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Iron awe as swaps surge

Iron ore swaps used to hedge against price volatility have seen a "surge" of interest with the shift away from annual price benchmarking.

The movement of iron ore forms a huge part of bulk carrier shipping with China alone last year importing 627.8m tons.

An increasing amount of iron ore has been sold during the last year on the spot market as producers and many steel mills failed to agree on an official annual price.

The fledgling Iron Ore and Steel Derivatives Association (IOSDA), managed by former Imarex executive Mikal Boe, claims buyers and sellers of iron ore now need to adopt forward pricing following what it describes as "the long-awaited end to the 40-year system of setting annual prices."

Swaps are financial contracts settled against the monthly average of spot prices for 62% iron ore content fines delivered into North China.

Said John Banaszkiewicz, chairman of IOSDA:"We have seen a 330% increase in volumes of iron ore swaps in the past 12 months." IOSDA describes it as a "major surge in interest."

Banaskiewicz is also the boss of derivatives' broker Freight Investor Services (FIS) which Singapore-based Boe joined last year.

Iron ore swaps are still in their infancy but many of the world's largest miners, banks, trading houses and exchanges attended in Singapore last week what host IOSDA describes as the first-ever iron and steel derivatives conference.

IOSDA highlights volatility in the market-- the driver behind paper trading--by giving as an example prices for April 2010 iron ore swaps which fell $0.50 to $149.75 per ton on Monday but are up $21.25 in the last month.

The Q2 2010 contract, the average for April, May and June, also traded down $0.50 at $147 but over the last month it has risen $19.50.

During the last 30 days, iron ore for delivery during 2011 is up $6 at $131.

IOSDA says it is establishing a daily forward curve of iron ore swaps prices based on concluded transactions and broker assessments, which will be available to the market in April.

Last year, FIS teamed up with LCH.Clearnet in developing a cleared over-the-counter (OTC) swap contract.It runs parallel, for example, to SGX AsiaClear, the Singapore Exchange also offering iron ore swaps.

Meanwhile, Chinese steel mills and global iron ore miners remain locked in pricing negotiations.Consequently, spot chartering activity has remained moderately firm, with China diversifying by taking larger quantities of iron ore also from India.Its main sources are Brazil and Australia.

It is seen as putting pressure on the miners who appear keener to see quarterly and index-linked contracts.

Coking coal contracts are already settled for pricing on a quarterly basis.

The Baltic Exchange earlier this month launched its trial East Coast India-China supramax iron ore voyage calculation.

It is based on the existing S7 time charter route.The Baltic Exchange says it should be of particular interest to shipowners, charterers and freight traders.It can be used as a tool for hedging freight and calculating implied fob (free on board) commodity prices, says Banaszkiewicz.

By **Geoff Garfield** in Singapore

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