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Brazil

Cotton and Products Update

Exports to Surge, Notwithstanding Modest Planting Expansion and Moderating Prices

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Report Highlights:

Post forecasts Brazil's 2019/20 marketing year (MY) cotton area to reach 1.6 million hectares (ha), nearly unchanged from the MY 2018/19 planted area estimate of 1.59 million ha. Post forecasts 2019/20 production and exports will top current records, at 12.5 million bales and 8.5 million bales, respectively. Post estimates MY 2018/19 production at 12.3 million bales, and exports at 5.9 million bales. The 44-percent surge in exports for 2019/20 is forecast based on the current season's bumper crop and the fact that Brazilian cotton farmers have already locked in sales contracts for around two-thirds of their production. As a result, Brazil is forecast to once again beat its cotton export record, despite the environment of moderating global prices.

PRODUCTION

Planted Area and Production Forecast to See Modest Gains in 2019/20

Post forecasts Brazil's total harvested area for the 2019/20 season at 1.6 million hectares (ha), approximately the same as the current season. The planted area stagnation comes on the heels of very rapid expansion of more than half a million hectares of additional cotton area in just two seasons, from 940,000 ha in 2016/17 to an estimated 1.59 million ha in 2018/19. This breakneck growth in sowing has been driven by ample available land suitable for cotton farming in combination with strong international demand and correspondingly high global prices. Anemic domestic consumption has not affected the growth of total planted area.

The 2019/20 Post planted area forecast is based on several factors. First, producers expect that in keeping with the already evident trend, global cotton prices will moderate on the back of ample global supply. Brazil is projected to have a bumper crop this season, with a massive exportable surplus carried over into the next export season. According to Post's conversations with contacts, most producers and traders in Brazil expect that the global market will not be able to absorb substantially higher cotton volumes than what Brazil will produce during the 2018/19 season.

Second, as a consequence of the rapid expansion of cotton farming in Brazil in recent years, Post believes that producers have largely maximized economies of scale with existing equipment and arable land. Given that cotton machinery is expensive, additional investment does not make sense amid tepid export growth expectations and subdued prices.

Post forecasts 2019/20 production at 12.5 million bales (2.72 million metric tons), based on the expectation of 1701 kg/ha yield. Post assumes that yield will be slightly higher than the one projected by Post for the current season, but below the record productivity set in the 2017/18 season. The yield forecast is based on the assumption that the recently added cotton area has yet to reach its maximum output potential, a process which takes several years to be completed. Mato Grosso state is forecast to continue its role as the dominant cotton producer, accounting for about two thirds of Brazil's total production while farmers in Bahia will contribute an additional 21 percent to the total output.

Area and Production Forecast by State for 2019/20

	Planted Area (1000 HA)	Percent of Total Area Planted	Production (MT)	Percent of Total Production
Total	1600	100%	2722	100%
Mato Grosso	1100	69%	1775	65%
Bahia	335	21%	600	22%
Goiás	43	3%	72	3%
Mato Grosso Do Sul	37	2%	67	2%
Minas Gerais	40	3%	61	2%
Maranhão	28	2%	47	2%
Piau	16	1%	28	1%

Source: Post Brasília Forecast

Current Cotton Harvest to Top Expectations

Post's estimate for 2018/19 harvested area is 1.59 million hectares (ha), an increase of more than one third on the 2017/18 season. As previously noted, factors such as ample arable land and favorable climate have enabled Brazilian farmers to rapidly expand planted area in order to capitalize on growing global demand for cotton. Producers also benefited not only from rising global prices, but also the relatively weak domestic currency, the Real. Over the last several years, the Real, lost value against the U.S. dollar – first, on account of a deep economic recession, and then due to a sluggish economic recovery that began in 2018. Given this extremely favorable backdrop of external market demand and strong global prices coupled with Brazil's internal production capacity, farmers chose to put the maximum planted area that they could into production this season.

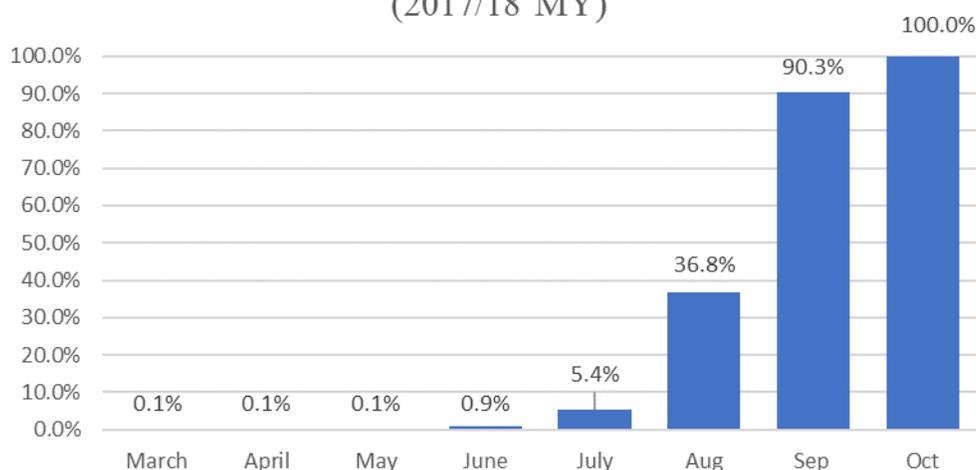
Planted area increased across all but one of the 10 cotton growing states, in some cases by more than 100 percent. Notably, production area remains extremely concentrated, with almost 9 out of 10 bales of cotton produced in the two states of Mato Grosso and Bahia.

Farmers in Mato Grosso are expected to finish the season with more than one million planted hectares, which will account for two thirds of all cotton planted area in Brazil. Overall, the production area in the state is estimated to increase by more than 37 percent in 2018/19, up from 780,000 ha that farmers planted last season. Producers both big and small expanded production in the state, with cotton planting catching on in municipalities that traditionally plant corn or cover crops to follow up the first season soybean crop. The majority of cotton planted in Mato Grosso is second season crop, after the first crop of soybeans. Cotton harvest technically starts in June, but picks up in July with the bulk of the crop picked in August and September. With some wet weather this spring, yields in Mato Grosso are expected to be marginally lower than initially expected, with production estimated by Ministry of Agriculture National Production Company (CONAB) at 8.2 million bales (1.78 million metric tons).

In Bahia, cotton area amounted to just over 330,000 ha, representing an almost 26 percent increase over last season. Harvest in the state typically runs June through November, though the current season may have a longer production cycle due to higher than average precipitation in March and April. CONAB estimates production in Bahia for 2018/19 at 2.75 million bales (598,000 metric tons). Goiás, the third

largest state in production, planted 42,000 ha, an increase of 30 percent over the previous crop year, and is projected to harvest close to 325,000 bales (70,000 metric tons).

Total Cotton Crop Harvested by Month
(2017/18 MY)



Source: Brazil's National Production Company (CONAB)

Post estimates cotton yield to be about one percent below the previous season, averaging 1.693 kg/ha. Overall, production is estimated at 12.3 million bales (2.7 million metric tons), up 34 percent from last season's crop of 9.2 million bales (2 million metric tons).

Prices Trend Down

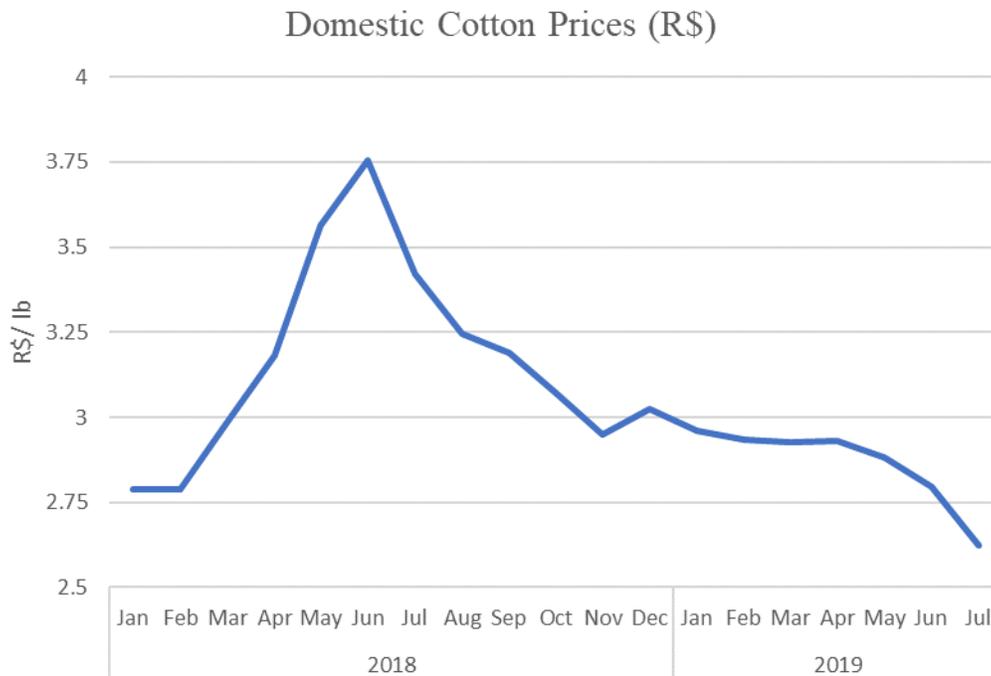
Domestic cotton prices continued their decline in the second quarter of the year, in line with the drop in global market prices. In July 2019, New York futures cotton price touched a three-year low of 62.6¢/lb. Looking into the second half of the year, global prices will likely continue to be weighed down by massive harvests in the United States and Brazil. U.S. inventories are projected to reach a 12 year high in the 2019/20 season. Meanwhile, global demand is also decelerating amid a global economic slowdown. Since the beginning of the year, domestic cotton prices have been on a steady downward trajectory, leveling off from R\$2.96/lb., to R\$2.62/lb. in July. The full data for August is not available yet, but as of the first three weeks of the month, the average monthly domestic cotton price is down to R\$2.47/lb.

Domestic Cotton Prices (in R\$)			
	2018	2019	% Change, Year-Over-Year
Jan	2.79	2.96	6%
Feb	2.79	2.93	5%
Mar	2.99	2.93	-2%
Apr	3.18	2.93	-8%
May	3.56	2.88	-19%
Jun	3.76	2.79	-26%
Jul	3.42	2.62	-23%
Aug	3.25		
Sep	3.19		
Oct	3.07		
Nov	2.95		
Dec	3.03		

Source: Center for Advanced Studies in Applied Economics (CEPEA)

* Cotton grade 41-4, staple 30/32mm, 8-day term payment, no interstate commerce tax. Includes freight for point of delivery to São Paulo city.

The new price trend is a marked departure from last calendar year, when global prices were soaring on constricted global supply and sharp acceleration in Chinese cotton imports. At the same time, Brazilian producers reaped the benefits of a weaker currency that came under pressure amid investor worry over political stability in the election season.



Source: Center for Advanced Studies in Applied Economics (CEPEA)

* Cotton grade 41-4, staple 30/32mm, 8-day term payment, no interstate commerce tax. Includes freight for point of delivery to São Paulo city.

TRADE

2019/20 Export Outlook Bright Despite Price Skid

Post has revised its forecast for the 2019/2020 marketing year (MY, August 2019-July 2020) exports to 8.5 million bales (1.85 million metric tons) – a more than 40 percent increase year-over-year – as a result of massive exportable supplies from the current harvest season and continued strong demand in China. Brazil’s cotton harvest and subsequent export of that season’s crop is split between two marketing years. Therefore, the current 2018/19 harvest will be exported during the 2019/20 MY. Importantly, about 70 to 80 percent of the 2018/19 crop has already been commercialized for 2019/20 delivery, as a result the current slump in cotton prices should not have a pronounced impact on volumes shipped next season.

However, there are several risk factors that may cause a downward revision in next season’s exports. First, Brazilian cotton exports may increasingly bump up against shipping logistics constraints (see GAIN BR 1905 for extended coverage). This marketing season, Brazil was able to export close to 215,000 metric tons in the month of December, indicating what is possible. However, the port of Santos may not have enough capacity for the expected volume of cotton exports each month, especially given the competition from other agricultural and non-agricultural commodities.

Second, and tied into logistical challenges, is the transit time to Asia, particularly to China, compared to other major cotton exporters. According to the Brazilian Cotton Exporters Association (ANEA), it takes 35 days on average, in some cases as long as 70 days, to ship cotton from Brazil to Asia. At the same time, transit time from the United States to Asia is 20 to 22 days, and from Australia to Asia just 10 to 12 days.

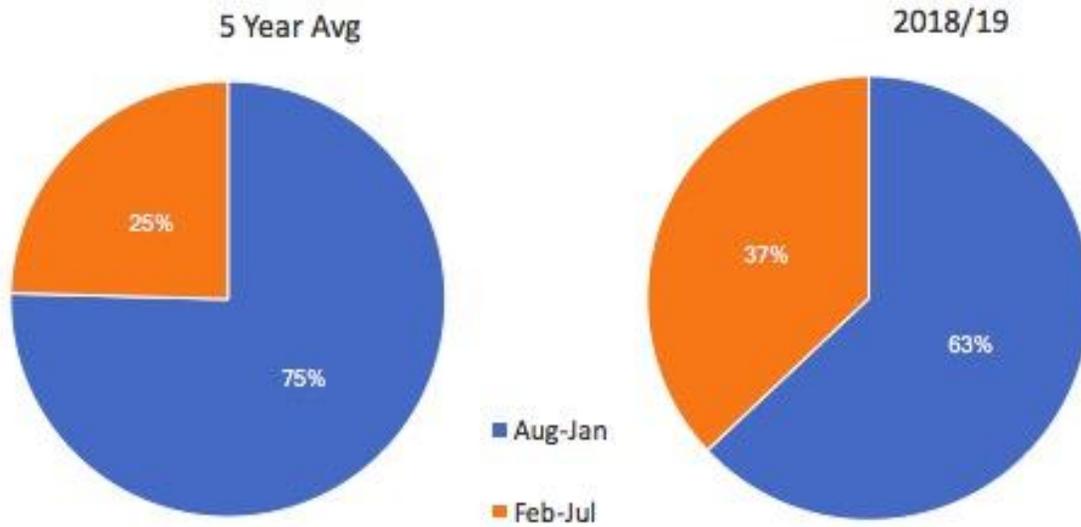
Finally, should U.S.-China trade tensions be resolved, Chinese buyers are likely to return to sourcing greater volumes of U.S. cotton at the expense of other suppliers, including Brazil. However, in conversations with Post’s contacts, sources noted that the impact of such an agreement would be cushioned by the market expectation that China will continue to aggressively rebuild its cotton State Reserve stocks well into 2019/20.

New Export Trends Emerge in 2018/19

Post maintains its estimate for cotton exports of 5.9 million bales (1.29 million metric tons) for the current 2018/19 marketing year (MY, from August 2018 to July 2019). The expected export volume will set a new record for Brazil, making it the second largest cotton exporter in the world.

Aside from record total cotton volumes shipped, it is worth noting several new export trends for Brazilian cotton. First, this marketing year solidifies a major shift in Brazil’s cotton export calendar. Traditionally, Brazil shipped more than two thirds of its cotton exports in the first half of the marketing year (August-December). However, the shipping calendar has increasingly stretched more evenly over the course of the calendar year. Currently, the split between the first and second half of the marketing year is almost 60/40. Post expects the export split to move toward 50/50 within another season or two.

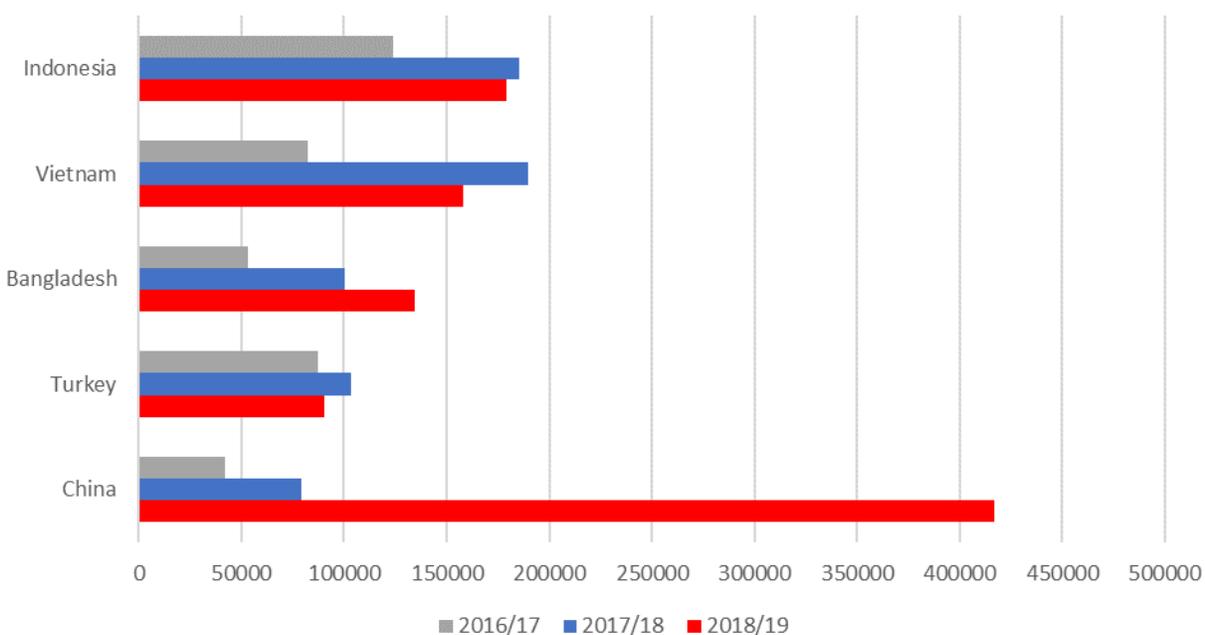
Brazil's Cotton Export Calendar Shift



Source: Foreign Trade Secretariat (SECEX)

Another recent trend is the emergence of China as the leading buyer of Brazilian cotton. Throughout the 2017/18 season, Vietnam and Indonesia were by far the two leading destinations for Brazil's cotton, importing close to 1.9 million metric tons each, followed by Turkey and Bangladesh, with just over 1 million metric tons in imports each, and China, with less than 0.8 million metric tons in import volume. However, in the current season, China catapulted to the leading place as top importer of Brazilian cotton with more than 4 million metric tons of cotton sourced. Two factors drove a sharp increase in Brazil's sales to Beijing, the overall surge in Chinese cotton import demand and the punitive 25 percent tariff on U.S. cotton imposed in July 2018 in the wake of escalating U.S.-China trade tensions.

Brazil's Cotton Exports by Destination (Metric Tons)



Source: Foreign Trade Secretariat (SECEX)

Overall, Brazil's top five buyers account for more than 80 percent of the total volume of exports for this season, with China accounting for more than a third. Post contacts anticipate that this trend will continue to consolidate. The Ministry of Agriculture, Livestock and Supply (MAPA) and the Ministry of Foreign Affairs (MRE), through the Brazilian Agency for the Promotion of Exports and Investments (Apex), and Brazilian Cotton Exporters association (Abrapa) are planning to open a permanent office in Asia, in order to increase promotion efforts from annual exchange missions.

CONSUMPTION

Domestic Consumption Expected to Remain Sluggish in 2019/20

Despite the government making headway with major structural reform of the pension system, Brazil's economy is only projected to grow just over two percent next calendar year. Slow growth is forecasted to have a corresponding impact on manufacturing and consumer sentiment that will impact all domestic manufacturing, including cotton. For MY 2019/20, Post forecasts domestic consumption at 3.5 million bales (762,000 MT), an increase of three percent compared to the previous MY.

For the current season, Post has revised expected domestic consumption to 3.4 million bales (740,000 MT), equating to stagnant growth compared to the previous season. The revised forecast stems from slower than originally expected economic growth in 2019. At the start of the calendar year, the market projected GDP growth was two to three percent. However, in the first half of the year, the Brazilian government and investors revised that figure. As of July 2019, market consensus is far below one percent growth, with the Brazilian government projecting 0.8 percent.

The Brazilian Association of the Textile and Apparel Industry (ABIT) projects growth of 0.5 percent in domestic textile production and 1.5 percent in retail. ABIT points to a sluggish domestic economy as the main culprit for the underperformance of the national cotton industry. ABIT's projections are based on the expectation that the government will be able to push through structural reforms in the second half of 2019, leading to a better investor sentiment. For the first half of the year, ABIT's figures actually show a contraction in both textile production and in retail of 1.0 and 2.5 percent respectively.

STOCKS

Clarification On Beginning/Ending Stock Estimates

The USDA official estimates, as well as this report, are based on an August-July Marketing Year (MY). As such, MY 2018/19 correlates with Northern Hemisphere countries, such as the United States and not with Southern Hemisphere countries such as Brazil. As a result, USDA's beginning/ending stock estimates capture Brazilian stocks during harvest when they are at their peak. In addition, the inevitable buildup of USDA reported stocks is also reflected in the structural delay between harvest during one season and the shipment of exports during the next season. This timing issue accounts for the relatively high stock levels and low volatility in stocks typically recorded by USDA as well as those used in this report.

Brazilian Cotton Production, Supply and Demand (in bales and metric tons)

Market Year	2017/2018		2018/2019		2019/2020	
Beginning of MY	Aug 2017		Aug 2018		Aug 2019	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Planted	0	0	0	0	0	0
Area Harvested	1175	1175	1595	1595	1550	1600
Beginning Stocks	6929	6929	8657	8657	12207	11717
Production	9220	9220	12800	12300	12000	12500
Imports	82	82	50	60	75	75
MY Imports from U.S.	0	0	0	0	0	0
Total Supply	16231	16231	21507	21017	24282	24292
Exports	4174	4174	5800	5900	8200	8500
Use	3400	3400	3500	3400	3600	3500
Loss	0	0	0	0	0	0
Total Dom. Cons.	3400	3400	3500	3400	3600	3500
Ending Stocks	8657	8657	12207	11717	12482	12292
Total Distribution	16231	16231	21507	21017	24282	24292
Stock to Use %	114.3	114.3	131.26	125.99	105.78	102.43
Yield	1708	1708	1747	1679	1686	1701

(1000 HA), (1000 480 lb. Bales), (PERCENT), (KG/HA)

Cotton	2017/2018		2018/2019		2019/2020	
Market Begin Year	Aug 2017		Aug 2018		Aug-19	
Brazil	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Planted	0	0	0	0	0	0
Area Harvested	1175	1175	1595	1595	1550	1600
Beginning Stocks	1509	1509	1885	1885	2658	2551
Production	2007	2007	2787	2678	2613	2722
Imports	18	18	11	13	16	16
MY Imports from U.S.	0	0	0	0	0	0

Total Supply	3534	3534	4683	4576	5287	5289
Exports	909	909	1263	1285	1785	1851
Use	740	740	762	740	784	762
Loss	0	0	0	0	0	0
Total Dom. Cons.	740	740	762	740	784	762
Ending Stocks	1885	1885	2658	2551	2718	2676
Total Distribution	3534	3534	4683	4576	5287	5289
Stock to Use %	107.15	109.15	110.15	112.15	113.15	115.15
Yield	1708	1708	1747	1679	1686	1701