

The mechanics of the fraud

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The frauds of 2020 exploited the structural weaknesses of transactional financing described in the previous chapter.

The first mechanism is multiple financing. A trader presents the same cargo to several banks, each of which believes it is financing a separate transaction and holds exclusive security. The absence of a central register of pledges over goods and the confidentiality of banking relationships make this practice difficult to detect. Agritrade's "overlapping" shipping lists and ZenRock's use of the same cargo for several loans fall under this mechanism.¹

The second mechanism is the fictitious cargo. A trader fabricates documents — contracts, bills of lading, invoices — relating to transactions that never took place, and then obtains financing on that basis. The principle of autonomy of the documentary credit, which obliges the bank to pay against documents that appear to be compliant, facilitates this fraud when the forgeries are well executed. The fictitious contracts for which the founder of Hin Leong was convicted fall under this mechanism.²

The third mechanism is the sale of the collateral. A trader sells goods pledged in favour of a bank without repaying the corresponding credit, using the sale proceeds for other purposes, in particular to cover losses. Hin Leong sold oil that had been pledged as security.³

The fourth mechanism is the concealment of losses. A trader that suffers trading losses keeps them out of its accounts and continues to obtain financing on the basis of falsified accounts, in the hope of recovering. Hin Leong is suspected of having kept loss-making transactions off its books.⁴

These mechanisms are often combined. A house that conceals its losses needs liquidity, which it obtains through multiple financing and fictitious cargoes, before selling the collateral in order to keep going. The spiral ends when prices collapse or when the banks tighten credit.

The mechanics of the fraud

Caution. The frauds of 2020 combined multiple financing against the same cargo, fictitious cargoes documented by forgeries, the sale of pledged collateral and the concealment of losses. They exploited the principle of autonomy of the documentary credit and the absence of a central register of pledges over goods.

1 Notes

1. Bloomberg via AJOT, 7 September 2020, cited above. ↩
2. AFP via Malay Mail, 10 May 2024, cited above. ↩
3. Global Trade Review, 12 August 2020, cited above. ↩
4. Global Trade Review, 12 August 2020, cited above. ↩

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