INTERNATIONAL COTTON ADVISORY COMMITTEE

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PRODUCTION AND TRADE POLICIES AFFECTING THE COTTON INDUSTRY

December 2015

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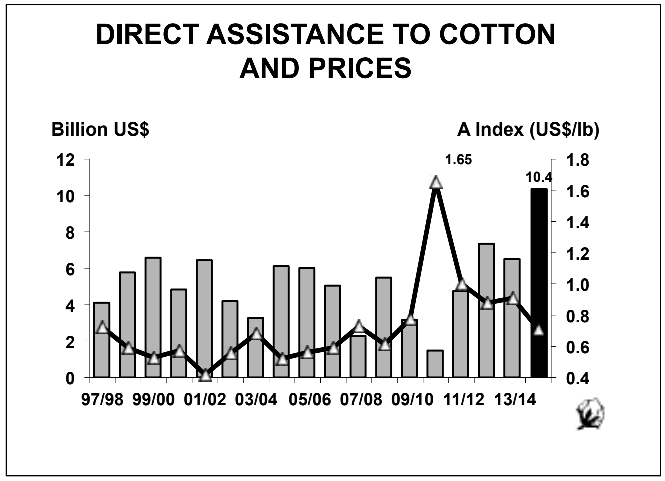
A report by the
Secretariat of the
International Cotton Advisory Committee

Washington DC, USA

GOVERNMENT SUPPORT TO THE COTTON INDUSTRY

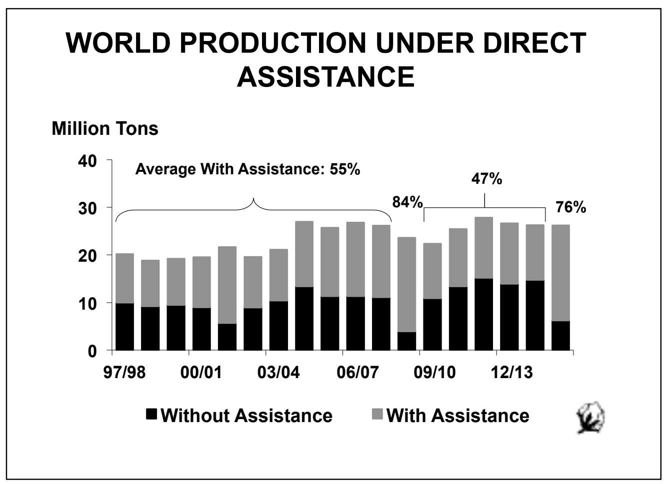
1. Subsidies to the cotton sector, including direct support to production, border protection, crop insurance subsidies, and minimum support price mechanisms are estimated at a record $10.4 billion in 2014/15, up from a record of $6.5 billion in 2013/14. Twelve countries provided subsidies in 2014/15, and the subsidies averaged 22 cents per pound, up from 15 cents per pound in 2012/13.

2. Since 1997/98, when the Secretariat first began reporting on government measures in cotton, there has been a strong negative correlation between subsidies and cotton prices: in years when prices are high, subsidies tend to decline and in years when prices are low, subsidies tend to rise. This relationship was maintained during 2014/15. The Cotlook A Index declined from an average of 91 cents per pound in 2013/14 to an average of 71 cent per pound in 2014/15, and subsidies provided to cotton growers increased.



3. In some countries, such as Brazil and India, minimum support price programs were triggered during 2014/15 because market prices fell below the government intervention prices.

4. Some countries provided subsidies for cotton inputs in 2014/15, especially for fertilizers, storage, transportation, classing services and other marketing costs. At the same time, the use of crop insurance subsidies is increasing, although still not widespread. However, information on the amounts involved is lacking in some cases.



5. The share of world cotton production receiving direct government assistance, including direct payments and border protection, increased from an average of 55% between 1997/98 and 2007/08, to an estimated 83% in 2008/09. During 2009/10 through 2013/14, this share declined and averaged 47%. In 2013/14 the proportion of production receiving direct assistance is estimated at 44%. However, the share increased to 76% in 2014/15.

China

6. The Government of China supports cotton production by controlling cotton import volumes and values and by applying border protection measures based on quotas and sliding scale duties, with an effective tariff of 40% on cotton imported without a quota. In addition, China maintains a strategic reserve of cotton, serving as a national buffer stock, which is managed by the China National Cotton Reserve Corporation (CNCRC). China releases cotton to the market from the reserve through a system of auctions when there is a shortage, and replenishes the reserve in times of abundance, thus supporting prices.

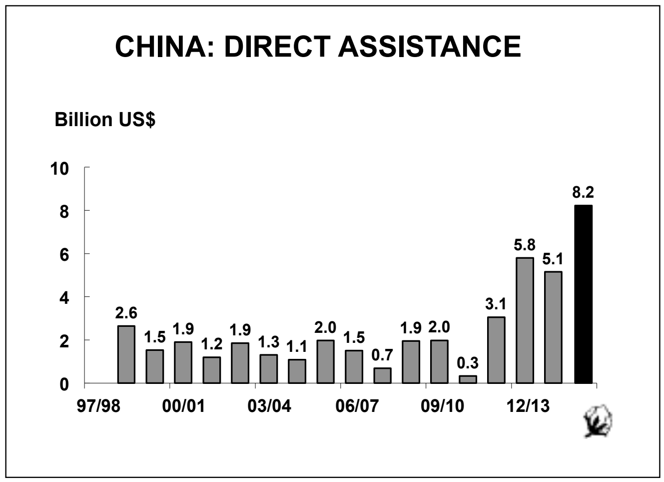
7. During the three seasons prior to 2014/15 (2011/12, 2012/13 and 2013/14), China implemented a system of minimum support prices by directly purchasing cotton from producers and rebuilding the government strategic reserve. The 2013/14 state reserve procurement price was set at 20,400 yuan/ton (151 US cts/lb at the seasonal average exchange rate), the same level as prevailed during the previous season. In 2013/14, China purchased 6.3 million tons of cotton for the state reserve (6.5 million tons were purchased during 2012/13). In 2012/13, Chinese government auc-

tioned 3.7 million tons from the reserve to mills at prices averaging 135 US cts/lb. In 2013/14, auction starting prices were reduced by 4% and about 2.2 million tons were auctioned from the reserve. The size of the reserve at the end of 2013/14 is estimated at 11.6 million tons, accounting for 149% of mill use by China in 2013/14 and 57% of world stocks. There were no purchases for or sales from the government reserves during 2014/15.

8. Three seasons of implementation of this policy of rebuilding government reserves by the Chinese government provided support to domestic and international prices and helped to keep world trade buoyant. At the same time, this policy also caused mill use and the market share of cotton in China to shrink. Release of the reserves to domestic mills reduces the need for imports and limits growth in world trade.

9. Under the terms of its accession agreement to the WTO, China is obliged to establish a calendar year tariff-rate-quota (TRQ). The in-quota tariff is 1% for the first 894,000 tons of imports each calendar year. Additional import quotas are released by China based on requirements. The additional quotas can carry a tariff of 1%, or quotas can be based on a sliding scale of between 5% and 40%. The purpose of the sliding scale is to ensure that the effective cost of imported cotton exceeds international market prices and thus boosts domestic prices paid to farmers in China. As a result of government interventions and quotas, domestic cotton prices in China have exceeded international prices.

10. The Secretariat uses the difference between domestic and imported cotton prices as an estimate of the border protection support to Chinese cotton prices resulting from government interventions. The price differential between the CC index (an index of mill-delivered cotton in China) and the FC Index L (an index of imported cotton arriving in Chinese main ports), adjusted to include value added tax, port charges and transportation to mills is used in calculations. The benefit (subsidy) received by producers in China as a result of the government interventions is estimated at $3.3 billion in 2014/15, or 23 US cts/lb, compared with $4.8 billion, or 32 US cts/lb, in 2013/14.



11. The Chinese government ended its reserve building policy in 2014/15 and instead provided a direct subsidy to cotton producers in Xinjiang with a target price of 19,800 yuan/ton (about 146 US cts/lb at the average seasonal exchange rate). Under this new direct subsidy system, Chinese government pays growers in Xinjiang the difference between the target price and the average market price for cotton. Using the difference between the target price and the average CC index, it is estimated that total direct subsidies paid to producers in Xinjiang totaled $4 billion, or 40 US cts/lb. In other provinces a direct subsidy of 2000 yuan/ton was provided to producers. It is estimated that these direct subsidies totaled $663 million, or 15 US cts/lb. Total direct subsidies provided to producers in China in addition to border protection support are estimated at $4.6 billion.

12. In addition, the government of China pays growers a subsidy for using high-quality planting seeds, amounting to about $150 million a year, although smallholder farmers do not benefit significantly from this policy. During the past several seasons, China provided subsidies for transportation of cotton from Xinjiang to mills in eastern and southern China, which are estimated at about $160 million per year.

13. All types of subsidies provided by the Chinese government are estimated at $8.2 billion in 2014/15 or 58 US cts/lb, up from $6.5 billion in 2013/14 (34 US cts/lb).

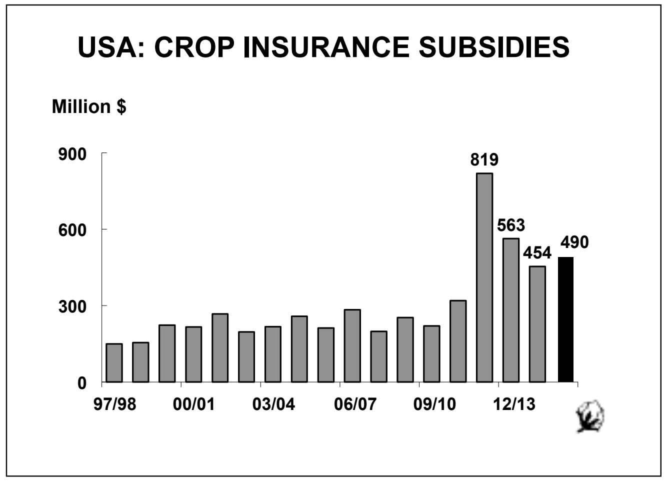
United States

14. During 2014/15 and 2013/14, the only subsidy effectively received by producers under the U.S. cotton program was for crop insurance. The U.S. government provides support to cotton production through subsidized crop insurance to protect producers against losses to crop yields caused by natural disasters. This multi-peril crop insurance

covers nearly every cause of declines in crop yields, such as weather, pests, and fire, with the exception of producer negligence. The insurance is sold to farmers, largely through private insurance providers, but the Risk Management Agency (RMA) of the U.S. Department of Agriculture pays more than half of the premiums. Additionally, the RMA pays the private insurance providers for their administrative and operating costs, as well as the RMA's own administrative costs under the program. On average, more than 90% of planted cotton acreage is enrolled in this program.

15. The crop insurance program is statutorily mandated to be actuarially sound, meaning that total premiums are supposed to cover total indemnities over time. Underwriting gains and losses are allocated between the companies and government according to formulas contained in the reinsurance agreement between the parties.

16. During 2014/15, cotton insurance subsidies are estimated at $490 million, or 6 US cts/lb, compared with $454 million, or 7 US cts/lb in 2013/14.



17. On February 7, 2014, President Obama signed the 2014 U.S. Farm Bill into law. The new five-year farm bill marks a significant change in farm policies, to an environment in which guaranteed payments no longer exist and eligibility for payments will be based on declining prices, crop failures or reductions in revenue. The new Farm Bill marks an evolution from traditional farm income support programs to a focus on production and price risk management, with government-subsidized crop insurance as the primary instrument. Direct Payments, Countercyclical Payments and Average Crop Revenue Election (ACRE) programs have been repealed for all commodities. Upland cotton is not eligible for other commodity risk management programs established under the bill but becomes eligible for a new and unique "safety net" program, the Stacked Income Protection Plan (STAX).

18. STAX provides upland cotton producers with premium subsidies on the purchase of insurance policies that cover "shallow" revenue losses--those below the level generally covered by standard crop insurance policies. Producers may use this program alone or in combination with existing underlying crop insurance. Under STAX, a payment is triggered if the actual income in a county falls below 90% of the expected income. STAX provides coverage for revenue shortfalls between 10 and 30% of expected income and producers may select coverage in 5% increments. The federal government will subsidize about 80% of the premium. In addition, the federal government will partially subsidize the administrative and operational costs of the insurance companies offering STAX.

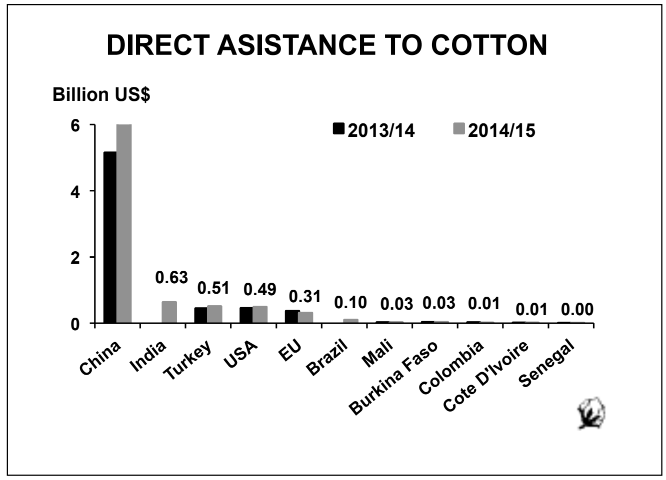
19. STAX will be available during the 2015 growing season (starting in August 2015). During 2014/15 a cotton transition assistance payment was provided through the Farm Service Agency, which was calculated using a formula involving marketing year average prices for upland cotton, the national program yield of 597 pounds per acre and 60% of the cotton base acres[1] for the farm in 2014 and 36.5% of the base acres in 2015. It is estimated that transitional payments during 2014/15 totaled $500 million.

20. The Marketing Loan Program (MLP) will continue with a marketing loan rate based on the world cotton price, calculated as the simple average of the adjusted prevailing world price for the two immediately preceding marketing years (announced October 1 preceding the next domestic plantings), but in no case lower than 45 cents per pound or higher than 52 cents per pound. The loan rate for extra-long staple (ELS) cotton is set at 79.77 cents.

21. The export promotion subsidy for Pima cotton has been retained, in the form of special competitiveness provi-

1) The term `generic base acres' means the number of base acres for cotton in effect under section 1001 of the Food, Conservation, and Energy Act of 2008 (7 U.S.C. 8702), as adjusted pursuant to section 1101 of such Act (7 U.S.C. 8711), as in effect on September 30, 2013, subject to any adjustment or reduction under section 1112 of this Act. Source: http://www.gpo.gov/fdsys/pkg/BILLS-113hr2642enr/pdf/BILLS-113hr2642enr.pdf

sions for ELS cotton, through payment of a subsidy, calculated by a set formula, to domestic users and exporters of ELS cotton under special circumstances. The aim of the program is to promote domestic use and exports of ELS cotton. No payments under the U.S. Pima competitiveness program have been made since May 2010.



India

22. India has a Minimum Support Price (MSP) system, but there were no direct cotton purchases by the government and no payments to growers during 2013/14 because market prices were above the MSP. In 2013/14, the MSP for medium staple cotton (J-34) was set at Rs3,900 per 100 kg of seed cotton, equivalent to 85 US cts/lb of lint at the season average exchange rate. The average domestic price for the same variety during the period was above this level.

23. For 2014/15 the MSP for medium staple cotton (J-34) was set at Rs3,950 per 100 kg of seed cotton, equivalent to 85 US cts/lb of lint at the season average exchange rate. Domestic prices in India stayed below the MSP during 2014/15. As a result, the Cotton Corporation of India, an agency of the central government, and state cotton organizations directly purchased an estimated 1.6 million tons of cotton at MSP prices as of May 30, 2015, at an estimated cost of $2.9 billion. Current domestic spot prices in India for a representative variety are estimated at 66 cents per pound. Based on the difference between the procurement price and the current value of the government stock at market prices, it is estimated that the cost of MSP operations to the Indian government would reach $633 million, if cotton were sold at current prices. This would represent a subsidy of 4 US cts/lb if applied to total production.

24. Cotton farmers in India benefit from debt forgiveness and fertilizer subsidies from the government of India. India also provides some backing in the form of subsidies for crop insurance, although the value of this support is not known. In addition, the Government of India provides support to cotton production through several programs, such as the development of infrastructure facilities for production and distribution of quality seeds. Under the government's Technology Mission, support was provided for the modernization of ginning and pressing units and the improvement of cotton marketing in recent years. These benefits are difficult to quantify, and some are not specific to cotton. In addition, the government supports the textile sector with a number of programs that provide direct support and soft loans.

European Union

25. Changes were introduced in the EU Common Agricultural Policy starting in 2009/10. As before, cotton producers receive 65% of EU support in the form of a single decoupled payment (income aid) and the remaining 35% in the form of an area payment (coupled, or production aid). Greece and Spain are the major cotton producers in the EU. For production aid the maximum base eligible areas are set at 250,000 hectares for Greece and 48,000 hectares for Spain. To be eligible for aid, the area must be located on agricultural land authorized by the EU member states for cotton production, sown under authorized varieties and actually harvested under normal growing conditions. The aid is paid for cotton of sound, fair and merchantable quality. The aid is paid per hectare of eligible area by multiplying fixed reference yields by the reference amounts fixed for each country. For the purpose of calculation of aid, the seed cotton yield per hectare is fixed at 3.2 tons per hectare for Greece and at 3.5 tons per hectare for Spain. The amounts per hectare are fixed at 251.75 euros for Greece and 400 euros for Spain. If the eligible area exceeds the maximum base area, the aid per hectare is reduced proportionally.

26. In 2014/15 the amount of direct subsidy to production in Greece was estimated at $238 million ($274 million in 2013/14), equivalent to 39 cts/lb of lint production (42 cts/lb in 2013/14). The subsidy in Spain is estimated at $72 million in 2014/15 ($91 million in 2013/14), or 44 cts/lb of lint (84 cts/lb in 2013/14). The decline is a result of budgetary cuts and a stronger U.S. dollar in relation to the euro.

Turkey

27. The government of Turkey pays a premium per kilogram of seed cotton to producers. In the past the premium for seed cotton produced from certified seeds was higher than that from non-certified seeds. No premium has been paid for non-certified seed since 2012/13. The premium for 2014/15 was increased to 0.65 TRL/kg, from 0.55 TRL/kg in 2013/14, for seed cotton produced from certified seeds. Assuming that 90% of Turkish cotton production is produced from certified seeds, and that all cotton producers applied for the premium, the Secretariat estimates that total payments to cotton producers in Turkey increased from $449 million in 2014/13, to $508 million in 2014/15.

Brazil

28. Brazil operates a marketing program that provides direct subsidies to producers based on guaranteed prices, but without direct acquisition of cotton by the government. The program is called the Equalization Price Paid to Producers (PEPRO – Prêmio Equalizador Pago ao Produtor). The PEPRO was used for several seasons prior to 2010/11 to compensate farmers for the weakening of the U.S. dollar in relation to the Brazilian real. No payments were made from 2010/11 to 2013/14. The PEPRO became operational again in 2014/15, when a number of auctions were held during September to November 2014. The premium paid under the program represents the difference between the minimum guarantee price and the price buyers are willing to pay. The minimum guarantee price is set at R$ (Brazilian real) 54.90 per arroba (15 kg) of lint, or an equivalent of 68 US cts/lb at the average exchange rate prevailing during September–November 2014. The actual size of the premium is determined at auctions organized by the government. In 2014/15, government payments under the PEPRO totaled $102 million (3 US cts/lb of total production).

29. The government of Brazil also provides support to cotton production through subsidized credit for production, marketing and investments. It is estimated that subsidized annual credit to cotton producers averaged around $500 million during the past decade. Low-income cotton growers receive a subsidized interest rate of 5%, compared with market rates of 20-25%. Based on this difference, it is estimated that the maximum annual subsidy received by cotton growers in the form of subsidized interest averaged $75 million over the past decade.

Colombia

30. In Colombia, direct government payments to producers in 2013/14 were estimated at $24 million, averaging 40 cents per pound. In 2014/15, direct government payments are estimated at $14 million, averaging 22 cts/lb. Actual payments in Colombian pesos declined by 27% during 2014/15, but payments in U.S. dollar equivalent declined by 42% due to the depreciation of the domestic currency.

West Africa

31. Several countries in West Africa provided subsidies for cotton inputs in 2014/15 and 2013/14, especially for fertilizers and planting seeds. In 2014/15, Mali provided an estimated $26 million (5 US cts/lb); Burkina Faso $30 million (5 US cts/lb); Côte d’Ivoire $14 million (3 US cts/lb); and Senegal $2 million (9 US cts/lb).

Table 1: Total Level of Assistance Provided by Governments to the Cotton Sector*

	2013/14			2014/15**		
Country	Production	Average Assistance per Pound Produced	Assistance to Production	Production	Average Assistance per Pound Produced	Assistance to Production
	1,000 tons	US cents	US$ Millions	1,000 tons	US cents	US$ Millions
China	6,929	34	5,149	6,480	58	8,224
India	6,770	0	0	6,507	4	633
Turkey	760	27	449	847	27	508
USA	2,811	7	454	3,553	6	490
Greece	296	42	274	274	39	238
Brazil	1,734	0	0	1,506	3	102
Spain	50	84	91	73	44	72
Mali	184	6.4	26	231	5	26
Burkina Faso	274	5	30	285	5	30
Colombia	27	40	24	27	24	14
Côte d'Ivoire	173	4	14	190	3	14
Senegal	12	8	2	11	9	2
All Countries	**20,020**	**15**	**6,513**	**19,983**	**22**	**10,353**

*Credit assistance not included. **Preliminary.

Table 2: Total Level of Assistance Provided by Governments to the Cotton Sector*

	World Production	Average Assistance per Pound Produced	Assistance to Production
	1,000 tons	US cents	US$ Millions
1997/98	20,181	9	4,108
1998/99	18,810	14	5,772
1999/00	19,194	16	6,588
2000/01	19,524	11	4,833
2001/02	21,667	13	6,446
2002/03	19,574	12	4,193
2003/04	21,131	7	3,270
2004/05	27,003	10	6,114
2005/06	25,701	11	6,008
2006/07	26,831	9	5,045
2007/08	26,155	4	2,292
2008/09	23,585	11	5,492
2009/10	22,334	6	3,155
2010/11	25,453	3	1,477
2011/12	27,847	8	4,866
2012/13	26,667	13	7,351
2013/14	26,283	11	6,525
2014/15**	26,209	18	10,353

*Credit assistance not included. **Preliminary.