ARGENTUM
Asset Management Inc.

CASE STUDY 3: HEDGING AN EXISTING EXPOSURE USING OPTIONS

Hedging an Existing Exposure

The Argentum team has used futures and options contracts to hedge as follows:

(a) The adverse price risk of a large (over 80%) precious metals position in its portfolio. To hedge the precious metal bullion position, the Argentum team sold gold and silver futures contracts and gold and silver call options around the current market price, to lock in the current price.

To fully hedge, the total notional value of the futures and options contracts would be equivalent to the value of the physical metal in the portfolio. Any adverse price movements in the physical metal prices were offset by the gains in the short futures contracts or increase in value of the short call options.

(b) The currency risk exposure in a portfolio invested in USD denominated assets where the reporting currency for the investor was CAD. The Argentum team used both Forward Exchange Contract and Futures contracts to hedge the currency exposure.

A futures contract is a contractual agreement, generally made on the trading floor of a futures exchange, to buy or sell a particular commodity or financial instrument at a pre-determined price in the future

A forward exchange contract is a special type of foreign currency transaction. Forward contracts are agreements between two parties to exchange two designated currencies at a specific time in the future.