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Dr M: LTCM bailout is worst form of cronyism

Hardev Kaur in Tokyo

THE US\$3.5 billion (RM13.3 billion) bailout of Long Term Capital Management is the "worst form of cronyism" which also amounts to corruption, Prime Minister Datuk Seri Dr Mahathir Mohamad said yesterday.

In reply to a question from a Japanese journalist, he said the money for the bailout of the hedge fund last month was provided by banks whose board members had invested in LTCM. "By using the banks' money to rescue LTCM, they were using the banks' money to rescue their own investments. It is the worst form of cronyism."

The Greenwich-based hedge fund was headed by John Meriwether, a Wall Street star of long-standing. His team included two Nobel prize-winning economists and a former vice-chairman of the Federal Reserve. In addition, a number of leading Wall Street executives had personal investments in the hedge fund.

Goldman Sachs, Merrill Lynch, UBS and J.P. Morgan acted in their own self-interest when they joined a consortium of financial institutions and investment banks, facilitated by the New York Federal Reserve, to put up US\$300 million each to bail out LTCM. Germany's Deutsche Bank AG also joined in.

Since the collapse of LTCM, a large number of banks have suffered, so much so that the Federal Reserve had to get banks to bail them out, lest the whole banking system in Europe and the US be jeopardised. Among others, the Central Bank of Italy is believed to have lost 25 per cent of its reserves due to its involvement in LTCM.

By any measure the rescue of LTCM is certainly a bailout of a number of Wall street executives.

Dr Mahathir, who is here on Friday for a five-day working visit, met Japanese media representatives from Nihon Keizai Shimbun, Mainichi Shimbun, Yomiuri Shimbun, Asahi Shimbun, Kyodo News, Tokyo-Chunichi Shimbun, The Japan Times and NHK.

With the collapse of the LTCM, many countries are now beginning to take steps against hedge funds. While initially many blamed governments in developing countries as being corrupt, they are now beginning to get to the root of the problem - the role of hedge funds.

Said Dr Mahathir: "I think with a few more LTCMs they will change their minds completely. We need to see a few big banks in developed countries go bankrupt, people become poor and jobs lost. Then they will understand the role of hedge funds."

Today the hedge funds only attract attention in Asian countries and they feel that it is not going to be bad for them. It is argued that the so-called free market is fine. But Dr Mahathir said it was based on greed.

They have destroyed whole economies as is evident from the destruction and devastation in Southeast Asian economies.

"They have destroyed all the Tiger economies of Southeast Asia. Totally destroyed. All of them," the Prime Minister told the journalists.

"The hedge funds make a lot of money from these activities. It is the greed for money that motivates them. They (hedge funds) do not do these things because they want to correct governments, they do this because they make money. It is not a desire to shape a new morality in the governments of Southeast Asia that hedge funds do these things. That is all nonsense.

"They do not care if they destroy whole countries as long as they make money. We have seen that booming economies of Southeast Asia governed by

the same people for 40 years suddenly collapsing because the hedge funds have come in in order to devalue their currencies.

"Once you devalue the currencies you make people poor, you make countries poor."

Citing a CNN report, Dr Mahathir said poverty among children in Indonesia had increased by 50 per cent compared with below 20 per cent before the crisis, due to lack of food and medicine. "They are poor because you devalue the currency."

Similarly in Malaysia the ringgit has been devalued and Malaysians are now 60 per cent poorer. In some countries the devaluation is by 600 per cent which means the inhabitants of these countries need 600 units of the currency now against just one unit, which they cannot afford, and they therefore become poor.

Asked how the hedge funds could be regulated, Dr Mahathir replied that they should not be allowed to leverage as much as they do now, they should be transparent and their trading system should be revised.

Currently hedge funds leverage almost 50 to 60 times of their capital. Dr Mahathir said "maybe one to one" leverage should be the case.

They should also be required to trade openly and announce every transaction they make. "Because they ask us to be transparent, we ask that they be transparent."

Under today's trading system, each time they sell the currency its value falls. "What we want to see is that if they sell and there is a buyer and the buyer is going to buy it at a certain price, the currency should not depreciate."

Their operations in developing countries like Malaysia also needed looking into, he said.

"Other countries may be able to defend their attack but it is not fair to destroy the economies of countries which have taken many years to build up just because they (hedge funds) want to make money for themselves."

The world knows now currency traders can destroy not only the economies of countries like Malaysia but even that of the US can be threatened by unregulated currency trading.

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