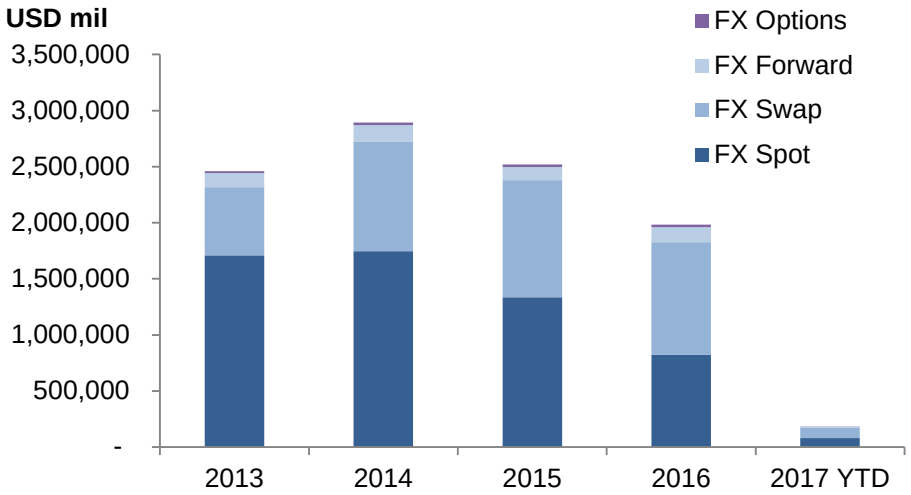
Initiatives to Develop the Onshore Financial Market

- Onshore FX hedging by non-resident investors

BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Malaysian Foreign Exchange Market

Turnover by major instruments



Major onshore FX (2016)

Rank	Spot	Forward
1	CIMB	HSBC
2	MAYBANK	MAYBANK
3	HSBC	CITIBANK
4	CITIBANK	STANDARD CHARTERED
5	STANDARD CHARTERED	CIMB
	Market share: 56%	**Market share:62%**

Source: BNM Ringgit Operations Monitoring System (ROMS)

- Over the past 4-years, the overall annual FX liquidity averaged around USD2.5 trillion
- Non-resident have been a major contributor to FX market turnover with 44% market share.
- Average daily volume (Jan 2016-Jan 2017) :
  - Spot: USD3.4 billion
  - Forward & Swap: USD4.7 billion
  - Forward: USD536 million
- Bid-offer spread for spot and forward is around 10 to 25pips

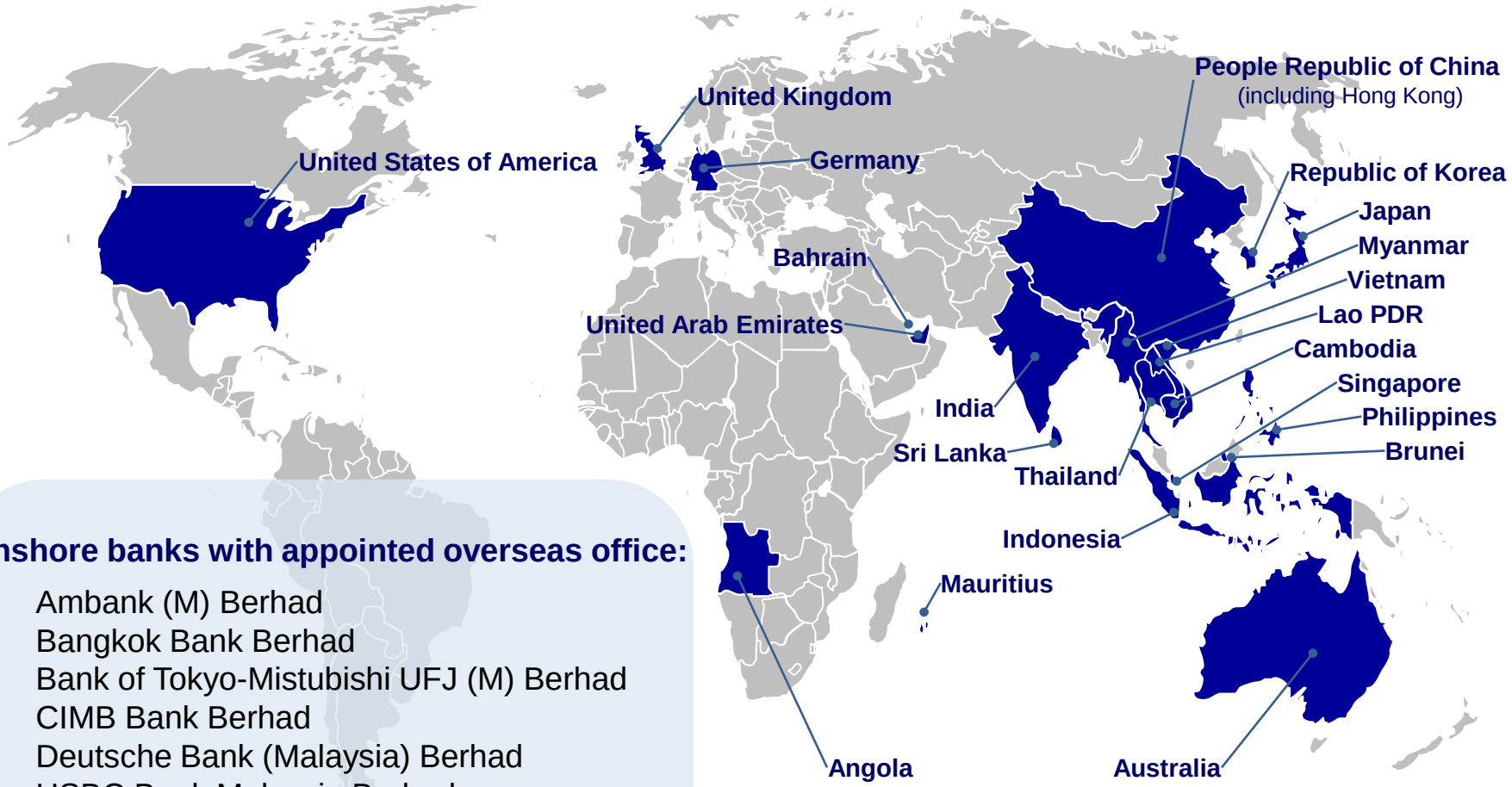
Update on Investor Registration for Dynamic Hedging

- To date, a total of 20 participants (consisting of 39 funds) have successfully registered, comprising 10 non-residents and 10 residents with total eligible assets amounting to RM44.7 billion.

Status	Non-resident	Eligible Assets *(RM bil)*	Resident	Eligible Assets *(USD bil)*	RM bil Equiv.
Registered	10	16.6	10	6.3	28.1
Registered Eligible Assets *(RM bil)*	44.7				
Total Registered	20				

* Data as at 24th February 2017

Location of Appointed Overseas Office in 23 countries



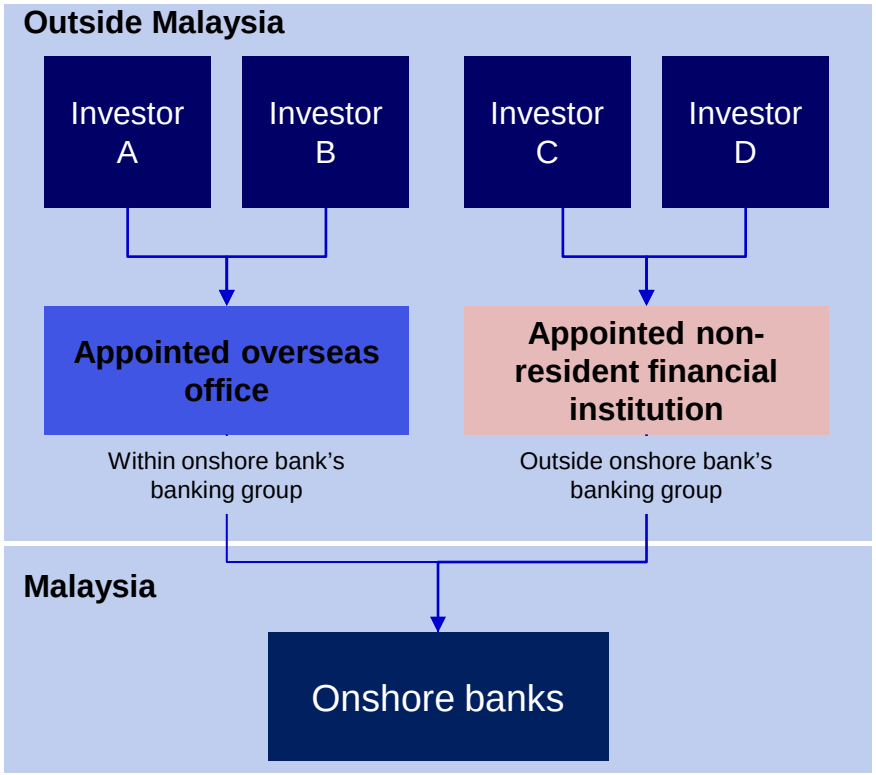
Onshore banks with appointed overseas office:

- Ambank (M) Berhad
- Bangkok Bank Berhad
- Bank of Tokyo-Mistubishi UFJ (M) Berhad
- CIMB Bank Berhad
- Deutsche Bank (Malaysia) Berhad
- HSBC Bank Malaysia Berhad
- Malayan Banking Berhad
- Public Bank Berhad
- Standard Chartered Bank Malaysia Barhad
- United Overseas Bank Malaysia Berhad

(Full list of the appointed overseas office is made available on Bank Negara Malaysia's website as at 1 March 2017)

Non-residents to have enhanced accessibility to the onshore financial market through Appointed Overseas Office

- Facilitate ringgit settlement for trade and investment through an authorised platform overseas.
- Appointed overseas office may include non-resident financial institution outside the licensed onshore bank's banking group.



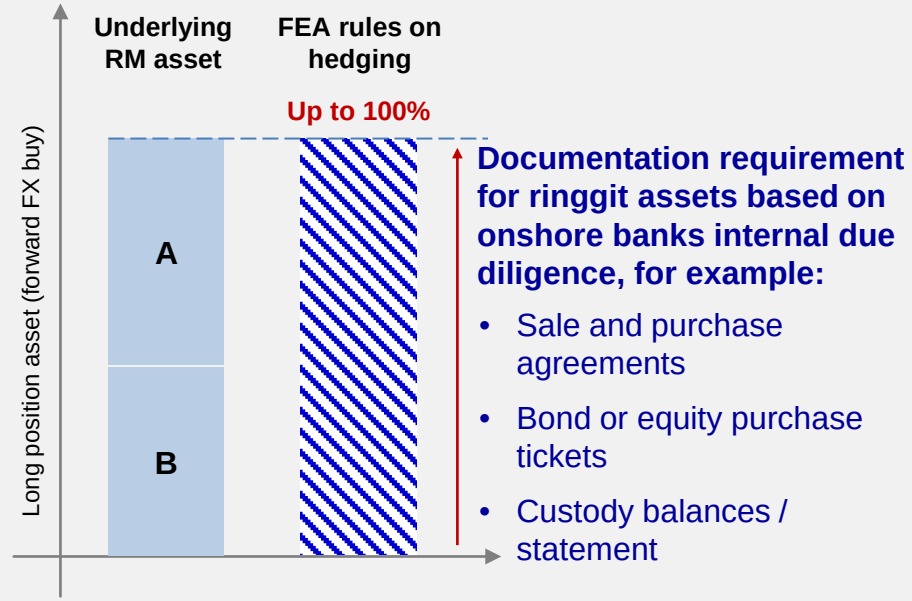
- Through Appointed Overseas Office framework, the type of ringgit transactions include:
  - Spot (any purpose); or
  - Forward (supported by underlying trade or ringgit asset).
- Transactions undertaken under the framework, must be made back-to-back with the onshore bank.

In December 2016, Bank Negara Malaysia announced measures to create a deeper, more transparent and well-functioning FX market

Transactions (by non-resident)	**Pre December 2016**	**Post December 2016**
Spot	Freely allowed	
Ringgit Deposit Onshore	Freely allowed	
Forward Hedging	▪ Passive hedging with underlying on transactional or portfolio basis	▪ Passive hedging with underlying on transactional or portfolio basis ▪ Dynamic hedging upon registration
Counterparty for FX transactions	▪ Licensed Onshore Bank ▪ Appointed Overseas Office (AOO) within same banking group	▪ Licensed Onshore Bank ▪ AOO within same banking group ▪ AOO outside banking group*

* Upon approval from Bank Negara Malaysia

Passive hedging by non-resident investor



Documentation requirement for ringgit assets based on onshore banks internal due diligence, for example:

- Sale and purchase agreements
- Bond or equity purchase tickets
- Custody balances / statement

(Submission of documentation can be post-trade depending on bank's internal due diligence)

Forward	A. Passive hedge	B. Dynamic hedge
FX buy	Up to 100% of underlying	Up to 25% of underlying
FX sell	Cancellation not allowed if underlying still exists	
Documentation of underlying asset	Required	Not required

HEDGE BASED ON UNDERLYING RINGGIT ASSET

1. Non-resident may hedge up to the full amount of underlying based on firm commitment with –
- ✓ Onshore banks
- ✓ Appointed Overseas Office

Forward FX shall be less or equivalent to the amount of Ringgit asset (no over-hedge position).

2. Investor is allowed to hedge on transactional or portfolio basis.

3. Liquidation of RM assets associated to hedge.
Not required to adjust or may hold contract upon sale of securities provided that the total amount of forward contract does not exceed the total amount of ringgit asset including proceeds and income arising from sales of ringgit asset held in the external account.

4. Price movement of underlying or forward contracts.
The investor is allowed to adjust the hedge to ensure that the security is not over-hedged or hold the contract until maturity.

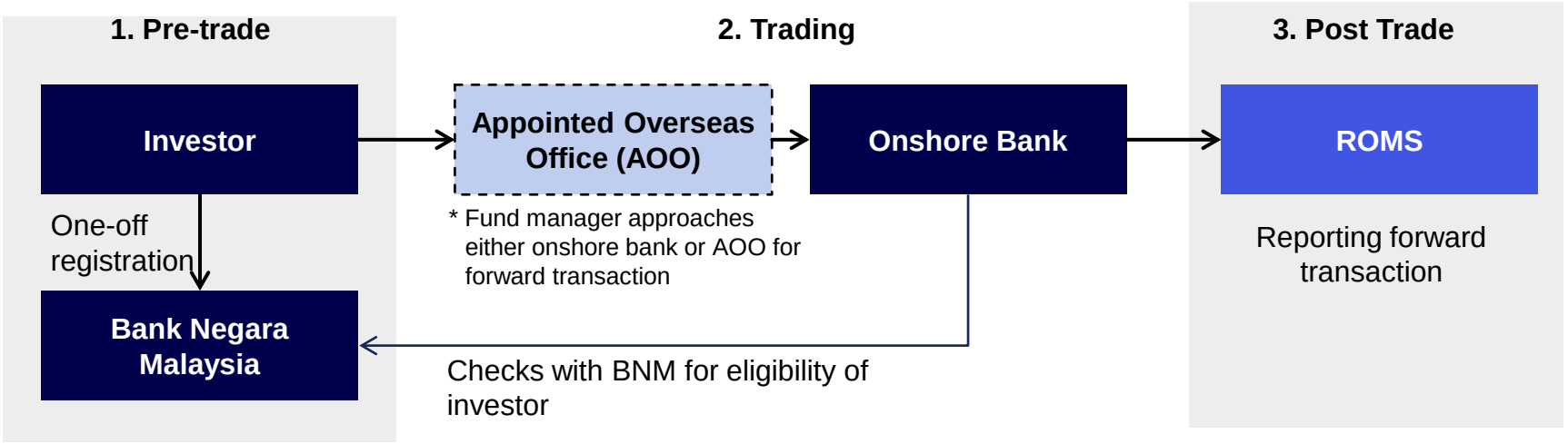
5. Cancellation or unwinding of FX forward
Requires approval from Bank Negara Malaysia if underlying still exists.

6. Investors have the option to lapse the forward contract or rollover as long as underlying amount > forward contract

Non-resident institutional investors can engage in dynamic hedging up to a threshold of 25%

- **Flexibility:** Institutional investors (resident and non-resident) to hedge and un-hedge forward contracts for underlying investments

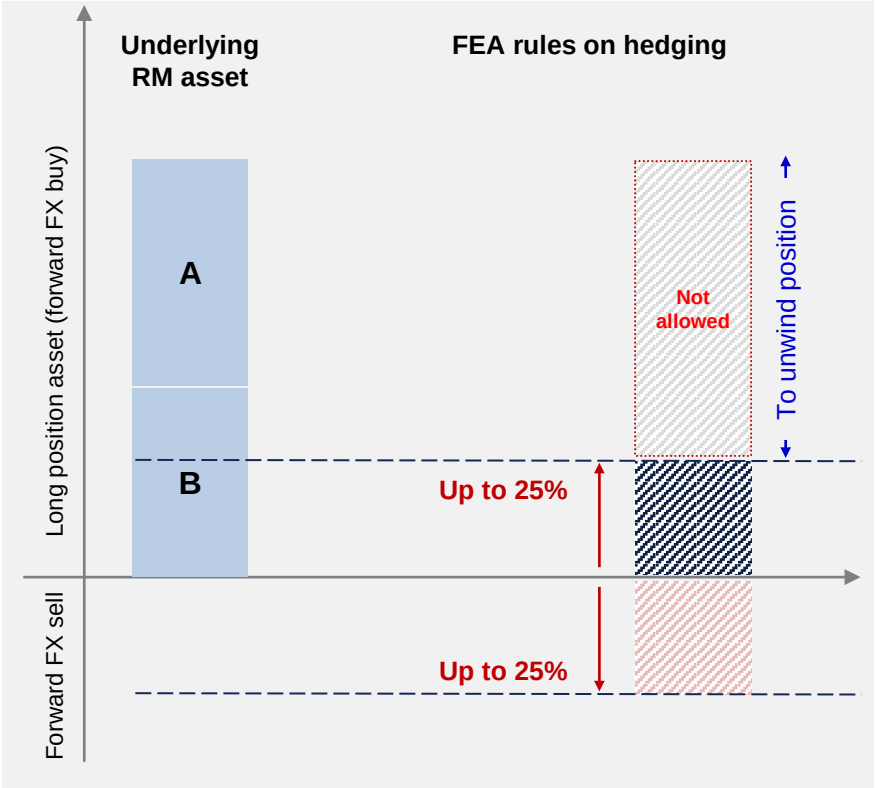
- **Threshold:** 25% of nominal value of asset holdings upon registration with BNM



Example:
A fund manager holds RM100 mil worth of Malaysian Government Securities (MGS), maturing December 2018. Fund manager is allowed to undertake forward transaction i.e.: forward sell or buy FX/MYR up to RM25 mil.

Position \Day	T+1	T+2	T+3	T+4	T+5	T+6
Forward	-20	+10	-15	+25	-20	+35
Net forward position	-20	-10	-25	0	-20	+15

Dynamic hedging by non-resident institutional investor



Forward	A. Passive hedge	B. Dynamic hedge
FX buy	Up to 100% of underlying	Up to 25% of underlying
FX sell	Cancellation not allowed if underlying still exists	
Documentation of underlying asset	Required	Not required

DYNAMIC HEDGE

1. Investors may enter into dynamic hedging upon registration with Bank Negara Malaysia using the "Forward Market Participation Form"...

- Registration for the scheme can be undertaken at a firm level.

2. Freedom to actively manage up to 25% of nominal value of asset holdings (net forward position) with onshore banks or AOO.

- Investors/ fund managers are responsible to monitor their net outstanding forward position to ensure the 25% threshold is observed.
- BNM will be in contact with investors should the threshold is breached.
- Position above 25% threshold must be unwound. BNM may review investor's eligibility for this framework.
- Investor is also able to apply for higher threshold and is subject to approval on a case-by-case basis.

(Resident institutional investors may also register for dynamic hedging)

Frequently Asked Questions – Dynamic Hedging

No	Questions	Answers
1	Are investors permitted to register for dynamic hedging at the firm level instead of the fund level?	Yes.
2	If an investor is registered at the firm level, is it permitted to “carve out” specific funds for passive hedging?	Yes. Investor has to make a one-off declaration. Funds that are “carved out” for passive hedging are not eligible for dynamic hedging.
3	Can an investor use their existing Legal Entity Identifier (LEI) ?	Yes. If an investor does not have an LEI, BNM will provide an ID to the investor.
4	Is there a requirement to have segregated cash accounts for settlement of onshore forward transactions?	No.

Frequently Asked Questions – Dynamic Hedging

No	Questions	Answers
5	Licensed onshore bank is required to verify the registration status of an institutional investor, how is this achieved?	Licensed onshore bank to conduct a one-off verification with BNM.
6	How shall the 25% limit be allocated if the investors maintain accounts with several custodian banks?	The 25% limit is applicable on the combined overall holdings of the respective custodian banks.
7	Can an investor continue with the forward contract which has exceeded 25% limit by providing documentary evidence to prove the firm commitment for the forward contract?	Yes. Investor need to inform BNM on the action plan.
8	Can an investor register for dynamic hedging prior to the purchase of MYR assets?	Yes.

Frequently Asked Questions – Passive Hedging

No	Questions	Answers
9	What is deemed as documentary evidence?	It depends on banks internal due diligence, for example: • Sale and purchase agreements • Bond or equity purchase tickets • Custody balances / statement
10	Can investors enter into a forward passive hedge for any tenor within a security's maturity and then roll it over once the forward matures?	Yes. Investors have the option to lapse the forward contract or rollover as long as underlying amount is greater than forward contract
11	Can a passive hedge be unwind or cancel?	Cancellation or unwinding is allowed if underlying no longer exist or fails to materialise. Prior approval from the Bank is required if the underlying still exists.
12	Can investor unwind/cancel a hedge position with a different counterparty?	No

Frequently Asked Questions – Passive Hedging

No	Questions	Answers
13	Can investor rollover a hedge position with a different counterparty?	Yes.
14	When the price of the security or the forward FX rate moves, is it possible to adjust the hedge accordingly or does the security have to remain under- or over-hedged?	Investor has the option to adjust or maintain its existing exposure.
15	When a bond is liquidated can the associated passive hedge be used to hedge the sale proceeds?	Yes. Investor may continue to hold its forward contract even when the ringgit asset is sold prior to maturity of the tenure of the forward contract.
16	Can a passive hedge be at portfolio basis or securities by securities basis?	It can be both.

Frequently Asked Questions – Others

No	Questions	Answers
17	Are there any restrictions on retaining sale proceeds onshore?	No there is no restrictions. The sales proceeds can be retained onshore in ringgit or foreign currency.
18	If the passive hedged sale proceeds from an investment continue to be held onshore and the forward hedge matures, does the cash have to be repatriated or can a new forward trade be entered into to hedge the cash?	No, the cash can be retained onshore. Investors can't enter into a new forward trade to hedge the cash.
19	Can investor transact FX with banks other than their own custodian banks?	Yes, with onshore banks or appointed overseas office.
20	Can investors access the onshore market via the Appointed Overseas Offices without having to set up accounts an account with a counterparty resident onshore?	Yes.