PLEXUS Market Comments

MARKET COMMENTS – OCTOBER 21, 2021

NY futures ended another zigzag week slightly lower, as December gave up 96 points to close at 106.14 cents. The Dec/March inversion dropped from 215 to 199 points.

When the market broke out of a corrective flag pattern yesterday, it looked like the bulls were once again up and running, but today's reversal quickly dashed their hopes. This week's trading range for December narrowed to 610 points, from 105.25 to 111.35 cents.

The average daily trading volume dropped to just 34k contracts, which compares to 46k the week before, signaling that the market is losing some momentum. Open interest hardly changed over the last five sessions, as we started today's session with 285.2k contracts, or just 0.7k less than a week ago.

Since prices started to take off on September 20, open interest has gone up from 272.7k contracts to the current 285.2k contracts, as spec longs and trade shorts have been digging in and there is still no sign of either side wavering.

It is therefore no surprise that the CFTC on-call report showed not much progress in getting fixations out of the way, even though December had dropped to a low of 103.50 last week. As of last Friday there were still 3.34 million bales in unfixed sales on December, down just 0.18 million bales from the week before, while the total amount of unfixed on-call sales rose by 0.85 to 15.95 million bales.

On-call purchases on December saw a decline of 0.15 to 1.09 million bales, but increased by 0.41 to 4.36 million bales overall. The difference between total on-call sales and purchases now amounts to 11.59 million bales.

What these numbers are telling us is that mills are apparently not too concerned about prices running away to the upside, otherwise they would have been more proactive during last week's price break. While mills are securing cotton in view of all these supply-chain disruptions, they are not yet prepared to fix prices that would translate to over 120 cents landed Far East today.

However, mills are playing a dangerous game with their procrastination on fixations, because sooner or later they will be forced into action. As explained last week, unlike speculators, who can sit on their hands and roll their net long down the calendar, while picking up some roll gains along the way, mills don't have that luxury. They still have to fix nearly nine million bales by the middle of February, between the 3.34 million bales on December and the 5.43 million bales on March.

US export sales didn't disappoint this morning, as a total of 479,900 running bales of Upland and Pima were sold for both marketing years combined, which was the 2nd highest amount this season. There were 17 markets buying, with China taking about 2/3rds of the total. Shipments continued to lag due to a lack of available supplies, as just 122,800 running bales were exported to 20 destinations.

For the current season we now have commitments of 8.5 million statistical bales, of which 2.0 million bales have so far been shipped. By comparison, last year we had 9.1 million bales in commitments and 2.9 million bales exported.

China accounts for around 2.45 million statistical bales of these US sales, of which just a little over 0.42 million bales have so far been shipped. This lags considerably behind last year's 3.42 million bales in commitments and 1.32 million bales shipped.

However, China seems to be catching up quickly, as more business took place this week, which was one of the reasons behind the market's mid-week bounce. It makes sense that China would import more cotton, because not only had the Reserve to release more stocks than originally planned to tie mills over to new crop, but there is also a huge price incentive to chase after foreign cotton.

Chinese futures closed the week slightly higher, with the January contract settling at around 152 cents, while the CC-Index stood at around 157 cents, which means that the premium to NY futures is still a massive 46-51 cents, or around 15 cents more than two month ago.

This means that we should expect the Reserve to be there to load up on US cotton and other foreign growths on dips. Likewise there should be continuous strong demand for yarn and fabric imports by Chinese mills, which are not subject to quotas like raw cotton.

So where do we go from here?

Not much has changed since last week, as neither the large spec and index fund long nor the sizeable trade short have been willing to reduce their exposure. The latest CFTC report still showed a big 19 million bale net position on both sides. The question is who will blink first?

With only three weeks to go until December options expiration, mills have their work cut out to reduce their still large unfixed on-call position in December and this could generate buying pressure.

Speculators are so far unfazed by these pullbacks and if they continued to hang on to their longs, it could cause a problem for trade shorts who need to buy out. With Chinese buyers also ready to jump in on breaks, it is difficult to construct a bearish case at the moment.

For that to happen we would need a ‘risk off’ event that prompts speculators to liquidate. Not inconceivable, but unlikely at this point!

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