## New Way to grow your money

Retail investors may soon have a new vehicle with which to grow their money. Negotiable instruments of deposit are expected to provide higher returns than fixed deposits, making them an attractive investment tool in uncertain times.

rates than fixed

deposits, would be

## BY KUEK SER KWANG ZHE

by the end of this year is good news for in- term bank deposits, property and equity." vestors looking for another vehicle to steadily grow their money over the medium to long term with lower risk.

Mainly used by financial institutions, NIDs work be a positive for the country's economy. like fixed deposits in that they are issued by banks to "The initiative is very good for the country as it for a longer period.

"It is a very good idea by Bank Negara Malaysia as damentals," says Lee. Markets Committee.

Lee says NIDs could become an attractive investment tool in the current low-yield, low-return environment. WILL NIDs TAKE OFF? Depending on the final pricing structure, a five-year At press time, the minimum investment amount for to invest in,

est rate of 4.5% provides investors a total return of Bank Negara's Explanatory Notes of Negotiable Instru-25% over five years. Not many asset classes today can ments of Deposit and Islamic Negotiable Instruments. give you such stable and predictable returns. And the are solvent]," he says.

bly give you 50% returns in five years. But they could to withdraw their money before the maturity date. also give you -20% or -30% returns. This is the same "The fact that banks have to return investors' monfor property and commodities."

for their long-term goals, such as their retirement tor at CIMB Group Holdings Bhd and CIMB Bank Bhd. or children's education. Those who have stronger As NID investors will not be allowed to withdraw holding power could opt for NIDs while those with a their money before the maturity date, banks will shorter time horizon can keep their money in fixed have greater certainty and flexibility in utilising the deposits, he adds.

Malaysia Sdn Bhd, says NIDs will be attractive to those will certainly be the key," says Lee. looking for a safe place to park their money. "NIDs, The structure of NIDs will be similar to that of

try has a high saving rate. "This will be an important declines, they will make some gains on their prinasset class for a country like Malaysia, which has a cipal if they choose to sell the NID before maturity,"

5% of its gross domestic product. Though our rate is lower than those of China and Singapore, which are he likely introduction of negotiable instru- 50% and 40% respectively, it is still quite high. Hence, ments of deposit (NIDs) to the retail market the need for more investible products beyond short-

By giving retail investors access to NIDs, banks will have an additional source of capital, allowing them to provide more loans to companies. This will

certify that a sum of money has been deposited with will provide banks with more capital to lend. This them for a specific period of time at a particular inter- will take away foreign currency funding, which is est rate. The difference is that the financial instrument toxic to sovereign and corporate bonds, especially if allows banks to offer investors a higher interest rate there is an economic crisis. The investment committhan fixed deposits in return for parking their money tees sitting in different time zones can end your life line regardless of your country's or company's fun- higher interest

it will allow banks to offer investors a medium-term, NIDs are also attractive to banks as they will be fixed-rate investment product that comes with a higher able to hedge their risks with interest rate swaps, he interest rate than fixed deposits," says Datuk Lee Kok adds. "Banks can hedge interest rate risks by swap-Kwan, president of the Financial Markets Association ping the fixed interest rate of NIDs with the floating of Malaysia and a member of Bank Negara's Financial rate of products such as mortgages, credit cards and corporate and commercial loans," he says.

NID could fetch an interest rate of 4% to 4.5%, com- these NIDs had yet to be decided, says Lee. Existing NIDs, especially in pared with the average fixed deposit rate of 3% to 4%. however, are required to have a nominal value of more "Let's assume that a five-year NID with an inter- than RM60,000 per account or customer, according to

It should be noted that unlike fixed deposits, which > Meor Amri principal is guaranteed by the banks [so long as they allow account holders to withdraw the principal in full (plus 50% accrued interest in certain circumstances) "Other asset classes, such as equities, could possi- at any time, the NIDs will not allow retail investors

ey in fixed deposits and that it could be withdrawn Lee says the predictable nature of NIDs makes anytime make it hard for the banks to offer a higher the instrument attractive from a financial planning interest rate [than what is currently offered]," says perspective, especially for investors who are saving Lee, who is a non-independent, non-executive direc-

money deposited with them. Hence, they will be able Meor Amri Meor Ayob, CEO of Bond Pricing Agency to offer investors a higher interest rate. "The pricing

assuming they offer higher interest rates than fixed bonds in that investors will be able to sell them on deposits, would be welcomed by retail investors, who the open market. "They will be able to trade them like are constantly seeking safe alternative instruments bonds. Also, if the key interest rate goes up, they will to invest in, especially in the current low interest rate lose some of their principal if they sell it back to the issuer (unlike a fixed deposit, which returns 100% of Lee says there will be demand for NIDs as the countheir principal). Conversely, if the key interest rate saving rate of 30%. In the US, the saving rate is only he says, adding that the pricing mechanism will be

structured to discourage investors from arbitraging when the key interest rate fluctuates.

"Let's say you buy a five-year NID that yields 4.5% for RM100 and need to sell it three months later. If the interest rate is still 4.5%, you will get back your RM100 plus accrued interest of RM1.10, netting you RM101.10.

"But if the interest rate has gone up to 5.5%, you will only be able to sell the NID for RM95.90 plus the accrued interest of RM1.10, netting you RM97. You will lose RM3 on your principal of RM100."

Lee points out that if the RM97 is invested in a new five-year NID that yields 5.5%, the total return upon maturity will be almost the same as what he would have received if he had not sold his first NID.

"However, if the interest rate has declined to 3.5%, you will be able to sell the NID for RM104.30 plus the accrued interest of RM1.10, netting you RM105.40,"



## Spurring the retail bond market, but not ETBS

The introduction of negotiable instruments of deposit (NIDs) for retail investors could help boost the retail bond market in the future as NIDs share similar traits with retail

"This is a good introduction to the retail bond market because investors take on interest rate risks and bank credit risk," says Datuk Lee Kok Kwan, president of the Financial Markets Association of Malaysia and a member of Bank Negara Malaysia's Financial Markets Committee.

Kevin Chan, head of fixed income investment at Apex Investment Services Bhd, says the two products have similar features and the launch of NIDs could warm investors to the idea of trading retail bonds in the future. However, he adds that NIDs are not expected to spur the trading volume of the existing retail sukuk on the Exchange Traded Bonds & Sukuk (ETBS) platform for a number of reasons.

For one, the bid and offer spread is too wide on the ETBS compared with the spread offered by the over-the-counter platform. "The spread on the ETBS is about 15 to 20 basis points (bps) compared with the not more than 5bps if you buy it over-the-counter. This is a lot for bond investors as the yields are generally lower than equities as it is. They would rather buy into a bond unit trust fund, where the pricing and liquidity issues are managed by an investment management company," says Chan.

On top of that, the brokerage fee to trade on the ETBS platform is the same as for trading equities, which makes the cost of trading retail bonds on the exchange even higher, he

Chan says the wide bid and offer spread on the ETBS is caused by a lack of liquidity for the instrument, which in turn is due to several things such as a lack of variety of exchangetraded bonds on the exchange. "Corporates may be reluctant to issue bonds on the ETBS as the cost of the issuance process is higher and it is less efficient than raising funds through investment bankers."

There are only three retail sukuk listed on the ETBS, all of which are issued by DanaInfra Nasional Bhd. The yields offered by the retail sukuk of about 4% (excluding the cost of bid and ask spread and brokerage fee) are also not attractive to retail investors as the returns are just slightly higher than fixed deposits, and sometimes lower, says Chan.

Edward Iskandar Toh, chief investment officer for fixed income at Areca Capital Sdn Bhd, believes the ETBS will not take off as long as there is not enough liquidity and products listed on it. "The low-yield, low-rate environment globally also makes it hard for corporates to offer retail investors a higher bond yield, which is the main attraction for them to subscribe."

Currently, most retail investors access bonds either through the ETBS or bond unit trust funds that cost at least RM1,000 as the minimum investment amount to buy into a single bond could be as high as a first to launch global sukuk more few hundred thousand to a few million than 10 years ago. The issuers of ringgit. High-net-worth investors access these corporate and sovereign bonds through private banks.

In fact, bonds have been gaining

traction among high-net-worth retail investors in recent years, says Toh. "The more sophisticated bonds, such as asset-backed securities, have been gaining traction in recent years under the low-yield and volatile markets globally. These bonds are usually more complicated [in structure] and the minimum investment requirement is also beyond the affordability of retail investors."

An industry practitioner points out that one of the main reasons retail bonds and sukuk have not been introduced to retail investors is due to the lack of a prospectus. A simple task like this is an additional cost to companies and banks. More importantly, it impedes the issuance of bonds and the fundraising process.

"It will probably delay the whole process for a few months," he says, adding that the regulators and banks should look into promoting over-thecounter retail bonds such as those commonly offered at banks in other

He says retail investors who buy the shares of local companies should be able to evaluate the risks and returns of these companies and have the option of buying bonds instead of equities. Unlike exchange-traded platforms, banks could offer retail investors better pricing than the exchange.

"Malaysia is the world's leading Islamic financial centre and was the sukuk, which are local companies, also have a very good track record. Retail investors should have access to bonds and sukuk," he adds.

Meor Amri says the transaction cost of buying and selling NIDs is an important factor in determining the success of the instrument. The terms and conditions of the product, particularly the risks involved, must be conveyed clearly to the general public.

Lee says investors will take on interest rate risks and credit risk when they put their money in NIDs, just like they do when they keep their money in fixed deposits. He adds that while the credit risk is minimal as most local banks have good credit ratings and strong fundamentals, it is important for investors to know that the money kept in NIDs will not be insured by the Malaysia Deposit Insurance Corporation (PIDM), which was established by the government in 2005 to protect depositors in the event of bank failure. Under the PIDM's Deposit Insurance System, all the depositors of its member banks are automatically provided deposit protection of up to RM250,000.

"There is no deposit insurance for NIDs, so it is important for investors to look at the strength of the issuing bank such as its credit rating, capital ratios, profitability levels and asset quality," he says.

Kevin Chan, head of fixed income investment at Apex Investment Services Bhd, says the success of NIDs will also depend on how much effort banks are willing to put in to promote the instrument. "Private bankers have indicated that from a [high-net-worth] investor's perspective and appetite, NIDs may not be their preferred choice as there are other structured products, such as equity, credit or currency-linked investments, which can provide them with higher

"From a commercial perspective, it will make more sense for them to sell other investment products such as unit trust funds, bonds and currencies, as the revenue generated from these products will justify the time spent promoting them to their clients."

Lee hopes that NIDs will be made scriptless in the future when they are introduced to the retail market. NIDs for financial institutions are a script-based product that requires many forms to be filled in before a transaction is performed. He says it will be helpful if the NIDs are made scriptless as it would allow retail investors to trade online. "Hopefully, it can be made scriptless so retail investors could open an account with the bank and trade the instrument online."



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