

Cleveland on Cotton: Cotton Prices Improve, But Demand Remains Bearish

April 07, 2023

By Dr. O.A. Cleveland



Cotton prices surged higher going into the three-day weekend as the Easter holiday gave speculators reason to try the long side of the cotton market once again. In fact, all contracts out to March 2024 settled above 83 cents – a welcome relief not seen in recent weeks.

Speculators jumped on Saudi Arabian news that it would back a necessary portion of the International Monetary Fund's (IMF) 2019 package loan to help keep Pakistan afloat. The news gave some relief to technical chart patterns, suggesting the potential of a rally possibly up to 86-87 cents for old crop. However, that potential has existed for six months and has not moved to fruition.

More importantly, the 85-cent price resistance level has been a major barrier faced by prior attempts to move higher. Neither the technical nor the fundamental situation facing the 2023

new crop December contract has changed. Specifically, world carryover and world economic conditions have stifled demand.

Demand remains as the big bear facing the new crop. However, the ongoing U.S. drought has yet to be broken – and must – or the New York cotton contract will move significantly higher. It is noted that the infamous weatherman has promised that the drought will be broken. Breaking the drought could drag new crop prices down to the exceptionally low 70s. However, a continuation of the drought will generate a daily discussion of dollar cotton.

As discussed last month, the Pakistani government had only two months of hard currency with which to guarantee payments for imports, and that most would go for food. The Saudi guarantee was part of an IMF loan initially approved in 2019 and is now believed to be sufficient to keep the Pakistani economy afloat until at least June 2023.

The loan is especially important to the world cotton industry and to the U.S. cotton industry. The Pakistani textile industry consumes some 9-10 million bales annually. Their 2022 domestic crop was only 3.7 million bales, thus establishing the need to import 5 to 7 million bales (majority U.S. cotton).

Shipments across the globe to Pakistan have slowed because of the country's inability to pay for the cotton. In fact, shipments of one million bales of U.S. cotton, previously sold to Pakistan, are on hold because letters of credit cannot be opened. Pakistani mills continue to contract for new purchases, but shipment potential is very questionable.

Europe is facing its highest level of inflation since 2001. Interest rates continue to rise, and the consumer remains under severe financial pressure. It is exceedingly difficult to become bullish on cotton with the market trading under its 100-day and 200-day moving average.

Yes, my desire is to be bullish. But my economics tells me this market will only tease the bull. The bears will remain in control.

The only factor that can bull up this market is the supply side of the price equation. Demand is dead in the water. Hopefully, we can move more cotton to Pakistan. Hopefully, we can move more cotton to Turkey. Yet, both countries are behind the eight ball. More importantly, markets are not made of hope but rather from the fundamentals of supply and demand. Absent demand, the only hope is supply.

New crop has hope. Not so for old crop.

Old crop continues to face an increasing level of bearishness from the on-call sales versus on-call purchases, basis the May and July futures contract. On-call sales (grower selling) facing the May and July contracts are overwhelming. Growers will continue to lose the price game to storage and carrying cost.

I will say it for you: please make this guy be wrong.

The U.S. and the world must pay for the enormous government spending of 2021. Government does not create wealth, it destroys it. As Europe, the U.S., and the Western world move through this cycle, commodities will remain under pressure. The burden is left to be carried on the backs of commodities via very weak demand. The direction of old crop cotton prices is flat to lower. Mother Nature has total control of new crop prices.

Old crop prices: The 78-85 cent range continues.

New crop prices: Mother Nature, 70-100 cents.

Give a gift of cotton today.