PLEXUS Market Comments

Market Comments – May 13, 2021

NY futures cratered this week, with July falling 560 points to close at 84.98 cents, while December dropped 342 points to settle at 83.30 cents.

After July had managed to gain over 1200 points between April 5 and 27, it has since given back more than half of this advance and is now trying to regain its footing.

Basis pressure from competing origins, notably Australia, combined with some profit-taking in several commodities, including soybeans and grains, contributed to the weakness in cotton. Today's sharp drop looked like a washout of recently established spec longs after support levels were breached.

Wednesday's WASDE report, which provided us with a detailed look at the 2021/22 season, failed to stimulate the market, since the numbers came in near the consensus view. A sanguine outlook for the US was offset by a slightly bearish global picture, with ROW ending stocks expected to hold near current levels.

The USDA chose a middle-of-the-road approach with its 17.0 million bale estimate for the US crop, which most traders feel is on the optimistic side considering that West Texas is still dealing with drought conditions and some acreage has been lost to corn and soybeans in the

Southeast and Midsouth. In other words, a lot needs to go right over the coming months to achieve that target.

Even with a 17 million bale crop we are looking at the lowest supply figure in six years at 20.3 million bales. In the previous five seasons we had US supply between 20.98 and 24.77 million bales.

Thanks to strong exports of 16.25 million bales this season, US ending stocks are now pegged at no more than 3.3 million bales at the end of July, while next season's remaining inventory is estimated at just 3.1 million bales, despite a 2.4 million bale bigger crop and 1.55 million fewer exports.

Global numbers are a different story, as world production of 119.44 million bales is up 6.33 million from this season, while global mill use is estimated at 121.61 million bales, up 4.06 million from the current season. The relatively small production gap of 2.17 million bales is not enough to cause any concerns, especially since ROW stocks are expected to remain basically unchanged, since Chinese imports are down 1.5 million bales.

ROW ending stocks are estimated at 54.44 million bales, down slightly from 54.56 million this season. The peak was reached two seasons ago, when we had 60.92 million bales, but before that ROW ending stocks never amounted to more than 44.35 million bales. In other words, there is still enough cotton around the globe, it's just not evenly distributed, with the US basically sold out, while others still have plenty.

US export sales were decent last week at 130,500 running bales of Upland and Pima cotton for both marketing years, with 16 markets participating and 23 destinations receiving shipments of 296,500 running bales. For the current marketing year we now have 16.45 million statistical bales sold, whereof 12.5 million bales have so far been exported.

When we look at the current US balance sheet, we have total supply at 21.85 million statistical bales, of which 16.45 million bales have been sold for export and 2.3 million will be consumed domestically by the end of July. This leaves 3.1 million bales, but from that we need to reserve around 1.3 million bales out of 1.85 million bales in 2021/22 export commitments and 0.6 million bales are being consumed by domestic mill use in the August to October period. In other words, we believe that just a little over a million bales are left unspoken for at this point.

Unfixed on-call sales actually grew larger last week, with unfixed sales on July going up 0.3 million to 3.33 million bales, while the overall number increased by 0.58 million to 11.13 million bales. On the purchase side we have 0.56 million open on July and 4.79 million bales overall. It will be interesting to see how these unfixed Julys play out over the coming 4-5 weeks. We still feel it is dangerous to hitch the price of physical cotton, especially that of foreign growths, to a volatile US futures market that might take on a life of its own.

So where do we go from here?

With such a tight US balance sheet and all the uncertainty surrounding US new crop it is difficult to see the market trade much lower at this point. For that to happen we will need to see a decent crop in the field and we are still several months away from that.

If anything were to go wrong in Texas and/or we see more acres shifting away from cotton in other parts of the country, it could ignite the market. There is a reason why out-of-the-money call options remain so expensive, even after this week's drop.

The tight US vs. ample global situation has put pressure on the selling basis and we expect this to continue as long as US new crop remains in limbo. This season the US was able to take the lead in the export race, but next season we might see it back in a residual supplier role.

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