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Sachs: Asia must export its way out of the crisis

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HARVARD: Malaysia'S decision not to go to the International Monetary Fund (IMF) is the right one according to Jeffrey Sachs, Director of the Harvard International Institute for Development (HIID), who says Malaysia has "escaped the sharp contraction that has taken place in its neighbours".

One of the biggest differences in 1998, compared with Indonesia and Thailand, is that Malaysia "will emerge better". This is because Malaysia would not have gone through a credit squeeze as Indonesia and Thailand would have done as a result of IMF policies.

(Indonesia and Thailand had turned to the IMF for assistance. The Fund in turn imposed strict conditions which caused even greater hardships in the two countries. In the case of Indonesia, the conditions had to be revised at least twice.)

Sachs' prescription for Malaysia is: Do not to go to the IMF; export out of the crisis; inject liquidity especially for the export sector and liberalise the financial sector to attract increased levels of foreign direct investment.

Malaysia needs to "export its way out of the crisis," (as do other countries), as it is difficult to sustain internal demand in such a crisis. For exports, there is a need to keep the exchange rate flexible and ensuring that there is adequate financing available for exports is crucial. Malaysia, according to Sachs, should turn to countries like Japan to inject liquidity into its system.

While the situation in South Korea is still fragile and complicated, Sachs is confident that the problem will not "cascade to Malaysia. But Malaysia needs more liquidity and if I were a Malaysian official I would ask Japan for liquidity. The decision not to go to the IMF (for Malaysia) is the right one", he stressed.

Malaysia's strategy to attract foreign direct investment, which has long been part of Malaysia's policies, remains very important. "None of this will provide a miracle, as it is very difficult to sustain internal demand in this kind of crisis. But the export sector will certainly be a cushion," he adds.

While it is good advise that countries in the region should "export out of the crisis" it is based on the premise that their major markets, in the US and Europe, will remain open. It is hoped that protectionist sentiments and barriers do not go up in the face of "cheap" exports from crisis hit Asian economies.

Sachs says he does not accept the premise that the markets for Malaysian goods and those from the region will close. He suggests that from a diplomatic and economic viewpoint, "Malaysia should act on the basis that markets will remain open for its products".

He warns that if "we (the world) do slip into protectionism we will have a very intractable crisis on our hands, adding that "we still have the hope that world markets are going to remain open and there are no protectionist moves.

However, the irony of the situation is that despite the cheaper exports from East Asian economies due to the depreciation and devaluation of the currencies "there has hardly been any increase in exports from East Asia".

This is due to the tight credit situation in these countries. The conditions facing exporters are so adverse that they have not been able to organise export credit. A shoe manufacturer in Indonesia is said to have

large orders but is unable to export due to lack of credit. In this crisis the exporters who remain liquid will do well.

Thus there is a need for countries in the region and multilateral organisations, including the IMF, to ensure that policies, conditions and prescriptions to solving the crisis do not jeopardise and dry up essential liquidity.

The countries in the region were among the world's largest exporters. Malaysia was the 19th largest exporter and 17th largest importer in 1996.

Malaysia's US\$78.4 billion (US\$1 = RM3.77) exports and US\$78.6 billion imports in 1996, respectively accounted for 1.5 per cent of the world totals.

Nevertheless Sachs says that the export growth in Malaysia and Asean has been based on a "narrow range" of electronics. "South East Asia rode the electronics boom," which he says is not over yet. But unfortunately the prices of electronics have declined so much that the US dollar earnings in these exports is not particularly strong.

Thus there is a need for countries to diversify their export base, even during these difficult times, away from electronics into other areas. "This is much easier said than done," Sachs admits. But it has to be done. Just as in electronics it means sourcing international partners that find Malaysia a reliable home base for operations in new sectors.

In this, Malaysia's move up into Information Technology (IT) could not have been better timed. The Multimedia Super Corridor (MSC) is an important concept for technological advancement. Malaysia's focus on IT with the MSC should be used to enhance its economic position.

"It is not a naive decision but a correct decision to move into IT," Sachs says adding that there is a need however, to be conscious of the fact that the private sector should take the lead in this area.

IT is an important area for many countries and even the US is taking a closer look at it. It is the fastest growing sector and have been generating increasing employment opportunities in retail and manufacturing. Even the US Commerce Department acknowledges the important role of electronic business and IT in the US economy.

Malaysia, according to Sachs, which has "resisted liberalising the financial sector" needs to liberalise it in order to attract increased levels of foreign direct investment. This he argues is necessary for greater stability. "Malaysia will be more stable with the presence of major international banks who will stay for the long term."

Sachs agrees with Prime Minister Datuk Seri Dr Mahathir Mohamad that the crisis was caused by the instability of international capital. Referring to his research which shows that the causes of the "crisis lie with the international institutions and the unstable short term loans", he nevertheless makes a case for FDI which he says is more stable and does not run for the door as soon as a problem emerges in host countries.

FDI is there for the long haul. During a crisis FDI does not flee the region and is even counter cyclical as there can be increases in FDI even as short term money declines. As for the foreign banks, Sachs argues, that they will be cautious about the region if they do not have operations there. But if they do have operations in a country or region they "will stay even during a crisis".

They will in fact help provide the necessary export credit required for exports. Foreign direct investment is not new to Malaysia. Sachs points out that Malaysia recognised the importance of FDI some 20 years ago, when other developing countries were not even looking to open their economies to foreign investments. It needs to continue remaining "FDI friendly".

Malaysia recognised all along the importance of the export sector which has paid dividends. It provided jobs, helped diversify the economy away

from primary commodities, helped increase income, transfer technology and provided stability.

Despite the crisis, Sachs says, Malaysia should continue to attract increased foreign investments, including into the banking sector. While in the short term there will be a contraction of the economy with slower economic growth, he says, the basic fundamentals of the Malaysian economy remain intact.

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