Please note the following errata. Amendments are in red below.

3.8.4 FFA Trading Example

- Date March 22, 2003
- FFA buyer. A charterer has four cargoes from South Japan to Nopac, one cargo a month June to September. He fears the market may substantially strengthen for the September cargo and therefore wants to secure his freight against potential adverse market movements.
- FFA seller. A panamax shipowner has three vessels in the Far East, redelivering from various period charters in September. He would like to have a guaranteed income on at least one of his vessels and is therefore looking to sell an FFA.

The owner is happy to lock in $13,000/day forward in September. The charterer is also happy as he has locked in a rate which is considerably less than the spot market.

- BPI Route 3a (trans-Pacific Round voyage) time charter.
- After a short negotiation a price is agreed between both parties at a rate of $12,900/day for a duration of 50 days.
- A commission of 0.25 pct (of the agreed price x duration) is payable by both parties to the FFA broker that put the deal together.
- Settlement against Route 3A of the BPI as an average of the last seven indices published in September 2003.

CONCLUSION – September 13, 2003

- The average of the two indices used for settlement is $13,500.
- The settlement price being higher than the fixed price, therefore the FFA seller pays the buyer $600 × 50 days duration = $30,000 and payable within five business days.
- The charterer is happy as he gets $30,000 to offset against the higher rate he will have to pay for a vessel on the spot market. The owner is happy as the market is higher than he anticipated.
- The problem with derivative markets of all types is that they are rarely confined to key players such as shipowners and charterers but will also attract speculators. The sort of win-win situation described above is a good example of the benefits of such a system but it must be added that where there are winners there are also losers and when the winner is a speculator and the loser a shipowner or charterer then the whole system begins to fall down.

A lot of big names in shipping have had their fingers burnt by dabbling in derivatives and many have turned their back on them altogether. In other sectors of commerce, trading in derivatives has led to massive price rises in essential commodities and there are calls for the activities of derivate traders to be curtailed.