1982 Outlook for Cotton Markets and Marketing

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1981 was a very big disappointment for not only cotton growers but also cotton price forecasters. A year ago a very small expected carryover at the end of the 1980-81 marketing year was causing cotton prices to hold at relatively high levels and everyone expected the prices to stay high at least until the 1981 crop entered the market in large quantities.

The small expected carryover should have caused the December futures price to rise to 97 cents on April 1 of 1981. Instead the December futures price was less than 83 cents. Why the discrepancy between the expected price of 97 cents and actual price of 83 cents? It appears that essentially all of the discrepancy was caused by extremely high interest rates. Those interest rates were very high even after allowing for current rates of inflation. Low carryover normally makes it profitable to own inventories of cotton, but the high interest rates killed the normal speculative demand and cotton prices fell far short of the price normally implied by the small carryover.

To this writer the December futures price at 82 cents on April 1 meant that cotton prices would rise from April 1 to December 1, but the actual April 1 price of December futures was an inaccurate signal. The correct forecast----a substantial drop in cotton prices from April 1 to December 1----would have resulted from using the 97 cent price of December futures on April 1 that would normally result from the small carryover. Apparently the market responded to the low carryover (and implied price of 97 cents) rather than the actual December futures price at 82 cents.

What should we expect from the markets in 1982? Current expectations indicate that August 1, 1982, carryover will be about 5.5 million bales. That is a relatively high carryover and should hold December futures price down with reinforcement from continued high interest rates. While a continued low price of December futures is bad for those farmers who have not already sold all their 1981 crop, it does not point the way to higher cotton prices in the fall of 1982. The low December futures price in the spring results in a smaller cotton crop and increased cotton consumption.

The U.S. and most western economies are clearly in recessions and this is bad for the demand for cotton. The U.S. economy should begin to pull out of the recession by early summer of 1982, and this should be very visable by late summer or early fall. The Federal Reserve Board's tight money policy is making substantial progress in bringing down the rate of inflation, and this should allow interest rates to continue to fall until at least mid summer. The recovery from the recession and the falling interest rates are both positive factors for cotton prices as the harvest begins in the fall of 1982.

The probabilities seem to lie decidedly on the side that would have prices for 1982 crop cotton rise from early in the year to late in the year 1982. This suggests that forward contracting the 1982 crop would be a losing strategy. The recent history of forward contracting over the years 1973 through 1981 shows that in 6 of the 9 years cotton prices rose from spring to fall. 1974, 1977 and 1981 were the three years that prices fell from spring to fall and therefore, forward contracting resulted in higher average prices for Arizona cotton growers.

The dismal record of price forecasters in 1981 might logically lead to the conclusion that no one can consistently forecast cotton prices. Because producers and consumers of cotton respond to price signals from the futures market, the futures market has produced consistently bad forecasts of cotton prices. If the cotton producer believes that no one can forecast cotton prices with any meaningful accuracy, then his best strategy in selling his cotton is to distribute his sales of a given crop over at least an 18 month period. Forward contracting could begin in November or December before the crop is planted and cotton could be sold out of storage as late as May or June after it is harvested. The following article shows that forward contracting during the planting-period was the worst time for forward contracting during the years 1974-79.