COLLAPSE of MGRM

WHO WAS MGRM
- 1A&Bacardi, Cuba, 2009-2011
- 1B&Panama, Panama, 2012-2014
- 2A&Bacardi, Cuba, 2011-2012
- 3A&Bacardi, Cuba, 2012-2013
- 3B&MGRM, Panama, 2014-2015
- 4A&MGRM, Panama, 2012-2014
- 4B&MGRM, Panama, 2014-2015
- 5A&MGRM, Panama, 2012-2014
- 5B&MGRM, Panama, 2014-2015
- 6A&MGRM, Panama, 2012-2014
- 6B&MGRM, Panama, 2014-2015

WHAT WENT WRONG
- False assumption of market dominance
- Inadequate strategy development
- Unrealistic expectations of duration
- High-level engagement, but not enough
- Limited resources, workforce, and capital
- High level of challenges and obstacles
- Misalignment of strategy goals
- Limited role by management

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COLLAPSE of MGRM

WHO WAS MGRM
- Who failed to take full advantage of the
  potential of the MGRM
- Situation as of January 2007
- Lack of planning and analysis

WHAT WENT WRONG
- Assumptions of maintainers of security were mistaken
- tunnel was not identified as the open
  source
- Critical bug discovered in May 2007
- Tunnel widened until it could not
  be plugged
- Crack in the window

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WHO WAS MGRM

- Metallgesellschaft Refining and Market
- Germany Energy subsidiary of MG
  - specialized in oil trading
- Owned 49% of Castle Energy
  - US company
- Allowed MGRM to make financial contracts.
  - Sold 160 million barrel by 1993
Risk and Strategy

- Stack (Rolling) Hedging Strategy: closing out existing positions as they are near maturity and then concurrently opening new position with maturity dates further in the future.
- Basis Risk: correlation between two investments creates the potential for excess gain or losses in a hedging strategy
CONTRACTS

- Firm-Fixed:
  - customer agrees to a fixed monthly delivery at a set price
- Firm-Flexible:
  - customer has flexibility over delivery
- Guaranteed Margin:
  - Deliver at a fixed margin relative to the local area retail price
MGRM STRATEGY

- MGRM provided customers with a way to limit/transfer price risk
- Manage spot price risk
  - Use front-end months futures contracts on the NYMEX
- Stack hedging strategy
  - Depend on short term dates instead of spreading risks over long term contracts
  - Prove to be a sound economic standpoint
- Long in OTC energy swap
BENEFIT OF THIS STRATEGY

- Held futures equivalent to 110 million barrels of gasoline and heating oil
- 102 million barrels agreements in firm fixed supply
- 52 million barrels agreements in firm flexible supply
- 54 million barrels agreements in guaranteed margin
WHAT WENT WRONG

• Assumptions of economies of scales were mistaken
  • Invested majorly in the open interest market
  • Forward supply contracts left them in a vulnerable position
  • Only hedge for potential increase in oil price
  • Timing of cash flows to maintain hedge