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# Recapitalisation and Consolidation of the Banking Sector

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*Statement by the Finance Minister*

## Introduction

The banking system in Malaysia has remained relatively resilient amidst the regional financial turmoil. Past initiatives to develop and strengthen the banking system have placed the banking system in a better position to withstand the present economic crisis. Nonetheless, a prolonged economic downturn may place further stress on the banking system.

Under current economic conditions, it is inevitable that non-performing loans would continue to rise. Nevertheless, a number of pre-emptive measures have been put in place to ensure that NPLs would remain at manageable levels. Among the recent pre-emptive initiatives that have been introduced is the establishment of the Asset Management Company known as Pengurusan Danaharta Nasional Berhad. Danaharta was established to help remove the non-performing loans distraction from banking institutions so that they can give greater emphasis to provide financing to viable businesses and productive economic activities to accelerate the economic recovery process.

## Rationale

Given the important intermediation role played by the banking sector in the economy, it is crucial that the banking sector is further strengthened as a weak banking sector can exacerbate and prolong the economic slowdown. In this regard, the banking system must also be well capitalised to be able to absorb higher business risks and enhance their ability to generate new loans to support the next phase of economic growth.

If the economic crisis prolongs, the rising level of non-performing loans would continue to erode the capital base of the banking institutions. Hence, we must address the issue of recapitalising the banking sector to further strengthen the resilience of the banking sector. As Danaharta was set up to help remove NPLs from the banking system, there is a need for us to explore other pre-emptive alternatives to recapitalise the banking system. In this regard, I hereby wish to announce the establishment of a special purpose vehicle (SPV) to spearhead the recapitalisation exercise of the banking sector. The SPV would complement Danaharta to reinforce the ability of the banking institutions to play a more meaningful role in the future development of the Malaysian economy.

The main objective of the SPV is to recapitalise the banking system to healthy levels. It would also serve as a catalyst to consolidate and rationalise the banking sector as well as to accelerate the formation of a core of strong domestic banks to spearhead the development of the banking system.

Through the SPV, we would adopt a flexible two-pronged approach:-

- To further strengthen the core banking institutions and recapitalise the weaker institutions The SPV would inject capital into core domestic banks to further strengthen their resilience to meet greater domestic and international competition. The SPV would also recapitalise the weaker institutions through injection of fresh capital;
- To consolidate the banking sector As a strategic shareholder in a number of core and weak banking institutions, the SPV would then merge the institutions to consolidate the banking system.

We have also observed that there are strong linkages between the shareholders and market confidence on the strength of the banking institutions. In this regard, the SPV does not preclude the option of purchasing stakes from weak shareholders where there are strong beliefs that these weak shareholders would not have

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the capacity to meet the recapitalisation needs of the banking institutions. This would be in line with our policy to institutionalise the shareholding structure of the banking institutions. Nonetheless, any consideration paid to the existing shareholders would be set at fair market values. The parameters against which the agency is established, its general organisation and operating mechanism would be made transparent with maximum disclosure.

The SPV would also be expected to play an important role to restructure the banking institutions and utilise relevant expertise to provide benchmarks on best practices to revamp the management of the banking institutions. This would be in line with its role as a strategic shareholder to further strengthen the resilience of the banking institutions.

#### Structure of SPV

The establishment of the SPV would be initiated by Bank Negara Malaysia. Bank Negara Malaysia would provide the seed capital and would also invite reputable multilateral agencies to play an active role in this SPV. With strong and credible shareholders, the SPV would be able to raise additional funding through the issuance of Ringgit bonds.

#### Lifespan of SPV

As the SPV is set up for a specific objective, it would have a finite life. Once it has achieved its ultimate objective and fulfilled its role in the economic recovery programme, it would then sell its stakes in the banking institutions.

#### Financing Requirements

NPLs (on a net basis) have risen to 8.4% as at end-May 1998 compared with 4.7% as at end-December 1997. If the conditions under the worst case scenario materialise, the projected recapitalisation required for the banking system to maintain the RWCR at not less than 9% would be in the region of RM16 billion over the period 1998 and 1999.

#### Operating and Financing Arrangements

Bank Negara Malaysia together with international consultants will work out operational details and financing arrangements of the SPV.

#### Conclusion

The SPV would be the focal point in our efforts to strengthen and consolidate the banking system. The consolidation and rationalisation exercise of the banking system would ensure that the system is resilient enough to withstand further shocks. The consolidation exercise would also further enhance the competitiveness and efficiency of the banking system so that it can support the next phase of economic development and more importantly, it will be able to generate its own growth momentum to be a significant contributor to GDP. The recapitalisation of the banking sector would also help to restore domestic and foreign confidence and would serve as a catalyst in accelerating the economic recovery process.

#### Bank Negara Malaysia 13 Jul 1998

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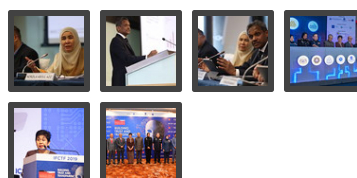
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