

626-A EXPANDED FOREIGN CURRENCY DEPOSIT UNIT INVESTMENTS IN FOREIGN CURRENCY DENOMINATED STRUCTURED PRODUCTS

The following guidelines allow UBs and KBs without expanded derivatives authority to invest in certain specified structured products.

Policy statement. The Bangko Sentral encourages banks to diversify their EFCDU investment portfolios in order to stabilize earnings, control maturity mismatches and minimize over concentration of exposures.

Scope. EFCDUs of UBs and KBs without expanded derivatives authority may invest, for their own account, in foreign currency-denominated structured products issued by banks and SPVs of high credit quality: *Provided*, That the revenue streams of such products may only be linked to interest rate indices and/or foreign exchange rates other than those that involve the Philippine Peso: *Provided, further*, That the minimum all-in return of such investments may not be lower than zero. For purposes of this Section, structured products do not include asset backed securities, credit-linked notes and other similar instruments.

Other conditions.

- a. *Maturity* – The maximum contractual maturity of any investment in structured products shall be five (5) years.
- b. *Credit quality of issuer* – Acceptable issuers are banks and SPVs collateralized by securities rated at least “A” or its equivalent by an international rating agency acceptable to the Monetary Board.
- c. *Booking* – Investments in structured products as herein defined shall be booked in accordance with *Appendix 33*.
- d. *Prudential limits* – The total carrying value of all investments in structured products as defined herein at any given point in time must not exceed twenty percent (20%) of the total investment portfolio of the EFCDU [combined amount of Trading Account Securities (TAS), ASS and IBODI].
- e. *Risk management* – Investing banks must have established internal processes to identify, evaluate, monitor and manage the risk exposures, e.g., credit risk, market risk, liquidity risk, operational risk, legal risk, compliance risk, created by their investments in structured products. As a minimum:

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- (1) Such investments must be specifically approved by the board of directors and be subject to appropriate internal limits and periodic reporting to the Board.
- (2) Banks must comply with generally accepted accounting and disclosure standards and/or rules and regulations prescribed by the Bangko Sentral.
- (3) An independent risk management function must be in place.
- (4) Banks should have the ability to value their investments on a continuing and consistent basis and to measure their sensitivity to market movements. This should include performing, at regular intervals, stress tests that reflect extreme market conditions. As part of the valuation exercise, banks should be able to obtain bid prices from the issuers of the investment instruments on a monthly basis.
- (5) Management should ensure that the risks of the investments are accurately aggregated in risk reports on a timely basis.

Capital treatment of structured products. The capital treatment shall be in accordance with existing rules and regulations as modified for structured instruments.

Bangko Sentral approval not required. No prior Bangko Sentral approval is required to enter into authorized transactions. However, it shall be the responsibility of UBs/KBs to fully comply with appropriate risk management standards including, as a minimum, those prescribed under this Section. The regulatory requirements enumerated in *Appendix 64* shall be fully complied with by UBs/KBs investing in products allowed under this Section.

Sanctions. Non-compliance with the provisions of this Section shall subject the bank to a fine of one-tenth of one percent (1/10 of 1%) of the outstanding investment per day, but not to exceed P30,000 per day, to be reckoned from the day the bank is deemed in violation of regulations, until the day the bank has complied with the requirements. Banks may also be temporarily or permanently prohibited from such investments as circumstances may warrant.

(Circular No. 1011 dated 14 August 2018)