

SGX OTC Container Swaps



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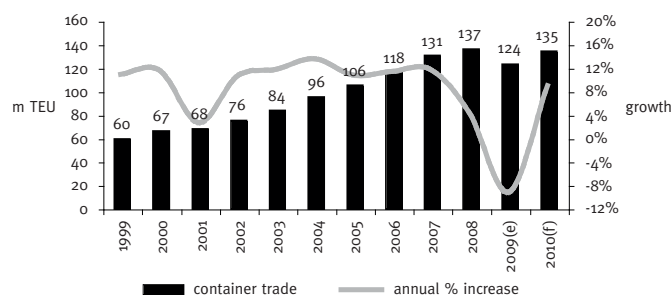
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SGX OTC Container Swaps

In recent decades, container trade has been one of the fastest growing segments of the global freight industry, particularly trades to and from China. From the mid-1990s to 2008, containerised traffic tripled to 136 million TEU valued at US\$137 billion. This is several times the size of the Forward Freight Agreement (FFA) market, which was US\$36 billion in the same period.

SGX AsiaClear offers clearing for OTC Container Swap trades referencing the Shanghai Containerized Freight Index (SCFI) routes. The availability of SGX OTC Container Swaps enables hedgers such as liner companies, large manufacturers, exporters, commodities traders and freight forwarders to buy or sell the swaps and hedge against fluctuations in spot container freight rates. It also allows speculators the opportunity to take directional positions or engage in arbitrage, spreading or volatility trades.

World Container Trade and Annual Growth



Source: Clarkson Research, April 2010

Advantages of using SGX OTC Container Swaps

- Effective hedging instrument to manage price volatility
- Ease of taking and liquidating positions with no risk of physical delivery
- Reduced counterparty credit risk
- Multilateral netting of opposite positions
- Single clearing agreement to trade with a growing pool of counterparties

Contract Specifications		
Product Name	SGX OTC Container Swaps	
Ticker Symbol	Shanghai-Europe Container Swap (B1) Shanghai-Mediterranean Container Swap (B2)	Shanghai-US West Coast Container Swap (B3) Shanghai-US East Coast Container Swap (B5)
Contract Size	1 lot = 10 TEU	1 lot = 10 FEU
Minimum Price Fluctuation	US\$1.00 per TEU (US\$10.00)	US\$1.00 per FEU (US\$10.00)
Contract Months	12 consecutive months	
Trade Registration Hours (Singapore Time)	8.00am – 4.00am Last trading day: 8.00am – 3.00pm <i>Note: System is not available from 4.00.01am to 7.59.59am daily</i>	
Last Trading Day	Last business Friday of contract month, according to Shanghai public holiday schedule	
Final Settlement Price	Cash settlement using the arithmetic average of all Shanghai Shipping Exchange's Shanghai Containerized Freight Index (SCFI) weekly spot assessments for the contract month for the relevant route, rounded to 2 decimal places	

Hedging with Container Swaps

Example: Manufacturer Fixing Container Freight Cost

It is Jan 11 and the container freight rate for Shanghai-Europe currently stands at US\$1,900/TEU.

Buyer (Manufacturer)

A manufacturer expects to move 750 TEU of goods from Shanghai to Europe in Mar 11 and wishes to fix this cost as it has just clinched a major deal to supply products in 2011. To protect against the container freight market rising, the manufacturer bids \$1,850/TEU for Mar 11 Shanghai-Europe Container Swap.

Seller (Shipping line)

At the same time, a shipping line with open vessels open for spot market cargo wishes to hedge against a possible decline in freight rates. The shipping line would like to lock in the container rate for the Shanghai-Europe route of \$1,900/TEU.

Broking

An OTC broker matches the two counterparties together and they agree on a negotiated price of \$1,875/TEU. Both parties request for credit clearing on SGX AsiaClear.

The broker prepares a summary of the agreed terms and conditions:

Buyer	Manufacturer	OTC Clearing on SGX AsiaClear
Seller	Shipping line	The initial margin deposit for each counterparty will be:
Product	Shanghai-Europe Container Freight Rate	
Quantity	750 TEU (75 lots)	No. of lots x initial margin for that period (\$2,150)
Contract Price	US\$1,875/TEU	= 75 x \$2,150
Settlement Date	25 Mar 2011	= \$161,250
Settlement Basis	Average of the SCFI spot price assessments for the contract month	The maintenance margin is at \$1,600 per lot or \$120,000.

Each counterparty may be subject to commission payable to the OTC broker.

Hedge Results of Buyer (Manufacturer)

Mar 2011

Hedge Results of Seller (Shipping line)

As a result of weaker demand, the Shanghai-Europe container freight rate falls from \$1,900/TEU to \$1,600/TEU in Mar 11. The manufacturer benefits from a reduction in transport cost.

$$\text{Reduced Cost} = (\$1,900 - \$1,600) \times 10 \text{ TEU} \times 75 \text{ lots} \\ = \$225,000$$

In Mar 11, the manufacturer sells 75 lots of Shanghai-Europe Container Swap for Mar 11 at \$1,600/TEU to close its open position.

$$\text{Payoff} = (\$1,600 - \$1,875) \times 10 \text{ TEU} \times 75 \text{ lots} \\ = -\$206,250$$

A \$225,000 cost reduction and a \$206,250 loss on SGX OTC Container Swap transaction result in a net gain.

$$\text{P/L} = \$225,000 - \$206,250 \\ = \$18,750$$

Physical

SGX AsiaClear

Net Result

As a result of weaker demand, the Shanghai-Europe container freight rate falls from \$1,900/TEU to \$1,600/TEU in Mar 11. The shipping line suffers a decrease in container freight revenues.

$$\text{Revenue Loss} = (\$1,600 - \$1,900) \times 10 \text{ TEU} \times 75 \text{ lots} \\ = -\$225,000$$

In Mar 11, the shipping line buys 75 lots of Shanghai-Europe Container Swap for Mar 11 at \$1,600/TEU to close its open position.

$$\text{Payoff} = (\$1,875 - \$1,600) \times 10 \text{ TEU} \times 75 \text{ lots} \\ = \$206,250$$

Revenue loss of \$225,000 is offset by a \$206,250 gain on SGX OTC Container Swap transaction.

$$\text{P/L} = \$206,250 - \$225,000 \\ = -\$18,750$$

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