MALAYSIA

Growing Confidence

THE CONSENSUS FORECAST OF 15 securities houses places Malaysia's GDP growth this year at 5.6%. That would make it the third-fastest-growing country in the region after pacesetters Thailand and Vietnam, which are expected to record growth rates exceeding 6%.

Malaysia is back on the fast track and the renewed optimism has also brought with it some loosening of shackles. Subjects once considered taboo are now up for discussion, even issues like the ringgit peg. In the wake of the Asian financial crisis, former Prime Minister Mahathir Mohamad imposed capital controls and fixed the ringgit at 3.80 to the United States dollar in September 1998. Since then, any

% change over previous year	*2002*	*2003**	*2004†*
GDP	4.1	4.8	5.6
Private consumption	4.4	4.7	5.9
Fixed investment	0.3	2.9	5.2
Industrial production	4.5	8.1	8.7
Current account (*$ billion*)	7.2	10.0	9.7

*Estimates †Forecast — Source: Consensus Economics

talk of flexible exchange rates has been dismissed out of hand. On January 12, Abdullah Ahmad Badawi, who replaced Mahathir on October 31, opened the door a crack. While saying that the peg would "remain as it is," he added that "we are not dogmatic to say that it will stay forever."

The ringgit's dollar-driven decline has made Malaysia's exports competitive vis-à-vis its regional peers, but economists say the currency is undervalued—by as much as 19%, according to a recent estimate from Standard Chartered Bank in Kuala Lumpur, for instance. Even so, any distortion has hardly been noticeable: Inflation in December rose to 1.2% from 0.9% in November, a sign of imported inflation but hardly worrying to the authorities. Indeed, political imperatives lean towards keeping the peg. Analysts note that the people who would be happy with a ringgit appreciation are mainly foreigners holding ringgit assets. Meanwhile, local businessmen and exporters want the status quo. In any case, there isn't any pressure on Malaysia to revalue. "If China can hold out for so long, Malaysia has no problems whatsoever," says JPMorgan Chase's Tan Pye Sen, a Kuala Lumpur-based analyst.

Indeed, the benign economic climate points to a snap general election, maybe as early as March or April. The stock exchange is up 26% from October, interest rates are low (the three-month interbank rate is 2.9%) and unemployment is falling (down to 2.9% last year from 3.2% in 2002).

Meanwhile, the country continues to rack up surpluses. Malaysia's current-account surplus on its balance of payments is expected to top 38 billion ringgit ($10 billion) in 2003. That has pushed up reserves, which topped $44 billion at the end of December. Only one festering issue remains: Malaysia's sixth straight budget deficit, which, at its peak, was 5.6% of GDP. Tackling it would make international borrowing cheaper for Malaysia as it would encourage international agencies to upgrade its sovereign ratings. S. JAYASANKARAN