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China - Peoples Republic of

Cotton and Products Update

Importers Seek to Utilize Added Cotton Import Quotas

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Report Highlights:

China's addition of 0.8 MMT of cotton import quotas this year is expected to push imports up to 1.5 million metric tons (MMT) in marketing year (MY) 18/19. With imports from the U.S. constrained by the additional 25 percent tariff applied by China beginning in July 2018, importers will seek alternative cotton supplies from Brazil and Australia. China's cotton production is forecast to remain virtually unchanged in MY18/19 at 6 MMT. Maintained by steady economic growth, cotton use will be stable at 9 MMT in MY18/19. With increased sales from the state reserves, cotton stocks are forecast to fall significantly by the end of MY18/19, down to 6.7 MMT from an estimated 10 MMT at the beginning of MY17/18.

Executive Summary:

China's cotton production is forecast at 6 million metric tons (MMT) in marketing year (MY) 18/19, virtually unchanged from an estimated 5.95 MMT the previous marketing year. The very small production gain reflects increased cotton acreage in Xinjiang Province and a higher average yield compared to the previous year. China's cotton support policy for Xinjiang and the high yield achieved in that province contributed to higher cotton profits in MY17/18 and a moderate acreage expansion in MY18/19. However, cotton acreage declined in the other cotton-producing provinces in MY18/19, due to higher corn profits in 2017 and fewer subsidies for growing cotton. Overall MY18/19 cotton planting area is forecast at 3.35 million hectares (MHa).

Steady economic growth, limited growth of yarn imports, and the recovery of the cotton fiber share (vs. polyester) in yarn production are expected to maintain stable domestic cotton consumption, which is forecast at 9 MMT in MY18/19 compared to the estimated 8.9 MMT in MY17/18. Due to increased sales from the state reserves, cotton stocks are forecast to fall dramatically by the end of MY18/19, down to 6.7 MMT from an estimated 10 MMT at the beginning of MY17/18.

The government's decision to add 0.8 MMT of cotton import quotas (TRQ) in June 2018 is expected to boost cotton imports, which are forecast up to 1.5 MMT in MY18/19 from the estimated 1.25 MMT the previous year. Imports of U.S. cotton are hindered by the additional 25 percent tariff implemented by China in July 2018, which industry estimates will add RMB 4,000 (\$600)/ton to cotton imported from the United States. In the first two months of MY18/19 (August-September), U.S. cotton exports to China were down fifty percent from the same period in MY17/18. While supplies of high-quality cotton from other exporting markets are limited, importers will reportedly seek to increase cotton imports from Brazil and Australia to compensate for lower imports from the United States.

Cotton Production Forecast to Remain Flat in MY18/19

MY18/19 domestic cotton production is forecast at 6 MMT, compared to an estimated 5.95 MMT in MY17/18. The production is based on a higher yield and slight decline in planted area compared to the previous year. The government's continued subsidies to Xinjiang farmers during MY17/18 and an increase in cotton profitability contributed to area expansion in Xinjiang in MY18/19. Chinese information sources continue to vary on forecast cotton area and production, with forecast production ranging from a low of 5.7 MMT to a high of 6.28 MMT.

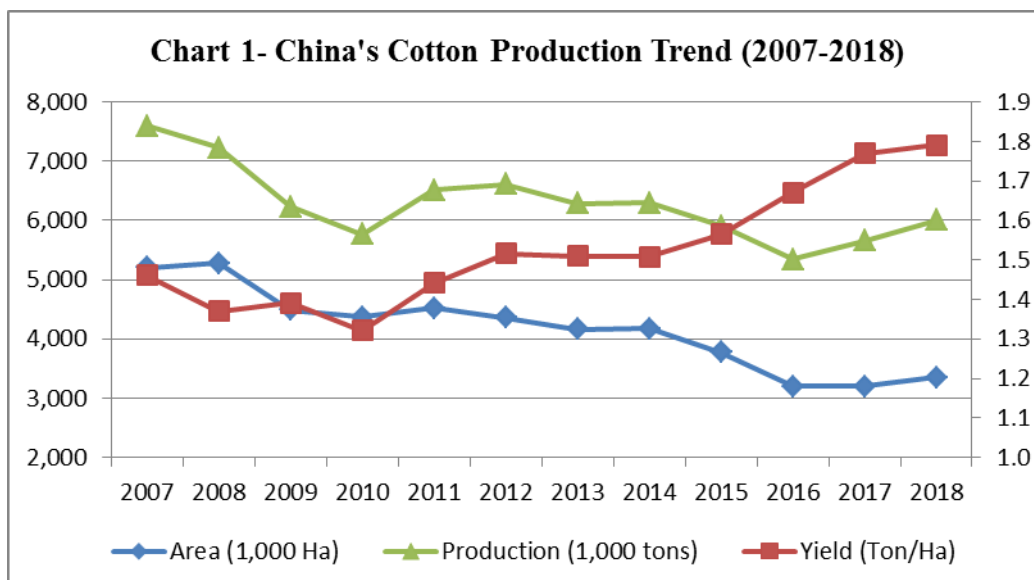
Cotton Area, Yield, and Production

Year	NBS			Forecast MY18/19 Data by Sources				
	MY16/17	MY17/18	Percent Change	CCA	Cncotton.com	CCO	MARA	FAS/Beijing
Area/ 1,000 Ha	3,198	3,195	-0.1				3,367	3,350
Yield/ Ton/Ha	1.671	1.769	+5.9					
Production/ 1,000 Ton	5,343	5,653	+5.8	6,110	6,280	5,700	5,890	6,000

Sources: National Bureau of Statistics (NBS), China Cotton Association (CCA), Cncotton.com, China Cotton Outlook (CCO) (National Cotton Exchange affiliate), Ministry of Agricultural and Rural Affairs (MARA)

China National Bureau of Statistics adjusts 2007-2016 area and production data

In October 2018, the China National Bureau of Statistics (NBS) released adjusted 2007-2016 crop data based on China's 3rd Agricultural Census. Chart 1 below shows the NBS cotton area, yield and production trend from 2007 to 2017.



Source: NBS; Data for 2018 is FAS/Beijing forecast; Left axis: production and area, Right axis: yield

The data shows a production recovery beginning in 2016 that coincides with the government's establishment of significant subsidies for Xinjiang Province cotton farmers. In addition, the average yield exhibits a growing trend, due to Xinjiang's relatively high yield compared to the other cotton regions and the province's increased share of total cotton area. The Ministry of Agriculture and Rural Affairs (MARA) is expected to publish its detailed Agricultural Statistical Report by the end of the year, providing specific data by province.

Planted Area

MY18/19 total planted area is forecast at 3.35 MHa, virtually unchanged from the previous year. The area for Xinjiang Province is forecast up 2.1 percent to 2.47 MHa due to expected high farmer earnings and continued government support. The planted area for all other provinces is forecast to decline to 0.88 MHa in response to stagnant cotton earnings and higher MY17/18 corn prices in regions where farmers can fairly easily substitute corn for cotton.

As previously reported, China's 2017-2019 target price subsidy for Xinjiang Province guarantees basic cotton profits, stimulating continued cotton expansion in MY18/19. The target price is fixed at RMB18,600 (\$2,900)/ton for MY17/18 through MY19/20.

Yield

Average yield is forecast at 1,791 Kg/Ha for MY18/19, up from the estimated 1,774 Kg/Ha for MY17/18. Forecast MY18/19 yield for Xinjiang is 2,065 Kg/Ha, almost unchanged from that in the previous year. The forecast yield for the other cotton-producing areas is 1,023 Kg/Ha, slightly up from the previous year.

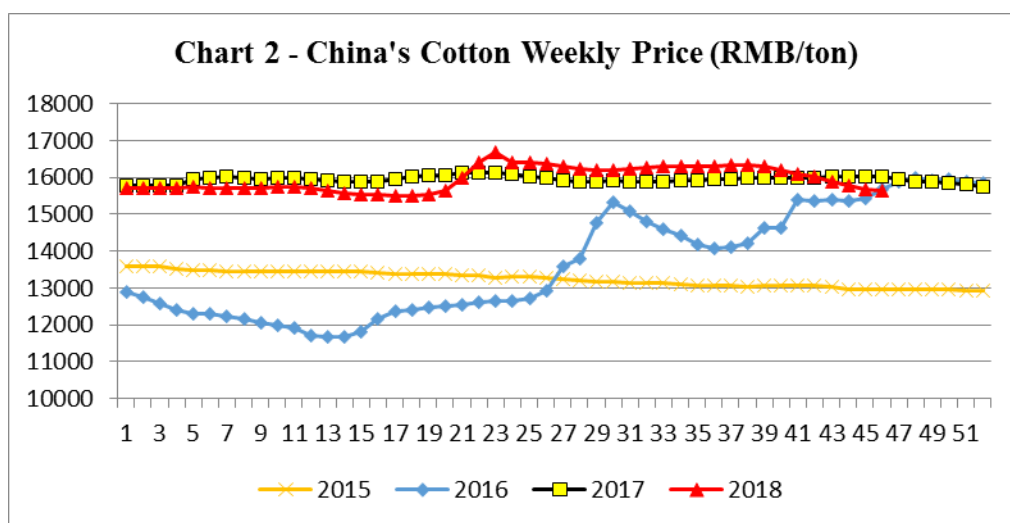
According to CCA, the sowing of the MY18/19 cotton crop went smoothly overall. Beginning in mid-July, the temperature was higher than average in all three cotton-producing regions, which generally facilitated growth. Weather conditions in most areas of Xinjiang Province from September to October 2018 facilitated crop maturation and the harvest. However, low temperatures and snowfall in parts of Xinjiang in late October moderately impacted harvest and sales of seed cotton. As of November 2, Xinjiang's harvest was 88 percent completed, or two percentage points higher than the previous year; seed cotton sales were 82 percent finished, four percentage points higher than the previous year. The cotton harvest is expected to be completed by mid-November in Xinjiang. Based on field surveys by several different organizations, the Xinjiang cotton yield continues to be as high as the previous year.

Forecast yield for all other cotton regions besides Xinjiang averaged 1,023 Kg/Ha, up slightly from the previous year. The weather conditions were favorable in the pre-harvest months, with less rainfall and adequate sunshine facilitating cotton maturation and harvest. As of the end of October, the harvest was 92 percent completed, or 21 percentage points higher than the previous year. In the Yellow River region, the sunny weather in October helped the maturation and harvest of the crop with 97 percent of the harvest completed as of the end of October.

Stocks

Due to increased sales from the state reserves, Chinese cotton stocks are forecast to fall dramatically to 6.7 MMT by the end of MY18/19 from an estimated 10 MMT of cotton at the beginning of MY17/18. As previously reported, the Chinese government has been seeking to reduce its high state cotton reserves since 2014. The government's cotton reserve sales in 2018 began on March 12 and ended on September 30. Out of the 4.3 MMT offered in daily auctions, 2.5 MMT, or 58 percent, were sold. Xinjiang cotton comprised 62 percent of the cotton sold. According to industry sources, the Chinese government deems that the state reserve has fallen to a "reasonable level" at the completion of the 2018 auctions.

The domestic cotton price has exhibited a declining trend since the end of September 2018. Chart 2 below shows China's weekly cotton prices from 2015 to the 46th week of 2018.



Source: China JCI Consulting Co.

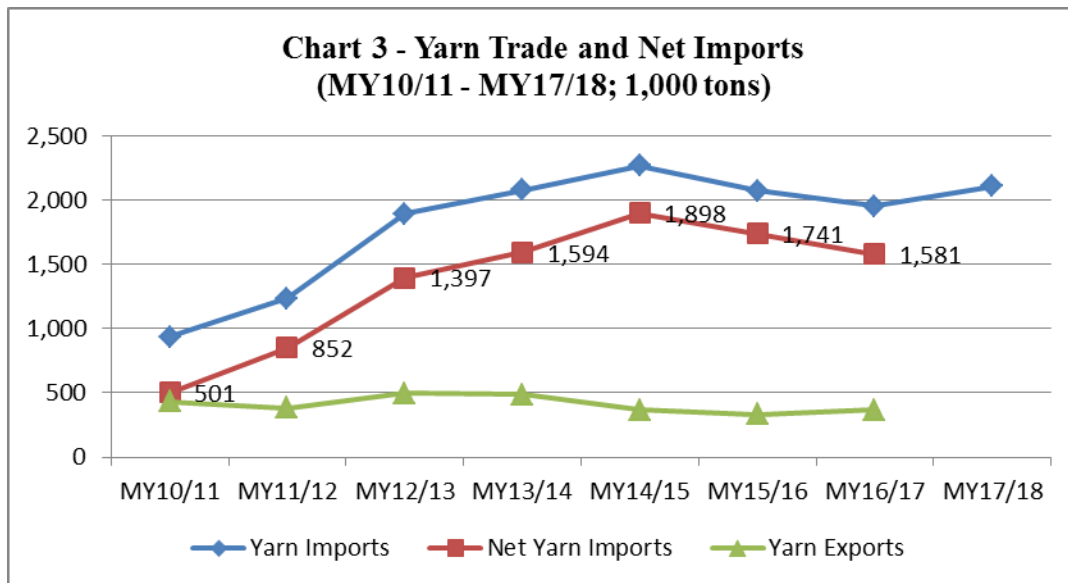
Cotton Trade

Despite challenges, cotton imports expected to recover to 1.5 MMT in MY18/19

China's cotton imports are forecast to recover to 1.5 MMT in MY18/19 from 1.25 MMT in MY17/18. The Chinese government added 0.8 MMT of additional import TRQ in June 2018, aimed at facilitating more cotton imports to meet domestic demand for higher-grade foreign cotton. Access to the TRQ was likely distributed to applicants in late October and will be valid until the end of February 2019.

Imports of U.S. cotton are hindered by the additional 25 percent tariff, which industry sources estimate will add RMB 4,000 (\$600)/ton to cotton imported from the United States. In the first two months of MY18/19 (August-September), U.S. cotton exports to China were down 50 percent from the same period in MY17/18. In addition, Chinese mills are concerned about the impact the increased duties on Chinese textile and apparel exports to the United States will have on yarn demand. Due to this potential risk, mill managers are reportedly hesitant to accept long term orders from the United States and prefer domestic cotton to imported cotton at this time. Finally, some analysts have suggested that mills have not yet fully utilized the cotton purchased from the state reserve, which may also slow the pace of imports.

In recent years, increasing yarn imports have been another factor exerting downward pressure on cotton imports, with yarn imports not subject to quota restrictions like cotton imports are. High yarn imports partly reduced cotton imports from 2015 through 2017. In the first two months of MY18/19, yarn imports stood at 0.38 MMT, up from 0.33 MMT the previous year. Since increased yarn imports are linked to an inadequate supply of cotton through the TRQ, the additional 0.8 import TRQ is expected to push China's mills to import more cotton and less yarn in MY18/19. Although complete Chinese Customs data has not yet been released, industry sources report that cotton imports recovered in the first two months of MY18/19, with total imports at 0.3 MMT, up 69.5 percent from the previous year.



Source: GTA; Data for MY17/18 are industry estimate and yarn export data are not available

Importers seek to increase cotton imports from Brazil and Australia

According to a Chinese industry source, representatives of the Brazil Cotton Association visited China in October to better understand the Chinese market and potential opportunities for Brazilian cotton. Brazil's traditional focus for cotton exports has reportedly been Southeast Asia and Turkey, due to concerns over China's import restrictions via the TRQ. Brazil's total cotton production is estimated to be 2.2 MMT in 2018/19 and there is potential to expand in the future. In a survey administered at a Chinese industry forum in October, half of the respondents indicated that they planned to source Brazilian cotton to meet the supply gap resulting from U.S.-China trade frictions, while 22 percent of those surveyed said they would buy from Australia.

Chinese cotton exports are forecast to remain low in MY18/19

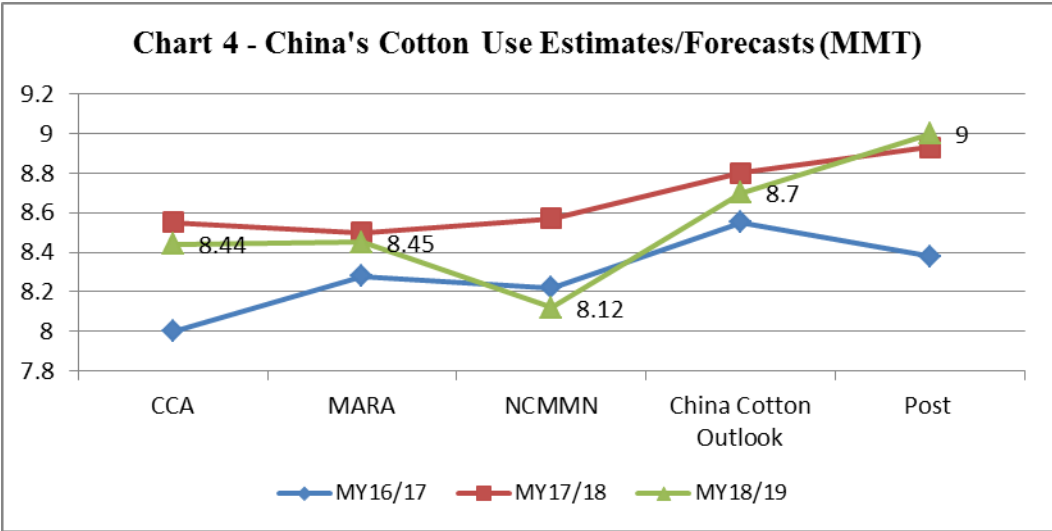
China's cotton exports average about 10,000 tons annually, a nominal amount compared to total domestic cotton use. Cotton exports reached a 9-year high in MY15/16 at 28,000 tons before falling to 13,000 tons in MY16/17. Cotton exports are forecast at 30,000 tons in MY18/19.

Consumption

MY18/19 cotton consumption is forecast at 9 MMT, up from an estimated 8.9 MMT in MY17/18. The growth in cotton use is mainly driven by an increase in cotton TRQs, and a more market-oriented

domestic cotton price, which is expected to restrain yarn import growth and stimulate cotton fiber use in yarn production. Anticipated growth in domestic demand for textiles and apparel products is also expected to moderately boost China's cotton use.

As shown in the following chart, the forecast for China's MY18/19 cotton use varies greatly by the Chinese data source.



Source: November report/update of the relevant agencies; NCMMN data cover spinning use only

Tables

Production, Supply and Demand (PSD)

Note: Exchange rate is: \$1=RMB6.64 in 2016; \$1=RMB6.67 in 2017; \$1=RMB6.8 in 2018

Table 1. PSD (in 1,000 Bales and 1,000 Ha)

Cotton China	2016/2017		2017/2018		2018/2019	
	Market Year Begin: Aug 2016		Market Year Begin: Aug 2017		Market Year Begin: Aug 2018	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Planted	0	2,950	0	3,355	0	3,350
Area Harvested	2,900	2,950	3,400	3,355	3,350	3,350
Beginning Stocks	56,698	56,698	45,919	45,919	38,019	37,971
Production	22,750	22,750	27,500	27,330	27,500	27,558
Imports	5,032	5,032	5,725	5,725	7,000	6,890
Total Supply	84,480	84,480	79,144	78,974	72,519	72,419
Exports	61	61	125	125	150	138
Use	38,500	38,500	41,000	40,878	42,500	41,337
Loss	0	0	0	0	0	0
Total Dom. Cons.	38,500	38,500	41,000	40,878	42,500	41,337
Ending Stocks	45,919	45,919	38,019	37,971	29,869	30,944
Total Distribution	84,480	84,480	79,144	78,974	72,519	72,419
Stock to Use %	119	119	92	93	70	75
Yield	1,708	1,679	1,761	1,774	1,787	1,791
TS=TD	0	0	0	0	0	0

Table 2. PSD (in 1,000 Tons and 1,000 Ha)

Cotton China	2016/2017		2017/2018		2018/2019	
	Market Year Begin: Aug 2016		Market Year Begin: Aug 2017		Market Year Begin: Aug 2018	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Planted	0	2,950	0	3,355	0	3,350
Area Harvested	2,900	2,950	3,400	3,355	3,350	3,350
Beginning Stocks	12,344	12,344	9,998	9,998	8,278	8,267
Production	4,953	4,953	5,987	5,950	5,987	6,000
Imports	1,096	1,096	1,246	1,246	1,524	1,500
Total Supply	18,393	18,393	17,231	17,194	15,789	15,767
Exports	13	13	27	27	33	30
Use	8,382	8,382	8,927	8,900	9,253	9,000
Loss	0	0	0	0	0	0
Total Domestic Consumption	8,382	8,382	8,927	8,900	9,253	9,000
Ending Stocks	9,998	9,998	8,278	8,267	6,503	6,737
Total Distribution	18,393	18,393	17,231	17,194	15,789	15,767
Stock to Use %	119	119	92	93	70	75
Yield	1,708	1,679	1,761	1,774	1,787	1,791
TS=TD	0	0	0	0	0	0

Table 3. Tariff Rate Quota

Description	HS Code	Initial Quota and Tariff Rate	Final Quota and Tariff Rate	Implementation of Final Quota
Cotton		780,750 MT	894,000 MT	2004
	5201 - 0000	1%	1%	
	5203 - 0000	1%	1%	
Other terms and conditions:				
1) STE share = 33% (See Note)				
2) History of China's TRQ for Cotton:				
Year TRQ quantity:				
2002 - 818,500 MT				
2003 - 856,250 MT				
2004 - 894,000 MT				
2005 - 894,000 MT (China added 1.4 MMT TRQ in 2005)				
2006 - 894,000 MT (China added 2.7 MMT TRQ in 2006, subject to variable import duty)				
2007 - 894,000 MT (China added 2.6 MMT TRQ in 2007, subject to variable import duty)				
2008 - 894,000 MT (China added 2.6 MMT TRQ in 2008, subject to variable import duty)				
2009 - 894,000 MT (China added 400,000 MT TRQ only for processing trade, due to weak demands for cotton)				
2010 - 894,000 MT (China added 2.67 MMT TRQ subject to variable import duty)				
2011 - 894,000 MT (China added 2.7 MMT of TRQ subject to variable import duty)				
2012 - 894,000 tons (China added 2.4 million tons of TRQ subject to variable import duty)				
2013 - 894,000 tons (China added an estimated 2.3 million tons additional TRQ subject to variable duty for processing trade)				
2014 - 894,000 tons (China added about 1.3 million tons additional TRQ subject to variable duty were distributed but not officially announced)				
2015 -- 894,000 tons distributed (Industry sources estimated about 300,000 tons of cotton were imported by China's bonded zones* and destined for processing-trade for re-export in 2015)				
2016 -- 894,000 tons distributed				
2017 -- 894,000 tons distributed				
2018 -- 894,000 tons distributed; (China added 0.8 MMT of TRQ subject to variable tariff import duty which was distributed in October 2018 and valid till the end of February 2019)				
2019 -- Announced starting application for the 894,000 tons in mid-October 2018 and to reach end-users usually in January 2019				

*Cotton imports by China's bonded zones are included in China's total cotton import data. However, industry sources explained that these imports are not subject to TRQ control if the processed products are proven to be exported.

Note: China's WTO commitment does NOT mandate a TRQ for CY05 and after, but China maintained an identical quantity of TRQ as CY04. In addition to those volumes, China issues additional TRQs based on market demand. The additional TRQs are subject to a variable import duty.

Source: NDRC and industry estimates.

