New York Futures outlook

By Hibbie Barrier, The Jernigan Group

In our latest update, New York was trading in the low to mid 70s and I was predicting a return above 80 cents as still being a possibility. I was also left trying to explain an unexplainable 20 cent collapse in New York futures.

Well, here we are all over again. Except this time it's a 10 cent fall. Last time New York fell far enough to ignite world export demand for US cotton. The same would seem true again this time. And while I use the term 'world export demand' what I really mean is that big red cotton consuming dragon called China.

Armed with a new 1,000,000 ton import quota, Chinese mills again sit atop cotton's chain of command. At times it seems the cagey dragon plays a maniacal game of hide and seek with the market. On one hand showing the obvious. Real demand for high quality cotton demonstrated by the high prices being paid domestically.

Then, on the other hand, exercising the patience of Job standing by while New York falls below most everyone's sense of fair value given the tightness implied by the USDA's supply and demand estimates. The same could be said for the ICAC and Cotton Outlook's estimates as well.

In fact, in the USDA's March estimates, world ending stocks fell 760,000 bales to 31.73 million bales. The decline was fueled by the 700,000 bale reduction in the US ending stock figures to 3.55 million. This is the lowest level since the 1994–95 season. The USDA arrived at this number by reducing beginning stocks 400,000 bales to 36.37 million.

BRAZILIAN PRODUCTION INCREASES

Production estimates increased 210,000 bales to 92.86 million, primarily the result of a 200,000 bale increase in Brazilian production to 5.40 million.

Imports were forecast to rise 1.49 million bales to 33.86 million. This comes on the heels of a 1.5 million increase in China's imports to 8.50 million bales.

Consumption was placed at 97.88 million bales, up 640,000. A 1.0 million bale increase in China led the change.

Exports rose 1.42 million bales to 33.44 million. An increase of 600,000 bales to 13.80 million from the US provided much of this change.

In any other year I would view the type of corrections we have had in New York as an indication that the general bullish perception of the market and the USDA's numbers were just flat wrong. This year it is hard to argue with the known facts. China's stocks have fallen to levels not seen since 1994.

It should be further noted that in 1994 China's domestic use was only 20.0 million bales versus today's 31.50 million. US ending stocks have fallen to eight year lows at 3.55 million. Volatile New York has also meant volatile yarn prices. This has undermined mills confidence and as a result turned most of them into hand to mouth buyers.

DEMAND HARD TO GAUGE

This type of demand is always hard to gauge in terms of depth. Every day is like a high stakes poker game featuring mills and merchants on opposite sides of the table. Despite the volatile nature of the market, cotton would appear undervalued in the low 60s and at the same time overvalued in the low 70s.

The undervalued aspect comes as we compare New York to the other world growths. As long as the A Index stays relatively supported, New York can only fall so far. On the top side, China's domestic prices continue relatively high and it will be hard to justify New York much above 74 to 76 cents.

That is when high grade SM $1\frac{1}{8}$ cotton reaches 80 to 82 cents delivered China. So there are natural barriers at these areas. This will not change until we get a better idea of the degree of the shortage. That should become more apparent in the next two months.

The other factors affecting New York price direction has been the build up of certificated stocks and new crop planting intentions. As for the certificated stocks, the lack of international demand for US SM $1\frac{1}{16}$ cotton has made New York an attractive destination.

Stocks climbed from around 180,000 to back over 300,000 in just two months. This build up pressured the market inverse to new crop as it became apparent the merchants would be forced to carry nearly 4.0 million bales into next year. The July/December spread has collapsed along with the buildup of certificated stocks.

NEW CROP OUTLOOK

Now a look at new crop. In the US, soybean prices have rallied to levels only seen a few times in history and none very recently. Midsouth and southeastern cotton growers are grappling with the switch. In Louisiana and Arkansas, cotton acreage is already being lost. Mississippi is not far behind either. In the southeast, $3.00 corn, $9.00 beans and strong peanut prices have cotton farmers seriously contemplating planting decisions.

I think it is safe to say US acreage will be down sharply from the National Cotton Council's early estimate of 14.759 million. Today I would place this figure closer to 14.0 and falling. While in past years this would be an extraordinary event, this year the focus will be on China and the other producing/consuming countries.

Acreage increases in China have been rumored as much as 16 per cent. This follows an 18 per cent increase the year before. In other words, that would imply acreage will grow over 30 per cent in two years. That is tough to do in any country. Regardless, my point is that until we get a better picture of China's new crop potential, New York may continue to struggle even if US acreage continues to fall.

This is the result of the transition of the US market from domestic to exporter. My view on this all changes if China fails to plant the expanded acreage. At that point all exporting countries will find their cotton dear again.

As for the remainder of this season, I can't help but feel we are sitting on a powder keg. The fuse is probably one to two months long. By then we should know whether or not there is truly a shortage of cotton or just a hoarding by merchants who bought early and cheaply.