Cleveland on Cotton: Cotton Prices Dip Despite Bullish Fundamentals

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This week's apologies go to Rodney Dangerfield: Cotton can't get any respect. Cotton fundamentals were very good all week with one exception, yet the market moved lower. It didn't just lower; it recorded a new life of contract low. Export sales were strong, and shipments were exceptionally strong. On-call sales fixations dwarfed on-call purchase fixations. Yet, prices moved lower seemingly every day. Obviously, the downward sloping trading channel we declared to be over some two months ago remains alive and kicking.

The market adage continues: Never bet against the trend. The worm in the apple remains a weakening demand, a fundamental that actually defines market strength, and the worm is getting fatter.

The nearby March contract, facing first notice day on February 23, or 14 more trading sessions, has lost about 175 points over the past two weeks. It's been down in 10 of the last 11 sessions, while open interest has increased in each of those sessions. Prices are hanging in the low 63s and making a serious threat to fall into the 62s. The certificated stocks position is being evaluated as new stocks are coming to the Board in quantities of ones and twos. It appears someone wants to bring stocks to the Board but wants to test the water first. We mentioned the possibility of a price squeeze last week. With just two weeks to go before first notice day and (1) open interest at an all-time high, (2) certificated stocks currently at only 8,600 bales, (3) speculators holding near record short positions, and (4) metals markets—speculations, melting down will combine to give rise to an increasing probability of a market squeeze. Yet, we do not see it occurring. We expect a strong taker of stocks will surface for any increases in certificated stocks, and a short covering rally will be averted.

Traders are not attuned to trading a market that is all about supply and one without any positive demand factors. Thus, the bears command the trading. Cotton's hope, and no marketing strategy can be based on hope, is that something will spur demand and allow prices to move higher. The only solution, given declining demand, is lower prices to discourage lower plantings. That defies the grower's desire to plant cotton. Yet, the U.S. has been boxed out of maintaining its cotton acreage and the industry is suffering through a stage of reduced plantings. Until the U.S. can define its new range of cotton plantings, cotton prices are doomed to remain at or just below the average U.S. cost of production.

The new crop December contract has slipped below the 69-cent level but will find good support between 67 and 68 cents until planting of the northern hemisphere crop is well underway. Once planting has begun, prices will receive direction from planting progress, coupled with any weather difficulties given by Mother Nature. World stocks, about 75 million bales, are very adequate, but not in excess. With almost half (36 million) of those stocks held in China, any production difficulty will support December futures in the high 60's. Depending on the planting/production difficulties, the potential for 75 cents exists, but only based on weather.

Nearly one million bales of Upland have been sold in the export market over the past three weeks. Thus, at a low price, the U.S. crop is moving. Weekly sales were 203,700 bales of Upland. Primary buyers were Pakistan, Vietnam, China, Guatemala, and Turkey. Of the 257,000 bales in shipments, Vietnam took 114,400 bales. Sales to date lag prior year sales by 1.3 million bales. Traders will continue to view the slow pace of sales as bearish.

However, shipments to date are about 100,000 bales ahead of the prior year’s pace.

Mills fixed the price of 483,900 bales, basis the weekly on-call sales report. This was an aggressive number and does suggest that some mills are comfortable with current New York futures. Nevertheless, mill activity continues to suggest a combination of lower to slightly lower prices, or a sustained period of prices at current low levels. A growing concern is the increasing buildup of December on-call purchases. This activity portends that the December contract will eventually face the same bearish price pressure currently faced by the March and May futures contracts, in the absence of planting difficulties.

The coming two weeks will give the market the results of the National Cotton Council’s annual planting intentions survey. The survey is respected for its historical accuracy. Additionally, the February world supply demand report is on the horizon. Current expectations are that U.S. growers will plant 9.3 million acres. We suggest that as many as 9.7-9.8 million acres could be planted. New fundamental information is not expected, but surprises are always in the next report.

Market technicals suggest that the market is looking to expand its trading range. It is difficult to see the market moving lower. Yet, the market trend points lower.

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