



FYI FROM FCI

Commodity Markets: This isn't ^{Just} Kansas, anymore!

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Remember when gas was under \$2.00/gallon, "Made in China" was only stamped on items in the discount bargain bin, and commodity markets were predictable? Times have changed and the big influencers of grain prices aren't in Kansas, or any other grain producing state. It used to be that supply and demand ruled the markets. Demand was a relatively known while supply was determined by acres planted, growing conditions, carry-over, and ultimately, harvest size. USDA market reports were influential and futures varied based on weather in the grain belt. The lowest price of the year could be expected in fall...simple, in comparison. Today's reality is that the markets are unpredictable. The factors influencing markets today are not new forces but are more influential and volatile, due largely to a globalized economy.

Demand

The biggest driver on the demand side is the competition from food and fuel for grain crops. An increasingly important factor is the influence capital investment funds can have on commodity markets.

Fuel. A new player has emerged on the demand side – energy. The glut of grains being consumed for ethanol and biodiesel production has vastly increased competition for grains both domestically and abroad. Corn is being converted to ethanol; soy, palm oil, tallow, and other products are being converted to bio-diesel (palm oil and tallow are sources of fat for animal rations). Two years ago, there were 50 ethanol plants in production; today, there are about 120 with 80 either expanding or in construction.

Food. Made in China? Or...consumed in China? The impact that small per capita consumption increases have in countries with large populations are HUGE! China and India's billions have the potential to impact demand for food grain and energy in ways never before experienced. As consumption in these countries increases, we can expect the impact to be felt in commodity markets.

Investment Funds. Although not end users, capital funds that invest in commodities markets are huge impactors of future prices and, therefore, commodities prices. There are VAST sums of money, controlled in large part by sophisticated computer models that, on any given day, can flood capital into, or out of, a given commodity. Factors influencing the computer models include:

- prices of other commodities (oil)

- prices of any stock, fund, or bond in any world market
- any other economic indicator included in the calculations of the computer model

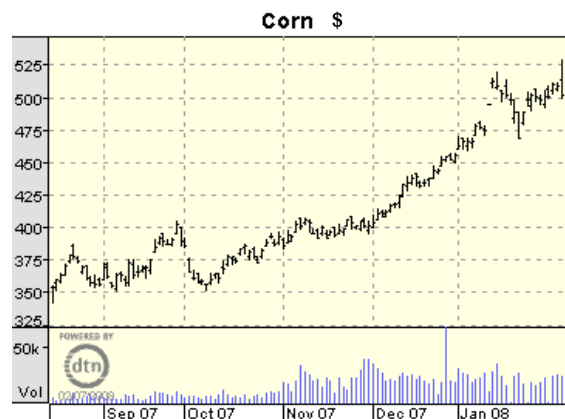
Supply

They're not making more land so, ultimately, grain production has a limit. However, the global scope of the markets mean growing conditions in China, India, South America, Australia, etc. can influence the US market. Different crops compete for the same acres. A bidding war ensues where the highest priced crop wins the most acres. The overall effect is to push all prices higher.

Why so Unpredictable? The reason markets are so unpredictable is that a seemingly minor event, anywhere in the world, not even directly related to agriculture can dramatically shift demand. Take, for example, what occurred in the run-up on grain prices that occurred last fall. Oil was hitting new record highs on a daily basis. Commodity investment fund computer models saw any commodity not at a record high as a relative bargain. Considering high demand for soy and corn, fund investors saw those commodities as a good alternative investment. Money poured in and prices of corn and soy soared. Factors that caused the record high oil prices include the following:

- unrest in the Middle East
- a hurricane in the Gulf of Mexico
- oil consumption by India and China
- OPEC policy

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Commodity Markets Continued...

What influenced the demand for ethanol and bio-diesel? – a political policy that supports them.

The number of factors to consider are numerous. What would happen in the following scenarios:

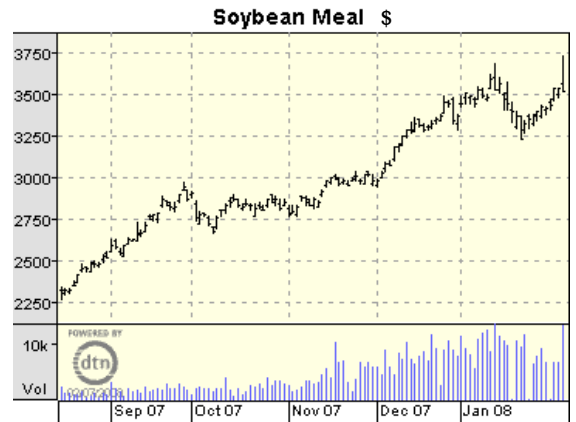
- A recession in India/China causing decreased consumption in those countries?
- A stronger or weaker dollar?
- A change in Middle East dynamics?
- Tension with Iran?
- The new farm bill?

Consider the impact the sub-prime crisis has had on the value of the dollar and resulting impact on global demand for US grain. These are factors that never before seemed to impact grain prices. Today they are big influencers.

What Should a Dairyman Do?

One thing is certain, NO ONE can predict the markets. You cannot know when the bottom will come, only that it has passed. What does that mean for booking strategy? Should you bother to book? It depends on your risk tolerance because booking is really just this – risk management. Markets are more volatile and they will vary more.

With greater increase expected in demand than supply in the foreseeable future, prices overall are expected to rise. Booking means creating a known in a world of unknowns. Determine a grain price that will be profitable for you within the coming year's expected market range and when the market gets nearer that number, buy all or a portion – don't attempt to win the lottery by trying to pick the low. If you really like to gamble go to Las Vegas, otherwise, book at a price that you can live with, then move on and don't second guess yourself.



PA Dept. of Ag Backpedals.

G. Weber

The Pennsylvania Department of Agriculture has taken a step back from its hard line on dairy labeling. After consultations between the Secretary of Agriculture, the governor, and public response, Pennsylvania will allow labels that state products are produced without rBST. The label must, however, include language stating that rBST is safe and any processor using such a label must legally document that rBST was not used.

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