



# INTERNATIONAL COTTON ADVISORY COMMITTEE

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October 13, 2003

## IMPACTS OF GOVERNMENT MEASURES ON AFRICAN COTTON PRODUCERS\*

The harm being done by below-average cotton prices to the world economy and to the economies of numerous countries is significant. Cotton is grown in over 80 countries, and the activities associated with growing, handling and ginning cotton provide a significant source of income for approximately 300 million people each year. Exports of cotton lint represent a significant portion of the foreign exchange earnings of countries as diverse as Burkina Faso and Uzbekistan. Among the Least Developed Countries in Africa, Angola, Benin, Burkina Faso, Burundi, Central African Republic, Democratic Republic of Congo, Chad, Ethiopia, The Gambia, Guinea, Guinea-Bissau, Madagascar, Malawi, Mali, Mozambique, Niger, Senegal, Somalia, Sudan, Tanzania, Togo, Uganda, and Zambia are cotton producers.

### Structural Change Leading to Lower Prices

The world cotton industry is in the midst of a downward shift in average prices. The cost of producing cotton is falling because of the expansion of new producing areas and advances in technology, including genetic engineering. As a consequence of falling production costs, higher world production is occurring at each price level, resulting in lower average prices compared with the 1970s, 1980s and 1990s. The ICAC Secretariat estimates that average cotton prices are likely to be between 50 and 60 U.S. cents per pound this decade, 10 to 20 cents per pound lower than the average of the last thirty years.

Prices were particularly low during the 2001/02 cotton season (the season measured from August 2001 to July 2002). The average world price of cotton fell to a thirty year low of 42 cents per pound. Cotton was not alone in experiencing devastatingly low prices in that time period, as the prices of wheat, maize, soybeans and other crops that are competitive with cotton for planted area were also at or near the lowest levels in decades at that time. The low prices of 2001/02 led to reduced production and increased consumption in 2002/03, and the average international price rose to 56 cents per pound. During the current season, 2003/04, poor weather earlier this year and strong import demand from China (Mainland) are boosting prices further, and the season average is forecast at more than 60 cents per pound. Nevertheless, prices remain below the long-term average of 70 cents, even with the bullish factors affecting prices today. While this downward shift in average prices is painful for producers, the change represents a necessary industry response to competition with chemical fibers.

### Government Measures Distort

The cotton industry faces many challenges and all are important, but perhaps none is timelier than the challenge of developing a constructive approach to the problem of distortions to cotton production and trade caused by government subsidies. Competitive realities and changes in technology that are restructuring the modern cotton economy. However, producers in a

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\* A statement by the Executive Director of the ICAC before the annual session of the Trade and Development Board, United Nations Conference on Trade and Development.

liberalized world economy supposedly operating according to free market principles should not also have to contend with distortions to production caused by subsidies.

Agricultural industries are among the most distorted markets in the world economy, and direct income and price support provided to the cotton industry in 2001/02 was \$5.8 billion worldwide, equivalent to about one-fourth of the value of world cotton production. Government support for cotton production declined to \$3.8 billion during 2002/03, equivalent to about one-seventh of the value of world production. The lower levels of government expenditure during 2002/03 were the result of program formulas driven by lower production and higher market prices, not because of changes in government programs or policies. Should market prices turn lower again in future seasons, government spending in support of cotton under current policies would automatically rise.

Direct income and price support expenditures on cotton by the U.S. government were \$3 billion in 2001/02. New legislation came into effect in 2002, and the 2002 farm bill determines the levels of support for the U.S. cotton industry for the next 5 years. Total direct income and price support in the USA for cotton amounted to \$2 billion in 2002/03.

Government expenditures to assist cotton growers in China (Mainland) are estimated at \$1.2 billion in 2001/02 and \$750 million in 2002/03.

Cotton growers in Spain and Greece are offered assistance through the EU Common Agricultural Policy (CAP). Payments under the CAP amounted to \$979 million in 2001/02 and \$957 million in 2002/03.

The government of Egypt provided between \$23 million and \$33 million a year to cotton growers during the last two seasons.

The Government of Turkey provided direct support payments totaling \$59 million in 2001/02 and \$57 million in 2002/03.

Support by the Government of Cote d'Ivoire to cotton growers is estimated at \$8 million in 2001/02 and \$14 million in 2002/03.

Support by the Government of Mexico to cotton growers is estimated at \$18 million in 2001/02 and \$7 million in 2002/03.

In addition to production subsidies, China (Mainland) and the USA provide subsidies to exports of cotton. However, these subsidies are far smaller than the levels of support for production. Export subsidies provided by China (Mainland) and the USA amounted to \$121 million in 2001/02, and \$317 million in 2002/03.

Estimates by the ICAC Secretariat indicate that in the absence of government support for the cotton industry in 2001/02, market prices would have been approximately 70% higher than they were. For 2002/03, the ICAC Secretariat estimates that cotton prices would have been about 15% higher than the actual result if government measures had not supported production in some countries.

Economists often differ in their choice of models and assumptions, and consequently different studies result in different estimates of the impacts of subsidies on prices. Nevertheless, even conservative estimates of the impact of subsidies paid to producers in the USA, Europe, China (Mainland) and elsewhere are substantial. The ICAC Secretariat estimates that losses to all producers in 2001/02 caused by lower prices linked to government measures amounted to \$14 billion, and that losses during 2002/03 amounted to \$3 billion.

For sub-Saharan African producers alone, the losses in income linked to subsidies to cotton production are estimated at \$920 million in 2001/02 and \$230 million in 2002/03. The impact of these losses to individual countries with high cotton dependency, such as Benin, Burkina Faso, Chad, Mali and Sudan was substantial.

## Developments in the WTO

An unprecedented aspect of the current round of world trade talks is the emphasis on cotton. Cotton is unusual in being both a labor-intensive crop in developing countries and a capital-intensive crop in developed countries. Even though government measures in cotton constitute approximately 1% of all support to agriculture in OECD countries, the Financial Times declared that the talks in Cancún unraveled over cotton.<sup>1</sup>

The venue for the negotiation of reductions in government measures that distort cotton production and trade is the World Trade Organization (WTO). An agreement to reduce subsidies that distort production and trade in agriculture will not be easy. Cotton is important to the history and culture of Greece, Spain and the USA. Within the U.S. and Europe cotton farming occurs in lower-income regions, often in areas where economic alternatives are not attractive. Consequently, there is a long chain of political support for cotton among landowners, cotton input suppliers and small-town merchants with vested interests in continued cotton production. Areas of cotton production in Greece and Spain are categorized as the lowest-income regions within the European Union, and average cotton farm size in Europe is less than 5 hectares. Consequently, the EU sees the cotton income support program as a justified mechanism to help small, low-income producers with limited impact on the world cotton market.

Both the U.S. and the EU argue that as net importers on a whole trade pipeline basis, each is actually helping to sustain the world cotton market. The EU is the largest import market for textiles in the world, and the U.S. is the largest retail market for cotton. The U.S. industry and government contribute approximately \$60 million per year in domestic and international cotton market development efforts. These efforts, begun in the 1950s, are boosting world demand for cotton, perhaps by more than subsidies boost U.S. production.

## Future Action

Producing countries need to respond to the declines in cotton prices with strategies that expand the demand for cotton, facilitate the adoption of competitive technologies and reduce government measures that distort production and trade. In particular there are five areas of activities in which the support of UNCTAD can be of benefit to the world cotton economy.

1) In order to strengthen the market for cotton, the ICAC is encouraging all countries to require fiber content labels in all textile products sold at retail. There is abundant research showing that when consumers are aware of fiber content, they consistently choose cotton products. However, only 59 out of 166 countries recently surveyed have laws requiring that fiber content be labeled in products sold at retail. Consequently, many consumers are not able to readily identify the fiber content of products offered for sale in their countries, thus inhibiting efforts to boost retail level demand for cotton. There was a consensus at the 62<sup>nd</sup> Plenary Meeting of the ICAC in September 2003 in Gdansk, Poland that countries should encourage fiber content labeling of products sold at retail, and the support of UNCTAD for this initiative by helping the ICAC to communicate this need to governments will be appreciated.

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<sup>1</sup> Financial Times, Tuesday, September 16, 2003, page 17.

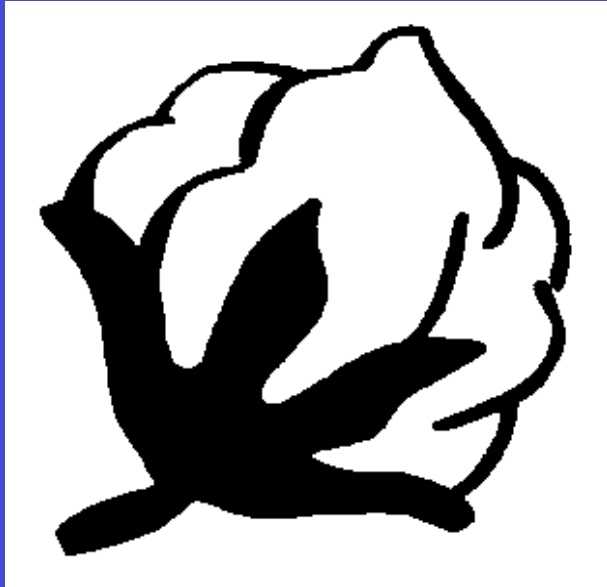
2) Improvements in cotton quality and quality measurement are components of an overall strategy of improved cotton industry competitiveness. There is an emerging international consensus that instrument-based quality evaluation programs are superior to traditional hand-classing methods for cotton, but these systems are expensive and involve the operation of complex instruments in air-conditioned environments with trained personnel. The ICAC is working to assist developing countries with the adoption of new cotton classing technologies to enable them to compete in the international marketing of cotton, and the assistance of other international organizations in the achievement of this objective will also be very helpful.

3) Input supply to smallholder cotton producers is important for increasing cotton production in Africa. Cotton is a relatively input-intensive crop, requiring certified planting seeds, quality fertilizer and appropriate insecticides applied using the latest approaches in integrated pest management to optimize yields and improve profitability. A constraint to increased production is a lack of accessibility to inputs by small holders. For this reason, the ICAC Secretariat and the Commodities Branch in UNCTAD are working together on a project to study the input markets of countries in West and Central Africa to determine how best to strengthen the delivery of inputs to small holders. The project, approved for funding by the Common Fund for Commodities (CFC), will also suggest measures for improving the sustainability of cotton production in the region. Following completion of this initial project, which will include a workshop on input supply to small holders next year, a full project could be developed to improve cotton production conditions in the region, and the cooperation between the ICAC and UNCTAD in this initiative will be highly positive.

4) Institutional support for the ICAC, and other International Commodity Bodies (ICB's), can also help to strengthen commodity markets. It is a harsh reality that in a liberalized world economy, some governments are questioning the importance of commodity industries and re-evaluating the worth of membership in international commodity bodies. The ICAC was created in 1939 with a mission of assisting governments to facilitate a healthy world cotton economy. Together with the CFC and sister ICB's, we work to raise awareness of commodity problems, to provide scientific and statistical information critical to decision making and to facilitate cooperation between governments and industry segments on issues of shared concern. The number of governments in Africa, Asia and Latin America that maintain their memberships in the Committee demonstrates the value of the work of the ICAC to developing countries. The support of UNCTAD in encouraging governments to maintain their memberships in ICB's can be of significant benefit and will be greatly appreciated.

#### WTO Talks Key to Progress

5) Finally, the most constructive effort the international community can make at this time is to ensure that the talks on agriculture and the problems of the cotton industry are priorities in negotiations within the WTO. At its most recent plenary meeting in Poland in September, the ICAC strongly supported a successful outcome to the talks on agriculture and other topics being conducted under the auspices of the WTO. The overwhelming majority of member governments reaffirmed the negative impacts of subsidies and other government measures on cotton production and trade affecting cotton farmers, especially in the developing and least developed countries, and urged that all government measures and subsidies on cotton be removed. International organizations can advance the interests of agricultural trade liberalization by articulating a positive program of mutual benefit within the talks on agriculture being conducted under the auspices of the WTO. Given the importance of cotton to the livelihoods of hundreds of millions of cotton producers, the specific concerns of the cotton industry regarding production subsidies deserve the full attention of governments and the international community.



# **International Cotton Advisory Committee**

# COTLOOK A INDEX

U.S. Cents per Pound

100

90

80

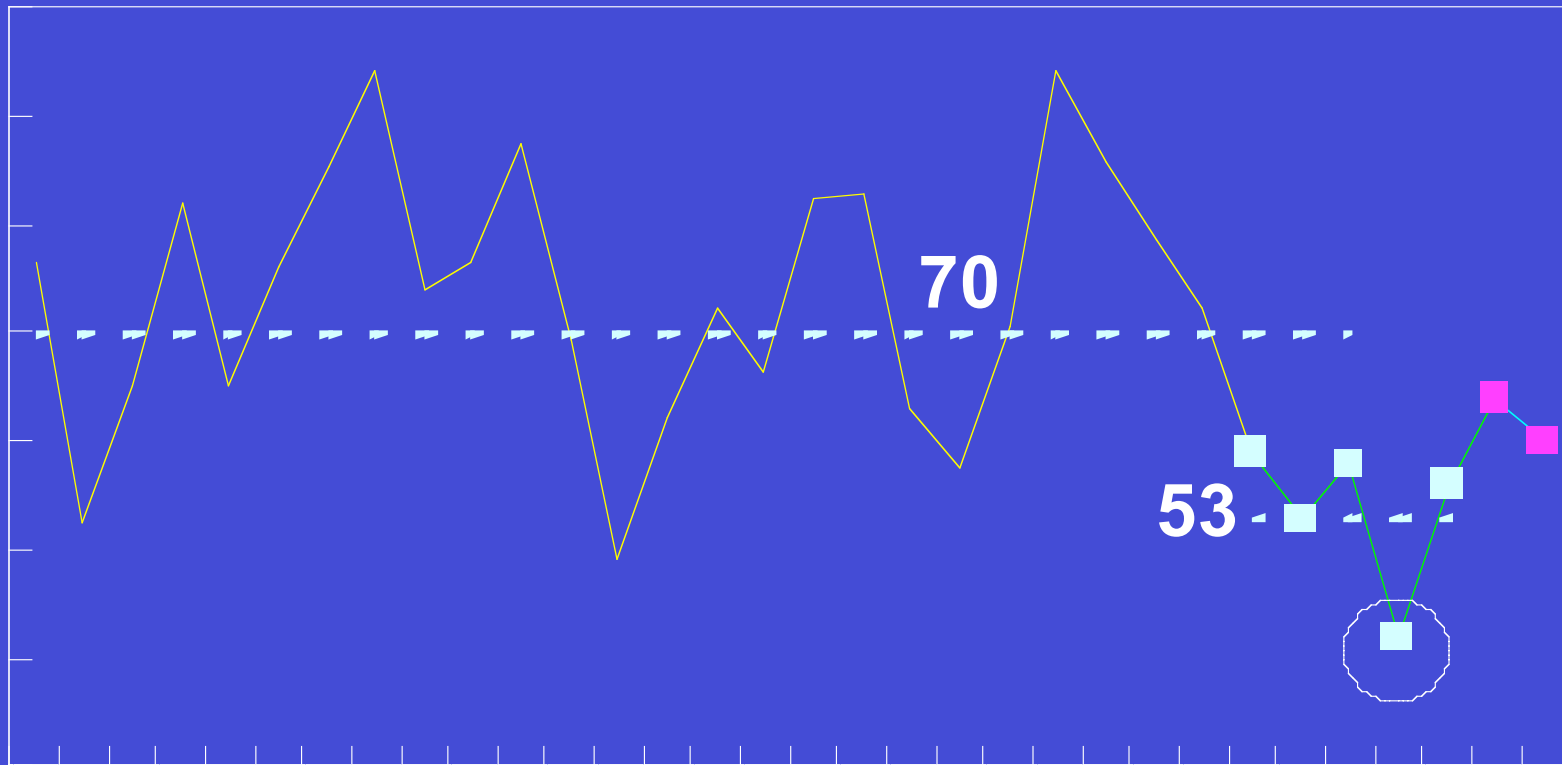
70

60

50

40

30



73/74

83/84

93/94

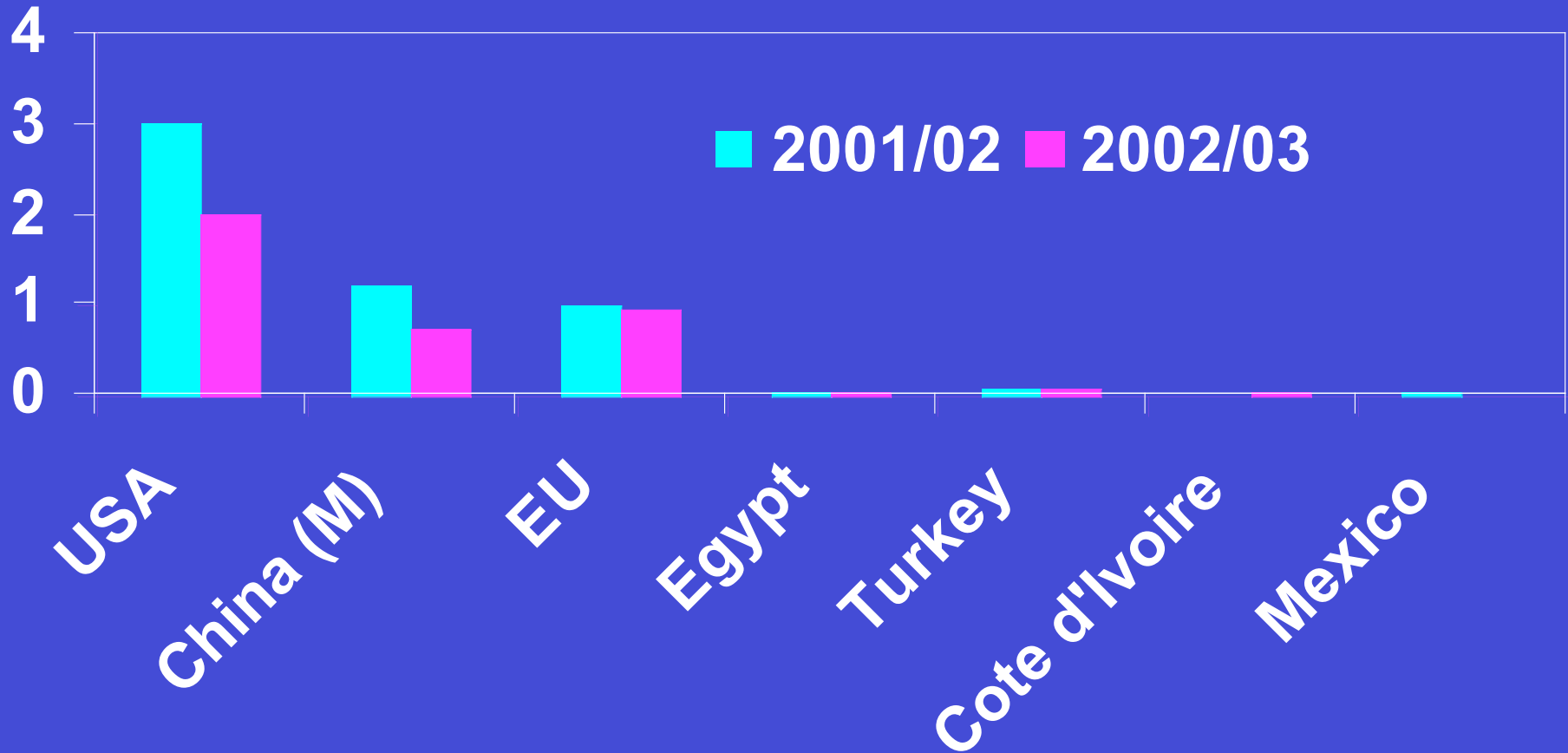
2003/04

70

53

# COTTON SUPPORT

\$ Billions



# COTLOOK A INDEX

U.S. Cents per Pound

100  
90  
80  
70  
60  
50  
40  
30



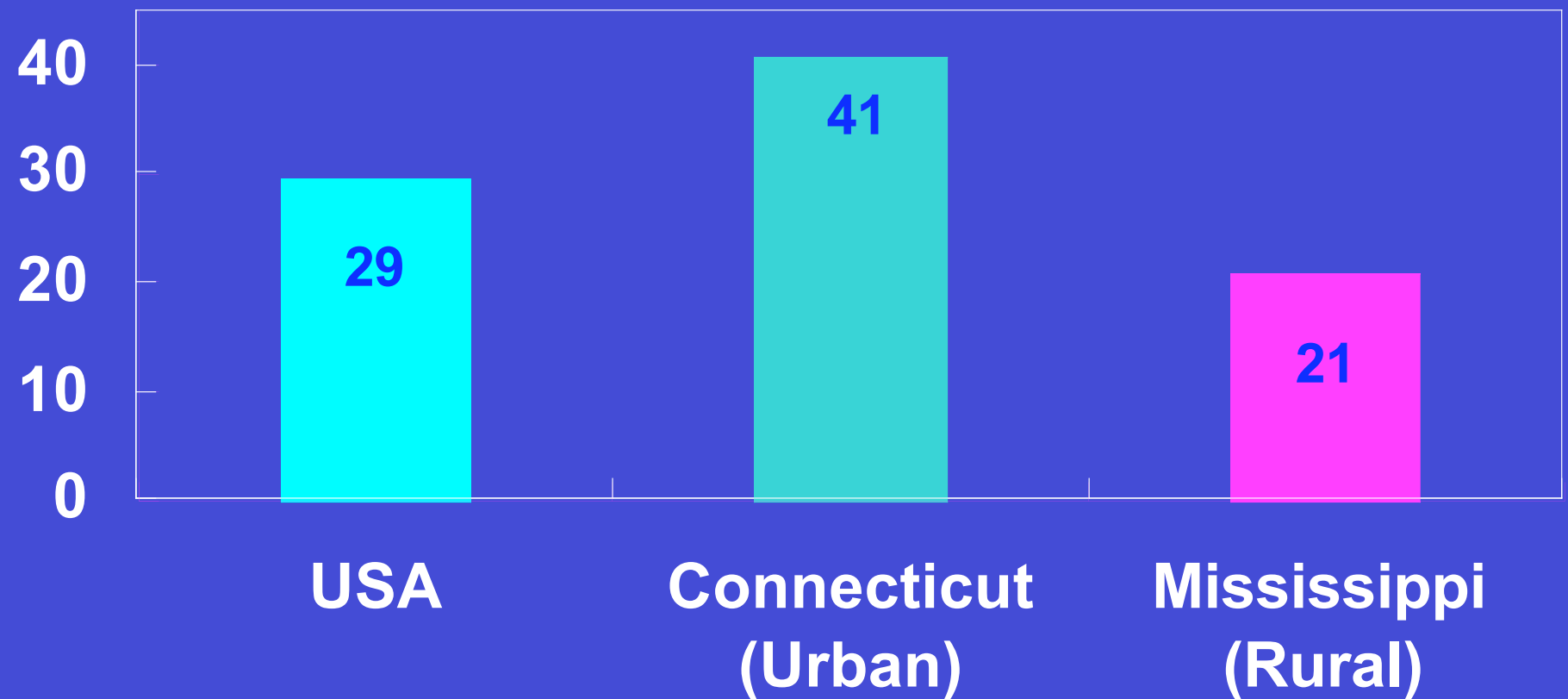
00/01

2001/02

2002/03

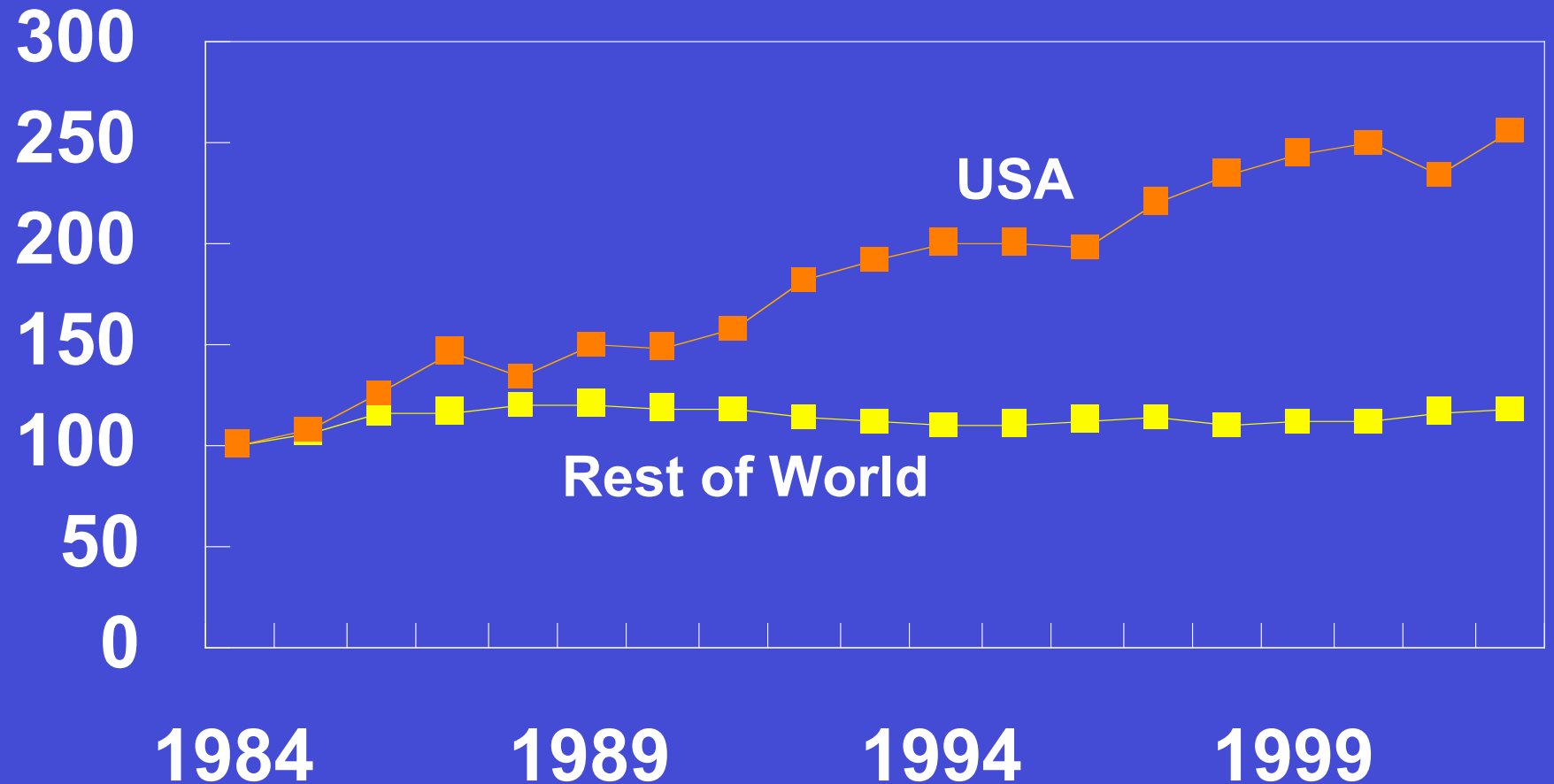
# PERCAPITA INCOME

Thousand \$



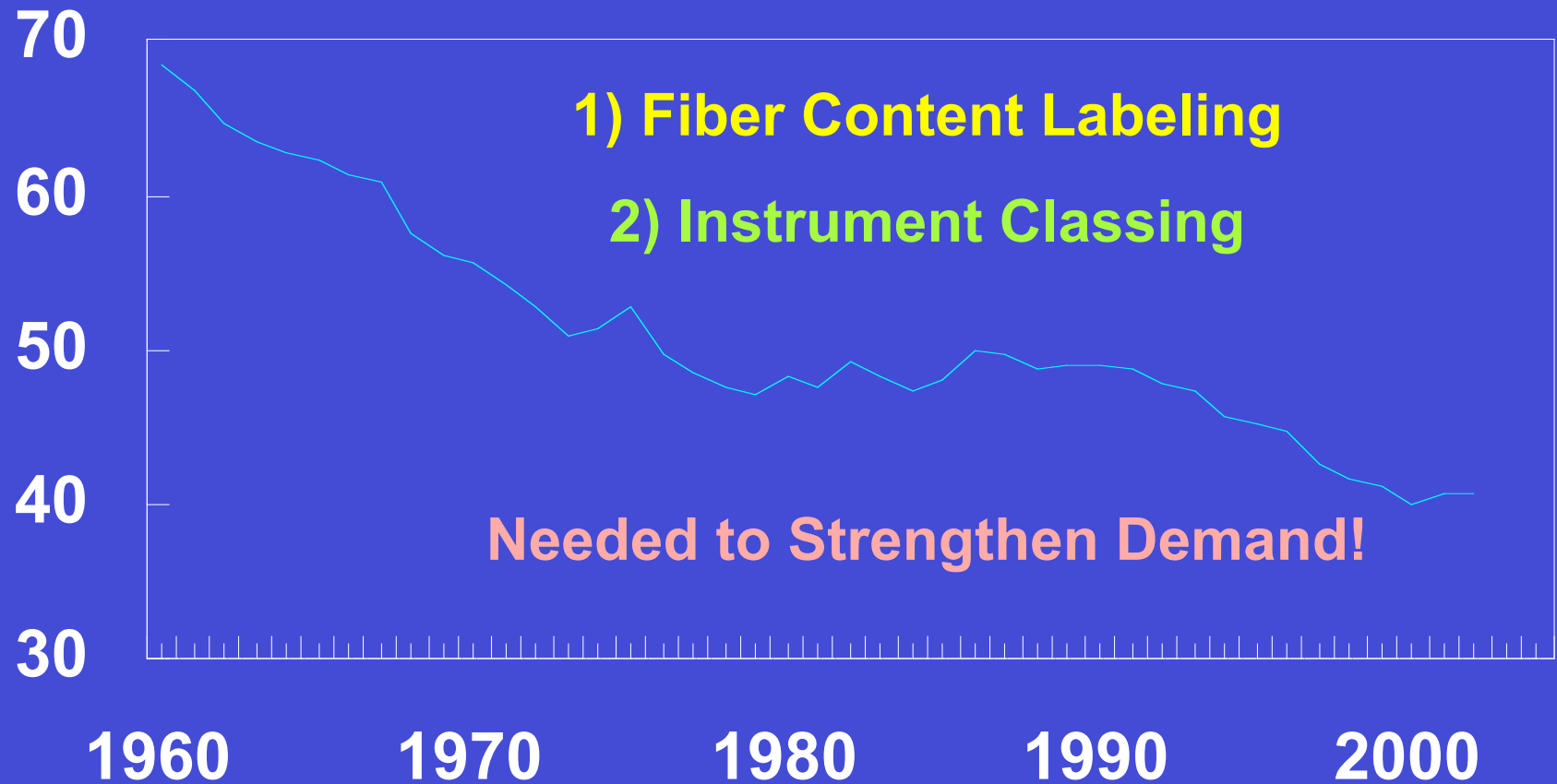
# RETAIL COTTON CONSUMPTION

1984 = 100



# COTTON'S SHARE OF FIBER USE

Percent of End-use Consumption



# COST OF PRODUCTION:

2000

Cents per Pound



# 4) International Commodity Bodies

**Mission: Assist governments in fostering healthy commodity economies**

**Raise Awareness**

**Provide Information**

**Facilitate Cooperation**

## **5) WTO Key to Progress**

- 1) Reduce Export Subsidies**
- 2) Improvements in Market Access**
- 3) Reductions in Domestic Support**