

19/11/1997

The dance of currencies

Wan Imran Wan Chik

THE Dr M-Mr Soros exchange sure made the news. The world's leaders and a bunch of important bankers tuned in to interesting viewpoints on money. It always comes down to the bottomline, doesn't it?

Meaty developments took place at the International Monetary Fund-World Bank meetings in Hong Kong last September. Everybody there wore million-dollar suits with the deepest pockets. For people in the money business, it was THE event.

But did you understand what the fuss was about? I want to explain.

Money, like most things, can be bought and sold. When you go overseas, you change ringgit into that country's currency. Let's say you're shopping in New York. To get US\$1, you have to pay RM2.50, RM2.60, or RM3 or so. The price varies daily. If an American comes here, he'll get RM2.50 (or so) for every US\$1.

Technically, that's a sale. It's called an exchange, hence "foreign exchange", or forex in short. The RM2.50 (or so) is the exchange rate. On ordinary days, a jump or fall in the exchange rate may be just one sen, like RM2.50 to RM2.51.

Who and what determines the exchange rate? Guys in the money market do. In the share market, buyers and sellers agree on a price after some haggling. Prices go up or down depending on what share is hot.

When everybody is hungry for a certain share, the price climbs. When everybody wants to sell it, the price falls. The same mechanism (basically "who has, who wants", otherwise known as supply and demand) applies to all things - wheat, petroleum, cattle.

Use this idea on cold cash. Money traders literally buy and sell ringgit, as they do with other currencies. They determine what that exchange rate is. These are the dancing digits you see on computer screens and on TV.

You could profit from this. Say you bought US dollars at RM2.50 each, and later sold it for RM3, you make a profit of 50 sen per US dollar.

Using the same rate, imagine you bought US1 million (that's RM2.5 million) and sold it (that's RM3 million), the profit is RM500,000. Wow! Say you bought at RM2.50 and sold at RM2.51, your profit would be RM10,000. Not bad, huh?

Do we need all this? I'm afraid we do. When we travel to other countries, we spend money on food, hotel and souvenirs. A corporation may need to buy machinery from another country.

As nations, we need to import food, like wheat flour because we don't grow wheat in Malaysia. Although we produce rice, we still import some because we eat more rice than we grow. To do business with other countries, we must have currency exchange.

How does this affect you? Things cost more, or less. Say you bought jeans worth US\$100 in January, technically you paid RM250 because the exchange rate was US\$1: RM2.50. Got that?

Then, say six months later, the exchange rate alters to US\$1: RM3. This means you have to pay RM300.

When you buy imported jeans, you also pay for freight, packing and other invisible costs. Those fees are affected by the exchange rate too. You could buy locally-made jeans, but the denim is imported, and so's the thread and the sewing machine!

Is this a bad thing? It can be. If the ringgit falls and falls and

falls, we'll be stuck for a lot of things. Worst case scenario: So bad we can't import wheat flour which means no cake, no roti canai, no sliced bread. Never mind jeans!

What if it got really bad? Scholarships may be hit. It will become too expensive to study overseas. The Government and private companies will reduce the number of scholarships. It could be you who has to stay back. It would be tragic if you were half-way through your course.

Foreign exchange hikes can be especially hard on parents. A family who puts aside RM100,000 for a child's overseas university education needs RM200,000 overnight. What if they don't have it? Hence the small panic when the ringgit fell.

Malaysia is building a new airport and other major infrastructural projects. We have to pay for those. Some parts of these projects use imported goods. These are affected.

Is there any advantage to the ringgit fall? Yes, WE become cheaper. An American tourist got RM2.50 for each US\$1 in January, now he gets RM3.30. Malaysian-made goods being exported are therefore cheaper. But it is vital that we don't push up our prices on things.

What makes money traders buy a certain currency? Mostly, they're interested in making some money. Confidence is another factor. When a country is doing well, everybody wants to buy that currency. When a country goes to war (or is invaded), everybody panics and ships out. Money traders instantly sell off that currency. It can crash to serious nothing - like you need 1,000 bucks to buy one banana.

Bankers also know that powerful nations find it useful to keep Third World currencies down, so we are cheap for them to invest in. Then again, when we become too cheap, the same powerful nations begin to worry about their investments here.

What's George Soros got to with it? Soros is one of many money traders in the world. He happens to be a really big one. When he buys or sells money, he does it in the millions, sometimes billions. Other money traders follow - when he buys, they buy. When he sells, they sell.

As a result, you get many traders doing the same thing at the same time and that causes a visible fall or rise in currency value. On occasion, the ringgit is affected. Remember, they're in the game for profit.

If that's how the system works, wasn't Soros (plus other traders) doing the normal thing? Our PM says yes, but up to a point. Dr Mahathir thinks that if you know that your actions are going to cause such a drastic, damaging effect, you must control yourself or be controlled. He suggested certain curbs which amount to official or government intervention. Some people agree, some don't.

Question: How would you feel if it was YOUR scholarship that was cut? See a point.

Question: If you were a money trader, how would you feel when your profit-making is curbed? See a debate.

Question: In a free world, should such things be left to natural market behaviour or have official controls? See a dilemma.

Question: Would it play on your conscience when a bunch of Malaysian students is forced to come home half-way through their overseas education? See a moral issue.

Those are the questions the PM has on his mind. As you can see, the answers don't come easy.

* This article appeared in YouthQuake (Nov 14-20).

(END)