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Cotton and Products Annual

Cash Subsidies Removed, Farmers to Contract their Crop before Cultivation

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Report Highlights:

The Ministry of Agriculture and Land Reclamation announced it would not directly provide cash subsidies for MY2015/16, after offering such subsidies to farmers for the first time in MY2014/15. Now, with a revised policy, the government requires farmers to have sales contracts in place in order to receive seed and fertilizer subsidies. Due to deteriorating seed quality, the government will be the only producer and supplier of cottonseed, in an effort to improve cotton quality. The changes in policy will alter production; MY2015/2016 cotton production is expected to drop by 40 percent to 315,000 bales. Lint consumption is to remain stable at 650,000 bales, prompting an increase in imports by 30 percent to a record 450,000 bales, while exports are expected to drop by 13 percent.

Commodities:
Cotton

Production:

Post forecasts total lint cotton production to drop by 40 percent to 315,000 bales for the upcoming MY2015/2016 crop from 525,000 bales in the current marketing season. The drop in production is in direct proportion to a decrease in total area harvested of 40 percent to 93,000 hectares (ha). Total area harvested in MY2014/2015 is expected at 155,000 ha. The government of Egypt is expecting cotton area planted to drop in the coming 3-4 years; consequently, the Ministry of Agriculture and Land Reclamation (MALR) announced that the targeted area for cotton in 2015/2016 is 105,000 ha.

The projected reduction in total area and production is attributed to government's new policy for cotton cultivation and marketing. It has decided to stop cash subsidies to farmers and spinners. Under the new policy, in order to qualify for subsidized fertilizer and seeds, the government requires farmers to have contracts with third parties, urging spinning and weaving companies to sign the contracts with farmers based on their needs at government fixed prices announced in early February. The price for the extra-long staple varieties planted in the Delta region is set at LE1300/qintar or $1,086/MT and for the medium-short staple varieties planted in Upper Egypt, the price is set at LE1150/qintar or $960/MT.

In terms of consumption of the local crop, spinners, weavers, and traders have been hesitant to sign contracts stating that it would add undue risk to their operations as international prices are very attractive, let alone the uncertainty of pricing in late 2015 and on into 2016. The government's written contract stipulates that if international prices during the harvest and delivery time are lower than the contracted price, traders need to fulfil their commitments and pay farmers the contracted price.

The Head of the Farmers' Union, Mohamed Farag, said to media outlets that up to March 5, 2015, no single farmer had contracted his crop as spinners, weavers, and traders are reluctant to sign contracts under the stipulated conditions. The government said that farmers have to contract their harvest by the end of March 2015. To date, only state owned mills working under the Holding Company for Spinning and Weaving (HCSW) have entered into contracts with farmers. This came after government's instruction to HCSW to contract and buys the best finest quality cotton to use its seeds for next season's planting.

Nonetheless, the government is moving ahead with its policy, stating that removing cotton subsidies will benefit farmers, by coordinating favorable contracts between buyers and farmers aimed at eliminating price volatility and ensuring that farmers receive a profit margin. Former Minister of Agriculture and Land Reclamation, Dr. Adel Al-Beltagy, who approved this policy before being removed from office in March 2015, stated that cultivating Egyptian cotton, especially extra-long staple cotton, is a costly endeavor and that international and local markets are no longer interested in its purchase. He also attributed the decline in Egyptian cotton's worldwide consumption to the development of the short/medium staple cotton industry, which is cheaper than Egyptian cotton.

Under the new policy, the government will take sole ownership of cotton seed production and distribution, in an effort to reverse the crop's deterioration that has been ongoing for the last ten years due to the mixing of seed varieties. Extra-long staple cotton varieties like Giza 88 and 86 have been mixed with medium staple varieties like Giza 90. This has resulted from lax or inexistent regulatory

oversight over private seed operators, as traders seek additional profits by intentionally mixing extra-long staple varieties with medium and short staple varieties and then selling the seeds as long-staple varieties. It's also a result of the ginning process as separating huge amounts of seed by lots is very difficult, thus occasioning the mixing of seed from different lots of cotton.

The results are noticeable. The length and strength of the extra-long staple Giza 88 has deteriorated significantly. In MY2011/12, the upper half mean length was 35.2 mm dropping to 33.9 mm by MY2014/15. Its uniformity index dropped from 86.9 in MY2011/12 to 85.2 by MY2014/15. Giza 88's strength deteriorated from 44.4 g/tex in MY2011/12 to 43.1 g/tex in MY2014/15. The length and strength for other varieties including Giza 86 also declined during the last couple of years see table (1).

Table (1) Physical Fiber Properties of Egyptian Cotton Varieties Measured by HVI &Micromat

		Length		Strength	
		Upper Half Mean mm	Uniformity Index	Strength g/tex	Elongation %
Giza 87	2011/2012	36.1	88.5	44.3	4.7
	2012/2013	34.6	86.1	42.3	5.0
	2014/2015	34.7	87.5	41.9	5.0
Giza 88	2011/2012	35.2	86.9	44.4	4.9
	2012/2013	34.3	85.2	42.5	4.9
	2014/2015	33.9	85.2	43.1	5.2
Giza 92	2011/2012	33.5	87.6	46.0	5.4
	2012/2013	33.3	86.6	45.0	5.4
	2014/2015	32.4	86.7	46.7	5.6
Giza 86	2011/2012	32.6	86.8	44.1	5.8
	2012/2013	32.6	86.1	43.4	5.8
	2014/2015	31.0	85.3	41.1	6.2
Giza 80	2011/2012	29.6	83.9	35.2	7.5
	2012/2013	29.3	82.5	34.8	7.4
	2014/2015	29.4	84.3	35.3	7.1
Giza 90	2011/2012	28.4	83.3	33.8	7.8
	2012/2013	28.5	82.6	34.2	7.6
	2014/2015	28.1	83.2	34.3	7.8

Source: CATGO

Although a law prohibits transporting seed cotton between governorates without a permit from the Ministry of Agriculture and Land Reclamation to avoid mixing, its enforcement has faced difficulties mainly after the 2011 revolution and the absence of regulatory control.

MY2014/15 Subsidy Regime

The value of subsidies allocated for the cotton sector in MY2014/2015 was LE1.025 billion ($134 million) for spinners, exporters, seeds, fertilizers and farmers. Out of this LE1.025 million, about LE350 million ($46 million) were utilized to subsidize the spinning mills in the public and private sectors and

exporters, while LE150 million ($20 million) were utilized to subsidize seeds and fertilizers. Spinners received a subsidy of LE350/qintar ($46/qintar) or LE72/bale ($9.5/bale) of Egyptian cotton purchased during the 2014/2015 marketing season that ends on August 31, 2015. Similarly, exporters also got a subsidy of LE200/qintar ($26/qintar) or LE41/bale ($5/bale) for the cotton exported by them.

For the crop harvested in 2014, the government, for the first time ever, provided cash subsidies to cotton farmers. In October 2014, President Abdul Fatah Al-Sissi issued a presidential decree to subsidize cotton farmers for the MY2014/15 season by LE1400/feddan ($184/feddan) or LE588/ha ($77/ha). According to Ministry of Agriculture and Land Reclamation (MALR), the total amount allocated for farmers was LE425 million ($56 million) in addition to LE100 million or $13 million reserved from subsidies from the previous season.

Under the regime, it was assumed that the government's subsidizing of spinners would encourage them to buy local cotton at higher prices – compared to international prices– and by this way farmers would continue growing cotton. Government used to pay the spinners the price difference between the prices of local cotton and prices prevailing in the international market. The prices of local cotton were determined by a committee composed of government officials, farmers and traders. The committee set the price that was equal to the total production cost of each feddan and added a percentage as profit to the farmer.

In reality, the subsidies were not efficient in improving cotton quality or in increasing the sale of Egyptian cotton to the local industry. The government provided cotton subsidies to encourage farmers to grow more cotton, which they did at the expense of quality. The result was a higher supply with less demand from local and international markets. The industry was reluctant to pay high prices for the low quality cotton, but due to the government's import policy, the government practically forced the domestic industry to pick-up the tab. In return, prices of local cotton with lower quality were much higher than higher quality imported cotton, leading to an unsustainable subsidy regime.

Cotton Varieties Produced:

Egypt produces three different types of cotton: 1) Extra-long staple (ELS); 2) Long staple (LS), and 3) Short and medium staple cotton. Extra-long staple cotton consists of five main varieties: Giza 45, Giza 70, Giza 87, Giza 88, and Giza 92; however, the main variety among the extra-long staple varieties is Giza 88. This variety accounts for 20 percent of Egypt's total production and is grown in the northern part of the country.

Of the long staple cotton varieties, Giza 86 is the most widely grown, accounting for 70 percent of Egypt's total cotton production. Long staple cotton is grown in the Nile Delta area. The third variety grown in Egypt is short and medium staple (Giza 80 and Giza 90) cotton which accounts for about 10 percent of total cotton production, and is grown in Upper Egypt) (See Figure 1).

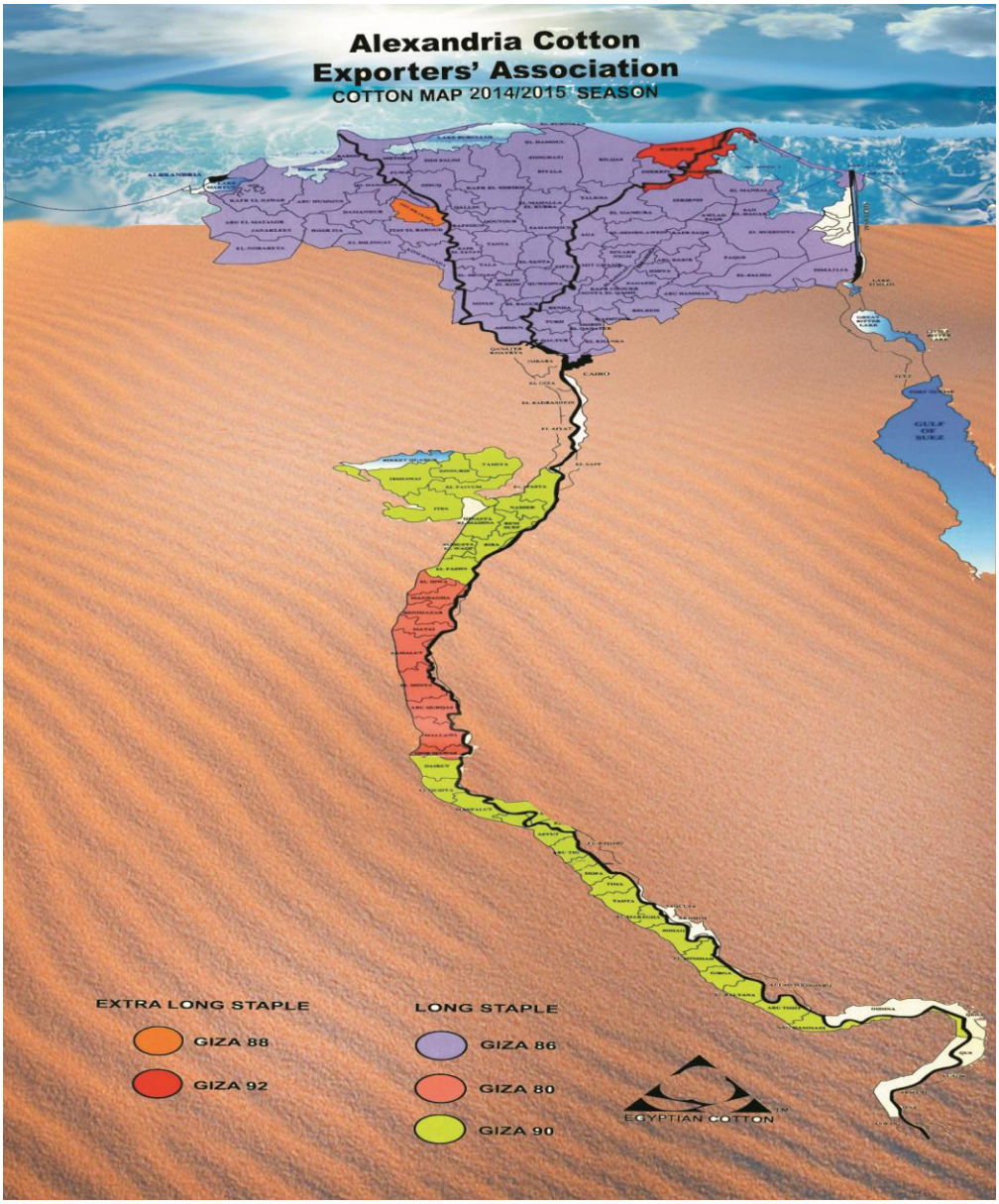


Figure (1) Cotton Map 2014/2015 season Source: ALCOTEXA

Consumption:

MY2015/16 total lint cotton consumption is forecast to remain unchanged from MY2014/15 at 650,000 bales. Local spinners will absorb about 70 percent of their cotton needs from imports and the remaining 30 percent from local cotton production.

Local spinning mills always find it cheaper to import their cotton needs from international suppliers instead of buying domestic cotton. Some industry sources also point out that besides prices; local spinning mills are equipped with machines that only use medium and short staple cotton, which make-up the majority of the factories in Egypt. Consequently, the Egyptian textile industry needs yarn produced from short and medium stable cotton to produce most of its garments such as denim, T-shirts, jeans, and others. The finer Egyptian cotton is used for bed sheets and more expensive clothing.

The lack of security and political instability in Syria has resulted in many Syrian businessmen moving to Egypt where they have re-established business on Egyptian soil. Post met with a Syrian businessman who moved and started a new spinning and textile operations. He reported that two other Syrian businessmen in this field have moved their operations to Egypt and others are planning to as well.

Prices:

As in years past, in early 2015, the government announced indicative target prices for the MY2015/16 crop with the intent that farmers and buyers would sign contracts based on these prices. The price for the extra-long staple varieties is set at LE1300/qintar ($171) or $1,086/MT and for the short/medium staple varieties the price is set at LE1150/qintar ($151) or $960/MT.

For the finest and highest quality cotton coming from about 50,000 feddans in the delta, from which seeds will be used for the next season, the government has instructed the Holding Company for Spinning and Weaving (HCSW) to contract and buy this cotton in order to protect the seeds. Prices paid for this cotton by HCSW are the LE1400/qintar ($184/qintar) or $1,169/MT for the extra-long staple varieties and LE1200/qintar ($171) or $1,086/MT for the short/medium varieties planted in the Upper Egypt.

In MY2014/15, prices ranged between LE800-1000/qintar ($105-131/qintar) or $668-835/MT for the extra-long staple varieties based on the quality and the grade of the cotton. Traders indicated that the prices offered during the season were lower compared to other seasons due to the deteriorating quality of the varieties. Some traders confirmed that there was around 10-30 percent mix between varieties.

Marketing:

On March 4, 2015, the Ministry of Agriculture and Land Reclamation, based on Presidential Decree 14/2015, established the Contract Farming Center. The center will provide services for producers and buyers who have signed contracts, which include contract registration, market information, sales leads, and a dispute settlement mechanism.

Trade:

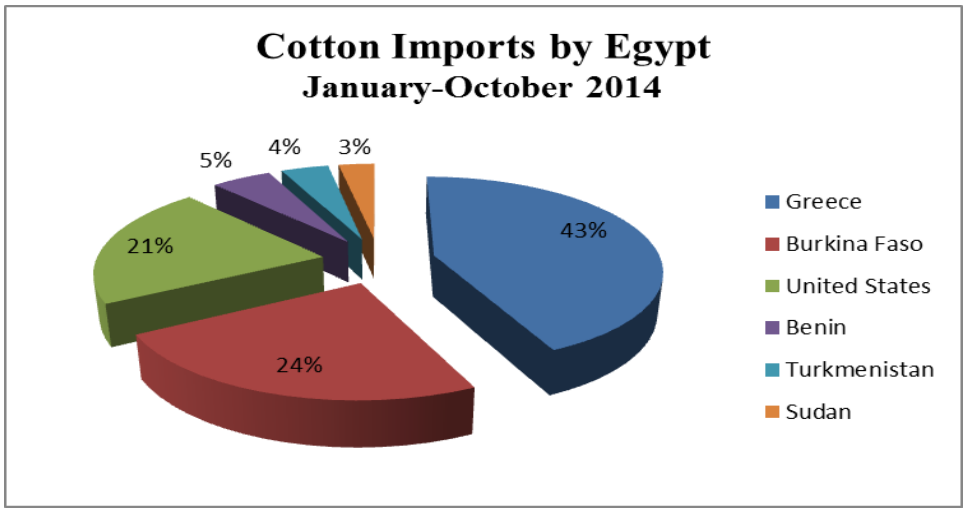
Imports

MY2015/16 cotton imports are forecast to increase by 30 percent to a record 450,000 bales, up by 100,000 bales from MY2014/15. Post attributes this increase to the drop in local cotton production and the spinning mills increasing reliance on international suppliers to meet their needs. Cotton imports have increased during the last couple of years due to the price differential between local cotton and imported cotton. In addition, local spinning mills find imported cotton is better suited to their production capabilities and market needs.

A local spinner stated to FAS Cairo staff that Egyptian cotton is not suitable to manufacture most of the fabrics produced in Egypt, as the yarns required must come from medium and short staple cotton, rather than using Egyptian extra-long staple cotton. Even U.S. pima cotton is highly competitive in the Egyptian markets against Giza 88 and 86, and local spinners view U.S. pima cotton as an alternative to long-staple Egyptian cotton due to the latter's deteriorating quality.

From January-October 2014, Greece was the leading exporter with 43 percent of Egypt's total cotton imports; Burkina Faso was the second with 24 percent, and the United States was the third with 21 percent of Egypt's total cotton imports. Benin was the fourth with 5 percent of Egypt's total cotton imports. For the same period in 2013, Greece was the leading exporter with 33 percent of Egypt's total cotton imports; The United States was the second with 21 percent; Burkina Faso was third with 16 percent and Benin was the fourth with 13 percent of Egypt's total cotton imports.

While Greece and the United States dominated cotton exports to Egypt, since approving imports from Burkina Faso and Benin three years ago, Egypt cotton imports from these two suppliers are increasing and will continue during the coming years.



Exports

For MY2015/16, post forecasts cotton exports to drop by 13 percent to record low of 130,000 bales, down by 20,000 bales from MY2014/15. Cotton exports in the course of the current MY2014/2015 year are expected to reach 150,000 bales. Post attributes the drop in exports to the decrease in total cotton production, as well as the decreasing demand from international yarn producers for Egyptian extra-long staple cotton, because of deteriorating quality.

India, China, Italy, Turkey, Bangladesh and Pakistan were Egypt's top export destinations in MY2014/2015 and are expected to remain so in MY2015/2016. According to the Alexandria Cotton Export Association (ALCOTEXA), total exports through the beginning of March 2015 were 123,000 bales, and average export prices during the week of February 1-7, 2015 were $1.45/lb. for Giza 92 and $1.11/lb. for Giza 86.

Opportunity for U.S. Cotton, but Quality Concerns must be addressed

In calendar year 2014, total exports of U.S. cotton were at 10,000 MT or around 46,000 bales compared to 14,200 MT or around 65,000 bales in calendar year 2013.

Table (2): U.S. Cotton Exports to Egypt in CY

Year	CY2010	CY2011	CY2012	CY2013	CY2014
Exports	4,223	12,425	7,608	14,285	10,033

Numbers in MT Source: GTIS

Post believes that U.S. cotton has an excellent opportunity in the Egyptian market in the coming 2015/16 marketing year in view of the expected increase in Egypt's total cotton imports. During the month of January 2015, the United States exported around 4,000 MT of cotton compared to only 500 MT in January 2014. Post forecasts Egypt's total imports in MY2015/2016 to reach 450,000 bales or around 100,000 MT. Post expects the U.S. cotton exports could reach 35-40 percent of Egypt's total imports in the coming years if some quality concerns are addressed.

Over the past two years, there have been a few shipments of U.S. cotton that have met with clearance issues or importer dissatisfaction due to seeds and stickiness found by inspectors inside the baled cotton. Of course, other supplying countries have not been immune from periodic clearance problems. Egyptian regulations (Article 51 of the Egyptian Plant Quarantine Rules & Regulations: Ministerial Decree 3007/2001) stipulate that cotton bales must be free from cottonseed or any foreign matters. Containers and vessels should also be free from plant waste, especially cottonseed. Egyptian plant quarantine authorities refused to release the shipment found to contain cottonseed, stipulating that the importer either re-export the shipment to another destination or back to the U.S., or be subject to destruction by local authorities. The importer managed to re-export the shipment, but with significant losses.

In early 2015, a shipment of U.S. pima cotton was received by an Egyptian spinner who discovered during processing that the shipment was rife with "sticky cotton". In spinning mills, sticky cotton can cause serious problems because it contaminates the equipment's opening line, card, drawing, roving, and spinning frames. The contaminants are sugar deposits produced by the cotton plant itself or by feeding insects, the latter being the most common source of stickiness.
Some of the solutions that were provided to the importer to remove the stickiness were to blend sticky cotton with non-sticky cotton. The spinner bought more cotton, from a different supplier, and blended it with the sticky cotton but even slowing down the processing and output rates and cleaning the equipment constantly did not solve the problem.

Given the tight-knit Egyptian cotton industry which is largely located in the city of Alexandria, it is important that U.S. and other suppliers strive to ship clean cotton to buyers in the Egyptian market. With the prospects for bigger cotton export sales to Egypt, there should be every incentive to deliver what the customer wants and can efficiently use.

Policy:

There is no government ban or restriction on cotton imports from the United States or other approved origins. Importers have to apply for an import permit at the MALR's Central Administration for Plant Quarantine (CAPQ) which is valid for one year. Egypt imposes zero import tariffs on raw cotton or cotton lint (HS: 520100) and 5 percent import tariffs on carded or combed cotton (HS: 520300).

Egypt's cotton import regulations stipulate that imported cotton should be free from whole or broken seeds or foreign materials (Article 51 of the Egyptian Plant Quarantine Rules & Regulations: Ministerial Decree number 3007/2001). When a shipment is found to have whole or broken seeds (even if one seed

is found in the baled cotton) it will not be released. The importer can either destroy it under the supervision of CAPQ or re-export it to another destination or to the country of origin. If the importer decides to re-export, he will receive a certificate from CAPQ addressed to the destination stipulating the reason for its rejection.

Egypt also requires that cotton exported into Egypt must be fumigated at the country of origin using *methyl bromide, magtoxin or phostoxin* at the specified concentrations found in the import permit. Fumigating the shipment at country of origin does not exclude it from being fumigated in Egyptian ports if necessary.

The following statement "the cotton is free from boll weevil "A*nthonomus grandis*" must be in the phytosanitary certificate. The government also recommends an optional pre-shipment inspection at origin. If done, two CAPQ inspectors travel and inspect the shipment prior to its departure. Although pre-shipment inspection is optional, some importers prefer to bear the cost and send inspectors to avoid delays at the port of entry.

Value-added cotton

Egypt has a total of 2,526 textile plants. Out of them, there are 26 government-owned and 2,500 private companies. The 26 government-owned companies are affiliated with the Holding Company for Spinning, Weaving and Textile and most of them are working in spinning and weaving with around 65,000 employees producing 35 percent of Egypt's textile production. The 2,500 private companies are mainly small-to-medium operations, mostly involved in garment manufacturing. The private companies employ around 1.135 million workers and account for 65 percent of Egypt's textile production.

Egypt's textile industry faces serious problems and has been in decline the last 30 years. The industry suffers from lack of renovation, high input prices, limited skilled labor, high salaries, and high tax and finance costs. The industry lacks the modernization needed to increase productivity. Most of the 26 government-owned companies are equipped with the same machines since the 1960s (Figure 2). The government has announced plans to renovate the 26 companies, but only one company is currently under renovation.

Figure2: Government's owned factories are equipped with old machines from 1960s

The industry also suffers from the high cost of inputs, as raw cotton represents at least 70 percent of the total cost of the spinning production. For years, the industry was forced by the government to buy local cotton at prices higher than international prices. Although the government paid the industry the difference between the local and international prices, the industry faced difficulties in selling yarn due to waning demand as the world textile industry shifted its demand towards cheaper medium and short staple cotton, relegating Egyptian yarn and cotton to niche markets for which is use is limited to a limited number of textile products.

The government continues to impose various taxes on the industry which adds to the burden on yarn and spinning companies. These include a sales tax of 18 percent, a tax on imported machinery of 10 percent, customs duties on assets ranging from 15-40 percent, the general revenue tax ranging from 8-50 percent, and the commercial and industrial profits tax of 32 percent. Additionally, included in last year's structural reform were reforms to energy subsidies, increasing electricity and fuel costs by 30-40 percent. Industry sources indicate that energy represents around 20 percent of the total production cost. The highest increase was for natural gas which increased by 150 percent, severely affecting those that use this fuel for energy.

Last year, striking workers requested the government intervene with the industry in order to improve their working conditions as well as their salaries. The government responded by highlighting the importance of the textile sector in Egypt and agreed to make some reforms. The government conducted meetings with local and international consultants specialized in the industry to develop a study with an investment plan timetable. It was announced that the study would be completed by early 2015 and the objective is to improve the situation of companies and to deal with the losses that hinder their growth, providing new plans for the industry's development and to address workers' demands to improve working conditions and salaries.

Cotton yarn exports were estimated at 24,000 MT in 2014 compared to 26,000 MT in 2013. Italy, Turkey, Portugal, Spain, Pakistan, Switzerland and France are Egypt's main export destinations for cotton yarn. Cotton fabric exports were estimated at 14,000 MT in 2014 compared to 13,000 MT in 2013. Turkey and Pakistan are Egypt's main export destinations for this product.

Cotton yarn imports were estimated at 48,000 MT in 2014 compared to 40,000 MT In 2013. India, Turkey and China are Egypt's suppliers for cotton yarn and cotton fabrics. Cotton fabric imports were estimated at 27,000 MT in 2014 compared to 25,000 MT in 2013. Egypt imposes 5 to 10 percent import tariffs (depending on the type) on cotton yarns and cotton woven fabrics.

Since July 2012, Egypt has applied gradual definitive safeguard duties (Minister of Industry, Trade and SMEs 589/2012) on imports of cotton yarn and cotton mixed yarns for a three-year period ending December 2014. The duties were LE3.48/kg ($0.46/kg) during the period from July 2012 through December 2012, LE3.13/kg ($0.41/kg) for 2013 and LE2/kg ($0.26/kg) for 2014.

Table (3): Statistical Position of Egyptian Cotton
MY2014/2015

Variety	Beginning stock	Lint produced	Total Supply	Gin Commitments till February 19, 2015	Export Commitments till February 19, 2015	Total Distribution	Remaining in February 19, 2015
Giza 45	34	0	34	0	0	0	34
Giza 70	92	0	92	0	0	0	92
Giza 87	337	0	337	0	0	0	337
Giza 88	14,713	1,886	16,599	0	3,155	3,155	13,444
Giza 92	2,344	11,573	13,917	132	8,237	8,369	5,548
Giza 93	19	76	95	0	8	8	87
Giza 86	4,882	470,274	475,156	11,503	114,691	126,193	348,962
Giza 80	0	446	446	0	0	0	446
Giza 90	6,867	40,807	47,674	10,668	0	10,668	37,006
Under Trial	1,157	0	1,157	0	87	87	1,071
Total	**30,445**	**525,062**	**555,507**	**22,303**	**126,177**	**148,480**	**407,026**

Data in 480 lb. Bales Source: IDC/CATGO

Cotton Egypt	2013/2014		2014/2015		2015/2016		
	Market Year Begin: Aug 2013		Market Year Begin: Aug 2014		Market Year Begin: Aug 2015		
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post	
Area Planted	0	0	0	0	0	0	(1000 HA)
Area Harvested	130	130	155	157	0	93	(1000 HA)
Beginning Stocks	139	139	189	189	0	254	1000 480 lb. Bales
Production	435	435	525	525	0	315	1000 480 lb. Bales
Imports	400	400	350	350	0	450	1000 480 lb. Bales
MY Imports from U.S.	0	0	0	0	0	0	1000 480 lb. Bales
Total Supply	974	974	1,064	1,064	0	1,019	1000 480 lb. Bales
Exports	175	175	175	150	0	130	1000 480 lb. Bales
Use	600	600	650	650	0	650	1000 480 lb. Bales
Loss	10	10	10	10	10	10	1000 480 lb. Bales
Total Dom. Cons.	610	610	660	660	0	660	1000 480 lb. Bales
Ending Stocks	189	189	229	254	0	229	1000 480 lb. Bales
Total Distribution	974	974	1,064	1,064	0	1,019	1000 480 lb. Bales

Note: “New Post” data reflects Post’s assessments and are NOT official USDA data.

Commodities:

Select