

1992 Cotton Management Economic Notes

The University of Arizona • College of Agriculture • Tucson, Arizona, 85721
 Department of Agricultural and Resource Economics

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James C. Wade and Russell Tronstad
Extension Economists



168 lbs/acre from 1991 and is 434 lbs below the 1987 record of 1,126 lbs.

1992 Cotton Review

1992 comes to an end today and for Arizona cotton farmers -- not a minute too soon. Low prices and diminished yields have caused much concern on the part of farmers. But in the end, some hope can be seen for 1993.

The new year starts with prices on a slight upward trend and with foreign production lower than previously forecasted. The December estimate of foreign production was 16.26 million bales; down 1,400,000 bales from November and 1,780,000 from August. However, forecasted foreign use is also down; resulting in a decrease of only 310,000 bales in forecasted foreign stocks by the end of the 1992-93 crop year.

The U.S. situation is summarized in the table to the right. Estimated yields nation-wide returned to 696 lbs/acre, the August estimate. Stocks-to-use ratio increased from 26.9 to 28.0% from November to December. The 1991-92 ending stocks-to-use ratio was only 22.0%.

Arizona appears to be finishing the harvest season with yield estimated at 1,063 lbs/acre and 692 lbs/acre for Upland and Pima cotton, respectively. The Pima yield dropped

U.S. COTTON SUPPLY AND USE ESTIMATES

ITEM	1992/93			
	1991/92	AUG	NOV	DEC
Million acres				
Planted	14.05	13.42	13.42	13.42
Program	10.66	11.34	11.34	11.34
Non-Program	3.40	2.08	2.08	2.08
Harvested	12.96	11.40	11.21	11.22
Yield/harvested acre	652	696	681	696
Million 480-lb. bales				
Beginning Stocks	2.34	3.90	3.70	3.70
Production	17.61	16.53	16.21	16.26
Total Supply	19.97	20.44	19.91	19.96
Mill Use	9.61	9.70	9.70	9.70
Exports	6.65	6.70	6.30	6.00
Total Use	16.25	16.40	16.00	15.70
Unaccounted	-0.01	-0.07	-0.09	-0.14
Ending Stocks	3.70	4.10	4.30	4.40
Percent				
Stocks-to-Use Ratio	22.8	25.0	26.9	28.0

Source: USDA, ERS, "Cotton & Wool Situation & Outlook Update", December 4, 1992, Washington D.C.

The 1993 crop year may bring even more U.S. production, since the USDA has announce a preliminary 7.5% side-aside for Upland cotton in accord with the legislation requiring the production aim at producing a stocks-to-use ratio of 30%. This relative low set-aside should bring more acreage into production. In addition, the relatively low price of cotton should also bring higher deficiency payments. For the first time, a set-aside has been established for Pima cotton at 20%.

<u>Recent Prices</u>	<u>December 30, 1992</u>	
	<u>Upland (c/lb)</u>	<u>Pima (ELS) (c/lb)</u>
Spot	51.16	75.50
Target Price	72.90	105.80
Loan Rate	51.15	88.15
December Futures(93)	58.84	

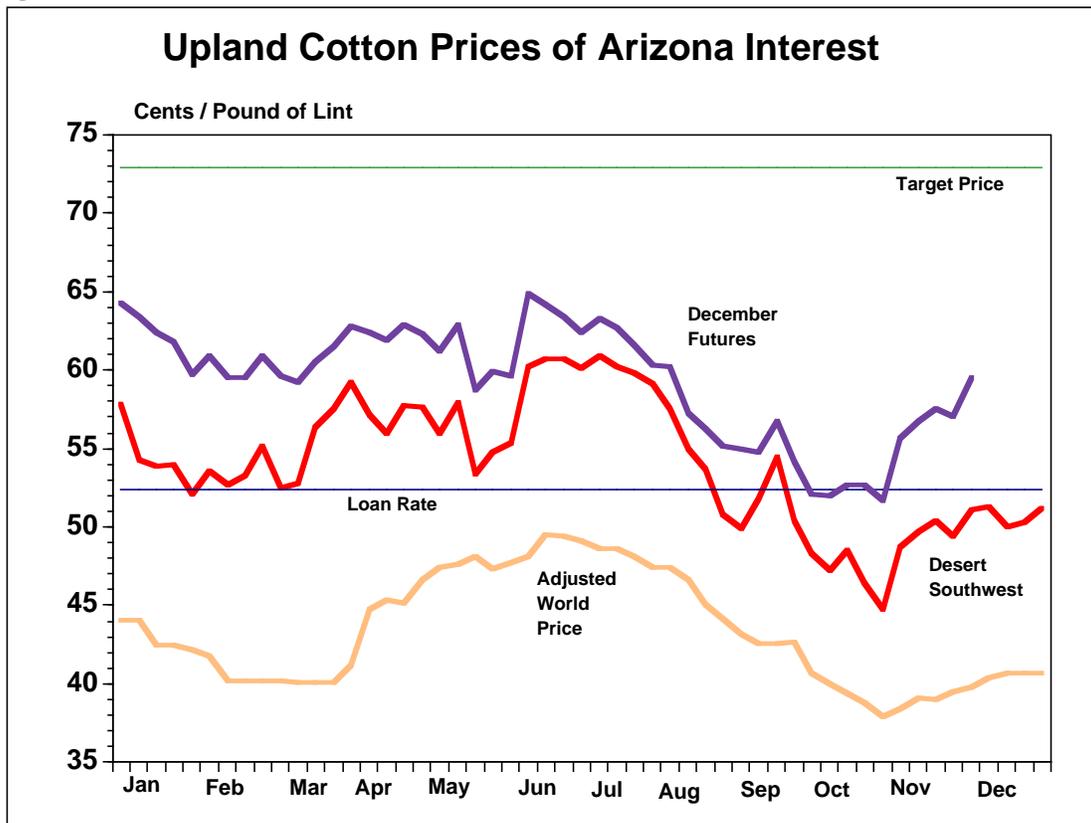
Note: Upland Spot for Desert SW grade 31, staple 35;
 Pima Spot for/ grade 03, staple 46 12/18/92; Phoenix Loan Rates/

1992 Price Summary

A summary of Upland cotton prices for 1992 is shown in the following graph. While prices steadily declined throughout the year, the uncertainty of the production season resulted in several important swings, both upward and downward. The adjusted world price shows that foreign supplies are high relative to demand. The foreign stock-to-use ratio is about 38%.

Recent upturns in prices appear to be limited somewhat by stagnant export demand. An improving domestic economy could increase consumption and, thus, cause domestic prices to increase slightly. December 1993 futures closed the year at 58.84 ¢/lb.

Pima cotton prices closed the year at about 75.50 ¢/lb. for Grade 3/Staple 46.



Call Option Harvest Strategy

A call option harvest strategy refers to a marketing approach where a call option is substituted for cotton storage. Rather than placing cotton in storage after harvest hoping that prices will improve, selling cotton in the cash market and purchasing a call option may be an alternative worth exploring. A call option is the right to purchase at a specified strike price so that the value of a call option will increase when prices rise. The main advantage of purchasing a call option over storage is that typical storage costs (physical storage costs plus interest on the monetary value your cotton would bring at harvest) are not incurred with the call option strategy. A disadvantage to purchasing a call option is that a premium must be paid upfront. To obtain the right to purchase March 93 futures at a strike price of 59 cents/lb. (12-31-92 March 93 Futures

closing price) anytime between now and March 93, a premium of 1.42 cents/lb would have to be paid. If prices dropped, the value of this call option could decline to nothing but this loss (a maximum of 1.42 cents/lb) may be less than having cotton in storage with a declining market. Also, a decreasing basis (cash-futures) would favor a call option strategy whereas an increasing basis would favor storage. Because current basis levels are at seasonally low levels for the last decade, a call option strategy should be approached with caution. In summary, an evaluation of storage costs against premium expenses, government program options, basis, and risk preferences need to be evaluated before deciding whether a call option harvest strategy is appropriate.