Cleveland on Cotton: Cotton Price Improvement Is On the Horizon

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Buy December calls. Buy July calls. Maybe do a 71-75 cent spread.

Enough is enough. The worm has turned. Turn on a dime.

Choose the phase that you like best. Maybe it's time to choose them all. Price improvement is imminent. Contain the excitement.

Higher prices are ahead for both old crop and new crop. The May contract will continue to back and fill. There will be discussions about a major squeeze in the May contract on the shorts, and this will elevate prices – but very probably only for a brief period as my guess is that the big boom will come on the July contract. The big merchant will make that decision as to the time of the explosion.

Old crop and new crop prices are moving higher. Yet, there is a major caution. Demand still has all the signs of a big, big bear, so the price advancement will be strictly based on the supply side of the price equation. Nevertheless, growers can now look to the December contract climbing to a minimum of 75 cents, and any continuation of drought problems in the giant Southwest can get the market excited enough to climb to the 85-cent level.

Production problems anywhere in the major cotton production areas will be enough to push prices as high as 85 cents. The U.S. Southwest is facing another significant drought (yet we know big rain always comes in late May/very early June – i.e., the Memorial Day magic.) We never know from year to year, but at the market highs or lows, we are always cognizant that a typically active cotton market will always trace through 25 cents from the price high to the price low.

Old crop is not out of the woods, but the worldwide decrease in planted acreage and impending production problems spell higher prices. Too, the planting season is seeing a reduction in plantings, and the current imbalance in production and consumption is being somewhat relieved. Thus, the bottom is in for both old crop and new crop, and prices are headed higher for both.

The potential squeeze on old crop will prevent old crop prices from moving lower. That is the basis for suggesting the consideration of buying call options. Consumption/demand remains a significant problem. The month-long increase in both sales and shipments of U.S. growths is being interpreted by some as a turnaround in demand. It could be, but more likely the stronger sales of U.S. are coming at the market bottom, as should be expected. Additionally, other growths are becoming more difficult to obtain.

We welcome the increase in U.S. sales but contend the increased U.S. sales are a function of the fire sale price rather than improving demand. The market simply remains supply based; thus, any price rally will be short winded. However, we

cheer with enthusiasm any increase in price. A profit is on the horizon.

Weekly net sales of U.S. cotton were very strong as 271,800 bales of upland were sold. Too, weekly exports did establish another marketing year high as 403,500 bales were shipped. This is the peak season for shipments of U.S. cotton; thus, this level should not be expected to continue past April. If it does, then export shipments could exceed the 11.0 million bales projection of USDA.

There are 20 weeks remaining in the marketing year, and shipments must average about 260,000 bales per week to reach the USDA estimate – easily within reach. Yet, even if the U.S. ships 200,000/300,000 bales more than the USDA estimate, the market will still have to work through a 4.5/4.6 million bales carryover.

Cotton must reconnect with the consumer if any rally is to be sustained.

The On Call report confirms the considerable bearishness in the market. However, with the July expiry period beginning in just eight weeks, the bearishness will be overcome. That bearishness will become very vulnerable to a short covering price rally that could take July to the 71-73 cent level.

Regardless, the decline in U.S. and foreign plantings will help support higher prices in the July futures contract.

Finally, we can plant cotton.

Give a gift of cotton today.