



BANGKO SENTRAL NG PILIPINAS

OFFICE OF THE GOVERNOR

CIRCULAR NO. 1116
Series of 2021

Subject: Guidelines on the Management of Liquidity Risk by Islamic Banks and Islamic Banking Units

The Monetary Board, in its Resolution No. 584 dated 12 May 2021, approved the following guidelines on the management of liquidity risk by Islamic banks (IBs) and Islamic banking units (IBUs).

Section 1. Sec. 145 of the Manual of Regulations for Banks (MORB) on Liquidity Risk Management is hereby amended to read, as follows:

Policy Statement. The Bangko Sentral is cognizant that the viability of financial institutions, particularly banks, is heavily influenced by their ability to manage liquidity, including intraday liquidity positions. X X X

X X X

Relative to the single regulatory approach of the Bangko Sentral where Islamic banks (IBs) can operate alongside conventional banks under the same regulatory requirements, this Section together with its appendices shall be applicable to IBs and Islamic banking units (IBUs), as appropriate. Further, additional guidelines under Appendices 71, 72 and 130 of the MORB are provided to cover the specificities of Islamic banking operations.

Liquidity Coverage Ratio (LCR)

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Section 2. Appendix 71 of the MORB on the Guidelines for Liquidity Risk Management is hereby amended to read, as follows:

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GUIDELINES ON LIQUIDITY RISK MANAGEMENT

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XI. Guidelines for Islamic Banks (IBs) and Islamic Banking Units (IBUs)

The provisions of this Appendix apply, as appropriate, to IBs and IBUs. The IBs/IBUs are expected to have written policies on liquidity risk management. For the IBUs, their assets and liabilities are segregated from those of the conventional bank proper, thus IBUs are expected to establish their separate liquidity management arrangements. In applying the provisions of this Appendix, the IBs/IBUs shall consider the following:

1. In assessing instruments to be used to meet liquidity requirements, IBs/IBUs should consider the specific liquidity characteristics of the Shari'ah-compliant instruments that are available in the market. Accordingly, IBs/IBUs are expected to be familiar with the peculiarities of these liquidity instruments against their conventional counterparts and utilize such information in assessing instruments to be used to meet liquidity requirements. For example, sukuk or Islamic bonds held as liquid assets may be less liquid than conventional bonds held for the same purpose. Similarly, where the management of liquidity risk involves the possibility of raising funds in the money market, the behaviour of the Islamic money market may not be identical to that of the conventional market.
2. In developing a funding strategy and a contingency funding plan, IBs/IBUs should consult their Shari'ah Advisory Council (SAC)¹. Any instrument to be used in liquidity management should be acceptable to the SAC and is appropriate to the context in which it is to be used.
3. IBs/IBUs should also assess the liquidity risk arising from the various modes of Shariah-compliant financing that they employ, including any risk transformation that may take place at different stages thereof. For example, if a customer has an option to cancel a transaction, the exercise of that option may cause the IB/IBU to hold an asset that it may need to dispose even under stressed market conditions.
4. IBs/IBUs should consider Shari'ah limitations, if any, on the ways in which liquidity can be transferred between entities in a banking group, or between the IBUs and the bank proper, including the instruments that can be used for this purpose.

¹ Or Shari'ah adviser or consultant as the case may be, per Circular No. 1070 dated 27 December 2019.

Section 3. Appendix 72 of the MORB on the Basel III Framework on Liquidity Standards-Liquidity Coverage Ratio is hereby amended to read, as follows:

Appendix 72

BASEL III FRAMEWORK ON LIQUIDITY STANDARDS-LIQUIDITY COVERAGE RATIO

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Part III. Applicability to Islamic Banks (IBs) and Islamic Banking Units (IBUs)

The provisions of this Appendix apply to IBs/IBUs, subject to the provisions of Section XI of Appendix 71, which requires, among others, that the instruments to be used in liquidity management must be acceptable to the Shari'ah Advisory Council. Further, IBs/IBUs shall consider the following guidelines:

1. A conventional bank should consider the provisions set forth below when consolidating IBU's activities in its LCR report. Furthermore, an IBU shall submit a separate LCR report if its aggregate liabilities represent at least five percent (5%) of the bank's total liabilities as of measurement date.
2. For purposes of computing the consolidated LCR as mentioned in Item "7", the qualifying HQLA that are held by the IBU shall be counted towards the stock of HQLA in an amount up to the total net cash outflows of said IBU that are included in the consolidated LCR of the conventional bank proper.
3. As part of or as a supplement to its internal liquidity management guidelines, the IB/IBU should have in place internal guidelines in compliance with the expectation of the Banko Sentral on the mapping of accounts for purposes of LCR computation and reporting.
4. References in this Appendix to:
 - a. "Debt instruments" should be taken to include sukuk or Islamic bonds. Sukuk, subject to meeting the requirements for eligibility, rank as "eligible securities" for HQLA.
 - b. Retail deposits and wholesale deposits should be taken to include retail investment accounts and wholesale investment accounts, respectively, of IBs and IBUs.



5. Sukuk issued by the International Islamic Liquidity Management Corporation² and other similar organizations as may be determined by the Bangko Sentral, should be treated as though they were issued by multilateral development banks.
6. Assets held against on-balance sheet investment accounts as defined in Appendix 139³ of the MORB may be included within the stock of HQLA subject to meeting the requirements for inclusion and to any overall limits applicable to HQLA of particular classes.
7. On-balance sheet investment accounts as defined in Appendix 139 of the MORB shall be included in the calculation of total expected cash outflows.
 - a. All retail investment accounts shall be assigned with specific run-off rates depending on the outstanding balance per account:

Outstanding Balance Per Account*	Run-off Rate**
Up to ₱4,000,000	10%
Over ₱4,000,000	15%

* Amount (not covered by deposit insurance)

**Run-off rate is patterned after conventional banks.

- b. All investments accounts from wholesale clients shall be subject to the run-off rates applicable to non-operational deposits which are not insured by the Philippine Deposit Insurance Company (PDIC), as specified in paragraphs 32 and 33 of Item II (LCR Calculation), Part I (LCR Framework).
8. For purposes of paragraph 74 of Item II (LCR Calculation), Part I on LCR Framework, all cash placements made by the IB/IBU with another financial institution shall be treated in the same way as deposits.
9. Investment accounts booked by IBs/IBUs shall be reported in Annex C of Appendix 72 under the appropriate/equivalent category of deposits of conventional banks.

Section 4. Appendix 130 of the MORB on the Guidelines on the Bangko Sentral Implementation of the Net Stable Funding Ratio (NSFR) is hereby amended to read, as follows:

² The International Islamic Liquidity Management Corporation or IILM is an international organization established by central banks, monetary authorities and multilateral organizations to create and issue Shari'ah compliant financial instruments to facilitate effective cross-border islamic liquidity management.

³ Prudential Regulations for Islamic Banks and Islamic Banking Units.

GUIDELINES ON THE BANGKO SENTRAL IMPLEMENTATION OF THE NET STABLE FUNDING RATIO (NSFR)

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E. Guidelines for Islamic Banks (IBs) and Islamic Banking Units (IBUs)

68. The provisions of this Appendix apply to IBs/IBUs, subject to the provisions of Section XI of Appendix 71, which requires, among others, that the instruments to be used in liquidity management must be acceptable to the Shari’ah Advisory Council. Further, IBs/IBUs shall consider the following guidelines:

- a. An IBU need not submit a separate NSFR report. Nonetheless, a conventional bank should consider the provisions set forth below when consolidating IBU’s activities in its NSFR report. Further, as part of or as a supplement to its internal liquidity management guidelines, the IB/IBU should have in place internal guidelines in compliance with the expectation of the Bangko Sentral on the mapping of accounts for purposes of NSFR computation and reporting.
- b. Investment accounts appearing on the liability side of the balance sheet of the IB/IBU shall be treated in the same way as deposits of similar type, except that all retail investment accounts with residual maturities of less than one (1) year shall receive an Available Stable Funding factor of ninety percent (90%).
- c. Financings provided by the IB/IBU shall be treated in the same way as loans of similar type advanced by a conventional bank.
- d. Sukuk held by the IB/IBU shall be treated in the same way as debt securities of similar type held by a conventional bank.

Section 5. Implementation. The minimum LCR and NSFR will be implemented following the timelines set out below:

Observation Period	LCR and NSFR of 100%
Upon effectivity of this Circular until 31 December 2024	01 January 2025 and thereafter

The availability of liquidity management instruments which are appropriate for IBs/IBUs is very limited. The observation period will provide ample time for the IBs/IBUs to strategize on their liquidity risk management

system including choice of liquidity tools to mitigate the risks arising from their business activities. Likewise, this will be an opportune time for the Islamic interbank and money market system as well as the secondary markets for Islamic funds/products to develop and gain traction as the market players gradually meet the set regulatory standards.

Requirement during the observation period. For monitoring purposes, the IB shall submit within 30 banking days from end of the reference quarter, LCR and NSFR reports in a single currency. With regard to IBU, the conventional bank proper shall **not** consolidate the IBU activities in its bank-wide LCR and NSFR reports **during the observation period**. Instead, the IBU shall submit separate LCR and NSFR reports in a single currency within 30 banking days from end of the reference quarter. The submission of the LCR and NSFR reports shall be subject to the governance process on the quality of bank reporting under Section 171 of the MORB. Any non-compliance with reporting standards, or non-submission or delayed submission of such reports shall be subject to the monetary and non-monetary sanctions under Section 171 of the MORB.

The Bangko Sentral, on its part, shall continuously review and keep an open line of communication with stakeholders to ensure that the regulatory framework remains appropriate and relevant. As the domestic Islamic banking market is still in its early stage of development, the Bangko Sentral shall adopt a flexible approach on regulatory compliance, including the submission of required reports. It shall engage and be responsive to the market players and new entrants to the Islamic banking system in implementing the minimum LCR and NSFR requirements.

While no interim target level shall be required during the observation period, the supervising department, as part of effective monitoring is expected to engage the IB/IBU on its degree of compliance with the LCR and NSFR. Moreover, there will be continuous dialogue/discussion with industry players to assess readiness for the strict implementation of the Circular.

Section 6. Reportorial Template. IBs/IBUs shall use the same LCR and NSFR reporting template adopted for conventional banks.

Section 7. This Circular shall take effect fifteen (15) calendar days following its publication either in the Official Gazette or in a newspaper of general circulation.

FOR THE MONETARY BOARD:



BENJAMIN E. DIOKNO
Governor

25 May 2021