

New York Futures outlook

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“New York futures have been misbehavin’ lately and quite frankly I am growing tired of being very patient”

This is a common theme among the calls I take on a daily basis. The frustration seems to stem from the disparity between the tightness projected by the supply and demand statistics versus the reality reflected by New York’s price behavior. Not even a strong taker for the May contract has been able to revive the wounded bull’s market.

Events in China, as has been the case all season, continue to lead price action. China’s appetite for quality 1³/₃₂ and up cotton was nothing short of fantastic, at least up until a month or so ago. Now China’s interest is only for selective top grades.

NEW CROP EXPECTATION

Furthermore, the central government has tightened credit and demand is being hampered by cash flow restrictions. What else could befall our bullish setup? Try a whopping new crop expectation for world production to exceed 100 million bales. Yep, that’s right, 102.50 million to be exact. So here we are with the tightest projected world and US ending stocks in eight years set off against the largest projected world new crop on record.

In the USDA’s May supply and demand projections the government made its first new crop projections. Beginning stocks were placed at 32.66 million bales while production was forecast at a record 102.50 million bales. World consumption was estimated at 99.0 million bales. This left world ending stocks at 36.46 million, predicting an increase of 3.80 million bales next year.

In addition, the USDA raised 2003–04 ending stocks 1.05 million bales to 32.66 million. This change came primarily as the result of increased production in India of 500,000 bales and 250,000 bales for Brazil.

In the US, new crop projections suggested production of 17.60 million bales versus 18.26 this year. Domestic consumption was put at 5.80 million versus 6.30 this year. Exports were set at 11.50 million, down from 13.80 million this season. These projections pushed the ending stock forecast for 2004–05 up 300,000 bales to 3.90 million bales.

DEMAND THE KEY

The current mood of the market suggests demand, not supply, is where people will place their bets. This is dead opposite of the market’s focus in the fall.

Consuming patterns are ever changing and this year has been no exception. China continues atop the food chain in this regard. Right now the market only sees the short term effects of credit tightening and the more important projection of production increases of 10 to 15 per cent for new crop. Between the two, it seems hard to imagine a return to the pre-Christmas bullish euphoria.

Let’s suppose, however, for a moment that either one of these

two scenarios begins to change. For instance, let’s take demand first and say the Chinese central government gets growth back under control. Does that lead to more or less demand? My guess is China will continue to consume steadily.

SUPPLY UNCERTAINTY

The other side of this question is what happens if China fails to plant the extra 10 to 16 per cent acreage? Or the acreage gets planted, but weather and what not conspire against the crop to limit production as happened last season? What will world prices do then?

For these reasons it is hard to envision prices much lower before some of the supply side questions become clearer. We could extend these questions into other countries as well. In the US, new crop acreage in my opinion is closer to 13.5 than 14.4 million acres.

Yes, Brazil is expanding area and with some additional rains Australian production could climb back above 2.5 million. This will help offset somewhat but what if these crops come in short? My point is stocks are the lowest in years and it would seem to me the market is not pricing in much yield risk at current levels. And until there is more certainty in new crop production it is hard to be bearish beyond the mid 50s. 