RESPONSE TO FEEDBACK RECEIVED - CONSULTATION PAPER ON BORROWING GUIDELINES FOR PROPERTY FUNDS

On 16 December 2002, MAS issued a Consultation Paper inviting comments from the industry and the public on proposals to raise the borrowing limit for property funds. The objective is to give property funds more flexibility in managing their capital structures while retaining appropriate safeguards so that the funds can service and repay their borrowings. The Consultation Paper also sought comments on proposals for enhanced risk disclosures associated with investing in property funds.

The consultation period closed on 16 January 2003. The recommendations to allow property funds to borrow up to 35% (25% previously) of their deposited property and above that threshold if certain credit rating requirements are met were well received. Many respondents agreed that the value of new properties to be purchased with any proposed borrowing should be taken into account in determining the gearing of the fund. Guidance on proposed enhancements to risk disclosures by property funds also received support.

MAS thanks all respondents for their comments. Some of the comments and our responses are highlighted below.

1. Need for Borrowing Guidelines

One respondent suggested that property funds should not be subject to any borrowing guidelines. The rationale is that, unlike general securities funds which can invest in securities with unrestricted gearing levels, property funds invest directly in ungeared property.

MAS? Response: MAS considers it prudent to retain borrowing guidelines for property funds.Although a general securities fund may invest in highly-geared securities, it cannot borrow to make investments. (The 10% borrowing limit on securities funds is only for redemption and short-term bridging requirements.) Further, such a fund?s exposure to any single highly-geared security is capped because of the 10% single party exposure limit. Property funds on the other hand are able to borrow to finance property purchases and are not required to maintain a diversified portfolio of assets (so long as this is disclosed in the prospectus). Finally, a property fund is liable for its own borrowings, unlike a securities fund which need not be liable for the borrowings of the company whose securities it has purchased.

2. Credit Ratings

The Consultation Paper proposed that property funds be allowed to borrow more than 35% of their deposited property if

(i) all the borrowings by the property fund are made via debt issues which are rated at least A by Fitch Inc., Moody?s or Standard and Poor?s; or

(ii) the property fund itself is rated at least A by Fitch Inc., Moody?s or Standard and Poor?s.

Some respondents suggested that the minimum credit rating should be set at investment grade (BBB) instead of ?A?. Others proposed requiring two ratings instead of one, to discourage ?shopping? for the best rating. A few respondents were of the view that the ability of a property fund to service its debt is more accurately reflected in the credit rating of the fund itself rather than of its debt issues. One commentator suggested clarifying whether the relevant credit rating should be before or after incurring the borrowings.

MAS' Response: For prudential reasons, an ?A? rating was proposed to provide a cushion for any subsequent rating downgrade. To keep fund management costs low, MAS proposes to require only one credit rating. Allowing a property fund to use the credit rating of its debt issues besides that of the fund itself provides greater flexibility. Risks are still kept in check since the debt issues must be rated at least A. As to the relevant credit rating to consider, the guidelines will clarify that the rating must take into account any new borrowings.

3. Use of Borrowings

One respondent suggested that there should be safeguards to prevent borrowed funds from being used for purposes other than the intended property purchase.

MAS' Response: The guidelines will require that borrowings be utilized for the purchase of the property for which the borrowings are intended. Further, if the manager becomes aware that the purchase will not take place, the manager must repay the borrowings as soon as practicable.

MONETARY AUTHORITY OF SINGAPORE

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