

Agricultural Outlook Forum 2008

Presented: Friday, February 22, 2008

THE UNITED STATES AND WORLD COTTON OUTLOOK

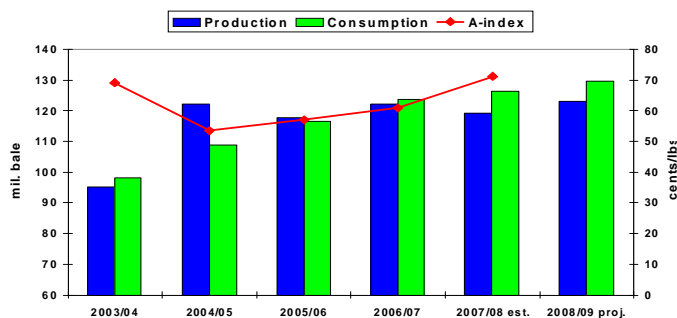
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U.S. Department of Agriculture

Introduction

A combination of lower production and higher consumption is reducing world stocks for the 2007/08 season. Sharp declines in production in the United States, Pakistan, the African Franc Zone, Australia, and Turkey are partially offset by an increase for India. Growth in world cotton consumption is slowing to 2.2 percent, well below the average of the previous seven years, due both to weaker growth in world GDP and higher cotton prices. World stocks are forecast to decline nearly 6 percent to about 57 million bales. The A-index (Northern Europe) averaged about 71 cents per pound from August 2007 – January 2008, an increase of 16 percent from the 2006/07 average.

USDA's first projections for 2008/09 include a recovery in foreign production which will more than offset a further decline in U.S. production. With consumption rising at a pace similar to that of 2007/08, world stocks are projected to decline further.

World Production, Consumption, and Prices
2003/04 through 2008/09 proj.

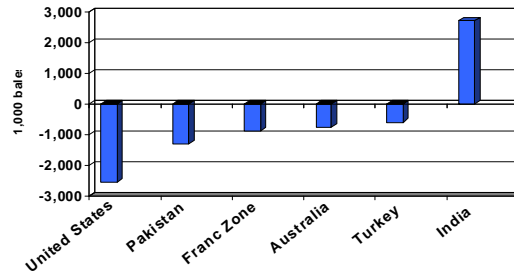


World Cotton Situation, 2007/08

World Cotton Production, 2007/08

World cotton production declined 2.3 percent in 2007/08, to 119.2 million bales, its third highest ever. Smaller crops in the United States, Pakistan, Australia, the African Franc Zone, and Turkey more than offset increases in India, Brazil, and Uzbekistan.

Estimated Changes in World Production 2007/08 vs. 2006/07



China's production in 2007/08 is estimated to be unchanged from the 2006/07 level on marginally higher area. Major questions persist about the absolute level of production in China, as a number of Chinese government agencies are working toward more accurate estimates of production, especially for the Xinjiang Autonomous Region.

For India, both area and yields rose in 2007/08 from the year before, as the adoption of genetically engineered Bt cotton continued transforming cotton cultivation across the country. The opportunity to cultivate Bt varieties that yield 40 percent more than even hybrid varieties has drawn additional area into cotton production. As the proportion of India's cotton devoted to Bt-varieties grows, the country's average yield grows as well. India's 2007/08 cotton crop will be a record for area and the fifth consecutive record for both yield and production. Production rose 2.7 million bales, or 12 percent, to 24.5 million bales.

Pakistan's 2007/08 estimated production of 8.6 million bales is down 13 percent. Area is unchanged from the previous season but the 2007/08 yield is the lowest in a decade. Excessive rainfall and an infestation of mealybugs have negatively affected production.

Brazil's 2007/08 estimated production increase of 200,000 bales is significantly smaller than India's in both absolute and percentage terms. With a southern hemisphere crop cycle, planting intentions in Brazil were influenced by the increase in soybean prices during August-December 2007 compared with the same period a year earlier. A lesser increase in cotton prices had only a slight impact on area, which was up 4 percent. Yields are expected to be nearly unchanged.

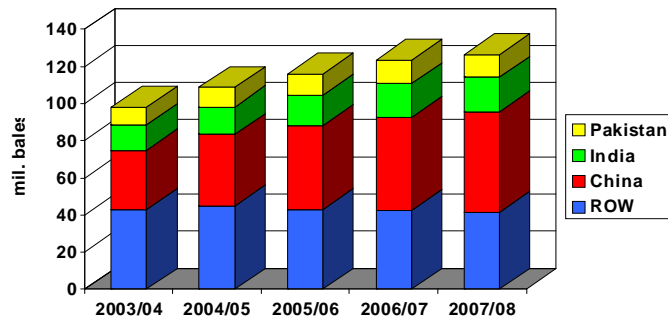
Australia's crop also follows the southern hemisphere crop cycle, but a continued severe shortfall of precipitation has further reduced crop expectations. At 75,000 hectares, area for Australia's cotton crop is the lowest since the 1979/80 season. The absence of rainfall at planting hit dryland cotton particularly hard, but recent rainfall has been beneficial to crop development. Yields are expected to be similar to the 5-year average. At 600,000 bales, Australia's crop would be its smallest in 25 years.

World Cotton Consumption, 2007/08

World cotton consumption is only expected to increase by 2.2 percent in 2007/08. This is unusually slow growth compared to cotton's performance since the end of the 1990s, but still remains above the long-run growth rate. During 2000-2006, growth in world cotton consumption averaged 4.5 percent

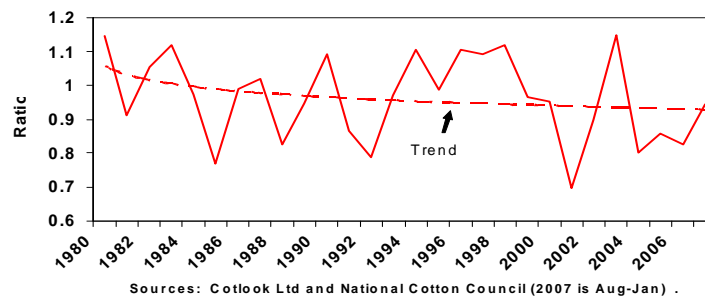
annually. Over this period, China's consumption increase was equal to almost 90 percent of the global increase in world consumption. Both India's and Pakistan's increased consumption equaled 15 percent of the global increase. Large declines in the United States and the European Union offset some of these gains, but the basic fact remains that the growing textile industries of China, India, and Pakistan have accounted for much of the world's strength in mill consumption of cotton over the last 7 years.

China, India and Pakistan Account for 2/3 of World Consumption



The global economy demanded more cotton products during 2000-2006 due to unusually strong economic growth and shifts in relative fiber prices that favored cotton. Recently revised estimates by the International Monetary Fund indicate that during 1980-1999, world income growth averaged 3.0 percent. However, during 2000-2006, the rate of global economic growth jumped to 3.9 percent on average. Similarly, cotton prices relative to polyester (A-Index/U.S. polyester) averaged essentially even during 1980-1999 (1.0). However, during 2000-2006, the ratio dropped to an average of 0.88, an 11-percent shift favoring the consumption of cotton.

Cotton-Polyester Price Ratio Rose in 2007



World economic growth during calendar year 2007 was an extraordinary 4.9 percent, but is expected to fall to 4.1 percent during calendar year 2008. The world economy is still expected to grow at a very strong rate, but the decline in growth between 2007 and 2008 is the largest such drop since 2001. Since, unlike food, clothing is a semi-durable good whose purchase can be postponed, the market can be strongly affected even by shifts in economic activity as well as the level of economic activity.

The price of cotton has also risen with respect to polyester. During August-December of 2007, the ratio of the A-Index to U.S. polyester prices averaged 0.94, or 7 percent higher than the 2000-2006 average. By January, the ratio had even risen back to parity (1.0). Given that cotton's share of world fiber

consumption declined significantly during the years that cotton and polyester prices stayed at this ratio, this suggests that the continued strong global economic growth may not sustain as high a rate of cotton consumption growth as in the recent past.

Evidence of the negative impact of slowing economic growth and rising fiber prices has been observed in the textile exports of India and China. The textile industries of these countries are the largest consumers of cotton fiber in the world, and exports of textile products account for a substantial portion of their cotton demand. The most recent trade data available for India is May 2007, but even then, textile export growth had shifted from strongly positive rates to declines compared with last season.

India's strong currency accounts for some of this weakness, but evidence from the United States and China suggests that slowing world economic growth may also be a factor. During August-November of 2007, total U.S. net imports of cotton products grew only 5 percent, less than half the rate of the previous year, and the slowest since 2003. Furthermore, in December 2007, the volume of China's cotton textile and apparel exports grew only 13 percent compared with the year before, the slowest in more than a year. This corroborated widespread reports that demand for China's apparel exports had diminished as the U.S. credit crunch and slowdown deepened and spread to Europe.

In 2007/08, China's cotton consumption is expected to increase 8 percent. This would mark only the second time in 9 years that China's consumption growth rate was below 10 percent. In addition to slowing demand in its developed-country textile export markets, China's cotton consumption has reportedly been hampered by tightening credit as China's government seeks to reign in economic growth, changes in VAT rebates for exports, and power shortages for mills in China as coal prices soar. India's consumption is only expected to grow 1.6 percent, and Pakistan's is expected to shrink by 4 percent.

China's Domestic Consumption and Trade

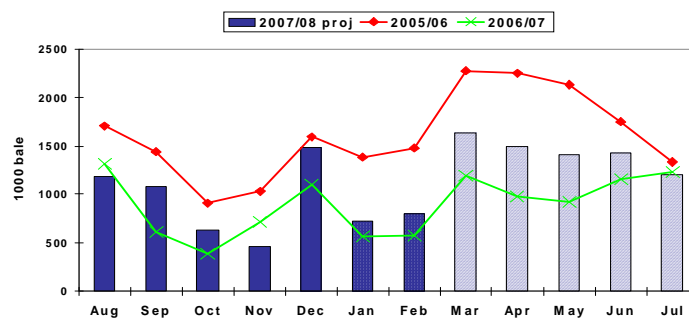
China's consumption is expected to rise in 2007/08 while production remains stable, resulting in higher imports and declining stocks. With 54 million bales total consumption and production forecast even with last year at 35.5 million bales, imports of 13.5 million bales, about 3.0 million above last season, will be needed to maintain adequate stocks.

China Cotton Balance Sheet

	mil. Bales	
	<u>2006/07</u>	<u>2007/08</u>
Beg. Stocks	20.3	18.7
Production	35.5	35.5
Imports	<u>10.6</u>	<u>13.5</u>
Total Supply	<u>66.4</u>	<u>67.7</u>
Consumption	50.0	54.0
Exports	<u>0.1</u>	<u>0.1</u>
Total Use	<u>50.1</u>	<u>54.1</u>
Residual	-2.4	-3.5
Ending Stocks	18.7	17.1
Stocks/Use %	37.4%	31.7%

Purchases by China in world markets, especially purchases from the United States, were relatively weak through the first half of the season. China's imports are reported to have reached 5.6 million bales by the end of January, about 41 percent of the total import forecast. Despite the slow start, there are valid reasons to think that China's imports will exceed last season's 10.6 million bales. First, growth in China's textile exports and the incomes of consumers in China remain relatively strong. Second, since China's mills tend to buy cotton only to fill immediate needs, they are likely to demand significant imports once their 2007-crop domestic supplies are committed. Finally, a build-up of stocks during the 2005/06 season is likely to have depressed 2006/07 imports – and those stocks have now been depleted.

China Projected 2007/08 Monthly Imports
Based on 2005/06 and 2006/07 Seasonality



World Trade, Ending Stocks, and Prices

Total 2007/08 world import demand is rising by 8 percent to 40.3 million bales, mainly reflecting higher expected imports by China. Excluding China and the U.S., the world will maintain import, export, and stock levels similar to last season. The U.S. began the season holding most of the world's surplus stocks and, thus, U.S. exports will increase to meet rising import demand. World ending stocks are forecast at 57.3 million bales for 2007/08, about 3.5 million bales below the year-ago level. The forecast world stocks-to-consumption ratio of 45.4 percent will decline about 3 percentage points from last season, continuing a gradual decline from the beginning of the decade, when China held large stocks. The A-index (Northern Europe) has averaged about 71 cents per pound thus far this season, compared with 61 cents for 2006/07 and 57 cents for 2005/06. In addition to tighter world stocks, cotton prices are supported by higher prices for grains and oilseeds resulting from demand for biofuels and a lower foreign exchange value for the U.S. dollar.

World Cotton Balance Sheet

	(mil. bales)	
	<u>2006/07</u>	<u>2007/08</u>
Beg. Stocks	60.2	60.7
Production	122.1	119.2
Imports	<u>37.3</u>	<u>40.3</u>
Total Supply	<u>219.5</u>	<u>220.2</u>
Consumption	123.6	126.3
Exports	<u>37.4</u>	<u>40.1</u>
Total Use	<u>161.0</u>	<u>166.4</u>
Residual	-2.2	-3.5
Ending Stocks	60.7	57.3
Stocks/Consumption %	49.1%	45.4%

U.S. Cotton Situation, 2007/08

Area and Production

U.S. Cotton Area, Abandonment, Yield and Production

		<u>2003/04</u>	<u>2004/05</u>	<u>2005/06</u>	<u>2006/07</u>	<u>2007/08</u>
Planted acres	mil. acres	13.5	13.7	14.2	15.3	10.8
Harvested acres	mil. acres	12.0	13.1	13.8	12.7	10.5
Abandonment rate	%	11.0	4.4	3.1	16.6	3.1
Yield/harvested acre	lbs./acre	730	855	831	814	871
Production	mil. bales	18.3	23.3	23.9	21.6	19.0

As spring planting time approached for the 2007 crop, U.S. harvest futures prices for competing crops, like corn and soybeans, were sharply higher, while cotton futures were similar to their year-earlier level. As a result, relative net returns favored corn, in particular, and soybeans, to a lesser extent, over cotton in 2007. Based largely on market return expectations for competing crops, cotton area was expected to decline from 2006.

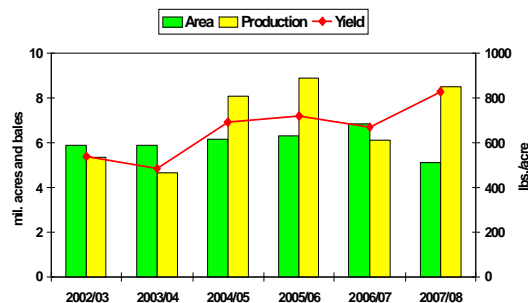
When the March 2007 *Prospective Plantings* were released, indications for 2007 U.S. cotton area were at 12.1 million acres, a 20-percent decline from 2006. By the time plantings were complete, however, cotton acreage had declined further due to additional increases in competing crop prices and excessive moisture in the Southwest, which prevented planting of some area intended for cotton. As a result, final cotton plantings were estimated at 10.8 million acres in 2007, 29 percent below 2006 and the lowest since 1989. Upland cotton area totaled only 10.5 million acres in 2007, 4.4 million (nearly 30 percent) below 2006 and the smallest crop planted in nearly two decades. Meanwhile, extra-long staple (ELS) acreage declined only 10 percent to 292,300 acres, as rising demand in 2006/07 prevented significant area declines in 2007. Most of the ELS decrease occurred in California where more than 90 percent of the crop is grown.

Although a significantly smaller U.S. area was planted to cotton this season, the national abandonment rate was well below average and provided a higher-than-anticipated area harvested. The 2007 abandonment rate for the Southwest decreased to 4 percent, the lowest since 1981; nationally, the abandonment rate totaled only 3 percent, similar to the 2005 season. As a result, 2007 harvested area approached 10.5 million acres, 2.2 million acres below 2006 and the smallest since 1989.

U.S. cotton production in 2007/08 is estimated at 19.0 million bales, compared with last season's 21.6 million bales. The 2007/08 season marks the lowest U.S. output in four years despite the national yield per harvested acre reaching a record. Cotton crop conditions were mixed across the Cotton Belt in 2007. Nationally, the growing conditions were above those in 2006 and similar to the 5-year average. In addition to generally favorable growing conditions this season, recent technological advances—including new varieties, improved irrigation, and precision farming techniques—have consistently raised the U.S. yield potential. The U.S. yield is estimated at 871 pounds per harvested acre in 2007/08, 16 pounds above the previous record set in 2004/05. Upland production is currently estimated at 18.2 million bales, the lowest in four years, with an average yield of 857 pounds per harvested acre, a record. The ELS crop is projected higher at a record 825,000 bales, as the ELS yield averaged its second highest at 1,374 pounds per harvested acre.

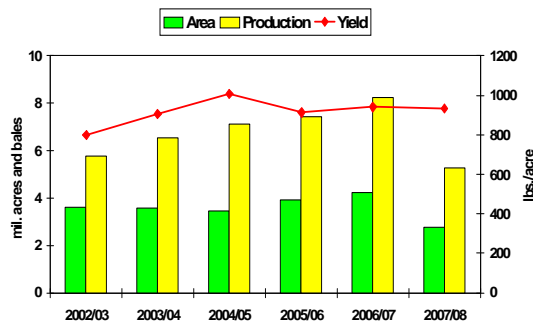
Compared with last season, 2007/08 upland cotton production was lower in three of the four Cotton Belt regions. The exception was the Southwest, where the upland crop approached 8.5 million bales, the second largest on record. Excellent moisture conditions throughout the growing season contributed to both a record yield (829 pounds per harvested acre) and low abandonment (4 percent) in the Southwest in 2007/08. In addition, the Southwest crop accounted for nearly 47 percent of the U.S. cotton output in 2007/08, the highest since the mid-1920s.

Southwest Region
Upland Cotton Area, Production, and Yield
2002/03 to 2007/08

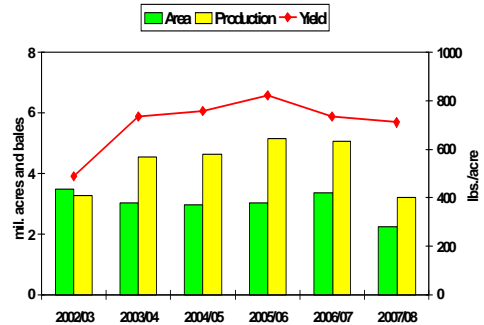


In contrast, the Delta saw a significant decline in production this season, despite above average yields, as area there declined 35 percent to about 2.8 million acres, the lowest since 1986/87. The Delta crop is estimated at nearly 5.3 million bales, about 3 million below 2006/07 and the lowest since a similar crop was produced in 2000/01. Delta production contributed 29 percent of the U.S. cotton crop in 2007/08, the lowest since 1985/86. Similarly, the Southeast region produced a smaller crop in 2007/08 at 3.2 million bales, as planted area was reduced by one-third to 2.3 million acres. Harvested area was the lowest since 1994/95 while the yield of 711 pounds per harvested acre was the lowest in 5 years due to drought. The Southeast accounted for approximately 18 percent of the U.S. upland cotton output.

Delta Region
Upland Cotton Area, Production, and Yield
 2002/03 to 2007/08

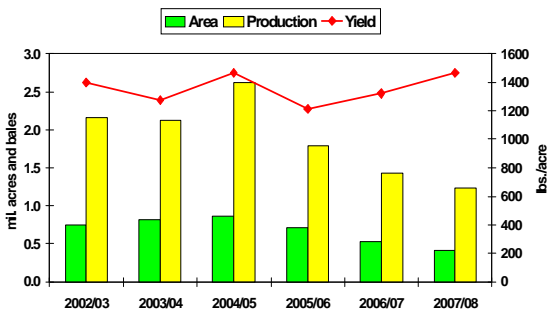


Southeast Region
Upland Cotton Area, Production, and Yield
 2002/03 to 2007/08

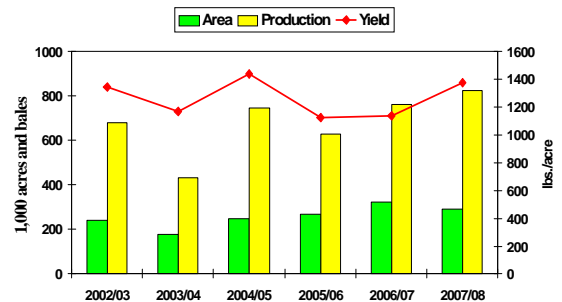


In the West region, upland area declined for the third consecutive season to 411,000 acres—the region’s lowest since 1932/33—as upland area there continues to follow the downward trend since the early 1980s. However, a record yield of 1,471 pounds per harvested acre kept upland production in the West from falling significantly this season. The upland crop in 2007/08 totaled 1.2 million bales, the lowest in six decades; the region accounted for only about 7 percent of the total upland crop in 2007/08. The ELS crop had an above-average yield produced from lower acreage.

Far West Region
Upland Cotton Area, Production, and Yield
 2002/03 to 2007/08



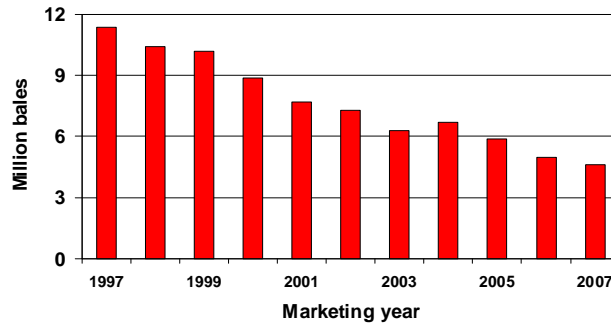
ELS Cotton Area, Production, and Yield
 2002/03 to 2007/08



Domestic Mill Use

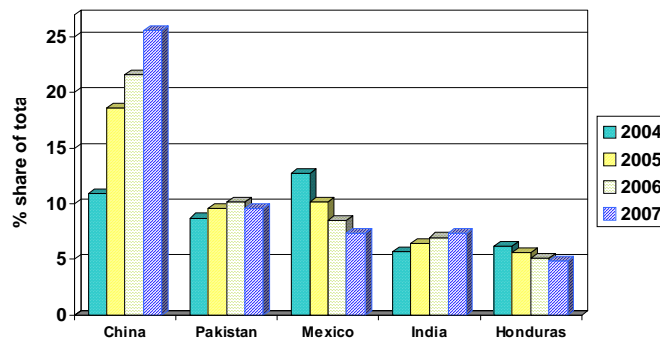
Domestic mill use is forecast at 4.6 million bales for 2007/08, 350,000 bales or 7 percent below the 2006/07 estimate. The current projection is just 40 percent of the level of a decade ago and is expected to be the lowest since 1910/11.

U.S. Cotton Mill Use 1997/98 to Present



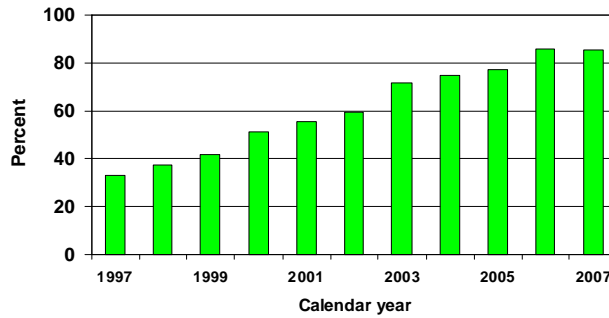
The substantial decrease in U.S. cotton mill use has resulted from increased competition of imported textile and apparel products, particularly since 2002. Also, the final apparel quotas were lifted in January 2005 and the U.S. industry faced additional pressure from imported products, particularly from China. In calendar year 2005, China replaced Mexico as the leading supplier of cotton textile and apparel products to the United States, accounting for about 19 percent of the 2005 total. U.S. imports are increasingly made in Asia, as China's share expanded to 26 percent in calendar year 2007. Pakistan continued to account for about 10 percent of the U.S. cotton textile and apparel market, while Mexico's share decreased from 10 percent in 2005 to about 7 percent.

U.S. Cotton Textile Imports Share by Origin for Top 5 Suppliers (raw fiber equivalent basis)



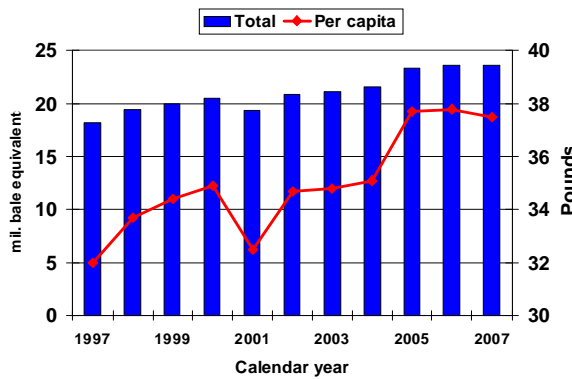
The U.S. textile trade deficit expanded slightly in 2007, as cotton product imports were about equal to that in 2006 while product exports decreased about 12 percent. The cotton product trade deficit in 2007 expanded to a record approaching 18.8 million bale-equivalents, about 40 percent higher than the trade deficit in 2002. During 2007, U.S. cotton textile and apparel imports reached an estimated equivalent of 22.9 million bales of raw cotton, similar to 2006. In contrast, cotton product exports have declined to an estimated 4.1 million bale-equivalents in 2007, or roughly 85 percent of domestic cotton mill use. This share is similar to 2006 but well above 59 percent in 2002, a time when the U.S. textile industry was spinning more raw cotton for the domestic industry.

**U.S. Cotton Textile Exports as a Share of Mill Use
(raw fiber equivalent basis)**



With these changes in U.S. cotton product trade and the domestic spinning industry, U.S. estimated household consumption of cotton, as measured by U.S. mill use plus net textile trade, is expected to rise only slightly in 2007/08. In 2007, U.S. domestic consumption of cotton once again approached 24 million bale-equivalents, compared with 21 million in 2002. U.S. per capita cotton consumption reached an estimated 37.5 pounds in calendar 2007, marginally below the preceding two years.

**U.S. Domestic Cotton Consumption:
Total and Per Capita**

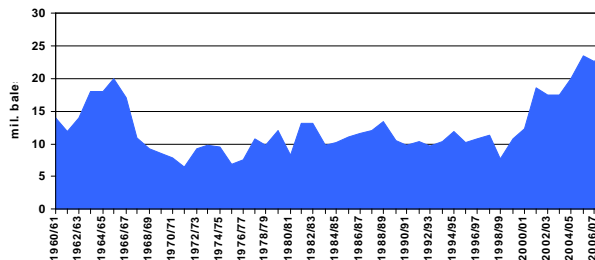


Exports and Ending Stocks**U.S. Cotton Supply-Demand Estimates**

	mil. bales	
	<u>2006/07</u>	<u>2007/08</u>
Beg. Stocks	6.0	9.5
Production	21.6	19.0
Imports	<u>0.0</u>	<u>0.0</u>
Total Supply	<u>27.7</u>	<u>28.5</u>
Consumption	4.9	4.6
Exports	<u>13.0</u>	<u>15.7</u>
Total Use	<u>18.0</u>	<u>20.3</u>
Ending Stocks	9.5	8.2
Stocks/Use %	52.8%	40.4%

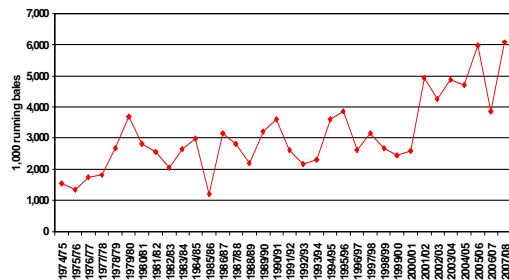
USDA is forecasting total 2007/08 U.S. exports at 15.7 million bales, up 20 percent from last year's 13.0 million bales, which would be the second highest on record. Beginning stocks at a 40-year high combined with ongoing reductions in domestic mill use and the high-yielding 2007/08 crop have resulted in the largest exportable supply in over 100 years.

**U.S. Exportable Supply at
Highest Level in over 100 Years**

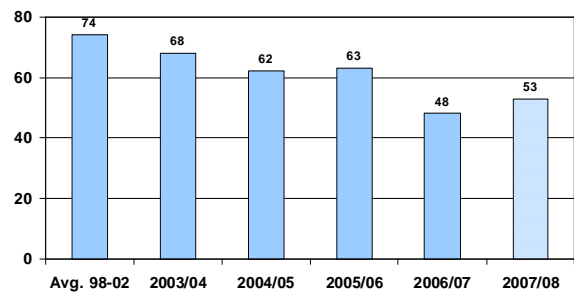


Shipments from the United States in the first half of the season of 6.25 million 480-lb. bales are a record and significantly ahead of last season's 4.0 million. Total export commitments had reached 53 percent of the level needed to reach the export forecast of 15.7 million bales. The recent trend is for export commitments to shift to later in the marketing year, and this season's activity to date is consistent with the trend.

Accumulated Exports as of Week 26

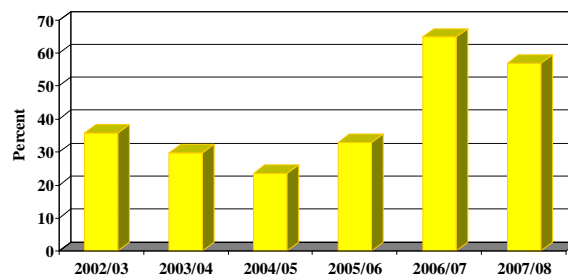


Percent of Annual Export Sales by Week 26 – Export Estimate of 15.7 MB



As of the end of January, 57 percent of 2007-crop upland cotton production was outstanding under CCC loan, slightly below last season but nearly double the percentage of earlier years. Heavy loan placements have occurred in part because the trade used large carry-in stocks from the 2007 crop to meet demand in the fall and early winter. Since the adjusted world price (AWP) is currently about 5 cents higher than the CCC loan rate, the loans are expected to be redeemed gradually as demand develops.

Percent of Upland Cotton Production Outstanding under CCC Loan on February 1

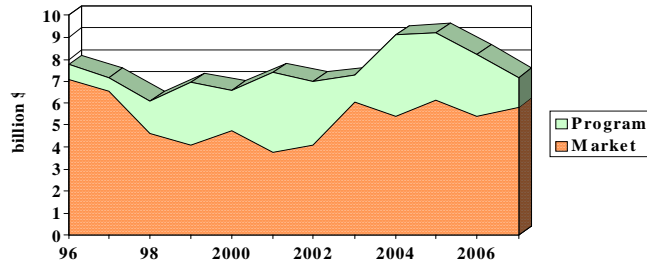


U.S. ending stocks are forecast at 8.2 million bales this season, down 13 percent from 2006/07, but still the third highest level in forty years. At this stock level, the U.S. would hold about 14 percent of global stocks, a decrease of 2 percentage points from last season. The U.S. stocks-to-use ratio would decrease substantially from last season's 53 percent to 40 percent, and would be the second highest since 1988/89.

Prices and Farm Income

Gross upland cotton farm income from the 2007 crop is estimated about 13 percent below 2006 at \$7.2 billion. With respect to market income, higher prices more than offset the smaller crop, raising income 7 percent to \$5.8 billion. Program payments are expected to fall 51 percent as the smaller crop and higher prices reduce marketing loan benefits and counter-cyclical payments. The upland cotton marketing year price has averaged 53.5 cents per pound for August through December 2007, an increase of 13 percent from the same period a year ago.

**Gross Cotton Farm Income
1996/97 through 2007/08 est.**



World Cotton Outlook, 2008/09

World Production, 2008/09

World production is projected to reach 123 million bales in 2008/09, marginally above the previous records set in 2004 and 2006, as higher foreign production more than offsets a 20-percent projected decline in the U.S. (see U.S. section). The increase is supported by higher production in China and India, and by recovery of several of the world's major cotton-producing countries and regions from adverse conditions in 2007/08, including Pakistan, the African Franc Zone, and Australia.

China, the world's largest cotton producer, is projected to raise production 4 percent to about 37 million bales, due to a combination of slightly higher area and yields. While rising grain prices and concerns about food security might indicate a contraction in cotton plantings, surveys suggest that China's farmers are satisfied with prices received in 2007/08 and plan to expand area. Also, yields in China follow a consistent rising trend, due partly to increases in planted area in the high-yielding Xinjiang Autonomous Region. The government's program to promote the use of better seed will also be supportive.

Like China, India is expected to both expand area and raise yields in 2008, resulting in a production increase of 5-10 percent. India has followed a strongly expansionary path in recent years due to the adoption of Bt cotton, which may have accounted for as much as 70 percent of planted area in 2007. More widespread adoption is likely to further increase yields and reduce production costs; at the same time, India's farmers are benefitting from higher domestic prices. Prices for competing crops have risen as well, but the relative gains between cotton and other crops still suggest more area will be planted to cotton in India in 2008/09.

Pakistan's production in 2007/08 suffered from excessive rain which led to widespread damage from mealybugs, resulting in yields nearly 20 percent below the preceding three-year average. With stable planted area and a return to normal conditions, Pakistan's production could increase 10-15 percent.

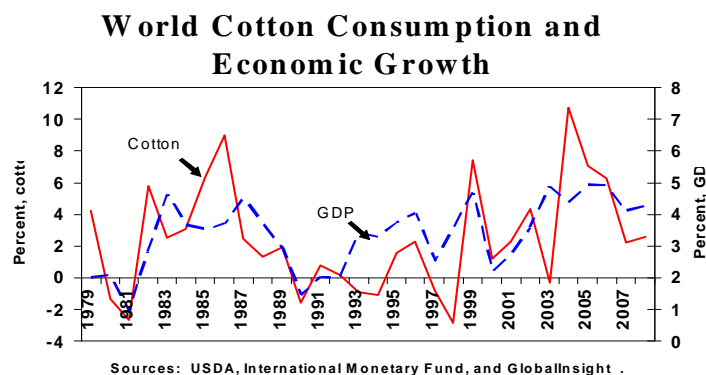
Brazil has the capacity for significant expansion of planted area in 2008, but with soybean prices rising more rapidly than cotton prices, it is likely that much of any expansion would be devoted to soybeans rather than cotton. Brazil's cotton production is projected to increase 3-5 percent in 2008/09.

The countries of the African Franc Zone saw their production decline by more than one-third between 2005 and 2007, due to a combination of price, input, and weather issues. A partial recovery is projected for 2008/09, as world cotton prices have risen strongly and a more normal--and timely--pattern of rainfall is assumed. Little further appreciation of the Euro and CFA Franc is foreseen during 2008, and some depreciation is even expected with respect to the U.S. dollar as 2008 comes to a close. This means that more of the recent increases in world prices could reach producers in the Franc Zone, increasing the attractiveness of planting cotton. Production could increase by about 30 percent from 2007/08.

Australia has received significant rain starting in late 2007, and reservoirs are refilling, especially in New South Wales. Local authorities estimate that area could rise from the current season's 75,000 hectares to 200,000 hectares or even more if the rain continues. Thus, Australia's production is projected to rebound to the 2.0-million-bale level in 2008/09, more than triple its 2007/08 production.

World Consumption, 2008/09

World cotton consumption in 2008/09 is expected to grow slightly faster than the current year, rising 2.5 percent. World economic growth in calendar 2009 is expected to improve compared with 2008 as the U.S. and Eurozone countries work through the economic slowdowns that began with their housing markets. While the world economy is expected to rebound as a result, the fastest growing economies in the developing world are still expected to continue the gradual deceleration in growth that began in late 2007. While economic growth in India and China is expected to remain quite strong in 2009, it is forecast a few percentage points below the extraordinary levels seen during 2007. The shift toward slower growth in the developing world will have an impact on cotton consumption since the income elasticity of clothing is stronger in lower income countries than in the United States and Europe.



During 2000-2006, U.S. household consumption of cotton products rose 3.1 million bales, while world cotton consumption rose 31 million bales. Unlike the 1990s, the source of world gains in cotton consumption since 2000 has been in emerging markets. Therefore, while a recovery of economic growth in the developed world is expected to boost global economic growth, world cotton consumption in 2008/09 is forecast to grow at a rate much more similar to 2007/08 than to the 4.5 percent averaged during 2000-2006.

Current relative fiber prices also highlight the likelihood that the economic environment in 2008/09 will be less favorable to cotton consumption than it was during the first half-dozen years of the 2000s. As of January 2008, the A-Index was at parity with the U.S. mill-delivered price of polyester. These prices averaged at parity during 1980-1999, and cotton's share of world fiber consumption fell from 48 percent to 41 percent over that time. Cotton's share of fiber consumption has largely stabilized since then, falling only to 40 percent through 2007. However, since the ratio of cotton to polyester prices was significantly more favorable during 2000-2006, it is reasonable to assume that cotton's share of a more slowly growing world fiber market is likely to shrink in 2008/09.

China's cotton consumption is expected to grow only about 5 percent from the year before in 2008/09. China's economic growth is expected to become more domestically oriented during 2008, and while the economy is expected to grow strongly, the rate of expansion is diminishing. The renminbi is also expected to continue to appreciate with respect to the dollar, even as the currencies of the developed world stabilize or even begin to depreciate in U.S. dollar terms.

World Trade and Stocks, 2008/09

World Cotton Balance Sheet

(mil. bales)

	<u>2007/08</u>	<u>2008/09</u>
Beg. Stocks	60.7	57.3
Production	119.2	123.0
Imports	<u>40.3</u>	<u>43.1</u>
Total Supply	<u>220.2</u>	<u>223.4</u>
Consumption	126.3	129.5
Exports	<u>40.1</u>	<u>42.7</u>
Total Use	<u>166.4</u>	<u>172.2</u>
Residual	-3.5	-3.5
Ending Stocks	57.3	54.7
Stocks/Consumption %	45.4%	42.3%

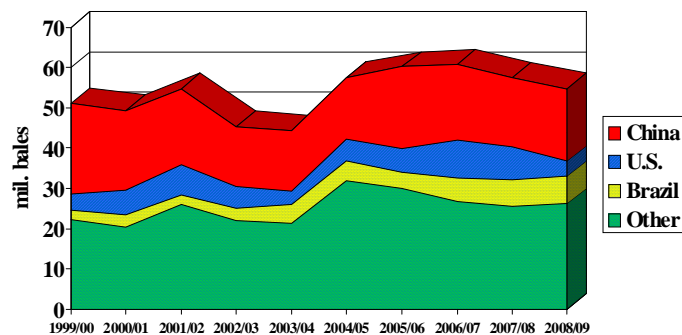
World trade in 2008/09 will once again be driven mainly by China's import demand. China's consumption is projected to exceed production by 19.5 million bales. With limited stocks to draw upon, the shortfall will have to be supplied by imports; thus, China's imports are expected to climb more than 12 percent to 17 million bales, raising China and world imports to their second-highest level. USDA's China balance sheet residual is maintained at 3.5 million bales.

China Cotton Balance Sheet

	mil. bales	
	<u>2007/08</u>	<u>2008/09</u>
Beg. Stocks	18.7	17.1
Production	35.5	37.0
Imports	<u>13.5</u>	<u>17.0</u>
Total Supply	<u>67.7</u>	<u>71.1</u>
Consumption	54.0	56.5
Exports	<u>0.1</u>	<u>0.0</u>
Total Use	<u>54.1</u>	<u>56.5</u>
Residual	-3.5	-3.5
Ending Stocks	17.1	18.1
Stocks/Use %	31.7%	32.0%

With world exports expected to rise 6.5 percent to 42.7 million bales, many of the world's cotton exporters will continue to reduce surplus stocks. At 54.7 million bales, global stocks will be, in absolute terms, at the tightest level in 5 years. The world stocks-to-use ratio will be its lowest since 1994/95. For the world outside China, stocks-to-use will be the lowest since 2003/04.

U.S., China, Brazil, & Other Foreign Stocks through 2008/09



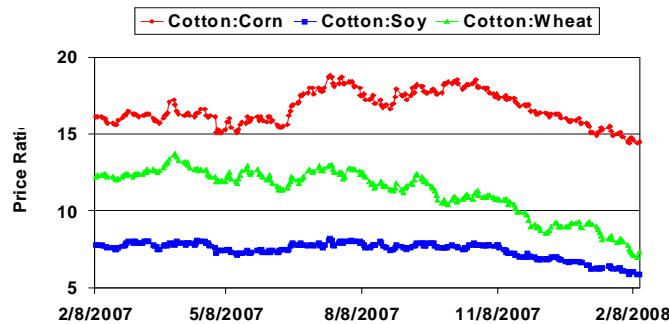
U.S. Outlook for 2008/09**Area, Production, and Supply****U.S. Cotton Area, Abandonment, Yield and Production**

		<u>2007/08</u>	<u>2008/09</u>
Planted acres	mil. acres	10.8	9.5
Harvested acres	mil. acres	10.5	8.6
Abandonment rate	%	3.1	9.5
Yield/harv. Acre	lbs./acre	871	835
Production	mil. bales	19.0	15.0

USDA is currently projecting that U.S. cotton producers will plant 9.5 million acres in 2008, which would be the lowest planted area in 25 years. Cotton planted area fell 29 percent in 2007, including reductions of about one-third in the Southeast and Delta due to significantly higher prices for corn and soybeans. With prices of alternative crops rising more than cotton prices in recent months, and cotton returns affected more than alternative crops by higher input costs, early industry expectations for 2008 are for a further drop of 10 to 20 percent in cotton plantings. The National Cotton Council's (NCC's) survey, released February 8, indicated that cotton area in 2008 would decline a further 12 percent to 9.55 million acres. Since that survey, prices for grains and soybeans have increased further, while cotton prices have shown considerable volatility, with moves higher and lower. The fluctuations in price signals to producers, combined with uncertain weather, suggest greater than normal uncertainty as the 2008 planting season approaches.

Attractive alternative crop prices - relative to cotton prices - are the main factor drawing acreage away from cotton again in 2008. With prices of all commodities above their respective loan rates, 2008 planting decisions will be based mainly on expected market returns rather than government program benefits. Harvest futures prices in mid-February for corn (\$5.25/bu), soybeans (\$13/bu), and winter wheat (\$10/bu) are far above a year ago, overshadowing cotton's more modest advance. Winter wheat seedings were higher in 2007 than in any recent year, including in cotton-growing areas, and many of those acres are expected to be double-cropped with soybeans after the wheat is harvested. The NCC survey indicates that cotton acreage will decrease most in the Delta, where alternative crops will displace cotton, and in the West, where environmental rulings will curtail water availability in California. On March 31, USDA's National Agricultural Statistics Service will provide its first survey-based producer intentions for 2008 crop acreage.

**Futures Price Ratios,
Cotton to Competing Crops
Feb. 8, 2007 to Feb.12, 2008**



USDA is projecting production of 15.0 million bales, based on average abandonment of about 10 percent, and a national yield of 835 pounds per harvested acre. Abandonment was unusually low and yields unusually high in 2007 due to excellent moisture availability on the Texas High Plains. In addition to an assumed return to normal weather, 2008 yields are likely to fall from the 2007/08 record due to proportionally larger reductions in planted area for the two highest-yielding regions, the Delta and the Far West.

Acreage and yields in 2008 will also be affected by weather conditions. While this analysis assumes normal weather, the National Weather Service's (NWS's) early February Drought Monitor shows abnormally dry conditions in the Southwest and moderate to extreme drought in most of the Southeast. Despite some recent rain in the Southeast, the NWS forecast is for conditions to deteriorate in both the Southeast and Southwest through the end of April, due to La Nina effects. Since cotton is sometimes a preferred alternative for dry conditions, continued dryness could boost planted area, while also raising abandonment and reducing yields.

If realized, the production level of 15 million bales would have fallen 37 percent from 2005 production, marking three consecutive declines to the lowest level since 1998/99. The expected decline in the cotton crop, in combination with the current beginning stocks estimate of 8.2 million bales (down 14%), results in U.S. cotton supply in 2008/09 of 23.2 million bales, the lowest since 2000/01.

U.S. Cotton Supply-Demand Estimates

	mil. Bales	
	<u>2007/08</u>	<u>2008/09</u>
Beg. Stocks	9.5	8.2
Production	19.0	15.0
Imports	<u>0.0</u>	<u>0.0</u>
Total Supply	<u>28.5</u>	<u>23.2</u>
Consumption	4.6	4.5
Exports	<u>15.7</u>	<u>15.0</u>
Total Use	<u>20.3</u>	<u>19.5</u>
Ending Stocks	8.2	3.7
Stocks/Use %	40.4%	19.2%

Mill Use and Exports

U.S. cotton domestic mill use is projected to fall 2 percent in 2008/09 to 4.4 million bales. With a slowdown in overall consumer spending, especially for home textiles, only slight gains in U.S. consumer end use of cotton are projected for 2008/09. At the same time, however, the weaker dollar has slowed the increase in cotton textile imports, resulting in more stable U.S. cotton mill use when compared with the precipitous declines of the first half of the decade.

In a departure from the past several years, a sharply reduced U.S. cotton supply is anticipated to constrain U.S. exports in 2008/09. Since 2001/02, U.S. exports have filled the gap between foreign demand and supplies, averaging nearly 40 percent of world exports. During this period, the U.S. frequently held stocks well in excess of pipeline requirements, with stocks-to-use ratios averaging about 33 percent. In contrast, projections for 2008/09 indicate that foreign import demand will absorb most if not all of the U.S. exportable supply. U.S. exports are projected at 15.0 million bales, equal to 35 percent of projected world trade.

U.S. and Foreign Ending Stocks, 2008/09

USDA's projections include a 4.5-percent reduction in world ending stocks to a level of 42.3 million bales, bringing stocks to 42 percent of consumption, well below the 5-year average of 49 percent. World stocks have declined over time mainly because China, the world's largest cotton consumer and importer, has reduced stocks, relying on foreign suppliers to deliver cotton "just-in-time." Likewise, in recent years, foreign countries outside of China have not held significant surpluses. For 2008/09, USDA projects that foreign countries will draw upon U.S. supplies to support rising consumption and maintain adequate stocks. Thus, U.S. stocks are expected to fall 4.5 million bales to a relatively tight 3.7 million bales at the end of 2008/09.