

OPERATIONAL GUIDELINES FOR DISCOUNT HOUSES

NO. OG1-02/FMO

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PART I: OBJECTIVES, AUTHORISATION AND APPLICATION

1. Objectives

The purpose of these guidelines is to establish a consistent and uniform mechanism whereby the Reserve Bank of Malawi (the Bank) may:

- a. Provide support to discount houses in terms of their liquidity management to ensure smooth operations in the money market
- b. Ensure that discount houses adhere to appropriate prudential requirements so that their business is conducted in a safe and sound manner in the interest of depositors and creditors.

2. Authorisation

Sections 4 (g), (h) and 46 of the Reserve Bank of Malawi Act 1989 Cap 44:02, and Section 38 of the Banking Act of 1989, Cap 44:01

3. Application

All discount houses licenced as such under the Banking Act, 1989

PART II: PERMISSIBLE ACTIVITIES AND PRUDENTIAL REQUIREMENTS

1. Permissible Activities

Unless the Bank's approval is granted, a discount house shall restrict itself to the following activities:

- a. Overnight loan accounts with banks
- b. Call money accounts with banks and corporate sector
- c. Repos/reverse repos with banks and corporate sector
- d. Making markets in money market instruments

2. Prudential requirements

a. A discount house shall maintain a reasonable level of borrowing in relation to its capital base in order to avoid over-exposure. The capital base shall consist of paid up capital and retained earnings. For this purpose, the borrowing liability ratio, which shall be defined as call money plus borrowing over capital base, shall not exceed 30.

i.e., $\text{Call money} + \text{Borrowing} < 30 \text{ Capital base}$

b. The short-term nature of the liabilities of a discount house shall require that its assets be very liquid. In this regard, a discount house shall be required to have 70 percent or more of its adjusted total assets (i.e. Short-Term Asset Ratio or total assets less fixed assets) in short-term securities. In these guidelines short-term assets shall consist of the following:

- Malawi Government Treasury Bills
- Reserve Bank of Malawi Bills
- Bankers Acceptances
- Negotiable Certificates of Deposits
- Commercial Paper
- Cash balances with banks
- Other stocks and bills determined by the Bank from time to time

c. Non-collateralised call or term deposits by the corporate sector shall be subject to the Liquidity Reserve Requirements (LRR) as stipulated in the ruling LRR Directive to commercial banks. In this regard the discount house shall be required to maintain 30 percent of their weekly total non-collateralised deposit liabilities in their clearing account at the Bank. A sample form for the computation of the LRR is attached as Appendix 3.

d. Failure to maintain the weekly average minimum Reserve Requirement as specified in the preceding section will constitute a violation of the LRR Directive. Penalty for non-compliance shall be as stipulated in the ruling LRR Directive.

e. Assets in the form of the following fixed assets shall not exceed 30 percent of capital base:

- Motor Vehicles
- Furniture and Fittings
- Office Equipment
- Company Premises

PART III: PROCEDURES TO BE FOLLOWED

1. Primary Auctions and Open Market Operations

- a. A discount house shall participate through competitive bidding in primary auctions of securities issued by the Bank.
- b. If in surplus, a discount house may be allowed to purchase on tap securities available at the Bank's open market operations dealing desk. Allotment of securities will be at a negotiated rate.
- c. A discount house may be allowed to sell, at a negotiable rate, securities to the Bank's open market operations dealing desk. For the time being, such securities shall be Treasury bills and Reserve Bank of Malawi bills

2. Borrowing facilities at the Bank

The Bank shall provide accommodation to discount houses under the terms and conditions of the Standing Facilities Directive issued by the Bank.

3. Reporting Requirements and on-site Inspection

- a. To ensure compliance with the controlling ratios and also to monitor its activities in the money market, a discount house shall submit daily, weekly and monthly returns in a prescribed format (as in appendices 4, 5, and 6, respectively) to the FMO department of the Bank.
- b. After settlement each day, a discount house shall submit returns of its asset composition and borrowing and lending rates and discount rates by 10.00 a.m. the following day.
- c. A discount house shall also be required to submit weekly reports of its assets and liabilities for the normal business week of Monday to Friday. These reports shall be submitted to the Bank by close of business on the Wednesday of the following week.
- d. Within the first five working days of every month, a discount house shall submit monthly returns on the composition of its assets and liabilities as at end of the preceding month. For the assets, the discount house must disclose all its debtors
- e. Failure to comply with the above reporting requirements will attract a penalty as determined by the Bank from time to time.
- f. The Bank shall conduct on-site inspection at least twice a year to confirm that the information contained in the returns agrees with what is actually on the ground.

PART IV: AMENDMENT TO GUIDELINES AND REMEDIAL MEASURES

1. These guidelines are subject to amendment by the Bank from time to time as appropriate.
2. The Bank may impose appropriate administrative sanctions upon a discount house or its board of directors and managing executive officers for noncompliance with these guidelines.

PART V: EFFECTIVE DATE AND SUPERSEDEANCE

1. These Guidelines become effective on 18 November 2002 and supercede Guidelines dated June 2000.
2. Questions relating to these Guidelines should be addressed to the Director, Financial Market Operations Department of the RBM.

Dr E E Ngalande
GOVERNOR
November 2002