ROSE ON COTTON – CORONAVIRUS HAMMERS MARKETS, ICE COTTON SUFFERS GREATEST CASUALTY AMONG AGS

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It was an unmercifully ugly week for ICE cotton. The May contract gapped 90 points lower on last Sunday evening's opening bell and it just got worse from there. May ultimately gave up 751 points on the week, finishing at 61.49. Dec lost 721 at 62.44. Still, the May – July spread strengthened a bit at (78), which is significantly short of full carry. Our proprietary model, which has produced cumulative weekly gains of 1582 points over the previous 52 weeks, predicted a settlement for Mar that was to be near unchanged to higher Vs the previous Friday's finish, which proved to be woefully incorrect, making this column a chore to pen this week.

ICE cotton moved lower on a rise in coronavirus infections outside of China and the realization of "community spread" within the US. The market effectively ignored all other news. Cotton crashed with worldwide equity markets, which were also roiled last week.

Novelty is the feature of the Wuhan (COVID-19) virus that is the most vexing. While we are certainly not attempting to downplay the severity of the current epidemic (which may soon officially be termed a pandemic) deaths caused by common flu strains, both domestically and internationally, will almost certainly be factors of magnitude higher than those ultimately attributable to COVID-19. But flu season has never had such a negative effect on markets. Given these facts, coupled with evidence that markets strongly overreact to occurrences such as COVID-19, we believe the break in the cotton (and other) markets is overdone.

In fact, the market has divorced itself from fundamentals. Fundamentals were not bullish per se, but there is/has been notable demand for US cotton. China is making purchases for its strategic reserve, the Australian crop is short, 2020 US production is very uncertain, and a better and better case is being made for lower planted area Vs the average forecast of USDA and NCC of 12.75M acres. Further, mill fixation and new sales of US cotton could still provide formidable support. Additionally, multiple new trade deals are now in force.

On the production side, most of The Belt is expected to see more rain and showers this week, with the southeastern US expected to see rather heavy accumulations. At the time of this writing, strong storms are moving across the Mid-south.

US net export sales and shipments against 2019/20 were off, but remained strong, for the week ending Feb 20 Vs the previous sales period at around 243K and 342K running bales (RBs), respectively. The US is 88% committed and 42% shipped Vs the USDA's export projection. Sales were again well ahead of the average weekly pace required to meet the USDA's 16.5M bale export target while shipments were approximately 85% of the pace requirement. Sales against 2020/21 were higher at 199K RBs; total gross new sales were nearly 500K RBs. Sales cancellations were significant at almost 43K RBs and were mostly attributable to China.

Internationally, we understand that Pakistan's textile mills are operating at full capacity, with import duties now removed and with increased demand from the slowing of China's textile sector amid the current viral epidemic. Increased consumption and lower to no export duties by Pakistan and Turkey should offer some fundamental demand support for our market.

For the week ending Feb 25, the trade reduced its aggregate futures only net short position against all active contracts to around 8M bales while large speculators trimmed their aggregate net long position to approximately 2.9M bales. However, we expect the trade has reduced its net short position significantly, at least, while also thinking that the spec sector (less index funds) has plausibly taken their net long position to near flat. The latest data suggest that business for US cotton continues to be conducted.

For an in-depth analysis of CFCT data see our weekly CFTC analysis and commentary.

We have sympathy for producers holding old crop cotton. Before COVID-19 effectively killed the May contract at the 70-cent level, there was substantial spot volume offered against a 72-75 cent market. We have seen very little panic selling from producers as most have more sense than to try to catch a falling knife.

We do expect a recovery and given the (in our opinion) dramatic overreaction to the news of COVID-19, we won't be surprised to see a dramatic recovery (if or when) the progress of the virus is stopped or at least stabilized. There are promising reports from several labs in several countries of advances in our understanding of the virus and the likelihood of a vaccine by year's end. If these reports prove justified, we won't be surprised to see futures recover most of the losses seen in the past 2 weeks. In the meantime, however, we think producers with old crop need understanding bankers and a good supply of their favorite stress reducing substance.

We don't see any reason to price new crop at current levels. While there is still risk to the downside, we believe there is much more potential to the upside, and given the uncertainties associated with COVID-19, US elections, flooding along the Mississippi and in the Southeast, etc., we believe pricing opportunities are likely in the next few months.

For this week, the standard weekly technical analysis for and money flow into the Mar contract are bearish, with the market in a significantly oversold condition. Overall, we think ICE futures are likely to continue to find strong support below the current market. Given the 70-point gap (68.30 – 69.00) above the current market, we think there is strong potential for a near-term rally.

Have a great week!

Report Courtesy: Rose Commodity Group

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