ROSE ON COTTON – COTTON MARKET MOVES LOWER ON WASDE WEEK; PRICES REMAIN WELL NORTH OF $1

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The ICE Dec cotton contract gave up 327 points last week, finishing at 107.33, with the Dec – Mar spread inversion contracting to 233. The cotton market failed to challenge the previous intraweek high, which was northward of 116. Last weekend our models predicted a finish on the week that was to be near unchanged to higher Vs the previous Friday's settlement, which proved to be incorrect. Still, we did not recommend trading any bias due to the release of the Oct WASDE report on Tuesday.

Futures moved lower despite significantly lower projected domestic carryout and rains across The Belt, on noticeable price demand rationing, USDA's sizeable debit to its aggregate world consumption forecast (which we believe is overdue) and a modest strengthening of US currency. Continued inflation concerns amid supply chain bottlenecking likely affected USDA's decision making with respect to its world consumption projection.

In its Oct WASDE report, the USDA projected 2021/22 domestic carryout 500K bales lower Vs Sept at 3.2M bales.

The adjustment came on a lowering of the estimate of yield across Texas that reduced the production projection to 18M bales. This was no surprise, and we have long advised against being bullish on production for a late-sown crop. USDA continues to officially hold 2020/21 exports at more than 16.35M bales, despite USDA-FAS only reporting 16.03M bales were shipped for the previous marketing year. We will be speaking with USDA analysts this week regarding this matter.

Aggregate world carryout for 2021/22 was projected 450K bales higher Vs Sept, which was not generally expected, at 87.13M bales. Production was estimated 690K bales higher Vs Sept and consumption 740K lower at 123.4. It seems that USDA is finally factoring in higher cotton prices, overall inflation, and IMF slashing of its estimate of world and US GDP growth.

One thing is now painfully clear – China is completely at the heart of the market's run. That is, business outside of China has fallen off as China purchases cotton for its reserve and domestic industry. The world's pushback on cotton from Xinjiang and China's ban on Aussie imports has significantly raised the projection of domestic carryout in China. Pain for China is increased as Xinjiang produces the lion's share of the country's machine harvested cotton. Overall, the aggregate world S&D balance sheet is not bullish at all. However, projected carryout in the balance of the world and the US is supportive to bullish. It is the structure of the S&D rather than the overall projections that has been driving our market.

For the week ending Oct 10, the US crop was rated in 64% good, or better, condition, up 2 percentage points Vs the previous assay period. The US harvest was estimated at 20% complete, up 7 percentage points on the week and Vs the rolling 5-year average of 26%. We think harvest progress over the past week will prove to have been modest.

On the production side, most of The Belt is expected to see excellent harvest weather over the coming week. Over the past week many producers within the Mid-south, northern Texas, Oklahoma, and Kansas saw significant rainfall. We caught 2 inches in our gauge just east of Memphis, TN. Out partner Scott called in from a drive through the Florida panhandle, southern Georgia, and Alabama last week to report that fields were mostly open and looked good. The North Delta crop is withstanding the rains to date, with yields near 5-year averages. Some areas have had 5-8 inches since opening, and we are eagerly waiting to see classing data on these fields. Spot checks to date show little to no discoloration and good staple length.

Net export sales and shipments were lower for the week ending Oct 7 Vs the previous assay period at approximately 154K and 106K RBs, respectively. So, demand appears to have been rationed further. Turkey and Mexico accounted for the lion's share of new sales while China purchased less than 20K RBs.

For the week ending Oct 14, the USDA classed approximately 252K running bales (RBs), of which more than 85% are deliverable against ICE contracts. The cumulative total for the season is now more than 1.1 million RBs (which is low), with almost 88% tenderable. We have seen color quality fall off a bit as rains have occurred across The Belt and we expect to see much more of this going in coming reports.

Internationally, Conab has projected 2021/22 Brazilian production 14% higher Vs 2020/21 at around 12.3M 480lb bales. Harvest continues across the northern hemisphere while sowing and preparations thereof continue below the equator.

For the week ending Oct 12, the trade reduced its futures only net short position against all active contracts to approximately 17.6M bales as the trade continues to pick up cotton from producers; large speculators reduced their aggregate net long position to just south of 8.9M bales. However, managed money firms moved their outright shorts to less than 70K bales, and this could lead to quick (and potentially lasting) market breaks.

For this week, the standard weekly technical analysis for and money flow into the Dec contract remain bullish, with the market no longer overbought. Harvest pressure and economic concerns could cause problems for the Dec contract over the near- to medium-term, with scheduled index fund rolling (which is also normally less than supportive) to commence on Oct 28.

Producers with cotton to price can pat themselves on the back for having outsmarted a host of market consultants, brokers, and the best minds at the coffee shop who argued for pricing cotton in the 80s and 90s. By many estimates, between 60 and 70% of estimated yield is priced, and nearly all of it is priced above the cost of production. Those producers who maintained bullish sentiment and managed risk should be holding call options with a nice profit made. Kudos to you.

Producers who descended from riverboat gamblers and home run kings, however, now find the market in historically high territory, merchants eager to buy, but levels of volatility that make nearly any price between 95 and 1.20 seem like a reasonable place to sell. We do not see a major selloff in the cards anytime soon, and with support strong in the 90s, we see little downside to selling rallies in the next few weeks.

New crop prices are also looking attractive. While it is possible that 2021 futures levels will be the “new normal”, and we could see prices above a dollar several times in 2022, we believe prudent producers will forward contract 10-30% of estimated 2022 production with Dec 22 trading north of 90 cents.

Have a great week!

Report Courtesy: Rose Commodity Group

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