The Chicken McNuggets' secret ingredient is not what you think...

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They come in four iconic shapes: 'boot', 'bell', 'ball', or 'bone' (also known as 'bow tie').

McDonalds can't sell them fast enough.

And they almost didn't happen.

That is, until an upstart Wall Street trader came up with a brilliant idea.

This is the story of the Chicken McNugget.

Or, to be more accurate, the story of how you've got hedging to thank for being able to scoff a boxful of them whenever you want for less than a fiver.

Here's how it went down.

Sheer heart attack

The story of the Chicken McNugget starts in America in the 1960s.

The 60s are the decade of huge leaps forward in civil rights. The age of free love and the British Invasion.

But they're also the decade when heart disease reached epidemic levels.

Where, as recently as two decades prior, heart disease was relatively rare, by 1965 it had become the leading cause of death in the US. And according to most doctors, there were two reasons for this: people were smoking too much and eating too much red meat.

At the time, there were around 1,000 McDonalds restaurants across the globe — big, but hardly the fast food behemoth it would eventually become.

More to the point, beef was the backbone of the menu. Growing awareness of beef's potential health risks was bad for business. And when the US government took the exceptional step of explicitly recommending eating less red meat, they went from bad to potentially disastrous.

Wanted: a healthier alternative to the classic hamburger

Faced with a development that could really hurt their business, McDonalds pulled out all the stops. They hired René Arend — a French-trained Luxembourgish chef who'd cooked for the Queen of England and the King of Belgium — and tasked him with developing healthier alternatives to diversify the beef-heavy menu.

Arend chose to work with chicken, a leaner and, so, more heart-healthy type of meat. But, unfortunately, he hit snag after snag.

After several false starts — including a deep-fried chicken pot pie which failed in testing (and probably wouldn't have done much for our collective cholesterol levels either) — McDonalds founder Ray Kroc suggested an onion nugget.

Lucky for us, chairman Frank Turner had his heart set on chicken.

'Why not a chicken nugget?' he suggested.

And, just like that, they had their idea.

Right idea, wrong time

To say that the Chicken McNugget aced testing is a huge understatement. It did better than anyone could have ever hoped for. Not only did it break all previous sales records, but franchises from all over the world were falling over themselves to get their hands on it.

There was just one problem.

Actually, two problems that created an even bigger one:
A boom in chicken's popularity
A tough economic climate

Chicken's image problem

Throughout the 20th century, chicken producers worked hard to make chicken more affordable for everyone. But in the post-war years, red meat became a symbol of prosperity while chicken was viewed as one-note and 'boring'.

Sales plateaued and supply started exceeding demand. So chicken producers made a huge marketing push to raise their product's profile and position it as a delicious, nutritious, and versatile ingredient.

Needless to say, news that eating too much beef could be bad for your health was an unexpected boon. Consumption picked up. And chicken's popularity grew even more when the authorities recommended it as a healthier alternative to red meat.

The 1970s economic recession

At the same time as demand for chicken was rising, the economy went into stagflation — slow economic growth coupled with rapidly increasing prices. As a result, the cost of energy and grain, which producers needed to raise their chickens, shot up.

The combination of higher demand, higher cost of production, and a poor economy caused the price of chicken to become volatile.

And this is where the issue for McDonalds lay.

The state of the market meant chicken suppliers couldn't guarantee their prices wouldn't shoot up or nosedive. With the price of the core ingredient in Chicken McNuggets potentially varying widely from one consignment to the next, McDonald had two options:

- Absorbing the cost
- Putting prices up at a moment's notice

Neither was good.

Absorbing the cost meant they could end up losing money.

But putting up their prices was equally bad.

McDonalds was known for being affordable. Sudden price increases would damage the brand.

What to do?

A winning formula

As it happened, McDonalds were one of two clients Ray Dalio had at the time. In an earth-shattering coincidence, Dalio's other client was a chicken producer.

A Harvard Business School graduate, Dalio worked as a trader on Wall Street for two years, after which he started his own business, Bridgewater Associates, from his bedroom.

Dalio mulled over the problem until he came to a realisation:

Grown chicken = baby chick + corn + soymeal

Chicks aren't a volatile commodity in and of themselves. What producers had to worry about was the cost of the grains they needed to feed them. If they could somehow fix the price of these variables, it followed that the price of chicken would stabilise.

Having had this lightbulb moment, Dalio went to his chicken producer client with a proposition.

What if they entered into a forward contract with corn and soymeal producers?

The arrangement would be fairly simple.

The chicken producers would bind themselves to buy X tonnes of corn and X tonnes of soymeal at X price on X date.

This would be a win-win for everyone.

The corn and soymeal producers had a guarantee they'd sell a certain volume of product, and that this would fetch a certain amount. This meant they could plan production ahead of time.

Chicken producers could also plan ahead, because the agreement meant they could budget accurately for two of their biggest expenses.

More importantly, chicken producers could sell their product to McDonalds at a fixed price. Which solved the issue of how they'd price Chicken McNuggets so they'd be profitable.

Hedging is for everyone

Dalio's brainwave may have saved the day for McDonalds — and given the world a much-loved snack.

But the wider lesson is that hedging isn't a complex, exotic technique for corporate financiers and Wall Street types.

It's a practical, useful tool that matters in the real world.

Whether your business sells grain, raises chickens, or offers a service for which your customers pay in foreign currency, a slew of complex, interrelated factors can cause prices to change in ways that could instantly wipe your profit or make your business model financially unfeasible.

The good news is that you're not powerless.

Hedging is your insurance. Or the raincoat and umbrella you can rely on to keep you dry on rainy days.

Forward contracts and other hedging instruments can help you lock in preferential rates, so you can minimise risk and run your business with certainty no matter what the markets throw your way.

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