Required Report - public distribution

Date: 3/28/2013

GAIN Report Number: BR0909

Brazil

Cotton and Products Annual

2013-14 Cotton Production Forecast at 6.5 million bales

Approved By:
Robert Hoff, Agricultural Counselor

Prepared By:
Jeff Zimmerman, Agricultural Attaché

Report Highlights:
Brazil’s 2012/13 cotton production is estimated at 5.5 million bales on a planted area of 900,000 hectares, representing decreases of 27 percent in production and 32 percent in area compared to last year. Because of reduced yields due to pests and dry spells in the second ranked producing state of Bahia, Post reduced the national production estimate for 2012/13. Brazil is estimated to export 3.9 million bales of cotton in 2012/13. Post estimates 2012/13 cotton imports at 345,000 bales, predicated on the approval of a sector proposal for temporary removal of the import duty on an estimated 300,000 bales for contracts through the end of May, in order to supply industry demand. Under this presumed scenario, imports of U.S. origin cotton are estimated to reach 205,000 bales in 2012/13. Post forecasts 2013/14 production to increase slightly to 6.5 million bales based on improved yields on an increased planted area of 1,000,000 hectares. Post forecasts 2013/14 exports to decrease 55 percent to 1.85 million bales.

Brazil's 2012/13 Cotton Production Estimated at 5.5 million bales

Brazil's 2012/13 cotton production is estimated at 5.5 million bales on an area of 900,000 hectares. Post's estimate is in line with industry sources and incorporates reduced yields in the last month, due to pests and dry spells, in the second ranked producing state of Bahia**.** In its March survey, the Brazilian Ministry of Agriculture's Food Supply Company (CONAB) estimated 2012/13 cotton production at 6.4 million bales and planted area at 967,000 hectares. The 2012/13 estimated production decrease of 27 percent when compared to the last two years will ensure adequate availability of cotton pickers and ginning capacities. In the past two seasons, deficiencies in harvest equipment, ginning capacity and export capacity adversely affected the quality of cotton. Both the 2010/11 and the 2011/12 crop were still being ginned well into the first quarter of the following year's rainy season, further reducing the post-harvest quality of some cotton. As a result, Brazil's long struggle to supply a consistent quality product to the international market was challenged even further these past two export seasons as they entered into new markets with record exports. Industry sources have indicated that inconsistent quality has affected Brazil's ability to retain new clients.

The top producing state of Mato Grosso, with over 50 percent of national production, sharply reduced planted area by 37 percent to 452,098 hectares, according to the state's Institute of Agricultural Economics (IMEA). Mato Grosso planted a 30:70 ratio of first-to-second crop cotton in the 2012/13 season. Mato Grosso plants cotton during two different periods with three predominate row spacing approaches. First crop cotton accounts for 142,500 hectares and was planted in early December in 90 centimeter (cm) spaced rows. The second crop cotton is largely planted in either 90 or 76 cm spaced rows by January 25 or narrow-row spacings of 45 or 50 cm by February 20 and accounted for 272,983 and 36,584 hectares, respectively. The second crop plantings occur directly following the harvest of early maturing soybeans. Industry sources in Mato Grosso indicate that 500,000 hectares of planted area is an adequate level to ensure proper utilization of ginning and logistics capacities across the state in relation to other crops. Hence, the ginning season of the smaller 2012/13 crop should return to historic lengths and finish by the end of November. First crop (90 cm spaced) planting in December represents 55 percent of planted area. Second crop narrow-row (45 or 50 cm spaced) cotton has been established as a viable production model in Mato Grosso - expanding from 5,000 hectares in 2008/09 and peaking at 123,000 hectares in 2010/11. The Cotton Producer's Association of Mato Grosso (AMPA) indicates that narrow-row cotton will always maintain a small presence as part of crop rotation schemes accounting for 7.3 percent of planted area in 2012/13. The cotton boll worm "*helicoverpa armigera"* has plagued the 2012/13 crop and reduced yields. It appears that in Mato Grosso growers were able to control this pest more due to more favorable weather conditions than those experienced in the second largest producing state of Bahia.

Bahia is responsible for 30 percent of national cotton production. The 2012/13 crop in Bahia suffered irreversible losses due to dry spells that contributed to the infestation of the cotton bollworm "*helicoverpa armigera."* Developing cotton bolls are being consumed by the pest, as well as developing soybeans in the pod, and significance in yield losses to both crops is still not determined. Effective pesticides against this particular species of corn earworm or cotton bollworm have been readily available outside of Brazil for a while. Producers have been applying various less effective approved pesticides and seen their costs double to US$200 per hectare this season. With over US$1 billion in estimated damages over the last two crop seasons, on March 14, the Ministry of Agriculture, Livestock and Food Supply (MAPA) issued an emergency measure to allow for imports of effective pesticides to bring the problem under control. The soybean crop has already suffered irreversible losses and concern has now shifted to the cotton crop that will be ready to harvest in less than 60 days. Producers in western Bahia are in their second consecutive season of significant crop losses and those financially overextended will be forced to sell some or all assets to mainly more capitalized, larger producers. The adjacent state of Piaui also has experienced dry spells of over 45 days and as a result, will have lower production of cotton and other crops in 2012/13.

Outlook 2013/14: Increased Domestic Demand and Favorable Futures Prices to Slightly Increase Planted Area

Post forecasts 2013/14 cotton area will increase to one million hectares, or an 11 percent increase compared to 2012/13. Production is forecast to increase to 6.5 million bales, representing an 18 percent increase over 2012/13, based on a yield trend of 1.4 mt/ha. China's current minimum price regime set at levels equal to US$1.47/lb coupled with increased domestic demand have buoyed futures prices making cotton a viable crop choice in 2013/14 for large vertically integrated producers. Trade sources indicate that break-even production costs in 2012/13 for large vertically integrated producers are estimated at US$0.50-0.55/lb. The increase in the price of cottonseed, lower costs of an owned gin, access to cheaper financing, and other synergies serve to lower the break-even production cost. By comparison, the break-even production cost for a producer not vertically integrated is estimated to be between US$0.75-0.80/lb for 2012/13.

Brazil continues to be deficit in fertilizer production. Studies show that Brazil's dependence on imports reaches 65, 50, and 90 percent for nitrogen, phosphorus, and potassium, respectively. According to the National Fertilizer Association (ANDA), fertilizer deliveries totaled a record 29.5 mmt in 2012, up over four percent from 2011. Total annual imports of fertilizer in 2012 equaled 19.5 mmt, down nearly two percent from 2011. National production in 2012 equaled 9.7 mmt, down 1 percent from the 9.8 mmt produced in 2011. For 2013/14, fertilizer usage is expected to remain unchanged due to increased variable costs which face producers.

Possessing 20 percent of the planet's fresh water, Brazil has tremendous potential to expand planted area via irrigation projects that make possible second and third crops rotated over a yearly growing season. Currently, around 8.3 percent of all cropland is under irrigation, which represents 4.5 million hectares. Recent historically high crop prices have greatly improved the timeframe for return on investment with the main constraints being water use licenses and capital investment requirements. Large irrigation project investments are increasing cotton planted area and improving yields and quality. More recent supplemental irrigation schemes are bringing vast new areas into second or third crop rotation and improving yields and quality. For instance, post travel to western Bahia found 10,000 continuous hectares of a new supplemental center-pivot irrigation system to be planted next year with early-maturing soybeans followed by cotton. The producer indicated he that expects better quality control of the cotton as he will be able to plant later and shift the opening of mature bolls to after the heavy rainfall period and help avoid boll rot and damage. The rainy season does not normally accommodate two crops per year in this growing region; however there are sufficient ground water resources available for an estimated additional 200,000 hectares of second cropping under varying irrigation schemes.

Biotech Cotton Seed Use Estimated to increase to 60-80 Percent in 2013/14

Sources confirm the biotechnology adoption rate for cotton in Brazil in 2013/14 should reach 60-80 percent at par with most other cotton producing countries. Seed development firms and research institutions are awaiting import licenses for second generation double and triple-stacked trait seed varieties. MAPA is assisting in quickening the approval process for the import of seeds to help combat the cotton bollworm next season. Producers in the 2012/13 were left without adequate seed or chemical technology to combat a specific cotton bollworm that has reduced yields greatly. If the cotton seed imports arrive in time, trade sources estimate that 15-20 percent of the 2013/14 cotton area will be planted with second generation varieties that include two biotech events resistant to insects and one event tolerant to herbicide, such as Bollgard II with RRFlex. Limited seed quantities will not allow for area beyond this percentage to be planted with these varieties next season, and producers will turn to other biotech varieties that are solely resistant to insects, such as, Bollgard II and Widestrike. Single-event genetically-engineered (GE) varieties, such as Bollgard, will be planted even though these do not provide broad protection against regionally specific pests and disease. Under increased pest and weed pressure, producers appear willing to pay for the benefits of second generation double and triple-stacked trait seed varieties. Brazil's National Technical Commission of Biosafety (CTNBio) has approved 12 biotech cotton events for commercial use.

Consumption:

Brazil's domestic consumption for 2012/13 is estimated at 3.95 million bales. 2013/14 domestic consumption is estimated to recover to 4.25 million bales, driven in large part by the hotel sector. Large investments are being made in preparation for Brazil's hosting of the World Cup soccer tournament in 2014 and the Summer Olympics in 2016.

The H5 textile industry concentration ratio for Brazil is estimated at 75 percent of total market share. The drastic oscillation in cotton prices in recent years has resulted in a permanent reduction of at least 15 percent in Brazil's textile industry capacity. Since the beginning of 2013, domestic prices have already increased 36 percent, faster than international prices, and the industry is facing new challenges. Many are still recovering from high and volatile prices in recent years and have little access to financial credit and the federal government does not have financial programs available for the industry. Furthermore, the industry is able to fully pass on the significant input price increases to consumers. Textile production fell by 15 percent in 2011 due high prices and fell an additional 4.5 percent in 2012. In 2013 the textile industry is expected to recovery slightly with an estimate growth of 2-3 percent in output. Smaller textile manufacturers are also operating hand-to-mouth with an estimated 4-6 weeks of stocks-to-use ratio. With the cotton price returning to levels over $1.00/lb, there has been some increased substitution from natural cotton fiber to man-made fibers. Brazil enjoys one the highest cotton usage ratios in world with cotton representing 60 percent of all fiber usage compared to the worldwide average of 35 percent. However, the Brazilian Textile and Apparel Industry Association (ABIT) estimates cotton usage in the apparel sector will decrease from 60 percent to 50 percent in approximately 12 years. The apparel sector is forecast to grow by three percent annually; however, 2.5 percent of the growth will be attributed to cotton. Hence, the share of man-made fibers will increase from 40 to 50 percent in around 12 years.

The textile industry reports that imports of ready-made clothing remain equivalent to over 100 tmt of cotton fiber in 2012, and continue to impact domestic production. It is shown that 60 tmt, or more than half of this increase, is derived from imports via tourism (70 percent from the United States) with each Brazilian tourist estimated to return to Brazil with clothing purchases equivalent to 10kg of cotton.

Prices:

Since the beginning of 2013, domestic prices have increased faster than international prices in the inter harvest period. This has been driven by increased domestic demand coupled with export demand. The University of Sao Paulo's Superior Agricultural School Research Center (CEPEA/ESALQ) shows current domestic prices of over R$2.15/lb (US$1.07/lb), representing 41-4 type, delivered to Sao Paulo, have not reached this level since June of 2011, in nominal and real terms. These high current prices still pale in comparison to the record historic international highs of over US$2.30/lb reached in March 2011. International prices have settled at under US$0.90/lb, still very profitable given production costs estimated at between US$0.50-$0.80/lb this season depending on the producer's level of vertical integration. Domestic prices have returned to levels around US$1.00/lb in the near term. Post expects domestic prices to continue around this level given the upcoming short-crop coupled with increasing domestic demand.

The last time the minimum price for cotton was changed was before the 2003/2004 crop, when it was raised from R$33.90/15kg (US$0.57/lb) to R$44.60/15kg (US$0.75/lb). Brief price spikes above the minimum price occurred in early 2006, 2007, and 2008. A price increase of nearly 8 percent in 2007 prompted the government to sell 20,400 bales in stock and resulted in a 5.6 percent reduction in the domestic price. The government's primary means of intervening in the cotton market during this time was by supporting the marketing of over 1 mmt of cotton through the PEPRO program. (See POLICY section below.)

Cotton Prices

Domestic Prices* in cents of R$ per lb

Year	2011	2012	% Change
Jan	339.14	171.06	-98
Feb	385.24	170.23	-126
Mar	397.56	161.17	-147
Apr	357.2	160.47	-123
May	227.94	160.02	-42
Jun	218.44	151.06	-45
Jul	171.07	157.56	-9
Aug	181.17	161.91	-12

Sep	179.42	165.19	-9
Oct	174.63	155.21	-13
Nov	171.42	155.49	-10
Dec	165.81	158.41	-5

Source: CEPEA
* Cotton grade 41-4, staple 30/32mm, 8-day term payment, no ICMS included (interstate commerce tax), includes freight for point of delivery Sao Paulo city.

2012/13 Minimum Price for Cotton

Region	Unit	Price (R$/unit)	Price (R$/lb)	Price (US$/lb)
All	15 kg	44.60	1.3487	0.67

Source: MAPA/SPA/DEAGRO
Exchange rate: US$1.00 = R$ 2.00

Trade:

Post now estimates 2012/13 cotton exports to reach a 4.1 million bales, the second highest on record. This will make Brazil fourth in cotton export rankings worldwide following the United States, India and Australia. The Brazilian Real vis-a-via the U.S. dollar has depreciated over the last month reaching R$2.00 to US$1.00. The monthly export record was set in October, 2012 at 862,360 bales well exceeding the previous monthly export capacities considered at 460,000 bales. The limits on export capacity are due to limited availability of adequate port capacity, storage and handling for cotton that is restricted mainly to Santos, Sao Paulo and Paranagua, Parana. However, new ports are starting and/or preparing to export cotton including, Itajai, Santa Catarina; Suape, Pernambuco; Pecem, Ceara and Salvador, Bahia.

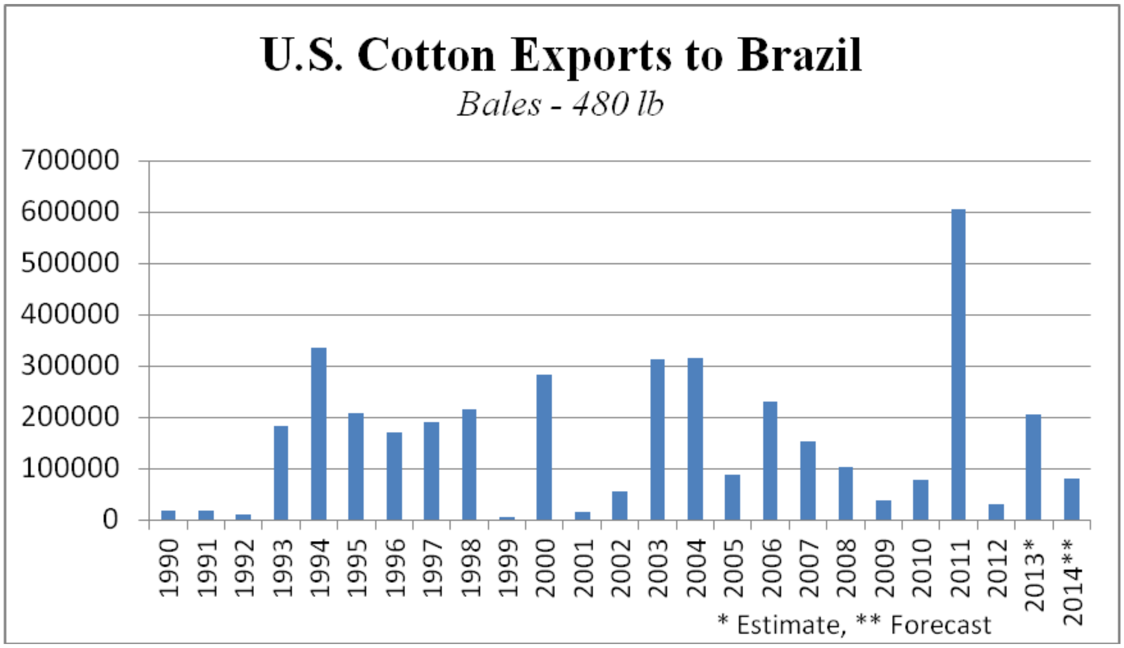
ABIT is assisting sector efforts to reverse Brazil’s trade deficit across clothing and textiles that reached US$4.5 billion in 2012. Brazil’s 2012 export revenue from clothing sales was valued at US$1 billion. The industry is promoting Brazilian clothing brands overseas and has a goal to reach US$6 billion in exports in ten years. The combined textile and clothing sector is Brazil’s second largest in value terms for manufactured goods, following the beverage sector, and employs 1.7 million workers.
Post forecasts Brazil’s 2013/14 cotton exports at 1.85 million bales based on a short-crop harvest of 2012/13. There is an interest by the Brazil to maintain a strong international market presence after gains made over the past two years, and depending on international prices, export forecasts may increase. Under this scenario, the domestic industry demands would have to be met by increased import forecasts, the majority of which would be supplied by U.S. cotton. Brazil still sells over 80 percent of its cotton only after the merchant or buyer has conducted his own visual inspection of the lot samples at the ginneries as opposed to confiding in the HVI (high volume inspection) classification data and visual classification done by the laboratory technician. Progressive producers and industry players have begun to meet the sustainability standards of the Better Cotton Initiative (BCI) which should improve marketability of Brazilian cotton and products.

Trade sources indicate committed forward sales for export of the current 2012/13 crop to be harvested are between 300,000-400,000 mt (1.37 – 1.84 million bales) signifying the potential for more import demand in 2013/14. Significant imports in 2013/14 would be predicated on government intervention to offer addition unknown import volumes temporary removal of the import duty. In addition, international demand in Asia for yarn imports has reduced Brazil’s imports of yarn to an estimated monthly average of 2,000 mt in 2012/13, down 60 percent from and estimated 5,000 mt per month import average in 2010/11. This reduction in available yarn will support higher cotton lint imports in 2013/14.

Post estimates 2012/13 cotton imports to reach 345,000 bales, predicated on a temporary lowering or removal of the import duty on an estimated 300,000 bales (65,000 mt) for contracts through the end of May, in order to supply industry demand. Under this presumed scenario, imports of U.S. origin cotton are forecast to reach 205,000 bales in 2012/13. The three associations that support and represent the cotton sector – ABIT, Brazilian Cotton Producers Association (APRAPA), Brazil's National Association of Cotton Exporters (ANEA) – are negotiating to reach a consensus on a proposal for lowering the import tariff temporarily which would be submitted to the Brazilian Trade Commission (CAMEX) for consideration. In 2010/11, a similar proposal was approved by CAMEX and resulted in Brazil's importing 703,000 bales, of which a record 605,000 bales originated from the U.S. That government intervention had temporarily reduced the import duty to zero from ten percent (between October 2010 and May 2011) on up to 250,000 mt (1.15 million bales) of cotton imports. Post estimates 2013/14 imports of cotton at 135,000 bales, of which 80,000 bales are estimated to be of U.S. origin.

In June 2010, the United States and Brazil signed a Framework for a Mutually Agreed Solution to the Cotton Dispute in the World Trade Organization (WTO). As part of the Framework Agreement, Brazil did not impose countermeasures authorized by the WTO.

Source: SECEX



Source: U.S. Census Bureau

Trade Tables

Brazil Cotton Exports (1000 480-lb bales)			
Country	2009	2010	2011
	2009/2010	2010/2011	2011/2012
	Market Year Begin: Aug 2009	Market Year Begin: Aug 2010	Market Year Begin: Aug 2011
World	1,990	2,000	4,792
China	190	364	1,612
Indonesia	480	448	655
Korea South	432	379	628
Turkey	91	148	392
Malaysia	34	18	278
Vietnam	44	61	207
Pakistan	196	116	206
Thailand	132	129	201
Taiwan	103	81	172
EU27	24	21	80

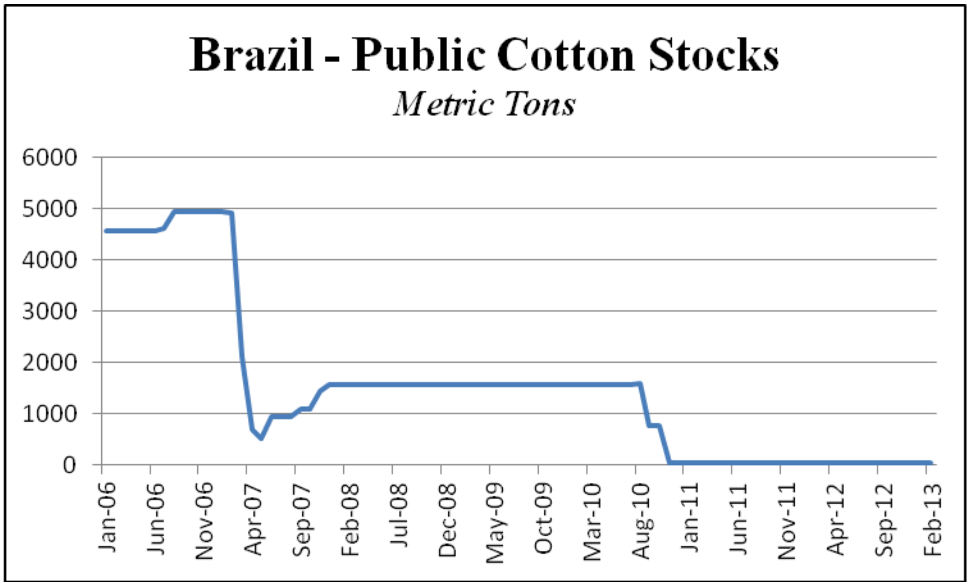
Bangladesh	23	64	79
Japan	53	67	66
Argentina	69	32	37
Ecuador	30	19	35
Morocco	9	11	28
South Africa	0	2	19
Mexico	0	2	16
United States	0	0	9
Others	80	38	72

Source: SECEX

Brazil Cotton Imports (1000 480-lb bales)			
Country	2009	2010	2011
	2009/2010	2010/2011	2011/2012
	Market Year Begin: Aug 2009	Market Year Begin: Aug 2010	Market Year Begin: Aug 2011
World	151	703	29
Argentina	7	66	14
United States	94	605	9
Israel	2	5	3
Egypt	8	12	1
Turkey	0	0	1
Paraguay	40	13	0
Turkmenistan	0	1	0

Source: SECEX

Stocks:



Source: MAPA/CONAB

Government public stocks were nearly all sold in the fourth quarter of 2010 with 170 bales (37 mt) remaining in storage. This intervention by the government had no effect on rising domestic prices.

Policy:

In 2012, the Brazilian Ministry of Agriculture did not make any official government payments to cotton producers. A rebound in domestic prices since the beginning of the year has guaranteed minimum revenue levels for producers and exceeded the minimum trigger cotton price set by the Federal Government.

The quantity of cotton supported by the government from 2005-2012 is provided in the table below, as well as descriptions of the major government support programs. These programs are utilized to support commodity prices and to assist in the flow of cotton from production areas to 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 Agricultural Agreement allows for Brazil to subsidize transportation.

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

Program	2005	2006	2007	2008	2009	2010	2011	2012
Acquisition (AGF)	4.5	0	1.1	0	0	0	0	0
PEP	136.5	1.8	0	0	0	0	0	0
PROP	272.2	0	0	0	0	0	0	0
PEPRO	0	461.5	428.9	1,023.6	792.2	0	0	0
Total	413.2	463.3	730.0	1,023.6	792.2	0	0	0
Production	1,298.7	1,037.8	1,524.0	1,602.2	1,213.7	1,194.1	1,959.8	1,877.3
Participation %	31.8	44.6	47.9	63.9	65.3	0	0	0

Source: Brazilian Ministry of Agriculture/SPA/DEAGRO

Government Programs:

Risk Premium for Acquisition of Agricultural Products Deriving from Private Contracts of Sales Options (PROP): 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 Equalization Premium Paid to the Producer (PEPRO): PEPRO is a premium granted to the farmer or cooperative which sells its products at a public auction. The government pays the difference between the Official Reference Value and the value of the premium (the maximum value paid by the government as a guarantee of the Reference Value).

Premium for Product Outflow Program (PEP): Through this program, the government pays the difference between the prevailing market price and the minimum price of the product. The federal government through MAPA's National Company of Food and Supply (CONAB) conducts public auctions to set a premium for buyers of a given product. These buyers then contact producers interested in selling their production at the current minimum support price. Buyers must transport the product to the destination previously established by the program. The objective of PEP is to move commodities from areas of high product concentration to areas of need, typically in the demographically-sparse parts of the North and Northeastern regions of the country. In PEP, the product is taken from private stocks.

Federal Government Acquisition (AGF): This program 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 Family Agriculture Program and to build strategic stocks.

Production, Supply and Demand Statistics:

Cotton Brazil	2011/2012		2012/2013		2013/2014	
	Market Year Begin: Aug 2011		Market Year Begin: Aug 2012		Market Year Begin: Aug 2013	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Harvested	1,400	1,400	975	900		1,000
Beginning Stocks	7,906	7,919	7,993	7,906		5,701
Production	8,700	8,600	6,300	5,500		6,500
Imports	29	29	50	345		135
MY Imports from U.S.	0	9	0	205		80
Total Supply	16,635	16,548	14,343	13,751		12,336
Exports	4,792	4,792	4,600	4,100		1,850
Use	4,000	4,000	4,100	4,100		4,400
Loss	-150	-150	-150	-150		-150
Total Dom. Cons.	3,850	3,850	3,950	3,950		4,250
Ending Stocks	7,993	7,906	5,793	5,701		6,236
Total Distribution	16,635	16,548	14,343	13,751		12,336
1000 HA, 1000 480 lb. Bales, PERCENT, KG/HA						

Other relevant reports:

BR0824 Cotton and Products Update - November 30, 2012
BR0808 Cotton and Products Annual - 2012