

24/12/1997

Bank: Foreign perceptions ignore Malaysia's strengths

INTERNATIONAL investment bank Dresdner Kleinwort Benson, in saying that negativity on Malaysia is overdone, pointed out that foreign perceptions see weaknesses not strengths, and these misconceptions had caused stocks, markets and currencies to overshoot this year.

"Misconceptions will be revealed to what they are and markets will turn when the direst predictions prove to be false. The key to 1998 is to understand these misconceptions so that the evidence against them can be identified as it appears," it said.

In a report by its Asian Markets Strategy Team, Dresdner Kleinwort Benson said in the property sector for example, the bulk of mass residential housing in Malaysia would continue to sell, and was no threat to bank balance sheets.

It said although household income growth would slow to five to eight per cent from 10 to 12 per cent, wealth would continue to be generated.

"Only the upper end of the market is vulnerable and this is a relatively small portion."

It identified the commercial real estate in the Klang Valley as the main problem with vacancies likely to rise to 20 to 25 per cent by 1999.

"However, this is not as great as in the mid-1980s, and both rentals and values are much more attractive on a regional basis (compared to) the last slump."

It also noted that many developers have the balance sheets, often from non-property core businesses to absorb the decline in values. Also the banks have largely seen it coming over the last three to four years, in other words, the banks are generally protected.

The investment bank also pointed that the Malaysian property scene is currently dominated by large plantation-based companies which have turned to property developing as a new earnings avenue.

"The (plantation companies) have strong balance sheets, land at exceedingly low cost, usually minimal debt and no pressure to sell in a weak market."

Commenting on Malaysia's leadership, Dresdner Kleinwort Benson said: "Contrary to perceptions of detachment from reality, Malaysia, under Datuk Seri Dr Mahathir Mohamad has shown an ability to take tough decisions and deal surgically with problems."

It said the late 1980s recovery was the result of letting numerous entrepreneurs collapse, including several supposedly well-connected, slashing infrastructure spending to three per cent of gross domestic product from five per cent, while "slaughtering the sacred cow" of reducing foreign ownership to 30 per cent and otherwise diluting the New Economic Policy.

Touching on perceptions, the investment bank said non-Malaysian investors also have to learn not to take Malaysian statement literally or at face value.

"The subtlety and indirect messages of wayang kulit will have to be grasped if policy and hence markets are to be understood fully."

Dresdner Kleinwort Benson said it was also hard to see Malaysia as a leader in misallocating resources when around 25 per cent of gross domestic capital formation and over 40 per cent of manufacturing investment in the country is made by world-class multinational corporations, plus a further significant amount made by local suppliers on

whom are imposed global best practices.

"More likely it is a case of out of sight of the stock market, out of mind," it said.

Meanwhile, weak electronics export growth did not point to terminal decline, Dresdner Kleinwort Benson added. What is obscured in the figures is a sharp decline in once-dominant consumer electronics and the equally rapid rise of information technology products.

"By mid-1998 IT industries growth will more than offset the decline in consumer electronics, enabling the industry that comprises nearly half of all exports to return to double-digit growth by 1999," it said.

Dresdner Kleinwort Benson said foreign direct investors continued to rate Malaysia very highly, often ranked second only to Singapore. The things that portfolio managers hate about Malaysia - obsession with infrastructure, high growth, interventionism and strong political leadership - foreign manufacturers love.

"A much weaker ringgit and less-tight labour markets will endear Malaysia to them all the more."

Dresdner Kleinwort Benson said non-traditional exports appeared to be responding faster to the currency depreciation than expected, implying a significant improvement in the current account confirmed by the second quarter.

The investment bank said while the excesses of borrowing in both domestic and foreign currencies had not escaped Malaysia, what was significantly different from countries like Thailand and Indonesia was that there were still numerous cash-rich or lightly-leveraged entities that could step into the breach once asset prices had fallen far enough.

Not only did this enable the economy to operate with less friction, it also protected the banks from becoming the receptacles of unwanted assets, it said.

"Given our views on property and the fact that some of the bad loans will be suffered by foreign banks, we are not as pessimistic on non-performing loans as the consensus which overlooks two facts: Malaysian banks, under Bank Negara guidance, have doubled their equity in the last few years.

"Furthermore, bankers and regulators went through Pan-Electric and the co-operative bank crises in the mid-1980s. Not all of the lessons have been forgotten, hence banking supervision has improved: other countries did not have the benefit of these lessons," Dresdner Kleinwort Benson said.

It said despite compelling valuations in many blue chips, the market was likely to wait until there was conclusive improvement in the current account before rallying. This might not be until the second quarter, by when the annual results will confirm the earnings trend.

"The second half should be a better phase for the market and currency. By then an evidently improving current account should attract attention towards the survivors who can capitalise on their strengthened positions. We see the index recovering to 800 while trading on 13-14 times (price earnings ratio)," Dresdner Kleinwort Benson said.

It said Asia as a whole could still boast its long-term strengths of high savings and investment, low taxes and youthful demographics.

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