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Seeing into the future

Do freight capacity futures have a place in the supply chain? A former HP logistics exec thinks so.

[By Eric Johnson](#)

These are the words that carriers of any ilk loathe to hear: Transportation as commodity.

Analysts have said it for years. Corner a carrier representative and he'll probably whisper it. The act of transporting goods has become a commodity in and of itself, and perhaps that's why a select group of people is excited by the potential of seeing it sold as such.

One of those people is Petere Miner, co-founder of FutureFreight, a fledgling company trying to establish a global market for freight futures - the buying and selling of freight capacity on the open market.

The concept is gaining traction. For one, there's an already established futures market for ocean bulk capacity, well-chronicled in a Jan. 4 *Wall Street Journal* report.

"It used to be freight was a service industry for moving oil or dry cargo around," the *Journal* quoted Barry Bednar, head of freight derivatives at Dutch bank ABN Amro. "Now freight has become its own commodity."

But Miner wants the concept to expand beyond oil tankers and breakbulk fleets into ocean containers, railcars and truckloads.

"The industry is poised," Miner said. "I think you're looking at the purchasing of capacity at some point in the future."

Miner, who started FutureFreight with partner Pierre Laurent in 2003, didn't just come in off the street. She worked for 20 years in air, ocean and truck carrier relations for Hewlett Packard before becoming director of logistics at Internet start-up Converge in 2000.

"At Converge, all our models were built on constrained supply," putting a burden on suppliers, she said. The idea of freight futures, "from the shippers' standpoint, is it gives them the ability to have more influence over what they're paying."

There are two kinds of futures: a forward contract, which is a commitment to something specific; and a futures contract, which is transferable.

“A forward contract is like buying space on a certain plane for a certain flight,” she said. “A futures contract would be where an ocean carrier could sell X number of container slots and forwarders might buy a slot and sell it later. Both have different virtues.”

Miner views freight futures as a way for companies to minimize risk, which she said is the greatest cost to anyone involved in trade.

“You have to ask yourself, what are the risks in my supply chain, and what can I do to minimize the costs of that risk?” she said.

Capacity could be bought and used, or bought and sold, or a mixture of the two.

“With futures, you really have to stay on top of it,” Miner said. “So the best market for futures is one where there’s a lot of variability. The thing that makes it interesting on both sides is, how much does price vary?”

High demand lanes, like Shanghai to Southern California, might be an example of such high variability. Transportation costs can vary 20 percent on say, air freight, between Asia and North America.

“That’s a lot, because then the seller is concerned about whether they’re going to have to do a fire sale,” she said.

It’s important not to minimize the expertise component necessary to venture into what’s essentially a gambling game.

“As a shipper, you have to be on point about total demand and understand the range around that demand,” she said. “If I’m going to ship 100 tons in January, but I know my range varies plus or minus 20 percent, for the part of my demand that I’m most certain about, I can do some interesting things.

“If I know I will definitely ship 50 tons, I can get a fixed commitment. But if part of the demand is uncertain, that’s where the marketplace comes in handy. If I overbuy, I can go and sell 30 tons on the open market. And for the extra 20 tons, I can pay a small premium and buy options.”

That scenario runs in stark contrast to the current order of doing things.

“Right now, you negotiate,” Miner said. “You arm wrestle with your carrier, but chances are the carrier will get the more variable part of that demand.”

Miner said the concept of futures could apply to every mode of freight transportation - forwarders would likely be the buyers of air freight futures, shippers or non-vessel-operating common carriers would go for ocean futures, and shippers or trucking 3PL giants like C.H. Robinson or Ryder would go for truck futures.

She sees futures being bought up three to six months out for ocean capacity and no more than three months out for air capacity. “Shippers have long-term agreements with carriers, so it could be as far out as a year,” she said.

There have been past attempts to instigate a futures market in the trucking and air freight industries. But the place where futures are truly already in play is the bulk ocean market, where exchanges in London can land you units of capacity that you can use or trade. The *Journal* reported that trades on bulk and breakbulk capacity have reached \$35 billion to \$45 billion annually, up from roughly \$20 billion to \$30 billion a couple of years ago.

Of course, what’s stoking the discussion about futures is rising freight rates, and a major component of that is the volatile nature of fuel prices. Even if prices rise, as long as they rise steadily, companies can account for those costs in earnings forecasts. But when prices spike, then drop, then spike again, it creates more than just headaches.

In a freight futures environment, an NVO could buy capacity on a ship without having any specific cargo to move, but be safe in the knowledge that the cargo will come. If the NVO does its homework, it could follow in a real-time manner what a slot on an ocean carrier is actually worth and reap the benefit. Or the NVO could simply ensure capacity if the company is concerned demand will outstrip capacity at a certain point in time in the future.

“You can be a buyer and a seller, if you think it’s a really hot market,” Miner said. “But you have to be smart enough to buy and sell and stay on top of it.” She is fairly convinced that capacity derivatives will make their way into container shipping.

“I think it’s going to happen in the freight industry,” she said. “It’s only a matter of time before it spreads. But it will take the big players - shippers, airlines, the FedExes - to let the marketplace decide how it will be used. But it will only work if everyone gets something out of it. You only get out what you put in.”

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