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The Clob impasse

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FOR over a year, the Central Limit Order Book (Clob) issue has been consistently identified as a significant factor inhibiting foreign investor confidence in the Malaysian stock market. The thinking was that the international funds were jittery about coming back as long as there was no satisfactory resolution.

Judging by the current surge in the Kuala Lumpur Stock Exchange (KLSE), the issue is no longer as deterrent a factor as market-watchers once believed. Foreign investors are increasingly drawn to the local bourse, never mind that the deadlock has not ended. And there is a nice twist here - the bull run will give more value to Clob investors.

'The fact that the foreign funds are buying shares in the KLSE indicates they are confident the Clob issue will be resolved,' points out Sarawak Securities research head Hudson Teh. 'It's still an issue, but you have to look at the fundamentals. Fundamentals override everything.'

Nevertheless, everybody will definitely be more at ease once the matter is laid to rest. The loudest sighs of relief should come from the 172,000 Clob investors. They have been waiting for the light at the end of the tunnel since Malaysia imposed capital controls in September 1998, a move which froze Malaysian shares bought on Clob, Singapore's over-the-counter market. The shares' estimated market value in mid-January is RM17 billion.

The Malaysian government maintains that Clob is an illegal market because it had traded in Malaysian shares without Kuala Lumpur's permission. Last December, Finance Minister Tun Daim Zainuddin reiterated the Malaysian authorities' stand: 'Our point of view has always been clear. We have never recognised Clob. It's a problem created by Singapore, so they should resolve it with the KLSE.'

This position has led to the perception that the Clob investors have been unjustly penalised. How the matter is resolved is widely seen as a litmus test of transparency and fairness. The international investing community is watching closely.

Indeed, some people believe that the issue has sway over Malaysia's impending reinstatement in Morgan Stanley Capital International Inc's (MSCI) benchmark indices. An August news report quoted MSCI executive director John Fildes as clarifying that settlement of the issue is not a precondition. At the same time, it remains a weighty consideration. 'What is important to us is the treatment of the issue and the general treatment of investor rights,' he added.

Which is why any attempt to free the shares attracts a lot of scrutiny. Not that there is a shortage of people willing to try. Several parties have come up with proposals (see table), but it appears close to impossible to please everyone. The Clob investors' knee-jerk reaction was to demand immediate migration of their shares to the KLSE so that the shares could be traded. But the Malaysian bourse will not let that happen for fear that the swell of selling pressure may lead to a market plunge.

This is a flawed view, according to some observers, who say most of the shares are of companies not in the KL Composite Index. They argue that even panic selling by the Clob investors is unlikely to cause anything more than a mildly annoying dent in the index. That may be so, but the investors have accepted that a staggered release is the next best option.

What they have snubbed so far are proposals involving deep discounts, less liquidity and more uncertainty. The Securities Investors Association

(Singapore) (SIAS), which claims to represent about 30 per cent of the Clob investors, has been especially vociferous about extracting a good deal. 'People are out to rob us,' association president David Gerald Jeyasegaram said recently. 'We've rejected the discount offers.'

For each investor, finding the way out is a question of making a choice, albeit a tough one. But it has to be done soon. The authorised nominee status for the Central Depository (Pte) Ltd (CDP) has been extended for the second time to June 30. The KLSE insists that this is the final opportunity for CDP to resolve the Clob issue. Come July 1, any securities not held in the account of a beneficial owner or an authorised nominee will be transferred to the Finance Ministry.

The long-drawn affair is bugging Malaysia's Federation of Public Listed Companies as well. Its president, Datuk Megat Najmuddin Khas, says it is high time the parties involved buckle down to working out a settlement. He frets that further delays will subject Malaysia and its plans to develop its capital market, to ridicule. 'It doesn't reflect too well on us as a nation and a people.' He cites the greed and confusion of the investors - some believe the group is roughly an equal mix of Singaporeans and Malaysians - as major obstacles. He adds, 'The investors are very happy to see the KLSE go up so they can renegotiate and renegotiate. And there's a great deal of people out there who don't have all the facts.'

Teh of Sarawak Securities agrees that a speedy solution requires some give and take. 'Bear in mind that you can't satisfy everybody,' he asserts. 'SIAS says it represents 30 per cent of the Clob investors. But who knows what the other 70 per cent wants?' In particular, the investors must understand why there is a profit element in the private sector proposals. 'The promoters will naturally ask what's in it for them for taking the risks,' he reasons. The main problem, of course, is in putting a dollar figure to the risks.

The first proposal was from Singaporean businessman Akhbar Khan Ali Khan via his Kuala Lumpur-based Effective Capital Sdn Bhd. It was a cash offer for all the shares at a premium of 45 per cent to market values as at Sept 15, 1998, the day Clob stopped trading Malaysian stocks. The investors saw it differently. They were fuming that they had been asked to swallow huge discounts to market values at the time of the offer. In the end, only 359 investors with holdings worth RM11.15 million said yes, accounting for a negligible 0.1 per cent of the affected shares.

This has set the tone for the rest of the proposals; they have to be more creative and the investors should have a belated chance to benefit from Malaysia's recovery. Subsequent schemes included closed-end funds, staggered release, share swaps, an investment-linked insurance policy and pledging the shares as collateral for borrowings.

Fortunately, the KLSE's bullish undertones have made things easier. There is more room to fine-tune and sweeten the proposals. Effective Capital, for instance, is a persistent suitor. This time, it is offering a scheme for the migration and staggered release of the Clob securities.

With the bourse performing well, the Clob investors may find it harder to hold out for new proposals. The market surge has another plus - the investors are less inclined to sell once their shares migrate to the KLSE, thus reducing the worry of the KLSE CI tumbling.

Kuala Lumpur City Securities research manager Soh Meng Hui says Effective Capital's latest offer may get the most response on the strength of its claim that it is 'the best and only approved migration proposal'. He adds, 'It is the only one that has the Malaysian authorities' approval. At the moment, there's simply no other choice.'

In a statement issued on Dec 30, SIAS disputed Effective Capital's claim, saying the company had not obtained written approval for the

migration of shares. In response, the company said it had secured a 'basket approval' from the Malaysian authorities for its earlier offers. It added that the migration approval did not need any statutory approvals, only policy approvals, which it had received from the KLSE and the Malaysian Central Depository.

It may, however, be too early to discount the other proposals. SIAS, for one, is hoping that its proposal (in partnership with Bintang Melewar Sdn Bhd) will get the blessings of the relevant authorities. The Stock Exchange of Singapore (SES) too has proposed a staggered release of Clob securities over 12 months. At the time of writing, it is still awaiting the KLSE's reply.

The KLSE's apparently cool demeanour towards its Singapore counterpart's scheme underscores the thorniness of the Clob issue, which entwines with the health of Malaysia-Singapore ties. Kuala Lumpur says it prefers to let the private sector sort things out. 'The Government will only come in if it is requested to,' said Daim in December. In contrast, Singapore feels that the private sector offers cannot resolve the issue. On Jan 10, its Prime Minister, Goh Chok Tong, said he hoped to meet Prime Minister Datuk Seri Dr Mahathir Mohamad early this month to settle the frozen securities problem, among other bilateral issues. 'In the ultimate, if there is no solution, Singapore has no choice but to take the matter to the WTO (World Trade Organisation),' he said. 'Perhaps the shareholders may also take Malaysians to the courts in Malaysia.' Dr Mahathir said he was prepared to meet Goh, but added that the Clob issue had nothing to do with the WTO.

Soh of KL City Securities believes that the high-level discussions may not mean much to many of the investors. They are probably more concerned about getting into the thick of the KLSE action as soon as possible. 'Would you accept a reasonable proposal or wait for the dispute to go to the WTO?' he asks.

The extension of CDP's authorised nominee status is a signal that the Malaysian government is equally keen to see an upbeat conclusion to the Clob saga. A decision to step in to help shape such a solution will certainly do no harm to investor confidence.