

8th Annual
Islamic Finance Summit

EUROMONEY SEMINARS

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**IIFM Master Agreement for Treasury Placement (MATP)
 and Managing Liquidity - challenges faced and overcome**


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Managing Liquidity in Islamic Finance

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- Limited number of Liquidity Management Products
 - Commodity Murabaha
 - Inter-bank Mudaraba
 - Wakala and Unrestricted Wakala (regional)
 - Short-term Sukuk (Bahrain, Brunei, Pakistan, Singapore)
 - Open-ended funds
 - Others (Qard Hassan, Malaysian LMT, CBB LMT, ABC LMT etc)
 - Absence of lender of last resort



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Managing Liquidity in Islamic Finance

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Surplus of Liquidity


- Liquid: Islamic Financial Institutions (IFI's) are generally more liquid than their conventional counterparts
- Low Returns: Limited short-term investments, hence IFI's earn low returns on liquid assets

Shortage of Liquidity

- Inter-Bank Market: IFI's have limited ability to tap short-term funds to meet cashflow requirements
- Lender of Last Resort: Most banking failures are due to liquidity shortages. There is a need for a "lender of last resort"

Maturity Mismatch


- Long-Term Assets: IFI's main investments are long-term e.g. sukuk, project finance, real estate
- Short-Term Liabilities: IFI's main funding is from short-term customer deposits
- Gap: IFI's have a mismatch risk



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Commodity Murabaha as a Product - Facts February 2009

- No Shari’ah Issues but excessive use raises concerns
- No Secondary Market trading options
- Doubts on amount of commodities vs transaction volume
- Low Returns



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Commodity Murabaha as a Product - Facts February 2009


Commodity Murabaha Volume (10 GCC Islamic Banks)

■ Murabaha (US\$ Billions)



Year	Murabaha (US\$ Billions)
2005	\$6.35
2006	\$14.36
2007	\$14.44
2008	\$9.95


Source: IIFM Analysis


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Why Standardize February 2009

- Most common and widely used product in number of jurisdictions (in absence of other viable liquidity management instruments)
- Frequent legal, Shari'ah, operational and other costs due o minor changes
- Lengthy negotiation time and constant Shari'ah involvement
- Variations in documentation processes and procedures leads to Shari'ah divergence
- Moving away from costly bilateral documentation to efficient standardization approach..... IIFM MATP

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IIFM Approach to Standardization February 2009

IIFM Master Agreement for Treasury Placement (MATP)

- IIFM's global working group; brings IFI's, regulators and other market participants on a common platform
- Working Group members more than 40 institutions from 9 jurisdictions
- IIFM Shari'ah Panel – 8 renowned scholars

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MATP – Challenges Overcome February 2009

IIFM Master Agreement for Treasury Placement (MATP)

WG = Working Group
S = Shari'a Meeting

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MATP – Approved Structures February 2009

Murabaha Deposit Placement – Structure I (Agency)

Deposit Taker acts as buying agent of the FI

Key:
 —> Commodity
 - - - -> Cash flow

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Structure I (Agency) - Salient Features

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- The Deposit Placing Entity will appoint the Deposit Taking Entity as its (disclosed or undisclosed) buying agent
- This purchase will be effected by spot payment by the Deposit Taker (acting on behalf of the Deposit Placer) and immediate delivery of the Commodity by the Supplier
- The Agent will only be obliged to purchase the Commodities from the Supplier once it has been put in clear funds by the Deposit Placing Entity for an amount equal to the purchase price
- Following conclusion of the Purchase, the Agent will hold legal title to the Commodity on behalf of the Deposit Placing Entity. The Agent will take possession of the Commodity (either actual or constructive) on behalf of the Deposit Placing Entity
- Once the Agent holds legal title to the Commodity on behalf of the Deposit Placer, the Deposit Taker (in its corporate/personal capacity and not in the capacity as Agent) may offer to purchase the Commodity from the Deposit Placing Entity and upon the Deposit Placing Entity accepting such offer, a sale shall be effected (the First Sale)



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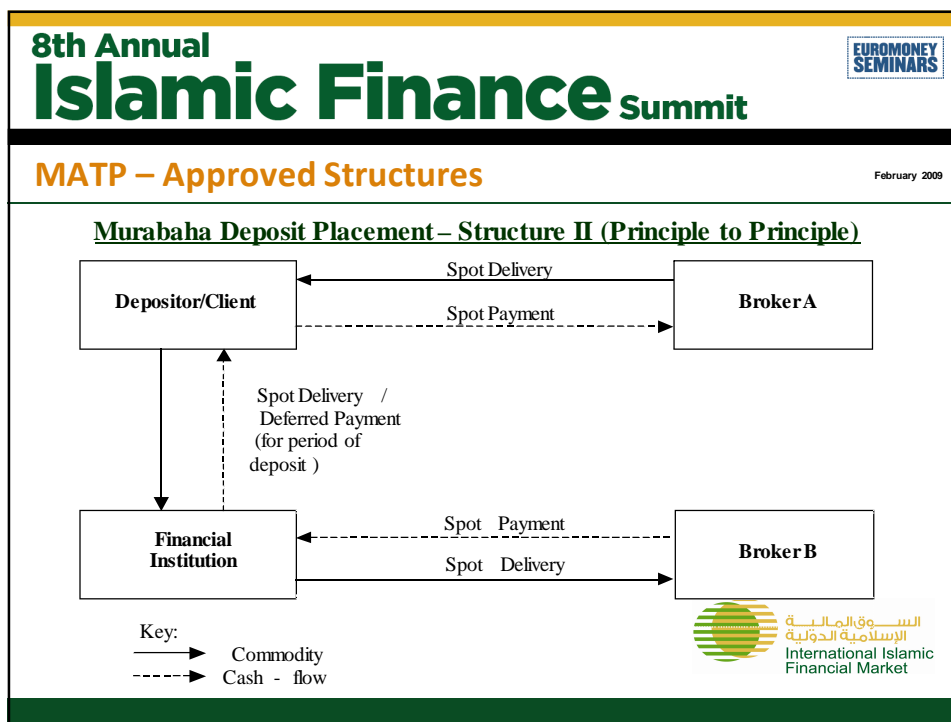


Structure I (Agency) - Salient Features


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- Once the First Sale is concluded and the Deposit Taker becomes the owner of the Commodity which is in its possession (either actual or constructive) it will be entitled to sell the Commodity to the Purchaser (a third party other than the Deposit Placing Entity or the Supplier) for immediate delivery and spot payment (the Second Sale). The purchase price for the Second Sale will be as agreed between the parties to that sale
- To mitigate commodity settlement risk, the Deposit Taking Entity (both in its capacities as principal and agent) and the Purchaser will be required to have a commodity account with the Supplier
- To mitigate cash settlement risk under each of the Purchase and the Second Sale, the purchase price payable by the Deposit Taking Entity (as Agent) to the Supplier under the Purchase may be 'settled' against the purchase price payable by the Purchaser to the Deposit Taking Entity under the Second Sale






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Structure II (Principle to Principle) - Salient Features

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- Once the Deposit Taking Entity holds legal title of the Commodities along with possession (either actual or constructive), the Deposit Taking Entity may offer to sell the same Commodities to the Purchaser (a third party other than the Deposit Placing Entity or the Supplier) for immediate delivery and spot payment and upon the Purchaser accepting such an offer, a sale shall be effected (the Second Sale)
- The purchase price under the Second Sale will be agreed between the parties. Legal title will pass from the Deposit Placing Entity to the Purchaser along with possession (either actual or constructive)
- Mitigation of commodity settlement risk – same as Structure I
- Mitigation of cash settlement risk – same as Structure I



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IIFM Master Agreement for Treasury Placement


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Documentation:

- Master Murabaha Agreement (MMA)
- Master Agency Agreement for Purchase of Commodities (MAA)

Important Clauses and Schedules:

- Prepayment (Rebate/Grant & Late payment amount)
- Governing Law
- Arbitration
- Language
- MMA 4 schedules including timetables and MAA 2 schedules




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MATP Adaptation Procedure February 2009

- **Use of MATP with Shari'ah Pronouncement**
 - Institution to obtain IIFM acceptance in order to use Shari'ah pronouncement (copyrights apply)

Recommended procedure to gain true benefit and moving towards convergence
- **Use of MATP as reference or guidance document**
 - MATP is used as a base document and as a starting point for negotiation only


Also leads to convergence

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Benefits of MATP February 2009

- Based on widely acceptable Shari'ah ruling and market practices
- Document of highest standard developed by international external legal counsel
- Reducing transaction arrangement cost (critical factor at present)
- Improving documentation standard and bringing smaller institutions on same level as large International banks
- Improving transparency
- Ideal for new jurisdiction entering Islamic finance
- Reduces burden on Shari'ah scholars – frees up time to concentrate on other more flexible and innovative liquidity management products thereby making Commodity murabaha
 - **Supplemental product in medium term (IIFM aim)**

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MATP Going Forward

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- Market response since launch
 - MATP accessed by over 150 institutions
- Initial beneficiaries of MATP
 - Kuwait Finance House Group
 - Albaraka Banking Group
 - Jordan Islamic Bank
 - ABC Islamic Bank
 - West LB
 - Barclays Capital
 - Calyon Corporate & Investment Bank
 - Islamic Bank of Asia
 - Gulf Finance House etc, etc
 - Ideal for all jurisdictions and their institutions



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Introduction to IIFM

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IIFM is a non-profit international development institution supported by the central banks and regulatory bodies of Bahrain, Dubai, Saudi Arabia, Sudan, Pakistan, Malaysia, Indonesia and Brunei as well as number of financial institutions

The objective of IIFM is to take part in the establishment, development and promotion of the Islamic Capital and Money Market (ICMM)

IIFM's primary focus lies in the advancement and unification of Islamic financial documents, structures, contracts, instruments, infrastructure and recommendations for the enhancement of ICMM



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Benefits to Industry February 2009

Financial Industry

Financial Institutions
Fund Managers
Legal Firms
Advisory Firms
Accountants

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Regulatory Bodies

Market Body with regulatory heritage
Wider Shari'ah Acceptance
Uniformity & Standardization
Knowledge Sharing
Infrastructure Development



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IIFM Current Projects February 2009

Initiative completed

- IIFM Master Agreement for Islamic Treasury Placement

Initiative in progress

- IIFM/ISDA "TaHawwut" (Hedging) Master Agreement



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Thank You!

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