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Do Chinese owners and charterers consider the use of cleared freight derivatives for hedging purposes?

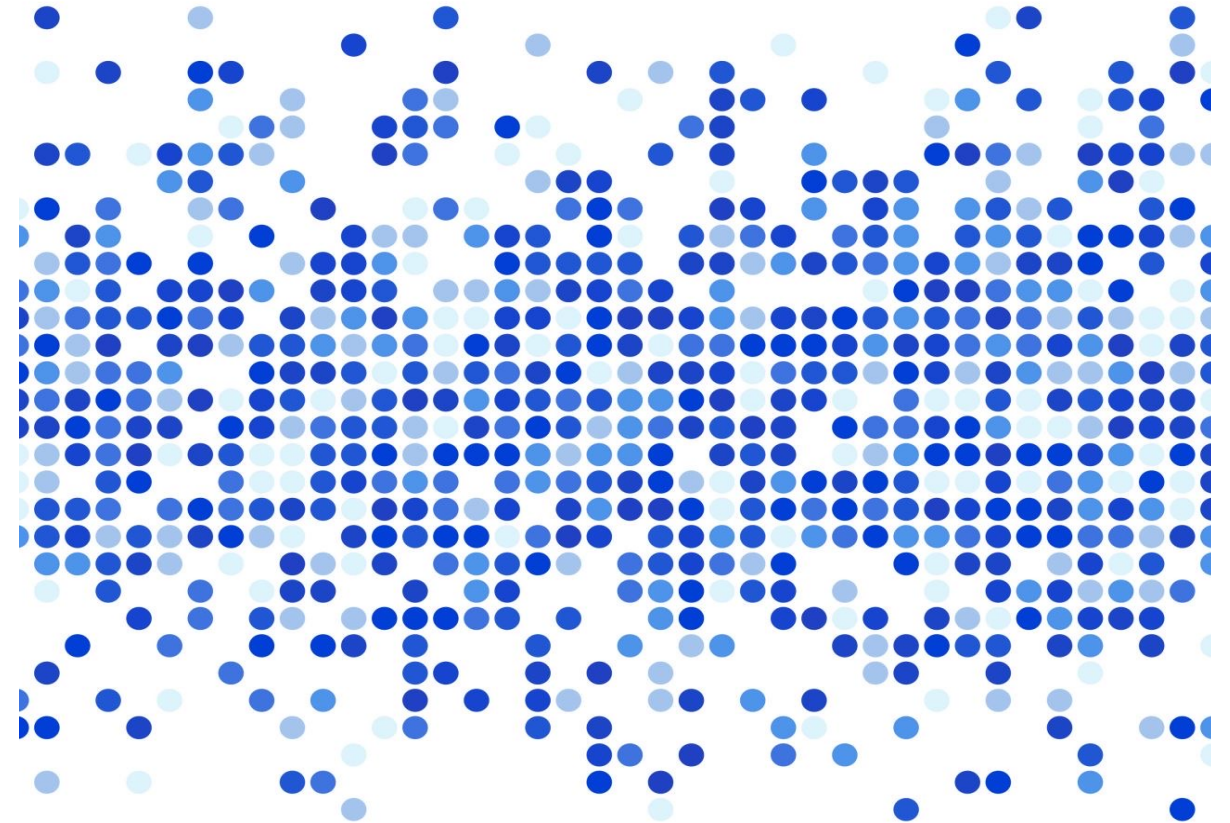
MARINTEC Senior Maritime Forum | Pudong Shipping Week

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Synopsis

- Speaker Introduction
- History of FFAs : 1992 till now
- What are FFAs?
- Why are FFAs more and more popular?
- Who uses FFAs in 2023 ?
- How are FFAS traded ?
- FFA product description
- Transaction Flow
- What determines FFA prices ?
- How involved is China in the FFA market?
- IFFAA : Independent FFA Association



History of FFAs



- January 1985 saw the start of the first ever dry bulk freight index : Baltic Freight Index(BFI)
- May 1985 : launch of the first ever freight futures contract called BIFFEX
- June 1992 : First ever dry bulk FFA traded between Burwain and Bocimar and brokered by Clarksons.
- April 1995 : FFA's for the tanker industry were introduced by Clarksons
- Between 1992 and 2008 the vast majority of FFA transactions were not cleared : massive credit risk
- 2006 : Introduction of financial clearing of FFAs by LCH and NOS
- 2009 : Dry Bulk and Wet FFA markets go fully cleared following the 2008 financial crisis
- 2021 : Highest number of transactions ever in the Dry Bulk FFA market

What are FFA's ?

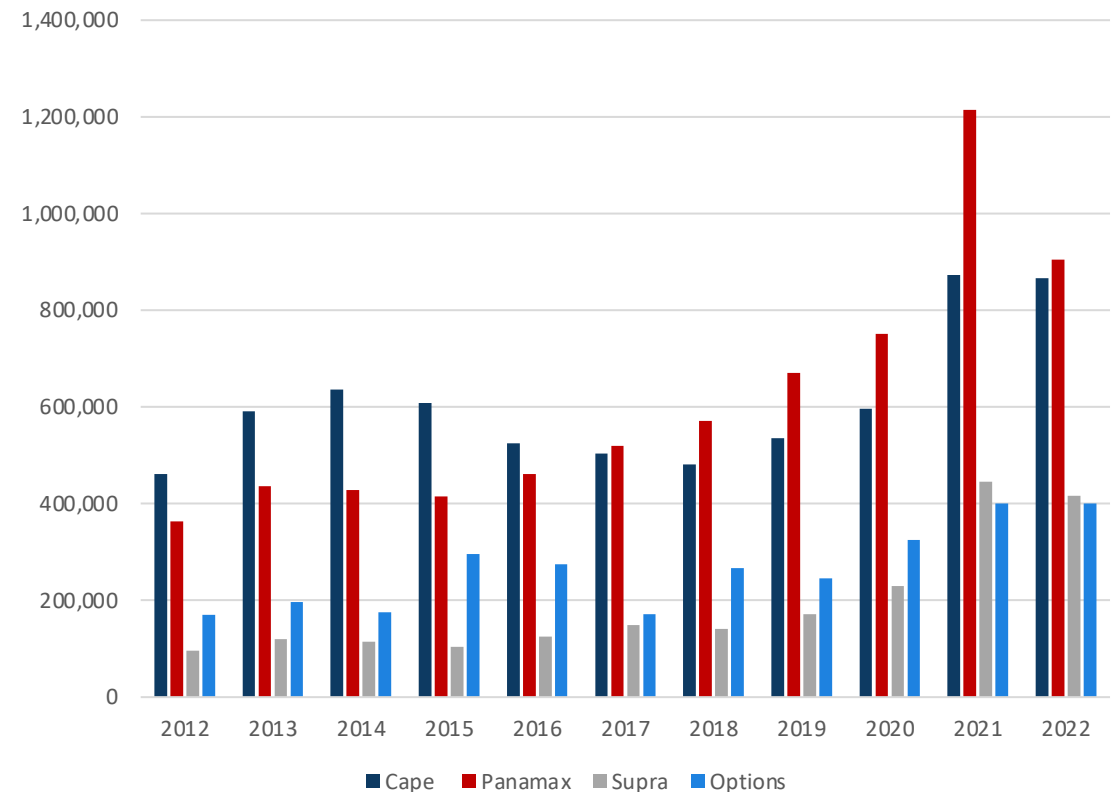
- Cash settled financial products mirroring the value of dry and tanker freight prices in the future
- FFA prices are derived from bids and offers provided by market users/traders
- FFA prices are determined by the expectation of market players of where the spot market should be priced in the future.
- Hedging vs Speculative strategies : Managing future exposure of freight prices vs investing to make a profit.
- Financial agreement to fix a forward/future freight price expressed in \$/day or \$/ton
- Dry Bulk FFAs remain by far the most liquid as over 2.5 million lots changed hands in 2021 (1 lot = 1 day)



Why are FFAs more and more popular ?

- Uncertainty created by geopolitical , black swan events and climate change
- Increased transparency of dry freight indices
- Volatility of freight rates are on the increase as markets become more transparent
- Better quality data sets and AI allows traders to take better investment decisions
- Increased exposure due to social media and more FFA brokers pushing prices
- GFI/Braemar screen
- Over the counter (OTC) Clearing with SGX/EEX/ICE providing full clearing services

• Dry FFA volumes 2012 to 2022



Who uses FFAs?



- Shipowners : Protecting their forward income a/o locking in a profit by selling FFAs
- Charterers : Covering forward freight exposure by buying FFAs
- Freight Traders : Managing exposure on their physical book which can be long or short
- Financial Traders : Investing in where the market will go in the future and provide a positive return to their investors/shareholders
- Freight related ETF's : Using FFAs to manage their exposure related to their product definition (BDRY)
- In 2023 the vast majority of traded volumes comes from Europe (70%) , USA (12.5%), Asia (17.5%)

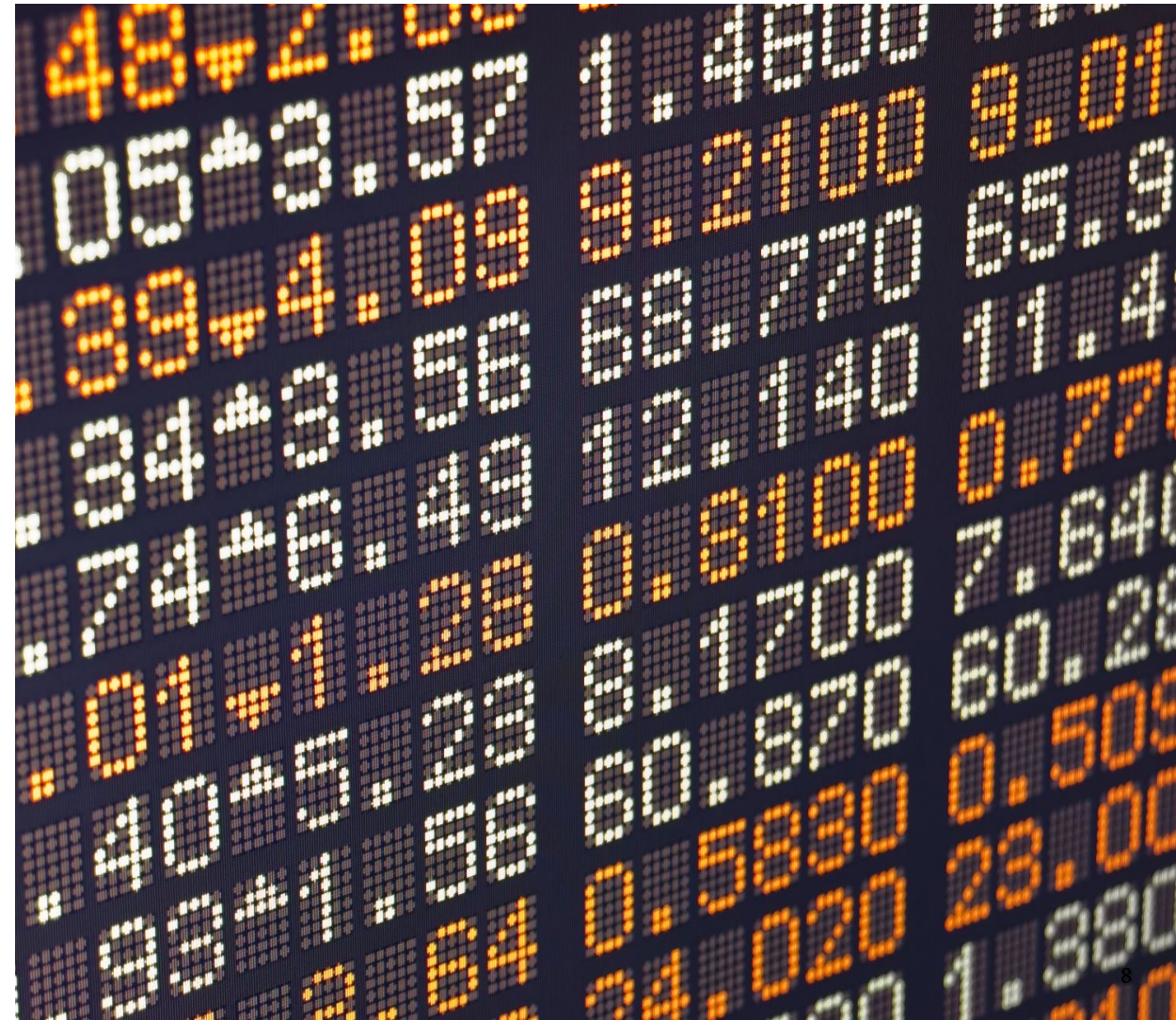
FFA Trading

- Cleared over the counter (OTC) : no credit risk
- Regulated : FFA brokers must be FCA compliant or equivalent
- Main liquid products : Cape 5TC/Panamax 4TC/Supramax 10 TC
- Price discovery : provided by regulated FFA brokers and assisted by screens (GFI/Braemar)
- Price communication : by Whatsapp/Refinitiv/recorded lines between brokers and principals
- Execution speed is paramount .



FFA product description

- Basket of Routes : Capesize 5TC/Panamax 4TC/Supramax 10TC/Handysize 7TC
- Traded periods : Month/Quarter/Year
- Quantity : Minimum tick size is 5 days
- Price : Agreed price in \$/day between the buyer and the seller
- Cash settlement contract : settled on a monthly basis by taking the daily average of the published spot price of the traded basket of routes
- OTC cleared : EEX/SGX/ICE



Transaction Flow in practice

- **Step 1** : Principal asks 1 or 2 FFA brokers a price on a specific period for a particular type of ship
- **Step 2** : Within 1 min one of the brokers gives him a competitive bid/offer spread
- **Step 3** : Principal gives a firm price and awaits a quick reply from the designated broker
- **Step 4** : Broker confirms the price and the transaction is done
- **Step 5** : Choice of clearer is agreed between buyer and seller
- **Step 6** : FFA broker recaps the agreed trade by e-mail to both buyer and seller



Transaction Flow in numbers

MAIN TERMS OF THE FFA

- **Trade date** : 16th May 2023
- **Buyer** : Cargill
- **Seller** : Star Bulk
- **Clearer** : SGX
- **Product** : Cape 5TC
- **Period** : Q3 2023
- **Agreed price** : \$19,000/day
- **Quantity** : 30 days per month , total 90 days
- **Period** : July, Aug, Sept 2023
- **Settlement** : Average of all Cape 5TC index days
- **Settlement date** : last day of each month

2 POSSIBLE SCENARIOS

- **Market rises :**
- If July Settlement : \$30,000/day
- Settlement calc : \$ 30,000-\$19,000= \$ 11,000/day
- \$11,000/day x 30 days : \$330,000
- **Seller pays the Buyer**
- **Market falls:**
- If July settlement : \$14,000/day
- Settlement calc : \$14,000-\$19,000/day
- -\$5,000/day x30 days : \$ 150,000
- **Buyer pays the seller**

What determines FFA prices ?

DEMAND

- Demand for vessel space by large commodity players
- Ton-Mile Demand
- Commodity prices
- Health of the Chinese and US economy
- **Example** : Large grain purchases by China => FFA prices



SUPPLY

- Availability of open tonnage
- Scrapping
- Port congestion
- Vessels speed changes due to weather and regulations
- Forward order book
- **Example** : Decrease in Chinese port congestion => FFA prices



How involved is China in the FFA market ?

- Approximately 17.5% of all Dry FFAs traded by Chinese entities
- Approximately 542,500 lots so far in 2023, out of a total of 3,100,000
- 75% speculative/25% Hedge
- Main users in 2023 : Solebay/Cofco/Theme/Joy Ace/PacBulk/Contango/Able Trend

- 1 lot = 1 day of TC hire



How involved is China in FFA's?

2023 CHINA DRY SEABORNE IMPORTS (9 MTHS)

- Iron ore : 878 million tons
- Coal : 348 million tons
- Grains & Beans : 118 million tons
- Bauxite : 107 million tons
- **Total basis Jan 1- Sep 30 : 1.451 billion tons**

2023 COMPARATIVE ANALYSIS (9 MTHS)

- Iron ore : 878 x \$15/ton : \$ 13.17 bln
- Coal : 348 x \$ 25/ton : \$ 8.70 bln
- Grains : 118 x \$ 30/ton : \$ 3.54 bln
- Bauxite : 107 x \$ 20/ton: \$ 2.14 bln
- **Total basis Jan1 –Sep 30 : \$ 27.55 bln**
- FFA market in 2023 so far : \$ 55 bln
- China's share of FFA market : 17.5% => \$9.625billion
- **China's share of the Dry Bulk FFA market will grow !!**

IFFAA (Independent FFA Association)

- Created in March 2023
- **Principal objectives :**
- To represent the voice of companies and individuals active in the dry bulk FFA market
- To provide a unique venue for open and unbiased discussions on developments in FFAs
- To foster and promote transparency , liquidity and fair competition
- Common voice in dealing with exchanges, clearers and other key sectors of the industry
- Join us and become active members of the Association to grow the dry bulk FFA market
- WWW.IFFAA.ORG



Consortium Capital Ltd (UK)

- FCA regulated Investment Manager
- Investing in cleared freight and freight related commodity derivatives
- Operational since January 2017
- Managed Accounts on behalf of Shipping related investors/family offices/Investment funds
- 100% discretionary investment mandate
- Excellent liquidity terms
- Competitive management fee and performance fee structure
- \$40 million under management with capacity to raise \$35 million more
- In excess of 20% return on annualized basis since 2017
- Please contact : Philippe van den Abeele on +447770 883320 /e-mail : pvdabeele@consortiumcapitalgroup.com