

Malaysia's debts a potential time bomb, say economists
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By Lee Wei Lian

KUALA LUMPUR, July 19 — The government's debt, which nearly doubled since 2007 to RM421 billion, pose a fiscal risk to the country if not managed carefully as it impairs Malaysia's resilience to economic shocks, analysts and economists have said.

They say that while government debt — currently at about 54 per cent of gross domestic product (GDP), and the second highest in Asia — has not significantly impacted the country and its credit standing yet, the volatile nature of global markets may manifest such a risk at any time.

While the Najib administration has vowed not to let federal government obligations exceed 55 per cent of the country's GDP, there is increasing worry that when government-backed loans or "contingent liabilities" are taken into account, the government's total debt exposure rose to about 65 per cent of GDP last year — above the comfort level for many analysts.

RAM Ratings chief economist Yeah Kim Leng said that while Malaysia's debt levels are currently considered moderate, it should still be vigilant against the possibility of debt levels hitting the "tipping point" whereby it could be punished with higher borrowing costs.

"The threshold at which the market sentiment can turn against you is unknown," said Yeah. "If market sentiment does turn against Malaysia, it could result in very high borrowing costs and capital pull-out."

The reason we have not had a higher debt burden is because we have a piggy bank called Petronas. — Cheong Kee Cheok, senior research fellow at University of Malaya's Economics and Administration Faculty.

He added that careful management of debt levels could inject greater resiliency into the economy, which was desirable given the increasing frequency of economic shocks that characterises the global economy today.

"It's not just about economic growth but also the country's ability to withstand shocks," he said.

Figures from the Federal Treasury's Economic Reports shows that the federal government's domestic debt almost doubled in the space of less than five years — from RM247 billion in 2007 to an estimated RM421 billion in 2011 — far outpacing its revenues which only grew 31 per cent or from RM140 billion to RM183 billion during the same period.

In contrast, 2001 to 2005 saw domestic debt level growing from RM121.4 billion to RM189 billion, or just 56 per cent.

Government-backed loans rose rapidly as well between 1985 to 2010 — from RM11 billion to RM96 billion — representing a growth of 8.7 per cent per annum.

Cheong Kee Cheok, a senior research fellow at University of Malaya's Economics and Administration faculty, said that while Malaysia's debt level of 55 per cent of GDP is "not an

outright disaster” when compared to countries like Greece, he expects the level of debt to continue to rise.

“The rise in this debt level over the past few years is worrying though, and so far, I have not seen any effort to try to rein in spending given that revenue sources have not expanded,” he said. “The reason we have not had a higher debt burden is because we have a piggy bank called Petronas.”

Wan Saiful Wan Jan, chief executive of the Institute for Democracy and Economic Affairs (Ideas) said that politics played a role in why Malaysia is grappling with debt.

He said that while deficit spending was “completely wrong”, as long as governments could roll over their debt, there was little urgency to address the issue as politicians rarely look beyond the next election.

“Politicians will spend what they need to win elections,” he noted.

He added that his was not a criticism only of the Najib administration as he found Pakatan Rakyat’s many promises even “more reckless”.

“Pakatan Rakyat say that they can pay for spending by removing corruption but if you want to be responsible, you should plug the hole and pay the debts not plug the hole and spend the money,” he said.

The country’s fiscal track record has apparently already affected investor confidence, as evidenced by the weakness in the country’s currency and relatively high yields on government bonds.

Despite Malaysian government securities offering higher yields than either Singapore or the US, investors last week still flocked to the two perceived safe havens over places like Malaysia, sending the ringgit markedly lower in recent weeks.

Countries with strong credit ratings such as Switzerland can even afford to offer negative yields to investors due to their perceived comfort factor while weaker countries, such as Italy and Spain, have a harder time raising funds even when offering vastly superior yields due to the perceived higher risks involved.

While Malaysia is not yet in the category of Spain or Italy, it is notable that investors prefer to switch their money to US and Singapore assets rather than Malaysia’s in times of uncertainty despite the 10-year MGS (Malaysian Government Securities) offering a yield of about 3.4 per cent as compared to less than 1.5 per cent for both 10-year Singapore government bond and 10-year US Treasury bonds.

This generally means that investors harbour stronger doubts over Malaysia’s ability to pay back its debts, and outflow of funds led to the ringgit slumping to a 14-year low against the Singapore dollar and also saw the currency lose ground to the greenback.

With both its debt and budget deficit among the highest in Asia as a percentage of GDP, it would be difficult for the government to pare down debts without it either raising taxes or cutting spending, both options which are likely to make it unpopular with the public at large.

The saving grace for the government is that it can tap into the vast savings pool of Malaysians instead of going outside the country and the revenue it gains from oil and gas.

Hydrocarbon income, however, could be under threat this year as petroleum prices have weakened significantly due to the economic uncertainty.

Should another global economic crisis hit, it is unclear how much fiscal space the Najib administration has left to implement stimulus measures given its commitments to reduce its budget deficit and keep a lid on debt.

Another issue is that the RM96 billion in government-backed debts is likely to grow even more in light of an expected raft of rail and road infrastructure projects, which some reports have estimated will cost as much as nearly RM100 billion over the next few years.

Even Malaysia's National Higher Education Fund Corporation (PTPTN) is going down the route of government-backed debt, recently selling RM2.5 billion of federally-guaranteed Islamic debt as it looks for financing to provide more loans to a growing number of eligible students entering university.

The PTPTN scheme, however, has been a source of controversy as only 84 per cent of students are reported to be repaying their loans as at February this year.

For the moment, investors are still willing to buy Malaysian government bonds used to raise money for the country's development.

The question is whether falling petroleum prices, stubborn fiscal deficits or rising contingent liabilities could one day shake their confidence.

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