



## PLEXUS COTTON LIMITED MARKET REPORT

August 18 2005

The past week has featured a significant amount of bearish news. The US Crop was increased by the USDA to 21.29 million bales and the world carryover was increased to 49.81 million bales. In addition, it is believed that with the recent rains in Texas the crop there is underestimated, as is the Indian crop.

Whilst we are all focusing on the supply side of the equation let us not forget that we are still in August, and many is the time that the expectations of August have proved to be some way from the realities of October. Nevertheless, at the moment things look good.

The demand side of the equation is where attention should be focused. At current man made fibre price levels cotton is regaining market share with alacrity. It is quite easy to see, with 115 million bales of polyester consumption worldwide, that a further 10 percent of that can move to cotton. That is an extra 10 - 11 million bales on top of the figures currently being consumed.

Furthermore, at these levels it makes sense for the Reserve Corp in China to add to stocks for the longer term, to help balance out the volatile movements in cotton prices suffered by many consumers in China. We believe that these figures and this business will show up at some time in the not too distant future, including some in the sales report issued today.

China, India and Pakistan currently produce 75 percent of the world's textiles, and whilst India and Pakistan are not self sufficient in cotton, they are close to it. When you consider the coverage of the important mills and the stocks held by Government bodies, there is plenty of cotton in the two countries. This leaves China and markets such as Turkey and Indonesia. We do not believe the figures of 5.75 - 5.8 million tons for the Chinese crop. We believe that it is more inclined towards 5.5 million tons, and this crop is far from made yet, so if the figures for consumption are accurate, 3 million tons of imports will happen. That said, the US government works against itself by restricting Textile imports, because by doing so it pushes business into other regions that are less likely to use US cotton.

At some stage, cotton consumption increases will meet smaller crops, because below 50.00 cents/lb only Africa, India and Pakistan can produce profitably; but that time does not appear to be now. Markets work on psychology, and at the moment there is no fear of a cotton shortage. This is likely to keep prices low until people start to think about next year, and that does not really happen before January / February. Meanwhile the removal of Step 2 and the GSM program, when it happens (probably July 2006,) will have little to no effect on plantings in the USA. The farmer will get everything that he used to get, with the exception of the small amount the merchants calculated into their purchase price from Step 2. So, until the Farm Program radically alters, US crops are unlikely to change except for weather influences. One must bear in mind that the Texas crop can be badly

damaged between now and harvest if the weather is bad, and the US weather service is expecting another 14 named hurricanes between now and the end of hurricane season.

At below 50 cents/lb on New York there is plenty of demand, and all involved in the Textile industry admit that these prices are cheap. Speculators are bullish commodities long term, and whilst Funds having been taking new short positions for short term profits, strategic hedge funds have not moved their long position from New York.

This time last year the trade was short and mills were not so well covered. Today, only China has a real short coverage position, and that is mostly financially driven. The trade is unlikely to be too short physical new crop, although they might be short New York. It is hard to see anything in the market that will change the policy of buying when the market gets below 51.00 - 50.00, and therefore it is hard to be too bullish on physical cotton prices at the present time. Someone once said that "low prices cure low prices and high prices cure high prices." It is likely that we may see fairly low prices for a while yet (weather considerations aside) in order that increased cotton consumption will then meet reduced crops. The timing on this might be many months off, and so in the meantime we tend to believe that cotton prices will stay relatively flat and may even weaken a bit further, if crops increase and harvest pressure is there.

Best Regards