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INTERNATIONAL FINANCE CORPORATION
INTERNATIONAL DEVELOPMENT ASSOCIATION
INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
MULTILATERAL INVESTMENT GUARANTEE AGENCY

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Statement by the Hon. **DATO SHAFIE MOHD SALLEH**,
Governor of the Fund and the Bank for **MALAYSIA**,
at the Joint Annual Discussion

**Statement by the Hon. Dato' Dr. Shafie Mohd. Salleh,
Governor of the Fund and the Bank for Malaysia,
at the Joint Annual Discussion**

Mr. Chairman,
Distinguished Governors,
Excellencies,
Ladies and Gentlemen.

1. Amidst a challenging external environment, the ASEAN economies have shown remarkable resilience and have recorded stronger growth in the first half of this year. With sound economic fundamentals in place and as a result of the successful implementation of various fiscal stimulus packages, Malaysia has been able to weather the impact of volatility in the external sector. Domestic demand has strengthened and latest economic indicators show that economic recovery is underway and, conditions have improved in the second quarter of 2002.
2. Malaysia posted a strong 3.8% GDP growth in the second quarter of this year after experiencing a modest growth of 1.1% in the first quarter. Growth was mainly driven by private consumption with manufacturing and services sector providing the impetus. The stimulus for growth in private consumption was higher income arising from fiscal expansion, low interest rates and an improvement in the exports of commodities. Over the short to medium-term, growth prospects are expected to further improve following measures to boost domestic investments in all sectors as announced in the recent Budget 2003.
3. Our banking sector continues to strengthen further with risk-weighted capital ratio (RWCR) of 12.8%, NPL of 8.1%. The Corporate Debt Restructuring Committee (CDRC) has successfully resolved the debt of 47 cases or 98% of the number of cases accepted with total debts amounting to RM43.97 billion. The recovery profile of the resolved cases has shown that 83% of the recovery proceeds were in the form of cash, redeemable instruments and rescheduled debts.

Mr. Chairman,

4. When the IMF/WB met five years ago in Hong Kong, the "burning issue" was the Asian financial crisis. During the intervening period, we have seen significant progress in terms of measures on crisis prevention at the country level. In particular, the international community had pressed for economic, financial and corporate sector reforms in the crisis-affected countries to reduce vulnerabilities and strengthen the foundations for sustainable growth. At the height of the crisis, there were also calls for reforms in the international financial architecture to reduce, if not eliminate, the frequency and severity of crises.
5. Today, as we meet in Washington, it is encouraging that the Asian economies are, by and large, fully on the path to sustained growth. The progress made reflects the success of reform measures by the national authorities as well as closer economic and financial cooperation at the regional level. Policy initiatives by the Asian countries to promote domestic sources of growth and enhance intra-regional trade have also helped to sustain domestic growth in an increasingly uncertain and fragile external environment.

6. Malaysia is well aware of the need to continually adjust its policies to address the challenges of an increasingly uncertain global environment, which has clouded the brighter outlook in Asia. While the global economy has improved since late 2001, many downside risks remain. Recent indicators suggest a weaker and more uncertain outlook, with the financial markets becoming more volatile in recent months amidst concerns over developments in the United States, particularly the weakening of the dollar as well as developments in the corporate sector. In addition, developments in the Western Hemisphere have also heightened the risk of renewed crises. Volatility in financial markets has become more intense, with adverse implications for capital flows and foreign exchange rates. An increasing concern is also the rising trend towards protectionism in the developed countries, particularly in the United States.

7. In the circumstances, the international community, notably the major industrial countries, have a moral obligation to individually and collectively pursue policies that contribute to continued global prosperity. We urge the major industrial countries to resist the tide of protectionism and to open their markets to freer trade. Closer coordination of policies among the major industrial countries is also essential to ensure a stable international financial environment that will reduce volatility among the G-3 currencies. In particular, we call upon the G-3 countries to give due cognisance to the widespread impact of their domestic policy actions on the rest of the world.

Need for Fundamental IFA Reforms

8. The international community's efforts in addressing the problems arising from the Asian crisis have only been partially successful. Asian economies have undergone significant restructuring and reforms to rebuild the foundations for sustained growth. Notwithstanding the efforts at the domestic level, all countries remain vulnerable to abrupt external shocks, as long as there is no real progress in the reform of the international financial architecture (IFA).

9. To date, progress in real IFA reforms remains elusive. In the wake of the tragic events of September 11, the focus of the international community's efforts on IFA reforms has been on combating money laundering and terrorist financing activities.

10. Malaysia fully appreciates and supports the international efforts on this front. We recognise that terrorism constitutes a threat to international peace and stability. In this regard, we have put in place comprehensive measures to curb any abuse of Malaysia's financial system for terrorist financing and money laundering purposes. We recognise that it is crucial that comprehensive international efforts be put in place to combat money laundering and terrorist financing, as we are a firm believer in preventive and pre-emptive action in managing potential areas of risk and vulnerability.

11. While Malaysia fully supports decisive measures to curb money laundering and terrorist financing activities, we consider it equally important that international efforts be redoubled on fundamental reforms to the IFA. We need to move beyond measures that merely tinker with the existing system, when a fundamental and complete overhaul is required.

Standards and Codes

12. Progress on IFA reforms has been mainly in the efforts by the IMF, among others, to “encourage” countries to adopt international standards and codes, and to be more transparent. Malaysia supports such efforts to provide markets with more timely and accurate data so that they can make more “informed” investment decisions. Malaysia was among the pioneer group of countries to sign up for the IMF’s Special Data Dissemination Standard (SDDS). While we appreciate the rationale for international standards and codes, we strongly believe that its implementation must remain voluntary, with due consideration to differences in country specific circumstances and priorities in terms of the level of economic development, and structure of the economic and financial system. Under no circumstances should countries be pressured into adopting standards and codes, nor should they become part of IMF conditionality.

Transparency

13. The emphasis of the international community is still skewed towards enhancing transparency of the public sector, with limited progress for the private sector. As recent events in corporate America have revealed, more concerted efforts are required to ensure that the “checks and balances” are in place to make the private sector more accountable for disclosing timely and accurate information.

14. It should also be recognised that enhanced transparency and disclosure is not an end in itself. Transparency does not guarantee stability, nor does it prevent a crisis. The reality has been that greater transparency and disclosure have led to “information overload”, with financial markets misinterpreting and over-reacting to the information provided, thereby creating greater instability. Accurate analysis and interpretation of the information disclosed is equally important in ensuring that enhanced transparency and disclosure are effective in promoting stability. At the same time, the IMF’s transparency initiative must strike a balance between greater disclosure, while maintaining confidentiality. Here, we have strong reservations on the proposed policy of presumed publication of all IMF country reports, as this could undermine frank discussions between the IMF and its members.

15. While we support the IMF’s initiative on transparency, we should caution that this initiative must strike a fine balance between the need for transparency and the need to maintain the confidentiality of the dialogue between the IMF and its member countries. In this connection, we have strong reservations on the merits of the proposed policy of “presumed publication” of all IMF country reports, including the Article IV consultation reports, which contain highly market sensitive information. Efforts to promote greater transparency of the IMF’s operation and policies should not be at the expense of betraying the trust and confidence of IMF member countries.

Exchange Rate Issues

16. The urgency for IFA reforms to ensure a safer world for globalisation and liberalisation is particularly evident in the current environment where the major international currencies are subject to excessive volatility. Concerted efforts are needed to mitigate the risks of a disorderly adjustment in the U.S. dollar exchange rate, as it

would have wide-ranging negative implications for the global economy. Closer collaboration among the G-3 currency areas is essential to ensure stability in world currency and financial markets. In this regard, the G-3 countries must give due cognisance to the wider implications of their policy decisions, instead of focussing solely on domestic imperatives. This is particularly urgent in the light of the recent assessments that there is little that monetary policy can do to rein in market excesses, without imposing damaging consequences on the real economy.

Reform of IMF – Governance Issues

17. Reform of the IFA would not be complete without changes in the way the IMF and other international financial institutions operate. Current efforts at fine-tuning the existing institutional framework, for example, the review of IMF conditionality and programme design, are grossly inadequate. Fundamental reforms are needed to address governance issues, particularly, the IMF quota structure.

18. The views of developing countries have been marginalised for too long as they are not adequately represented in the IMF's decision-making process. A comprehensive reform of the distribution of IMF quotas is urgently needed to better reflect the changes in the global economy, notably the increased relative position of emerging market economies. The IMF, as a multilateral institution, must be a representative of all its member nations and not just a privileged few. There should be no room for veto powers in the IMF, and it cannot be seen to be an instrument of foreign policy for any particular member, however large.

19. Past efforts to improve the quota formulas have not resulted in significant changes in the way the quota structure is determined. While there is merit in considering alternative formulas, it is important that the development and inclusion of new indicators or new methods does not merely represent a change in the technical formulation but represents a step forward in ensuring better governance at the IMF. The 12th General Review of Quotas should take this into consideration and ensure that developing countries are adequately represented and their views are taken into account in the decision-making process of the IMF. While this may be a protracted process, one way to address this issue is to increase the basic vote of each member, which has progressively eroded over the years, back to the Bretton Woods level.

20. There is no room for complacency in the reform of the IFA, given an increasingly globalised economy and highly integrated financial markets. In the aftermath of the Asian crisis, the international community has urged the Asian countries to set their economies in order by cleaning up in the financial and corporate sectors, and strengthening macroeconomic fundamentals. Progress on this has been encouraging and has borne results. The challenge is for the international community to move ahead with real IFA reforms to ensure a more efficient and stable international financial system.

World Bank Operations

Mr. Chairman,

21. On the brighter side, we wish to take this opportunity to commend the World Bank Group for its achievement in increasing its lending from US\$17.3 billion for the

year 2001 to US\$19.5 billion for the year 2002, taking into consideration the slowdown in the global economy and the worldwide impact of the September 11 event. We take note of the Bank's emphasis on extending more than half of its International Development Association (IDA) to the poorest countries in the East Asia Pacific region and the Bank's continuous efforts to provide policy advice, technical assistance and analytical services to member countries.

22. Malaysia is pleased that the Bank has mobilised its resources in its International Finance Corporation (IFC) to catalyse foreign investment in difficult environment, particularly to emerging markets that are expected to remain depressed and volatile for the foreseeable future. However, Malaysia would like to call upon the IFC to extend its financial assistance to regions and sectors underserved by investment from private sector, especially in the infrastructure sector as it lays the foundation for the rural development and improves market access for agriculture and farm produce.

23. On leveraging trade for development, we support this new initiative by the Bank as trade is a crucial vehicle for developing countries to reap benefits from globalisation. Market access by the developed world for products from developing countries will have direct impact on growth and poverty reduction outcomes and will enhance the Bank's role in developing supply and export capacities of low income countries. Provision of analytics and technical assistance in understanding trade liberalisation implications and necessary skills, knowledge and tools to ensure adequate negotiating capacities in WTO forums should be the Bank's priority. The Bank's analytical work can offer avenue on how to mitigate possible negative short-term effects of trade liberalisation on previously protected sectors of the economy and on fiscal revenues as a result of tariff reduction.

24. Malaysia takes note of the Bank's New Water Resources Sector Strategy. This will provide great opportunities for financing the development of much needed water resources and subsequently expedite economic growth and development in poor countries. Furthermore, providing easy access to safe drinking water, particularly to the poor, is one of the Bank's highest development priority under the Millennium Development Goals.

25. Malaysia also welcomes the launching of the Education For All (EFA) Fast-Track Initiative to help countries that have already made progress toward EFA to accelerate the achievement of Universal Primary Completion (UPC). However, our greatest concern is the 29 countries lagging farthest behind in achieving universal primary completion by 2015. This will remain the biggest challenge for our work and for all stakeholders.

Thank you.