PLEXUS Market Comments

Market Comments – August 29, 2019

NY futures closed the week basically unchanged, as December inched up just 6 points to close at 59.00 cents.

It was a volatile week, but in the end the market didn't go anywhere. December has now settled the last 20 sessions in a range of just 231 points, between 57.82 and 60.13 cents, and today is closed right in the middle of this range.

Trump's Twitter tirade last Friday sent the market tumbling, with the spot month falling to its lowest level since March 2016 when it traded at 56.59 cents on Sunday night. However, after a more conciliatory tone emerged on Monday, the market started to rebound, with December reaching a high of 59.49 cents by Tuesday.

This erratic price action formed a bullish "hammer" pattern on the candlestick chart, which was confirmed by higher settlement prices in subsequent sessions. Speculators, especially the ones relying on pattern recognition, seemed to react to this candlestick signal and were probably sponsoring the market's bounce.

By mid-week the market's focus started to shift from twitterstorm 'Donald' to hurricane 'Dorian', which is currently headed for the Florida coast as a major strength 3 or 4 hurricane. After making landfall in Florida on Monday, the system is currently expected to turn north into Georgia and the Carolinas, which could bring copious amounts of rain to cotton fields in the Southeast.

As of last Sunday Georgia had 30 percent of its bolls opening, while for Alabama it was 29 percent, South Carolina 24 percent and North Carolina 15 percent. By the time the storm is going to arrive next week, these numbers will have to gone up by another 5-10 percentage points.

Some areas of the Southeast have already been dealing with boll rot and if this storm brings as much rain as advertised, it will inevitably lead to further yield and quality losses. Southeast growers simply can't seem to catch a break from these impactful storms that hit the area year after year.

The latest CFTC report showed that speculators continued to be net buyers for a second week, while the trade expanded its net short position. As of August 20 speculators were 4.66 million bales net short (down 0.23 million), while the trade was 1.25 million net short (up 0.53 million). Index funds were still the sole net long in the market with 5.91 million bales (up 0.30 million). However, as pointed out before, outright long and short positions within these groups remain quite large and therefore contain a lot of potential buying and selling power.

US export sales came in at 174,100 running bales net for both marketing years, which wasn't bad considering that traders are still expecting to see large cancellations out of China one of these days. Shipments slowed considerably to just 177,200 running bales. For the current season we now have commitments of around 8.45 million statistical bales, of which a little over 0.9 million bales have so far been exported. For the 2020/21-season there are already 0.5 million bales on the books.

Traders are starting to get frustrated with this market, because it doesn't look like it is going to be able to break out of this narrow range anytime soon. The US loan seems to provide decent support at around 57 cents, at least until the crop has moved in. The upside is still limited by a slowing global economy and rising ending stocks, with private estimates expecting US ending stocks to potentially exceed 9 million bales by the end of this season.

Narrow, boring trading ranges are nothing new in the cotton market, we just try to forget them. Between February 2005 and June 2007 the market was locked into a 46-58 cents range for nearly 30 months and from July 2014 to August 2016 the market was in a 56-70 cents range for over two years. We are afraid that we might be in for another long stretch like that, since the market needs to digest excess stocks and this could take a year or longer.

So where do we go from here?

Despite the market's wild gyrations we haven't gone anywhere, as December has now closed the last four Thursdays within a 68-point range, between 58.94 and 59.62 cents. This is not likely to change anytime soon, as the US loan continues to provide support at around 57 cents, while a move to the upside would have to overcome massive grower selling.

For the market to take off we would need to see a reversal of the spec net short position to a sizeable net long, but at the moment there is no reason for speculators to do so. And even if they were buying several million bales net for some reason, the trade would likely be there to assume these short positions, unless there was a fundamental reason for the trade to move to the sidelines.

Hurricane Dorian might cause some excitement over the coming sessions, but even if it were to affect crops in the Southeast, we don't see this changing the overall bearish scenario. In other words, we believe that the market will remain stuck in a trading range between 57 and 62 cents in the foreseeable future.

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