ICAC

International Cotton Advisory Committee

December 2020

PRODUCTION AND TRADE SUBSIDIES AFFECTING THE COTTON INDUSTRY

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A report by the
Secretariat of the
International Cotton Advisory Committee

Washington DC, USA

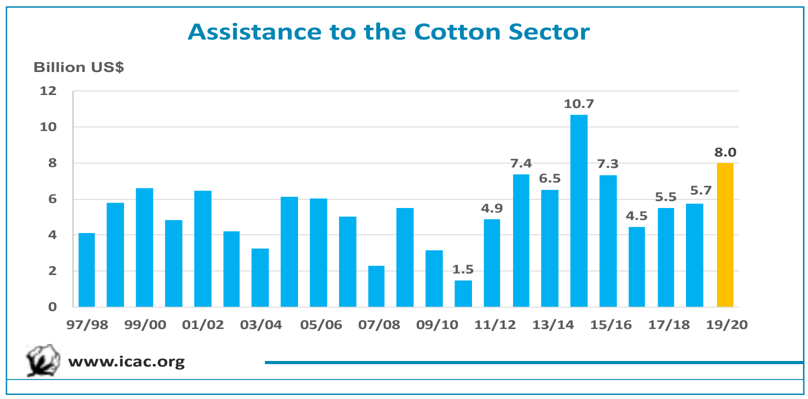
Goverment Support to the Cotton Sector

Subsidies to the cotton sector, including direct support to production, border protection, crop insurance subsidies, input and transportation, and minimum support price mechanisms, have been estimated at $8 billion in 2019/20, which is a 39% increase from the $5.7 billion in 2018/19. Eleven countries reported providing assistance to the cotton sector averaging 20 cents/pound in 2019/20, up from 15 cents/pound in 2018/19.

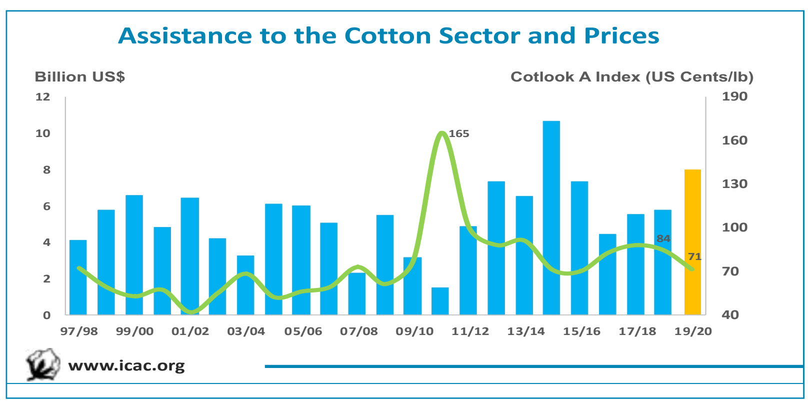
Since 1997/98, when the Secretariat began reporting on government measures in cotton, there has been a strong negative correlation between subsidies and cotton prices:

- In years when prices are high, subsidies tend to decline.
- In years when prices are low, subsidies tend to rise.

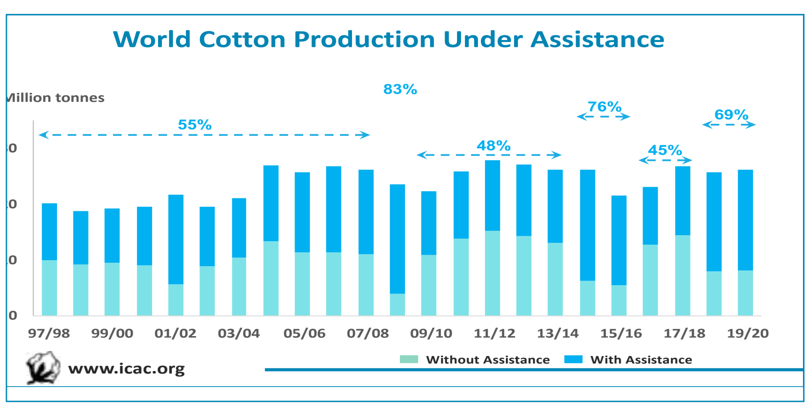
This correlation has remained fairly consistent during the past several seasons. The Cotlook A Index declined from an average of 91 cents/pound in 2013/14 to an average close of 70 cents/pound in 2014/15 and 2015/16, before rising to 83 cents/pound in 2016/17. Subsidies provided to cotton growers declined in 2016/17 from record levels. However, during 2017/18 average prices rose to 88 cents per pound and subsidies increased as well, while in 2018/19 a moderate decline in prices was accompanied with a moderate decline in subsidies. In 2019/20, world prices declined to 71 cents per pound while subsidies increased substantially, thus continuing the long-term relationship.



In some countries, including Brazil and Pakistan, minimum support price programs were not triggered in 2019/20 because market prices were above the government intervention price levels during most of the season.

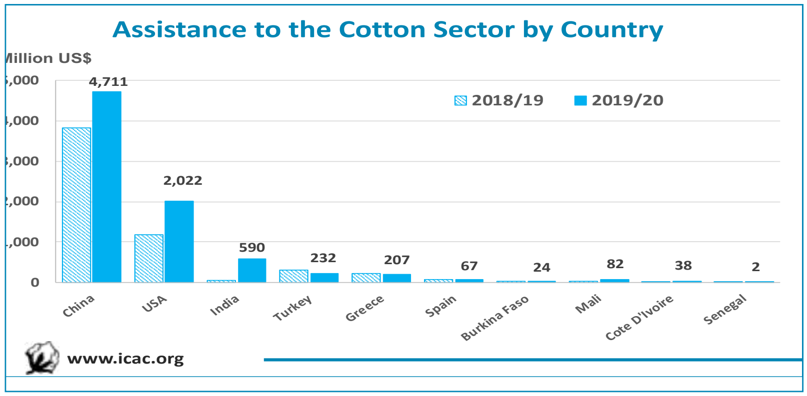


In 2019/20, some countries continued to provide subsidies for cotton inputs, especially for fertilisers, storage, transportation, classing services and other marketing costs. At the same time, the use of crop insurance subsidies is increasing although still not widespread.



The share of world cotton production receiving direct government assistance increased from an average of 55% from 1997/98 and 2007/08, to an estimated 83% in 2008/09. From 2009/10 through 2013/14, this share declined to an average of 48%. Between 2014/15 and 2019/20, the average percentage of production receiving direct assistance has ranged between 45% and 76%. The variance can be explained by the increase/decrease of both cotton production and international prices.

While most of the data was provided by government agencies, some open-source information has also been used. The Secretariat makes every effort to report on the impact of all government measures when they are quantifiable. The Secretariat encourages countries to provide data and comments on the figures to enhance the accuracy of the data.



China

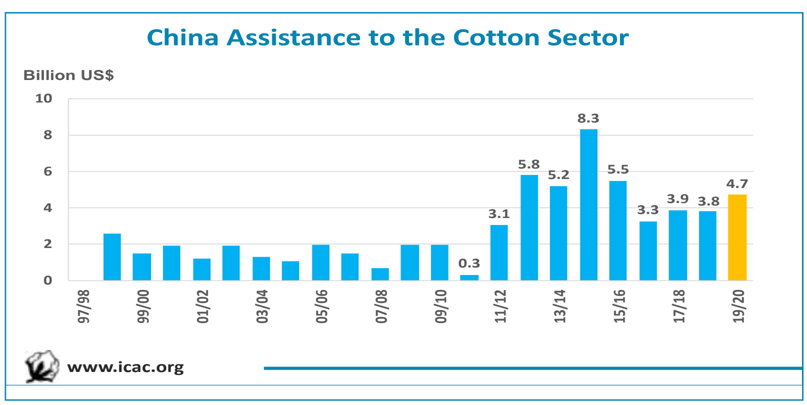
The government of China supports cotton production by controlling cotton import volumes and values and by applying border protection measures based on quotas and sliding scale duties, with an effective tariff of 40% on cotton imported without a quota. In addition, China maintains a strategic reserve of cotton, serving as a national buffer stock, which is managed by the China National Cotton Reserve Corporation (CNCRC). China releases cotton to the market from the reserve through a system of auctions when there is a shortage, and replenishes the reserve in times of abundance, thus supporting prices.

Under the terms of its accession agreement to the WTO, China is obliged to establish a calendar year tariff-rate-quota (TRQ). The in-quota tariff is 1% for the first 894,000 tonnes of imports each calendar year. Additional import quotas are released by China as required. The additional quotas can carry a tariff of 1%, or quotas can be based on a sliding scale of between 5% and 40%. The purpose of the sliding scale is to ensure that the effective cost of imported cotton exceeds international market prices and thus boosts domestic prices paid to farmers in China. Since 2015/16, China restricted imports by issuing only the TRQ import quotas, with the objective of reducing government stocks. As a result of government interventions and quotas, domestic cotton prices in China have exceeded international prices during the past three seasons.

The Secretariat uses the difference between domestic and imported cotton prices to estimate the border protection support to Chinese cotton due to government intervention. The price differential between the CC index (an index of mill-delivered cotton in China) and the FC Index L (an index of imported cotton arriving at China's main ports) adjusted to include value- added tax, port charges and transportation to mills, is used in the calculations. The estimated benefit (subsidy) received by producers in China as a result of the government border protection was declining in recent seasons. In 2018/19 the border protection by China was estimated at $890,000 (7 cents/pound). In 2019/20 the difference between the FC and CC indexes declined to almost negligible bringing the border protection benefit to zero.

In addition, starting in 2014/15, the Chinese government provided direct subsidy payments to cotton producers in Xinjiang based on the difference between a target price set for the season and an average market price. The target price system essentially guarantees the given price level, which means that whenever the market price is below the target level, the government will make up the difference. For 2018/19 and 2019/20, the target price was unchanged at 18,600 yuan/tonne (about 120 cents/pound at the average seasonal exchange rate in 2019/20). Using the difference between the target price and the average CC index (domestic cotton price), it is estimated that direct subsidies paid to producers in Xinjiang totalled $4.2 billion (38.3 cents/pound) in 2019/20, up from $2.37 billion (21.1 cents/pound) in 2018/19.

In other provinces, a direct subsidy of 2,000 yuan/tonne (about 12.9 cents/pound at the average seasonal exchange rate in 2019/20) was provided to producers during both seasons. It is estimated that this direct subsidy totalled $243 million in 2019/20, down from $272 million (13.3 cents/pound) in 2018/19.



It is reported that typically, the central government calculates the total subsidy amount based on province-level production data and the gap between the market and target prices. The central government then provides the funds to provincial authorities, who develop their own plans to distribute the payments in their respective provinces.

As border protection support was zero in 2019/20, total direct subsidy payments provided to producers in China are estimated at $4.4 billion in 2019/20, up from $2.6 billion in 2018/19. The increase is attributed to a lower market price during 2019/20, while the target price remained unchanged.

In addition, the government of China pays growers a subsidy amounting to about $150 million a year for using high-quality seeds, although smallholder farmers do not benefit significantly from this policy. During the past several seasons, China provided subsidies estimated at about $150 million per year for the transportation of cotton from Xinjiang to mills in eastern and southern China, where most of China's textile industry is located.

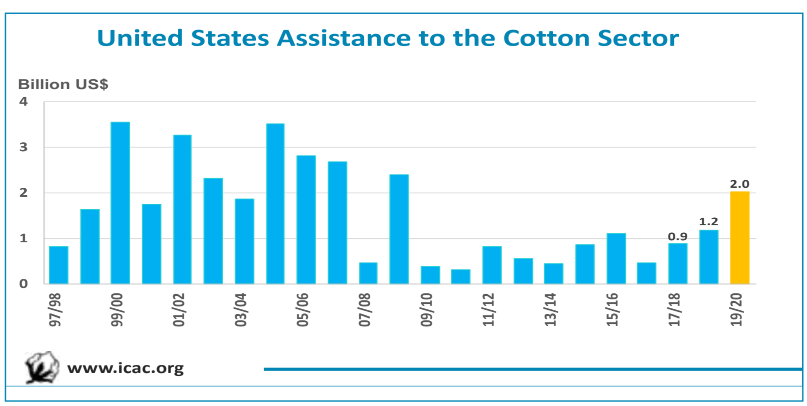
The sum of all subsidies provided by the Chinese government are estimated at $4.7 billion (37 cents/pound) in 2019/20, up from $3.8 billion in 2018/19 (29 cents/pound).

United States

The US 2018 Farm Bill has been in effect during the past two crop years. The bill includes the continuation of the designation of seed cotton (unginned upland cotton that includes both lint and cottonseed) as a covered commodity under the Title 1 Price Loss Coverage (PLC) and Agriculture Risk Coverage (ARC) programs. Coverage of seed cotton under these programs was established by the Bipartisan Budget Act of 2018 enacted in February 2018 and was effective for 2018/19 season. The 2018 Bipartisan Budget Act changes, continued in the 2018 Farm Bill, mark a significant shift in historical farm policies associated with cotton production by removing the production link to payments on those base acres, known as generic acres, under the 2014 Farm Bill. The cotton specific STAX Insurance program instituted in 2014 continues, but only for farms on which the generic base was not converted to a seed cotton base. Owners of seed cotton base will now be eligible for ARC or PLC program payments triggered by reference price or revenue benchmark on the same basis as for base acres for other covered commodities for programs which began under the 2014 Farm Bill. This change could mean that producers who held generic acres under the 2014 Farm Bill will now be able to plant upland cotton on that base without forgoing eligibility for ARC or PLC payments which could result in increased US cotton plantings. However, the payments, if any, are decoupled from actual planting decisions since they are tied to historical, and not current, cotton acreage and yields.

Cotton producers continue to have access to support under the new Farm Bill through both the marketing assistance loan program and subsidised premiums for crop insurance products.

The reference-price-based program, PLC, is similar to the counter-cyclical payments program under the 2008 Farm Bill and has been in place for other covered commodities since the 2014 Farm Bill. The PLC program makes a payment to owners of base acres (now at a rate of 85% of base acres) when the market price, or Marketing Year Average (MYA) price, for a commodity falls below the fixed reference price. Seed cotton MYA price is a weighted average of the upland cotton lint price and the cottonseed price. The PLC reference price for seed cotton is set in the 2018 Farm Bill at 36.7 cents per pound and the floor price is at 25 cents per pound. To calculate the payment, payment yield has to be established. The seed cotton payment yield will be a historical lint yield associated with the base acres multiplied by 2.4. Payment is made when the reference price exceeds the higher of the MYA price and the price floor.



The ARC-CO program provides income support payments based on the difference between actual revenue and a benchmark revenue at the county level (a county is a unit of government in the United States; there are about 700 counties that produce cotton). Owners of farms with base acres select ARC or PLC on a commodity-by-commodity basis. The ARC-CO payments are issued when the actual county seed cotton revenue is less than the ARC-CO county seed cotton benchmark guarantee, calculated using a moving five-year Olympic average (excluding the years with the highest and the lowest values) of county yields and national prices. ARC-CO payments are based on 85% of the farm's base acres of the covered commodity when actual county revenue is below 86% of the county benchmark revenue, capped to be no more than 10% of the benchmark revenue value.

Calculations for the PLC/ARC enrolment and actual payments were made based on available data published on the USDA FSA site. Most of the seed cotton base acres were enrolled in PLC in 2018/19 and in 2019/20. PLC/ARC payments for seed cotton are subject to the payment limit of $125,000 applicable to all covered commodities (other than peanuts), with the adjusted gross income test set unchanged at $900,000. PLC/ARC payments for 2018/19 totalled $371 million. PLC/ARC payments increased to around $1.13 billion in 2019/20 as a result of lower market prices.

The Marketing Assistance Loan Program (MALP) continues with a marketing loan rate for upland cotton based on the world cotton price, calculated as the simple average of the adjusted prevailing world price (AWP) for the two immediately preceding marketing years (announced on 1 October, preceding the next domestic plantings). However, it cannot be lower than 98% of the loan rate established for the preceding marketing year for base quality cotton. In addition, the loan rate cannot be less than 45 cents/pound or higher than 52 cents/pound. Under MALP, upland cotton producers are eligible for a loan deficiency payment (LDP), certificate exchange gains or marketing loan gains (MLG). Commodity certificate exchange gains and marketing loan gains provide benefits to producers by allowing them to repay short-term commodity loans at market prices (AWP) when those prices fall below the loan rate. Producers who choose not to take out commodity loans can receive the same benefit as an LDP, a direct payment equal to the difference between the market price (AWP) and the loan rate. For 2018/19 crop there were no LDP payments for upland cotton and about $1 million in MLGs. For 2019/20, LDP payments for upland cotton totalled $14.6 million and MLGs[1] reached $200.4 million.

In addition, the US government provides support to cotton producers through subsidised crop insurance to protect producers against crop yield and revenue losses. This multi-peril crop insurance covers certain causes of declines in crop yields, such as weather, pests and fire, with the exception of producer negligence. The insurance is sold to farmers through private insurance providers, although the Risk Management Agency (RMA) of the US Department of Agriculture subsidises a percentage of the premiums. On average, crop insurance policies are purchased for more than 90% of planted cotton acreage.

The crop insurance program is statutorily mandated to be actuarially sound, meaning that premium rates are to be set so that total premiums cover total indemnities over time. Underwriting gains and losses are allocated between participating private insurance companies and government according to formulas contained in the reinsurance agreement between the parties. During 2019/20, cotton insurance premium subsidies totalled $634 million, down from $669 million in 2018/19.

The STAX insurance program is also administered by RMA and was available during 2018/19 and 2019/20 for upland cotton producers, except on farms with seed cotton base enrolled in the ARC/PLC program for that year. STAX provides upland cotton producers with premium subsidies on the purchase of insurance policies that cover 'shallow' revenue losses — those below the level generally covered by standard crop insurance policies. Producers may use this program alone or in combination with existing underlying crop insurance. Under STAX, a payment is triggered if the actual revenue in a county falls below 90% of the expected revenue. STAX provides coverage for shortfalls between 10% and 30% of expected revenue; producers may select coverage in 5% increments. The federal government subsidises about 80% of the premium.

Total premium subsidies provided under STAX in 2018/19 totalled $141 million. In 2019/20, STAX premium subsidies declined to $35 million. Most of STAX policies were purchased in combination with an underlying standard crop insurance policy.

In addition, the federal government provides an administrative and operational payment to participating private insurance companies for delivery and servicing of crop insurance products, including STAX.

During the second week of February 2020, the US extra-long staple competitiveness payment went into effect for the first time in a decade and was equal to 6 cents per pound. The ELS competitiveness program provides a payment to ex-

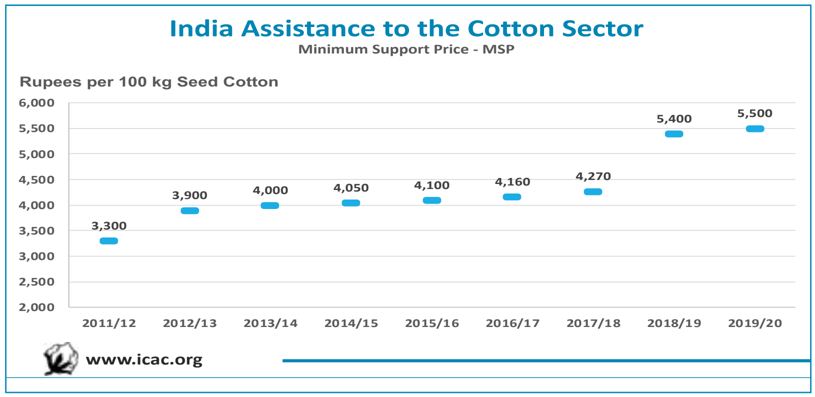
1) Includes certificate exchanges gains and cash redemptions

porters and domestic users of US Pima when, for four consecutive weeks, average quotes for comparable foreign growth (LFQ) are lower than US Pima quotes; and the adjusted LFQ (the LFQ adjusted for transportation between the US and Far East) is less than 113% of the current crop year loan rate level for ELS. During 2019/20, the US extra-long staple competitiveness payment was $7.9 million.

The sum of all types of support related to cotton that are provided to U.S. producers — including crop insurance, LDP, MLGs, STAX, ELS competitiveness and PLC/ARC payments — was $2.02 billion in 2019/20[2], up from $1.2 billion in 2018/19.

India

India has a Minimum Support Price (MSP) system that becomes operational during seasons when market prices are below the MSP during at least part of those seasons and functions through direct cotton purchases by the government-owned Cotton Corporation of India (CCI). CCI sells this cotton later to domestic mills or exporters, sometimes at a loss that is covered by the government of India.



The 2018/19 MSP for long staple Shankar-6 was increased substantially to Rs5,400 per 100kg of seed cotton, equivalent to 102.09 cent/pound of lint[3], at the season average exchange rate from Rs4,270 (87.04 cents per pound) in 2017/18. In 2017/18, CCI purchased 66,313 tonnes of cotton from producers and 181,970 tonnes were acquired during 2018/19.

According to its data, CCI sold about 238,653 tonnes of the MSP cotton it acquired during those two seasons, leaving a balance of 9,631 tonnes in CCI warehouses. The sales made by CCI during 2018/19, incurred estimated losses of $46 million[4], which represent a subsidy by the Government of India.

The MSP for 2019/20 was raised to Rs 5,500 per 100kg of seed cotton, equivalent to 100 cent/pound of lint[5]. Since the beginning of the season (October 1, 2019) CCI has purchased an estimated 1.79 million tonnes of cotton, the largest in five years and approximately more than one-third of their total production).

Additionally, it is estimated that the Maharashtra State Cooperative Cotton Growers Marketing Federation (MSCCGMF) — a subagency of the Cotton Corporation of India in Maharashtra that undertook cotton procurement operations at Minimum Support Price (MSP) from farmers — bought approximately 340,000 tonnes of cotton in 2019/20.

As of November 2020, CCI has sold 1.2 million tonnes of the MSP cotton it acquired and still holds the remaining stocks, while the current domestic prices for Shankar-6 fell to an equivalent of 69 cents per pound, due to an oversupply situation and COVID-19 cancelations. It is estimated, that based on the difference between the MSP and the market price the Government of India would have to cover or subsidise CCI's losses of $590 million, or 4.4 cents per pound of total production.

2) The Agriculture Risk Coverage (ARC) and Price Loss Coverage (PLC) have been included in the final calculations for 2018/19 and 2019/20, even though these payments are based on historical acres rather than current planted acres. Both ARC and PLC provide income support to farmers with cotton base, whether or not they are producing cotton, when market prices or average county revenues for seed cotton are below the statutory reference price or county benchmark revenue for prolonged periods. It is important to note that the USDA notified these payments together with other historical base acre payments as nonproduct specific outlays.

3) It does not take into account the market value of seed that is recovered by the CCI.

4) Cotton Corporation of India, Financial Results. https://cotcorp.org.in/financeresult.aspx

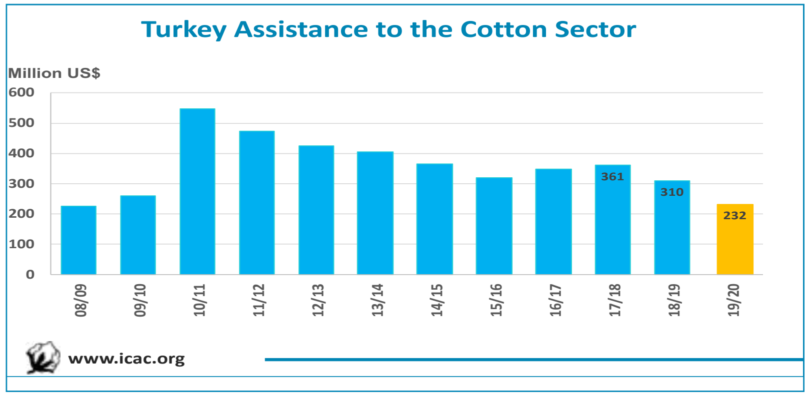
5) It does not take into account the market value of seed that is recovered by the CCI. It is estimated that the actual procurement value of lint after deducting cotton seed value comes to 77.91 cents/lb.

Cotton farmers in India also benefit from debt forgiveness and fertiliser subsidies from their government. India also provides some backing in the form of subsidies for crop insurance, although the value of this support is unknown. In addition, the government of India provides support to cotton production through several programs, such as the development of infrastructure facilities for production and distribution of quality seeds. Under the government's Technology Mission, support was provided for the modernisation of ginning and pressing units and the improvement of cotton marketing in recent years. No information on these programs is publicly available. In addition, the government supports the textile sector with a number of programs that provide direct support and soft loans.

Turkey

The government of Turkey pays a premium per kilogram of seed cotton to producers. In the past, the premium for seed cotton produced from certified seeds was higher than that from non-certified seeds.

No premium has been paid for non-certified seed since 2012/13. The premium for 2019/20 remained unchanged from 2018/19, at 0.8 lira (TRL)/kg for seed cotton produced from certified seeds.



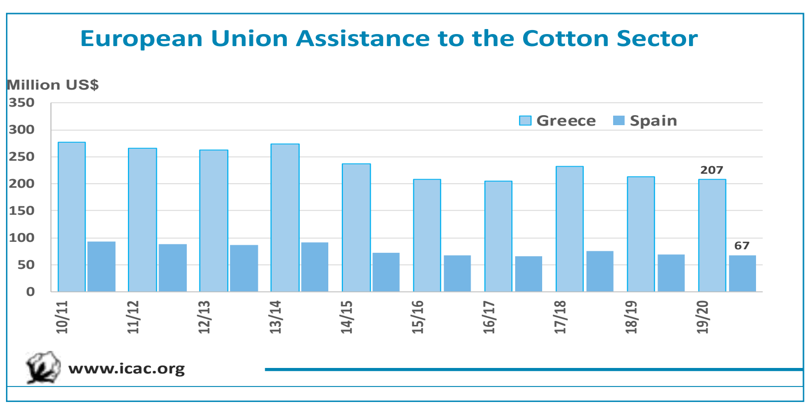
Assuming that 90% of Turkish cotton production is produced from certified seeds and that all cotton producers applied for the premium, the Secretariat estimates that total payments to cotton producers in Turkey declined from $310 million (14 cents/pound) in 2018/19 to $232 million (13 cents/pound) in 2019/20. The decline was caused by a devaluation of the TRL and lower production.

European Union

Changes were introduced in the EU Common Agricultural Policy starting in 2009/10. As before, cotton producers receive 65% of EU support in the form of a single decoupled payment (income aid) and the remaining 35% in the form of an area payment (coupled, or production aid). Greece and Spain are the major cotton producers in the EU. For production aid, the maximum base eligible areas are set at 250,000 hectares for Greece and 48,000 hectares for Spain. To be eligible for aid, the area must be:

- Located on agricultural land authorised by EU member states for cotton production,
- Sown under authoriased varieties, and
- Be harvested under normal growing conditions.

The aid is paid for cotton of sound, fair and merchantable quality. It is paid per hectare of eligible area by multiplying fixed reference yields by the fixed reference amounts for each country. To calculate the aid, the seed cotton yield per hectare is fixed at 3.2 tonnes/hectare for Greece and at 3.5 tonnes/hectare for Spain. The amounts per hectare are fixed at 234.18 euros for Greece and 362.15 euros for Spain.



If the eligible area exceeds the maximum base area, the aid per hectare is reduced proportionally. In 2019/20 the amount of direct subsidy to production in Greece was estimated at $207 million (27 cents/pound), down from $213 million (32 cents/pound) in 2018/19. The subsidy in Spain is estimated at $67 million (43.6 cents/pound) in 2019/20, down from $69 million (44 cents/pound) in 2018/19. The decline is mostly the result of a stronger US dollar relative to the euro.

Colombia

In Colombia, direct government assistance to producers declined during the past several seasons. Lower cotton production together with the devaluation of the Colombian peso explains the decline in total payments to cotton producers in this country. In 2019/20[6,7], direct assistance to cotton producers in Colombia reached $890,000 (2 cents/pound).

West Africa

Several countries in West Africa provided subsidies for cotton inputs in 2018/19 and 2019/20, especially for fertilisers and planting seeds. In 2019/20, estimates are that Burkina Faso spent $24 million (6 cents/pound); Mali provided $82 million (12 cents/pound); Côte d'Ivoire provided $38 million (8 cents/pound); and Senegal provided $2 million (14 cents/pound)[8].

Estimated Assistance Provided by Governments to the Cotton Sector*

Country	2018/19			2019/20**		
	Production	Average Assistance per Pound Produced	Assistance to Production	Production	Average Assistance per Pound Produced	Assistance to Production
	1,000 tons	US cents	US$ Millions	1,000 tons	US cents	US$ Millions
China	6,040	29	3,831	5,800	37	4,711
USA***	3,999	13	1,182	4,336	21	2,022
India	5,610	0	46	6,069	4	590
Turkey	977	14	310	815	13	232
Greece	277	35	213	292	32	207
Spain	65	48	69	66	46	67
Burkina Faso	183	10	39	193	6	24
Mali	276	6	35	299	12	82
Cote D'Ivoire	202	3	13	211	8	38
Senegal	6	7	1	6	14	2
Colombia	13	0.7	0.2	17	2	0.9
All Countries	**17,648**	**15**	**5,739**	**18,104**	**20**	**7,975**

* Credit and other assistance not included.

** Preliminary

*** Assistance to production for the USA includes $371 million in 2018/19 and $1,130 million in 2019/20 of support that is not tied to cotton production entirely and thus may be going to producers of other commodities or to idled land.

6) https://sioc.minagricultura.gov.co/Documentos/RESOLUCI%C3%93N%20NO.%20000300%20DE%202019.pdf

7) https://www.minagricultura.gov.co/Normatividad/Resoluciones/RESOLUCI%C3%93N%20NO.%20000247%20DE%202019.pdf

8) In recent years, the governments of Senegal and Cote d'Ivoire have modified their cotton policy to incentivize cotton production based on supporting farm gate prices for farmers instead of providing subsidies for fertilisers and inputs that can be targeting other crops.

Long-Term Assistance Provided by Governments to the Cotton Sector*

	World Production	Average Assistance per Pound Produced	Assistance to Production
	1,000 tons	US cents	US$ Millions
1997/98	20,181	9	4,108
1998/99	18,810	14	5,772
1999/00	19,193	16	6,588
2000/01	19,527	11	4,833
2001/02	21,667	13	6,446
2002/03	19,580	12	4,193
2003/04	21,129	7	3,270
2004/05	26,989	10	6,114
2005/06	25,678	11	6,008
2006/07	26,832	9	5,045
2007/08	26,162	4	2,292
2008/09	23,550	11	5,492
2009/10	22,309	6	3,155
2010/11	25,868	3	1,477
2011/12	27,855	8	4,866
2012/13	27,078	12	7,351
2013/14	26,224	11	6,513
2014/15	26,234	18	10,653
2015/16	21,477	15	7,321
2016/17	23,079	9	4,454
2017/18	26,714	9	5,509
2018/19	25,682	10	5,739
2019/20**	26,185	14	7,975

* Income and price support programs only. Credit and other assistance not included.

** Preliminary