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Brazil

Cotton and Products

Cotton Annual Report

2007

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Report Highlights:
Post estimates that 2006/07 production will be 6.5 million bales, with exports of 1.35 million bales and imports of 500,000 bales. Due to the increase in production in 2006/07 (most of which will be harvested in June and July 2007), exports in 2007/08 are expected to increase to 2 million bales and imports to decrease to 200,000 bales. Post anticipates that area will decrease ten percent in 2007/08 due to a continuing strong exchange rate, leading to 2007/08 production of 5.8 million bales.

Includes PSD Changes: Yes
Includes Trade Matrix: Yes
Annual Report
Brasilia [BR1]
[BR]

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Executive Summary

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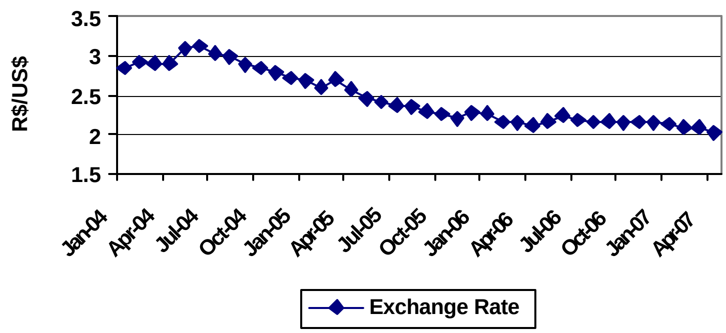
Economic Situation

In 2006, GDP growth was 3.7 percent, up from 2.9 percent in 2005, and inflation was under control at 3.1 percent. 2006 per capita GDP was $5,710, and unemployment remains high. The export sector was the main driver of economic growth in 2006, as total exports expanded 17 percent. The outlook for 2007 is for economic growth between 3.5 and 4.0 percent and lower inflation and interest rates. The Real, however, will likely remain strong.



PS&D

Cotton							
	2005	Revised	2006	Estimate	2007	Forecast	UOM
	USDA Official	Post Estimate [New]	USDA Official	Post Estimate [New]	USDA Official	Post Estimate [New]	
Market Year Begin		08/2005		08/2006		08/2007	MM/YYYY
Area Planted	0	0	0	0		0	(‘000 HA)
Area Harvested	850	856	1065	1075		970	(‘000 HA)
Beginning Stocks	5081	5081	3917	4084		5584	(‘000 480lb bales)
Production	4700	4767	6500	6500		5820	(‘000 480lb bales)
Imports	308	308	600	500		200	(‘000 480lb bales)
MY Imp. from U.S.	0	0	0	0		0	(‘000 480lb bales)
TOTAL SUPPLY	10089	10156	11017	11084		11604	(‘000 480lb bales)
Exports	1972	1972	1400	1350		2000	(‘000 480lb bales)
USE Dom. Consumption	4200	4100	4150	4150		4200	(‘000 480lb bales)
Loss Dom. Consumption	0	0	0	0		0	(‘000 480lb bales)
TOTAL Dom. Consumption	4200	4100	4150	4150		4200	(‘000 480lb bales)
Ending Stocks	3917	4084	5467	5584		5404	(‘000 480lb bales)
TOTAL DISTRIBUTION	10089	10156	11017	11084		11604	(‘000 480lb bales)
Stock to Use %	63.46403	67.25955	98.5045	101.5273		87.16129	(PERCENT)
Yield	1204	1213	1329	1316		1306	(KG/HA)

Production

Of the main crops in Brazil, cotton is considered to have one of the best returns. This is despite its high cost of production, approximately 40 percent of which is for agricultural chemicals (pesticides, etc.).

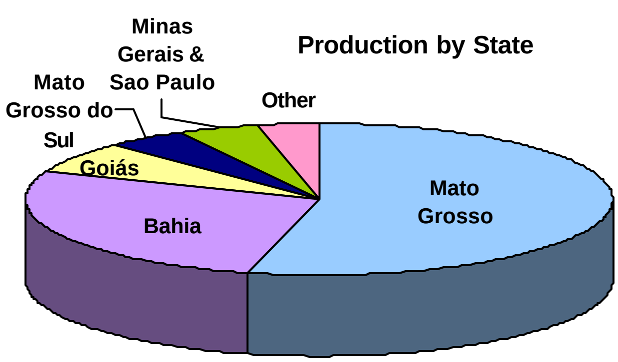
In March 2005, the National Technical Commission on Biosafety approved one type of Bt cotton for planting and commercialization. However producers were not allowed to plant biotech cotton in the 2006/07 year, as the event needed to be registered with the Ministry of Agriculture (MAPA) following studies on the value of the use of the seed.

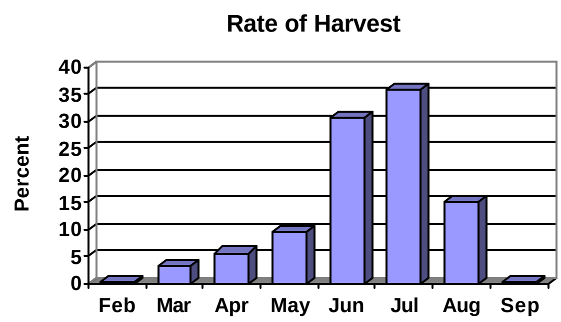
In 2006, MAPA found 18,000 hectares of illegally planted Roundup Ready cotton. The cotton was confiscated and the fields were cleared and burned. Estimates are that producers planted approximately 100,000 hectares (11 percent of total area) with illegal Roundup Ready cotton, following in the footsteps of soybean producers, who planted pirated biotech seeds that were only approved by the government after the fact.

In 2006/07, producers increased area approximately 26 percent. The largest increases were in Mato Grosso and Mato Grosso do Sul (47 and 45 percent, respectively), as corn and soybean prices were low during the planting season. However, the South and Southeast experienced a large reduction in planted area, with the largest reduction in Sao Paulo (37 percent). This was mainly due to producers increasing sugar cane area. In Goias, producers increased area approximately 16 percent as they moved cotton to the higher elevations, making room for sugar cane in the lower elevations. The resultant longer growing cycle, along with increased technology, has increased productivity in Goias by 20 percent.

Reports to date indicate that the current crop looks good, with few problems. If all continues to go well, 2006/07 production could reach 6.5 million bales (1.4 million mt).

Post expects a 10 percent reduction in area in 2007/08 due to the strong exchange rate, which increases the cost of production (in part due to higher fertilizer prices). Soybeans and corn require less fertilizer than cotton, and require no fertilizer the first year after a cotton crop. A rotation to soybeans or corn would also fulfill the need for crop rotation. With yields following the normal trend, this reduction in area would result in production of 5.82 million bales (1.27 million mt) in 2007/08.





Prices/Minimum Prices

The last time that the minimum price for cotton was changed was before the 2003/2004 crop, when the price was raised from R$33.90/15 kg to R$44.60/15 kg. Except for a brief spike in prices in early 2006, the average monthly price of cotton had been below the minimum price since October 2004. However, in early 2007, the average monthly price rose above the minimum price, increasing nearly eight percent between December 2006 and February 2007 (to an average February price of R$1.4431/lb). This prompted the federal government to begin selling stocks (see Stocks), resulting in a 5.6 percent reduction in the domestic price (to an average April price of R$1.3623/lb).

2006/07 Minimum Price for Cotton

Region	Unit	Price (R$/unit)	Price (R$/lb)	Price (US$/lb)
All	15 kg	44.60	1.3487	0.6639

Source: MAPA/SPA/DEAGRO
Exchange rate: US$1 = R$2.03160 (5/07/07)

Cotton Prices

Prices in cents of R$ per lb

Year	2005	2006	% Change
Jan	122.86	135.09	10%
Feb	128.64	138.26	7%
Mar	121.10	136.25	13%
Apr	126.36	130.10	3%
May	113.24	125.17	11%
Jun	118.35	133.04	12%
Jul	119.10	128.44	8%
Aug	111.98	132.43	18%
Sep	106.60	130.13	22%
Oct	105.72	129.54	23%
Nov	104.87	128.89	23%
Dec	109.79	133.77	22%

Source: CEPEA

Consumption

In spite of annual variations, Brazilian industrial use of cotton has remained relatively stable over the last 15 years, with an average annual growth rate around one percent. In comparison, industrial use of artificial and synthetic fibers has increased an average of nearly five percent over the last 15 years, evening out slightly in recent years with a 5-year annual growth rate of 1.5 percent. Cotton consumption is expected to remain relatively stagnant in 2007/08, increasing only slightly from 4.15 million bales to 4.2 million bales. (see Policy)

Trade

Despite a 43 percent decrease in exports to Europe between 2004/05 and 2005/06, Brazilian cotton exports increased 27 percent, mainly as a result of significantly higher demand from China and Pakistan. This was helped by government utilization of the PEPRO program, as high domestic prices resulted in much cotton that had been sold for export being diverted to the domestic market. (See Policy section and GAIN report BR7602 for more info.)

Due to the small crop in 2005/06 (which was harvested towards the end of the 2005/06 year), a 30 percent reduction in exports is expected in 2006/07, to 1.35 million bales

(294,000 mt). The majority of these exports are going to Pakistan, Indonesia and South Korea. As of end-April 2007, South Korea had already imported 82 percent more Brazilian cotton than the entire 2005/06 year.

As most of the 2006/07 production will be harvested towards the end of the trade year, exports from this crop will be made in 2007/08. Post expects exports will rebound to 2 million bales (435,000 mt), slightly higher than the 2005/06 record of 1.97 million bales. Reports indicate that 65 percent of the coming crop has already been sold, with nearly half of the amount sold destined for export. However, some of the cotton sold for export is expected to be switched to the domestic market.

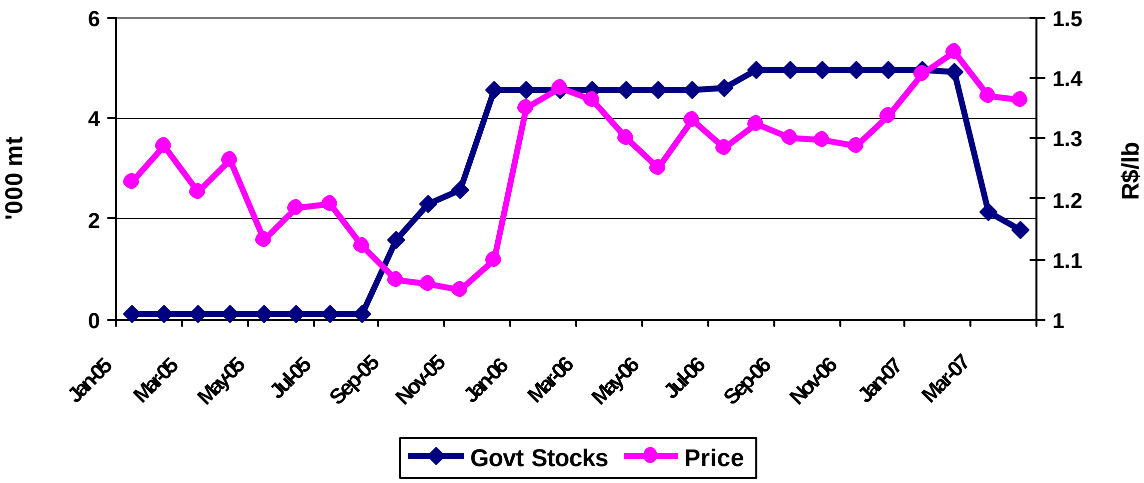
The majority of Brazilian cotton imports is supplied by the United States and Paraguay, with the next largest suppliers (in recent years) being Benin and Mali. Brazil is expected to import 500,000 bales (109,000 mt) in 2006/07 as a result of low domestic production in 2005/06 (which was harvested primarily in June and July 2006).

Industry groups assert that a significant amount of cotton and textiles enter the country illegally in order to avoid paying taxes. According to them, approximately 60,000 bales (13,000 mt) of contraband cotton entered the country from Asia in 2005. In response, the Receita Federal (the equivalent of U.S. Customs) has set up a website for people to provide tips of possible fraud or illegal withholding by importers.

Due to the increase in domestic production in 2006/07, imports are expected to fall to 200,000 bales (43,500 mt) in 2007/08.

Stocks

The Brazilian government (GOB) purchases and sells cotton as part of its effort to control prices. When prices were low in the second half of 2005, the government purchased 4,500 mt of cotton, increasing government stocks to the highest level in two years (but still well below the March 1987 high of 166.5 million tons). In January 2007, prices rose above the minimum guaranteed price and continued to rise in February. In response, the GOB sold nearly 2/3 of its stocks during March and April in an effort to lower the domestic price.



Policy

On April 25, the Government of Brazil (GOB) approved raising the tariff on textiles and ready-made items from 20 percent to 35 percent, the maximum allowed under its WTO commitments. This change would be primarily a means of dealing with competition from China, whose products are cheaper in the Brazilian market than locally-made products (some say unfairly so). Brazilian imports of apparel and footwear increased 124 percent between 2004 and 2006, with approximately half of those imports coming from China. Imports of Chinese apparel alone increased 171 percent during this period. The new tariff can not go into effect unless all members of Mercosul agree to it. The next meeting of the Mercosul Counsel of Ministers will be at the end of May, at which point they will determine whether or not to raise the tariff. If agreed to, the tariff increase could be in effect by July. Meanwhile, Brazil is challenging in Peruvian court the nine percent antidumping duty that Peru has established on Brazilian textiles under the argument that they are being sold in Peru at a lower price than they are sold in Brazil. While the increased import tariff has the potential to increase domestic consumption of cotton, the strong exchange rate hurts the export of textiles and is leading to issues such as that faced in Peru. Post expects the two to balance each other, resulting in continuing stagnant domestic consumption in the coming year.

According to the Ministry of Agriculture, Brazil provided R$255.5 million (US$125.8 million) to the cotton industry in support for commercialization in 2006. This amount, while significant, is considered to be de minimis spending, as it is less than 10 percent of the value of production, and is therefore never counted against Brazil's Aggregate Measurements of Support (AMS) commitment in the WTO. This support was provided almost exclusively through the use of the PEPRO program (see Government Programs). It was very popular with the industry, which considers it to be critical due to the current strong Real that is making Brazilian cotton increasingly expensive on the international market. They requested that it be used again in 2007. Between April 18 and May 4, the GOB responded with three PEPRO auctions, offering a total of 729,932 mt (3.35 million bales).

The quantity of cotton supported by the government in 2006 is provided in the table below, as well as descriptions of the major government programs. These programs are utilized to support commodity prices and to assist in the flow of cotton from the production areas to the consumption areas. While some of this cotton is exported, these programs are not considered to be export subsidies since the recipient is not required to export the product. In addition, a waiver for developing countries in the WTO Agriculture Agreement allows them to subsidize transportation.

Government Support for the Commercialization of Cotton ('000 mt)

Program	2004	2005	2006
Acquisition (AGF)	0	4.5	0
PEP	89.6	136.5	1.8
PROP	0	272.2	0
PEPRO	0	0	461.5
Total	89.6	413.2	463.3
Production	1,309.4	1,298.7	1,037.8
Participation %	6.8%	31.8%	44.6%

Source: Brazilian Ministry of Agriculture/SPA/DEAGRO

Government Programs

The Equalization Premium Paid to the Producer (Prêmio Equalizador Pago ao Produtor, PEPRO) is a premium granted to the farmer or cooperative which sells its products at public auction, where the government pays the difference between the Reference Value established by the government and the value of the premium (the maximum value paid by the government as a guarantee of the Reference Value).

Risk Premium for Acquisition of Agricultural Products Deriving from Private Contracts of Sales Options (Prêmio de Risco para Aquisição de Produto Agrícola Oriundo de Contrato Privado de Opção de Venda, PROP) is a subsidy program granted in the form of a public auction for the consumer to acquire, at a future date, a determined product directly from the producer and/or cooperative at a prefixed price, utilizing a private contract for the option to sell.

The Premium for Marketing of Products (Prêmio de Escoamento de Produto, PEP) provides the minimum guaranteed price to producers and cooperatives by paying the difference between the minimum guaranteed price and the market price. The objective is to supplement the supply of commodities in areas of the country considered to be deficient in agricultural production, such as the Northeast of Brazil. In PEP, the product is taken from private stocks.

Federal Government Acquisition (Aquisição do Governo Federal, AGF) allows the government to acquire agricultural products at the minimum price when the market price is below the minimum. It also allows the government to acquire products at market prices for use in the A*gricultura Familiar* Program and to build strategic stocks.