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Confidence in measures key to recovery

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MUCH has been said, and more has been written, about the slew of measures the Government has put into place to revive the economy, especially over the past one month.

Assessments, whether the monetary initiatives will work, crystallise into two broad and diametrically opposing views.

The first is benign verdict. Many economists, both local and foreign including the paragon of American economists, Prof Paul Krugman, have declared that these are hard and difficult times.

They have conceded that the radical, unorthodox and unconventional economic remedies might nurse the country's ailing economy. They accept the precepts of Bank Negara underlying its decisions to reform the financial system of the country.

One, to loosen the tight interest rate regime. Two, to turn the spigot of the Statutory Reserve Requirements, releasing funds as much as RM16 billion, into the financial system. Three, to impose capital controls. Four, to fix the exchange rate of the ringgit to the US at RM3.80. And five, to declare loans that have been in default for six months, rather than the earlier three, as non-performing loans.

The benign assessors are now many. Among them is the hitherto doubting Thomas who has now been converted and is now a believer, the International Monetary Fund. They have declared the Malaysia has bought time to kick-start its economy. Their summation is that the measures might work. The key word is, might.

The second view is a malign assessment. It is expressed by the Cassandras in the foreign media who have the perception that Malaysia can never do not any right, any which way the Government acts. (Cassandras, for information of the uninitiated readers, are the mythological choruses in the ancient Greek plays. They are messengers of gloom and doom.) The malign verdict is epitomised in an article in the Oct 12 issue of Fortune, "The Malaysian Contagion". The introductory paragraph is reproduced to underscore the mindless malignancy of the foreign media has conceived of the country's economic initiatives.

"By imposing stringent captial controls on Malaysia's economy on Sept 1, Prime Minister (Datuk Seri Dr) Mahathir Mohamad launched an assault on the foreign `speculators' and the international financial orthodoxy that he hates.... If Mahathir's extreme plan works, which is highly unlikely, virtually every emerging economy would be tempted to follow suit, leading the world back to the closed capital account regimes of the 1950's. Even more worrisome: the Prime Minister's recent (behaviour) points up the extent to which the Asian financial and economic debacle has now shuddered through to politics and geopolitics - another frightening reminder, as if any more (is) needed, of how much 1998 is coming close to 1931."

The writing is verbose. Which means it is a wordy camouflage of the basic message of the writer. And when the shaft is winnowed, the residual grains will emerge.

At least two inferences can be drawn from the summation of the Fortune's article. One, the measures set into motion by the country's central bank is "highly unlikely" to work. Two, that other emerging countries might be tempted to follow our economic initiatives which might lead Asian and other countries down to the road of world-wide recession, last ecountered in the early 1930s.

The question is: will that eventuality come to pass? That is a secondary question. Especially when we analyse it against the earlier benign view that the Government's initiatives will work.

So the question is which of the two views, that of the benign and malign, is valid. Both views are based on the main question whether our economy will re-emerge from the recession engendered during the first half of this year. That question is the preponderant for all of us.

But that is an enigma. It forces us to look at a crystal ball. But a look at the future must necessarily take us to the past road we had travelled.

The last 14 months have been trying times. Our currency was battered. The local stock exchange saw the devaluation of the shares of all listed companies.

Financial institutions faced liquidity problems as a result of bad loans. Hence they tightened lending. Interest rates soared as a consequence. The Base Lending Rate of commercial banks peaked at an annual 12.6 per cent. Margin spreads lengthened to almost four per cent to cover bad loans.

As a result businesses were stifled. So also retail borrowings for buying of houses and cars. These, and other factors, ground the economy to a halt. And so the country registered a negative economic growth of 4.8 per cent over the first half of this year.

This is the background against which we should assess the economic recovery measures.

That is past history. And the measures the Government, through Bank Negara, has implemented is recent history. Now we have to look at the future. We are now in the third quarter of the financial year of the country.

On Friday, Oct 23, the Prime Minister and now the First Finance Minister, will present the 1999 Budget in the Dewan Rakyat. The attendant 1998/1999 Economic Report, produced by the Ministry of Finance will also be tabled on that date.

No one can divine the contents of the 1999 Budget Dr Mahathir will present. But it surely will be a revival budget. The Economic Report would lay bare basic truths on the status of our economy.

The Economic Report would declare that the country achieved a Gross Domestic Economic growth of 7.1 per cent for 1997. The GDP growth rate for 1998 is still uncertain. For the forecasts of economists and statisticians are simply forecasts, nothing more.

And so, evaluating all statistical data, we can surmise that the country's economy will emerge out of 1998 with a GDP contraction of less than four per cent. It might be lower if the measures the Government have implemented bear fruit.

And what are the effects of these measures? Analysis of these measures would tilt the scale in favour of the benign observers. Why? The reasons are many. And they have worked so far.

One, detractors of the beleaguered Asian economies have pointed to the weak financial institutions that borrowed heavily and lent imprudently. True, our banks, finance companies and merchants were culprits on this score.

But they were forced to rewrite their balance sheets. Until early 1997, financial institutions could carry defaulting loans for as long as six months in their balance sheets. Bank Negara then decreed that the defaulting period is three months. Overnight, the non-performing loans spiralled to nine per cent of all loans last May to 12 per cent last July.

This works out to RM45 billion in May and RM60 billion in July, considering the loans of financial institutions were about RM500 billion.

And the maligners averred that the NPLs would spiral to 20 per cent or about RM100 billion by the end of the year.

But Bank Negara's simple decree of changing the format of NPLs, from three-month default to six months, changes the equation and the liabilities of the country's financial institutions. This surely would rejuvenate financial institutions which are carrying bad loans on their balance sheets.

Then we have the reduction of the SRR from 13.5 in February to four per cent. This turn of the spigot has released RM38 billion. True, a portion, a good portion was absorbed by the floatation of Malaysian Government Securities and Treasury Bills. Still, at least RM16 billion flowed into commercial banks, financial companies and merchants. Which pricked them to lend more to purchases of houses and cars and hopefully to businesses such as manufacturers and builders of houses.

Such lending is showing nascent signs that the economy is picking up. For economy is nothing more than about supply and demand. About consumption of goods and supply of goods.

When a house is sold and bought, it is not just the builder who profits. The subcontractor who renovates, the electrical man who rewires and the furniture seller who makes the house livable. All make money out of a single purchase of a house. This is what galvanises the economy.

But above all, there is a significant factor that makes or breaks an economy. It is the perception of the populace. As Special Functions Minister, and Executive Director of the National Economic Action Council, Tun Daim Zainuddin, is on record as saying, people must have faith in the Government, in its economic policies. If they don't nothing that the Government can devise will work.

So whether the economy of the country will revive depends on the confidence the people entrust on the Government, its economic decisions and policies. Without that trust, no governmental edict would prevail.

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