PLEXUS Market Comments

Market Comments – October 01, 2020

NY futures closed the week slightly higher, as December added 45 points to close at 65.91 cents.

The cotton market is still devoid of any momentum, as December has settled the last eleven sessions in a very tight range of just 71 points, between 65.24 and 65.95 cents. The trade is still looking for a way out of its fixation bind, but speculators won't provide the necessary sell-side liquidity as long as the chart remains in bullish mode.

The CFTC spec/hedge report as of September 22 showed no big changes. This makes sense, because December didn't move much during the week of September 16-22, as it traded between 64.72 and 66.88 cents, which was nearly identical to this week's range of 64.70 to 66.60 cents.

Speculators reduced their net long by 0.06 million to 4.66 million bales, while Index funds cut their net long by just 0.03 million bales to 7.34 million bales. The trade was a light buyer, reducing its net short by 0.09 million to 12.0 million bales.

US export sales continued to impress, as they amounted to 273,900 running bales of Upland and Pima cotton for both marketing years. Once again we had broad participation with a total of 18 markets buying. Shipments were decent as well considering that we are in-between seasons, as 229,000 RB were exported to 21 destinations. For the current marketing year we now have commitments of 8.5 million statistical bales, of which 2.3 million bales have so far been shipped.

There is something amiss with the US beginning stocks number, which the USDA has at 7.25 million statistical bales as of August 1. When we look at open EWRs (electronic warehouse receipts), which this morning were at just under 3.0 million bales for 2019/20 and earlier crops, and we add back in what has been exported and used domestically since the beginning of August, plus we allow for some cotton in transit, then we come up with no more than 6.5 million statistical bales.

We therefore believe that shipments have been underreported by merchants and other entities, which is nothing new, and we expect there to be a downward revision of US stocks over the coming months.

There are also some question marks behind India's ending stocks, which the Textile Ministry's 'Committee on Cotton Production and Consumption' pegged at 10.54 million local bales at the end of September, or around 8.23 million statistical bales. If we add 4.0 to 4.25 million bales back in for an end of July comparison, we arrive at around 12.5 million statistical bales, which is still considerably less than the 17.86 million bales the USDA posted in its latest WASDE.

The US and India are two of the most important price setters in the international cotton market, and if stocks are not quite as depressing as traders thought, it might alleviate or at least delay price pressure as we head into the harvest period.

When we look at the US balance sheet, we may end up with beginning stocks of just 6.5 million and a crop of 16.75 million bales, which would give us a total supply of 23.25 million bales. If we then take off 2.5 million for domestic mill use and 8.5 million already sold for export, we would have 12.25 million bales left.

That's still a large number, but as the last two export sales reports have shown, we are now seeing broad-based interest in US cotton, whereas before it was basically just China and Vietnam who were buying. We have also noticed a pickup in yarn values, which may be why the current price level is finding greater acceptance.

However, it remains to be seen whether the current activity is simply a temporary boost ahead of the Christmas shopping season or whether it can be sustained past the holiday period. The recent flare up in Covid cases in many parts of the world, persistent layoffs and insolvencies, and the delay of more stimulus are pointing to a rough patch ahead for the global economy.

Crude oil has been weakening lately, lumber futures have dropped back to earth and copper prices took their biggest tumble since March today, down over 4%. With these important commodities rolling over, cotton traders should take notice!

So where do we go from here?

Although some consuming markets have seen a decent recovery, most of cotton's strength has no doubt come from spec and index fund buying. The trade hasn't helped matters by building this large unfixed on-call position, from which it is now trying to escape. For that to happen we need to see sell-side liquidity, which has been lacking so far.

However, it won't take much to trip the spec longs up, as the primary uptrend line is now above 65 cents, while the 50-day moving average sits not far below at 64.38 and the 200-day is at 62.87. In other words, we could easily get another washout like we saw three weeks ago and maybe this time China won't be there to catch the fall. With 3.38 million bales in unfixed on-call sales on December however, there is still a strong layer of support underneath the market.

The upside is only going to be in play if mills are forced to fix in an illiquid market, but there is still some time before that might happen. In the meantime the highest odds remain with a sideways market.

https://plexus-cotton.com