Summer 2011

StaplReview



High Prices and Volatility

Battling Weather Extremes

High Prices and Volatility

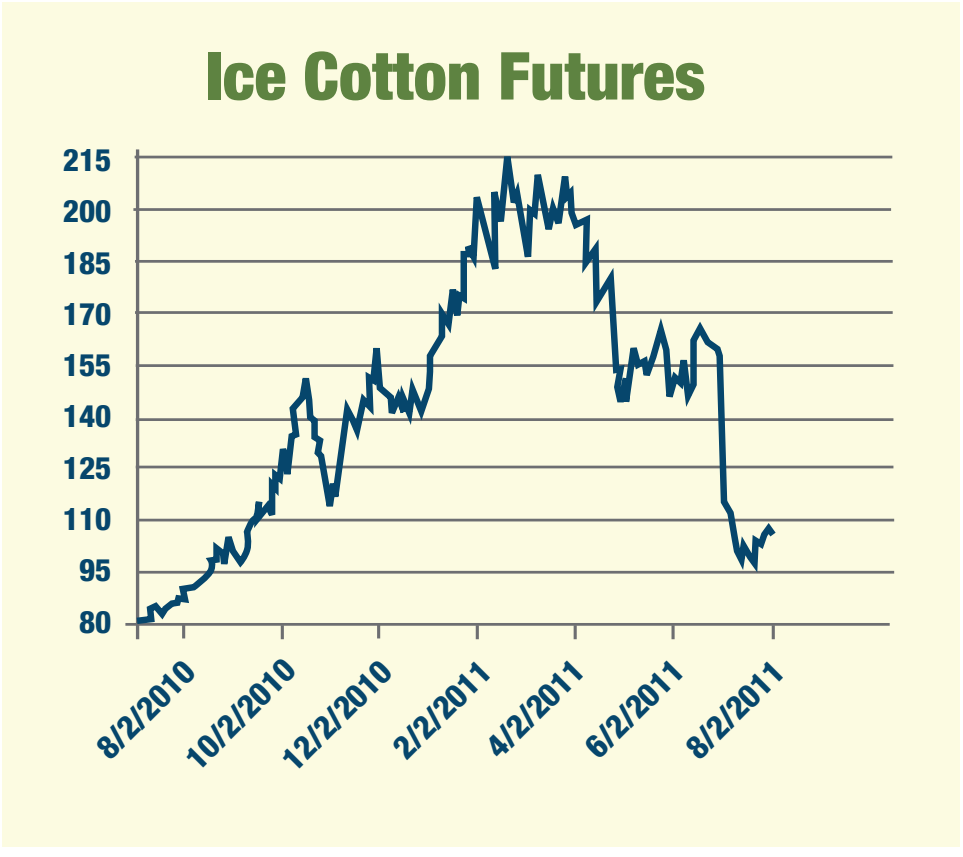


Meredith Allen
President & CEO

The old saying, "High prices cure high prices" has proven once again to be very true. The extreme prices that we witnessed last winter and early spring have caused much anxiety throughout the cotton industry. Have higher prices been good for producers? Absolutely, but obviously more beneficial to the 2011 crop than the 2010 crop. Most of the 2010 crop had been priced before the market exploded to the upside last fall. However, most producers have taken advantage of higher market prices for a portion of the 2011 crop. The negatives for producers from the extreme price rise are a large increase in cotton plantings around the world as well as a decrease in consumption due to much cheaper competing fibers. Also many textile mills were caught long cotton and/or cotton products when the market finally collapsed. As a result of this price drop, these mills were left with significant financial losses and far less ability and confidence to hold cotton inventory. So, at least for now, high prices have cured high prices. In the short-term, our industry will have to suffer through the damage caused by last season's extreme price action. However, I am optimistic that long-term cotton prices will be attractive to producers as the worldwide competition between food and fiber continues.

Recently, management has talked to the Board of Directors and the Advisory Committee members about why a wider than normal initial advance is necessary. With the extreme volatility in the futures market comes extreme volatility in the basis. Projecting a final basis to apply to both the Call and Seasonal Pools' hedges is now nearly impossible until a majority of the cotton is sold. This price volatility also means Staplcotn may experience large margin calls from the cotton futures exchange when prices move up sharply. A wider advance coupled with the large line of credit we have secured means Staplcotn can withstand those extremes. A good example of what can happen occurred just last year. Members in the Call Pool and management on behalf of the Seasonal Pool called December futures between 75-80¢ per pound. Staplcotn sold futures at that level and put up margin on many of those futures to market levels exceeding $2.00 per pound. When you consider the advance to the membership plus the margin, Staplcotn had close to $1,000 per bale cash outlay on a substantial amount of our inventory. Staplcotn does not recoup that money until the textile mills price their cotton and take delivery of it. The unknown created by the potential for extreme price movements dictates that management be even more conservative financially than in the past. Until most of the cotton is at least sold and a substantial portion is shipped and paid for, a wider advance is necessary to protect our members' equity in the company. This wider

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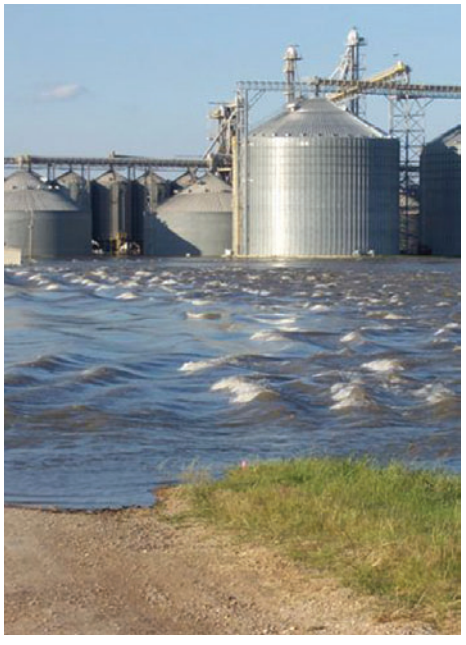


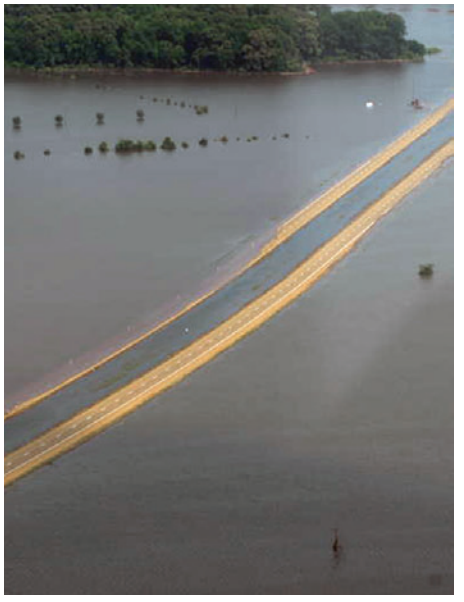
Battling Weather Extremes

It seems when you talk to any one of the Staplcotn directors who have witnessed the extreme weather problems this year, whether they are from the Mid-South or the Southeast, the response is the basically the same, "I've never seen anything like this is all my years of farming".

The spring of 2011 brought floods to many areas of the Mid-South, some of which were followed by severe wind and sand storms. On the other end of the spectrum, much of the Southeast has battled drought conditions which have left many of these seasoned cotton producers desperate for an extended fall.

Johnny Hux, director from Sikeston, Missouri, explained how his area was affected by the floods in early May. "We are in the part of Missouri—Mississippi County—where the decision was made to blow the Birds Point Levee to ease the pressure of the water flowing into the Mississippi River. That obviously flooded all of the lower level farm land which was mainly bean and corn ground. Then, we had 28 ½" of rain which flooded the west side. That





Flooding in the spring of 2011 put thousands of acres of cropland under water as well as roads.

was cotton ground and it wasn't able to drain very quickly because the ditches couldn't handle more water. Most of the cotton crops had to start late as a result. East of here, some of the farms had ground that eroded too much and they couldn't plant. Further west, some farmers got a crop in but had to change plans because after the flooding, we had a drought. We've had farmers that had to replant a couple of times and the weeds have been like you wouldn't believe. Lately we've had a few showers, though. It looks like we should make a good crop IF we don't get an early frost. We've had to do a lot of irrigation though, and without that we would be 'up a creek'. Many around here are just hoping to break even."

Like Hux's area of Missouri, Staplcotn Director Lowry Robinson's area around Osceola, Arkansas, experienced flooding both from the river itself and the "dry" side of their levees with the standing water due to heavy rains. But, after that subsided, they were faced with horrendous wind and sand storms for over a month that wiped out whole stands of cotton. Robinson explained, "Farmers in the area found themselves planting two or three times and some finally ran out of calendar. Some of the cotton acreage went to beans for that reason. Had we not had such severe weather in northeast Arkansas, we would probably be seeing 10-15% more cotton here. The amount of cotton acreage lost would have been even higher had some of the farmers not called their cotton already. They did whatever it took to get cotton in the ground and pushed their calendars a little further. Things are looking better now around here, though. It will still be a late crop and we will need a nice fall to have a reasonable yield. It's about as strange a year as I have ever seen." Robinson's area has also experienced significant weed problems. "I've haven't seen this many people chopping cotton in the fields in years," he said.

Staplcotn Director Bowen Flowers said his area around Clarksdale, Mississippi, was fortunate in that it avoided the flood water problems but it wasn't so lucky with the wind and sand storms. "Mid-May, after most had finished planting, we witnessed serious wind storms and sand storms that wiped out the sandy land cotton and many had to replant. Now, we are about three weeks late. In some of the areas around here, farmers had to replant about a third of their total acreage. The sand storm was so severe, that in some spots in Tunica County, they had to get a road grater to get the sand off the road."

Although Mother Nature dealt a polar opposite hand to many in the Southeast, the challenges they've faced have been quite similar. Mike Newberry, Staplcotn Director from Arlington, Georgia, reported that his area has had complications



Meredith Allen and Stan McMikle inspect an irrigated field in Georgia.

from the drought since the onset of planting season. "From this area and south, many of the fields are irrigated with a Floridian aquifer which is usually recharged in the wintertime with the rains we normally get. We went into this season without our normal underground supply of water—only about half of what we normally have—and the daily temperature has averaged three degrees higher than normal. So it was hard to get the crops in the ground, hard to get them to make a stand. Many area farmers with dry land crops have had to plant two or three times and some of those farms have been harrowed up. We have several more weeks to keep water on the irrigated crops but some of the wells went dry about a month ago. In the last three weeks, Southwest Georgia has seen some pretty good rainfall, but the dry land crop is late so they need an extended warm fall to make the crop here. We need at least four extra weeks and we sure don't need a frost between now and Christmas!"

Allen Whitehead, Staplcotn Director from Ashburn, Georgia, had a similar report. "Many farmers in this area had to water two or three times just to try to get the cotton in the ground. Then, they had to plant two or three times to make a stand. One farmer replanted five times and still didn't have a stand. Many of the smaller farms have had to be abandoned and thousands of acres around here have been harrowed up. On some of the crops that have been irrigated with center pivots, you can look in the corners and see nothing, not even weeds. In the fields, though, the weeds and bugs have been extremely difficult to deal with. Because of the height differential, some have either not been able to use herbicides or they've seen a significant



"You can look in the corners and see nothing, not even weeds."

resistance to the herbicides. Farmers around here have had to do more hand weeding than they've ever done. The input costs on this year's crop have increased tremendously—more irrigation, more fuel costs, and higher herbicide costs.I've talked to some people around here who have said they've had planters out this year longer than any other time in their farming careers. This is my 32nd or 33rd crop and I've never seen it this way," said Whitehead.

George LaCour, Staplcotn Director from Morganza, Louisiana, explained that his area has been affected by both extremes—record setting floods AND a record setting drought all in the same year. "Half the parish has been under water and the other half is burning up," he said. "Out of the 280,000 acres of cotton in Louisiana, 10% was affected by the water, but 90% is affected by the drought. The non-irrigated cotton looks awful and rains continue to be sporadic here. There's only been maybe an inch of rain here since April. Some folks affected by the flood were able to replant, but some of the land never got a crop on it. The mood of the people this year though, is much better than you would expect. At least this year, the insurance will cover their costs because it was figured at around $1.30 per pound which helps the anxiety level. We couldn't wait for this year to start and now, we can't wait for this year to end. But the general attitude is that we'll be back. We'll try it again next year."

Even with all of the challenges and adversities brought on by this history-making spring weather, it appears that there could be a rainbow ahead. Most of those who have "weathered the storm" are now experiencing good growing conditions for the late planted crops. If these conditions continue until harvest season, and they get a little extra help from Mother Nature with a delayed frost, they should be able to realize the true potential of this 2011 crop.

Advisory Board Meetings–A Valuable Exchange

From its beginning, Staplcotn has been fortunate to have a strong and active Board of Directors which today consists of 33 members. They represent their regions well and are charged with the responsibility of setting policies for the Cooperative. The Board meets quarterly at the Staplcotn Main Office in Greenwood, but all board members give a significant amount of their time in between meetings to participate in conference calls, committee meetings, and other forms of communication with management when their input is needed. This structure has proven to be successful for 90 years and their contributions are more than appreciated.



In addition to the Board of Directors, Staplcotn also relies on a larger number of its members who represent their areas as advisors to the company. The number of advisors varies, but averages out to be around 23 members from each Staplcotn region. Each year, Staplcotn conducts a series of Advisory Board meetings in July in order to have face-to-face interaction with these advisors. This year's Advisory Board meetings were held in Memphis, TN; Rayville, LA; Greenwood, MS; Statesboro, GA; and Albany, GA. These meetings are of critical importance on many levels.

First, Staplcotn is able to report to the advisors on the happenings of the previous year. They are given specific data on how the company has performed on sales, shipments and inventory. They are presented information on industry trends, challenges and projections. In the last two years, management introduced a change in format which includes a focus on a specific department for each year's presentation. This year's focus was on the Marketing Department. Hank Reichle, VP of Export Sales and Market Administration, along with Frederick Barrier, VP of North American Sales, gave presentations on what their department's responsibilities are, who are involved, how sales and hedging are executed, and much more valuable information. Meredith Allen, President and CEO, commented, "I think it's really important for them to get to know the people who are working in the different departments. In this case, they were able to meet and talk to the people who are selling their cotton for them."

The purpose of these Advisory Board meetings is not only to report information to this group, but also to receive information from them. Sterling Jones, VP of Cotton Services, explained, "It's extremely important to be able to have face-to-face conversations with our advisors. We like to know what they expect from Staplcotn. We like to talk to them about problems or situations that their area is having and they provide us with very valuable crop analysis information. This year was especially important. There are so many different problems in different areas that it is critical to get their feedback. The information we receive helps us to make projections and decisions that will better serve our membership."

Advisors are not required to attend the Advisory Board Meetings, but they are encouraged to do so if their time allows. This year's attendance was lower than usual due to the challenges so many were facing in the fields. "It's difficult for advisors to break away sometimes, especially in years like this when their struggles are so prevalent. We really do appreciate the ones that are able to get to the meetings, but completely understand when their farm prohibits them from joining us. We were still able to get great information from those who were able to come which is tremendously helpful," Jones said.

Jones further explained that there are often times "slots" to fill on the Advisory Board and Staplcotn encourages its members to participate. "Every year we have members who ask to resign for various reasons—some are retiring, some are no longer planting cotton, or some feel like the younger generation needs to become more involved. Should a member have an interest in serving on the Advisory Board, he or she should contact their Cotton Specialist and make their interest known. It is so important to have members who want to serve and assist in making Staplcotn the best company it can be for the entire membership."

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President's Message continued

than normal advance also means that the progress payments in both the Seasonal and Call Pools will be larger, as a percent age of the total payments, than in the past. Hopefully the wider basis will be brought back to normal levels with the first two progress payments. Management does not expect more conservative advances in any way to adversely affect the competiveness of our final return to the membership. As our mission statement says, we are to enhance our members' income, and we will certainly continue to do that. This company is owned by the members, and it is management's responsibility to recommend policies and procedures to the Board that keep the company strong financially. These types of actions assure our members that they will continue to have direct and dependable markets for their cotton. With the consolidation that has taken place in the last few years in the merchandising segment of our industry, it is more important than ever that our producers have a strong and viable cooperative to market their cotton.

In closing, I am excited about the prices that members have been able to lock in so far for the current crop. For our members that were not devastated by floods and/or droughts, 2011 should be a very profitable year. Good luck with your harvest this fall.

Meredith Allen

Staplcotn

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