Southern Cotton Growers, Inc.
REPRESENTING COTTON PRODUCERS THROUGHOUT ALABAMA, FLORIDA, GEORGIA, NORTH CAROLINA, SOUTH CAROLINA AND VIRGINIA

COTTON MARKETING NEWS

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Soaring Market Makes Decisions Tough

New crop Dec08 cotton futures closed today at 87.45 cents per lb—up limit (300 points) for the day and up 5.69 cents for the week. New crop prices have gained about 11 cents over the past 2 weeks.

The recent upsurge in price is hard to explain in terms of traditional supply and demand forces. Fundamentally, little has changed that would adequately explain the strong gain in prices. In fact, the most recent export numbers were down. We now have to wonder what this most recent surge in price will do to export demand.

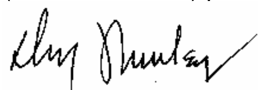
Industry sources seem to agree that this recent gain in price is due to an increase in "speculative buying". In other words, folks looking for something they consider still relatively cheap in which to put their money. We have to admit that with grains and soybean prices already escalated that cotton in the mid-70's seemed cheap. What about 90 cents-- is that now too high? We need to be reminded that the global supply/demand forces resulting in high grain and soybeans prices are not applicable to cotton although cotton must certainly compete for acres. Another factor to consider—should cotton futures prices remain in the 80's into spring, how might this impact planting decisions? Would it coax more acres into cotton? I would think so.

This surge in price, although we may not fully understand the reasons for it, is exactly what the cotton producer has been looking for. Many producers have said they need 80 cents or better for cotton to compete with corn and soybeans. Well, here it is………… but, now it seems producers are reluctant to pull the trigger. And you know what, I fully understand. Prices have moved so high, so fast that it makes us wonder just how much higher they could go.

How does the producer get protection from prices going lower and at the same time be in position to take advantage of the situation if prices go higher? I've had several calls over the past week or more and I suggested contracting at a fixed price then buying a cheap out-of-the-money December Call Option. That was a good strategy if followed at the time but the market has now moved so high now that I'm beginning to wonder about the continued feasibility of that strategy—i.e. it seems to me we now need to be more concerned about downside risk than further upside potential.

For producers who have yet to do anything on a portion of the expected '08 crop, now seems to be an opportune time to get started. Several producers I have talked to already have a very good basis quote (150 to 200 points under Dec08). One strategy would be to simply contract (fix a price) on a portion of expected production. If you're concerned about the market continuing to go up you could then also buy a cheap Call Option. But again, this strategy although it might work, doesn't seem as feasible as it did a week or 2 ago.

Another strategy would be to buy a December Put Option. Anything close to "at-the-money" is expensive, however. The purpose of a Put is to set a floor while leaving the upside open. Thus, something below the "floor" needs to have a reasonable chance of occurring in the market place. A floor at anything less than 70 to 72 cents seems impractical (see above chart) particularly considering the producer could possibly contact for around 85 cents per lb at present.



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