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The destiny of Malaysia lies in our own hands

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THE Malaysian economy is still mired in the regional financial crisis that has swept across a number of East Asian countries since the middle of 1997. Although the crisis has continued for almost 16 months, there is still no sign of stability. In the meantime, several Asian countries have fallen victim to currency speculation and volatile short-term capital flows. In fact, Hong Kong, a free market with substantial foreign reserve holdings was also not spared from pressures on its currency and stock markets. The crisis has also spread to Russia and the Latin American countries. Despite this, the international community has not shown any sense of urgency, determination and commitment in addressing this problem. The international community, including the International Monetary Fund has established several committees and working groups ostensibly to create a new architecture for the international financial system. These were merely rhetorical sessions with no concrete solutions. In the meantime, it is obvious that more and more countries have been affected by the economic crisis. The breakdown of the global financial system may also become a reality.

Since the onset of the crisis more than a year ago, countries that have been affected by the turmoil like Thailand, Indonesia and South Korea have implemented a variety of macroeconomic adjustment measures and financial reforms, including measures to tighten monetary and fiscal policies as required by the IMF. These measures, according to the IMF, will restore international investor confidence in the currency and stock markets of these economies besides shielding them from systemic risks of the financial crisis. Unfortunately, investors were not convinced and speculators continued to exert pressure on the currencies and shares until the economic situation worsened. The management of the economy became more difficult and the cost of business increased. Banks' non-performing loans increased and companies incurred substantial losses. The governments were also unable to collect sufficient revenue to finance expenditure.

Although Malaysia was not under an IMF programme, we had initially adopted an approach, which was recommended by them to crisis-affected economies. Bank Negara had increased interest rates on loans and curtailed credit. The period for classifying NPLs was reduced from six to three months on Oct 18, 1997. Overall credit growth was limited to 25 per cent in 1997. In fact, there were also suggestions that banks facing difficulties should be immediately closed.

These measures which were implemented over a very short space of time were obviously detrimental to the financial markets and the economy.

Shortening the period for NPLs when the ringgit and share market were fast depreciating and under repeated attacks by speculators, in a regime of high interest rates, was unwise as due consideration was not given to the potential negative effects that could occur. The amount of additional loan-loss provisions that had to be made by banking institutions to comply with the three-month NPL period and 20 per cent specific provision policy was approximately RM7 billion. Therefore, the actual profit recorded was only RM169.8 million for banking institutions for the financial year 1997. There was really no reason to tighten the NPL since the banking system had more than adequate provision for bad loans.

When credit growth of 25 per cent was set as the target for 1997, a number of financial institutions had already exceeded the target. Banks

were forced to withdraw credit facilities and ceased to extend loans or new credit. This resulted in companies, entrepreneurs, businessmen and individuals facing serious cash flow problems to the extent that their businesses were severely affected and debt repayments could not be made.

Even though the nation's economic and financial position had obviously deteriorated, a tight monetary policy continued to be implemented by Bank Negara and those responsible for supervising the economy. They were completely taken in by the IMF, which was perceived to be the authority in economic policy.

Although the National Economic Action Council had, since January 1998, proposed a variety of appropriate measures to restore economic recovery, Bank Negara was reluctant to implement them. Throughout this period, Bank Negara maintained that the banks remained healthy.

In normal circumstances, countries that implemented IMF measures received billions of dollars. However, we did not receive even a single sen although we implemented similar measures.

In the meantime, the world economic situation continued to worsen. Although the developed countries in Europe and North America have maintained that they would not experience any negative effects from the East Asian economic crisis, it is patently clear that over time, even their economic and financial positions were beginning to deteriorate.

In the light of this development and the reluctance of the developed countries to take action to contain the activities of currency traders, we had no alternative but to pursue our own course of action to protect our economy. We have to reiterate our belief that kita boleh (we can do it), that this is our nation and we are solely responsible. The Government and the people must unite in efforts to restore the nation's economic health. Others will not help us.

Therefore, the Government felt that the nation had to try another approach, albeit, unorthodox. A thorough study was undertaken by the NEAC on alternative approaches that could save the nation.

It became clear that the nation's economic and financial problems were caused by currency traders who manipulated to depreciate the ringgit, thereby impoverishing both the nation and the people. The NEAC, therefore, decided to protect our ringgit and shares from being traded by foreign parties. By making the ringgit an acceptable currency only in Malaysia, and preventing the re-entry of offshore ringgit, our currency was no longer accessible to currency traders. They have, therefore, been forced to bring back the ringgit immediately to Malaysia and that in turn, enhanced our banking liquidity. They are also unable to appreciate and depreciate the value of the ringgit as they please. The power to determine the value of the ringgit against foreign currencies once again reverted to the Government. As anticipated, off-shore ringgit was brought home. Repatriation of ringgit from abroad contributed mainly to the increase of deposit of currency notes by Malaysians of RM1.5 billion at end-September and in addition as at Oct 8, RM4.9 billion were deposits in external accounts held by non-residents in the Malaysian banking system. As a result, our banking system had sufficient funds to provide loans.

In the country, the ringgit can be used as usual. Foreign currencies can be exchanged with the ringgit only in Malaysia. There are no problems in purchasing imported goods since there is adequate foreign exchange convertible to the ringgit to pay for such imports. Sales of Malaysian goods to foreign countries will be settled in foreign currencies so that the country can acquire sufficient foreign exchange to pay for imported goods.

Meanwhile, the pressure on the stock market is being addressed by ensuring that all trading of Malaysian shares not transacted through the

Kuala Lumpur Stock Exchange be considered invalid and will not be recognised. With this, the trading of shares in Singapore through the Central Limit Order Book or CLOB is no longer possible. It was this market which caused the sudden and drastic decline in our share prices. Rumours, which were often created and disseminated in Singapore to influence the market and which would bring down our share prices could no longer affect us. All shares must be traded on the KLSE in the name of the beneficial owners and no longer in the names of nominees. This is because trading between shareholders in the names of nominees need not be registered with the KLSE. Their trades, however, influenced the KLSE share prices. With the elimination of the nominee system, the hidden trades between registered owners through the same nominee is no longer possible. Trading in shares becomes more open and transparent. Therefore, all trading of shares is brought back to Malaysia. All share trading and commissions will be undertaken and earned by Malaysians and Malaysian brokerage firms. The brokerage companies need to intensify efforts towards enhancing efficiency, strengthening their financial positions and also consider mergers. This will also contribute to increasing government revenue.

As the Malaysian currency and shares of Malaysian companies could no longer be traded by foreign parties, when the Government took action to revive business and the nation's economy, currency traders and foreign investors could no longer threaten and exert pressure on the stock market to thwart the Government's efforts. Consequently, several measures could be undertaken to revitalise the nation's economy.

Some of the early measures taken were to reduce the interest rates on loans and ease restrictions on debt repayments by banks. The period for classifying NPLs was extended from three to six months.

The Government encourages infrastructure development, as it will revive almost 120 industries related to producing building and other materials. Loans for purchases of vehicles and houses have also been made easier.

At the same time, the Government was able to establish an asset management company, Danaharta and a special-purpose vehicle, Danamodal, as well as several other funds to address the financial problems brought about by the depreciation of the ringgit and the fall in share prices.

With these measures in place, there has been some revival in economic activity and there are already clear signs of a recovery. Foreign exchange reserves have increased from US\$20.2 billion at the end of August, 1998, to US\$22.99 billion as at Oct 22, sufficient to finance 4.4 months of retained imports. This increase, among others, has been due to gains resulting from the strengthening of some currencies against the US dollar. Reserves are not entirely held in US dollars. A significant proportion is being held in currencies of major trading partners. This will ensure that our reserves would not decline should the US dollar depreciate as it did just recently.

Our international trade has also registered good performance. The trade balance for the first eight months of 1998 showed a surplus of RM32 billion.

Sales of passenger cars increased from 5,641 units in February to 12,338 units in September 1998. There are many more indicators to show that the economy is improving.

In the meantime, the performance of the world economy was not encouraging. The collapse in value of the Russian rouble gave rise to very negative effects for the European and Latin American economies. The collapse of the rouble adversely affected the performance of one of the largest hedge funds, namely the Long-Term Capital Management Fund.

Since hedge funds are not supervised in any way and lending to hedge funds have not been monitored, hedge funds including LTCM have been able

to leverage up to 200 times its capital. In the case of LTCM, with a capital of US\$4 billion, it was able to borrow US\$120 billion. Subsequently, this sum was used by LTCM to borrow US\$1 trillion, that is, one million million dollars. Almost all the giant banks of the West provided this large sum. Following the problems at LTCM, UBS, the largest bank in Europe, experienced losses of US\$700 million. There were other funds and banks that experienced losses of more than US\$1 billion.

Given the great likelihood that their financial system would completely collapse, the Federal Reserve Bank of the United States, compelled western banks to bail out LTCM through the granting of loans totalling US\$3.5 billion. The depositors' money was utilised to facilitate this bailout. The fact that the banks' directors who provided the money for the bailout were also investors in LTCM was not at all perceived as unethical. If Asian countries did this, they would most certainly have been accused of help their cronies, but used other people's money to help themselves.

The collapse of LTCM will also affect other financial institutions and this may adversely affect the US economy. As it is, the US dollar has fallen sharply against the yen. The US dollar, which was previously equal to 140 yen, had fallen to an intra-day low of 112 yen.

Although the yen has strengthened, the Japanese economy has not yet shown signs of recovery. According to western experts, when the value of a currency strengthens, the economy should improve. However, the strengthening of the yen has not been accompanied by a rise in the Japanese stock market. Once again, it is clear that western experts do not really understand the factors influencing economies and markets.

However, Japan has tried to revive its economy using various policies. What Japan did was criticised by western experts as "too little too late". At the same time, Japan is criticised because it has not assisted in the recovery of Asian economies.

But when Japan proposed the Asian Fund and offered US\$100 billion, the United States pressured Japan to withdraw the proposal because it undermined the power that the IMF had over the financial policies of countries in the East. Now, Japan has once again offered US\$30 billion as loans to Asian countries. We hope that the United States will not, once again, oppose it.

As the West can now see the possibility that they too, may face a financial crisis as a consequence of currency trading by hedge funds, they have begun to speak a little about the importance of controlling currency trading. Several meetings have been planned, including one by the Prime Minister of Britain. The IMF and World Bank have also had many discussions on the subject.

However, up to now, their actions have been limited to mere talk. It does not appear that they intend to regulate currency trading. We are concerned that if they impose any rules, they will be directed at saving their own economies and finances only. The interests of developing countries like Malaysia are not important to them. They only want to retain their dominance over developing countries in order to further their own political and economic position.

As such we cannot depend on their assistance. Our destiny is in our own hands.

They condemn the recent measures we introduced. They frequently ask when we will remove the controls on the trading of our currency and the restrictions imposed on the complete take-over of our banks and companies.

Although we believe in free markets and the free flow of capital, we have witnessed how they can abuse this freedom. We have seen their greed to the extent that they were willing to rob the poor to enrich themselves. We have also witnessed how they can destroy the world economy.

We will, therefore, not allow them to trade our currency as they please. As long as they do not put in place rules to effectively control the trading in currencies, we will not permit the value of our ringgit to be determined by them. They are of the opinion that controls on currency trading cannot be long-term in nature. However, in China - where currency trading has never been allowed - the economy in fact remains healthier when compared with the other Asian countries.

Our measures do not restrict foreign direct investment and do not also prevent the repatriation of profits. At the same time, trade between Malaysia and other countries continue to be promoted.

Similarly, our stock market remains open to foreign investors. The only condition is that the trading of shares must be more transparent to the public and the Government. There is no reason why the sale and purchase of shares should be kept a secret.

The lack of transparency in the trading of shares has resulted in several rules being broken, in particular by foreign traders in our stock market. Rightly, any party that owns more than five per cent of shares in any one company should inform the KLSE as required by the rules on disclosure. But, because trading was kept confidential, disclosure did not take place. Even when ownership reached 33 per cent, they did not make a public offer to buy the remaining shares. They also ignored the principles of the New Economic Policy.

Many abuses took place because KLSE rules were not enforced or enforcement was not possible.

The laws and regulations that are now being enforced will bring order to the stock market. This will make the KLSE stronger even though the share indices are not likely to reach the extremely high levels it did before, when share prices did not reflect asset values or the performance of companies.

The nation's economic growth may not be as high as in the past. This is because all our trading partners are experiencing an economic slowdown. All the countries in Asia, Europe, and North and South America are experiencing low growth. As we are a trading nation, the recession in the economies of our trading partners will obviously affect our growth adversely.

However, with discipline, determination and perseverance, the economy will recover in 1999. We expect that the economy will grow by one per cent.