

Returned stability and strength, whither our financial markets...

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Financial Markets Committee

It has now been a full year since the Financial Market Committee (FMC) and Bank Negara Malaysia began its first series of financial market development initiatives in December 2016. The onshore foreign exchange market has become more stable, and the ringgit has strengthened, better reflecting the underlying strength of our fundamentals. More importantly, the vulnerabilities to the type of volatility we saw a year ago has reduced substantially. Ownership by foreign investors of ringgit debt securities has reduced, the ringgit non-deliverable forward (NDF) market has declined and so has the number of participants in this market. The onshore foreign exchange market has also become more liquid with greater volume and range of products. One part of the job done for now, but we can't be complacent.

For one, financial markets are always on the lookout for gaps and opportunities. And they look out for signs whether the central bank will ease off on the NDF stance. If things have settled down, why not? I think it would be more productive for them to focus on enhancing their business operation and efficiency within the current parameters. There really can be no turning back on the offshore NDF stance. If anything, more should be done to keep chipping away at this offshore market. We have seen the risks it brings and the damage its done. And not just the past few years. The financial crisis of 1997-98 was brought about and amplified by a dominating ringgit offshore market. There are so many parallels between the offshore ringgit markets in the 1990s and the ringgit NDF of past years, the only major difference is that the ringgit is now non-internationalized. This proves to be a very crucial difference as it forms an over-arching policy and explains why we don't recognise ringgit offshore products and markets. It also backs the legitimacy of our position in clamping down where we can. So, if that's the case, what does the future hold for the ringgit financial market.

For many years, the onshore financial market structure and rules has been to its own disadvantage. A legacy of the policies that dealt with the 1997-98 crisis. There were liberalization measures afterwards that were important, but overall, the pace fell behind to meet the demands of the financial markets. This was a key factor that led to a greatly lopsided foreign exchange market. On hindsight, we should have undertaken corrective measures earlier and in better times. That was always the intent, definitely at the onset of when we formed the FMC in May 2016. One thesis that drove the FMC was that as a result of tighter onshore market rules meant to curb speculative activity, we were instead pushing investors to trade in the offshore market. As offshore liquidity increased with greater volume, even our domestic corporates and SMEs were beginning to find ways to transact in the offshore market. Our onshore market was being hollowed out and if this

were to continue, the ringgit exchange rate would have been completely driven and determined by the offshore market, subjecting it to greater volatility and at the mercy of external developments.

But this is much less the case today. With the series of FMC initiatives, we have corrected this course. Volume and liquidity in the onshore market has sustained and picked up. More foreign investors and corporations are now transacting in the onshore market either directly or via the arrangements that effectively are an extension of the onshore market. Onshore financial market liberalization is an important journey to enhance the liquidity and depth of the markets. Yet we have to be cognizant of the risks. Further liberalization can come but must be in a balanced form and with conditions that will ensure the central bank will always have the surveillance capacity and the instruments to intervene when necessary. Markets need to be balanced and cannot be relied on to correct itself. But markets also have to be demand driven. To this the FMC needs to work further, meeting the ever-evolving market demands in ways that will satisfy our aspirations of an efficient, yet balanced and resilient financial markets. Best wishes for 2018.

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