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ALASKA

ALASKA RIGHTRISK NEWS

Risk Scenario Planning
from RightRisk.org

Production agriculture is a rough business. Profit margins are razor thin for many commodities, input costs continue to climb, markets are unstable, and the potential for failure seems to be increasing.

Drafting a solid risk management plan to help manage risk exposure and account for uncertainty is imperative. Planning should include partial budgets for alternative strategies. Partial budgeting comes in many forms and is a method often used to evaluate potential changes to an enterprise. This change could include anything from a cropping change, keeping extra breeding livestock, or a capital purchase.
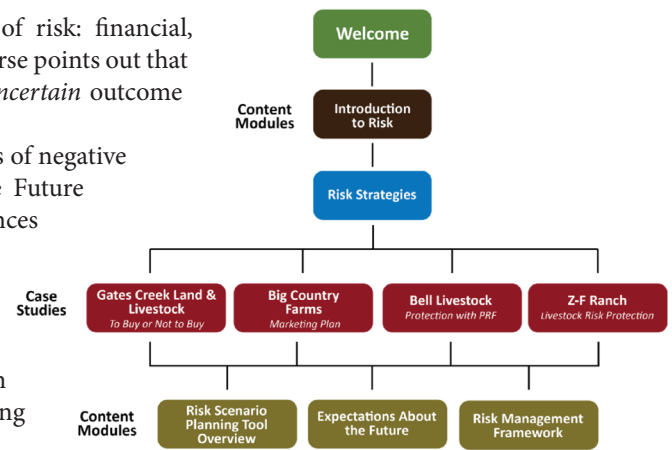
Risk Scenario Planning

RightRisk.org has developed a *Risk Scenario Planning* (RSP) tool and companion RSP course to help identify sources of business risk and uncertainty, as well as learn how to use the RSP tool to manage the risk. The RSP course has three primary modules, including four case studies highlighting how the RSP tool can be used in the partial budgeting process.

The course begins with an overview of the different types of risk: financial, production, human, institutional, and marketing/price risks. The course points out that risk doesn't necessarily imply a negative outcome, but instead an *uncertain* outcome that could be positive, negative, or neutral.

The point of risk management planning is to reduce the chances of negative outcomes and increase the chances for positive outcomes. In the Future Expectations module, the course describes three risk preferences (seeking, neutral, averse) and outlines many risk biases than can influence decisions. The Risk Management Framework module discusses how to implement a risk management culture in a business. Effective risk management should be viewed as a competitive advantage, proactive, a priority, and an integral part of an organization. Risk management should be as much about maximizing positive opportunities as it is about minimizing negative outcomes.

The course highlights each level of the risk management framework and how to begin following the approach it suggests when making management decisions. The Future Expectation module explores factors that influence decision-making associated with risk. Factors that contribute to uncertainty such as risk attitudes and human factors are discussed. Decision makers are often classified as risk averse, neutral, or risk loving (seeking). The biases and heuristics that affect our decision-making are covered. Emphasis is made on how to identify these factors affecting decisions and how to account for them.

Risk Scenario Planning Course Modules
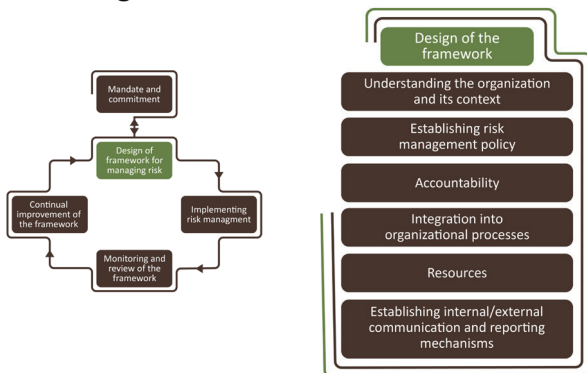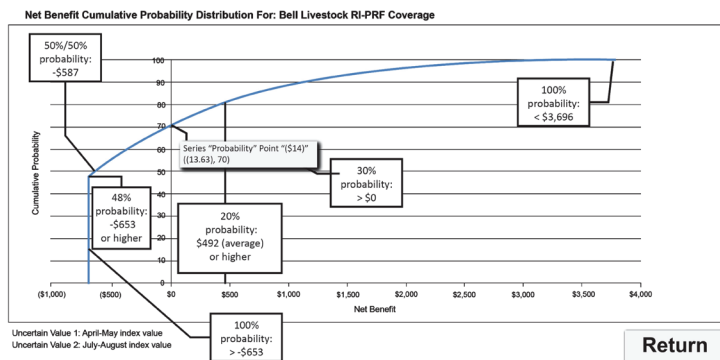

The RSP Tool

The third module in the RSP course highlights the *Risk Scenario Planning* (RSP) tool, designed to offer users a comprehensive view into partial budget analysis. The risk analytics tool entries are designed in the form of a typical partial budget, including sections for any added and reduced costs and returns. The analysis section of the tool is unique where it allows users to evaluate the effects of the changes introduced by one or two uncertain variables. The problem with many traditional partial budgets is that many of the variables being considered are imperfect, where the inherent risk in the assumptions used are not accounted for.

Risk Management Framework

How Much Risk is Right for You?

For example, if you are looking at changing from one crop to another, what price for the new crop production should be used? If this price changes, how will it affect the decision-making process when considering the partial budget results? The RSP tool was designed to account for some of this uncertainty by assigning a range of probable outcomes associated with a change in one or two variables. In this way, it can help users account for variability as they consider alternative management strategies by considering the effects on the bottom-line and ultimately resulting in better-informed management decisions.

This unique feature allows a range of estimates (minimum, maximum, and most likely) for up to two variables under consideration. The tool then generates a probability distribution describing the range of potential outcomes. Users can view a range of possible outcomes from the analysis, providing a much clearer understanding of the scope of potential decisions and associated results than possible when using best-guesses.

Partial Budget Framework

Added Returns	Added Costs
Reduced Costs	Reduced Returns

RSP Tool Example Output

Net Benefit Cumulative Probability Distribution For: Bell Livestock RI-PRF Coverage

50%/50% probability: ~$587
100% probability: < $3,696
Series "Probability" Point "($14)" ((13.63), 70)
30% probability: > $0
48% probability: ~$653 or higher
20% probability: $492 (average) or higher
100% probability: > ~$653

Uncertain Value 1: April-May index value
Uncertain Value 2: July-August index value

Return

Case Study Examples

The RSP course includes four case-studies offering crop and livestock production examples. Big Country Farms highlights wheat producers examining marketing plans for their wheat crop. They use the RSP tool to examine a strategy of forward contracting some of their wheat crop as compared to their historic cash sales approach.

Gates Creek Land and Livestock uses the RSP tool to examine the feasibility of trading-up to a newer windrower and the opportunities that accompany that potential purchase.

Bell Livestock shows how the RSP tool can be used to examine a potential insurance decision: Pasture, Rangeland, Forage-Rainfall Index (RI-PRF) in this case. The example describes how to input historic data from the Risk Management Agency (RMA) online RI-PRF Decision Tool into the RSP and evaluate the likelihood of indemnities at various coverage levels.

The final case study, Z-F Ranch, offers an example on how the RSP tool can be used to examine a Livestock Risk Protection (LRP) insurance decision.

For More Information

The RSP course is just one of many online courses covering risk management topics ranging from estate and legacy planning to financial management.

Visit **RightRisk.org** to access the *Risk Scenario Planning* course under the Courses tab, or view one of the many resources available, including: The *Risk Scenario Planning* tool, producer profiles, recorded presentations, and other materials to gain insights into developing a viable risk management strategy to meet today's challenges.

RightRisk ANALYTICS

Risk Scenario Planner
Machine Risk Calculator
Forage Risk Analyzer
Enterprise Risk Analyzer
RD Financial
Multi-Temporal Risk Analysis
Risk Navigator Toolbox

RightRisk Analytics is a toolbox of alternative risk analysis tools.

Click one of the buttons on the left to learn more about what each tool can do and to access the tool.

PROFIT / LOSS / RISK

Tool Support

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How much risk is right for you and your operation?

RightRisk helps decision-makers discover innovative and effective risk management solutions

RightRisk News is brought to you by the RightRisk Team

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