

Unconventional wisdom

Tun Dr Mahathir Mohamad made many bold and controversial decisions during his 22 years as prime minister. But historians may well judge his imposition of capital controls during the Asian financial crisis in 1998 as his bravest and biggest contribution to Malaysia. **Tan Sri Nor Mohamed Yakcop**, who worked closely with Dr M during those trying days, pays tribute to the man he says saved the country from economic disaster.

THE EDGE 3 - NOV 2003

A moment comes, which rarely occurs in a lifetime, when a particular event redefines a person's life and changes his course permanently. For me, the meeting with Tun Dr Mahathir Mohamad in Buenos Aires, Argentina, on the evening of Oct 3, 1997, was such an event. It enabled me to devote the next six years of my life working for him, meeting him almost daily. In the process, it enabled me to see, at close range, the abilities of this great man.

The combination of many noble qualities in one person is rare, and it is this unique combination that has enabled Mahathir to transform Malaysia from an otherwise typical Third World country into

a thriving and vibrant nation, well on the way to becoming a developed nation. It is also this combination of qualities that enabled Mahathir to save Malaysia from becoming another IMF nation during the financial crisis of 1997/98.

I am often asked about my involvement in the recovery plan implemented on Sept 1, 1998. It began on Sept 29, 1997, when I received a telephone call from Mahathir's office informing me that he wanted to see me. The PM was in Cuba at the time, and I asked, in jest, if I was to meet him there!

I was told, not in jest, that he would be arriving in Buenos Aires on Oct 3 and I was to make sure I was in the city at least a day before he arrived. I packed my bags

and left for Argentina, arriving on Oct 2.

The PM arrived the following day at 5pm and we met immediately at his suite. He informed me that he had asked many people what was causing the financial crisis but no one was able to give him a satisfactory explanation. He asked me whether I could clarify what exactly was happening.

I asked him how much time he had, and he said two hours. I explained to him how the foreign exchange market works, about short positions and long positions, about hedging and how currencies are borrowed and sold, the difference between "bid" and "offer" and how funds can be transferred from one country to another at the click of

continues on page F22

'He saved neighbouring countries as well'

THE EDGE 3 - NOV 2003

KENNY YAP THE EDGE

from page F2

a button. I also explained how the equity market works and the relationship between the forex market and the equity market. Mahathir hardly said a word, asked one or two questions, and listened intently.

After two hours, he had to end the meeting to get ready to go for an official dinner. He asked me about my plans for the night and I said I had been invited for the same dinner. Mahathir said to me: "You go back to your room and write down all that you have told me for the last two hours, and see me at 7am tomorrow." I went back to my room, skipped dinner and wrote it all down, finishing at about 6am.

I gave him the report an hour later. He asked me to take a rest and come back again at 2pm. When I returned, he told me that he had read the report and that he now understood what was happening in the financial markets. We started discussing various methods of overcoming the crisis, and our discussions continued when we returned to Malaysia. I met him almost daily for discussion, sometimes at his home, other times at his office. We tried a few mechanisms to overcome the crisis, some of which worked initially, but the hedge funds were so strong that it was difficult to proceed successfully with these mechanisms.

In early 1998, Mahathir asked me to explore the idea of imposing an exchange control regime to overcome the crisis. I remember preparing voluminous notes on this subject. Mahathir went through the notes carefully, and kept asking for more and more

and the currency would also be pegged at an overvalued rate.

It is often assumed that the system of exchange control (including fixed exchange rate) that we implemented on Sept 1, 1998, saved the country. The measures were undoubtedly a necessary condition, but were not enough to overcome the crisis. Malaysia was saved, not by exchange control measures per se, but by Mahathir.

Let me explain. Had any other developing country facing a similar crisis introduced the measures that we introduced in September 1998, it probably would have failed. The fact that these measures succeeded in Malaysia is due to Mahathir's ability and character. The economy and financial system, under Mahathir's leadership, was in a healthy state — healthy enough for the exchange control measures to be implemented without negative consequences. Moreover, the Prime Minister's hands-on management style enabled quick and timely decisions to be made, which was vital under the new exchange control regime.

The PM had ensured that the Malaysian economy was fundamentally strong. The

the group regularly, though not as often. And Mahathir continued to go through all the economic data with a sharp pencil.

they, therefore, stopped their activities in the track. Speculators backed off. They bought back the currencies that they had sold. This resulted in the appreciation of regional currencies.

Moreover, the IMF was unhappy with Malaysia's moves, particularly since after implementing the measures, we did exactly the opposite of what the IMF wanted us to do — we lowered our interest rates and injected liquidity into the system. The IMF then started relaxing conditions in other countries and allowed them to lower their interest rates and inject liquidity to stimulate their economies so that Malaysia would not outperform these IMF countries.

Therefore, it is no exaggeration to say that Mahathir not only saved Malaysia, but other affected countries in the region as well.

My second point is on what would have happened had the exchange control measures not been implemented. Many corporations in Malaysia would have gone under due to high interest rates. When corporations fall like dominos, banks would face

severe liquidity and solvency problems due to ballooning non-performing loans.

The problems of the banks would have

details. We went through many rounds of discussion, until he was finally convinced both of the concept as well as the proposed mechanism. The rest, I guess, is history.

Mahathir also asked me to prepare a paper on how to put an end to Malaysian shares traded on CLOB (Central Limit Order Book) in Singapore. He was of the view that an important reason for the falling stock market was the short selling of Malaysian stocks on CLOB. I prepared the report and Mahathir understood, for the first time, exactly how CLOB operates. The report, which was also implemented on Sept 1, 1998, put an end to the trading of Malaysian shares on CLOB.

I should add that the exchange control measures were crafted in such a way as to minimise the control aspects and maximise the outcome. The PM went through the proposed mechanism many times to make sure that there were as few control elements as possible, but adequate to ensure a positive outcome. There were no bureaucratic elements in these measures, such as requiring importers to obtain Bank Negara's permission to import. The ringgit was also pegged at a level where it was not overvalued.

In almost every other country that imposes exchange control measures and pegs its currency, there would, almost by definition, be numerous bureaucratic controls,

ringgit was strong and stable. On the back of the currency stability (at RM2.50 against the US dollar) Malaysia was doing very well. At the end of 1996, real gross domestic product grew at almost 8.5% and the growth was expected to continue for many more years. The government was enjoying a fiscal surplus. External debt was low, at 40% of gross national product. The current account of the balance of payments had narrowed from a deficit of 10% to 5% of GNP, and was expected to improve further. Inflation was at its lowest at 2.1%. We had steady growth of over 8% for the major part of that period. And this fundamental strength was a critical factor that enabled the exchange control measures to succeed.

For more than a year after the measures of Sept 1, 1998, were implemented, the Prime Minister met a small group of us six days a week — for at least two hours a day — to go through various economic data, including data on loans growth, exports, imports and property overhang. This enabled him to take quick action, whenever required. I remember one morning, when we were going through property figures, he looked at me and directed me to organise a property fair to clear the overhang of properties. I did, and property worth more than RM3 billion was sold. Even after the crisis was over, Mahathir continued to meet

The period 1997/98 was, to paraphrase Charles Dickens, the worst of times, but it was also the best of times. The worst conditions brought out the best in Mahathir. There is a saying that a good leader is like good tea — you only know his true qualities when he is in hot water!

Throughout the crisis, the Prime Minister focused on resolving the crisis. Day and night, he thought of nothing else. He read all he could on finance; he kept asking me to prepare notes on various technical issues. Sometimes, even though sick with flu, he continued to work. He was convinced that he had to understand the issues before he could work out the solutions. His innate intelligence and ability to focus on core issues showed throughout the crisis. He showed no sign of fear even at the worst of times; his only concern was the fast deteriorating state of the economy. He was, at all times, confident that he would prevail in the end.

I would like to add two more points on the financial crisis. The first is that, in implementing the measures of Sept 1, 1998, Mahathir not only saved Malaysia but neighbouring countries as well. Let me explain. When Malaysia imposed its exchange control measures, currency speculators realised that the other affected countries (Thailand, Indonesia and South Korea) could also impose similar controls, and

resulted in a credit squeeze, which would have led to another round of corporate failures. The government's revenue would have fallen drastically as fewer firms would be paying corporate taxes, thereby reducing the government's ability to stimulate the economy through fiscal policy measures. As a result of the problems faced by corporations and banks, unemployment would have increased substantially, leading to a second round of problems.

This is the classic vicious circle, which could have, in the end, destroyed the social and political stability of the country. This was a scenario that was waiting to happen. It did not happen because of the decisiveness and guts of Mahathir, who decided to take the path less travelled.

We owe Mahathir much gratitude for what he has done for Malaysia over the last 22 years. Solving the financial crisis of 1997/98 was just one, maybe the most important, of his many contributions to the nation.

On a personal note, over the past six years, I have come to admire this great man for his abilities, his high moral values and, most of all, his sincerity. Certainly, a man like Mahathir Mohamad is not born every day. **E**

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