TURKISH MILLS RETURN TO THE MARKET

BRAZIL PLANTING OF 2019 SECOND CROP BEGINS

VENEZUELA: COULD A TEXTILE/APPAREL BUSINESS RETURN

CHINA/US TRADE TALKS CONTINUE BUT BIG DOUBTS REMAIN

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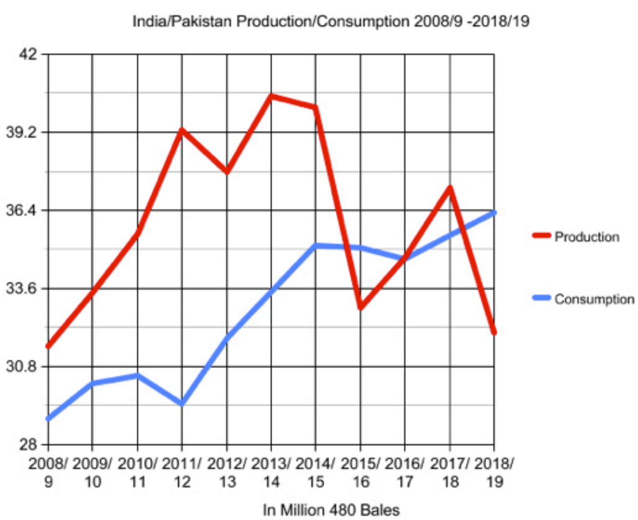
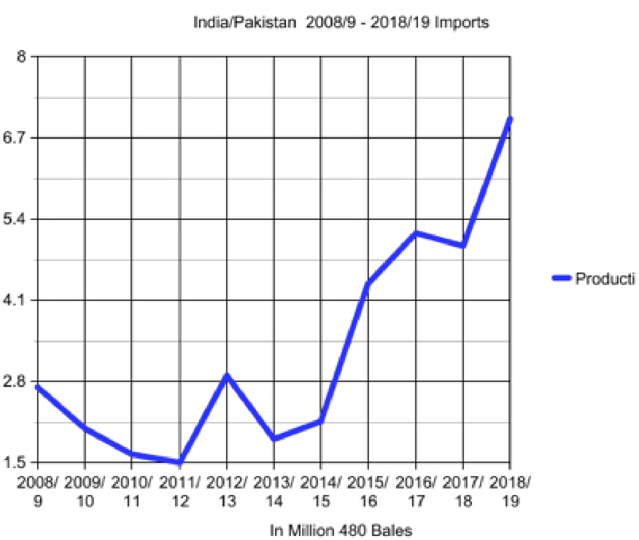
SUBCONTIENT IMPORT DEMAND INCREASES AS CROP SHORTFALL GROWS





The 2018/19 crop season was not good in India and Pakistan due to poor quality BT cotton seed, and due to the monsoon failing to provide the conditions necessary for a successful crop. Yields in both regions fell sharply in 2018/19, and this lower production is happening at a time when cotton use in the region is holding better than expected, as US retailers seek alternatives to China. US retailers are under significant pressure to develop a supply chain outside of China, and there appears to be serious risk that 25% or more import duties on future shipments could be applied, including even shipment embargos.

Given the reaction of equity markets shareholders, they are not willing to show much mercy on companies that are not preparing. These conditions are allowing sourcing agents to show more flexibility in securing a reliable supply chain. Thus, cotton use in both India and Pakistan is expanding and will likely reach record levels in 2019/20, despite the global weakness. Chinese exporters will be more affected by the weakness in Europe. Both markets are very price sensitive importers and always seek value. The attraction of long staple SLM color grades from the USA and other destinations has added to the attraction of imports, as basis offers have been very aggressive.

In Pakistan, the final 2018/19 crop arrivals appear set to fall 800,000-one million bales (local) from 2017/18. This is occurring as cotton use may exceed estimates, and it could push cotton imports to 3.5 to 3.6 million bales. The US is expected to be the largest supplier, followed by Brazil, Greece, West African, Turkish and Argentina. The contraction of cotton production in Pakistan is reaching a crisis stage, as output continues to erode, falling sharply from the 2011/12 highs. Behind the fall are several factors. The major issue is the lack of profitability of the crop due to a poor yield that has its roots in poor quality seeds.

The seed sector has been plagued by fake seeds and by the use of outdated BT seed technology. New current BT seed technology is needed, as is a reform of the seed sector. The sector has been faced with poor rainfall, inadequate irrigation infrastructure, and technology challenges. The new government has faced a host of challenges brought on by their need to arrange emergency funding to pay for imports and the expanding debt under the Chinese Belt/Road projects. It has, however, moved quickly to eliminate the duty on cotton imports, which has aided the apparel sector.

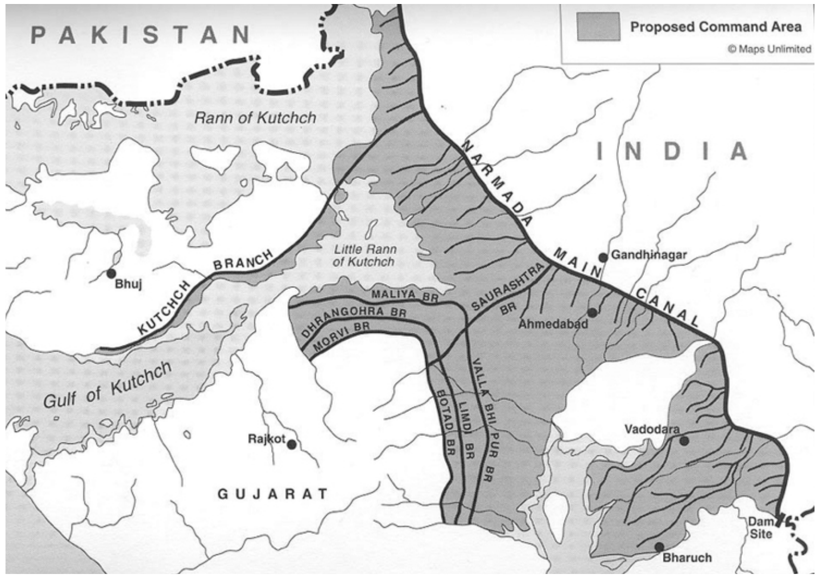
Pakistan's average cotton yield has failed to improve over the past ten years, and yields during the past several years have been down sharply from the 2014/15 highs of 782 kilograms per hectare. Again, the poor quality of the seed and the lack of improved irrigation infrastructure are behind the stagnation. The 2018/19 average yield is expected to reach only 670 Kilograms per hectare. The lack of an increase in yields has pushed growers to sugarcane, which has provided better returns. The quality of the lint has also failed to improve, with quality issues occurring each season, along with the problems associated with contamination. There are major influences from the environment, but the quality of the lint begins with the seed. India is also now experiencing similar problems.

Imports by Indian mills have been light so far, because credit limits are restricting forward purchases, because of the Rupee/USD weakness, and because the 2018/19 Indian crop continues to move. The much smaller Indian crop and the high MSP has also limited mill buying of domestic cotton. The very long staple, SLM color grade US styles are attractive due to the discounted basis and cheaper freight to the southern Indian mills. India is facing a sizeable crop shortfall as well, due to the decline in yields and the poor performance of the 2018 monsoon. One difference between the 2018 collapse in production and other seasons is that it has been focused in Gujarat, and the problem was not tied to the pink bollworm.

One of the great mysteries of 2018/19 will be, "What happened to Gujarat's irrigation supplies?" Gujarat has been the leader in cotton production for years, with the state's expanding irrigation scheme a model for the rest of India. However, the events that unfolded in 2017-2019 raise a lot of questions, all of which revolve around, 'What happened to all the water that was in storage at the time of the December 2017 state elections?" By the time the 2018 crops were planted and needed water, special police forces were put in place to prevent farmers from taking water from the Narmada main canal. The Narmada irrigation scheme is crucial to providing irrigation water to the Kutch, Saurashtura and northern Gujarat, the center of the state's cotton acreage. Thus far in 2018/19, these three areas have provided 93% of all cotton deliveries.

The Gujarat state government has invested billions to expand the Narmada irrigation network. The Saurashtra Narmada Avtaran Irrigation project was launched in 2016 with phase 1, which included 58 km of pipelines to 10 dams connected to the Narmada canal network. This will provide irrigation to 47,943 hectares in the Jamnagar, Rajkot and Morbi districts. Overall, the Gujarat cotton crop depends on rainfall, but irrigation has become important and the source of the highest quality upland cotton production in India.The 2018/19 season was marked by the lack of irrigation supplies.

At the heart of the large irrigation project is the Sardar Sarovar Project on the Narmada River, which is called the lifeline of Gujarat. The water level at the dam was reported at a record level of 128 meters in December before the Gujarat state elections. However, by the summer of 2018, no water was left, with dam levels below the minimum of 110.63 meters. The state government called out police to guard the Narmada main canal to prevent farmers from taking water. Speculation is that the water after the elections was diverted to urban and industrial users.



Since that time several major corruption scandals have come to light around the irrigation scheme. The Gujarat state government was forced to shut down a state company established to finance and set up irrigation farm ponds because of financial irregularities. Significant problems also surfaced with the state's scheme to clean irrigation ponds and canals. These problems all occurred at the same time, in which 67% of the state's districts recorded a rainfall deficit in 2018.

These conditions have set the stage for much speculation regarding the size of the 2018/19 Gujarat crop. New crop arrivals, as of December 31st, have totaled only 3,553,520 170 kg bales, which is far short of the 8.0-8.8 million bale estimates. Many growers have already destroyed plants and delivered the crop. Ginners are operating at reduced capacity and reported to be losing money. It appears unlikely that crop will reach the Trade estimates, but the exact size of the crop is difficult to determine, because of the deliveries to Gujarat gins from Maharashtra. The shortfall will have major ramifications for imports and lead to a halt to exports. Strong export demand early in the season has been noted from Pakistan, Bangladesh, and a smaller volume from China. The supply of the higher quality Shankar-6 lint from Gujarat is already in short supply.

The final size of the Indian crop appears poised to fall to the 30-32 million 170 kg bale level or 23.4-25.0 million 480 lb. bales, which is down sharply from the last USDA estimate of 27.5 MB. A crop decline of that magnitude sets the stage for record imports, with stocks drawing down to minimum levels. The imports are likely to come at the end of the global 2018/19 season, and continue through the arrival of the 2019 Indian crop.

Credit tightness is also likely to limit forward coverage. US and Brazilian styles are expected to be the main styles, given the firmness in the West African basis. Any West African discounted lots will be taken up quickly. With Indian imports of up to a possible 3.5 million bales, the combined strength of India and Pakistan means that this region may rival China for commercial imports (outside of Reserve purchases).

CHINA BELT & ROAD CORRUPTION APPEARS TO INVOLVE TEXTILES AND APPAREL

Corruption in China's Belt & Road scheme has been in the headlines since the discovery of the massive corruption in Malaysia, which included spying on journalists. A new scandal, which directly involves textiles and apparel, has been exposed in the EU, and centers around the Greek port of Piraeus. China was quick to capitalize on the Greek financial and EU debt crisis. During the outbreak of the crisis, the Chinese state-owned global shipping and port company, COSCO, entered the scene in 2008, purchasing a 35-year lease on container terminals 2 and 3 at the port. Then, in 2016, it took control of the port, increasing to a 67% ownership stake. This investment was part of a Belt & Road plan to expand into Europe. China's COSCO is a state-owned company, one of the largest in the world, with ownership in many key ports, including

Zeebrugge, Belgium's second largest port, Spain's Noatum port, as well as a minority interest in the third largest container port in Turkey.

The EU has revealed that Piraeus Port was at the heart of an illegal scheme run by unnamed Chinese companies to allow apparel and footwear from China into the EU without payment of duties or VAT taxes. The scheme was quite elaborate and involved local truck drivers, fraudulent documents, managers, false declarations, etc. The scheme ran from January 1, 2015 to May 31, 2018, and the EU is fining Greece 200 million Euros for failing to stop the scheme. COSCO, the owner of the port, was not mentioned in the EU action even though it owned and managed the port.

Collectively the European Union is the largest customer for Chinese textile and apparel exports in the world, and any ability to avoid duties and VAT offers exporters a significant price advantage.

"MADE IN CHINA" IS GOING OUT OF STYLE WITH US GROUPS

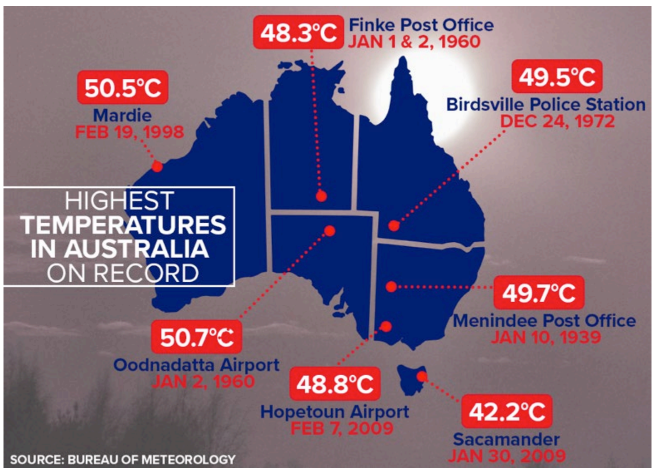
The headlines from companies at a major conference in the US were that "Made in China" was going out of style with US manufacturers, brands, and retailers. The theme of the conference focused on companies explaining how they were modernizing their supply chains with a much-reduced reliance on China. The reasons were tied to risk management, as we have been discussing, and companies now must manage political, economic and logistical risk in their sourcing.

This will be the theme of 2019, as the shock of 2018 continues to impact profitability. One major US outdoor brand announced that many of its products will be made in the Philippines by the end of 2019, ending its near total dependence on China. The pressure by China on US multinationals operating there is increasing; the latest demand is that they must now refer to Taiwan as part of China in all its materials. This demand was issued to 66 multinational firms last week, including Apple and Nike.

Evidence is also surfacing of Chinese apparel companies accelerating the moving some of their operations to locations that will be unaffected by the trade war and have favorable trade arrangements with the US. The first locations to benefit are those that are mainly cut and sew, which require only the shipment of Chinese fabric to the local zone. They receive a Made in BLANK label, and are sent off to the US. One location that is drawing rapid Chinese investment is the Egypt QIZ trade zones that were set up in 1996, but are drawing new interest. These zones were part of a peace process between Israel and Egypt. If 10% of an apparel product is made in Israel and then finished in Egypt, its qualifies for duty free entry to the USA. Egypt is a hot spot for Chinese firms since wages are cheap, at less than 100 USD a month, and the access to the US market makes it a cut and sew center. Shandong Ruyi, the largest textile and apparel group in China and the world, announced a new factory in the Suez Canal Economic Zone. 46.7% of all Egypt's exports to the US come from QIZ benefits. Exports of textiles and apparel to the USA in the January-October period reached 841.879 million USD, which was up 12.05% year to date. Li & Fung is reported to have set up new focus on sourcing in Egypt.

Jordan is also drawing Chinese investment interest because of its access to the US market with duty free entry. In the same period, Jordan exported 1.298 billion USD of textiles and apparel to the US. The export of knitted and crocheted apparel is the number one export for the country. In 2017, it exported 1.5 billion USD of knitted and crocheted apparel with 1.33 billion going to the US. The base of much of the apparel is man-made apparel, which accounted for more than 75% of all 2018 exports. Jordan is an important ally of the US in the Middle East and has a free trade agreement with the US, which affords it duty-free access even when using third party fabric. The country's apparel industry was born with the QIZ agreements and then expanded under the free trade agreement. Jordan imports most of its fabric. In 2017, it imported 225.4 million USD of fabric from China and 22.6 million from Turkey. Jordan also imported apparel for its domestic market from China and Turkey. Overall, in 2017, fabric was the country's ninth largest import at 515.1 million USD. A Chinese group just announced a new cut and sew operation in the southern part of the country. Taiwan was the earliest investor in the country.

AUSTRALIA'S HEAT WAVE CONTINUES, BUT COOLS AS WEEKEND BEGINS



The southern NSW cotton belt of Australia continued to experience record heat, with some places reaching 45C/113F on Friday. Such heat has made it extremely difficult for growers to meet their water needs; boll shed is an issue. The northern areas of NSW and Queensland have been hot, but in the 39 - 40C range. A cool front is expected Sunday, which is forecast to bring temps back to normal. Dryland crops have never experienced such heat, and the fear is yield losses could be serious. The debate over water use is continuing and will likely be at the center of a new election at some point. The rural sector faces a difficult challenge of educating the politicians on both sides about the real issues. At this stage it appears that the will to really address the water problem does not exist. Some farmers are considering setting up small test operations in the Northern Territory or Western Australia's new agriculture zones, because of the availability of reliable water and expectations that a gin will be built soon.

The early picked Queensland crop appears to be yielding well, but below the previous records. Most trading activity appears quiet; the 2019 crop is bid at near 1100 points on May futures, but no selling from growers is evident. Even the merchants are not placing big bids for the 2020 crop, as there are increasing fears regarding just what will be the available volume. Final 2019 water needs will finish off all water supplies until it rains. A satellite photo on social media showed that the vast water storage reservoirs of the famous Cubbie Station were dry. The industry faces significant challenges for the 2020 crop, not only concerning production but also what new polices will be forthcoming for the management of irrigation supplies. One of the biggest 'Big Wets' in history is needed to replenish the system.

The requirement that Shandong Ruyi reduce its ownership from 80% of Cubbie Station to 51% has so far not occurred, and it's back in the news. When the Chinese group led the purchase, it agreed to the reduction in ownership in 3 years, but it was extended in 2016 until 2019. The drought has reduced interest in the sale, and it remains to be seen how the government will handle any additional extension. The volume of water allocation owned by Cubbie is also a focus of the press, as news outlets want to know the foreign ownership level of water rights.

It remains unclear where Chinese buyers that normally depend on Australian cotton will turn for additional 2019 crop needs. The CFR basis levels on the small SJV Acala crop has dropped as a result of the Chinese duty on US cotton to levels near par with Australian. The duty remains the issue. No comparable Brazilian or other machine picked cotton is available.

TURKISH MILLS RETURN TO US COTTON AS BASIS DISCOUNTS EXPAND

The Turkish economy appears to have at least stabilized, and the Lira/USD exchange rate is now back at 5.3 per USD, which is close to the crisis low of 7.2362. US relations are better, but volatile, as the Syrian war solution remains a difficult issue. The Turkish textile and apparel sector appears to have made it through the darkest days of the crisis, with exports providing the cushion when the Lira's collapse provided a boost. Cotton spinners seem to have used up all inventories, moved to take up the remaining local supplies, and now reentered the markets for imports in some volume. Local supplies are now at a premium to international values after falling to sharp discounts, which moved a large block of cotton to export. Importers are focusing on the very aggressively priced US 41/42/52 color grade, long staple lots that are presently heavily discounted. Turkish mills are well experienced with US cotton and can always utilize discounted US lots. The volume of US cotton sold during the past 30 days is unknown, but has likely exceeded 100,000 bales. The purchases could also mean that steady offtake may continue through the end of the season.

Turkey apparel exports for 2018 reached 17.6 billion USD, and combined textile and apparel exports reached 26.1 billion USD which reflects an increase in shipments from 2017. Europe has taken more than 70% of all exports, but the USA has moved up into the top ten markets. Turkey is in an excellent position to take business from Chinese exporters. Its modern, fully integrated operations can offer US brands and retailers a turnkey solution, something they have been used to with China. Turkey is also expanding apparel exports to Russia with shipments up 48% year to date. The improved apparel exports bode well for cotton use, and domestic yarn has replaced imported yarns since the crisis, which is helping domestic cotton use to rebound. The volume of cotton exports has also increased the deficit in supply, which should help maintain demand for the discounted US styles through the end of the season until new crop moves. Turkish buyers will remain very price sensitive as margins remain an issue.

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BRAZIL: ALL FOCUS ON SECOND CROP COTTON AS RAINS ARRIVE

Mato Grosso's soybean harvest was moving rapidly in dry conditions before rains arrived. This past week, 12.3% of the soybean crop was already harvested, with rapid progress in the North. Rains are now forecast for the next 7 days or longer across Mato Grosso, which will slow harvest but provide a considerable boost for the second crop cotton which follows. IMEA still forecasts that 937,786 hectares will be planted to cotton, with a large block being first time acreage. CONAB has acreage slightly higher. The first full season crop is developing quite well. Local press reports are warning first time growers to focus on the crop, which is a much higher input crop than corn. Beneficial rains are also expected across the Bahia cotton belt, where most of the crop has been planted. El Nino conditions have raised concerns about the reliability of the 2019 weather. The heavy focus on the second crop will add new risk to the 2019 crop in Mato Grosso.

Brazil is a Federal Republic, and each state has its own set of complicated tax policies. The taxes differ in many cases based on if a commodity or product moves within Brazil or goes for export. Many states provide an incentive to move products to export. Mato Grosso's finances have always been a bit difficult to understand and have been impacted by many scandals, especially under the Socialist administrations. Each state collects an ICMS tax and has regulations on the rebate of a portion of that tax (kind of a VAT) if products are exported. This is complicated, and it leads to cotton sold for export being exported at times when domestic prices offer a higher price because of ICMS rebates. In 2000, Mato Grosso introduced a FETAB tax on the key commodities of cotton, soybeans, cattle, wood, and diesel. The purpose was to allow money to go to the development of infrastructure in the state, which would aid the agriculture sector and housing. Now it appears that, due to the financial condition of the state, the FETAB is being expanded both in the amount of the tax and in where the money goes. The largest increase in the FETAB tax appears set to be placed on cotton headed for export. The percentage charged on soybeans will go up slightly, but cotton will face a large increase. The amount of the tax paid will affect the ICMS rate.

The tax is set to be optional to the taxpayer, which we don't understand. What happens if the payers opts out? In any event, the dire finances of the state say that only 30% of the proceeds will go to transportation needs, 10% to state projects, and 60% to the treasury of the state. Cotton appears to be facing the greatest increase, as the state attempts to benefit from the current export boom. The proalmat tax incentive for cotton will increase the ICMS for cotton from 3% to 4.8%. Cotton is estimated to provide 250 million Real to total tax revenue. The rate of the tax per ton has been calculated at 290 Real a ton, which at todays exchange rate is about 77.00 USD a ton, or about 3.5 cents a lb. It would appear this change is headed toward implementation, but in the past the agribusiness lobby has prevented efforts to heavily tax agriculture products. The fact that much of the increase is focused on cotton and not soybeans may make for easier passage. Mato Grosso is expected to produce a record cotton crop in 2019/20.

COULD VENEZUELA HAVE POTENTIAL FOR NEW CUT AND SEW OPERATIONS; THE HUNT FOR AN AMERICAS SUPPLY BASE IS UNDERWAY

Venezuela has plunged into the economic abyss while the world sat by watching. No longer though, as the US and Brazil have combined to exert leadership necessary for a new Venezuela. In the US, Senator Mark Rubio of Florida has been a staunch advocate for change in Venezuela and last week he convinced the Trump administration to act. It appears the US's effort was also in conjunction with the new anti-Socialist president of Brazil. This marked the first time Joint US/Brazil cooperation moved to solve a Latin American crisis. First, the US announced it was recognizing Venezuela's opposition leader, Juan Guaido, as the interim President of Venezuela. Within a few hours, Brazil followed suit and recognized the interim President, saying it would provide political and economic support for the country to return to democracy. This was a watershed change, as Brazil was once one of the strongest allies of Hugo Chavez, who started the whole Socialist nightmare in 1998. Canada soon followed and recognized the new leader, along with several other countries. Venezuela went from being the richest economy in Latin America to the poorest, with 90% of its population today living in poverty. The country's economy is worse than that of Syria, which has endured unending civil war, with their GDP falling 15.7% in 2017.

The extremely poor condition of food supplies in the country suggest that the US and Brazil should provide a joint massive aid package. In the US several sources are available for such aid, with commodity stocks plentiful and cheap.

Venezuela once had a booming textile and apparel sector and has experimented with growing cotton in

the past. One major effort was launched in 2012/13 by a textile group to grow cotton in rotation with corn and soybeans, similar to what was quite successfully practiced in Mato Grosso. The project never gained traction when the country collapsed. The once booming textile and apparel sector collapsed early in the Socialist period, with the country depending on imports from Columbia and China. At one time, several major US brands had plants operating there. The Hugo Chavez régime attempted to revive the industry with state ownership. In 2005, he launched a major revitalization effort from Tinaquillo. However, today that plant is abandoned and in ruin. Later, he opened the largest textile plant in the country, with a 41 million USD investment in Maracaibo, which has also failed.

Venezuela has nationalized almost every sector of the economy, from the oil sector to agribusiness. One estimate reports that the 511 official state-owned companies lost 129 billion USD in 2016. The government also seized unproductive farmland and redistributed it, like Zimbabwe. It took over the largest cattle farm in the country, 494,000 acres, which was owned by a British meat group. Some companies were paid for the seizure of their property after launching international court cases, while others were paid nothing or received only a fraction of their commercial value. It is unclear how the massive number of seizures would be handled with a new government.

The US apparel industry is seeking new sourcing bases, and so far a viable production base in the Americas has been missing. The lack of security in Mexico and other factors has kept it from evolving, which has limited investment. CAFTA has been a big success, but political unrest in the region is limiting its potential to grow. This leaves the opportunity for other regions. First, Venezuela has a good location, with its wide coastline on the Atlantic and short transit time to the US providing a logistical advantage. Secondly, it borders Columbia and Brazil.

Columbia has a free trade agreement with the US, and a developed but small textile and apparel sector. Brazil is now an ally of the US and is seeking a secure Venezuela on its border to stop the flow of refugees and to end socialism in the region. Brazilian textile and apparel companies have lots of expertise and are eager to reassert themselves. All this combined suggests that the beginning of the new Venezuela and the start of US/Brazil cooperation raise the possibility of significant new opportunities. The hurdles will be sizeable, with the corruption that has become widespread, the collapse of infrastructure, and management of the debt left behind to China.

Between 2007 and 2014, China lent the country 63 Billion USD, which has been partially repaid in oil. One estimate has the country still owing China just less than 20 billion USD, and it is unknown how it is secured. Many loans have already been written off. No details of the loans have been made public, and none were approved by the legislature, which means they may be null and void. China has also had market access, which it purchased, and has been supplying almost all consumer goods and textiles and apparel to the market for some time. Despite these economics, China has not provided any food aid as the economy has collapsed. It is unclear how much of the loans have gone to the corrupt military officials and others who run the Madero administration.

The collapse of Venezuela has pushed wages, in USD terms, to some of the cheapest in the world at 20-30 USD a month. This gives the region a low starting point to be competitive in wages. It is a major oil producer, which gives it the potential to provide cheap electricity to industry. The work force is intelligent and ready to work. Over 10% of the country has left the country, but some of them would possibly be willing to return to invest and work. Over the next several months, with a complete fall of the current Socialist administration and the establishment of new election and government, the talks about adding Venezuela to the CAFTA trade pact with special terms, and with a regional trade pact, are likely to start taking shape.

It is in the US interest to aid returning the Venezuela to economic health. A stable, prosperous country could aid in bringing Central America back to stability. For the US industry, an alternative to Chinese sourcing is needed, and from a logistical standpoint a regional supply hub is top priority. The potential for innovative cooperation between the US and Brazil, along with Columbia, gives the potential of a regional supply base great promise. For cotton, the country's local industry at its peak consumed 325,000 bales, so today, as a regional production base, the potential is for consumption to reach a million bales or more, with the fabric capacity the largest hurdle. Any such regional supply base would have to have firm safeguards against the import of fabrics from non- approved partners.

CHINA COTTON IMPORTS IN DECEMBER MUCH STRONGER THAN OTHER AGRICULTURE COMMODITIES

China imported 220,000 tons of cotton in December, up 116% from a year ago. The full breakdown of origins is not yet available, but we know Brazilian cotton played a major role based on the Brazilian shipment data, as did Australian. Total 2018 cotton imports reached 1,580,000 tons, with 600,000 tons of that total in the September-December period. Soybean imports in December were weak in comparison. Cotton yarn imports in December were also strong at 160,000 tons. One motivation for the imports continues to be the import by traders of cotton into port warehouses, where spinners can take up on an as-needed basis.

NOT ONE MAJOR CHINESE AGRICULTURE PURCHASE ANNOUNCED SINCE DEC 1 TRADE TRUCE –WHY?

The final 30-day period before the US/China trade truce is scheduled to end is drawing close, and not one sizeable purchase of US agriculture products has been announced by China since December 1st. We are simply shocked at the total silence on both sides despite the December headlines, "China Will Begin Purchases of US Agriculture Products Immediately." If indeed China did agree to this, they have failed to live up to their obligations in what would appear to be any legitimate way. They have not even respected the promise by negotiations. On the other hand, did the US side take a token commitment to resume buying US agriculture products as needed, and attempt to exaggerate the affect? The Chinese have not moved to lift the 25% import duty on any US agriculture product, but only purchased a small volume of US soybeans for the Reserve. This behavior suggests the latter theory. It is really discomforting that the US side did not achieve a more specific result, given the importance to US agriculture. Now, as the negotiations continue, we do not hear of any movement by the US to achieve a side deal on US agriculture, or on addressing the trade deficit, or a separate longer-term attempt to deal with the structural issues.

No one has confidence, as the US/China trade talks garner confusing, conflicting headlines; one hour state progress is being made, while an hour later they are miles apart. Last week, rumors would spread, only to be later refuted by the Trump administration. The earlier reports that China had proposed a buying program to balance the trade deficit have not advanced, with at least one former WTO official saying that any such preferential buying program would violate WTO rules. This, of course, drew a laughable response since the WTO has failed to enforce any rules against China in agriculture products. It remains extremely unclear if any deal can be reached, as China does not appear to be moving to really address Washington's concerns.

It is still unclear how a trade deal can be reached when China continues to exert hubris on the global front, causing great harm to good will. China continues to issue threats against Canada, even arresting Canadian diplomats and denying access. This action has been followed by several threats against Canada, even though they have been one of the more pro-China countries in the world. As if this wasn't enough, last week China arrested a well-known Australian writer visiting China. This was a direct insult to Australia and the USA. The writer was an Australian citizen of Chinese descent who was living in the US. If you cared about good will, what is to be gained by such a move. China clearly believes it is above any international law or accepted norms, and has no respect for any citizen of Chinese descent from any country. It has also offered some rather weak arguments justifying the continued detention of over a million of its on citizens in Xinjiang, and has continued its crackdown on Christians as if no one is watching. Then, it continues to threaten Taiwan, despite the US/Taiwan defense commitment.

On the US side, the total dysfunction caused by the Democratic Party control of the House and their failure to be willing to deal with the Trump administration on almost any issue has given the Chinese pause in the security of any agreement. For example, the same group of radicals said they do not approve the Mexico-Canada trade agreement already signed by all parties. Despite the ramification of such a move, they still obstruct. Many are suggesting Trump provide Congress with notice that NAFTA will end. The sheer ignorance of disrupting US agriculture trade to Canada and Mexico by failing to approve the agreement should be very troublesome to US farmers and agribusiness interests. The Democratic Party's unwillingness to provide additional funding of a border wall, something they have supported until now, has been drawn into the China/US discussion. An editorial in the South China Morning Post last week said that Beijing was monitoring the Border Wall debate to see if Trump would fold or stand his ground. Thus, the final fate of a trade deal may even hinge on the outcome of this debate.

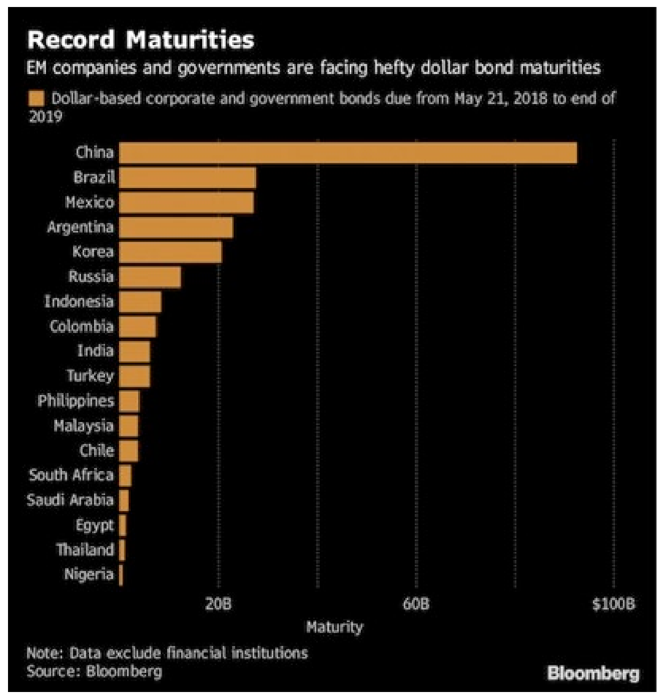
For cotton and US agriculture products, the lack of a side agreement for assured access suggests very uncertain times ahead. China's COFCO was the third largest exporter of soybeans from Brazil in 2018, which highlights a massive increase in volume over the last few years, and illustrates the new relationship in sourcing soybeans. Regarding cotton, Brazilian cotton in the second half of 2018 rapidly replaced US Cotton, as the sourcing relationship has changed. With no assured access agreement, the US faces major issues. Yet there has been nothing but silence from the US Trade as to the serious repercussions from the failure to obtain this access.

COTTON PRICES GO NOWHERE AS TRADE TALKS AND CHINA'S SLOWING ECONOMY UNDERMINE CONFIDENCE

The cotton market has seldom, if ever, seen a time when so much uncertainty faced world trade and consumption. For at least the past 20 years the world has become accustomed to China as its growth engine, and no one viewed a China/US conflict as a real threat to world trade. 2019 has brought an entirely new set of revelations, and many of what were assurances are simply no longer true. For the first time global economists are voicing their concerns that China's economic growth has been overestimated, which means the size of its economy is not as big as estimated. This has led to an attempt to review China's balance sheet, raising fears that the much-discussed 3 trillion in FX reserves has been fully committed or is now overcommitted after a major global spending spree since 2013. Giving these estimates, there is some credibility in the slowing in overseas spending and in Belt/Road commitments.

As it relates to cotton, this can be seen in the behavior of China largest textile and apparel group. In 2017 and 2018 the company went on a global acquisition spree, spending billions on the takeover of major fashion icons and making record commitments to new Belt/Road projects. At one time it appeared there was no limit to their access to cash. At the peak of the buying spree, the CEO and founder purchased a 33.5 million AD Mansion in the influential Sydney Point Piper area. Now, here in 2019, the company has delayed the completion of a very small cash injection of 16.5 Million USD in an Israel apparel brand located in the UK, stating the lack of approval of Beijing. A new deadline later in 2019 has been set. The group receiving the capital injection has planned to use the proceeds to expand manufacturing in Ethiopia, where China has invested and loaned billions along with Chinese companies in building a new apparel hub. This suggests that the MOU spending billions on a new textile mfg. plant and cotton-growing plantation in Nigeria may now be in doubt.

Against this backdrop, the financial sector is becoming skeptical about the new issuance of massive debt by China through such different instruments as perpetual bonds, which do not have a repayment date. Another interesting revelation was the fact that Chinese companies issuing bond debt were buying their own debt to increase the impression of demand. This is raising fears over the true economic condition of the country. No true assessment of the funds spent or lost since the turn back to State Capitalism in 2014 are available. At the same time, record expenditures and liabilities have occurred through the Belt/Road, State crackdown on internal security, the re-education of one million people in Xinjiang, or the massive South China Sea building spree of artificial islands, along with the military build-up of these islands. The lack of transparency makes all these discussions occur in the dark without the true facts. In China, this is undermining confidence and causing the consumer to become much more cautious, which means they tend to hold on to cash and spend less.



Strong demand for the heavily discounted US cotton has provided support to ICE futures during this period. However, the rally stalled just ahead of the 75 cent area in March, as demand is unwilling, for now, to follow the market higher. With future Chinese demand in doubt and lack of access to the Chinese market for US cotton, buyers feel no reason to worry about future supplies. In many cases, spinners have demanded basis concessions for volume offtake. At the same time, Merchants are fearful of building large basis long positions in such an environment. The news is not all negative however. As we have discussed in this issue, the import demand from Pakistan and India is likely to reach a record in 2018/19, which will absorb global and US supplies. Moreover, Turkey seems to have stabilized, and its mills have returned as cautious buyers.

The US government shutdown means no one knows the exact level of sales and shipments from the US.

However, data from Australia and Brazil suggests the US could dominate sales until new crop movement. US export shipment volume is important, and the markets do not know how much the shutdown and slower CCC loan redemptions have impacted the rate.

Adding to the spinner's unwillingness to chase price strength is the expectation that a larger US crop is coming, which will add to the export burden. The size of the increase is still a subject of great debate. Overall, the market is transfixed on a successful Chinese/US trade deal, and the confidence of such an event is a moving target. The US has not openly talked about assured access for US agriculture products or its importance. Instead, the discussion to the farm sector has lacked specifics and been tied to generalities, with more focus on the success of passing a farm bill and making sure US farmers got access to the aid granted for losses tied to the China trade dispute. There has been almost no mention of the importance of volume sales to China in 2019. Surveys are showing near 86 million acres will be planted back to soybeans in the US despite the full bins and lack of access to China. This is setting the stage for very uncertain times in 2019/20.

As we said earlier, the market needs to retain the current, very featureless range in the near-term, and allow the US to move additional volumes to export, while the price level also will allow cotton to compete against man-made fibers. The man-made fiber sectors, despite all their issues, are not going quietly into the night. Just last week an executive of the industry was in India forecasting the sectors growth in 2019 and the new investment in a refining complex in east India, which would produce MEG and PTA and would boost consumption in the cotton stronghold of India. This is occurring at a time when India already faces a crisis with polluted and poor air. Despite the issues caused by the man-made fiber sector, cotton is not being aggressive in calling these things out and offering alternatives with cotton. Cotton needs innovation and aggressive marketing.

For now, spinners' greatest risk is in securing the needed supply of Middling and above color grades in the longer staple upland styles. These should be taken up ASAP when offers are found. Supplies will be very tight until the 2019 US and Brazilian harvest. Growers should discuss with their risk management advisors maintaining floor prices for the 2019/20 crops, which face the most uncertainty in years.

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