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REPLACE BLANKET SUBSIDY WITH TARGETED AID, USING DIGITAL SOLUTION

Some startling facts have emerged from the government's subsidy of some food essentials. Malaysia is the only country in the region where the government subsidises chicken and egg producers. The other countries do have subsidy schemes for selected essentials but they do not cover chicken and eggs.

Second, not all Malaysian companies are suffering losses like the sugar refineries. The companies dealing with chicken and eggs are making more money compared with pre-Covid 19 days. Companies producing edible cooking oil are also making decent profits.

The higher profits are coming in despite increases in the price of raw materials, thanks in part to subsidies from the government, higher average selling prices and increased volume.

Prices of corn and soybean, two ingredients vital for the production of feedstock for livestock, have gone up by more than 50% in the last 18 months. But the latest results from companies selling eggs and livestock show that their bottom lines are increasing owing to higher demand.

The question that arises is whether these companies would continue to remain profitable and to supply their produce to the domestic market without government subsidies.

Nobody would be able to answer that question easily.

But try asking any company operating poultry farms or processing cooking oil and the feedback is that without the government subsidies, the supply situation would change. The reason is primarily price controls.



ALTERNATIVE
views

BY
M SHANMUGAM

Price controls do not allow the price of the end product to reflect the actual cost of production. Hence, products become unprofitable to produce and smaller and less efficient producers are forced to shut down operations. For instance, chicken and egg producers would shut production if they are unable to make a profit.

Those who remain in business with restrictions such as price controls will tend to export their products to neighbouring countries where prices are higher.

The government's subsidy and social assistance bill has shot up significantly since 2021. That year, the amount allocated from the budget was RM23 billion. The following year, when prices of food commodities and energy had risen significantly, subsidies and financial assistance jumped almost threefold to RM68 billion.

This year, according to the Budget 2023 retabled by Prime Minister Datuk Seri Anwar Ibrahim, the amount allocated for subsidies and social assistance is RM59 billion. It makes up about 20% of federal government expenditure.

Surely, some of the government spending is going to the companies producing food items that are being subsidised.

The companies cannot be blamed for making more money in the midst of the government's efforts to keep prices artificially low. They are in business to make profits and pay taxes on their gains. They are not in business to do national service.

The problem lies with the subsidy system that is in place, together with price controls.

It is not only food items that have a price con-

trol mechanism. Electricity and petrol are also subsidised. While everyone benefits from the lower prices, the companies in the business of supplying the items are seeing improved profits because of the inefficient subsidy system.

Which is why the government has made it a priority to implement targeted subsidies to replace the existing system of blanket subsidies that benefit all sections of the population.

It is starting with removing the subsidy on electricity for households that are in the top-20 category of income earners. Typically, these are households that have a total income of more than RM10,000 per month.

Prime Minister Datuk Seri Anwar Ibrahim has been talking about targeted subsidies since he took the helm last November. He is not the first person to broach the subject. It has been talked about for at least 10 years.

In 2014, there were several proposals on implementing targeted subsidies for fuel. It was reported that the Economic Council then had evaluated a proposal by a consortium comprising Fuelsubs House Sdn Bhd (FSH), Datasonic Bhd and Pos Malaysia Bhd.

Datasonic and the principal figure behind FSH have cropped up in recent high-profile court cases. A subsidiary of Datasonic was named as having dealings with Datuk Seri Ahmad Zahid Hamidi during his corruption trial. However, Datasonic had denied that it had paid Zahid any money. FSH is a private company with Tan Sri Habibul Rahman Kadir Shah as its managing director. During Datuk Seri Najib Razak's SRC trial, Habibul Rahman said that he had been



ZAHID IZZANI/THE EDGE

Malaysia is the only country in the region where the government subsidises chicken and egg producers. These producers are doing better thanks in part to the subsidies, higher average selling prices and increased volume.

paid for collecting “intelligence” for the former prime minister.

It was reported that the government had evaluated several proposals before deciding on the solution offered by the consortium. However, the proposal did not take off.

Most of the proposals on implementing the targeted fuel subsidy used MyKad as a digital infrastructure to identify citizens and assess their risk profile.

In fact, the MyKad is already being successfully used by non-profit organisation MyKasih Foundation to channel aid to impoverished families and students. Beneficiaries use their MyKad to purchase food items in selected stores and fill up petrol. They cannot purchase cigarettes or alcohol.

Even in countries with large populations, digital identification cards are used to channel assistance to the poor so as to minimise leakage. In India, the government launched the Aadhaar card system in 2012 to channel benefits to the population amid opposition from some quarters who contend that the system compromises their personal data. The Aadhaar card system is used to channel food items including rice and flour, and kerosene, among others.

Anwar’s government has no choice but to do away with the current system of blanket subsidies. The sooner it is done, the better it will be for him to reform public finances and reduce the fiscal deficit.

The current system has its shortcomings, as evident from the growing profits of some companies providing subsidised food items. ■

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Is de-dollarisation an inevitable trend?

Where are US markets going? Specifically, will the dollar continue to be strong?

JP Morgan FX strategists recently highlighted the observation that de-dollarisation seems to be a trend, since central bank holdings of US dollars had slid from 71% of total global official reserves in 2000 to a historic low of 58%. The US remains the world’s largest economic, financial and military power, but in the last two decades, the rest of the world has other ideas about a multipolar order.

The big issue has been the rise of China, replacing Japan as the world’s second largest economy at the end of 2000, when its gross domestic product (GDP) was about half the size of that of the US. Today, Japan has retreated to roughly one-third of US GDP, whereas China has grown to between two-thirds and 80% of the American economy in terms of market GDP or net wealth.

The global economy is now roughly divided into three geopolitical regions: North America, Asia and Europe. According to International Monetary Fund (IMF) numbers, the North American core centred on the US, which has a nominal GDP of US\$25.5 trillion, compared with China (US\$18.5 trillion) and the European Union (US\$16.6 trillion).

In the post-war era, the dollar emerged as the main reserve currency, since it is used for invoicing the major commodities such as oil, and as a store of value. The dollar is superior as a cross-border currency because anyone investing in dollar assets would have superior return on equity (ROE), excellent market liquidity with low transaction costs and lowest risks, since US Treasuries are considered the ultimate benchmark financial asset.

Asset managers know from experience that in the last four decades the ROE and liquidity on a dollar-denominated portfolio of 60% equity and 40% bonds would generally outperform similar foreign currency portfolios. This is owing to the superior equity performance of US stocks over European, Japanese and Chinese peers.

Central banks are heavily invested in US Treasury bonds, which made up a significant part of the US\$7.3 trillion in foreign ownership of US Federal debt at the end of 2022. Because the rest of the world wants to hold dollars to fund their trade and investments, external demand for dollars is higher than domestic demand. Effectively, the US can run a current account deficit with the rest of the world equivalent to the amount the rest is willing to hold in extra dollars.

This “exorbitant privilege” allows the US government to massively fund its expenses through external borrowing with no serious consequences to its credibility. However, running increasingly large fiscal and trade deficits, the US has accumulated US net foreign liabilities of over US\$16.1 trillion, which it was owing to the rest of the world at the end of 2022, becoming the largest global debtor. The balance is so large as to soak up the net international investment surplus of the top 10 countries and then some.

Dollar bulls claim there is no alternative. Trade is naturally dollar-denominated within the Americas but is also dominant in most of the world, including Asia where the dollar accounts for at least 74% of all export invoicing, according to the US Federal Reserve’s research for data from 1999 to 2019. Only in Europe is the dollar dethroned by the euro currency union.

Bank of International Settlements data suggests that about 60% of international and foreign currency deposits and loans are denominated in dollars, with the euro share at 20%. Consequently, the Fed fostered swap and repo lines with major central banks to ensure sufficient dollar funding is available through emergencies. These lines were heavily utilised during the 2008 global financial crisis and 2020 Covid-19 crisis.

The dominant position of the dollar is reinforced by the performance of the US stock market, which accounts for 38% of global market capitalisation, adding 8% relative to other markets. This is in no small part due to the attractiveness of US technology and services companies that offer high earnings growth. To borrow a metric often referenced by Warren Buffett — the worth of the US stock markets has exceeded the country’s GDP by about 54%. By comparison, China’s stock market capitalisation was only 94% of its nominal GDP.

Despite being the second largest economy and largest trading partner with many countries, the renminbi



Convergence

BY ANDREW SHENG
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has not been able to achieve its fair share of currency trading. China has taken incremental steps to internationalise its currency with only modest gains. In China, the share of renminbi-based cross-border transactions exceeded dollar settlements for the first time in April of this year. However, the overall share of renminbi in global foreign currency trade volume remains under 10%. As long as exchange controls remain, it will be difficult for the renminbi to internationalise. For the foreseeable future, the US dollar will retain its unchallenged position.

Because the dollar hegemony wields considerable political power, in recent years, the currency has become weaponised in the form of sanctions. Since the 1990s, the US has been responsible for imposing two-thirds of the world’s sanctions and there are about 12,000 entities currently under restrictions. These sanctions have widened in scope and scale from addressing conflict (sanctions against Russia for its invasion of Ukraine) to industrial policy (containment of China’s technological development). By some estimates, 29% of global trade is under some form of sanctioning.

Sanctions can be a double-edged blade. When asked in the US Congress recently about the impact of sanctions on de-dollarisation, Treasury Secretary Janet Yellen said that the dollar, while “far and away the dominant reserve asset”, would gradually lose share as countries seek to diversify. Total foreign exchange reserves have increased 1.6 times from the end of 2008 to 2022, according to IMF data. Reserves in US dollars grew at a slower pace, up 1.4 times. Meanwhile, yen and sterling reserves grew 3.2 times and 2.1 times respectively, but amounted to less than one-fifth of total dollar reserves. Central banks have also looked to gold as an alternative, buying US\$70 billion’s worth last year, the most since 1950.

Increased trade barriers will exacerbate these trends by forcing countries to seek regional alternative arrangements. Asia’s aggregate GDP of US\$27.2 trillion has the economic heft to support a regional grouping that could finance trade with regional currencies rather than using the dollar. Europe has set the example, where 66% of export invoicing is euro-denominated, enabled by friendlier euro settlement and payment systems.

However, de-dollarisation does not mean that it would be replaced by any single currency. A pilot project for cross-border transactions by the central banks of China, Hong Kong SAR, Thailand and the United Arab Emirates is looking at a regional multi-currency environment with an eye to using central bank digital currencies (CBDCs). In other words, payment and settlement arrangements can use digital ways of netting and settlement, reducing the need to use dollars as an intermediating currency.

As leading dollar and trade economist Barry Eichengreen pointed out recently, “while there is evidence of a decline in the dollar’s share of allocated foreign exchange reserves, reports of its demise as the dominant global currency have been greatly exaggerated”. In other words, dollar dominance is not for others to erode, but for the US to lose through strategic blunders.

Yellen put it bluntly to Congress, that toying with defaulting on US government debt hurts the country’s global leadership and threatens the dollar’s credibility, which is entwined with the country’s creditworthiness. She warned American politicians that political brinkmanship “cannot be normalised as the way we do business in Washington”, reminding her audience that the US lost its AAA credit rating in 2011 due to fighting over raising the debt ceiling.

Thus, currency wars are, ultimately, high political drama. ■

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