Source AgFax le 18 juillet 2022

Thompson on Cotton: Traders Focused on Economic Troubles Rather Than Fundamentals

©Debra L Ferguson Stock Photography

Some key economic data and the monthly WASDE report were released last week. With a market keen on reacting to the news of the day, active trading came as no surprise. The week began with expectations of a follow through to the prior week's rally. Instead, we experienced a reversal wherein it sold off twelve cents before a limit up move on Friday cut these losses nearly in half closing the week at 88.71.

Sound familiar? The market has now posted a loss in eight out of the past nine weeks. Also, this week saw an intraday low of 82.54, a level not seen in ten months. Cotton continues to be caught up in the spec community's mass exodus from commodities prompted not by weak fundamentals but rather fear of a recession. Bloomberg's Commodity Index being down eighteen percent in just the past five weeks is further evidence of this.

Another illustration of the market's strict focus on economic troubles was seen when it traded limit down on what was a very positive WASDE report. In response to above average abandonment in West Texas, USDA lowered domestic production a million bales to 15.5 million. Subsequently, ending stocks declined to a miniscule 2.4 million bales. We feel they are still underestimating the severity of the situation thus look for these numbers to fall even lower.

The greatest concern last week was the consumer price index, which reflected a red-hot economy and growing inflation. The Labor Department indicated the consumer price index rose 9.1 percent in June from a year ago, far exceeding expectations. In addition, the producers price index rose 11.3 percent in June.

This marks the fastest pace of inflation since December 1981. As a result, there is talk the Fed may raise interest rate by 100 points since they have vowed to take a hawkish stance toward curbing inflation. Such a move would certainly strengthen the Dollar and drive the economy further toward a recession, both of which would take a toll on U.S. cotton exports.

Weekly export sales figures released on Thursday did little to excite the market as seen by it slipping four hundred points following the report. Combined current and new crop sales totaled a meager 150,000 bales, down 65 percent from last week and 51 percent below the four-week average. Shipments were a respectable 317,000 bales, but must average 428,500 bales over the next two weeks to meet USDA export estimate for 2021/22. The only bright spot was the lack of cancellations which were only 5,300 bales.

Finally, the only positive economic news was retail spending figures issued Friday. Despite what has become a steady diet of dire economic news, consumer demand remains. In June, retail sales rose by one percent, slightly higher than the estimated 0.9 percent and much improved over May's decline of 0.1 percent. However, these numbers may be skewed as they are not adjusted for inflation. Nevertheless, equities market viewed it as friendly with the Dow up 658 points on the day, as did cotton closing the week on a 500-point limit up move.

Where to from here? The answer lies with the managed funds and how much further they will reduce their long position or even worse revert to shorting the market. Last week, they further reduced their long position by 5,000 contracts to a net long position of 3.5 million. Their liquidation from a high of over 11 million bales net long has driven cotton prices down over half a dollar since last May's high.

If the uncertainty in their future actions is not enough, what's scarier is people are beginning to talk about LDPs, the furthest thing from our minds a few months ago and not in play since October 2020. Current cost to market calculations indicate 67 cents would be a price floor for growers as an LDP would kick in at that point.

However, with such low inventory and prospects of smaller crop, we are much more optimistic and do not foresee such drastic moves by the funds. Remember that patience is a virtue and we would recommend everyone to practice such.