

# External Relations

- 184-184 Overview
- 185-193 Reform of the Financial Architecture
- 193-196 Financial Sector Liberalisation
- 196-202 Regional Co-operation Initiatives
- 202-202 Bilateral Co-operation

# External Relations

## OVERVIEW

The conduct of Bank Negara Malaysia's (BNM's) external relations in 2001 was focused on regional initiatives to further strengthen regional surveillance and support mechanisms for crisis prevention. BNM also participated in international meetings in the global efforts to reform the international financial architecture (IFA). This also included initiatives to strengthen the domestic financial systems and to enhance the voluntary adoption of appropriate standards and codes of good practices in the banking sector and in capital market regulation and supervision.

As the year unfolded, the attention of international and regional fora turned progressively to surveillance issues when the weakening of global economic conditions became increasingly pronounced. Malaysia's participation in regional and international meetings provided opportunities to benefit from the sharing of experiences and exchange of views in assessing the efficacy of alternative policy responses to manage the adverse impact of developments in the major industrial countries on the global and regional economies.

During the year, significant progress was achieved at the regional level in terms of the implementation of concrete measures to assist regional economies in crisis prevention. This included the successful implementation of the Chiang Mai Initiative (CMI), a regional financial arrangement for crisis prevention among the ASEAN+3 countries (namely, members of the Association of South-East Asian Nations, and the People's Republic of China, Japan and Korea). Malaysia concluded a bilateral swap arrangement with Japan under the CMI. The aim of the arrangements are to enhance the capacity of regional economies to respond expeditiously to avert emerging crises. Progress was also made in further strengthening the economic review process among the ASEAN+3 countries to complement the implementation of the CMI. In addition, further work was undertaken at another regional forum to enhance regional co-operation in information sharing on capital flows. The South-East Asian Central Banks (SEACEN) Expert Group on Capital Flows developed a common framework to address gaps in data on capital flows. This co-operative effort

aims to facilitate an exchange of country experiences on the risk management of capital flows, an issue of high priority to Malaysia and regional economies.

At the international level, progress in terms of the IFA reforms was limited. Although some improvements were made in enhancing transparency and streamlining the operations of the International Monetary Fund (IMF), fundamental reform remained elusive, particularly in the area of reform of the IFIs and managing the risks of excessive volatility in capital flows. As part of on-going efforts on IFA reforms, BNM hosted a meeting of the Group of 15 (G-15) Expert Group on the Reform of the International Financial Architecture in Kuala Lumpur on 26 February 2002 to maintain the momentum for the reforms as well as to ensure that the views and concerns of developing countries, including the G-15 members, were addressed.

Although the issue of global co-operation to counter money laundering and terrorist financing activities became a major theme in the international and regional fora only after September 2001, Malaysia's involvement in promoting co-operation in this area had been evident since early 2001. As the co-chair of the Asia/Pacific Group on Money Laundering, BNM's involvement in the Group's work focused on promoting regional and international co-operation to counter money laundering activities. Malaysia also implemented a series of measures to prevent the abuse of the Malaysian financial system to finance any criminal or terrorist activities. A further development in Malaysia's external relations in 2001 was the enhanced participation of BNM in promoting international co-operation in the development of Islamic banking and finance.

During the year, BNM's external relations continued to accord importance to enhanced bilateral co-operation. Additional contacts were made to promote bilateral payment arrangements, in line with the Government's objective to strengthen South-South trade. This would also facilitate efforts to diversify Malaysia's export markets and reduce vulnerability to adverse developments in the traditional export markets. In 2001, BNM continued to provide technical assistance to a number of central banks, primarily in the form of attachments and training programmes.

## REFORM OF THE INTERNATIONAL FINANCIAL ARCHITECTURE

In 2001, efforts toward reforming the IFA continued to emphasise crisis prevention and management. Progress had been made in the areas of transparency and standards and codes, which were considered essential for crisis prevention. Some headway was also made in the reform of the international financial institutions (IFIs). However, progress was limited in addressing the issue of the governance of the IFIs and risk management of

IMF's role in capital account crises, the role of IMF surveillance in crisis prevention and the IMF's approach to capital account liberalisation.

The establishment of the IEO was in response to calls by the IMF membership, including Malaysia, for an independent evaluation of the IMF's role and operations and an objective assessment of issues related to the IMF. Following the Asian financial crisis, it was considered important that the IMF drew lessons from the crisis and improved its operations and capacity to respond more effectively to the changing needs of its diverse

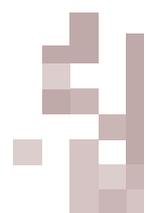
Reforms in the international financial architecture in 2001 made further progress in the areas of transparency, and standards and codes. Progress in fundamental reforms, particularly in addressing governance issues in the international financial institutions and risk management of international capital flows, has been more limited.

international capital flows. In this connection, BNM participated in a number of regional and international meetings, focusing on the concern that there was an urgent need for the international community to persevere with concrete measures to reform the IFA to ensure greater efficiency in international financial markets. Malaysia supported the international community's efforts to counter money laundering and terrorist financing activities following the events on 11 September 2001. Such efforts should, however, not weaken the resolve to pursue on-going IFA reform initiatives to promote international financial stability and address the risks and challenges of globalisation.

Besides the continuing emphasis on transparency and standards and codes, an equally important element of IFA reforms was the **reform of the IFIs**. Progress was mixed, with some improvements in streamlining conditionality in IMF programmes while governance issues at the IMF (notably the issue of IMF quotas) remained unresolved. The IMF's Independent Evaluation Office (IEO) began operations during the year, with the appointment of the Director of the IEO in August 2001. In December, the IEO outlined its work programme, which included plans to conduct an independent assessment of various aspects of IMF operations, as mandated by the IMF Board of Governors. Among others, the work programme included a study on fiscal adjustments and structural conditionality in IMF-supported programmes, an evaluation of the

membership. In doing so, it would be essential for the IEO to operate independently of the IMF management, as stated in its terms of reference.

During the year, the IMF introduced several reforms to streamline its financing facilities and the conditions associated with their use (IMF conditionality). Work in this area is ongoing. In addition to safeguarding IMF resources, the conditionality associated with IMF financing was seen as important in ensuring the success of its financial assistance to member countries. There was general consensus that conditionality should be streamlined to focus on areas that were critical to achieving the macroeconomic objectives of the programme and enhanced country ownership of reforms. It was also agreed that conditionality should aim to achieve a clearer division of labour and a more systematic and co-ordinated working relationship between the IMF and the World Bank. During the year, the IMF organised several outreach seminars to seek the views of its members on IMF conditionality. BNM forwarded a note to the seminar that was held in Tokyo on 10 July 2001 to discuss these issues. The note highlighted the importance for IMF conditionality to be more focused and tailored to the requirements of its member countries, and that the application of IMF conditionality needed to take into account country-specific circumstances, and a country's ability or capacity to adopt and implement the required policy reforms. Malaysia also reaffirmed the importance of enhancing the IMF's capabilities in



## IMF Meetings in 2001

### International Monetary and Financial Committee (IMFC) Meetings in 2001

- 29 April 2001, Washington D.C., United States of America
- 17 November 2001, Ottawa, Canada  
(The 2001 IMF-World Bank Annual Meetings were cancelled following the September 11 incident.)

### Conclusion by IMFC Members

- **World Economic Outlook**
  - Noted that the September 11 incident would result in a more prolonged slowdown of the world economy, despite policy actions to support a recovery in 2002.
  - Emphasised the important responsibility of advanced economies to promote early recovery in global growth.
  - Noted the importance of pursuing sound and proactive policies in emerging markets and developing countries in the context of weakening global demand and higher risk aversion in financial markets.
  - Noted the importance of increased trade opportunities in promoting recovery.
- **The Role of the IMF**
  - Welcomed the move by the IMF to refocus its work on crisis prevention and supporting policies aimed at sustainable growth and poverty reduction.
  - Considered the Contingent Credit Line to be an important signal of the strength of countries' policies and a safeguard against contagion in financial markets.
  - Urged the IMF to work on outstanding issues in the area of private sector involvement in crisis prevention and management.
- **IMF Surveillance on Financial Markets and Crisis Prevention**
  - Welcomed the decision to establish the International Capital Markets Department to enhance the IMF's understanding of and assessment on capital market issues; to enhance its early warning capabilities; and to strengthen crisis prevention.
  - Emphasised the need to make progress on early warning indicators of potential crises.
  - Noted the progress in the implementation of the IMF's initiatives on crisis prevention and financial sector surveillance, pertaining to the following:
    - Agreement on a list of international standards and codes;
    - The IMF's work with countries to strengthen data underpinning external vulnerability analyses;
    - Implementation of initiatives on the IMF's transparency policy; and
    - Progress in strengthening national and international financial sector surveillance, particularly on the joint IMF-World Bank Financial Sector Assessment Programme.
  - Welcomed the expansion of the IMF's financial sector work to include voluntary assessments of offshore financial centres.
- **Conditionality in IMF-supported Programmes**
  - Welcomed the on-going review of conditionality and emphasised that it remained indispensable; and reaffirmed that the objective of the streamlining was to make it more efficient, effective and focused.
  - Endorsed that conditionality should focus on measures critical to achieving macroeconomic objectives of a programme.
  - Noted the importance of taking into account the country's decision-making processes and capacity to implement reforms, and the need for strong country ownership of a programme.
  - Noted the importance of enhanced collaboration and clearer division of labour between the IMF and other international financial institutions in streamlining conditionality.

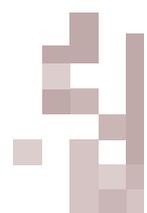
- **Combating Financial Abuse/Money Laundering/Financing of Terrorism**
  - Called on member countries to ratify and fully implement the United Nations instruments to combat terrorism.
  - Agreed that the 40 Recommendations by the Financial Action Task Force (FATF) be accepted as the international standard for combating money laundering, and that the Recommendations should be made operational in the work of the IMF.
  - Supported the Special Recommendations of the FATF to combat terrorist financing.
  - Urged international action to combat terrorist financing, and called for countries to take the following measures, preferably by 1 February 2002:
    - Establish financial intelligence units to receive and process reports of suspicious transactions from the country's financial sector, and to monitor suspected terrorist funds; and
    - Institute mechanisms for sharing of information and co-operation among national financial intelligence units.
  
- **Efforts in Poverty and Debt Reduction in Poor Countries**
  - Expressed concern at the adverse impact of the global slowdown on low-income and heavily indebted poor countries, and called on the IMF and World Bank to respond flexibly and proactively to address the needs of these countries.
  - Emphasised the different roles to be played by heavily indebted poor countries, developing countries and advanced economies in fighting poverty.
  - Recognised the importance of close collaboration and effective partnership among the international institutions in poverty and debt reduction efforts.
  
- **Other Issues**
  - Welcomed on-going measures to improve transparency, governance and accountability in the IMF, with the expectation that the Independent Evaluation Office would improve IMF operations and enhance its accountability.
  - Agreed that the IMF should address governance issues that had a significant macroeconomic impact.
  - Underscored the importance of open markets, and urged both the developed and developing countries to find a common ground for the launch of a new round of multilateral trade negotiations in 2001.
  - Looked forward to further progress on the work on IMF quotas, which reflected the changing conditions in the international economy.

analysing issues of political economy, to ensure that programme design would address social and political concerns as well as to ensure the successful implementation of a programme. Consideration of these factors would contribute towards enhanced country ownership of a programme. In this regard, closer consultation and collaboration with local or regional "experts" would enhance the IMF's understanding of situations in a particular country. BNM's views were recorded in the proceedings of the IMF seminar in Tokyo.

Malaysia also highlighted that the application of conditionality must remain consistent with the IMF's Guidelines on Conditionality, and not violate the principle of equal treatment across its membership. There was also a need for shared accountability by

the IMF in a programme. To the extent that an IMF programme adopted by any member country was designed by IMF staff and based on the advice of the IMF, the IMF should also assume some responsibility to ensure success of the programme.

The issue of IMF governance, notably the under-representation of developing countries in the decision-making process at the IMF, remained unresolved in 2001 as discussions on this issue were focused on the technical aspects only. The IMF held an Executive Board seminar in October 2001 to further examine issues pertaining to the choice and specification of the IMF quota formula (which determined a member's quota or capital subscription in the IMF). The aim was to develop a more representative quota formula. The Executive Board



agreed that further work is needed to further develop quota formulas that appropriately reflect members' position in the global economy. It noted that this task is made difficult as quotas are overburdened by having to perform a variety of roles (quotas determine a member's voting power in the IMF, its ability to contribute resources to the IMF as well as access to IMF financing facilities). The seminar was held following an independent review of the quota formula carried out by the Quota Formula Review Group (QFRG). The QFRG believed that quotas should be adjusted to recognise the constantly changing world economy, and the continual relative change of the circumstances of individual members.

Malaysia remained concerned over the lack of significant progress on the review of IMF quotas. To ensure a more equitable representation in the decision-making process in the IMF, radical changes are needed to reform the quota structure. A new approach or formula to governance may be necessary to ensure that representation at the IMF Executive Board reflects the relative position of individual countries in the current global economy.

A major activity of the IMF in 2001 was the implementation of standards and codes to enhance **transparency**. On the issue of adherence to the standards and codes, adherence should be voluntary and the IMF's Report on Observance of Standards and Codes and the Financial Sector Assessment Programme (FSAP) should not become mandatory elements in the IMF Article IV Consultation process. Malaysia supported the transparency initiative. However, also of importance was the need to ensure that this greater transparency resulted in more informed decision-making by investors. In this connection, the conclusions of an IMF economic forum entitled "Transparency at the IMF: The Road Ahead" on 13 December 2001 provided useful insights. The consensus was that good transparency practices did not necessarily guarantee economic and financial stability. It was also important that there was a clear legal framework governing the IMF's operating rules and procedures to enable the public and the market to understand how the IMF conducted its business and made its policy decisions.

Malaysia has remained committed towards transparency of its data and economic policies. Malaysia continues to meet all the requirements of the Special Data Dissemination Standard, including the forward-looking templates on Malaysia's external

reserves as well as the continued publication of the Public Information Notice of the IMF on the Annual Article IV Consultation on Malaysia.

Efforts toward enhancing greater transparency by the private sector made further progress at the 9th Manila Framework Group (MFG) Meeting in Auckland in December 2001. Malaysia had emphasised the need for a more balanced approach to the issues of transparency, in particular on disclosure by the private sector. There was a general consensus that there should be greater disclosure by market participants. This should include those institutions that were of systemic importance, such as the highly leveraged institutions and international credit rating agencies whose activities had implications on market stability.

An issue of particular interest to Malaysia, namely, the risk management of **capital flows**, continued to feature prominently on the agenda of several international fora in 2001. Some progress was made on work on capital flows, notably at the IMF and the BIS. The ongoing work programme of the IMF in the area of crisis prevention and financial sector surveillance included wider use of the IMF's Special Data Dissemination Standard and the General Data Dissemination System; expanded coverage of the IMF's Coordinated Portfolio Investment Survey to include additional instruments and jurisdictions, including offshore financial centres (OFCs); and progress made with respect to the FSAP.

During the year, the BIS continued with its efforts to replace the existing capital adequacy framework (the 1988 Capital Accord) with a more risk-sensitive framework. In supporting this initiative, BNM provided feedback and participated in discussions on issues related to the draft new Accord. The Basel Committee on Banking Supervision planned to undertake a review of the impact of the new Accord on banks and issue a consultative paper in 2002. The Accord will be finalised during 2002 for implementation in 2005.

BNM had the opportunity to relate its experience on the issue of capital flows and policy in emerging economies, which was the subject of a BIS Monthly Board meeting in September 2001. During the year, BNM also accepted the invitation by the BIS to participate in the BIS survey on international banking statistics. Data were submitted on a quarterly basis, based on currently available international banking data on a locational basis by instrument.

## Transparency at the IMF

### IMF's Publication Policy

On 4 January 2001, the IMF Executive Board agreed on a set of principles for the IMF's publication policy as follows:

- The publication of **country papers** should aim at:
  - i. Ensuring that frank policy discussions and reporting to the Board would be maintained;
  - ii. Striking the appropriate balance between transparency and confidentiality in dealing with sensitive issues; and
  - iii. Continued improvement in the quality of IMF staff reports.
- Publication of country papers should be subjected to a **uniform deletions policy**, which would be minimal and limited to the highly market-sensitive information.
- The presumption that the **Letters of Intent/Memoranda of Economic and Financial Policies** would be released. Such Letters would state a government's policy intentions. These Letters would include Technical Memoranda of Understanding with policy content and Poverty Reduction Strategy Papers.

These documents would be published in full, subject to the agreed deletions policy. A member that did not intend to publish these documents would explain its reason prior to the IMF's approval of its request for an arrangement.

- The publication of **Heavily Indebted Poor Countries (HIPC) Initiative papers** and relevant Poverty Reduction Strategy Papers and **Chairman's Statements**, conveying key points to the public would be continued.
- The Board would continue with the policy of **voluntary publication** of Public Information Notices (PINs) following Article IV Consultation and Board discussions on regional surveillance papers, concluding statements of Article IV Consultation, Recent Economic Developments, Selected Issues, Statistical Appendices and Reports on Observance of Standards and Codes (ROSCs).

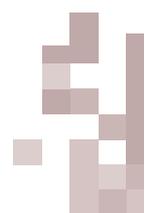
### Assessment of Implementation of Standards and Codes

On 29 January 2001, the IMF Executive Board reviewed the experiences in the implementation of standards and codes, and discussed the next steps of action. The Executive Board agreed that:

- The development and implementation of standards in areas relevant to the effective functioning of members' economic and financial systems were central to strengthening the architecture of the international financial system;
- Increased attention to standards and the introduction of standards assessments would help sharpen the focus of IMF policy discussions with country authorities and strengthen the functioning of markets; and
- ROSCs, as the principal tool for assessing implementation, would provide rigour, content and focus to the work on standards. The ROSCs were initiated in January 1999 as a pilot programme for the preparation and use of summary assessments of members' implementation and observance of standards and codes.

### Code of Good Practices on Fiscal Transparency

On 23 March 2001, the IMF Executive Board approved a revision of the Code of Good Practices on Fiscal Transparency as well as the Manual on Fiscal Transparency, with the objective of placing greater emphasis on the importance of fiscal data quality.



### Review of the IMF's Data Standards Initiatives

On 23 July 2001, the IMF Executive Board conducted its Fourth Review of the IMF's Data Standards Initiatives, and agreed on the following:

- Observance of the Special Data Dissemination Standard:
  - Observance issues would be addressed by placing notices on the observance of the Standard, indicating the nature of non-observance, and stating the time-bound plans for coming into observance by subscribers; and
  - Outreach efforts would be strengthened through seminars on international standards and codes and surveys on users of the Dissemination Standards Bulletin Board.
- A common voluntary database for reserves template data would be established and disseminated over the IMF's website.
- Work should continue on finalising the Debt Guide and raising awareness of the data dissemination standard for external debt.
- Establishment of a General Data Dissemination System (GDDS) unit at the IMF. Meanwhile, the IMF and the World Bank would collaborate closely on the socio-demographic component of the GDDS and the development of metadata for countries wishing to participate.
- An assessment methodology to assess data quality called the Data Quality Assessment Framework would be integrated into the structure of the data module of the ROSC as a central element of a Data Quality Assessment Programme.

During the 11th Summit of the Heads of State and Government of the Group of 15 (G-15) in May 2001, concern was expressed that increased reliance on private capital flows in financing development accentuated the inequality in resource distribution among countries while simultaneously inducing more volatility in financial flows. Given the shortage of capital inflows in many developing countries despite restructuring and reform efforts, participants called for effective public and private partnerships in efforts to increase such flows. Investors were called upon to give due cognisance to the development objectives of their host countries.

At the regional level, Malaysia continued to play an active role in the SEACEN Expert Group on Capital Flows (SEG). Progress made included the development of a common set of data templates for SEG members to exchange information on capital flows. Moving forward, the SEG would work towards developing concrete and practical proposals that members could implement individually or collectively to enhance the risk management of volatile capital flows.

In the light of the challenges posed by increased globalisation and financial liberalisation, Malaysia

emphasised the need for additional initiatives at the 9th Meeting of the MFG in December 2001. At the international level, Malaysia proposed that an IFI assume an increased role in promoting and safeguarding international financial stability. Initiatives at the regional level could encompass the strengthening of regional surveillance and the improvement of regional financing arrangements. At the national level, an integrated risk management framework could be developed to monitor debt- and non-debt creating flows, identify acceptable levels of risk and develop the methodology and technology to measure and monitor increased risks.

During the year, there was some progress in ongoing initiatives with regard to the **Highly Leveraged Institutions (HLIs)**. The Joint Working Group on HLIs (of the Basel Committee on Banking Supervision and International Organisation of Securities Commissions) reviewed issues related to the dealings of banks and securities firms with HLIs in March 2001. Encouraging progress in the firms' implementation of the HLI Sound Practice recommendations made by both the Basel Committee and International Organisation of Securities Commissions was evident from the strengthening of

the oversight of senior managements through improved policies and a clearer definition of risk appetites. Additional progress was needed in the assessment of firms' exposure to HLLs. While disclosure by HLLs to their counterparties had improved, progress was inconsistent.

In its review in March 2001, the Financial Stability Forum (FSF) Working Group on HLLs reported similar findings in the areas of counterparty risk management and disclosure. In the area of market conduct, the Principles for Foreign Exchange Trading released in February 2001 would be incorporated into existing codes of market conduct. Progress in the development of legal documentation practices was good, although progress in resolving issues in the area of improving consistency between different industry standards of documentation had been difficult.

Despite the progress, the issue of HLLs remained a matter of concern in various fora, including the 11th Summit of the Heads of State and Government of the G-15 in May 2001 and the 9th Meeting of the Manila Framework Group in December 2001. In view of the need to maintain international financial stability, the G-15 Leaders called for the monitoring and regulation of HLLs to safeguard countries from the destabilising effects of their activities.

At the 9th Manila Framework Group Meeting, concern was expressed that not much attention had been given to the impact of hedge fund activities on the integrity and stability of small emerging markets, as current initiatives were focused on enhancing disclosure by the HLLs and ensuring that counterparties strengthened risk management practices when dealing with the HLLs. Malaysia reiterated its stance that "self regulation" among HLLs was not a viable option. Additional measures were proposed in the area of improving risk management by both hedge funds and banks, dealing practices of hedge funds, identifying incentives for observance of practices by hedge funds and identifying mechanisms to solve disputes between economies on hedge fund activities.

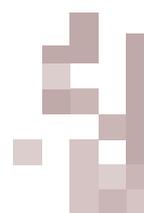
The issue of **private sector involvement** (PSI) in forestalling and resolving financial crises gained further ground in 2001. Based on the basic principle that a market economy required debtors and private creditors to bear the consequences of their decisions, principles for transparency and good communication were drawn up by the Working Group on Creditor-Debtor Relations set up by the IMF's Capital

Markets Consultative Group. The latter comprised a group of senior representatives of private financial institutions, which had an informal dialogue with the IMF on a regular basis.

Going forward, in November 2001, the IMF proposed a framework which would encourage both debtors and creditors to restructure unsustainable sovereign debts in a timely and efficient manner. The IMF mechanism offered the debtor country legal protection from creditors who stood in the way of a necessary restructuring, while the debtor country was obligated to negotiate with its creditors in good faith and implement policies to prevent a similar problem in the future. The proposed mechanism attempted to deal with the complex issue of sovereign debt restructuring in an orderly, predictable and prompt manner. However, many issues, ranging from legal to political concerns, needed to be resolved before the mechanism could be implemented. Further work would need to be done to make the principles and rules of the mechanism clear, credible and operational.

Discussions on **exchange rate regimes** continued to feature prominently among members of the international community, with widespread acknowledgement that no one exchange rate regime was suitable for all countries in all circumstances. Furthermore, there was consensus in the international community, including the Executive Meeting of East Asia and Pacific (EMEAP) Central Banks and the Asia-Europe Meeting (ASEM) as well as international financial institutions such as the IMF, that countries should adopt exchange rate regimes that supported and complemented their macroeconomic and structural policies.

Amid the debate on the costs and benefits of the two "corner regimes", namely an independent floating exchange rate or a hard peg, the IMF underscored the importance for countries to adopt exchange rate regimes consistent with their specific macroeconomic fundamentals. With respect to Malaysia's pegged exchange rate system, the IMF observed during its Annual Article IV Consultation with Malaysia in August 2001 that the pegged system was sustainable as long as the level of the ringgit exchange rate was not misaligned from its long-term equilibrium and that economic fundamentals remained strong. The issue, therefore, was not the type of exchange rate regime itself that was adopted but whether the exchange rate regime was supported by sound policies which served the



## FSF Meetings in 2001

### Meetings of the FSF

- 22 - 23 March, Washington, D.C., United States of America
- 6 - 7 September, London, United Kingdom

### Issues Discussed

- **International Financial System Outlook**
  - Assessed the implications of the current global economic outlook on financial stability, and agreed on the need for continued vigilance.
  - Reviewed the responses of key financial systems and markets to the world economic slowdown.
- **Highly Leveraged Institutions (HLIs)**
  - Reviewed the actions taken so far to address concerns raised in the report of its Working Group on HLIs.
  - Welcomed the completion of the work of the Multidisciplinary Working Group on Enhanced Disclosure and urged taking this initiative forward.
  - Welcomed and encouraged further progress by the Global Documentation Steering Committee in efforts to improve the consistency of the documentation standards.
- **OFCs**
  - Welcomed the efforts of standard-setting bodies and international financial institutions to improve supervisory, regulatory, and cooperation and information practices in OFCs.
  - Encouraged OFCs to further enhance their implementation of relevant international standards, seek assistance from the IMF and World Bank, and participate in assessment programmes.
  - Noted that disclosure of action plans and assessment findings were a useful means for OFCs to demonstrate their progress towards meeting such standards.
  - Reviewed the actions taken so far to address concerns raised in the March 2000 Report of the FSF Working Group on OFCs.
  - Welcomed the proposal of the Basel Committee on Banking Supervision to set up a contact group with offshore supervisors.
- **Implementation of Standards**
  - Reviewed work to foster the implementation of international standards for sound financial systems.
  - Discussed progress in providing incentives to foster the implementation of standards.
- **International Guidance on Deposit Insurance Systems**
  - Welcomed the development of guidance for the benefit of countries establishing or reforming a deposit insurance system.
- **Risk Management and Capital Regulation**
  - Welcomed the work of the Joint Forum (Basel Committee on Banking Supervision, International Association of Insurance Supervisors and International Organisation of Securities Commissions) in comparing approaches to risk management and capital regulation across the banking, insurance and securities sectors.
- **Financial Sector Robustness**
  - Welcomed the work of the Joint Forum in comparing the three sets of Core Principles for effective banking supervision, insurance supervision and securities regulation.
- **Developments in E-finance**
  - Discussed developments in e-finance for supervision, regulation and market functioning.

needs of the economy and did not create macro-economic imbalances. In this regard, it was concluded that Malaysia's pegged exchange rate was well sustained by strong fundamentals of the Malaysian economy.

### **Participation in IMF Meetings**

As part of its outreach programme, the IMF organised periodic study visits to member countries, in order to familiarise IMF Executive Directors with the current situation in member countries. Malaysia hosted a visit from a group of IMF Executive Directors on 25-27 October 2001, who were on a study tour of four South-east Asian countries (the others being Cambodia, Thailand and Vietnam). The IMF Directors had wide-ranging discussions with the Deputy Prime Minister, the Governor of BNM, the Secretary-General of the Ministry of Finance, the Executive Director of the National Economic Action Council, the Chairman of Securities Commission, other senior government officials, and representatives from the private sector. Malaysia updated the IMF on the current economic situation and policies in Malaysia. In response to questions posed by the Executive Directors, Malaysia shared its concern that there should be greater flexibility in IMF policy prescriptions, with due consideration being accorded to the institutional framework and the specific economic, social and political situation in individual countries. Malaysia also conveyed its view that while it supported the IMF's efforts to improve the transparency of IMF operations, there was a need to achieve a balance in terms of preserving the confidentiality of its policy advice to member countries.

On exchange rate policy, BNM highlighted that in small, highly open trade-oriented economies such as Malaysia, stability in the exchange rate was important. In Malaysia, the pegged exchange rate system was well supported by the macroeconomic fundamentals of low inflation, a strong external balance, low external indebtedness, a high level of reserves, and a well-capitalised banking system. The stable foreign exchange and financial market environment allowed significant progress to occur in the reform in the financial and corporate sectors.

In the area of Islamic banking and finance at the international level, BNM participated in the IMF meetings, both at the preparatory committee and Governors' consultative meetings, on Risk Management and Regulatory Standards for Islamic Financial Institutions. These meetings discussed and deliberated on the feasibility of establishing a standard-

setting body for Islamic financial institutions that was expected, among others, to develop and disseminate uniform prudential, disclosure and regulatory standards to govern risks inherent to Islamic financial products. Among the participants who attended the meetings were Governors and senior officers of the central banks from Bahrain, Bangladesh, Egypt, Iran, Indonesia, Jordan, Kuwait, Malaysia, Pakistan, Saudi Arabia and Sudan, and representatives from the IMF, the Islamic Development Bank and Accounting and Auditing of Islamic Financial Institutions (AAOIFI).

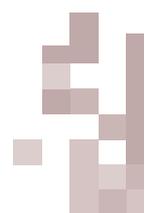
The preparatory committee met in March 2001 (Washington D.C.), June 2001 (Kuala Lumpur), July 2001 (Bahrain) and January 2002 (Paris) to prepare the framework and Articles of Agreement of the standard-setting body for deliberation at the Governors' consultative meeting. The consultative meetings of Governors were held in April 2001 (Washington D.C.) and November 2001 (Paris). At their meeting in November, Governors agreed on the establishment of a standard-setting body for Islamic financial institutions, with Malaysia as the host country of the standard-setting body. During the year, Bahrain and Malaysia also concluded a Memorandum of Understanding in October 2001 with the objective of entering into greater co-operation in the area of finance. This involved the collaborative efforts with other countries to develop the International Islamic Financial Market.

## **FINANCIAL SECTOR LIBERALISATION**

### **World Trade Organisation**

The most significant event for the World Trade Organisation (WTO) in 2001 was the Fourth WTO Ministerial Conference (4th MC), which was held in Doha, Qatar, on 9 - 14 November 2001. The 4th MC agreed to launch a new round of multilateral trade negotiations, to be called the Development Agenda. The new round of trade negotiations would include the continuation of current negotiations in the agriculture and services sectors, as well as negotiations or possible negotiations on a range of issues, including market access for non-agricultural products, implementation issues, environment, investment, competition policy and transparency in government procurement. Negotiations under the Development Agenda were scheduled to be concluded by 1 January 2005.

Malaysia was supportive of a new round of multilateral trade negotiations but highlighted the importance of having a balanced and manageable



agenda, which gave due consideration to the interests and concerns of all members, particularly the developing countries. In this regard, Malaysia supported the inclusion of negotiations in the agriculture and services sectors, as well as market access for non-agricultural products. In addition, the new round also recognised the special needs of the developing countries, particularly in implementing the existing WTO agreements, and committed WTO

1997, Malaysia made a number of improvements in the insurance and offshore financial sectors. Malaysia had committed under the General Agreement on Trade in Services (GATS) to allow an aggregate maximum foreign equity limit in the domestic banking institutions of 30%. In line with the policy to consolidate the banking sector, no commitment was made to issue new banking licences to either locals or foreigners. In the

## A new round of multilateral trade negotiations, covering negotiations in the agriculture and services sectors as well as several new areas, was launched in 2001. Negotiations are to be completed by 1 January 2005.

members to addressing the particular vulnerability of these countries through technical assistance and capacity building. On the contentious issues of investment, competition policy, transparency in government procurement and trade facilitation, the educative process with a more focused work programme would continue. In deference to the views of a number of developing countries, negotiations on these areas would only start after the 5th MC, provided that explicit consensus on the modalities of negotiations was achieved.

Negotiations to further liberalise the services sector, including the financial services sector, were formally launched on 25 February 2000. The 4th MC further agreed that member countries should submit initial requests for specific commitments by 30 June 2002 and initial offers by 31 March 2003. It was also agreed that negotiations on the services sector were to be completed by no later than 1 January 2005.

BNM was involved in the services negotiations in 2001, especially in discussions relating to the further liberalisation of the financial services sector. With negotiations entering into the "request and offer" phase on 28 March 2001, a number of countries had submitted negotiating proposals in the financial services sector, identifying areas and issues that they intended to pursue in the current round of negotiations. These included requests for the removal of existing restrictions on market access and any preferential treatment currently accorded to domestic players, as well as calls for national authorities to improve transparency in the regulation of the financial sector.

At the last round of negotiations on the financial services sector, which were concluded in December

insurance sector, a commitment was made to allow existing original foreign shareholders to own up to 51% of the insurance companies. In addition, new entry of foreign insurance companies was also welcomed through participation (up to 30% of total equity) in locally-incorporated insurance companies.

The negotiations for the further liberalisation of the financial sector would be in accordance with the financial sector development path charted in the Financial Sector Masterplan (FSMP). To date, the foreign presence in the domestic financial sector is significant. Of the 27 commercial banks (including two Islamic banks), 14 are wholly foreign-owned and foreigners further owned an average of 18% of the total equity of five domestically-owned banks. Together, foreigners accounted for about 32% of total commercial bank assets. Similarly, foreign presence is also significant in the domestic insurance industry, with 25 out of 63 insurance companies being foreign-owned. The market share of foreign-owned insurance companies operating in Malaysia amounts to 64% of life insurance premiums and 39% of general insurance premiums.

In line with the commitment towards further liberalisation of the financial sector, the focus of policy in 2001 was to strengthen the capacity and capability of the domestically-owned financial institutions. This was aimed at enhancing their ability to compete on a more level playing field with the foreign financial institutions. The negotiations to liberalise the financial services sector under the new round have further increased the urgency to strengthen the capacity of the domestically-owned financial institutions. A number of capacity-building initiatives had been

<b>Schedule of WTO Negotiations on Trade in Services (2000-2005)</b>	
<b>25 February 2000</b> The new round of services negotiations was formally launched	<p>Negotiations began with the “rules-making” phase where Members negotiated the new rules and disciplines relating to specific provisions of the General Agreement on Trade in Services (GATS), including on subsidies, emergency safeguards and government procurement.</p> <p>The discussions also focused on the procedures and guidelines for the “request and offer” phase of negotiations, scheduling guidelines and disciplines on domestic regulation.</p> <p>BNM was actively involved in negotiations to formulate an agreement on emergency safeguard measures for the services sector (see BNM Annual Report 2000).</p>
<b>28 March 2001</b> Services negotiations entered into the “request and offer” phase	<p>The adoption of negotiating guidelines by Members marked the start of the “request and offer” phase of negotiations. Negotiations for further liberalisation would be conducted on the basis of negotiating proposals submitted by Members.</p> <p>“Request and offer” is essentially a bilateral negotiating approach, whereby negotiations are conducted based on requests submitted by a country to a trading partner and offers submitted by the trading partner.</p>
<b>30 June 2002</b>	Members to submit initial requests for specific commitments from other Members by 30 June 2002.
<b>31 March 2003</b>	Members to submit initial offers of specific commitments by 31 March 2003.
<b>1 January 2005</b>	Services negotiations to be completed.

identified under the FSMP, including appropriate strategies to raise performance standards. Indeed, as part of the measures to further develop the financial sector, the FSMP had identified a number of liberalisation measures that would be undertaken over the next 10-year period.

#### **ASEAN Framework Agreement on Services**

The ASEAN Framework Agreement on Services (AFAS) was signed on 15 December 1995 by the ASEAN Economic Ministers at the Fifth ASEAN Summit in Bangkok. The aim of AFAS was to develop and enhance the competitiveness of the services industry in ASEAN through, among others, liberalising trade in services beyond the commitments undertaken in the GATS (that is, “GATS-plus”). The

first round of negotiations under AFAS to liberalise the services sector, including the financial services sector, was concluded in 1998. Subsequently, a second round of negotiations was launched in January 1999, and scheduled to be concluded in 2001. In this connection, in August 2000, the “Working Committee on ASEAN Financial Liberalisation under AFAS” was formed to provide a forum for negotiations to liberalise the financial sector among the ASEAN countries. BNM participated in a number of meetings held by the Working Committee throughout 2001, during which ASEAN member countries tabled and negotiated their GATS-plus offers. The offers of commitments by member countries had been finalised and the “Protocol to Implement the Package of

Commitments on Financial Services under the AFAS” was expected to be signed in April 2002.

## REGIONAL CO-OPERATION INITIATIVES

### ASEAN Financial Co-operation

In 2001, significant progress was achieved in a number of initiatives to further enhance regional

co-operation. At the ASEAN level, BNM assumed the chairmanship of the ASEAN Central Bank Forum (ACBF), a forum for the Deputy Governors of the 10 central banks and monetary authority in ASEAN to exchange views on economic and financial developments in the region. In this connection, BNM hosted the 8th and 9th ACBF Meetings, which were held in Kuala Lumpur on 3 April and 13 September 2001 respectively. At the 9th ACBF Meeting, member central banks agreed to strengthen the format of the ACBF in order

Efforts to strengthen regional co-operation intensified in 2001. Significant progress was made in the implementation of the Chiang Mai Initiative and work had started on enhancing the effectiveness of regional economic reviews and policy dialogue.

to further enhance the peer review process and encourage frank exchange of views among the members.

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### ASEAN Central Bank Forum (ACBF) Meetings in 2001

- I. 8th ACBF, 3 April 2001, Kuala Lumpur, Malaysia
- II. 9th ACBF, 13 September 2001, Kuala Lumpur, Malaysia

#### Issues Discussed:

- **Peer Review:** Members discussed extensively the implications of the global economic slowdown for the ASEAN countries and exchanged views on the policy responses adopted by member countries to mitigate the consequent adverse effects. It was agreed that strengthening domestic demand was critical in mitigating the effects of the slowdown in external demand on the region’s economic growth. Members also agreed that it was important to maintain exchange rate and financial stability in the region, and to strengthen financial and corporate sector restructuring.
- **Bilateral Swap Arrangements (BSA) under the Chiang Mai Initiative:** Members discussed the progress of the implementation of the BSA.
- **Proposed Modalities to Enhance Regional Economic Reviews and Policy Dialogues:** Members exchanged views on proposed ways to enhance existing economic reviews and policy dialogues among the ASEAN+3 countries.
- **ASEAN Common Currency and Exchange Rate Mechanism:** Members discussed the report presented by the Chairman of the ASEAN Currency and Exchange Rate Mechanism Task Force, and agreed that the Task Force should analyse the costs and benefits of having a common currency in ASEAN, and identify measures that would need to be undertaken for the common currency arrangement to be feasible.
- **ASEAN Central Bank Governors’ Conference:** Members discussed the proposal to hold an annual ASEAN Central Bank Governors’ Conference to complement the ACBF. The Conference would provide a forum for the Governors to exchange views on recent economic and financial developments in the region as well as to identify possible areas for co-operation among the ASEAN central banks. A consensus was reached to hold the first Governors’ Conference tentatively in June 2002.

BNM, as the chair of the ASEAN Currency and Exchange Rate Mechanism Task Force, organised a seminar on “Common Currency Arrangements and Exchange Rate Mechanisms in ASEAN” in Kuala Lumpur on 6-7 August 2001, as well as hosted the inaugural meeting of the Task Force on 8 August 2001. The seminar provided an opportunity for participants to hear the views of experts on the preconditions, costs and benefits of common currency arrangements. The inaugural meeting of the Task Force agreed that the work of the Task Force would focus on identifying the costs, benefits and feasibility of having a common currency arrangement in ASEAN.

Another important development in ASEAN financial co-operation in 2001 was the finalisation of the memorandum of understanding to establish the ASEAN Insurance Training and Research Institute (AITRI) in Malaysia as the ASEAN network centre for insurance education and research. Initially, the operations of the

AITRI would be co-ordinated by the Malaysian Insurance Institute. On 8 April 2001, the ASEAN Finance Ministers signed the “Protocol to Establish an ASEAN Scheme of Compulsory Motor Vehicle Insurance”. The implementation of the Protocol represents the first step towards the establishment of an insurance scheme within ASEAN which would facilitate the movement of goods among the ASEAN countries by reducing delays in cross-border crossings.

#### **ASEAN+3 Financial Co-operation**

During 2001, significant progress was made in the implementation of the Chiang Mai Initiative (CMI), which was launched by the ASEAN Finance Ministers and their counterparts from the People’s Republic of China, Japan and Korea (that is, the ASEAN+3 Finance Ministers) on 6 May 2000.

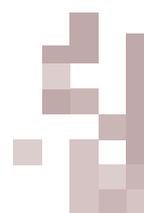
BNM entered into two Bilateral Swap Arrangements (BSA) with the Bank of Japan, acting on behalf of the

#### **ASEAN and ASEAN+3 Finance Ministers’ Meetings in 2001**

- I. 5th AFMM, 7-8 April 2001, Kuala Lumpur, Malaysia
- II. AFMM+3, 9 May 2001, Honolulu, United States of America

##### **Issues Discussed:**

- **Peer Review:** Ministers noted the deterioration in the global economic outlook and pre-emptive measures taken by some of the member countries to alleviate the effects of lower external demand. Ministers agreed on the need to continue with financial and corporate sector restructuring, as well as to promote robust and strong financial systems to better withstand external shocks. Ministers also agreed to have closer policy dialogues and strengthen regional co-operation in the areas of monitoring capital flows, support mechanisms, and international financial reforms.
- **ASEAN Finance Co-operation:** Ministers welcomed progress made in implementing the ASEAN Finance Work Programme, including in the areas of strengthening the financial system, capital market development and liberalisation of the financial sector under AFAS.
- **East Asia Finance Co-operation:** Ministers noted the progress of the implementation of the BSA under the CMI and agreed to review the main principles of the BSA in three years, taking into account the actual operation of the BSA and other relevant factors.
- **Study Group to Enhance the Effectiveness of Economic Reviews and Policy Dialogues:** Ministers agreed to establish an ASEAN+3 Study Group to enhance the effectiveness of economic reviews and policy dialogues among the ASEAN+3 countries.
- **Monitoring of Capital Flows:** Ministers agreed to engage in regular exchange of information on short-term capital flows. In this connection, member countries agreed to exchange information on capital flows using an agreed format on a voluntary basis.
- **International Financial Architecture:** Ministers noted the latest developments in the G-7, G-20 and the FSF in 2001.



Ministry of Finance, Japan, on 5 October 2001. The agreements comprised a new US\$1 billion BSA under the CMI and the renewal of the existing swap arrangement of US\$2.5 billion under the New Miyazawa Initiative (NMI). These agreements are for a period of three years.

Regionally, Japan has also entered into a swap arrangement of US\$2 billion with Korea on 4 July 2001. This was in addition to their existing US\$5 billion swap arrangement with Korea under the NMI. Japan has also signed swap agreements with Thailand amounting to US\$3 billion on 30 July 2001, and with the Philippines also for US\$3 billion on 27 August 2001. Thailand and the People's Republic of China concluded an agreement for a swap arrangement of US\$2 billion on 6 December 2001.

Another important milestone in the area of regional financial co-operation was the establishment of an "ASEAN+3 Study Group to Examine Ways of Enhancing the Effectiveness of Economic Reviews and Policy Dialogues" by the ASEAN+3 Finance Ministers at their meeting in Honolulu on 9 May 2001. The task of the Study Group was to examine ways to further enhance the effectiveness of economic reviews and policy dialogues among the ASEAN+3 countries. Enhanced reviews and policy dialogues, encompassing peer review, would aid in identifying emerging issues and potential problems, and thus enable authorities to take prompt corrective and pre-emptive policy actions and minimise the risk of contagion. In addition, an enhanced regional policy dialogue process would also promote sound macroeconomic policies and address any moral hazard problem that might arise in implementing the CMI. The Study Group was co-chaired by Japan and Malaysia, and comprised senior officials from finance ministries and central banks of the ASEAN+3 countries. The First Meeting of the Study Group was held in Kuala Lumpur on 22 November 2001. The Meeting discussed the possible modalities to enhance regional economic reviews and policy dialogues as proposed by Japan and BNM.

### **SEACEN**

During the Thirty-sixth Conference of Governors of South-East Asian Central Banks (SEACEN), which was held in Singapore on 1-2 June 2001, Governors shared their countries' experiences in maintaining financial stability. Discussions ranged from the issue of exchange rate management to upgrading supervisory capabilities and framework; and the implementation of the New Basel Capital Accord.

A significant activity undertaken by the SEACEN Research and Training Centre (SEACEN Centre) was the completion and submission of the SEACEN Strategic Review to the SEACEN Board of Governors in June 2001. The Board of Governors deliberated on the Review's recommendations on the structure, resources and mode of operation of the SEACEN Centre. The proposed changes were aimed at ensuring the Centre's relevance in enhancing the skills capacity of its members to meet the challenges of globalisation and strengthening its role as a unique and reputable training and research institute in the region. In this regard, the Governors agreed in principle to the proposals to realign and give greater focus to the Centre's activities and organisational structure. An immediate enhancement of the governing structure of the SEACEN Centre was the establishment of an Executive Committee comprising the Deputy Governors of member central banks. The new governance structure would enable the Board of Governors to delegate the responsibility for the management and oversight of the SEACEN Centre's operations, such as its annual work programme and budget to the Executive Committee. This would allow the Board of Governors, which remained the highest policy-making body of the SEACEN Centre, to focus on deliberations on key issues in monetary and financial policies.

To upgrade the quality of its training programmes, SEACEN continued to strengthen its strategic alliances with international financial institutions such as the IMF, BIS and the Toronto Centre. The Centre's financial resources were augmented by the Bank of Japan's pledge to provide financing for five SEACEN training events a year as agreed by the Bank of Japan. During the SEACEN Centre's operating year 2001/2002, BNM hosted two training activities, namely the Workshop on Communication Strategy for Monetary Policy (19-21 February 2002) and the SEACEN-Toronto Centre Leadership Seminar for Senior Management of Central Banks on Financial System Oversight (18-22 March 2002).

The SEACEN Expert Group on Capital Flows (SEG) made further progress in developing a regional framework to promote information sharing on capital flows among its members. At its third meeting which was held in Kuala Lumpur on 3-4 May 2001, members agreed to provide information, based on a common set of data templates, which sought to address current gaps in data on capital flows. The data would be shared via a secure electronic data exchange facility at the SEACEN Centre. During the meeting, members exchanged country experiences on

the risk management of capital flows. In addition, a half-day workshop on managing risks associated with capital flows was held, with presentations by the World Bank and the private sector. Going forward, the SEG would commence work on the second objective of drawing up concrete and practical proposals that members could implement individually or collectively to enhance the risk management of volatile capital flows.

Under the SEACEN Trust Fund (STF) Grant and Scholarship Scheme, four scholarships were awarded to eligible member countries, while one was awarded to a SEACEN observer central bank. The Scheme, which began in 1993, provided financial assistance to eligible member and observer central bank officers to attend training programmes conducted by the SEACEN Centre.

#### **EMEAP**

The Executive Meeting of East Asia and Pacific (EMEAP) Central Banks continued to be an important forum for monetary and financial co-operation among central banks and monetary authorities in the East Asia and Pacific region. During the year, the EMEAP Deputies held their bi-annual meetings in Beijing on 26 March, and in Auckland on 3 December. The 6th Annual Governors' Meeting was held in Sydney on 7 July 2001. EMEAP, through the activities of its three working

2001, comprising all Governors of the EMEAP central banks in the BIS, including Malaysia. The ACC provides a vehicle for communication between the Asian and Pacific members of the BIS and the Board and Management of the BIS on matters of interest and concern to the Asian central banking community. Its inaugural meeting was held in Basel in June 2001.

#### **Manila Framework Group**

The Manila Framework Group (MFG) of Finance and Central Bank Deputies met twice in 2001, in Beijing on 27-28 March, and in Auckland on 4-5 December, to review economic developments in the Asia-Pacific region and discuss relevant policy issues. On regional surveillance, the Group recognised that the prevailing weak global economy had heightened the need for members to maintain supportive macroeconomic policies and strong structural policies to facilitate a return to growth, stability and poverty reduction. In view of the events of 11 September, the Group agreed to support the Group of 20 Action Plan on Terrorist Financing and committed to implement steps in the Plan by February 2002.

The Group also discussed the report of the Task Force of the MFG Financing Arrangement, with emphasis on the possible principles to govern the operation of a co-operative financing arrangement, as proposed in

Discussions at the regional level (EMEAP, APEC, MFG and the ACC of the BIS) focused on macroeconomic policy options to manage the global economic slowdown. Collaborative work by working groups contributed to domestic capacity building among members.

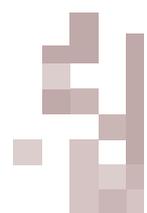
groups, contributed to capacity building among member central banks. The Working Group on Payment and Settlement Systems focused on ways to reduce foreign exchange settlement risk in the EMEAP region. The Working Group on Banking Supervision focused mainly on the proposed new Basle Accord. Meanwhile, the Working Group on Financial Markets continued to discuss the development of the continuous-linked settlement system for foreign exchange and its implications for central bank market operations and reserves management in the region. The major themes in EMEAP's discussions in 2001 included promoting financial stability; focusing on progress and challenges; and asset prices and central bank policy.

A related development was the establishment of the Asian Consultative Council (ACC) of the BIS in March

the Manila Framework in 1997. The Group agreed that any MFG financing arrangement would involve bilateral financing in support of IMF programmes on a case-by-case basis and that participation would be voluntary. These issues would be revisited by the Group to ensure its continued suitability to members of the Group in terms of principles and modalities governing the financing arrangement.

#### **Asia-Pacific Economic Co-operation**

Under the theme "Growth with Restructuring, Stability and Equity", the Finance Ministers of APEC met in Suzhou, People's Republic of China on 8-9 September 2001 and focused their attention on the policy challenges faced by APEC economies in promoting sustainable economic growth and financial stability in the region. Finance Ministers



## APEC Meetings in 2001

- I. APEC Finance and Central Bank Deputies' Meeting, 1 May, Washington D.C., United States of America 6-7 September, Suzhou, People's Republic of China
- II. 8th APEC Finance Ministers' Meeting, 8-9 September, Suzhou, People's Republic of China

### Issues Discussed

- **Macroeconomic Challenges and Policy Responses**

In view of the less favourable global economic environment, APEC stressed the importance for the international community to take the appropriate policy actions to facilitate an early recovery in global economic activities. APEC affirmed its commitment to enhance macroeconomic policy dialogue and co-operation in managing the economic difficulties faced by member economies and to build a strong foundation for sustained and broad-based growth in the region. In addition, APEC emphasised the importance of continuing domestic structural reforms to enhance the ability to respond to economic and financial shocks.

On the trends in globalisation, APEC stressed the need for appropriate policies and framework to be in place to enable all member economies to benefit from the process of increased economic and financial integration.

- **Strengthening the International Financial System**

APEC welcomed current steps taken to reform the IFA and urged continued implementation of the reforms. Although APEC endorsed the implementation of international standards and codes, it was emphasised that the implementation and assessment of compliance with these standards and codes need to take into account individual country circumstances and institutional capacity.

agreed that wide-ranging structural reforms were essential to strengthen the foundation for macroeconomic stability and sustainable improvement in living standards. APEC members also maintained their collaborative efforts under various APEC initiatives during the year. In addition, to ensure that APEC kept abreast with emerging economic and financial challenges, Ministers also endorsed the Strategic Review of the APEC Finance Ministers' Process. The Strategic Review provided a new framework that would anchor the work undertaken in the finance process so as to complement APEC's overall vision. The new framework took into consideration APEC's unique characteristics, comparative advantages and limitations, such as the diversity of APEC's membership, voluntary nature of economies' involvement and limitations on resources to develop policy initiatives.

As part of the collaborative effort, BNM continued to participate in APEC work programmes conducted under the various initiatives. These work programmes included core group activities; policy dialogues; and training programmes. In this regard, BNM participated in policy dialogues on banking supervision; and bank

failure management; as well as in training programmes organised under the Financial Regulators' Training Initiative. BNM also participated in the APEC Working Group on Electronic Financial Transactions Systems and the Working Group on Fighting Financial Crimes.

### Group of 15

The 11th Summit of the Heads of State and Government of the Group of 15 (G-15) was held in Jakarta, Indonesia on 30-31 May 2001. At the Summit, members expressed concern over the lack of progress in IFA reforms, which was vital in effectively addressing the risks and challenges posed by globalisation. In order to sustain and accelerate the reform effort, G-15 members agreed with Malaysia's proposal to establish an Expert Group on the Reform of the IFA. The Expert Group had been tasked to assess the progress of the current work on IFA reform, and make recommendations to address the concerns and interests of developing countries, particularly that of the G-15. The establishment of the Expert Group would serve as a means by which the views of the G-15 members would be presented at the various

international fora. The Expert Group held its meeting in Kuala Lumpur on 26 February 2002.

### Asia-Europe Meeting

Subsequent to the 3rd Asia-Europe Meeting (ASEM) Finance Ministers' Meeting which was held in Japan in January 2001, an ASEM Core Group Meeting was held in Washington D.C., United States on 13-14 April 2001. During the meeting, ASEM members reviewed the progress of on-going ASEM activities such as the Kobe Research Project, ASEM Trust Fund II and ASEM Anti-Money Laundering Initiative. In addition, ASEM members were updated on recent initiatives in regional co-operation in Asia and Europe. On the progress of regional co-operation in Asia, Malaysia updated ASEM members on the status of the CMI, that consisted of the expanded ASEAN Swap Arrangement and the Bilateral Swap Arrangement. Malaysia also informed the Meeting on developments in the ASEAN surveillance process. The next ASEM Finance Ministers' Meeting is scheduled to be held in Copenhagen, Denmark on 5-6 July 2002. The ASEM Leaders' Summit, which is held on a biennial basis, will also take place in Copenhagen, Denmark on 22-24 September 2002.

### Asia/Pacific Group on Money Laundering

International initiatives against money laundering, which were started more than a decade ago by international bodies and task forces, have intensified in recent months. In 2001, efforts to combat money laundering were stepped up after the 11 September 2001 events. Malaysia has actively supported regional and international efforts in fighting money laundering. Malaysia enacted the Anti-Money Laundering Act 2001, which came into force on 15 January 2002. The initiative to put this Act in place commenced with the formulation of the concept paper in October 2000, and the Act was gazetted as law on 5 July 2001. The Act criminalises money laundering and provides for related enforcement powers; imposes customer identification, record-keeping and reporting requirements; and mandates the competent authority to receive, analyse and disseminate financial intelligence relating to money laundering activities. For the purpose of carrying out its functions under the Act, BNM has established a new department in 2001 called the Financial Intelligence Unit to implement measures for the prevention and detection of money laundering.

Malaysia became a member of the Asia/Pacific Group on Money Laundering (APG) on 31 May 2000. The APG was formally established in February 1997 at the

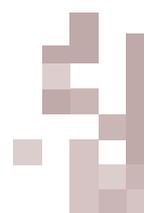
4th Asia/Pacific Money Laundering Symposium in Bangkok. The APG Secretariat is based in Sydney. Its mission is "to provide a co-operative regional solution to the global problem of money laundering". The APG's principal strategy is to facilitate the adoption, implementation and enforcement of internationally accepted anti-money laundering standards in the legal, financial and law enforcement sectors and to use mutual evaluations to encourage member compliance.

Malaysia together with Australia are the current co-chairs of the APG. The co-chair arrangement is for a 2-year period, ending in mid-2002. BNM was the lead agency representing Malaysia at the APG, and as co-chair, assisted the APG Secretariat in preparing for its meetings. During the year, BNM was involved in organising the 4th APG Annual General Meeting in Kuala Lumpur (22-24 May 2001). The meeting was the largest APG meeting held to-date, attracting more than 200 attendees, representing 38 jurisdictions, and 13 international and regional bodies. Three new jurisdictions, namely, the Cook Islands, Macau and Niue, were admitted as APG members at the meeting, bringing the APG's total membership to 22. The APG also included eight observer jurisdictions. The 4th APG meeting discussed:

- Four mutual evaluation reports on member jurisdictions;
- Current and future typologies workshops on money laundering methods and counter measures;
- International and regional co-operation; and
- Global anti-money laundering initiatives.

In accordance with the APG membership, member jurisdictions commit themselves to participate in mutual evaluations. The mutual evaluation process gives recognition when standard benchmarks are met, and identifies the areas for improvement. Malaysia was evaluated by the APG during the year. The APG and the Offshore Group of Banking Supervisors jointly evaluated the Labuan IOFC separately as an offshore regime (2-6 April 2001). The APG also evaluated Malaysia's anti-money laundering programme on 9-12 July 2001. The evaluators met the various government agencies and financial institutions in Malaysia during their mission. The mutual evaluation report on Malaysia will be presented for discussion and acceptance at the 5th APG Annual Meeting in June 2002.

During the year, Malaysia participated in the APG's Mutual Evaluation Training Workshop in Bangkok and the Money Laundering Methods Typologies



Workshop in Singapore. Malaysia also became a member of the APG Working Group on Information Sharing. The primary objective of this Working Group was to make recommendations for improving the efficiency and effectiveness of information sharing between jurisdictions, in terms of accuracy, timeliness and reciprocity.

## **BILATERAL CO-OPERATION**

### **Bilateral Payments Arrangement**

During the year, BNM continued to promote the Bilateral Payments Arrangement (BPA) as part of Malaysia's effort to diversify its export markets and to enhance bilateral trade with other developing countries.

BNM also participated in a review on the Palm Oil Credit and Payments Arrangement (POCPA), which was under the purview of the Ministry of Primary Industries. The review was conducted in the wake of an over-supply situation in the palm oil industry, which resulted in historically low prices for palm oil. To promote the POCPA scheme, the counter trade arrangement was introduced as an alternative to cash settlement. In addition, the new POCPA credit would be offered on a revolving basis for three years, during which the recipient country could roll over the credit upon repayment within a stipulated period of time.

### **BNM Technical Assistance and Information Exchange**

In 2001, BNM continued to actively promote closer co-operation with other central banks and monetary authorities, as well as with foreign public and private sector institutions in line with the Bank's policy to share its experience and interact with interested parties.

During the year, BNM received 58 foreign delegations for **discussions, study visits and attachment programmes**. The delegations were from the central banks, government agencies and other public and private sector organisations of Africa, Asia, Europe, North America and Oceania. Interest was focused on various aspects of central banking, including investment and treasury operations,

payment system, monetary and financial policy, bank regulation, bank supervision, information technology, exchange control, currency management and operations, human resource management and training and Islamic banking.

In May 2001, BNM launched a two-year Technical and Training Arrangement Programme, at the request of the State Bank of Pakistan. Funding for the programme was provided by the Asian Development Bank. The programme included an attachment arrangement for officials of the State Bank of Pakistan in Kuala Lumpur.

Sixteen participants from the central banks of the African, Asian, European and North American continents joined mid-level BNM officers for the **20th Central Banking Course** conducted by BNM in Kuala Lumpur on 10-29 September 2001. Financing for the participants was provided under the Malaysian Technical Co-operation Programme. To date, a total of 166 participants from 64 foreign central banks had attended this programme. The course, covering topics such as monetary and financial policy formulation and the role of the central bank in regulating the financial system, was structured to prepare officers for their career as central bankers. At the end of the programme, participants are expected to have gained a broader perspective beyond their own areas of work.

In 2001, BNM hosted three **annual bilateral meetings** in Kuala Lumpur, with the Bank of Thailand, the Hong Kong Monetary Authority and the Monetary Authority of Singapore. These bilateral meetings were considered important as they provided an opportunity for an exchange of views and sharing of experiences at a closer level. The meetings contributed to the strengthening of co-operation and ties between BNM and the other central banks. Among the issues discussed at these meetings were the implications of the recent global economic developments; policy strategies and common risks in macro-economic management; exchange rate developments; performance of the banking system; and risk management.