

New York Futures

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After one of the most bearish markets in recent history, cotton seems to be on the verge of a sustainable rebound. This prediction stems from resurgence in demand driven economics and a projected reduction in world supplies.

The first hints of production cuts came in the Southern Hemisphere crop areas this year as low world prices at planting time affected planted acreage in South America and Australia. At the same time, low world prices stimulated demand for cotton in several key cotton consuming markets as world economies rebounded and cotton gained share on the spinning system.

Several Far Eastern markets like Taiwan, Indonesia, Bangladesh, Korea and Thailand have witnessed a strong appetite for raw cotton imports as they have moved to rebuild inventories after the slow down last year. In addition, China has seen a tremendous recovery in textile consumption and exports.

In the US, domestic consumption had fallen into a state of depression. Mill closures and bankruptcies were a monthly event in the months leading up to and following September 11. Since the beginning of 2002, US mill demand has been improving.

At first the demand seemed to come from a rebuilding of yarn stocks and consolidation in the industry. But as time passed it became more apparent that US consumption was on the rebound as retailers sought to rebuild inventories as well.

As the northern hemisphere cotton production areas approached planting time, world prices were again under pressure. This seemed to discourage planting intentions in the US as well as other major cotton producing regions.

Early estimates of Chinese acreage cuts floated around the 15 to 19 per cent level. This followed the March US planting intentions report that indicated a 6.4 percent decrease to 14.77 million acres.

Since this estimate it is our belief that acreage has fallen even further to perhaps 14.2 million acres. This is primarily due to a 200,000–300,000 acre decrease in insurance acreage and a reduction in California acreage of another 100,000–200,000.

US farm policy

US farm policy changes also played a part during this period. As it became apparent a new farm



bill was likely, initial perceptions were decidedly bearish. But as time passed it became clearer that may not be the case.

In fact, some acreage is going to be removed from planting as growers can now receive payments on acreage whether they plant or not. This is likely to have the effect of taking some marginal land out of production.

Adding further support to more bullish developments was the USDA's May supply and demand estimates. In this report 2002-03 world ending stocks were forecast to drop nearly 4.2 million bales. World production is forecast to decline 6.95 million bales while consumption is forecast to rise by 2.04 million bales.

In the US, ending stocks are forecast to fall by 1.0 million bales to 6.7 million. This is primarily due to a drop in production to 17.8 million bales from this year's 20.3 million. US exports are estimated at 11.0 million bales while domestic consumption is likely to remain at or near the 7.8 million bale level.

As the US summer arrives the market may need some additional weather premium. If so, we could see the December contract trading toward the upper 40s.

One caveat to this is the July delivery period. Right now certificated stock against New York has risen to over 280,000 bales. This is likely due to the abundance of 1 1/16 cotton available for delivery against the board.

Export demand from the US this year has centered on the low grades and high grades. This leaves the 1 1/16-1 3/32 cotton available for tender. In the past US domestic mills consumed the 1 1/16 cotton.

As US consumption has fallen so has the demand for this type of cotton. This leaves an abundance of supply with no really good marketing outlet other than New York. The abundance of medium grade cotton has most traders expecting heavy deliveries on July.

While this may be the most popular view there is another possible scenario that could emerge. A need for this stock could appear as the demand for third and fourth quarter shipments continues high. It was first thought that as new crop supplies become available and converge with the large carryover, the board would melt under the pressure.

But two events could delay or all together prohibit this occurrence. First, the south Texas crop is a disaster. This represents the bulk of the early US crop.

Secondly, if prices are not attractive enough at harvest, cotton could again move into the loan. If so merchants who sold forward aggressively in anticipation of available supplies might see basis levels rise. Therefore, this risk may entice merchants not to tender in July but hold supplies through the fourth quarter. Especially since the

market is currently giving full carry.

Good price support

As we go forward, prices are likely to continue to show good support on any breaks back toward 35.00. This is largely due to the forecast of contracting world stocks and improving demand.

Whether or not prices can rally more than seven to 10 cents is questionable due to the burdensome carryover of stocks. A rally of this magnitude would only come with some sort of crop disaster in the US or in one of the other major cotton producing areas.

Another factor to watch is the US dollar. Continued weakness would result in even larger US exports and smaller world production. Notwithstanding a total economic meltdown with extreme deflation, I predict the lows we made this season are the last we will see for a while.