



Uranium Futures Contract Turns One Year Old

The uranium futures contract was launched one year ago this week by NYMEX partnering with Ux Consulting. While to date the "UX" contract has not been terribly active, totaling about 700,000 pounds of material (2,783 contracts at 250 pounds each), there has been enough activity to demonstrate how it functions on a number of different levels, show the benefits associated with a futures market, and address some of the issues that have arisen about the contract. Here, we review activity over the past year and talk about the changes that have occurred and the prospects for this market in the future.

Despite the considerable attention that uranium futures attracted with its launch, it was clear that it would take time for this contract to take hold, given the newness of futures to this industry and the newness of the uranium market to those accustomed to trading futures. To this end, NYMEX and UxC held a series of seminars (in New York, Atlanta, Washington, and London) to provide background about the contract – and futures trading in general – and about the uranium market.

One of the early concerns with the uranium futures contract from the nuclear fuel industry's standpoint was the relatively small size of the contract (250 pounds) relative to the needs of utilities which may desire to hedge prices in contracts that may have annual delivery quantities of 500,000 pounds or more. Obviously, you need multiple contracts to get to these much larger quantities, and while 100,000 pounds is the largest single-lot transaction so far (a total of 400 contracts), it does show the "scalability" of the contract.

Although the 250 pound size of contract is not large relative to a utility's needs, it is attractive to an individual or company that wants to speculate on future movement in uranium prices. The value of the futures market is that it allows price risk to be transferred from one party to another, and the more parties that can be attracted to the contract (and the relatively small size increases the pool of potential participants), the more opportunities for price risk transfer. The transference of price risk is another aspect of the futures market that is much better appreciated now than it was this time last year.

Another attribute of early trading was that it focused on specific months that were relatively close in. For a while, traders concentrated on the months of June and December 2007 (the middle and the end of that year), but then more months began to be traded. NYMEX has introduced several features to help facilitate efficiency and increased trading in out months including strip trading (Sep 2007), and more recently (April 2008) the introduction of calendar spreads, which allow traders to roll their positions forward. The original contract term, which was 36 months, was expanded to 60 months in June 2007. This lengthening of the contract addressed another concern of uranium industry participants that have long-term contracts that go far out into the future. The uranium contract could be further extended if the need arises; NYMEX's light crude contract currently runs through 2016.

Currently, December 2009 is the most distant price point on NYMEX uranium platform, and it is for just one contract. However, there are 400 contracts for June 2009, which is more than a year away, showing a willingness on the part of some parties to trade out in this timeframe. The June and December 2009 contracts along with the other contracts from May through December 2008 result in the formation of a forward price curve, as shown in the chart below. While this currently does not go very far into the future, it does provide the industry with additional price information that was not available before.

Activity on the futures contract has picked up in 2008 (1,336 of the 2,783 total contracts have been entered into during the past two months alone). This may be partly due to greater familiarity with the contract and the fact that more parties are now approved to trade it. However, it may also be due to the recent credit crisis, which makes the underlying credit worthiness of NYMEX and its members more attractive.

The credit aspect serves to remind us that the futures contract is just one element of uranium derivative activity that has taken place over the past year. (Thus, just looking at futures activity understates what has transpired in this arena.) There have been a number of over-the-counter (OTC) bilateral swaps (forwards) where price risk is hedged. In fact, the larger deals on NYMEX were OTC swaps that were later cleared on the futures market. Clearing breaks the link between the buyer and seller and in the process reduces the exposure to credit risk.

What does the future hold? Uranium futures activity seems poised to increase, as more and more industry companies are setting up to trade these contracts, as price volatility is unlikely to abate anytime soon given an uncertain future supply and demand situation, and more and more traders are drawn to uranium as nuclear power becomes an even more important part of the energy

mix. One important dimension to how quickly uranium futures trading grows is how the underlying physical market evolves. There is currently a push for a more liquid and transparent spot market, which if successful would enhance futures trading in uranium as traders would gain confidence in the robustness of the underlying physical market and the settlement prices it produces.

Finally, when looking back on the first year's level of activity in the uranium futures contract, it must be remembered that futures trading in oil and natural gas was not immediately embraced and took some time to develop. This must be contrasted with the observation that today probably the single most watched statistic in the world is the price of crude oil published by NYMEX on the futures exchange. While uranium may not achieve these lofty heights, increased activity is expected for the futures.

For more online information on the NYMEX UxC Uranium U_3O_8 Swap Futures Contract (UX) please see:

http://www.nymex.com/UX_csf.aspx

http://www.nymex.com/UX_spec.aspx

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