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HongLeong Bank

Global Markets Research

Fixed Income Alert

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Update on EPF's liquidity position following the revised i-Sinar withdrawal conditions

*In this publication, we provide an update on the potential impact to EPF liquidity and local bond market based on the announcement of the latest PERMAI package announced on 21st January 2021; and **the latest relaxation in withdrawal conditions for i-SINAR** program, which is expected to allow more savers to withdraw to tie them over this thriving time.*

Nevertheless, we do not foresee the local bond market reeling from this measure as the well-capitalized and large investment-based institutions including other GLIC's and Lifers are expected to be able to readily absorb the impact, especially for government bonds in the secondary market. In addition, the revenue stream from both the potential divestment of its investment assets and coupon plus dividend payments should be sufficient to cover the potentially higher withdrawals, whilst we are comforted by the fact that these are only short term measures.

EPF's contribution & withdrawal estimate update, February 2021

Updates on estimation on contribution and withdrawal under the various programs which we originally penciled in our earlier report dated 23rd November 2020 are detailed in the table below:

RM (Billion)	Initial Target	Initial Projection	Current Target	Current Plausible	Remarks/Assumptions
Gross contributions	76.0	76.0	76.0	76.0	Normal contribution/withdrawal; assume to be as per 2019 levels
Withdrawals	(45.0)	(45.0)	(45.0)	(45.0)	
Net contributions	**31.0**	**31.0**	**31.0**	**31.0**	
i-Lestari withdrawals from Account 2 (Jan-Mar 21 only)	(7.5)	(3.8)	(14.1)	(15.5)	Initial projection based on 50% take-up rate. Current plausible maintained @ additional 10% from actual data reported of 14.1b pending disbursements
i-Sinar withdrawals from Account 1 (Jan 21-Jun 21)	(14.0)	(7.0)	(70.0)	(40.8)	Initial projection based on 50% take-up rate. Current plausible 20% from actual data reported of 34.0b pending disbursements
Employee contribution rate cut from 11% to 9% (Jan 21-Dec 21)	(9.3)	(7.4)	(7.4)	(7.4)	Based on 80% take-up rate
Estimated Total Outflows/Reduction for 2021	**(30.8)**	**(18.2)**	**(91.5)**	**(63.7)**	
Revised net contributions before dividends & coupon payments	**0.2**	**12.8**	**(60.5)**	**(32.7)**	
Fixed income coupon payments	**9.1**	**9.1**	**9.2**	**9.2**	2% from RM462b (49% of RM942b AUM)
Equities dividend income	**7.1**	**7.1**	**7.3**	**7.3**	2% from RM367b (9% of RM942b AUM)
Total Estimated Investment Income	**16.2**	**16.2**	**16.5**	**16.5**	
Estimated Net Inflows	**16.4**	**29.0**	**(44.0)**	**(16.2)**	

Source : MOF, EPF, HLBB Global Markets Research

The relaxation of conditions surrounding the i-SINAR withdrawal facility involves:

- Those below the threshold of 55 years are now allowed to withdraw subject to their existing balance.
- Documentary evidence that income/revenue has fallen by at least 30% due to the economic malaise caused by the COVID-19 pandemic is now removed. Hence no further proof required for this.

However the existing payment schedule will be maintained i.e.

1. Those with <RM100,000 and below in Account 1 are able to withdraw up to RM10,000; staggered over six (6) months ~with the 1st payment amount of up to RM5,000.
2. Those with >RM100,000 and above can withdraw up to 10% in Account 1, capped at maximum of RM60,000; staggered also over 6 months ~with the 1st payment of up to RM10,000.

As mentioned in the table above**, we have maintained take-up rates of additional 10% from the actual i-Lestari but revised to 20% the unconditional withdrawals from i-Sinar via Account 1 which is expected to create a larger cash-flow deficit.** Drilling further we opine that bulk of withdrawal interest (if any) will be forthcoming mainly by the estimated 5.7m contributors that have balances of RM100, 000 and below**.** We have revised estimates for i-Lestari and also conservative revenue streams of ~2.0% for both fixed income coupon payments and also dividends from equities holdings which will provide timely boost to cash-flows. **Hence we arrive at a potential cash-flow deficit of RM16.2b (representing only ~1.7% of overall AUM of RM942b).**

Implications on the local bond market

We expect EPF to play a slightly less pro-active role in the liquidity and robustness of the local bond markets; namely via private placements in the government bonds sector at least until June 2021. Nevertheless we do not foresee adverse impact on the local bond market based on the following observations;

1. BNM's initiatives to provide a deep, liquid bond market to ensure that Malaysia continues to remain in key global bond indices such as FTSE Russell WGBI can easily be shouldered among other GLIC's such as PNB and KWAP which can easily step up their presence in the secondary market to ensure the continuance of a developed and orderly market and mitigate the adverse impact from EPF's lower presence temporarily in the secondary markets.

2. Based on its existing holdings, the EPF is expected to receive additional relief via MGS/GII maturities totaling RM13.0b in Q12021 and RM12.0b in 2Q2021.

3. In the event partial divestment of existing assets are required to fund the lower contribution and higher withdrawal, the current low yield environment following four (4) interest rate cuts in 2020 provides opportunities for EPF to raise funds via realization of decent profits. Similarly, the same applies to the equities asset class for which the various health-care, technology sectors and other large-cap/ trustee stocks sectors that EPF had invested earlier may allow it to reap the benefits in the present liquid market.

4. EPF's prudent management in maintaining ~between 7.0-7.2% of its total AUM in short-term money market funds amounting to RM67b puts in good stead to meet its immediate withdrawal obligations.

5. Being the 13th largest sovereign fund in the world, EPF has successfully built a large portfolio with ~32% of its assets invested abroad in the various asset classes based on excellent foresight in recent years. This strategy has allowed itself to spread its concentration risk besides boosting returns. Lately it has notified its intention to streamline and cash-in some of its property assets to the tune of ~RM350-450m both within and outside of Malaysia.

Whilst we take cognizance of concerns over EPF's current liquidity status, we opine that it is able to overcome these hurdles which are not expected to stretch beyond 2021, based on the various factors stated above.

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