Thompson on Cotton: Firm Support, Speculators Still in Control

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By Jeff Thompson, Autauga Quality Cotton

Once upon a time, a triple digit move in the market after a day of trading would grab everyone’s attention. Nowadays, such swings are made in a matter of minutes. Needless to say, this market is not for the faint of heart. Just last week it traded within a range of ten cents, which included two limit up moves.

In the end, however, it gave up 327 points to close at 107.33 in a rare selloff. Though this is a 50 percent retracement in its run from 89 cents to a high of 116, don’t be alarmed for a correction was sorely needed. View this as healthy thus setting the stage for the next advance.

Dominating last week’s news was the October WASDE report followed by weekly export sales figures. USDA bullishly lowered domestic production from 18.5 million bales to 18 million, a move we feel was warranted. With exports unchanged, U.S. ending stocks fell to a very favorable 3.2 million bales.

Unfortunately, world numbers were not as friendly. An increase in global production combined with a reduction in consumption raised ending stocks by 400,000 bales to 87.1 million. Though considered somewhat market neutral, it did encourage spec profit taking resulting in December futures losing six cents in early week trading.

Delayed until Friday, last week’s export sales figures were dismal for the third consecutive week. Current net sales of 153,100 bales were 80 percent of the daily average needed to meet export estimates. More disappointing, shipments at 105,810 bales were 30 percent of that needed.

Granted, supply chain and logistical disruptions are largely responsible for the latter, export sales have dwindled as prices have risen. Hopefully these numbers will improve as China returns from their weeklong holiday.

We mustn’t forget speculative funds are still in control of this market. Though paying some attention to fundamentals, more often they weigh the cotton market versus outside markets as to which poses the greatest risk to their investments. Still long cotton at near historic levels one can assume they still see cotton as a haven.

The latest COT report showed them reducing their position by 9,298 contracts which was no surprise given the market selloff. However, they still maintain a sizeable net long position of 8.7 million bales. Conversely, the trade holds a hefty net short position of 17.4 million bales, which should give the funds greater confidence.

On the week, there was little change in Open Interest, down only slightly. This would indicate the tug of war between the longs and the shorts ensues with each side holding firm.

In this contest, to our good fortune, the specs have the luxury of time for they can roll their position unlike the trade shorts where three million bales of on call mill sales must be priced over the next six weeks along with an additional 4.6 million bales by the end of February.

Where to from here? As seen last week at 103 to 105, there is firm market support. Last week’s minor correction should reenergize our bull as it makes another run at the contract high of 116.48. Also aiding our cause, strong buying on the Chinese futures market is allowing U.S. prices to remain very competitive even at these lofty levels and poised to capture any underlying demand.