

TECHNO FUNDA REPORT ON

COTTON

[JUNE]

6th June, 2019



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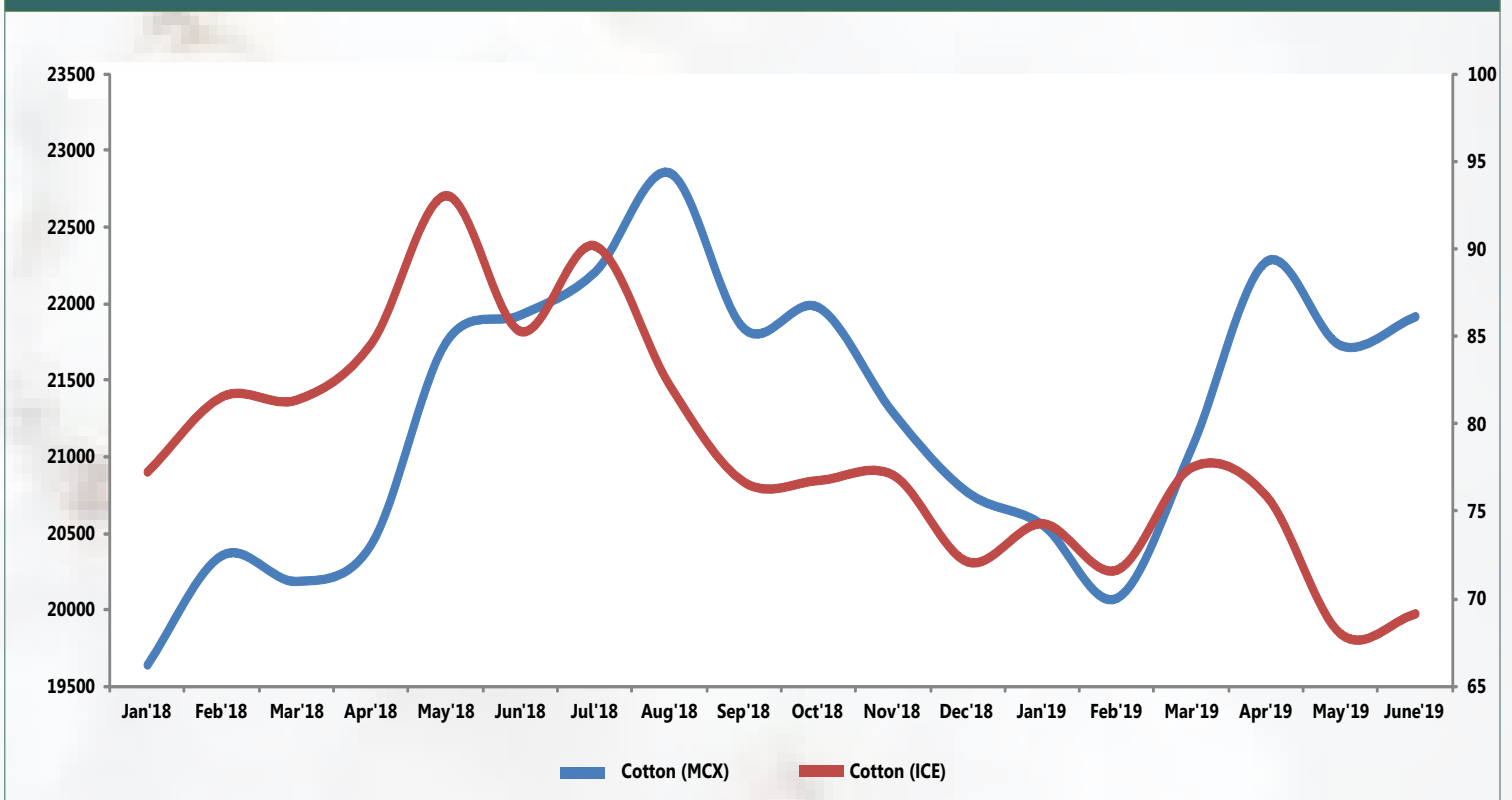
History

Last month, cotton prices across the globe moved lower over the past month. Prices for the July NY futures contract fell from values near 64.50 cents/lb. Indian cotton prices on the national bourse made a low of 19950 taking negative cues from the international terms. But, by the end of the month, cotton prices in the domestic market recovered from its lows, owing to weaker rupee against dollar. In the international market, this downward movement was mainly due to two major factors i.e escalated trade war & prospects of rising area under cultivation in U.S. Moreover, there was forecast for the steep increase in U.S. stocks, primarily as a result of the projection that the U.S. crop will increase. The larger U.S. harvest number is based on an assumption of lower abandonment. Lower abandonment is expected because of improved soil moisture in West Texas, where U.S. cotton acreage is concentrated, where little irrigation is applied, and where the drought conditions experienced in 2018/19 have dissipated.

Secondly, the deterioration of trade negotiations between the U.S. and China has been coincident with the recent downturn in cotton prices. It is to be noted that China represents more than 40% of U.S. apparel imports and over half of U.S. home furnishings imports, so this would be highly disruptive for U.S. supply chains.

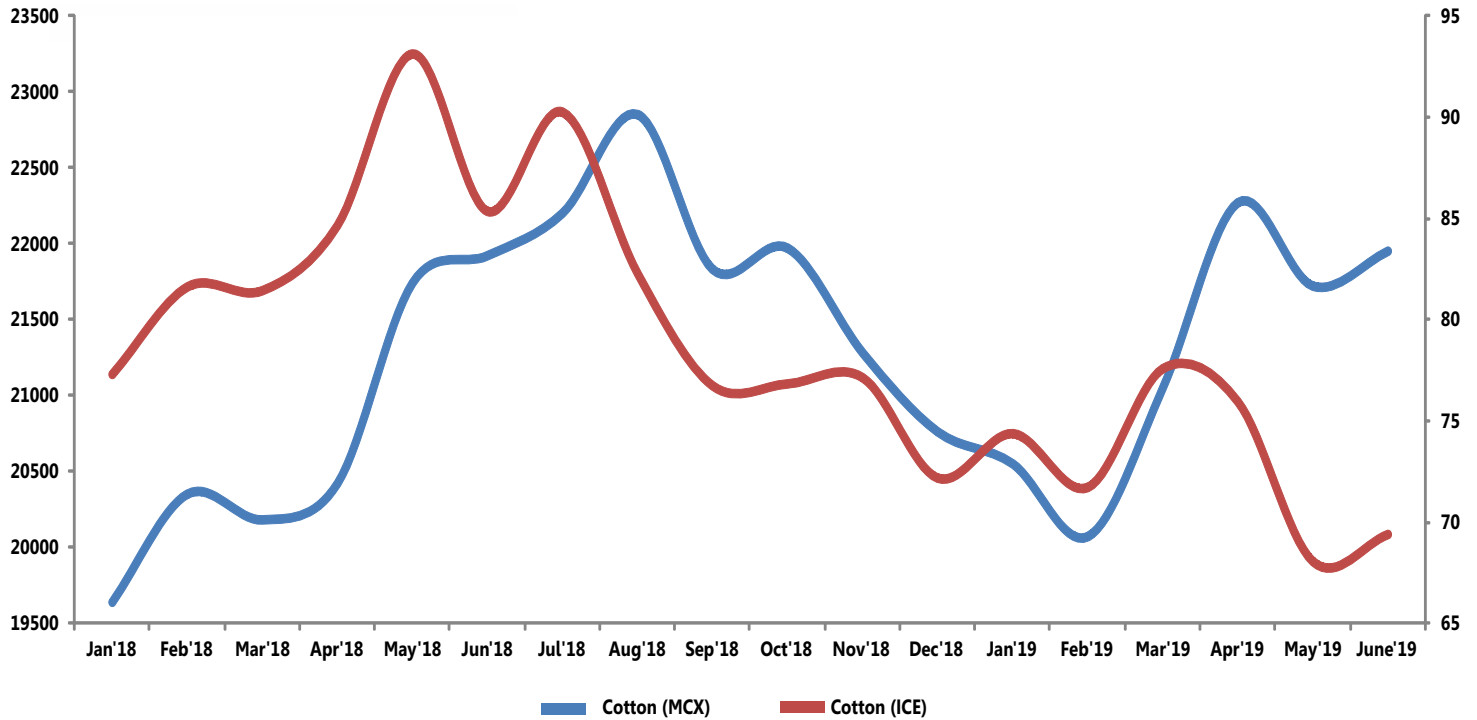
However, despite of the correction in cotton futures due to trade war tension in the international market, the trend of this soft commodity in the domestic market is still positive due to a sharp fall in domestic supply amid lower crop in the current season. **But, we are expecting this uptrend trend to continue on the national bourse on the back of increasing deficit in the domestic market.**

Monthly price movement of Cotton (MCX) & Cotton (ICE)



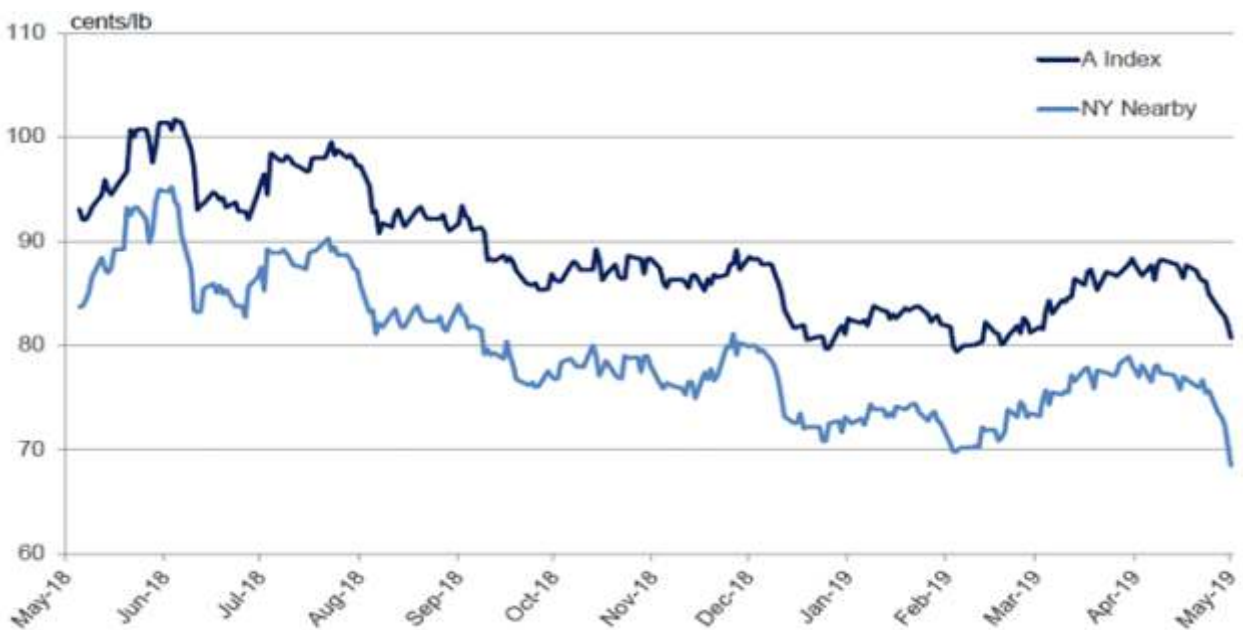
Source: SMC Research

Yearly price movement of Cotton (MCX) & Cotton (ICE)



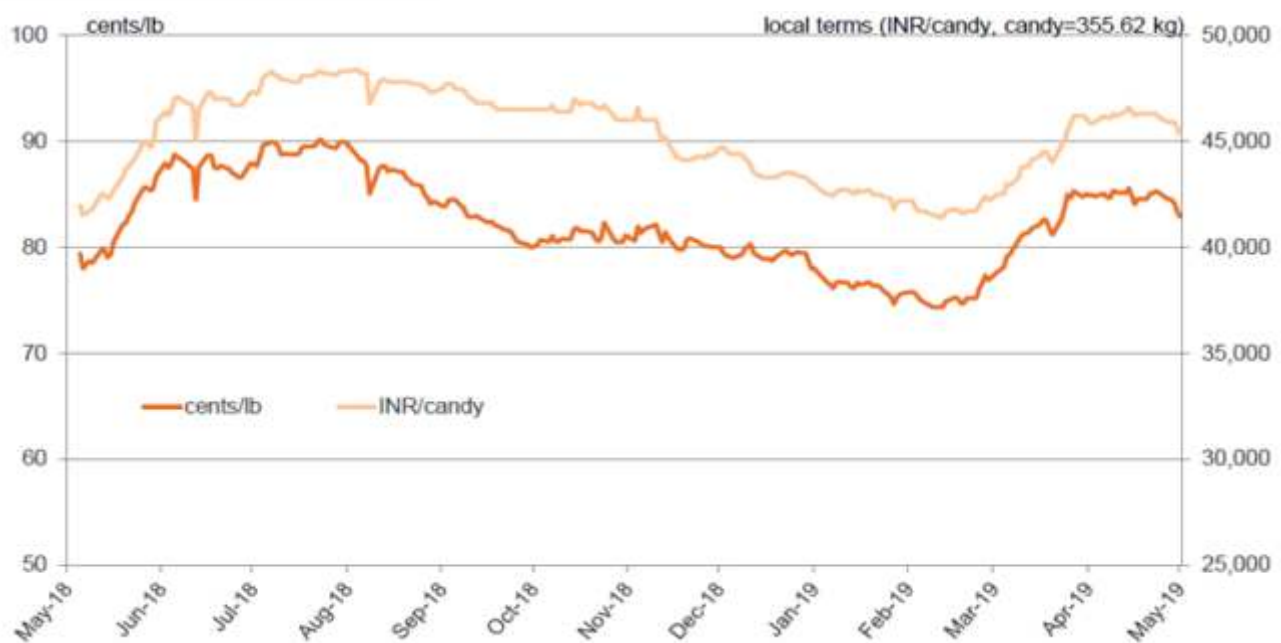
Source: SMC Research

One Year of Daily A Index and NY Nearby Prices



Source: Cotton Incorporated

One Year of Daily Indian Spot Prices (Shankar-6 Variety)



Source: Cotton Incorporated

Domestic market fundamentals

- The 3rd Advance Estimates of production of major crops for 2018-19 released by the Department of Agriculture, Cooperation and Farmers Welfare Production of, mentioned that cotton output is estimated at 27.59 million bales (of 170 kg each).
- The Cotton Association of India has maintained its estimate for production in the 2018-19 (Oct-Sep) season at 31.5 mln bales (1 bale = 170 kg). In its first estimate at the beginning of the current season, the association had pegged the country's 2018-19 crop at 34.8 mln bales.
- The production estimate is significantly lower than the output of 36.5 mln bales in 2017-18 mainly because of water scarcity in major producing states.
- The cotton body has also kept import and export estimate steady at 3.1 mln bales and 4.6 mln bales, respectively. The estimates for domestic consumption are seen at 31.5 mln bales.
- Considering the consumption and exports, ending stocks of cotton for the 2018-19 season are now estimated at 1.3 mln bales.
- Production in the central zone, which includes Gujarat, Maharashtra, and Madhya Pradesh, is estimated at 18.0 mln bales. In the northern zone, which includes Punjab, Haryana and Rajasthan, production is seen at 5.9 mln bales, while output in the southern zone is pegged at around 7.2 mln bales.
- At the end of May, arrivals of cotton across the country were pegged at 28.8 mln bales, up from 27.9 mln bales in April.
- This season, with the sowing going on in major growing states, in a reversal of sorts, the area under cotton cultivation has crossed 4 lakh hectares in Punjab for the first time in five years. The last time cotton was sown on more than 4 lakh hectares was in the 2014-15 season. Primarily, the rise in area under the cash crop is seen as a reflection of its price crossing the Rs.6,000-per-quintal mark at the end of the 2018-19 season. More farmers returning to cultivating cotton is seen as a positive trend because paddy consumes more water, which is in scarcity in Malwa.

	2018-19	2017-18
SUPPLY		
Opening stock	2.80	3.60
Output	31.50	36.50
Imports	3.1	1.50
Total supply	37.40	41.60
DEMAND		
Domestic consumption	31.5	31.9
Exports	4.6	6.90
Total demand	36.10	38.8
Closing stock	1.30	2.80

Source: CAI

- USDA Foreign Agricultural Service estimates India's marketing year (MY) 2019/20 cotton production at 29.3 million 480 lb. bales (37.5 million 170-kilogram bales/6.4 MMT) from 12.45 million hectares of planted area. Assuming a normal monsoon, the nationwide average yield estimates for MY 2019/20 is 512 kilograms per hectare. Also projected that MY 2019/20 cotton consumption at 25.3 million 480 lb. bales (32.4 million 170-kilogram bales/5.5 MMT). The reports anticipated cotton and cotton yarn prices will remain competitive as mills will have ample fiber supplies (domestic and imports) to cater to both the domestic and export markets. Hence, MY 2019/20 exports at 5.2 million 480-lb bales (6.6 million 170-kilogram bales/1.1 MMT). Even though a large crop is expected, imports will remain strong as mills import for processing and re-export to cover yarn export commitments. It is estimated MY 2019/20 imports at 1.5 million 480 lb. bales (2 million 170-kilogram bales / 327,000 MT).

International market fundamentals

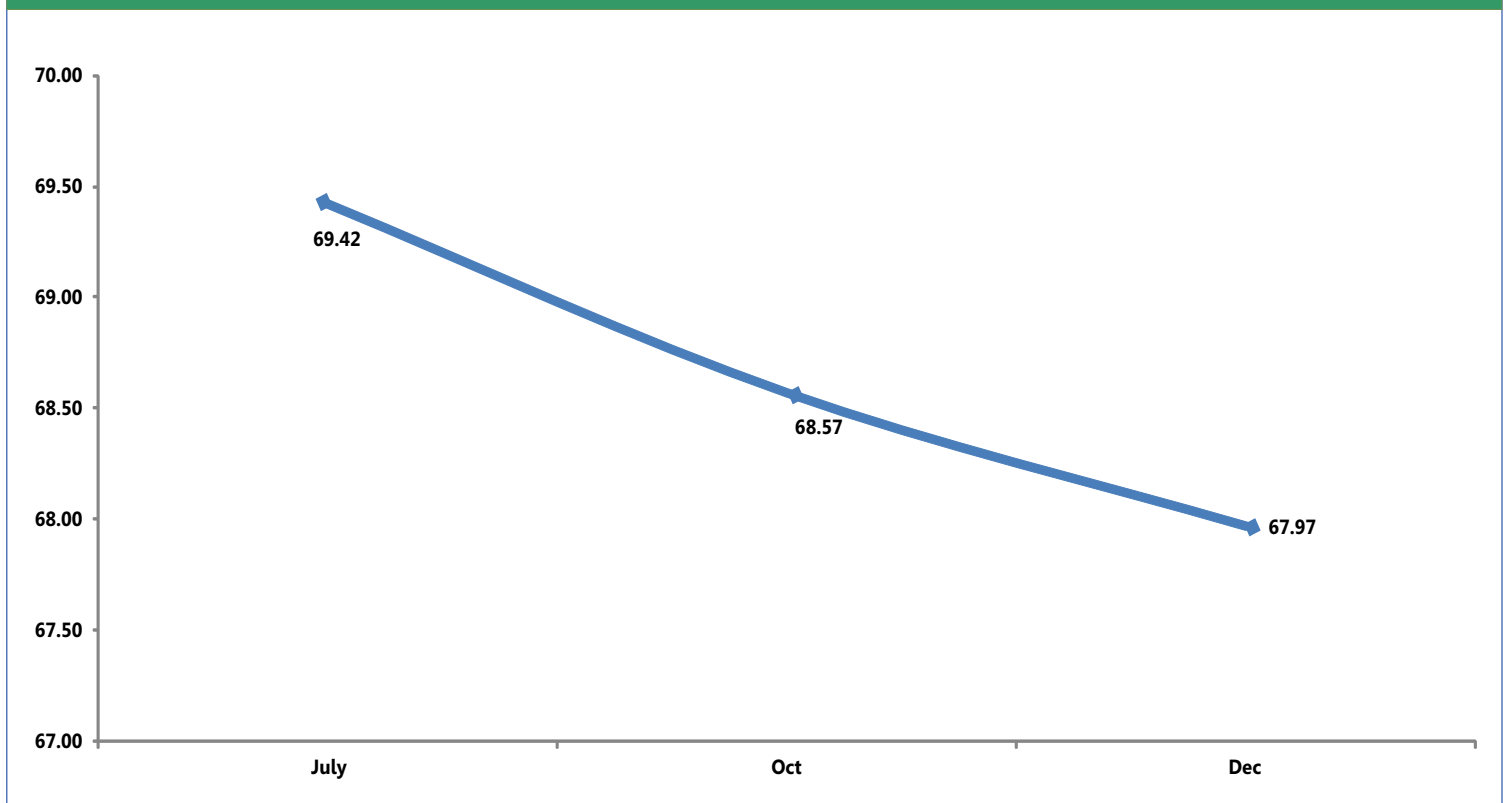
- The weather this spring has been rough across the U.S. agriculture belt, and cotton farmers may have had some of the worst of it. Both the top-two producing states in the U.S. are being affected by adverse. Meanwhile, the area considered abnormally dry in Georgia. Through May 26, about 57% of the crop has been planted, down from 61% a year ago, government data show.
- The USDA reported net cotton export of 288,800 bales (1 US bale = 218 kg) for the week ended May 23, down 24% from the previous week. Of the total US cotton exports, around 120,700 bales were shipped to Vietnam, 77,700 bales to India and 29,000 bales to Turkey.
- UK-based Cotton Outlook raised its estimates for 2019-20 (Aug-Jul) global cotton crop estimate by 308,000 tn to 27.36 mln tn, led by likely increases in the US and Uzbekistan, according to the agency's latest report. The agency has raised the production estimate for the US by 303,000 tn to 5.04 mln tn.
- The agency has also raised its 2019-20 global cotton consumption view to 26.69 mln tn from 26.64 mln tn forecast in the previous month. Global ending stock levels of cotton are now seen at 667,000 tn, compared with 409,000 tn projected in April.

Foresight

Global cotton prices are seen up in the near-term because of the recent weather adversities. Heavy rains in the last few days saw plantations in Arkansas, Louisiana and Mississippi fall 10-20% behind their respective five-year averages, thus raising concerns. Rain has prevented growers from getting into fields in states including Oklahoma. In many areas of the Texas Panhandle, cotton is struggling after an extended period of rainy & cool weather. Wireworms are also active.

Going ahead, forecasts are calling for rainfall in most of the Cotton Belt over the next week, slowing planting and causing some concerns due to already saturated ground

Forward curve of Cotton futures (ICE)



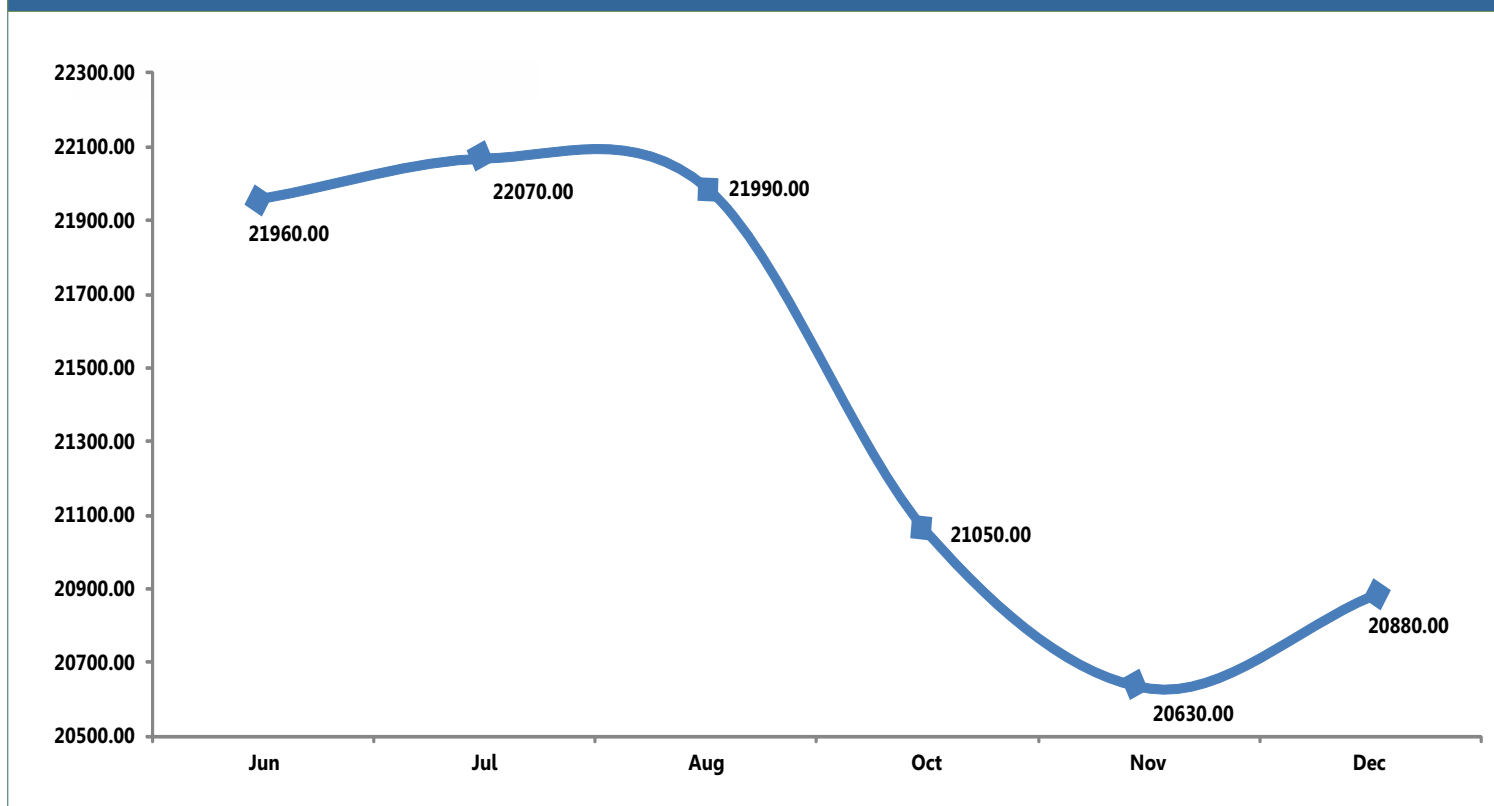
Source: Bar Chart

USDA reported cotton planting progress at 71% complete, a 14% move from last week. That is vs. the 72% average and 74% last year. The crop was also reported at 8% squared, vs. the normal pace of 7%.

The market participants would be definitely keeping a close watch on the the USDA planting report, which is scheduled to be released on June 28.

Also, Australia's cotton production has been halved this season with drought and low-to-no water allocation for most growers taking a toll on crops. While cotton picking and ginning was still underway throughout New South Wales and Queensland, Cotton Australia chief executive Adam Kay forecast the 2018/19 national crop would be around 2.1 million bales. The farmers there would have been more rain through the season with some inflows, but when that didn't happen they fell short with water and that impacted yields.

Forward curve of Cotton futures (MCX)



Source: MCX

In the domestic market, the market participants would keep a close watch on the progress of the monsoon, with sowing progress going on in the major growing states. Private weather forecaster Skymet has cautioned farmers in Maharashtra, Madhya Pradesh, Andhra Pradesh, and Telangana against early sowing of crops as the monsoon onset is going to be mild and the progress is expected to be sluggish.

Hence, for the time being, an upside could be seen in the cotton prices, due to the rising deficit between demand & supply.

The India Meteorological Department today maintained its forecast for southwest monsoon rains at 96% of the long-period average. The weather bureau has also forecast rainfall is likely to be 95% and 99% of the long-period average, respectively, in July and August. IMD said the average rainfall in June-September is likely to be 96% of the LPA, with a model error of +/-4%. In its first long-range forecast, too, the weather office had put the projection at 96% of LPA (+/-5%). The weather department will issue the next forecast at the end of July, after the monsoon covers the entire country.

Forward curve of Cotton futures (MCX)



Source: SMC Research

MCX Cotton has been in long term uptrend with the formation of higher highs and higher lows. The higher low at 19950 remains the key support for bulls in the short term and prices should not break below it. **As of now, prices are rebounding after retracing 61.8% of the previous fall from 24280 to 19950.** Break above 22470 can take counter towards 24500-24800. Dragonfly Doji pattern is identified on the monthly chart which also confirms that bull overpowers bear and prices will continue to move upward. As per the pattern, a small pullback is expected in the counter, confirmation of pattern only after prices breach the high of dragonfly doji. **Buying advised in MCX Cotton in June contract above 22470 with the target of 24500-24800.**

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