

COTTON

July 04-09 2005

MAJOR HIGHLIGHTS

- **Domestic Cotton Prices Showed Further Improvement**
- **NYBOT Cotton Futures Declined this Week Overall**
- **Pak Trading Remained Dull, Spot Prices Improved**
- **Chinese Cotton Futures Improved Slightly this Week**
- **USDA Reported Mixed Export Sales for the Period June 24 June 30**

NEWS ANALYSIS

ICAC Forecasts Firm Cotton Prices

In its latest report released on 1st July the International Cotton Advisory Committee (ICAC) has reported that the season-average Cotlook A-Index will be 65 cents per pound in 2005-06, 13 cents more than the average expected for 2004-05.

Global cotton production in 2005-06 is anticipated to decline by over 10 per cent from the record output in the previous year, while consumption would continue to be driven by economic growth and rising Asian demand, especially from China. World cotton output is forecast to decline to below 24 million tonnes in 2005-06, down 2.4 mt, but still the second largest crop ever. Consumption is expected to rise to a new high of 23.8 mt (23.3 mt in 2004-05), with use in Asia likely to witness a big expansion. World trade in cotton during 2005-06 is poised to reach a new high of 8.1 mt (7.3 mt). China will be the main driver of world trade growth. Import requirement of the country is projected by ICAC at an unprecedented 2.8 mt. China's imports may end up at 2.5 mt, a record nonetheless.

Depending on levels of precipitation, it may be safe to expect a crop size of anything from 220 lakh bales to 250 lakh bales, as compared with 240 lakh bales produced in 2004-05 in India. Steady domestic prices in the wake of large production for the second season in a row coupled with firm global prices would open a window of opportunity for exporting Indian cotton next season.

According to ICAC, initial projections for 2006-07 indicate that production will rise to 24.7 mt, slightly above consumption and that the season-average Cotlook A-Index is expected to remain between 60 and 70 cents per pound for a second season.

Cotton Acreage Went Up in Pakistan

The cotton sowing area has increased by around eight percent in Sindh and 0.6 percent in Punjab at the close of the cotton sowing season across the country according to the market information. An area of 2,559,000 hectares has

been targeted in Punjab for cultivation this season against the 2,547,000 hectares set last season. 638,000 hectares have been targeted in Sindh against last year's target of 635,000 hectares. The area targeted for Balochistan remained unchanged at 40,000 hectares. However, the target for the NWFP was increased by 3,000 hectares to 10,000 hectares this year to help the government achieve the target. A total of 3.247 million hectares had been targeted for cotton sowing in the Kharif season against last year's sown area of 3.229 million hectares, which is an area-wise increase of 0.55 percent. Earlier the federal committee on agriculture (FCA) had targeted the cotton production at 12 million bales for the year 2005-06. However, the government revised the area and increased the target to 15 million bales for the same period. The Ministry of Food, Agriculture and Livestock (MINFAL) formed a cotton production strategy. Under this strategy, the estimated cotton production will remain at 11,650,000 bales in Punjab this fiscal year against the production of 11,500,000 bales in the last fiscal year. According to MINFAL estimates, Sindh will produce 3,250,000 bales in 2005-06 against the production of 3,000,000 bales in 2004-05. The production expected from Balochistan and NWFP will remain unchanged at 90,000 bales and 10,000 bales in the fiscal year 2005-06. The strategy pointed out that yield per hectare is expected to be 773 kg per hectare in Punjab against the 768 kg per hectare achieved in 2004-05. In Sindh, the expected yield is 866 kg/hectare against the yield of 804 kg per hectare achieved in the last fiscal year. Though the target is being seen as more ambitious the government would try to achieve this as cotton contributes significantly to the country's foreign exchequer.

Cotton: Brazil may Complain against US over WTO Issue

Brazil plans to ask the World Trade Organization (WTO) for permission to penalize the U.S. for its failure to comply with a WTO ruling against U.S. subsidies for cotton growers by the July 1 deadline. Brazil may file a formal complaint in which it will ask the WTO to allow it to increase import duties on certain U.S. goods to penalize the U.S. for failing

to sufficiently alter its export programs, reports said. The Bush administration has proposed ending a cotton subsidy program that has provided \$1.58-billion (U.S.) since 2001 to exporters such as Cargill Inc., complying with a World Trade Organization ruling that found such payments illegal. The U.S. Department of Agriculture Secretary Tuesday it proposed to end the Step 2 cotton-marketing program that pays shippers and exporters to use more expensive U.S. cotton for their needs. The USDA will also remove a 1% cap on fees that can be charged under the export credit programs and it will terminate the Intermediate Export Guarantee Program, commonly known as GSM-103. The United States in March lost an appeal of a WTO ruling backing Brazil's complaint that \$2.7-billion in annual aid intended to boost demand for U.S. cotton breaks spending commitments signed in 1994. Brazil's government estimates its cotton farmers have lost more than \$600-million because of the U.S. aid. Brazil's government estimates its cotton farmers have lost more than \$600-million because of the U.S. aid. As part of a draft WTO accord reached Aug. 1 last year, the United States has already agreed to negotiate scaling back cotton payments after years of pressure from farmers in Chad, Mali and Burkina Faso. More than 10 million people in West Africa rely on cotton for their livelihood, according to the British-based aid agency Oxfam.

China: Cotton Crop Progress in Xinjiang

The temperature was slightly higher than the average level since June, so the crop developed satisfactorily. And now the condition in Northern Xinjiang and Southern Xinjiang is different. In the North, farmers in Shawan, Yili and Shi Hezi planted the cotton earlier than other districts, and the young plants are growing very well now. The crop is 10-15 days ahead of the previous years. If the weather remains fine in July and August, the new cotton would come into the market ahead of the schedule. In the South, the upland cotton's height in A Kesu and Ku'Erle was 40.6-52.2cm in June, which was 6.59 cm higher than that in the same period of last year. The crop grew quickly in squaring period in view of the higher temperature, but the flower settled later than the previous years. Moreover, to some extent, the bolls of some long staple cotton had fell off, and the boll's quantities in the single plant was less than last year.

Cotton: Recent US Trade Scenario

A second round of trade talks between China and the U.S. is going to start Friday in Beijing, though China's Ministry of Commerce informed Thursday on its Web site that it was uncertain about the outcome of talks with the U.S. on bilateral textile trade issues. However, the ministry pointed out to the successful recent agreement between the European Union and China on textiles issues. Meanwhile, the National Cotton Council criticized the U.S. Department of Agriculture's proposal to eliminate Step 2 subsidies for U.S. cotton exporters and domestic mills. The NCC said the approach would alter a fundamental piece of the sales and marketing structure for cotton and thereby harm U.S. cotton merchants and textile manufacturers. The USDA made the proposal to satisfy a World Trade Organization ruling against the Step 2 program. USDA is making changes in

three export credit guarantee programs as the first stop on the long road to complying with the World Trade Organization ruling in the case brought by Brazil against the U.S. cotton program.

Cotton: US may Find Some Alternative to Subsidies

The US is not going to stop the aid to its cotton farmers according to the chairman of the Senate Agriculture Committee. The subsidy issue is in news recently when Brazil opposed to the US export subsidies to the cotton farmers saying that it was the violence of the WTO rules. The WTO agreed with Brazil this year that U.S. subsidies violated trade rules. To comply with the ruling, the Bush administration this week proposed termination of the so-called Step 2 subsidy and long-term export credit guarantees. Step 2 gives exporters and millers an incentive to buy higher-priced U.S. cotton. At \$350 million, this year's payments would be a small part of overall U.S. cotton supports, estimated at \$3.5 billion this year. Ending Step 2 will reduce outlays by \$400 million for fiscal 2004-07 according to the Agriculture Department. According to the Oxfam America the US cotton dumping costs the poor African countries \$400 million in revenue from 2001 to 2003. It said full compliance with the WTO ruling will require reforms later this year that go beyond elimination of Step 2 and the long-term credits. In a procedural step to preserve its rights, Brazil asked for WTO approval on Tuesday for up to \$2.9 billion in retaliation against U.S. products. But no action will be taken while the United States re-works its cotton program as per the opinion of the U.S. officials. Without Step 2, cotton exports would drop by 200,000 to 250,000 bales a year, and the farm-gate price for cotton could drop by 2 to 3 cents per pound. Up to three-fourths of US cotton is exported, with China a leading buyer. Therefore, that would directly reduce the world cotton prices also.

Cotton: USDA Reported Mixed Export Sales

USDA reported strong export sales for the period of June 24-30. However, the exports declined during this period. Net Upland sales of 318,400 running bales (RB) were 4 percent above the prior week and 63 percent over the previous 4-week average. China (231,600 RB) was the dominant buyer, with smaller quantities to Turkey (33,900 RB), Mexico (17,700 RB), and Taiwan (8,400 RB). Net sales of 29,200 RB for delivery in 2005/06 were primarily for Mexico (19,700 RB) and South Korea (5,200 RB). Exports of 254,100 RB were 16 percent below the previous week and 11 percent under the prior 4-week average. The primary destinations were China (75,700 RB), Turkey (73,700 RB), Mexico (24,100 RB), Thailand (16,500 RB), and Indonesia (13,100 RB). Also, U.S. cotton in good-to-excellent condition declined to 57% for the week ended July 3, from 62% the previous week, the U.S. Department of Agriculture said Tuesday afternoon. Cotton in fair condition increased to 30%, from 27% previously, while very poor-poor cotton rose to 13%, compared to 11% the prior week. The USDA said 55% of the crop was squaring, up from 41% the previous week, while 13% of the cotton was setting.

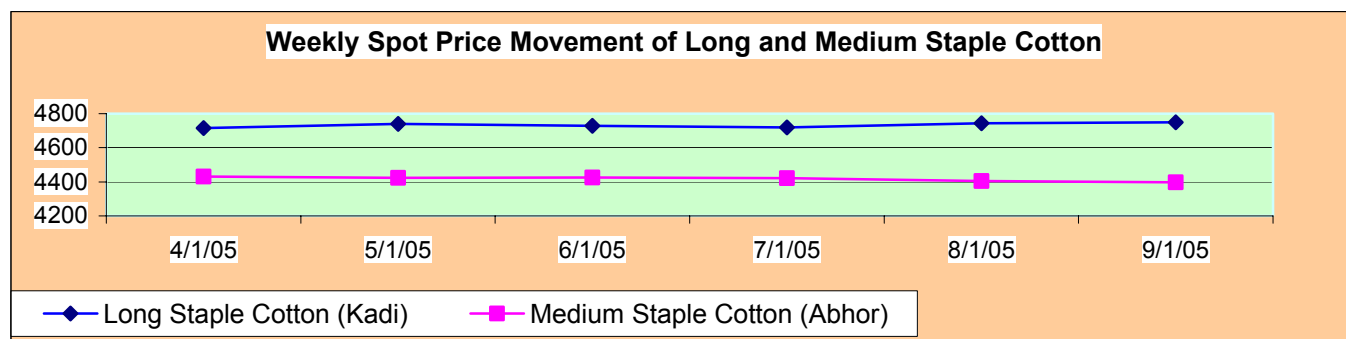
PRICES

Spot (Domestic)

| Date | Rates (Rs/Quintal) | |
|----------|---------------------------|-------------------------------|
| | Long Staple Cotton (Kadi) | Medium Staple Cotton (Abohar) |
| 04/07/05 | 4716.10 | 4431.15 |
| 05/07/05 | 4740.15 | 4423.60 |
| 06/07/05 | 4728.80 | 4424.95 |
| 07/07/05 | 4719.45 | 4421.80 |
| 08/07/05 | 4742.80 | 4404.95 |
| 09/07/05 | 4748.45 | 4398.20 |

Futures: December contract (NYBOT CTZ5)

| Contract | Open | High | Low | Close | Change |
|----------|-------|-------|-------|-------|--------|
| 04/07/05 | - | - | - | - | - |
| 05/07/05 | 55.8 | 57.2 | 55.6 | 57.07 | 0.92 |
| 06/07/05 | 56.35 | 56.75 | 54.93 | 54.96 | -2.11 |
| 07/07/05 | 55.06 | 56.35 | 54.82 | 55.88 | 0.92 |
| 08/07/05 | 55.45 | 55.8 | 54.6 | 55.47 | -0.41 |



FUNDAMENTAL ANALYSIS

INTERNATIONAL MARKETS

USA

The cotton futures at the New York Board of Trade (NYBOT) this week remained weak overall. The futures closed higher for a couple of days and ended lower for other couple of days. On Monday the NYBOT was closed due to the Independence Day holiday. The cotton futures at the New York Board of Trade closed higher Tuesday on speculative buying and crop concerns in Texas. Speculative buying supported by the technical factors helped the futures go up smoothly. However, on the very next day the futures declined drastically on weather concern. Tropical storm Cindy was earlier expected to be harmful however, it brought beneficial rain in some locations of the Southeast and West Texas. The storm blew over Louisiana and Alabama coastlines and caused 3-5 inches of rain, which was seen good for the crop in the stage of development. The storm also benefited the crop in Mississippi delta. Meanwhile, options-related selling also pressured cotton. Speculative accounts were net long 20.3% of open interest, from 8.6% net long the previous week, according to NYBOT's spec/hedge report for the week ended July 1. Open interest for the same week increased 3,319 positions to 91,908 contracts. The report was a bit bearish, because it revealed that much of the recent gains were due to short covering. The futures however, rebounded on Thursday. Hurricane Dennis was projected to make U.S. landfall on Sunday or Monday somewhere along the Gulf Coast from the Florida Panhandle west to Alabama or Mississippi, according to projections on the U.S. National Hurricane Centre Web site.

Expectations for solid weekly export sales also boosted cotton futures. On the last trading day of the week the cotton futures settled lower amid technical activities and subdued market sentiments. The USDA is scheduled to issue 2005-06 cotton production and supply-demand data on Tuesday. The expectation is about 19.7 million bales, compared to the USDA's 19.5 million June projection. The higher estimate is based on the USDA's June acreage estimate of 14.03 million, from 13.8 million in March. Ending stocks for the 2005-06 crop year are expected to be raised to 6.5 million, from the USDA's 6.2 million estimate. At present cotton crop is showing a steady growth all over the world, a bearish factor for cotton and on the other hand the weather condition is indicating a possible damage. Thus, the short-term scenario is a bit uncertain. However, the strength is likely to continue for more days.

China

Cotton futures in China remained with a very less movement this week. However, the cotton futures showed an overall strength this week. In the five days' trading the cotton futures settled higher for two days and mixed for other two days. The prices declined significantly for only one day. The China Cotton Index (CCI) also improved throughout the week. The volatile movement in the NYBOT cotton futures contributed partly to the Chinese cotton futures. On the last trading day the average prices of each contract had increased 2-49 Yuan, except MA0511, which

had, fell 40 Yuan. The cotton prices may remain strong in the coming week.

Pakistan

The week opening day for cotton trading in Pakistan was marked sluggish as leading mills and exporters were busy in auction. Throughout the week the cotton trading remained dull at the Karachi cotton market in Pakistan. The auction by the Trading Corporation of Pakistan (TCP) continues to dominate the cotton trading in Pakistan. Mills offered the highest bids for the stocks put on auction by the corporation. According to the traders around 50,000 bales lying in Karachi warehouses were sold. According to the market information the international bidders, Version Trading, Beijing limited, Hong Kong, East West and Plexus of UK offered to buy 5,000 bales each at 45.81 USC/lb, 45.00 USC/lb, 44.26 USC/lb and 43.78 USC/lb, respectively. The TCP accepted bids for 194,000 bales from local bidders. It also accepted bids by foreign buyers for 14,000 bales. Deals were also made for imported lint by mills, which are eager to pile up stocks of good quality lint for manufacturing fabric and yarn. The leading spinners remained on the sidelines, as they were eyeing the Trading Corporation's next auction on Monday. The TCP has so far sold 685,371 bales to local buyers and 85,000 bales to foreign buyers. Despite thin trading the spot rate increased by Rs 25 per maund to Rs 2,325 per maund. Around 1,000 bales of new crop has arrived in the market so far. Flood situation in some of the cotton growing areas in Punjab province is likely to provide support to the lint prices. The stocks lying with Trading Corporation of Pakistan (TCP) have shrunk to around 800,000 bales. This coupled with the large increase in the demand for cotton by the mills is indicating towards the strength in the prices in the next week too.

DOMESTIC MARKET

Stable trend in the cotton prices this week also maintained in all the major markets. The prices of J-34 cotton in the North Indian states remained strong this week. In Gujarat rain stopped at last however, the prices maintained firm undertone. The futures at the NCDEX posted slight gain today.

North Indian Markets

Scattered rainfall continues in some parts of the North Indian states. The prices of cotton throughout the week remained stable here. Sellers remained inactive. The market sentiments got support from the low stocks. Some buying of Bengal deshi cotton was also seen by the exporters. In Sri Ganganagar market of Rajasthan prices of J-34 improved in last two days. In the coming week it is expected that the spot prices in these markets would remain strong. The price of J-34 was recorded between Rs 1600-1620 per mon in Sirsa and Bengal deshi fetched Rs 1270-75 per mon. Price of J-34 cotton in Sri Ganganagar market of Rajasthan was quoted between Rs 1550 to Rs 1570 per mon whereas Bengal deshi fetched Rs 1360-70 per mon.

Gujarat Market

At last the rain stopped in Gujarat. The weather improved in the middle of the week. However, the prices did not go down as it was earlier expected. The abundant rain forced the re-sowing of cotton in the state. The crop also is

expected to harvest by at least one month late. This remained as the primary support behind the prices. Some exporters also came back to the market making deals in Shankar. Thus, the prices in Gujarat are not likely to go down in the near future. The prices of Shankar were recorded between Rs 15000 to Rs 17500 per candy. Price of Shankar (28 mm) remained between Rs 16500-17000 per candy. Prices of V-797 were quoted between Rs 11600-12500 per candy for ready delivery.

Maharashtra and MP Market

In the states of Maharashtra and MP the prices of cotton maintained the range-bound movement throughout the week. Cotton prices improved at the later half of the week in MP. Sowing is going on in Maharashtra and almost 60 per cent sowing is over. In MP however, some of the cotton areas require more rains for better sowing activities of cotton. Cotton prices here also are likely to remain unchanged with a stable undertone in the next week. This week in Maharashtra MCU-5 fetched Rs 17500-18500 per candy. Price of H-4 cotton in MP was quoted between 15000-16300 per candy. Prices of cotton khal in Akola remains between Rs 269.0-284.5 per 50 kg. Prices of cotton oil in Mumbai remained between Rs 374 to Rs 378 per 10 kg.

Vayda Bazaar

The medium staple cotton futures at the NCDEX this week posted a marginal gain over the last week. The intra-day price movement throughout the week remained very slow. The sentiments in the NYBOT futures did not affect the NCDEX futures. On the last trading day the NCDEX August contract closed at Rs 4480 per quintal, up by Rs 20 over the last week's closing. In the coming week too there is expectation that the cotton prices would maintain the strong movement.

WEATHER WATCH (IMD) (Latest)

Weather Systems:

The southwest monsoon has further advanced over the remaining parts of West Rajasthan on 30th June and thus covered the whole country almost two weeks ahead of its normal schedule.

The seasonal monsoon trough at sea level was near its normal position throughout the week. During this week enhanced rainfall activity occurred over central India which extended westwards into northwest India and Western Himalayan Region during 2nd half.

During the week, heavy to very heavy rainfall occurred at a few places over Gujarat Region, East Madhya Pradesh, Himachal Pradesh, Konkan & Goa and isolated over Andaman & Nicobar Islands, West Bengal & Sikkim, Jammu Division, Uttaranchal, Haryana, West Uttar Pradesh, West Madhya Pradesh, Chhattisgarh, Madhya Maharashtra, Saurashtra, Coastal & South Interior Karnataka and Kerala on 2-3 days during the week.

Light to moderate rainfall also occurred in the rest regions of the country, however the rainfall activity remained generally subdued over parts of Northeastern States, interior Peninsula, Marathwada and Vidarbha.

Outlook:

Rainfall activity is likely to increase over Orissa, Chhattisgarh, peninsular India and Maharashtra during 1st half of the week and over central parts of the country during

2nd half. It may also increase over northeastern States and Sub-Himalayan West Bengal & Sikkim during the 2nd half of the week. Generally subdued rainfall activity likely over the remaining parts of the country.

Exchange Rate in INR

| Currency | 04/07 | 05/07 | 06/07 | 07/07 | 08/07 |
|----------|-------|-------|-------|-------|-------|
| 1 USD | 43.56 | 43.57 | 43.57 | 43.64 | 43.63 |
| 1 Euro | 51.95 | 51.84 | 52.05 | 52.01 | 52.02 |
| 1 GBP | 76.72 | 76.45 | 76.67 | 76.43 | 75.99 |
| 100 Yen | 39.03 | 39.95 | 39.08 | 38.88 | 38.85 |

Latest ICAC Estimates on Global Cotton Scenario (As on 1st July)

| Particulars | 2004-05 | 2005-06 | 2006-07 |
|------------------|---------|---------|---------|
| Production | 120.6 | 110 | 114 |
| Consumption | 106.8 | 109 | 113 |
| Exports | 33.4 | 37 | 38 |
| Ending stocks | 49.2 | 50 | 51 |
| Cotlook A index* | 52* | 65* | 65* |

(Figures in million bales) *- US cents per pound

TECHNICAL ANALYSIS

Due to insufficient data technical analysis for Medium Staple Cotton (NCDEX - August contract) has not been included in this report.

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