MARKETPLACE INSIGHTS
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Good morning, ladies and gentlemen.

As I have said in previous years, it is always an honor to have an opportunity to share my thoughts and feelings with the producer segment of the National Cotton Council. I said last year producers were experiencing difficult times, but in my career in the cotton business I cannot ever remember a time when all seven segments have been under the pressure of financial strain and uncertainty that we are currently experiencing, and I cannot yet see the light at the end of the tunnel.

You as producers have experienced incredibly low yields on most of your acreage this season and the quality of this year's crop has been a disaster. Last year I talked about the Asian economic crisis and its impact on the Asian textile industry, and today the Asian disaster has come to the United States in the form of cheap textile imports, which are cutting into U.S. cotton consumption and are directly affecting your markets. Textile imports coming into the U.S. are predominantly produced by foreign grown cotton, not U.S. cotton.

U.S. export sales have come to a screeching halt because of the expiration of Step 2 funds, which occurred on December 14. We are now non-competitive to the tune of four to eight cents. I want producers to monitor U.S. export sales and domestic consumption over the next six months, and you will get the feel of how important Step 2 funds were to U.S. cotton competitiveness at home and abroad.

Today I will go through my traditional thoughts in four areas, and close with some comments to try to stimulate your thoughts on what the future may hold.

- First, the current U.S. supply-demand and carryover projection for the U.S.
- Second, the current world supply-demand and carryover prospects as I see them today.
- Third, what are the current acreage, production and consumption expectations for the U.S. and world for the 1999-2000 marketing year with new December trading at 64.45?
- Fourth, what are my price projections for the balance of this season; and then I would like to discuss price potential for 1999-2000.
- Fifth, I would like to close, as I said earlier, with some thoughts on what is needed for the cotton industry for the future.

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USDA projected in December that the final U.S. crop would be 13,452,000 bales, and I think the final number on the crop today will be very close to 13,700,000 bales. The Texas, Georgia and North Carolina crops have all grown since the last USDA report.

I think domestic consumption will not be more than 10,400,000 bales versus USDA's number of 10,600,000 bales. The loss of Step 2 funding will definitely impact domestic consumption. In my opinion, U.S. exports will struggle to reach a level of 3,900,000 bales, even though there have been 3,950,000 bales registered for export. I think there will continue to be cancellations of our U.S. sales as shippers try to switch their sales to cheaper foreign growths. Remember, USDA is carrying our exports at 4,300,000 bales, which I don't think is attainable as long as we are not price competitive.

The other part of our carryover equation is, what are imports into the U.S. going to be?

USDA says we are going to import 400,000 bales, and I believe the final number for this crop year will be close to 400,000 bales. The quantity would not be that high if we had produced normal quality in the U.S. this season. A substantial number of bales will be imported because of the shortage of really high quality cotton.

Remember, we have registered 3,950,000 bales for export and have shipped 2,470,000 bales through December 31st. Export shipments in December were phenomenal because of the scramble to ship cotton and collect Step 2 funds before they expired. Later in my comments I will share my thoughts on future Step 2 funds.

Last season we exported 7,600,000 bales and, in my opinion, as I have already said, that number will be dramatically reduced this season for two reasons – non-competitive prices and continued very poor textile business abroad.

We started this season with a carryover of 3,900,000 bales. If we produce 13,700,000 bales, consume domestically 10,400,000 bales, export 3,900,000 bales, import 400,000 bales, then our U.S. carryover will only drop to 3,700,000 bales. It is important to point out that USDA is carrying our projected carryover at 2,800,000 bales, which today I believe to be definitely on the low side. Cotton futures prices today are reflecting well in excess of a 3,000,000 bale carryover.

Now let's look at the world numbers as they begin to shape up for this season.

We started the season with a world carryover of 38,900,000 bales. As always, our Dunavant numbers are a little different than USDA numbers. We think world production will be 83,400,000 bales and world consumption will be

83,900,000 bales, versus USDA numbers of production at 84,200,000 bales and consumption of 85,800,000 bales. We continue to believe that cotton consumption in the world will not rebound in the short term, and that there can be another wave of problems in Asia during 1999. I believe that improvements will occur, but over a longer term rather than shorter term.

China continues to hold huge carryover stocks, but as yet have not put a volume of cotton on the market at a competitive price. Yes, China sold last May about 250,000 tons, or 1,150,000 bales, at a then competitive price, but a very small percentage of that cotton has found a home in the world markets. It is reported that these cottons are quite old and have colored up substantially from age. It is my opinion that if U.S. futures prices get back to sixty-eight cents, that China would aggressively try to market additional cottons in volume. We think China this season will produce 19,000,000 bales and consume 19,500,000 bales, and their carryover stocks will be reduced to 15,300,000 bales versus last season's carryover of 16,700,000 bales.

Yes, China would like very much to sell cotton in the world markets, but they would sustain huge losses because of prices they have paid the producers over the last six years. The Chinese government as yet is not willing to bite the bullet and suffer those tremendous losses. Some of the Chinese cottons are of very good quality, particularly out of the Xinjang province. It competes with any premium cottons produced around the world, but bale sizes are very small, weighing approximately 200 pounds.

China continues to be very quiet on importing cotton. The central government is not permitting import licenses in any volume and are forcing Chinese mills to spin Chinese cotton. I strongly believe that China in the months ahead will continue to import only a small volume of foreign cotton. We peg China's imports this season at only 500,000 bales versus last season's number of 1,800,000 bales.

China, as other Asian countries, also has a problem with an oversupply of manmade fiber, and China has an excess capacity to produce manmade fiber. The price in China for manmade fiber is currently under forty cents a pound.

For us to achieve and maintain any major rally in cotton prices, I believe the Chinese have to permanently reduce their stocks. They will be a threat to higher prices until their stocks decline substantially.

Australia again has planted increased acreage, and the crop has the potential with normal weather to produce 3,300,000 to 3,400,000 bales, versus 3,150,000 bales last season. This will be another record crop for them. Remember, they produce in Aussie dollars and sell in U.S. dollars, and the Australian cotton farmer continues to make high profits with lots of yields of three bale cotton.

Argentina has reduced their cotton acreage this season by approximately 25% because of their disaster last year in quality, quantity, and price.

As I discussed last year, the U.S. has developed new markets for U.S. cotton, predominately Mexico and Turkey. The U.S. has currently sold 1,440,000 bales to Mexico this season versus last season's 1,277,000 bales at this time. We think Mexico will ultimately only import about 1,250,000 bales this season versus 1,500,000 bales last season. Even though I just stated that we had registered 1,440,000 bales, we think there will be about 200,000 bales cancelled or rolled into new crop before the end of the season.

Over the last six months Turkey's textile industry has fallen into a deep recession. They consumed 5,200,000 bales last season and their cotton consumption this year will be fortunate to be 4,200,000 bales. They purchased 635,000 bales of U.S. cotton last season and will only purchase about 80,000 bales this season. The reason we have not sold a similar volume of U.S. cotton to Turkey is declining textile business – and the prices of U.S. cotton compared to foreign growths have been higher.

There are still sufficient bales of cotton to meet demand for the balance of this season. However, by summer some of the real high grade cottons could be in short supply, especially if Australia does not produce a high grade crop. The following countries still have a volume of cotton for sale – West Africa, Central Asia, Australia, Greece, Syria and Turkey. I have not named China, because, even though they have volume, they are not price competitive.

When you put all the numbers together, the world carryover will drop from 38,900,000 bales last season to 38,400,000 bales this season – a step in the right direction.

Now let's examine the potential U.S. and world cotton acreage, production and demand for 1999-2000.

We feel that U.S. cotton acreage for next season will be 13,200,000 acres with the potential of producing 17,000,000 bales using historical averages. You might ask, why will that many acres go into cotton with December cotton trading at 64.45? In my mind there are two answers: the prices of competing crops – corn, soybeans and wheat – are very low at this time, and I think the eight to ten cent P.O.P. for this year's cotton will give producers encouragement for cotton. If we had made normal yields this season, cotton farmers with the P.O.P. payments would have fared quite well versus competing crops.

We think the domestic textile industry will consume 10,800,000 bales next season versus 10,400,000 bales this season; and exports will rise to 5,500,000 bales versus 3,900,000 bales this season. Of course, the export number could change dramatically with additional Step 2 funds for new crop and prices can also respond to competitiveness. If these numbers prove correct, then the U.S. carryover for next season will rise to about 4,400,000 bales -- not a bullish number.

As we all know, what the world produces and consumes for 1999-2000 will have a major impact on U.S. and world prices. We project the world will produce 85,000,000 bales next season versus 83,400,000 bales this season, and consume 87,400,000 bales next season versus 83,900,000 bales this season, leaving the world with a carryover of 36,000,000 bales at the end of 1999-2000 crop year. Again, we are moving in the right direction by reducing the world carryover.

I projected last year at this meeting that the world carryover would drop to 35,000,000 bales this season, and today we are projecting the world carryover to be 38,400,000 bales -- a decline, but not to the extent I anticipated. A year ago it was difficult to predict how deep the Asian crisis was going to be, and it is not over yet.

Again, I do not see China being a robust importer next season, and I also think they will reduce cotton production to 17,000,000 bales versus this year's number of 19,000,000 bales.

As always, I will now share my price observations for the balance of this season and projections for 1999-2000. Today March cotton is trading 60.36, and this looks cheap until you compare the price of U.S. cotton with foreign cotton. We are not competitive today because the $701 million dollars of Step 2 funds are exhausted, currently we are selling high grade C.I.S. cotton, landed Asia, at 60.00, and for the same bale of Texas high grades, we would need 66 cents.

However, none of us can accurately assess price movement until we see what direction we are headed in the spring in the discussion and formulation of new farm legislation. New legislation could have major price implications.

I think all of us recognize that Step 3 for imports will kick in about the end of February or the first of March. I think in excess of 200,000 bales of imports have already been committed to the U.S. The growths already involved are Greek, Chinese and C.I.S. It is certain that until foreign supplies are depleted, that these cottons, with a U.S. import quota open, will keep U.S. prices from having any major rally. I did not say U.S. prices can't rally, but I see no possibility for a major rally.

We must also recognize that the speculator and commodity funds are 20.1% short, and if they decide to cover, we could see prices temporarily rise two to three cents.

We must also monitor the world price in the Liverpool index. The world price seems to have reached bottom or near bottom, but I don't think with economic conditions that exist, that there will be any rapid rise in world price in the next two months – a potential modest rise, but a rapid rise is not in the cards. I believe until March futures expire, we are in a trading range of 58 to 63 cents.

Now, let's look at the price potential for the 1999-2000 crop. If we do not reopen the current farm bill in the spring, then it is very difficult to be bullish on new crop looking at the projected U.S. and world numbers of supply, demand and carryover. Remember, March cotton is trading today at 60.36, and we only produced 13,700,000 bales this season, and we are projecting a crop of 17,000,000 bales for next season, and December is trading at 64.45. Under that scenario it would seem you would want to fix prices on new crop, but I think it is too early. I would not recommend any grower hedging his new crop at today's price level. There are just too many question marks for the future, especially with potential legislation in the spring.

The one point that I strongly believe is that cotton options are more important in your marketing strategy for the future than they ever have been. If there is no new legislation, and conditions remain fairly stable, I would recommend at some point buying out-of-the money puts. Conversely, if we were able to obtain new Step 2 funds to make us competitive at home and abroad, then I would want to own out-of-the money calls. Under no circumstances would I fix my new crop price at today's December level until the picture becomes clearer.

In closing, I want to recommend an improved farm program for cotton that works for all seven segments. I understand that there is no program that works perfectly for all of us, and there must be give and take. This past season it has been hard for any segment to give when the situation dictated you take for your financial survival.

The primary objective is to maintain the marketing loan for cotton in any new piece of legislation.

Secondarily, I strongly support additional Step 2 funding in 1999-2000 for the future to make U.S. cotton competitive at home and abroad. However, I cannot support Step 2 unless it can be maintained for a full marketing year. To allow funds to be exhausted in the middle of a marketing year makes no sense and creates uncertainty in our ability to be competitive at home and abroad. Remember, I said earlier we had committed for export 3,950,000 bales and 2,200,000 bales had been shipped when the certificates expired. There is room for a lot of financial hurt when a shipper, a mill or a cooperative makes its sales 8of cotton or yarn, figuring a ten to twelve cent payment, and he ends up with zero.

Another feature that should be in new legislation is some type of mechanism that allows imports when they are needed, but a safeguard where, if we need 500,000 bales of imported cotton for quantity or quality, that the door is not opened for two million bales. I think the psychology that is created under those situations is not healthy for our industry.

I believe that new legislation for cotton must have a marketing loan, Step 2 payments, and some type of improved import regulations, and if we obtain these goals, the cotton industry will be improved for the future. I personally have been a huge advocate during my cotton career for a free market for cotton. If you look around the world and examine our competitors, there is some type of financial support or financial assistance for cotton in most producing countries around the world. For the next five years I don't see how we can compete without some type of competitive program. I think my comment is reality for all of us.

Someday I hope when my children are running our company, they will have the opportunity to compete in a free market environment. The business would certainly be easier and more efficient if every day we did not have to worry about Step 1, Step 2 or Step 3, but until we turn that corner, I am going to support the modifications I have outlined this morning.

I have struggled over the last three months with some of the legal developments in Washington concerning the cotton program, but I am positive that the National Cotton Council was not a participant to any of these negotiations. I still believe today that we must try to maintain a strong National Cotton Council with all seven segments participating. History has proven that when we all work together for the good of the industry, much can be accomplished in Washington. In my opinion, our future will become more clouded and distorted without a National Cotton Council. Let's work together as an industry in the months ahead.

Thank you.