Thompson on Cotton: Supply Increasingly Bullish, but What About Demand?

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As if on steroids, last week's market continued its near vertical climb from 89 cents. The December contract has now posted new closing highs in nine of the last 11 trading sessions. Last week, in heavy volume prices traded in a very wide range of thirteen cents from a low of 103.58 to a high of 116.48, closing Friday at 110.60 for a gain of almost six cents on the week.

Most notable of late has been huge daily price swings. On Tuesday, all current crop futures (December through July) closed limit up, something possibly never seen before. The following day December traded limit up early before retreating for a gain of only 213 points. Lastly, Friday overnight trading hit a high of 116.48 before surrendering over six cent in a matter of hours. Such volatility can be expected as spec longs and trade shorts jockey for position.

The driving force behind this run-away market continues to be speculative buying, mill fixations, and inflation concerns. Perceived strong demand and production uncertainties are enticing spec Funds to buy in. Last week they bought an additional 2,144 contracts bringing their net long position to 9.6 million bales. The U.S. crop rating was lowered to 62 percent good to excellent with only six percent poor to very poor.

However, adverse weather is creating harvest delays in most all production areas, not to mention possible yield and quality losses. Currently, only 13 percent of the crop has been harvested versus a four-year average of 19 percent. The Southwest will have to meet its lofty yield expectations if an 18.5 million bale crop is to be made. In addition, there are now global production concerns as Cyclone Gulab is rumored to have severely damaged India's crop. If so, this could significantly limit their exports which compete with us.

Even though the supply side appears increasingly bullish, demand is the key influencing factor. When looking at demand one first turns to China, the world's largest consumer. It is estimated they will consume 41 million bales this year, 24 percent greater than in the past two marketing years. In turn, U.S. cotton exports to China are currently 84 percent higher than at this same time last year.

At first glance, last week's export sales were less than stellar. Combined current and new crop sales totaled 315,350 bales versus the prior week's 588,300 bales. Looking closer, China accounted for only 174,400 bales versus 420,318 the previous week.

The fact prices were trading 10 cents higher could have been a reason for the decline in sales but more likely it was the Golden Week holiday celebration wherein most all businesses in China shut down. Nevertheless, the number of purchasing countries has declined in recent weeks which could be an early sign of price rationing. Something to be watchful for going forward.

Where to from here? No doubt this market is overheated and trading a bit irrationally. But who says commodity markets must be rational? It’s important to understand the specs are large and in charge of the current market. If they are content putting their money in cotton, prices will move higher and mill fixations will gird any dip in prices.

Next Tuesday’s WASDE report will certainly capture the attention of traders if any major adjustments are made. As hot as this market has been a selloff is imminent. The question then becomes will it be a minor correction setting the stage for the next advance or a top wherein a reversal begins. Those large and in charge hold the answer.

All being said, we remain cautiously optimistic current crop prices will move higher. To your good fortune, new crop prices will follow. This creates an excellent opportunity to price a portion of your 2022 crop. We at Choice Cotton strongly encourage you to do so and have a 2022 contract with a very competitive basis now available. Please contact us at 334-365-3369 if we can assist in your marketing needs.