

Get more from information on marketed cotton prices

Reference :

Fok, A. C. M. (2000) Get more information on marketed cotton prices, *in* Joint meeting and workshop of the Inter-regional cooperative research network on cotton Adana, 19-25/09/2000, pp. 289_293.

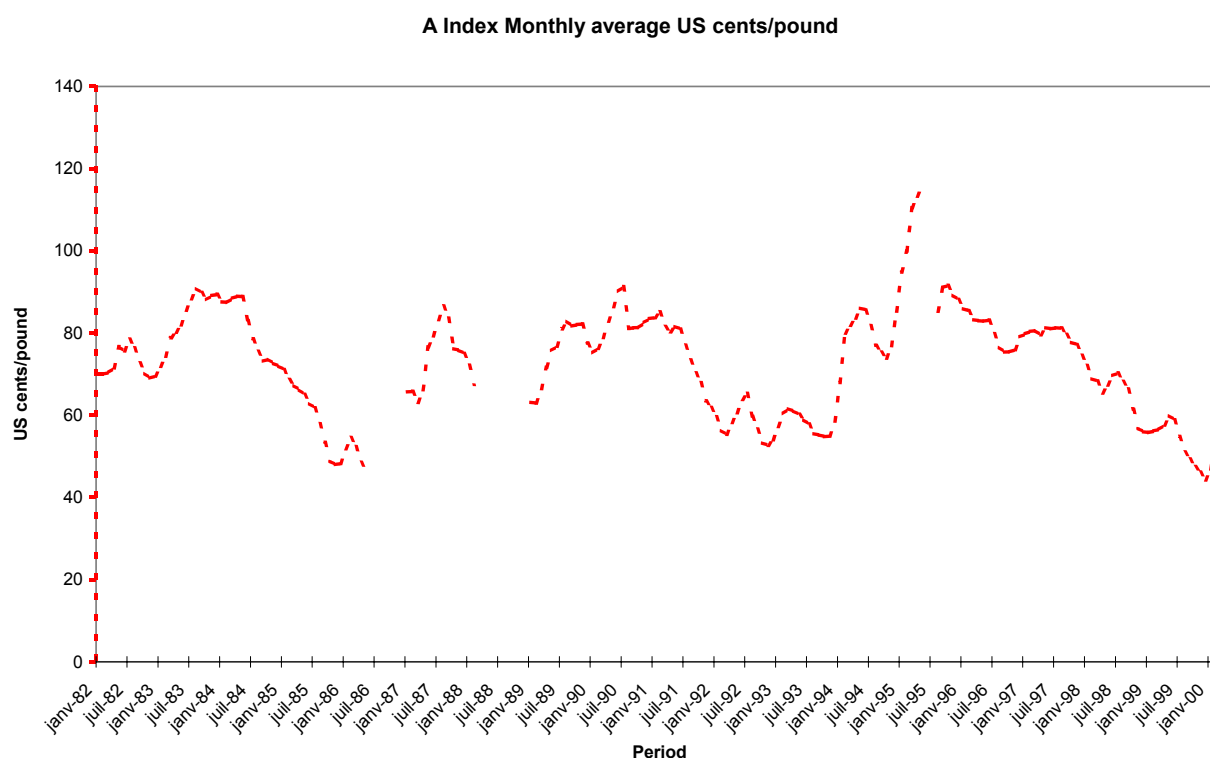
In the area of international trading, it is unrealistic to expect a great transparency and a wide diffusion about the actual prices that conclude the international trade on a specific product. Information asymmetry is the rule between seller and buyer; any initiative from one country to deliver information on the trading of its product encompasses a risk of undesirable effects against its own interest. From this view point, it seems fundamentally contradictory to hear people advocating for the use of modern risk management tools in the exportation of agricultural product while calling in the same time for such management transparency.

Cotton trading is not different in the sense that there is no diffusion on actual trading prices, however we have some indication from information delivered weekly by Cotton Outlook for a long time. The A index of this organism is established from 1966 onwards and it performs as a reference basis in the determination of the price to be paid to cotton producers where such determination still exists. This index is an average of the prices from 5 growths of cotton with the lowest levels among a basket of 15 cotton growths, Middling, 1³/₃₂. It is worthwhile to notice that prices taken into account are those provided by cotton offers and therefore they may be slightly higher than the actual prices after bargaining with buyers.

1. Going beyond the A Index towards a richer exploitation of the available information

It is very common to base upon the only evolution of the A index to assess the cotton market trends. For sure this index is information rich : the Graph 1 shows the evolution of the monthly averages which has reached a historic high record in 1995 and has followed a continuing decrease from 1997 till a historic low record in early 2000 (close to the values experienced during the 1985/86 and 1992/93 cotton crisis).

Graph 1



We think however that we should make better use of the available information and go beyond the evolution of the A index; this is in particular essential for those cotton countries that export the main part of their production. A very quick analysis of the weekly cotton exchanges enables to notice that there are some countries with a very good availability of their cotton (French speaking African countries, Greece, Australia

for instance), It then makes sense to clarify in what extent such an availability is an asset for the related countries in getting better selling performance. While advocating for a better exploitation of the cotton price information, we are quite aware of the pitfalls in trying to compare prices from cotton of various origins which are traded according to diverse commercialization systems. Comparing cotton prices is not an easy task as it is founded upon the hypothesis that the compared cottons are exactly similar according to the buyers' criteria which is quite difficult to assess for an external observer. This is nevertheless feasible for internal observers, through confidential approach. We think that this should be done for this is the only way for a country to refer its performance to its competitors and to identify means and ways to move towards improvement.

We are not going to implement such price comparisons between countries but, through limited number of examples of information processing, to point out the market signals that could help cotton exporting countries in managing their competitiveness.

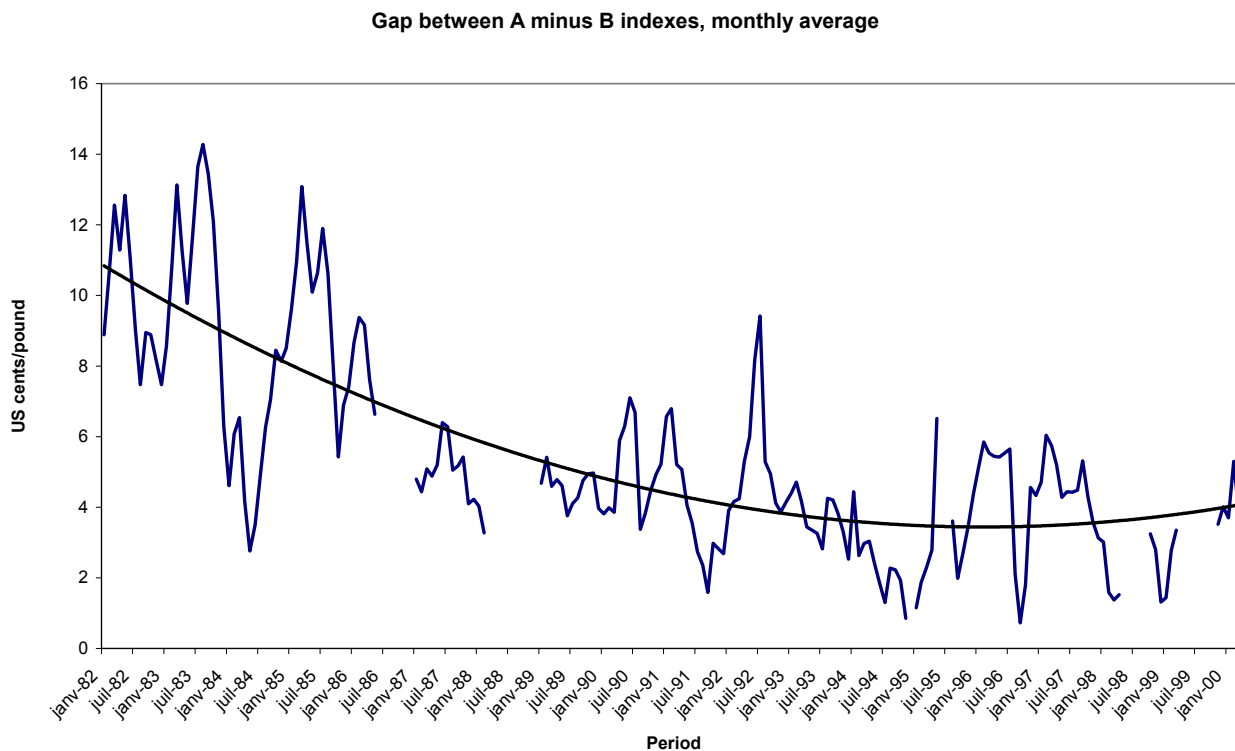
2. A signal in the decreasing gap between A and B indexes?

The existing gap between A index and B Index (which pertains to a shorter lint) is engaged into a decreasing trend from the mid-1980s onwards.

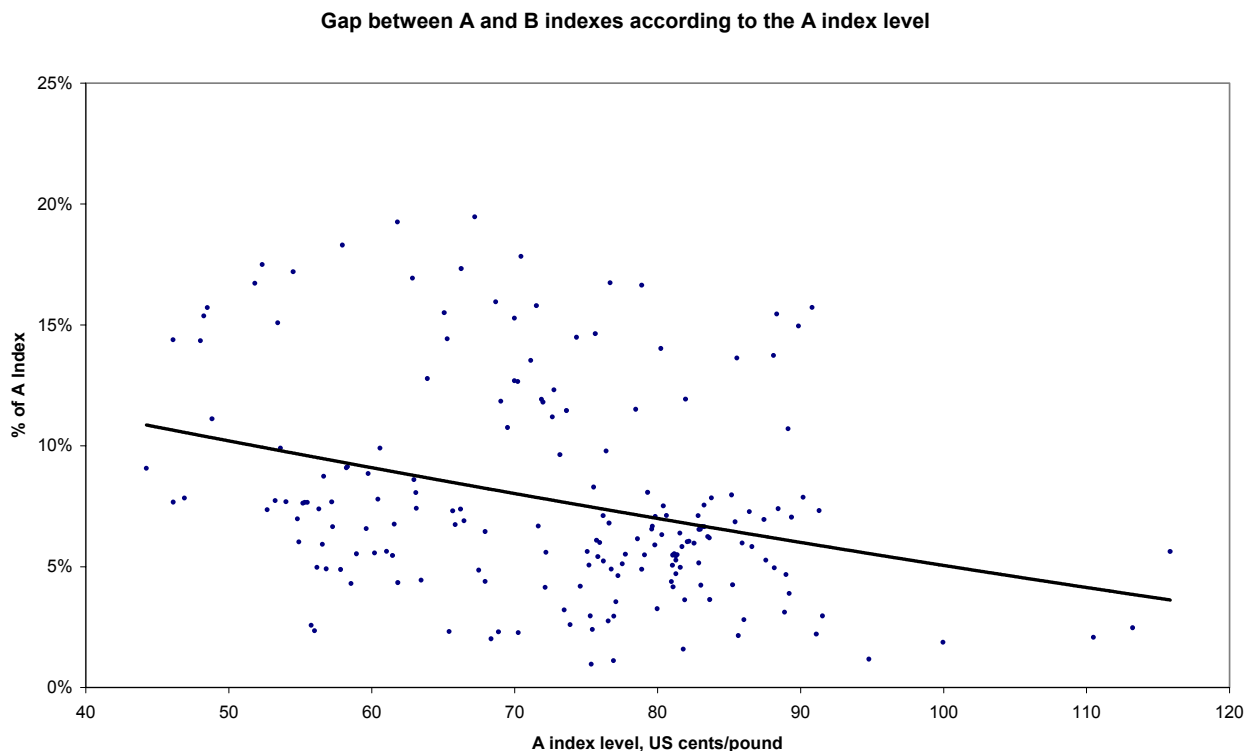
This gap has reached a value as high as 14 cents/pound, but it is no longer higher than 3-4 cents/pound or even lower than 1 cent/pound in some months (Graph 2). Certainly, this gap is fluctuating, one can suspect some negative relationship between this gap and the A Index level, although such relationship is not as tight as one may think (Graph 3).

Such gap reduction could be interpreted as a risk for some cotton growths, in particular for those which are at the lowest end of the A index basket, to be pushed out the A basket into the B basket. Certainly, this risk may sound limited as the B basket refers to shorter cotton lints, one should however remember that the lint length of the cotton growth constituting the A basket could evolved and it has reached the current value of $1\frac{3}{32}$ only in 1972 onwards.

Graph 2



Graph 3

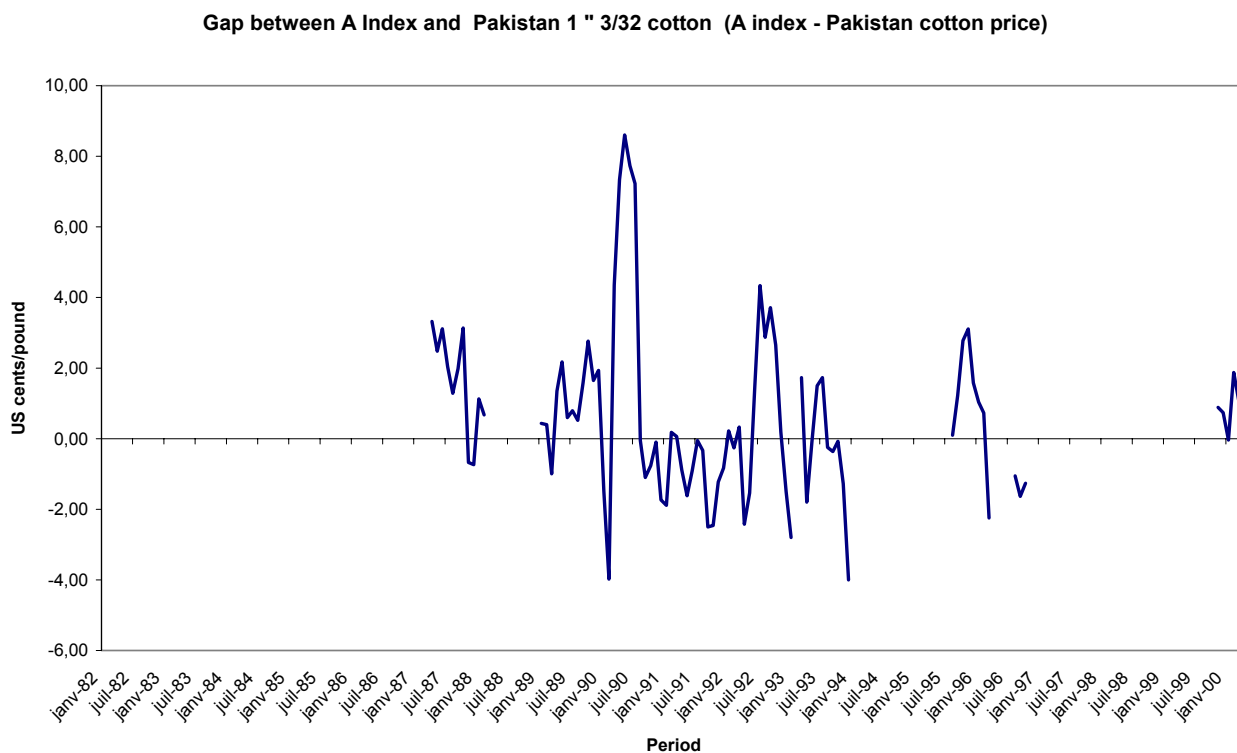


3. Learn from lessons of countries that have improved their cotton market value

The fear of falling into the B basket is not a recent one. Till the end of 1980s, such fear was known as the risk of getting one's cotton becoming "pakistanised", as Pakistan cotton was assumed to be representative of the B Index cottons.

We would like to warn against any attitude consisting in associating Pakistanese cotton to a cotton of lower quality and shorter length.

Graph 4



Pakistan has offered cotton of 1³/₃₂ length since 1987 at prices which are promising in the face of the A Index values (Graph 4). This country could hardly be only considered as a short length cotton lint provider although longer lint cotton remains little available internationally likely in connection with the increasing internal demand.

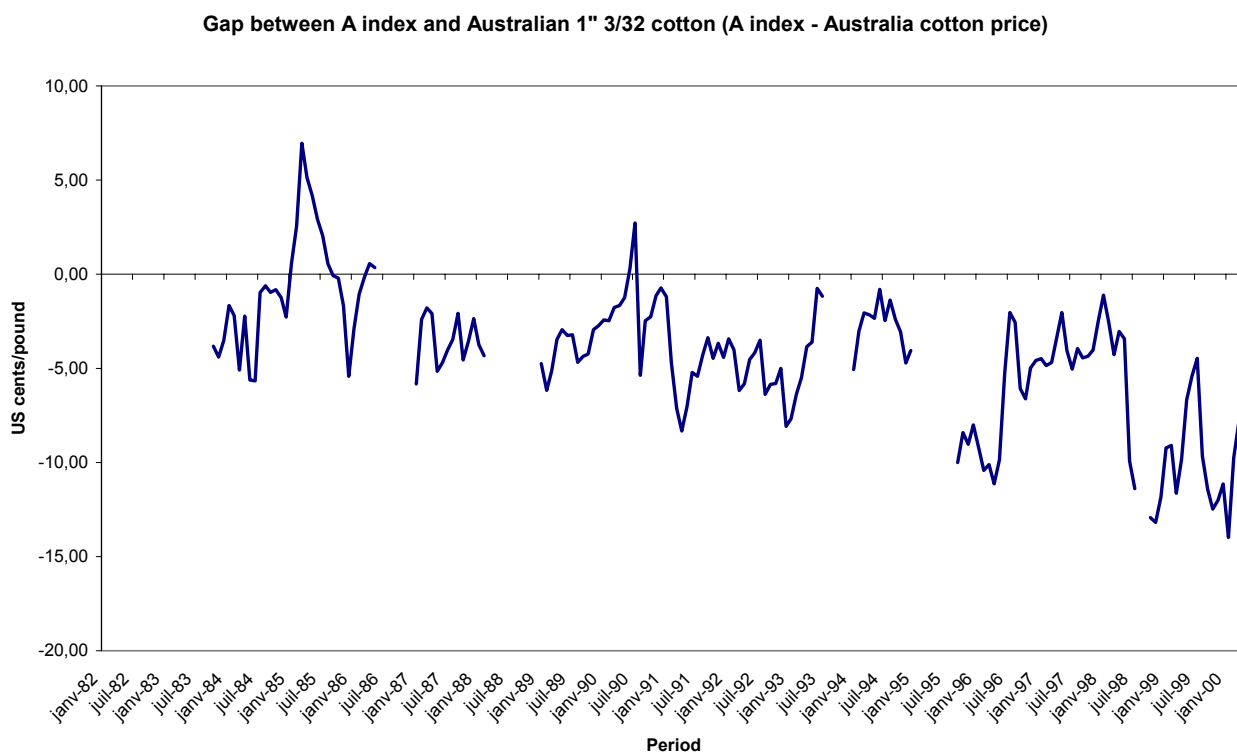
Each cotton exporting country must then wonder whether its cotton remains well appreciated enough by its buyers. In this sense, the Cotton Outlook information about the composition of the five growths that contributes to the A Index is a good indication.

For sure, Australia has not to worry about this issue as its cotton, in the opposite, has gained a comfortable and increasing premium in the World market during the recent period (Graph 5).

Referring to the last 4 years, the Australian cotton has got an average premium of 5-15 cents/pound while it was lower than 5 cents/pound during the preceding ten years. The negative relationship between such premium and the A Index level seems to be quite clear. The Australian cotton seems to be less penalised when the World market is bearish (Graph 6), this confirms that a positive image of one's cotton is of particular impact in case of unfavorable market.

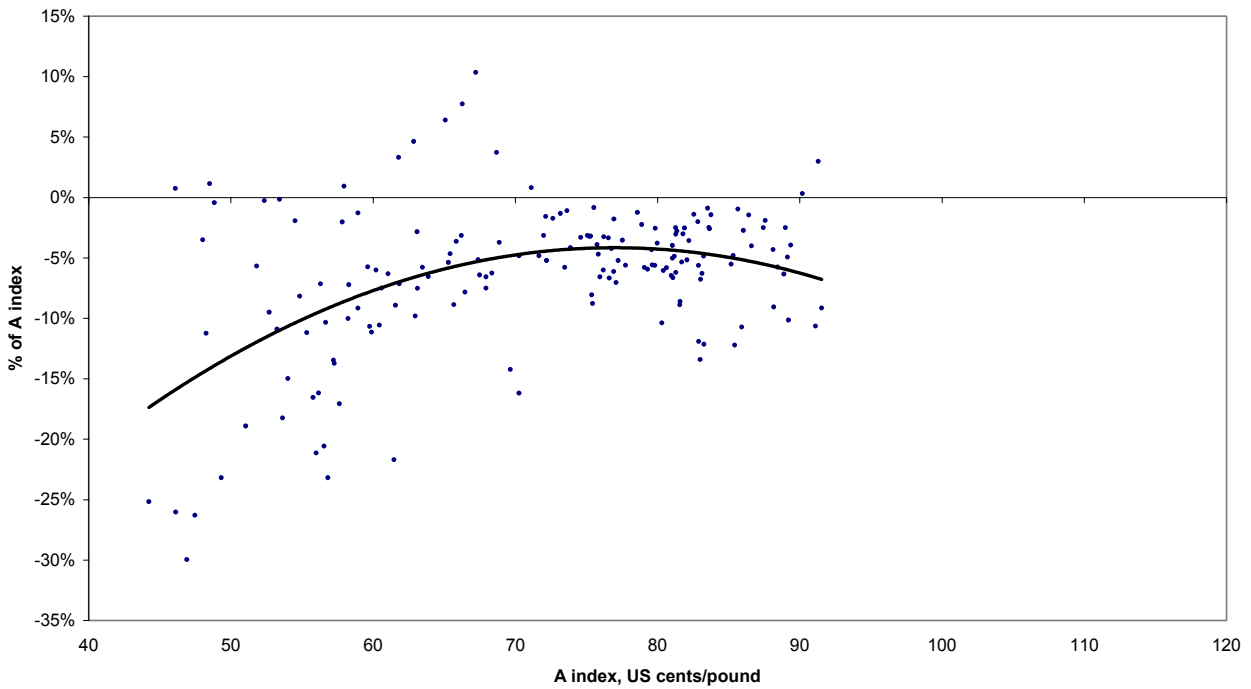
The reasons that lead Australia to gain such premium could be very diverse : more efficient trading policy connected to special credit offered to importing countries (with some help from the Government), objectively better lint quality, advantage of being closer to the main importing countries...It is worthwhile for each cotton exporting country to be more informed on this issue and to learn from the Australian lesson in order to identify procedures of improving its exportation performance.

Graph 5



Graph 6

Gap between A Index and Australian 1" 1/32 cotton according to A index level



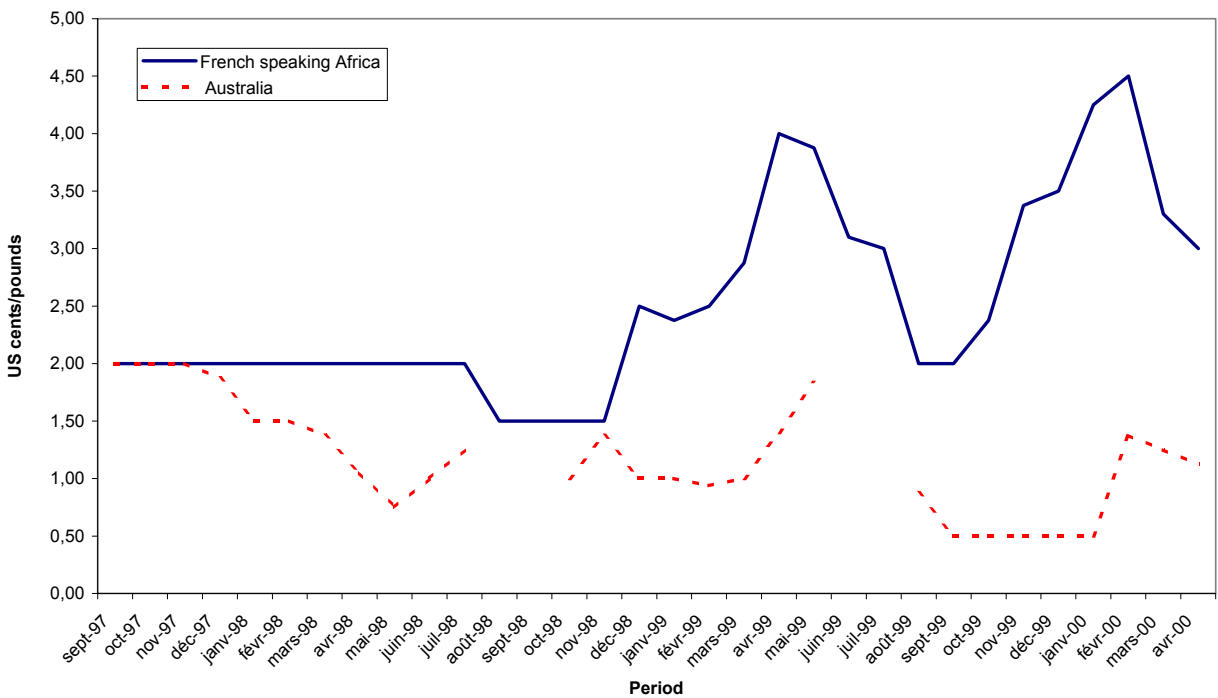
Globally speaking, the cases of Pakistan and Australia sustained the fact that there are countries that have achieved in improving the market appreciation of their cotton, necessarily (as an effect of communicating vessels) at the expense of the countries which have not conducted similar actions.

4. Is the market expecting for cotton of longer lint?

Finally it makes sense to observe that Australia and French speaking African Countries have started providing 1"1/8 cotton at the same period, from september 1997 onwards (Graph 7).

Graph 7

Price gap linked to lint length for 2 cotton growths (price of 1"1/8 - price of 1"3/32)



It comes out that the price gap in favor of longer lint is far more attractive for the cotton from the French speaking African countries in comparison to the Australian cotton (2-4 against 0.5-1.5 cents/pound). There is also a clear trend for this gap to become even higher.

Furthermore, such gap seems to be higher for the African cotton when the A index is low while the relationship is rather reverse for the Australian cotton (Graph 8).

Our analysis tends to show that, in the case of the studied African countries, the market is expecting longer lint from this countries. There is rationale to check whether similar signal is provided to other countries. In case that our analysis is correct, there is need to foresee adaptation measures to help satisfy the world market. Obviously, one would think about growing new cultivars giving longer lint. One should not overlook however technical practices that enable to reach longer lint nor to revisit the ginning processes that may diminish the ginning outturn and the the lint length.

Graph 8.

