MARKETPLACE INSIGHTS

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Good afternoon, ladies and gentlemen.

Again I am honored to have the opportunity to once again make a presentation to the Beltwide Conference. It has always been the highlight of my year's speaking engagements.

Every year is certainly different, and this season is no exception. However, we have really not experienced the fireworks of the past two seasons, but this season is a long way from being over, and many different factors are present that were not there during the past two years.

As normal, I will talk on U.S. and world supply and demand for 1996-97 as I view it today. Second, I will project the 1997-98 scenario under today's conditions. Third, I will then take a stab at prices for the next eighteen months; and fourth, I will close with a few comments on imports, which have created so much controversy over the last ten months.

Last year I said in my speech that I didn't think I was qualified to speak, after watching cotton prices for the previous twelve months. However, this season I think I am reasonably qualified, because cotton prices have behaved in a more rational manner.

Two years ago in January I said the U.S. would run out of cotton in August, unless prices went high enough to ration demand; and this happened as prices rose to $1.17. This past season again we would have experienced an unprecedented rise in cotton prices in May and July of 1996 if it had not been for imports. The imports last spring and summer put a lid on prices and gave the American Textile Industry a chance to survive with additional quality and quantity.

Let's now look at the U.S. supply and demand scenario for this marketing year.

In August, USDA said the crop would be 18,577,000 bales, and the industry guesses were way off base with USDA. In September USDA said the crop had dropped to 17.9 million bales, again off base with industry projections. The reality is that many of us in the industry were fairly accurate on the crop size we projected in September; and finally in December the government is adjusting to our number.

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In fact, after we missed the government's September number so badly, I asked our Economic Department to quit spending money on our crop surveys, because we couldn't come close to the government. In October and November we made our educated guesses and were closer to USDA.

Whether we are right or wrong at Dunavant with our numbers, the market is going to temporarily trade USDA projections, and that is a fact. I think all of us will admit USDA certainly has more tools at its discretion to make better projections than the industry, but many times those tools are used in an unusual way.

Anyway, the final USDA crop number will be 18.8 million bales to slightly higher; domestic consumption will reach a level of 10.9 million bales; and exports will be 6.4 million bales. Currently U.S. export registrations are nearly 4.5 million bales, so we have to register approximately 2.3 to 2.5 million more bales to reach our number of bales shipped of 6.4 million bales. Remember, we historically must sell 400,000 to 500,000 more bales than export registrations, for history has proven that we normally will carry that many bales of export sales from one season to the next. Imports this season will be 400,000 bales, and most of those came into this country in August, September, and October. When you put all those numbers together, the U.S. ending carryover will be between 4.5 and 4.6 million bales, compared to 2,610,000 bales the previous season. These numbers are quite different from the last two years and certainly tell me imports will not be on the agenda for the balance of this season, even with a quota available of 6 million plus bales.

Now let's look at the world conditions as they exist today, because production in the world has not been nearly as favorable as what we experienced in the U.S.

We think final world production will be 86.3 million bales versus USDA's number in December of 85,930,000 bales, and we think final world consumption will be 84.3 million bales versus USDA's December number of 85.3 million bales. Our sources tell us that consumption is still lagging around the world.

When you adjust these numbers, the year ending world carryover will be 36 million bales, versus USDA's December number of 36,960,000 bales. Remember, the world carryover this past season was nearly 34.2 million bales, so there are no dramatic bullish conditions present today. The USDA will release new numbers on Friday, and, in my opinion, they are going to show a considerably higher world carryover than our Dunavant numbers, probably in the neighborhood of 1.5 to 2 million bales.

What we are experiencing in the world today is a tightening of world supplies of very high grade cotton. Central Asian Republics have traditionally been producers, particularly

Uzbekistan, of very high quality cottons, and this season that volume and their quality are substantially reduced.

In April forward we probably will have some tightening of the basis in high grade cottons. However, Australia is on track to produce a record size crop of 2.6 to 2.8 million bales, and they are traditionally a high quality producer. This could tend to ease the pain in the spring.

China is not rearing its head to be a bull in the cotton market, and I do not think they will emerge this season as a bull. Internally they have very high priced local cotton to use and have also increased substantially manmade fiber consumption. The only purchases, to my knowledge, that China's Central Government has made are of C.I.S. cotton, because it, at the time, was much cheaper than U.S.

Currently we think China will import a total of 2.1 million bales in the world, and 1,025,000 bales will be from the U.S., and today the U.S. has 728,000 bales registered on sales to China. Practically all of these sales are to joint venture mills or provincial governments. In my opinion, they must work off their inventories of locally produced cotton, in which they have between 90 cents and $1.12 invested. Their own cotton is primarily used by their state owned mills.

Our company in the last few days has sold cotton to China for joint venture mills, which we did not think we would sell until late spring, so evidently there is a little more needed by joint venture mills than I had anticipated.

We think China's final crop this year will be 17.6 million bales, and consumption will be 18.8 million bales. USDA in December was carrying China's cotton production at 17.5 million bales, and we are close to that number. However, I think on Friday USDA will increase China's cotton production and lower China's cotton consumption. If USDA makes these adjustments, and we do not agree that they should, then we think they will readjust production lower and consumption higher in the months ahead. They are carrying China's cotton consumption at 19 million bales, and we are also very close to that number. If our numbers are correct, then their year ending carryover will be between 15.5 and 16 million bales.

Now let's look at 1997-98 intentions as I view them today, both in the U.S. and around the world.

We certainly have a different equation in the U.S. than we did a year ago as we look at the price of competing crops, and this will be a major criteria for how much cotton will be planted in the spring.

Last season on March 1st corn prices for September delivery were nearly 3.27 per bushel, and soybean prices for November delivery were about 7.30 per bushel. These prices definitely affected cotton acreage last spring prior to planting time.

Today, ladies and gentlemen, corn prices for new crop are nearly 2.59 per bushel, and soybean prices are 6.65 per bushel. This is a major change from last year's conditions, because on March 1st, corn and soybean prices were quite a bit higher than they are today, and this had a direct impact on cotton acreage. On this date last year December cotton was trading at 76.50, approximately where it is today. With our new Freedom to Farm Bill this will have direct impact on what is planted.

Before talking about new crop acreage for cotton, let's look at the offtake picture to see what will be needed next season.

I think domestic consumption will escalate to 11.1 million bales and exports will rise from 6.4 to nearly 6.9 million bales, for a total offtake of 18 million bales. At this time for 1997-98 I do not see imports as a factor affecting U.S. cotton producers. I have said the final U.S. carryover will be between 4.5 and 4.6 million bales this season, so that is our starting point of supply for next season.

We think next season we will plant 13.8 million acres in the U.S., and that number of acres with a 650-pound yield and a 5 percent abandonment will produce 17,750,000 to 17,850,000 bales, which will reduce next season's carryover to a level of between 4.3 and 4.4 million bales.

Again, we need to study the world projections for 1997-98, because that will be the final determinate of prices next season.

We think planted cotton acreage in the world, based on 76.50 December futures, will generate 83.7 million acres in the world, versus 84.1 million acres last season **--** a very, very slight decline. We project that acreage will produce 87.3 million bales. We project world cotton consumption next season to be 86.8 million bales. We must, and I have said this for two years, have a sharp rebound in consumption of cotton for me once again to really get pumped up on cotton prices.

Based on the above assumptions, the world carryover in 1997-98 will be 36.5 million bales, compared to our number this year of 36 million bales. You must remember that the world perceives 76.60 cent December cotton as a very satisfactory level to continue cotton production.

Next season we project China will produce 18,350,000 bales and consumption will probably be no more than 20 million bales. Remember, when you deal with China, it is always projections.

As we all know, China has had some unpleasant experiences on yield, but I think it is getting better, and this will be a factor in their new crop plantings. Just as in the U.S., the price of competing crops is going to be the major factor, but not as major as it is in the U.S.

Now that we have examined the 1996-97 production and consumption and made projections for production and consumption in 1997-98, let's step out on a limb and talk about what we may all expect in cotton prices if my projected numbers are accurate.

Before making price predictions, let me say on a long term basis our company has had an excellent track record, but trying to predict what prices will do on a daily or weekly basis, I think we rank as the worst in the world. Obviously, we are long term merchants and traders who experience from time to time a considerable amount of short term pain.

Will there be fireworks in cotton prices during the balance of this season? March cotton is trading today at over 74 cents and I believe it will trade between 73.00 and 76.00 between now and March expiration. We still have millions of bales of producer selling between here and 80 cents. However, I think there is a substantial support level below 74 cents, basis March, and the U.S. and foreign textile mills are there to fix prices on any pullback.

As I said earlier in my speech, the world is talking about a shortage of high grade cottons because of the quality problems in Uzbekistan, and maybe this will be true, but today there is an abundance of better quality cottons for quick shipment. Remember, we have a very high quality West Texas crop this season with a tremendous amount of 3134 and 2134 and better cottons with no sugar content. Part of the problem last season was high sugar content in the West Texas cottons, which made the cotton spin very poorly and caused major problems. This does not exist in Texas or Arizona this season.

Even if we export my projected 6.4 million bales, as I have said, our numbers show a year ending carryover of between 4.5 and 4.6 million bales in the U.S. If I am wrong, and we export 6.9 million bales -- 500,000 bales more -- we still have a carryover of 4 million bales, a very adequate carryover compared to the previous two years' 2.6 million bales of carryover. Also, the world carryover with additional sales of 500,000 bales will be 35.5 million bales, an increased carryover from the previous season. However, a very important point for all of us to remember is that the exportable supply in exporting countries is going to be tight in the out months of this season, and this is what could make prices fairly firm during the spring and summer. The U.S. and China are the only countries who are going to be building carryovers.

One word of caution for producers who have not fixed their prices for this season is the ten month loan, which we haven't had until this season. If loan stocks reach a level of 5 million bales, then at the end of ten months, this cotton will be coming to market and could really hammer prices in July if demand is not roaring and we are not having major problems with the new crop.

What prices do in May and July is going to rest on two factors. First, what quantity and quality of crops do Australia, Argentina, Brazil and Paraguay produce in the Southern Hemisphere, which will be harvested in April through July; and second, and very importantly, what kind of U.S. and world crops do we get planted in the spring of 1997?

If we experience average textile business and normal plantings and harvesting in the Southern Hemisphere, the price is going down in May or July. Conversely, if there are major problems during that period, the price is going up for old and new crop.

Today, for the next sixty days, I think we are trapped in a range of 73.00 to 76.00, basis March futures, and in April we will have to take another look at the conditions that exist.

Based on current conditions, if I were a producer, I would have all of my old crop cotton sold within sixty days.

Now let's talk about the new crop price scenario. December 1997 is now trading at 76.60, and I said earlier that if we plant 13.8 million acres in the U.S., the U.S. carryover will be 4.3 to 4.4 million bales, only a slight decline from this season's level of 4.5 to 4.6 million bales. If it is economical, I would be hedging from 77 to 80 cents, basis New York futures, for new crop.

I am shocked how little new crop cotton has been priced, looking at the new crop situation and prices of competing crops. You know 77 cents is not a bad price looking at soybeans at 6.65 per bushel and corn at approximately 2.59 per bushel.

Looking back over the last few years, there always seem to be a window to fix prices at a higher level sometime during the crop year. Fortunately for all of us, speculators seem to drive markets higher and lower than what is realistic and, if and when they drive them higher, you should capitalize on fixing your new crop prices.

Remember, last year in some of my speeches I said producers should be fixing prices from 78 to 80 cents, and prices rose three to four cents higher than that, and yet Dunavant Enterprises had less U.S. cotton fixed this past October than at any time in many, many years.

The world's cotton production is going to be at least stable with the prices of new crop cotton today.

To sum it up, I am not bullish more than a few cents to the upside for this season's crop, and I would be selling or fixing if I had cotton unsold. Remember, it costs about 100 points a month to carry a bale of cotton and three months from now if the market goes up three cents, you haven't gained anything and you run the risk of a lower market, because of supply in the late spring and early fall. There can be a window of higher prices for new crop with problems in the spring, but I would be hedging on a scale up and play the average.

Before closing let me talk about imports, because it is a tender subject with both producers and textile mills. Yes, imports kept prices last season from running away to the upside. Our company has been severely criticized by producers and ginners for bringing in foreign grown cotton last season.

A number of mills in the U.S. textile industry came to us in the spring of last year and asked us to please find a substitute for U.S. cotton because of price and quality. We produced in the Memphis Territory and Southeast last season an over abundance of high micronaire cotton and also West Texas and Arizona cotton had a high sugar content.

Many of those cottons went to the futures contract, which also tended to press prices lower, as well as imports. We brought foreign cotton into this country for one reason, because our customers demanded it, and it was perfectly legal under the existing farm bill. It is hard for me to understand how we can come under severe criticism when we are trying to serve our textile mill customers.

There have been import quotas triggered since April 6, 1995 and there still is a quota for approximately 6.5 million bales. Is the quota too large? The answer is a definite yes. We do not need the kind of volume that has been triggered. However, the only way to change the quota system is to open up the Farm Bill in Congress, and, my friends, this today is very dangerous.

The American Mills do need a vehicle to import when quality or quantity is in jeopardy, and this happened last spring. It was not our company's fault.

Also, it is my opinion it is going to be an unusual occurrence when volumes of foreign cottons come into this country, as happened last season. The American Textile Industry would much prefer U.S. cotton over foreign cotton and will definitely pay a three to four cent premium.

Last spring foreign cotton was six to twelve cents cheaper than U.S. cotton, and imports became a reality. Our company had foreign cottons sold for November/March delivery of this season, and just recently we cancelled the portions and substituted U.S. cotton. I promise you they want your cotton -- not foreign cotton.

One of the good things that came out of the imports was it gave the U.S. Mills a chance to maintain cotton consumption during some difficult times. I strongly believe last spring and summer if our mills had not had imports, domestic cotton consumption would have fallen in the summer and early fall. Mills would have increased manmade fiber blends and some would have just cut back their production.

I can assure you that anything that looks like dollar cotton loses big money for the U.S. and world textile industries. Maybe that will change in the years ahead, but, in my opinion, not in the next few years.

As usual, thank you again for giving me the opportunity to express my feelings on these very important subjects.