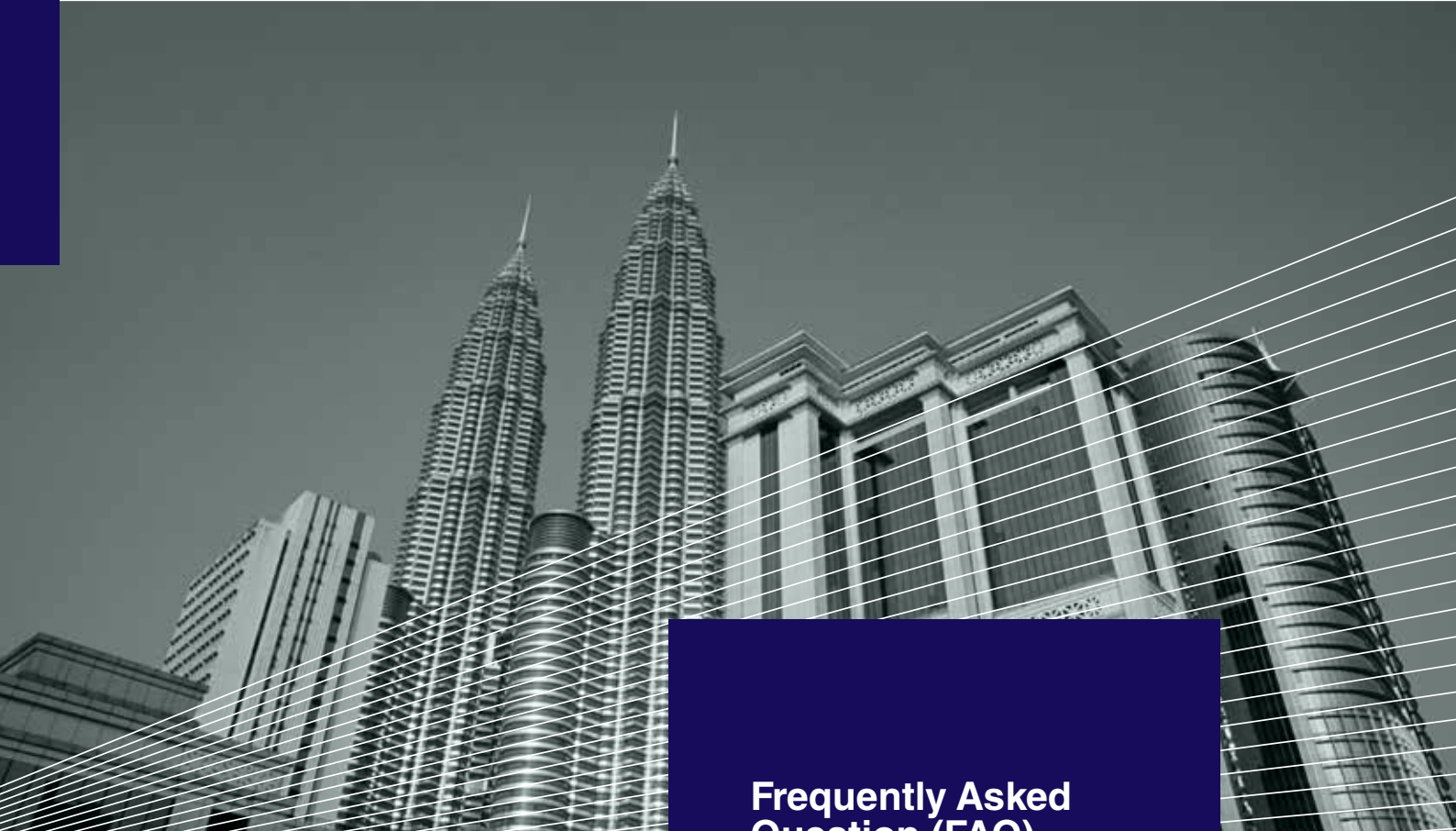




BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA



Frequently Asked
Question (FAQ)

**MALAYSIAN
GOVERNMENT
INVESTMENT
ISSUE (MGII)**

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MALAYSIAN GOVERNMENT INVESTMENT ISSUE (“MGII”)

Instrument Overview

What is MGII?

MGII stands for Malaysian Government Investment Issue and is a form of marketable government debt securities issued by the Government of Malaysia to raise funds from the domestic capital market to finance the Government’s development expenditure. MGII is Islamic securities issued in compliance with *Shariah* requirements and is an alternative debt instrument for the Government. Other forms of government debt instruments are the Malaysian Government Securities (MGS), Malaysian Islamic Treasury Bills (MITB) and Malaysian Treasury Bills (MTB).

What is the governing law for MGII?

MGII is issued under the Government Funding Act 1983 to enable the Government of Malaysia to raise funding in accordance with *Shariah* principles. The terms and conditions of the MGII are governed by, and construed in accordance with, the laws of Malaysia.

Issuance structure of MGII

Effective from 22 July 2013, MGII is issued based on *Murabahah* concept. MGII based on *Murabahah* contract is essentially a certificate of indebtedness arising from a deferred mark-up sale transaction of an asset, such as commodity (mainly crude palm oil), which complies with *Shariah* principles. This new issuance under *Murabahah* contract will involve commodity transactions to create indebtedness between the sukuk issuer and the investors (refer to Appendix I).

Meanwhile, the MGII issued prior to 22 July 2013, is based on *Bai Al-Inah* contract, which involves sell and buy back of asset in Islamic finance (refer to structure in Appendix II).

Reference can be made by following these websites:

Shariah Advisory Council (SAC) of Bank Negara Malaysia

<http://www.bnm.gov.my/index.php?ch=7&pg=715&ac=802>

Shariah Resolution in Islamic Finance, Second Edition

http://www.bnm.gov.my/microsites/financial/pdf/resolutions/Shariah_resolutions_2nd_edition_EN.pdf

The Government of Malaysia reserves the right to opt for other *Shariah* compliant structures depending on the strategic outcome and factors that are in line with the development of a vibrant Islamic financial market.

What is the mode of issue for MGII?

MGII is auctioned by Bank Negara Malaysia in its role as issuance agent to the Government, through a variable-rate multiple-price auction format (also known as English auction) via Fully Automated System for Issuance/Tendering (FAST). The auction process of MGII is similar to the conventional government securities, the Malaysian Government Securities (MGS).

All bids at primary issuance must be submitted through the Principal Dealers’ (PDs) network whom are appointed by Bank Negara Malaysia.

Players/Investors of MGII

Who are the investors of MGII?

Both Islamic and conventional players can subscribe and trade MGII. Among the primary investors of Government securities are the Employees Provident Fund (EPF), financial institutions including PDs, insurance companies including Takaful operators (Islamic insurers), asset management companies and foreign financial institutions.

Trading and liquidity of MGII

What are the issuance size and tenure for MGII?

MGII issuance programme is pre-announced in the auction calendar with issuance size ranging from RM2 billion to RM5 billion and with original maturities of 3-, 5-, 7-, 10-, 15- and 20-year.

In 2015, the gross issuance of MGII accounts for 44% of Government borrowing programme with a total outstanding size amounting to RM214 billion or 39% of total government debt securities. The size is expected to grow larger as the Government is committed to issue MGII regularly.

What contract is used for MGII secondary trading?

Secondary trading of MGII is undertaken by Islamic contract known as *Bay' Al-Dayn* (debt trading). *Bay' Al-Dayn* or sale of debt can be defined as the sale of payable right or receivable debt either to the debtor or to any third party. This type of sale is usually for immediate payment or for deferred payment.

On 21 August 1996, the Malaysian Securities Commission *Shariah* Advisory Council passed a resolution that unanimously agreed to accept the principle of *Bay' Al-Dayn* as one of the concepts for developing Islamic capital market instruments. This was based on the views of some of the Islamic jurists who allowed this concept subject to certain conditions for instance there is a transparent regulatory system in the capital market to safeguard the *maslahah* (public interest) of the market participants.

Is MGII actively traded in the secondary market?

MGII is actively traded in the secondary market with annual turnover reaching RM456 billion in 2015. Average daily turnover of MGII has increased from RM864 million (2010) to RM1.85 billion in 2015. The most actively traded MGII are the benchmark issues of the 3-, 5-, 7- and 10-year maturity.

Principal Dealers (Islamic and conventional) play a key-role in market making and promoting liquidity of the paper.

What is the standard trading lot for MGII?

RM10 million, similar to MGS.

What is a MGII Reopening?

The MGII reopening, similar to an MGS reopening, aims to build the outstanding value of MGII stock to a desired level, hence promoting greater liquidity in a particular stock and the market as a whole.

Settlement

How does the settlement of MGII take place?

The settlement of the primary and secondary market transactions of MGII, which are similar to other government and unlisted corporate debt securities, take place via the Scripless Securities Depository System (SSDS), which is part of the Real Time Electronic Transfer of Funds and Securities (RENTAS) system. The RENTAS system, which has straight-through-processing capability would process, transfer and settle interbank funds and scripless transactions simultaneously in real-time. The RENTAS system is a delivery versus payment (DvP) Model 1 system, i.e. securities and funds settle gross throughout the day.

The standard settlement day for primary issue is T+1 while the settlement for secondary market trading is T+2.

Tax Treatment

Is the income derived from the MGII investment subject to any tax?

There is no capital gains tax in Malaysia and there is no stamp duty relating to the issuance and transfer of government debt securities or private debt securities approved by the Securities Commission (SC).

Resident individuals, unit trust companies and listed closed-end fund companies are exempted from income tax for interest income/profit earned from ringgit-denominated government debt securities and private debt securities in Malaysia. Non-resident investors are also exempted from withholding tax on interest income/profit earned from ringgit-denominated debt securities issued by Government of Malaysia as well as private debt securities approved by the SC.

Regulatory Treatment

What is the regulatory treatment accorded to the MGII?

MGII is accorded the same regulatory treatment as MGS as follows:

- (i) 0% risk weight under the Risk-Weighted Capital Adequacy Framework and the Capital Adequacy Framework for Islamic Banks;
- (ii) Class-1 liquefiable assets status under the Liquidity Framework, subject to a yield slippage of 2%;
- (iii) Eligible collateral for Standing Facility;
- (iv) Excluded from *Single Customer Credit Limit*;
- (v) 0% risk charge under the Risk-Based Capital Framework for Insurers;
- (vi) Holdings of MGII in the trading book can be deducted from the eligible liabilities base for the purpose of computing the SRR. For PDs, entire holdings of MGII can be deducted from the eligible liabilities base for SRR computation.

Similarities and differences between MGII and MGS

What are the similarities and key differences between MGII and MGS?

MGII is similar to MGS in terms of effective cash flows, issuance mode, and legal status in being a direct obligation of the Government and its nature of transaction as financial products (trading on the normal yield-price relationship).

MGII and MGS differ in its structure in terms of complying with *Shariah* requirements in its issuance. Due to its structure, coupon for MGII is referred to as 'profit rate'.

Does MGII represent the same certificate of indebtedness or liability of the Government as the MGS?

Yes. The MGII is similar to MGS in terms of their legal status in being a direct obligation of the Government.

How does profit payment in MGII differ from coupon payment of MGS?

The profit payment for MGII is to represent the sale of *Shariah*-compliant assets which is made up by half yearly profit payable to the investors similar to MGS coupon payment (see table

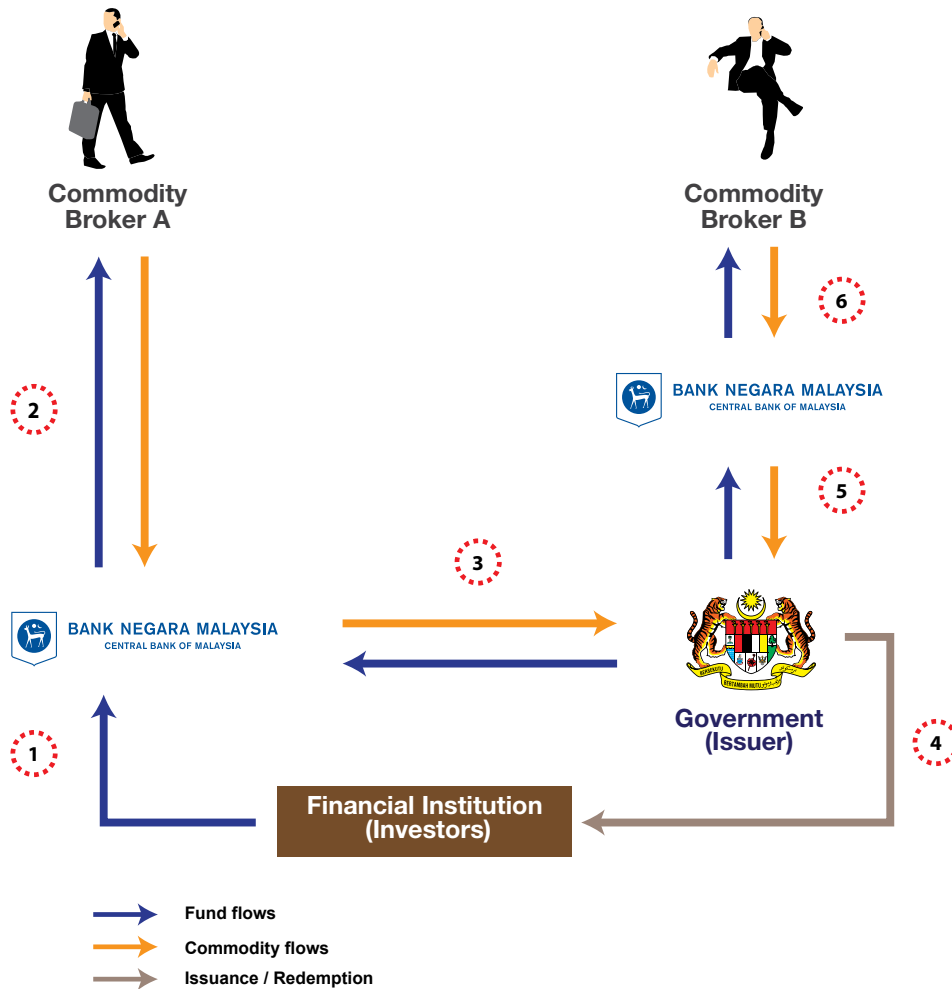
Comparison table between MGII and MGS

Features	MGII	MGS
Issuer	Government of Malaysia	Government of Malaysia
Tenure	3 - 20 years	3 - 30 years
Issue size	RM2 - RM5 billion	RM2 - RM5 billion
Return payment (interest/profit)	Profit payment is semi-annual. Profit rate is market-determined based on the weighted average successful yield of the issue. Day count basis is Actual/Actual.	Interest payment is semi-annual. Coupon rate is market-determined based on the weighted average successful yield of the issue. Day count basis is Actual/Actual.
Odd coupon	For odd coupon periods, coupon payment will be adjusted accordingly. For example, a long coupon period will be compensated by a higher number for the day count.	For odd coupon periods, coupon payment will be adjusted accordingly. For example, a long coupon period will be compensated by a higher number for the day count.
Method of sale in the primary market	Competitive multiple-price auction. Bids are submitted by Principal Dealers (Islamic and conventional) on a yield basis for new issues and price basis on reopened issues.	Competitive multiple-price auction. Bids are submitted by Principal Dealers (conventional) on a yield basis for new issues and price basis on reopened issues.
Redemption	Sukuk are redeemed at par upon maturity.	Bonds are redeemed at par upon maturity.

Appendix I

Malaysian Government Investment Issue Structure

(Based on *Murabahah* concept)

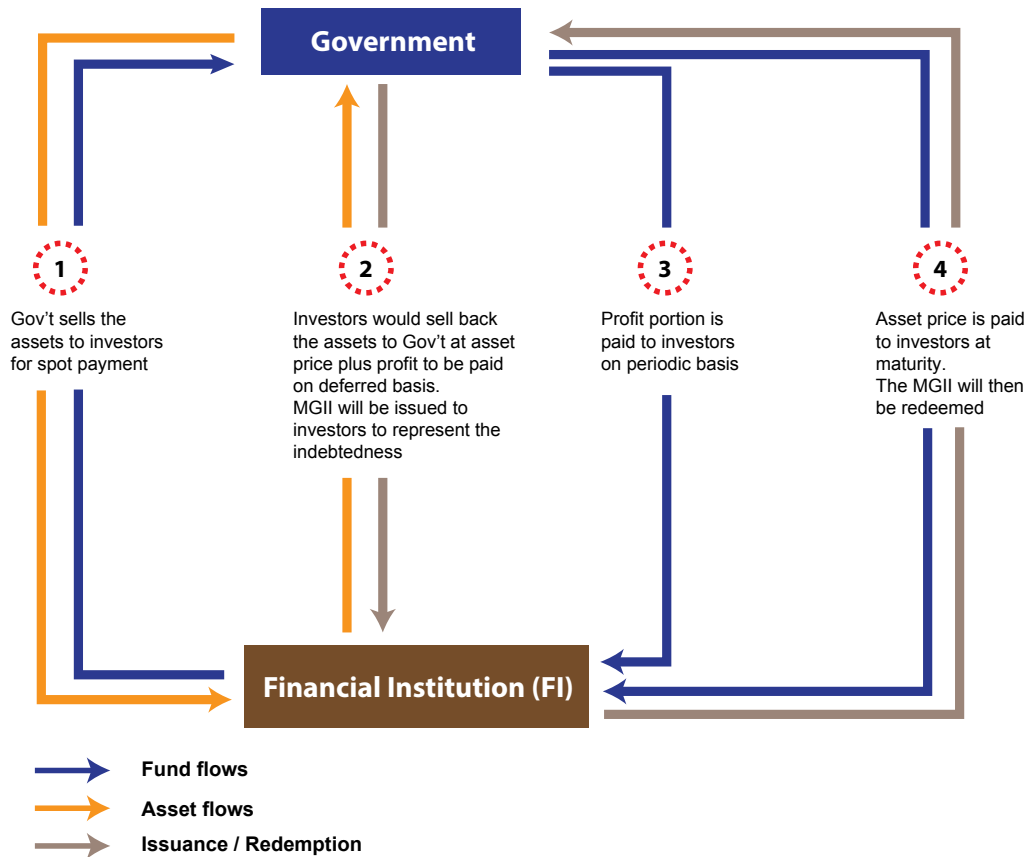


- 1 Investor will appoint BNM as their agent to buy the commodities.
- 2 BNM as the commodity agent will buy the commodities e.g Crude Palm Oil.
- 3 Upon completion of purchase, BNM as an agent to the Investor will sell the commodities to Government at mark-up price to be paid on deferred payment date. Profit from sale will be paid periodically such as semi-annual basis, representing the coupon on MGII.
- 4 MGII will be issued to evidence the indebtedness. Profit portion is paid to investors on periodical basis. On maturity (i.e. deferred payment date), Government will make payment, representing the principal amount and final profit, and MGII will be redeemed.
- 5 Government will appoint BNM as their agent to sell the commodity at cost to raise the required funding.
- 6 BNM as the commodity agent will sell the commodity and remit the cash to Government.

Appendix II

Malaysian Government Investment Issue Structure

(Based on *Bai Al-Inah* concept)



1 To raise the required financing, Government will first sell its *Shariah*-compliant assets, e.g. equities, to investors for spot cash payment.

2 Upon completion of sale, investors will subsequently sell the assets back to Government at profit paid on deferred, and MGII will be issued to evidence the indebtedness.

3 Profit from sale will be paid periodically such as semi-annual basis, representing the coupon on MGII.

4 On maturity (i.e. deferred payment), Government will pay the asset cost, representing the principal amount, plus profit and MGII will be redeemed.

