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Cotton and Products

Annual Report

2006

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Report Highlights:

Despite an expected larger local cotton production in Marketing Year (MY) 2006-2007, Argentine spinners are likely to import 35,000 tons of cotton. Lint exports are projected to continue low at 12,000 tons. Domestic consumption of cotton is forecast to achieve a new record at 160,000 tons.

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Annual Report
Buenos Aires [AR1]
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SECTION I. SITUATION AND OUTLOOK

The Argentine cotton chain is projected to import 35,000 tons of cotton lint in Marketing Year (MY) 2006-2007, the highest level of the past three years, and the second highest level ever. This is as a result of a shorter than expected 2005-2006 cotton crop and to a continuing strong recovery of the domestic textile industry.

Cotton imports in MY 2005-2006 are expected to total about 30,000 tons, valued at approximately US\$34 million. During August 2005/March 2006, 28,000 tons were imported. Most cotton imported is good quality, mostly Strict Low Middling (SLM). Brazilian cotton accounted for 95 percent of Argentine imports in Calendar Year 2005, and 85 percent of what was so far imported in 2006 (through April). Although local spinners have to pay in advance to import Brazilian cotton, they prefer it due to the lack of contamination, quality, volume, homogeneity, and relatively short transportation time. Some cotton is also imported from Paraguay.

Cotton lint from the U.S. is not frequently imported. Although several merchants offer it, it has several disadvantages versus the regional product. In general, freight costs and import duties (6.5 percent) significantly increase the final cost. Some merchants also mention logistical problems and even some quality differences compared to Brazilian product. Most local spinners are now in a good financial situation, but they could be encouraged to purchase U.S. product if prices were competitive and credit were available. A local producer of denim will receive in the next few months a total of 640 tons of U.S. lint (SLM quality), which was purchased in late 2005. This purchaser has already received 60 tons, at an average FOB price of US\$1,110 per ton and an average CIF price of US\$1,180 per ton. At the moment of purchase, the decision was made based on the suitability of the final cost. The results in processing have been satisfactory.

There are approximately 15 local spinners which are currently importing lint. The first six companies accounted for 75 percent of 2005 imports. Most produce yarn and some denim too.

Argentina, once an important southern hemisphere cotton exporter (350,000 tons in 1996), is expected to continue to decrease its exports to a mere 12,000 tons in MY2006-2007. In the past few years, the conjunction of low world cotton prices, strong competition of profitable soybean production, weather problems, and more recently, strong domestic cotton demand, have resulted in reduced exports.

Lint exports in MY 2005-2006 are expected to total 18,000 tons, somewhat lower than the previous year. Exports during August 2005/March 2006 totaled 11,000 tons, and the balance is expected to be shipped from the new crop which is currently being harvested. The main exports are inter-company shipments, in hands of a Brazilian textile company which operates regionally and exports lint from Argentina to its branch in Chile. During this period, Chile accounted for approximately 40 percent of the total exports, followed by Thailand, Turkey, and Indonesia. In general, current exports are of medium to low quality cotton. The average FOB price of Argentine lint exports in the last months of 2005 was about US\$880 per ton.

One of the Argentine Government's (GOA) main policies is to maintain a competitive exchange rate in order to expand exports and limit imports. The exchange rate for 2006 is expected to range between 3.05 to 3.10 pesos to the dollar. However, with annual inflation rates of about 10-12 percent, the competitive advantage has been undercut.

Cotton production for 2006-2007 is forecast at 165,000 tons, the highest of the past five years. Despite erratic weather, most producers in the cotton area are quite enthusiastic as prices were better than the past year and a great number of producers made good profits in the current crop. Based on a comparison of returns on different crops produced by the National Institute of Agricultural Technology (INTA), cotton production in Chaco (the number one cotton-producing province) is more profitable than soybean and sunflower production in 2006. However, a strong limitation to further expansion is the weak financial situation of many small and medium producers and the lack of credit availability. The adoption and expansion of new technology and management, which increases yields at the farm level and reduces harvest costs significantly, is encouraging larger producers to refocus again in cotton production.

The local cotton complex is encouraged by the reduction of cotton subsidies which the U.S. has to implement and that the WTO Doha round is paying special attention to cotton due to its economic and social importance in developing countries.

A significant drawback to cotton production in future crops will be the imminent arrival of the boll weevil to the heart of the Argentine cotton producing area. During the current crop, it was detected only a few kilometers away from the city of P. R. Saenz Pena. It has not yet caused any significant damage, but most likely it will affect the coming crop, resulting in lower yields and higher production costs.

The local textile industry has been recipient of large investments in the past few years. However, practically all has been focused on improving quality, reducing costs and expanding the manufacturing capacity in spinners as the result of strong domestic demand. Investment in the farm and ginning level has been insignificant. In fact, many harvesters and some gin equipment have been exported to Brazil in the past few years. To get an idea of the installed capacity, in 1996, Argentina planted over one million hectares, produced 455,000 tons of lint and exported 350,000 tons of cotton.

Cotton domestic consumption for 2006-2007 is projected at 160,000 tons, the highest ever. A strong recovery of purchasing power, limits on inexpensive textile imports, and a strong tourism industry is expected to continue to fuel growth.

Cotton production in Argentina is not officially controlled nor promoted. Farmers freely decide what crops to produce. In the case of the very small producers (approximately 5 hectares of cotton) and small farmers (20 hectares of cotton), which are roughly estimated between 15,000-20,000, they generally receive some support from provincial or county governments. In most cases, it is seed, fuel or even some mechanical labor which have to be paid back, but in practice, they are seldom returned. After several years of low world cotton prices, some provincial governments implemented in 2005 (and the current one) a system by which, through a rented gin, they purchased raw cotton from small producers. By doing this, they set a minimum price in the market, making private gins and cooperatives pay similar values. In some cases, this cotton was exported, some was sold in the domestic market and even some was used to manufacture sheets to supply public hospitals. Small producers, whose production is significantly poor in quality and dirtier, received better prices. Last year the Argentine Congress voted in a law which promotes cotton production. It creates a system to protect producers from drastic price reductions, and calls for crop insurance. The law was approved, but the sector is still waiting for details on how it will be implemented.

SECTION II. STATISTICAL TABLES

PSD Table

Country Commodity	Argentina Cotton					
	(HECTARES)(MT)					
	2004	Revised	2005	Estimate	2006	Forecast
	USDA Official [Estimate[1]	USDA Official [Estimate[1]	USDA Official [Estimate[1]
Market Year Begin	08/2004		08/2005		08/2006	
Area Planted	0	404000	0	315000	0	410000
Area Harvested	374000	374000	285000	305000	0	400000
Beginning Stocks	112129	112129	124757	124757	98848	99757
Production	146965	146965	119750	118000	0	165000
Imports	23950	23950	21773	30000	0	35000
MY Imp. from U.S.	0	0	0	0	0	0
TOTAL SUPPLY	283044	283044	266280	272757	98848	299757
Exports	21337	21337	30482	18000	0	12000
USE Dom. Consumption	134990	134990	134990	153000	0	158000
Loss Dom. Consumption	1960	1960	1960	2000	0	2000
TOTAL Dom. Consumptic	136950	136950	136950	155000	0	160000
Ending Stocks	124757	124757	98848	99757	0	127757
TOTAL DISTRIBUTION	283044	283044	266280	272757	0	299757

SECTION III. NARRATIVE ON SUPPLY AND DEMAND, POLICY & MARKETING**Production**

After an erratic 2005-2006 crop, where some areas had excellent yields and others suffered floodings (like the case of the irrigated area in Santiago del Estero) or drought (in the central-north part of Chaco), most contacts expect increased plantings this coming year, compared to 2005-2006. The reasons for increased planting include: improved farmers' price, high yields in southwest Chaco last year, and expected lower profitability of alternative crops compared with cotton. Post estimates harvested area at 400,000 hectares. Contacts' projections range between 340-440,000 hectares.

Some large producers in the south west of Chaco are adopting a narrow-furrow planting system. Instead of sowing at 0.70 centimeters or 1 meter between furrows, they sow at 0.25-0.35 meters between furrows. Despite somewhat higher costs than the traditional system, raw cotton yields are significantly higher. They then harvest with a modified picker called stripper. This machine harvests the whole plant, reducing harvest costs tremendously. INTA has also developed a harvester which is pulled by a tractor, reducing costs significantly as it is a quite inexpensive machine. They indicate that for a yield of 1.5 tons of raw cotton, hand picked harvest costs US\$150 per ton. Using a cotton picker costs US\$60 per ton and with the "pulled" stripper the cost is only US\$17 per ton. With the combination of higher yield at the farm and lower harvest costs, many believe this technology will change cotton production in Argentina. However, yields at the gin drop significantly (some say they go as low as 25 percent), due to large amount of trash and foreign matter, the ginning process is more expensive, and the quality of the final product is not as good as with the traditional method. Several technicians and private companies are in the process of adjusting this system, which if works as a whole package, it will definitely improve farmers' returns and allow a greater expansion of the cotton acreage.

The following table is based on information prepared by INTA (Feb. 2006), and shows returns (not including overhead costs) of different crop alternatives in Chaco province. The analysis is based on efficient producers (in US\$ per hectare):

	Cotton	Sunflower	Soybeans
Gross Income	865	299	433
Marketing Costs	68	64	89
Production Costs	164	100	118
Harvest Costs	104	30	43
Total	529	105	183

Planted and harvested cotton area generally differs, as practically in every crop there are losses either because of floodings or drought. In 2005-2006 there were a few thousand hectares lost in the irrigated area of Santiago del Estero due to strong rains in a short period of time. The central-north part of Chaco was affected by drought, but total losses were not large, as most farmers will harvest even though yields are low.

Most cotton produced in Argentina is not irrigated. However, there are several areas in which irrigation is used. This is the case of Santiago del Estero (approximately 22,000 hectares in 2005-2006), Cordoba, and La Rioja provinces.

The use of agricultural chemicals is efficient in most medium and large producers. Small producers usually do not have the possibilities of good crop protection. GMO seed was

launched in late 1990s and has helped to increase yields and reduce the use of insecticides. Bt cotton, a variety developed in the United States, has cut in half the average 5-6 applications per crop when using traditional seed. Roundup Ready cottonseed (using a local variety) has also helped weed control and reduced production costs. Although some people state that seed combining both technologies is ready to be approved, it is doubtful it will be marketed as seed companies have had serious trouble collecting fees and controlling illegal multiplication. INTA is currently working on and testing colored cotton varieties. The release in the market is expected in a few more years and will be focused on niche markets for small and medium producers.

At this point, nobody knows what the real impact would be if there was a general boll weevil attack in the cotton area of Argentina. However, some estimate that yields would drop about 10-15 percent and the cost to fumigate would be around US\$100 per hectare. If this were the case, cotton competitiveness vis-à-vis other alternatives could diminish significantly.

Consumption

Local cotton consumption for 2006-2007 is projected at 160,000 tons, a record high. This is as a result of a strong economic recovery, higher purchasing power, the limitation of large imports of inexpensive textiles, a strong dollar which discourages imports and encourages exports, more expensive artificial yarn due to high oil prices, and an incredibly large influx of foreign tourism which buy large volumes of products. The combination of all these factors has strengthened demand to such a point that almost all players are back in business and strong investment in quality and capacity are demanding more and more lint. Private sources estimate that about 70 percent of the fabric produced locally is transformed domestically.

Local production of artificial fibers and yarn in 2005 was almost unchanged from the previous year, while production of cotton textiles grew significantly. The most popular products are polyester yarn and fiber, and industrial nylon. Acrylic fibers are making a come back after several years of insignificant consumption. Demand for artificial fibers for 2006 is forecast to remain unchanged.

Stocks

The government does not intervene in cotton stocks. However, some provincial governments last year began buying raw cotton, but with the focus on establishing a higher minimum price for small producers not to regulate the market. Most cotton is in the hands of spinners, which buy large volumes during harvest, gins, and large producers. The MY 2005-2006 will be short, with the need to import large volumes.