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Groundhog Day did not repeat itself this year. Just the opposite, it seemed. When traders woke up on that first Tuesday of February, it was partly cloudy and confusing. It felt like a Thursday. The markets had been up and down and all around so much that Spring still seemed a long ways off.

Just take a look at the recent price action witnessed in the U.S. Dollar Index, as well as major world currencies, stocks, crude oil, gold, and dairy for that matter. What do they all have in common? Volatility. Extreme volatility at that. You know the feeling. Like when you're leaning against the railing to get a good look a mile down into the Grand Canyon. Then somebody grabs you by the shoulders. Shudder!

The shakes

So where's all this commodity commotion headed and how can anybody make sense of it? You have to remember that everything in the markets is related to everything else to varying degrees – from the U.S. Dollar to crude oil to corn to dairy. If investor confidence gets the shakes and fund managers lose confidence in certain sectors, then watch out. We're watching the shakes play out in stocks, crude, and the greenback. So what about dairy?

It's certainly been an interesting start to 2016, especially in the international dairy markets. Butter and non-fat dry milk (NFDm) are running with rampant volatility while cheese watches with relative calm from the sidelines. How long will it last and where is this game headed? It's a function of cycles and external factors. The export arena remains shaky and suppressed, with the latest tallies from December down 20% from the previous year, cheese down 9%, total whey down 20%, and butterfat down a whopping 51%.

Risk Management

Dairy groundhog foresees partly cloudy near term



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Relatively tremor-free butter

Daunting as the export stats might seem, you have to respect the fact that domestic butter pricing has held in there with amazing resiliency. The disappointing export numbers are a direct result of the strength of the Dollar, as its high value in relation to other currencies makes U.S. goods more expensive for foreign entities to purchase. But domestic butter demand and the fear factor of losing opportunity remain strong enough to lend price support despite tribulations on the global scene.

At the same time, when it comes to domestic production, canny producers are taking advantage of nutritional technology to prolong the seasonal rise in milk fat concentration (see DV Monitors in this issue). Every farm is different, but diet formulation with an eye to optimize the seasonal trends in milk components may help some producers reinforce their bottom line in an overall down market.

That said, one has to wonder whether the overall bearish market dynamic has begun to wheeze to a halt. Over the past two weeks, the U.S. dollar has moved sharply lower as traders began to bail on the concept that "all is well" with the U.S. economy. Dovish comments from the U.S. Federal Reserve hint that the four rate hikes once expected for 2016 now seem so far to the back of the stove as to be in the fridge.

Greenback less than invincible?

The less-than-rosy economic outlook translates directly into a weaker U.S. dollar, which suddenly looks less than invincible. Also, there's the renewed slide in crude oil prices as commercial inventories set at 80-year highs. The rising tide of oil pushes the futures market lower and casts a shadow over the entire commodity countryside.

Yet markets are cyclical. At some point, low prices generate traction and those baby bull hooves dig in. We may be watching such a dynamic play out in the NFDM market now. NFDM prices may be getting some grip now that the forward curve had been flattened a bit. The silver lining is that NFDM exports are showing a recent spike of 36% compared to last year in December – possible confirmation that things are starting to turn.

I recall a wise mentor reminding me more than once: "Follow the powder and you have your answer." Therefore, we look for the day when the NFDM market fully corrects. When it does, it's likely be a "vacuum trade" that could lead the entire dairy complex out of the canyon shadows and back into the bright sunlight on the opposite slope.



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