

Joseph Yam: HKMA congratulates the Central Bank of Malaysia on 50 years of achievements

Address by Mr Joseph Yam, Chief Executive of the Hong Kong Monetary Authority, at the Ceremony for the 50th Anniversary of Bank Negara Malaysia: "50 Years of Central Banking – Stability and Sustainability", Kuala Lumpur, 8 February 2009.

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YANG AMAT BERHORMAT PERDANA MENTERI MALAYSIA Dato' Seri Abdullah Haji Ahmad Badawi

YANG BERBAHAGIA KETUA SETIAUSAHA NEGARA Tan Sri Mohd Sidek Haji Hassan

Dear Governors, Distinguished Guests, Ladies and Gentlemen,

It is an enormous honour and pleasure to be invited to speak at today's ceremony. The honour is a special one because over the years Bank Negara and the Hong Kong Monetary Authority have worked in close partnership on many projects, to the extent that a deep friendship has been built between our institutions: with that friendship has developed great admiration on the part of my colleagues and myself for Bank Negara's many achievements. The pleasure is not just in having the opportunity to visit once again this beautiful and hospitable country, but also in being able to pay tribute to a valued colleague and dear friend, Governor Tan Sri Dr Zeti Akhtar Aziz. Governor Zeti's strong and inspired leadership of Bank Negara for most of the last decade has turned it into a first-rate central bank and a great force for good in this region.

We are all mindful that we celebrate this 50th anniversary in the midst of intense global financial crisis. This will not – and should not – diminish the happiness of the occasion. Indeed, much of the history of Bank Negara Malaysia is the history of timely, productive, and often courageous response to crisis, and examining that history gives cause for optimism in our present circumstances. In my comments today, I shall touch only briefly the current crisis. Instead, I shall reflect on the achievements of Bank Negara during the decade or so that followed the last great crisis – the Asian financial crisis of 1997-8. As I hope I shall demonstrate, these achievements are more than of merely historical interest.

It is clear to any observer that Bank Negara Malaysia has been a driving force in the building of this country. To speak only of its purely central-banking functions, Bank Negara has fully discharged its responsibilities through keeping inflation under control and maintaining stable interest and exchange rates, despite rapid economic growth. This has been crucial in supporting rising living standards and an increasingly diverse external trade. As adviser to the Government, the Bank has played a key role in formulating economic policies. The Bank has also been at the forefront of financial-sector development, in particular through building efficient and advanced payment systems. This work has stimulated a diverse financial system, with impressive growth in stock-market capitalisation and other non-bank activity.

All of this is indeed impressive, and reason enough for celebration. But Bank Negara's contributions to the well-being of the country go somewhat beyond the more conventional central bank functions. Of great interest in any survey of its role in nation-building is Bank Negara's promotion of forms of financial intermediation that are of special relevance to Malaysia's needs and culture. The Bank has been a pioneer in the promotion of microfinance, and a leading participant in the national agenda to promote a strong SME sector. Considerable funding and expertise have been devoted to these activities in recent years, with the result that the share of SME financing in total business financing has increased from 31% in 2000 to 44% in 2007. The experience and networks established in this field have been of great value in the Government's efforts to mitigate the effects of the current global financial crisis, which have included the recent launch of a substantial Micro

Enterprise Fund. Like many other economies in this region, Malaysia is a land of small businesses, but the attention that has, during years of stability, been given to strengthening channels of finance to the smallest of enterprises offers lessons for all economies at this time of pervasive credit crisis.

Bank Negara has also taken a prominent part in the development and advocacy of Islamic finance, which has seen rapid growth in the country since 2003, with annual growth rates in Islamic banking assets and insurance assets approaching 20%, and Malaysia now accounting for about 70% of all global sukuk issues. Islamic finance is increasingly recognised as an important alternative channel of financial intermediation, and not only within primarily Islamic communities. As Governor Zeti has persuasively argued, Islamic finance encourages business activities that generate legitimate profits, and rests on principles of fairness, shared risk and ethical practices.¹ There is, I think, much for us all to reflect on in this when considering how badly things have gone wrong recently in what might be called "traditional" finance.

No institution with such a long history can have escaped controversy, and BNM has had its fair share. What is interesting, however, is that perhaps the most controversial action by the Malaysian authorities in recent years – the response to the 1997-8 Asian financial crisis – has now come to be understood as appropriate and effective. At the centre of this response was the imposition of capital controls to contain speculative capital flows, stabilise the ringgit, and give the economy a breathing space. This was widely criticised internationally as a retrograde step. Yet it was a limited and temporary measure, which, along with other policies succeeded in stabilising the system and providing the conditions for economic recovery. The role of Bank Negara in promoting international understanding of this measure was crucial to its effectiveness. It is not, of course, my purpose to recommend capital controls as a general solution to financial crisis. The lesson here is that unorthodox measures can be effective, provided that they are well thought out and properly implemented. At a time like the present, when governments around the world have been ready to adopt measures that were barely conceivable a few months ago, this is perhaps a lesson that has already been quickly learned.

The region's recovery from the Asian financial crisis was nearly as rapid as the unfolding of the crisis itself, thanks to the vigorous measures taken by authorities in the region and the underlying momentum and vibrancy of the Asian economies. The experience of this shock generated a determination in the region to try to ensure that such a crisis did not happen again, and to strengthen financial systems against other forms of crisis. It would be complacent to suppose that we have been completely successful in these aims. We are, after all, in the midst of a serious financial crisis that no efforts by this region on its own could have prevented. The region's financial systems may have been largely undamaged by the first wave of that crisis. But the second wave is now upon us, and this second wave may well carry greater risks to emerging markets. Even so, the determination among Asian economies in the aftermath of 1998 to build strength against future crises has placed this region in a much more resilient position.

The raw resources for maintaining financial stability – foreign exchange reserves – have more than doubled in most of the economies in this region over the past decade. Many economies have embarked on financial-sector reform, with the aim both of ensuring that the banking system is well capitalised and of promoting other forms of intermediation. Central banks have seen a strengthening of their capabilities and a clarification of their policies and roles. Most heartening of all, co-operation among central banks in the region has flourished. Many examples could be cited, from bilateral swap agreements to payment system linkages.

¹ Zeti Akhtar Aziz: "Enhancing the Resilience and Stability of the Islamic Financial System": Governor's Keynote Address at the Islamic Financial Services Board and Institute of International Finance Conference, Kuala Lumpur, 20 November 2008.

At the centre of this regional co-operation has been the work of EMEAP in facilitating practical co-operation in all areas of central bank activity, and particularly in surveillance and crisis management. I should add that these activities have benefited enormously from the wisdom and leadership of Governor Zeti and her colleagues. The Zeti Taskforce – the EMEAP taskforce on Regional Financial Co-operation – has laid out a comprehensive framework for enhancing central bank co-operation, which has been adopted by EMEAP as a blueprint for action.

Calls were also made in the aftermath of the Asian financial crisis for a reform of the global financial architecture. Yet one of the great disappointments from those years, particularly when set against the real progress in regional co-operation, was the general absence of concrete measures on an international scale. There was, it must be said, a greater determination at least to pool expertise and discuss possible solutions in various international forums. But the political motivation for further reform gradually weakened during the period of strong global growth for most of the last decade.

The present financial crisis has much in common with the Asian financial crisis in that it has involved massive failures in financial intermediation, a rapid transmission of problems, and a strong element of surprise. However, the present crisis is global, not regional, and it centres on the world's most advanced economies. At its climax, in September 2008, the crisis raised the real possibility of a collapse of the world financial system. The reputations of many leading institutions and individuals have been damaged or destroyed. Large sectors of major financial systems have been effectively nationalised. Disillusion has spread, and fundamental questions have been raised about the future of free markets, as people count the cost of the excesses of the past few years.

Inevitably, central banks and regulators have been among those that have faced criticism: for not seeing – or not heeding – the danger signals; for having allowed financial innovation to get out of hand, to the benefit of intermediaries but to the detriment of the public; and for not responding quickly enough when the crisis began to emerge. Although there are many lessons to learn, not all of these criticisms are fair. The rapid, unconventional and co-ordinated response by central banks at the peak of the crisis undoubtedly averted a collapse of the system, and the vigorous measures to maintain the functioning of financial systems have been largely effective – so far. Nevertheless, the crisis itself, and the very scale of the response, have brought central banks more into the foreground than ever before. As the full implications of what has happened unfold there will undoubtedly be questions about their role and the policies they pursue.

The appropriate response to this is for central banks, international organisations, and government authorities to seize the initiative for reform so that financial crisis does not become a crisis of confidence in the system itself. Since, as recent events have resoundingly demonstrated, the financial system is a global system, the reforms must be organised along international lines. The limited achievements in international co-operation following the Asian financial crisis might make us sceptical. But, in fact, the signs are positive. Co-ordination among central banks in crisis management has been effective. Technical blueprints for regulatory reform on an international scale have already been drawn up. And the political will has been demonstrated in the commitment by the world's largest economies to implement far-reaching reform. One area of progress is the movement towards greater participation by developing economies in international forums and in the process of reform. This is important, not just because of the growing influence of these economies – nor even because the leading international forums are currently dominated by the very economies that are now in the deepest trouble – but because the ordinary people of developing economies are usually the ones who suffer most in a global financial crisis.

International co-operation will also, I hope, act as a countervailing influence against any repeat of the disastrous mistakes that were made in the 1930s. There has so far been a resistance to trade protectionism, although the idea has begun to gain some ground as a

spurious answer to economic distress. There is a risk that the idea will spread to the financial sector, particularly if there is political pressure to include protectionist measures in rescue packages for troubled banking systems in the developed economies. I need hardly point out that – no less than trade protectionism – such a trend would deepen the hardship of the developing economies, many of which rely heavily on international finance. It would also be a matter for serious concern in financial markets across the world. One of the central aims in building a more robust international financial architecture must be to ensure that there can be no excuse for resorting to financial protectionism as a solution to global or national crisis.

This will be a year of hardship and anxiety throughout the world. Much effort will be spent in fire-fighting and managing expectations. But this is also a time when central banks, international organisations, and leaders generally must work with optimism and resolution towards improving the international financial system. Crisis can provide the stimulus to reform, the determination to change, and the spirit to co-operate. There is no better illustration of this spirit than Bank Negara Malaysia. Nor is there a more happy example of a central bank working in partnership with the people it serves to the benefit of the country. It is therefore with the greatest of pleasure and respect that I join you all in congratulating Bank Negara on its 50 years of achievements and in wishing the Bank and all who are associated with it continued success and happiness in the next 50 years and beyond.

Tahniah kepada Bank Negara Malaysia di atas Ulangtahun ke lima puluh!²

² Congratulations to Bank Negara Malaysia on its 50th anniversary.