FAQs

FHIM Trade Logistics 2021-1

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The Fund and Experience of Manager

1. How do the Fund Managers get comfortable with receiving, checking, processing, and presenting Bills of Lading?

a. The underlying Fund encourages Electronic Bills of Lading which means everything is digital, secured, and authenticated through E-BL providers like BOLERO, WAVE, ESSDOCS who are leading providers of this process and have many Shipping firms connected to their platforms.

b. The E-BL is legally as good as the Paper version. If in a paper format, the Fund has implemented Intelligent (AI) OCR and data capture which scans, reads, and extracts all the data from the Bills of lading, and feeds the data from the BL into the Fund systems for auto checking and processing.

c. The Intelligent OCR IT is running at a 98% accuracy. The Fund is training the AI system to be able to read all other documents which are sometimes obtained to help in the scalability of the Fund's strategy.

2. Please explain their team structure and experience of this documentary process, which is very detailed in nature.

a. In total the Underlying Fund Manager has 12 staff in Singapore. There will be 3 new hires, Q4/21 one head count for Operations. In January 2022, there will be 2 hires, systems development. In addition, the Fund has access to additional resources via the 15 + staff in Europe.

b. The Fund has experienced team members, 4 x operational staff, all with minimum 10 years' experience in physical trade operations, accounting, KYC & AML, and documentation.

c. The Fund has shipping expertise in the team with an ex-Maersk shipping agent who has experience in trading too. Within the team is commercial banking expertise and legal commercial expertise. The General Terms and Conditions architecture has been created by the legal team which has been tried and tested over the past 3 years and has been vetted and supported by external counsel.

d. The principal co-founders of the Fund, the CEO/CIO has over 30+ years of years of commercial experience in trading, investment, risk management, finance, of commodities and has a systems architecture experience.

e. The CRO has enormous commercial expertise in English Law, and French Law and has been instrumental in developing the legal infrastructure and the KYC & AML policies of the Fund for its trading counterparts.

3. Which bank will be handling the L/C in the transactions?

a. Letters of Credit receipt/issuance are handled by the Trade Finance bankers of the Fund, DBS Bank Ltd in Singapore.

b. This Bank was chosen due to its high credit rating, all suppliers can accept LC's issued by this Bank.

c. It is a very innovative bank offering Digital Services and the Fund has been integrating the banking system with their own back-office processes to automate reconciliation of payments received against invoices for cargoes being delivered to SME Customers. This helps with the scalability of the Fund's strategy.

4. Warehouse receipts/warrants require approval of warehouse-keepers and appropriate insurance of the goods; if these are changing for each transaction the KYC + DD would be extremely burdensome. How does the fund handle this workload?

a. The Fund undertakes very little warehouse transactions and if they do, they are for bonded warehouse transactions where the Bill of Lading document is still applied as the goods have not met their final delivery location with duty unpaid.

b. There are only a few warehouse destinations the Fund handles as they are Bonded distribution points that then go onshore Africa or onshore Europe etc. Therefore, this is not a vast workload for the fund.

Fund Holding, Risk Mitigation and Enforcement Details

5 What is an example of current underlying fund holdings?

a. As the Fund is dealing with physical goods and shipping there are sensitivities around showing details of live portfolios as there are security and commercial risks around disclosing this information which may prejudice the Fund's investment position and its SME counterparts. Aggregated data in a Monthly report is sent to Investors with a detailed description of the Fund's performance and traded Cargo.

6. What is the scope of insurance coverage?

a. Standard Insurance – full 100% all risk marine Insurance from IG rated Insurer (A rating or above..

b. There are no exclusions in these insurance contracts.

7. What is representative of standard purchase and sales agreement?

a. These contracts are standardised by the Fund and only the commodity details change.

8. What is the current and historical data (30/60/90/180d. for credit loss allowance, reserves, losses realized and insurance claims/disputes?

a. The Fund does not lend money therefore it does not have credit loss allowance. The Fund has zero losses realized and no insurance disputes since inception.

b. The Trade Support Fee (volatility margin paid up front by the buyer) gives the Fund a price risk buffer in the unlikely event that an end buyer is unable to take delivery and make final payment.

c. The Fund uses the Trade Support Fee to fund the disposal of that Commodity cargo in the spot market and allow the Fund to recoup the investment in the Cargo.

d. Minimum 10% Trade support fee, 20% average support fee and no maximum.

e. The Fund has had some cargo which was 60% Trade Support Fee during 2020 Covid period.

9. What is the Fund's Expected Credit Loss Methodology?

a. The Fund does not lend money therefore doesn't have an expected credit loss. The Fund focuses on a proprietary score card which has a proven track record of setting the appropriate Trade Support Fee (up front non-recourse payment from the Buyer). This results in a net investment by the Fund in each transaction to ensure that in the very unlikely event that the end buyer is unable to make final payment and take delivery of the Commodity Cargo, the Fund can have a high degree of confidence of being able sell the Commodity in the spot market and recoup its investment.

b. The Trade Support Fee level is made up of various dynamics, a core component is 2008 Commodity price crisis data history and the 2020 Covid crisis impact on Commodity markets. The two were very different scenarios.

c. The 2008 is still the Fund's primary stress test scenario.

10. How is the Due Diligence conducted upon each shipment to minimize fraud – what is the process and who are the involved/contracted parties for this?

a. This is another benefit of being the principal in the transaction because the Fund has veto rights and control the quality of the surveyor, usually SGS or equivalent standard testing and inspection agency for each cargo to certify the Quantity and Quality.

b. The Fund knows the container numbers, and vessels.

c. The load port survey data is the one legally binding on the end-buyer.

11. The Fund has no credit risk exposure to the end-buyer – how is this possible if the initial discount is ~10-30% of goods and the Fund is acting as principal in the transaction (ie owner of the commodities)?

a. The Fund does not have "direct credit risk exposure" because they do not lend money.

   i. If the end buyer defaults and does not take final delivery of the goods, the Fund is then the owner of those goods and can sell the Commodity in the spot market.

   ii. During the shipment of goods, the Fund monitors the Marked to Market (MTM) fair value of the Commodity and ensures that in the unlikely event the Fund had to sell the Commodity to another end buyer, the Trade Support Fee (non-recourse payment paid up front by the buyer) is always adequate.

   iii. These are short tenor transactions typical between 20 to 45 days, max 90 days. The typical Trade Support Fee, which is equivalent to 20% of the cargo purchase value, is more than adequate in a normal market situation.

   iv. During March/April 2020 some commodity prices dropped (but equally many went higher in the Fund's portfolio) those that dropped quickly were Diesel and Cashew Nuts. The Fund had a few contracts in these commodities and because of their MTM monitoring, if 60% of the initial Trade Support Fee is utilised on a Marked to Market basis the Fund puts the end buyer on notice that they may have to top-up the Trade Support Fee.

   v. During March/April 2020 this happened on a few occasions with Diesel cargo and once on Cashew Nut contracts. The Fund requested additional Trade Support Fee from the end Buyer when 75% of the initial Trade Support Fee was utilised and requested cash to bring the Trade Support Fee level back to below 50% utilisation level.

   vi) At no time was the Fund ever at risk of a loss if it was forced to sell the commodity into the spot market.

12. How does the Fund mitigate concentration/diversification risk?

a. Concentration risk is mitigation by the Fund selecting a commodity trade where there is an active spot market at the delivery port. For example, you don't want excessive concentration by cargo type and have it delivered to a small port with a small spot market for that cargo type.

b. All traded cargo must have a spot market which can be actively tracked via the spot price (which is the alternative disposal price tracked MTM), this drives the volatility margin paid up front by the buyer and during the during of trade if required.

c. If the buyer can't make the requested volatility margin during the trade the fund owns the cargo.

d. The fund doesn't want cargo concentration (too much cargo of the same type. going to a smaller port which has the one spot market. The underlying business risk viewpoint is that the Fund takes client credit risk (buyer concentration risk) and transforms it into an insurable real asset risk (cargo) and therefore a key risk is around the commodity price.

e. The cargo concentration risk method used by the Fund is to adequately manage the price risk of the commodity which must be broken down into the price risk by destination port.

f. In summary, each traded Cargo must have a spot market and that spot market is relevant to the port that it is being delivered to (there may be other spot markets in ports that are nearby which are factored into the pre-trade assessment) Therefore, concentration risk should be largely viewed as a risk mitigated by cargo type and by destination port rather than considerable focus on the traditional measurement of counter-party/client/end buyer and or jurisdiction.

g. Things to consider in concentration risk in this instance are cargo type not so much counterparty/client/people, if the buyer can pay the fee and any requested margin increase. The Fund trades cargo where there is a spot market and little concentration (by cargo type. at the destination port.