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Daring to adopt a different strategy

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THESE are hard times. And hard times warrant harsh and unorthodox measures.

Since Sept 3, the Government, through Bank Negara, has put into place several bold monetary measures to stabilise the ringgit, to inject confidence in the stock market and to kick-start the economy by rejuvenating the financial system with the injection of fresh funds.

One initiative was conceptualised to insulate the ringgit against speculators in the foreign currency exchange market. The ringgit was declared non-tradable outside the country.

Locally the currency was pegged to the US dollar at the rate of RM3.80 to the American unit.

Another was to cut the Statutory Reserve Requirements to release funds into the system.

The percentage of deposit liabilities of financial institutions placed with the central bank were reduced from eight per cent to six per cent.

Effective Sept 16, the SRR would be cut further, from six per cent to four per cent. Together they would inject a total of RM16 billion into the financial system.

Will these new initiatives work? That is the question uppermost in the minds of Malaysians.

The Prime Minister, Datuk Seri Dr Mahathir Mohamad thinks so. Last Tuesday he said signs have emerged to indicate that the radical initiatives are working.

For one, trading on the Kuala Lumpur Stock Exchange that had been listless over the past several months sprung alive since Sept 2.

Traded volume over four days, from Sept 2-5, averaged more than 500 million shares. That figure is a sharp increase from the daily average traded volume of about 100 million over the past 13 months.

For another, the new exchange control regulations render the ringgit valueless in foreign countries, after Sept 30. They had fixed the local currency at an exchange rate of RM3.80 to the US dollar.

This monetary policy would help importers and exporters to chart their accounts more accurately. But its effect on the economy will only emerge in the last quarter of this year or in the first quarter of next year.

That exchange control measure and the demonetising of the RM1,000 and RM500 currency notes would perforce the repatriation of ringgit currently held in ringgit accounts with foreign banks. All these are currently enjoying high interest rates.

It is said that RM100 million in cash is floating overseas. Another RM20 billion in fixed deposit accounts in Hong Kong, Thailand and Singapore. In the latter country, are deposited ringgit totalling almost RM15 billion.

All these funds should, theoretically, flow back into the country by the end of September, given the exchange control measures.

But whether all, much or little of these overseas ringgit will be brought home remains to be seen.

Local bankers and analysts forecast that they will. That view is shared by many foreign economists. The merits of the exchange controls are now appreciated by a few foreign countries, like Taiwan, Hong Kong and South Korea.

All also share the sentiments of Dr Mahathir that the measures introduced by the central bank will have a positive effect on the economy.

And some East Asian countries, according to news reports, have expressed interest in the currency control measures our country has implemented.

But others have a different perception. Indeed the US, the prime financial backer of the IMF, is expressing a Cassandra-like warning of gloom and doom about our country's initiatives and the possibility that they might be adopted by others in the region.

John Wolf, Washington's chief negotiator at the Asia-Pacific Forum in Tokyo, rang the resounding bell of warning that a spread of Malaysian-like finance market controls could threaten the entire world's financial system.

He said, "we (read that for the US) are watching with some anxiety the reversal in the way Malaysia is moving".

"There are real risks and there would certainly be risks to the whole system (of world finance if there were a patchwork series of financial controls in the world."

Wolf, like others who have similiar doomsday sentiments, is imbued in traditional economic theories. He and others of his ilk do not see the practicality of an alternative to the Anglo-American model of domestic monetary policy.

Others say nay. The Malaysian model might succeed, given time. One perception is another American, Patrick Smith.

He is a partner with the US consulting firm, Marshall Auerback. In an article that was carried in last Wednesday's edition of the International Herald Tribune, Smith implicitly endorsed our country's exchange control measures.

He wrote that our country's measures should be seen in the context of "preservation of an economic model that (had) advanced the region at a rate and for a duration with no parallel in history".

He went on to say that the clear intent from Tokyo to Jakarta is to stimulate economies while avoiding the structural changes that the IMF has long deemed essential.

"Wall Street and the (US) State Department are shocked that Dr Mahathir has taken this step. They should be, as we now have an alternative to the Anglo-American (financial system) model which ranks unfettered capital flows among its significant features."

Two different perceptions. But they do not deliver the verdict whether the exchange control regulations will contribute to reviving the economy. They will, says the new Bank Negara Governor, Tan Sri Ali Abul Hassan.

Upon his appointment last Monday, Ali Abul Hassan made it clear that monetary policy of the central bank has to complement development initiatives. They would have to engender funds to finance the most recent development programmes.

Those development initiatives were formulated by the National Economic Action Council. Its secretary was Ali Abul Hassan since the establishment of the NEAC. He knows well the road mapped out for economic recovery.

The NEAC addressed first the problematic issue of rejuvenating the financial system. Banks overextended loans to non-productive sectors in the past.

Defaults in the past squeezed their capacity to lend. Businesses were denied funds to maintain operations. Some failed; others faltered. The effect was a downturn in the economy.

The NEAC decided that an asset management company should be established to buy out the non-performing loans of the financial institutions. It also decided that some financial institutions had to be injected with fresh funds. And so another special purpose vehicle was established.

Both these companies required funds, billions of ringgit, more than RM30 billion.

The Government decided to raise the money through the issue of bonds, in the international market. But the two international rating agencies, Moody's and Standard & Poor, reclassified the country's sovereign credit ratings by three notches which made it difficult for the country's economic managers to undertake an international road show to float Malaysian bonds.

Given these constraints the Government had to resort to novel initiatives. It, rather the NEAC, realised that a lot of money was locked up in SRR. Some RM32 billion. And so it decided to turn the spigot, funnelling as much as RM8 billion into the financial system.

That much of money back in the coffers of financial institutions should spur them to lend more aggressively. To lend to businesses and other productive sectors, one of which is the construction industry, especially the housing sector.

In good times as well as in bad times, the homeless need housing. They range from the low-cost and low-medium cost, for which units the demand is high, to the medium and even the high-cost, that is housing priced above RM100,000.

The initiatives have also had a salutary effect on lending rates. Why? It frees funds that do not yield any interest.

Banks can now parley them and earn an interest. Which is why the average base lending rate has been shaved by a hefty three per cent or more from 12.6 to the current 9.03.

That should encourage borrowings for business and the buying of houses. At least the initiatives should spur the housing sector. More would buy which would encourage developers to build more houses.

Then we have the latest pronouncement from the new Bank Negara Governor last Wednesday. A further reduction in the SRR from four per cent to two per cent.

Though he did not declare when it would be instituted, that RM8 billion would have to be invested in bonds that the Government intends to float to finance Danamodal Nasional Bhd, the vehicle that would revive ailing financial institutions.

Clearly then some of the measures to revive the economy that have been enunciated by the NEAC through its National Economic Recovery Plan have been backed by the funding of the monetary policies of the central bank.

Whether these, and other imminent measures would help to revive our economy remains an enigma.

Malaysians would like to see a fruition; others, like the US and the IMF, would desire a calamity to befall on a country that had dared to take a different road.

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