Testimony of Shawn Holladay
Producer Perspectives on the 2023 Farm Bill
Subcommittee on General Farm Commodities, Risk Management, and Credit
House Committee on Agriculture
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Introduction

I am Shawn Holladay, a fourth-generation West Texas cotton producer residing in Lubbock, and I currently serve as chairman of the National Cotton Council (NCC). I also served as chairman of the American Cotton Producers (ACP) in 2018 and 2019 and previously chaired the ACP's Farm Policy Task Force for multiple years, working closely with Congress on the creation and implementation of the seed cotton program for U.S. cotton producers.

Along with my wife, Julie, and daughter, Katy, our family owns and operates H2H Farms. Our operation includes land in Dawson and Martin Counties of West Texas, primarily producing cotton. I am also a partner in United Gin Corporation, located south of Lamesa, Texas.

The National Cotton Council (NCC) is the central organization of the United States cotton industry. Its members include producers, ginners, cottonseed processors and merchandizers, merchants, cooperatives, warehousers, and textile manufacturers. A majority of the industry is concentrated in 17 cotton-producing states stretching from California to Virginia. U.S. cotton producers cultivate between 10 and 14 million acres of cotton, with production ranging from 12 to 20 million 480-lb bales annually. The downstream manufacturers of cotton apparel and home furnishings are in virtually every state. Farms and businesses directly involved in the production, distribution, and processing of cotton employ more than 115,000 workers and produce direct business revenue of more than $22 billion. Annual cotton production is valued at more than $5.5 billion at the farm gate, the point at which the producer markets the crop. Accounting for the ripple effect of cotton through the broader economy, direct and indirect employment surpasses 265,000 workers with economic activity of almost $75 billion. In addition to the cotton fiber, cottonseed products are used for livestock feed and cottonseed oil is used as an ingredient in food products as well as being a premium cooking oil.

Economic Overview

The U.S. cotton industry continues to navigate an environment characterized by increased production costs, sluggish consumer demand, and supply chain disruptions. For the current 2022/23 marketing year, the U.S. Department of Agriculture (USDA) estimates world cotton consumption at approximately 110 million bales, down 5% from the previous year and down 11% from 2020/21. The decline in global demand stems from several factors. First, continued price inflation, especially for energy and food products, is putting additional pressure on consumer purchasing power, thus limiting demand for apparel and textile products. Second, events such as the foreign currency crisis in Pakistan and the devastating earthquake in Turkey are limiting the demand for U.S. cotton by those two textile industries. Third, global supply chains are continuing to adjust to China's slow post-COVID economic reopening and the implications of the Uyghur Forced Labor Prevention Act. Projections for the upcoming 2023/24 marketing year call for a modest recovery in world cotton

consumption, but those estimates hinge on a continued recovery in the global economy and moderation in overall inflation.

In 2022, U.S. growers planted 13.8 million acres of cotton, as higher prices encouraged a 23% increase in area. However, due to extreme drought conditions in the Southwest, harvested acreage of 7.4 million acres was at the lowest level since 1983. U.S. production of 14.7 million bales was 2.8 million bales lower than in 2021.

Looking ahead to the 2023/24 marketing year, production costs remain elevated and are only slightly lower than year-ago levels. According to USDA's Economic Research Service, U.S. cotton production costs increased by $161 per acre between 2018 and 2022 – an increase of 20 cents per pound based on an average yield of 800 pounds per acre. Cotton harvest-time futures prices in mid-April 2023 are 19% lower than a year ago, while the prices of competing commodities are just 7-8% lower than year-ago levels. Cotton producers will face difficult economic conditions in 2023 with lower cotton prices and high production costs.

The current economic signals are reflected in the latest acreage expectations with USDA calling for 11.3 million acres planted in 2023, a drop of 18%. Given current drought conditions in the southwestern United States, there remains much uncertainty regarding cotton production for the 2023/24 marketing year. To estimate U.S. production for 2023/24, the NCC applies the 5-year average (2018-2022) abandonment rate and yield for most cotton-producing states. In the Southwest, adjustments were applied to the 5-year average values to account for current drought conditions. For 2023/24, U.S. harvested area is estimated to be 8.7 million acres with an overall abandonment rate of 22.6%. 2023/24 U.S. production is estimated to be 15.5 million bales with an average yield of 853 pounds per acre.

Additional Budget Resources

The general program structure authorized by the 2018 Farm Bill has served the industry well and should be maintained in the new farm law. However, as Congress charts the path for the 2023 Farm Bill, additional funding is necessary to address challenges both on the farm and throughout the supply chain.

Since the implementation of the 2018 Farm Bill, ongoing trade tensions and geopolitical disputes have caused major disruptions in cotton exports, revealing gaps in cotton's safety net. A major disruption in the global demand for cotton fiber also occurred due to the worldwide COVID-19 pandemic, leading to increased storage, supply chain disruptions, and an overall reduction in global cotton consumption. Since passage of the 2018 Farm Bill, cotton growers have also been impacted by record droughts across the Southwest and Western portions of the Cotton Belt as well as devastating hurricanes across South Texas and the Southeast.

Thankfully, Congress and USDA responded to the needs of the cotton and agricultural industries by authorizing several *ad hoc* assistance programs. Since 2017, Congress has provided more than $90 billion in *ad hoc* assistance to agriculture, and between 2018 and 2021, *ad hoc* assistance comprised approximately 70% of all direct farm payments, which includes traditional farm bill support provided through the commodity and crop insurance titles. Although the U.S. cotton industry continues to face a challenging economic environment, Congressional budget procedures do not allow this past funding to be captured in the new farm bill without additional dollars being allocated

by the House and Senate Budget Committees. We must ensure the House Agriculture Committee has the necessary resources to draft a farm bill that addresses the current needs facing the cotton industry.

Producer Safety Net

The cotton safety net must consist of two key components: 1) an effective commodity policy that provides either price or revenue protection to address prolonged periods of low prices and depressed market conditions that span multiple years; and 2) a strong and fully accessible suite of crop insurance products that producers can purchase to tailor their risk management to address yield and price volatility within the growing season.

The annual producer election of either Agriculture Risk Coverage (ARC) or Price Loss Coverage (PLC) included in the 2018 Farm Bill has worked well for growers and should continue in the new farm bill. Cotton producers have overwhelmingly selected the PLC program, with more than 90% of seed cotton base acres enrolled under that option. Agricultural markets are cyclical, and an effective safety net is imperative for the inevitable times of low prices. The combination of commodity program options and crop insurance provides farmers as well as their lenders the confidence entering the planting season that downside risk is mitigated in periods of steep price decline or a significant loss of production.

Supply chain disruptions and geopolitical crises in nations that provide a substantial portion of critical production inputs have led to a dramatic increase in cotton production costs, leading to tighter profit margins and decreased profitability. Since 2018, cotton costs of production have increased by 20 cents per pound, based on average yields of 800 pounds per acre. For many producers, total production costs now range between 90 cents and $1.00 per pound, which exceed current futures prices trading in the mid-80s. When calculated based on seed cotton, the total costs to produce a pound of seed cotton have risen nearly 9 cents since the 2018 Farm Bill, with current costs of production of almost 48 cents, far above the seed cotton reference price of 36.7 cents per pound (Exhibit 1). The current costs facing producers are diminishing the effectiveness of the current PLC reference price.

In addition, growers enrolled in the ARC/PLC programs are currently limited in their access to crop insurance due to a prohibition on the purchase of the Stacked Income Protection Plan (STAX) on their enrolled farms. STAX is a crop insurance product for upland cotton that provides coverage for a portion of a producer's revenue based on the county, or area-wide experience. In 2018, when seed cotton became eligible for the ARC/PLC under the commodity title, Congress prohibited the purchase of STAX on ARC/PLC-enrolled farms, beginning with the 2019 crop. At the beginning of the prohibition, most growers chose to enroll their base acres in PLC. However, with higher cotton futures prices for the 2021 and 2022 crops and limited effectiveness of the current seed cotton reference price, STAX has become a more attractive option.

Cotton producers should not be limited on their crop insurance options and should be able to manage risk based on the needs of their operation. Eliminating the prohibition on simultaneous enrollment in PLC and STAX, as well as boosting the top coverage level of STAX for those farms with no seed cotton base or who forego enrollment in ARC/PLC, would allow a grower to tailor their risk management options according to the needs of their operation while also decreasing their reliance on *ad hoc* programs, putting producers in charge of their own production risks.

Upland Cotton Marketing Assistance Loan

The non-recourse marketing assistance loan program for upland cotton remains a cornerstone of farm policy for the U.S. cotton industry. While current prices are well above the loan rate, we know that will not always be the case. During times of low cotton prices, the marketing loan program is an essential tool for multiple segments of the cotton industry to effectively market cotton and provide cash flow for producers to meet financial obligations. Even in times of higher market prices, the marketing loan is utilized by the cotton industry to provide cash flow for producers and flexibility in marketing to encourage orderly movement of the crop throughout the year. In recent years, over 50% of the upland cotton crop enters the loan, and use of the loan approaches 80% in times of low prices. Also, in periods of low prices, if growers choose to forgo the marketing loan, they may receive a Loan Deficiency Payment (LDP) representing the difference between the loan rate and the market price. This is an important component of the marketing loan program that should be retained.

Despite higher production costs, the maximum level of the loan rate has remained at 52 cents since 2002. The level of the loan rate should be increased to better reflect current costs of production and recent market prices. In addition, loan repayment provisions should be modernized to better reflect the competitive landscape in the global market and the higher storage and logistics costs facing the industry by: 1) allowing storage credits to better reflect actual storage charges; and 2) determining a globally competitive Adjusted World Price (AWP) based on the three lowest international prices, limiting the amount of the annual decline in the costs-to-market values, and a 30-day window for finalizing the AWP (Exhibit 2).

Since being implemented in 2006, maximum storage credits have declined, while actual storage charges have increased. Between 2006 and 2022, average storage charges across much of the Cotton Belt increased by 45 cents per bale per month, while the effective storage credit fell 8 cents per month. Currently, the effective storage credit is 78 cents below the average storage charge.

Basing the AWP on an average of the three lowest quotes in the international market, rather than following the current practice of using the five lowest quotes, would create more value for cotton during loan redemptions and prevent cotton from stagnating in the loan and accruing costs. This will in-turn make the cotton loan more effective in providing support for producers and ensuring fluid movement into the marketplace. Moving to the three lowest quotes is also consistent with other provisions of the marketing loan program that are already based on three quotes.

Establishing limitations on the annual decline in the costs-to-market calculation is imperative. USDA currently conducts an annual survey of costs-to-market, and in recent years the industry has witnessed large changes in this calculation, which can negatively affect marketing decisions. While USDA would continue to conduct the annual survey of costs, this provision would establish limitations on the annual decline from the previous year to mitigate negative impacts on the competitiveness of U.S. cotton.

Providing increased flexibility in AWP determinations during loan redemptions would allow producers to realize a more optimum AWP from the day of the loan redemption or the locking in of a LDP. Growers would then have the benefit to lower their costs to redeem cotton for a thirty-day period following the redemption date. This provision would be another tool to help move cotton

from the loan and into the marketplace. Similar flexibility should also be provided to the determination of the LDP.

Complete automation of the marketing loan program should also be addressed in the next farm bill. During the December 2018 lapse in government funding, these programs were severely impacted due to the need for direct personnel involvement in processing the entry and redemption of cotton in the marketing loan program. During this period, some growers were not able to enter cotton into the loan and access those funds, while others could not market their cotton because they could not redeem the loan. We urge this Committee to work with USDA to provide the necessary support to ensure that any future lapse in government funding does not negatively impact the marketing loan program.

Extra Long Staple (ELS) Cotton Policies

There are important policies in place for ELS, or Pima, cotton. ELS cotton is grown in California, Arizona, New Mexico, and parts of Texas. The 2018 Farm Bill continued the ELS cotton loan program as well as a provision to ensure U.S. Pima cotton remains competitive in international markets. The balance between the upland and Pima programs is important to ensure that acreage is allocated in response to market signals instead of support levels.

ELS producers, like their upland counterparts, have experienced sharp increases in production costs in recent years, with current costs exceeding the safety net provided by the loan program. While ensuring that market signals remain the driver of planting decisions, the 2023 Farm Bill can address deficiencies in the safety net provided to ELS cotton producers by increasing the ELS loan rate to a more reflective level of pricing and costs of production.

The next farm bill should also add "marketing loan" functionality to the ELS loan. Of all the commodities eligible for Commodities Credit Corporation (CCC) loan, ELS is one of only two commodities with a non-recourse loan that lacks the provisions of an alternative repayment provision during periods when market prices are lower than the statutory loan rate. The new farm law should also maintain the ELS Cotton Competitiveness Payment Program and the Pima Cotton Trust Fund.

Economic Adjustment Assistance for Textile Mills

After a decade of experiencing a precipitous decline in the amount of cotton used by U.S. textile mills, U.S. mill consumption has stabilized since 2008 due to ongoing assistance provided in the Farm Bill. The recent years of stability and expected future growth can be attributed to the continued benefits of the Economic Adjustment Assistance for Textile Mills (EAATM) program, originally authorized in the 2008 Farm Bill. Recipients must agree to invest EAATM proceeds in equipment and manufacturing plants, including construction of new facilities as well as modernization and expansion of existing facilities.

EAATM funds have allowed investments in new equipment and technology, thereby reducing costs, increasing efficiency, and allowing domestic mills to be more competitive with foreign mills. This was shown to be prophetic during the COVID-19 pandemic as the U.S. textile industry was able to quickly shift their manufacturing facilities to the production of personal protection equipment (PPE). In addition, the industry continues to be a critical supplier of products to our defense

industry. The yarns and fabrics produced by the U.S. textile industry are also integral products in the two-trade occurring with the Dominican Republic-Central American Free Trade Agreement (CAFTA-DR) and the United States-Mexico-Canada Agreement (USMCA) countries.

When EAATM was initially implemented in 2008, the support level provided was set at 4 cents per pound of cotton consumption by the U.S. textile industry. Yet, budget pressures reduced that number to 3 cents in 2012. We urge Congress to restore EAATM support to the original 4-cent level in order to further support this critical employment and manufacturing base.

Payment Limits and Program Eligibility

Our industry is opposed to any further tightening of payment limits and program eligibility requirements, as we believe these policies are already too burdensome and restrictive considering the size and scale of production agriculture necessary to be competitive and viable in today's global market. The NCC has always maintained that effective farm policy must maximize participation without regard to farm size or income. Artificially limiting benefits is a disincentive to economic efficiency and undermines the ability to compete with heavily subsidized foreign agricultural products. Artificially limited benefits are antagonistic with a market-oriented farm policy. In fact, the current program limits are incompatible with the cost structure and capital investments necessary for today's family farms.

We are encouraged that Congress recognized this reality in recent disaster assistance by including increased payment limit levels for producers who realize the majority of their income from their farming operation. This same consideration should be given to Title I program limits in the next farm bill. Other proposed arbitrary restrictions regarding the contribution of management and labor through changes to the definition of "'actively engaged'" are out of touch with today's farming operations and would only contribute to inefficiencies. These policies also discourage the next generation from returning to their rural communities. Under these proposals a son or daughter who wants to return to the farm and utilize their accounting degree to market the crop and keep the books would not be considered as "actively engaged" in the operation. The 2023 Farm Bill should not include policies that seek to discourage the next generation of farmers.

Conservation

A strong conservation title benefits the environment and is an important tool for producers across the United States. Voluntary conservation programs reward producers for implementing sensible environmental practices on working lands and provide a means to devote marginal production acres into long-term use.

Working lands conservation programs are of utmost importance to most producers. Going forward, the application of conservation funds, both provided by the 2023 Farm Bill and the 2022 Inflation Reduction Act, should 1) recognize the diversity of production practices by rejecting a one-size-fits-all approach; and 2) reward – not penalize – the environmental contributions of early adopters.

International Programs

The Market Access Program (MAP) and Foreign Market Development Program (FMD) are extremely important tools that support U.S. exports. Cotton Council International, the foreign

market promotion arm of the U.S. cotton industry, utilizes both programs and the industry has seen clear benefits from these programs. Our industry supports the Coalition to Promote U.S. Agriculture Exports proposal to double funding for both MAP and FMD. MAP has not been increased since 2006 and one-third of funding has been lost to sequestration, inflation, and program administration. FMD has not been increased in almost 20 years. With market volatility and economic disruptions causing greater risks and uncertainties, the new farm bill can provide the additional resources necessary for U.S. agricultural exports to remain competitive.

Conclusion

In closing, I encourage the Committee to write a farm bill that provides long term stability for the future. There will be price declines from current levels, there will be natural disasters with losses more severe than the essential assistance that commodity programs and crop insurance can respond to, and there will be trade disputes and geopolitical turmoil that will wreak havoc on our export markets. However, it is critical that the 2023 Farm Bill provide an economic safety net to address the challenges that will continue to be faced by our industry.

The NCC looks forward to working with the Committee and all commodity and farm organizations and other stakeholders to develop and pass a new farm bill that effectively addresses the needs of all commodities and all producers in all regions of the country.

Thank you for this opportunity, and I would be pleased to respond to any questions.

Exhibit 1. Costs of Production per Pound of Seed Cotton

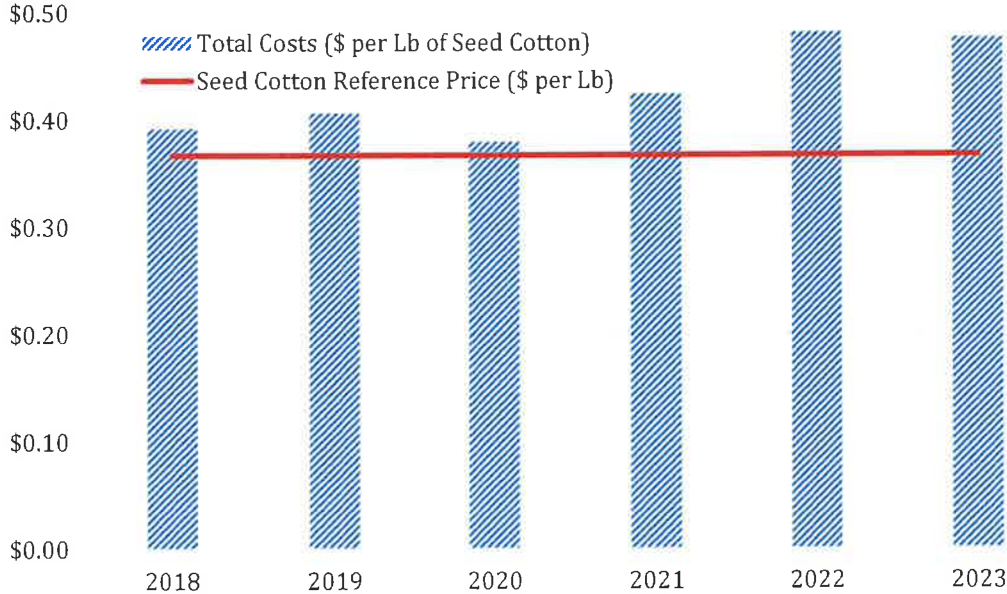

Exhibit 2. Structure of the Upland Cotton Marketing Loan Program
Farm Bill Recommendations Highlighted in Blue