EIRBooks

Malaysia's Challenge to IMF: A Lesson on 'Method'

by Michael Billington

The Tragedy That Didn't Happen: Malaysia's Crisis Management and Capital Controls
by Dr. Marie-Aimée Tourres
Kuala Lumpur: Institute of Strategic and International Studies (ISIS Malaysia), 2003
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This book, to be officially released on Aug. 25, is the only comprehensive review of the extraordinary confrontation between the Government of Malaysia under the leadership of former Prime Minister Dr. Mahathir bin Mohamad, and the International Monetary Fund (IMF), the nest of speculators in the Western banks and hedge funds, and the institutions of the Washington Consensus, during and after the 1997-98 financial crisis in Asia. Its author, the Frenchwoman Marie-Aimée Tourres, was a visiting fellow at the International Institute of Strategic Studies (ISIS) in Kuala Lumpur in 1997-98, and again from January 2000 until the present. A skilled economist, Dr. Tourres presents both an economic analysis and a compelling political account of the Malaysian response to the speculative assault on the currencies of the Southeast and East Asian "Tiger" economies, which began in Thailand in 1997. It is an inside account, sponsored by the ISIS and its director Dr. Noordin Sopiee, (a close friend and collaborator of Dr. Mahathir), by Petronas, the state petroleum agency, and with direct support from Dr. Mahathir himself.

Even more important than the fascinating details of the initial collapse, the debates, and the intricate planning of the historic decision to reject IMF policies, imposing instead partial currency controls on the national currency, is Dr. Tourres' insight into the *quality of thinking* which *generated* these policy decisions. It is this method of thinking which is the real object lesson for the rest of the developing sector, facing similar but unique crises in their own countries today.

Readers of *EIR* know that the fight waged by Dr. Mahathir, often acting alone among national leaders of the world against "IMF orthodoxy," was both strongly supported by *EIR* and its founder, physical economist Lyndon LaRouche, and was covered extensively in the pages of this magazine. Although we had reported occasionally on developments in Malaysia, and Dr. Mahathir's leadership through the early 1990s, sometimes critically, when the currency speculation against the region hit with full force in July 1997, *EIR* made it a practice to convey the speeches of Dr. Mahathir, and some of his closest associates, on a regular basis. Since 1997, *EIR* has published extended excerpts from over 20 speeches by Dr. Mahathir, as well as an exclusive interview conducted by *EIR*'s Gail Billington and Dino de Paoli on Jan. 22, 1999. For many developing sector leaders and others, this *EIR* coverage was the only source of truthful reporting of Malaysia's fight—a point which Dr. Tourres notes clearly in her book.

We thus present this review with a special eye towards the many readers in the developing sector who have closely followed Malaysia's innovations and progress through the pages of *EIR,* with a recommendation to read the full text. This review will add several complementary references from *EIR* reports over the years.

The Wall Street Journal's Attempted Slander

Quite by chance, Dr. Mahathir had been invited many months in advance to give a keynote speech to the annual meeting of the IMF and the World Bank in September 1997, held in Hongkong, as the head of one of the most successful

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Dr. Mahathir bin Mohamad, Prime Minister of Malaysia, is interviewed by EIR*'s Gail Billington and Dino de Paoli, January 1999. Dr. Tourres' book reports how the Malaysian leadership became convinced that LaRouche and* EIR *were right in their analysis of the global economic crisis, whereas their detractors were dead wrong.*

"Asian Tiger" economies. When the speculative assault was launched in the Summer of 1997, Dr. Mahathir immediately broke ranks from the other Asian nations, which scrambled to accommodate to the criticisms and demands of the IMF. Instead, as we shall see below, Dr. Mahathir named and denounced both the speculators and the IMF for their subversive actions against the Asian economies, naming in particular the infamous hedge fund operative George Soros.

But the IMF's invitation for Dr. Mahathir to speak could hardly be withdrawn. In an attempt to poison the well for Dr. Mahathir's expected unwelcome truth-telling at the IMF confab, the voice of the synarchist banking circles, the *Wall Street Journal,* posted a headline story on the front page of its European and Asian editions in the hours preceding Dr. Mahathir's speech, attempting to slander him as a follower of the (supposedly) discredited Lyndon LaRouche! Titled "Malaysia's Mahathir Finds Strange Source for Soros Campaign: Asian Country's Media Tap U.S. Conspiracy Theorist Lyndon LaRouche, Jr." Complaining that the *EIR* report of April 1997, "The True Story of Soros the Golem—A Profile of Mega-speculator George Soros," was widely circulating in Malaysia, the *Journal* wrote: "Mr. LaRouche has long been at odds with the U.S. political mainstream, which regards him as an extremist in his views about reforming the global financial system. But his theories receive a warmer reception in Malaysia, where the 60-page *EIR* report on Mr. Soros has been passed among Malaysian editors, intellectuals and politicians."

If the *Wall Street Journal*'s intent was to dampen Dr. Mahathir's critique of Western speculators, it failed miserably.

The Tragedy That Didn't Happen

Dr. Tourres makes clear that Malaysia, in the years preceding the speculative assault, had been far more careful about "hot-money" flows into the country than some of its neighbors. "In contrast to Thailand and Indonesia (where there was recourse to unbridled short-term private sector offshore borrowing), capital inflows to Malaysia were dominated by FDI (foreign direct investment) and portfolio investment," writes Dr. Tourres. "External borrowing was regulated by Malaysia's Central Bank, which sought to ensure that with the exception of mostly very large infrastructure projects, borrowing was done in ringgit (the Malaysian currency)." Dr. Mahathir takes delight in quoting IMF Managing Director Michel Camdessus, who said in June 1997, just weeks before the assault on the region's currencies: "Malaysia is a good example of a country where the authorities are well aware of the challenges of managing the pressures that result from high growth and of maintaining a sound financial system amidst substantial capital flows and a booming property market." Camdessus's tone changed dramatically once the speculative attack had begun, accusing Kuala Lumpur of poor governance!

Still, Malaysia was not immune to the regional hot-money bubble, especially in the real estate sector. While Malaysia was taken by surprise by the sudden attack on the currency, there had been warnings. One person often quoted as having warned of a crash is Paul Krugman of MIT. However, Dr. Tourres notes that the credit given Krugman is "misguided"; that he had warned of a "slowdown," but admits that "he never anticipated such a fall."

The only clear warning, in fact, came from *EIR.* The Feb.

7, 1997 issue of *EIR* carried an article by Mike and Gail Billington titled: "London Sells a Killer 'Tiger' Tonic to Southeast Asia," and a national *EIR* conference in that month featured a presentation by Gail Billington on the same theme—that the Asian Tigers were about to "head down Mexico way," referring to the collapse of the Mexican currency and economy in 1994.

In the speech referenced above by Dr. Mahathir, to the Hongkong IMF Conference in September 1997, the Prime Minister said: "We dismissed the rumor that Malaysia would go the way of Mexico. . . . But now we know better. We know why it was suggested that Malaysia would go the way of Mexico. We know now that even as Mexico's economic crash was manipulated and made to crash, the economies of other developing countries too can be suddenly manipulated and forced to bow to the great fund managers who have now come to be the people to decide who should prosper and who shouldn't."

Think Globally, Plan Regionally, Act Nationally

Dr. Mahathir repeatedly told the world that if the international financial institutions had found a way to restrain the speculators, he would not have advocated imposing currency controls. He further insisted that if the regional economies had been allowed to create regional safety nets against the speculators, then currency controls might have become unnecessary. Such international or regional solutions were not to be, however. Discussions about a "new world financial architecture" were introduced at many international forums, but no action was forthcoming. Dr. Tourres quotes President Bill Clinton's Treasury Secretary Robert Rubin, one of the few Wall Street bankers who acknowledged the problem, in 1998: "The IMF has changed from 'we have the capacity to advocate but not to force sovereign countries to take actions they do believe to be in their interest,' to 'our approach requires that these countries take the concrete steps necessary to reform their economies'. . . . If countries don't take these steps, no financial assistance is made available." IMF Deputy Managing Director Stanley Fischer dismissed calls for a new financial system out of hand, insisting that the Asian problems were caused by policy errors and bad governance by the regional governments, not by speculators or the IMF.

Similarly, on the regional level, a proposal supported most vigorously by Dr. Mahathir, and Japan's Vice Minister of Finance for International Affairs, Eisuke Sakakibara, for an Asian Monetary Fund (AMF), was discussed at a September 1997 meeting in Tokyo. The idea was to raise $100 billion, half from participating countries, half from Japan, to provide liquidity in the region for the fight against speculative attacks, and assistance for development. The plan was squelched by U.S. and IMF strong-arm methods, when Japan was told that the scheme would undermine the capacity of the IMF to impose conditions on nations in trouble—just as Rubin had indicated.

Ultimately, Dr. Mahathir had to find means to act nationally, when the required international effort to correct the dysfunctional system did not materialize. As he said in 2002, looking back on the decision to impose controls: "We were strongly criticized by the Western countries, but we never bowed to them in any field, because we are responsible to our country, to our people. They are not responsible for our country. To them, if our people suffer, it is not their problem. But we are responsible. We are elected by the people, and it is our responsibility to look after the people's security and well-being."

Internal Dissent

The IMF had its supporters within Malaysia, and they used them to full advantage to attempt to bring down the recalcitrant Mahathir regime. Foremost among the IMF assets was Deputy Prime Minister and Finance Minister Anwar Ibrahim, whom Dr. Mahathir had once chosen as his likely successor. This reviewer had appealed directly to Anwar in the year before the crisis, in a public letter, to reflect on his failed worldview, after Anwar published a book called *The Asian Renaissance.* The book utterly misinterpreted the European Renaissance, confusing it with the degenerate worldview of the Enlightenment, which rejected all universal truth in favor of a bestial concept of man devoid of any higher moral purpose. Worse, Anwar praised the leading spokesmen for the British Empire's economic policies, Adam Smith and Bernard de Mandeville, as proponents of a highly moral approach to economic policy, through radical free trade and the pursuit of personal greed!

As the speculative assault on the Asian economies unfolded, Dr. Mahathir made clear that Malaysia would not accept IMF help, due to the destructive conditionalities placed on all IMF loans. However, Anwar, as Finance Minister, announced a budget in October 1998 which was recognized worldwide as "an IMF program without the IMF." Sounding every bit like an IMF representative, Anwar told the *Wall Street Journal* in December 1997, "We have reached a stage where we must undertake further strategic but painful measures to strengthen the nation's resilience so that we can withstand any systemic risks. We'll have to take the these tough measures if we want to help ourselves."

Dr. Mahathir, reflecting back on this period in a February 1999 interview, said: "Although we didn't ask for any loans from the IMF, the IMF kept on coming here and telling us what we must do, which is that in order to stop currency traders, we must raise interest rates. We must squeeze credit. We must force companies to go bankrupt by shortening the period for non-performing loans. At that time the IMF had a lot of influence over the then Minister of Finance [Anwar] and the Central Bank. They followed IMF conditions." In an interview with Dr. Tourres in January 2002, Dr. Mahathir said that Anwar "kept wanting to cut the operating expenditures . . . , wages . . . , development expenditures. . . . Either he did not understand, or he was too influenced by the IMF. He even scolded his Ministers for not cutting further."

In an interview with *EIR* in January 1999, when asked for his comments on the economic advice given by Lyndon LaRouche to Mexico and others, Dr. Mahathir responded: "This kind of contact must serve a useful purpose, and we would welcome that, certainly. Unfortunately, of course, the words are passed around that the *EIR* is a fascist grouping, which is trying to—this is told to me by some of your detractors, including my former deputy [Anwar], who told me earlier that *EIR* is a fascist paper, so we shouldn't listen to it. So that is the way of undermining any attempts on your part to try and promote the kind of ideas the *EIR* has always been focused on."

Defining the Principle

The Sept. 1, 1998 announcement of partial currency controls was by no means a snap decision. On Dec. 20, 1997, the Malaysian Government formed the National Economic Action Council (NEAC), at the recommendation of ISIS chief Noordin Sopiee, to devise a strategic plan of action for confronting the economic and financial attack on the nation. The NEAC was made up of the top government officials, including the Prime Minister and his Deputy, but also other government agencies, trade unions, corporate figures, bankers, and other civil organizations. The 26 members met five days a week, three hours a day, throughout 1998 and into 1999, with Dr. Mahathir in attendance at all meetings! This body, over time, assumed more responsibility than the Cabinet on certain economic issues, and, although Dr. Mahathir reports that it was not intended to sideline his Deputy Anwar, it did come to represent national interests, as against the IMF policies promoted by Anwar and some at the Central Bank.

Dr. Mahathir also called upon the former head of the Central Bank's foreign exchange department, Nor Mohamed Yakcop, who best understood the workings of the speculative markets (he had been burned before—he was involved in a disastrous loss on the British derivatives markets in 1992, when George Soros brought down the British pound, and caught Malaysia backing the pound). The two men held countless meetings, trying to come to terms with the character of the international financial markets, and devising a means to protect the nation from their power.

It became clear that only a clean break from the long reach of the speculative markets, through currency controls, could possibly prevent the further looting of the nation's economy and its population. There was no doubt in Dr. Mahathir's mind that there was a *global* crisis, which was the result of the demise of the Bretton Woods system in 1971, when President Richard Nixon pulled the dollar off gold and unleashed the speculative floating-exchange-rate system. In his *EIR* interview, Dr. Mahathir said: "When, for the first time, countries decided to float their currencies and allow the market to determine the exchange rates—that was way back in the 1970s—I felt even then, at that time, that the sovereignty of countries had been lost. And when you leave it to the market, the market is motivated entirely by profits—actually, greed—and you cannot expect greedy people to act in a sensitive way. If they see how they can make money for themselves, they couldn't care less if they destroy whole countries or they impoverish people."

Dr. Mahathir told Dr. Tourres that he had demanded an investigation of the hedge funds by the IMF (the subsequent IMF report claimed the hedge funds were guiltless in the Asian currency crisis), and had written to IMF chief Camdessus, asking for a curb on the currency traders. "Mr. Camdessus merely wrote," said Dr. Mahathir, "to say that the currency trading is so huge, and involved the great banks of the West, that nothing could be done to regulate it."

And yet, the NEAC realized, China had continued to control their currency, while allowing foreign investment in approved categories. After careful study, and discussions with Malaysian businessmen who did business in China, it was determined that some variation of the China model was the most appropriate for Malaysia. As Dr. Tourres notes: "In order to force foreign capital into 'real' economic sectors (in China), rather than investments in equity, controls had generally successfully favoured long-term over short-term inflows."

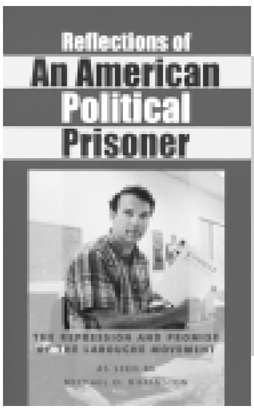
The Decision

The announcement came on Sept. 1, 1998: currency controls on the capital account (not on the current account); demonetization of the ringgit outside of Malaysia; a one-year freeze on the repatriation of portfolio funds; pegging of the ringgit to the U.S. dollar; and other measures. The official announcement included the following unambiguous reflection on the actual cause of the emergency measures: "The over-riding objective of the new measures is to regain monetary independence and insulate the Malaysian economy from the prospects of further deterioration in the world economic and financial environment. In the process, the nation would be adequately prepared to minimize the impact of a possible global economic crisis and a breakdown in the international financial system." Acting Governor of the Central Bank, Dr. Zeti Akhtar Aziz, who made the announcement, added that "We had to act on our own, considering the international community has failed to come up with any meaningful solution to the global financial turmoil. Ideally, the world should have acted in concert, instead of forcing countries to act individually."

Immediately, all hell broke loose in the Western capitals and the Western press. I will not report here the numerous slanders, denunciations, predictions of catastrophe for the Malaysian people, and so on, which Dr. Tourres reviews in the book. In retrospect, in view of the fact that the Malaysian people escaped the horrible collapse which ripped at the fabric of several of its neighbors—Indonesia perhaps worst of all—the hysteria is quite disgusting. The free-market gurus, and George Soros in the forefront, pronounced Malaysia dead, and called for Dr. Mahathir's ouster.

Most of the critics, including the IMF itself, have now admitted they were wrong, but without taking any measures to rectify the horrific damage their policies wrought across the region, or to change the system in any significant way. Dr. Mahathir answered the free-market preachers ironically in a speech in 1999: "We in Malaysia subscribe to the free-market system, but it is not a religion with us. It is just an economic system devised by imperfect man. While we should try to adhere to it closely, we see no reason to accept everything done in its name when we no longer reap any benefit from it. . . . No one declared that currencies should be regarded as commodities and traded like sugar or wheat or coffee. . . . Indeed, for a long time there was no currency trading, while the world traded and grew economically. Fixed exchange rates enabled values to be attached to goods and services."

Dr. Tourres reports that among the very few international organizations which defended Malaysia's decision was the Schiller Institute, which is associated with *EIR.* She quotes *EIR* Asia correspondent Gail Billington, speaking at ISIS in Kuala Lumpur on Jan. 25, 1999, that "by imposing capital controls, Malaysia had become the first country to place the human rights and general welfare of the people before the financial interests." Tourres takes pleasure in noting that Ms. Billington, despite being an American, did not support "Al Gore's outrageous behaviour during his visit a few weeks earlier." Tourres was referring to Gore's open support, while speaking at an Asia Pacific Economic Cooperation (APEC) Forum in Kuala Lumpur on Nov. 16, 1998, for anarchists who were rioting on the streets outside the conference to bring down the government, in support of deposed Deputy Prime Minister Anwar Ibrahim.



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Lessons

When the evidence of Malaysia's success in averting tragedy became too obvious to ignore, the critics instead switched to a variation on their theme, aimed at justifying their earlier hysteria: Malaysia has recovered from the crisis, they argued, but the currency controls were not responsible, as shown by the fact that those nations which had accepted IMF conditions were also recovering. There are several fallacies in this argument, including the fact that once Malaysia had broken from IMF orthodoxy, the IMF and Washington quickly began relaxing the conditions they had imposed on the other Asian economies, afraid that they would follow Malaysia's lead!

Dr. Tourres notes two other crucial differences. The Malaysian controls imposed "stability in economic conditions," which "helped to avert political and social instability as witnessed in Malaysia's neighbouring countries at that time. This, in itself, was a significant achievement, and possibly the most important one for this multiracial country."

Secondly, although foreign investment returned at a faster rate in South Korea and Thailand, much of the foreign capital inflow in those two nations was "acquisition by foreign companies of assets or equity of domestic companies. . . . Malaysia did not resort to promoting acquisitions or take-overs by foreign companies as part of the process of corporate and banking restructuring." Malaysia retained its dignity and its economic sovereignty.

These qualities of national independence are challenged across the globe today, both by the collapsing debt bubble in the Anglo-American banking system, and the strategic threat of the Bush/Cheney pre-emptive war doctrine. While the Malaysian policies can not be simply reproduced in other crisis countries, the method of approach, to "think globally, plan regionally, act nationally," serves as a guide to action. Dr. Mahathir, under pressure to lift the controls after the first year of successful implementation, said: "We are not about to do so, not unless the world curbs the currency traders and designs an international financial structure that is less liable to abuse by the avaricious." And, as he said in October 1998, just one month after the implementation of the controls: "We may fail, of course, but we are going to do our damndest to succeed, even if all the forces of the rich and powerful are aligned against us. God willing, we will succeed."