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`Give recent measures chance to work'

Zainul Arifin in Washington, DC

INFLATION for this year, as measured by the consumer price index, is expected to be much lower than anticipated despite the depreciation of the ringgit that has made the cost of imports higher.

Second Finance Minister Datuk Mustapa Mohamed said on Sunday inflation for this year was expected to be about five per cent, an increase from about three per cent for much of the 1990s.

The projection, if realised, would be quite good as following the weakened ringgit, inflation rate was expected by many analysts to exceed 10 per cent.

But, the import-substitution effort - especially for food items - drastically eased inflationary pressures and shaved off much of the anticipated price hikes. Mustapa was speaking at a seminar on Malaysia here.

The seminar was held in conjunction with the World Bank/International Monetary Fund annual meetings set to begin today.

In keeping with the good news, the economic outlook for the second half of the year is expected to be better than the first, with economic contraction narrowing substantially.

For the whole of this year, economic contraction is expected to be five per cent, down from 6.8 per cent reported for the first half of 1998.

The Treasury is now finalising the figures for the economic indicators and will release them during the Budget presentation by Prime Minister Datuk Seri Dr Mahathir Mohamad a few weeks from now.

Much of the improving scenario could be attributed to recent measures to reflate the economy by boosting economic activities, as well as the currency control mechanism put in place last month to stop speculation on the ringgit.

Mustapa said calculations had shown that with the lower interest rates, the amount needed to recapitalise the banking system had been reduced by almost half than what was computed during the tight monetary policy period a few months ago.

A more relaxed monetary policy, that included lower interest rates and the availability of more credit, was also expected to help commercial activities and consequently help companies in their loan repayments.

Following the smaller level of bad debts, recapitalisation of banks could be done using only domestic funds for the moment.

Mustapa also said initial plan to tap the foreign market to boost the banking system had been shelved following the current prohibitive rates in the market. Nevertheless, Malaysia is not discounting such a possibility at a later date.

The recent directive for banks to increase credit availability as well as the shelving of plan to raise funds abroad were not going to slow down the process to restructure and reform the banking system.

While there were some strong banks and some weaker ones, all of the banks in Malaysia were solvent.

Mustapa said Malaysia was asking the world community to give its recent measures on selective exchange controls a chance to work.

The measures were introduced only four weeks ago and it was unfair for the international financial community to ask Malaysia to give an assessment at this early stage.

The measures were not permanent nor were they a substitute for sound

macroeconomic and financial policies.

However, the initiatives would provide Malaysia some breathing space to undertake structural adjustment measures without being distracted by external factors.

Interest rates had adjusted downwards based on the assessment of the expected inflationary trend while Malaysia's reserves had also risen by US\$1 billion since the controls were introduced.

As at mid-September 1998, international reserves stood at US\$21.3 billion (RM80.94 billion), sufficient to finance 3.7 months of retained imports.

(END)