

Investment Activities and Portfolio Management – Experience of Malaysia

Jazimin Izzat Wan Zoolkifli
Financial Controller
Malaysia Deposit Insurance Corporation

**Investment Management for
Deposit Insurance Agencies**



February 20-22, 2013
MUMBAI, INDIA



निक्षेप बीमा और प्रत्यय गारंटी निगम

DEPOSIT INSURANCE AND CREDIT GUARANTEE CORPORATION

(भारतीय रिज़र्व बैंक की संपूर्ण स्वामित्ववाली सहयोगी Wholly owned subsidiary of the Reserve Bank of India)

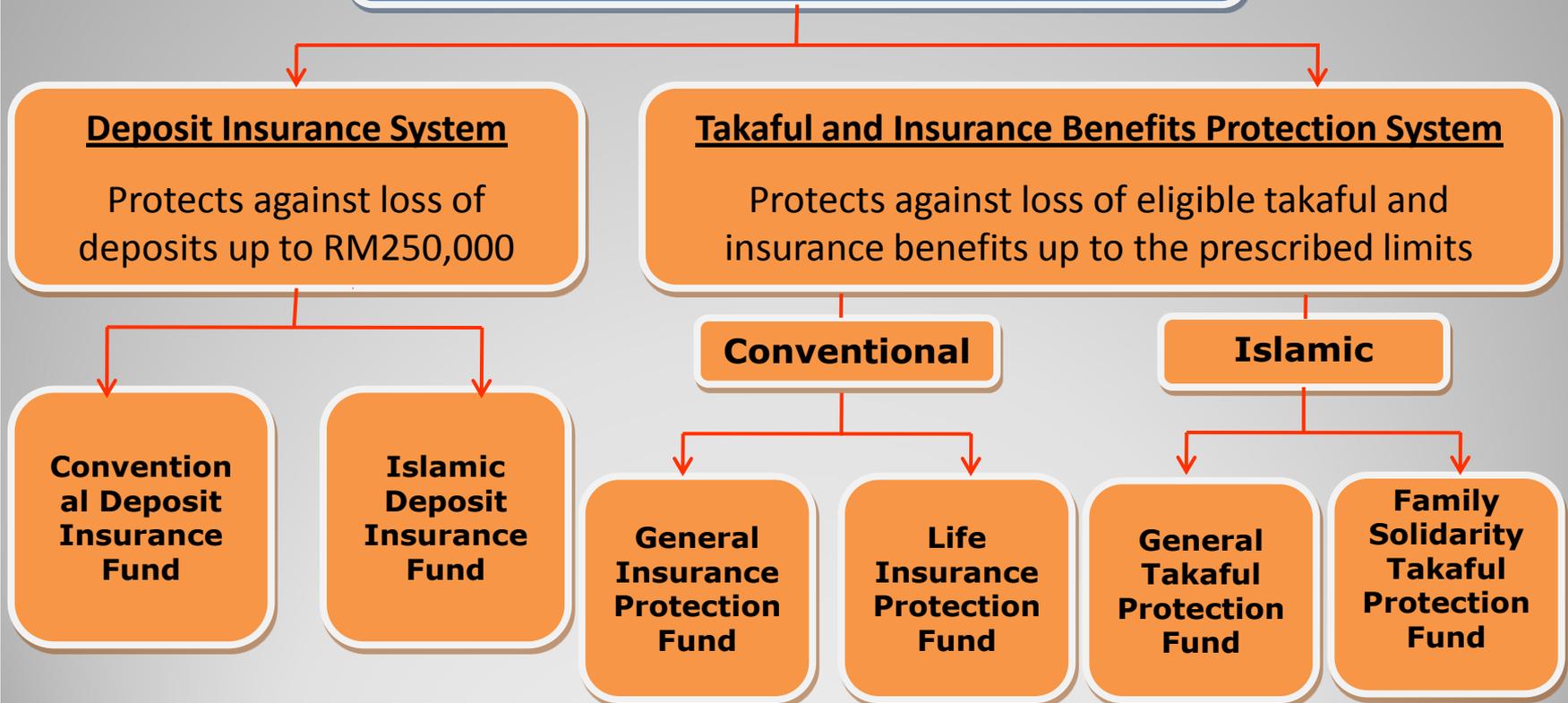
MDIC: A GOVERNMENT STATUTORY BODY ...

- with legislated mandate to:
 - administer a deposit insurance system and a takaful and insurance benefits protection system
 - protect part or all deposits and part or all takaful or insurance benefits
 - provide incentives for sound risk management
 - contribute to the stability of the financial system
- the mandate to administer a takaful and insurance benefits protection system was legislated effective 31 December 2010
- with no capital structure therefore, no dividend payable
- exempted from income tax
- fully backed by the Government
- subject to:
 - audit by the National Audit Department of Malaysia
 - financial reporting requirements (tabling of annual financial statements to Parliament)
 - compliance with approved Financial Reporting Standards

* *Takaful: Islamic insurance*

MANAGEMENT OF FUNDS

MDIC administers 2 separate financial consumer protection schemes



No commingling of funds

Investment Management for Deposit Insurance Agencies

February 20-22, 2013, Mumbai, India

FUNDING FRAMEWORK

Objectives:

- To cover day-to-day operating expenditures
- To build funds available for meeting future obligations to depositors

Considerations:

- MDIC's role in the financial safety net
- Legislative powers relating to sources of funding
- Clear objectives for internal and external sources of funding

Sources of Funds

INTERNAL FUNDING

Ex-ante premiums and levies

Ex-post premiums and levies

Investment income

EXTERNAL FUNDING

Borrowings from Government

Raise funds from capital market

Others and necessary and appropriate

Purpose

- To cover operating expenses
- To build Funds over time to reach "Target Funds"
- To address liquidity needs in case of intervention and failure resolution

Sequencing of funding:

1. Internal Funds (Liquidate portfolio of investments)
2. Borrow from Government
3. Replace with capital market funding or repay with premiums

Investment Management for Deposit Insurance Agencies

February 20-22, 2013, Mumbai, India

BACKGROUND

Section 30 of the Malaysia Deposit Insurance Corporation Act 2011 (“MDIC Act”) empowers the Corporation to invest in:

- Ringgit denominated securities issued or guaranteed by the Government or Bank Negara Malaysia (“BNM”) or of high investment grade rated by a reputable rating agency;
- deposits with BNM or any financial institutions; or
- any other investment approved by the Minister of Finance, upon recommendation of the Board.

The Act also specifies that the Corporation shall invest surplus Islamic funds in accordance with Shariah principles.

INVESTMENT

- Legislative provisions and Board-approved investment policy (reviewed annually) set out the parameters within which MDIC invests surplus funds.
- Investment policy:
 - ✓ Funds are invested in safe and liquid investment instruments to enable easy access when the need arises
 - ✓ Key objectives: Capital preservation and liquidity
 - ✓ Types of investment: Short-term government and central bank papers Islamic funds managed in accordance with Shariah principles
- Investments are held-to-maturity.
- Investment cycle.

INVESTMENT INSTRUMENTS

- Invests in short-term Government and Central Bank Papers.
- MDIC inherited certain investment assets (Insurance Guarantee Scheme Funds - IGSF) from the Central Bank, which were previously the guarantee funds for general insurance and life insurance businesses.
 - ✓ Part of these investments relate to long-term government and central bank papers as well as Private Debt Securities (not in line with the current Investments Policy).
 - ✓ Specific exemption and approval was obtained from the Board of Directors to maintain a portion of these investment portfolio.

RISK MANAGEMENT FRAMEWORK

- MDIC's current Financial Risk Policy primarily covers:
 - ✓ Market risk
MDIC's Market Risk arises from financial market conditions (e.g. interest rates, liquidity of market and availability of investments) that may reduce the value of the Corporation's investment portfolio.
 - ✓ Liquidity risk
MDIC's Liquidity Risk relates to the unavailability of funds for the Corporation to meet its future liabilities and commitments arising from the mandate or the day-to-day working capital requirements.
- MDIC's financial risk exposure may increase as a result of intervention and failure resolution.
- Risks policies reviewed regularly.

RISK MANAGEMENT PRACTICES

- On-going monitoring of financial risk exposure:
 - ✓ Marked-to-Market
Comparison of Marked-to-Market position against net book value (costs adjusted for amortisation of premiums and accretion of discounts).
 - ✓ Market Intelligence
Information and analyses from bond pricing agency, investment houses as well as Central Bank.
- On-going reporting:
 - ✓ Quarterly to Audit Committee (“AC”) and Board, monthly to Management.
 - ✓ Detailed information of portfolio reported to AC, Board and Management.
 - ✓ ALCO – portfolio information as well as financial risk issues.

ADMINISTRATION OF INVESTMENT ACTIVITIES

- Investment strategy is guided by the Assets & Liabilities Management Committee “ALCO” and reviewed on an annual basis.
- MDIC has entered into a service level agreement with Central Bank of Malaysia (“BNM”). BNM provides treasury and custodial services in respect of MDIC’s investments (front office service). This arrangement is partly to manage any **signalling issues** as well as facilitate high volume transactions (when required).
- MDIC manages middle and back-room processing. Investment decisions are made by MDIC.

STRUCTURE OF TREASURY FUNCTION

- MDIC operates middle and back-room office. This involves making investment decisions based on approved investment policy and strategies, preparation of investments instructions and record-keeping (maintaining of investment schedules and journalise investment transactions into financial system).
- Front office function is carried out by the Central Bank under the Treasury and Custodial Services Agreement.

ISSUES AND CHALLENGES

Shariah matters:

- Compliance with Shariah tenets in managing the 3 Islamic Funds.
- Funding must be from sources that are Shariah compliant, i.e. does not have any element of interest or gambling and any borrowing must be based on Islamic contract.
- Additional processes over and above the normal accounting processes to manage such issues and ensure compliance with Shariah tenets.

Investments:

- Nature of insurance/takaful business and its exposure which are different to that of banks – insurance business liabilities more long-tailed.

QUESTIONS AND ANSWERS

**Investment Management for Deposit Insurance Agencies
February 20-22, 2013, Mumbai, India**

THANK YOU

**Investment Management for Deposit Insurance Agencies
February 20-22, 2013, Mumbai, India**