ICE futures benefit from weaker USD

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ICE Cotton futures have enjoyed a steady uptrend from their March lows. The rally has taken the December contract to near the 64 level and has occurred despite the lack of a fresh export stimulus. One of the strongest influences has been the continued weakening of the US dollar against most currencies.

For Australian growers, the USD weakness has had a negative impact on returns, as the Australian dollar has strengthened to over 0.90. The USD weakness and improving technical outlook has led to several waves of commodity fund buying. By the week ending September 22, managed money longs had reached 42,157 contracts, which represented 28.7 per cent of the total open interest. In addition, the index funds held 77,655 contracts long, which represented 37.7 per cent of the open interest.

The attraction to the speculative sector has occurred despite the grain complex weakness. In addition to currency and technical influences, the speculative element has been attracted to cotton as a play on the improving global economic climate. In its twice-yearly World Economic Outlook, the IMF has revised upward its projections for world growth in 2010, now forecasting global economic growth of 3.1 per cent in 2010, which compares to a contraction of 1.1 per cent in 2009 and also represented a 0.6 per cent upward revision from its previous forecast.

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Emerging economies are expected to grow 5.1 per cent. This rebound has ramifications for global cotton consumption at the retail level. What is making this growth more difficult to analyse at the retail level is that it is Asia-centered. The traditional US–Europe–Japan trio remains at marginal growth, and the consumer in this entire block is showing only nominal signs of spending.

The question is can the new consumers of Asia and the other emerging economies take up the leadership? The global textile sector was suffering from a major problem with overcapacity when the current global recession began – it still has excess capacity today that is making a recovery in consumption at the mill level more difficult.

Global cotton consumption shows nominal improvement

Global cotton use appears to have bottomed during the calamity of the 2008–09 time period, falling to near 23 million tonnes. Much of this steep decline from near 26.5 million tonnes occurred in China.

The recovery in 2009–10 will be led by a different consumer with a new set of spending habits, which could prove quite a challenge for cotton. Retail sales of apparel/home textiles are expected to remain at only nominal growth as 'saving' takes prevalence in the US–European–Japanese economies. This region has always represented the top import markets for textiles and apparel. Lack of growth in these markets today means that the export engines of China, India, Southeast Asia and Pakistan will face great difficulty in resuming any meaningful growth.

As a result, all industries in this region will have to increase concentration on their own consumers. For cotton, this could mean a loss in market share to polyester. So total growth in global cotton consumption in 2009–10 will be nominal. Even in 2010–11, total usage may not exceed 24 million tonnes, which leaves usage far below the peak of 2007–08. Industry in China continues to face a need for additional reform and modernisation, which would mean closure of old inefficient spindles.

US yield prospects hold

So far, the 2009 harvest in the US has been marked by extremely wet weather across the cotton belt of the mid-south and south eastern crop areas, causing concern as to the quality of the crop. Very little new crop has been classed, as the harvest has been delayed. The wetter-than-normal pattern has thus far missed the important West Texas cotton belt. This situation has left US production prospects near the 2.925 million tonne level.

India's 2009 crop now appears likely to produce over 30 million 170 kilogram bales. The latest CAB estimate is 30.5 million bales, which represents a five per cent increase over the previous year. New crop harvest has begun in the northern production zone, and a few areas in the central zone. In Pakistan, yield prospects have deteriorated in Punjab, lowering overall output prospects to near 12.0–12.4 million 170 kg bales. Yield prospects in China have also declined with a crop of near 7.4–7.5 million tonnes. While overall global production will fall below last season, the decline has not been large enough to influence price.

ICE futures face stiff resistance

The nearby ICE futures contract faces very stiff resistance on any attempt to breach the 64 to 65-cent level. One reason for this is lack of fresh import demand from China. Given the size of the current Chinese crop, weak consumption prospects and continued market intervention by the government, fresh import offtake through the end of the year is likely to be limited.