



BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Reference Rate Framework

Issued on: 19 March 2014

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework
------------------	---	--------------------------

PART A	OVERVIEW	1
1.	BACKGROUND	1
2.	OBJECTIVE	2
3.	APPLICABILITY AND SCOPE	2
4.	LEGAL PROVISIONS	3
5.	EFFECTIVE DATE	3
6.	INTERPRETATION	3
7.	GUIDELINES SUPERSEDED	4
PART B	POLICY REQUIREMENTS	5
8.	REFERENCE RATE AND FINANCING RATES	5
9.	DEPOSIT RATES	7
10.	NOTIFICATION REQUIREMENT	8
11.	DISCLOSURE REQUIREMENT	9
12.	SUBMISSION OF INFORMATION	9

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 1/9
------------------	---	--------------------------	-------------

PART A OVERVIEW

1. BACKGROUND

- 1.1 Reference rates allow financial service providers (FSPs) to vary floating lending rates to reflect changes to funding costs that could arise from changes in central bank policies or market funding conditions. As such, reference rates form the basis for the pricing of floating rate loans/financing facilities, while ensuring that changes in monetary policy are transmitted to borrowers. The way in which reference rates are determined and used would support efficient financial intermediation and facilitate effective monetary policy transmission.
- 1.2 The base lending rate (BLR) framework was introduced in 1983. Over time, FSPs have been given greater flexibility to set their own BLR based on cost structures and business strategies. FSPs can also determine their own lending rates for all credit facilities and loan products based on internal and commercial considerations.
- 1.3 With the liberalisation of interest rates, retail lending rates in the financial system have been observed to move in tandem with the costs of lending and the risks assumed by FSPs. However, while the BLRs have moved in response to changes in the Bank Negara Malaysia (the Bank) Overnight Policy Rate (OPR), retail lending rates have typically adjusted by less. This suggests that the link between the BLR and retail lending rates has weakened. In addition, the increasing level of competition in the retail segment in an environment of excess liquidity has spurred the offering of retail loans/financing facilities at a substantial discount to the BLR over the

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 2/9
-------------------------	---	---------------------------------	--------------------

past few years. This has also resulted in an uneven transmission of changes in monetary policy to the cost of financing observed between existing and new borrowers. These developments indicate that the BLR has become less relevant as a meaningful reference rate in the pricing of retail financing products. The lack of transparency and comparability in how BLRs are set by FSPs has also increased the challenges of assessing and communicating the effectiveness of monetary policy transmission to retail lending rates.

2. OBJECTIVE

This policy document outlines a reference rate framework which aims to:

- (a) promote a transparent reference rate that allows meaningful comparison to be made for informed decision making by consumers;
- (b) better reflect changes in the cost of funds arising from monetary policy or market funding conditions; and
- (c) encourage more disciplined and efficient practices by FSPs in the pricing of retail loans/financing facilities.

3. APPLICABILITY AND SCOPE

3.1 This policy document is applicable to all FSPs as defined in paragraph 6.2.

3.2 This policy document is applicable to all retail loans/financing facilities, including Shariah-compliant financing, which are priced against a reference rate.

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 3/9
------------------	---	--------------------------	-------------

4. LEGAL PROVISIONS

The requirements in this policy document are specified pursuant to:

- (i) sections 47(1), 123(1) and 143(1) of the Financial Services Act 2013 (FSA);
- (ii) sections 57(1), 135(1) and 155(1) of the Islamic Financial Services Act 2013 (IFSA); and
- (iii) sections 41, 126 and 116(1) of the Development Financial Institutions Act 2002 (DFIA).

5. EFFECTIVE DATE

The policy document shall come into effect on 2 January 2015 (“effective date”), except for paragraph 10.1.

6. INTERPRETATION

6.1 The terms and expressions used in this policy document shall have the same meanings assigned to them in the FSA, IFSA and DFIA, as the case may be, unless otherwise defined in this policy document.

6.2 For the purpose of this policy document:-

“**S**” denotes a standard, requirement or specification that must be complied with. Failure to comply may result in one or more enforcement actions;

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 4/9
------------------	---	--------------------------	-------------

“**G**” denotes guidance which may consist of such information, advice or recommendation intended to promote common understanding and sound industry practices which are encouraged to be adopted;

“**Base lending rate**” or “**BLR**” includes reference to the Base Financing Rate (BFR) in the context of Islamic retail financing facilities;

“**Financial service provider**” or “**FSP**” means -

- (a) a licensed bank under the FSA;
- (b) a licensed Islamic bank under the IFSA; and
- (c) a prescribed institution under the DFIA.

“**Retail lending rates**” refer to lending rates for conventional retail loans and financing rates for Islamic retail financing facilities; and

“**Retail loans/financing facilities**” refer to loans or financing facilities extended to individuals which are priced against a reference rate, including but not limited to mortgage loans/financing, vehicle loans/financing, personal loans/financing and loans/financing to individuals for business use. Credit card facilities which are subject to the maximum financing rate of 18% per annum as stipulated in the Credit Card Guidelines are excluded from the scope of this policy document.

7. GUIDELINES SUPERSEDED

The Guidelines on Reference Rates, Lending Rates and Deposit Rates of Banking Institutions are superseded from the effective date.

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 5/9
------------------	---	--------------------------	-------------

PART B POLICY REQUIREMENTS

8. REFERENCE RATE AND FINANCING RATES

- S** 8.1 FSPs shall use the Base Rate (BR) as the reference rate for the pricing of retail loans/financing facilities. This requirement applies to applications received for new retail loans/financing facilities and refinancing of existing retail loans/financing facilities, and the renewal of existing revolving retail loans/financing facilities, on or after the effective date.
- S** 8.2 FSPs shall determine the BR based on the FSP's benchmark cost of funds and statutory reserve requirement (SRR). The benchmark cost of funds shall reflect the FSP's specific funding strategies.
- S** 8.3 The use of benchmark cost of funds for pricing retail loans/financing facilities would ensure a more effective monetary policy transmission from OPR adjustments to lending rates on retail loans/financing facilities for both existing and new borrowers. The BR is intended to reflect the management of interest rate risk that is directly influenced by monetary policy changes and market funding conditions.
- S** 8.4 FSPs shall adjust the BR to reflect changes to the benchmark cost of funds due to changes in the OPR and the SRR.
- G** 8.5 FSPs are allowed to adjust the BR to reflect changes to market funding conditions.

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 6/9
------------------	---	--------------------------	-------------

- S** 8.6 FSPs shall have in place proper policies and clear governance arrangements for determining the BR (including its basis), periodic review of the BR and changes in the BR. The process, methodology and data used for determining the BR shall be documented and made available for the Bank's supervisory review as and when required.
- S** 8.7 FSPs shall exclude other components of pricing from the computation of the BR such as credit and liquidity risk premiums, operating costs, profit margins and others. FSPs shall reflect these components in the spread over the BR.
- S** 8.8 Where the pricing for a retail loan/financing facility is tied to the BR, the lending/financing rate charged to the borrower shall be the BR **plus** a spread.
- S** 8.9 Where there are any changes made to the BR, FSPs shall effect a corresponding adjustment to all new and outstanding retail loans/financing facilities which are priced against the BR.
- S** 8.10 Once a contract for a retail loan/financing facility is concluded, any revision to the spread above the BR during the tenure of the retail loan/financing facility shall only be made to reflect changes in the credit risk profile or creditworthiness of the borrower over the life of the loan/financing facility.
- S** 8.11 Apart from changes in the creditworthiness of the borrower, FSPs shall not increase the spread on outstanding retail loans/financing facilities to reflect changes in operating cost, funding management strategies or portfolio default experience. FSPs shall not increase the spread to gain a higher profit margin during the tenure of a retail loan/financing facility.

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 7/9
------------------	---	--------------------------	-------------

- S** 8.12 Existing floating rate retail loans/financing facilities which were granted prior to the effective date shall continue to remain priced against the BLR.
- S** 8.13 When FSPs adjust the BR, the FSPs shall make a corresponding adjustment¹ to the BLR in respect of retail loans/financing facilities under paragraph 8.12 to reflect changes in the FSPs' benchmark cost of funds.
- S** 8.14 For any upward or downward adjustment to the BR and the BLR, FSPs shall revise the monthly instalments of retail loans/financing facilities which are priced against the BR or the BLR as the default option. FSPs shall provide borrowers with particulars of the revised monthly instalment amount at least seven calendar days prior to the date the revised monthly instalment comes into effect.
- S** 8.15 FSPs may allow a borrower to retain the monthly instalment amount upon the borrower's specific request. In such an event, FSPs shall clearly communicate to the borrowers the implications of maintaining the existing monthly instalment amount, including any new terms and additional cost of borrowing that will be incurred as a result of an extension of the tenure of the retail loan/financing facility.

9. DEPOSIT RATES

- G** 9.1 FSPs may determine the rates payable on deposits accepted based on their funding requirements and strategies.

¹ FSPs shall adjust the BLR by the same magnitude for any revision to the BR.

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 8/9
------------------	---	--------------------------	-------------

- S** 9.2 In the case of conventional children savings accounts, the deposit rates payable on accounts with balances of up to RM50,000 shall not be lower than the 1-month fixed deposit rate of the respective FSPs.
- S** 9.3 In the case of a Housing Development Account, the rate payable shall be computed on the daily balance and is set at:

1 month fixed deposit account rate – 1%

10. NOTIFICATION REQUIREMENT

- S** 10.1 FSPs shall submit to the Bank (i.e. the Director of Consumer and Market Conduct Department) the basis and methodology used to set the BR as well as the triggers or conditions for change to the BR at least two months prior to the effective date. FSPs shall also notify the Bank of the proposed BR level to be adopted at least one week prior to the effective date.
- S** 10.2 For revisions to the level of the BR and the BLR, FSPs shall notify the Bank (i.e. the Director of Consumer and Market Conduct Department) at least one working day prior to the date the revision comes into effect. Any proposed revision to the level of the BR and BLR due to factors other than a change in the Bank's OPR must be accompanied by the reasons for the revision. The advance notification to existing borrowers on the revised monthly instalment amount as required under paragraph 8.14 shall take place only after the lapse of the one working day's notice to the Bank.

BNM/RH/STD 028-6	<ul style="list-style-type: none"> • Consumer and Market Conduct Department • Monetary Assessment and Strategy Department 	Reference Rate Framework	Page 9/9
------------------	---	--------------------------	-------------

11. DISCLOSURE REQUIREMENT

- S** 11.1 FSPs shall ensure that the BR and its effective date is prominently displayed at all branches and websites. Apart from disclosing the BR, FSPs shall continue to display their BLRs at all branches and websites until the maturity of all retail loans/financing facilities priced against the BLR.
- S** 11.2 FSPs shall display changes to the BR and BLR at the FSP's branches and website no later than the date in which the revision comes into effect.

12. SUBMISSION OF INFORMATION

- S** FSPs shall submit to the Bank the information as specified in the following returns at a regular interval:
- (a) Weekly Interest and Islamic Deposit/Financing Rates (ISS);
 - (b) Monthly Interest and Islamic Deposit/Financing Rates (ISS); and
 - (c) Financing rates on new loans approved during the month (submission to Statistical Services Department).