

## **National budget must reflect guarantees by nation**

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**Oleh Tommy Thomas**

My attention has been drawn to your article posted on 1st October 2012 which quoted Mohd Irwan Serigar Abdullah, the Secretary-General of the Ministry of Finance, stating that "the government does not take into account contingent liabilities such as off-budget borrowing into its debt to GDP ratio as these are not 'realised debt'".

In a Parliamentary reply to a question by MP Dzulkefly Ahmed (PAS-Kuala Selangor) on 28th March 2012, the minister of finance stated that the amount of contingent liabilities in 2011 totalled RM117 billion.

The reason why contingent liabilities should, as a matter of prudence, be included is because it is in effect "a liability" which may sometime in the future be crystallised.

The largest component under "contingent liabilities" is apparently the guarantee, a long established and widely used financial instrument, which involves three parties; the lender, the borrower and the guarantor.

It arises because the lender is not sufficiently satisfied that the borrower has the financial means to repay his debt.

Accordingly, the lender insists that the borrower's debt be guaranteed by a third party, the guarantor, which then entitles the lender to have recourse against two separate persons (the borrower and the guarantor) in the event that the borrower defaults.

In such a tripartite relationship, the borrower and the guarantor assume legal liability at the time their respective contracts are signed. Thus, the guarantor faces an exposure.

I understand that the accounting profession has no universal rule or principle as to how guarantees are to be treated in the accounts of the guarantor.

Nonetheless, prudence, which should be the touchstone of every minister of finance, requires that provision be made in the national budget every time a nation gives a guarantee.

Additionally, making provisions should enhance financial discipline on the part of the Treasury by either not giving guarantees at all or keeping them to an absolute minimum.

From the lender's perspective, no guarantee is more valuable and risk-free than one given by a nation: After all the nation's reputation and credit-standing would ensure that the guarantee is honoured.

Most significantly, a nation can always print money, (which is the current fashion in the US

and Europe with "quantitative easing") and pay off the guaranteed sum.

Because there is always a real risk that the Malaysian government would have to honour its legal liability if the borrower (whether a GLC or other governmental agency) defaults, I suggest that Malaysia's true natural debt should include contingent liabilities like governmental guarantees.

This would mean that our national debt at December 2011 is RM573 billion (and not RM456 billion) which would represent 67% (and not 52%) of GDP.

In the light of the current crisis involving Greece and other European nations over their sovereign debt, steps must immediately be taken to reduce our national debt, in both absolute and relative terms.

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