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USDA PERSPECTIVE ON THE OUTLOOK FOR COTTON

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World and Foreign Cotton Situation for 1999/2000

The world cotton situation for 1999/2000 is characterized by higher production, consumption and trade, and lower ending stocks. While the average world price A-index for the period August 1999-January 2000 fell by more than 11 cents per pound from the preceding marketing year, the monthly average price for January 2000 is nearly 8 percent higher than the previous month, reversing the falling trend of the previous 7 months. World consumption is estimated at 88.5 million bales, up 3.9 percent from last season, and world production is estimated at 86.9 million bales, up 2.8 percent from a year ago. Ending stocks are estimated to fall to 40.3 million bales, reversing the rising trend of the previous 5 years.

Foreign Area, Yield and Production

Three developments characterize world production in 1999/2000: the rebound in the U.S. crop, the decline in China's production, and the surge in yields in Central and Southern Asia. The U.S. rebound from the previous year's drought-reduced crop was quite significant, but the largest year-to-year change in world cotton production in 1999/2000 occurred in China. The current marketing year marks a momentous change in China's cotton policy: as guaranteed government procurement prices came to an end, cotton producers and consumers began to look to the market for price signals; at the same time, authorization of multiple purchasing agents ended the government cooperative's monopoly on procurement from farmers.

Procurement prices had already been falling before this year's reforms, but the transition to the new policy brought further sharp reductions. Cotton producers in China apparently correctly divined the likely price trend, and planted substantially less cotton in 1999/2000 than the year before; area in China fell 700,000 hectares to its lowest level since 1962. As has so often been the case over the last decade, area shrinkage was largely confined to lower yielding regions. Xinjiang, China's highest yielding region, reduced its area little, if at all, and China's national average yield rose from a year earlier to its second highest level ever. China's crop dropped 3.1 million bales compared with a year earlier, slipping below 19 million bales for only the second time during the 1990's.

While the effects of lower prices and shifting weather helped lower production from the year before in Mexico, Argentina, and Australia, the most significant foreign changes outside of China in 1999/2000 were yield and production increases across a number of countries.

Like China, Pakistan's cotton sector saw significant policy innovations during 1999/2000, as the government responded to a production increase of 1.9 million bales from the year before. Yields soared in Pakistan during 1999/2000, reaching a level previously exceeded only during a brief window early in the 1990's, before a set of high-yielding varieties was overwhelmed by leaf-curl virus. More recently, yields during the

last few years have also suffered due to a succession of problems including whitefly, heliothis, and fog. During 1999/2000, yields rose 25 percent from the preceding year's low level; factors supporting yields included more widespread use of new varieties and better application of higher quality inputs. In addition, weather conditions appear to have been particularly felicitous, as evidenced by extraordinary yields in India's Punjab, and across much of Central Asia. With early-season arrivals surpassing year-ago levels by an even larger margin, Pakistan's government felt obliged to revive a program of government cotton purchases.

Uzbekistan and Turkmenistan both reported surprising yield gains during 1999/2000, and together increased their production 950,000 bales from the year before. Yields rose 26 percent in Turkmenistan and 14 percent in Uzbekistan. According to Turkmenistan's government, seed cotton arrivals this year suggest an even larger yield gain, but most observers are awaiting additional confirmation before accepting the possibility that yields there have returned to levels last seen during the early 1990's. Turkmenistan has reportedly privatized some portions of its agriculture, and 1999/2000 marked its third consecutive yield increase. Information from Turkmenistan is not widely available, but the improving trend in cotton yields, and in wheat yields, suggests the agricultural sector's deterioration there has at least halted, if not reversed.

In Uzbekistan, this year's yield gain was less dramatic, but still took many observers by surprise. Like Turkmenistan, Uzbekistan has essentially maintained its cotton area constant for the last 4 years, in contrast to a precipitous decline during the early 1990's. Similarly, yields have generally stabilized in recent years after a prolonged decline. While both countries have made considerably less progress toward privatization than, for example, much of Central Europe, both seem to have completed at least some phase of their cotton sector's adjustment to the post-Soviet era. However, with no obvious technical or policy developments during the year that could have accounted for their yield gains, it seems reasonable to ascribe much of their good fortune to weather.

India's production rose about 300,000 bales from the year before in 1999/2000, despite the extraordinarily late onset of the monsoon in Gujarat, one of the major producing states. Excellent conditions in Punjab and Haryana have resulted in yields estimated to be 50 to 100 percent higher than the year before, more than offsetting Gujarat's downturn, and rounding out South and Central Asia's apparent good fortune with weather and yields in 1999/2000.

Among other producers: production in West Africa's Franc Zone in 1999/2000 was essentially unchanged from the year before as yields failed to rebound from 1998/99's loss, but crops increased by about 100,000 bales each in Sudan, Kazakhstan, Spain, Turkey, Brazil, and Greece, largely due to improved yields.

Foreign Consumption, Trade, and Ending Stocks

Foreign cotton consumption is estimated to increase significantly this season and reach a record 78.3 million bales. This is an increase from the previous year of 4.7 percent, and is the largest year-to-year growth since 1986. Several factors have contributed to the increase in foreign cotton consumption, including continued recovery in the world's economies following the Asian financial crisis. Falling prices, which have reached their lowest levels since 1986, have also boosted demand for cotton fiber. In addition, reforms implemented in China's textile and cotton industry are expected to boost consumption there by 3.5 percent, reversing the previous year's reduction of 4.8 percent.

According to Oxford Economic Forecasting, world economic growth is estimated at 2.5 percent in 1999 and 3.3 percent in 2000. While world economic growth for 1999 is less than the previous 4-year average of 2.8, it is greater than the previous year's GDP of 1.8 percent. Southeast Asia's GDP is estimated to rebound strongly in 1999 to 3.2 percent from the previous year's decline of 6.2 percent, and the rest of Asia is expected to grow by more than 5 percent. Japan is expected to recover from negative growth of 2.5 percent in 1998 to 0.9 and 1.7 percent in 1999 and 2000, respectively.

Contraction in the economies of several South American countries will dampen economic growth in Latin America to -0.6 percent in 1999, although Brazil will post a slightly positive GDP of 0.3 percent. The countries of the former Soviet Union are also expected to contract to -0.6 percent in 1999. In 2000, however, both Latin America and the countries of the former Soviet Union are expected to post positive GDP of 1.4 and 2.7 percent, respectively.

Foreign consumption increases in the major cotton-producing countries of China, India and Pakistan are expected to comprise 55 percent of worldwide growth in consumption, whereas increases in Turkey, Brazil and Southeast Asia, will comprise 35 percent of worldwide consumption growth. Imports are expected to grow commensurate with consumption with the greatest year-to-year increase in Mexico of 600,000 bales or 41 percent. Increased imports in Brazil, Southeast Asia and Turkey, combined with Mexico, will account for worldwide import growth of 1.7 million bales from the previous year.

Increased exports by the United States and China currently dominate the world trade picture. China's transformation, beginning in April 1998, from net importer to net exporter is perhaps the single most significant factor underlying the decline in world prices through the end of calendar 1999. This change came about as a result of a government decision to stop supporting internal cotton prices above world market-clearing levels, a practice which had resulted in an accumulation of 42 percent of the world's cotton stocks by 1998/99. With the new floating procurement prices in place for the 1999 crop, and partial government subsidies available to help dispose of higher-priced 1998 crop, USDA currently estimates China's cotton exports at 1.2 million bales this season. The combination of lower Chinese production, higher consumption and exports, and limited imports, is expected to reduce China's stocks by nearly 4 million bales or 23 percent from the previous year.

The change in China's net trade position and resulting drawdown in stocks has had negative impacts for other foreign countries. As a result of the Asian financial crisis, which depressed domestic consumption and limited the export market for textile products, ending stocks in many countries rose in 1998/99. While foreign stocks are expected to fall to 35.9 million bales or 5 percent from the previous year, foreign stocks outside China are expected to increase 2 million bales, or 10 percent from the previous year. India, Pakistan and Brazil will account for 44 percent of foreign growth in ending stocks outside China.

U.S. Cotton Situation for 1999/2000

U.S. Area, Yield, and Production

U.S. cotton production in 1999/00 is currently estimated at 16.95 million bales, compared with last season's 13.9-million-bale crop. The U.S. production increase was the result of gains in planted acreage and higher harvested area than a year ago. Yields, however, were below those of 1998/99. Planted area of nearly 14.9 million acres was 11 percent above the previous season and the second largest since the early 1960's. During

1999, cotton acreage in each State equaled or exceeded that of the preceding year as depressed prices for alternative crops and the safety net supplied by the marketing loan program proved favorable for cotton. Upland area expanded from 13.1 million acres to nearly 14.6 million. In contrast, 1999 extra-long staple (ELS) acreage decreased from 328,000 to 290,000 acres. While conditions seemed more favorable this season, a persistent drought across much of the Cotton Belt and damage from hurricane activity forced U.S. producers to abandon 10 percent of the area planted, half of the percentage abandoned in 1998. Estimated harvested area of 13.4 million acres reflects a 25-percent increase in area from 1998/99. And with the higher harvested acreage, the national yield of 608 pounds per harvested acre fell for the third consecutive season and is the lowest since 1995.

Upland production is estimated at 16.3 million bales this season, but with an average yield of only 596 pounds per harvested acre. U.S. upland production was significantly above last season, but only three of the four cotton regions produced a larger crop than in 1998/99. The exception in 1999 was the Southeast region, where drought and hurricane damage took its toll on the crop there. Despite an increase in area, historically high abandonment and a low regional yield produced a Southeast crop of only 3.6 million bales, the smallest since 1993. The region's yield averaged 538 pounds per harvested acre and was the lowest in 9 years.

In the Delta, cotton planted area reversed its 3-year decline as 3.7 million acres were planted in 1999. The lack of alternative crop prospects led to a 500,000-acre increase in plantings. Coupled with a higher--but still below average--yield of 667 pounds per harvested acre, Delta production rose nearly 1 million bales from last season to 5.1 million. For the Southwest, upland area increased 10 percent to 6.4 million acres in 1999/00. However, drought conditions in this region reduced harvested area to 5.3 million acres, but still well above last season's 3.4 million harvested acres. As a result, yields in the Southwest were reduced to 474 pounds which produced an upland crop of 5.2 million bales, the second largest in 6 years. In the West, upland area fell slightly in 1999 as more cotton was planted to ELS in the region. Upland acreage remained below a million acres for the second consecutive year, the lowest in over 30 years. However, yields improved significantly from last season's weather-reduced yield of 949 pounds per harvested acre to 1,200 pounds this season. As a result, the upland crop in the West exceeded 2.3 million bales, still below the 5-year average.

Meanwhile, ELS cotton production is estimated at a record 696,000 bales in 1999/00. The rise in the ELS crop is attributable to an increase in both harvested area and yields. Harvested area totaled 288,000 acres while the ELS yield averaged a record 1,159 pounds per harvested acre. California continues to increase its dominance of the ELS crop, accounting for nearly 90 percent of the 1999/00 production.

U.S. Mill Use, 1999/00

U.S. cotton mill demand is projected to decline in 1999/00 despite the continued growth in the U.S. retail market for cotton products. Filling much of this consumer demand, however, are less expensive imported textile products from around the world. Due to the continued effects of the Asian crisis and the ongoing trade liberalization of textile and apparel products, the rise in U.S. textile imports is outpacing the gain in exports. And as a result of these rising imports, U.S. mills have been forced to curtail production somewhat to alleviate the buildup of inventories.

U.S. cotton mill use is expected to decline this season to 10.2 million bales, 2 percent or 200,000 bales below 1998/99. Upland mill use is projected to reach 10 million bales while ELS consumption is expected to

approach 160,000 bales. During the first 5 months of 1999/00, data from the Department of Commerce indicate that U.S. mills used 4.2 million bales of cotton, about 3 percent below the comparable period for 1998/99. And despite a slow start, the seasonally adjusted annual rate (SAAR) of cotton consumption has averaged over 10.1 million bales for the August through December period, with the latest available month reaching a SAAR of 10.3 million bales.

A projected slower growth in the U.S. economy, reduced denim production, and the rising textile imports, which have widened the cotton textile trade deficit, will help moderate mill use again this season. And despite rising manmade fiber prices being reported, manmade fiber usage has risen this season. As a result, cotton's share on the cotton spinning system during the first 5 months of 1999/00 has averaged 78.5 percent compared with 79.3 percent for the entire 1998/99 season.

U.S. cotton textile imports, textile exports, and the net trade deficit all rose in calendar 1999. Cotton textile imports increased nearly 11 percent and exceeded 6.5 billion pounds, or the equivalent of 13.5 million bales of raw cotton. On the other hand, U.S. cotton textile exports in 1999 gained over 6 percent reaching approximately 2.1 billion pounds, or the equivalent of 4.3 million bales of cotton. And as a result, the cotton textile trade deficit has risen substantially for the third consecutive year to a new record of more than 9-million-bale equivalents of raw cotton. In total, U.S. consumers purchased the equivalent of 19.5 million bales of cotton in calendar 1999, which indicated a similar per capita consumption of cotton of 34 pounds as in 1998, the highest in 55 years.

U.S. Exports, 1999/00

Unlike mill consumption, U.S. cotton exports are projected to rebound this season. U.S. exports are forecast to jump over 2 million bales from last season's dismal shipment level to reach 6.4 million. Upland exports are projected at 6 million bales while ELS shipments are expected to reach 375,000 bales in 1999/00. Despite strong competition from other major exporters, the U.S. share of the global export market is expected to return closer to the long-term average. Based on the current projections, the U.S. share of world cotton trade is estimated at 24.2 percent, well above last season's 18.4 percent and a relatively strong level when China--as forecast this season--is not a net importer of cotton.

During the first half of 1999/00, U.S. cotton exports totaled about 2.6 million bales, or a shipment average of 95,000 bales per week. With only 40 percent of the forecasted exports shipped, U.S. exports for the last half of the season need to average 154,000 bales per week. Meanwhile, commitments (shipments plus outstanding sales) at the halfway point stood at 6.2 million bales, or 97 percent of the forecast. However, sales beyond the 6.4-million-bale level are needed as some sales are traditionally "rolled over" to the new season. But, unlike last season, these remaining export sales will have the availability of the Step 2 competitiveness program. The Step 2 program, which provides payments to users and exporters of U.S. cotton as needed to improve price competitiveness, was reinstated last October and extended through July 2003.

The increase in U.S. exports--at a time when excess foreign supplies are prevalent--is attributable to several key factors. A much-improved worldwide demand for cotton coincided with a rise in the U.S. crop, which has provided plentiful supplies for the export market, including increased production of short-staple export type cottons. In addition, two U.S. government programs--the marketing loan and the Step 2 payments--have supported U.S. export competitiveness. Merchants' expectations of Step 2 reauthorization permitted them to

compete as world prices fell in the first half of the season under pressure from China's sales, at a time when some major competitors were less aggressive sellers. At the same time, the marketing loan program, for which differentials reached a record of nearly 22 cents per pound, encouraged U.S. producers to actively market their cotton, rather than delay in the hope of a turn-around in prices.

U.S. Imports, Ending Stocks, and Farm Income, 1999/00

While the legislation that revived the Step 2 program also made some changes to the Step 3 program, the effects are expected to be negligible this season. The Step 3 trigger mechanism was shortened but a season limit on raw cotton imports was added. The import limitation equals 5-weeks' consumption of upland cotton by domestic mills at the seasonally adjusted average rate of the 3 months immediately preceding the first special import quota established in the marketing year. Currently, raw cotton imports of less than 100,000 bales are projected for the season, well below last season's imports, which approached 450,000 bales and were largely the result of the small 1998 U.S. crop which was lacking in certain qualities of cotton needed by U.S. mills.

Despite projections of total demand for U.S. cotton rebounding 13 percent from 1998/99 to 16.6 million bales, the gain in production this season is expected to more than offset higher demand and thus boost stocks from beginning levels. Currently, U.S. cotton stocks at the end of 1999/00 are forecast to be 4.4 million bales. Although the actual stock level is 500,000 bales above the previous season, the ratio of ending stocks to total use is virtually unchanged at 26.5 percent.

Government payments are instrumental in supporting farm income this season. At the August-December average farm price of 44.9 cents per pound, gross farm receipts from market sources will reach only \$4.1 billion, the lowest in ten years. However, when government payments are added, including contract payments and marketing loan benefits (but excluding Step 2 payments), gross cotton farm income rises to \$6.7 billion, above last season but below the 1997/98 level. Looking at returns on a net basis, the combination of 1999/2000's low market prices and low yields results in a market income below estimated variable costs. Adding government payments raises net returns to an estimated \$150 per planted acre, the lowest level since 1995/96.

World and Foreign Cotton Outlook for 2000/2001

USDA's early projections show lower foreign, but higher U.S. production for next season. World consumption is likely to continue to rise and reach a record 89-91 million bales, and there is good potential for the United States to capture a very competitive share of the world export market. The scenario that we envision, which is based on normal weather and crop conditions, results in lower world stocks at the end of the season, with U.S. stocks rising. China is forecast to revert to a net importer by a modest margin, following two years in which total exports reached a cumulative total of 1.8 million bales.

Foreign Production for 2000/2001

In 2000/2001, world production is likely to total between 84 and 86 million bales, or between 2 percent and 3.5 percent lower than during the year before. With U.S. production rising, foreign production is foreseen between 65 and 67 million bales. Foreign production is expected to decline 2 to 4 million bales from the year before in 2000/2001 as China's producers respond to lower procurement prices, yields return to normal in Central Asia and Pakistan, and low world prices during the first half of 1999/2000 discourage 2000/2001 production in a number of countries.

It is a longstanding truism that inflation-adjusted prices for cotton and other farm and unprocessed products fall over time, but 1999/2000's price developments were remarkable nonetheless. With the A-index averaging 47.7 cents for the marketing year through January, it has averaged to date 34 percent below the index's inflation-adjusted average for the 1985/86 marketing year, and, if unchanged during the rest of year, appears on track to mark the second consecutive year below this previous nadir. Some decline in foreign area seems likely in such circumstances, but currently, only a modest decline in foreign area and production is foreseen.

Based on its year-to-date level, the A-index in 1999/2000, in inflation-adjusted terms, has fallen for its fifth consecutive year, a string of declines last approached during the first half of the 1980's. Looking back at that time, it is difficult to discern a foreign area price response during that period--most of the decline at that time occurred in China, which was far less integrated into world markets than today and had internal reasons for drastically reducing area. Conceivably, the surge and decline in China's area during the first half of the 1980's was a government-coordinated attempt to respond to the world price signals of the last half of the 1970's and early 1980's, but that still leaves a price response from the rest of the world during that period that was not particularly strong.

During two other periods that followed declining prices (1975/76-76/77 and 1992/93-94/95), foreign area outside of China declined by about 10 percent. Given that recent price changes have been of comparable magnitude to those earlier, one could hypothesize a foreign area of 24.5 million to 25.5 million hectares for 2000/2001. However, based on a survey of Foreign Agricultural Service attaches, USDA analysis in Washington, and historical trends for countries lacking attache reporting, USDA currently foresees 2000/2001 area to total between 26 and 27 million hectares. In comparison, the International Cotton Advisory Committee forecasts foreign area to be even higher, exceeding 27 million hectares. Clearly, according to more than one source, foreign production in 2000/2001 is not expected to decline as strongly as during the mid-1970's and early 1990's. As has sometimes been the case in the past, low levels for competing crop prices, supportive government policies in some countries, and random shocks are expected to partly mute the world's area response to 1999/2000's precipitous decline in prices.

China's area is likely to decline in 2000/2001 despite recently recovering prices there. While competing crop prices are weak in China, the effects of 1999/2000's reforms and drastic price decline will continue to unfold, and production could range between 16 and 17 million bales even if yields maintain their strength of recent years.

Lower production is also likely across much of Central and Southern Asia as yields revert to mean levels. While technical advances probably improved 1998-crop yields in Pakistan and Turkmenistan, geographic proximity suggests that favorable weather was a major factor raising yields across the region extending from India's Punjab north to Uzbekistan and Turkmenistan, and all of the affected countries are thus likely to face more average circumstances in 2000/2001.

Together, Turkmenistan and Uzbekistan could produce about 500,000 bales less than the year before in 2000/2001, as their production falls from 6.5 million bales back to 6.0 million, its average over 1997/98-1999/2000. In India, in addition to the possibility of lower yields in Punjab and Haryana, area planted to cotton is likely to fall since prices have fallen, and stocks are expected to rise. Area could even decline in Pakistan, albeit by a slight amount, following low prices, and, with Pakistan's yields dropping closer to recent

averages, Pakistan and India could together produce about 2 million bales less cotton than the year before in 2000/2001.

Elsewhere in the world, area is likely to be down in Mexico, traditionally a country highly responsive to world price changes, but there are few remaining obvious candidates for lower area given the circumstances peculiar to each of the major producers.

Turkey's area would not necessarily be expected to change, given that the Southeast region's decades-spanning irrigation development project is steadily bringing new area into production, offsetting declines in traditional cotton growing regions. Similarly, Australia's irrigated area seems to fluctuate more in response to the availability of irrigation supplies--which are expected to be good in 2000/2001--than in response to declines in world prices. Nearly every year seems to bring news of newly irrigated cotton areas opening up in Australia. And Africa's Franc Zone also has been on an upward trend, responding to lower prices over the long run with pauses in expansion rather than with area contractions. Finally, Brazil has been on an upward trend in recent years, and with government support for agriculture, new highly-productive regions increasingly investing in cotton, and an earlier devaluation that has improved the competitiveness of its textile industry and economy in general, a reversal is not widely foreseen for Brazil's area and production in 2000/2001.

Foreign Consumption and Trade in 2000/2001

World cotton consumption is forecast to increase 1.5-2.0 percent from its year earlier level due to the lagged effect of very low prices. This would bring consumption above the peak achieved in 1996/97 before the Asian financial crisis. Stronger projected world GDP of more than 3 percent in 2000 and 2001 supports the rise in consumption, as does the current more favorable relationship of cotton prices to those of manmade fibers. In the longer run, a slower rate of consumption growth is expected, but 2000/2001 is expected to be slightly above average due to lagged cotton prices and recovering economic prospects in several markets. While the U.S. economy is likely to slow as 1999/2000 moves into 2000/2001, improvement is expected for much of the rest of the world.

Recent reports suggest Italy's textile industry has shown signs of recovery in recent months, such that the European Union's cotton consumption could perhaps stabilize, rather than fall for a third consecutive year. Similarly, while Russia's late-1998 devaluation was initially disruptive, the prospect of the first notable GDP increase in more than a decade--now that the currency's correction has been internalized--suggests better prospects for cotton textiles in Russia. In neither case is a substantial increase likely, but the world consumption total is less likely to be burdened with declines in these regions as has been the case in recent years.

In China, the return of the textile sector to profitability has reduced the emphasis on the spindle-reduction program of the last few years. The textile industry's input costs in 2000/2001 will certainly be below pre-reform levels, and a second year of consumption growth is likely for the world's largest consumer. Both larger textile exports and increased domestic demand are likely to boost cotton consumption. China's GDP growth is expected to reach 8.6 percent in 2001, compared with 7.7 percent in 2000 and 7.1 percent in 1999; rising incomes will, in turn, raise consumer demand for textiles and improve prospects for global cotton consumption.

China's net trade position will continue to play a pivotal role in the world cotton situation, as it has the past several seasons, and uncertainties about China's policies and statistics cloud the outlook. We project that consumption will exceed production for the second consecutive year—with China's cotton

mill use rising, 2000/01 consumption of roughly 21 million bales is anticipated to exceed production by 4 to 5 million bales.

China could meet this need by: (1) releasing stocks from the government-held inventory; (2) increasing quotas to allow foreign imports and/or (3) forcing textile mills to operate with less cotton. Given the importance of China's textile industry to its domestic economy and foreign trade, we deem it unlikely that the government would permit a serious cotton shortage to develop. On the other hand, we also believe that central government decisions to incur the considerable cost of releasing cotton from stocks may lag the expanding requirements of China's mills. This leads us to the conclusion that China is likely to be a modest net importer of cotton in the 2000/01 season.

With decreased world production and increased consumption, world ending stocks are forecast to fall 8 to 16 percent, to 34-37 million bales. China's stocks are forecast to fall by nearly 4 million bales, accounting for the majority of the reduction in world stocks.

U.S. Cotton Outlook for 2000/2001

U.S. Area, Yield and Production, 2000/2001

Preliminary estimates for 2000 U.S. area suggest an increase to 15.0-15.5 million acres, including about 250,000 acres of ELS cotton. With a normal weather assumption, an abandonment rate of about 7-8 percent is projected, about equal to the 1990's average. A national average yield of 630-635 pounds per harvested acre is applied. This yield projection, which is below the long-run trend, reflects the recent stagnation in U.S. yields overall and a larger share of total area in the lower-yielding Southwest region. Combining these projections results in the production range of about 18.0-19.0 million bales. However, this is at best an indicator of direction, given the uncertainties surrounding producers' planting intentions and likely yield variations across the Cotton Belt. USDA's survey of producers' planting intentions will be published on March 31.

Both statistical analysis and anecdotal evidence suggest that cotton planted area will rise slightly from 1999's 14.86 million acres. An area response model developed by USDA's Economic Research Service indicates that plantings may increase by about 500,000 acres in the spring of 2000. The model projects shifts in acreage based on a comparison of the prices producers expect for cotton and alternative crops (see the *Cotton and Wool Situation and Outlook Yearbook*, USDA, November 1999). These effective prices are based on the current values of 2000-crop futures prices plus any anticipated marketing loan benefits. For example, as of February 1, the model assumed that producers were expecting a 2000 cotton price of 68 cents per pound, including the December 2000 futures price plus an anticipated marketing loan gain of 10 cents per pound.

Using the same methodology, producers expected only about 64 cents per pound for the 1999 crop in the spring of 1999. While year-to-year changes for alternative crops, such as corn, grain sorghum, and soybeans, were also positive, alternative crop prices have not risen sufficiently to offset the increase for cotton. Thus, the model projects a small net area shift to cotton, confirming recent survey estimates by the National Cotton Council and others. Increases are expected for all regions of the Cotton Belt, but ELS planted acreage is expected to decline due to the price-depressing effects of the recent accumulation of surplus stocks. This

area projection would be the second-highest since 1962, exceeded only by 1995's 16.9 million acres planted.
U.S. Mill Use, 2000/01

On the demand side, U.S. GDP has been spectacular over the past 3 years and is expected to grow more slowly in the upcoming marketing year than it has in recent years. As a result, slower growth in retail cotton consumption, coupled with increased cotton textile imports, will likely result in mill use exhibiting little change in the 2000/01 season. U.S. retail cotton consumption could exceed 21-million-bale equivalents in 2000/01 with only modest growth. However, as in the current season, much of this growth will likely be satisfied with textile imports. A marginal offset to some of the growth in textile imports will be provided by the expected increase in cotton textile exports, gains largely attributable to NAFTA and CBI. Given the effects of ongoing trade liberalization, cotton textile trade will likely continue to expand and play a major role in the amount of cotton demanded by U.S. mills. Based on current projections, U.S. cotton mill use in 2000/01 is likely to range somewhere between 10 and 10.5 million bales, about unchanged from the current season.

U.S. Exports and Ending Stocks, 2000/01

With higher U.S. production, lower foreign production and continued support from the Step 2 program, the U.S. is expected to capitalize on the recovery in world demand with increasing U.S. exports next season. In addition, export competition from China is forecast to diminish next season as China once again could return to the net importer status. Much, of course, will depend on the success of policies to reduce stocks and the quality and accessibility of those stocks in relation to the rest of the world.

Exports in the range of 7.5 to 8 million bales are consistent with the world projections outlined here and would be near the levels achieved during the mid-1990's. This range would be as much as 25 percent above the current season's projection and well above the 5-year average of approximately 6.5 million bales.

And despite the projected rise in U.S. exports in 2000/01, larger anticipated production gains are likely to push U.S. stocks higher. Based on these projections of cotton supply and demand, U.S. stocks could rise as much as one million bales from beginning levels. However, this gain in 2000/01 stocks would imply perhaps only a slightly higher ratio of stocks relative to total use, ranging between 25 and 30 percent.

Effect of the MFA Phaseout on the Medium-Term U.S. Outlook

International trade in textiles and apparel has been governed by quantitative restrictions under the Multi-Fiber Arrangement (MFA) and earlier agreements for more than 30 years. During the Uruguay Round, however, the conclusion of the Agreement on Textiles and Clothing provided for the dismantling of those restrictions. These MFA restrictions are to be phased out over a 10-year period and are scheduled to end by 2005. With quotas and other restrictions eliminated, tariffs will become the primary mechanism for border protection as the same rules will apply to trade in textiles and clothing as in other goods.

For the United States, cotton textile imports have played an increasing role in total domestic consumption (mill use plus net textile trade). In calendar 1999, the raw-fiber equivalent of cotton textile and apparel imports has exceeded the quantity used by domestic mills for the second consecutive year. Just 10 years ago, these imports totaled only about 60 percent of U.S. cotton mill use. Although a larger percentage of U.S. cotton is estimated to now be contained in these textile imports, the import trend has risen dramatically, suggesting a structural shift in the related industries that will likely continue as the MFA phaseout is completed. While adjustments to the phaseout almost certainly imply a declining trend over the longer term for U.S. mill use, U.S. raw cotton exports could more than offset this decline as the U.S. remains a reliable supplier to a

growing world demand for cotton textile and apparel products.

Conclusion

It is important to keep in mind the many uncertainties, including weather developments, economic growth trends, and government policies, that will affect the supply-demand outlook. China's policies, especially those directed at surplus disposal, will have a fundamental impact upon the world outlook. In examining income prospects, producers have a menu of tools for managing price risk, most of them based directly or indirectly on the New York futures market; however, they must also be cognizant of the role of the world price A-index in determining the loan deficiency payment (LDP) level. Thus, it is important to follow both U.S. and world developments in planning for the 2000 crop.