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Cotton Update

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Report Highlights:

Cotton production in Peru is expected at 28,000 metric tons (MT) in calendar year (CY) 2009, a nosedive from the 64,383 MT produced in CY2008. Cotton imports into Peru are expected at 48,000 MT in CY2009, almost entirely from the United States. Cotton imports into Peru have shrunk nine percent, compared to the previous year, due to increasing supply of cheap threads and textile products from India and China.

Executive Summary:

Cotton production in Peru is expected at 28,000 metric tons (MT) in calendar year (CY) 2009, a nosedive from the 64,383 MT produced in CY2008 and the average 84,000 MT/year produced between CY2005 and CY2007. Many factors have come together to worsen the already decaying cotton industry in Peru. Farmers' inefficiency and unwillingness to establish associations, the ongoing economic crisis that has reduced textile orders from foreign markets, cotton subsidies in other supplying countries, thread and textile dumping from India and China, and better profit opportunities in other crops such as rice and corn have all contributed to the decline in the Peruvian cotton industry.

General Information:

Production:

Cotton production in Peru is expected at 28,000 metric tons (MT) in calendar year (CY) 2009, a nosedive from the 64,383 MT produced in CY2008 and the average 84,000 MT/year produced between CY2005 and CY2007. Many factors have come together to worsen the already decaying cotton industry in Peru. Farmers' inefficiency and unwillingness to establish associations, the ongoing economic crisis that has reduced textile orders from foreign markets, cotton subsidies in other supplying countries, thread and textile dumping from India and China, and better profit opportunities in other crops such as rice and corn have all contributed to the decline in the Peruvian cotton industry.

While Peru has been a traditional cotton producer, area planted has dropped dramatically in the last decades. Between 1990 and 2000, Peru, on average, planted 99,709 hectares annually, much less than the average of 136,400 hectares planted in the 1980's. Harvested area in CY 2010 is forecast at 35,000 hectares.

Cotton: Production and Harvested Area (Metric Tons, Hectares)

COTTON	2000	2001	2002	2003	2004	2005	2006	2007	2008
Production (fiber)	58,320	51,167	48,605	48,148	72,191	79,737	89,003	82,861	64,383
H. Area	89,263	68,634	71,905	65,269	88,908	93,250	91,787	89,428	70,507

Peru grows two major and two minor varieties of cotton. Of the major varieties, Tanguis, a long staple cotton (LS) grown in the central coast of Peru, is used for yarns. Pima, an extra long staple cotton (ELS), is grown in the northern region (mostly in Piura) and it is used for higher quality textiles. Del Cerro and Aspero (rough) are the minor varieties.

Accounting for about 70 percent of the total cotton grown in Peru, Tanguis is the most common cotton variety produced. However, the long growing season for Tanguis, nine months, is a major disadvantage for producers since it does not allow them a "small crop." In Peru, farmers generally harvest two crops per year (the "big crop" and the "small crop"). Cotton is used for the "big crop" and a type of bean is usually planted for the "small crop." The long growing period for cotton also increases the incidence of pests such as the Pink Boll Weevil. In some cases the cost of pesticides in the Tanguis producing areas accounts for almost 50 percent of the total cost of production.

Tanguis cotton is doomed to disappear in the near future, especially in the northern coast where more efficient ELS cottons such as Hazera (an Israeli hybrid) and IPA-59 are gaining terrain due to the better yields and shorter vegetative cycle. Tanguis on the other hand has poor quality seeds as result of the lack of research for the past thirty years.

After twelve years of research, the Peruvian Cotton Institute (IPA) has developed and is currently marketing a new cotton

variety, IPA-59. This is an ELS white cotton with a vegetative period of six months. IPA-59 is 37 mm long with a micronaire of 4.2 - 4.5 and a resistance of 38 grams per tex. There are 1,300 hectares already planted with this variety. IPA is a private, non-profit organization that brings together most players in the cotton value chain: producers, gins, traders, and the textile industry. IPA's primary responsibility is to increase competitiveness of the cotton industry through research.

Cotton Characteristics by Variety				
	Tanguis	Pima	Del Cerro	Aspero
Growing period (days)	260 - 280	235 - 250	180 - 190	240 - 250
Fiber length (mm)	29.4 - 32.5	33.3 - 36.5	33.3 - 36.5	26.2 - 27.0
Resistance (lbs/sq.inch)	86,000 - 88,000	92,000 - 95,000	92,000 - 95,000	80,000
Micronaire (units)	4.6 - 5.8	3.5 - 4.2	3.6 - 3.8	6.5
Color	white	white/beige	white	white/beige

In addition to the long growing season and pests, Peruvian cotton producers also face other weaknesses such as inefficiencies caused by:

- Extremely small size of the average producing unit—90 percent of producers farm less than five hectares which prevents them from benefiting from economies of scale.
- Low yields—the average yield in CY2009 is expected to be 900 kilograms of fiber per hectare) as the result of inadequate agricultural practices, including replanting harvested seed and a lack of fertilization.
- Insufficient credit access—most producers do not have land titles or viable collateral to guarantee a credit line and commercial banks do not risk lending to them. Producers obtain credit from informal lenders at interest rates as high as 8 – 10 percent per month.

Low prices are another hurdle that affect Peruvian cotton producers. Average farm prices for cotton in CY2009 are expected to fall 20 percent to 1,745 per MT of fiber.

Average Cost of Production per Hectare (Intermediate Technology)	
DIRECT COST	1455.04
1. LABOR	585.51
- Land preparation	49.65
- Planting	33.11
- Cultural practices	124.13
- Harvesting	378.62
2. EQUIPMENT	157.93
3. INPUTS	671.17
- Seeds	82.76
- Water	39.17
- Fertilizers	214.97

- Insecticide	302.96
- Fungicide	2.29
- Others	29.02
4. TRANSPORTATION	40.43
INDIRECT COST	261.9
1. Technical Assistance	72.75
2. Administration	145.5
3. Other	43.65
TOTAL COST	1716.94

Trade:

Cotton imports into Peru are expected at 48,000 MT in CY2009 with almost all of it coming from the United States. The nine percent reduction in imports, compared to the previous year, is mostly due to increasing supply of cheap threads and textile products from India and China.

Thread imports from India jumped from 19,264 MT in CY2007 to 33,243 MT in CY2008, and are expected at 28,000 MT in CY 2009. Fabric (with equal or more than 85 percent cotton content) imports from China are expected to reach 13,800 MT in CY2009, a 30 percent increase compared to CY2007 levels.

Pima production is unstable and varies depending on water availability which dictates whether more profitable crops, such as rice, are planted. The supply of Peruvian Pima is limited and insufficient to satisfy the domestic spinning mills. Harvested area for Pima in CY2009 is estimated at 2,500 hectares a considerable reduction from the 15,000 hectares harvested five years ago.

Trade: Textile Industry

The Peruvian textile industry has grown steadily since it was granted access to the U.S. market in CY2002 under Andean Trade Preference and Drug Eradication Act. Peruvian textile and apparel exports to the world in CY2009 reached \$2 billion. As of October 2009, the U.S. market accounted for 41 percent of Peruvian textile and apparel exports, while the Venezuelan market accounted for 24 percent.

Peru's textile industry has an installed capacity of around 110,000 MT of cotton per year. Textile exports have become one of Peru's top exports. The Peruvian industry's export strategy is to position its products in the higher end market. They are aware that it would be difficult to compete against China in the low price sector so they have turned to high value added products.

Peruvian textile exports to Venezuela have increased significantly in recent years. Textile and apparel exports to Venezuela reached \$641 million in 2008. This increase has been driven by an exchange rate preference (CADIVI) implemented by the Chavez administration. Under this system Venezuelan importers receive U.S. dollars from the Venezuelan government at an exchange rate of 2.15 Bolivares Fuertes per dollar. They then sell their products in the local market at the regular exchange rate, about 5.3 Bolivares Fuertes per dollar. Needless to say, this is an extremely profitable business for the "eligible" importers. However, due to the constant differences between the Peruvian and Venezuelan Presidents, the Government of Venezuela has phased out this system for Peruvian textiles; consequently Peruvian exporters have seen their sales to Venezuela drop 50 percent in CY2009.

Policy:

There is no official government policy to support cotton production in Peru. However, under the cotton formalization initiative approved in 2004, producers receive \$2.85 per hundredweight of cotton sent to the gin. The Government of Peru (GOP) has faced some problems and delays in making this payment in CY2009, which has resulted in continuous protest by producers.

One of the most important issues for cotton producers, as for any other farmer, is the availability of credit. After the

bankruptcy of the Agricultural Bank, a state owned bank that lent subsidize credits without collateral, it is very difficult for farmers to obtain credit from formal credit institutions. The ginning industry plays a key role in cotton production; not only do they process raw cotton, but also grant financing for inputs, and, sometimes, technical assistance to producers. Since credit from the formal banking system to the agricultural sector is very limited, processors usually assume the risk of production. This system creates higher production costs, often gins apply to bank loans and turn it over to producers at a much higher interest rate.

Though Peruvian cotton production is far from satisfying the industry's requirements, producers are demanding more protection for local production from the GOP. Recently, INDECOPI (the Peruvian property right protection agency) ruled against a counter vailing duty (CVD) initiative against U.S. cotton filed by the Peruvian Cotton Producers Association. After months of studying the case and consulting with interested parties, INDECOPI concluded that there were no grounds to apply a CVD. Cotton imports are currently assessed an import duty of 9 percent.

Safeguards

There is a strong concern among the industry about Asian, specifically Chinese, textiles coming into the country at “dumped” prices. At this moment, there is reportedly a serious damage caused to the industry from Chinese products imported mostly by the two largest department store chains and Indian threats.

Reportedly, INDECOPI ruled in favor of implementing anti dumping duties (ADD) against Indian threats but the Executive did not favor this initiative. Apparently there was concern among the Cabinet the ADD would trigger protest in “Gamarra,” Peru’s textile cluster which comprises several thousand small manufacturers.