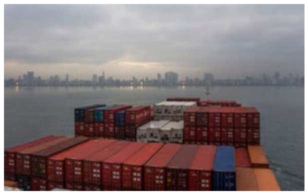
CHINA CORONAVIRUS A MAJOR THREAT TO CHINESE ECONOMY



BRAZIL 2020 CROP OFFERS TURN AGGRESSIVE

AUSTRALIAN RAINS CONTINUE

ICE FUTURES SHOW SIGNS OF A TOP

JERNIGAN GLOBAL

KNOWLEDGE IS THE NEW CAPITAL

BANGLADESH RISKS ITS FUTURE WITH AN INCREASED FOCUS ON MAN-MADE FIBER

The strong growth in the Bangladesh apparel industry has stalled over the past year, which has many seeking a new direction. We were shocked by a press article promoted by the *Sourcing Journal* that promoted the idea that the industry should turn to increased investments in man-made fiber supply chains. It's been our belief that a lack of investment in quality and a government that has failed to put strong customs control in place lies at the root of many of the problems the sector has experienced. For years, strong investment in fully integrated operations allowed for a crucial alternative in sourcing to develop. Cheap illegal imports of Chinese yarn and fabric have undermined confidence in investment. Illegal imports have become a significant problem for Bangladesh as they have moved more into the China orbit with its involvement in Belt and Road. The illegal imports do not pay the import duties that have damaged local spinners. In

addition, after the trade war between the US and China expanded, Chinese exporters cut prices and began to offer yarn and fabric at prices far undercutting the local spinners. It has been discovered that the Chinese government is providing incentives for the export of Chinese fabric, according to some exporters. The Bangladesh government established import taxes of 32.4% on man-made fiber, 38.4% on yarn, and 91.37% on fabric. However, corruption and weak enforcement have allowed the taxes to be avoided.

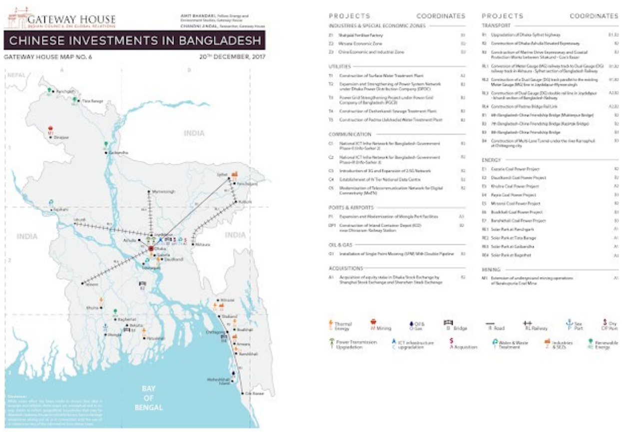
The increased Chinese influence is the result of the US failing to grant GSP duty free access for textile and apparel imports due to concerns over the on-going labor conditions and treatment of workers. The Bangladesh government has failed to clear US hurdles, and the US has failed to show any innovation in the situation or to offer new assistance. The failure of duty free entry being granted by the US also reflects a failure of US cotton export policy. No new strategies were proposed to provide a link to US cotton purchases and access as suggested by the Bangladesh delegations. Several Bangladesh companies even proposed bold investments in the US textile sector, which was ignored. Thus, the movement toward greater collaboration with China is understood, even though it is damaging to the textile sector, as increased Chinese fabric flow into the country occurred.

There is evidence that cotton has lost market share in Bangladesh during the past year due to the decline in polyester staple prices and the inflow of cheap, Chinese man-made fiber yarn and fabric. Bangladeshi spinners have traditionally depended heavily on Central Asian and Indian cotton. The flow of Central Asian cotton has been drying up as the region switched to a consumer of its production instead of an exporter. Indian cotton was at extreme premiums for much of 2019, which forced spinners to seek alternatives. Polyester was the cheapest alternative. The fact that polyester is at a record discount to cotton has made it attractive as spinners and the entire chain battle the lower-end business its exporters have traditionally battled for. The denim sector has made strides and had successes, but denim demand has not been as strong as many expected.

Bangladesh has over 13 million spindles (including more than 230,000 open end rotors), a large fabric sector with over 800 weaving mills, large dyeing and finishing sector, a vibrant denim, and a home textile sector. The man-made fiber industry is small, consuming approximately 100,000 tons of polyester fiber annually, and includes a small Viscose fiber sector. Some expansion has occurred, including the setup of a plant to produce polyester yarn from recycled plastic bottles.

The cotton-spinning sector is on the defensive and is operating at nearly 60% of capacity and will consume only 7.0-7.5 million bales unless conditions improve. Bangladesh has the capacity to consume 11.5-12.0 million bales.

China foreign direct investment in Bangladesh



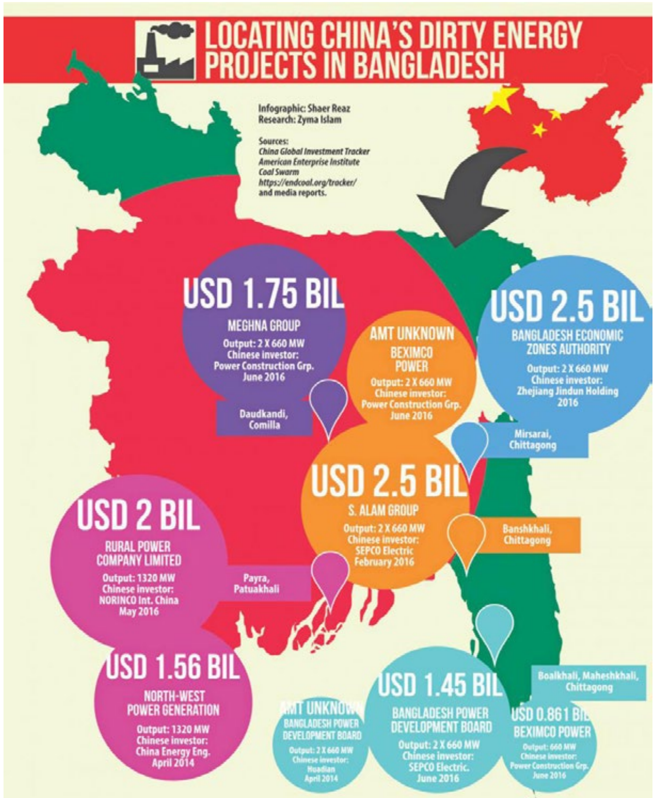
Chinese investment in Bangladesh

The cut and sew industry has enjoyed robust growth until the past 12 months, with a few operations closing as the undercutting of prices by Chinese exporters turned margins negative. In the past fiscal year Bangladesh exported 34.13 billion USD of apparel. A *Bloomberg* analysis of China's export performance in 2019 showed that shipments to the US market fell sharply, but Chinese exporters then attempted to increase shipments to all other markets to offset this loss. This strategy included cutting prices and utilizing government subsidies, which hurt Bangladesh's exporters in the non-US markets. Europe accounts for 50% of all exports, while the US has accounted for about 20% of the market.

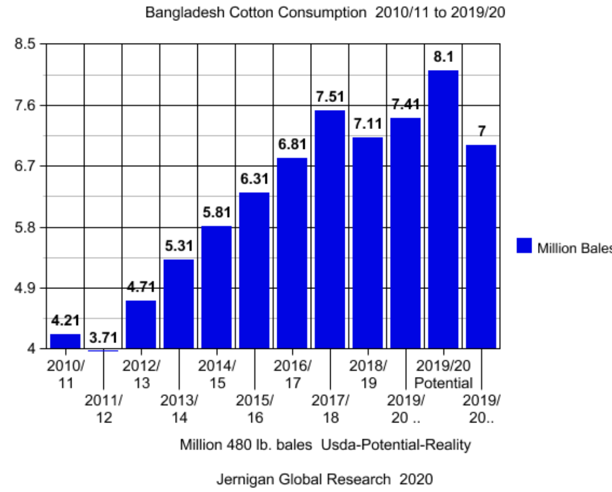
Bangladesh has several strategic advantages over many of its competitors. These center on cotton and natural fibers, not man-made fiber apparel. China currently dominates the world's man-made fiber market, which is due to continued expansion of petrochemical plants. New capacity came online in 2019, despite the oversupply in the market and the lack of profitability. Massive additional new plants will come online after the Chinese New Year that will further add to the glut in supply. This supply will keep the price of polyester fiber and all man-made products depressed and below the cost of production. Outside of China, the shale oil boom in the US has triggered massive raw material production of MEG from natural gas, which is further undercutting man-made fiber prices. Due to this increase in production, any Bangladesh producer of polyester will be at a major disadvantage and soon driven out of business.

This massive supply chain for man-made fiber provides China's textile sector with cheap raw material that flows into fabric. Chinese exporters dominate the man-made fiber market globally, which translates into almost crushing domination by Chinese exporters in all man-made fiber apparel products. China has a 36.53% market share in the US of all man-made fiber apparel imports. Vietnam, Jordan, Cambodia, and Sri Lanka apparel sectors are controlled by Chinese fabric, as are others. When these are totaled, Chinese man-made fiber apparel ends up with a 63.4% market share. The Bangladesh textile sector cannot compete against the Chinese man-made fiber industry, which continues to enjoy record investment from state-owned groups in the petrochemical sector. If Bangladesh attempts to compete, it will become just another Cambodia, which is close to being a Chinese colony without a single spinner or any real textile infrastructure. Basically, its industry is simply cheap labor.

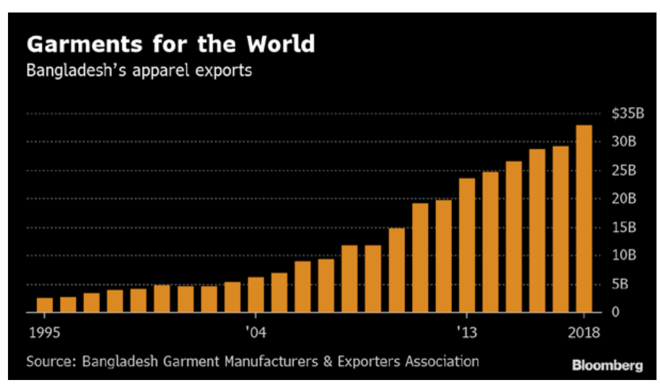
The future for Bangladesh lies in cotton and natural fibers. Since 2018, there has been a serious effort by brands and retailers to move sourcing of textiles and apparel out of China. That has not been possible in many products, because there were no alternatives. The brands and retailers have been looking for complete supply chain alternatives. Vietnam has a robust industry but still has only a small fabric sector, leaving the apparel industry to rely on Chinese fabric. Bangladesh, India, and Pakistan offer brands and retailers the ability to have a complete supply chain from fiber to finished goods. All three markets have holes in the supply chain but, for the most part, have the start of a complete chain. Bangladesh is very advanced and needs to focus on making their cotton textile supply chain stronger and providing the ability to move into more advanced high quality fabrics. It needs additional training in the more advanced apparel.



Chinese investment in power plants



Bangladesh has suffered from the creed of the supply chain, where attempts are always made to achieve the cheapest price. China's cost without subsidy are rising. Bangladesh will have to reinforce the rule of law first in allowing better labor working conditions and punishing violations. It also must allow higher labor rates and seek approval from major importing countries for assistance on market access when conditions are met. The rule of law must be strengthened and custom and border regulation enforced, which will mean taking a tough stance against Chinese and other violators. The country has great potential as an alternative complete supply chain for cotton products. Once this is achieved, growth will be rapid, given the lead time for others. Bangladesh's extensive cotton textile supply chain gives it a significant advantage over many other competitors, because most alternatives have not made the investment in fabric and finishing that Bangladesh has.



CHINA'S CORONAVIRUS OUTBREAK SPARKS FEARS OF ECONOMIC IMPACT

Wuhan Wild Animal Market

Fears are rapidly growing that Chinese officials and their institutions have failed to report the early spread of the Coronavirus from Wuhan. It has now surfaced that a Wuhan Level 4 biolab may be at the root of the virus. The number of people impacted is spreading rapidly, and the US CDC announced Tuesday the first case in the US. By Saturday, it had been reported around the world. The fear regarding the outbreak of the unknown virus is that it could exceed SARS, or even Ebola, and that China's poor healthcare system and lack of transparency has allowed it to spread very rapidly before being widely known. The virus has been traced to a wet market in Wuhan where wild animals are held in small cages along with dogs, snakes, bats, rats and cats for purchase and slaughter. Videos of the market soon went viral, showing the inhumane condition of the animals sold for food, which ranged from dogs, porcupines, wild cats, rats, fox, hedge hogs, exotic seafood, crocodiles, wolf puppies, snakes, and the extreme, which included the banned cat that caused SARS. Even koalas were offered for sale for food. Can anyone explain how a live Koala first got out of Australia and then to Wuhan? Animals that were never meant to be eaten have been raised in the wild and entered the food chain in very unsanitary conditions. The virus is now spreading from animal to human and from human to human. Social media posts showed that hospital staffs were not testing family members of affected people, and that the wet market continues to operate, as many across China did until just a few days ago. This breakout follows the destruction of the world largest pork herd by the swine flu virus that continues today. Fortunately, this virus seems incapable of spreading to humans.

China's food supply chain has always been suspect, but it is now becoming quite dangerous. Over the years it has been hit with scandal after scandal. Many attempts have been made to address the concerns, but the problem of many Chinese eating unusual wild animals, rats, bats, cats, badgers and foxes, often undercooked, continues to carry serious risk. Exotic animals are smuggled and sold for food, and there exists no real control over the flow of these animals. It is somewhat surprising that while billions are being spent on the surveillance of its citizens, this same technology is not being used to clean up the food supply chain. China claims to be the second largest economy in the world as it has some of the most modern infrastructure in the world, yet its food chain still has much of the risk of a Third World country. African Ebola, which came from humans eating monkeys, is one of the deadliest diseases in the world. The deadly SARS epidemic came from Chinese eating the wild civet cat. Now the new virus is spreading again, coming from China and an exotic wild animal entering the food chain.

The technological advance of China allows such a disease that would normally be isolated to spread globally, which was illustrated by the first case already in the US. China has failed to manage the outbreak. Again, it has the most advance surveillance system in the world for monitoring its citizens, but it cannot be used for disease control. Instead, control of the press continues, with the fear that the outbreak is much larger than reported, which we are sure it is. A group of Hong Kong journalists that traveled to Wuhan was forced to delete their stories. Even stories in the Hong Kong press have been censured. By mid-week, the fear of the economic damage of the new virus had already taken millions of USD off the market cap of global equity indexes. The Coronavirus fears caused sharp losses in travel stocks and triggered health alerts around the world. By January 22nd, 17 people had died that we actually know of, and 540 cases were reported, putting Wuhan, a city of 11 million people, in panic. The government on Wednesday halted all travel to Wuhan, and people are banned from traveling with the city under quarantine. The World Bank estimates that the 2003 Chinese SARS outbreak cost the global economy an estimated 54 billion USD. This now has the world's attention as China's 1.4 billion population travels for the New Year holiday, opening the possibility for the disease to spread like wildfire. This is a rational fear. What is the virus were to mutate to a more viral strain?

Despite the quarantine of a city with more than 11 million people, the *People's Daily* Thursday edition did not carry the story on the front page. The real concern was the fact that Chinese officials have been covering up the outbreak since it first occurred. Conservatively, this outbreak could be 10 times larger than the SARS epidemic. We have passed through the 'golden period' for prevention and control. Never has a city the size of Wuhan ever been quarantined. Wuhan is five times larger than London, twice the size of Shanghai, and eight times larger than Hong Kong. It is also a transport hub with high-speed trains and airlines. On Thursday, the government expanded the quarantine to a total of seven cities with a population of 23 million people. The new crisis is creating a shortage of medical supplies, as many of the main Wuhan hospitals issued calls for donations of medical supplies. Major cities across China also began to announce a cancelation of major New Year Celebration, including Macau. The situation in Wuhan is extremely troublesome. Videos from cell phones showed crowds at hospitals and scenes of people collapsing on the street from the virus. Bloomberg did an in-depth look at the leadership of Wuhan and found that the same leadership that is managing the virus outbreak has been going to any length to cover up and hide massive environmental violations. The local government has gone as far as kidnapping a group of locals that went to Beijing to get the issue addressed. It was the same government team that allowed the wet market to continue to operate for weeks after the outbreak.
The *Washington Post* reported, "A bigger outbreak is certain," said Guan Yi a virologist who helped identity SARS in 2003. He estimated "conservatively" that this outbreak could be 10 times bigger than the SARS epidemic, because the SARS virus was transmitted by only a few "super spreaders" in a more defined part of the country. It is estimated that 300,000 people traveled to all areas of China on Wednesday before the network was shut down. The shutdown of all transportation came without notice and left thousands stranded. With over 20 million people now under quarantine, grocery stores are beginning to run out of supplies, as videos of empty shelves posted on social media seem to indicate.

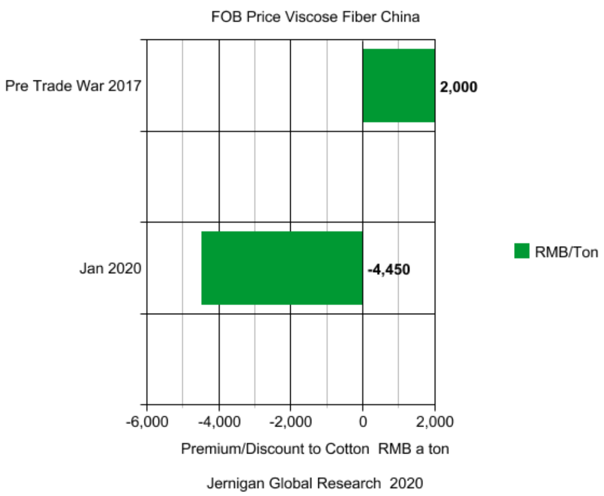
These measures will have a significant impact on retail sales. Regular sales, along with the volume of sales that occurs during the extended Chinese New Year celebrations, must be considered. In 2019, Lunar New Year retail sales reached one trillion RMB (148.33 billion USD). Of that total, a large block of sales was apparel. The 2020 retail sales will certainly fall, and the decline in sales will come at a tough time for the Chinese apparel industry, further undermining confidence. Mills have now closed for the holiday and are waiting for a return to business after the New Year holiday to determine raw cotton purchases. The expansion of the medical emergency will only serve to further delay any restocking decisions. Thursday was the last official trading day before the holiday, and the China CSI 300 Index closed 3.10% lower. Economists fear the damage to global economic growth may be greater than experienced during SARS. Rabobank estimates the share of world GDP from China was 15.8% in 2018, compared with 4.3% in 2003, while its post-crisis debt binge generated around 50% of global growth since 2008. China is now the largest consumer of almost every commodity in the world. The RMB that had been firming against the USD since the trade deal was announced fell sharply at the end of the week, losing 1.2% to close Thursday at 6.9426.

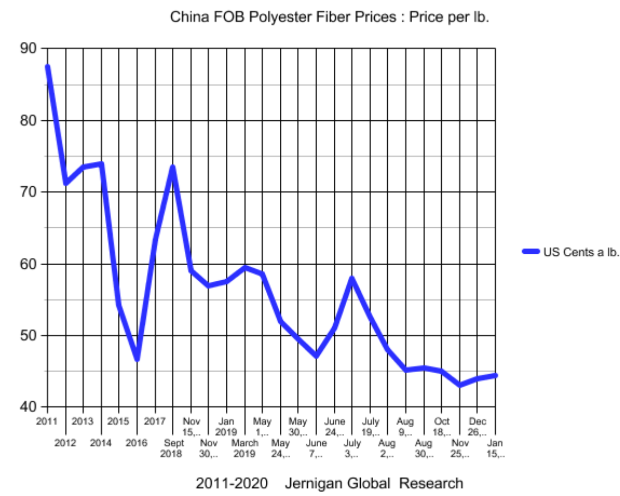
Earlier estimates are now beginning to place the cost of the epidemic at 100 billion USD, or twice that of SARS, and this is a very early estimate. Such a cost will come at a crucial time for the economy and will have a major impact on consumer confidence. The handling of the crisis could also impact the CCP and its image and control. Criticism on social media is already building regarding the handling of the crisis and the lack of warning. As last week ended, the crisis was continuing to spread as many areas appeared in panic. At Nanjing airport, two parents abandoned two children because they had a fever and were refused boarding. The video of the children and the story was a feature on Chinese social media. Shanghai Disney, which handles 100,000 people daily, announced that it is closed. China also announced the closure of 70,000 movie theaters. The travel ban was expanded to 36 million people, but people were still leaving by private car. The virus has been found in 32 of the 34 provinces. McDonald's restaurant announced it was closing in five cities.

A video appeared of people attempting to profit by collecting used face masks, washing them, and reselling, which illustrates the lack of understanding of the crisis or more likely the greed taking place. Videos of Wuhan hospital appeared in which dead people were lying in the hallways next to patients, indicating that the death toll is much larger than reported and just how overwhelmed the hospital is. China also announced a ban on travel tours both domestic and international. Another alarming story broke that the outbreak was linked to the lack of security at the Level 4 biosafety lab set up in Wuhan in 2017, located 20 miles from the wet market. The US has warned of the dangers to the lab several times.

By Friday, S&P began to look at a decline in discretionary spending, and they found a 10% decline would trim 1.2% off China's GDP. The decline may be greater than that, given the panic now underway. Apparel retailers are reported to already be offering large discounts due to worry over sales. There is analysis currently underway looking at how this crisis will impact government spending. The weakness in China's healthcare system has been clearly exposed to the Chinese people. There is official data that indicates a massive shortage of doctors. Only 23.8% of all doctors serving at community hospitals actually have a bachelor's degree or higher. With 1.4 billion people, China has only 60,000 doctors that are educated and trained on par with the US. France, with 67 million people, has 226,470 doctors. The lack of spending on healthcare has shattered the myth of China's economic power, as has the complete lack of a secure food chain. Some believe this could trigger a new focus, if not major crisis. The lack of healthcare and just how fragile their food supply chain is are now clear to 1.4 billion people.

CHINESE MILLS REPLACE COTTON WITH POLYESTER DUE TO THE PRICE SPREAD





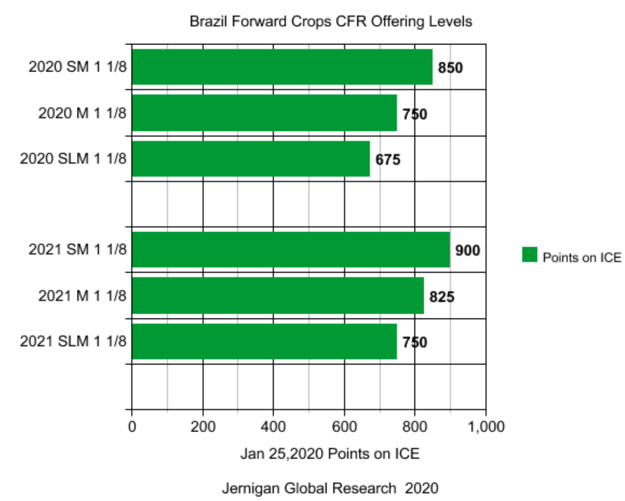
As mills closed for the Lunar New Year holiday, it was clear that cotton is overpriced in China compared to polyester, rayon, and viscose fibers. A survey showed that the average profit/loss of the average cotton carded or combed 32-count yarn was a loss of more than 50 RMB a ton. This was dramatically different from the current margins on poly/cotton 35/65 32 count of 600-700 RMB a ton, and over 900 RMB for a 32-count, 35/65 rayon/cotton blend yarn. Demand for 100% cotton yarns has not followed the market higher, which turned the margins negative. The cotton/poly ratio and cotton/Viscose have both reached extreme levels in the premium of cotton. While cotton rallied over 1500 RMB a ton from December lows before prices corrected, polyester and Viscose fiber prices have not moved. The demand for physical cotton turned very weak as prices rallied and mills substituted polyester and Viscose for cotton. The May ZCE cotton futures contract by the close on January 23rd had fallen nearly 1,000 RMB a ton, or over 6 cents a lb., since the recent high.

EXPORTERS TURN MORE AGGRESSIVE ON 2020 BRAZILIAN EXPORT OFFERS

The 2020 crop is rapidly being planted, and the rains over most areas have increased the selling interest of growers and merchants. The prospect of another record Brazilian crop and uncertainty over Brazil's market share of Chinese trade has merchants turning aggressive on 2020 crop offers for October 2020 and forward shipment. Strict Middling 1 1/8 offers are now at 850-900 points on Dec 2020 and March 2021 ICE futures out of the most aggressive sellers, Middling 1 1/8 offers are at 775-825 points on, and SLM 1 1/8 offers are 675-700 points on Dec and March. Pakistan was a major buyer of new crop last week.

Growers are also arranging to barter for inputs for the 2020/2021 crops following the decline in fertilizer rates. Rains are now falling daily in most of Mato Grosso and western Bahia, which is very welcome. Growers do face higher freight rates to move their cotton and grain to Santos port. An 11-15% increase in minimum freight rates has gone into effect. Brazil's ESALQ Index of a 41-4-34 landed Sao Paulo remains at a discount to ICE, with the price on 1/23 at 66.16 cents. The Real/USD exchange rate stands at 4.17 per USD.

The aggressive export offers for 2020/2021 from exporters suggest we may have a weaker tone to CFR basis levels due the uncertainty regarding Chinese demand.



ONCE CHINA'S LARGEST COTTON SPINNER, SHANDONG RUYI IS NOW BLACKLISTED FROM BUYING COTTON

Shandong Ruyi's credit woes increased as the International Cotton Association places it on a cotton trader's blacklist for failing to pay an arbitration award. This means no ICA member firm can trade with Shandong Ruyi, which suggests all cotton used from this point on by Shandong Ruyi mills will have to be Chinese cotton sold by a local firm. This means that even these firms may put the textile and apparel group on credit watch. This is not good news for Chinese cotton consumption. The operating rate of its largest mills, including those in Xinjiang, is very unclear. The *Financial Times* reported that Shandong Ruyi said it could not make payment on the arbitration award. A new worry on the financial health of the group appeared when *Bloomberg* reported a bond prospectus of the state-owned Jining City Construction Investment Group that had made a large commitment to buy a portion of Shandong Ruyi for 3.5 billion RMB (507 million USD) had not actually been made. *Bloomberg* noted that in the bond issue the group had to pay 1% above its rated peers for the bonds to be placed, indicating concern over repayment. This sparked concern that it may not be able to complete the investment. Jining itself was reported to have received a large injection of government capital, which would mean big problems for the company. Then, new debt woes are evident at Lycra, according to Bloomberg. Lycra USD and Euro bonds due in 2023 and 2025 are trading near 78 cents on the dollar. It was also revealed that a dispute has risen with creditors over a 400 million USD mezzanine credit line it used to pay two billion for Lycra. It was reported that Shandong did not make the payments and has breached covenants.

Shandong Ruyi woes are having ramifications around the world due to the companies it purchased in its post-2018 buying spree that was built on debt. Its part state ownership has not shielded it from the problems. Its problems are part of China's binge on debt that is now coming due. Lycra was once a vibrant US company, and now its debt has been downgraded to B, which is far below investment grade. For the global textile and apparel industry, the Chinese companies prior to 2018 had come to dominate much of the global industry, not only in China but around the world. The dramatic slowdown or halt to expansion is being felt in every corner of the world.

US COTTON EXPORTS SURGE WITHOUT CHINA, BUT SHIPMENTS LAG

US export sales were brisk during the week ending January 16th, with gross upland sales at 390,000 running bales. However, cancellation of 82,200 bales reduced net sales to 307,800 running bales. China was a minor buyer of a net 10,400 bales. The largest buyer was Turkey, which purchased 82,700 running bales. Turkey has now purchased 1,1160,600 running bales of upland cotton, more than double last year's sales at the same time of 549,200 running bales. This was followed by Pakistan, which purchased 116,200 running bales and canceled 44,000 for net sales of 72,200 running bales. Vietnam purchased 70,800 running bales, Indonesia 33,600 running bales, Egypt 17,600 bales, and India purchased 1400 bales and canceled 26,500 bales. Pima sales were also brisk at 20,200 running bales. India was the largest buyer of Pima at 6400 bales, followed by China at 6,000 bales. Bangladesh and Pakistan each purchased 2,400 running bales each of Pima.

Export shipments remain the concern, as shipments reached only 282,600 running bales of upland and 6,500 of Pima. The US must experience average shipments of 397,174 running bales for the rest of the season to meet the USDA target of 16.5 million 480-lb. bales. At the current pace of shipments near 300,000 bales a week, the US export shipments will reach only 13.5 million bales, which would result in the US carryover being raised three million bales.

AUSTRALIA RAINS CONTINUE OVER COTTON BELT

It's not the "Big Wet" yet, but pockets of heavy rains have continued over the Australian cotton belt. Weekly rainfall as of January 22nd ranged from 10-50 mm over most of the NSW cotton belt. The rains extended to the south and covered the Riverina. Additional heavy rains have continued. Moree, for example, received an additional 61 mm from a storm on January 24th, which follows 56 mm the week before. Sand and and mud storms also occurred. Heavier rains have fallen in Queensland. Emerald received 79 mm in the week ending January 22nd, Biolela 54 mm, and Theodore 90 mm. Oakey reported weekly rainfall of 122 mm, and the Leslie Dam reported 110 mm. Chinchilla recorded 45 mm, St George 25 mm, and Toowoomba 56 mm. Rains are forecast to continue through Tuesday. Conditions are improving and dam levels have also begun to build. The outlook for the 2021 crop has begun to improve.

ICE FUTURES RALLY STALLS AS CORONAVIRUS CRISIS PRESENTS NEW CHALLENGE TO CHINESE ECONOMY

ICE futures collapsed on Tuesday then surged on Wednesday before beginning to retreat on Thursday. Wednesday's price action created a technically important outside range session and 68.71-71.30, suggesting that the rally had reached a possible turning point. This was followed by the underreported explosion of the Chinese Coronavirus. By Friday, a global health crisis was underway, with Chinese New Year celebrations shut down and over 40 million people placed under travel bans. Social media provided no confidence that the crisis was under control as videos circulated of hospitals overwhelmed with patients, with dead located next to the living. People were panicking to get out of the banned cities, parents even abandoned their children at the airport in a panic to get out. Major New Year Celebrations were canceled across China, and the virus was reported in 32 provinces as people traveled. One social media posting even showed of a couple from Wuhan, the center of the outbreak, who had escaped, saying they had a fever but were out partying in another city anyway. First, the entire crisis has sparked a major health crisis in China and concern about the state of China's health system to serve 1.4 billion people. Second, the event could cause significant economic damage to the Chinese economy and to the global economy. We expect domestic Chinese apparel sales to suffer a major impact, as will sales in markets such as Hong Kong that depend on Chinese tourism. Commentary from cities located away from the impact zone has indicated that retailers had already begun to discount apparel in order to draw customers out to shop. In the eastern areas, the authorities are making a significant effort to get people to stay home, which will affect sales.

This crisis is coming at a crucial time for the Chinese textile and apparel industry, since hopes were that domestic sales of apparel would improve during the New Year celebration and set the tone for a rebound for the reminder of 2020. Moreover, the signing of the US/China trade agreement had raised hopes that export orders would improve. As we discussed earlier, the sharp rally in domestic cotton prices had turned cotton yarn margins negative and increased the use of polyester and Viscose fiber in place of cotton. The rally was halted, with ZCE prices collapsing into the holiday close. The May contract closed at 13,440 RMB a ton, retracing over 60% of all gains since the trade agreement. Outside of China, cotton demand in the largest consuming markets is strong and supplies tight. Turkey, Pakistan, Indonesia, Bangladesh, and Vietnam remained active last week and took up additional supplies after the futures setback to 69 cents. US, Brazilian, Mexican, East African, and ELS cotton moved off. As we mentioned, Brazilian exporters have increased the aggressive nature of their 2020 crop CFR Asian basis levels in order to give spinners the incentive to begin to increase coverage. This worked in Pakistan where 2020 SLM 1 1/8 moved in volume.

The Davos World Economic Forum was last week, and the theme was a new focus on sustainability investing and the end of the age of fossil fuels. This, however, occurred as the supply of natural gas was such that prices moved below 2 USD. This means that the US will add to the pressure in the byproducts such as PET that make polyester staple. Then, in China, new large capacity will come online after the New Years holiday. This capacity is from new projects by the large state-owned companies that have traders in China fearing new price pressure, even with PET and polyester at record lows. The NDRC in China has made no effort to rein in the insane expansion in this sector. It was estimated by Neill Ferguson in Davos that 60% of all global CO_2 emissions come from China. All of this means that, in the near-term, polyester and man-made fiber prices are a real inhibitor to the advancement of cotton prices.

As Friday closed, the US commodity and equity markets posted losses due to the situation in China, and the travel restriction had been expanded to 46 million people by the close of the markets. The CRB Commodity Index closed 1.55% lower, with crude oil down 2.34%, natural gas off 1.97%, copper down 1.49%, corn posting 1.65% losses, soybeans -.87% and hogs down 2.52%. Cotton closed on its lows. US equity markets closed near their daily lows, with the largest drop since October. These losses were linked to fears that demand from China will be weaker than expected. The CFTC data showed generally that the Managed Funds, Other Funds, and Index Funds all had halted their buying in cotton.

Last week we discussed that we had turned cautious, and that has proved correct. The market rally has technically shown the first signs of a top. A close below 68.70 in March would suggest this has occurred, and prices will retreat to the 64/65 area. A close above 71.30 in March would suggest a new up move.

The major US agriculture commodity markets that should receive a boost from the new China/US trade agreement are now trading well below the market levels reached just before the agreement was signed. The markets are concerned over demand and the timing of Chinese purchases. As we have stated several times, the agreement did not create new demand. It just assured the US a portion of the Chinese demand if the agreement is honored. For cotton, the issue remains that demand in China is weak, likely to remain weak, and will contract further as a result of the economic fallout of the current health crisis. The demand from the major markets outside China is good, which is cushioning the impact of the China situation. If China does fulfill the trade agreement and cotton does get 1.3-1.6 billion USD allocated, it will come from the shipment of outstanding sales and purchases by the Reserve. The timing of this or its reallocation to other commodities with greater demand are the unknowns.

China today is not the China of 2003 when SARS occurred. The weakness in the Chinese health system, lack of doctors, inadequate hospitals, and government incompetence are well broadcast over social media. As we finish this week, the virus has spread further, reaching France, Australia and others, and Singapore has forced a plane to return to China after being quarantined. Social media showed a voice mail from a Wuhan health care worker stating that the infection had reached 100,000, far greater than the official total. This has further shaken confidence. This could have major consequences for allocation of resources and government spending. For now, demand and confidence have been impacted, and consumer confidence will not quickly return to normal.

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