PLEXUS Market Comments

Market Comments – June 27, 2019

NY futures ended the week little changed, as December edged up just 13 points to close at 66.09 cents.

As expected we saw December moving sideways and it has now settled the last 33 sessions in a narrow band of just 343 points, between 65.04 and 68.47 cents. Market participation continues to drop, as overall open interest amounted to just 176,283 contracts this morning, which is the lowest level since November 2015.

The latest CFTC report as of June 18 showed no improvement in the trade's hedge position, as it grew by just 0.02 million bales net to 3.01 million bales. Last season the trade, which is comprised of growers, merchants and mills, was 18.25 million bales net short at the same date. In other words, the trade remains extremely under-hedged and this has been keeping a lid on rallies.

Meanwhile speculators bought 0.18 million bales net during the week of June 12-18 and thereby reduced their net short slightly to 3.87 million bales, whereas Index funds sold 0.16 million bales to trim their net long to 6.88 million bales.

The CFTC report showed that the stalemate continues, as both the speculators and the trade are net short in the futures market, while index funds are holding a net long position. The trade needs to get a lot more short, but that requires speculators to buy the market. We therefore need to be on the lookout for potential triggers that might get the specs to reverse their position.

The G20-meeting, which is going to be held in Osaka over the coming two days is holding some promise, since the US and China have started to talk again and the meeting between Presidents Trump and Xi Jinping could lead to some progress on the trade front. A positive outcome would provide a boost to commodity markets and might spark some profit-taking by speculators.

Tomorrow's USDA Planted Acreage report could also provoke a market reaction. In March prospective plantings were estimated at 13.78 million acres, which was a lot lower than the NCC's 14.45 million acres. So the question is from what base should we start to discount the acres that weren't planted due to all this wet and cold spring weather? Based on field reports we feel that in Texas/Oklahoma/Kansas about 15-20% of the intentions didn't materialize, while in the Midsouth and Southeast it was probably just 5%.

However, while some acres didn't make it, the acreage that did get planted will have plenty of moisture available to produce above average yields, especially since summer has finally arrived. The twelve-month period from June 2018 to May 2019 was the wettest on record in the US and when we look at the current drought monitor, there are only 10% experiencing some moderate drought conditions. We therefore believe that despite all the early struggles this US crop had, the potential to produce 22 million bales is still there.

US export sales remained slow last week, as just 130,100 running bales of Upland and Pima cotton were sold for all three marketing years combined. At least cancellations of just 6,000 bales weren't too bad compared to last week. There were still 18 markets buying, while 25 destinations received shipments of 339,700 running bales.

Considering that unsold US supplies are limited (unless more cancellations were to free up additional bales) and with new crop is behind schedule, we feel that this export sales report wasn't all that bad. For the current season total sales are now at 16.3 million statistical bales, of which 12.2 million bales have so far been exported. For the coming season there are so far 4.2 million statistical bales on the books.

One development worth mentioning is that gold has broken above US$ 1,400/oz last week, which represents a 5-year high. To us gold is like the ‘canary in the coal mine’, warning of potential changes or problems on the monetary front. There are indeed some worrisome developments, namely that we now have US$ 12.7 trillion in sovereign bonds around the globe yielding negative interest, with the ECB and the Fed signalling to markets that they will reduce rates even more.

Supplying the world with cheap money will only serve to inflate asset bubbles even more. Last week all-time highs were reached by the S&P 500, sovereign bonds, corporate bonds, junk bonds and real estate, which means that while inflation may still be somewhat contained when it comes to consumer prices, it is certainly alive and well in asset bubbles. Commodities have so far been left behind, but we believe that against this monetary backdrop speculators are increasingly feeling uneasy to run short commodity positions.

So where do we go from here?

By and large the market is still stuck in a 400-point trading range, as growers are unwilling to sell the market below 6500, but are waiting for rallies towards 70 cents to do so. Speculators are still holding a sizeable net short position, but the loss of downside momentum and/or one of the potential triggers mentioned above could spark some spec short-covering and new buying.

Tomorrow’s acreage report and the G20-meeting will probably decide the market’s next move, but we feel that it will take a lot of new momentum (=strong spec buying) to get through all the trade selling that’s waiting on the way up.

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