PLEXUS Market Comments

Market Comments – April 22, 2021

NY futures closed mixed this week, as July dropped 21 points to close at 86.05 cents, while December added 67 points to close at 83.75 cents.

After gaining nearly seven cents in just nine sessions, July has been consolidating in a sideways pattern over the last five sessions, with settlement prices ranging from 84.71 to 86.23 cents.

Meanwhile December has been pushing higher as the uncertainty regarding new crop keeps short sellers at bay. Since posting a low of 75.34 cents four weeks ago, December has been on a steady climb higher, gaining 841 points in the process and closing today within four cents of its February 24 settlement high of 87.66 cents.

The situation in West Texas remains dire, as there is still no rain in the forecast. As if the weather wasn't enough to worry about, farmers are also facing much higher input costs this season, as energy and fertilizer prices have gone up sharply. Therefore, unless there is soaking rain soon we could see acreage drop dramatically, including irrigated acres. Some growers fear that we might end up with a similar situation like in 2011, which was the driest year on record that saw only 3.5 million bales produced in Texas.

Soybean and corn prices scored a big assist for cotton this week, as they raced to new contract highs, with July corn closing today at 6.31 dollars/bushel, while July soybeans reached 15.14 dollars/bushel. With November soybeans closing at 13.38 dollars/bushel, December cotton needs to keep pace if it wants to avoid a big shift in acreage. Corn and soybeans have lower input costs per acre than cotton, which apart from these stellar prices is another incentive for growers to opt for food crops this season.

US exports sales came in about as expected last week, as 152,600 running bales of Upland and Pima cotton were sold for both marketing years. Participation remained active with 15 markets buying, while 21 destinations received shipments of 348,600 running bales.

Total commitments for the current season have now reached 16.25 million statistical bales, whereof 11.3 million bales have so far been exported. New crop sales are at just over 1.7 million statistical bales so far. There are still 15 weeks left in the current marketing year and shipments need to average only around 283k running bales in order to reach the USDA export estimate of 15.75 million statistical bales.

Unfixed on-call sales remain a strong element of support for current crop futures, as mills once again failed to make much progress with their fixations. As of last Friday there were still 0.32 million bales in unfixed sales open on May, whereas July had 3.10 million bales to fix. The combined 3.42 million bales were down just 0.21 million bales from the week before. Unfixed on-call purchases on May and July amounted to 0.63 million bales.

While NY futures have been moving higher, yarn prices have stalled and are trending slightly lower, which in turn has been weighing on the basis of physical cotton. Since the tight statistical situation in the US is at odds with a more ample global supply scenario, we question whether mills should continue to buy so much of their requirements "on-call", especially in light of the uncertain outlook for West Texas.

It doesn’t make much sense to us to hitch the procurement price to a potentially explosive US futures market. At the moment there are still 9.56 million bales in unfixed on-call sales dependent on where futures prices take them over the coming months. They’d better pray for rain in West Texas or at least buy some upside protection!

So where do we go from here?

NY futures are currently on hold, waiting to see how much cotton makes it out of the ground over the next 6-7 weeks. If it rains and we get a decent amount of acres planted, then the market will likely back off a little. But if the drought continues and we are suddenly looking at a 13-14 million bale crop only, then watch out!

With the July/Dec inversion still at around 230 points, shippers will try to clean out remaining inventories, which should drop ending stocks to near sold out levels. This in turn puts all the more emphasis on a successful new crop campaign. In other words, there is no room for error in the US and the options market knows it. That’s why the December one-dollar calls are still worth around 270 points today!

Competing crops, the US dollar and inflation expectations are all playing a role in this as well and at this point they are still acting in support of higher cotton prices. However, the seemingly never-ending pandemic has us a bit nervous and we need to be prepared for mood swings in the financial markets in case the situation worsens.

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