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The Prime Minister

EVENT: The 17th Financial Institutions' Annual Dinner

VENUE: Renaissance Hotel, Kuala Lumpur

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Terlebih dahulu saya ucapkan terima kasih kepada pihak Persatuan Bank-Bank dalam Malaysia kerana menjemput saya untuk hadir di Majlis Makan Malam ke-17 Institusi-Institusi Kewangan pada malam ini.

2. The Malaysian economy has grown from strength to strength since it came out of the recession in 1985-86. Indeed, during this period, the economy enjoyed the strongest cyclical upswing, with growth in GDP averaging 8.9 percent per annum for the period 1988-95, one of the highest rates of sustained growth experienced by a developing country. At this point in time, the economy is still looking distinctly robust and expected to register 8.3 percent growth for 1996. However, for an economy which has undergone a prolonged period of strong economic growth, the key question is how to sustain this high growth and achieve the annual growth target of at least eight percent that we have set for ourselves in the next five years of the Seventh Malaysia Plan. Given the attendant problems of economic success, including the strong competition for domestic resources, the challenge to Malaysians is how to use our ingenuity to steer the economy so as to maintain rapid and sustained growth with price stability and a balance in the external trade, while at the same time managing anything that might threaten to derail the development process.

3. Over and over again I have emphasised the importance of partnership and the complementary roles of the Government and private sector in the development process. The banking institutions form a part of the private sector in this partnership. The banking institutions play a major role in the development process because of their responsibility to encourage and mobilise savings. And based on these savings, they provide credit to businessmen, investors and entrepreneurs who need funds for business activities involved in producing goods and services to meet the expanding demand in the home market as well as for export. In so doing they also provide employment and help to support a rising standard of living for Malaysians. However, for the banking institutions to be a strong partner to the business sector and to play a more effective facilitating role, they must themselves understand the economic policies and creed of the nation.

4. Malaysia's strategy for economic development is simple. The objective is to maintain low cost of living through curbing inflation while increasing incomes through higher productivity. In this way the standard of living of Malaysians will improve without Malaysia losing its competitive edge. With continued competitiveness Malaysia will continue to attract investment and increase its trade. In other words Malaysia will continue to grow economically. In view of the shortage of workers and in order to increase their productivity and accordingly their income, new high technology, high capital automated manufacturing industries will be given

priority.

5. This strategy calls for a complete reorientation not only on the part of the planners and those involved in promoting the Malaysian industrialisation programme, but it involves a change in the mindset of the bankers who will have to provide the funds for these capital intensive industries. Actually the adoption of this strategy is unavoidable, that is if we wish to continue our high growth objective.

6. There are some who believe that high growth will lead to economic overheating whose symptoms are high rates of inflation, upwards trend in wages and deficits in the balance of payment. It is worthwhile pointing out that high rates of growth in Japan in the 60s and 70s, in many instances double digit growth, did not result in deficits in the balance of payments. Instead there was a steady increase in surpluses in the balance of payment.

7. However as the yen was so cheap then, being only worth 1/3 of an American cent or US\$1.00 was equal to 300 yen, the Japanese allowed wages and prices to increase unchecked. The result was high inflation in domestic prices. Thus by the time of the Plaza Accord one rock melon was selling for RM250 and one kilo of Kobe beef was selling for as much as RM1,800. This high prices was all the more remarkable because Japan used to be the cheapest country to live in. In 1961 when I visited Japan for the first time, hotel rooms in a four star hotel was only RM60 and taxi fare was 40-60 Malaysian sen per kilometre. The standard of living was also very low.

8. Perhaps to improve the standard of living, wages were allowed to go up rapidly, outstepping the inflation rate. Under Prime Minister Ikeda the Japanese targeted a standard of living measured by ownership of three important household appliances. The small car was also introduced to enable the Japanese to own a motorcar or a small pick-up truck.

9. High wages and high cost of living in Yen did not affect Japanese competitiveness. This was because of the high productivity of the Japanese work force and of course the low value of the Yen relative to the currencies of Japan's trading partners.

10. The oil shocks disrupted Japan for a short while but as soon as prices steadied Japan reorganised its production so as to reduce cost. The result was rapid recovery and a return to the situation prior to the shock. The same happened when the value of the Yen was forced up by the other members of the Group of Seven. As soon as the exchange rate stabilised the Japanese industries became competitive again followed by good growth and a continuing surplus in the balance of payment. Recession set in only when the revaluation of the Yen was continuous leaving the Japanese economy breathless and their industries unable to adjust. Even then the balance of payment remains high.

11. There is apparently no definite relation between the balance of payment and the rate of growth. Indeed even when there is inflation, and revaluation of the currency, the balance of payment can remain unaffected. It is worthwhile to remember that when the Yen was revalued upwards the enormous Japanese imports of raw material including fuel was cheap. Even if the contribution of raw material and energy makes up a small percentage of production cost, it would still help Japanese products remain competitive.

12. The point I am trying to make is that a deficit in the balance of payment need not result from high growth, nor is inflation a necessary accompaniment of high growth. If we can hold down inflation and improve productivity, and consequently our export growth, we can counter the deficit in the balance of payment.

13. Whether a country has high growth or not, there can be inflation. There is no way a country can really effectively counter imported inflation. We can subsidise, as many countries do their fuel prices, but what it mean is that the Government is paying. In terms of the national economy there is still inflation.

14. We have to accept increases in the price of imports but the cost of essentials i.e. basic food items, working man's clothing, low-cost housing and public transport can be kept almost inflation free. It is these essential items which affect the cost of living of the average worker. For as long as their prices remain stable wages need not go up in order to maintain the same standard of living. If wages remain steady then production cost need not go up and our goods would remain competitive.

15. But it is not Government policy to keep wages fixed for all times as we would the price of essentials. We want the wages to go up so that the standard of living of even the ordinary workers can go up. It would be meaningless to attain developed country status if the living standards of our workers remain the same. But increases in wages must be related to productivity, i.e. producing more at the same unit cost or producing products with higher value.

16. Obviously there must be a limit to what a worker can produce through his own effort. To increase productivity new investments in new methods of production will have to be made to produce more of the same or better value added products. Even if productivity is the result of new investments the increase in company earnings must be shared with workers. This is only fair since any increase in productivity due to the workers efforts will also be shared by the owners.

17. The switch to high technology and high capital industries is intended to reduce labour inputs as well as increase the value of the products. In fact even labour intensive industries are the response to the need to increase productivity per worker as compared to the old disorganised worker-producer industries before the industrial age. The proposed switch is really a normal progression for an industrialising nation.

18. The question may be asked; can we do it? Can our workers accept retraining and new responsibilities, that of overseeing production machinery instead of handling the products at the various stages of production? Malaysian workers can. They have already demonstrated how rapidly they could acquire new skills. Given the right prospects and incentive they will learn and learn fast.

19. The problem will be in the readiness of investors to switch to high-tech capital intensive industries. As a corollary, will the financing institution be up to supporting the switch?

20. Malaysia will continue to need direct foreign investment. This will

involve well-known companies which bankers would be ever ready to lend money to. They are usually good pay masters. And bankers will be very confident of their technical knowhow and their forward and backward linkages. They will have the full backing of their parent companies. To lend to them would require little banking savvy. Banks can confidently lend blindfolded.

21. Unfortunately direct foreign investment will not contribute as much to the economy and the balance of payment equation as investment by local investors. Although Malaysia's trade is big and we are the 19th biggest trading nation in the world, much of this trade is done by foreign-owned industries. Their operation consist of importing parts, adding value to them and then exporting them. Obviously as exports grow, imports must also grow. In addition most of the earnings are repatriated tax-free. Very little is spent here, thus contributing little to the national economy and the balance of payment.

22. We do not grudge the foreign investors maximising their return. We have benefited greatly from their investment in this country, and we still want them to come. We certainly will need them for many of the high-tech industries that we are aiming for. Indeed for the Multi-media Super Corridor we are going to give them even more benefits, including 100 percent ownership and unrestricted employment of foreign knowledge workers.

23. But in order to really benefit from our industrialisation we need to have more local entrepreneurs going into manufacturing for exports. Naturally even if the local companies are wellknown they will not be in the same league as the huge multinationals of the Fortune 500 category. They are going to be relatively small and relatively inexperienced. Yet if they it is Government policy and drive which has contributed most to the present economic achievement of Malaysia.

29. Malaysian banks cannot forever be camp followers. The time has come for them to take the lead. We know that when Japan's economy was growing by leaps and bounds, the interest rate in Japan was very low, around three percent. Banks took equity in Japanese industrial entrepreneurs. Their representatives sat on the boards. Indeed the banks were often owned by the big industrial corporations. Earnings were invariably ploughed back for expansion and diversification.

30. I am not suggesting that as part of the Look East policy we adopt in toto the Japanese model. But surely there must be lessons to be learnt from the operation of the Japanese banks during the rapid post-war recovery of Japanese industry and commerce. As far as I know Malaysian banks do not take equity in business projects, much less in companies.

31. For economic expansion capital is absolutely necessary. Fortunately for us Malaysian saving habits are good. This of course is partly due to low inflation and a strong currency. Banks must encourage savings and make more capital available to the investors. They must take risk. Venture capital is difficult to come by in Malaysia. The small entrepreneurs have no credibility. The big ones are too big a risk.

32. If we are going to grow and grow in such a way as to increase our own wealth, including of course overcoming our balance of payment deficit, we

have to expand local investment in industries manufacturing for export. There will be risks. Someone will have to take the risk. If it is not the bank, then it must be the investor or the Government. We cannot expect banks to take all the risk but we can reasonably expect them to share the risk with the investor and the Government.

33. Lately we have been seeing a new phenomenon involving Malaysian businesses. At the urging of the Government, Malaysian companies have been investing abroad. This must cause at least some outflow of Malaysian capital. But we hope that the prosperity that our investments will bring to other countries will help create new markets for Malaysian products. This was what happened when the Japanese invested in Malaysia. We have now become such a good market for Japan that the biggest trade deficit we have is with that country.

34. We would prefer that our investors borrow from the banks in the countries they invest. But there must be occasions when they may need to borrow from Malaysian banks. If Malaysian banks are chary of lending for local manufacturing enterprises, how much more reluctant will they be to lend for business activities in foreign countries. For the small entrepreneur there is perhaps no hope at all. It would be a pity because some of these investments in foreign countries can result in the sourcing of numerous items from Malaysia i.e. they will help our exports.

35. We are concerned about outflows of our money. But foreign investments by Malaysians have long-term objectives, although immediate benefits can accrue to our country in many instances. Bankers must find ways and means to help. Prudence, yes. But bankers who want to be certain always, who will take no risk at all will become pure money-lenders or chettiars. I don't think you want to be that. I do hope you will play a role. We cannot get for you unlimited banking licences in other countries.

36. At the beginning I had emphasised the importance of partnership and complementarity between the Government and the private sectors in the development process. I stressed that the banking institutions form a part of this partnership. I pointed out that the banking institution play a major role in the development process.

37. Times have changed. We are the victim of our own success. We have to change strategies and methods. The Government has decided to change. I think the Malaysian investors are prepared to change. The question is, are the banks prepared to change? I leave this question with you.

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