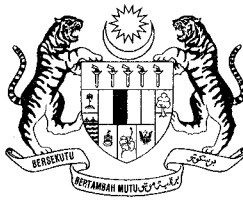


# Economic Report 1998/99

Ministry of Finance  
Malaysia



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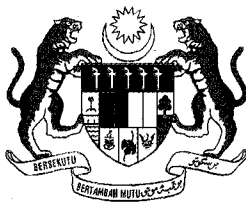


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## MINISTER OF FINANCE I MALAYSIA

### PREFACE

**M**ore than one year has passed since the onset of the Asian financial crisis. 1998 has been both difficult and challenging. We have witnessed Malaysia's real Gross Domestic Product declining sharply by 2.8% in the first quarter and 6.8% in the second quarter of 1998, after almost a decade of strong growth. As a nation, we have become impoverished by the ongoing crisis. The ringgit has depreciated significantly and now we have to pay 60% more for every one US dollar. At the same time, the KLSE has lost two third of its market capitalisation since the crisis began in June 1997, equivalent to 186% of 1998 GNP or two years of national income. We have therefore lost both in terms of income and wealth. Meanwhile, Government revenue has been adversely affected and the budget surplus we have enjoyed since 1993 has reverted to a budget deficit. The ramifications are bound to be severe if the real economy is left to contract under the continuing contagion effects of a volatile financial environment. This reaffirmed the Government's belief that Malaysia must act decisively to revitalise the economy whilst concurrently addressing the need to insulate it from the destabilising effects of the external environment. To contain the severity of economic contraction, the Government had to reassess the IMF prescription of a tight monetary and fiscal stance and decided to adopt expansionary macroeconomic measures and ease monetary policy. In July, the Government implemented the National Economic Recovery Plan aimed at stabilising the ringgit, restoring market confidence, maintaining stability in the financial markets and strengthening economic fundamentals. The Plan also focussed on revitalising affected sectors of the economy and continuing the equity and socio-economic agenda pursued thus far by Government.

It became increasingly clear that in the absence of a concerted effort on the part of the international financial community to identify a permanent solution to the financial crisis, individual efforts by economies, such as Malaysia, to stabilise the financial markets in an open regime were obviously ineffective. Disillusioned with the lack of urgency to improve the international financial system and given the build up of risks of further contagion, the Government decided on September 1 to implement a series of measures to insulate the Malaysian economy from externally generated risks and vulnerabilities. These include new exchange control rules and administrative measures aimed at regaining monetary independence and requiring all dealings in securities listed on the Kuala Lumpur Stock Exchange (KLSE) be traded on the KLSE to ensure greater transparency in the stock market.

The new measures implemented by Government essentially remove the threat of speculation as the market for ringgit is brought home to Malaysia and discourage destabilising short-term capital flows. The newly introduced measures in no way restrict foreign direct investment flows to Malaysia. On the contrary, we continue to depend and, therefore, welcome foreign direct investment. We have always been a very open economy and have benefitted significantly from foreign direct investment. We remain committed to encouraging such investment and the free repatriation of profits and dividends from foreign direct investment. In fact, selective exchange control and the other measures offer an environment of greater certainty and stability for foreign investors.

These measures have started to yield some positive results as we begin to see the signs of economic recovery. The banking institutions and private sector have benefitted from the enhanced liquidity and lower interest rates and total loans extended by the banking system have begun to expand. Domestic demand, especially for passenger cars, has picked up. Our external reserves position has strengthened

while market capitalisation of the KLSE has improved. The Government is confident that the underlying economic fundamentals will strengthen further in the coming months. The current account of the balance of payments has recorded a surplus of RM15 billion during the first half of 1998. For the whole of 1998, a surplus of at least RM20 billion is envisaged. Although the real economy is estimated to contract by 4.8% in 1998, it should turn around in 1999, with a growth of 1%. Inflation will remain low, especially with a firmer ringgit.

This Economic Report is the 27th volume published by the Ministry of Finance in conjunction with the presentation of the 1999 Budget. I hope this Economic Report will provide an adequate insight on the performance of the Malaysian economy in 1998 and its prospects for 1999, the issues and challenges confronting the Government in managing the economy and the policy responses we have taken. We must have faith and confidence in the policies that the Government has adopted, as the Government has the experience and the tenacity to put the economy on an even keel again towards sustainable growth. I stress that the Government has acted in the interests of the nation to preserve the gains we have made over four decades of our economic development. With your continued strong support, we can together look to the future with confidence.

KUALA LUMPUR  
23 October 1998



DR. MAHATHIR BIN MOHAMAD