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Act of defiance bears fruit for our economy

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MALAYSIA'S stimulus package has received favourable and positive response from the word go. The package is seen as targeting specific areas that need help in the current sluggish world economic environment.

But this was not the case in 1998, when measures to isolate the country from adverse external speculations came under scrutiny, the leadership was condemned.

But almost five years later there is more positive response and support for Malaysia's selective capital controls. They have neither been "condemned" nor seen as being "irregular" with the rules of the International Monetary Fund (IMF).

Michel Camdessus, former managing director of the IMF, now says they were "within the rules of the IMF and the fund had no objection to them".

But at the helm of the IMF then he was reported to have said that capital controls "were not desirable, or even feasible, in today's globalised economy".

The IMF was pushing for financial liberalisation and "administrative controls were not beneficial in promoting the long-term development of Kuala Lumpur as a financial centre".

Malaysia went against conventional wisdom as "liberalisation" which had become the mantra was causing problems in developing countries. Joseph E. Stiglitz winner of the 2001 Nobel Prize in Economics pointed out that capital account liberalisation is the single most important factor leading to the Asian financial crisis in 1997.

There is little doubt that IMF and the US Treasury policies contributed to an environment that enhanced the likelihood of a crisis by encouraging, in some cases insisting on, a rapid pace towards financial and capital market liberalisation.

Malaysia's controls were running counter to "liberalisation policies" and considered opinion in Washington.

No country had previously been singled out for special mention by Camdessus for "defying" the powerful Washington Consensus.

The main players in the global financial system, including the IMF and the US Treasury, rejected exchange controls and taxes on speculation as both harmful and useless. But more hardship was inflicted on the poor and suffering.

The fund was recommending and demanding that the crisis-hit countries implement austerity measures, cut back on public expenditure, have budget surpluses, increase interest rates.

This threatened social disintegrations and caused ethnic unrest as was clearly evident in Indonesia.

Malaysia in sharp contrast implemented selective capital controls to guard against volatility, prevent financial contagion, enable infant financial industries to develop in domestic markets, and be an effective measure of last resort that gave the Government room to breathe while it pursued reforms.

For this Prime Minister Datuk Seri Dr Mahathir Mohamad was called a "mad man". The country was labelled an international financial pariah with fund managers, bond traders and rating agencies seeking the shortest route out.

Rapid downgrades of Malaysia's sovereign ratings prompted many to exit.

The country was labelled a "renegade economy" and it was suggested that "Malaysia was suffering from an 'IQ crisis'." Investors were advised to

avoid the country like the plague as the "black market economy takes hold".

Thus panicky investors, and jittery fund and bond managers were seeking the nearest exit. Their recommendation? "Sell Malaysia".

But Camdessus met at the Banque de France in Paris where he is Honorary Governor, said the fund continued to offer advise to Malaysia "which was not always taken".

The former IMF chief said even during the peaks of rhetoric the team (from the IMF) continued to deal with the banking problems in Malaysia. "Look at the facts and you will see that it is much less black and white than it has been painted".

Today the situation is vastly different. Not only have the controls worked and Malaysia has emerged much faster from the crisis with its economy more resilient. Its "act of defiance" also showed the world that there are alternatives and solutions to financial problems.

Camdessus, when he saw that the selective controls were beginning to show results and helped stabilise the region, softened his criticism.

He then said: "I praise the way in which Malaysia has been able to adopt a soft system of controls".

He admitted, "Consensus seems to be emerging that controls may have a place when there's risk of a crisis ...but only as a breathing space while other fundamental measures can take effect."

The tone now is decidedly more conciliatory from the man whose image with his arms folded overlooking President Suharto signing the IMF agreement at the height of the 1997-1998 crisis has been etched in the minds of millions.

Blame for much of the problems in developing countries is laid at his feet. Instead of helping the poor countries during crises, the IMF became the "main bill collector for the G7".

But Camdessus was quick to defend the fund's policies.

He took comfort from the fact that there was no historical precedent of such a dramatic and rapid turnaround in the economic fortunes of two crisis-hit countries - Thailand and South Korea.

Even Indonesia, he argued, would have recovered much faster if not for the political turmoil that erupted. But others, including Stiglits, point out that the political turmoil was fuelled by IMF policies.

Camdessus, calling himself "a common man in the street", is now focused on the plight of the poor, their need for clean water and development needs of Africa.

This is a far cry from his high profile and powerful position at the IMF, which has been blamed for many of the problems and hardships of the poor including those in Africa.