HUMAN RIGHTS ISSUES COULD STILL IMPACT TRADE AGREEMENT

CREDIT ISSUES A MAJOR CONCERN AS CHINESE CAPITAL WINTER ARRIVES

BRAZIL HOUSEHOLD CONSUMPTION GROWS AGAIN

US COTTON MOVEMENT CONTINUES AS ICE RALLIES

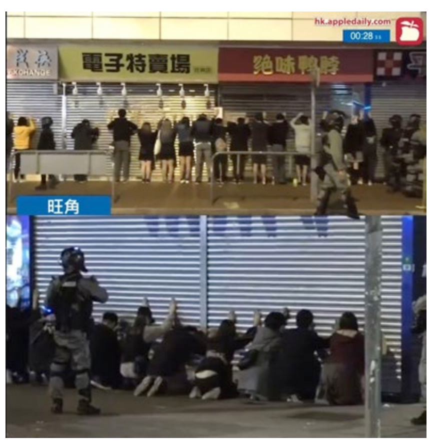
JERNIGAN GLOBAL
KNOWLEDGE IS THE NEW CAPITAL

CHINA & US APPEAR HEADED TOWARD SIGNING OF TRADE AGREEMENT; HUMAN RIGHTS ABUSES IN HONG KONG & XINJIANG IGNORED

China-backed, black clad thugs in Hong Kong mall attack citizens, Dec 26, 2019

Hong Kong police dressed for war attack shoppers in shopping mall Dec 25.2019

Global headlines were dominated on Christmas Day and Boxing Day by the China-trained and -based Hong Kong police thugs attacking unarmed citizens at Christmas church services, shopping malls, and on the street. Commentary from around the world suggested the behavior of the Hong Kong police had never been seen before by a modern police force. Videos and photos left little to the imagination as the abuses were captured for the entire world to see. Hundreds have been arrested and appear to be disappearing, with rumors that



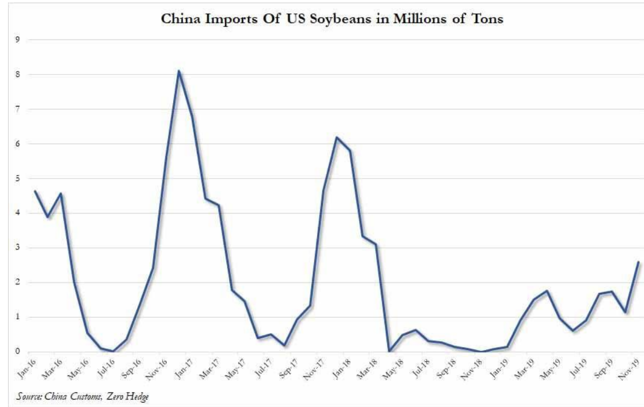
Hong Kong police attack citizens on street, Christmas Eve, 2019

the prisoners have been taken to the mainland to special camps. The US has been quiet, which is shocking given the passage of the Hong Kong Human Rights Act that is used to punish officials involved in abusing Hong Kong citizens and to monitor violations of the Hand Over agreement. Clearly both have happened. The concentration camps in Xinjiang have also not drawn much reaction from the US. Global headlines were a bit different as All Blacks rugby superstar Sonny Bill Williams called out China for the Xinjiang camps. The notes for help found in UK Christmas cards that were made in China continued to be in the headlines, drawing attention to the treatment of Chinese prisoners. UK support for Hong Kong generally remains lacking.

One reason is the Christmas holiday, due to the US Senate and House both being in recess. Comments have come from individual Senators but little from the administration. Instead, positive comments have been noted from the administration regarding a signing of the Phase I trade agreement. For the moment, human rights appeared to have given way to the effort to reach the signing ceremony for the agreement. A rare bipartisan effort is underway to produce veto-proof legislation to punish China for its Human Rights abuses, and to force President Trump to act. At the forefront is the Uyghur Human Rights Policy Act that has passed both houses but has not yet reached the President's desk. So far, President Trump has stopped short of a call for sanctions on the Chinese officials responsible for the camps for fear of impacting the trade deal. The Uyghur Act will force the President to act. Additional pressure occurred last week from videos on social media of Han Chinese forcing Uyghur Women into relations.

On the Chinese side, a host of lifting of tariffs has been announced ahead of the signing. The press interpreted November soybean imports from the US of 2.6 MMT as a positive sign for the agreement, while imports from Brazil reached 3.9 MMT. Cotton remained in the background, with weekly export sales negative as China canceled 15,000 bales. Overall, weak domestic cotton demand in China remained a problem, with international prices at a slight premium to local values. China clearly appears to be expecting a trade agreement with the US to provide an economic boost. On Friday, the *South China Morning Post* carried headlines that it could help China reach 6% growth in 2020. Such growth seems far away given the forecast that the economy is expected to grow only 1%-2% or less. One estimate released last week indicated that 25% of all Chinese apartments are empty, and building is still underway as the birthrate falls.

Expectations remain that cotton has received an allocation in the agreement, but the exact total is anticipated to vary with the level of overall demand for other commodities. One point raised is that, due to seasonal changes in demand, actual Chinese purchases of the individual commodities will not become clear until at least the second half of 2020. This means that if cotton demand internally remains soft no purchases may occur for some time. The US is expected to attempt to be tough on enforcement on many parts of the agreement. However, the commodity purchases will have to have flexibility. In other words, if total aggregate of agriculture purchases is progressing, no action will occur. For example, if they include no cotton but the total is meeting the targets, then no violation has occurred. At the end of the day, demand remains a driver.



China persecution of Christians, 2019

Some feel that, given the past experiences with the Reserve holding large volumes of cotton, and the losses and corruption, they may be reluctant to use it for large purchases. During the 2011-2013 purchase scheme, it is believed that 5-10% of all cotton purchased was lost or unaccounted for when audited five years later. Also, it is expected that new reforms on large, state-owned companies will be announced shortly to assist in making them competitive with international companies. The cotton Reserve was absorbed by the grain reserves company SINOGRAIN earlier. Since then, it appears they have a reduced role. It's unclear if the giant inefficiencies of the grain reserve system will be reformed. There are thoughts that large amounts of the grain inventories are unsuitable for human consumption. It remains to be seen how the cotton Reserve will be used to meet obligations under the agreement.

Boycott Xinjiang cotton effort

Chinese prison labor forced to sew clothes

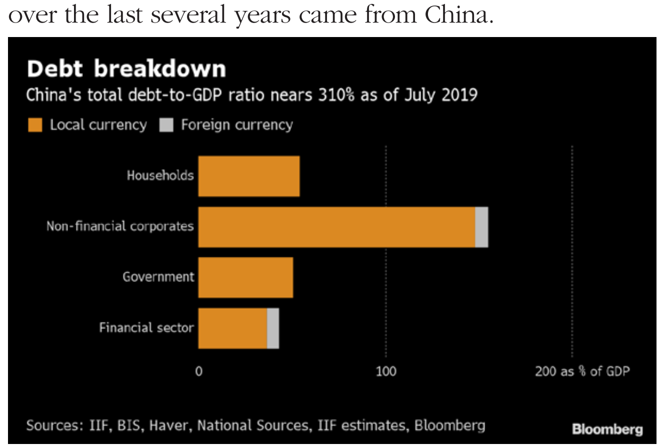
The Chinese debt crisis is expanding, which is impacting Chinese commodity trading and the textile and apparel industry. Shandong Ruyi's 345 million of USD bonds due December 19th traded down to 47 cents before reaching maturity. It was reported the payment was made to HSBC despite the expectations of a default. Many major bondholders liquidated their bonds ahead of maturity for fear of nonpayment. Other bonds come due in 2020, 2021, and 2022, and many of these are trading at deep discounts. Meanwhile, around the world, the company's issues are causing problems for its subsidiaries, halting expansion of its planned projects in the Belt and Road locations. Questions are being raised on how Shandong Ruyi was able to arrange the purchase of Lycra in the US, and who provided the credit. It is rumored the seller provided a note of 500 million USD. Plans to take Lycra public in China have stalled. Shandong Ruyi issues are at the forefront because of their size. However, Shandong is at the epicenter of the default crisis.

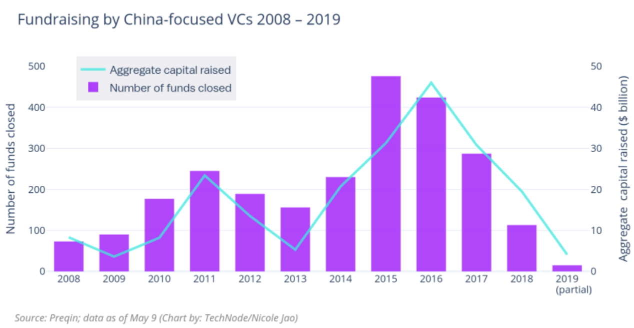
100 cents or its equivalent is the same in Beijing or New York, and at some point it all has to balance. Prior to the arrival of Xi Jinping and his resurrection of the failed policies of Mao, the world had come to admire the Chinese version of capitalism with Chinese characteristics. When Deng opened China, the CCP was focused on maintaining power, not on its own genius at running the economy or companies. The result was a wild west that gave us the China 'Price.' This combination of government planning, subsidies, and shear raw capitalism gave birth to modern China and transferred the entire manufacturing base of the US, much of Europe, and others to China with barely any resistance. Deng's advice to not cause ripples served the country well. They developed a National Development and Reform Commission that sought advice and council, floated ideas, judged market reaction, and then decided. As someone who was heavily involved in the country and the NDRC, there

was little hint of anything related to communism, and there was no attempt to interfere with private companies. The result was impressive growth, which all ended with the arrival of Xi Jinping. Centuries of collective wisdom and seeking the council of the wisest minds in the world ended, with many men and women who had served the country being arrested while free thought ended. The arrival of Xi Jinping thought is centered on the genius of Xi Jinping and the Communist Party. Neither can do any wrong and are to be worshipped. Each company has now become a vessel of the party, and free thought is history.

The roots for the birth of Xi Jinping thought were born in China's success in avoiding the worst of the global recession of 2008/2009. This led to open discussion that the Chinese model was superior to the West, and no additional reform was needed, which began the idea that the party was a genius. Those visiting Beijing shortly after Xi Jinping rose to power quickly realized that a different China was emerging. Local governments have stopped reforming, making the party the center of all, and focusing on trying to please Beijing. Gone is any attempt to manage the books. Local governments have set up massive state-owned companies that have inflated real estate, hired people, increased corruption, made party officials rich, and provided the provincial officials with the needed economic targets. The lack of oversight and any input from the citizens has allowed massive debts to accumulate. After all, in China, the issuance of local bonds is easy, and in reality no one ever really checks the credit worthiness or the total liabilities of the issuer. The result is a credit binge like the world has never seen. Again, under Xi Jinping, the CCP propagated the myth it was infallible, that China's rise could not be stopped, and that it had unlimited funds to spend. This attitude was clear for the world to see in 2017/2018, before someone in Beijing began to stop the madness. The Belt and Road was launched in this era. The state-owned companies bought the concept full bore and soon went on a global buying spree. Remember, Shandong Ruyi purchased brand after brand, signed grand MOU to build record plants, and actually made the proclamation that if you had a company to sell please call them. At the time, we all ask where the money was coming from. After all, it overpaid for each purchase, and no one seemed to care. Now we know there was little cash, and it was debt provided by either domestic Chinese credit markets or international markets with the assistance of banks that failed to do the due diligence. It seemed these groups also believed the CCP was golden and that China's rise would go on forever, and that this time it was different.

Shandong province now finds itself at the epicenter of the start of the day of reckoning. As the birthplace of Confucius, Shandong is a province rich in history. For cotton, it was once the largest cotton growing area in China before Xinjiang production expanded. It was also the birthplace of the modern Chinese textile industry, and many of China's largest groups have roots in the province. The official GDP of the province was 1.13 trillion USD, or about one fifth of Japan. The province has emerged as an industrial powerhouse. It also has always been a bit of Wild West as the great opening started, as state-owned companies merged and became powerhouses, with many going private. It always seemed unclear how the privatization worked, and certain old state company employees became some of the richest men in China. It also was at the forefront of the development of a new set of economics, with books being adjusted and practices changed to please the latest edict issued to the banks by Beijing. One practice that emerged was the issuance of Cross Company Guarantees in which companies would pledge to meet the debt of other companies, and in return they received the same. This pleased the banks and stimulated more credit to flow. No real attempt was ever made to limit or manage risk. After all, the party, which had invaded the Central Bank, all policy, and China had a Supreme Ruler for life that ended centuries of group leadership. It was all about getting rich, and there were no boundaries. One estimate is that 45% of all global debt over the last several years came from China.





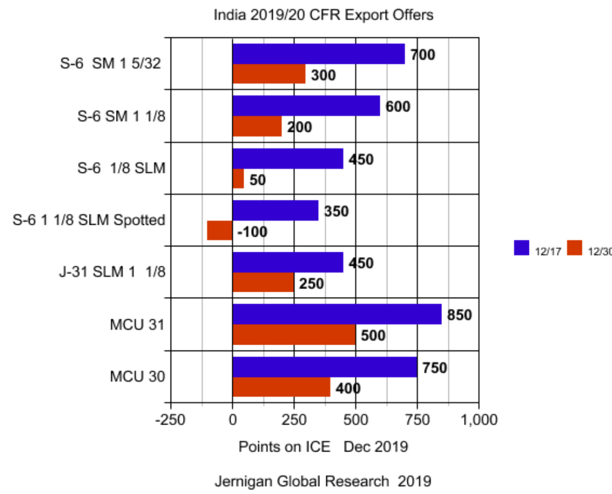
China's capital winter has arrived

For our commodity trading friends, remember how speculative fever used to move the Chinese markets as they were developing. In most markets, the exchanges have developed techniques that have made the lead month in volume the 5-6 months out contract instead of the nearby as in the US. The reason is to manage the speculative element, with the margin starting to increase several months out, and accelerating as the month becomes a spot month. The credit bubble and the issuance of local government and corporate bonds have followed that pattern, and now the reckoning is here. It is ironic that MSCI Global Index has expanded its inclusion of Chinese companies in 2019, and Bloomberg is pushing these Chinese bonds to global investors. This, of course, increases the contagion risk.

Chinese companies are reported to be entering a "Capital Winter," with private funding drying up. Despite the track record and trade war, Chinese companies raised 3.4 billion USD on the New York exchanges in 2019. Only 13 of the 58 Chinese companies that have gone public in the US over the last two years are trading above their IPO prices according to CNBC. The acceleration of defaults in China is raising fears. The former chairman of Henafeng Bank, which had to be rescued, was sentenced to death for corruption. It appears the shortage of US Dollars is for real and has spread to the Belt and Road projects. In Kenya, China has abruptly withheld 4.9 billion USD needed to finish the Mombasa-to-Nairobi railway. Instead of reaching Nairobi, the line stops 75 miles west in the middle of nowhere. In Zimbabwe, where China has lost over 10 billion, it abruptly withheld the funds to complete a solar project. As discussed earlier, at some point every country has a limit, and China appears to have surpassed theirs. This issue is very important to the Chinese textile and apparel industry and Chinese cotton consumption. We fear the credit and capital issues will be at the forefront in 2020, even as the trade agreement takes the headlines.

INDIAN STYLES COMPETITIVE AS ICE FUTURES RALLY

The rally in ICE futures over the holiday period has again made Indian cotton the cheapest in the world. Shankar-6 1 5/32 is now offered at 300 points on March for prompt shipment. This is an 800-point discount to a Brazilian 1 5l32 or US E/MOT style. At such discounts the Indian offers are attracting attention in Vietnam, Indonesia, Bangladesh, and other markets. MCU 30 mm lots are offered at a 100-point premium to the Shankar-6 styles. It remains to be seen if economics will overrule politicians in Pakistan at such discounts. Export demand for US styles has slowed as ICE has rallied. The CCI increased purchases, but still Indian prices have not followed ICE higher. New crop arrivals reached 844,230 bales through December 20th for the month. Lower quality export offers have also been noted.



BRAZIL HOUSEHOLD CONSUMPTION IMPROVES AS CONFIDENCE IS RESTORED UNDER BOLSONARO

Brazil economic growth returns

Brazil is building again

Brazil appears to again be on the path to economic growth under the leadership of the country's first honest, uncorrupt president in years. Confidence is being restored, Sao Paulo real estate is hot, household consumption is improving, and crime is dropping. The agribusiness sector is booming, and infrastructure improvements are being noted. Construction cranes dominate the skyline in Sao Paulo, and with it are new jobs. This time the construction is not linked to corrupt government projects with payoffs to the Workers Party. Instead it is the private sector building apartments for the people. There is no inflation, domestic interest rates are down to 4-5% and October retail sales rose 4.2%. The Bolsonaro administration brought the pensions under control and has curtailed government spending.

The economy is also benefiting from the lack of the corruption that took a major toll on the economy. The massive Car Wash scheme created a corrupt upper class of rich. That wealth is returning to the economy. It is hard for those outside Brazil to fully understand the scale of corruption that took place under Lula, which impacted both the federal and state economy. For example, in Cuiaba, the capital of the booming Mato Grosso state, the electrical tram started before the World Cup was left only about a third finished, blocking an important highway lane, as corrupt officials stole the balance of funds. Just think about the efficiencies to the local economy if the project had been finished. In the countryside, bridges are missing from rural roads after local corrupt officials stole the funds. The Cuiaba

Airport air conditioning system is subpar, despite the funds that were stolen. It went on and on until it was curtailed by the Car Wash clean up and now the Bolsonaro presidency.

The question is whether the government is willing to exert the political capital to restore the industrial sector, including the textile and apparel industry. This will be a challenge given the vested interest, and the various taxes and regulations that burden the industry. Today, imports are a major problem. January-November textile and apparel imports have reached 5.029 billion USD, which is down 4.34% for the year, but the volume of imports is up 1.42% as exporters cut prices. China is the top supplier, with imports reaching 2.74 billion USD. The volume imported from China is up 13% year on year. The industry has such potential but needs a revolution to clean up and modernize the sector. As the economy improves, it remains to be seen if the domestic industry can retake any of the market left to imports. Apparel products in Brazil cost substantially more than in the USA due to taxes, transportation costs, and regulation.

Brazil's ESALQ cotton index has failed to follow the ICE futures higher, as the market fears that Brazilian cotton will lose market share in China after the trade agreement. The ESALQ Index of a 41-4-35 landed Sao Paulo on December 17th was 66.01, and on December 26th was 66.18 US cents a lb. The Real ended the week near 4.05 per USD, and Brazil ETFs traded at record highs.

ICE FUTURES MOVE HIGHER WITH TRADE SELLING INCREASING

ICE futures breached the 70-cents barrier in the May and forward contracts, with the March contract stalling amid active US grower selling. The buying pushing ICE higher has come largely from the speculative sector, which was triggered first by the trade headlines and then by the technical indicators. Missing from the rally has been heavy demand. The basis is turning weaker as the rally expands. In the US, the FOB basis outside Texas is weaker. In Brazil, the ESALQ Index of local prices is not following the ICE gains. The average Indian CFR basis has weakened almost point for point with any ICE gains. This has occurred because the rally is based on expectations that the Chinese/US trade agreement will contain an allocation for cotton, and that at least a billion USD or more of export shipments to China will occur. The rally is easy to understand from a psychological standpoint and from a technical standpoint. The trouble from a fundamental point of view, however, is how will the agreement impact world trade? With no agreement, Chinese import estimates are too high, and with the agreement import estimates may be met with Reserve purchases. The problem is the lack of major impact on total world demand. If the agreement holds and China complies, then maybe order books will at least expand, restoring some confidence and thus increase import demand. This could happen, and if it does the impact on world trade will be larger. But the human rights obstacles appear very sizeable.

The Trump administration appears less driven by human rights, but the Senate will apply pressure in January that will force action by the administration. Major Republican Senators are pushing for action on Xinjiang and protection of Hong Kong, as well as for greater US support for Taiwan. Its election season, and these Senators' support is needed. These actions will impact confidence and demand. Some hope was reached recently by the extension of the trade deal influence to the North Korea situation. Actions suggest China is controlling the North Korean actions and are seeking to maintain the calm. However, that same calm has not been reached regarding Hong Kong, where the thug police are showing no restraint.

We believed the rally in ICE could extend to the 70-72.50 level in March, and this remains possible, but US grower movement has been heavy daily, which has slowed the advance. The weaker basis levels for other growths illustrate that demand has not yet followed. US cotton is also no longer the cheapest in the world. 2019 is ending, and a new year and century will begin. The positive for cotton is that many believe we have just experienced the peak in fossil fuel demand, which could include man-made fibers. The negative is China and the time it takes to move supply chains. China's role as the center of the global cotton market is ending, and its future role will be determined by its politics, which have tainted its supply chain by the attempt to exterminate the Uyghur population, persecute its Christian population, and use forced labor in export products. Xinjiang modernization, an engineering marvel, has been marred by the concentration camps and use of prison labor. Brands and retailers simply cannot afford the liabilities of a Chinese supply chain for export markets. This will not change with the trade agreement. Unfortunately for China, the concern regarding its policy in Xinjiang was never recognized prior to the start of the trade war. Again, the behavior in Xinjiang against Christians, and its bullying around the world, along with the earlier view of its infallibility, is drawing attention. If the current CCP does indeed comply with the agreement, it would suggest recognition of the external problems that have developed, and maybe a lull in the battles. We hope this is the case, but we have no faith it is.

Happy New Year to all. We hope 2020 brings peace to Hong Kong, a respect for Human rights, an end of the concentrations camps in Xinjiang, an end to the persecution of Christians in China, and greater market share and expanded global demand for cotton.

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