Student Loan-Backed Securitization for Higher Education Loans in Malaysia

1Bakri, M.H., 2Ismail, S., 3Ali, R., and 4Azman M.N.
1Faculty of Technology Management and Technopreneurship, Universiti Teknikal Malaysia, Melaka 76100, Malaysia
2Faculty of Business and Management, Universiti Teknologi MARA, Bandaraya Melaka 75300, Malaysia
3Arshad Ayub Graduate Business School, Universiti Teknologi MARA, Shah Alam 40450, Malaysia
4Kulliyyah of Economy, Universiti Islam Antarabangsa, Kuala Lumpur 50728, Malaysia

Abstract

Expanding access to higher education has been a vital task to most countries. Access to higher education has been essential not only for national development, but also for individual advancement. However, governments in many countries have been under financial constraints to adequately support their higher education institutions (HEIs). Many researchers have tried to address this issue, usually by analyzing the repayment collections to reduce the default rate. The introduction of asset-backed securitization (ABS) in Malaysia has benefited the economy. This study particularly focuses on the student loan problem, which has not yet been implemented as a securitization process in Malaysia. The main purpose of this research is to investigate the use of Student Loan-Backed Securitization that meets shariah-compliance and can be implemented in Malaysia. This framework is proposed to create its structure and issue a highly graded and marketable sukuk that complies to global shariah principles, and hence, help the Malaysian government to produce high income nation with high labour skill and qualification.

INTRODUCTION

As of May 2012, National Higher Education Fund Corporation (NHEFC) has approved loans for some 1.98 million students amounting to RM 44.18 billion, with the actual dispersed stood at RM 30.44 billion (NHEFC). While the total sum owed to NHEFC is RM 6.83 billion from 1.09 million borrowers, the corporation has so far only managed to collect RM 3.31 billion. Further statistics by the Corporation indicated that although many NHEFC borrowers are showing their interest to pay, the actual sum collected still remains low.

In a particular country, government and private parties have their own system to finance their higher education students (Chapman, B. and A. Harding, 1993; Barr, N., 2003) and each country adopts different way to handle it. Many governments set up an institution or a corporation to manage student loans (Chapman, B., 2006) to offer to university students who qualify for the loans. According to (Khan, A., 2008) main reasons for non-repayment of student loans are their unemployment and desire to continue for higher degree.

Various loans schemes have been in operation in around 75 countries, with the largest loans schemes found in advanced economies such as the United States and Australia (Shen, H., and A. Ziderman, 2009). Two basic forms of student loans exist, with variations of each or hybrid versions of the two (Johnstone, D.B., 2004a and the type of repayment schedule being the major difference among them (Salmi, J., and A. Hauptman, 2006). The conventional mortgage-type loan is characterized by fixed interest rate and repayment period, with the burden of repayment being the varying element; while the progressive loan type — income-contingent loans (ICL) — requires an obligation to commit a fixed proportion of the borrower’s future earnings until the loan is repaid. ICL was introduced in Australia in 1989 and the U.K. in 1997, and more recently in transition and developing economies (Albrecht, D., and A. Ziderman, 1991; Johnstone, D.B., 2007).

The value of the equity—from which new loans can be made—depends on the value of the notes as assets, which in turn depends on the repayment flows (a function of the interest rates on the notes) and on the aggregate likelihood of default (a function of collection capabilities and the presence or absence of guarantors or co-signers). In this method, the private capital market estimates the likely losses on the
student loan notes to calculate the value of the equity; this estimation is similar to that used to calculate the appropriate discount for a direct purchase of the notes. The advantage of securitization is that the risk is essentially managed by the large numbers of revenue-producing notes and by the ability of the market to impose discipline in collection and servicing (Kendall, Leon T., and Michael J. Fishman, eds. 1996).

Description of the proposal framework Islamic Student Loan Backed Securities (i-SLBS) in Malaysia:

The new i-SLBS system contemplates the participation of six key agents throughout the process: students, higher education institutions (HEI), government, capital market, financial system and the Managing Commission for the whole system, see Figure 1.

![Proposed Conceptual Framework of i-SLBS](image)

**Fig. 1: Proposed Conceptual Framework of i-SLBS**

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<th>Table 1: Explanation of agents functions.</th>
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<td><strong>Agents</strong></td>
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<tr>
<td>Students</td>
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<tr>
<td>Federal Government / Ministry of Higher Education (MOHE)</td>
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<tr>
<td>AKPK – Counselling Credit</td>
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<td>BNM – Central Bank</td>
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<td>KWSP – Employees Provident Fund</td>
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<td>Angkasa – National Cooperative Society in Malaysia</td>
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<td>SSM – Registrar of Malaysian Companies</td>
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<td>JPJ – National Road Transport Department</td>
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<td>LHDN – Inland Revenue Board</td>
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<td>JPN – National Registration Office</td>
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of cash resources available to repurchase loans from the NHEFC. The Government will assume the cost of the unemployment contingency and therefore contributes to financing the NHEFC for the first 3 years.

**Originator**

The NHEFC centralizes all applications in a single system and orders them from poorest to richest. NHEFC will setup Special Purpose Vehicle that determines the maximum number of students that can receive the benefit based on the resources assigned in the fiscal budget law. It organizes the bank tender process. It acquires the loans that the NHEFC are not willing to maintain in their portfolio (those loans continue to be administ ered by the MOHE loan guarantees).

**Trustee**

The trustee's primary duty is to protect the interests of the investors who purchase the securities issued pursuant to the securitization and administer the duties of the SPV under the requisite agreements. The natures of the trustee's duties are specifically set forth in the trust agreement, and frequently require more intensive involvement by the trustee if covenants made by the Originator as part of the transaction are breached.

**Merchant Bank / Financial system**

Merchant banks will receive the tender and prepare documents; as well as to evaluate and presenting the offers to students. They will grant loans to students with direct disbursements and select the loans to be sold to the NHEFC. They also manage the loans in the adjudicated portfolio (including the loans they sell back to the NHEFC).

**Investors / Capitals market**

Long-term investors such as pension funds, Takaful companies, and mutual funds acquire the securitized portfolios, both those owned by the National Higher Education Fund and the banks that decide to securitize them.

**Takaful (Islamic insurance)**

Takaful (Islamic insurance) will cover the student loan if anything happen to the borrower (student).

**Collection Agency**

NHEFC will tie up with many collection agencies to improve collection from student such as the financial institutions, government agencies which is linked to the student database.

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**Conclusion and Recommendations:**

Overall, the Malaysia case shows the complex dynamics between reforms in the loans system and expansion of higher education in Malaysia. The interaction among the various factors, the relationship between the funding structure of higher education and private HEIs, the regulation on university establishment and deregulation of student quota, education fever, and economic conditions such as introducing Ministry Education Blueprint 2013 has influenced the role of student loans policy on expansion of higher education.

Malaysia experience has several policy implications for developing countries looking to increase higher education opportunity in the midst of financial austerity to build the human capital needed for a knowledge economy. First, it is important to link the expansion of student loans with an economic development of the nation. When a nation needs unskilled labor for the rapid industrialization of the economy, it should invest more in basic and vocational education than in higher education as Malaysia did when the government changes Vocational school to Vocational College. As the nation progresses towards a knowledge-based economy, however, it should increase investment in higher education to produce high-skilled human resources by means of student loans system. By effectively linking strategies for economic development and student loans policies, both the financial efficiency of student loans and higher education accessibilities can be improved. Second, it is necessary to expand loans based on the supply and demand of higher education graduates. With the tertiary enrollment rate increasing every year in Malaysia, the growth in loans funds has led to an over-supply of college graduates, producing a rise in the number of unemployed graduates. Therefore, while the loans system has contributed to a surge in the number of beneficiaries, its efficiency has gradually been declining. In conclusion, the Malaysia case demonstrates that the government need new source to funding student loan so the introduction of i-SLBS right on track.

**REFERENCES**


National Higher Education Fund Corporation (NHEFC) has approved loans for 2 million students The Star p. 3.