Cleveland On Cotton: Let's Talk (A Small) Profit

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USDA teased the bears this week with the release of its May world supply/demand report. This was the monthly report that included both the current-year estimates (2019-20) and USDA's first formal estimates of the upcoming season.

While the stats seemed bearish, trading has built some short-term bullishness in the price outlook, albeit probably short-lived.

At any rate, cotton traders are loving the market. As expected, the long-term forecast remains bearish while short-term price action created a price inversion (July trading higher than December). That reflects immediate demand for cotton relative to distant demand.

While world carryover was projected higher for both the 2019-20 season and even higher for 2020-21, the real key to USDA's estimates was the market's realization — for the first time in a number of years, China will not be holding the bulk of the world cotton carryover.

Such a phenomenon will make for a very competitive export market, even more so than in the past. Growers will not want to pay the cost of carrying cotton over into the following year(s).

Yet with low prices, the LDP/POP will be profitable. As commented in prior weeks, the 60-cent level will be near-impossible to penetrate for the new crop December futures contract.

The old crop July contract could ease up to 60 cents due to the price inversion. But, if so, it will be very short lived. After first notice day, prices could get a bit wild, but that is when only the bad boys are allowed to play.

Let's Talk Specifics

The USDA supply demand report lowered 2019-20 world consumption to 105 million bales, very much in line with expectations. Of course, this decrease was in line with world concerns about Covid-19 but also reflected the understanding that some textile operations have returned sooner than expected.

It was also reflective that much of the world's economy has not suffered as much as the U.S. economy. Most of the world did not "close for business" as the U.S. did.

World production for 2020-21 was projected at 119 million bales, down from the 2019/20 estimate of 123 million. World ending stocks for 2020-21 were placed at 99.4 million bales, up from 2019-20 of 97.2 million bales.

Pre-coronavirus, world ending carryover was estimated to be about 80 million bales.

Profit? Nothing Huge But Perhaps Real

China remains an active buyer of U.S. cotton. Net sales of Upland for the week ending May 7, totaled 238,100 bales with China taking 198,000 bales. Thus, non-China business has slowed substantially for now.

Weekly shipments were just below 250,000 bales. It has become apparent that carryover shipments into next year will be greater than usual. However, the current pace of shipments remains well on track to meet or exceed USDA's annual export estimate of 15.0 million bales.

The battle now is between ChinaTex and the big Memphis merchant as they battle on the board over the July contract. Likely, the Memphis merchant has major export requirements to both China and other Asian markets and will be likely to hold all market shorts accountable.

In the very short run, their actions also support December, but it will be minor and with a chance to move slightly above 59.50 cents, basis December.

As mentioned last week, 2020-21 grower marketing decisions will be tied to the CCC loan program and LDP. Most growers, if not all, should enjoy a profitable year, but revenue will be limited, with the focus on sound cotton production management practices. There will not be any fluff, but premium quality grades and staples will be rewarded.

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