PLEXUS Market Comments

MARKET COMMENTS – OCTOBER 28, 2021

NY futures rocketed higher this week, as December gained 759 points to close at 113.73 cents. The Dec/March inversion narrowed slightly from 199 points to 190 points.

After the surprising selloff last Thursday, which saw December trade to a low of 105.88 cents, the bulls regained control of the market this week. The triangle formation on the chart alerted us to an impending breakout, and as in most cases, it occurred in the direction of the prevailing trend, which is up.

Today's move propelled December to a new contract high settlement of 113.73 cents, while the October 8 intraday high of 116.48 cents still stands for now. After a marked drop in daily volume and momentum over the last couple of weeks, the last two sessions brought renewed vigor to the market, with today's volume reaching 49k in futures.

Open interest continued to hold steady, as we started today's session with 286.7k contracts, which compares to 285.2k last week and 284.6k two weeks ago. There has been some rolling of positions, as December open interest dropped from 120.1k to 104.3k over the last two weeks, which will intensify as we head into the index fund roll period.

Chinese futures continue to provide a vacuum into which NY futures are able to rise. With the US arb session finishing at 21,730 yuan/ton today, which equates to 154 cents, there is still plenty of room for arbitraging these two futures contracts. The current 40 cents difference compares to a 26-33 cents spread before this bull run began in September.

US export sales were once again meeting high expectations, as a total of 389,300 running bales of Upland and Pima cotton were sold for both marketing years combined. China accounted for 53% of the total and Turkey for 38%, while the other 15 markets shared the remaining 8%. Shipments were still slow, as just 65,600 running bales went to 18 destinations, but that's actually more bullish than bearish, because it is a reflection of the empty supply pipeline.

For the current season we now have commitments of 8.9 million statistical bales, whereof just 2.05 million have been exported so far. This compares to 9.4 million in sales and 3.15 million in shipments a year ago.

What comes to mind when we look at the latest CFTC on-call report is the old adage "when you find yourself in a hole, stop digging!". As of last Friday there were still 3.14 million bales in unfixed sales on December, down a minimal 0.25 million bales from the week before, while March added 0.06 million and now has 5.48 million bales still to fix.

Total unfixed on-call sales rose by 0.12 million to 16.08 million bales and the difference between unfixed sales and purchases increased to a worrisome 11.60 million bales. This provides plenty of punch to keep this bullish party going!

While spec longs liquidated around 1.79 million bales net in the last two CFTC spec/hedge reports, with new trade longs and trade short-covering on the other side, this week's breakout has probably put a stop to further spec selling and we also had some new longs come in from the sidelines as the rising open interest shows.

This puts trade shorts - particularly mills - into a dangerous situation, because they have only 2-3 weeks left to square away their unfixed Dec on-call position. This creates buying pressure in a market that suddenly doesn't have a lot of willing sellers anymore.

Spec longs like the current price action and there are not a lot of traders willing to short this unpredictable market. Or as a famous trader recently stated about shorting hot markets: *"I don't like putting campfires out with my face".*

So where do we go from here?

When we look at the recent chart action, we see a steep rise of 2753 points between the September 20 low and the October 8 high, which was followed by an almost perfect 50% percent retracement when the market corrected to 103.50 cents on October 13.

From there December traded sideways into a pennant or triangle, from which it broke out over the last two days.

When we look at the textbook definition of a 'bullish pennant', it states the following: *"It is a continuation pattern that marks a pause in the movement of a price halfway through a strong uptrend, giving us an opportunity to go long and profit from the rest of the price rise. The uptrend then continues with another similar-sized rise in price"*.

With mills having to fix/buy the market, with China still an active buyer thanks to the large spread between international and Chinese prices, and with fundamentals not offering a compelling reason to go short at this point, we believe that the path of least resistance is higher, potentially quite a bit higher.

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