



Can Cotton Survive the Great Lockdown? Initial Demand-Side Impacts of the Covid-19 Lockdown on the Global Cotton Market and Scenarios for Recovery

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Figure 1. Textile processing has resumed, but only partially in some countries.



Summary

The cotton sector plays a vital role in the global economy. Cotton as an agricultural commodity supports over 100 million families engaged in production and as an industrial commodity that is used to produce apparel and textiles. The global cotton market is affected by fundamental factors of supply and demand and thus has been impacted by the Great Lockdown resulting from the COVID-19 pandemic. The pre-COVID-19 trade environment had already been characterised by slowing global economic growth, slowing demand, geopolitical tensions, trade tariffs and a general move away from globalisation. The containment measures that have effectively halted an overwhelming portion of the global economy have and will continue to have deep impacts on the cotton sector.

As countries adopted severe containment measures to limit the spread of disease and protect human health, business activity and many other facets of life have come to a halt. The stringent containment measures to slow the spread of COVID-19 have, and will continue to have, important social and economic costs. As many businesses have been required to slowdown or close for the consideration of public health, in the cotton sector, clothing retailers have closed physical businesses, consumers have slowed clothing demand and manufacturing and supply chain activity in Asia and Southeast Asia have decelerated as orders have slowed or have been cancelled. Although the full impact of the Great Lockdown is not yet known, the potential for a further slowdown in global economic growth is expected and thus provide additional stress to the sector.

This brief provides an initial assessment of the demand side impacts of the Great Lockdown on cotton consumption from a reduction in global GDP growth, employment and consumer demand followed by recovery prospects. While uncertainty has not abated, responsive and transparent policies will help the sector recover in a new normal scenario until the public health crisis can be alleviated.

Additional analysis on support policies and pandemic response policies to small businesses is needed for greater understanding of the impacts on the cotton value chain. Even when the health impacts of COVID-19 have been controlled and uncertainty from the pandemic induced lockdown has abated, the cotton market will likely still be impacted by global trade tensions.

Current Supply and Demand Situation

Prices continue to fall under the pressure of the current environment. The ICAC's global production estimate for the 2019/20 season remains at 26.2 million tonnes as the consumption estimate has been revised downward to 22.9 million tonnes. Consumption estimates are near a 10-year low last seen in 2011 when cotton consumption slowed from a surge in cotton prices. With production outpacing consumption, ending stocks for the 2019/20 season are currently estimated to increase to 21.9 million tonnes, putting pressure on prices and forward season (Figure 2). With supply estimates increasing amidst decreasing demand, the stocks-to-use ratio is expected to rise to 0.96, a historical high, signalling a year's worth of manufacturing supply available in reserve without the

additional need of cotton production. Broadly speaking, when prices are low, farmers are less incentivised to plant cotton. While agricultural commodities are always subject to the uncertainty from weather, the current environment provides additional variability from the erosion of confidence and heightened uncertainty.

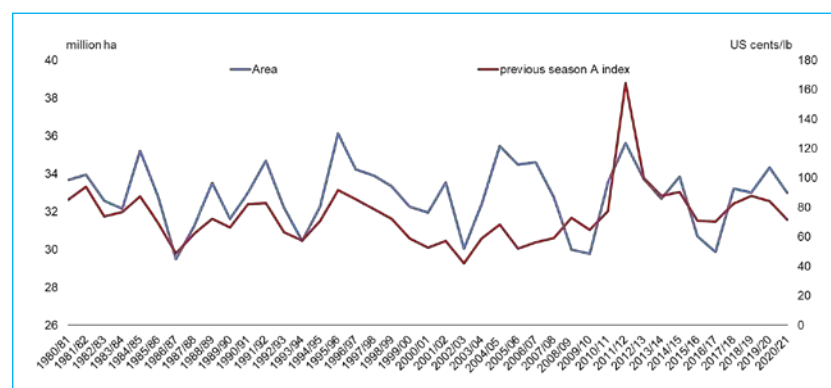


Figure 2. Prices Impact Planting Decisions

Consumption, or mill-use, is dominated by Asian and Southeast Asian countries where textile mills are primarily located. Consumption has been revised down for the current season and the forward season as demand has slowed dramatically from retailers in Europe, North America and China. Global consumption is expected to be 12% lower than the previous season with decreases across all major consuming countries. Consumption or mill-use of cotton lint in China had already been revised down for 2019/20 season considering the trade dispute with the United States and slowing economic growth. The additional slowdown in consumption in China from the COVID-19 lockdown has further reduced textile manufacturing. The consumption estimate for China is now 7.1 million tonnes, a 16% decrease from the previous season. The largest decrease expected in consumption may be in Bangladesh where mill-use is estimated at 1.2 million tonnes, a 25% decrease from the previous season as manufacturers have reported the cancellation and suspension of new orders as consumer demand drops off.

	2018/19	2019/20	change
World	26.0	22.9	-12%
China	8.3	7.0	-16%
India	5.4	4.8	-12%
Pakistan	2.4	2.2	-7%
Turkey	1.6	1.4	-8%
Vietnam	1.5	1.4	-8%
Bangladesh	1.6	1.2	-25%

Table 1. Mill-use Decreases Across All Major Apparel and Textile Manufacturing Countries

Likely Impacts from the COVID-19 Containment Measures and Potential for Recovery

The stringent containment measures needed to halt the spread of the disease have severely impacted economic activity. Restrictions on mobility have shut down business and schools. With non-essential activity limited, employment has increased further contributing to decreased consumer activity. As the pandemic situation continues to evolve, quantifying the impacts is difficult. Economic recovery will be able to begin only once the health impact of the pandemic has been brought under control. While a widely available and distributed vaccine would signal a return to normal, the current best-case scenario timelines for population wide vaccination are likely to be 12-18 months. A new normal, with protective measures in place that allow for the resumption of a greater level of business and economic activity could be envisioned as a mid-term scenario that would reduce unemployment and increase consumer confidence.

The IMF has currently projected that the global economy will contract sharply by 3% in 2020 and hedged the forecast as being made with extreme uncertainty¹. Slowing economic growth leading to a recession would lower cotton mill-use. When GDP growth has slowed, consumption growth has followed (Figure 3) as demand for goods decrease with falling disposable income. Apparel and textile goods are income elastic with demand responsive to changes in consumer income. It should be noted that when economies expand and GDP growth is positive, consumption growth has recovered in the cotton sector. Although other sectors, particularly services such as tourism, may have longer recovery lags, manufacturing should be expected to respond when economic growth recovers. While the IMF's current projection for a 3% decline in GDP is more severe than the 2008 financial crisis, this crisis differs in that it was induced by a public health event rather than weak policies in the financial sector signaling the possibility of a smoother and swifter recovery under appropriate policy responses.

1) IMF, World Economic Outlook, April 2020.

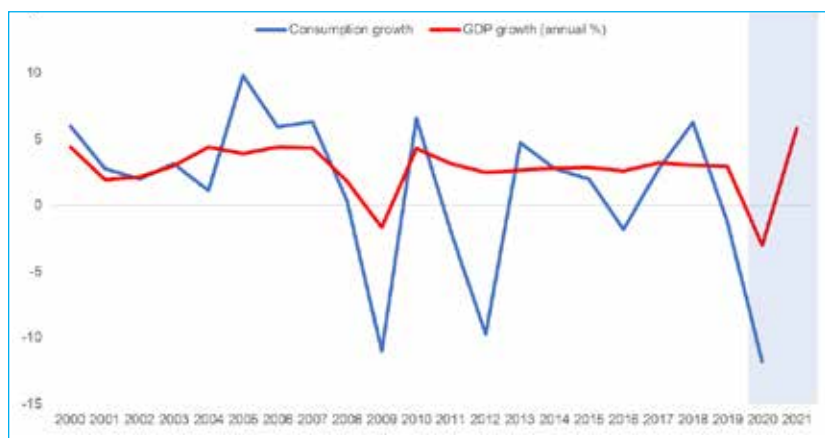


Figure 3. Consumption and GDP growth

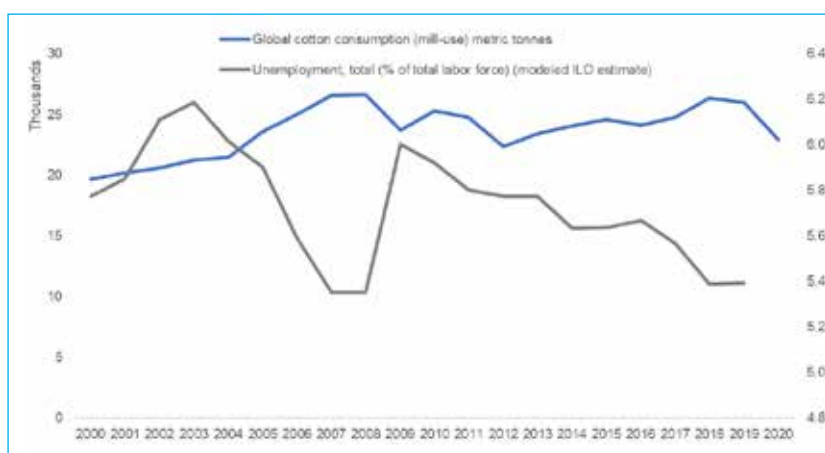


Figure 4. Cotton Mill-Use Increases with Falling Unemployment

Changing consumer behavior from the containment measures have indicated an increase in online spending, but not enough to offset the losses. The widespread lockdown has resulted in record levels of unemployment. In the short term, these are expected to be temporary and social protection policies in many advanced economies provide income protection. Should unemployment become a longer-term impact, cotton consumption would be expected to decrease, however the speed at which workers return from temporary unemployment should mitigate the negative potential impact as income levels and consumer confidence return. According to a consumer confidence survey², sentiment varies across the set of major economies evaluated with greater confidence by consumers in China, India and North America and weaker confidence in Europe. While consumers may expect

to see income losses in the short term, expectations of increased spending should be anticipated as economies recover, thus indicating that with economic recovery, apparel and textile purchases should be expected to rebound (Figure 4).

With higher incomes, consumers in Europe, the United States and Japan are responsible for importing 61.5% of the global apparel imports (Table 2). However, with increasing wealth, other consumers in Asia, particularly in China and Korea, are responsible for emerging growth with 13.7% and 15.9% growth in imports from 2017 to 2018. While GDP growth in advanced economies is expected to contract by 6.1%, growth in emerging economies, again particularly those in Asia and primarily China are expected to slow by a lesser margin. China remains the motor for growth in the global economy with a projected growth in 2020 of 1% (Table 3). While this would be the smallest growth in over 20 years, the resiliency of economic expansion is expected to enable a stronger rebound than other countries. Recovery from the pandemic lockdown has already begun in China and many other Asian countries as containment measures have been eased and businesses begin to reopen.

Importer	Value (billion USD)	Global Share (%)	Growth rate (%)
Korea	11	2.0	15.9
China	8	1.6	13.7
Switzerland	8	1.4	12.6
Japan	30	5.7	7.8
Russia	8	1.5	7.3
Canada	11	2.0	4.9
EU28	204	38.4	2.8
USA	92	17.4	0.7
Australia	7	1.3	2.7

Source: WTO, World Trade Review, 2019

Table 2. Asian Imports of Clothing Grow Faster than Rest of World, 2018

2) McKinsey, A global view of how consumer behavior is changing amid Covid-19, 2020.

The COVID-19 pandemic will severely impact growth across all regions.

(real GDP, annual percent change)	PROJECTIONS		
	2019	2020	2021
World Output	2.9	-3.0	5.8
Advanced Economies	1.7	-6.1	4.5
United States	2.3	-5.9	4.7
Euro Area	1.2	-7.5	4.7
Germany	0.6	-7.0	5.2
France	1.3	-7.2	4.5
Italy	0.3	-9.1	4.8
Spain	2.0	-8.0	4.3
Japan	0.7	-5.2	3.0
United Kingdom	1.4	-6.5	4.0
Canada	1.6	-6.2	4.2
Other Advanced Economies	1.7	-4.6	4.5
Emerging Markets and Developing Economies	3.7	-1.0	6.6
Emerging and Developing Asia	5.5	1.0	8.5
China	6.1	1.2	9.2
India	4.2	1.9	7.4
ASEAN-5	4.8	-0.6	7.8
Emerging and Developing Europe	2.1	-5.2	4.2
Russia	1.3	-5.5	3.5
Latin America and the Caribbean	0.1	-5.2	3.4
Brazil	1.1	-5.3	2.9
Mexico	-0.1	-6.6	3.0
Middle East and Central Asia	1.2	-2.8	4.0
Saudi Arabia	0.3	-2.3	2.9
Sub-Saharan Africa	3.1	-1.6	4.1
Nigeria	2.2	-3.4	2.4
South Africa	0.2	-5.8	4.0
Low-Income Developing Countries	5.1	0.4	5.6

Source: IMF, World Economic Outlook, April 2020

Note: For India, data and forecasts are presented on a fiscal year basis, with FY2020/2021 starting in April 2020. India's growth is 0.5 percent in 2020 based on the calendar year.

Table 3. IMF Projections for Economic Growth

Recovery Scenarios for the Cotton Sector That Look Beyond the Immediate

Economic recovery and within this, recovery for the cotton sector, can occur once the public health crisis has been brought under control through eradication of disease threat, most likely through population wide vaccination. A timeline for vaccine development, testing and deployment to population level are likely to be lengthy with estimates from 12 to 18 months in a best-case scenario. Widespread vaccination and ongoing monitoring would need to be maintained successfully for the world to return to a pre-COVID-19 normal. Even in this scenario, the economic environment could likely be one in which trade tensions move toward to protectionism that dominated the pre-COVID-19 trade landscape in which cotton mill-use growth

had already been muted due to slowing economic growth. However, even prior to disease eradication or population vaccination, government responses can help in the interim to enable a safe increase of business activity as countries emerge from lockdown. In this 'new normal' with safety ensured by proper local and national government responses and policies, businesses could safely reopen, and economic activity could begin to increase with appropriate precautions being taken to provide for health and wellbeing. As temporary unemployment levels begin to decrease and societies begin to find an equilibrium of operating in safe conditions, consumer confidence will increase and an uptake in apparel sales could be envisioned.

In a 'new normal', where the proper safeguards for human safety and well-being are ensured through appropriate government responses, a moderate recovery could be envisioned where consumer demand for apparel goods begins to pick up. The timeline for a moderate recovery would be dependent upon government responses that permit the reopening of business activity while ensuring that the pandemic does not spread without the need for the most stringent level of containment measures. This would provide for 1) a decrease in unemployment and 2) easing of uncertainty as more normal patterns of business and social activity are able to resume. With decreasing levels of uncertainty that have arisen from the pandemic, consumer confidence could return within a few months with a gradual increase of retail activity. With increases in demand, retailers would begin to increase the pace of orders from manufacturers. In this scenario, cotton mill-use could see little or no contraction in 2021. Business activity would be lower and GDP growth would be within the IMF's projections.

However, as China has emerged from lockdown and is able to continue economic expansion, incomes in China would increase and could provide an uptake in consumer demand for apparel. A shorter or more moderate recovery could also allow an uptake in manufacturing activities in the developing countries of Southeast Asia where the small to medium sized enterprises that make up the spinning industry in this region to continue to operate.

A moderate recovery would impact

- **cotton mill-use** less severely as apparel demand could increase as business activity and employment increase even moderately as consumers, particularly those in Asia, resume clothing purchases. Little or no contraction in cotton-mill use could be expected for the 20/21 season if consumers in emerging economies are confident in their economic prospects.

- **prices** that are already under pressure are likely to remain low even at zero growth consumption as stock levels are at record level highs.
- **production** less severely as planting decisions for the forward season have been mostly made for the Northern hemisphere growers accounting for 80% of global production.
- **trade** less severely as supply chains that have shifted in the wake of the US-China trade dispute appear to be in place and able to supply cotton to needed markets.
- **manufacturing** less severely as the much of textile and apparel manufacturing in Southeast Asia has been undertaken by small and medium sized enterprises. While many brands have retained orders, others have been cancelled putting in jeopardy a spinning industry with little cash reserve to weather a long crisis. If orders even at slower pace can be resumed, these SME's may be able to survive.
- **production** severely as planting decisions for the 21/22 season would be impacted by the prices already under pressure. Farmers would see little financial incentive and the likelihood of food crisis would put greater value on food crops particularly for smallholder farmers in West Africa and India.
- **trade** severely as trade follows both GDP and consumption growth.
- **manufacturing** severely as many small and medium sized enterprises in Southeast Asia would likely be unable to survive with reduced orders from brands and retailers.

A slower recovery could be envisioned where either stringent containment measures remain in place and government policies including those for public health systems, small business and unemployment remain weak or ineffective. Similarly, a prolonged recovery would be envisioned if containment measures are eased without appropriate provisions for human safety and well-being leading to a resurgence of disease spread. Either of these events would lead to a slower recovery, although a failure of government response and policy would likely also increase uncertainty, further prolonging economic recovery. A slow recovery extending beyond 12 to 18 months with little action to promote consumer demand would lead to a more severe contraction in cotton mill-use in 2021. With the 20/21 production estimated at 25.1 million tonnes, an additional slowdown would increase pressure on ending stocks which in turn increase downward pressure on prices. In a prolonged crisis, food security would become an important issue and smallholder farms in developing economies would likely switch to food crops.

A slow and prolonged recovery would impact

- **cotton mill-use** severely if businesses and stores remain closed, and temporary unemployment becomes more permanent, income levels will drop, and uncertainty of prospects will increase. Consumer demand for apparel and textiles being income elastic will decrease and mill-use which is currently near a 10-year low would decrease further.
- **prices** that are already low in real terms would have little upward movement without consumer demand for apparel. Prices which have had less volatility in recent years and have responded to market fundamentals would likely see greater price volatility a possible food security issues and economic uncertainty.

The type of recovery in the cotton market will largely depend on the response of government in the form of transparent and effective policies to support agriculture, industry and consumers. While tremendous uncertainty remains, through appropriate policies, countries will recover at differing speeds. Countries need to provide transparent policies and data and work cooperatively within the international system. Cooperative international responses may also help to mitigate the trade and geopolitical tensions pre-COVID-19 that had provided and already uncertain environment of slowing growth, slowing demand and move away from globalisation. China's role in the global cotton market is pivotal and likely to remain so as the global leader for imports and mill-use as well as for the reserves quantities the country maintains.

Government interventions for recovery and reinvestment due to the pandemic are needed as well as eventual trade resolutions for a broader economic recovery, including the cotton market. During this unprecedented global pandemic which emerged as global economic growth had already begun to slow, the uncertainty in markets has increased as countries struggle to manage the spread of Covid-19. Containment measures, unprecedented shifts in the labour market and growing unemployment have led to sharp decreases in textiles and apparel sales as consumer demand has dropped. The current economic environment is an atypical slowdown from a typical recession as the containment measures for COVID-19 have closed business activity in a way not experienced in the modern era. A recession is defined as two consecutive quarters of negative economic growth and typically declared in retrospect. However, this recession is unlike others in some respects as it has been induced by a public health crisis rather than an event in the financial market. A depression is a long recession where unemployment reaches and remains at high level typically around 25-33%. The Great Depression was marked by a decade of high unemployment that had also been induced by ineffective economic policies. Additional analysis on the policy responses by countries will be key to understanding economic recovery and the speed of recovery for the sector.