Summary

S&P Global Ratings assesses the ability of First Digital USD (FDUSD) to maintain its peg to the U.S. dollar at 4 (constrained). FDUSD is a fiat-collateralized stablecoin issued by FD121 Ltd. (First Digital Labs), a subsidiary of First Digital Group that is incorporated in Hong Kong.

Our asset assessment is 3 (adequate) due to limited information on the identity or creditworthiness of the financial institutions that hold the stablecoin’s reserves, and which thereby represent potential counterparty risk exposure. FDUSD is backed by reserves comprising low-risk assets, such as short-term U.S. treasury bills, as well as cash and cash equivalents in U.S. dollars. The reserves are held by a custodian, First Digital Trust Ltd., a public trust company registered in Hong Kong, and at financial institutions in Switzerland, Australia, and Hong Kong.

Our stablecoin stability assessment of 4 includes a negative adjustment from the asset assessment. We see weaknesses in relation to the absence of asset segregation to protect holders in the event of the issuer’s insolvency and the lack of a regulatory framework. In addition, we note limitations regarding FDUSD’s primary redeemability, its liquidity not yet being fully established in the secondary market, and its short track record, since it was issued only in June 2023.

The stablecoin stability assessment could improve if there is increased transparency, allowing us to evaluate the creditworthiness of the bank account providers and custodians holding the reserves. Factors such as regulatory oversight or supervision, improved secondary liquidity, and a longer history of price stability could also support a stronger assessment. Conversely, the stablecoin stability assessment could worsen if we observe a shift toward more high-risk assets.

Asset assessment

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<tbody>
<tr>
<td>1</td>
<td>Very strong</td>
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<tr>
<td>2</td>
<td>Strong</td>
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<tr>
<td>3</td>
<td>Adequate</td>
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<tr>
<td>4</td>
<td>Constrained</td>
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<td>5</td>
<td>Weak</td>
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Adjustment

Negative (1)

Stablecoin stability assessment

Constrained

Assessed on a scale of 1-5, where 1 is very strong and 5 is weak.

This report was not produced at the request of the stablecoin issuer or sponsor.
First Digital USD (FDUSD)

Asset assessment: 3 | Adequate

FDUSD was issued in 2023 and is a fully fiat-collateralized stablecoin. It is issued by FD121 Ltd. (First Digital Labs), which is part of Hong Kong-based First Digital Group. The reserves for FDUSD consist of highly liquid and secure assets, such as short-term U.S. treasury bills—held directly or as collateral for repurchase agreements (repos)—and U.S. dollar cash deposits. However, we are uncertain about the identity and creditworthiness of some financial institutions where these reserves are deposited.

FDUSD has published a monthly reserve report since July 2023. Based on the most recent report published by First Digital Labs and audited by Prescient Assurance LLC, as of Oct. 31, 2023, FDUSD had $565.0 million of reserves backing $563.0 million of FDUSD in circulation. The overall collateralization ratio stood at 100.3%: 72.0% ($405.3 million) representing U.S. treasury bills maturing in less than three months, 21.8% ($122.7 million) cash deposits in U.S. dollars, 2.0% ($11 million) one-month U.S. dollar fixed deposits, and 4.6% ($26 million) overnight reverse repos collateralized by U.S. treasury bills. The assets are being held by the appointed custodian, First Digital Trust Ltd., a public trust company registered in Hong Kong, as well as by financial institutions in Switzerland, Australia, and Hong Kong. The identities and creditworthiness of these entities have not been disclosed.

Exposure to currency or interest rate risks appears limited. Since FDUSD’s reserves are either held as U.S. treasury bills with tenors of less than three months, or as U.S. dollar cash deposits, there is no exposure to foreign currency risk. Exposure to interest rate risk is limited by the short-dated nature of these instruments.

Lack of information on the financial institutions where reserves are held weighs on our asset assessment. Although the reserves are made up of highly liquid, secure assets, limited information regarding the identities and creditworthiness of the bank account providers holding the cash deposits and the custodians of the U.S. treasury bills implies potential counterparty risk for the reserves. Hence, our asset assessment is 3 (adequate).

FDUSD—Asset composition

Sources: S&P Global Ratings, First Digital Labs.
Adjustment: Negative

Overall adjustment
We applied a negative adjustment to reflect certain weaknesses: There is no asset segregation to protect FDUSD holders in the event of the issuer’s insolvency and FDUSD is not subject to a regulatory framework. In addition, we note limitations regarding FDUSD’s primary redeemability, its liquidity not yet being fully established in the secondary market, and its short track record, since it was issued only in June 2023.

Governance: Transparency of reserves through monthly reporting and third-party attestations
- The founders and core team at First Digital Labs comprise Vincent Chok (CEO) and Gunnar Jaerv (chief operating officer). The FDUSD whitepaper states under its investment mandate that the reserve is to be composed of cash; very short-dated, highly liquid U.S. treasury bills; and overnight reverse repos.
- Transparency is maintained through monthly reporting of reserve holdings and third-party attestations. First Digital Labs publishes a monthly reserve report outlining the composition of reserves.
- In addition, these assets are subject to monthly review and attestation by an independent auditor. The most recent attestation was in October 2023 and conducted by Prescient Assurance, a U.S.-based accounting firm. The auditor reviews the assets of the company at the end of each month.

Regulatory framework: Lack of regulation and information about asset segregation
- The issuing entity, First Digital Labs, is part of the Hong Kong-based First Digital Group. FDUSD is not subject to regulation or supervision by a regulatory authority. We see this as a weakness compared with other stablecoins that are subject to regulation and/or supervision. We note that the Hong Kong Monetary Authority is in the process of seeking comments regarding the regulation of stablecoins and aims to introduce a regulatory framework by the end of 2024.
- FDUSD’s reserves are held in segregated bank accounts in the name of First Digital Labs through First Digital Trust, a Hong Kong-registered trust services provider. We understand from FDUSD’s white paper that the reserve assets are segregated from the assets of the trust provider (First Digital Trust) in the event of the trust provider’s bankruptcy. However, there is no publicly available information about the segregation of FDUSD’s assets and their remoteness from a bankruptcy of the issuer, First Digital Labs.
Liquidity and redeemability: Restricted primary redeemability and FDUSD is yet to be established in the secondary market

- FDUSD can be redeemed directly with First Digital Labs. However, redemption is restricted to institutional clients of First Digital Labs that comply with specific requirements, including anti-money-laundering and counter-terrorism-financing checks. Details of the redemption terms—such as minimum amounts, associated fees, and processing time—are not disclosed.

- Retail holders of FDUSD must go through the secondary market to redeem them. Currently, Binance is the only major exchange facilitating FDUSD trading, having encouraged its trade by eliminating trading fees. There has been an increase in the trading volume and market capitalization of FDUSD. However, FDUSD has yet to fully establish its presence in the secondary market.

- The availability of parties that can support redemption payments 24 hours a day, seven days a week, remains limited. Therefore, FDUSD’s redemption is constrained by the banking system’s operating hours.

Technology and third-party dependencies: The smart contract has recently been audited but the code is not open source

- FDUSD was deployed on the blockchain networks Ethereum and BNB Smart Chain as the standard tokens ERC-20 and BEP-20, respectively.

- The FDUSD smart contract was audited by Peckshield in May 2023, which did not find any major issues. However, the auditors pointed to potential risks associated with using a centralized, externally owned account as an owner’s wallet. The issuer has addressed this by switching to a multisignature wallet, which requires more than one private key and thus adds a layer of security.

- The smart contract for FDUSD is not open source, unlike that for most other stablecoins. Hence there is also no bug bounty program offering incentives for identifying and reporting vulnerabilities. The smart contract has, however, been verified and is written in the industry’s standard programming language, Solidity. There is no dependence on oracles to connect to data and information from external market systems.

- Since all FDUSD’s reserves are held and managed outside the blockchain network, there is less reliance on blockchain technology. Therefore, a major disruption of the blockchain network is likely to have a limited impact on FDUSD’s stability.

Track record: Only about six months in circulation

- Since its launch in June 2023, FDUSD has maintained a generally stable price. There is no long-term track record of price stability, particularly during times of major market volatility.

- FDUSD’s market capitalization almost quadrupled to $590 million as of Nov. 1, 2023, from $155 million on Aug. 1, 2023. As of Nov. 30, 2023, its market capitalization had reached $965 million.
First Digital USD (FDUSD) | Stablecoin Stability Assessment

This product does not constitute a rating action.

Dec. 12, 2023

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