



**GUIDELINES ON REGULATED SHORT SELLING OF
SECURITIES IN THE WHOLESALE MONEY MARKET**

**BANK NEGARA MALAYSIA
7 OCTOBER 2005**

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1.0 INTRODUCTION

- 1.1 The regulated short selling framework for Malaysian Government Securities (MGS) currently accorded to Principal Dealers as part of their market making responsibilities, is now extended to interbank participants and universal brokers. This effort is consistent with the broad objectives of the Capital Market Masterplan to further improve secondary market liquidity and enhance the development of the domestic bond market.
- 1.2 The expansion of the regulated short selling framework to include interbank participants and universal brokers will achieve the following benefits: -
 - i) Create continuous flow of activities in the bond market;
 - ii) Accelerate price corrections in overvalued securities;
 - iii) Facilitate hedging of interest rate risks; and
 - iv) Promote activity in the repo and securities borrowing and lending market
- 1.3 These Guidelines set out the terms and conditions for short selling of securities permitted by Bank Negara Malaysia (BNM) in the wholesale money market.
- 1.4 These Guidelines shall be effective from 7 October 2005.

2.0 COVERAGE

- 2.1 These Guidelines do not apply to “when-issued” trading of securities as defined in Rules on Bond Information and Dissemination System (BIDS).
- 2.2 These Guidelines should be read together with: -

- i) The ACI Model Code with Malaysia's local addendum;
- ii) The Rules on the Scripless Securities under the Real Time Electronic Transfer of Funds and Securities (RENTAS) System;
- iii) Rules on BIDS;
- iv) Rules on FAST;
- v) Guidance Notes on Repurchase Agreement Transactions;
- vi) Guidelines on Securities Borrowing and Lending Programme under RENTAS;
- vii) Guidelines on Access to Interbank Market by Universal Brokers; and
- viii) Any other rules, guidelines and directives issued by BNM from time to time.

3.0 DEFINITIONS

3.1 Unless the context otherwise requires, the following expressions shall bear the following meanings: -

“BNM” means Bank Negara Malaysia, a body corporate established under the Central Bank of Malaysia Act 1958;

“Guidelines” means the Guidelines on Regulated Short-selling of Securities in the Wholesale Money Market;

“BIDS” means Bond Information and Dissemination System;

“FAST” means Fully Automated System for Issuing/Tendering;

“Short selling” refers to a sale of securities where the seller does not have presently exercisable and unconditional right to vest the securities in a purchaser at the time of the sale. Specifically,

- *Covered short selling* refers to short-selling activities with borrowed securities, obtained via reverse repo or securities borrowing and lending facilities on the short selling transaction date; and
- *Naked short selling* refers to short-selling activities without borrowed securities. Dealers close out the naked short-selling position by conducting an offsetting deal at a later date.

“RENTAS” means Real Time Electronic Transfer of Funds and Securities System which is the real time gross settlement system operated by BNM which provides for: –

- interbank funds transfers in Malaysia
- scripless securities transfers on delivery-versus-payment mode; and
- such other transaction or transactions as may be approved by BNM from time to time.

4.0 ELIGIBLE MARKET PARTICIPANTS

- 4.1 All commercial banks, finance companies, merchant banks and discount houses licensed under Banking and Financial Institutions Act 1989 that are interbank players, and universal brokers as approved by the Securities Commission to undertake short selling transaction.
- 4.2 Any other institutions permitted by BNM.
- 4.3 All short selling transactions must be for own positions of Eligible Market Participants.

5.0 ELIGIBLE SECURITIES

- 5.1 Any specific issue of Malaysian Government Securities with an outstanding nominal amount of at least RM2.0 billion and remaining tenure to maturity of 10.5 years or less, at the time when the short selling position is created.
- 5.2 BNM, at its discretion, may review the list of Eligible Securities for short selling purposes.

6.0 PERMITTED SHORT SELLING TRANSACTIONS

- 6.1 Only Eligible Market Participants are permitted to conduct short selling of Eligible Securities in accordance with these Guidelines.
- 6.2 Only covered short selling of Eligible Securities is allowed whereby the Eligible Securities to be short sold must be covered on the same transaction day the short selling position is created via repurchase agreement or securities borrowing.
- 6.3 With the exception of intraday transactions, naked short selling of Eligible Securities is not allowed in order to minimize market manipulation activities.
- 6.4 Illustration of permitted short-selling transaction is provided in Appendix I: At T_0 (day 0), a short selling transaction is entered into by an Eligible Market Participant for value date T_x (day x). To avoid a naked short selling position,

the Eligible Market Participant must borrow the Eligible Securities on T_0 for settlement not later than value T_2 via reverse repo (1st leg) or securities borrowing. The maturity date of the reverse repo (2nd leg) and securities borrowing must be at least on T_x or later.

7.0 SECURITIES BORROWING AGREEMENT

- 7.1 An Eligible Market Participant must have executed the Global Master Repo Agreement or the Securities Borrowing and Lending agreement with at least 2 other market participants (excluding BNM) to ensure reasonable access to borrow Eligible Securities to cover short positions and mitigate settlement risk.
- 7.2 For repo/reverse repo transactions, at least one party of the transactions must be a licensed financial institution.

8.0 PERIOD OF SHORT SELLING

- 8.1 A short selling transaction should not exceed 12 months from the trade date, T_0 . The period of short selling as per Appendix I, refers to the period between T_0 and T_x .
- 8.2 The borrowing transaction for each covered short sale must be entered on T_0 for a borrowing period that begins not later than value T_2 to at least T_x .

9.0 SHORT POSITION LIMIT

- 9.1 An Eligible Market Participant's short position should not exceed 10% of the outstanding nominal amount of each Eligible Security issue.

10.0 INTERNAL CONTROLS

- 10.1 Eligible Market Participants engaging in short selling must be aware of the risks involved and must have the financial capacity to assume such risks.
- 10.2 Eligible Market Participants are required to establish internal guidelines for short selling prior to conducting short selling transactions.

- 10.3 The internal guidelines shall establish adequate internal control systems and procedures for the supervision and monitoring of covered short selling activities by Eligible Market Participants to ensure compliance with the Guidelines.
- 10.4 The internal procedures must clearly differentiate between covered and naked short selling transactions and ensure that naked short selling must not be undertaken.
- 10.5 BNM may, at its discretion, withdraw the eligibility of any market participant to conduct short selling activities due to weak internal controls.

11.0 BNM SECURITIES LENDING AND REPO FACILITIES

- 11.1 Subject to the availability of Eligible Securities, interbank participants may borrow from BNM via the securities lending or repo facilities to cover short sale positions.
- 11.2 The Eligible Securities may be obtained from BNM via tender in accordance with such procedures set by BNM.

12.0 REPORTING REQUIREMENTS

- 12.1 Eligible Market Participants shall report in BIDS or any other such system specified by BNM, as follows: -
- i) All short sale transactions reported as part of securities sale transactions on the short selling trade date;
 - ii) Report in BIDS or any other such system specified by BNM, all borrowing transactions to cover the short selling transactions on the short selling trade date;
 - iii) Report in BIDS or any other such system specified by BNM, all close out transactions to the short selling positions when conducting the offsetting deals at a later date;
 - iv) Report weekly, the daily outstanding short positions to BNM, categorized by tenure buckets in the format provided in Appendix II. The information

provided by Eligible Market Participants must be based on transaction date;

- v) Immediately report any short position of 5% or more of any Eligible Securities in the format provided in Appendix III.

13.0 DELIVERY AND SETTLEMENT

- 13.1 All short selling transactions and respective borrowings must be initiated and confirmed through RENTAS on the short selling trade date.
- 13.2 Deal date and value date of short sale transactions must be keyed-in correctly as RENTAS will generate reports on naked short-selling position.
- 13.3 In the event of failure on the part of the short seller to deliver the Eligible Securities on the value date, the procedure for such unsettled transactions shall be in accordance with the procedure specified in Part VII “Settlement Principles and Procedures for Compensation of Delayed or Failed Settlement of Securities Transactions and Procedures for Buy-In or Sell-Out Arising From Unsettled Transactions” of the Rules on the Scripless Securities under the RENTAS System.

14.0 DISPUTE RESOLUTION OF SECURITIES BORROWING ARRANGEMENTS

- 14.1 Any dispute, difference, controversy, breach, termination or claim arising from borrowing transactions via repurchase agreement or securities borrowing and lending shall be settled, in accordance with the Securities Borrowing and Lending Agreement or Global Master Repo Agreement signed between the parties.

15.0 SUSPENSION OF SHORT SELLING ACTIVITIES

- 15.1 If market conditions warrant it, BNM will, in its absolute discretion, exercise the following options to safeguard market stability: -
 - i) Suspension or withdrawal of Eligible Market Participant to conduct further short selling transactions;
 - ii) Suspension of BNM securities lending / repo facilities;

- iii) Suspension of short selling activities of specific Eligible Securities; and
- iv) Any other action that BNM deems appropriate

15.2 Penalties will be imposed on Eligible Market Participants in breach of the guidelines leading to market manipulation and abuse.

16.0 REVIEW OF GUIDELINES

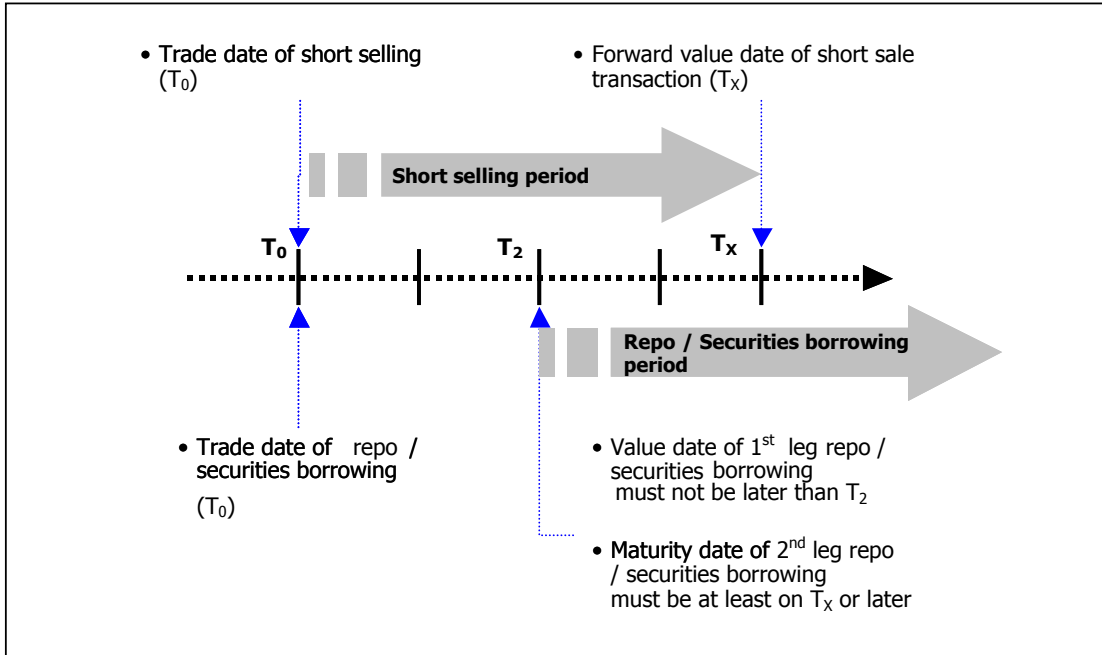
16.1 These Guidelines are subject to review and amendments by BNM from time to time.

Jabatan Operasi Pelaburan dan Pasaran Kewangan
Bank Negara Malaysia
7 October 2005

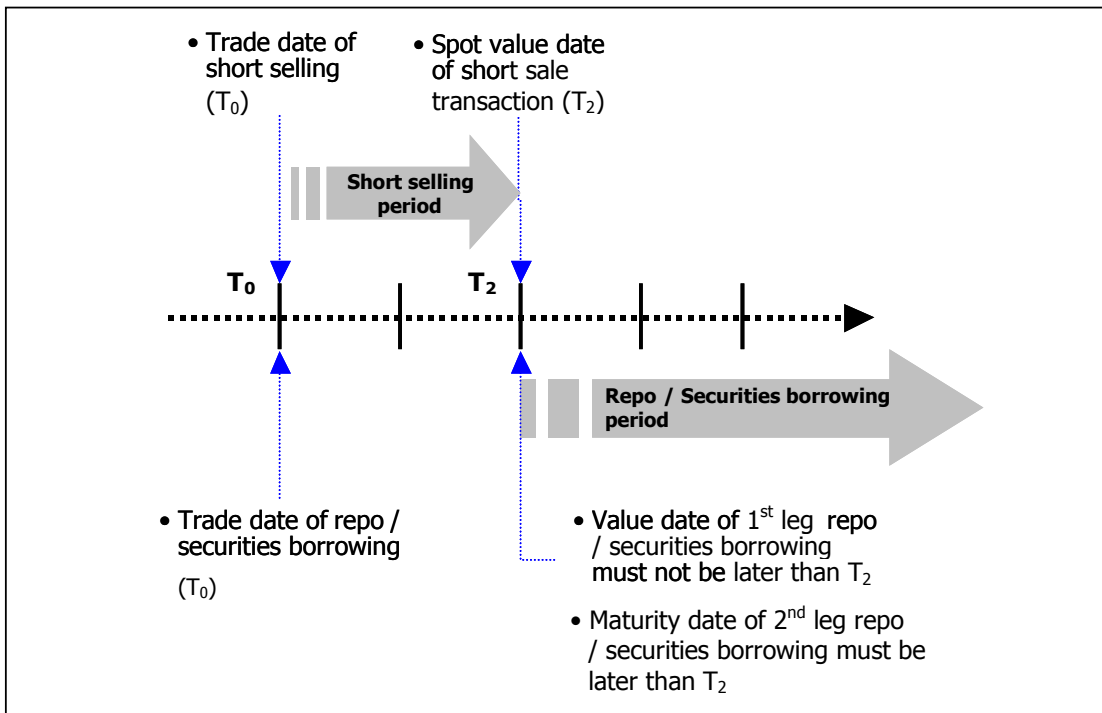
APPENDIX I

ILLUSTRATIONS OF COVERED SHORT SELLING TRANSACTIONS

i) Covered Forward Short Sale Transaction



ii) Covered Spot Short Sale Transaction



APPENDIX II

**WEEKLY REPORTING REQUIREMENTS FOR
REGULATED SHORT SELLING OF ELIGIBLE SECURITIES**

(Attention: Monetary Policy Implementation Section, Investment Operations and Financial Market Department, Bank Negara Malaysia)

Institution Name: _____

Reporting Period: _____

(Figures in RM million)

Transaction Date	< 1 year ^A	1 yr ≤ maturity < 3 yrs	3 yrs ≤ maturity < 5 yrs	5 yrs ≤ maturity < 10 yrs	≥ 10 years	Total Amount
Day 1						
Day 2						
Day 3						
Day 4						
Day 5						

^A years to maturity from the transaction date

Note:

- I. Weekly reporting must reflect the daily outstanding short position for the whole week according to maturity buckets.
- II. Report must be reported on excel spreadsheets and are to be submitted to the following addresses latest by Monday of the following business week: -
 - najib@bnm.gov.my
 - fhazim@bnm.gov.my
 - onglm@bnm.gov.my
 - ashraf@bnm.gov.my

Authorised by:

(Signature of Authorised Officer)

NAME:
DESIGNATION:

APPENDIX III

REPORTING OF SHORT POSITIONS EXCEEDING 5% OF ANY ELIGIBLE SECURITY ISSUE

(Attention: Monetary Policy Implementation Section, Investment Operations and Financial Market Department, Bank Negara Malaysia)

Institution Name: _____

Reporting Date : _____

(Figures in RM million)

No.	Deal Date of Sale	Value Date of Sale	Stock Code	Coupon	Maturity Date	Years to Maturity	Total Short Amount	Stock Outstanding Nominal Amount	% of Outstanding Nominal Amount

Note:

1. Report must be submitted by the end of the business day to the following addresses or fax to 03 – 2691 8936 / 2694 6240.

- najib@bnm.gov.my
- fhazim@bnm.gov.my
- onglm@bnm.gov.my
- ashraf@bnm.gov.my

Authorised by:

(Signature of Authorised Officer)

NAME:

DESIGNATION: