Twitter Thread by Just A Finance Aficionado



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We often come across the term "BALTIC DRY INDEX" whenever we read about shipping industry, container shortage issues, commodity prices etc.

Made a quick informative thread about what exactly it is and what to interpret from it.



WHAT IS IT?

The Baltic Dry Index issued daily is a market barometer and leading indicator of the shipping industry.
The Baltic Dry Index (BDI) is issued daily by the London-based Baltic Exchange.

The BDI is a composite of the Capesize, Panamax, Supramax Timecharter Averages.

How BALTIC DRY INDEX dropped in 2008 ?■

ANSWERED BELOW ■



REASON ?

China buys most concrete, aluminum, copper & steel in the world.
But as services have started to play bigger role in world's 2nd largest economy its demand for commodities has leveled off.
Too many ships & falling demand from its biggest customer puts a cap on the BDI.

BDI ALONG WITH OTHER ECONOMIC INDICATORS -

GDP, volatility index, crude oil prices, interest rates and exchanges like S&P 500, FXI, Japan Nikkei 225 and London FTSE.

These are followed by Economists/Investors as leading indicator for economic growth and production

RELATIONSHIP BETWEEN VIX AND BDI ?

There is a negative relation between the BDI and VIX.

While the world economy is in recession,
The VIX is expected to increase, the BDI is expected to decrease.

ROLE OF DEMAND AND SUPPLY ?

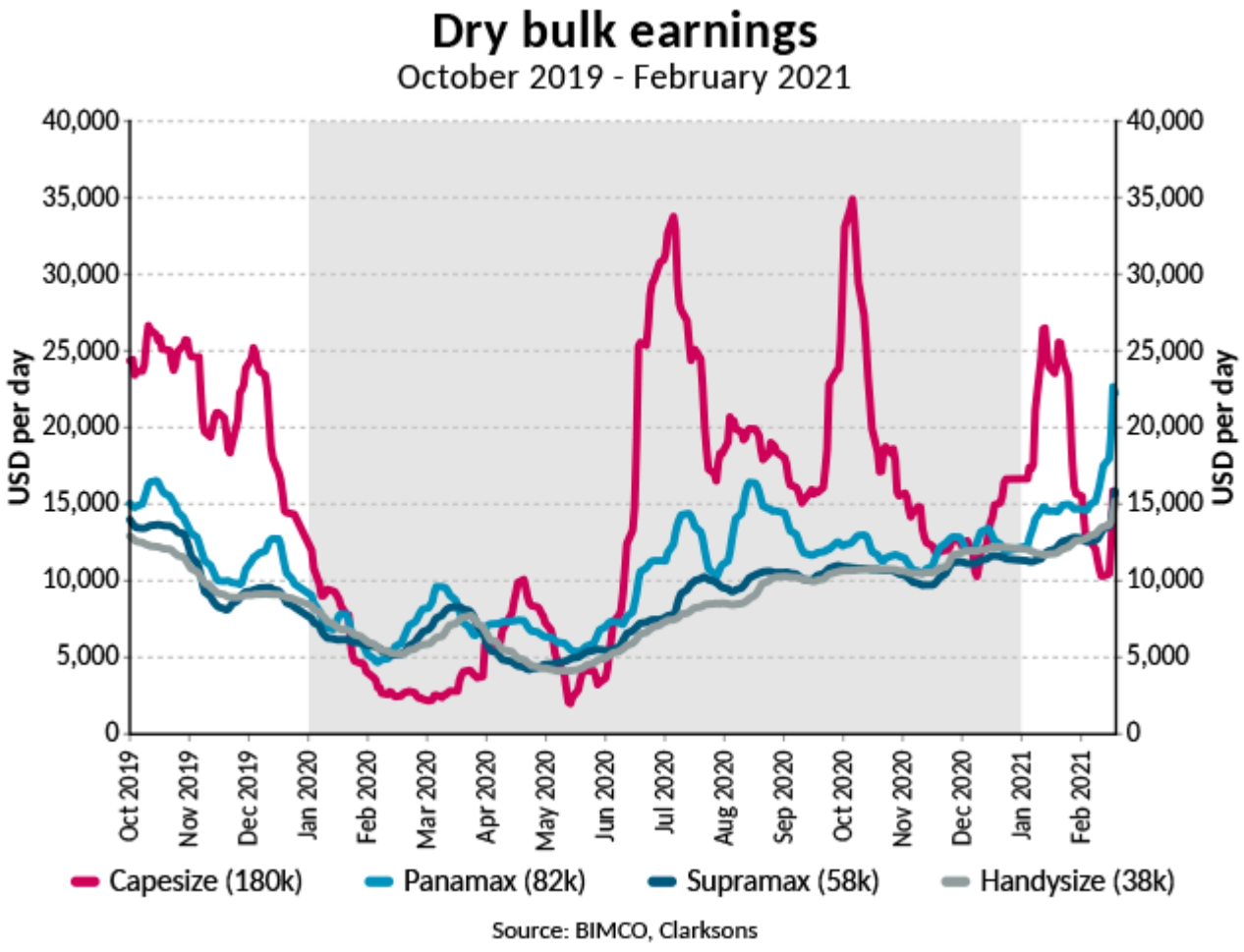
Index measures the demand for shipping capacity versus the supply of dry bulk carriers.
The demand for shipping varies with the amount of cargo that is being traded or moved in various markets (Dd/Ss).

The supply of cargo ships is tight & inelastic

WHAT IS DRY BULK COMMODITY ?

Raw material shipped in large unpackaged parcels. Dry bulk consists of mostly unprocessed materials (grain, metal, and energy materials) that are destined to be used in the global manufacturing & production transported by sea in large cargo vessels.

DRY BULK EARNINGS REPORT -



INTERESTING FACT -■

Shows high correlation to equity markets.

Besides the BDI is a leading economic indicator, recently, many researchers has been also seeing it as a leading indicator of the stock markets.

Movements in BDI tend to precede movements in global equity markets.

TWO CATEGORIES -

■MAJOR BULKS include iron ore, coal, and grain. These major bulks account for nearly two-thirds of global dry bulk trade.

■MINOR BULKS include steel products, sugars, cement, and cover the remaining one-third of global dry bulk trade.

■MOST TRADED ?

Coal and Iron ore are most traded bulk commodities by volume in the world.

Countries most involved in the importation of coal for their primary energy and electricity needs are India, China & Japan.

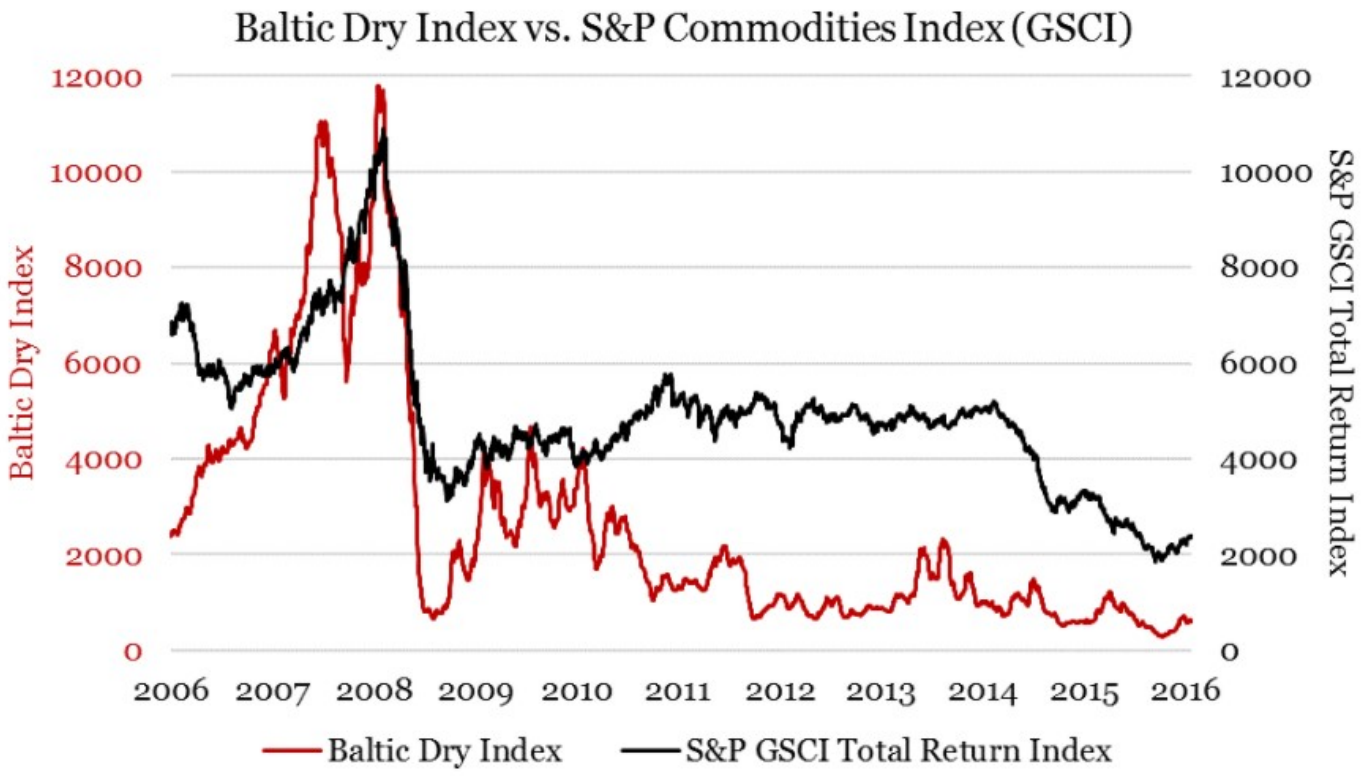
Grain - Another major cargo in terms of seaborne bulk trade.

HOW QUICK CAN WE BUILD A SHIP ?■

Takes 2years to build a new ship, and the cost of laying up a ship is too high to take out of trade for short intervals.

So, marginal increases in demand can push the index higher quickly, and marginal demand decreases causes to fall rapidly.

CORRELATION BETWEEN -
■BALTIC DRY INDEX
■■S&P COMMODITIES INDEX (GSCI)



RELIABLE ?

Producers buy raw materials when they want to start building more finished goods & infrastructure (automobiles, machinery, roads, buildings)

They stop buying raw materials when they have excess inventory

"People don't book freighters unless they have cargo to move”

WHATS BUNKER FUEL ?

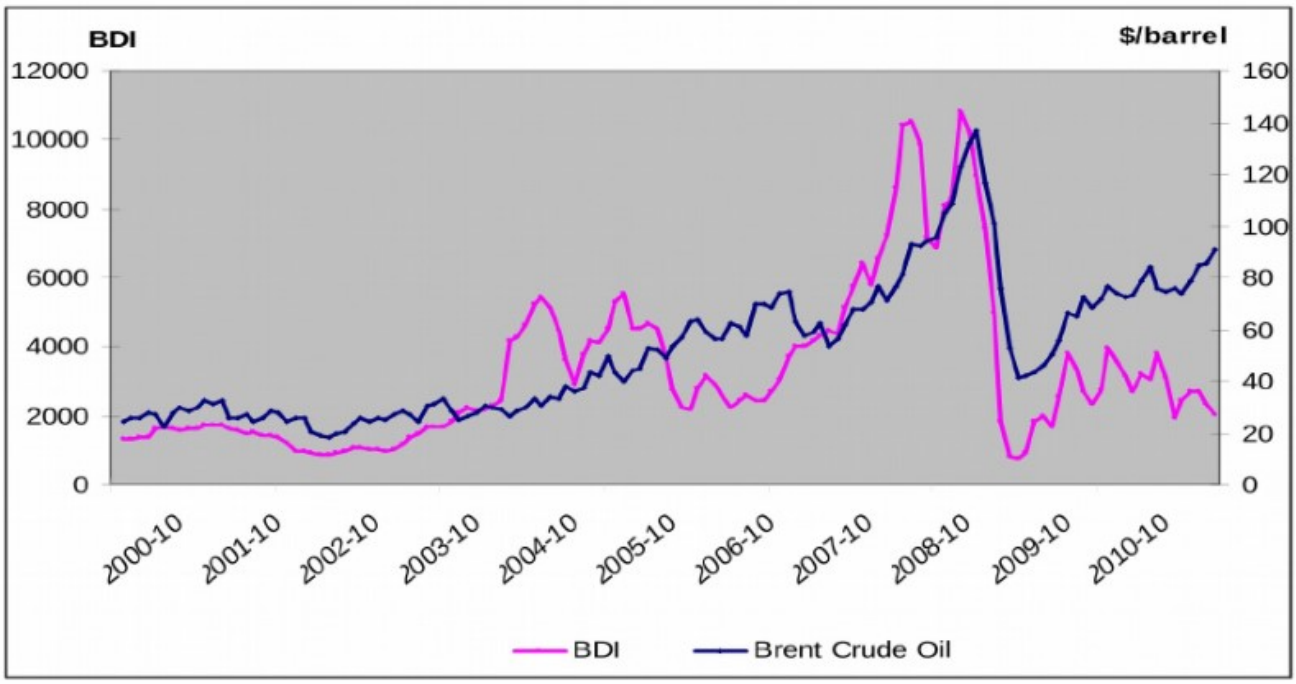
Bunker fuel accounts for between a quarter and a third of vessel operating costs.
Furthermore it is a type of fuel oil a ship uses for propulsion and moves with the crude oil price.

CRUDE OIL VS BDI -■■

Fuel is the largest voyage dependent cost for a voyage of a ship.

Higher crude oil prices also mean higher bunker fuel prices which will be reflected in higher BDI prices.

Therefore the BDI is sensitive to changes of the price of crude oil



TRUE ECONOMIC INDICATOR -■

Dry bulk primarily consists of materials that function as raw material inputs to the production of Intermediate/Finished goods (Eg- concrete, electricity, steel, food)
The index is also seen as an economic indicator of future economic growth.

CURRENTLY BALTIC DRY INDEX COOLED OFF AFTER A SHARP RISE. ■

Here's why ? ■

https://t.co/vZB7x24TTg



■■■■NO MANIPULATION -

BDI reflects the demand of commodity buyers who need the goods for production.

Its difficult to manipulate demand because it is calculated solely by those who have placed orders to have goods shipped. Nobody would pay to book a Capemax without genuine need.

BDI VS INTEREST RATES -

Rising BDI typically points to increased global economic activity, increased production, rising stock prices, rising commodity prices, rising interest rates and rising value in commodity based currencies
(New Zealand, Australian and Canadian Dollar)

HOW DOES THIS WORK ?

Every working day, a panel of international shipbrokers submits their assessment of the current freight cost on various routes to the Baltic Exchange.

The routes are meant to be representative, i.e. large enough in volume to matter for the overall market.

WHAT TO INTERPRET WHEN "BALTIC DRY INDEX" STARTS RISING -■

✍■Global economies are starting to, or continuing to, grow
✍■Companies and stock prices should start to, or continue to, increase in value
✍■Commodity prices should start to, or continue to, increase in value

FREIGHT DERIVATIVES ?

Freight derivatives derive their value from freight rates.
These instruments help shipowners and operators manage freight rate risk.

They include exchange traded futures, swap futures, (FFAs), and container freight swaps etc.

PLEASE NOTE -

No indicator is a magic bullet for identifying a market bottom, monitoring a few broad economic indicators can give you a good idea of how healthy the global economy and the stock market are.