	0.40	

- World cotton supply/demand statistics since 1940/41 and by country since 1980/81
- Monthly and season average prices of cotton and polyester
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