



**Rabobank**

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January 25, 2011*

## ***Record production and high prices forecast – Rabobank cotton update***

Despite the impacts of recent severe weather, record production is still expected for Australia's cotton 2010/11 harvest, while strong international demand should keep prices well above long-term averages, according to a newly-released Rabobank report.

In the report, **Cotton update – the durable fabric**, agri finance specialist Rabobank says a bumper crop of record-breaking proportions is still projected for Australia this season, despite downgrades resulting from recent extreme floods damaging cotton crops in Queensland and northern New South Wales.

Following the flooding in Queensland, the bank's forecast for Australian cotton production in 2010/11 has been revised down by eight per cent to 3.95 million bales.

Report author, Rabobank analyst Tracey Allen says despite these losses, "this 3.95 million bales is still a record harvest, and is forecast to be reached in conjunction with well above-average prices".

While continuing price volatility is expected in the first half of 2011 with cotton prices forecast to moderate over the next 12 months, they should remain above the long-term average, the Rabobank report says. Weather also remains a "key upside risk factor" likely to put upward pressure on cotton prices.

"High cotton prices on their own have delivered a significant supply-response in the past, with the area planted to cotton rising in the following season, particularly in major exporting countries. On this occasion there are a number of factors that will influence this response in the coming few years such as weather-related events, competition for land, government policies, and capital constraints," Ms Allen says.

### **Weather**

"Weather will be the main telling factor in reaching cotton production expectations in the next two to three years," Ms Allen says.

The Bureau of Meteorology's (BOM) seasonal outlook for January to March 2011 indicated that cotton-growing regions of New South Wales and Queensland are highly likely to receive above-average rainfall during summer. However rainfall patterns are likely to moderate toward average levels as the influence of La Niña wanes. Ms Allen says this provides an optimal outlook for cotton growers, looking for warmer weather to increase plant vigor during summer, with solid water allocations in hand to finish off crops.



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## **Global demand**

Internationally, the report says, strong domestic consumption from China has underpinned demand growth for cotton, as China is the world's largest importer of the commodity.

"Growth in the Chinese cotton trade is shifting the market into a new, elevated price environment," Ms Allen says.

India also has a large role to play in how the international cotton market dynamics will develop, the Rabobank report highlights, with the country now the second-largest global cotton producer and consumer. "Strong rates of growth are expected to support Indian cotton demand domestically, which will reduce the availability of cotton from India to the global market in coming years," Ms Allen says.

While global cotton production is expected to increase in the coming year, leading to increased supply availability, this situation is expected to be short-term.

"For the first time in four years, the global balance sheet is expected to shift slightly back into positive territory driven by supply-side improvements. Global cotton production is forecast to increase by 10 per cent in 2010/11, coming from traditional stalwarts such as the US, Brazil, India, and Australia," Ms Allen says.

"However, as demand continues to outpace supply, the only concrete conclusion is that strong global production will be required over two to three consecutive seasons if stocks are to rebuild to near-average levels.

"Once stocks are rebuilt, or global demand growth slows, we may see prices moderate. Until then, we expect prices to remain well above average, and believe the risk to prices will remain skewed to the upside in the near-term."

Ms Allen, who is based in Rabobank's Sydney head office, is part of the bank's Food and Agribusiness Research and Advisory division (FAR) – a team of analysts who research developments in food and agricultural markets and industries and advise the bank and its clients on the strategic implications for their businesses.

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