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THE SHIFTING PATTERN OF COTTON SUPPLY SINCE 2000

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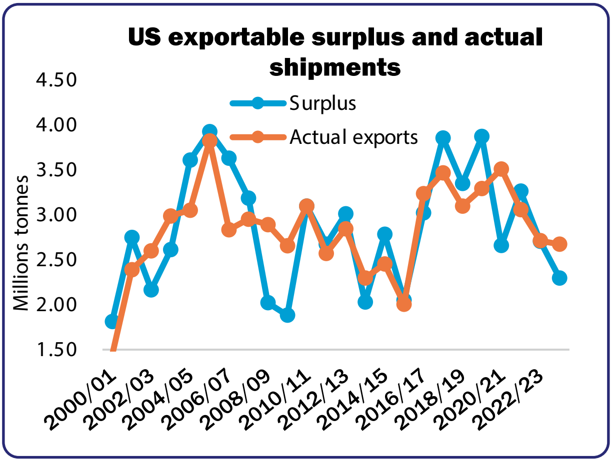
In 2023, a feeling of stasis seemed to settle over the cotton market. Futures and physical prices were range bound as consumer demand for apparel and home textiles stagnated, prompting a slowdown in activity throughout the cotton value chain. However, if we adjust our perspective and consider a longer timeframe, it becomes apparent that deeper undercurrents in the market have nevertheless been in motion. The source of supply to the global market is shifting southwards, a move that has major implications for the patterns of trade both now and in the future.

Unstable US supply

First, let us take a view of the northern half of the globe, historically the location of most cotton production and the source of the majority of international trade. In terms of exports, the US is clearly the stand-out market, and has been for hundreds of years. However, the crown is now under threat and indeed may already have been snatched away by Brazil, which we will come to in due course.

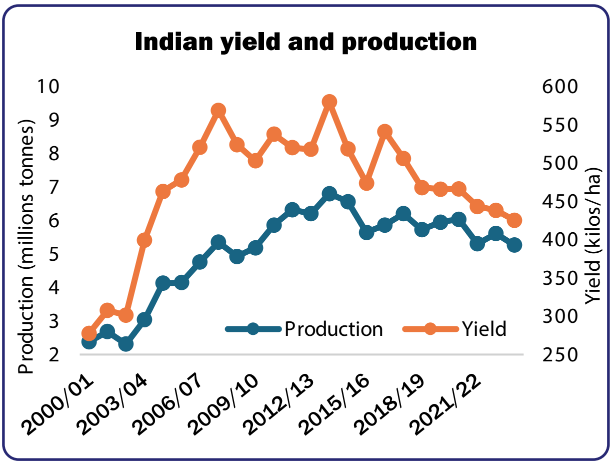
As domestic consumption has declined substantially since the start of the 21st century,



the volume of US cotton available for shipment is now determined almost exclusively by the outcomes of the successive growing campaigns, with a particular focus on Texas. In the past three seasons, that state has accounted for between 55 and 58 percent of the total area planted to cotton across the nation. However, the results have been extremely variable, in terms of both yield and abandonment, such that output has fallen from 7.7 million bales in 2021/22 to just 2.8 million in 2023/24. It is apparent, then, that exportable surplus is extremely vulnerable to the growing conditions in Texas. The reason these are so unreliable is down to the fact that much of the area cultivated is in non-irrigated land in West Texas, which is supremely susceptible to periods of drought, exacerbated in recent years by climate change and the *La Niña* pattern. In 2023/24, the exportable surplus is estimated to be the second smallest of the decade and actual exports (according to the USDA's February forecast) the lowest since 2015/16.

India's stagnating yields and declining exports

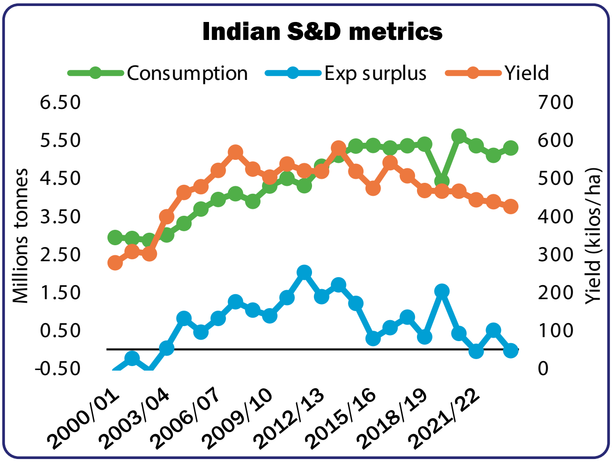
Another shift in the pattern of supply that has been observed in the years since the turn of the century is the accession of India to the position of the world's largest producer, and its subsequent relinquishment of that title. India's progress between 2000 and 2014 to its highest ever output of 6.8 million tonnes (40 million local-sized bales) is directly attributable to the widespread adoption of genetically modified cotton varieties. In that period, yields climbed from below 300 kilos per hectare to a peak of 580 (still a long way below those achieved in the mechanised producing centres, i.e. the US, China, Brazil and Australia). However, those yields were not sustained and for the past ten years, productivity per hectare has plateaued and then fallen.



The reason for the decline is not absolutely clear, and more than one factor is certainly at play.

In fact, many explanations are advanced, including poor soil health, erratic Monsoon patterns associated with global climate change, outdated seed technology and counterfeit seed production. Moreover, with a cotton farming population of six million cultivating 12 million hectares on an annual basis, the transfer of technology is logistically complicated and expensive.

While a repetition of a 40-million-bale crop seems out of reach for now, cotton demand in India has risen more or less steadily for the past 20+ years. Between 2000/01 and 2023/24, consumption by the domestic textiles industry (which serves both the huge Indian consumer base and export markets in the US, Europe and the UAE in particular) has increased by 80 percent. At the peak in 2011/12, India’s exportable surplus was as high as two million tonnes. However, the combination of falling supply and increasing demand means that in the past nine years (ignoring for these purposes 2019/20 when the textile industry was most acutely disrupted by Covid), the surplus has declined to less than half a million tonnes on average, and a deficit has begun to emerge.



In fact, it is possible to imagine that the path forward in India might resemble that taken by other erstwhile suppliers to the global market (China, Pakistan and Turkey, for instance) which have grown their domestic textiles industries to the point where demand now outstrips the local supply and the pattern of trade has shifted in favour of imports. To illustrate: just ten years ago, Central Asian countries contributed 11 percent of the total exportable supply. Today, that figure is negligible. India accounted for 21 percent in 2013/14, while in 2023/24, the Cotton Association of India forecasts exports at just 1.4 million bales or 238,000 tonnes.

Challenges for the Franc Zone

The third major source of exports in the Northern Hemisphere is now the African Franc Zone. This market shares many characteristics with India – the cotton produced here is handpicked, yields are stubbornly low, and output is once again affected by rainfall patterns that have become increasingly erratic thanks to climate change. The key difference, of course, is that there is virtually no corresponding domestic textile industry, so the majority of output is destined for export, with a large focus on Bangladesh, which takes around 50 percent of all exports from the AFZ in any given year.

Of course, any over-exposure to a single market creates a vulnerability and this appears to be the case for the Franc Zone. While Bangladesh spinners remain loyal in their preference for West African cotton for now, the rise of Brazil – which we will come to momentarily – must surely represent a clear threat. For a textiles market where margins are increasingly tight, it is not difficult to envisage a future in which more Bangladesh spinners switch allegiance in favour of a more consistent and cheaper supply from elsewhere.

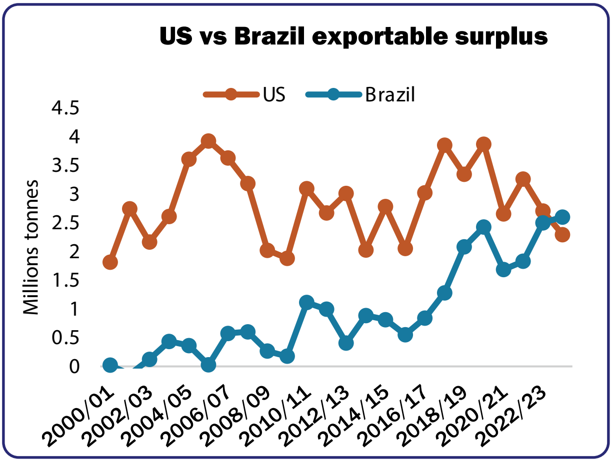
As in India, the barriers to achieving a sustained improvement in yields in a smallholder environment are significant. The development of technology and mechanisation adapted to the African production model represents a major challenge – as does sustaining the commitment to cotton of a younger generation of producers. The alarming (since it was largely unheralded) damage inflicted by *jassids* in the 2022/23 season saw regional output fall below a million tonnes for the first time since 2015/16. Broader issues with a negative impact include a fragile security situation in certain countries and the threat to cohesion posed by the departure of three countries from the ECOWAS regional economic community. For all these reasons, although the record Franc Zone crop (over 1.3 million tonnes) was achieved as recently as 2021/22, that figure may for now prove to be the high-water mark of regional production.

The rise of Brazilian cotton

And so, let us turn to the southern half of the globe. The fact that Brazil has already crept into this narrative twice – in the discussions of the US and African Franc Zone – indicates its substantial and growing influence on the world market for cotton. The fact is that by any measure – area, yield, output, exportable surplus, profitability – the performance of Brazilian production has been extraordinary in the past 24 seasons.

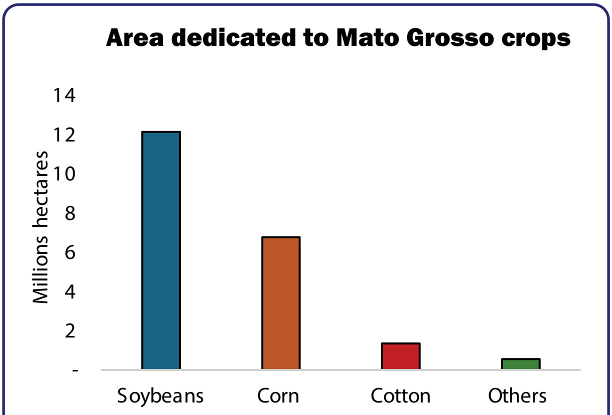
The area cultivated with the crop has doubled over the period, as production has migrated to then expanded in Mato Grosso state. Yields have improved by a similar margin, farmers assisted in their enterprise by a sophisticated R&D programme and large-scale investment in cotton-specific infrastructure. (It is worth remembering, also, that these per-hectare returns are achieved in a rain-grown environment, albeit one with an enviably predictable pattern.) As a result, cotton output, which amounted to around 900,000 tonnes at the turn of the century, has exploded to the extent that three million tonnes per annum may now be considered a minimum.

The record of 3.17 million achieved in 2022/23 seems very likely to be surpassed in the current campaign.



expansion. The major producing state, Mato Grosso, which is forecast to contribute more than 70 percent of national production in 2024, is two and half times the size of Germany. The bulk of the state's cotton is cultivated according to a lucrative double-cropping model, whereby cotton is planted immediately after the early soybean harvest, thus providing the producer with two crops in a single season. Moreover, the state's cotton

Meanwhile, consumption of lint in the domestic textiles market has remained stable, so all of the increase is now directed at the export market. In 2023/24, Brazil's surplus is expected to amount to around 2.6 million tonnes, which would take it higher than the equivalent figure for the US for the first time.



Source: CONAB

Of course, there are a few limitations in this relatively young market. Establishing the production infrastructure takes time and is expensive, while the logistics of transporting such a large quantity of cotton over vast distances and effecting timely delivery (at present most cotton is shipped from a single port) represent a significant challenge. However, the dynamism apparent within the industry is remarkable and it feels unwise to underestimate its capacity to respond to and overcome the problems it currently faces.

Most of all, though, it is the availability of land that affords the greatest opportunity for further

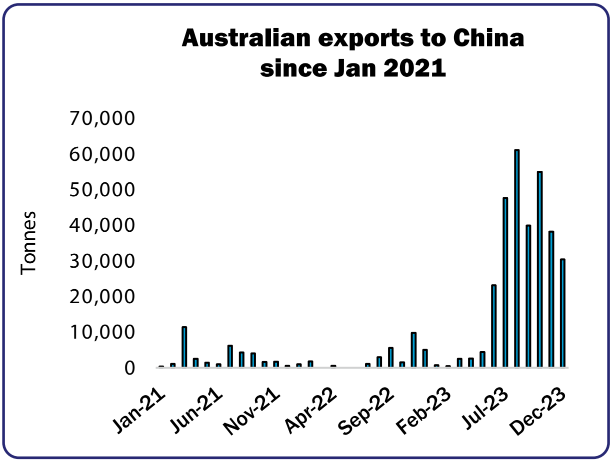
area (estimated this year at nearly 1.35 million hectares) is dwarfed by that devoted to soybeans (12.13 million) and corn (6.77 million).

Cyclical production in Australia

Lastly in our tour of the major producers, we come to Australia. While for other countries, the impact of a shifting climate may be a fairly recent phenomenon, Australian farmers have been navigating cyclical droughts for many years. In dry periods, output can be sustained by water in storage.

However, in an extended drought (such as the one endured towards the end of the last decade), irrigated production will also succumb. Thus, with little to no domestic consumption to consider, exportable supply can fluctuate between less than 200,000 tonnes and 1.25 million. This season, *La Niña* conditions (associated with greater rainfall in the Southern Hemisphere) gave way to an *El Niño* pattern ahead of the 2023/24 planting period. However, no drought has appeared so far; indeed, water storage facilities have been replenished by atypical rainfall, and prospects seem good.

In any case, the principal impact on the pattern of export trade in recent seasons has arisen from political rather than productivity concerns. Diplomatic relations with China – by virtue of its proximity the 'natural' market for Australian fibre – have been strained and a "soft ban" on imports of goods from



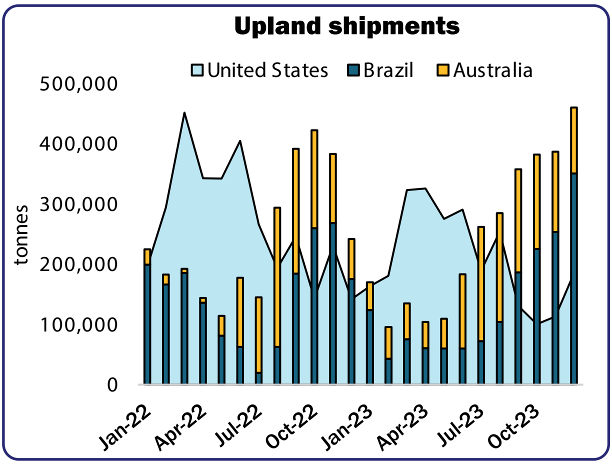
Australia (including cotton) was imposed in 2020. Now, there are signs that the unofficial injunction has been lifted: shipments to China between June and December 2023 amounted to almost 300,000 tonnes, compared to around 75,000 tonnes in the two and a half years before that. How the situation develops from here remains to be seen, of course.

New patterns emerging

So, where do all these shifts take us? First of all, it is clear that exports from the Southern Hemisphere now represent a strong challenge to the supremacy of the US. In 2022/23, USDA estimates that trade in Australian and Brazilian cotton alone overtook exports from the US by 0.5 percent. In 2023/24, the Department expects that margin to grow to 37 percent – and while Australian availability will always tend to fluctuate, as discussed above, Brazilian output above three million tonnes is expected to endure.

The implication, in the first instance, is a shift in the timing of the supply to greater year-round availability in favour of the traditional rises and falls associated with Northern Hemisphere production cycles.

Secondly, though, it also begins to call into question the efficacy of the ICE futures market as a primary mechanism for global cotton price discovery. For instance, at the time of writing, the No. 2 contract has just broken out of its long-term range between 75 and 90 cents per lb, principally in response to a tightening of the US balance sheet. The restrictions on



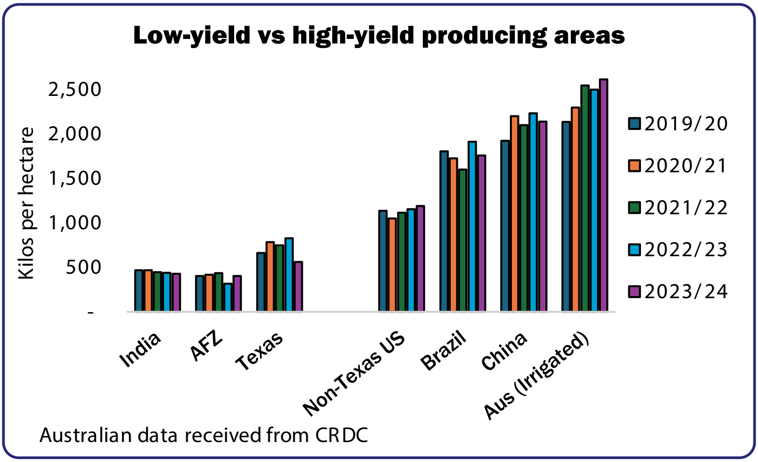
supply in that market are not replicated elsewhere, however: plenty of cotton remains unclaimed from the Brazil 2023 crop and another bumper output is looming just over the horizon. If these higher levels for ICE futures were to persist in the months ahead, they may well ration supply of US cotton, but the downward pressure on the basis for Brazilian would be likely to increase, bringing greater stratification of physical pricing.

Then, while it should be no surprise that the different models of production (commercial vs smallholder) achieve significantly different results in terms of yields, the contrasting – and further diverging – fortunes are striking. In India and the African Franc Zone, productivity has flatlined or is in decline, while a steady improvement is perceptible in China, Brazil and Australia, so the already substantial gap is widening.

Finally, one other marked pattern in terms of yield is the growing disparity in the productivity per hectare in Texas and the rest of the US. While non-Texas yields seem to be following the same pattern as in other mechanised cotton-producing zones, yields for the most important US state have averaged no more than 725 kilos per hectare in the past 24 seasons. In the current season, USDA calculates a total of just 558 kilos per hectare.

Conclusion

On the supply side of the balance sheet, the outcomes of the 2023/24 production campaigns are by now fairly clear. Crops in the US, China, Pakistan and the African Franc Zone have been harvested, as has more than half of Indian production. Even in the Southern Hemisphere, the forecasts are viewed with no little confidence, discounting for now the possibility of any unforeseen events.



Meanwhile, at the start of this essay, we observed that since the beginning of the year, there have at last been some signs that the tide of demand is turning. Increased purchases of shipment cotton by Pakistan and China have dovetailed with a strong rise in nearby ICE futures largely inspired by speculative reaction to the apparent tightening of the US balance sheet. This means that some of the assumptions set out here might already be on the point of being tested. In particular, there has been a sudden spike in demand for Indian cotton on the world market prompted by a sharply falling basis in respect of New York futures. While the magnified price differential may be relatively short-lived, estimates of total exports from India this season are under review.

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At the same time, the pace of new sales and export shipments of US cotton over the remaining five months of the season will determine to a large extent the actual (rather than perceived) tightness of the supply. More purchasing interest from China directed at Brazilian cotton, for instance, could again shift the price and trade dynamics significantly.

The factors that influence the ebb and flow of supply and demand are legion and often unpredictable. However, as we have seen, over time some far-reaching changes in the cotton landscape have taken place. These will be reflected in international trade flows that will continue to shift as the century progresses.

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