Cleveland on Cotton: USDA Gives the Market a Small Gift

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By O.A. Cleveland, Consulting Economist, Cotton Expert

Big Report from USDA–USDA gave the cotton market a small gift with its April supply demand report. Estimates included higher consumption and lower carryover of U.S. stocks. Estimated world consumption was increased, world production was lowered, and world carryover was lowered.

The estimates were a sight for sore eyes as the market had spent the past month wishing and hoping USDA would finally adjust its numbers to industry estimates. The changes should be significant enough to bring speculative money back to the cotton market and providing the spark for more pricing opportunities.

The market continues to feel that more bullish adjustments to carryover stocks, both in the U.S. and the world, will be forthcoming. Thus, the bullish tone has returned to the market.

Traders are looking for more speculative interest. Both the May and July old crop futures contracts have returned to the low to mid 80’s. The new crop December has traded back to 82 cents, just 6 cents below its high. Expectations are that the 88-cent high will be challenged.

We will touch on the report’s key point at the conclusion of the newsletter.

Two factors have risen to the apex of traders ideas of market activity. Old crop ideas relate to just how much cotton will be required to maintain current Chinese spinning activity. China has an immediate need for imports to keep its spinning capacity at current levels. Not only must China build stocks for immediate use, they must also replenish its reserve stocks of imported cotton.

Essentially every single bale of U.S. high quality will get shipped to China in the coming months. As has been commented for months the demand for a combination of U.S., Brazilian, and Australian growths is paramount. With China starting a spitting contest with Australia, it enhances the need for not only U.S. and Brazilian, but also Indian, as well as limited amounts of other growths.

Plain and simple, the world’s largest spinning industry mush import cotton. The country cannot afford for its textile industry to slow down as the textile industry remains as the country’s major source of employment outside of production agriculture. The unabashed principal requirement in the country is to keep the population employed.

The other factor is the persistent drought spreading across the Plains of Texas and Oklahoma. Further the Texas Coastal Bend and South Texas crops are up and growing, but only with spotty stands. It is early, but yield potential is being seconded guessed.

China’s import needs stretch well into the worlds 2021-22 crops. Thus, the potential drought facing nearly half of the U.S. crop becomes more of an immediate market issue with each passing day. The "market deadline" for the Texas Plains crop is the traditional Memorial Day rains (May 30- June 1).

The rains always come, or do they? The million-dollar rains have become the billion-dollar rains. The new crop December contract is beginning to feel the upward price pressure of the expanding drought. With U.S. stocks falling, and the coming absence of high-quality cotton, the New York ICE contract is upward bound and will only be slowed by rumors of light sprinkles of Mother Nature's rain.

USDA made only two changes it its estimate of the U.S. cotton situation. It increased its estimate of U.S. cotton export sales to 15.75 million bales, up 250,000. Subsequently, it also lowered ending stocks for the 2020-21 marketing year to 3.9 million bales.

This is important in that the psychological trading view is overall much more price supportive when ending stocks are below 4.0 million bales, even if just barely so. Further, most analysts feel that stocks will be lowered 200,000 or more in the coming three months.

Changes in the world balance sheet were even more bullish: world production was lowered some 300,000 bales; world consumption was increased 400,000 bales; and world ending stocks were lowered 1.1 million bales.

Most likely the market had already faded some of these changes. Thus, the bullish impact of the report will likely be only 2-4 cents. The higher daily price increases just before the report's release were likely part of that price increase. Yet, as prices move higher the market will back and fill.

The most bullish point in the report was that USDA increased its estimate of world cotton trade almost one million bales. A key thought here, the least of which was an increase in Chinese imports. The real meaning is that this is very hard evidence that pent-up demand for cotton is just beginning. The estimate for world trade has increased over 1.5 million bales in the past 60 days. Demand…Demand…Demand.