



USDA Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Template Version 2.09

Required Report - public distribution

Date: 11/28/2008

GAIN Report Number: IN8140

India

Cotton and Products

Quarterly Update - December

2008

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Report Highlights:

Post continues to estimate MY 2008/09 cotton production at 24.0 million bales. The government of India (GOI) has raised the minimum support price of different varieties of seed cotton by 28 to 46 percent over last year, while cotton prices have declined sharply. Consumption has been revised lower to 17.5 million bales on poor demand; and exports have been revised lower to 5.1 million bales due to weak international prices. Other PSD estimates remain unchanged from Post's September 2008 Cotton Update (IN8102).

Includes PSD Changes: No
Includes Trade Matrix: No
Quarterly Report
New Delhi [IN1]
[IN]

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SECTION I – SITUATION AND OUTLOOK

Table 1: Commodity, Cotton (480 lb bales), PSD

Cotton India	2006			2007			2008		
	2006/2007			2007/2008			2008/2009		
	Market Year Begin: Aug 2006			Market Year Begin: Aug 2007			Market Year Begin: Jun 2008		
	Annual Data Displayed		New Post	Annual Data Displayed		New Post	Annual Data Displayed		Jan
	USDA Official	Old Post data	Data	USDA Official	Old Post data	Data	USDA Official	Old Post data	Data
Area Planted	0	9,142	9,142	0	9,550	9,550	0	9,100	9,340
Area Harvested	9,166	9,142	9,142	9,550	9,550	9,550	9,400	9,100	9,340
Beginning Stocks	8,064	8,064	8,064	7,664	7,664	7,664	7,014	7,114	6,914
Production	21,800	21,800	21,800	24,600	24,600	24,600	25,000	24,000	24,000
Imports	465	465	465	450	450	450	500	800	500
MY Imports from U.S.	0	0	157	0	195	195	0	250	200
Total Supply	30,329	30,329	30,329	32,714	32,714	32,714	32,514	31,914	31,414
Exports	4,565	4,565	4,565	7,400	7,200	7,400	5,900	6,250	5,075
Use	18,100	16,823	18,100	18,300	18,400	18,400	18,000	18,500	17,500
Loss	0	1,276	0	0	0	0	0	0	0
Total Dom. Cons.	18,100	18,099	18,100	18,300	18,400	18,400	18,000	18,500	17,500
Ending Stocks	7,664	7,665	7,664	7,014	7,114	6,914	8,614	7,164	8,839
Total Distribution	30,329	30,329	30,329	32,714	32,714	32,714	32,514	31,914	31,414

Note: Production figures in the table include 937,000 bales of loose cotton.

Production

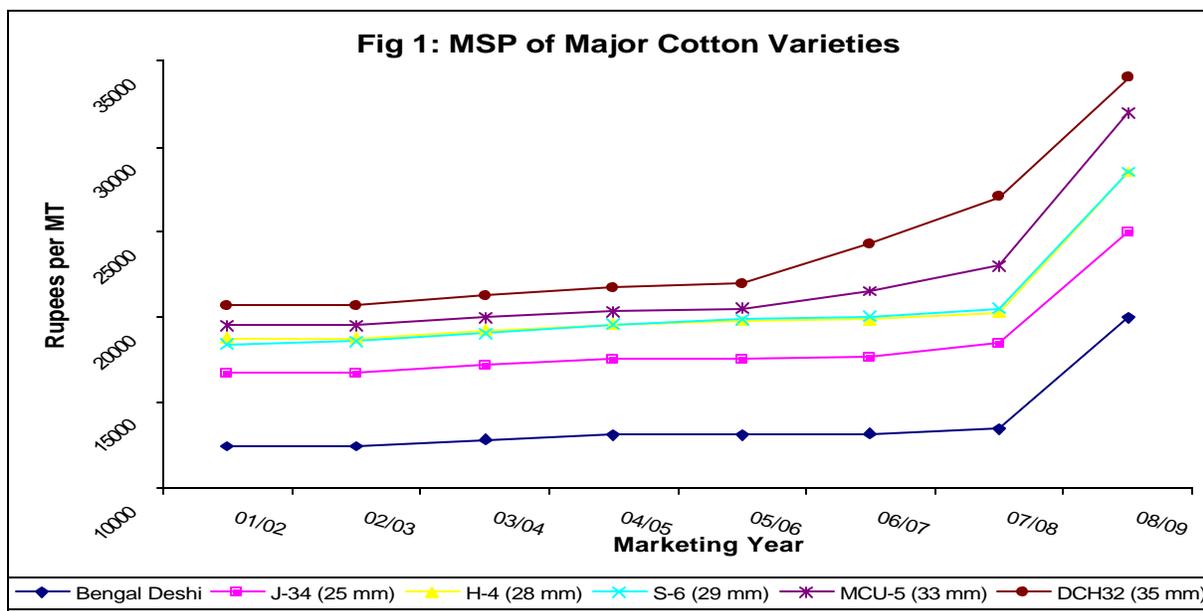
Post continues to estimate India's MY 2008/09 cotton production at 24.0 million bales despite higher than earlier estimated planting in September Quarterly Update (IN8102). Based on the latest planting estimates compiled by the Ministry of Agriculture, MY 2008/09 area is raised higher to 9.34 million hectares from the earlier estimate of 9.1 million hectares due to higher late season planting in the central states (Gujarat, Maharashtra, and M.P.), and record planting in Andhra Pradesh. However, yield prospects are expected to be adversely impacted by a delay in cotton planting and less-than-favorable weather conditions compared to last year in the central states of Maharashtra and Gujarat. After the initial optimism, most industry sources have lowered their crop expectations for the upcoming season, which is currently ranging from 21.9 to 24.2 million bales. The Cotton Advisory Board is expected to meet in December to review their first forecast of the MY 2008/09 crop of 25.1 million bales (32.2 million Indian bales) which was estimated in their last meeting on October 16, 2008.

The crop is progressing well under adequate moisture conditions and there are no reports of any major pests/disease attacks in most of the cotton growing regions. Provisional figures from the Ministry of Agriculture estimates the area planted under official Bt seeds in MY 2008/09 at 6.81 million hectare compared to 6.33 million hectare last year. However, trade sources report that a share of the incremental area has come from the cotton area previously sown under 'illegal' Bt seeds. Nevertheless, a 30-45 days delay in planting of the cotton crop may adversely impact their yield due to shorter crop duration and reports of farmers shifting

from higher yielding hybrid staple cotton varieties to lower yielding short staple conventional varieties. Market sources also report that the cotton crop in central states of Maharashtra and Gujarat has been slightly impacted by erratic rains in September/October and less-than-favorable weather conditions compared to last year. Consequently, Post expects overall cotton yields to be same as last year despite increased acreage under official Bt cotton seeds and absence of any major outbreak of pests and diseases.

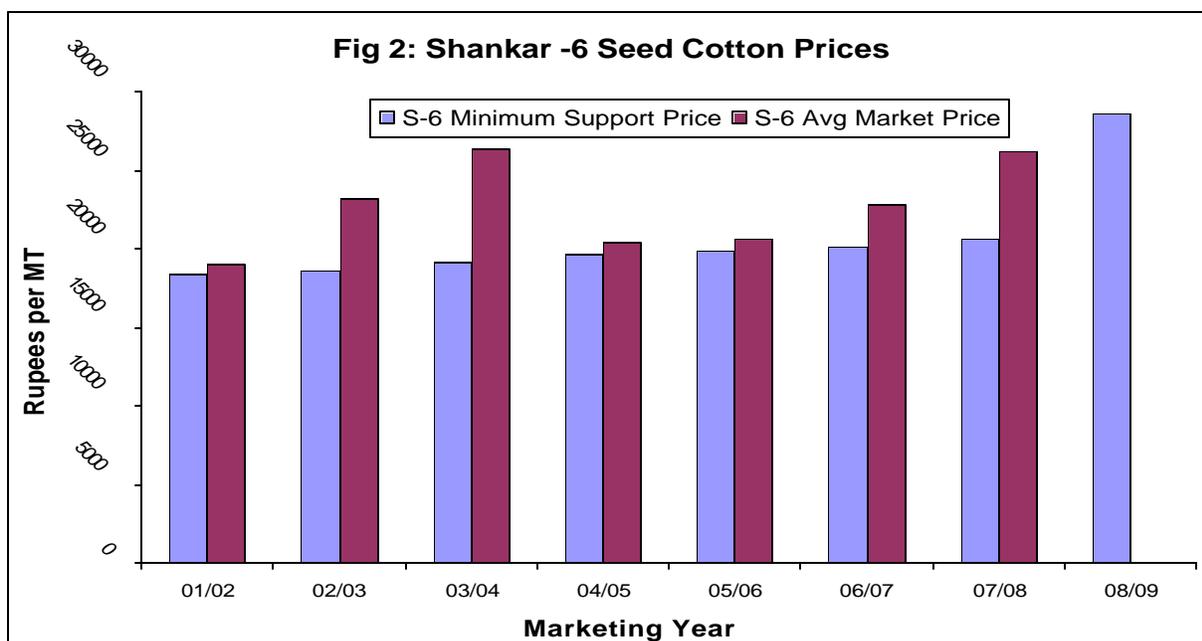
Government Hikes the Minimum Support Price but Cotton Price Crash

At the beginning of every marketing season, the Government of India (GOI) establishes minimum support prices (MSP) for seed cotton, the assured price at which government will procure seed cotton from the farmers. The Cotton Corporation of India (CCI), a government organization, is responsible for price support operations in all states. Sometimes, the National Agriculture marketing Federation and State marketing federations may assist the CCI in the MSP operations. In September, the government announced a significant hike in the MSP of seed cotton, with the increase ranging from 26 percent to 48 percent for different varieties.



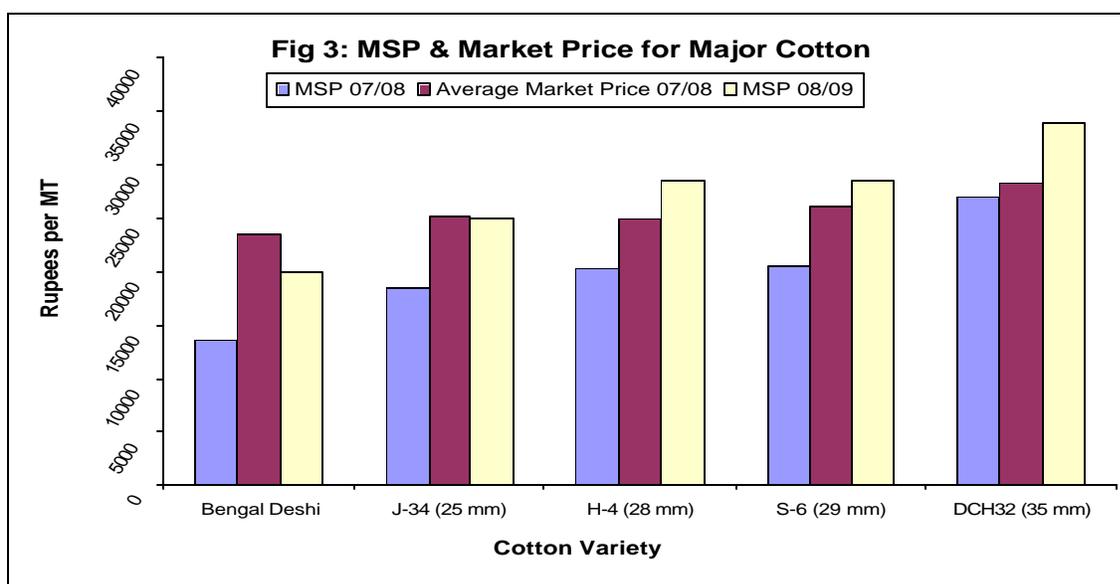
Source: Textile Commissioner’s Office, GOI.

Traditionally, the MSP are fixed based on the cost of production of seed cotton, and are not directly linked to market price of cotton (lint or fiber). Typically, market prices of seed cotton remains well above the MSP, and move in tandem with cotton prices.



Source: Cotton Corporation of India.

The cotton prices have been gaining strongly during the last marketing season (see figure 4), particularly after Feb/March when most of the seed cotton has been procured from the farmers. Some farmers and policy makers alleged that the traders gained from the late price increase and farmers were not adequately compensated. Assuming the cotton prices would continue to remain strong, the MSP for most of the staple cotton varieties were increased higher than the average market price for seed cotton during the MY 2007/08 in September.

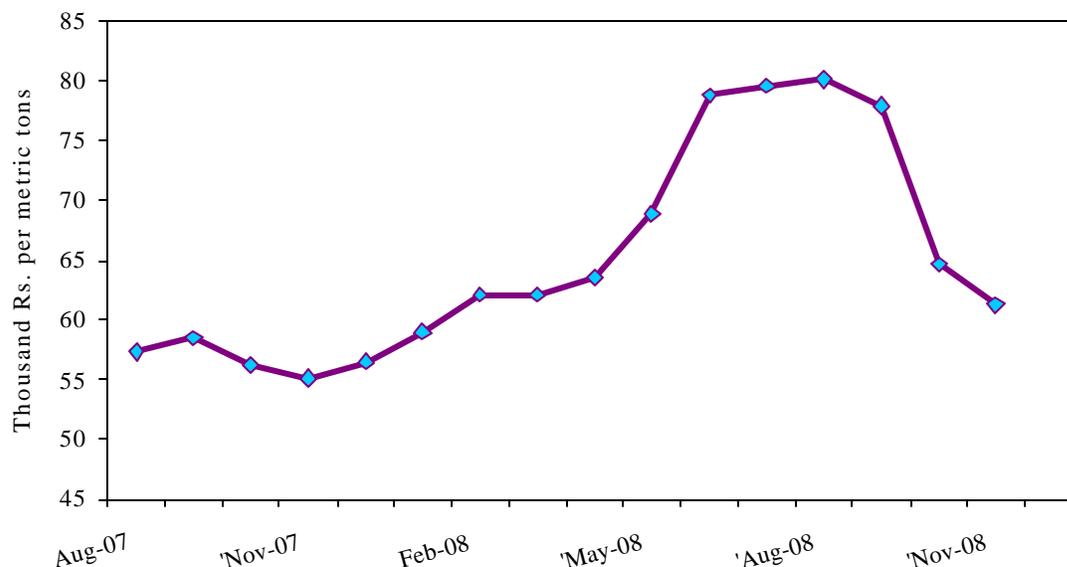


Source: Cotton Corporation of India.

Meanwhile, global commodities markets were in turmoil and international cotton prices declined sharply. The domestic cotton prices have also declined from the beginning of MY 2008/09 on weak international prices and slowdown in demand. Current prices of most staple varieties range from 56 to 63 cents/lb, about 18 to 26 percent lower than August

prices. Prices are expected to slide further as market arrivals gain pace in December/January.

Fig 4: Shankar -6 Cotton Prices



Source: Cotton Association of India (Formerly East India Cotton Association)-Spot Prices

Market sources report that the current cotton prices have declined to a level at which traders can not buy seed cotton at the MSP or above in order to process and sell cotton at market prices without incurring losses¹. Most of the mills are buying hand-to-mouth due to the demand recession, both domestic and international. Despite declines in the value of India rupee vis-à-vis U.S. dollars, Indian cotton is uncompetitive in the international market due to weak international cotton prices. Industry sources expect cotton prices to decline further as the market arrivals peak in December and January.

MSP Procurement Mounts

With the inflated MSP unrelated to local cotton prices, government agencies like CCI and state marketing federation are currently buying most of the seed cotton arrivals under the MSP operations. MSP operations in MY 2007/08 were minimal as market prices were higher than the MSP in most purchase centers. The CCI's procurement under the MSP is estimated at 1.27 million bales of the total market arrivals of 3.7 million bales of cotton till November 21, 2008². Initially farmers sold some cotton to the private trade at below MSP to meet their immediate cash needs. Now, most of the cotton arrivals are being offloaded by CCI under the MSP operation. Currently, nearly 80 percent of the daily market arrivals, estimated at 148-150,000 bales per day, are going to the CCI stocks.

The government sources claim that CCI and other state marketing federation will be able to procure 7.8 to 9.4 million bales under the MSP in the current season. The current arrival

¹ Market sources estimate that if they buy Shankar-6 seed cotton at Rs. 28,500 per ton, they will be incurring a loss of about 15-18 percent at current cotton and cottonseed prices.

² Please refer Cotton Corporation of India website http://www.cotcorp.gov.in/current_cotton.asp for latest state wise market arrivals estimate in 170 kg Indian bales.

trends indicate that CCI will reach its limits in terms of finance and logistics (purchase, storage and ginning/pressing of seed cotton, and storage of cotton bales), by January, 2009 when the season is not even halfway through.

Given that the next general elections are due in 2009, the government and CCI will be under tremendous pressure to procure cotton at the MSP. While the ginners, traders and local mills have approached the government to lower the MSP, the government is highly unlikely to review the MSP due to domestic political compulsions³. Industry sources report that the government is examining a proposal for extending a credit guarantee of Rs. 150 billion (\$3.13 billion) to help raise funds for CCI to procure seed cotton at MSP levels. However, besides huge carrying costs incurred in procurement and processing of seed cotton, CCI will have to eventually find a market for the cotton. Given the expected future international cotton prices, CCI will have to sell this cotton in both the domestic and international market at considerable cost to the government.

Consumption Lowered on Depressed Demand

Post's MY 2008/09 consumption estimate has been revised lower to 17.5 million bales due to poor demand, both domestic and export, for textile products. Due to the global slowdown, industry sources report that most of the mills are scaling down consumption due weak demand for textile products, both globally and domestically. Based on the latest official monthly consumption estimates (see table 3), MY 2007/08 consumption is estimated at 18.4 million bales.

Exports Prospects Weaken on Weak International Prices

Post has revised MY 2008/09 exports lower to 5.1 million bales due to weak international cotton prices.

Industry sources report that currently Indian cotton is uncompetitive in the international market as government's high MSP fixation has artificially supported local cotton prices. Currently, export registration for the new crop is estimated just around 80,000 bales to 120,000 bales by mid-November, whereas nearly 1.6-1.8 million bales had been already exported during the same period last year. The Indian cotton prices are currently 12-15 percent higher than the international quotation for similar varieties. However, market sources expect that the local cotton prices could come down after the CCI starts liquidating its MSP cotton in the market. Therefore, there may be a recovery in exports during the later half of the MY 2008/09. But the shipments of the MY 2008/09 crop are expected to continue through the next marketing season.

³ Historically, the government has never lowered the MSP after official announcement, and is unlikely to do so due to the upcoming elections.

SECTION II – STATISTICAL TABLES

Table 2: Area, Production & Yield of Cotton in Major States

(Area in 000 hectares, Production in 000 bales of 480 lb., Yield in Kg/Hectare)

		Final	Final	Final	Final	Revised	Forecast Rev
STATE		2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Maharashtra	Area	2766	2840	2889	3107	3191	3133
	Production	2420	4060	2811	3904	4841	4841
	Yield	191	311	212	274	330	336
Gujarat	Area	1647	1906	2077	2390	2516	2417
	Production	3904	5700	6949	8042	8745	7964
	Yield	516	651	728	733	757	717
Madhya Pradesh	Area	591	576	600	639	662	643
	Production	1534	1249	1405	1484	1640	1405
	Yield	565	472	510	505	539	476
Punjab	Area	452	509	557	607	641	560
	Production	808	1288	1562	1874	1718	1562
	Yield	389	551	610	672	583	607
Haryana	Area	526	621	583	530	483	418
	Production	898	1210	1015	1171	1249	1171
	Yield	372	424	379	481	563	610
Rajasthan	Area	344	438	472	350	368	217
	Production	714	859	859	703	703	586
	Yield	452	427	396	437	416	588
Andhra Pradesh	Area	837	1178	1037	972	1096	1312
	Production	2139	2538	2499	2811	3631	4294
	Yield	557	469	525	630	721	713
Karnataka	Area	313	521	450	378	388	425
	Production	328	625	508	468	625	625
	Yield	228	261	246	270	351	320
Tamil Nadu	Area	103	129	136	100	130	125
	Production	293	429	429	390	351	429
	Yield	619	725	688	850	588	748
Others	Area	51	68	72	71	80	90
	Production	78	78	78	78	156	156
	Yield	333	250	236	239	425	378
Loose	Production	859	937	937	937	937	937
All-India	Area	7630	8786	8873	9144	9555	9340
	Production	13976	18973	19051	21862	24595	23970
	Yield	399	470	467	521	560	559

Table 3: Cotton Consumption (Mills & Small Spinning Sectors) by Months
(Million US Bales)

Month\Year	2004/05	2005/06	2006/07	2007/08
Aug	1.096	1.350	1.402	1.448
Sept	1.068	1.186	1.400	1.408
Oct	1.109	1.206	1.353	1.430
Nov	1.071	1.178	1.391	1.323
Dec	1.186	1.277	1.444	1.473
Jan	1.129	1.281	1.423	1.448
Feb	1.095	1.190	1.336	1.416
Mar	1.184	1.342	1.436	1.441
Apr	1.170	1.278	1.410	1.404
May	1.206	1.312	1.397	1.479
Jun	1.192	1.309	1.394	1.451
Jul	1.218	1.361	1.438	1.435
TOTAL	13.726	15.268	16.823	17.155

Source: The Textile Commissioner's Office, GOI.

Table 4: Month-end Prices of Popular Varieties
(Prices in Rupees per metric tons)

	ICS 101	ICS 202	ICS 105 28mm	ICS 105 29mm	ICS 106 33mm	ICS 107
Year	Bengal Deshi	SG J-34	H-4	Shankar-6	MCU-5	DCH-32
	(below 22 mm)	(25 mm)	(28 mm)	(29 mm)	(33 mm)	(35 mm)
2007/08						
Aug	43870	53150	55400	57360	63270	89980
Sept	43870	52020	56520	58490	63270	89980
Oct	42740	50050	53990	56240	63270	80140
Nov	47240	51740	52430	55120	58490	80140
Dec	47800	52870	54270	56520	59900	80140
Jan	47800	54550	56520	59050	61300	82670
Feb	47240	56800	59050	62140	63550	87170
Mar	53430	56800	59900	62140	68050	87170
Apr	54550	57930	61860	63550	68890	87170
May	65800	68610	66080	68890	73390	89980
June	69170	77610	78450	78740	81550	92800
July	70300	77050	78740	79580	84640	93640
2008/09						
Aug	75360	74520	79020	80140	82960	91390
Sept	70020	68050	77330	77890	81550	89980
Oct	74520	60740	63830	64680	69740	88580
25-Nov	71140	55400	60460	61300	68330	84360

Source: Cotton Association of India (Formerly East India Cotton Association).