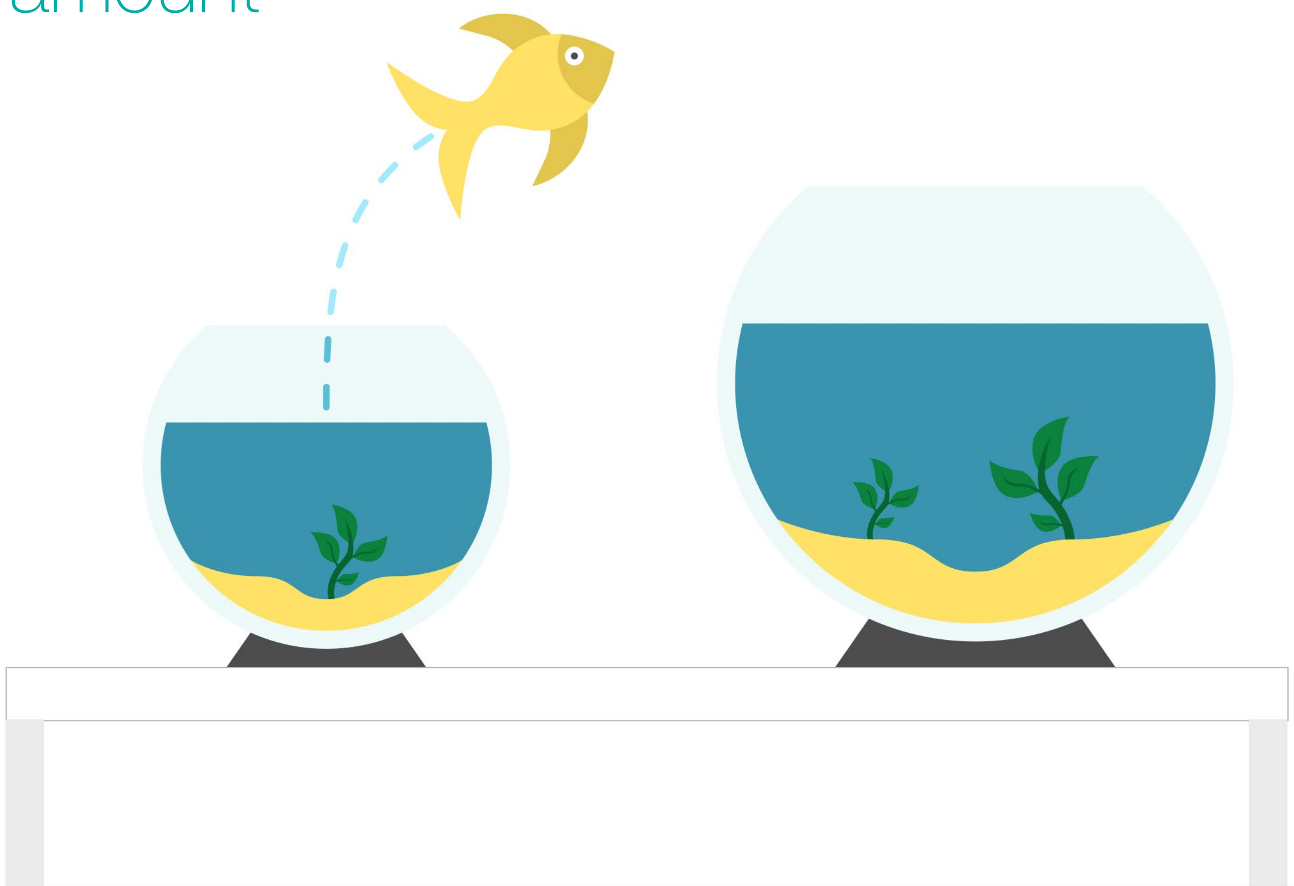
Risk and Reward

Start

What is Risk and Reward

Simply stated,

Risk and Reward is what you expect to make versus the amount you could lose.



Importance of Risk and Reward

Why is Risk and Reward an important concept and mindset?

- It provides an evaluation of both the gain and loss scenarios.
- It instills discipline in the process and evaluation of market opportunities.
- It enables calibration and comparison of different activities.
- It aligns risk appetite and sizing when evaluating market opportunities.

Relevance of Risk and Reward at Cargill

How is Risk and Reward relevant at Cargill?

01
It allows the organization to optimise the allocation of risk capital in order to achieve higher rates of return.

02
It enables us to test whether a hypothesis plays out and to improve our analyses and assessment.

03
It assists in ensuring the proper sizing of positions based on conviction levels.

04
It allows for the development of a framework for evaluating profit and loss scenarios under different market scenarios.

05
It aligns with the CRC expectations of holistic opportunity assessments to better evaluate limit requests.

Strengths and Weaknesses

Strengths

+

- Promotes a good risk culture by focusing on both the upside and downside earnings scenarios
- Useful as a communication tool to assist in understanding positive and negative scenarios
- Provides an ability to evaluate competing market opportunities
- Assists in challenging conviction and sizing

Weaknesses

-

- Simplistic assessment
- Specified outcomes may not materialize
- Assessments are not fixed and can change as market factors materialize
- Subjective in nature and can have inherent bias

Trading and Risk Management Performance

How does a Risk and Reward mindset support Trading and Risk Management performance?

Risk and Reward analysis provides an ability to evaluate and compare market opportunities and help to ensure that we are optimizing the right opportunities.

Select the button to view an example.

Example

Cargill

Trading and Risk Management Performance

Example

Assume a trader has a short position of 1mm bushels of corn which is currently trading at $3.50/bushel.

The trader believes that corn could trade to a low of $3.10/bushel and a high of $3.70/bushel.

If these ranges are realized he could potentially make $400k or lose $200k.

This represents a reward vs risk of 2:1. In this example, the position has higher upside potential relative to downside losses.

✓ Short position of 1mm bushels
✓ Current Trading Price - $3.50/bushel

$3.70/bushel

$3.10/bushel

Risk and Reward

- Potential reward = $400,000 = ($0.40 x 1,000,000 bushels)
- Potential risk = $200,000 = ($0.20 x 1,000,000 bushels)
- Represents a relative return vs the risk of 2:1
- The position has a higher potential reward vs risk

Application of Risk and Reward at Cargill

Select the play icon to watch the video in new browser window.

Summary

This concludes the module on Risk and Reward.

You have now learned:

1 Definitions for Risk and Reward

2 Importance, relevance, strengths and weaknesses of Risk and Reward at Cargill

We thank you for your engagement in learning about Cargill's risk practices.

If you have any questions about how to properly assess the risk and reward of a commodity-related opportunity, please contact your business or function's RMG partner.