

Financial Crises: A cyclical event



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Change in Economy Condition is a cyclical event – the Kondratieff Theory

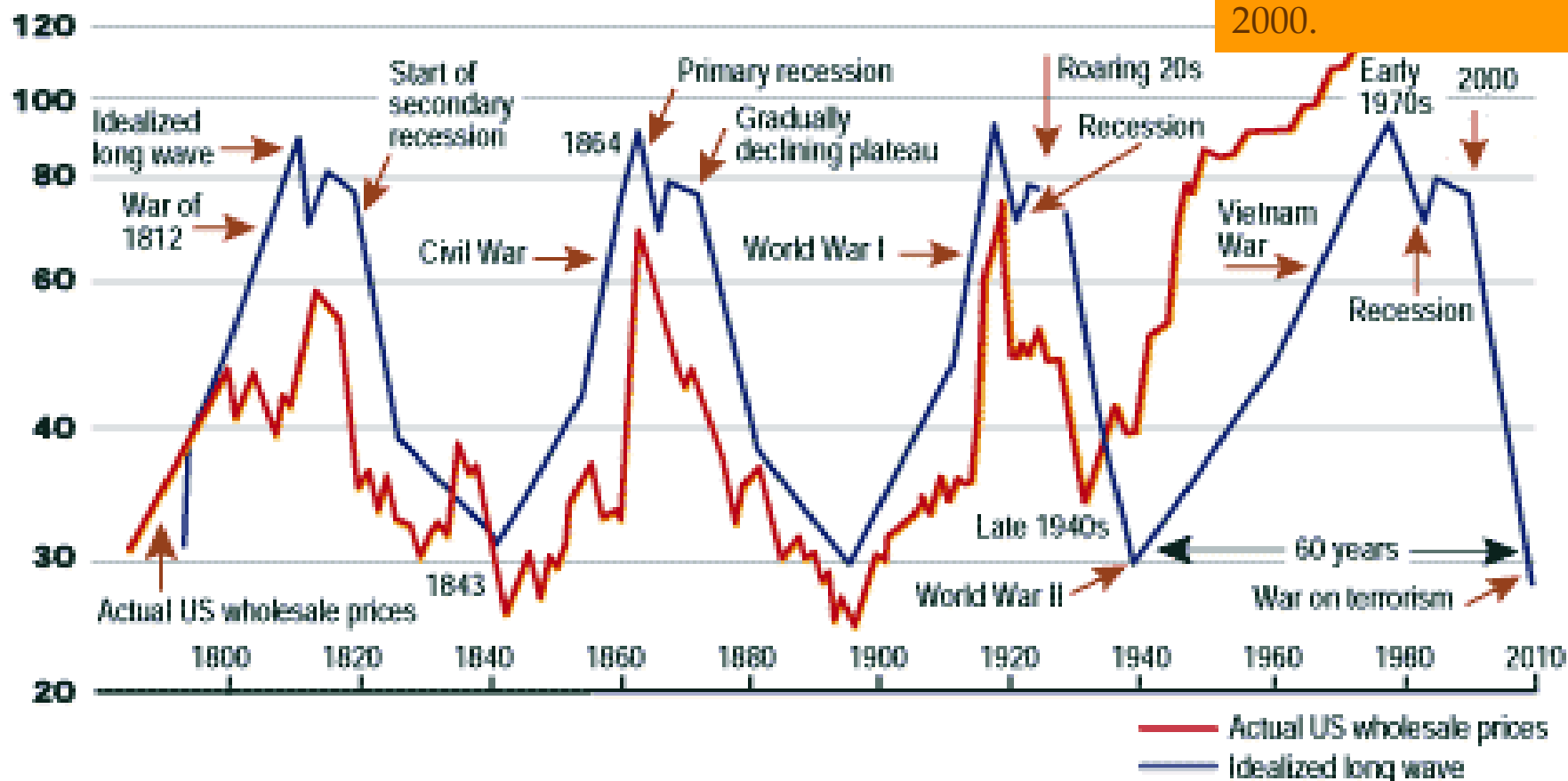


US Economy

- An empirical evidence based on the Kondratieff Theory

Based on the idealised long wave, down turn is anticipated, starting with dot.com crash in 2000.

The Kondratieff Wave



Similarly, Malaysian market has gone through similar cyclical ups and downs

KLCI Index (pts)



Notable financial crises: a historical perspective

Overend & Gurney, 1866

- Overend & Gurney was a key London discount bank, which provided funding for commercial and retail banks. After its bankruptcy, many smaller banks were unable to get funds and went under, even though they were otherwise solvent.
- The doctrine of central bank to act as lender of last resort to provide liquidity to the financial system during crises was introduced after this crisis.

Barings, 1890

- The new doctrine of lender of last resort was implemented by Bank of England to prevent a systemic collapse of UK banking system when Baring made a huge investment loss in Argentina.

Notable financial crises: a historical perspective

The Crash and Great Depression, 1929

- The Wall Street crash of Black Thursday in 1929 led US into Great Depression.
- This crisis resulted in creation of the US Securities and Exchange Commission, the Federal Deposit Insurance Corporation and the separation of commercial and retail banking activities through the Glass-Steagall Act.

US Savings and Loan Scandal, 1980s

- Deregulation in the 1980s led to Savings and Loans institutions (S&Ls) to expose to complex and unwise financial transactions. This resulted in many of them went into bankruptcy. As the individual deposits in the S&Ls are guaranteed by the government, it created a huge financial liability (\$150 bil) to the US government.
- Nevertheless, this crisis strengthened the bigger banks as their weaker competitors were eliminated and this laid the waves of mergers and consolidations in the banking sector in the 1990s.

Notable financial crises: a historical perspective

The Crash of 1987

- US stock markets suffered the largest peacetime one-day fall on 19 October 1987 when the DJIA index dropped 22% and European and Japanese markets followed suit.
- Circuit breakers were introduced to minimise impact of excessive trading.

Asian financial crisis, 1997/98

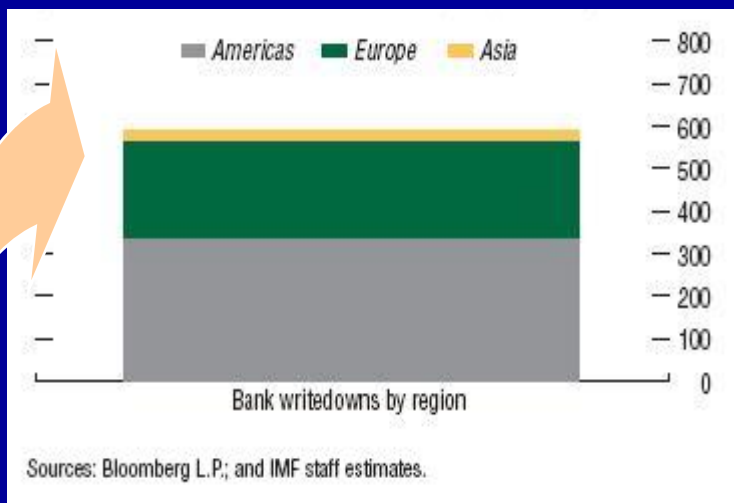
- The collapse of Thai baht triggered the financial crisis and spread to Malaysia, Indonesia and South Korea.
- Nervous investors moved USD100 bil out of the region during the crisis, about 5% of the region's GDP.

Dot.com Bubble, 2000

- The rise of internet companies led to keen interest of investors in such stocks, despite not having adequate profit track record.
- The Bubble eventual burst and technology weighted Nasdaq index fell by 78%.

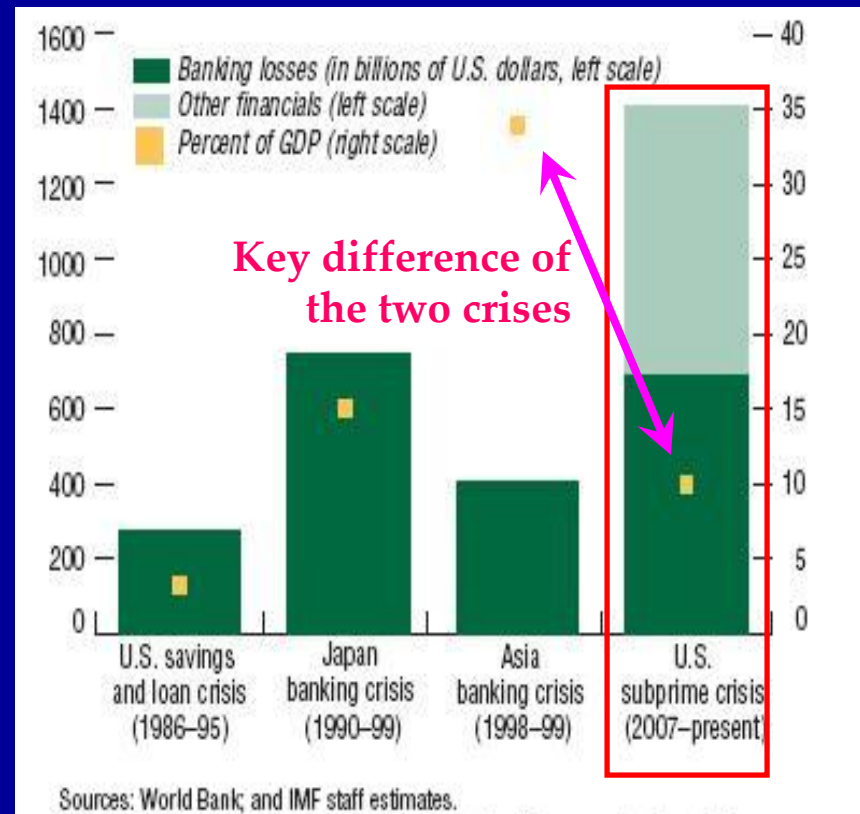
The emergence of sub-prime crisis continues to affect the global economies – the exposures are larger than the Asian crisis and spillover effects could be wide spread

Financial Sector Losses
(in USD'bil – Q2 2007 to August 2008)



Asia's exposure is limited

Comparison of Financial Crisis



Many of the measures being taken globally now are similar to those Malaysia took in response to 1997-98 crisis

- **Recapitalisation and restructuring**
 - National Asset Management Company (Danaharta) and CDRC to restructure
 - Danamodal to recapitalise
- **Comprehensive corporate governance reforms**
 - High Level Finance Committee (HLFC) on Corporate Governance in 1998
- **Enhancing investor protection and regulatory supervision**
 - Changes to the law to strengthen enforcement and oversight powers
- **Consolidation and strengthening of domestic capital market intermediaries and financial institutions**
- **Diversification of sources of financing, investment channels and investor base**
 - Domestic bond market development
 - Growth of unit-trust industry
 - Greater role of institutional investors
- **Clear strategic policy direction for capital and financial markets**
 - Capital Market Masterplan
 - Financial Sector Masterplan