

20/09/1998

Exchange controls: Reversal of fortunes

Shaik Osman Majid

IN the beginning they heaped scorn. Many economists of repute, the International Monetary Fund and the US administration, said the exchange control measures and the benign interest rate regime Malaysia implemented on Sept 1 would not work to revive the economy.

Whether the initiatives the Government has implemented will bear fruit, only time will tell. But nascent signs are encouraging. Indicators show that the economy might find its way out of the recession recorded over the first half of this year. Over the next year.

One indicator is the fact that more and more capital is flowing into the financial system. The reduction of the statutory reserve requirement of financial institutions, from six per cent to four per cent, effective last Wednesday, releases RM8 billion into the system.

And as Prime Minister Datuk Seri Dr Mahathir Mohamad said on Thursday, RM11 billion ringgit has been repatriated into the country, thanks to the exchange control measures.

Fresh funds totalling RM19 billion ringgit is a lot of money. It should enable banks to lend more. Indeed, henceforth they might be courting clients.

This is a reversal of the situation over the past year when loan applicants were regarded as beggars. Applications for business loans were either denied or scrutinised; credit lines were shaved or totally removed; applicants for even housing loans had to pay a hefty margin of as much as four per cent above the already high base lending rate.

The reduction of the SRR had forced down the BLR of commercial banks from a high of 12.6 per cent in July to as low as 8.9 per cent - as quoted by Maybank, the leading commercial bank, on Wednesday.

Borrowings would clearly be cheaper. Not just because of the lower BLR. Bank Negara has advised financial institutions to lower the interest margin spread over the BLR from the hitherto four per cent to two per cent.

The new governor of the central bank, Tan Sri Ali Abul Hassan, knows too well that even this reduced margin spread should enable lenders to make profits. His advice is only an intimation. But it might transform into an edict if the financial institutions do not toe the line.

These measures should help prod the economy. Then we have other economic strengths. Fundamentals as economists would describe them. Low foreign debt, strong economic growth over the last 10 years, relatively low inflation and still cheap labour.

Whether these factors were considered by the foreign analysts, we do not really know. But the Cassandras, messengers of doom and gloom, have metamorphosed into a chorus singing paeans. And more and more economists, international financial and economic institutions are singing songs of praise for the Malaysian way.

The United Nations Conference on Trade and Development, while not commenting on the Malaysian measures has, in its latest report, released on Wednesday, declared that novel measures are required for these trying times. These include changes in the international financial architecture.

What perforced this volte-face? Simple. They analysed and found the traditional prescriptions that called for a tight monetary policy and its attendant high interest regime are no longer the panacea for ailing economies.

That economic prescription did not work in Thailand, Indonesia and even in Malaysia, the first three countries devastated by speculators and manipulators.

As the erudite economists reached back to textbooks for new answers, Malaysia chose a different path. The Government established the National Economic Action Council. To man the council, it roped in the best and the brightest of economic and corporate minds. Named executive director was Tun Daim Zainuddin (now also Special Functions Minister).

Daim was the right man for the right time. His financial and corporate astuteness enabled him, when he was appointed Finance Minister in August 1984, to revive the economy which slipped into a mild recession in 1985.

Given his credentials as an economic turnaround artiste, he was the best man to head the NEAC team that had to come up with measures to revive the economy that had already contracted in the first quarter.

The NEAC, in its analysis of the economic and currency problems, traced one basic fault to the profligate lendings of financial institutions. They lent indiscriminately. So they suffered.

The amount of non-performing loans totalled RM45 billion, about nine per cent of all loans at the end of May. The forecast for the entire year was more grim.

It was averred then that the percentage would spiral to 20 per cent or about RM100 billion by the end of the year. Enough to sponge the entire shareholders' funds of financial institutions of the country.

To search out a remedy, the NEAC delved into economic history and modules. It came up with the concept of a national asset management company. The company's seminal objective would be to take over selected non-performing loans of financial institutions.

But the NEAC also realised that many financial institutions did not have sufficient shareholders' funds to carry on their banking functions. And so it recommended the establishment of a special vehicle company to organise mergers and to inject fresh funds into the problem-ridden institutions.

Then the NEAC addressed another fundamental problem that was enervating the economy. The local currency had been battered in the foreign exchange markets.

The ringgit's value diminished greatly vis-a-vis the major currencies. The weakened ringgit made the country and Malaysians poorer, by as much as 40 per cent.

A way had to be found to arrest the weakening of the ringgit. And so the NEAC recommended in the National Economic Recovery Plan that the only way to insulate the currency against the outrageous swings was to bring the ringgit home. And so exchange control measures to curb the gyrations of the ringgit in the foreign exchange market were implemented.

That single, ingenious measure, initially described by foreign economists and international institutions as unorthodox and unconventional, is manifesting signs that it is effective.

Under that measure, ringgit held overseas would have no value after Sept 30. And so the depositors of an estimated RM20 billion in overseas accounts were forced to reassess the benefits of holding the ringgit there.

That aspect of the exchange control measure has yielded some results. As the Prime Minister said, about RM11 billion has been repatriated.

It is only two weeks since the controls were put into place. Perhaps in the next two weeks, we might see more ringgit flowing back into the country.

All the measures, collectively should turn the spigot of funds to loan applicants. Businessmen will benefit because they now can chart their accounts, given the fixed exchange rate of the ringgit and the US dollar.

Builders and vendors of houses will benefit. They now know that interest rates have slid back to the halcyon days of the building boom. And so they will build.

House buyers will also benefit as loans will be cheaper. People will be more inclined to buy units priced between RM100,000 and RM150,000.

All told, the initiatives that have been put into place by the central bank might just provide the necessary fillip to revive the economy. If they materialise, we can proudly say, we did it our way. The Malaysian way.

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