Thompson on Cotton: Despite Recent Losses, The Sky's Not Falling Yet

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By Jeff Thompson, Autauga Quality Cotton

If cotton prices were an acorn, we know how Chicken Little felt when he thought the sky was falling. The cotton market has created quite a stir with four consecutive weeks of losses and falling into the seventies for the first time since last October. Closing limit down on Thursday after a respectable export sales report certainly heightened the anxiety.

Even Friday's attempt at a rebound did little to calm the fears of many. Unfortunately, December futures were along for the ride. In spite of all this, we must not forget the moral of the story. Jumping to conclusions and doing something irrational in a state of panic can often lead to more serious consequences.

We must remember the year-long rally from a low of 48 cents was driven by increased demand and tightening supplies which are still prevalent today. Although we feel May and July futures may have exhausted their run, there still remains some life in December. About the only support we see for the cover months are the on-call mill purchases that still must be fixed prior to July going off the board.

However, much lies ahead for December futures, most of which is uncertain this early in the season. Even amidst last week's disastrous trading, there were some positives telling us it is too early to panic where December is concerned.

For the week ending March 23, the Managed Funds decreased their net long position by 46,300 bales. They did so by decreasing old crop futures (May and July) by 51,700 bales, shorting old crop futures equal to 50,000 bales but adding to their new crop long position equal to 61,500 bales. In other words, though abandoning old crop they continue to exhibit bullishness toward new crop.

Conversely, the trade reduced their outright short futures by almost 400,000 bales, a good indication mills viewed this as a pricing opportunity. This became obvious on Thursday when May fell to 78.75 and a half million bales traded in 15 minutes with a third of this done in one minute. This is an unheard-of trading volume in such a short time but is a testament to the volatility in the current market.

Last week's export sales, when looked upon alone, were very respectable. Current crop sales of 278,200 bales were five times the needed weekly average. However, when compared to the over half million bales sold the previous week, traders were not pleased and drove the market limit down on large volume. Cumulative sales have reached 14.2 million bales. This is 99.5 percent of the USDA target and the largest sales total since 2010-2011.

One of the biggest negative influences now in play, and partially responsible for the recent price decline, is the rise in the U.S. Dollar. As mentioned before, there has been no bearish changes in cotton fundamentals in recent weeks as

December shed 10 cents and May gave up 15 cents. However, the Dollar has gained in value significantly.

There is a proven correlation that for every one percent change in the Dollar Index, there is a five percent inverse change in the price of cotton. This is something to keep an eye on because current economic conditions favor a strengthening of the Dollar.

Where do we go from here? The cotton market is in desperate need of some bullish news, and, better yet, new bullish news. The highly anticipated planting intentions report is scheduled for release on Wednesday. The consensus is that intended acres will fall in the range of 12 to 12.5 million acres. Anything outside of this range will heavily impact December futures.

Looking back, the March intended acres were greater than the final planted acres by an average of 1.1 million acres three out of the last nine years. The most recent was last year when final planted acres were 1.6 million less than that projected in March. We say all this to advise you to not be like Chicken Little and panic.

New crop has a long way to go, much can happen, and fundamentals are still strong, so exert patience. View any return to the mid 80’s as another pricing opportunity.