Ways to mitigate ag weather risk evolve

By **Ian Hart**

MULTI-peril agriculture insurance is set to become of greater importance to the European agribusiness as it looks to manage risk presented by hail, flooding, frost and other weather events.

Meeting in Paris, France, the Weather Risk Management Association (WRMA) appropriately focused attention on agriculture at its 10th European meeting.

In 2008, the EU made alterations in its crop, animal and plant insurance programmes, allowing member states to fund a certain portion of the insurance. Since then private insurance companies and state entities have been seeking to develop risk management beyond hail insurance – the most commonly used tool among farmers in France, the EU's top agricultural producer.

One new tool being developed is multi peril crop insurance. While hail is a random event a long loss history and experience in loss assessment mean it is easier to reinsure than storms, flooding or frost.

Jean-Christophe Garaix of Paris RE noted these events are problematic because they are somewhat predictable on a mid-term basis, exposure depends on relief and/or type of soil, very widely spread geographically, difficult to assess losses if different perils hit successively the same crop and finally there is not a perfect correlation between climatic data and actual loss on crop yields.

For developed countries Mr Garaix suggested a traditional insurance product with a payment based on valued damages may be more relevant though there are some loss adjustment issues, while for developing countries (and some agro industry and co-operatives) indices such as a weather index, satellite/biomass index or yield index may prove better. Finally revenue cover, which is based on yield multiplied by price, could be used.

Due to the need for significant historical meteorological, soil, relief and hydrological data, much of which crosses administrative borders, public-private co-operation has yielded the best results. This means at least 40% of the direct premium is subsidised and a specific state agency organises and controls the system, while for the insurer, statistical data, policy wording and insurance terms are gathered or designed globally for the whole market. Thus, there is some thought among WRMA members that an EU-wide risk management programme might have benefits for the EU agribusiness sector.

Carina Folkeson, of the European Commission's (EC) DG-Agri, explained that EU-wide schemes being analysed include crop insurance premia subsidy, the development of mutual funds and income stabilisation schemes. But she clarified that there is no European Council preference for any of the options, their introduction should not undermine national systems, they must comply with WTO "green box" criteria, they should be within budget limitations and joint responsibility is vital.

The state of the European weather derivatives market remains strong. While agribusiness interest is on the rise, the biggest users of weather risk management tools are in the UK, due to the natural gas market, followed by France and Germany. "There's potential for the Scandinavian weather markets to be large and Spain, due to drought and rainfall, could be a large market as well," concluded the WRMA.

Dogmatic US regulatory push could backfire

IT is "almost inevitable" US regulators will impose position limits in US commodity derivative markets but there could be a host of unwanted side effects, warned a leading official from JP Morgan.

James Proudlock, commodity product head for Europe, Middle East and Africa, futures and option, at JP Morgan, said that the sector would become regulated like never before as politicians seek transparency and control over money flows into the markets.

There was approximately $240bn in commodity assets under management at the end of October, with exchange traded futures seeing massive growth to $92bn, while active funds have eased to $18bn from a peak of $27bn. Precious metals like gold and silver have been the main beneficiaries ($61bn) while agricultural commodities have seen modest inflows. Even so, US politicians needed to blame someone for the 2008 peak in prices, he said.

"There is a huge move to take bilateral deals and put them on a transparent platform," Mr Proudlock said at the International Sugar Organisation seminar. "The questions politicians are seeking to answer are how to limit 'too big to fail', how to prevent systemic risk of one constituent from falling over and how to safeguard our people."

This has not gone down well among investors. "As investors we will be trading political dogma with one, maybe two hands, tied by the politics," said Mr Proudlock. "Position limits are almost inevitable."

For the over the counter markets, this has margin implications as firms would have to stump up funds each day the market goes against them. However, some progress is being made at allowing companies to monetise inventories, for example.

But Mr Proudlock warned of unwanted consequences from the policy, saying: "It will probably lead to the opposite of what politicians are seeking. Investors will find another way to do it and it will be worse long-term than having something very liquid. If, for example, investors like sovereign funds start taking stakes in the physical chain, the people start looking at self-sufficiency, which is an inefficient allocation of resources."

Do not ignore freight risk

FREIGHT rates will see more volatility in the coming years and sugar players should act now to limit the impact, Alex Gray, chief executive of Clarkson Securities, said at the International Sugar Organisation seminar.

He noted that sharp moves in sugar freight have added $1bn to the delivered cost of sugar in the past few years. "That's a very high figure to my mind and with seaborne volumes only likely to grow, you have to question why it is only the major commodity players that are in the derivatives market hedging that risk every day." he said.

He noted there are swap contracts available for all size of dry bulk vessels. "If you're not managing your freight risk, someone else is and they are selling at a better price than you," he warned.

people and places

NEWEDGE has promoted former Liffe trader John Ruskin to lead its trading business as it looks to capitalise on the shift of over-the-counter products to exchanges.

RICHARD Clark plans to step down as vice president and controller of Monsanto on December 7. Mr Clark will then serve as special assistant to Monsanto's chief financial officer Carl Casale, until Mr Clark retires on January 29, 2010. Nicole Ringenberg, currently the company's vice president of finance for its seeds and traits business, is expected to be appointed to succeed Mr Clark as vice president and controller in December.

THE American Coalition for Ethanol (ACE) has elected new officers for the coming year. Lars Herseth will be president, taking over from acting president Brian Wilcox, who will now become vice president. Owen Jones has been re-elected treasurer. Duane Kristensen has been named secretary.

FRANCISCO Castaner, executive vice president of human resources, centre administration, pharmaceutical and cosmetic products, will retire on December 31 2009 after a career with Nestle spanning 45 years. He will be replaced by Jean-Marc Duvoisin.

trading brief

CME has gone back on plans to limit the amount of vomitoxin in maize delivered against its Chicago Board of Trade contract following "consultations with our customers and further studies on vomitoxin". The move comes days before the December maize contract goes into delivery mode.