ISSUES & CHALLENGES IN INDONESIA

SHARI’AH MONEY MARKET

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ISSUES

• HIGH DEPENDENCY ON CONVENTIONAL PARENT BANK.

  • COMPOSITION OF ISLAMIC BANKS IN INDONESIA (TOTAL ASSETS IDR 380 TRILLION ~ USD 28.2 BILLION)*:
    • 13 SHARIA COMMERCIAL BANKS (TOTAL ASSETS IDR 268 TRILLION CIRCA USD 19.7 BILLION)
    • 21 SHARIA BUSINESS UNIT (SBU). 14 OUT OF 21 BELONG TO DISTRICT DEVELOPMENT BANK. TOTAL ASSETS OF SBU IS IDR 112 TRILLION CIRCA USD 8.2 BILLION
  
  • THIS COMPOSITION IS ASSUMED TO DETERMINE THE BEHAVIOR OF SHARIA MONEY MARKET:
    • HIGH DEPENDENCY ON CONVENTIONAL PARENT BANK TO SUPPORT ITS SBU LIQUIDITY REQUIREMENT RATHER THAN SHARIA MONEY MARKET.
    • FDR OF SBU DURING 2014 – AUG 2017 RANGED FROM 96.60% TO 109% WHILE SCB’S FDRS ARE RANGED FROM 81.36% TO 88.03%

• TREASURY DEPARTMENT IN MOST SHARIA BANKS ACTS AS SUPPORT FUNCTION TO ENSURE THE LIQUIDITY MANAGEMENT RATHER THAN PROFIT CENTER, HENCE THE MOTIVATION TO GENERATE REVENUE FROM TREASURY ACTIVITIES IS NOT TOO PROMINENT

During 2010 until July 2017, the transactions executed in Sharia Money Market as follows:

  • PUAS only 1%-3% (in average of IDR 500 billion ~ USD 37 million).
  • SBIS & FASBIS (non tradable) circa 88%-99% (in average IDR 19 trillion ~ USD 1.4 billion).
  • RRS transaction around 5%-10% (in average IDR 1.8 trillion ~ USD 133.3 million).
ISSUES

• THE “SAME SIDE POSITION” EVENT MOST OF THE TIME HAPPENS.
  • SHARIA MONEY MARKET HAS BEEN EXPERIENCING EXCESS OF LIQUIDITY SINCE HAJJ FUNDS STARTED TO BE MANAGED BY SHARIA BANKS IN 2014 AND ALSO BECAUSE OF SLOWING DOWN OF FINANCING DUE TO UNFAVORABLE ECONOMIC CONDITIONS.
  • THE BARRIER BETWEEN CONVENTIONAL AND SHARIA MONEY MARKET STILL EXISTS DUE TO DIFFERENT CHARACTERISTICS OF MONEY MARKET INSTRUMENT.
    • REQUIRED MONEY MARKET INSTRUMENT WHICH HAS THE FOLLOWING FEATURES:
      • CAN GIVE CERTAIN RETURN FOR THE FUND OWNER
      • AT MATURITY CAN PAY THE PRINCIPAL AND THE PROFIT
      • CAN BE RECIPROCAL BETWEEN SHARIA AND CONVENTIONAL BANK

• THE COST OF “BORROWING” FOR SHARIA BANK IN THE MONEY MARKET IS USUALLY HIGHER THAN CONVENTIONAL TO MITIGATE THE UNCERTAINTY RISK.

• SUKUK OWNERS TEND TO KEEP THE SUKUK “HOLD TO MATURITY”, SCARCITY OF AVENUES TO INVEST THE EXCESS FUNDS.
  • AS OF SEPT 2017, THE O/S OF SBSN WAS IDR 368 TRILLION (17.6%) OF TOTAL IDR 2,089 TRILLION SBN

ISSUES

• NOT SUFFICIENT INTERBANK COUNTERPARTY LIMIT AVAILABLE
  • ALMOST ALL THE INTERBANK INSTRUMENTS ARE UNSECURED, THEREFORE THE ASSESSMENT OF CREDIT RISK OF THE COUNTERPART IS VERY IMPORTANT TO DECIDE ON WHETHER TO GRANT THE LIMIT OR NOT AND HOW MUCH THE LIMIT TO GRANT.
  • ONE OF THE MOST IMPORTANT PARAMETER IS THE SIZE AND THE QUALITY OF THE COUNTERPART’S EARNING ASSETS.
    • THIS CAN BE LESS IMPORTANT IF THE INTERBANK TRANSACTION SECURED BY A SECURITY WHICH IS RISK FREE OR MET THE INVESTMENT GRADE CRITERIA.

• UNMATERIALIZED CROSS BORDER TRANSACTION.
  • STANDARDIZED INTERBANK INSTRUMENT THAT CAN WIDELY ACCEPTED AND APPLIED CROSS BORDER
SHARI’AH MONEY MARKET PRODUCTS - INDONESIA

• SHARI’AH MONETARY OPERATION BY BANK INDONESIA

• OPEN MARKET OPERATION

• ABSORPTION OF LIQUIDITY
  • **SBIS** = SERTifikat Bank Indonesia Syariah, Tenor 9 & 12 Months, Underlying ‘AQD IS JU’ALAH
  • **REVERSE REPO SBSN** = Bank PURCHASES (AL BAI’) SBSN FROM CENTRAL BANK WITH A PROMISE (WA’AD) TO SELL IN THE FUTURE, TENOR 28 DAYS.
  • **SYARIAH TERM DEPOSIT FOREIGN CURRENCY** = PLACEMENT OF FC FUNDS TO BANK INDONESIA VIA AUCTION BIDDING, TENOR 1-12 MONTHS, ‘AQD JU’ALAH, ONLY FOR SHARIA BANKS, EARLY REDEMPTION IS ALLOWED UNDER CERTAIN REQUIREMENT

• INJECTION OF LIQUIDITY
  • **REPO SBSN** = BANK SELLS SBSN TO CENTRAL BANK WITH A PROMISE TO BUY BACK IN THE FUTURE FROM CENTRAL BANK.

• STANDING FACILITIES
  • DEPOSIT FACILITY
  • **FASBIS** = ‘AQD WADIAH, TENOR 1 – 14 DAYS, UNTRADEABLE

SHARI’AH MONEY MARKET PRODUCTS - INDONESIA

• STANDING FACILITIES CONT’D...

• STANDING FACILITIES

• FINANCING FACILITY
  • **REPO SBSN/SBIS** = ‘AQD AL BAI’ AND WA’AD WADIAH, TENOR OVERNIGHT, NON BIDDING
SHARI’AH MONEY MARKET PRODUCTS - INDONESIA

SHARI’AH MONEY MARKET

1. INTERBANK MUDHARABA INVESTMENT CERTIFICATE – SE BI NO.17/27/DKMP
   - GENERIC NAME IS SIMA, ‘AQD MUDHARABA, IDR AND FC, O/N TO 12 MONTHS
   - THE CALCULATION OF PROFIT BASED ON CASH BASIS
   - NOT BACKED BY ASSET (UNSECURED)
   - PARTICIPANTS: SHARIA BANK CAN BE AS MUDARIB AS WELL AS SHAIBUL MAAL, CONVENTIONAL ONLY LIMITED TO SHAHIBUL MAAL
   - UNTRADEABLE
   - THE RETURN CAN BE FIXED AS WELL AS VARIABLE
     - FOR FIXED SIMA, AT MATURITY PAY PRINCIPAL + PROFIT
     - FOR VARIABLE SIMA, AT MATURITY PAY PRINCIPAL, PROFIT WILL BE PAID 1ST WORKING DAY NEXT MONTHS
   - CHALLENGES
     - VARIABLE SIMA
       - THE UNCERTAINTY HIGH DUE TO THE FLUCTUATIONS OF CASH BASIS INCOME FROM THE MUDHARIB  COST OF “BORROWING” IS HIGHER
       - THE PROFIT CAN NOT PREDETERMINE IN THE BEGINNING, AT MATURITY ONLY PAY PRINCIPAL  NOT SUITABLE WITH CONVENTIONAL MARKET PRACTICE
       - SO FAR THE TRANSACTIONS UNDER VARIABLE SIMA ARE EXECUTED AMONG SHARIA BANKS DESPITE OF BY REGULATION CONVENTIONAL BANK CAN INVOLVE AS SHAHIBUL MAAL
   - FIXED SIMA
     - BASED ON POOL OF ASSETS UNDER FIXED RETURN ‘AQD SUCH AS MURABAHA, IJARAH, SALAM. THE ASSETS ONLY TO “PREDETERMINE” THE PROFIT UPFRONT, NOT ASSETS BACKED.
     - THE PROCEEDS AT MATURITY CONSISTS OF PRINCIPAL AND PROFIT. (THERE MIGHT BE ISSUE IN SHARIA COMPLIANCE).
     - SINCE THE CRITERIA OF FIXED SIMA MATCHED WITH CONVENTIONAL BANK, THE BARRIER BETWEEN SHARIA AND CONVENTIONAL MONEY MARKET CAN BE OVERCOMED.
     - BOTH VARIABLE AND FIXED SIMA CAN ONLY BE APPLIED IN DOMESTIC MARKET
2. **INTERBANK SHARIA COMMODITY TRADING CERTIFICATE – SE BI 17/28/DKMP**

- ** GENERIC NAME IS SIKA, ‘AQD MURABAHA, IDR ONLY, O/N TO 12 MONTHS**

  **Assumptions**
  - Master agreement contains Wa'ad (promise to buy) between CIMB Niaga Syariah and BRI Syariah is in place.
  - BRI Syariah short IDR 25 bio
  - CIMB Niaga Syariah long IDR 25 bio
  - One month IDR interbank money market rate is 4.19%
  - Cost of transaction is IDR 40 per IDR 1 mio volume transaction
  - Both agree to use SIKA to facilitate the Money Market transactions

  **Terms used in SIKA**
  - Bank which has excess liquidity and purchases commodity in Bursa is called Commercial Participant.
  - Bank which suffers short liquidity and purchase commodity from Commercial Participant on deferred payment is called Commodity Consumer.

**Diagram:**
- **Commercial Participant**
  - Dealer will calculate effective CoM 4.20%, and propose new term
  - Terms: IDR 25 bio
  - One month tenor
  - One month rate 4.15%
  - Dealer will calculate effective CoM 4.20%, and propose new term

**SHAARIAH MONEY MARKET PRODUCTS - INDONESIA**

3. **SHARIA REPO (MINI MRA) – SE BI NO.17/10/DKMP**

- **‘AQD AL BAI’ MA’AL AL WA’D BI AL SYIRA’, IDR AND FC, O/N TO 12 MONTHS**

- **PARTICIPANTS: SHARIA AND CONVENTIONAL BOTH AS SELLER AND BUYER, AS LONG AS OWNS SUKUK/ISLAMIC SECURITY; NEED TO SIGN MINI MRA**

- **ASSET BACKED SINCE THE SALE OF SECURITY IS REAL SALE (BAI’ AL HAQIQI) AND THE SELLER AS WELL AS THE BUYER PROMISE (WA’AD) TO SELL BACK THE SUKUK AT AGREED TIME.**

- **MECHANICS:**
  - **1ST LEG**
    - THE SELLER OF SUKUK (SHORT FUND) SELLS THE AGREED SUKUK (SERIAL; AMOUNT; PRICE; 1ST LEG SETTLEMENT DATE) TO THE BUYER.
    - THE SETTLEMENT DATE MAX 2 DAYS SINCE TRANSACTION DATE
    - PREPARATION FOR 2ND LEG: BOTH SELLER & BUYER OF SUKUK PROMISE (MUWA’ADAH) TO SELL BACK THE SUKUK TO THE ORIGINAL SELLER AT AGREED DATE IN THE FUTURE (AGREE ON THE PRICE AND THE DATE IN THE 2ND LEG)

  - **2ND LEG**
    - THE SELLING BACK SUKUK TAKES PLACE AT THE AGREED DATE AND TERMS IN 1ST LEG

- **CHALLENGES:**
  - THERE IS NOT ENOUGH SUKUK AVAILABLE IN THE MARKET TO FACILITATE THE SHARIA REPO.
  - THE BEHAVIOR OF THE INDUSTRY IS TEND TO KEEP THE SUKUK UNTIL MATURITY.
  - BANK NEEDS TO IMPROVE THE INFRASTRUCTURE TO MEASURE THE MARKET RISK OF THE SUKUK.
  - THERE MIGHT BE HARD TIMES TO DECIDE ON THE TERMS BETWEEN COUNTERPART.
SHARI’AH MONEY MARKET PRODUCTS - INDONESIA

• SHARI’AH MONEY MARKET

4. **NCD (NEGOTIABLE CERTIFICATE OF DEPOSIT) SYARIAH – FATWA DSN MUI NO.97/DSN-MUI/XII/2015**

   • CURRENTLY THIS INSTRUMENT IS BEING DISCUSSED BY BANK INDONESIA & OJK WITH REGARDS TO THE REGULATION

   • BASED ON FATWA:

     • PARTICIPANTS
       • ONLY CAN BE ISSUED BY SHARIA BANK AS MUDHARIB
       • BUYER CAN BE INDIVIDUAL, SHARIA FINANCIAL INSTITUTION AS WELL AS CONVENTIONAL AND OTHER INSTITUTION

     • THE RETURN CAN BE FIXED AS WELL AS VARIABLE

     • CANNOT BE SOLD AT DISCOUNT

     • CAN BE SOLD BEFORE MATURITY USING AL BAI’

     • CAN BE USED AS INSTRUMENT IN REPO SYARIAH TRANSACTION IN SECONDARY MARKET

     • BANK NEEDS TO IMPROVE THE INFRASTRUCTURE TO MEASURE THE MARKET RISK OF THE SUKUK

     • THERE MIGHT BE HARD TIMES TO DECIDE ON THE TERMS BETWEEN COUNTERPART

END OF PRESENTATION