Cleveland on Cotton: Small Market Rally Provides Second Chance to Price Cotton

March 31, 2023

By Dr. O.A. Cleveland

Two weeks of sub-80 cent cotton was enough foolishness. The market hit buy stops, thus generating a 5-6 cent short covering rally. The move was significant enough to run all the weak shorts out of the market. Yet, they are likely to again try to push prices lower.

Hopefully, the 78-79 cent price resistance level will be strong enough to hold them at bay.

The low prices of the prior two weeks brought out the mill buyers, as over half a million bales of U.S. cotton have been sold during the past two weeks and another 250,000 bales were likely sold this week. The old crop May and July contracts are facing resistance at the 85-cent level. Should that be penetrated, the old 88 cent price resistance sits like a lead cap on the market. Yet, that is more of a hope than anything else.

Growers have been given a second chance to fix the price of their cotton. Too many held cotton as it moved below 90 cents and still held on as the 81-82 cent support and then the 78-79 cent support levels were penetrated. Now, the return to 83 cents has presented them an excellent second chance to fix the price of their cotton.

Storage costs are eating up grower profits and, with each passing month, the market must move a cent higher just for growers to stay even. Even with the rally this week, the market offers less than the grower could have extracted from the market just three months ago. Thus, it is time to price old crop cotton.

I am not saying prices will not challenge the 88-cent level. It is possible, but such a rally is based on nothing other than hope. Along with the absence of fundamental support, speculators are absent to run prices higher. Another short covering rally, you say? Well, there are few shorts left in the market now. The 5-cent rally this week took them out. Prices will have to be pushed below 78 cents if the market is to generate another short covering rally.

The new crop December contract rode higher all week, point for point with the short covering rally. The rally did have friendly support in the export sales report. But again, just like the prior week, exports should have been strong as sales were tallied with fire sale prices. During the year, mills have generally been good buyers every time market prices fell below 82 cents and increased their buying on a scale down basis.

Mills still have considerable new buying/fixations to do, but this market is all but perfectly set up for them to “sit and wait.” There is little reason to jump on the price bandwagon, rather they will continue their scale down buying and scale down fixation strategy. Just as growers were rewarded in past years at the expense of mills, this year mills are being rewarded at the expense of growers.

USDA's March 31 planting intentions survey of cotton growers confirmed the planting bullishness of America's cotton growers. They want to plant cotton. They have faith in cotton. Cotton has delivered repeatedly and will continue to deliver. Their planting intentions are significant. The *Cotton Grower* survey conducted in December 2022 suggested plantings of 11.8 million acres. We doubted it. Everyone doubted it. USDA's survey conducted the first week in March estimated 12.1 million acres.

The principal reason that December futures is holding above 80 or 83 cents is because the drought continues in the Texas Plains – the location of about 55% of the U.S. acreage (Texas, Oklahoma, New Mexico). The weather forecasters, as a unanimous unit, contend the drought will end in the April/May period. If that is the case, or even it ends by mid-June, then the rain will make cotton, and U.S plantings of 12.1 million acres will yield 19 million bales, maybe 21 million…and the bottom will fall out of the market. Yet, the drought may not end. If that is the case, the New York cotton contract will again stare the dollar bill right in its face.

Thus, some market participants are looking at a 70-75 cent market while others are pontificating a December price of one dollar. The technical charts will signal the market's intent and, for now, the intent is for higher new crop prices.

Nevertheless, as has been stated many times, my thoughts continue to fall back on the disastrous economic situation in the U.S and much of the world. I see world inventories increasing and a December contract that trades between 88-90 cents on the top side and 72-75 cents on the low side. That range suggests that growers should price as much as 10% of their new crop at current prices.

Yet, it is difficult to price at 83 cents, basis December futures. However, if there is profit there, it should be done. However, do not lock in a loss before planting begins.

So why? Why am I not bullish on this market given the excellent export sales? I would love to be. Yet, the overriding factor is the amount of old crop grower cotton that has yet to be fixed: 2,141,100 bales. That is a massive amount this late in the season.

Weak demand, an extraordinarily strong dollar, high interest rates, and very uncertain world events are trouble for the cotton market. We can see some rallies, but there seems to be a trap in this market just waiting to be sprung.

Give a gift of cotton today.