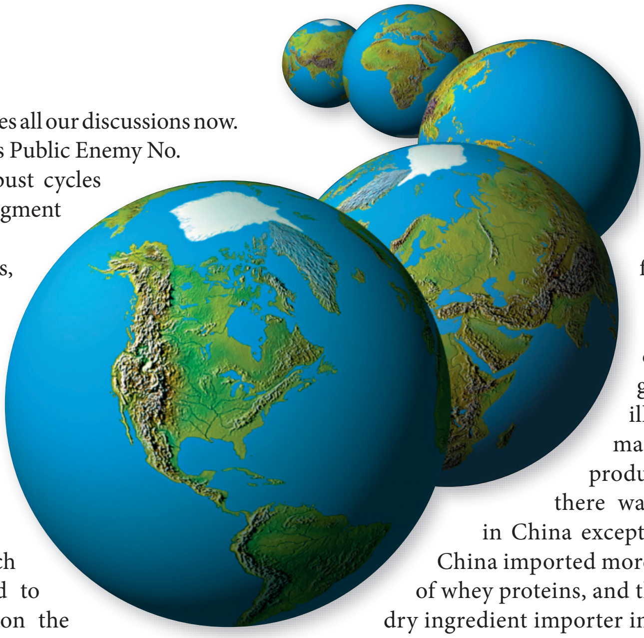
Tom Suber

The 'V' Word



Whipsaw price volatility frames all our discussions now. It has been characterized as Public Enemy No. 1, with continual boom-bust cycles wreaking havoc on every segment of the dairy supply chain.

While we're having these conversations, remember that dairy price volatility is a global issue now. If we've learned anything over the last few years, it's that the U.S. industry is no longer insulated from international drivers and factors.

Here's the thing: Everyone who has looked at the issue concludes that price volatility will continue. That's the nature of commodity markets. Other commodities have dealt with it for much longer, so they've become accustomed to using risk management tools. Dairy, on the other hand, is still learning. And there is no shortage of proposed solutions.

At this year's American Dairy Products Institute annual conference, Phil Plourd, president of Blimling & Associates, summed up the challenge this way: "You can manage volatility in one of two ways – industry-wide or on an individual basis. Risk management won't reduce industry-wide volatility, but it may reduce volatility for each individual."

Decisions by individuals would better suit dairy's diverse supply chain without the many complications that usually accompany attempts at suppressing industry-wide volatility.

So while some are looking at new systems that promise greater overall sector stability, others are looking at risk-management tools that might smooth out the highs and lows for individual processors, exporters, food companies, retailers, foodservice operators, farmers and consumers.

One of the templates I've referred to in past columns is the Globalization Study, a comprehensive look at how the U.S. industry might accommodate globalization, conducted by the Innovation Center for U.S. Dairy (IC) with support from management consultants Bain & Co.

Volatility is one of the key themes of the report. "The way the United States plays in the global market will have a significant impact on volatility," says a white paper developed from the study. "A more proactive attempt to maintain a higher export presence may lead to less volatility."

Just to be clear, this is not to suggest that becoming a more consistent exporter, or simply exporting more, will eliminate commodity price volatility. Exporting more, or less, would not have prevented the wide price swings we've endured the last four years.

In fact, increased exposure to global forces has made us more vulnerable to global booms and busts. But that's not because we're exporting more, though indeed we are. It's the result of many long-term trends that have been in motion for decades, encompassing changes in technology, logistics, living standards, dietary habits and government policies. To illustrate, think about one market – China – and one product – whey. Ten years ago there was little market for whey in China except in swine feed. Last year, China imported more than 600 million pounds of whey proteins, and the country was the largest dry ingredient importer in the world.

Volatility can't be legislated, regulated or wished away; it's an inherent trait of an increasingly globalized industry. Therefore, it's incumbent on the industry to address it in a global context.

"It has got to happen. At some point this industry has to get control of itself."

– Tom Vilsack

U.S. Secretary of Agriculture, April 13, 2010

The IC's Global Operating Committee formed a Volatility Subcommittee to help the U.S. industry develop and use risk management tools as a competitive advantage. They're brainstorming alternative methods of price discovery, looking at how to boost liquidity in existing contracts and conducting educational programs to get more participation.

Expect to hear more about this initiative in the months ahead. We've seen other sectors use hedging tools to take out the highs and lows, while simultaneously helping all players in the supply chain from farm to fork.

Ultimately we hope to use these tools as a competitive strength, giving us an advantage with global buyers both here and abroad who will be drawn to sources where pricing risk can be accommodated. It's something everyone in the industry wants – all the way up to the secretary of agriculture – and now necessity is forcing us to come up with solutions. ■

Tom Suber is president of the U.S. Dairy Export Council.