Cleveland on Cotton: Prices "Stuck in Mud, but Good Mud"

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Headed into the U.S. three-day holiday weekend cotton prices are stuck in mud, but good mud. That is, if you must be stuck it is good to be mired in 81 cent muck as opposed to 60 cent muck. USDA's January supply demand report validated the market's run above 80 cents and made a case for prices to trade higher.

Yet, market fundamentals improved as much as they are, are still somewhat neutral at the current price level. Nevertheless, the technical chart pattern has shifted in favor of even higher prices and this continues to attract heavy speculative funds.

The market had faded the world supply demand report. As bullish as it was, it only generated some 100 points to the upside and by week's end that gain had generally eroded. Thus, the market is trading on either side of 81 cents as it preps for a test of our 83-cent target.

A longer-range target, not predicted however, is the 87-cent mark. This market may not be trading strictly fundamentals and may be trading the enormous money inflow that is coming to all commodity markets, with cotton getting its fair share.

Nevertheless, the road to higher prices is being led by two necessary signals, improved demand and declining world and U.S. stocks. Again, the initial target is 83 cents with a following target of 87 cents. However, it is time, now, to be at least 50% priced.

USDA estimated the U.S. crop at 15.0 million bales, down 1.0 million from the December report. Domestic consumption was lowered 100,000 bales to 2.4 million and exports were increased 250,000 bales, up to 15.25 million. Thus, U.S. ending stocks were lowered to 4.6 million bales, down an unbelievable 1.1 million bales from the prior month.

Yet, as reported, the market saw this coming and had already factored in the changes via market prices some two to three months ago, despite USDA being so late to realize the need for adjustments. U.S. consumption could later be lowered another 100,000 bales and esports could be raised another 200,000 bales. Thus, U.S. carryover stocks could drop as low as 4.0-4.2 million bales, a very bullish level.

USDA reduced world ending stocks to 96 million bales, down only 1.2 million bales. World consumption was increased only 100,000 bales to 115.7 million bales. However, the driving force behind mill consumption, China saw its estimated mill consumption increase by 500,000 bales. Owing to the one million bale drop in U.S. production, world production was reduced to 112.9 million, a one million bale drop.

The January world supply demand estimates can be viewed here.

Led by increased U.S. cotton exports world trade in cotton continues to expand. China has replaced Vietnam and Turkey as the principal market for U.S. cotton. This should be viewed as cyclical. However, if the U.S. holds its current position on agricultural trade then China could import nearly another five million bales of U.S. cotton in the coming season.

It all depends on whether the U.S. enforces its trade agreement with China. The Chinese support price for its cotton growers is near $1.50 cents per pound, substantially higher than the world price of cotton. Thus, it is far cheaper for Chinese mills to import U.S. cotton rather than buy on the local Chinese market.

Additionally, as we have discussed in length, the ever reaching world ban on slave/child labor produced Xinjiang cotton has moved China to import more cotton; cotton to be used for manufacturing cotton goods that will be exported to Europe and the U.S. The U.S. formally reemphasized its ban on such goods again this week.

New York ICE cotton prices are also receiving a boost from the overall commodity complex. As soybeans streak toward the upper teens and corn looks to move toward $5.50, cotton must advance to bid for planting acres in 2021. Cotton plantings are expected to reach 12 million acres as December futures push toward the upper 70's.

The failure to plant such acreage will only serve to push cotton prices higher as the 2021 harvest approaches. The market does not expect cotton carryover stocks to increase during either the 2020-21 or 2021-22 marketing seasons.

Growers are encouraged to price 20% of their intended 2021 production at 77 cents and to price an additional 30% at 80 cents.

With respect to the 2020 old crop, growers should price at least 50% of their crop at the current price level (81-83 cents) and then price an additional 10% on a 2-cent scale up basis (at every 2-cent interval). Remember, 80 cent cotton appears only about five percent of the time.