PLEXUS Market Comments

Market Comments – November 05, 2020

NY futures ended the week basically unchanged, as December closed just 25 points higher at 70.07 cents.

December traded to a low of 68.06 cents on Monday on spec profit taking, dropping from a high of 72.60 cents in just four sessions. However, it managed to hold above its long-term uptrend line and then rebounded back to the 70 cents level, where it seems to have found its equilibrium for now.

The buoyant stock market certainly helped, as the Nasdaq gained about 10% this week and is once again closing in on its all-time high, with the S&P500 and Dow Jones following not far behind. This exuberant mood is the result of the Fed's renewed promise to support the economy with all its monetary might and an elections outcome that is seen as benign for financial markets, with a Republican controlled Senate expected to fulfil a 'checks and balances' role.

However, the market's election narrative may be jumping the gun, because Republican control of the Senate is far from being certain at this point. The two Senate races in Georgia might both be headed into a January 5th runoff, and if the Democrats were to win these two seats, then the new Senate would be at a 50-50 tie, with the presumed VP Kamala Harris being the tie-breaker.

In other words, there is still a lot of uncertainty regarding the balance of power, but markets seem to have already made up their minds, which could backfire. At the very least we might have to deal with another two months of uncertainly until the remaining two Senate races are decided.

The CFTC spec/hedge report showed that before the market started its deep correction, speculators and index funds were adding more longs. During the week of October 21-27, when December traded between 7057 and 7253, speculators added 0.30 million bales to increase their net long to 7.41 million bales, while the index fund net long grew by 0.06 million bales to 7.87 million bales.

The trade was on the other side and increased its net short by a corresponding 0.36 million to 15.28 million bales. This was the trade's largest net short since August 2018. When the market approached 73 cents on October 28, the trade was on the brink of being forced into a short-covering rally, but so far its stubbornness to stay short seems to pay off. The drop back to the 68 cents level has allowed trade shorts to reduce their exposure, which is reflected by today's on-call report.

The CFTC on-call report showed that as of last Friday there were just 2.07 million bales in on-call sales outstanding on December, while unfixed on-call purchases were a million less at 1.07 million bales. These numbers have come down further this week and most of the remainder will likely disappear during the upcoming Goldman Roll, which takes place over the coming five sessions. In other words, we feel that the trade short position no longer has explosive potential, at least as far as the December delivery is concerned. What happens further down the road remains to be seen.

US export sales came in slightly below expectations at 188,100 running bales for both marketing years, but remained above the pace needed to make the current USDA estimate of 14.6 million bales. Participation was still good with 18 markets buying, while shipments of 291,900 RB to 23 destinations were also respectable.

There were again a number of cancellations totalling 119,700 RB, but we don’t see this as a big deal, because the market is near its highest level in 18 months, so there is probably no money owed to shippers. It may actually have been shippers who initiated the buy-backs for a lack of suitable cotton.

Total commitments for the current season are now at slightly above 9.5 million statistical bales, whereof 3.45 million bales have so far been exported. Shipments are still running nearly 0.8 million statistical bales ahead of last season!

The US crop size continues to shrink according to private estimates, which have the US crop at just around 16.0 million bales. Reports from West Texas indicate that the freezing rain of last week has caused both quality and yield losses, as immature bolls won’t open, while many open bolls were stringing out. It will be a while until we know the full impact of this unusual winter storm.

So where do we go from here?

The recent correction has alleviated ‘overbought’ conditions and the fact the we held above critical support will probably keep most speculators on board as we head into the roll period and it may even bring in some new buying.

The trade finally got the price break it was hoping for, which allowed it to reduce its December exposure to a more manageable level. The upcoming roll period should provide the trade with the necessary liquidity to square away most of the remaining Dec positions.

With a delayed US crop getting smaller and with Chinese domestic prices still hovering at around 98 cents, we don’t see much market pressure ahead in the near term. At the same time we see no reason for prices to take off either, since the renewed economic slowdown due to escalating COVID cases is likely to slow demand. In other words, we don’t expect the market to make any big moves in the near term.

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