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Insulated from chilly international market?

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It's a chill wind that blows across dairy markets across Europe and Oceania, keeping them in the deep freeze. A giant iceberg of milk supply is crushing prices, triggering farmer protests in European Union countries and intervention efforts in New Zealand.

Meanwhile, the U.S. dairy market seems insulated somehow from the frostbite conditions, especially with the butter market heating up in a parabolic rise to 2015 highs.

So where's the thermometer headed as we prepare for the twilight of 2015?

Many factors have piled up this year to steal heat from dairy demand and bring on the hypothermia that grips the international market. It's becoming a litany, but bears repeating: Abolition of the E.U. quota system; fallout from the Russian dairy and ag products ban on imports from nations that imposed sanctions because of military interference in Ukraine; the absence of Chinese purchases; and global macro economic shudders, including the ongoing Greek fiscal crisis, economic slowdown in China, and concern over knock-on effects in the U.S. economy. All of these factors have kept dairy prices in the freezer, but also beg the question: Has the mercury hit bottom yet?

As we approach 2016, there are glints of warmer times ahead shimmering on the horizon, although it's an arduous trek across the tundra in that direction. Consider the steps taken by Fonterra to lower product volumes on GDT (global dairy trade), which has thus far incentivized bidders and proven to be supportive to price action.

Consider also Fonterra's announcement forecasting production to slump by 2-3% for the 2015-16 season due to increased culling efforts. Add the possible negative impacts from El Niño. Altogether, these factors are likely to constrict the milk tap, leading to a supply side adjustment and a tightening of market fundamentals. That's why there's a case to be made that prices may stabilize and recover into 2016.

In our own backyard, the U.S. market remains a bit greener than anywhere abroad, as prices have kept above freezing with butter's meteoric rise, NFDM (non-fat dry milk) establishing baseline support, and Class III milk and cheese prices averting outright collapse. It's not that domestic prices are completely insulated against the international deep freeze; I assure you they are not. However, robust domestic demand has been the catalyst for our warmer prices. And, as long as this dynamic remains unchanged, it's entirely plausible that our domestic market remains shielded from the worst of the international freeze.

There's nothing in the rulebook – or in the current dairy market forecast – that mandates U.S. convergence with international prices. With hedge interest for 2016 on a steady rise, there's price support as end users scale into purchases. California and the western milk shed continue to confront the same issues that have plagued production for years with no relief in sight. That's additional price support. Now factor in what appears to be a paradigm shift in the attitude towards natural fat intake in the American diet. So it seems a case can be made that domestic demand for dairy products has found sustained, long-term support.

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