



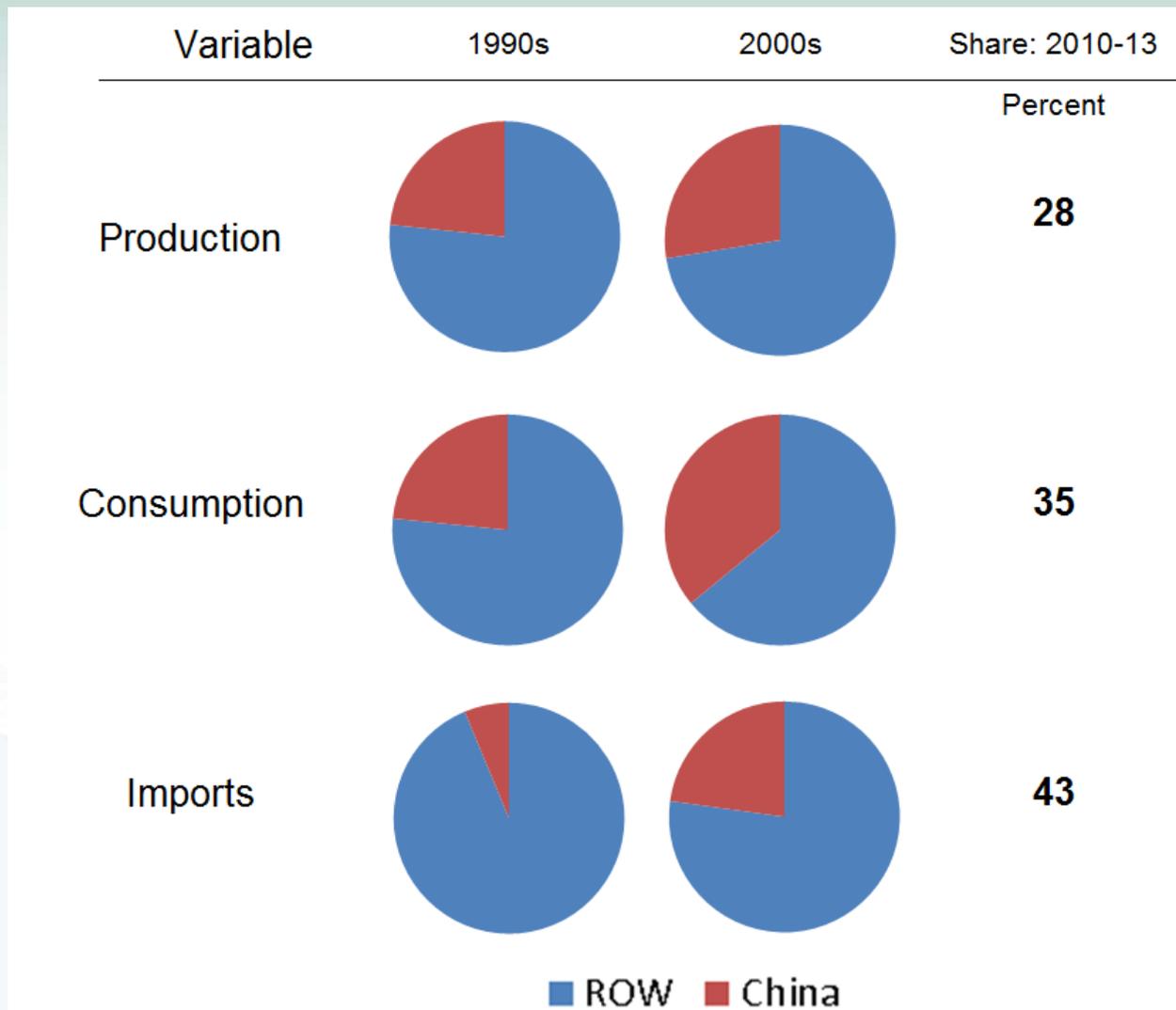
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China's Cotton Policy: New Directions in 2014

Stephen MacDonald, USDA/ERS

USDA Outlook Forum
February 21, 2014
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China Leads World Cotton Markets

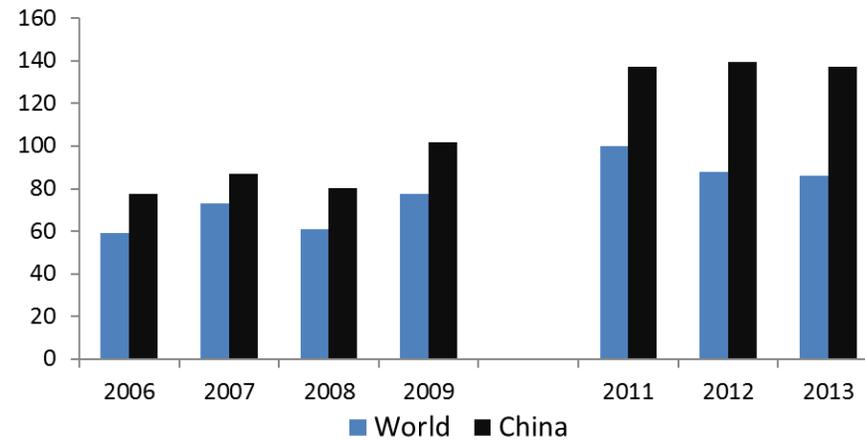


Source: ERS calculations based on data from PS&D Online
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The Problem for China

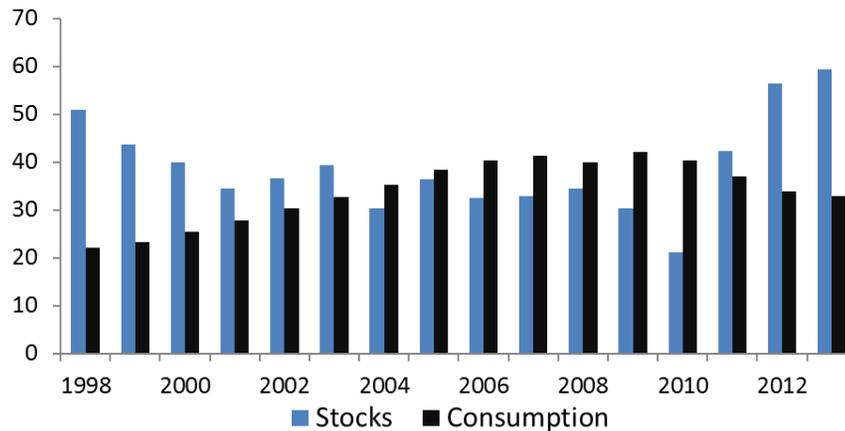
Cotton prices: World and China, 2006-2013

Cents/pound



China's share of world cotton stocks and consumption, 1998-2013

Percent



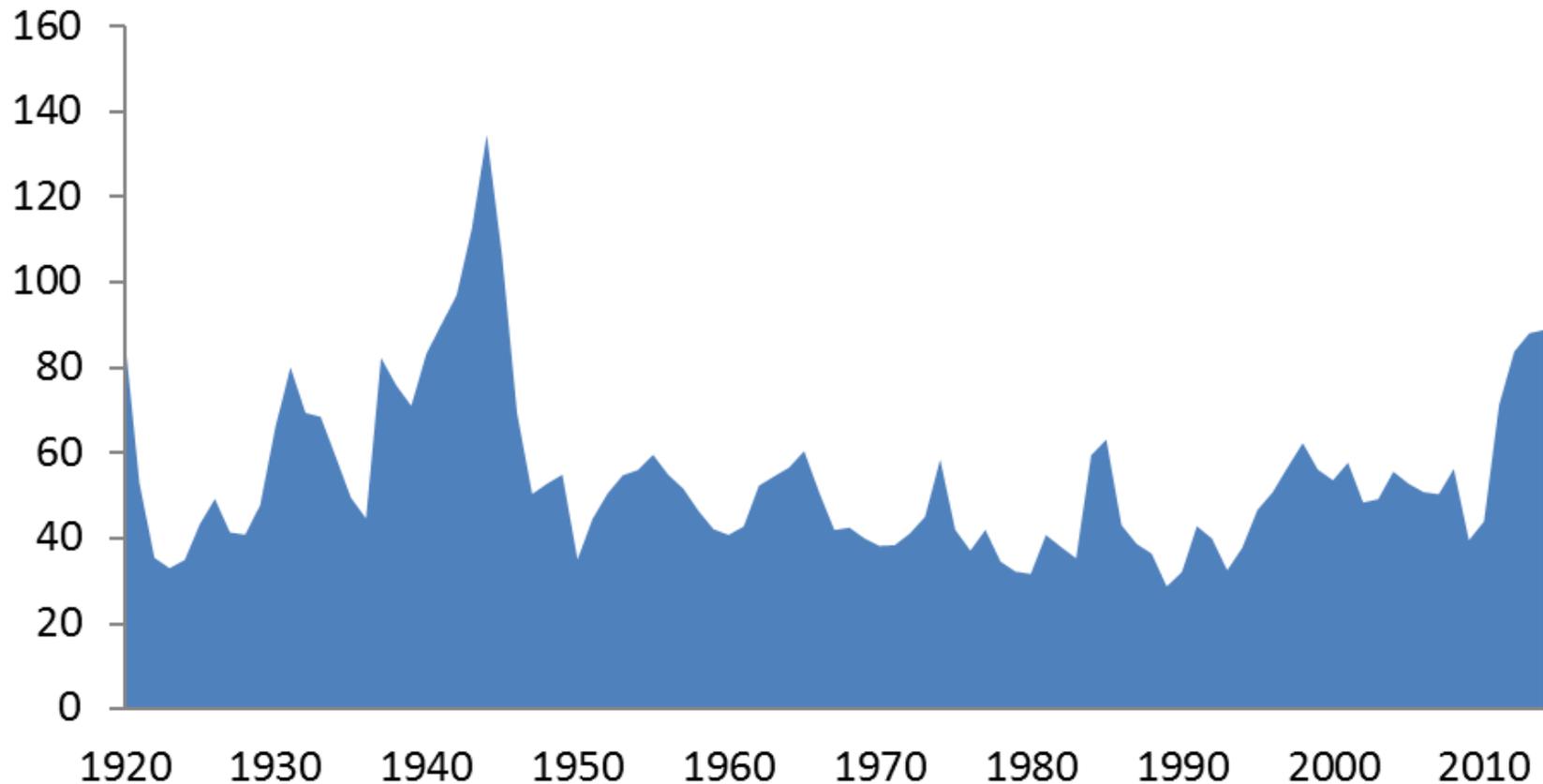
Source: ERS calculations based on data from PS&D Online, *Cotton Outlook*, Beijing Cotton Outlook, and IMF.

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The Problem for the World

World cotton ending stocks, as a share of use: 1920-2014

Percent



Source: ERS calculations based on data from USDA/ERS, *Statistics on Cotton: 1920-1973*, PS&D Online, and USDA estimates.

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China's Cotton Policy Shift

March 2011:

China announced its “temporary state reserve” program for cotton

- Committed to purchase domestic cotton fiber during September-March whenever prices fell below published reference price
- Similar support prices previously introduced for rice (2004), wheat (2005), and corn (2007)
- Grains also received direct subsidies, input subsidies, and benefited from mechanization subsidies.



Cotton Prices, 2011-13

China's reference price:

RMB/ton	19,800 – 20,400
USD/ton	3,100 – 3,360
cents/lb	141 – 153

World price:

cents/lb	81 – 111
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China went from a 25% price premium compared with rest of world to a 60% premium



Policy Affecting Cotton Indirectly

Economic Policy:

- Exchange rates

- Environmental regulations

- Monetary policy

 - Access to funds for investment

 - Rate of growth in China's domestic economy

- Textile trade policy

 - Import restrictions

 - Export VAT rebates

Agricultural Policy:

- Rural infrastructure and social welfare

- Support for alternative crops

 - Rising minimum prices for grains

 - Direct subsidies and input subsidies for grains



Policy Directly Affecting Cotton

Supplemental policies:

Subsidies for using “superior” planting seeds

Subsidies for transportation of cotton from Xinjiang

Subsidized credit for purchasing during harvest

-- access to credit conditional on cotton price guidelines

Fiber inspection services

Gin certification

Agricultural research, market information



Policy Directly Affecting Cotton

“Macro control”

Market intervention: changes in government-owned stocks of cotton to influence prices

Trade policy: annual changes in the availability of import quotas at preferential tariffs; less frequent changes in determination of a “sliding-scale” tariff that has applied to these imports since 2005.

This is similar to China’s policy for other agricultural commodities.

The crucial change in 2011 was the pre-season announcement of the intervention price, and its high level.



Reserve Activity: 2004-13

Large net sales: 2009, 2010

Large net purchases: 2008, 2011-13

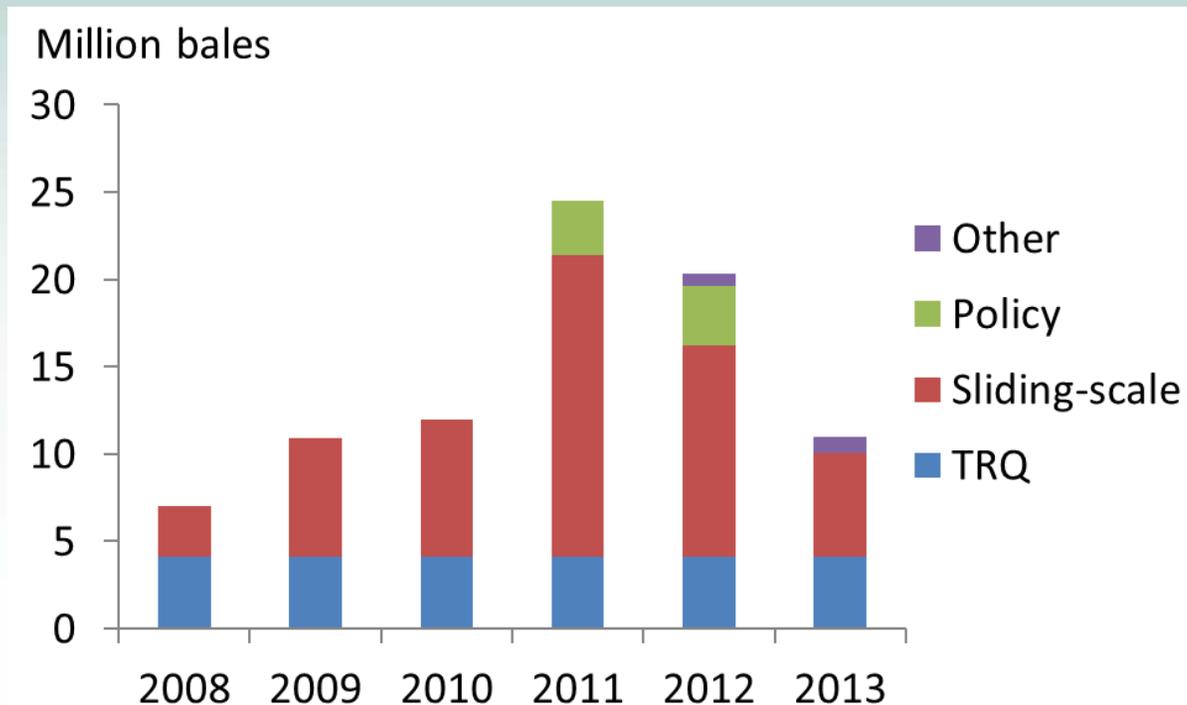
China's domestic cotton intervention purchases for and sales from government reserves, MY2004-13

	Reserves purchases	Reserves sales	Net domestic purchases for Reserves	
	Thousand bales			Percent of crop
2004	600	0	600	2
2005	0	0	0	0
2006	1,400	700	700	2
2007	0	0	0	0
2008	12,900	5,500	7,400	20
2009	0	6,400	-6,400	-20
2010	0	4,400	-4,400	-14
2011	14,400	0	14,400	42
2012	30,400	19,100	11,300	32
2013	27,800	14,800	13,000	41

Sources: ICAC *Review of the World Cotton Situation* (various issues), *Cotton Outlook* (various issues), and USDA estimates.



Cotton Imports By Category



“Policy:” e.g. imports by China National Cotton Reserves Corporation (CNCRC)

“Other:” imported at full 40% WTO-bound tariff



Sources: USDA attache reports, industry reports, and USDA calculations.
United States Department of Agriculture, Economic Research Service

Guidelines for New Policy: Goals

Top level (strategic)

- Maintain some capacity for domestic cotton production
- Augment the well-being of rural residents and companies
- Ensure the economic stability of Xinjiang
- Return a greater share of China's cotton spinning sector to profitability

Second-tier (process)

- Reduce reserve stocks to an optimal level
- Limit friction with trading partners and competitors
- Efficient use of resources while implementing policy
 - Limit the monetary losses associated with reserve management



Outline of New Policy

China's policy makers acknowledge current policy is unsustainable

Changes in 2014 will be steps towards:

- Less distortionary producer support

- Less generous producer support

- Significantly more support for Xinjiang than elsewhere

- Reserve stocks rising trend reversing

Changes in 2014 will not be dramatic:

- Gradualism and experimentation have been hallmark of China's reform over last 40 years



Production Policy in 2014

Xinjiang-Uighur Autonomous Region

pilot program of target price-based direct subsidies

target price reportedly about 19,500 RMB/ton

-- 5 percent below 2013 reference price

Other provinces (Yellow and Yangtze River growing areas)

excluded from pilot program

harvest price will be determined by interaction of market forces and reserve management

indications that farmers expect 15,000 RMB/ton

-- 25 percent below 2013 reference price



Import Policy in 2014

- Sliding-scale quota (SSQ)
 - quota level close to but above 2005-13 minimum of 3 million bales (third consecutive annual decline)
 - SSQ tariffs little changed
- Policy imports
 - little expected in 2013 or 2014, compared with more than 3 million bales annually in 2011 and 2012
- Other imports
 - TRQ level unchanged (894,000 tons at 1% tariff)
 - out-of-quota tariff remains at 40%
 - no additional impediments to out-of-quota imports



Reserve Management Policy in 2014

- Reserve purchases will occur during harvest
- Decline in reserve sales prices will continue

2012 price = 19,300 RMB/ton

2013 price = 18,300 RMB/ton to date

- review is expected after March

2014 price foreseen near 15,000 RMB/ton

- USDA expects 80 cent/lb world price
 - 17,000 RMB = 40%-tariff-paid equivalent
 - 13,000 RMB = typical domestic equivalent before 2011



Policy-makers Are Constrained

- Pursuing some policy goals precludes achieving others

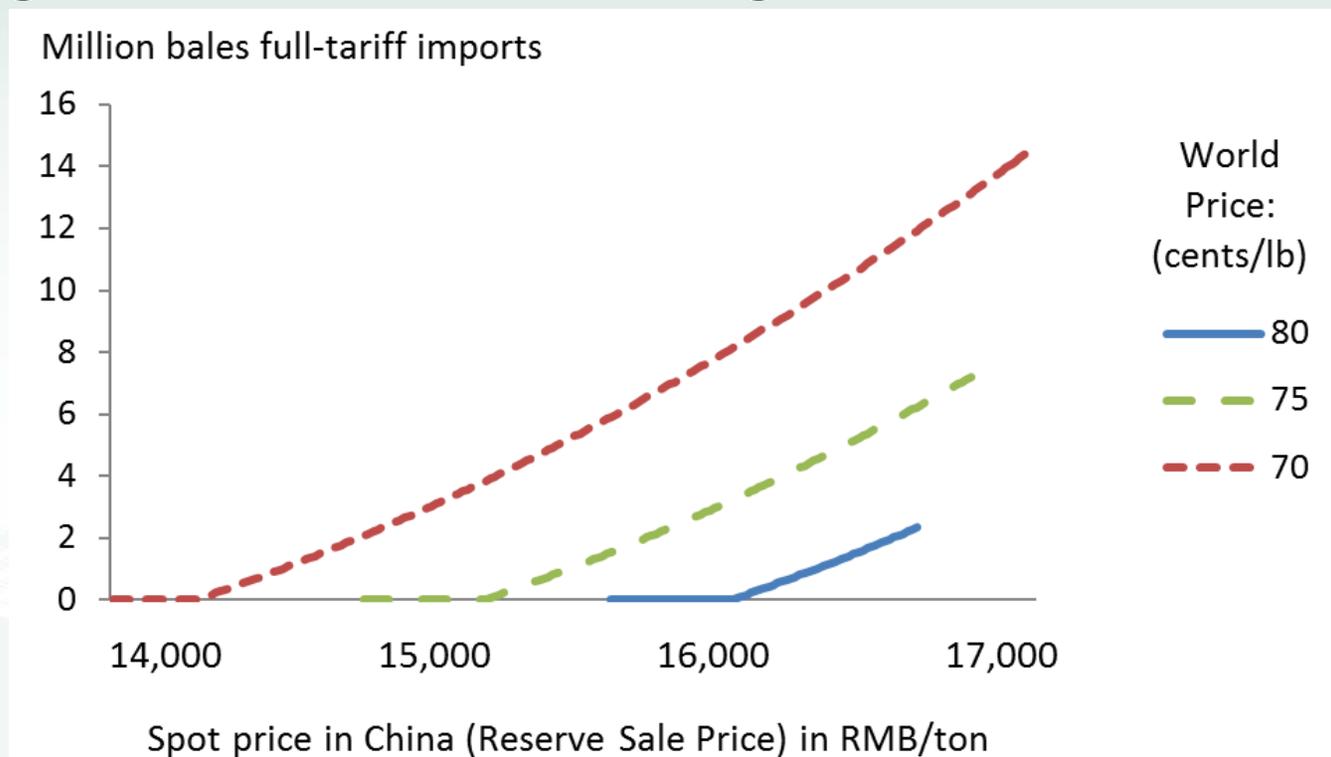
Scenario:

- Goals: reduce stocks at minimal cost
- Policies: high reserve sale price and low import quotas
- Result: large reduction in import quota drives world price down; China consumption declines, full-tariff imports rise, and stock changes limited



Full-tariff Imports Rise With:

Falling World Price or Rising Reserve Sales Price



- Full-tariff imports \approx 1 million bales in 2013

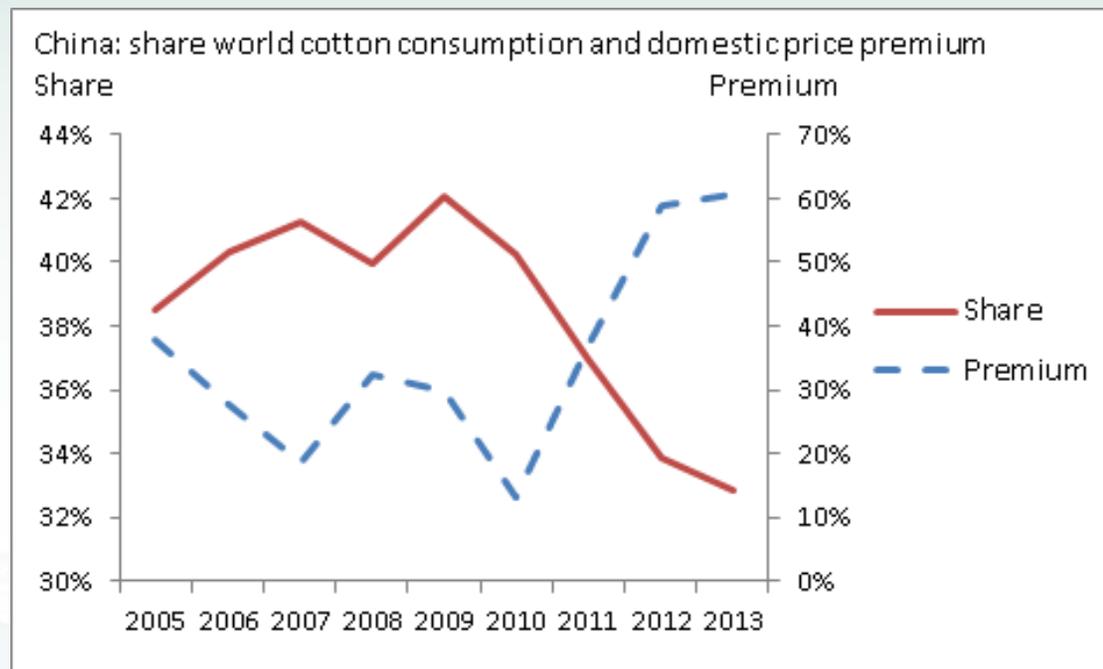


Source: ERS simulations based on data from China Customs, Cotton Outlook, Beijing Cotton Outlook, International Monetary Fund, and USDA estimates

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China Consumption Falls With:

Falling China imports and Fixed Reserve Sales Price



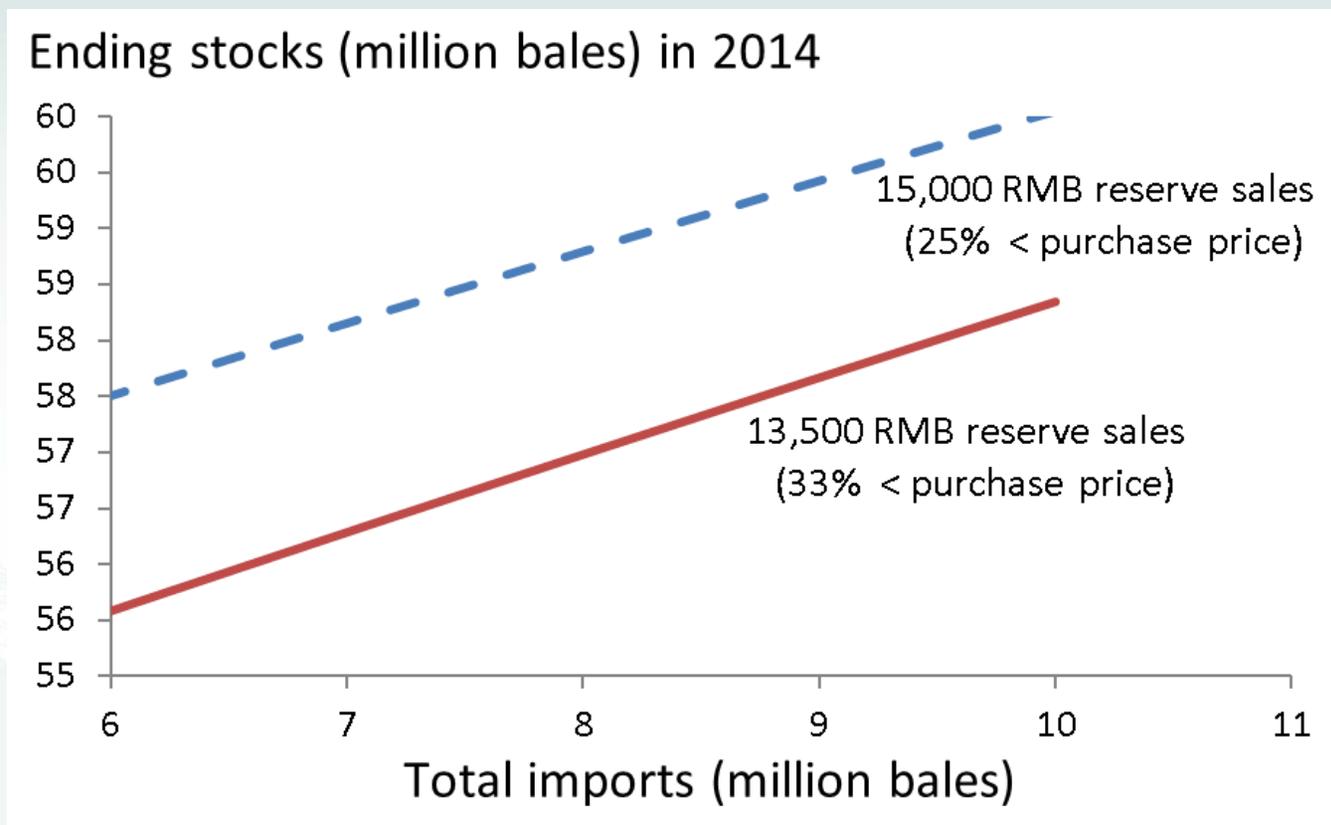
- Ending stocks little changed as falling consumption can offset lower imports



Source: ERS calculations based on data from PS&D Online, *Cotton Outlook*, and Beijing Cotton Outlook.

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Ending stock changes will vary with imports and reserve sale prices



- Reserve sale price reductions potentially costly



Source: ERS simulations based on data from China Customs, *Cotton Outlook*, Beijing Cotton Outlook, International Monetary Fund, PS&D Online, and USDA estimates

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Policy Choices for China in 2014

- Trade-offs between textile industry and farmers
- Trade-offs between financial loss on reserve sales and persistence of high stocks
- Trade-offs between reducing stocks by constraining imports or reducing reserve sale prices
- How to apply experience to inevitable further changes in future years

Acknowledgements:

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For more information on cotton:

Economic Research Service

<http://www.ers.usda.gov/topics/crops/cotton-wool.aspx>

Foreign Agricultural Service

<http://www.fas.usda.gov/commodities/cotton>

For more information on China:

Economic Research Service

<http://www.ers.usda.gov/topics/international-markets-trade/countries-regions/china.aspx>

