

Brussels rules could drive away over-the-counter freight trades

Liz McCarthy - Thursday 3 September 2009

THE Baltic Exchange has warned that increased regulation by the European Commission of over-the-counter trading in the freight derivatives market could drive business away from Europe to other global financial centres.

It has warned that market forces should be the judge of when the benefits of exchange or other electronic trading outweigh the benefits of OTC trading.

"In the commodity markets, specifically the freight market, private unregulated companies transact business with other private companies and often choose to keep this business confidential," the Baltic Exchange said yesterday.

"Not only are the benefits of greater transparency [of this nature] unclear, they are probably unattainable as other jurisdictions, such as Switzerland or Singapore, are attractive alternative locations for market participants. Overzealous regulatory intervention could easily drive business away from the EU."

Following a consultation paper produced by the commission, the Baltic Exchange has argued that the freight derivatives market has developed by an evolutionary rather than prescriptive approach. "OTC markets allow brokers and traders together to evolve contracts that meet their needs," the Baltic Exchange said.

The freight derivatives market clears around 90% of all trades and is provided with independent forward pricing and volume data by the Baltic Exchange. In response to requests for greater transparency in the derivatives markets, the Baltic Exchange said: "It is unclear why more transparency of trading activity could help instil better due diligence and more efficiency in the markets."

One of the largest brokers in freight derivatives, Freight Investor Services, supports the Baltic's response. FIS managing director John Banaszkiwicz urged the commission to recognise the differences between freight and other derivatives markets identified with the financial crisis when framing future regulation.

"Comparing freight with credit default swaps or collateralised debt is like comparing apples and dragon fruit. FFAs are an OTC market with almost 100% central counterparty clearing. Those clearing houses provide an effective means of managing exposure and counterparty risk," he said.

"Because our industry has evolved over time to fit the market, we are already well positioned in terms of what regulators might be considering."

The Baltic Exchange is a global freight provider with 560 members, including most forward freight agreement traders and brokers who settle FFAs against Baltic indices.