

28 OCT 1997

AMERICAN ACADEMIC SAYS: DON'T MEDDLE WITH INTEREST RATES

LANGKAWI, Oct 28 (Bernama) -- Jeffrey Sachs, an American academic and economist, has said that interest rates -- as a cost of borrowing for banks or companies -- would naturally rise because of the departure of short-term foreign capital.

But, he considered any increase above the regular market level as both "excessive" and "artificial" which, if carried out would merely exacerbate the economic conditions inflicted on it by the financial market turmoil.

Sachs prescription for a currency in difficulties coincides with Malaysia's decision, explained by prime minister Datuk Seri Dr Mahathir Mohamad in Edinburgh, of not raising its interest rates despite the weakened currency.

He was speaking to reporters after attending an international conference here. The conference is titled "The Impact of Globalisation and Privatisation on Malaysia and Asia in the year 2020".

Dr Mahathir has said that high interest rates could attract back the foreign capital into the economy, but he worried that such monies were not here to stay.

Against much of Asia where domestic currency values have fallen sharply, Malaysia stands alone not to have raised its interest rates.

Both Hong Kong and Singapore immediately lifted their rates at the first signs of any weakening of their currencies; the former because it has pegged one US dollar for buying about HK\$8.

Thailand, Indonesia and the Philippines have all lifted their interest rates in the past months. At double digit levels, their rates compare with Malaysia's 8.58 percent at yesterday's one-month interbank offered rate.

Sachs, a director at Harvard University's Institute of International Development, said past years of foreign fund inflows had swelled the volume of funds available for borrowing. Consequently, this lowered Malaysia's borrowing cost.

During capital flight, the conditions reversed, liquidity tightens and, Sachs said interest rates would tend to drift upwards. The country stands at the edge of slower economic growth as loans costs rise and begins to hurt companies.

In this fragile condition, he said a tightening of credit by the central bank could therefore push the economy into recession.

"I am not in favour of such an approach to slow the growth of loans and curb excessive consumption," he said.

When asked about his views on the Malaysian economy, Sachs said: "Your economy has long-term strengths. Rapid economic growth can recur.

"Foreign investors have withdrawn funds intensely in recent weeks. This has led to a short-term slowdown (of economic growth) which if not well-managed will cause serious long-term problems."

Under such a condition, the current account deficit could shrink, the property sector enters into a serious downturn, a number of banks would probably face difficulties because their balance sheets would be in grave shape.

The same crisis in other Southeast Asian countries may be much deeper, but he cautioned that Malaysia was not insulated from them because their performances influence opinions and investors' confidence of the region as a whole.

Malaysia with the rest of the region, he said, should act in unison to

effectively reduce the "pain", return to a path of high growth, and restore confidence.

Malaysia, he added, should improve its information disclosure and tighten the supervision of banks so that the borrowing of foreign funds were not used for highly speculative purposes. But, he also said foreign banks should be allowed greater participation in the domestic market. --

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