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Malaysia: Pengurusan Danaharta Nasional Berhad[1]

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Abstract

After the devaluation of the Thai baht in 1997, the Malaysian economy experienced turmoil and a financial crisis. As part of the government's response to the financial crisis, it established Danaharta, a national asset management company, alongside a recapitalization agency, Danamodal, and a debt restructuring body, the CDRC, to address instability in the financial system. The government established Danaharta with the purpose of removing nonperforming loans from the financial system and maximizing their recovery. The Danaharta Act granted the agency special legal authority to more efficiently resolve NPLs. Danaharta received funding from the government and issued zero-coupon, government guaranteed bonds in exchange for assets, which it purchased at market value. To incentivize financial institutions to sell NPLs, Danaharta implemented an incentive and penalty structure, including a profit-sharing arrangement. Danaharta also managed RM27.97 billion ($7.4 billion) in NPLs previously acquired by the government and central bank. Danaharta used a variety of methods to deal with acquired assets depending on whether the borrowers were viable or non-viable. Over its lifetime, Danaharta's portfolio totaled RM52.42 billion in face value of NPLs, and it recovered RM30.35 billion (58 percent), and recognized a net loss of RM1.14 billion on RM8.94 billion total invested. When Danaharta ceased operations in December 2005, the remaining residual assets were transferred to a subsidiary of the Ministry of Finance, Prokhas, for collection.

Keywords: Malaysia, asset management company, NPLs, asset-backed securitization, Asian financial crisis

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[1] This case study is part of the Yale Program on Financial Stability (YPFS) selection of New Bagehot Project modules considering broad-based asset management company programs.

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Malaysia: Pengurusan Danaharta Nasional Berhad

At a Glance

Economic instability increased in Malaysia after the devaluation of the Thai baht in July 1997. Though Malaysia was not subject to a debt crisis like other Asian countries, it had structural vulnerabilities in its financial system including increased foreign capital and rapid growth of foreign bank debt. The government established Pengurusan Danaharta Nasional Berhad (Danaharta), the national asset management company (AMC), in addition to a debt restructuring body and a recapitalization vehicle, in response to the growing NPL (nonperforming loan) problem in 1998. The Danaharta Act was the legal authority through which the government gave the AMC the mandate to remove NPLs from the financial system and achieve maximum recovery value.

Summary of Key Terms	
Purpose: "Danaharta's primary mission [was] to remove the non-performing assets from the system and manage them with the goal to maximize the proceeds from the recovery process" (Fung et al. 2003).	
Launch Dates	Announcement: May 20, 1998 (Danaharta 2005) Established: June 20, 1998 (Danaharta 2005) First transfer: August 26, 1998 (Danaharta 1998f)
Wind-down Dates	Date of last transfer: March 2001 Date of last asset disposal: December 31, 2005
Size and Type of NPL Problem	11.4% of banking system loans in August 1998 Primarily large loans
Program Size	Bond issuance limited to RM15 billion ($3.95 billion)
Eligible Institutions	All Malaysian financial institutions Open bank only
Usage	Acquired NPLs: RM 19.71 billion ($5.2 billion) (book) for RM8.94 billion ($2.35 billion) Managed NPLs: RM27.97 billion ($7.4 billion) (book) at no cost
Outcomes	Recovered RM30.35 billion ($8 billion) on managed and acquired NPLs for a total loss of RM1.14 billion ($300 million) (Danaharta 2005)
Ownership Structure	Government-owned
Notable Features	Incentive and penalty structure to encourage sale of NPLs; securitization

Danaharta acquired assets at market price in exchange for zero coupon government-guaranteed bonds with a five-year maturity. All financial institutions were eligible to transfer NPLs with a value of RM5 million or more to Danaharta. In order to incentivize the sale of NPLs, Danaharta implemented an incentive-and-penalty structure which included a profit-sharing arrangement. Danaharta also managed NPLs on behalf of the government and central bank, though it required no capital to acquire these assets. Over its lifetime, Danaharta's portfolio totaled RM52.42 billion ($13.8 billion) in assets, which included those it purchased as well as those managed for the government and central bank. Danaharta utilized different resolution or disposal methods depending on the viability of the borrower. Danaharta recovered RM30.35 billion, or 58 percent of its portfolio, and recognized a net loss of RM1.14 billion on a total investment of RM8.94 billion.

Summary Evaluation

Danaharta has been described as a successful example of a national AMC in reports published by agencies such as the World Bank and BIS. It is recognized as having had strong legal authority, appropriate pricing, political backing, adequate financial support, and a clear mandate. It has been noted that Danaharta's recovery totals were improved by including the NPLs it managed on behalf of the government, as these loans did not require payment. These loans had a higher recovery than acquired assets, and the income from these loans prevented Danaharta from incurring a greater loss.

Pengurusan Danaharta Nasional Berhad: Malaysia Context	
GDP (SAAR, Nominal GDP in LCU converted to USD)	\$101.4 billion in 1997 \$72.4 billion in 1998
GDP per capita (SAAR, Nominal GDP in LCU converted to USD)	\$4,638 in 1997 \$3,263 in 1998
Sovereign credit rating (5-year senior debt)	Data not available for 1997 Data for Q4 1998: Fitch: BBB Moody's: A3 S&P: A-
Size of banking system	\$137.9 billion in 1997 \$110.7 billion in 1998
Size of banking system as a percentage of GDP	100% in 1997 100% in 1998
Size of banking system as a percentage of financial system	100% in 1997 100% in 1998
5-bank concentration of banking system	64.8% in 1997 61.5% in 1998
Foreign involvement in banking system	18% in 2001
Government ownership of banking system	0% in 2001
Existence of deposit insurance	Yes in 2008 Yes in 2009
Sources: Bloomberg; World Bank Global Financial Development Database; World Bank Deposit Insurance Dataset; Cull, Martinez Peria, and Verrier 2018.	

I. Overview

Background

Malaysia's economy expanded rapidly between 1988 and 1996, growing an average of 9 percent annually. The Kuala Lumpur Stock Exchange (KLSE) likewise grew sharply, quadrupling between January 1988 and January 1997. In June 1997, the net NPL ratio in the banking sector was 2.2 percent and the ratio of loan provisions to NPLs was approximately 100 percent (Yu 2001). The risk-weighted capital ratio was 12 percent, exceeding the 8 percent Basel Committee requirement (BNM 1998a). Compared to other countries impacted by the Asian Financial Crisis (AFC), Malaysia was relatively less exposed to external debt, with the total outstanding foreign debt equal to $45.2 billion—or 42 percent of GDP—as of June 1997 (Yu 2001).

Despite its relative strength, there were signals of economic weakness and structural vulnerability in Malaysia, which included "rapid growth of foreign bank debt, imprudent lending to a booming property sector and share market, a pegged exchange rate, and rapid inflows of portfolio capital into the KLSE" (Liu et al. 2001; Pepinsky 2008). Rapid growth in the property sector and securities market led to a heavy concentration of lending with 42.6 percent of domestic loans to the two sectors. In 1997, Malaysia had the highest ratio of loans to GDP in Asia, with a ratio of private-sector debt to GDP of 192.5 percent (Pepinsky 2008).

Figure 1. Exchange Rate of Malaysian Ringgit to U.S. Dollar, January 1997-December 1998

Source: FRED.

Because of economic structural weaknesses, Malaysia—subject to the contagion effect—was impacted when Thailand floated its currency, the baht, in July 1997 (Liu et al. 2001). This led to pressure on the Malaysian currency, as the ringgit faced a drastic and rapid devaluation with the exchange rate falling from 2.48 ringgit per dollar in March 1997 to 3.77 ringgit per dollar by the end of 1997 (Yu 2001). The Malaysian central bank, Bank Negara Malaysia (BNM), attempted to defend the ringgit by raising short-term rates, though this was ultimately unsuccessful (Doraisami 2014). The ringgit fell to 4.88 per dollar by January 1998 (Yu 2001).

Figure 2. Kuala Lumpur Stock Exchange (KLSE) Composite Index between 1990-2000

Source: Trading Economics.

The stock market collapsed in tandem with the rapid decline in the exchange rate, as investors began selling stocks on the KLSE due to economic uncertainty and exchange rate devaluation (Yu 2001). The KLSE Composite Index fell from 1,216.7 in January 1997, to 594.4 by the end of 1997, before falling even further to 262.7 by September 1, 1998 (Azmi and Razak 2014).

Unlike other Asian countries during the financial crisis, Malaysia did not receive an IMF assistance package, though the country did receive technical advice and guidance (Liu et al. 2001). As a part of the government's initial response, it implemented policies in line with the IMF's recommendations such as raising interest rates and tightening fiscal policy (Ariff and Abubakar 1999). As Malaysia had a relatively low level of external short-term debt, it avoided the external debt crisis impacting other Asian countries that received IMF packages (Liu et al. 2001). Malaysia had financial regulations in place that prevented an excess of hedged or unhedged short-term foreign debt (Doraisami 2014).

However, conditions did not improve, and the NPL ratio reached 11.4 percent by August 1998 and was projected to reach 15 percent by the end of the year (Danaharta 2005). Despite tighter monetary and fiscal policy, devaluation of the ringgit continued (Doraisami 2014). On September 1, 1998, BNM introduced selective exchange controls and essentially eliminated the offshore market for the ringgit by prohibiting the transfer of funds between external accounts in order to prevent currency speculation and trading. BNM also pegged the ringgit to the U.S. dollar at 3.80 ringgit per dollar (BNM 1998b). These moves were considered controversial and unconventional when they were implemented (Yu 2001).

The Malaysian government adopted new banking industry regulations in response to the crisis. Because of the high portion of lending to the property and investment sectors, BNM imposed a cap on banks to limit the total percent of loans outstanding to 20 percent for the property sector and 15 percent for the purchase of stocks or shares. The NPL classification standards were loosened, with the period extended from three months to six months (BNM 1998a). The NPL ratio decreased from approximately 13.6 percent on the three-month measure to less than 8 percent using the new six-month measure by the end of 1998 (Fung et al. 2003). More stringent requirements were passed for NPL provisioning, and banks were required to comply with the risk weighted capital ratio on a quarterly basis, from a previous annual requirement (BNM 1998a).

Program Description

The government established the National Economic Action Council (NEAC) in January 1998 to prepare a National Economic Recovery Plan (NERP) to restore financial and economic stability.[3] The NERP included a recommendation that the government establish a national asset management company (AMC) to purchase NPLs as well as a separate agency to recapitalize financial institutions. Thus, the government announced the creation of Pengurusan Danaharta Nasional Berhad (Danaharta), the national AMC, in May 1998. Danaharta was established with dual objectives to "remove the NPL distraction from the financial institutions and thereafter extract maximum recovery value from the NPLs." Danamodal, the SPV established to recapitalize financial institutions, was established in August 1998, and the Malaysian government also established a debt restructuring agency, the Corporate Debt Restructuring Committee (CDRC) (Danaharta 2005).[4] The CDRC provided a platform for financial institutions and viable borrowers with outstanding loans of RM50 million ($13.2 million)[5] or more to negotiate debt restructuring out of court. A Steering Committee, chaired by the BNM Governor, coordinated the work of the Danaharta, Danamodal, and the CDRC (BNM 1998a).

Danaharta was incorporated on June 20, 1998. The Malaysian Parliament passed the Danaharta Act on August 5, 1998, and additional legal authority was designated through amendments to the National Land Code Act and the Development Funds Act, which were enacted in mid-September 1998 (Danaharta 2005). The Minister of Finance was responsible

[3] The NEAC was a consultative agency to the Cabinet and was chaired by the Prime Minister, Mahathir Muhammed (Danaharta 2005, 10).
[4] For more information on the capital injections, see Malaysia: Danamodal Nasional Berhad by Devyn Jeffereis (2021).
[5] Based on an average exchange rate of USD $1 = RM 3.79.

for the oversight of Danaharta, and it had a nine-member Board of Directors and a three-member Oversight Committee (Fung et al. 2004; Danaharta 2005).

The Danaharta Act granted the AMC special legal authority; specifically, it granted Danaharta the authority to appoint a special administrator and bypass the court process for foreclosure (Danaharta 2005). Though the Danaharta Act gave Danaharta special powers, it did not specify criteria for eligible assets, pricing, or financing (Cerruti and Neyens 2016).

The government provided the initial capital for Danaharta in stages, totaling RM3 billion, though Danaharta borrowed from the Employee Provident Fund (EPF)[6] and Khazanah Nasional Berhad[7] to meet its interim operational funding needs. In order to purchase assets, Danaharta issued zero-coupon, government-guaranteed bonds with five-year maturities to the transferring financial institutions. In some cases, such as the purchase of unsecured NPLs or the purchase of assets from development financial institutions and Islamic banks, Danaharta paid cash. All financial institutions were eligible to transfer assets to Danaharta, provided that the NPLs had a value of at least RM5 million. Danaharta acquired assets in two major purchase windows: the "primary carve-out" focused on removing NPLs from the banking sector while the "secondary carve-out" required assets to meet a more selective set of criteria (Danaharta 2005). Though it initially intended to acquire NPLs on a first-come-first-serve basis, Danaharta announced a prioritized acquisition approach in October 1998, with priority given to weaker institutions or those recapitalized by Danamodal in addition to placing priority on secured loans (Danaharta 1998a). The purchase price was determined by loan type: secured loans, unsecured loans, and exceptionally large loans. The purchase price for secured loans backed by property collateral was determined by an independent appraiser's valuation while the price of loans collateralized by shares was determined using a proportional stake in the company and the share prices. The purchase price for unsecured loans was 10 percent of the outstanding principal, and the purchase price of exceptionally large loans was a nominal sum (though this method was used infrequently) (Danaharta 2005).

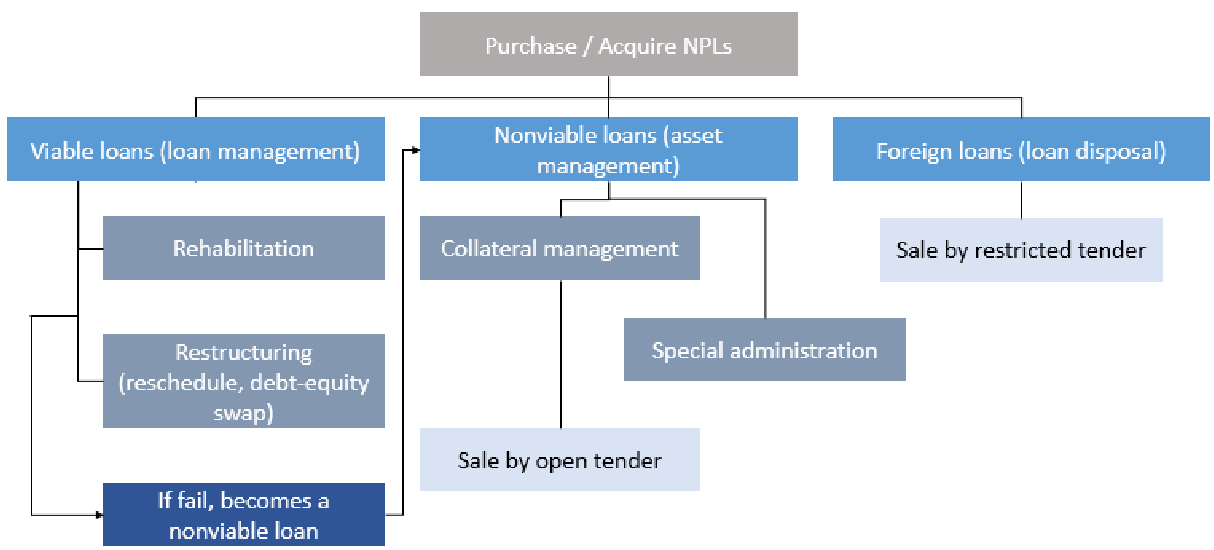
In order to encourage financial institutions to sell NPLs, Danaharta established an incentive and penalty structure. The first incentive (the so-called "carrot") was a profit-sharing arrangement under which the transferring institution received 80 percent of the profit recognized on the recovery of an NPL while Danaharta received the remaining 20 percent. Additionally, the transferring financial institution could amortize the loss on an NPL over a five-year period. The first penalty (the so-called "stick") included the requirement that NPLs not transferred to Danaharta be written down to 80 percent of Danaharta's valuation. Furthermore, the second "stick" was that Danaharta could only make one offer for each NPL. These incentives and penalties were put in place to encourage financial institutions to rid their balance sheets of NPLs, despite the possibility of losses and erosion of shareholder capital (Danaharta 2005). Furthermore, BNM required institutions with an NPL ratio greater than 10 percent to sell their NPLs to Danaharta, and financial institutions were required to

[6] The Employees Provident Fund (EPF) is the national pension fund of Malaysia.
[7] Khazanah Nasional Berhad was established in 1993 as the sovereign wealth fund of Malaysia, and it is responsible for managing the government's commercial assets and investing for long-term growth.

sell NPLs to Danaharta in order to be eligible for recapitalization by Danamodal (Danaharta 2005; BNM 1998a).

In addition to purchasing NPLs, Danaharta also managed NPLs acquired by the central bank and government in the forced merger of two struggling banks, Sime Bank and Bank Bumiputra Malaysia, with stronger banks. Sime Bank was merged with RHB Bank Berhad on June 30, 1999, and Bank Bumiputra Malaysia was merged with Bank of Commerce (M) Berhad on September 30, 1999. Both banks reported large losses due to nonperforming loans, and because of the size and impact of the two institutions' potential failure on the financial system, the BNM decided to intervene (BNM 1998a). The distressed assets of both banks were transferred to the government and central bank in order to facilitate the mergers. The government and central bank transferred the NPLs to Danaharta for management; in return, Danaharta collected a management fee and determined a recovery strategy. In reporting, Danaharta referred to the Sime Bank and Bank Bumiputra NPLs as "Managed NPLs" whereas purchased NPLs were referred to as "Acquired NPLs." Danaharta relaxed the minimum loan size requirement for "Managed NPLs" to RM1 million and above (Danaharta 2005).

Figure 3. Danaharta's Recovery Strategy by Loan Type



Source: Ito and Hashimoto 2007.

Danaharta's management specified that it would adopt an asset management company approach, as opposed to a rapid disposition agency or a bad debt warehouse approach. Danaharta's goal was to "elicit maximum recovery from its NPL portfolio." Danaharta determined the recovery strategy on a case-by-case basis, though there were two overarching strategies: one for viable borrowers and one for nonviable borrowers or those that failed to comply with prior restructuring efforts. Viable borrowers underwent restructuring and rehabilitation as part of the "soft approach." Nonviable borrowers or those that failed to comply with restructuring were subject to the so-called "hard approach," which involved foreclosure and special administration. For foreign loans, where Danaharta did not have special legal authority, the loans were disposed of through restricted tender exercises.

Outcomes

Danaharta completed asset acquisition during two windows: the primary and secondary carve-outs. The primary carve-out occurred between September 1998 and June 30, 1999. In the primary carve-out, Danaharta acquired loans with a face value of RM39.3 billion while financial institutions rejected RM1.78 billion in offers. The secondary carve-out occurred between July 1999 and March 31, 2000, and had a more selective set of criteria for eligible assets (Danaharta 2005; BNM 1998a).

At the end of its operations in September 2005, the book value of Danaharta's portfolio totaled RM47.68 billion in loan rights acquired (LRA), with RM19.71 billion in acquired assets and RM27.97 billion in managed assets. The adjusted loan rights acquired (adjusted LRA), which included the accrued interest at the time of restructuring, totaled RM52.42 billion (Danaharta 2005).

In exchange for NPLs, Danaharta issued 15 tranches of five-year, government-guaranteed zero-coupon bonds, which raised RM7.92 billion in capital and had a total face value of RM11.14 billion. Danaharta paid RM1.02 billion in cash for unsecured loans or assets from Islamic banks and development finance companies. Bonds were issued in exchange for the remaining acquired assets. On average, Danaharta purchased assets at a discount of 54.6 percent of book value.[8] Because Danaharta took over the management of NPLs from the merged Sime Bank (RHB Bank) and BBMB (Bank of Commerce [M] Berhad), these assets did not have an acquisition cost to Danaharta (Danaharta 2005).

Over the course of its lifespan, Danaharta recovered RM30.35 billion of its portfolio, with a total cash recovery of RM26.69 billion. The average recovery was 58 percent of book value; for the recovery on acquired NPLs, the average recovery rate was 49 percent while the average recovery rate for managed NPLs was 65 percent (Danaharta 2005).

Figure 4. Danaharta's Recovery on Acquired and Managed NPLs

Recovery Method	Adjusted LRA (a) (RM billion)		Recovery (b) (RM billion)		Recovery rate (%) c=(b)/(a)	
	Acquired NPLs	*Managed NPLs*	*Acquired NPLs*	*Managed NPLs*	*Acquired NPLs*	*Managed NPLs*
Plain loan restructuring	1.07	3.77	0.86	3.58	80%	95%
Settlement	3.55	8.55	3.11	6.41	88%	75%

[8] According to its final report, Danaharta paid RM8.94 billion at the time of acquisition for the RM19.71 billion in acquired NPLs.

Schemes of arrangement	3.14	6.82	1.84	4.32	59%	63%
Appointment of special administrators	1.66	2.59	0.84	0.58	51%	22%
Foreclosure	9.12	3.69	2.62	1.65	29%	45%
Others	3.81	3.29	1.74	2.60	46%	79%
Legal action	0.28	1.08	0.06	0.14	20%	13%
Total	22.63	29.79	11.07	19.28	49%	65%
Overall	**52.42**		**30.35**		**58%**	

Source: Danaharta 2005.

Of the RM26.29 billion in cash recovery, RM17.48 billion was recovered from NPLs managed for the Sime Group and BBMB Group. The cash recovery on these NPLs was repatriated to the government and BNM after deducting the management fee for Danaharta. Danaharta distributed RM760 million in cash and an unreported value of securities to 38 financial institutions, as there was a profit on the management of these NPLs (Danaharta 2005).

Danaharta had multiple methods to convert non-cash recovery assets to cash. Danaharta sold properties through open tenders after designing the tender process for Malaysia. Danaharta held ten major tenders and fifteen smaller tenders as of September 30, 2005. Over the course of its operations, 1,298 properties were listed for tender with a value of RM3.7 billion, and a total of 1,026 properties were sold for RM2.17 billion. Danaharta sold readily tradable securities through stockbrokers or financial institutions in order to convert the securities to cash. Danaharta also issued the first occurrence of a collateralized loan obligation (CLO) transaction in Malaysia through its asset-backed securitization (ABS). The ABS raised a total of RM308.57 million and had a subscription rate of 3.5 times for the senior notes (Danaharta 2005).

Danaharta repaid its liabilities by the time it ceased operations, including the RM3.0 billion in initial capital from the government and the RM11.14 billion in bonds. Due to a mismatch between bond maturity and cash flow for the last two bond redemptions in 2004 and 2005, Danaharta drew RM650 million from its revolving credit facility, which was capped at RM1.4 billion, in order to repay the liabilities. Danaharta repaid the RM650 million by September 2005 (Danaharta 2005).

Danaharta recognized a lifetime loss of RM1.14 billion when it ceased operations on December 31, 2005. The remaining recovery assets were transferred to Prokhas, a fully owned subsidiary of the Ministry of Finance Incorporated. Danaharta transferred assets including restructured loans, properties, securities, and assets under legal action to Prokhas, for collection or recovery (Danaharta 2005). In 2010, Prokhas had collected RM2.92 billion in cash and had an outstanding balance of RM650 million. Prokhas intended to collect the full RM3.57 billion by the end of 2011 to return to the government ("Corporate: Prokhas recoups" 2009). Since completing the collection of the residual recovery assets, Prokhas evolved into a consulting and advisory agency.

II. Key Design Decisions

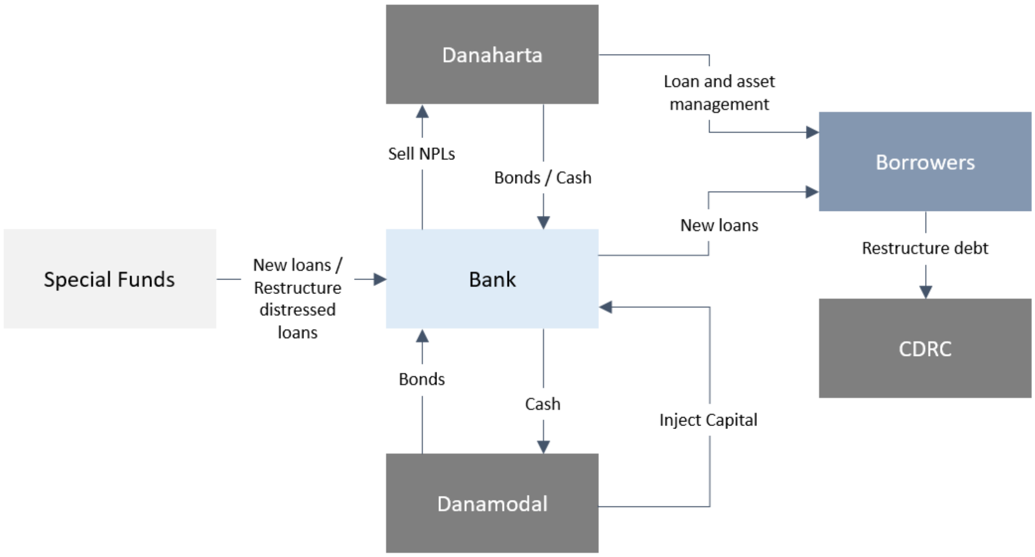
1. Part of a package: Danaharta was one part of the Malaysian government's response to the financial crisis, which also included a recapitalization SPV, Danamodal, and a debt restructuring agency, the CDRC.

In January 1998, the Malaysian government established the National Economic Advisory Council (NEAC), a consulting body to the Cabinet, to propose a plan to address the economic and financial instability in Malaysia. The NEAC proposed the National Economic Recovery Plan (NERP), which was published in August 1998, with six objectives for economic recovery and financial stabilization. The plan included the creation of a national asset management company (AMC) and a special purpose vehicle (SPV) to recapitalize financial institutions. Danaharta was established as the AMC, and Danamodal was established soon after as the recapitalization SPV (Danaharta 2005).

In order to be eligible for capital injections, financial institutions were required to transfer their portfolios of NPLs to Danaharta. Danamodal followed the first-loss principle, which meant that the financial institution's shareholders were required to absorb the first losses on the sale of assets to Danaharta. Danamodal only recapitalized viable financial institutions (BNM 1998a).

The government also established the Corporate Debt Restructuring Committee to facilitate debt restructuring negotiations. Danaharta, Danamodal, and the CDRC were overseen by a Steering Committee under the central bank, which coordinated the activities of the three agencies. Special funds were established to promote investment in priority sectors such as the Fund for Small and Medium Enterprises. The government announced a merger program for banks and finance companies in January 1998 to consolidate the banking industry, which was separate from the NEAC's proposal, though the NERP did encourage consolidation (BNM 1998a). Figure 5 below shows the relationship between the agencies, banks, and borrowers:

Figure 5. Relationship between Danaharta, Danamodal, and the CDRC



Source: BNM 1998a.

2. Legal Authority: The Malaysian parliament passed the Pengurusan Danaharta Nasional Berhad Act (Danaharta Act) in August 1998, and amendments to the National Land Code Act and the Development Funds Act were passed in September 1998.

The government announced the creation of Danaharta on May 20, 1998 (Danaharta 2005). Danaharta was established on June 20, 1998, and incorporated under the Companies Act of 1965 (Danaharta 1998a; 2005). Danaharta was granted its authority and special powers through the Pengurusan Danaharta Nasional Berhad Act (Danaharta Act), which was passed by the Malaysian Parliament in August 1998. In September 1998, amendments to the National Land Code Act and the Development Funds Act were passed by Parliament. The National Land Code (Amendment) Act of 1998 facilitated the implementation of Danaharta's special authority (Danaharta 2005).

The Danaharta Act was amended by parliament on July 31, 2000. The amendments were intended to clarify existing provisions and solve problems that arose after Danaharta began operations (Danaharta 2005). The amendments included provisions regarding statutory vesting, sale by private treaty, legal actions against Danaharta, the Oversight Committee, and special administrators (Danaharta 2002).

3. **Special Powers: Danaharta was granted special legal authority to more efficiently resolve its portfolio of NPLs outside the court system.**

Danaharta had special legal authority to manage and resolve NPLs. Danaharta could appoint a special administrator over borrowers unable to repay debts, bypassing court procedures. Furthermore, Danaharta could foreclose on a loan's underlying property collateral and avoid court procedures, which expedited its operations. The act also granted Danaharta the ability to acquire assets through statutory vesting, which allowed Danaharta to "step into the shoes of the selling financial institution" in order to expedite the transfer and management of NPLs (Danaharta 2005). Danaharta's legal authority enabled it to restructure loans in two to three months, rather than the standard fourteen to sixteen months under the Companies Act (Cooke and Foley). The Danaharta Act did not include provisions for pricing, financing, or eligible assets, which were to be determined by the Board and management (Cerruti and Neyens 2016).

Section 72 of the Danaharta Act prohibited courts from granting injunctions against Danaharta (Danaharta 2003). A borrower filed a legal suit against Danaharta in 2002, and the Court of Appeals declared that Section 72 was unconstitutional and void (Azmi and Razak 2014; Danaharta 2003). Danaharta filed an appeal against the ruling at the Federal Court, the highest court in Malaysia, arguing that the powers were constitutional and fair. The Federal Court unanimously decided that Section 72 of the Danaharta Act was constitutional and valid in January 2004 (Danaharta 2003). The Danaharta Act does not prevent parties from suing Danaharta or winning compensation as determined by the court (Danaharta 2002).

4. **Mandate: Danaharta had a mandate to both acquire NPLs and achieve maximum recovery value on its portfolio of assets.**

Danaharta's primary objectives "were to remove the NPL distraction from the financial institutions and thereafter extract maximum recovery value from the NPLs" (Danaharta 2005).

5. **Communication: Danaharta presented itself as a preemptive and key measure to mitigate economic and financial instability.**

When Danaharta was announced, the Managing Director, Azman Yahya, stated that he was confident that Danaharta would be beneficial for the Malaysian economy and allow financial institutions to return to "their vital role in supporting economic growth" (Danaharta 1998c). When the Danaharta Act was passed, it was framed as a "critical component in enabling Danaharta to undertake its unique mission" (Danaharta 1998d). The press releases related to Danaharta's operational set-up emphasized its quick establishment relative to other countries (Danaharta 1998e), and the 1998 BNM Annual Report asserted that "[t]he speed at which Danaharta was set up and the financial commitment extended by the Government clearly demonstrated the serious intention of the Government to restructure and strengthen the banking sector" (BNM 1998a).

Azman emphasized that Danaharta's ability to appoint special administrators could expedite resolutions and be a "win-win solution" for the involved parties (Danaharta 1999b). The government asserted that Danaharta would not become a bad-debt warehouse or a rapid-disposition agency; rather, Danaharta would focus on maximizing the recovery value of its portfolio of NPLs and minimizing the cost to the taxpayer (Danaharta 1999c). Though there were criticisms that Danaharta would be slow to resolve NPLs, Azman rejected the criticism and reiterated that Danaharta's "role is to maximize recovery on [its] assets" (Lopez 1999).

The final report on Danaharta framed the creation of the body as a "preemptive measure" to address growing economic distress, as the establishment of Danaharta, Danamodal, and the CDRC was "the Malaysian Government's pre-emptive strategy in accelerating the restructuring and strengthening of the financial system" (Danaharta 2005).

Furthermore, Danaharta claimed that it fought a public relations war as soon as it was established, as there were critics who believed Danaharta would bail out politically connected businesses. Others doubted that it would be transparent and free from political interference; furthermore, there was a common "misconception that Danaharta would forgive all NPLs" it acquired. Danaharta sought to combat public perception challenges through transparency in its operations, using frequent press releases and reports (Danaharta 2005). From the time of his appointment as the Managing Director, Azman committed to having "full disclosure and transparency" of Danaharta's operations (*Reuters* 1998).

6. Ownership Structure: Danaharta was fully government-owned.

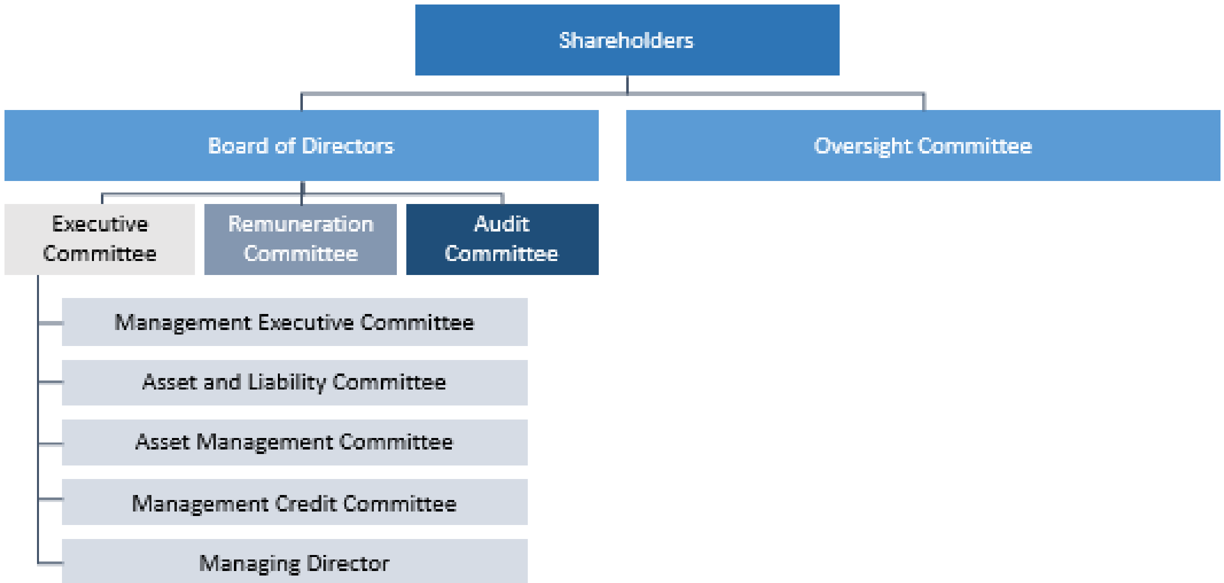
Danaharta was fully owned by the government, as the Minister of Finance Incorporated was the sole shareholder (Danaharta 1998b).[9]

7. Governance/Administration (1): Danaharta had a nine-member Board of Directors, a three-member Oversight Committee, and an executive committee and subcommittees responsible for daily oversight and guidance.

The Minister of Finance oversaw Danaharta and its operations, as it was the sole shareholder of Danaharta. Danaharta had a nine-member Board of Directors, which consisted of representatives from both the public and private sector, which included a Chairman, a Managing Director (i.e., the CEO), two federal government officials, three individuals from the private sector, and two international members (Act 587). Azman Yahya, the Managing Director from 1998 to 2001, also served as the head of the CDRC (Danaharta 2005). Because Danaharta, Danamodal, and the CDRC played complementary roles, a Steering Committee was established to ensure coordination across the agencies which was chaired by the BNM Governor (Danaharta 1998a).

[9] The Minister of Finance Incorporated (MOF Inc.) is a Government-Linked Investment Company (GLIC) in Malaysia which was established under the Minister of Finance (Incorporated) Act in 1957. It functions as an investment holding company for the government, and the Act allows the Minister of Finance to be represented by the MOF Inc. and enter into business contracts, acquire companies, and manage assets.

Figure 6. Danaharta's organizational structure



Source: Danaharta 2005.

The top-level management was divided into subcommittees which were overseen by the Management Executive Committee. The subcommittees evolved over the course of Danaharta's operations. The Management Executive Committee oversaw the operations of Danaharta, determined guidelines for the operations, made key decisions, and ensured adherence to policies. Other committees included the Management Credit Committee, which was involved in the acquisition and disposal of loans; the Asset Management Committee, which reviewed and decided on the purchase and sale of property assets; and the Asset and Liability Committee, which controlled liquidity, market, and interest risks (Danaharta 2005). In 2003, Danaharta's staff totaled 245 individuals (Danaharta 2003).

The Danaharta Act included a provision for the creation of the Oversight Committee (Act 587). This three-member committee was appointed by the Minister of Finance and tasked with the following functions: approval of special administrator appointments, approval of extension or moratorium periods for companies under special administrators, and approval of the termination of special administrators (Act 587). The Oversight Committee was established in November 1998 (Fung et al. 2003).

8. Governance/Administration (2): Danaharta established procedures for transparency, risk management, and corporate governance.

Danaharta established measures to ensure transparency of operations. Danaharta held press conferences, released public announcements, and maintained a public website. Danaharta published biannual operations reports, quarterly reports, and annual reports. Danaharta adopted the Malaysian Code on Corporate Governance which meant that it followed standards for professionalism and transparency. Danaharta also established the Danaharta

Authority Manual which defined the responsibilities and authorities of the Board and management committees. Furthermore, the Risk Management team reviewed all proposals, and Danaharta was established with a structure to ensure that there was no single individual who could make a unilateral decision regarding the resolution of NPLs (Danaharta 2005).

9. Governance/Administration (3): Danaharta adopted key performance indicators (KPIs) internally in order to achieve its organizational objectives.

Danaharta established KPIs internally in order to achieve its objectives during each phase of its operations; these phases were establishment, acquisition, and resolution. Danaharta linked staff remuneration to the achievement of the KPIs. Each KPI had a benchmark and a timeframe for achievement. The KPIs and the outcomes related to each KPI are in Figure 7 below:

Figure 7. Danaharta's Key Performance Indicators and Performance

Phase	KPI	Actual Performance
Establishment	Complete set-up within five months (including draft legislation, staff recruitment and formulation of policies and procedures)	Exceeded KPI: Danaharta began operations within three months of its announcement
Acquisition	***Timeframe***: • Complete primary carve-out by December 31, 1999 • Complete secondary carve-out by the March 31, 2000 ***Quantity***: • Acquire RM8 billion by December 31, 1998 • Acquire RM33 billion (total) by December 31, 1999	***Timeframe***: • Exceeded KPI: Completed six months ahead of schedule • Met KPI: Completed on schedule ***Quantity***: • Exceeded KPI: Acquired RM19.73 billion in loans by December 31, 1998 • Exceeded KPI: Acquired RM39.33 billion by December 31, 1999
Resolution	***Processing***: • Process (meet with borrowers to decide on an appropriate strategy) RM30 billion NPLS by June 2000 • Process remainder of portfolio by December 31, 2001 ***Loan Recovery Rate***: • Benchmark of 49.8 percent for the loan recovery rate	***Processing***: • Exceeded KPI: Processed RM31.5 billion by June 2000 • Did not meet: Completed processing the remainder by July 2002 ***Loan Recovery Rate***: • Exceeded KPI: Loan recovery rate of 58 percent as of September 30, 2005

Source: Danaharta 2005.

10. Size: Though legislation did not specify a size limit, Danaharta's portfolio ultimately totaled RM47.68 billion in loan rights acquired.

When Danaharta was established, the Danaharta Act did not specify a size restriction that limited the amount of NPLs Danaharta could acquire. By the end of its operations in 2005, Danaharta had a total portfolio of RM47.68 billion—acquired assets totaled RM19.71 billion while it managed the remaining RM27.97 billion of its portfolio on behalf of the government (Danaharta 2005).

11. Funding Source (1): The Malaysian government provided RM3 billion in initial capital to Danaharta as well as supplemental lending from other government funds; Danaharta also had access to a revolving credit facility from a consortium of private banks.

The government provided Danaharta with its initial capital of RM3 billion in. Danaharta borrowed from the Employees Provident Fund (EPF) and Khazanah Nasional Berhad to supplement its funding needs while waiting for the full capitalization. Danaharta borrowed a total of RM1.3 billion from the EPF and Khazanah Nasional Berhad over the course of its lifetime. Danaharta was also authorized to issue up to RM15 billion in zero-coupon, government guaranteed bonds in exchange for asset purchases (Danaharta 2005).

Danaharta also had access to a revolving credit facility from a consortium of banks which was established to provide short-term financing in the event of a cash shortage at the time of bond redemption (Danaharta 2004). Danaharta had access to RM1.4 billion in the revolving credit facility. Danaharta borrowed RM650 million from the revolving credit facility for the December 2004 and March 2005 bond redemptions, due to a mismatch between the cash flow and bond redemption. The RM650 million loan was repaid by September 2005 (Danaharta 2005).

Danaharta recognized a lifetime loss of approximately RM1 billion—which was borne by the government—when it ceased operations (Danaharta 2005).

12. Funding Source (2): Danaharta issued five-year, zero-coupon, government-guaranteed bonds as consideration for acquired NPLs from transferring financial institutions.

Danaharta elected to issue domestic bonds to finance the purchase of NPLs. Danaharta considered an international bond issuance, but due to exchange rate uncertainty and volatility, it determined that an international source of funding would be costly. Thus, Danaharta issued domestic bonds directly to financial institutions as consideration for the transfer of NPLs. The bonds were government-guaranteed, zero-coupon bonds with a five-year maturity. Danaharta issued 15 tranches of bonds between November 1998 and March 2000, approximately one tranche per month. Danaharta raised a total of RM8.22 billion in capital from bond issuances; the total face value of the bonds was RM11.14 billion (Danaharta 2005). Figure 8 below shows the details of the fifteen bond issuances:

Figure 8. Danaharta Bonds Issued for Acquired NPLs

Date of Issue	Face Value (RM billion)	Price for every RM100 in FV	Yield	PV at issue date (RM billion)	Maturity Date
20 Nov 1998	1.022	69.832	7.150%	0.713	31 Dec 2003

30 Dec 1998	1.580	72.012	6.672%	1.138	31 Dec 2003
29 Jan 1999	1.105	71.301	6.654%	0.788	31 Mar 2004
26 Feb 1999	1.242	72.296	6.475%	0.898	31 Mar 2004
26 Mar 1999	1.393	72.758	6.445%	1.014	31 Mar 2004
29 Apr 1999	1.050	75.584	5.487%	0.793	30 Jun 2004
27 May 1999	0.511	76.229	5.400%	0.390	30 Jun 2004
29 Jun 1999	0.744	76.862	5.330%	0.572	30 Jun 2004
29 Jul 1999	0.527	76.223	5.319%	0.402	30 Sep 2004
26 Aug 1999	0.204	73.585	6.111%	0.150	30 Sep 2004
29 Oct 1999	0.575	76.365	5.283%	0.439	31 Dec 2004
29 Dec 1999	0.392	77.3673	5.194%	0.303	31 Dec 2004
31 Jan 2000	0.162	77.244	5.063%	0.125	31 Mar 2005
29 Feb 2000	0.305	77.697	5.025%	0.237	31 Mar 2005
31 Mar 2000	0.328	77.494	5.165%	0.255	31 Mar 2005
Total Bonds Issued	**11.140**			**8.217**	

Source: Danaharta 2005, 54.

The bonds carried a zero-risk weight for banks for capital-adequacy purposes, and the bonds could be rediscounted with BNM under the central bank's role as lender of last resort (Danaharta 1998a). The bonds could be traded on the secondary market. The bonds also had a rollover option, which allowed Danaharta to refinance the bonds upon maturity for one, three, or five years (Danaharta 2005).

13. Eligible Institutions: All financial institutions were eligible to transfer assets to Danaharta; participation was mandatory for financial institutions that received government capital and for institutions with high NPL ratios.

All financial institutions were eligible to transfer assets to Danaharta. This included commercial banks, finance companies, development banks, merchant banks, Islamic banks, and locally incorporated foreign banks (Danaharta 2005). In order to be eligible for recapitalization by Danamodal, financial institutions were required to sell NPLs to Danaharta (BNM 1998a). BNM required financial institutions with an NPL ratio of 10 percent or higher to sell NPLs to Danaharta (Danaharta 2005).

Figure 9. Danaharta Usage by Institution Type

Institution Type	# of Accounts	Loan Rights Acquired (LRA) (in RM mil.)	Purchase Price (in RM mil.)
Commercial Banks	451	11,402.2	4,427.7
Finance Companies	131	3,769.5	1,804.1
Merchant Banks	172	3,211.9	1,811.7
Development Financial Institutions	42	1,161.2	749.1

Offshore	1	123.1	104.7
Others	1	42.7	42.7
Total	**798**	**19,710.6**	**8,940**

Source: Danaharta 2005, 56-61.

14. Eligible Assets: NPLs with a value of RM5 million or greater were eligible for acquisition.

Danaharta could acquire NPLs with a value of RM5 million or greater. The size criteria narrowed Danaharta's operations and allowed it to focus on the higher value loans while addressing approximately 70 percent of the total NPL value in the banking sector. Danaharta estimated that the RM5 million target translated to 2,000 to 3,000 accounts, which it deemed "a manageable number for Danaharta to resolve the NPLs on a case by case basis" (Danaharta 2005).

15. Acquisition – Mechanics (1): Danaharta established two purchase windows, with an open and general purpose for the primary carve-out and a more selective secondary carve-out.

Danaharta acquired assets during two purchase windows. The first purchase window, the "primary carve-out," occurred between September 1998 and June 30, 1999. The objective of the first round of acquisitions was to "relieve the pressure on the banking system caused by NPLs"; thus, all financial institutions were eligible to sell NPLs to Danaharta during this window (Danaharta 2005). Danaharta announced that the acquisition would prioritize weaker financial institutions, such as those receiving capital injections from Danamodal, as well as those that were likely to sell NPLs to Danaharta (BNM 1998a). Financial institutions were able to decline Danaharta's offers, and RM1.78 billion in offers were declined during the first window (Danaharta 2005).

The second purchase window, the "secondary carve-out," occurred between July 1, 1999, and March 31, 2000. Danaharta established a more selective set of criteria for assets to be eligible for transfer, which included NPLs from borrowers already in Danaharta's portfolio, NPLs from borrowers with a total value greater than RM50 million, unsecured NPLs to public companies, or NPLs from financial institutions with an NPL ratio higher than 10 percent (Danaharta 2005).

There were minor changes to Danaharta's portfolio following the two purchase windows, as more managed NPLs were transferred to Danaharta. Danaharta returned a small quantity of acquired NPLs to the selling financial institution (Danaharta 2005). For example, in 2001, Danaharta returned 23 accounts totaling RM570.5 million to the transferring financial institution due to their failure to meet requirements in the acquisition agreements (Danaharta 2003).

16. Acquisition – Mechanics (2): Danaharta was responsible for the management of NPLs from closed financial institutions on behalf of the central bank and government.

Danaharta managed NPLs on behalf of the central bank and government for two defunct banking groups. Sime Bank reported massive losses in 1998 due to increased loan defaults, and BNM took over the bank in 1998. In order to facilitate a merger of Sime Bank with RHB Bank Group, another commercial bank, BNM carved out Sime Bank's NPLs and moved them to Danaharta for management. Danaharta Managers Sdn Bhd (Danaharta Managers) was established and incorporated to manage the NPL portfolio from Sime Bank. Similarly, Bank Bumiputra Malaysia Berhad Group (BBMB Group), a government-owned banking group, reported large losses due to NPLs in 1998. BBMB Group was merged with Bank of Commerce (M) Berhad after its NPLs were transferred to Danaharta for management. In 1999, Danaharta Urus Sdn Bhd (Danaharta Urus) was created to hold the NPLs. Danaharta Managers and Danaharta Urus were fully owned subsidiaries of Danaharta (Danaharta 2005).

Unlike acquired NPLs, NPLs from BBMB Group and Sime Bank did not require payment from Danaharta to take over the management of the NPLs. However, Danaharta had to have legal ownership in order to use its legal authority to manage and resolve the NPLs. Thus, Danaharta Managers and Danaharta Urus issued zero-coupon bonds to Bank Negara Malaysia and the Ministry of Finance as consideration for the loans and redeemed them with the recovery from the respective loans. These bonds were different from the bonds issued by Danaharta to acquire NPLs from other financial institutions. The loan size restriction of RM5 million was relaxed for BBMB Group and Sime Bank. Danaharta managed loans with minimum value of RM1 million from the bank groups (Danaharta 2005).

In exchange for managing the NPLs from Sime Bank and BBMB for BNM, Danaharta received a management fee. If the recovery value was less than or equal to the net book value, Danaharta received 2 percent of the net recovery value. If the recovery value was more than book value, Danaharta received 20 percent of the excess recovery in addition to the 2 percent of net book value. After deducting management fees, the recovery on the management of these loans accrued to the government and BNM (Danaharta 2005).

17. Acquisition – Pricing: If an NPL was secured, Danaharta calculated its purchase price using a measure of market value; the purchase price of unsecured loans was 10 percent of the outstanding principal value.

BNM required every financial institution to submit details of its portfolio of NPLs with values of RM5 million and greater to Danaharta. Danaharta relied on the representations from the selling banks regarding the details of sold NPLs and included warranty provisions in the sales agreements. This allowed Danaharta to return NPLs to the selling financial institutions at a later date if the loan documentation was not in place (Danaharta 2005).

Danaharta determined the purchase price for NPLs depending on whether the loan was secured or unsecured. For secured loans, the purchase price was determined using the fair value of the underlying collateral. Danaharta only accepted property or shares as collateral. For property collateral, the fair value was 95 percent of the market value of the property, as determined by an independent appraiser. For NPLs backed by shares, the fair value was dependent on the size of the stake that the borrower held in the company, with premiums for larger stakes. The fair value was determined using the market price (MP), which was the lower of the three-month average price or the closing price at the point of purchase, and the net tangible assets (NTA) of the company based on its latest audited financial statements (Danaharta 2005). Figure 10 below shows the calculation of the fair value based on the percent stake in the company:

Figure 10. Calculation of fair value of shares based on the stake in the company

Stake in Company	Fair Value
Less than 5%	Lower of MP and NTA*
Between 5% and 33%	Average of MP and NTA
Above 33%	Higher of MP and NTA

Note: MP is market price and NTA is net tangible assets.

Source: Danaharta 2005.

Danaharta then used the calculated fair value for secured loans backed by property or shares to determine the purchase price (Danaharta 2005). Figure 11 below shows the purchase price for various scenarios:

Figure 11. Determination of purchase price for secured loans

Scenario	Purchase Price
FV is greater than or equal to the loan amount outstanding, defined as principal plus accrued but unpaid interest	Loan amount outstanding (principal plus accrued-but-unpaid interest)
FV is less than the loan amount outstanding but greater than or equal to the principal amount outstanding	Fair Value
FV is less than the principal amount outstanding	Danaharta paid up to fair value, but BNM allowed financial institutions to record the sale at the principal amount and record losses over five years

Source: Danaharta 2005.

For loans with collateral whose fair value covered the principal, Danaharta fully compensated the financial institution for the principal amount as well as any accrued but unpaid interest, up to the calculated fair value of the collateral.

For loans with insufficient collateral, Danaharta used a novel method to allow selling financial institutions to avoid writing down losses at the time they sold NPLs to Danaharta. Upfront, Danaharta paid the fair value as calculated. However, BNM allowed the selling financial institution to record the sale at the principal amount outstanding. As noted, BNM then allowed financial institutions to write down the difference over five years, rather than immediately. Not everyone took advantage of this carrot, however. “As it turned out, many financial institutions preferred the more prudent route of immediately writing off the entire shortfall in value of NPLs sold to Danaharta” (Danaharta 2005).

For unsecured loans, Danaharta paid 10 percent of the principal amount of the loan, an amount that Danaharta called an “arbitrary figure.” Danaharta noted that this nominal valuation “worked because unsecured loans were typically given to public listed companies and usually some value could be derived from the company’s listing status” (Danaharta 2005).

For exceptionally large loans with a value of more than RM200 million, the purchase price was set at a nominal value equal to a percentage of the loan outstanding or RM1. This method was used if the valuation was “onerous or inconclusive,” and it was used infrequently as few NPLs were acquired using this method. (Danaharta 2005).

18. Acquisition – Pricing (2): Danaharta developed an incentive and penalty structure to encourage financial institutions to sell NPLs.

Though Danaharta had to generally acquire loans on a willing-buyer, willing-seller basis, it established an incentive and penalty structure, which included two incentives, or “carrots,” and two penalties, or “sticks,” to encourage financial institutions to sell NPLs (Danaharta 2005).

The incentives to sell to Danaharta included a profit-sharing arrangement and loss amortization. The profit-sharing arrangement allocated the surplus recovery from the management or disposal of NPLs in cases where Danaharta had paid the selling institution less than the principal amount outstanding. Eighty percent of the surplus recovery went to the selling institution, while Danaharta kept 20 percent. The surplus recovery was calculated by account. It was equal to the total recovery, less the amount of Danaharta’s upfront payment for the NPLs. Danaharta also deducted its direct costs relating to the recovery and any holding costs related to the assets. Because Danaharta paid up to the fair value in cases where the fair value was less than the principal outstanding, the surplus for the selling institution was capped at the difference between the principal outstanding and fair value (Danaharta 2005).

There were exceptions to the profit-sharing arrangement, such as in the case of exceptionally large loans. When Danaharta paid a nominal sum for the loan, 95 percent of the surplus recovery went to the selling institution while Danaharta kept 5 percent. If Danaharta paid a percentage of the principal outstanding for the loan, the transferring institution received 90 percent of the surplus and Danaharta received 10 percent (Danaharta 2005).

As a second incentive, participating financial institutions were allowed to amortize losses from the sale of NPLs to Danaharta over a five-year period. Financial institutions were required to write off 20 percent of the shortfall in the first year, and a minimum of 20 percent in each of the following years until the loan loss was written off . When Danaharta completed the resolution of the loan, the transferring institution was required to write off any remaining loss (Danaharta 2005).

Danaharta also imposed two penalties, or "sticks." First, Danaharta provided financial institutions with only one opportunity to sell each NPL; any NPL the institution elected not to sell could not be sold to Danaharta at a later date. Danaharta also gave the financial institutions a limited timeframe to consider offers to drive efficiency and prevent price negotiation. If a financial institution decided not to sell an NPL to Danaharta, it was required to immediately write down the loan to 80 percent of Danaharta's valuation (Danaharta 2005).

19. Management and Disposal (1): Danaharta adopted a "soft" approach for borrowers with viable businesses and a "hard" approach for borrowers with nonviable businesses or who failed to comply with loan restructuring.

Danaharta evaluated the viability of a borrower's business, and if the business was considered viable, the NPLs were addressed using the "soft approach" method. Danaharta's soft approach—or loan management—included loan restructuring, loan settlement, and schemes of arrangement.[10] The goal of loan restructuring, which included the extension of repayment periods or rescheduling of loan payments, was to return the loan to a performing status. Every viable borrower was given one opportunity to restructure the loan in compliance with Danaharta's Loan Restructuring Principles and Guidelines. These guidelines included measures to maximize recovery, minimize taxpayer burden, ensure equal treatment of stakeholders, and utilize Danaharta's special powers. Danaharta also provided additional guidelines for corporate borrowers, individual borrowers, and guarantors. Loan settlement was another option for viable borrowers; these borrowers opted for an expedited settlement of the loans, usually within a year. Schemes of arrangement required agreement between creditors and borrowers and required court approval (Danaharta 2005).

For borrowers with non-viable businesses or for borrowers that failed to comply with loan restructuring, Danaharta's resolution strategy, the "hard approach," included the appointment of special administrators, foreclosure, legal action, or other resolution methods (Danaharta 2005).

Danaharta had the authority to appoint a special administrator over a corporate borrower, a subsidiary, a security provider, or a company whose shares Danaharta acquired, in the

[10] As Malaysia does not have an equivalent of Chapter 11 bankruptcy, a court administered scheme of arrangement is an option for debt restructuring. Pursuant to the Companies Act, the scheme of arrangement requires the approval of the High Court. (See Options for Debt Restructuring in Malaysia for a brief explanation.)

event that the borrower could not repay its loan (Danaharta 2005). The appointment of a Special Administrator effectively suspended the management and powers of the company's Board, as the special administrator was the only party allowed to manage the company's assets (Danaharta 2004). The Oversight Committee first approved the appointment of a special administrator. The special administrator assumed temporary control of the company under administration, and the company was automatically placed under a year-long moratorium which prevented creditors from taking action against the company. The special administrator prepared a workout proposal, which was reviewed for reasonableness by an independent advisor appointed by the Oversight Committee, and then approved by Danaharta. During the course of its operations, Danaharta appointed special administrators over 73 companies (Danaharta 2005).

Danaharta could foreclose on collateral if the borrower failed to repay its loan (Danaharta 2005). Danaharta was required to issue a 30-day notice to a borrower of its intent to foreclose and dispose of the property collateral if the borrower failed to repay the loan within the timeframe (Azmi and Razak 2014). Danaharta's special powers for foreclosure allowed it to bypass court procedures. Because of statutory vesting, the borrower maintained the ownership of the collateral properties, though Danaharta ultimately sold the property (Danaharta 2005).

However, Danaharta owned the properties that were transferred to it as a form of loan repayment. Danaharta adopted the open-tender approach to sell properties. Properties put up for tender were required to have their current value listed publicly, in addition to a confidential reserve price to prevent fire sales. Danaharta recruited real estate agents to assist with marketing properties nationally. Prospective buyers could reference the latest valuation report of the property, the sale and purchase agreement, and terms and conditions of the sale before placing a bid. Buyers received a stamp-duty waiver for all properties bought from Danaharta. Danaharta also provided financing at competitive rates for the first seven tenders and promised vacant possession of the property. The properties were promised to buyers free of encumbrances within nine months of the signing of the sale and purchase agreement or the buyer could terminate the sale. At the close of each tender exercise, the bids were collected by a Tender Committee, which was composed of senior management at Danaharta not involved in the tender process. The winning bids were presented to the Tender Board, which was comprised of the Managing Director of Danaharta, another Danaharta representative, an appraiser, and a representative from the government's Foreign Investment Committee. Only the agent whose client successfully won the bidding received a commission on the sale. Overall, Danaharta paid approximately 5 percent of the sale proceeds for agency fees and marketing costs (Danaharta 2005).

Legal action against a borrower was the "last resort" option for Danaharta, after it had attempted the other strategies. This was not a preferred resolution method due to the extensive time and monetary commitment and the minimal recovery value. Other methods included partial resolution, company liquidation, or the appointment of receivers or managers over a company or assets (Danaharta 2005).

20. Management and Disposal (2): Danaharta disposed of foreign loans and marketable securities through restricted-tender exercises.

Danaharta did not exclude foreign loans in its acquisition of eligible assets. Foreign loans included those that were non-Ringgit loans or marketable securities extended to or issued by foreign companies. The majority of these loans came from Sime Bank, Sime Labuan, and BBMB. For foreign loans and marketable securities, Danaharta determined that the best method to recover underlying value was to dispose of the NPLs for cash or swap for domestic debt, as Danaharta's special legal authority did not apply to foreign loans (Danaharta 2005).

Danaharta elected to use the restricted-tender exercise to dispose of foreign loans. International banks that expressed interest in purchasing the foreign loans were invited to participate; participants were divided into Principal Bidders, who could bid on loans and securities, and Marketable Account Bidders, who could bid only on marketable securities. Danaharta held four restricted-tender exercises, with a total offering of 110 accounts with principal of $743.32 million (RM195 million). In total, Danaharta sold 85 accounts for $631.84 million, at an average recovery of 48 percent (Danaharta 2005).

21. Management and Disposal (3): In order to recover non-cash assets, Danaharta managed its portfolio of securities and issued the first collateralized loan obligation in Malaysia.

Danaharta owned and managed a portfolio of securities that included irredeemable, redeemable, and convertible securities. Danaharta acquired these securities in cases where loan settlements were made using securities. Irredeemable securities included ordinary shares and irredeemable convertible loan stocks. Redeemable securities included secured loan stocks, unsecured loan stocks, and preference shares. Convertible shares were loan stocks and preference shares that were convertible to equity shares. Danaharta disposed of shares if the share price exceeded a predetermined target price. However, if the target price was not met, Danaharta used tender exercises for controlling blocks of irredeemable securities, market mechanisms for non-controlling blocks of irredeemable securities, and redemption of redeemable securities to dispose of the securities in its portfolio. Danaharta sold readily tradable securities through stockbrokers or financial institutions. For securities subject to call and put options, the decision to dispose was governed by its specific call and put option agreement (Danaharta 2005).

Danaharta adopted asset-backed securitization (ABS) as a method to expedite the recovery on restructured loans. Danaharta transferred a portfolio of loans and cash, valued at RM595 million, to an SPV, Securita ABS One Berhad, in exchange for cash and subordinated notes from the SPV. The portfolio included RM579.2 million in loans, a discount of RM1.5 million, and RM14.7 in reserve funding. On December 20, 2001, Danaharta issued RM310 million AAA-rated senior notes with a maturity of December 2005 and coupon rate of 3.75 percent. The senior notes were issued at 99.54 percent of par value, and the response to the issuance was positive with orders totaling over RM1 billion. Danaharta assumed the RM285.4 million unrated tranche of subordinated notes, which meant it would absorb any shortfall up to RM285.4 million. Danaharta raised RM308.57 million from the issue. Securita ABS One began redeeming the senior notes in stages from May 2003 to June 2004 and completed redemption eighteen months ahead of schedule, including RM18.4 million in interest costs. Danaharta only did one ABS exercise because the alternate recovery options "were generating cash well enough to retire Danaharta's bond on time." Danaharta's ABS issuance was the first occasion of a collateralized loan obligation (CLO) transaction in Malaysia (Danaharta 2005).

22. Timeframe: Danaharta did not have a predefined sunset date at the time of its establishment but ultimately ceased operations on December 31, 2005.

At the time of its establishment, Danaharta did not have a predefined sunset date. In the 1998 BNM Annual Report, it was estimated that Danaharta's lifespan would be between seven and ten years (BNM 1998a). However, by 2001, Danaharta set a target to wind down by the end of 2005 (Danaharta 2001). Danaharta ceased operations on December 31, 2005, and transferred remaining cash to the Ministry of Finance (Danaharta 2005).

Danaharta projected that a total of RM2.88 billion in residual recovery assets would remain by December 2005. The residual recovery assets were transferred to the Minister of Finance Incorporated, for conversion to cash beginning January 1, 2006. The Minister of Finance Incorporated designated Prokhas Sdn Bhd (Prokhas), a fully owned subsidiary, as the collection agency for the remaining residual recovery assets. Thus, the ownership of the assets remained with Danaharta, which became a dormant company, until the completion of recovery (Danaharta 2005).

III. Evaluation

In evaluations of AMCs, some consider Danaharta to be a "success story." Scholars recognize that Danaharta prevented further increases in NPLs, repaid its bonds on time, completed its operations in seven years, and incurred a small loss for the government (Cerruti and Neyens 2016). The IMF considered the plan for Danaharta to be "well-conceived," as it had a manageable portfolio of loans to resolve and an appropriate focus on resolution instead of warehousing or rapid disposition (Liu et al. 2001). Scholars from the Bank for International Settlements (BIS) considered Danaharta to be a "fairly effective policy instrument in removing and resolving NPLs in asset recovery" as it had legal authority, a coordinated strategy, financial support, and political backing that enabled it to operate efficiently (Fung et al. 2003).

During Danaharta's operations, the IMF warned that Danaharta's purchase price could operate as a tool to bail out existing shareholders if the price was set at a value higher than the fair value (Liu et al. 2001). The IMF noted that Danaharta was using an appropriate, market-based mechanism for valuation, as selling banks rejected Danaharta's offers on RM4.2 billion in book value because the offers were considered too low (IMF 1999).

Cerruti attributes Danaharta's success to a combination of factors which were the design, economic environment, and operations. The design had a "clear mandate and enabling legal environment" which helped Danaharta to operate effectively with strong guidance (Cerruti and Neyens 2016). The economic environment was also improving, as the economy rebounded and the capital controls and interest rates contributed to a positive environment for borrowers (Cerruti and Neyens 2016; Doraisami 2014). Furthermore, Danaharta had "strong corporate governance and transparency," as it adopted KPIs, followed the Malaysian Code of Corporate Governance, published frequent reports, and had stable management and governance (Cerruti and Neyens 2016). The IMF recognized similar attributes, such as the broad legal mandate which enabled Danaharta to operate efficiently. Furthermore, Danaharta's incorporation under the Companies Act required it to undergo regular auditing to ensure transparency and accuracy (Liu et al. 2001).

Danaharta provided ample self-evaluation in its final report. Danaharta asserted that it met all of the BIS's criteria for an effective AMC which include strong political will, supportive legal infrastructure, efficient market environment, clear AMC mandate, well-defined AMC lifespan, adequate governance, good transparency, realistic asset pricing, and speedy resolutions. Danaharta was visited by international agencies, such as the World Bank and IMF, as well as other national AMCs during the course of its operations. Danaharta credits its operations with preventing a banking crisis and lowering the cost of NPL resolution, as the NPL ratio began to decrease after Danaharta began its acquisition (Danaharta 2005).

However, Danaharta's recovery figures were improved by including the managed loans from BBMB and Sime Bank, as Danaharta did not have to purchase these assets. The managed loans yielded a higher recovery rate than the acquired assets. Without the income from the managed loans, Danaharta would have incurred a greater loss (Cerruti and Neyens 2016).

Furthermore, Inoguchi (2016) evaluated the effects of AMCs on the NPL ratio in Thailand and Malaysia and found that the effect of selling loans to Danaharta is unclear. This is due to the NPL ratio increasing after the period in which the asset management company completed its asset purchases. Inoguchi concludes that "[i]t is possible that the increase in loans sold to Danaharta affected the NPL ratio because some coefficients were significant and the NPL ratio rose after the period in which the asset management company ceased purchasing loans." He concludes that it is likely that Danaharta's role in solving the NPL problem was smaller than the impact of Thailand's AMC.

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An occasional paper from the IMF describing the financial crisis in Malaysia and economic policies and developments. https://ypfs.som.yale.edu/library/malaysia-crisis-recovery.

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A book on the breakdown of authoritarian regimes comparing the financial crisis experiences in Malaysia and Indonesia.
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