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Foreign perception misguided: Dresdner (HL)

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INTERNATIONAL investment banker Dresdner Kleinwort Benson, in asserting that negativity on Malaysia is overdone, said foreigners see only weaknesses not strengths and these misconceptions had caused the stock and currency markets to plunge.

"Misconceptions will be revealed for 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 Malaysian property sector, for example, the bulk of the mass residential housing will continue to sell, and is no threat to bank balance sheets.

"Even though household income growth will slow to 5-8 per cent from 10-12 per cent, wealth continues to be generated," it said, adding that the transformation from highly-g geared medium-sized developers to an industry increasingly dominated by large plantations is significant.

"The latter have strong balance sheets, land at exceedingly low cost, usually minimal debt and no pressure to sell in a weak market. Only the upper end of the market is vulnerable and this is a relatively small portion."

Dresdner Kleinwort Benson said contrary to perceptions of detachment from reality, Malaysia under Prime Minister Datuk Seri Dr Mahathir Mohamad has shown the ability to take tough decisions and deal "surgically" with problems.

"The late-1980s recovery was the result of letting numerous entrepreneurs collapse, including several supposedly well-connected; slashing infrastructure spending to 3 per cent of GDP from 5 per cent; slaughtering the sacred cow of reducing foreign ownership to 30 per cent; and otherwise diluting the pro-Bumiputera New Economic Policy," it said.

Touching on perceptions, the investment bank said non-Malaysian investors also have to learn not to take Malaysian statements 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 is 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 Malaysia is made by world-class multi-national 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.

As Malaysia's exports, weak electronics sales growth does not point to terminal decline. 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 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 noted that foreign direct investors continue 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," it added.

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

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

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

"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.

"(And) bankers and regulators went through Pan-Electric and the cooperative 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."

However, despite compelling valuations in many blue chips the market is likely to wait until there is 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.

Asia as a whole can still boast its long-term strengths of high savings and investment, low taxes and youthful demographics. "Many markets overshot in 1997 because of misconceptions. As these are revealed there will be plenty of opportunities to play their reversal in 1998."

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