

Frequently Asked Questions (FAQ) Regarding Six-Month Holding Period of SBI

Capital inflows in developing economies or emerging markets (EMs) are set to mount further even higher compared to 2010. In Indonesia, capital inflows are similarly predicted to climb. Although a shift is under way with longer-term capital for foreign direct investment (FDI) expected to take a more dominant role, inflows of short-term portfolio capital will also reflect this trend.

The massive influx of capital is influenced by both domestic and external factors. Regarding domestic factors, the high rate of capital inflows is encouraged by the buoyant outlook for the economy, stable monetary and financial system, fiscal sustainability, solid external side performance and continued attractive yields. From the external side, surging capital inflows come up as the effect of the policy stance pursued by advanced nations through low interest rates and liquidity expansion. Massive expansion in liquidity which is unabsorbed by the real sector has added to the already flush pool of global excess liquidity. Meanwhile, advanced economies are currently still intricately by fiscal sustainability and debt issue.

Considering significant portion of these capital inflows are short-term and vulnerable to sudden reversal, therefore appropriate management is necessary to prevent disruption to monetary stability. To this end, the holding period is being extended from 1 month to 6 months.

1. Question : What is the purpose of this rule?

Answer : The purpose of extending the Bank Indonesia Certificate (SBI) 1MHP to a 6MHP is to minimise adverse impact from short-term capital inflows on monetary and financial system stability. This policy is also expected to promote other transactions on the money market and improve effectiveness in monetary management.

2. Question : What is the Bank Indonesia Certificate Six-Month Holding Period (SBI 6MHP)?

Answer : The SBI 6MHP requires holders to retain their SBIs for a minimum of 6 months after the purchase settlement date before transacting these SBIs with other parties.

Points to note:

- a. SBIs may be used in transactions after holding for a minimum of 6 months or 182 calendar days.

During the SBI 6MHP, holders are not permitted to carry out a transaction of the SBIs with any other parties except in the case of SBI transactions conducted by participants in monetary operations with Bank Indonesia.

- b. Sell and buy back repo transactions of SBIs must be executed with a minimum term of 6 months or 182 calendar days.
- c. Sub-registries must maintain the registration of customer-held SBIs in compliance with the provisions described in letters a and b.

3. Question : When will the SBI 6MHP rule become effective?

Answer : The SBI 6MHP rule will become effective on Friday, 13 May 2011.

4. Question : Who is required to comply with the SBI 6MHP and which instruments do it applies to?

Answer : All holders of SBIs, including residents and non-residents, are required to comply with the SBI 6MHP rule.

The SBI 6MHP applies to all outstanding SBIs, whether issued before and after the introduction of the SBI 6MHP.

5. Question : What happens if a bank has a sudden need for short-term liquidity during the 6MHP, but is holding only SBIs?

Answer : The bank will still be permitted to engage in repo transactions with Bank Indonesia to meet short-term liquidity needs.

6. Question : What transactions are affected by the SBI 6MHP rule?

Answer : The SBI 6MHP applies to transactions including but not limited to outright, repo (sell and buy back *and* collateralised borrowing), pledges and endowment, with the exception of repos to BI to cover liquidity needs. Sell and buy back repo transactions must comply with the minimum tenor of 6 months or 182 calendar days.

7. Question : When can SBIs are able to be used again in transactions after a repo transaction second leg falls due?

Answer : In the case of repo transactions for collateralised borrowing (with ownership unchanged) and pledges, the SBIs may be used again in transactions after completing a 6MHP dating from ownership transfer.

In the case of sell and buy back repos; these SBIs may be transacted again after holding for a minimum of 6 months (182 calendar days) after the due date of the second leg.

8. Question : How will the SBI 6MHP apply to SBIs currently held by banks and non-bank parties?

Answer : The holding period for SBIs held before the 6MHP is launched on 13 May 2011 will be calculated on the basis of the minimum six-month holding period. For example, if an SBI has been held for 4 months prior to 13 May 2011, that SBI will need to be held a further 2 months to comply with the 6MHP before it can be used in a transaction.

9. Question : **What happens with transactions involving a second leg (including repos/pledges/SBL) with less than 6 month tenor, when the transactions were settled before the 6MHP and the second leg falls due after the 6MHP becomes effective?**

Answer : Transactions contracted before the introduction of the 6MHP with a second leg falling due after the 6MHP comes into force may continue to operate as agreed by the parties involved. Nevertheless, these transactions must still consider the 1MHP rule.

10. Question : **Regarding the SBI 6MHP rule, does a bank have to reclassify the accounting entry for an SBI instrument previously classified in the trading category?**

(In the elucidation to article 12 letter b of Bank Indonesia Regulation No. 9/13/PBI/2007 concerning the Minimum Capital Adequacy Requirement for Commercial Banks Taking Account of Market Risk, the criteria for financial instruments that may be designated Trading Book take account of matters including: 1) terms and conditions to be met, including holding period guided by generally accepted practice (maximum 90 days); 2) possibility of legal restrictions on trading; and 3) applicable financial accounting standards)

Answer : The use of the maximum 90 day period in the Bank Indonesia Regulation mentioned above is intended, among others, as a reference for banks in developing Trading Book policy and guidelines specifically concerning the criteria for financial instruments that may be designated Trading Book. The background to this is the application of PSAK 55 (2006 Revision) concerning Financial Instruments: Recognition and Assessment for Classification, as follows:

- a. Paragraph 8 stipulates that financial instruments shall be classified in the trading book, among others, if obtained or held primarily for sale or purchase in the near future. In banking practice, "near future" is normally interpreted as a maximum term of 90 days.
- b. Paragraph 51 stipulates that entities are not permitted to reclassify financial instruments from or to a category of financial instruments "assessed at fair market value in the profit and loss statement" for as long as these financial instruments are held or issued. Therefore, before classifying a financial instrument in the category of "Assessed

at Fair Market Value in the Profit and Loss Statement," the bank should consider and analyse its ability to sell the financial instruments in the near future (in these cases, customarily within 90 days), in addition to its intention for holding the financial instruments. If the financial instruments cannot be sold, the bank is not permitted to reclassify them to another category.

- ➔ The introduction of the SBI 6MHP rule should not influence the recording of financial instruments currently recorded in the trading category. Therefore, if SBIs are classified in the trading book by reason of the bank's intentions at the time of purchase, the bank may not reclassify these SBIs.
- ➔ Additionally, if the bank buys SBI financial instruments subject to the SBI 6MHP, it should record the instruments under the "Available for Sale/AFS" category if the intention is not to hold the instruments to maturity.

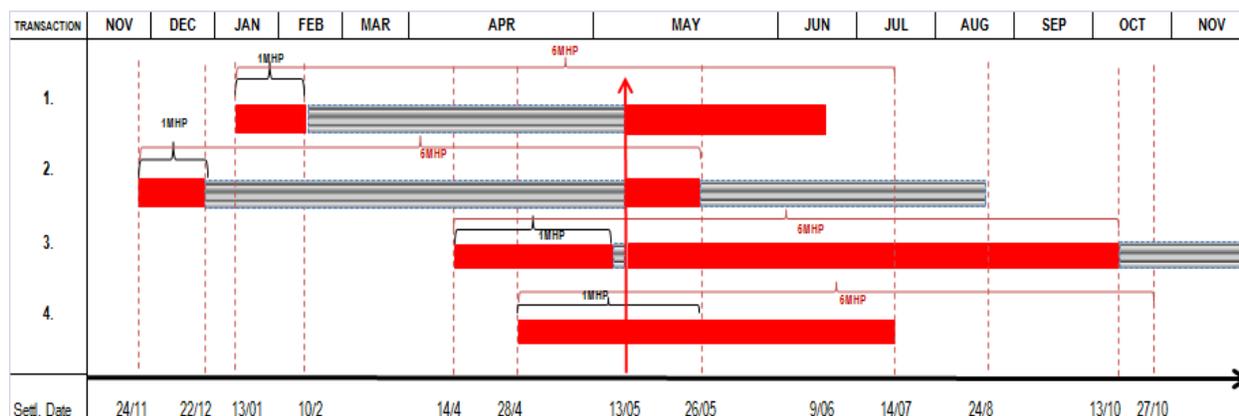
11. Question : Will transfers of SBIs between sub-registries without ownership transfer be restricted by the SBI 6MHP?

Answer : No. The MHP for SBIs transferred between sub-registries without change of ownership is *calculated* from the recording of the SBI in the original sub-registry.

12. Question : What sanctions will be imposed for infringements of the 6MHP rule?

Answer : Any violation of the SBI 6MHP will be liable to administrative sanctions and financial penalties. The procedure for imposition of sanctions will be stipulated in a Circular Letter issued at a future date.

**Diagram: Application of the Six Month Holding Period
For Outright Transactions**



Notes:

- The dates on the diagram and the explanatory notes are settlement dates.
- It is assumed that SBI holders are not selling their SBIs. The diagram illustrates when SBI holders are required to hold the SBIs and when SBI holders may use their SBIs in transactions.
- The red bars depict when the SBI holders are subject to the SBI minimum holding period, or are not permitted to sell SBIs that they hold to any other party except Bank Indonesia.
- The multi-shaded bars depict the times at which the SBI holders are no longer subject to the SBI minimum holding period, or may engage in transactions using the SBIs held.

1. Explanation of Transaction 1.

The SBI holder purchased SBIs with 147 days remaining maturity on 13 January 2011. Under the 1MHP rule, the SBI holder is required to hold the SBIs a minimum of 28 days, or until 10 February 2011.

If the SBI holder conducts no transactions from 10 February 2011 until 12 May 2011, the introduction of the SBI 6MHP on 13 May 2011 means that the SBI holder must hold until 14 July 2011. While the SBIs are assumed to mature on 9 June 2011, the holder will not be able to resume transacting these SBIs at this date.

2. Explanation of Transaction 2.

The SBI holder purchased SBIs with a 273 day tenor (9 months) on 24 November 2010. Under the 1MHP rule, the SBI holder was required to hold the SBIs a minimum of 28 days, or until 22 December 2010.

If the SBI holder does not engage in any transactions from 22 December 2010 until 12 May 2011, the introduction of the SBI 6MHP on 13 May 2011 means that transactions with the SBIs may resume after the 6MHP requirement is met, in other words from 25 May 2011.

3. Explanation of Transaction 3.

A Bank purchased SBIs with a 273 day tenor (9 months) on the primary market on 14 April 2011. Under the 1MHP rule, the SBI holder was required to hold the SBIs a minimum of 28 days, or until 12/05/2011.

If the SBI holder does not conduct a transaction on 12 May 2011, then following the introduction of the SBI 6MHP on 13 May 2011, the holder may resume transactions with the SBIs only after the 6MHP requirement is met, or from 13 October 2011.

4. Explanation of Transaction 4.

The bank purchased SBIs on 28 April 2011. Under the 1MHP rule, the SBI holder was required to hold the SBIs a minimum of 28 days, or until 26/05/2011.

The introduction of the SBI 6MHP requirement on 13 May 2011 means that the SBI holder is required to hold until 27 October 2011. While the SBIs are assumed to mature on 14/07/2011, the holder will not be able to resume transacting these SBIs at this date.

Diagram: Application of the Six Month Holding Period for Repo Transactions



5. Explanation of Transaction 5.

The bank sells SBIs on 28 April 2011 in a 31-day repo transaction maturing on 29 May 2011. The SBI repo transaction will continue to operate under the original terms agreed by the parties until the second leg is due, even after the introduction of the SBI 6MHP.

SBI repo transactions conducted on or after 13 May 2011 will be subject to the SBI 6MHP.

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