

27 September 2018

New Bunker Adjustment Factor (BAF)

Dear Customer,

From 1st January 2020, a new regulation will come into force to reduce air pollution from ships globally. Whereas today ships can use fuel with up to 3.5% sulphur content (outside Emission Control Areas), the new global sulphur cap will be 0.5%. For Emission Control Areas (ECAs), the Sulphur cap will be 0.1%

The new regulation has been developed and adopted by the International Maritime Organisation (IMO), which is a specialized agency under the United Nations (UN). It will reduce sulphur pollution from shipping by more than 80%, and therefore have a very significant positive impact on the environment and human health.

MCC fully supports the regulation, and our preparations to ensure compliance are well underway. The cost of compliance with the new regulation will be significant, so the cost of shipping might increase. It is also expected that the volatility of fuel costs for shipping will increase as the regulation enters into effect. In order to comply with the new global regulation, we will charge Bunker Adjustment Factor (BAF).

In order to allow customers to predict, plan and track how changes in fuel price will impact total shipping freight rate, MCC will introduce simple and predictive BAF. The new BAF will allow customers to simulate and calculate the BAF tariff at any fuel price. This new BAF will only be applicable for Long Term contracts (more than 3 months validity). It is designed to recover fuel related costs, and will be charged separately from the basic ocean freight as the fuel cost is a very significant part of shipping costs.

The BAF consists of a trade factor and the increase in bunker price:

$$\text{Bunker Price Increase*} \times \text{Trade factor} = \text{BAF}$$

**Ave. bunker price of a quarter minus bunker price baseline*

For MCC, the bunker price is calculated as the average fuel price in Singapore port for the last three months prior the BAF tariff review. The bunker price for 2019 Quarter 1 is set as "Bunker price baseline" based on 2018 Quarter 4 average fuel price. The trade factor reflects the average fuel consumption on a given trade as a result of variables like transit time, fuel efficiency and trade imbalance. For MCC's Intra-Asia operations, we have found the trade factor to be 0.5. Therefore the BAF tariff for 2019 Quarter 1 will be 0. Hence, at different increase in bunker price, the BAF tariffs would be as follows (illustration):

Bunker Price Increase (USD/ton)	-USD 10	USD 0	USD 10	USD 20	USD 30
BAF tariff (USD/FFE)	0	0	5	10	15

We have also included more details on the new BAF in the Q&A below. You will be advised of the actual BAF tariffs, which will be reviewed on a quarterly basis. We will introduce the new BAF from 1st January 2019. This will allow you get familiar with how the mechanism works before the new sulphur regulation enter into force in 2020.

We want to thank you for your business and look forward to continuously serving your global transportation needs.

Best regards,

MCC Transport Singapore Pte. Ltd.

Questions & Answers on the new BAF

QUESTION	ANSWER
What is the new BAF formula?	The new BAF will be calculated as: Bunker price increase x Trade factor = BAF
When would the new BAF be effective and would BAF be applicable to all contracts?	The new BAF will be effective 1 st January 2019. It is only applicable to Long Term Contracts (more than 3 months) with start date on or after 1 st January 2019. Long Term Contracts with start date before 1 st January 2019 will be subject to the old SBF until their expiry.
Why is BAF not applicable to Short Term Contracts?	For Short Term contracts, the rates change more dynamically and the Basic Ocean Freight can take into account the bunker price fluctuation.
What fuel types will be used in calculating the new BAF?	In all of 2019 the new BAF formula will be based on the fuel price for high-sulphur fuel (IFO 380). From Q1 2020 onwards, the new BAF formula will be based on fuels that comply with the new regulation (0.5% sulphur).
How do you calculate the fuel price used in the BAF?	The fuel price used in calculating the new BAF will be the average fuel price for Singapore port for the relevant period (typically three months).
Why does the BAF tariff only cater to bunker price increases and not decreases?	In Intra Asia, MCC has not charged BAF/SBF as part of our standard tariff structure (only exception being customer specific BAF or some exceptional corridors due to market practice). This was done since we considered the "normal bunker fluctuations" as part of doing business in our scope (Ref illustration in table below). In view of the recent steep bunker increase and to prepare ourselves and the market for the upcoming IMO 2020 regulations, we expect a steep increase in bunker price and therefore we would like to only charge the incremental / delta to today's (Q4 2018) baseline.
How do you calculate the trade factors used in the new BAF?	The key elements of the trade factors are: 1. The actual MCC fuel consumption (ton/FFE) per container moved on the trade; and 2. An imbalance factor reflecting that on some trades there is a dominant headhaul, which will be subject to a larger share of the fuel cost changes (up and down) than the backhaul. For MCC, we have balanced trade i.e. factor of 1. For MCC, the trade factor will be 0.5
Will there be a special BAF for reefer containers?	The BAF for reefer cargo will be calculated by multiplying the BAF for standard containers (dry) with a factor of 1.5, reflecting the average electricity consumption of reefer containers.
What will happen to the Standard Bunker Adjustment Factor (SBF) applicable to Korea?	SBF will remain for all origins to Korea destinations and Korea origin to Japan destination as per today.
When will you communicate the BAF tariffs for Q1 2019?	We will communicate the BAF tariffs for Q1 2019 by the end of November 2018.
How often will the new BAF tariffs be reviewed?	The BAF tariffs will be reviewed quarterly. However, during 2020 we will review and adjust the BAF tariffs monthly if the fuel price change is more than 50 USD/ton since the last adjustment.
Will you adjust the new BAF tariffs even when the fuel price change is insignificant?	When we do our quarterly BAF tariff review, we will only adjust the BAF tariffs when the fuel price has changed (up or down) more than 10 USD/ton since last adjustment.

IMPORTANT ANNOUNCEMENT:

Please be advised that from 1st October 2018, MCC Transport will officially adopt the name Sealand – A Maersk Company. [Click here for more information.](#)