

Rewriting
THE RULES

THE MALAYSIAN CRISIS
MANAGEMENT MODEL

MAHANI ZAINAL ABIDIN

Rewriting **THE RULES** THE MALAYSIAN CRISIS MANAGEMENT MODEL

*I thank Allah, the Almighty,
in whose hands lies all guidance*

*This book is dedicated to
Don and James Imran
with love*

Rewriting THE RULES

THE MALAYSIAN CRISIS
MANAGEMENT MODEL

MAHANI ZAINAL ABIDIN

PUSTAKA PERDANA



1004220

An imprint of Pearson Education

London · New York · Toronto · Sydney · Tokyo · Kuala Lumpur · Hong Kong · Cape Town
New Delhi · Madrid · Paris · Amsterdam · Munich · Milan · Stockholm



Published by
Prentice Hall
Pearson Malaysia Sdn. Bhd.
Lot 2, Jalan 215, Off Jalan Templer,
46050 Petaling Jaya,
Selangor, Malaysia
Tel: 03-77820466 Fax: 03-77853435

Pearson Education offices in Asia: *Bangkok, Beijing, Hong Kong, Jakarta, Manila, Kuala Lumpur, New Delhi, Seoul, Singapore, Taipei, Tokyo.*

Printed in Malaysia, KVP

ISBN 983-2473-22-5
Rewriting the Rules
Mahani Zainal Abidin

First published 2002

Perpustakaan Negara Malaysia Cataloguing-in-Publication Data

Mahani Zainal Abidin
Rewriting the rules: the Malaysian crisis management model
Mahani Zainal Abidin.
includes index
ISBN 983-2473-22-5
1. Monetary policy – Malaysia. 2. Crisis management – Malaysia.
3. Malaysia – Economic policy. I. Title.
332.4609595

Copyright © 2002 by Pearson Malaysia Sdn. Bhd.

All rights Reserved. This publication is protected by Copyright and permission should be obtained from the publisher prior to any prohibited reproduction, storage in a retrieval system, or transmitted in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise. For information regarding permission(s), write to: Rights and Permissions Department.



32243



Foreword



The Asian Financial Crisis was a watershed event that reshaped many Asian countries, not least the members of ASEAN. Although the worst is now thankfully over, and most of the affected economies have shown various degrees of recovery, the Crisis remains stubbornly with us. It not only influences and redefines our economic, social and political thoughts, but it also forms part of the economic realities of our region.

Malaysia's response to the Crisis attracted considerable comment and criticism, the latter mainly because we defied convention when we introduced capital controls and pegged the Ringgit. Now, as our economy recovers, we see growing acceptance and grudging respect of the Malaysian method. It will be many years however, before the events of the late 1990's can be seen in their true perspective. For now, the only relevant fact is that we met our primary objectives, and put the Malaysian economy back to work. Had we not done so, the Crisis could have led to both political and social instability. We were also equally convinced that, when markets fail, no government could abandon its "rakyat". We also draw confidence from the rigour of our research, debate and deliberations that led to the formulation of Malaysia's responses, as they were consistent with the best conventions of public policy making and governance.

Dr. Mahani is a member of the NEAC Working Group. This Group was specially convened to assist the National Economic Action Council, which formulated policy responses and action plans to address the impact and implications of the Crisis. Dr Mahani came to the Working Group from academic life, with high recommendations and objectivity, and clearly with none of the interests or preconceptions of a politician, administrator or businessman. When the peak of the Crisis had passed, and she spoke to me of her intention to document the past events, I thought it a good idea. "Rewriting the Rules: the Malaysian Crisis Management Model", provides a ringside view of our time of the Crisis. It will surely become an invaluable reference, both for the practitioners of national economic management and students of government.

A handwritten signature in black ink, appearing to read "Daim Zainuddin". The signature is stylized and fluid.

Daim Zainuddin

The People Page

When I started to do the final parts of the book, such as this acknowledgement page, I re-read the book, and belatedly realised that many organisations have been mentioned, but hardly any names of people. I have followed the conventional method of describing events in terms of organisations, their decisions, their achievements, and their shortcomings. This is a lot safer than a more personality-based approach, but leaves out a lot of important information. While organisations provided the framework in which the Crisis was played out, everything that happened was done by people. Therefore, I would like to acknowledge the people who have influenced and helped me in my work at the NEAC as well as in writing this book.

At the onset of the Crisis, I was teaching at Universiti Malaya (UM) and a bewildered observer of the turmoil. Then one day Tan Sri Thong Yaw Hong suggested my name to Tun Daim Zainuddin to join the NEAC Working Group. When Tun Daim decided to take me on, the UM agreed to the request for my secondment to the NEAC, and I record my appreciation to the management of the University for their cooperation.

My fellow NEAC Working Group members were Tan Sri Thong Yaw Hong, Tan Sri Wan Azmi Wan Hamzah and Datuk Dr. Zainal Aznam Yusof and they made me feel welcome at once and we became good friends. I had known Tan Sri Thong since my days at the Persatuan Ekonomi Malaysia (PEM) where he had supported our projects, particularly those for increasing the public awareness of economic issues. Tan Sri Thong's long and distinguished public service and especially his experience in the 1985 Malaysian economic crisis often helped us decide how the response measures should be implemented. Being a corporate player, Tan Sri Wan Azmi made sure we understood the Crisis from the private sector angle, including the causes, excesses and impact. Tan Sri Wan Azmi, thank you too for some irreverent opinions and lighter moments during our work. Datuk Dr. Zainal was always our idealist, and we often got the "how it should be" view from him. He was our media man, and often had to do the "graveyard shift" of late night TV appearances to explain the measures taken or the nature of the Crisis. The four of us developed excellent working relationships and personal friendships, forged in the intense heat of the Crisis. In the long hours spent together drafting the National Economic Recovery Plan (NERP) and in other NEAC work, I came to appreciate my colleagues dedication to the nation because they gave their unpaid contributions as a national service.

We had so much support from the NEAC Secretariat – Datuk Dr. Sulaiman Mahbob (Head of the Secretariat), Dr. Victor Wee, Dr. K. Govindan, Mohd. Saad Hashim, Dr. Muzahet Masruri, Adam Sulong, Harvinder Kaur, Ramzi Mansur and Julinda Mohd. Amin. Murtadza Mohd. Kassim from the NEAC Secretariat proved to be an expert at arranging meetings at short notice, with a blend of endless tact and relentless persistence.

We also worked alongside the NEAC Communications Team and I admired the way they got our decisions explained so well and simply. Among the Communications Team members, I would like to mention and thank Elena Shamsudin, who has since moved to the NEAC Special Consultancy Team on Globalisation, for her good work and commitment. Asgari Stephens, who was also on that Team, showed me the intricacy of financial entrepreneurship and our friendship has continued beyond NEAC. Other members of the Team were K. C. Leong, Azman Awaluddin, Jacqueline Teo and Sharon Saw.

The staff of Tun Daim's office were important in the functioning of the NEAC. I thank Mei Chuan, who is Tun Daim's super efficient private secretary, for many kindnesses. Abdul Rashid Mohd. Yusof, Badrul Hisham Mahzan, Rabbi Royan, Mohd. Gazali Abas, Suhaimi Kamaralzaman, Nik Azman Nik Abdul Majid, Tuminah Parto, Rosma Latiff, Jaafar Mat Zain and Hussin Abdul Hamid all helped our work too.

The Economic Planning Unit (EPU) was most helpful in the establishment of the NEAC and its operations. The EPU was generous in supplying office facilities but its most critical contribution was the secondment of its staff, who drafted large parts of the NERP. Their input has allowed us to quickly formulate the response measures. Tan Sri Dr. Samsudin Hitam, the former Deputy Director General of EPU, did a lot to make sure that NEAC functioned smoothly.

When the idea or "ilham" of this book appeared, I have Lyn Chai (formerly from the NEAC Communications Team) and Hardev Kaur (from the New Straits Times) to blame or thank for it. As the idea developed they have continued to show an interest too, insisting that the book should not be an economic tome but a book for the general public. Many a time Lyn also provided a reality check. As the work on the book progressed, I came to rely a lot on Norol Asma' Ruzi for her excellent research assistance and for her giving-up many weekends. For the tedium of editing, polishing graphics and cross checking facts and data I was fortunate to have the eagle eyes of Wan Khatina Nawawi, an economist who had followed the Crisis closely.

Discussion with Mohamed Ibrahim, the former Managing Director of Danamodal gave me the real picture of how Malaysia operationalised the capital controls. Marianus Vong, also from Danamodal was kind enough to provide the details of restructuring measures. NEAC continued to make their files available, where confidentiality allowed. As I am not well versed on

politics and public administration, Dato' Abdullah Abdul Rahman was particularly helpful in explaining key concepts about leadership. I am specially thankful to cartoonist Lat for his permission to include three of his drawings, published at the time of the Crisis. They inimitably captured the mood of the time. Cartoonist Lat has also drawn a picture specially for the book and it is on page xx. Kelvin Kallaugher gave permission to print his cameo on the stockmarket behaviour. The Faculty of Economics and Administration, UM, made available their facilities while the Edge newspaper offered the use of their charts to summarise the performance of the Malaysian economy. Ebi Azly Abdullah and Ahmad Azmi Ariffin were very resourceful in getting the pictures for this book. My thanks to the Information Department and Bernama, the national news agency, for these pictures.

I was flattered and grateful that the Prime Minister, Dr. Mahathir Mohamed, found some hours in his schedule to give his views on many important issues relating to the Crisis. His answers show the strength of the forces arraigned against Malaysia, and we should all be thankful for his single-mindedness and wisdom in charting Malaysia's own solution. My appreciation to the following leaders for their briefing: Tan Sri Nor Mohamed Yakcop (the Financial Adviser to the Prime Minister) on the idea of capital controls; Tan Sri Ali Abul Hassan (the Economic Adviser to the Prime Minister) on the setting-up of NEAC; Tan Sri Dr. Noordin Sopiee (Chairman and CEO of the Institute of Strategic and International Studies) on deliberations of the NEAC Exco; Tan Sri Dr. Zeti Akhtar Aziz (Governor of the Bank Negara Malaysia) on the Bank's role in implementing the capital controls; and Datuk Azman Yahya, (former Managing Director of Danaharta) on the formation and operation of Danaharta. The experience and insights of these major participants of the Crisis have helped me to make sense of what was previously just a tangle of disconnected facts.

I have used my academic and personal friends more than they have known. Their ideas have been adapted shamelessly in the hope of getting some academic credibility into this work. I start with Dr. R. Thillainathan, the former President of the PEM, who I believe has never completely left academia, even though he is now prominent in the private sector. I hope he is not offended. Prof. K.S Jomo has been a reliable sparing partner – if he disagrees I know that I have a very strong probability of being right. Dr. Mohamed Ariff and Dr. Tham Siew Yean stood as steady references. Many foreign academic friends asked challenging and thought provoking questions about the Malaysian approach as most of them are from the conventional school of economic thought.

Khoo Siew Mun, Prof. Shyamala Nagaraj, Prof. Sieh Mei Ling and Dr. Khadijah Khalid are a continuing link to UM and their interest and encouragement have helped to renew my sometimes flagging energy. Friday

lunches with Wan Norhayati Ibrahim, Datuk Latifah Merican-Cheong, Hardev Kaur and Zaiton Hasan unsurprisingly turned into an enjoyable, stimulating yet open discussion. Din Merican made available constructive reference materials.

As I continue with the work at the Globalisation Team at the NEAC, Dato' Mustapa Mohamed, the Executive Director of NEAC, has been most supportive, and I thank him for his indulgence in allowing me to finish this book.

More than anyone, Tun Daim has been a great influence on my work at NEAC and on this book. I would like to thank him for his trust and guidance. Mostly by example, he taught me economy of words, which I have not managed to emulate, and insistence on accuracy, where I hope I have done better. I am also amazed at his ability and stamina to read and digest the mountain of notes, memoranda and papers that were put on his desk and then to remember them in great detail. His decisiveness and drive are incomparable, in my limited experience.

I hope this book has provided a comprehensive story about Malaysia's Crisis management method.

Mahani Zainal Abidin
August 2002
Putrajaya

Contents

PROLOGUE: Rewriting the Rules	1
CHAPTER 1 National Economic Action Council	23
The Start of the Response Process	23
NEAC: The Idea of Its Formation	24
Objectives of the NEAC	26
Structure and Membership	27
Modus Operandi	31
Relationship with the Cabinet	32
Meetings of the Executive Director	35
The Meetings	36
Findings of the Meetings	46
NEAC Exco Deliberations	48
Effectiveness of the NEAC	51
Sense of urgency	51
Consolidated approach	52
Extraordinary Solutions to Meet on Extraordinary Challenge	54
CHAPTER 2 The Onslaught	59
From Darling to Villain	59
The Onset of Trouble	62
Foreign Reports	65
Domestic Confidence	73
NEAC Confidence Building Initiatives	76
Confidence and Economic Management	77
CHAPTER 3 Recovery Measures	81
The Ground work Has Been Done	81
Considerations in Formulating the NERP	82
Revival of the Domestic Economy	83
Exchange Rate Stability	84
Domestic and International Confidence	85
Financial Stability	86
Liquidity	87
Socio-economic Stability	88
Affected Sectors	89

The National Economic Recovery Plan	90
Tun Daim's speech	90
The Measures	91
Mechanism of NERP	95
Financing of the Plan	99
Financing Needs	99
Sources of Financing	100
Risks and Challenges	103
CHAPTER 4 Selective Capital Controls	109
The Plunging Ringgit	109
The Genesis of the Idea	110
The Currency Trader	110
Initial Moves to Support the Ringgit	112
The Environment that Pushed for the Selective Capital Controls	113
Debate	114
Selective Capital Controls: the Measures	117
Reasons for Choosing the Package	117
Why Control Outflow	118
The Measures	119
How the ringgit was Fixed	120
The Devil is in the Detail	121
Critical Components of the Implementation Mechanism	123
Operational Mechanism	124
Implementation Difficulties	126
CLOB	127
Reactions	130
Domestic Reaction	132
International Reaction	132
Reaction by Investors	134
Amendment to the Selective Capital Controls	135
An Extraordinary Solutions that Works	136
CHAPTER 5 Restructuring the Economy	143
Why Restructure?	143
What Needs to be Done?	143

Danaharta	147
Legislative Framework	147
Danaharta Lifecycle	148
Operations	149
Management of Acquired NPLs	150
Financing Resources	154
Reasons for Danaharta's Success	155
Danamodal	157
Governance and Management	158
Danamodal Operation	158
Financing of the Recapitalisation Exercise	161
Utilisation of Funds	162
Restructuring and Monitoring	165
Outcome of Danamodal's work	166
Corporate Debt Restructuring Committee (CDRC)	170
Progress of CDRC	171
Evaluation of CDRC Work	172
Banking Sector Restructuring	174
Review of the Malaysian Restructuring Programme	176
CHAPTER 6 Revitalising the Economy	183
Recovery Came Sooner Than Expected	183
Recovery	184
Contributory Factors	194
Challenges During the Recovery Period	196
Prognosis of Recovery	199
CHAPTER 7 Can the Malaysian Measures Be Copied?	203
How did Crisis-affected Countries Fare?	203
Pre-Crisis Economic Conditions	207
The Impact of the Crisis	212
Response Policies	218
Financial and Debt Restructuring Programme	227
Exchange Rate Regime	235
Were the Malaysian Measures Unique?	235
Can the Malaysian Measures be Copied?	241

CHAPTER 8 Learning from the Crisis: The Way Forward	249
After the Hurricane	249
Lessons	251
Independent Thinking	251
Effective Leadership	253
Prudent Policies During The Period Of High Growth	255
Crisis Management	257
Effective Implementation	258
Social Balance	259
Personal views	260
The Way Forward	265
Interview with PM	271
AFTERWORD: The New Malaysian Economy	279
Appendix A	283
References	287
Index	295

List of Tables and Charts

TABLES

Table 3.1	Funding Requirements for the Recovery Plan, 1998–2000	99
Table 3.2	Sources of Financing for the Recovery Plan	101
Table 3.3	Fund Utilised for the Recovery Programmes	102
Table 5.1	Acquired and Managed Loans by Sector	151
Table 5.2	Danaharta Financing Resources	155
Table 5.3	Banking Institutions' Recapitalisation Requirements	159
Table 5.4	Danamodal: Sources of Funding	162
Table 5.5	Danamodal's Investment in Recapitalised Banking Institutions	164
Table 5.6	Performance of Recapitalised Banking Institutions	167
Table 5.7	Recapitalisation of the Banking Sector: Regional Comparison	169
Table 5.8	Progress of CDRC Cases	173
Table 6.1	Malaysia: GDP Growth Rate	186
Table 6.2	Flow of Funds Through External/Special Accounts in as at 23 Nov 2000	198
Table 7.1	1999 and 2000 Performance for Indonesia, Malaysia, South Korea and Thailand	206
Table 7.2	Key Economic Indicators for Indonesia, Malaysia, South Korea and Thailand 1996–1998	209
Table 7.2	Key Economic Indicators for Indonesia, Malaysia, South Korea and Thailand 1996–1998	210
Table 7.3	Short-term Foreign Debt and Foreign Exchange Reserves, 1996	212
Table 7.4	Capital Flows to the Four Affected Countries	215
Table 7.5	Rate of Depreciation of the Four Countries' Currencies	217
Table 7.6	Indicators of the Impact of Crisis on Households	218
Table 7.7	Response Policies for Four Crisis Countries	220
Table 7.8	Monetary Policy of the Crisis Economies	224
Table 7.9	Social Programmes in East Asia during the Crisis	226
Table 7.10	Debt and Financial Restructuring	229

CHARTS

Chart A 1996: On Path to Wawasan 2020	10
Chart B 1997: Turmoil	11
Chart C 1998: Panic, Trauma and Drama	12
Chart D 1999: Recovery	13
Chart E 2000: Consolation	14
Figure 1.1 Structure of the NEAC	27
Figure 2.1 Ringgit Exchange Rate and KLSE Composite Index March 1997 to August 1998	62
Figure 3.1 Mechanism of NERP	95
Figure 5.1 Governance Structure of Restructuring Agencies	146
Figure 5.2 Relationship between Restructuring Agencies	146
Figure 5.3 Lifecycle of Danaharta	149
Figure 5.4 NPLs Carve-out as at 31 March 2000	151
Figure 5.5 Approach to Management of Non-Performing Loans	152
Figure 5.6 Stages of Danamodal's Operation	159
Figure 5.7 Resolution of 25 Banking Institutions' (BIs) Capital Adequacy Position	160
Figure 6.1 Production Indices	187
Figure 6.2 Consumption Indicator: Import of consumption goods	187
Figure 6.3 Consumption Indicator: Sales and Services tax	188
Figure 6.4 Kuala Lumpur Stock Market Performance	189
Figure 6.5 Investment indicators: Import of capital and Intermediate goods	190
Figure 6.6 Loans disbursement	190
Figure 6.7 Capacity utilisation	191
Figure 6.8 Labour Retrenchment	191
Figure 6.9 Trade performance	192
Figure 6.10 Malaysia's International Reserves	193
Figure 7.1 Incremental Capital – Output Ratio	208
Figure 7.2 Stockmarket Performance Index (% Change)	216
Figure 7.3 NPLs as % of Total Loans	216

Abbreviations

ADB	Asian Development Bank
AFTA	ASEAN Free Trade Area
AMC	Asset Management Company
ASEAN	Association of South East Asian Nations
BAFIA	Banking and Financial Institutions Act
BBMB	Bank Bumiputra Malaysia Berhad
BIs	Banking Institutions
BIS	Bank of International Settlement
BLR	Base Lending Rate
BN	Barisan Nasional (the ruling coalition)
BNM	Bank Negara Malaysia (the Malaysian central bank)
CAMEL	Capital adequacy, Asset quality, Management, Earnings and Liquidity
CAR	Capital Adequacy Ratio
CDP	Central Depository (Pte) Ltd.
CDRC	Corporate Debt Restructuring Committee
CDS	Central Depository System
CLOB	Central Limit Order Book International
CPI	Consumer Price Index
CSFB	Credit Swiss First Boston
Danaharta	Pengurusan Danaharta Nasional Berhad
Danamodal	Danamodal Nasional Berhad
Dewan Negara	The Upper House
Dewan Rakyat	The Parliament
EON Berhad	Edaran Otomobil Nasional Berhad
EPF	Employees' Provident Fund
EPU	Economic Planning Unit
ESCL	Exchangeable Subordinated Capital Loan
EXCO	Executive Committee
EXIM Bank	Export Import Bank
FDI	Foreign Direct Investment
FDIC	Federal Deposit Insurance Corporation
FIs	Financial Institutions
GDP	Gross Domestic Product
GNP	Gross National Product
IBRA	Indonesian Bank Restructuring Agency

IBRD	International Bank for Reconstruction & Development
ICOR	Incremental Capital-Output Ratio
IFC	International Finance Corporation
IHT	International Herald Tribune
IMF	International Monetary Fund
INCEPS	Irredeemable Non-Cumulative Convertible (Exchangeable) Preference Shares
IPI	Industrial Production Index
IPOs	Initial Public Offerings
KAMPO	Korean Asset Management Company
KLCI	Kuala Lumpur Stock Exchange Composite Index
KLIBOR	Kuala Lumpur Interbank Offered Rate
KLSE	Kuala Lumpur Stock Exchange
LRT	Light Rail Transit
MCD	Malaysian Central Depository Sdn. Bhd.
MIDA	Malaysian Industrial Development Authority
MIER	Malaysian Institute of Economic Research
MoF	Ministry of Finance
MSCI	Morgan Stanley Capital International
MTUC	Malaysian Trade Union Congress
NCT	NEAC Communications Team
NDP	New Development Policy
NEAC	National Economic Action Council
NEP	New Economic Policy
NERP	National Economic Recovery Plan
NGOs	Non-Governmental Organisations
NOC	National Operation Council
NPLs	Non-performing Loans
NST	New Strait Times
NUBE	National Union of Bank Employees
OECD	Organisation of Economic Cooperation and Development
PAS	Parti Islam Setanah Melayu
PLUS	Projek Lebuhraya Utara Selatan (North-South Highway Project)
PM	Prime Minister
ROC	Registrar of Companies
RTC	Resolution Trust Corporation
RWCR	Risk-weighted Capital Adequacy Ratio
SA	Special Administrator
SBCs	Stockbroking Companies
SC	Securities Commission

SCANS	Securities Clearing Automated Network Services Sdn. Bhd.
SGX	Singapore Exchange Ltd.
SIMEX	Singapore International Monetary Exchange
SPV	Special Purpose Vehicle
SRR	Statutory Reserve Requirement
SSB	Salomon Smith Barney
UEM	United Engineers Malaysia Berhad
UMNO	United Malay National Organisation
VAT	Value Added Tax
WTO	World Trade Organisation
1Q	First Quarter
2Q	Second Quarter
3Q	Third Quarter
4Q	Fourth Quarter
1H	First Half
2H	Second Half

