

18/11/1997

Fighting off the wolves

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THE speculators stampeded all over us but nobody believed our Prime Minister when he spoke up and pointed out who was responsible for the currency devaluation sweeping across the Southeast Asian economies.

Then Hong Kong got hit, taking the stock market in the United States down with it. People believe our PM now.

When events in the Thailand market came to a head, the Western media all but sneered at our Prime Minister's remarks on who was responsible.

"Soros couldn't have brought down the baht alone," cried Newsweek magazine. (Sept 1, 1997)

After Hong Kong though, editorial slants seemed to shift in what appeared to be an about-turn on what a speculator can, and has, done.

"Drawing from multi-billion-dollar war chests, hedge-fund operators such as George Soros and Julian Robertson intensified their attack on the baht ... the wolves who started this turmoil were very well fed, probably with profits in excess of US\$3 billion," proclaimed a mysteriously fickle-minded Time magazine (Nov 3, 1997)

How do speculators operate? What exactly did they do to us? How are we fighting back?

Basically, financial markets operate under the rule of thumb that the more information an investor has, the better. He will be able to predict what will happen to a stock, currency or market, and act accordingly to make a profit.

For example, if a potential investor were to know that a certain market is likely to slow down because of certain events, policies or the like, he will likely just avoid investing there. A speculator, however, will try to exploit the situation to his advantage.

Currency speculators take this to extremes, collectively seeking out prey which they foresee as wounded, and unable to fight in the event of an onslaught. In what has now become a classic example, Thailand was seen as the weakest amongst Asia's tigers - easy meat.

They acted accordingly. Gambling that Thailand was already burdened by the spectre of an imminent economic crisis and thus could not afford to devalue the baht, the speculators moved into the money market.

One of the traceable techniques employed was using forward contracts, where a buyer would agree to provide US dollars in return for a fixed amount of local currency, to be given after a specified period of time.

Their gamble paid off, with Thailand suffering the brunt of its effects, closely followed by the other Asian markets.

To top it all off, the herd mentality governing the opportunists in the market caused the ensuing stampede. Panic reigned, and as they walked off from the kill, the currencies of Southeast Asia, compared to what they were worth a year ago, (from June 30, 1996, to Nov 7, 1997) had taken a severe beating.

The Thai baht was down by over 55 per cent, the rupiah by 34 per cent, the ringgit by 31 per cent, and the Singapore dollar by 9 per cent.

After Malaysia, Indonesia and the Philippines got hit, many still refused to acknowledge the problem, arguing instead that the "Asian Miracle" constituted more of a myth.

However, the blow that hit Hong Kong also rippled through to the US financial market, proving that in today's world, markets are closely interconnected. Market globalisation has caused many to now rethink the

potential damage that a speculator is capable of.

What, then, has been the extent of the damage done by currency speculators to Malaysia?

According to the figures provided by Goldman, SBC Warburg on the foreign liabilities of each nation in the region, the total percentage of foreign debt for each country is much higher than the actual GDP.

Simply put, each country is found to now owe more money than the total value of its products.

Malaysia's total foreign liabilities is projected this year to be at 184.6 per cent of its GDP, Indonesia at 109.5 per cent, the Philippines at 131.1 per cent, and Thailand at a whopping 214.7 per cent. And in Malaysia, the ensuing negative effect on the stock market is RM162.96 billion, according to the Finance Minister's recent Budget speech.

After factoring out the usual causes for such an alarming figure, the experts found that these unusually large foreign debts and their breakdown are the tell-tale foot prints of the currency speculator.

"The problem," said a local analyst, "is that two economists, when asked to comment on the same problem, will provide two sets of differing data, with two opposing conclusions to boot."

This is not helped by the fact that the more open a market, the more vulnerable it becomes to speculative attacks. The analyst argued that developing markets like Malaysia are still fragile to this level of openness.

South Korea, she commented, was not badly affected by the currency turmoil, due to the closed nature of its markets.

"In Korea, if you dare attempt such an attack, you will find yourself locked in the market, unable to get out."

For Malaysia, the events in Thailand helped to prepare itself for measures to limit, and if possible, counter the attack. So what has Malaysia done?

Firstly, the underlying policy is that for an economy such as Malaysia, growth is still needed.

"It's actually a good thing that we didn't slam the brakes down as hard as others would have wanted us to," said the analyst.

"If we had artificially pushed interest rates to exceedingly high levels, we would have now had to deal with recession as well."

The second strategy for counter attack is to cut off the supply of money that a speculator would need to borrow to launch or profit from future attacks. These include efforts by Bank Negara which would raise interest rates at a controlled and gradual level, like the recent announcement to float RM2 billion worth of bonds.

"Local banks will have to subscribe to these bonds, meaning that they will have less to loan out," said the analyst.

Indirectly, this will lead to a more prudent lending policy, which, added with other recently introduced monetary policies, will help keep the speculators at bay.

Apart from this, efforts by the Government to get currency trading regulated provide the long-term measures to combat future attacks.

International monetary bodies are now beginning to realise the truth of our accusations.

Last September, British development agency Oxfam called for a tax on international currency transfers to prevent the danger caused by speculation. This was in part due to our PM's repeated suggestions from mid-August for a study for a tax on speculative foreign exchange transactions.

And, last month, the IMF agreed in principle to Malaysia's proposal for the possibility of introducing regulations on hedge-funds activities.

Perhaps we should never be too easily led by the herd mentality which governs not only the speculative markets but the Western media as well, for both, as our Prime Minister has unfortunately shown, can prove not only to be wrong but disastrous as well.

* Tomorrow: The adjustments that Malaysians are facing and the power that lies within the average consumer to weather the currency depreciation.

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