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When we look in the rearview mirror, we can see plenty of curves in the dairy price pavement behind us. Looking ahead, we can see boulders made of “what if?” littering the landscape on either side. But these boulders are distractions. We’re still driving into the bearish headwind, so what’s important is that nothing huge blocks the road immediately ahead.

Of course, serious pressure on dairy prices persists. The Russian dairy ban remains intact. The Chinese have yet to come back to the market. Even when they do, it’s doubtful that they will hammer away at purchases as aggressively as before for fear of launching prices to the moon and repeating the history of 2014.

The EU production quotas that were in place for more than 30 years are now history, soon to be summed up on a roadside marker. With the traffic light green, modern dairies in Ireland, Germany, and a few other countries may step on the accelerator. At the same time, the U.S. Dollar remains strong and domestic production continues to increase year on year.

This bearish wind is blowing dark clouds across the road, so let’s switch on the fog lights and try to see what else lies ahead.

On one side, I see a pretty thorny thicket. On the other, there’s a more promising pasture. First, the thicket of margins...

Risk Management

Bear on the road. Corn on the mind. Bull in the brush?



By Brendan Curran
Risk Management Consultant
INTL FC Stone

Although I'm largely bearish on the corn market, a dynamic is shaping up that is worth a closer look. The progressive drought strangling California for the past 4 years has octopus arms that spread throughout the West and tendrils that penetrate the Great Plains and the Upper Midwest, reaching as far east as the Ohio River Valley.

Meanwhile, we're sitting on multi-year bumper crops that have gone into bins instead of going directly to market. Also, corn farmers feel pretty good about hanging onto much of their grain because, over the past few years, they've reinvested profits into on-farm storage. Not surprisingly, they want to take advantage of their supply leverage and play a waiting game, holding out for higher prices. However, this is a gamble that has yet to pay off. Corn prices have yet to recover to expected levels.

Nonetheless, we must expect that "rallies will be sold." A dry spring planting in the Corn Belt is going to heat up worries about both drought and diminished acreage. If weather becomes an issue this crop year and a rally ensues, it's going to put a big crimp in margins for dairy producers.

Lower farm gate milk prices, coupled with higher grain prices, are going to crank the dairy tornado siren. Producers who have held out for higher prices themselves, and are not hedged, may wish they had built stormproof shelter. At this juncture – with dairy prices under pressure, bearish headwinds pushing against us, and the risk of a bullish turn in the corn market – I cannot stress enough the value of a proactive risk management stance.

But enough of the gloom, because there is a brighter side to the market, shown in a "wild card" development beginning to take shape. This card is no ace or even a face card, so there's no reason or recommendation to "bet the ranch." I recommend and remain adamant in favor of hedging and managing risk.

However, let me point out that the U.S. Dollar has been on an absolute tear – an unabated rally that has taken it to levels not seen in over a decade. The strength of the greenback has contributed to a massive short position in the Euro, which has the hallmarks of a "short squeeze" in the making. Couple such a short squeeze with a very short, skewed position in the crude oil market, and we have what amounts to a "trifecta of repositioning" at a crossroads just ahead.

What exactly does this mean? Short covering in the Euro would be bearish for the U.S. Dollar and a move higher in crude oil would likely exacerbate that dynamic. This situation would translate to a positive effect for exports and may prove to be the catalyst for a turn in the market.

The bear has gorged voraciously already this year. But the bull lurks nearby, wary but wise in the unexpected ways of the dairy market. He longs to break through the brush and take a shot at goading the bear, sending him back into hibernation.



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