Chinas’ Cotton Sector
Outlook and New Policy Regime

Dale Cougot | 20 February 2015
Creating value is our business
China Holds Dominant World Cotton Position

Current policies are shifting world S&D dynamics

Cotton Production

Cotton Imports

Cotton Mill Use

Cotton Stocks

Source: USDA World Agricultural Supply and Demand Estimates (million 480 Lb. Bales)
We must all think bigger than COTTON!!!
China National Policy Overview

Direct subsidies to Farmers
National Strategic Reserve Activities
Import Policies
  WTO 1% Tariff-Rate Quotas
  Sliding Scale Quotas
  Processing Quotas
  WTO 40% Tariff Rate Duty
Agricultural Policies
  Rural Infrastructure and Social Welfare
  Support for Alternative Crops
Textile Policies
  Export Vat Rebates
  Tax Exemptions, Refunds & Reductions
Economic Policies
  Exchange Rates
  Monetary Policies
  Macro Policies
  Preferential Lending/Debt Forgiveness

*Provincial Policies*

China Fiber Outlook 2015/16

Cotton Production Prospects
  Xinjiang
  Interior Region
Cotton Yarn Demand
  Domestic Mill Use
  Imports of Yarn
Cotton Lint Imports
  Quota
  Non-Quota
Textile Fiber Demand
  Cotton
  Polyester
Reserve Stock
  Purchases & Releases
  Overview
Ending Stock
  Impact to the World
  Impact to Prices and Cotton Demand

Impact to the World
Impact to Prices and Cotton Demand
1) To better control **scale and rhythm** of importing agricultural products.

2) To improve **management of import/export tariff and quota** of important agricultural products such as grain, cotton, sugar etc.

3) To strictly implement cotton sliding duty quota policy. To **crack down smuggling** of agricultural products.

4) To **improve the formation of the pricing mechanism** of agricultural products. To increase the income of farmers by maintaining reasonable prices of agricultural products.

5) To **improve the direct subsidy** mechanism based on the experience of subsiding Xinjiang cotton, northeast and Inner Mongolia soybean under target prices. Aim to reduce operating costs and ensure timely and full payment of subsidy to farmers.

6) To promote agricultural products **insurance system**.

7) To **regulate reasonable size of reserve scale** for important agricultural products like grain, cotton, sugar, meat etc.
Fiber Prices

China’s current situation stems from 2010/11, spike to over $2.00!

Cents per Lb

- **China Cotton Price**
- **A Index**
China’s cotton imports are under control?

Well how about:
40% duty,
Free Trade zones,
Yarn imports,
smuggling,
etc
# China Reserve Policy Overview

<table>
<thead>
<tr>
<th></th>
<th>Million Bales</th>
<th>Beginning Stocks</th>
<th>Reserve Domestic Purchase</th>
<th>Reserve Import Purchase</th>
<th>Release Local Cotton</th>
<th>Release Import Cotton</th>
<th>Reserve Ending Stocks</th>
<th>Total China Stocks</th>
<th>Target Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>08/09</td>
<td>5.49</td>
<td>12.87</td>
<td>0.00</td>
<td>3.14</td>
<td>2.43</td>
<td>12.79</td>
<td>21.37</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>09/10</td>
<td>12.79</td>
<td>0.00</td>
<td>0.00</td>
<td>4.33</td>
<td>.82</td>
<td>7.63</td>
<td>14.25</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>10/11</td>
<td>7.63</td>
<td>0.00</td>
<td>0.00</td>
<td>4.78</td>
<td>0.00</td>
<td>2.85</td>
<td>10.60</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>11/12</td>
<td>2.85</td>
<td>14.42</td>
<td>3.67</td>
<td>1.20</td>
<td>0.38</td>
<td>19.38</td>
<td>31.08</td>
<td>$1.40</td>
<td></td>
</tr>
<tr>
<td>12/13</td>
<td>19.38</td>
<td>31.41</td>
<td>3.45</td>
<td>14.97</td>
<td>4.42</td>
<td>34.57</td>
<td>50.36</td>
<td>$1.45</td>
<td></td>
</tr>
<tr>
<td>13/14</td>
<td>34.57</td>
<td>30.22</td>
<td>0.62</td>
<td>10.19</td>
<td>0.68</td>
<td>54.55</td>
<td>62.71</td>
<td>$145</td>
<td></td>
</tr>
<tr>
<td>14/15</td>
<td>54.55</td>
<td>0.00</td>
<td>0.00</td>
<td>1.43</td>
<td>0.32</td>
<td>52.80</td>
<td>64.46</td>
<td>NA</td>
<td></td>
</tr>
<tr>
<td>11 to 14</td>
<td>76.05</td>
<td>7.74</td>
<td>27.79</td>
<td>5.80</td>
<td></td>
<td>49.95</td>
<td>53.86</td>
<td>$1.40+</td>
<td></td>
</tr>
</tbody>
</table>

**2011** - Announce intent to support farmers at 19,800 yuan/ton ($1.35 to $1.40 per lb)
**2012** - Increases support price to 20,400 yuan/ton ($1.40 per lb.)
**2013** - Held support at 20,400 yuan/ton
**2014** - Change of strategy to direct farm subsidies, Target Price for Xinjiang at 19,800
  - Other provinces, direct support at 2,000 yuan/ton ($0.15 cents/lb)
**2015** – No release of reserve until the local crop is consumed and no damage to local prices.
China’s price support structure have derailed several times over the last several years.
Fiber Prices

The shaded area shows that China had several opportunities to buy using the 40% duty.

The average China Cotton Price was 22.76 cents per lb, while the A Index was 44.73 cents per lb.
## Supplies Around the Globe React

**2014/15 China stocks flat, rest of world rising!**

<table>
<thead>
<tr>
<th>Crop less Use Outside China</th>
<th>China’s Imports</th>
<th>Change in China’s Stocks</th>
<th>Change in Stocks Outside China</th>
<th>SUR Outside China</th>
<th>Annual A-Index</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>2009/10</strong></td>
<td>1.53</td>
<td>10.90</td>
<td><strong>-7.12</strong></td>
<td><strong>-7.73</strong></td>
<td>47%</td>
</tr>
<tr>
<td><strong>2010/11</strong></td>
<td>17.31</td>
<td>11.98</td>
<td><strong>-3.64</strong></td>
<td><strong>6.85</strong></td>
<td>57%</td>
</tr>
<tr>
<td><strong>2011/12</strong></td>
<td>27.44</td>
<td>24.53</td>
<td><strong>20.49</strong></td>
<td><strong>2.75</strong></td>
<td>65%</td>
</tr>
<tr>
<td><strong>2012/13</strong></td>
<td>16.80</td>
<td>20.33</td>
<td><strong>19.28</strong></td>
<td><strong>-3.11</strong></td>
<td>55%</td>
</tr>
<tr>
<td><strong>2013/14</strong></td>
<td>13.09</td>
<td>14.12</td>
<td><strong>12.35</strong></td>
<td><strong>-0.66</strong></td>
<td>52%</td>
</tr>
<tr>
<td><strong>2014/15</strong></td>
<td>13.616</td>
<td>7.30</td>
<td><strong>1.75</strong></td>
<td><strong>6.42</strong></td>
<td>60%</td>
</tr>
<tr>
<td><strong>2015/16</strong></td>
<td><strong>7.40</strong></td>
<td><strong>7.00</strong></td>
<td><strong>-2.60</strong></td>
<td><strong>-0.40</strong></td>
<td>57%</td>
</tr>
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Creating value is our business
<table>
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<tr>
<th>China Policy Impact</th>
<th>Non-China Supply Surplus</th>
<th>Non-China World Supply Deficit</th>
</tr>
</thead>
<tbody>
<tr>
<td>China Supply Surplus (Excluding Reserve Stocks)</td>
<td>2011/12/13/14</td>
<td>2014/15</td>
</tr>
<tr>
<td>• Limited import cotton demand</td>
<td>• Limited import cotton demand</td>
<td>• Weak import cotton demand</td>
</tr>
<tr>
<td>• Local price under pressure</td>
<td>• Local price under pressure</td>
<td>• Local prices under pressure</td>
</tr>
<tr>
<td>• Int’l price under pressure</td>
<td>• Int’l price under pressure</td>
<td>• Int’l prices on the rise</td>
</tr>
<tr>
<td>• Yarn imports growth flattened</td>
<td>• Yarn imports growth flattened</td>
<td>• Yarn exports on the rise</td>
</tr>
<tr>
<td>• Slim chance for reserve release</td>
<td>• Yarn imports in high demand</td>
<td>• Best chance to release reserve</td>
</tr>
</tbody>
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<thead>
<tr>
<th>China Supply Deficit (Excluding Reserve Stocks)</th>
<th>2014/15</th>
<th>2015/16</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Good import cotton demand</td>
<td>• Weak import cotton demand</td>
<td></td>
</tr>
<tr>
<td>• Local price Elevated (reserve action)</td>
<td>• Local prices supported</td>
<td></td>
</tr>
<tr>
<td>• Int’l price down (40% duty dependent)</td>
<td>• Int’l prices on the rise</td>
<td></td>
</tr>
<tr>
<td>• Yarn imports in high demand</td>
<td>• Yarn imports limited</td>
<td></td>
</tr>
<tr>
<td>• Good chance for release of reserve</td>
<td>• Best chance to release reserve</td>
<td></td>
</tr>
</tbody>
</table>
The reserve may be able to release in 15/16.....
BUT, wait did anyone think about polyester...
China Poly versus China Cotton Prices

Cents per Lb

Source: Cotlook Price Series
World Consumption of Textile Fibers

Source: PCI data
Wait the China Economy will build demand
A 1% increase in GDP per capita generates, on average, a higher increase in demand for each fiber than a 1% decline in (relative) prices.

World cotton use reached new high at 3.9 kg in 2006 and 4.0 kg in 2007, it then declined into 2012 falling to 3.3 kg, the lowest in over a decade.

Source: International Cotton Advisory Committee
World Synthetic Fibers continues to be dominated by Asia, specifically China!

1) Asia accounts for more than three quarters of the world ManMade fiber production.

2) When one refers to Asia, they mean China.

3) China the largest market, saw one of the largest gains from 2012 to 2013, +7.7%.

4) Global production of all manufactured fibers increased 5.0% in 2014 e.

<table>
<thead>
<tr>
<th>Global % Share</th>
<th>2012</th>
<th>2013</th>
<th>Subtotal</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>67.1%</td>
<td>68.3%</td>
<td></td>
</tr>
<tr>
<td>Taiwan</td>
<td>3.9%</td>
<td>3.6%</td>
<td></td>
</tr>
<tr>
<td>South Korea</td>
<td>3.1%</td>
<td>2.9%</td>
<td></td>
</tr>
<tr>
<td>Malaysia</td>
<td>2.4%</td>
<td>2.4%</td>
<td>77.2%</td>
</tr>
<tr>
<td>India</td>
<td>7.2%</td>
<td>6.9%</td>
<td></td>
</tr>
<tr>
<td>Pakistan</td>
<td>0.8%</td>
<td>0.7%</td>
<td>7.6%</td>
</tr>
<tr>
<td>USA</td>
<td>3.8%</td>
<td>3.7%</td>
<td></td>
</tr>
<tr>
<td>Mexico</td>
<td>0.4%</td>
<td>0.4%</td>
<td></td>
</tr>
<tr>
<td>Brazil</td>
<td>0.6%</td>
<td>0.6%</td>
<td>4.7%</td>
</tr>
<tr>
<td>Western Europe</td>
<td>2.3%</td>
<td>2.0%</td>
<td></td>
</tr>
<tr>
<td>Turkey</td>
<td>1.6%</td>
<td>1.5%</td>
<td>3.5%</td>
</tr>
<tr>
<td>Other</td>
<td>6.8%</td>
<td>7.0%</td>
<td>7.0%</td>
</tr>
</tbody>
</table>

Source: Fiber Organon 2014

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Source: PCI / Redbook & Fibre Organon 2014
2020 Polyester Filament and Staple accounts for over 77% of MMF and 56% of total fibers.

- **Capacity**
  - 2000
  - 2014 F
  - 2020 E

- **Fiber Use**
  - 2000
  - 2014 F
  - 2020 E

**Compound Annual Growth Rates**

<table>
<thead>
<tr>
<th>Period</th>
<th>Cotton</th>
<th>Wool</th>
<th>MMF Cellulosic</th>
<th>Acrylic</th>
<th>Nylon Staple</th>
<th>Nylon Filament</th>
<th>Polyester Staple</th>
<th>Polyester Filament</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000-2014</td>
<td>1.5</td>
<td>-2.2</td>
<td>6.0</td>
<td>-2.6</td>
<td>-10.9</td>
<td>1.0</td>
<td>4.5</td>
<td>8.3</td>
</tr>
<tr>
<td>2014-2020</td>
<td>2.5</td>
<td>1.5</td>
<td>4.8</td>
<td>0.9</td>
<td>12.2</td>
<td>3.8</td>
<td>2.2</td>
<td>4.5</td>
</tr>
</tbody>
</table>

**Source:** PCI / Redbook
China Holds Dominant World Cotton Position

Current policies are shifting world S&D dynamics

Cotton Production

Cotton Imports

Cotton Mill Use

Cotton Stocks

Source: USDA World Agricultural Supply and Demand Estimates (million 480 Lb. Bales)
Conclusions

China cotton production down (8 to 9%) in the interior and flat in XJ.
China farm subsidy tested again in 2015/16 on a wider basis
China crop insurance programs are tested in 2015/16
China cotton consumption grows (3%) modestly in the coming years.
China imports exceed the WTO level by 2 to 3 million bales
China yarn imports grow (investment in neighboring markets)
China cotton per capita continues to fade to new MMF materials
World cotton demand returns to long-term growth rate (2.5 to 3.0%).
Non-China cotton demand returns back to pre WTO markets
Non-China cotton supplies falls (specifically US, Australia and Brazil)
Cotton supplies are destined to remain high for several years.
China reserves fall modestly by 2 million bales
Cotton prices influenced by the large stocks, and limits growths.
Biggest cotton price influencer, China’s Policy changes.
- Short-term India’s stock policy.
Thank you