Volume 2 Number 27 July 9, 2004

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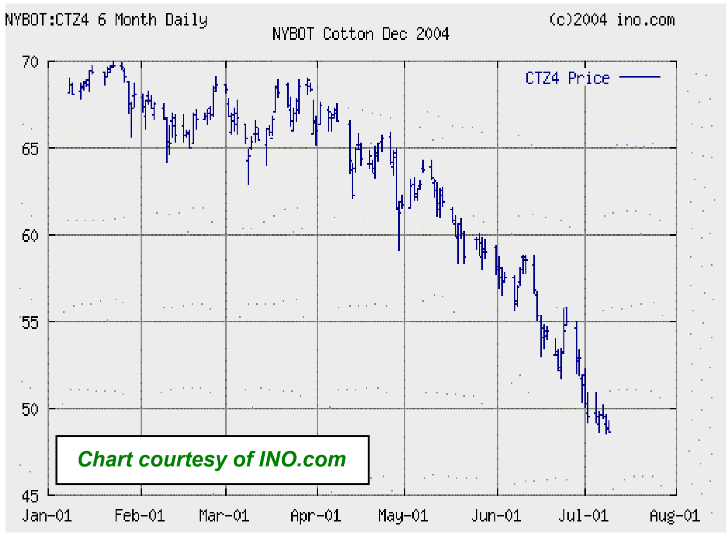


New crop prices (December futures) continue to trend downward under the pressure of the prospects for large US and world crops and simply the lack of buying support-- what might otherwise be called an "over-sold" situation.

Most observers and analysts continue to believe that a "correction" is due at some point and I'll continue to pitch my tent in that camp. But the downtrend since April is now so entrenched that it is doubtful any correction could be soon enough to get us back to where we'd like to be (something with a 6 in front of it) before harvest without a major new development in the supply and demand picture. So, in my opinion, producers must be patient and wait on such opportunities when and if they occur. With the market at these levels (roughly 45 cents basis December) relative to a 52-cent loan rate, there is no incentive to do otherwise. Some have asked about purchasing cheap out-of-the-money March or May Call Options with prices now at such low levels. This seems like a relatively low-risk move, but realize this is not hedging but speculating (gambling) on what you hope to be a move up in the market later on.

I have presented information similar to the table below in meetings and publications. It refers to what I call cotton's "no man's land". It makes 2 points about the cotton market under the 2002 farm bill-- (1) that producers can be worse off at higher prices and (2) on the 2004 crop we are already below the point of being impacted by what the cash market does.

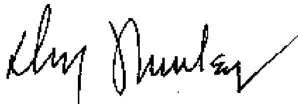
Futures Price	A-Index [1]	AWP [1]	LDP	Cash Price [2]	Total Cash+LDP	DP	CCP [3]	ALL TOTAL [4]
4000	4750	3290	1910	3600	5510	667	1373	7550
4500	5250	3790	1410	4100	5510	667	1373	7550
5000	5750	4290	910	4600	5510	667	1373	7550
5500	6250	4790	410	5100	5510	667	1373	7550
6000	6750	5290	0	5600	5600	667	973	7240
6500	7250	5790	0	6100	6100	667	473	7240
7000	7750	6290	0	6600	6600	667	0	7267
7500	8250	6790	0	7100	7100	667	0	7767

1/ Based on current price relationships. A-Index assumed to be 750 points above the nearby New York futures price and AWP assumed to be 1460 points below the A-Index. If this spread narrows (which it likely should), Total Cash+LDP will increase.
2/ Assumes a basis of –400 the futures price.
3/ Assumes the Marketing Year Average price (MYA) is equal to the cash price shown. DP and CCP are received on 85% of base acres times the DP and CCP yield.
4/ Total price plus all payments on actual acres harvested up to 85% of base acres at the DP and CCP yield.

When prices are low, whether you take the LDP or place cotton in loan and take the marketing loan gain, your total take home is really determined not by *prices* but by the *relationships* (spread) between US and world prices and the *formulas* built into the government payments.

When the AWP falls below the loan rate (52 cents/lb), the LDP increases at the same rate as cash prices decrease and total cash+LDP remains the same as long as the "spread" and basis remain the same. When cash prices increase above the loan rate, both the LDP and CCP are reduced and the total of price and all payments declines. There is a range of prices (futures) between the mid 50's and low 70's in which the producer may actually be worse off in terms of total price plus payments than if prices were lower (this range will differ slightly if the actual "spread" and basis are different than those assumed in the examples shown).

For pricing and risk management in terms of the 2004 crop, there is little that can be done at this point. Purchasing Call Options in anticipation of improving prices may be considered as a speculative move but would not be hedging and producers should know the risk involved. For remaining 2003 crop, the choices at this point appear to be (a) holding out for any remaining rally of 2-3 cents or so, (b) selling and purchasing a *very cheap* out-of-the money Call Option, or (c) selling and being done.



Don Shurley, University of Georgia
229-386-3512 / donshur@arches.uga.edu