Chairman's message

CHAIRMAN'S MESSAGE

The year 2007 proved to be challenging for the world's financial markets. Concerns over credit quality in the US subprime mortgage market quickly turned into a wholesale reappraisal of risk across financial markets. The resultant upheaval in credit and money markets, as investors fled to safe assets, soon gave way to contagion across other asset classes and bouts of equity market volatility that had not been seen for nearly a decade. But in spite of these concerns, the Malaysian capital market scaled new heights. The stock market surpassed many of its regional peers in terms of price performance, and experienced a significant rise in liquidity on the back of fair and orderly trading. The futures market also recorded strong gains while deepening considerably. The bond market, now Asia's fourth largest, saw record issuance and approvals of both ringgit and foreign-currency paper. These developments drove further growth in the unit trust industry, and a steady stream of innovation which included structured products and exchange-traded funds. Meanwhile, the Malaysian Islamic capital market continues to strengthen in terms of size and diversity of products.

The market's resilience and continuing growth reflect the strong foundations which have been built over the years. This has been important in instilling market confidence, and I welcome the clear affirmation of the market's strengths by various international organisations during the year. In its *Doing Business 2007* report, the World Bank ranked Malaysia fourth in the world for the quality of our investor protection; the Asia Pacific Group ranks us fifth worldwide for compliance with Financial Action Task Force standards on money-laundering and counter-terrorist financing; and Malaysia scored top marks for disclosure and transparency of accounting standards in the *Report on the Observance of Standards and Codes* by the World Bank. The market's international competitiveness was further underscored by PricewaterhouseCooper's review, which identified Malaysia as having recorded the third largest value of announced M&A deals in the Asia-Pacific ex-Japan (RM120 billion) after China and India, both economies many times the size of ours.

In 2007, we worked harder to reinforce these strengths, guided throughout by the clear vision set out by the *Capital Market Masterplan*: we continued to review and enhance the framework of regulation under which we and the market operate; we improved our capabilities and capacity for effective supervision, surveillance and enforcement; and we continued to introduce initiatives to improve the efficiency and competitiveness of Malaysia's capital markets.

Stronger Regulation

Over the past year, we introduced important changes to the regulatory framework targeted at key constituencies of the capital market. A major achievement was the *Capital Market and Services Act 2007*. The Act streamlines securities regulation, introduces a single licensing regime, facilitates the establishment of self-regulatory organisations, and strengthens investor protection. We also revised and updated the *Malaysian Code of Corporate Governance* to strengthen the role of independent directors in general, and of audit committees in particular.

The Code now requires all PLCs to carry out their own internal audits. The reporting line for internal auditors clearly holds the board accountable for ensuring that the internal audit process is effective. Audit committees have been strengthened: members must be non-executive and the majority must be independent; they must all be financially literate and one must be a qualified accountant – forming a nexus of continuous engagement between the company chairman, CEO, CFO, head of internal audit and external auditors. We also set in motion the establishment of an accounting oversight board, targeted at the accounting profession, to emphasise the significance of the role of auditors and audit quality in attesting and providing credibility to the financial statements prepared and verified by companies.

Tackling Market Abuse and Corporate Misconduct

We widened the scope of our financial and corporate surveillance, as well as the breadth of actions that we take against misconduct. These range from directing companies to restate and reissue their accounts and suspending auditors, to prosecuting company officials. We also expanded our principles-based approach into the area of supervision. This gives intermediaries the flexibility to innovate and compete without being hampered by unnecessary regulatory costs. At the same time, they have come under stronger oversight and made more accountable for their conduct.

We have taken a preventive approach to inculcate a strong compliance culture within the industry. For this, we actively engaged with directors, senior management and industry associations to ensure an effective application of regulatory requirements and responsibilities. We enhanced our inspection programmes using risk-based assessments on thematic and high risk areas to prevent possible market misconduct. During the year, we also stepped up our supervisory assessments of market participants by conducting a series of diligence reviews, surprise inspections, and routine risk-focused inspections of investment banks, stockbroking, and fund management companies. To reflect the growing importance of the investment management industry in our capital market, we established a specialised department to supervise the investment management industry with particular focus on the unit trust management and fund management companies.

As part of our drive towards improving the quality of our market and to ensure high standards of conduct, we have taken action where breaches of regulatory requirements were observed. Among the sanctions included substantial fines, reprimands and suspension from registering new dealer's representatives. To ensure we have relevant resources to monitor our increasingly sophisticated markets, we invested in state of the art surveillance systems and further enhanced the skills of our teams.

Tackling market abuse and corporate misconduct remains one of our highest priorities, and we continue to invest more in our capability to enforce the rules we set, to manage risks and to handle public complaints. In 2007, we adopted a new approach to enforcement that makes greater use of civil and administrative remedies to achieve a swift and fair resolution to cases. We actively applied the new approach: in 2007, we adopted pre-emptive measures to freeze assets and disgorge ill-gotten gains and make restitution. The following four cases alone involved a sum of over RM73 million covered by this new approach:

- In the case of Swisscash, we obtained a mareva injunction to prevent disposal of assets and secured an order to compel the return of RM35 million from 14 bank accounts in Hong Kong and Singapore. In Malaysia, 22 were also frozen. We facilitated a meeting of regulators from eight different countries in Hong Kong to trace fund transfers from bank accounts in one country to another;

- In the case of Ayer Molek Rubber Company, we obtained an injunction against RM20 million in proceeds from the company's sale of land;

- Investors in Powerhouse Asset Management Company received restitution worth RM10.9 million in total, and we filed a civil suit against the company and the fund manager for the shortfall of RM1.9 million; and

- We commenced a civil suit against the managing director of FTEC Resources for restitution of the RM2.5 million that he is charged with utilising for his own benefit.

Securities cases involving other jurisdictions highlighted the market's growing international linkages and the importance of cross-border co-operation with our counterparts. In 2007, the SC's strong standing in the international regulatory arena and our efforts in supervision and enforcement were recognised when we were admitted as a signatory to the

IOSCO Multilateral Memorandum of Understanding. The IOSCO MMOU is an international benchmark for co-operation and information sharing among leading global regulators for cross-border securities offences. The successful acceptance of the SC into this select group of regulators demonstrates our strong capacity in regulating the capital market.

The enforcement initiatives I have described are aimed at strengthening regulatory discipline. However, this is only one cornerstone of a "triangle of disciplines" that underpins a healthy and vibrant market. I am encouraged by signs that the other cornerstones, self discipline and market discipline, are also being strengthened. I especially welcome the growing efforts of independent directors to shoulder their responsibilities and blow the whistle on dishonest corporate officers. This self discipline, steeped in strong individual values, is the basis for fundamentally honest, decent boards, and top management who will not break the law and who will embed a culture that deters others from doing the same. I also wish to recognise the vigilance of others – including minority shareholders, auditors, and members of public and staff – who have contributed to the success of our enforcement work by coming forward with information on inappropriate corporate conduct.

Enhancing Quality of Listings

In terms of attracting foreign companies to make their primary or secondary listings in Malaysia, we see a window of opportunity in regional fund-raising. South-east Asian infrastructure funding requirements alone are estimated at US$150 billion over the next five years. Malaysia is in a good position to bridge this need.

First, we have a competitive market for initial public offerings: direct listing costs, including advisory fees, are low; the regulatory turnaround time is now comparable, if not faster, than other regional markets; and liquidity in Bursa Malaysia has improved considerably. Second, we continue to have a healthy market for IPOs, with strong interest on the part of issuers to access the market. There is also strong investor appetite to invest in these IPOs, judging from the oversubscription rate observed in 2007. And third, our stringent approach to vetting companies, mainly based on quality of governance, has led to higher quality of IPOs, translating into better returns for investors and the further strengthening of confidence. This is reflected in the higher net profits among the IPOs that have published their 2006 and 2007 accounts, while at the end of 2007, 63% of new IPOs for the year were trading above their IPO prices. Fourth, a high level of M&A activity goes hand-in-hand with a vibrant primary market, and we are seeing a healthy trend in M&A activities in Malaysia and the development of a Malaysian private equity industry.

Even so, we recognise that more can be done to make Bursa Malaysia a preferred listing destination for local companies, and to attract foreign companies to make their primary or secondary listings in Malaysia. We responded to these needs by freeing-up listing rules, wherever possible streamlining them with international practices, and by providing incentives to encourage M&A. Measures concerned with listing included allowing foreign companies to list their entire issued capital with full trading fungibility between Bursa Malaysia and other exchanges, and the introduction of a "greenshoe" option facility and price stabilisation mechanism for IPOs in line with international practices. Transparency is the key to instilling confidence in the fund-raising process and we will introduce a public exposure period for IPO prospectuses in 2008.

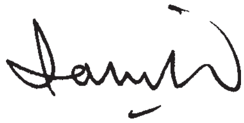
More Innovative and Efficient Intermediation

Our work involving the intermediation industry this year focused on bottlenecks in distribution and improving efficiency in general. We noted the experience of other markets, where deregulation and liberalisation helped to accelerate capital market growth by expanding the customer base. More open markets typically have a wider range of services, prices, and products of a higher quality. This year, we continued the process of liberalisation started in 2004 and welcomed two new foreign fund managers to our market. Further liberalisation was announced in Budget 2008 allowing for significant foreign participation to promote Malaysia's ICM as an international hub with three new stockbroking licences offered to facilitate business and order flows from the Middle East. We also raised permissible foreign ownership in fund management and REIT management companies to 70%. For the bond market, multilateral development banks and foreign multinational corporations may now issue both local and

To assess our performance, we undertook a feedback audit with internal and external stakeholders. The feedback was positive suggesting that the SC has been improving its perceived personality – in terms of professionalism and communication – with stakeholders and they are happy with our focus on investor protection and increased efficiency in processing applications. Following the feedback, a strategy was developed to enhance the SC name and the values that we want associated with our name. Internal alignment strategies are being rolled out.

Everyone's Contribution

We could not have fulfilled our regulatory and developmental mandate without the partnership of industry and all our stakeholders. I am grateful for the prompt response given to us whenever consultations are sought, resulting in a speedier delivery of results and services. Again, I would like to register my deep appreciation for my fellow Commission members, the Shariah Advisory Council members, and our management team. Without them, my journey through the many challenges of the year would have been difficult, if not impossible. I also want to say how proud I am of our staff who have worked hard and delivered on their job goals with much integrity and professionalism. To all who have contributed to our achievements in 2007, I thank you.



Zarinah Anwar