Directorate of Intelligence

~~Secret~~

25X1

Shifts in the World Cotton Market: Increasing Pressure on US Interests

25X1

A Research Paper

~~Secret~~

GI 85-10304
December 1985

Copy 404

Page Denied

Directorate of Intelligence

Secret [redacted] 25X1

Shifts in the World Cotton Market: Increasing Pressure on US Interests [redacted] 25X1

A Research Paper

This paper was prepared by [redacted], Office of Global Issues. Comments and queries are welcome and may be directed to the Chief, Economics Division, OGI, [redacted] 25X1 25X1

Secret

GI 85-10304
December 1985

Sanitized Copy Approved for Release 2011/06/27 : CIA-RDP86T00586R000500600004-6

 25X1

Shifts in the World Cotton Market: Increasing Pressure on US Interests 25X1

Summary

Information available as of 18 October 1985 was used in this report.

The glut in the world cotton market and changes in production and trade patterns are likely to increase pressure on US interests:

- The glut is damaging the already shaky economies of many cotton-exporting LDCs important to the United States. Pakistan, Sudan, Mexico, El Salvador, Peru, and Paraguay all earn considerable foreign exchange from cotton exports, have a myriad of economic problems, and have experienced a marked drop in cotton export earnings.

- As additional LDCs move into textile production because of low prices for raw cotton, the flow of textiles to the United States and other industrialized countries will increase, adding to protectionist forces and perhaps courting serious international disputes.

- By keeping prices depressed, the glut will also have an unfavorable impact on US cotton exports, adding to the US trade deficit and significantly increasing US farm support expenditures over the next few years. 25X1

These stresses are already being felt in US trade relations. Specifically, as the negotiations on the expiring Multifiber Arrangement unfold, the United States faces increasing pressure from LDCs for greater access to its textile markets in return for raw cotton sales. Burgeoning US stocks of surplus cotton—priced too high for current world market conditions—are attracting bids for concessional sales and grants from African and Asian governments that need cotton as feedstocks for their textile mills. 25X1

Beyond these trade concerns, the impact of continued low world cotton prices on export earnings will add to LDC economic and political problems in several countries. A Pakistani foreign exchange crisis brought about largely by lagging cotton revenues would precipitate demands on the part of the Zia government to postpone payments due the United States on foreign military sales loans. In Peru, economic straits caused in part by low cotton export earnings have fostered strengthened ties between Lima and Moscow. The economies of Sudan and El Salvador are also in poor shape to absorb any further losses in cotton earnings. 25X1

[redacted]

25X1

Moreover, we anticipate a spillover of tensions into the politically charged textile arena and the possible imposition of trade measures against the United States by some LDCs. Stimulated by low world cotton prices, the rapid development of labor-intensive textile industries in Thailand, Indonesia, India, and Pakistan has spurred stronger economic growth, greater employment, and a higher standard of living. If additional growth in textile exports is stymied by protectionism, serious strains in East Asian–industrial country relations could result. [redacted] 25X1

25X1

According to Embassy reports, moreover, he and Prime Minister Prem of Thailand have agreed to coordinate strategies for retaliation if the United States abrogates bilateral textile trade agreements. [redacted] 25X1

25X1

Shifts in the World Cotton Market: Increasing Pressure on US Interests

25X1

A Market in Transition

Shifts in the global market for raw cotton have fostered a huge stock overhang, pushing prices to 10-year lows with no relief in sight (figure 1). The surpluses stem in part from producers' overestimation of the growth rate of cotton mill use; since 1978 mill use has increased by an average 2 percent a year (table 1). Lack of investment capital and growing resistance by labor unions, as well as misguided government tax and trade policies, have retarded the progress in modernization of the cotton industry in many countries. Moreover, the governments of the emerging Asian textile producers—India, Pakistan, China, Thailand, and Indonesia—are emphasizing the production of synthetics, blended fabrics, and other natural fibers, such as ramie, in plans for expansion of their textile sectors.[1]

25X1

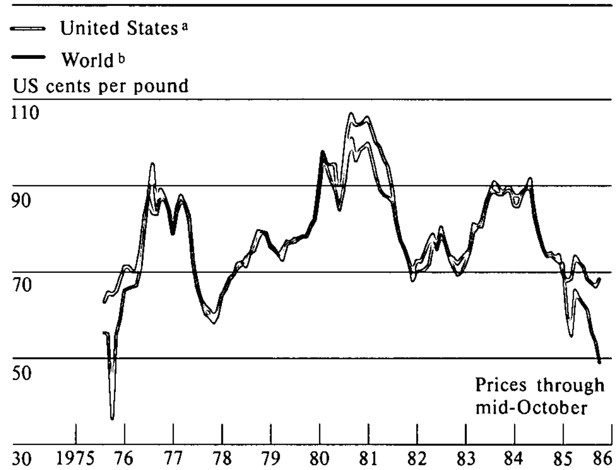
The weakness in demand was accentuated last year—marketing year (MY) 1984/85—when the market was flooded with cheap cotton, largely because of Chinese and Pakistani inability to absorb bumper crops generated by agricultural policy changes and unusually favorable weather. According to the US Department of Agriculture (USDA), production totaled 84 million bales, representing a 20-percent increase over the previous record (table 2). Shortages in MY 1983/84 encouraged increased plantings in China and in the United States, as well as in other major exporting countries; weather conditions were especially favorable for Southern Hemisphere crops. The Chinese crop increased by a third from a large base, Pakistani production doubled, and both the United States and Australia registered nearly a 70-percent gain. Only countries in political turmoil—Sudan, El Salvador, Nicaragua—suffered setbacks.

25X1

[1] Ramie, a natural fiber similar to flax, hemp, and jute, is grown and processed largely in China. Although it is valued for fiber strength and resilience, it has not been widely used in textiles because it must be prepared for weaving by hand.

25X1

Figure 1
Cotton Prices, 1975-85 (c.i.f. Northern Europe)



a Memphis territory middling 1 3/32.
b Cotton outlook A index.

25X1

307454 11-85

Shifting Regional Trade Patterns

The market is also experiencing significant shifts in the patterns of trade (figure 3). Most important, the bulk of cotton trade is moving to Asia, driven by the massive production gains in China—China, a net importer in 1980, now exports about 1.2 million bales a year, or about 6 percent of total world exports—as well as by the increasing mill use throughout Southeast Asia (table 3). Elsewhere:

- South American production is uneven and is increasingly being used in growing regional textile industries.

Table 1
World Cotton Market Trends

Million 480-pound bales

Year [a]	Beginning Stocks	Raw Production	Consumption (*mill use*)	Exports
1977/78	22.7	63.9	60.9	19.7
1978/79	26.2	59.6	63.3	19.8
1979/80	21.8	65.2	66.2	23.2
1980/81	21.3	64.8	65.9	19.7
1981/82	21.5	70.8	66.1	20.2
1982/83	25.4	67.4	68.2	19.4
1983/84	24.9	67.8	69.0	19.2
1984/85 (*preliminary*)	24.8	84.4	69.7	20.5
1985/86 (*estimate*)	40.1	79.6	71.3	20.1
1986/87 (*forecast*)	47.4			

[a] Marketing year, 1 August through 31 July.

Source: USDA/FAS, 4 September 1985.

25X1

- Cotton production has leveled off in Central America and Africa, and trade shares are largely declining.

- The United States, although handicapped by distance from expanding markets and high prices, has managed to hold on to a third of global trade by being a reliable supplier of high-quality cotton.

- The Soviet Union, the second-largest exporter, has been unable to increase production to keep up with increasing internal demand. The USSR has seen its share of world exports of raw cotton whittled from 21 to 17 percent in the last four years.

Submarket Shifts

Trade within the two main, highly differentiated segments of the market also is in flux. The United States still dominates trade in the high-quality, long-staple cotton used for fine fabrics—usually shipping about 3.5 million bales annually to markets in Europe and Japan—but price competition from Australia and Pakistan is rapidly eroding the US trade position. US prices are about 17 cents per pound higher on cotton delivered to Europe and 18 cents per pound higher on deliveries to Japan than offerings of similar quality from Australia, which emerged last year as a major exporter. US sales of high-quality cotton to the Soviet Union are also being pressured by Australian, Pakistani, and Chinese exports. Some African and Latin American producers—Egypt, Zimbabwe, Tanzania, Paraguay, Mexico—also have captured specialty shares of the high-quality cotton market with dependable and consistent quality shipments; however, limited resources, including water and arable land, will preclude major export surges from these countries.

25X1

Competition is even fiercer in the market for the short-staple cotton, which is used for heavier, coarser textiles. This segment of trade usually accounts for US sales of about 2 million bales annually; however, because of foreign competition, 1985 sales probably

Table 2
Major Cotton Producers

Million 480-pound bales

	1981/82	1982/83	1983/84	1984/85	1985/86 *(estimated)*
World total	**70.8**	**67.4**	**67.8**	**84.4**	**79.6**
China	13.6	16.5	21.3	27.9	22.5
United States	15.6	12.0	7.8	13.0	13.8
USSR	13.3	11.9	12.3	11.7	12.5
India	6.4	6.3	6.1	6.7	7.0
Pakistan	3.5	3.8	2.2	4.5	3.9
Brazil	3.0	3.0	2.6	3.8	3.2
Turkey	2.2	2.2	2.4	2.7	2.4
Egypt	2.3	2.1	1.9	1.8	2.0
Australia	0.6	0.5	0.6	1.0	1.0
Sudan	0.7	1.0	1.0	0.9	1.0
Mexico	1.4	0.9	1.0	1.3	0.9
Europe	0.9	0.8	0.8	1.0	0.8
Syria	0.6	0.7	0.9	0.8	0.8
Argentina	0.7	0.5	0.8	0.8	0.7
Paraguay	0.4	0.4	0.4	0.6	0.5
Colombia	0.4	0.2	0.4	0.6	0.5
Zimbabwe	0.3	0.3	0.3	0.5	0.5
Israel	0.4	0.4	0.4	0.4	0.5
Peru	0.4	0.2	0.3	0.5	0.4
Other	4.1	3.7	4.3	3.9	4.7

Source: USDA/FAS, 4 September 1985.

25X1

will amount to no more than 1 million bales, according to USDA estimates. Brazil is making inroads into US, European, and African markets, and China is selling in Hong Kong, Indonesia, Thailand, South Korea, and Japan. Although Chinese cotton is of inconsistent quality, it is cheap enough to tempt Asian textile manufacturers operating at the margin. Pressed by Chinese cotton, Pakistan is cutting prices and seeking new customers in northern Africa and Europe. Algeria and Morocco purchased Pakistani cotton for the first time in 1984 in response to a government trade promotion and have sent trade delegations to Tunisia, France, and several East European countries.

25X1

The Role of Countertrade

Stiff trade competition and cash shortages among cotton importers are pushing LDC exporters increasingly into countertrade arrangements. For example, in Sudan, where cotton is the principal source of revenue, more than 25 percent of the 1984 crop—with a potential value of $75 million—was shipped under barter and debt-servicing arrangements, according to Embassy reporting. About a sixth of 1984 Peruvian cotton exports was shipped to the Soviet Union under a bilateral agreement to pay for arms and other Soviet

Table 3
Major Cotton Traders:
Regional Patterns of Trade, 1984

	Amount Exported *(thousand 480-lb bales)*	Amount Imported *(thousand 480-lb bales)*	Index of Exports *(1980=100)*	Index of Imports *(1980=100)*
United States	6,485	NEGL	109	. . .[a]
USSR	3,200	1,000	79	654
Europe				
European Community	NEGL	2,600	. . .[a]	116
Spain	NEGL	210	. . .[a]	103
Switzerland	NEGL	406	. . .[a]	107
Turkey	640	NEGL	62	. . .[a]
Eastern Europe	NEGL	1,775	. . .[a]	102
Australia	600	NEGL	206	. . .[a]
Asia				
Japan	NEGL	3,300	. . .[a]	103
China	1,200	100	20,000	3
South Korea	NEGL	1,630	. . .[a]	107
Hong Kong	140	950	215	115
Taiwan	NEGL	1,150	. . .[a]	119
Indonesia	NEGL	575	. . .[a]	117
Thailand	NEGL	520	. . .[a]	129
India	150	120	28	600
Pakistan	1,150	NEGL	77	. . .[a]
Malaysia	NEGL	150	. . .[a]	115
Philippines	NEGL	95	. . .[a]	77
Singapore	NEGL	105	. . .[a]	122
Vietnam	NEGL	175	. . .[a]	125
Latin America				
Mexico	625	NEGL	76	NEGL
Paraguay	450	NEGL	130	NEGL
Brazil	400	NEGL	952	NEGL
Colombia	350	NEGL	138	NEGL
Argentina	275	NEGL	183	NEGL
Guatemala	250	NEGL	51	NEGL
Nicaragua	250	NEGL	77	NEGL
El Salvador	90	NEGL	63	NEGL
Peru	160	NEGL	109	NEGL
Venezuela	NEGL	80	. . .[a]	250
Africa				
Sudan	800	NEGL	188	. . .[a]
Egypt	600	NEGL	80	. . .[a]
Zimbabwe	250	NEGL	106	. . .[a]
Ivory Coast	250	NEGL	126	. . .[a]
Nigeria	NEGL	250	. . .[a]	1,786

Table 3 (continued)

	Amount Exported *(thousand 480-lb bales)*	Amount Imported *(thousand 480-lb bales)*	Index of Exports *(1980=100)*	Index of Imports *(1980=100)*
Africa (continued)				
Mali	200	NEGL	114	...[a]
Tanzania	150	NEGL	84	...[a]
Burkina	125	NEGL	147	...[a]
South Africa	NEGL	75	...[a]	268
Uganda	50	50	1,000	...[a]
Tunisia	NEGL	60	...[a]	113
Ghana	NEGL	30	...[a]	273
Senegal	35	NEGL	175	...[a]
Middle East				
Israel	370	NEGL	133	...[a]
Syria	500	NEGL	152	...[a]

[a] Not pertinent.

[redacted] 25X1

goods. China, historically a cash-only seller, has begun trading cotton for oil and exploring the possibilities of expanded trade through barter with several ASEAN countries and the USSR. [redacted]

Foreign Responses to Market Conditions

The severity of cotton market problems is leading cotton-exporting countries that have large surpluses in most years—Pakistan, China, and Brazil—to adjust their agricultural and trade policies to be able to compete more effectively for trade shares. According to Embassy reporting:

- Pakistan is setting up cotton sales offices in the Middle East and Europe.
- Brazil authorized a cotton export subsidy early this year to bring Brazilian prices in line with world prices.
- China began to address fundamental quality problems by planting higher quality seed last spring, by installing modern ginning and baling equipment, and by expanding storage facilities. In addition, liberalized free market opportunities now provide incentives to Chinese farmers to produce the kind of cotton that export markets and domestic mills will buy. [redacted] 25X1 25X1

Some exporters are also modernizing and revitalizing their textile sectors to use their increased cotton production to be able to compete internationally in value-added cotton products. Both China and Pakistan, increasingly concerned about the rapid depletion of foreign exchange reserves, recently announced major policy revisions aimed at stimulating exports of yarn, textiles, and apparel, according to Embassy reports. In January the Chinese National Textile Import and Export Corporation (Chinatex) was reorganized to allow mills greater autonomy both in purchasing raw cotton and in marketing textiles. At the same time, the new Pakistani Government announced increased investment incentives for the textile export industry, including the elimination of import tariffs on machinery needed for modernization of plants. The Government of Brazil is also taking steps in this direction, exempting cotton exports from value-added taxes and lowering export taxes on textiles from 12 to 1 percent. [redacted]

LDC importers of raw cotton are counting on the textile sector to spur economic growth, according to Embassy reports. In June, New Delhi announced a new textile policy designed to improve the export potential of India's textile industry. The government has taken measures aimed at better coordination between cotton farmers and textile industry planners, modernization of the textile sector, and providing incentives to textile exports. By increasing imports of raw cotton, both Indonesia and Thailand aim to expand textile exports significantly within the next few years, although their cotton production efforts have lagged far behind mill demand. Indonesia produces only about 3 percent of domestic consumption; the Thai harvest supplies only about a third of domestic requirements. [redacted]

Outlook for the Cotton Market

A turnaround in the international cotton market is unlikely for at least four years, according to USDA analysis. Trends in cotton mill use suggest continued slow growth of consumption. Modernization of the antiquated, problem-ridden textile industries of Pakistan, India, and China and expansion of the relatively new industries of the ASEAN countries could be slow in coming, particularly if export expansion is further limited by increased textile trade barriers in developed country markets. Similarly, cotton consumption will be held back by the growing popularity of polyesters and blends in the developing countries. [redacted]

In spite of sluggish growth in demand and low world prices, the global crop currently being harvested will be reduced by only about 6 percent from last year's record, according to USDA estimates; and no significant declines seem likely in MY 1986/87. Although China has lowered procurement targets and the level of guaranteed purchases for cotton, cotton production is still substantially more lucrative than other crops, according to Embassy reports; and we believe cotton acreage probably will increase. China can earn almost double the amount of foreign exchange from a hectare of land sown to cotton than from wheat—a positive inducement for the government to increase output and exports of cotton at the expense of wheat. [redacted] Pakistan plans to cut back its 1986 crop, government agricultural policies now being formulated suggest continued support to cotton production, according to Embassy reporting. [redacted]

25X1
25X1
25X1
25X1

As a result of increased production, most governments will intensify their efforts to gain increased shares of the cotton export market, largely by improving product quality. In view of Chinese, Pakistani, and Australian moves to develop new varieties of cotton that produce better quality lint, to modernize ginning and port facilities, and to renew marketing campaigns, we expect the share of fine staples in overall cotton production to increase and the international competition in high-quality cotton to intensify. [redacted] Australia hopes to double such exports next year, and India has a large exportable surplus of long-staple cotton. The Soviet Union is also concentrating on quality improvements, which could eventually lead to a larger volume of high-quality cotton for export. [redacted]

25X1
25X1
25X1
25X1
25X1

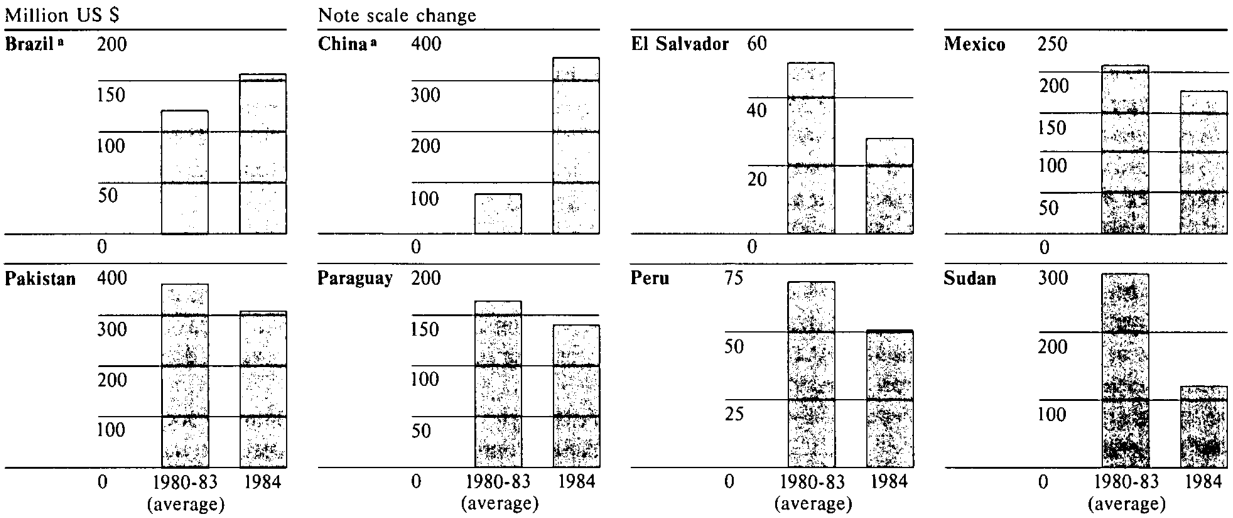
Implications for LDCs

The Cotton Exporters

The depressed cotton market is presenting an economic challenge to a number of countries important to the United States. The flexibility of government policy will determine how key exporters weather the slump (figure 2). Brazil has been able to adjust to low prices with increased exports. According to Embassy reports, however, other big cotton producers, including key debtor countries, are faltering: 25X1

- Because of declining prices, Mexico has been forced to cut back production by a third and has seen its earnings decline sharply.

Figure 2
Selected LDCs: Cotton Export Earnings



[a] The increase in 1984 export earnings reflects sharply increased export volume that more than compensated for reduced prices.

25X1

307455 11-85

- The Paraguayan economy, which had begun to recover from two years of steep recession, has been reeling since mid-1984 from the deterioration in the country's terms of trade in cotton.

- The new Peruvian Government has not yet announced plans for developing export markets for Peruvian cotton under current market conditions. According to Embassy reports, excessive stocks of unsold cotton are beginning to accumulate.

- Sudan, with 1 million bales of unsold cotton in deteriorating condition in warehouses and about a million bales currently being harvested, has so far failed to develop a feasible cotton marketing strategy.

- Pakistan has sought additional financial assistance from the United States and the International Monetary Fund to avoid a foreign exchange crisis brought about largely by lagging cotton revenues.

The Textile Exporters

In sharp contrast, some Asian governments—in Thailand, India, Indonesia, China—are attempting to turn the crisis in the cotton market to advantage in value-added exports. Although the modernization of textile export industries is being hampered by a range of constraints, including capital stock and investment shortfalls, bureaucratic corruption and inefficiency, and power shortages, significant political and economic forces should assure the continued dynamism of the sector:

- In Thailand, prominent political and military leaders have direct business connections in the textile industry. According to Embassy reports, these links, in addition to the industry's potential as an employer and foreign exchange earner, point to continued government advocacy of the sector's interests.

25X1

Africa: Being Bypassed Again

In Africa, where cotton and textiles are a key element in economic planning, cotton production is losing out to food crops in the competition for resources. Despite government attempts to increase exportable surpluses in the past few seasons by ratcheting farm prices up, disincentives such as poor farm-to-mill transport, higher prices for food and feed commodities, and increased domestic mill consumption are reinforcing a downward trend in exports. Although West African and Tanzanian cotton have been gaining popularity in Europe because of their fiber strength characteristics and Egypt, Sudan, and Zimbabwe have assured markets in East Asia and Europe for their premium-priced, extra-long-staple cotton, export supplies and shipping capabilities are extremely limited throughout the region. [redacted]

The slippage in African cotton production is retarding growth of the region's textile and clothing industries. This sector has been given economic priority because of the high employment potential of the cloth industry and the relatively small scale at which efficiency can be achieved. However, the spinning, weaving, and apparel manufacturing industries of western and southern Africa, as well as of Egypt, Sudan, and Tanzania, operate at no more than 80 percent of capacity as a result of unpredictable raw material availability and prices, [redacted] *Addressing these problems and recognizing the potential of cotton in value-added foreign currency earnings and import substitution, some governments have been diverting export supplies into domestic mills. Others have struck barter deals, such as the agreement Ghana signed with Mali in July involving the exchange of textiles for cotton.* [redacted]

- In India, the Gandhi government has not yet clarified the specifics of its new textile policy or worked out the financial implications. We believe New Delhi's handling of the implementation will be an important test of commitment to economic liberalization. Powerful interest groups—cotton farmers and textile labor unions that see the new policies resulting in raw cotton price cuts and loss of jobs—began protesting in October with a major public demonstration, and farm leaders are continuing to campaign with labor union and opposition party support.

- Embassy reports indicate that Chinatex is moving quickly to strengthen links with textile mills, and [redacted] the Chinese Government has been selling surplus cotton to domestic mills at greatly reduced prices. 25X1

- In Indonesia, Embassy reporting indicates the Ministry of Trade is systematically and consistently pushing both the government bureaucracy and the private sector in the textile export drive. [redacted] 25X1

Although the textile manufacturing sectors in these Asian countries have the potential to increase the rate of growth of export earnings as well as to provide more jobs, government leaders recognize that a slump in the industry could spark a political tinderbox. In Thailand, where a recent US embargo on 1985 Thai apparel imports could cost 50,000 workers their jobs, according to Embassy reports, Prime Minister Prem and his advisers consider the country's economic difficulties the most urgent problem facing the government. In our view, a cutback in textile industry earnings and jobs would bring considerable pressure for change from prominent bankers, opposition political leaders with business interests in the sector, critics of government economic policy, and labor groups. In India, unemployment in the textile industry touched off riots last spring, and the labor situation in the mills remains volatile, according to Embassy reports. [redacted]

25X1 25X1 25X1 25X1

Implications for the United States

Current trends and trade shifts in the global cotton and textile markets are creating serious economic and political worries for the United States by reducing US cotton export sales, increasing pressures for US textile import constraints, and contributing to economic and political problems in countries important to US interests. [redacted] 25X1

Reduced Cotton Exports

Prices well above Asian levels for comparable quality cotton will cut the United States out of a significant amount of trade in MY 1985/86, eroding the US market share from a third to about one-fifth, according to USDA estimates. Customers in the Far East and Europe, in particular, are taking increased advantage of lower cotton prices in nearby markets; and the governments of many developing country importers are finding the countertrade arrangements offered by China, Pakistan, and Brazil attractive in view of foreign exchange shortages. Brazil's recent cotton-for-oil deal with Nigeria and an Indonesian barter deal with China last summer exchanging cotton for man-made fiber are likely to cut US sales to those markets in half during the current marketing year, according to USDA. [redacted]

Rapid quality advances on the part of competing suppliers could permanently truncate US export sales. Despite a preference for US cotton, major customers, such as Japan and Taiwan, have adjusted to buying cotton from China, Pakistan, and Australia and are likely to find increasing amounts of consistently good quality, long-staple cotton available from these suppliers. [redacted] sales of very-high-grade Texas-Oklahoma cotton (harvested in the summer, well ahead of the rest of the world fall crop) were cut in half this year largely as a result of the increased availability of the cheaper but similar quality Australian cotton (harvested in the Northern Hemisphere spring). In addition, the USSR—a major buyer of US long-staple cotton—will, in our estimation, soon begin to buy from nearby sellers, such as China and Australia, as the quality of long-staple cotton now offered becomes more consistent. [redacted] 25X1

As a result of these shifts, the United States is likely to be burdened with a large cotton surplus when the current marketing year ends next July. With a fall 1985 harvest only slightly smaller than in 1984 and export sales limited to no more than 4 million bales, according to USDA estimates, about 9 million bales of unsold US cotton will accumulate at a cost of $2 billion—nearly as great as the cost of the US wheat surplus. As US cotton surpluses mount, pressure for increased concessions on cotton sales and grants will come, in our estimation, both from governments—the Philippines, Bangladesh, and Egypt—already receiving substantial amounts of US aid and from African countries—Nigeria, Zaire, Kenya, Ghana—that do not produce enough cotton for domestic mills and lack foreign exchange reserves to import. [redacted] 25X1

Multifiber Arrangement Renewal

Negotiations on the renewal of the Multifiber Arrangement (MFA), which sets guidelines under the auspices of the General Agreement on Trade and Tariff (GATT) for bilateral textile and clothing trade, have begun and will continue at least until June 1986, when the current pact expires. Although MFA renewal talks will not be directly linked to a new GATT round, developing country members of GATT are already placing liberalization of world textile trade high on their list of objectives. Knowledge that textiles and clothing could be a significant part of a new round's final package may prompt MFA participants to extend the MFA only until the end of the GATT round. [redacted] 25X1 25X1

Most exporter countries have opposed renewal in public statements, because the MFA allows importer countries significant latitude in limiting trade—a departure from GATT rules. The MFA permits importers to impose quotas without having to demonstrate injury to domestic producers, apply the quotas on a nondiscriminatory basis, or choose between compensating the restricted country or facing retaliation. However, most exporters—including the large ones: Hong Kong, South Korea, Taiwan, and China—fearing protectionism in the absence of any guidelines, already seem inclined to accept renewal while continuing to work for gradual phaseout and return to GATT rules. Many small- and medium-sized exporters—Thailand, Indonesia, Pakistan, for example—find MFA quotas helpful because they guarantee shares of industrial country markets and protect them against major exporters.[a] [redacted] 25X1 25X1 25X1

[redacted] 25X1

Even US concessional sales may be hard to come by, however. Although US cotton aid in the form of credit or credit guarantees has already been granted to several low-income, textile-producing countries, local sales have gone slowly as a result of the substantial price difference between US and Asian supplies. For example, according to Embassy reports, buyers in Zaire, under government pressure to participate in the recently initiated US PL-480 program, complained of a price differential of 40 percent between US and locally grown cotton and an even greater gap between US and Asian cotton. As compensation, they demanded further price discounts. Similarly, cotton millers and traders in the Philippines, although concerned about the quality of lower priced Chinese and Pakistani cotton, evinced little interest in buying US cotton under a proposed 1985 credit guarantee program because Australia, Pakistan, and China were offering cotton of the specified quality at prices 20 to 25 percent lower, according to Embassy reporting. [redacted]

Increased Pressure for Access to Markets

The indirect fallout from the use of low-priced cotton as feedstocks in growing Third World textile industries will be the intensified pressure from LDC governments for greater access to US textile markets. Caught in the squeeze between overproduction on one hand and growing textile protectionism on the other, governments such as Brazil, Pakistan, India, and China will continue to push for larger quotas in bilateral negotiations. Although generally pleased with the market-share protection available under existing trade arrangements, these governments can be expected in the long run to press for a freeing of textile trade as they gain confidence in their ability to compete. [redacted]

In our judgment, emerging textile traders, such as India, the Philippines, Thailand, and Indonesia, will attempt to trade concessions on US textile import quotas for purchases of raw cotton from the United States. A recent comment in the Thai press, for example, has suggested retaliation on US cotton imports in response to any US protectionist moves on textiles.[3] Similarly, Indonesia, which usually buys most of its cotton from the United States, recently signed letters of intent with China to purchase about half of its 1985 needs—partly in reaction to US textile policy, according to Embassy reports. As the marketing year progresses and textile talks enter full swing, the United States is likely to experience intensified strains on relations. According to Embassy reports, President Soeharto and Prime Minister Prem of Thailand have agreed to coordinate strategies for retaliation in the event of US abrogation of bilateral textile agreements [redacted] 25X1

LDC Political Fallout

The developed country response to LDC demands for market access could affect the future of Asian governments—India, Thailand, Indonesia—that have high political and economic stakes riding on the textile industry. Consequently, a failure to keep US markets open could strain relations with these governments. [redacted] 25X1
[redacted] considerable 25X1
apprehension on the part of President Soeharto of Indonesia about the outcome of current debates on textile protection legislation in the United States. 25X1
Although the Prem government in Thailand has demonstrated an ability to survive political difficulties, we believe that a sharp cutback in Thai textile exports would dramatically increase the chances for a second coup attempt. If disruption of the textile industry were to result in public disorder, a possible scenario might see some elements of the military intervening to oust Prem. [redacted] 25X1

Although the impact of textile industry problems on political stability in these countries is hard to predict, it could be considerable because they all have large investments in textiles. According to Embassy reports: 25X1

- Textile manufacturing, *India's* largest and oldest industry, generated 15 to 20 percent of industrial

[3] According to Embassy reports, US agricultural exports to Thailand were particularly hard hit by government tariff increases in October 1984 that increased duties on US cotton by 300 percent. [redacted] 25X1

jobs and accounted for more than 20 percent of manufacturing production, as well as 12 percent of exports in the period 1983-84.

- Cotton textile manufacturing is *Pakistan's* most important industry, accounting for about 40 percent of industrial employment and 35 percent of manufactured exports.

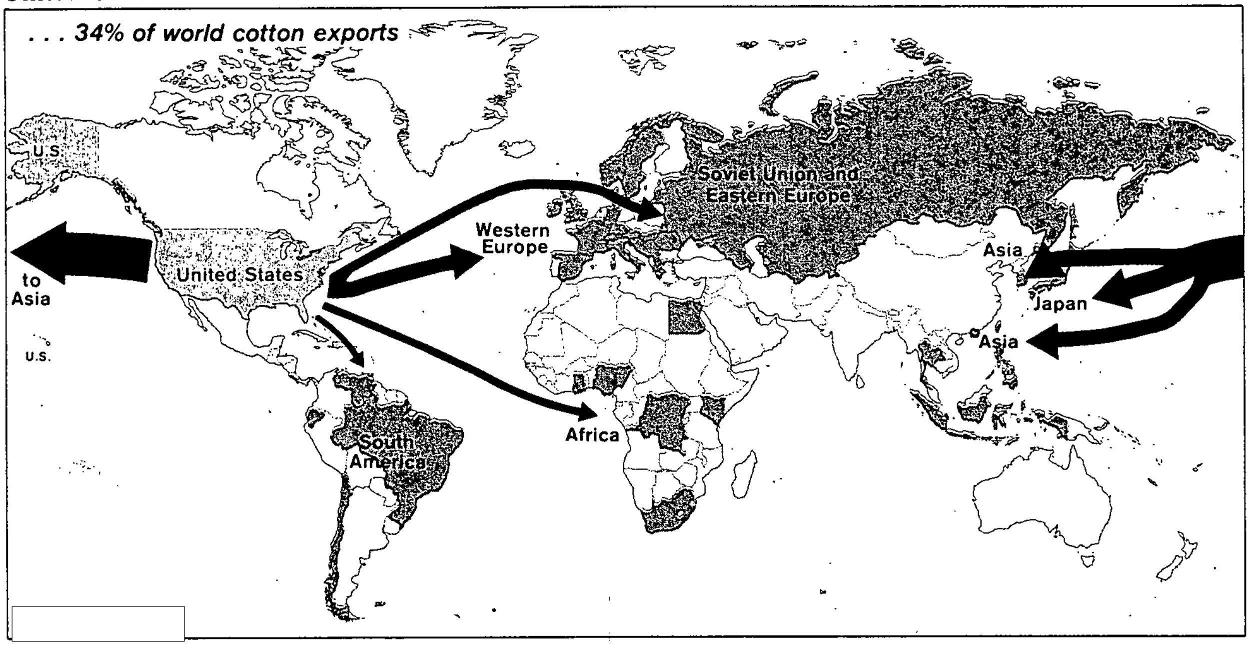
- The *Indonesian* textile industry employs 3 percent of the total work force, or 27 percent of all workers engaged in manufacturing. Textile and garment exports amounted to 9 percent of nonoil exports in 1984.

- Textile manufacture is by far the leading industrial employer in *Thailand*. The textile and apparel industry accounted for 25 percent of total Thai value-added manufacturing in 1984. 25X1

Apart from repercussions in countries with heavily politicized textile industries, continued depression in international cotton trade could have serious implications for the economies of Nicaragua, El Salvador, and Sudan—countries where cotton is a leading export earner and where diversification into value-added cotton industries or into other crops is not possible in the short term. For example, we estimate Nicaragua's revenues from cotton may amount to as little as $20 million in 1985, down from more than $100 million last year. Sudanese officials estimate that cotton revenues, which provide about half of all export earnings, may fall by as much as one-third in 1985. Finally, weak export prices for cotton will further undermine the slow progress of economic recovery in El Salvador, where the Duarte government has publicly acknowledged the importance of the cotton sector to stability. 25X1

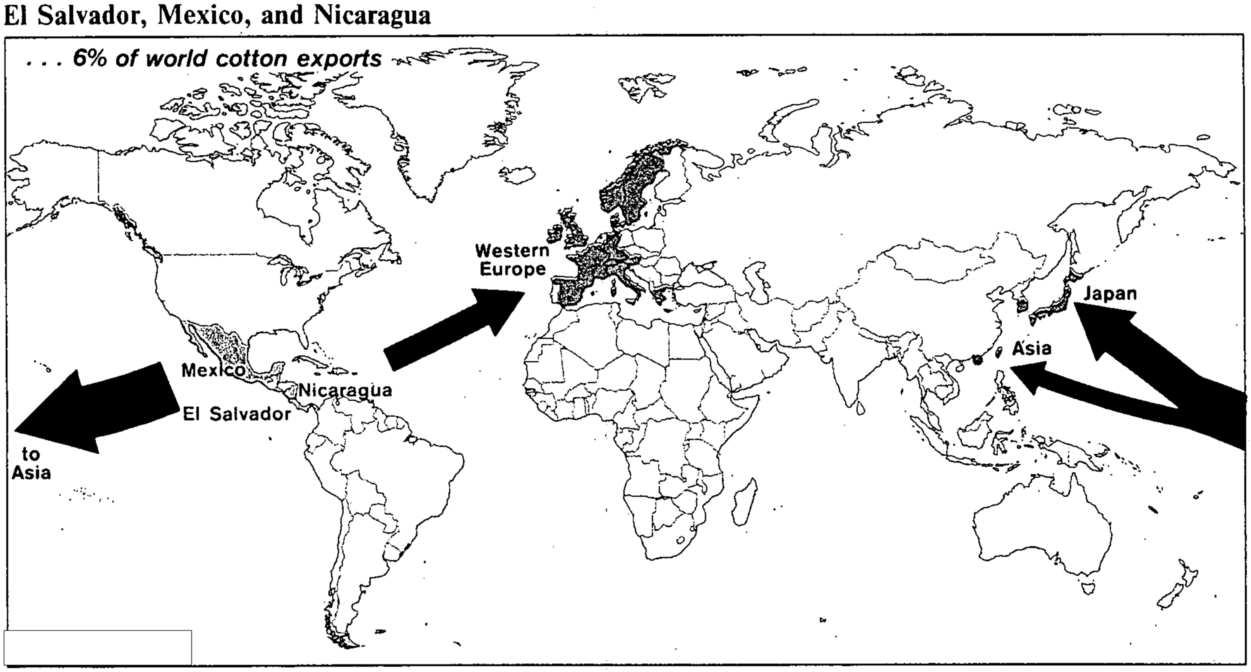
Figure 3
Major Cotton-Growing Countries and Their Export Trading Patterns, 1984

United States



25X1

El Salvador, Mexico, and Nicaragua

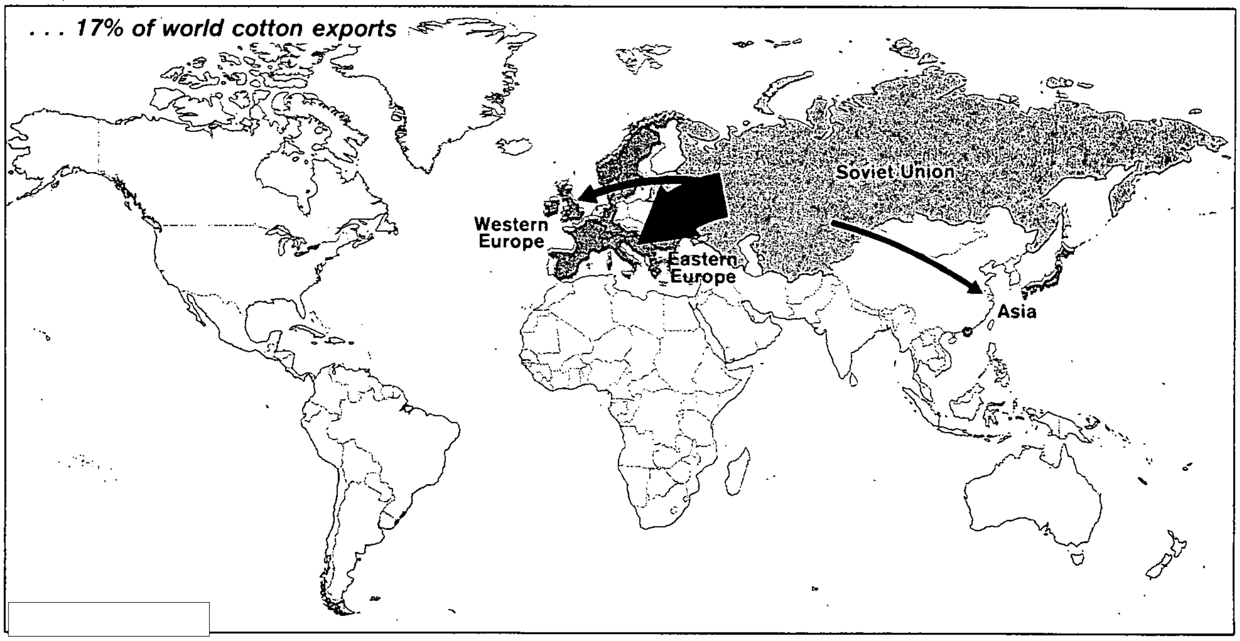


25X1

706421 (547564) 12-85

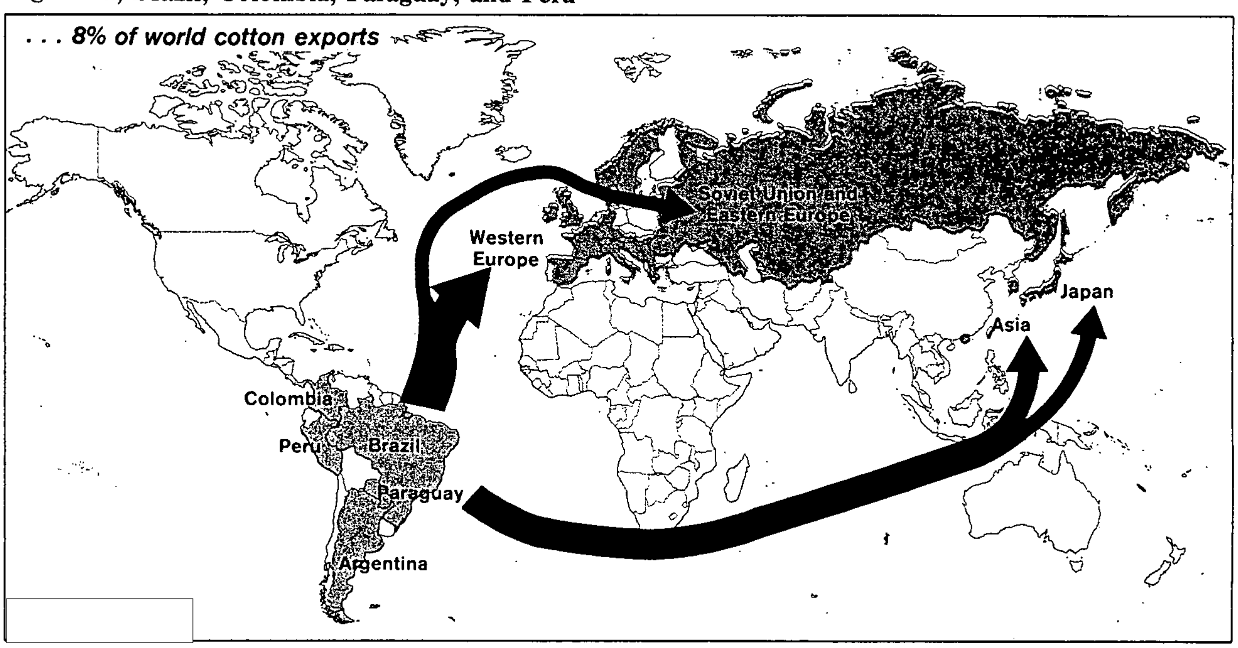
Sanitized Copy Approved for Release 2011/06/27 : CIA-RDP86T00586R000500600004-6

Soviet Union



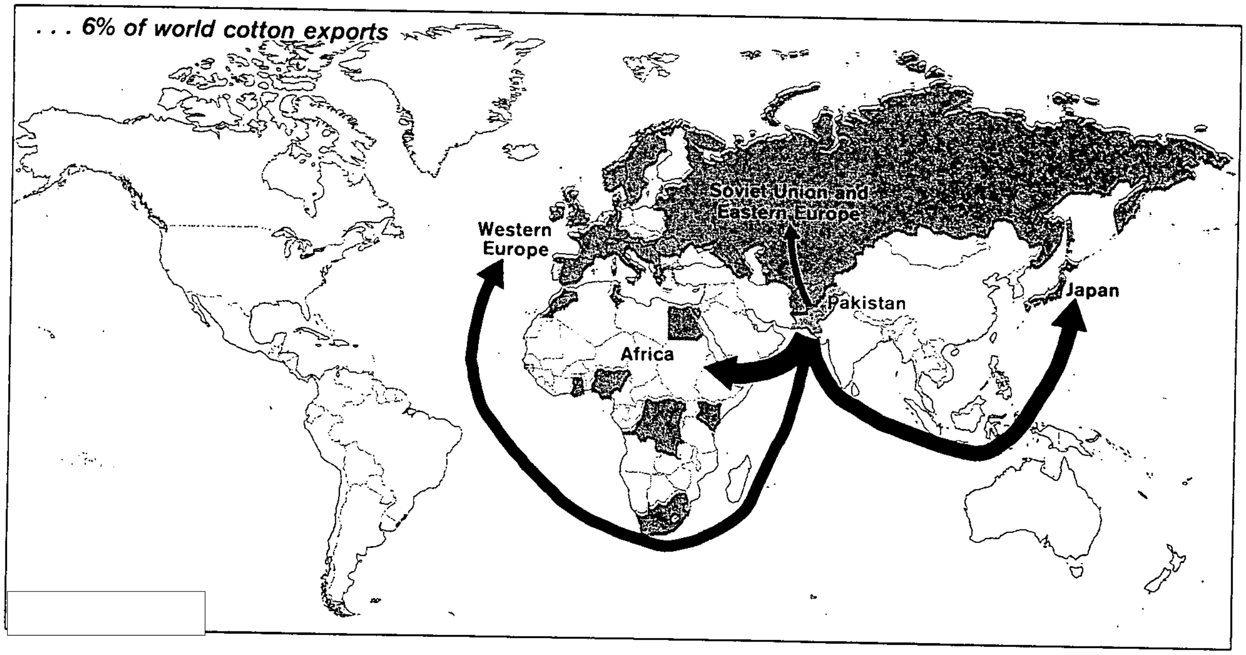
25X1

Argentina, Brazil, Colombia, Paraguay, and Peru



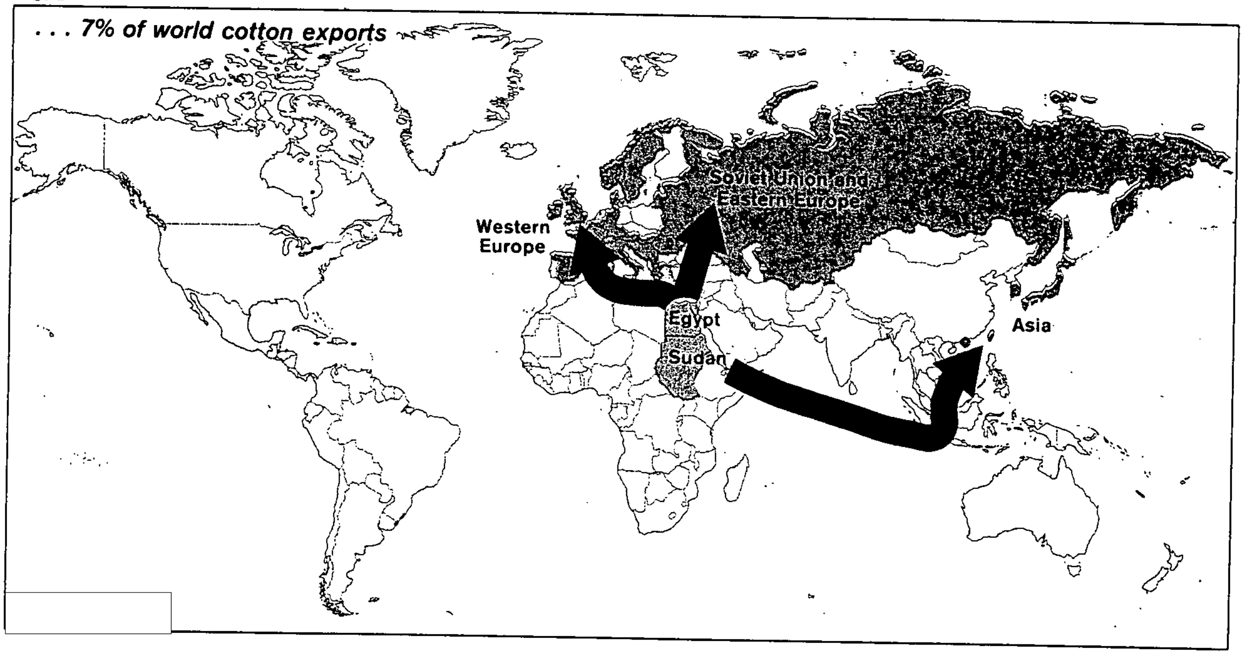
25X1

Pakistan



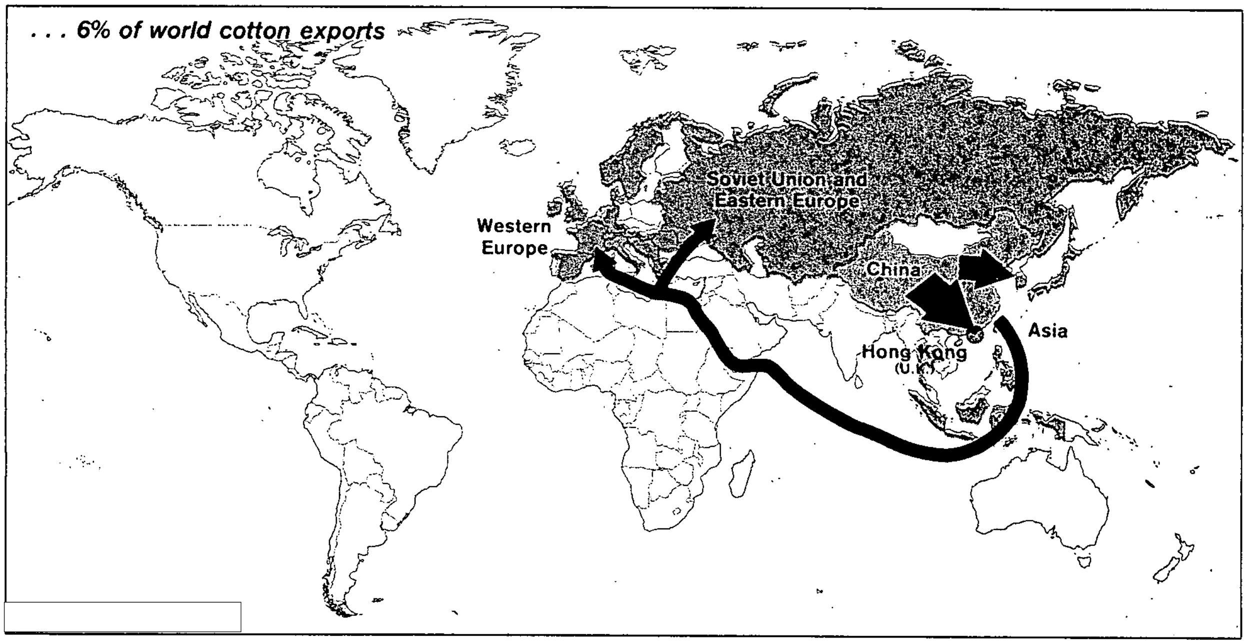
25X1

Egypt and Sudan



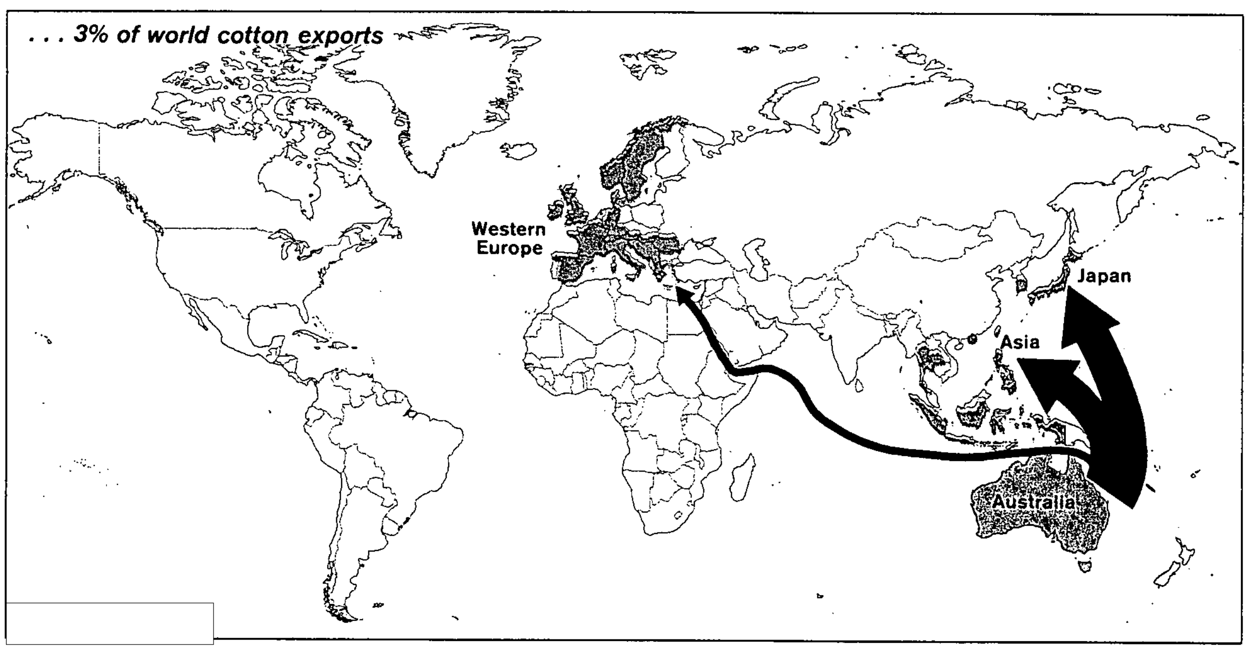
25X1

China



25X1

Australia



25X1