

Southern Cotton Growers, Inc.
REPRESENTING COTTON PRODUCERS THROUGHOUT ALABAMA, FLORIDA, GEORGIA, NORTH CAROLINA, SOUTH CAROLINA AND VIRGINIA

COTTON MARKETING NEWS



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Has The 2005 Market Yet Revealed It's True Stripes?

Is the 2005 cotton market defying the odds? Are prices too high? Are we only setting ourselves up for a "train wreck" as the season progresses?

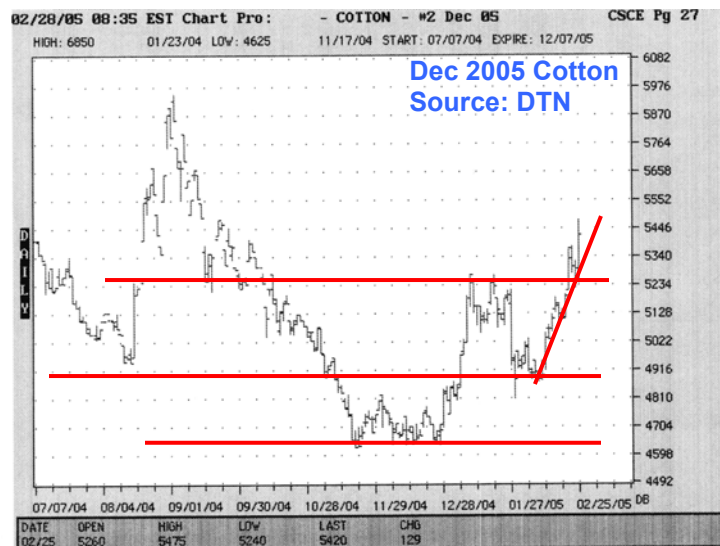
Let's capsule what we think we know at this point in time... admitting that we know nothing for certain and that opinions vary concerning this and the outlook. So, here goes:

2005 U.S. crop... we're coming off a record 23 million bale '04 crop. The 2005 crop could be 17.5 to 21.5 million bales depending on actual plantings, harvest, and yield. But regardless, barring another record or near record yield, the US crop will be smaller in 2005. But this is only one piece of the puzzle.

2005 Off-take... total off-take (US mill use plus exports) for the '04 crop is estimated at 19.3 million bales. Exports are expected at 13 million bales compared to 13.76 in 2004. For the 2005 crop, if off-take is maintained at 19+ million bales, there is a chance that stocks could be reduced if production comes in on the middle to low side of expectations (because production would be less than off-take). Lower stocks generally mean stable or rising prices.

Foreign production and demand... 2004 was a record year also as foreign production reached almost 94 million bales due in part to increased production in China, India, Pakistan, Australia, Kazakhstan, and Uzbekistan. But demand by foreign textile mills also was a record at almost 100 million bales. China increased use by 5.5 million bales from '03. Despite increased acres and yield well above average, China's production was still 8.5 million bales short us use. Most believe that foreign production will be lower for 2005.

US Exports... exports are projected to reach 13 million bales for the 2004 crop. This is down about 3/4 million bales from 2003-- but considering the size of the crop world-wide, this has to be considered a very good level of exports and can be largely attributable to growth in the Chinese/southeast Asia textile industry. The outlook for 2005 hinges squarely on foreign production and mill demand. Exports of the 2004 crop have been strong... leading some to believe that US exports will top the current 13 million bale projection and be even more during the 2005 crop marketing year.



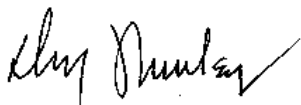
So it may be a somewhat safe assumption, at the present time, to say that the impressive run in new crop prices (December futures) in recent weeks has been, among other things, the result of (1) uncertainty of the production side (US acreage, etc) and (2) optimism on the demand side (good exports and expectations that this will continue for the 2005 crop).

So, in which camp do you want to pitch your tent and when? The run in December futures has brought on the thought by some producers, that perhaps it's time to take price protection in some form. December rallied almost 5 cents (from 4882 on February 8th to 5368 on February 22nd), declined (adjusted) slightly back to 5291 on the 24th before taking off again to 5420 today. Will (can) the market sustain this level or even higher or will prices eventually trend lower?

From this action in recent weeks I conclude that (1) the market for whatever reason has little reservation about moving into the 50's given what we think we know right now, (2) that 2005 cotton now has 3 levels of support that must be negotiated should prices decide to move lower, and (3) higher prices (to 58-60 cents) are possible but lower prices seem more likely. As I have stated in this space on several occasions, the keys are Chinese demand and US production and exports. *If US and foreign production for 2005 comes in lower than last year (lower by at least 3 million bales) and if foreign mill demand remains robust and supportive of US exports, then prices with a "5 in front" are on the right track—and I think that is what the market is trying to tell us.*

If prices should move lower by harvest time, producers know there will be an LDP/POP to help out. Basis Southeast, for the 2004 crop the average of cash+LDP or Loan Gain+Cash or Loan+Equity was about 59 cents. So, assuming the same market relationships as in 2004 (basis, cash-AWP spread, etc.) I think you analyze 2005 strategies in such a way that this would be your worst-case scenario—because you are likely to net about 58-59 cents with little risk and no decision-making. In other words, there no reason to lock-in a situation where you are more likely to net less than 58-59 cents.

If you are uncomfortable with the risk of prices moving lower from their current levels, your alternatives would include contracting or Put Options. A contract (basis Southeast) today would give you about 52 cents for base quality fiber. If the market were to move to the 46-cent area by harvest, the POP/LDP would be about 16 cents for a total of about 68 cents. The risk in this is that if prices were to increase rather than decrease, you could end up with both a low-price contract and low LDP. But you would have to be willing to purchase Call Options to try to offset the loss of LDP. Another strategy would be to purchase Put Options. This would net you no worse than your Strike Price minus premium minus basis plus POP/LDP. You would then still be able to sell at higher prices if the market moved up.



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