

07/05/1998

Don't push up interest rates, say economists

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ECONOMISTS agreed with the Government that current levels of interest rates should be defended against upward pressure that will push up the cost of doing business or even kill off companies.

Prime Minister Datuk Seri Dr Mahathir Mohamad on Tuesday said he disagreed with International Monetary Fund managing director Michel Camdessus' suggestion that Malaysia should keep interest rates high.

Interest rates should be maintained and not pushed up, economists contacted by Business Times, stressed yesterday.

Deputy director-general of the Institute of Strategic and International Studies, Dr Zainal Aznam Yusof, believes interest rates are already high now.

"Although the three-month KLibor rate is 11.3 per cent, the cost of real funds is much higher than that. It could be somewhere between 15 and 20 per cent," he said.

The cost is higher because the KLibor rate is not the final say in what banks can and would offer.

"It is punitive enough that costs of funds are high without increasing interest rates. Given the current scenario, growth is already expected to be 2 per cent or less. It will not be the best course to increase interest rates now," Dr Zainal said.

He added that there is a need to allow for growth impulses in order to prevent the economy from sliding into a recession.

"I am worried that if interest rates are increased, companies and industries will be strangled ... and then we will face a recession," he said.

Meanwhile, senior economist at TA Securities Anthony Dass said that if interest rates were increased further, businesses and companies will go bust.

"We will see lots of companies going under, more bankruptcies and a worse scenario.

"We are already maintaining a tight monetary policy. The 12 to 15 per cent loan growth should be achieved by the end of this year. The pressure on loan growth is in itself a tight measure.

"If loan growth is further tightened and were to continue, domestic growth will be hampered and in this case, real aggregate domestic demand will likely be in the negative," he told Business Times.

Bank Negara in its annual report forecast the real aggregate domestic demand for 1998 to be at 4.9 per cent. It was 6.4 per cent in 1997, 7.0 per cent in 1996 and 13.4 per cent in 1995.

Real aggregate domestic demand comprises private and public expenditure - which in turn is made up of private investment and consumption and public investment and consumption.

Dass added that if interest rates were to go up, it will not solve any problem.

"It will not defend the currency because even if interest rates are higher, it does not necessarily mean the currency will 'improve'. It may help the ringgit a little but the positive impact will be outweighed by the increase in interest rates.

"Higher interest rates will also not contain inflationary pressure because inflation has to be addressed in a different way. We have to look at inflation from the point of view of demand, supply and distribution,"

he added.

Dass said that increasing interest rates will possibly create social problems since it will cause businesses to fold, increase unemployment and make more people unhappy and poor.

Meanwhile, group economist for Arab-Malaysian Securities Encik Mustapha Mohd Nor said the question of whether interest rates should be maintained or increased is not an easy matter.

"Since we are operating within certain constraints, we cannot do things without having to accept the implications.

"We must first find out what we want to do. If we want to protect the economy, we need to lower interest rates. However, we cannot do that since it will have an adverse effect on the ringgit and the stock market.

"Meanwhile, if interest rates remain at the current level or are increased further, loan growth will decrease faster which inevitably will weaken the economy," Mustapha said.

He also said timing when implementing a change is important, adding that there is a need to wait for confidence to return before any decision can be taken.

Chief executive officer of Kompleks Metrowangsa, Dr Ghazali Atan, said he saw no need to increase interest rates.

He said, "There is no need for an increase because things will be worse."

Ghazali expected unemployment to rise and more uncertainty in the business arena.

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