NOT IF, BUT HOW

Munich RE

Contingent price index

Financial instruments to protect agricultural companies against economic losses due to adverse price movements in a low crop yield environment

Munich Re is a market leader in assessing and mitigating financial risks caused by natural catastrophes, weather variability, crop yield and price fluctuations.

Current situation

Hedging instruments are conventionally exchange-traded futures or options. These off-the-shelf products have a **limited flexibility** when it comes to limits and payouts. While futures can cause companies to experience **financial distress** due to unforeseen margin calls, options provide only **low liquidity.**

Challenge

Cash flow sensitive clients are prone to opting for traditional hedging instruments. However, futures contracts can be **operationally challenging** to manage because of margin calls and rollovers. On the other hand, with options, clients **pay for all potential adverse price movements,** although they might need such a hedge only in conjunction with adverse weather events.

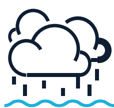
Solution

Contingent prices are unique coverages tailored to the client's specific exposure. They protect against predefined adverse price movements **only** when crop yields are poor **and** prices hit a certain threshold. In addition to their flexible contract size, since they are **triggered only when the client really needs them,** the pricing of contingent price coverages is more economical than standard futures and option transactions.

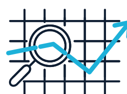
What is contingent price coverage?

Contingent price coverage (CPC) is an over-the-counter financial instrument, which compensates for bad local weather combined with adverse price developments.

How does CPC work?



Adverse weather event
Independent indices fall below a pre-agreed threshold



Adverse price developments
Established reference markets are trading above the predefined price

Payout
Payout = Price increase x tick size*

*Indemnification for each cent of price movement

Where and for which crops is it available?
It is available for all major cash crops in North America, Latin America and Europe, for which a liquid futures market exists as reference.

Who can benefit from CPC?
Anyone along the agricultural value chain, such as input suppliers, banks, investment funds, cooperative farms, grain off-takers, mills and crushers and other processors.
CPC can be structured to either protect cash flows, profits or the balance sheet.

What's in for you?

Innovative
Tailor your price hedges only for those situations in which you really need them

Flexible
Match the coverage with your individual risk limits

Transparent
Determine the payout using all major future markets as unbiased reference

Effective
Save money compared to traditional price hedges

Example
The payout is triggered by a defined yield proxy (e.g. area yield, modeled yield, NDVI, etc.). The actual payment is derived from exchange traded futures from CME and EuroNext.

Crop	Corn (e.g. 20,000ha)
Maxium cover	20,000,000 USD
Trigger 1	Modeled yield corn*; < 8t/ha
Trigger 2	Harvest price CME-Corn; > 5,00USD/bu
Payout	Trigger 1 <8t/ha **AND** Trigger 2 > 5,00USD/bu
Price limit	2,00 USD/bu
Exhaust	7,00 USD/bu

* This can be any pre-agreed index

Payout matrix in USD

Yield (t/ha) \ Price (USD/bu)	5	5,5	6	6,5	7	7,5	8
8	–	–	–	–	–	–	–
7,5	–	625,000	1,250,000	1,875,000	2,500,000	2,500,000	2,500,000
7	–	1,250,000	2,500,000	3,750,000	5,000,000	5,000,000	5,000,000
6,5	–	1,875,000	3,750,000	5,625,000	7,500,000	7,500,000	7,500,000
6	–	2,500,000	5,000,000	7,500,000	10,000,000	10,000,000	10,000,000
5,5	–	3,125,000	6,250,000	9,375,000	12,500,000	12,500,000	12,500,000
5	–	3,750,000	7,500,000	11,250,000	15,000,000	15,000,000	15,000,000
4,5	–	4,375,000	8,750,000	13,125,000	17,500,000	17,500,000	17,500,000
4	–	5,000,000	10,000,000	15,000,000	20,000,000	20,000,000	20,000,000

For more information visit our website:
www.munichre.com/crop-yield

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