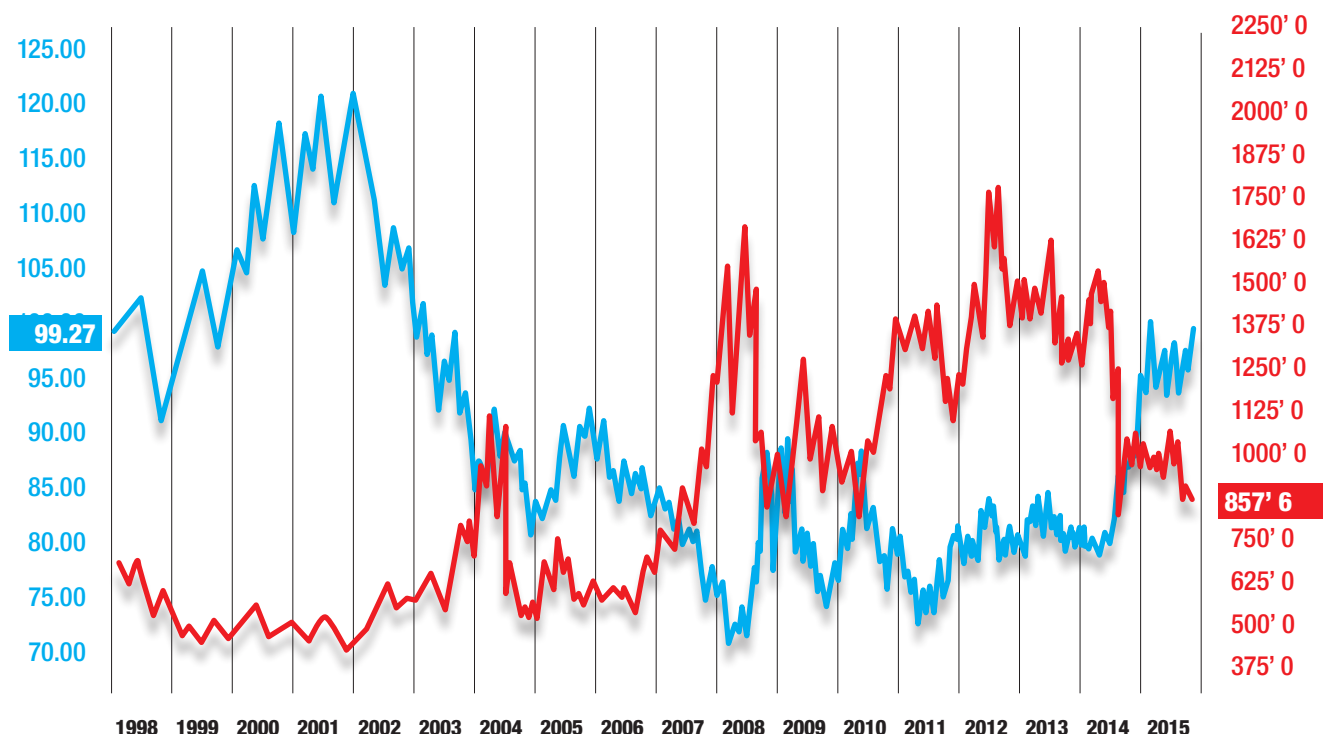


By Al Kluis

Monthly U.S. Dollar Index

Monthly CBOT Soybeans



DUE THIS YEAR: LONG-TERM LOWS IN FARM PRICES AND PROFITS

HERE'S WHY THIS WILL NOT BE A REPEAT OF THE 1980s.

As a young trader in the bull markets between 1974 and 1980, I was riding high. I was farming, trading grain, and advising farmers. Life was good. Then came 1983.

In 1983, the first lows started to arrive in the markets. In 1985, the super-bear market landed on our heads. In 1986, we were at the bottom of the price pit. The hard down in farm prices, farm profits, and land values fed into the collapse in the farm economy.

The good news: Two years of volatile bear markets (1985 and 1986) taught me more about the business of grain trading – and life – than any college class I could ever take.

Here are four big lessons I learned.

1 When the dollar goes higher, grain and meat exports will slow down.

above: This is the monthly chart of the U.S. dollar index (the blue line) and the monthly soybean continuation chart (the red line). You can see this is an inverse relationship, which means when the dollar is low, soybeans are almost always high.

When the dollar is high (like now), the price of soybeans is low. The good news is, the dollar does not stay high forever and the soybean market does not stay low forever. Right now, the grain trade and almost everything you read online is bearish.

Some farmers made panic sales back in November on the fear it would continue to go lower. Look at the chart and you can see how wrong and dangerous that decision could be.

2 When export markets slow down, farm prices get hit.

3 If prices and profits move below the cost of production for two consecutive years, it is impossible to work hard enough or to grow enough larger crops to make money.

4 In good years, this is the time to add to capital reserves. In down years, stay liquid.

WHAT DOES THE FUTURE HOLD?

At my many seminars this winter, I got a lot of requests asking me to compare today with the 1980s. My reply was always the same: This is not the 1980s, and I do not look for a repeat of the 1980s.

Instead, I expect a major upswing later this year or during the first half of 2017. Why do I think this? ▶

What is different this time? I can point to the following three main reasons.

1 Ethanol. In the mid 1980s, I had not heard of ethanol. Who had? The industry only started in 2005. How times change.

In 2015, it will have consumed 38% of the U.S. corn crop. This is a huge fundamental change in the demand equation for all U.S. crop farmers. This will limit how far corn can go down, and it is a very positive long-term fundamental for corn futures and basis.

2 China. China's economy has grown like a weed. In 1985, it was worth \$100 billion. Today, it is worth over \$10 trillion dollars.

This fast growth has made it the largest buyer in the world for cement, steel, copper, a host of other industrial commodities, and soybeans. The economic growth in China has slowed down, but it still is tremendous.

The demand for protein – especially soybeans – continues to grow.

3 Commodities as an asset class. Since 2005, Wall Street trading firms have started to look at commodities as

another asset class.

A well-rounded portfolio will now include stocks, bonds, and alternative investments including commodities. This has added to the volume of trading and the volatility in the grain and livestock markets.

You may not always like the volatility that these commodity funds created, but they will continue to be a major market factor in both the grain and livestock markets.

THE LIGHT AT THE END OF THE TUNNEL

In this time of low prices, there is a glimmer of hope. I believe the following factors will cause prices to turn higher.

• **Demand.** Believe it or not, price works.

With lower prices, the total amount of acres planted around the world started to drop in 2015. It will likely be lower again in 2016.

To top it off, since many farmers cut back on inputs, any weather problems that develop will have a huge impact on yields.

• **Weather.** Global crops are vulnerable in two very specific time windows.

First, this winter in South America (which is like summer in the U.S.) has the potential for being too dry. Odds of another great crop in 2016 are very remote.

Second, during the spring 2016 in the U.S., there are El Niño concerns. If the current very strong El Niño weather

pattern turns to a La Niña by later this winter or early spring, then it usually results in a below-trendline yield.

• Fund positioning.

Commodity funds are momentum traders. This means they buy on strength and sell on weakness. This sounds irrational, and it is.

In the choppy markets the last two years, it has created some huge losses for funds.

As I write this column in late November, funds are holding a huge short position. When they eventually swing around to the long side, it can create a big rally.

Just think back to what happened in the grain markets from late June to early July 2015. There was an 80¢ rally – right after the funds built a huge short position. **SL**

NOTE: Trading of futures and options has substantial financial risk of loss and is not for all investors.

AL KLUIS Commodity Trader

Al Kluis has been trading grain futures since 1974. Sign up for a free trial to his daily morning email and weekly "Al Kluis Report" by going to alkluis.com.



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