COTTON MARKET COMMENTS

Price Floor Crushed by Economic Crisis

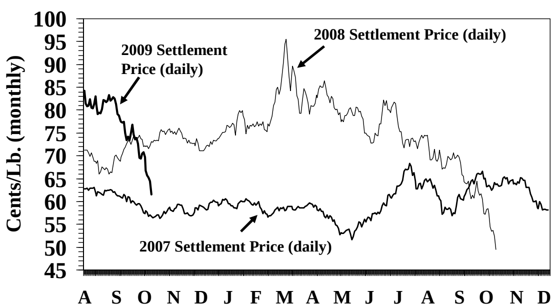
Carl G. Anderson
Professor Emeritus

October 13, 2008

December ’08 futures have dropped in excess of 30 cents per pound ($150 per bale) since late June to 49.44 cents on October 10, 2008. The economic crisis at home and abroad has weakened demand and “jerked the rug” out from under the market. Estimated world stocks have increased to more than 45 percent, indicating the “A” Index may slip below 60 cents, based on past fundamental supply/demand relationships.

The price rally for December ’09 futures to the dollar per pound level has disappeared for now. Yet, another 13 to 14 million bale harvest next season would leave tight stocks, unless exports fall below 10 million bales in 2010.

December 2007 Futures Settlement vs. December 2008 and 2009 Futures Settlement Price



The October USDA projection for the 2008/09 season average price for upland cotton was reduced substantially to the 51 - 62 cent range. A sizable counter-cyclical payment appears likely and possible marketing loan deficiency payments too.

The 2008 farm program provisions, based on a 71.25 cent target price, are expected to support cotton growers’ income. However, program payment yields and the 85 percent provision on direct and counter-cyclical payments will reduce total program payments well below the target price level. The expected decrease in energy, fertilizer and production expenses, will likely ease up on the current tight cost/price squeeze somewhat.

The USDA projections increased world production to 113.76 million bales and lowered consumption to 122.31 million. However, the economic crisis may further reduce mill use by some 4 to 6 million bales. With little change in 2008/09 production, the carryover of cotton could end up near the abundant 61.5 million bales carried over from last year’s crop.

The U.S. estimates for this season indicated slightly lower production at 13.7 million bales and much lower exports at 13.0 million for a total use of 17.4 million. The result is a big increase in expected ending stocks to 6.2 million.

The export market is shrinking. With China, India, and other foreign countries improving yields, the expected deficit in foreign production versus consumption has narrowed considerably to 17.86 million bales, from 20.98 million bales in September.

On the positive side, low prices are the best cure for improving consumption and reducing production. The surplus of cotton could still disappear next season.

Given the current depressed prices, the main market alternative for producers is to place their cotton in the CCC loan program. For those who followed a price risk program by purchasing December ’08 put options in early 2008 around 70 cents, cash flow looks good at 50 cent cotton. When needed, price insurance pays off well.

The Ag Market Network Teleconference will be Tuesday, October 14, 2008 at 7:30 a.m. Central Time. Speakers – cotton panel are O.A. Cleveland, Carl Anderson, Mike Stevens, and John Robinson. Pat McClatchy is the Ag Market Network Moderator. The conference will be live on radio station KFLP 900 AM Floydada, Texas; live over the Internet at www.AgMarketNetwork.net; or you can listen to a recording around noon at www.AgMarketNetwork.net. Weekly updates are made on Friday afternoon by Mike Stevens.

Partially funded by Cotton Incorporated