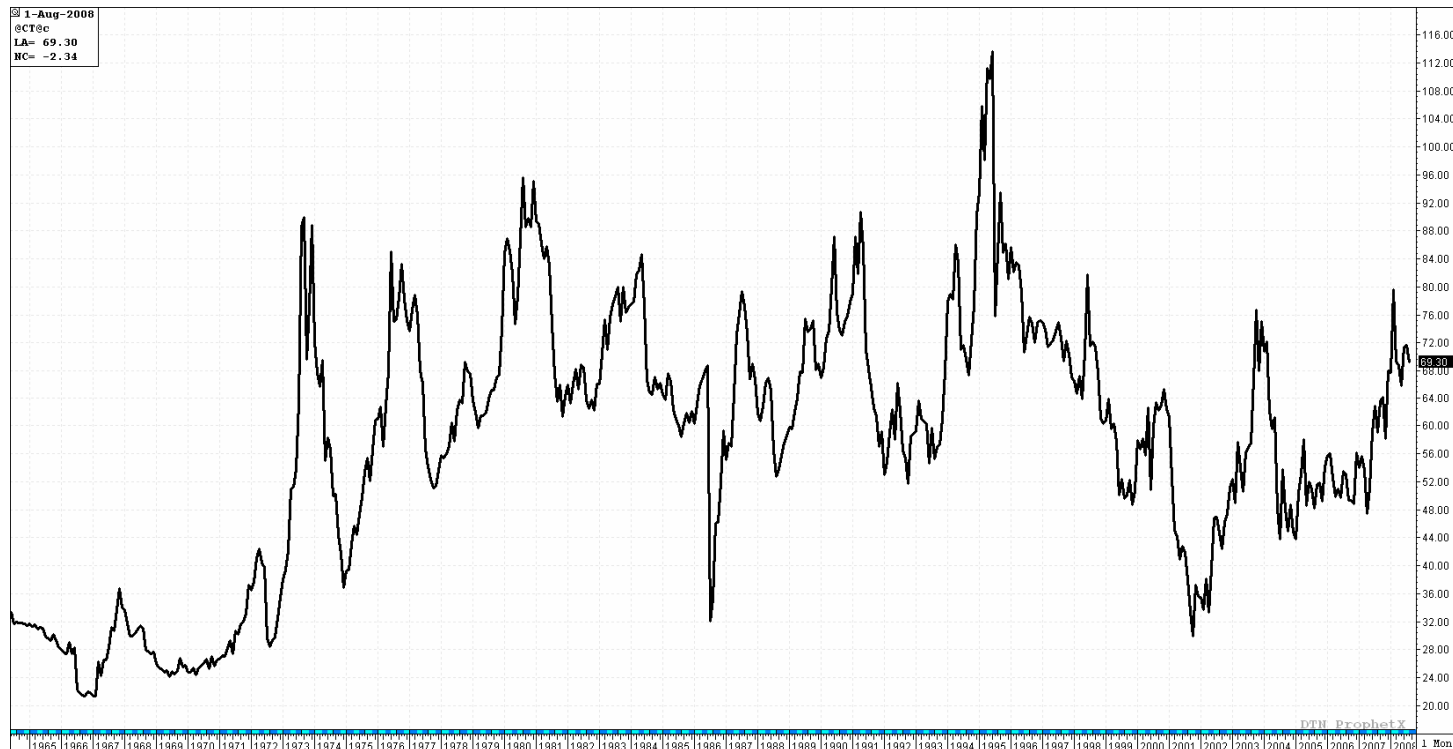




Six Factors That Will Rock Global Cotton Trade

**By Ed Jernigan
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Cotton is the underperformer of the agricultural sector; the single worst performing commodity since 2001.



World cotton trade is set to undergo the most dramatic changes in over 100 years.

SIX FACTORS ARE SET TO ROCK GLOBAL COTTON TRADE IN THE YEARS AHEAD.

Factor #1

The End of U.S. Cotton Surplus

Factor #1: The End of U.S. Surplus

The 2000 U.S. Farm Bill ushered in a period of record U.S. cotton production.

This provided the world with a supply cushion for the last eight years.

Factor #1: The End of U.S. Surplus

This means that global production growth outpaced the growth in consumption.

Each supply shock had limited impact; U.S. oversupply always meant ample supply.

Factor #1: The End of U.S. Surplus

**2006/07 U.S. carryout of 9.479 million bales
= 15% of world carryover.**

**2007/08 U.S. carryout of 10.200 million
bales = 16.7% of world carryover.**

Factor #1: The End of U.S. Surplus

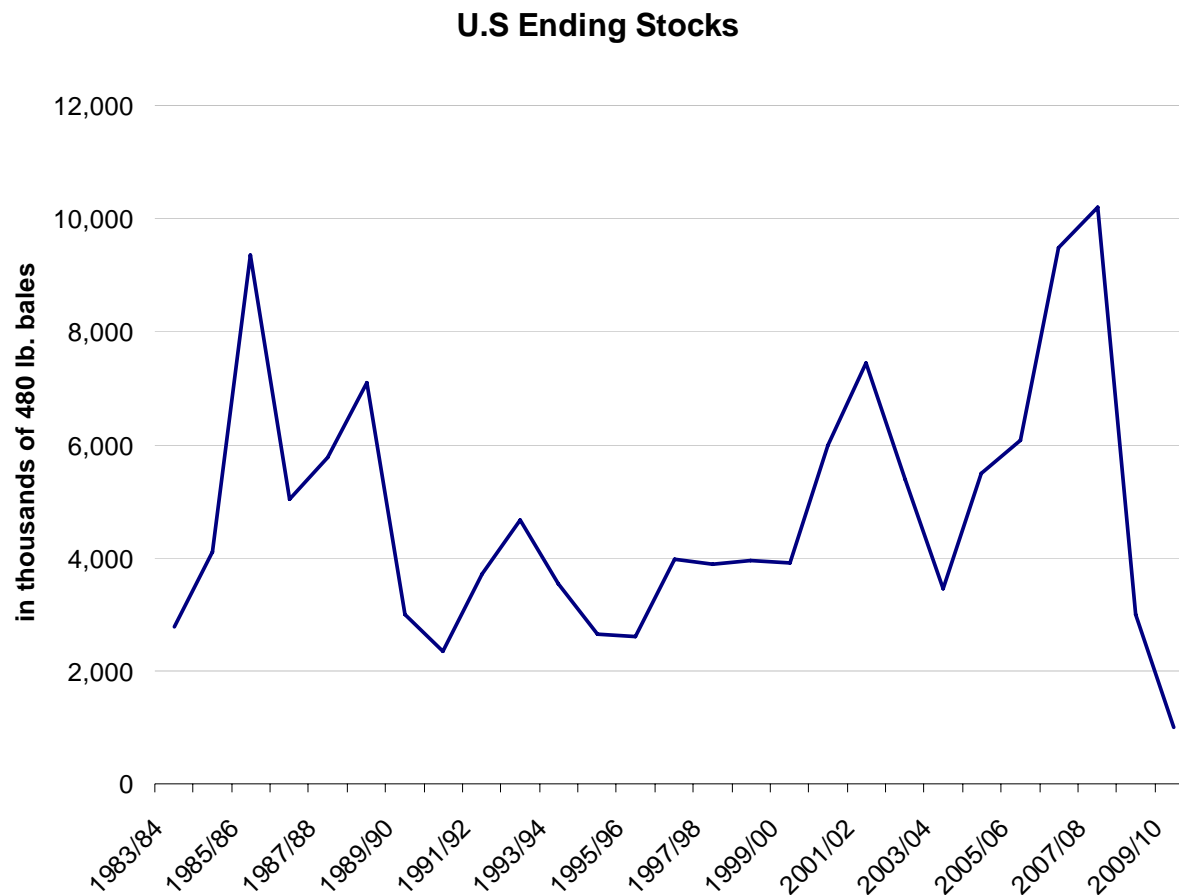
This is coming to an end:

2008/09 = 3.2

2009/10 = 1.0 or less

It is gone!

Factor #1: The End of U.S. Surplus



Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

After decades, the surplus in global food stocks is gone.

Driven by:

**Rise of China, India and Others
Increasing Population
Rise Ethanol and Biofuels
Climate Change
Growing Water Scarcity**

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Cotton now has to compete for acreage in most major-producing regions.

Acreage is determined by profitability, not government benefits.

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Rising input costs for all major crops.

Percentage of production costs related to fuel, fertilizer and chemicals.

Corn	56.7%
Wheat	49.3%
Cotton	35.4%
Rice	47.4%

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Fertilizer costs have exploded over 100 percent in 2008.

**Factor #2: Battle for Acreage is Now Worldwide –
Cotton versus Food**

**Biofuels: The rise of a new
consumer.**

**Biofuels used 7% of world
oilseeds in 2008.**

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

USA: Profitability of 2009/10 Crops

Prices as of July 30, 2008 – Average profit per acre in cotton belt states:

Corn	435.00
Soybeans	528.00
Cotton	200.00

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Under this profitability scenario, why would U.S. growers want to grow cotton?

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Brazil: Profitability of 2009/10 Crops

Prices as of July 30, 2008:

Corn	365
Soybeans	156
Cotton	141

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

In 2008, cotton acreage in India declined due to more profitable oilseed prices.

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Chinese grower input costs soared 35 to 50 % in 2008.

**Rising fertilizer costs
Rising labor costs
Rising pesticide/chemical costs**

**Pushed breakeven sharply higher;
profitability now requires record yields.**

Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

At current price levels, there is little incentive to expand cotton acreage anywhere.

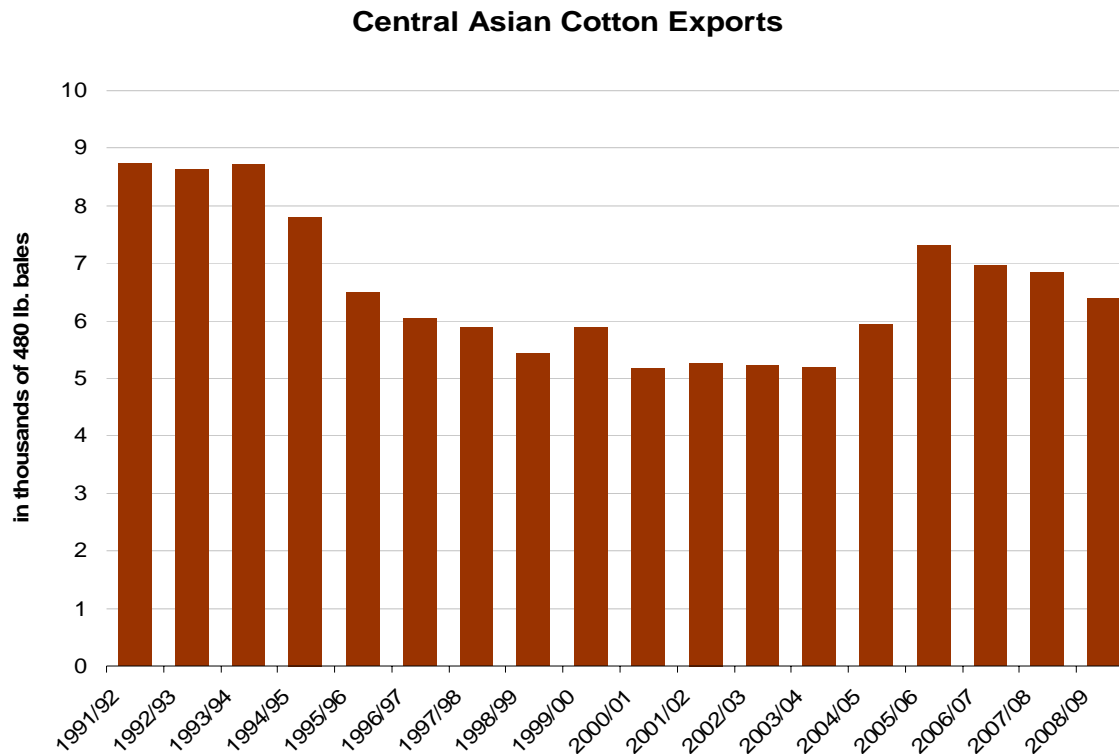
Factor #2: Battle for Acreage is Now Worldwide – Cotton versus Food

Cotton must now buy its acreage.

Factor #3: Central Asian Cotton Production to Sharply Decline – End of a Role.

Factor #3: Central Asian Cotton Production to Sharply Decline – End of a Role.

Central Asia has been one of the world’s largest cotton exporters since the breakup of the Soviet Union.

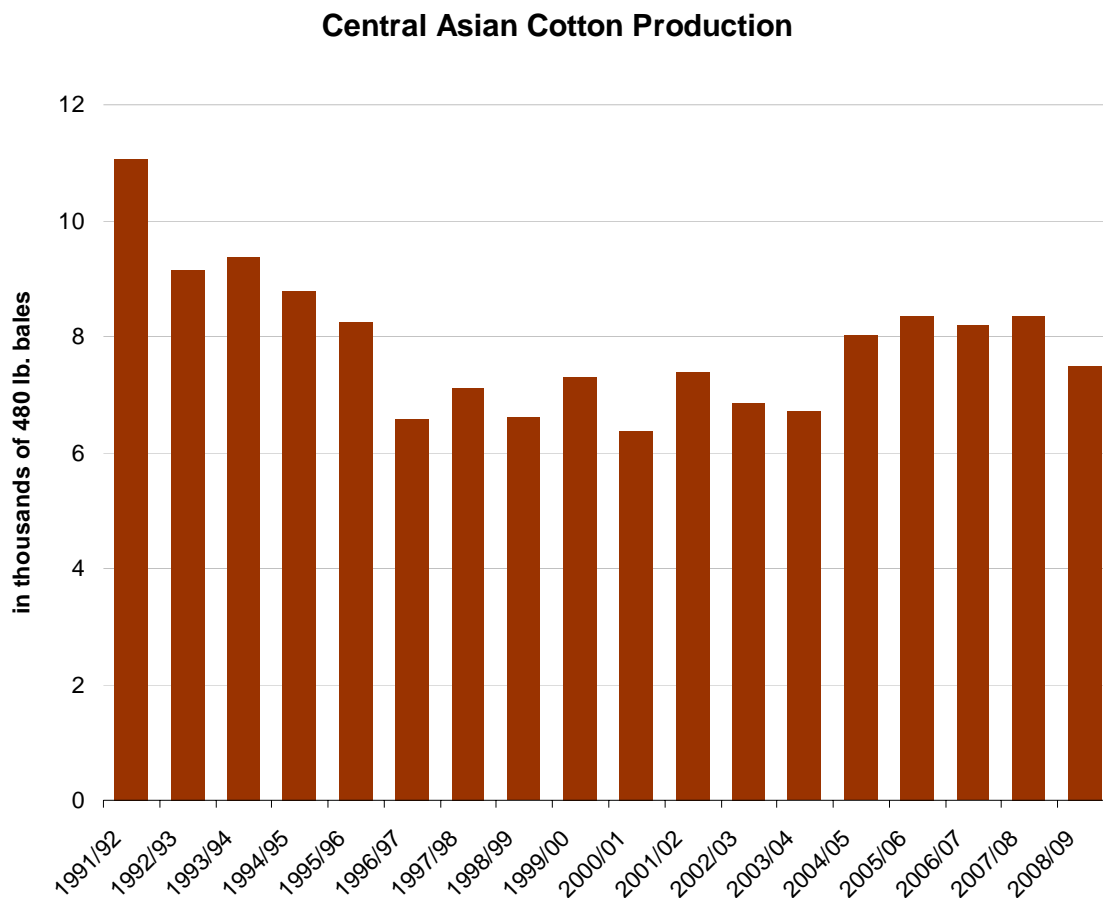


Factor #3: Central Asian Cotton Production to Sharply Decline – End of a Role.

Cotton production decline now accelerating.

- **Climate Change**
- **Drying of Aral Sea**
- **Inadequate investment in irrigation infrastructure**
- **Competition for dwindling water supplies, i.e. (Uzbekistan versus rest of region)**
- **Socialist farming practices continue**
- **Inadequate input investment**

Factor #3: Central Asian Cotton Production to Sharply Decline – End of a Role.



Factor #3: Central Asian Cotton Production to Sharply Decline – End of a Role.

Cotton in Central Asia has been a cash crop, always produced and sold regardless of price.

Now replaced by energy and metals as the leading export.

Factor #3: Central Asian Cotton Production to Sharply Decline – End of a Role.

Loss of Large Supplies from Central Asia will not be easy to replace.

- 1. Low freight costs to Subcontinent and Asia via Bandar Abbas Port;**
- 2. Short transit times to key import markets;**
- 3. Hand picked.**

Factor #4: Growing Importance of India

Today India is:

**World's second largest producer of cotton.
World's second largest consumer of cotton.
World's second largest exporter of cotton.**

Factor #4: Growing Importance of India

Tomorrow India will be:

World's largest producer of cotton.

World's largest exporter of cotton, replacing U.S.

World's second largest domestic market for textiles and apparel offtake.

Factor #4: Growing Importance of India

An additional 100 kilograms per hectare increase in average yield means 4.36 million bale increase in output.

2009/10 – 2010/11 output could exceed 30 million 480 pound bales.

Factor #4: Growing Importance of India

India enjoys a major advantage in shipping rates to Asia, making it a low cost supplier to the region.

Factor #4: Growing Importance of India

India has a large block of idle cotton spindles that await a return to profitability. This could significantly increase cotton consumption.

2007/08	18.400 million bales
2009/10	20.74 million bales
2010/11	22.26 million bales

Fact #5: Global Shakeout in Excessive Spinning Capacity

The world has an excess of cotton spindles.

Fact #5: Global Shakeout in Excessive Spinning Capacity

This overcapacity follows record investment in China, India and Vietnam.

Fact #5: Global Shakeout in Excessive Spinning Capacity

Global yarn prices will lag behind the sharp upward movement in cotton prices. This will significantly impact profitability of spinners – marginal inefficient producers will be forced to close down.

Fact #5: Global Shakeout in Excessive Spinning Capacity

World cotton consumption will dip in 2008/09; and as this takes hold, will bottom out in 2009/10 and show considerable growth in 2010/11.

2007/08	124.25
2008/09	124.00
2009/10	123.00
2010/11	130.00

Fact #5: Global Shakeout in Excessive Spinning Capacity

This will mean a return to profitability for the sector in 2009/10.

Factor #6: U.S./Japan/Europe No Longer the Center of the World

For the past 25 years, global cotton consumption at the retail level has been driven by the U.S., European and Japanese consumer.

Factor #6: U.S./Japan/Europe No Longer the Center of the World

These markets have seen:

- Slowdown in population growth.**
- Aging of Population.**
- Peak in consumer income.**

The growth markets are now:

- China**
- Russia/New Europe**
- Asia (Ex. China & Japan)**
- Middle East**
- India**

Factor #6: U.S./Japan/Europe No Longer the Center of the World

China: Apparel retail sales growing over 25 percent annually.

Doubling every four years – on track to surprise U.S. in next ten years.

Factor #6: U.S./Japan/Europe No Longer the Center of the World

This change in leadership means the offtake of textiles/apparel at the retail level is now dependent on the BRIC block of countries.

BRIC: Brazil, Russia, India & China.

Summary: Events Set to Rock the World of Cotton:

End of U.S. Surplus

Battle for Acreage – Cotton versus Food

Central Asian Production Set to Decline

Growing Importance of India

Global Shakeout of Excessive Spinning Capacity

U.S./Japan/Europe No Longer Center of the World

These events will reshape the world of cotton.

- **Price to be determined by supply/demand, not government subsidies.**
- **No global stockpile to act as cushion against supply stocks.**
- **Trade patterns.**
- **Production/consumption patterns.**

And finally the price.

**Prices will permanently breakout of the
50 to 80-cent range.**