Bank Negara Malaysia

Statutory Requirements

In accordance with section 48 of the Central Bank of Malaysia Act 1958, Bank Negara Malaysia hereby publishes and has transmitted to the Minister of Finance a copy of this Annual Report together with a copy of its Annual Accounts for the year ended 31 December 1999, which have been examined and certified by the Auditor-General. The Annual Accounts will also be published in the *Gazette*.

Tan Sri Dato' Seri Ali Abul Hassan bin Sulaiman
Chairman
Board of Directors

31 March 2000

Bank Negara Malaysia

Board of Directors

Tan Sri Dato' Seri Ali Abul Hassan bin Sulaiman
P.S.M., S.S.M.T., D.G.P.N., D.G.S.M., D.S.P.N., J.S.M., D.J.N., A.M.N., Hon. DCL (Northumbria, UK)
Governor and Chairman

Dr. Zeti Akhtar Aziz
D.P.M.J.
Deputy Governor

Tan Sri Datuk Dr. Aris bin Othman *(term of appointment was completed on 6 June 1999)*
P.S.M., P.J.N., K.M.N.
Secretary General to the Treasury

Dato' Othman bin Mohd. Rijal *(appointed on 7 June 1999)*
D.S.S.A., P.G.D.K., J.S.M., S.M.S., K.M.N.
Secretary General to the Treasury

Datuk Oh Siew Nam
P.J.N.

Dato' Muhammad Ali bin Hashim
S.P.M.J., D.P.M.J., J.S.M., S.M.J., P.P.B.

Tan Sri Datuk Amar Haji Bujang bin Mohd. Nor
P.S.M., D.A., P.N.B.S., J.S.M., J.B.S., A.M.N., P.B.J.

Tan Sri Dato' Dr. Mohd. Noordin bin Md. Sopiee
P.S.M., D.I.M.P., D.M.S.M.

Tan Sri Kishu Tirathrai *(term of appointment was completed on 31 January 2000)*
P.S.M.

Datuk N. Sadasivan a/l N.N. Pillay *(appointed on 1 February 2000)*
D.P.M.P., J.S.M., K.M.N.

Senior Staff

Governor	Tan Sri Dato' Seri Ali Abul Hassan bin Sulaiman
Deputy Governor	Dr. Zeti Akhtar Aziz
Adviser	Dato' Nor Mohamed bin Yakcop
Assistant Governor	Datuk Zamani bin Abdul Ghani
Assistant Governor	Datuk Dr. Awang Adek bin Hussin
Assistant Governor	Dato' Mohamad Daud bin Hj. Dol Moin
Assistant Governor	Mohamed Yusof bin Ahmad Muhaiyuddin
Assistant Governor	Dato' Huang Sin Cheng
Assistant Governor	Latifah Merican Cheong
Director	
Economics I	Ismail bin Alowi
Economics II	Dr. Phang Hooi Eng
Bank Regulation	Nor Shamsiah binti Mohd Yunus
Investment and Treasury	Lillian Leong Bee Lian
Bank Supervision I	Azizan bin Haji Abd Rahman
Bank Supervision II	Wong Yew Sen
Insurance Regulation	Zakaria Ismail
Insurance Supervision	Donald Joshua Jaganathan
Exchange Control	Bakarudin bin Ishak
Payment Systems	Che Sab bin Ahmad
Information Services	Ramli bin Saad
Finance	Abdul Aziz bin Abdul Manaf
Human Resource Management	Mainor Awang
Head of Department	
Corporate Services	Mohd Nor bin Mashor
Legal	Gopala Krishnan Sundaram
Statistical Services	Chan Yan Kit
Internal Audit	Yahaya bin Haji Besah
Human Resource Development Centre	Essah binti Yusoff
Special Investigation	S. Indralingam
Information Systems Supervision	Norainy binti Mohd Sahid
Risk Management	Teo Kee Tian
Currency Management and Operation	Hor Weng Keng
Property and Services	Maksom bin Kasan Widi
Security	Che Norudin bin Che Alli
Strategic Planning	-
Development Financial Institutions	-
Manager	
London Representative Office	Ab Razak bin Che Yusoff
New York Representative Office	Tan Sook Peng
Branch Manager	
Pulau Pinang	Kamalullail bin Ramli
Johor Bahru	Ahmad bin Ismail
Kota Kinabalu	Radin Nor Azam bin Radin Suhadi
Kuching	Marlene Margaret ak John Nichol
Kuala Terengganu	Md. Daud bin Dahar
Shah Alam	Hamzah bin Abu Bakar

Foreword

The Malaysian economy and financial sector turned around in 1999. Confidence was restored as evident in the rise in domestic consumer and investor activity; the rebound in stock market activity; the narrowing of credit spreads on Malaysian bonds; and the return of portfolio inflows into Malaysia. Significant progress has also been made in the financial sector, particularly in terms of the restructuring and merger of banking institutions. The risk-weighted capital ratio of the banking system has improved considerably as the banking system returned to profitability in 1999. The formation of the ten domestic banking groups arising from the current merger programme will further strengthen the banking industry to meet greater challenges in the future.

At the corporate level, there has been a trend towards deleveraging, while significant progress has also been achieved in the restructuring of corporate debt. This has enabled companies to better manage their funding risks and reduce their vulnerability to abrupt changes in interest rates. The greater efficiency in the use of resources (particularly imported capital goods) and the divestment of non-core activities have allowed companies to concentrate in industries in which the competitive edge is enhanced, niche markets tapped while at the same time reduce potential strains on the nation's balance of payments.

The economic recovery in Malaysia has been significant in many ways. The introduction of the selective exchange control policy was of paramount importance in restoring stability to the economy. At the same time, it provided flexibility for the Government to implement the appropriate monetary and fiscal policies to accelerate economic recovery. The speed and magnitude of the recovery have surpassed even the most optimistic market expectations. In the management of the crisis, Malaysia had consciously incorporated the social agenda into its recovery programme, to minimise social costs and dislocations. In the process, this has not only protected the social fabric of Malaysia but also ensured stable conditions to preserve investments and incomes of individuals and enterprises including foreign investors. In addition, an active debt management policy ensured that the external borrowings of the country were contained at manageable levels, which made Malaysia less vulnerable to exchange and interest rate developments abroad. Furthermore, Malaysia's recovery programme ensured that the private sector absorbed the costs of restructuring so that the impact on the public sector finances has been reduced. As a result, the burden of financing the adjustment to be borne by future generations will be minimised.

As the Malaysian recovery gathered momentum in the course of 1999, the international community, including the IMF, has acknowledged that there is no standard prescription to crisis management, given the diverse stage of development, structure, and circumstances of each economy. In an environment of highly destabilising and unrestrained capital flows, the

Malaysian approach to crisis management is a viable option that has produced results. In this context, the experience of East Asia has highlighted the need to address the adverse consequences of unregulated capital flows, examine the role of large market players and introduce greater accountability in the practices in financial centres offshore.

The experience of Malaysia during the crisis has made Malaysians more aware of the vulnerabilities confronting the economy. Far from being complacent, there is general awareness of the need to actively embark on efforts to seek new approaches to achieve greater heights of economic success and a better standard of living for all Malaysians. We need to position ourselves to promote sustainable growth under the new environment where technology, skills and innovation are the main drivers to enhance efficiency and competitiveness in this more globalised environment. In this regard, the Government has already embarked on a long-term strategy of accelerating the transformation of the economy towards a knowledge-based economy and growth in new areas which would be based on information, communication and technology. This requires a co-ordinated approach in engineering the transformation of the Malaysian economy into the next phase of economic development.

In the real sector, Malaysia has made a head start in infrastructure investments in information technology. Malaysia is now embarking on the next step to raise potential output by emphasising on increases in efficiency of capital investments. The narrowing of the output gap continues to be an issue of concern, due to the less than optimal complementarities between labour, skills and technology. Increasing investment alone to expand the output gap is insufficient, and could result in a further funding mismatch given the stage of development of the capital market at this juncture. Growth in the medium term would, therefore, need to be productivity-driven. Greater emphasis will be placed on skills development. In this regard, the Eighth Malaysia Plan (2001-2005) will represent an important framework to review Malaysia's strategies to chart the next phase of industrialisation and economic development.

In the financial sector, the challenge is to promote a dynamic and innovative financial system that has the capacity and ability to support the country's economic transformation. Of importance is the need to develop alternative financing mechanisms such as venture capital financing, "business angel" investment and "specialist seed capital" firms to support high-risk investment. It is also important to ensure that all players understand fully, and possess the necessary skills to deal with, the new risks involved and have in place internal controls and effective risk management systems. The establishment of the Malaysian Exchange of Securities Dealing & Automated Quotation Berhad, marks an important milestone in providing alternative financing avenues for growth and technology companies, and serving as an exit mechanism for venture capital companies. Equally important is the development of instruments that enable economic agents to better manage risks and allow the risks to be borne by those most able to manage these risks.

The Government, on its part, will continue to maintain a proactive approach in the development of the financial system to create a competitive, strong and resilient financial sector. The authorities will remain vigilant and take the necessary measures to continually strengthen the financial system and maintain financial stability. For the further development of the financial sector, progress is well underway to formulate the master plans for the financial system and the capital market, and the National Bond Market Committee is providing the impetus for the development of the bond market. In addition to providing the means for raising funds in a more effective manner, these initiatives will also help to chart the strategic positioning and future direction of the financial system so that the Malaysian financial institutions can effectively position themselves to face the challenges as the operating environment becomes increasingly liberalised and globalised. The accelerated pace of financial reforms underlines Malaysia's firm commitment to enhance the competitiveness of the sector. In formulating the framework for the financial sector, however, an important consideration is the proper sequencing between capacity building and reforms in the financial sector. The recent crisis has underscored the importance of proper sequencing in liberalising the financial markets to ensure that the associated risks are maintained at a prudent and manageable level. Such an approach is essential to ensure that Malaysia enjoys the full benefits of globalisation.

The financial reforms will also ensure that Malaysia has a core of strong and forward looking domestic financial institutions that can excel in a changing global environment through capacity building efforts with the enhancements of the necessary skills and technology base. In this regard, the recent consolidation exercise of the domestic banking institutions into ten banking groups represents an important step to transform the financial sector towards meeting the new challenges as well as the objective of supporting sustainable economic growth. Banking institutions that are well-capitalised would be able to enjoy economies of scale, while allowing them to have greater investment in information technology to remain competitive and efficient. At the same time, Bank Negara has also embarked on measures to encourage the consolidation of the insurance industry through mergers and acquisitions among insurers.

Measures to develop a more resilient corporate and banking sector have also been intensified through reforms to address areas of vulnerabilities as well as potential risks. Greater emphasis has been placed to improve corporate governance, enhance asset-liability management of corporations and banking institutions; and to avoid the problem of funding mismatch. While the overall leverage of the economy has been relatively stable and funded mainly by domestic bank borrowings, the maturity mismatch of some companies, have rendered such companies (and consequently banks) vulnerable to a sudden change in liquidity conditions, as experienced during the height of the crisis. As plans to implement a more stringent liquidity management framework and a comprehensive stringent capitalisation requirement for banking institutions come on stream, and a prudent asset-liability management strategy is put in place, the corporate and banking sectors will be well placed to absorb any eventuality or shocks.

The Government recognises that an important pre-requisite in encouraging the private sector to seek new opportunities is the creation of an environment of certainty and stability. Towards this end, the Government will continue to pursue stability-oriented macroeconomic policies. Balanced and consistent macroeconomic policy will be emphasised to ensure that current policies to revive economic activity will not lead to undesirable developments such as renewed inflationary pressures or external imbalances in the medium term. It is only under an environment of stability that the broader goals of public policy have the best chance of being realised. The Government will remain prudent in managing its fiscal policy, with emphasis on the quality and efficiency of public spending. While the conduct of monetary policy will continue to complement the fiscal policy stance, Bank Negara will remain vigilant against any signs of incipient inflationary pressures. A major priority of policy will be to ensure that the large inflows of capital within a fixed exchange rate regime and the increase in bank lending will not be a source of instability that could result in asset price inflation and, ultimately, inflationary pressures. An important consideration will be to ensure consistency between the exchange rate regime and the underlying macroeconomic policy framework.

While Malaysia and other crisis-affected countries have expedited the necessary economic and financial restructuring, the threat to stability posed by the unregulated financial flows, however, remains. Although international discussions have been proceeding on in numerous fora over the past two years, there is still no clear prospect of any concrete fundamental change taking place in the foreseeable future to implement reforms to strengthen the international financial architecture, and in re-defining the role of the international financial institutions. Under the current circumstances, small, open economies such as Malaysia, will remain vulnerable to market excesses and tendencies, which would create undue volatility and destabilising consequences on fundamentally sound economies. The Government remains committed to the market system and to a mutually beneficial engagement in the global economy. However, in the absence of global solution against volatile capital flows, individual countries will trend towards maintaining safeguards and toward strengthening regional integration.

A shared global growth is the key to enhance the prospects for long-term economic prosperity in this age of globalisation. Malaysia, on its part, will continue with its economic and financial reforms to ensure that its efforts to achieve sustainable growth in an environment of stable prices are well within its reach without creating unnecessary imbalances.

29 March 2000

Tan Sri Dato' Seri Ali Abul Hassan bin Sulaiman
Governor

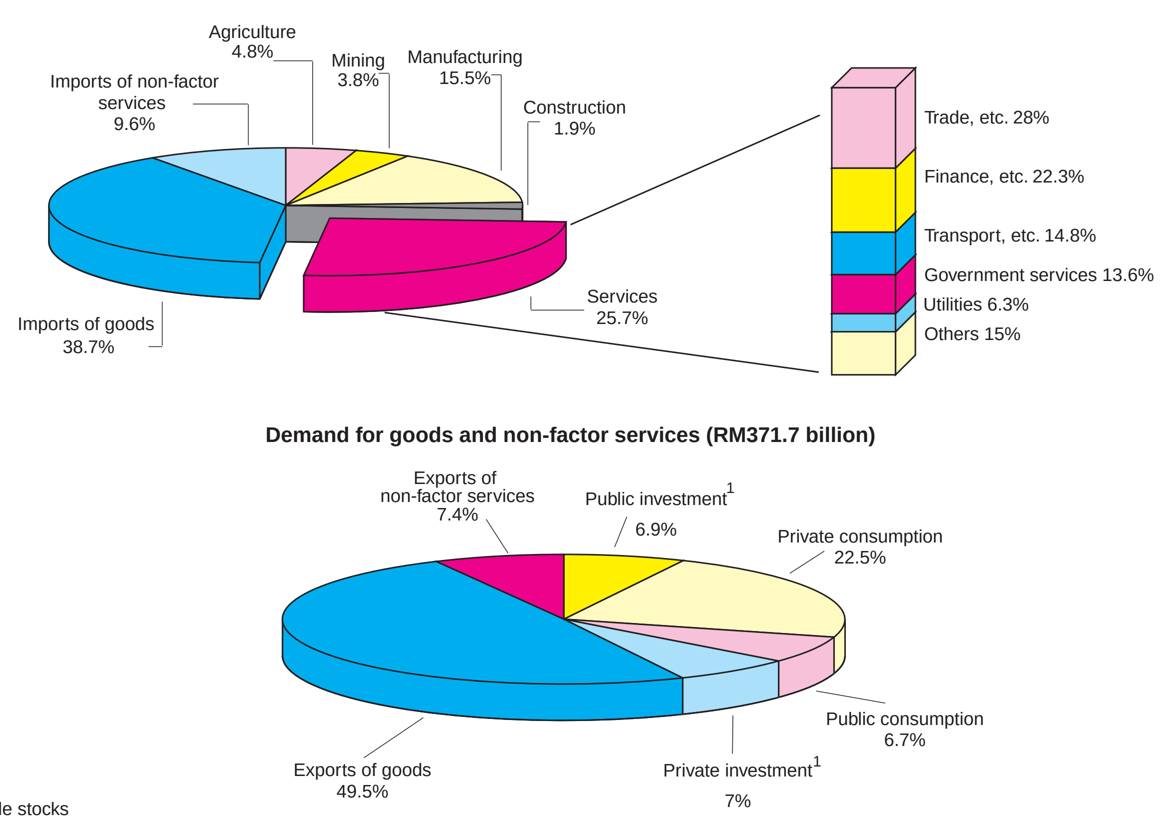
1 The Real Economy

Overview

While GDP growth in 1999 was stronger than forecast, all other developments in the Malaysian economy were in line with expectations. The selective exchange controls implemented in September 1998 allowed Malaysia to emerge from the recession with strengthened macroeconomic fundamentals. In 1999, economic activity in Malaysia rebounded from a contraction of 7.5% in 1998 to record a strong positive growth of 5.4%, higher than the earlier forecast of 4.3% in 1999. The value of GDP has returned to almost the same level as in 1997. Following the increase in nominal gross national income of 4.2%, per capita GNP turned around to register a positive growth of 1.7% to RM12,343 (US$3,248) in 1999 (1998: RM12,134 or US$3,093 and 1997: RM12,314 or US$4,377).

More importantly, overall macroeconomic fundamentals have strengthened. Remaining selective exchange controls and the fixed exchange rate continued to ensure stable financial markets. The policy measures implemented by the Government have been successful in addressing immediate-term issues without undermining medium-term growth potential. Despite a strong rebound in domestic economic activities, inflation moderated further. The balance of payments position strengthened further and the build-up of external reserves reflected the strong net inflows in both the current and long-term capital accounts. Total external debt, which has traditionally remained low, declined further. Further progress was achieved in banking and corporate restructuring. Aided by the economic recovery, the banking sector's balance sheets improved

Graph 1.1: The Economy in 1999 (at 1987 Prices)



[1]Include stocks

Table 1.1: Malaysia – Key Economic Indicators

	1997	1998	1999p	2000f
Population (million persons)	21.6	22.2	22.7	23.3
Labour force (million persons)	9.0	8.9	9.0	9.2
Employment (million persons)	8.8	8.6	8.7	8.9
Unemployment (as % of labour force)	2.4	3.2	3.0	2.9
Per Capita Income (RM)	12,314	12,134	12,343	12,893
(US$)	4,377	3,093	3,248	3,393
NATIONAL PRODUCT (% change)				
Real GDP	7.5	–7.5	5.4	5.8
(RM billion)	197.1	182.3	192.2	203.4
Agriculture, forestry and fishery	0.4	–4.5	3.9	2.0
Mining and quarrying	2.9	1.8	–4.0	2.1
Manufacturing	10.4	–13.7	13.5	10.0
Construction	10.6	–23.0	–5.6	5.0
Services	9.9	–0.8	2.9	5.4
Nominal GNP	10.3	0.9	4.2	7.0
(RM billion)	266.8	269.1	280.3	299.9
Real GNP	7.4	–5.4	4.3	5.4
(RM billion)	182.7	172.9	180.3	190.1
Real aggregate domestic demand[1]	6.8	–25.2	1.6	7.3
Private expenditure[1]	6.5	–30.2	–3.5	8.3
Consumption	4.3	–10.8	2.5	9.5
Investment	9.4	–55.0	–19.0	4.5
Public expenditure[1]	8.1	–8.3	14.8	5.2
Consumption	7.6	–7.8	20.1	0.2
Investment	8.5	–8.7	10.1	10.0
Gross national savings (as % of GNP)	39.4	41.9	40.8	38.4
BALANCE OF PAYMENTS (RM billion)				
Merchandise balance	10.3	69.0	83.5	83.4
Exports (f.o.b.)	217.7	281.9	315.7	350.3
Imports (f.o.b.)	207.4	212.9	232.2	266.9
Services balance	–22.7	–22.3	–28.9	–32.9
(as % of GNP)	(–8.5)	(–8.3)	(–10.3)	(–11.0)
Transfers, net	–3.3	–9.9	–7.2	–7.9
Current account balance	–15.8	36.8	47.4	42.6
(as % of GNP)	(–5.9)	(13.7)	(16.9)	(14.2)
Bank Negara Malaysia reserves, net	59.1[2]	99.4[3]	117.2[3]	–
(as months of retained imports)	(3.4)	(5.7)	(5.9)	–
PRICES (% change)				
CPI (1994=100)	2.7	5.3	2.8	3.2
PPI (1989=100)	2.7	10.7	–3.3	1.0
Average wages in the manufacturing sector	5.9	–2.4	2.7	–

Note: Figures may not necessarily add up due to rounding.

[1] Exclude stocks.
[2] In 1997, the foreign exchange gain on the balance sheet date was not recognised in the Bank's account, in view of the volatility of the exchange rates during that year.
[3] Arising from the fixing of the ringgit/US dollar exchange rate in September 1998, all assets and liabilities in foreign currencies have been revalued into ringgit at rates of exchange ruling on the balance sheet date and the cumulative gain/loss has been reflected accordingly in the Bank's current year account. The US dollar equivalent of international reserves as at 31 December 1999 was US$30.9 billion.
p Preliminary
f Forecast

Table 1.2: Malaysia – Financial and Monetary Indicators

	1997	1998	1999*p*
FEDERAL GOVERNMENT FINANCE (RM billion)			
Revenue	65.7	56.7	58.7
Operating expenditure	44.7	44.6	46.7
Development expenditure	14.4	17.1	21.5
Overall balance	6.6	–5.0	–9.5
Overall balance (% of GNP)	2.5	–1.9	–3.4
Public sector development expenditure	40.0	46.8	47.4
Public sector overall balance (% of GNP)	6.5	–1.3	0.2
EXTERNAL DEBT			
Total debt (RM billion)	170.8	162.0	159.7
Medium & long-term debt	127.5	129.8	136.8
Short-term debt	43.3	32.2	22.8
Debt service ratio (% of exports of goods & services)			
Total debt	5.5	6.4	5.3
Medium & long-term debt	4.7	5.7	4.8

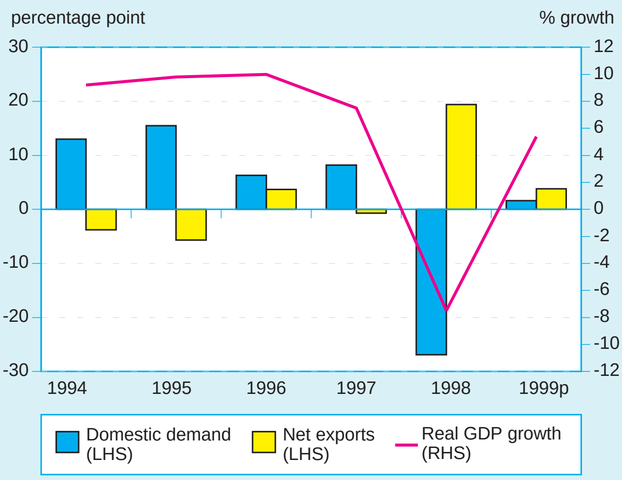
	Change in 1997		**Change in 1998**		**Change in 1999**	
	RM billion	**%**	**RM billion**	**%**	**RM billion**	**%**
MONEY AND BANKING						
Money supply M1	2.8	4.6	–9.2	–14.6	18.2	33.6
M2 54.0	22.7	4.3	1.5	34.4	11.6	
M3 61.1	18.5	10.6	2.7	33.1	8.2	
Banking system deposits	76.1	21.3	–2.1	–0.5	17.2	4.0
Banking system loans[1]	88.2	26.5	5.4	1.3	1.1	0.3
Manufacturing	9.9	18.5	1.8	2.9	0.9	1.4
Property sector	35.5	34.0	9.7	6.9	4.3	2.9
Finance, insurance and business services	3.4	10.3	1.8	5.0	–4.7	–12.3
Loan-deposit ratio (end of year)	92.7%		91.4%		84.1%	

	1997	**1998**	**1999**
	%	%	%
Interest rates (average rates at end of year)			
3-month interbank	8.70	6.46	3.18
Commercial banks			
Fixed deposits: 3-month	9.06	5.83	3.33
12-month	9.33	5.74	3.95
Savings deposit	4.23	3.87	2.76
Base lending rate (BLR)	10.33	8.04	6.79
Finance companies			
Fixed deposits: 3-month	10.32	6.43	3.49
12-month	10.25	6.57	4.13
Savings deposit	5.49	5.01	3.50
Base lending rate (BLR)	12.22	9.50	7.95
Treasury bill (3-month)	6.76	5.37	2.71
Government securities (1-year)	7.01	5.79	3.37
Government securities (5-year)	7.75	6.66	5.21

	1997	**1998**	**1999**
	%	%	%
Movement of Ringgit (end-period)			
Change against composite	–31.4	– 0.2	–1.3
Change against SDR	–30.8	–1.8	2.7
Change against US$	–35.0	2.3	0.0

[1] Beginning December 1996, loans by sector are classified using a new statistical reporting format.
p Preliminary

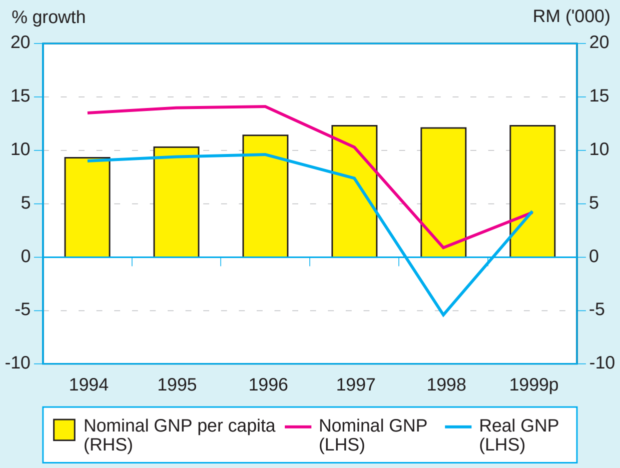
Graph 1.2
Contribution to Real GDP Growth: Domestic Demand and Net Exports



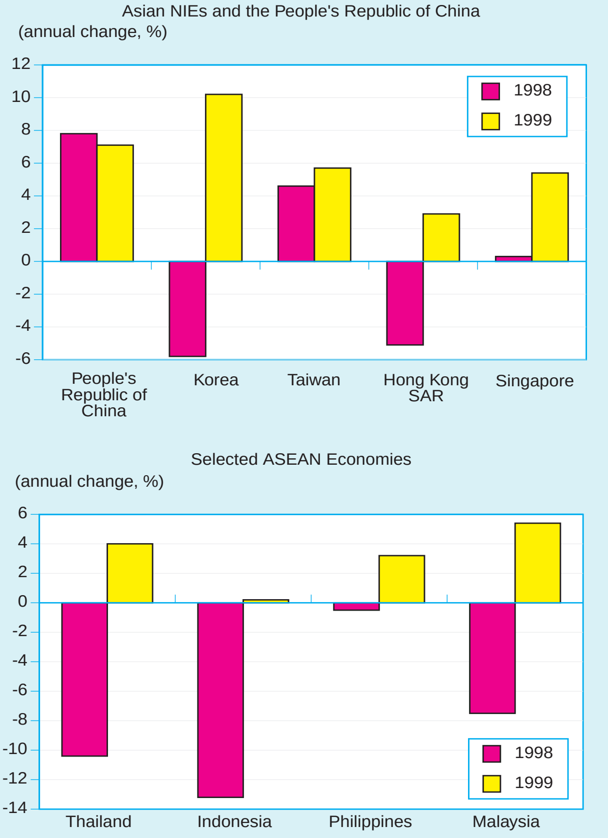
significantly. Consequently, loan disbursements by the banking system have increased, supporting the economic recovery. On the socio-economic front, labour market conditions improved. Macroeconomic adjustments were achieved without serious dislocations in jobs and social unrest.

The nascent signs of improvement seen since the fourth quarter of 1998 strengthened during the course of 1999. In the first half of 1999, the economy expanded by 1.5%. The expansion gathered momentum in the second half-year when expansionary fiscal and monetary operations as well as sustained buoyant external demand raised real output growth to 9.4% in the second half-year.

Graph 1.3
GNP Growth and Nominal GNP per Capita



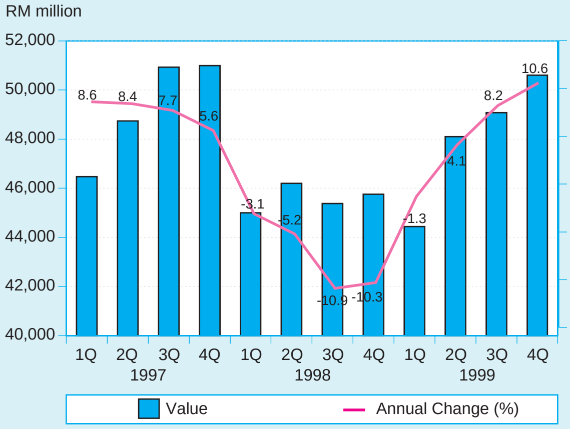
Graph 1.4
Regional Countries: Real GDP Growth



The better-than-expected performance in 1999 was due to both external developments and the prompt policy response to reduce the severity of the impact of the crisis on the Malaysian economy. On the external front, world growth picked up to 3% in 1999 (1998: 2.5%), reflecting higher growth in the industrial countries and stronger-than-expected recovery in Asia. In line with increased economic activity and a strong recovery in global demand, growth of world trade was sustained at 3.7% (1998: 3.6%). The uncertainties in the early part of 1999 of possible risk of deceleration in output growth in the industrial countries did not materialise. Growth in the major industrial countries increased by 2.7% in 1999 (1998: 2.4%). This together with the revival of domestic demand in other regional countries contributed to significant strengthening of demand for exports from Malaysia.

On the domestic front, the stability in the financial markets which emerged after the introduction of selective exchange controls and the fixed exchange rate in September 1998 provided fundamental support to the process of economic recovery. Stability in the financial markets after restrictions were imposed to eliminate the internationalisation of the ringgit enabled the Government to take proactive measures to bring

Graph 1.5
Malaysia's Quarterly GDP: Value and Annual Growth



In 1999, value added in the **manufacturing** sector increased at a double-digit rate of 13.5% (–13.7% in 1998), following expansion in output of the manufacturing sector since February 1999. Output in the export-oriented industries increased by 12.9% buoyed by the strong performance of the electronic goods initially and subsequently by higher output in the electrical products, off-estate processing and textiles and wearing apparel industries. The strong growth of the domestic-oriented industries as a group (13.1%) was due mainly to output expansion of the transport equipment (motor vehicles as well as motor vehicle parts and accessories), construction-related products and chemical products industries, with improved performance of most sub-sectors.

about an early recovery of the economy. The fixing of the exchange rate provided businesses with some degree of certainty to plan their operations. Stable market conditions were crucial to allow businesses to respond positively to rising export demand. The expansion in the export sector generated increases in income which provided the basis for a significant revival in private consumption. The expansion in domestic economic activity was further reinforced by measures taken to accelerate disbursements for projects under the fiscal stimulus package. At the same time, measures to strengthen the banking sector enabled the banking sector to refocus on lending activities. Although initial expansion in loans was slow, loan approvals and disbursements showed a significant increase in the latter part of the year, lending support to the expansion in economic activities. In terms of capital strength, the risk-weighted capital ratio (RWCR) of the banking system improved further while the ratio of net non-performing loans (NPLs) to total loans of the banking system stabilised. In value terms, the amount of NPLs was lower in 1999.

On the **supply side**, growth was initially driven by the strong performance of the export-oriented industries in the manufacturing sector. The recovery became increasingly more broad-based during the course of the year. Within the manufacturing sector, growth became broad-based from the second quarter onwards as both domestic and export-oriented industries registered positive growth rates. In the second quarter, all sectors except mining and construction recorded positive growth. By the third quarter, the construction sector had also turned around to record positive growth. The decline in value added in the mining sector in all four quarters reflected the deliberate decision under the National Depletion Policy to conserve reserves.

In the **agriculture** sector, growth in value added turned around sharply (+3.9%; 1998: –4.5%) mainly on account of the marked increase in crude palm oil production (+26.8%) and to a lesser extent, the growth in saw log production (+1.2%). The upturn in the biological yield cycle for the oil palm trees as well as increased mature area raised output of crude palm oil markedly.

The performance of the **construction** sector improved to record a smaller decline of 5.6% in 1999 (–23% in 1998). The improvement in construction activities was supported by the increase in Government spending in public sector projects such as roads, utilities and housing as well as revival of several critical privatised projects. Policy measures introduced since May 1998 focused mainly on reducing excess stocks (home ownership campaigns) and increasing access to finance (special housing fund for low- and medium-cost houses), while lower interest rates also helped to revive activities in the residential sector. As a result, value added in the construction sector registered a positive growth of 1.8% in the second half-year, after declining at a lower rate of 12.3% in the first half-year.

With the overall improvement in the economy, the **services** sector turned around to increase by 2.9% in 1999. Higher Government operating expenditure accounted for the growth in the government services sub-sector while strong manufacturing activities contributed to the improved performance of the utilities and transport, storage and communications sub-sectors. The increase in disposable income and increased tourist arrivals led to higher growth in the wholesale, retail, restaurants and hotels sub-sector.

Table 1.3
Private Consumption Indicators

	1998	1999				
		Q1	Q2	Q3	Q4	Year
Sales of passenger cars, including 4WD						
Annual change (%)	–54.8	141.3	105.4	76.7	40.1	79.9
'000 units	142.2	55.8	59.8	68.7	71.6	255.9
Imports of consumption goods[1]						
Annual change (%)	–32.9	1.7	16.7	30.6	36.2	21.3
US$ billion	3.4	0.9	1.0	1.0	1.2	4.1
Tax collection						
Sales tax (RM billion)	3.8	1.1	1.0	1.3	1.1	4.5
Service tax (RM billion)	1.4	0.4	0.3	0.5	0.3	1.5
Total loans approved by the banking system						
Consumption credit (excluding passenger cars) (RM billion)	4.1	1.0	1.2	1.8	1.8	5.7
Wholesale, retail, restaurant & hotels (RM billion)	4.9	1.6	1.6	2.7	1.7	7.6
Stock market indicators[2]						
Market capitalisation (RM billion)	374.5	317.9	532.0	457.6	552.7	552.7
KLSE composite index (points)	586.1	502.8	811.1	675.5	812.3	812.3
MIER Consumer Sentiments Index	–	84.0	101.6	111.3	117.7	–

[1] Broad Economic Classification
[2] End-period

Table 1.4
Private Investment Indicators

	1998	1999				
		Q1	Q2	Q3	Q4	Year
Sales of commercial vehicles, including 4WD						
Annual change (%)	–76.1	35.9	78.4	77.6	27.4	50.8
'000 Units	21.7	6.6	7.5	8.9	9.7	32.7
Imports of capital goods[1]						
Annual change (%)	–40.5	–36.0	–11.6	12.5	21.6	–5.9
US$ billion	9.2	1.8	2.0	2.5	2.4	8.7
Applications to MITI						
No. of projects	726	192	162	198	195	747
Total capital investment (RM billion)	18.9	3.7	3.9	4.2	2.3	14.0
Foreign	*12.6*	*2.0*	*2.6*	*3.0*	*1.4*	*9.0*
Local	*6.3*	*1.6*	*1.3*	*1.2*	*0.9*	*5.0*
Approvals by MITI						
No. of projects	844	171	197	146	194	708
Total capital investment (RM billion)	26.4	6.1	2.4	3.4	4.9	16.9
Foreign	*13.1*	*5.3*	*1.7*	*1.4*	*3.9*	*12.3*
Local	*13.3*	*0.8*	*0.7*	*2.1*	*1.0*	*4.6*
Total loans approved by the banking system						
Manufacturing sector (RM billion)	10.3	2.7	3.8	3.3	4.2	14.0
Construction sector (RM billion)	5.7	1.4	2.0	2.5	2.0	7.9
MIER Business Conditions Index	–	48.2	60.3	62.2	61.0	–

[1] Broad Economic Classification

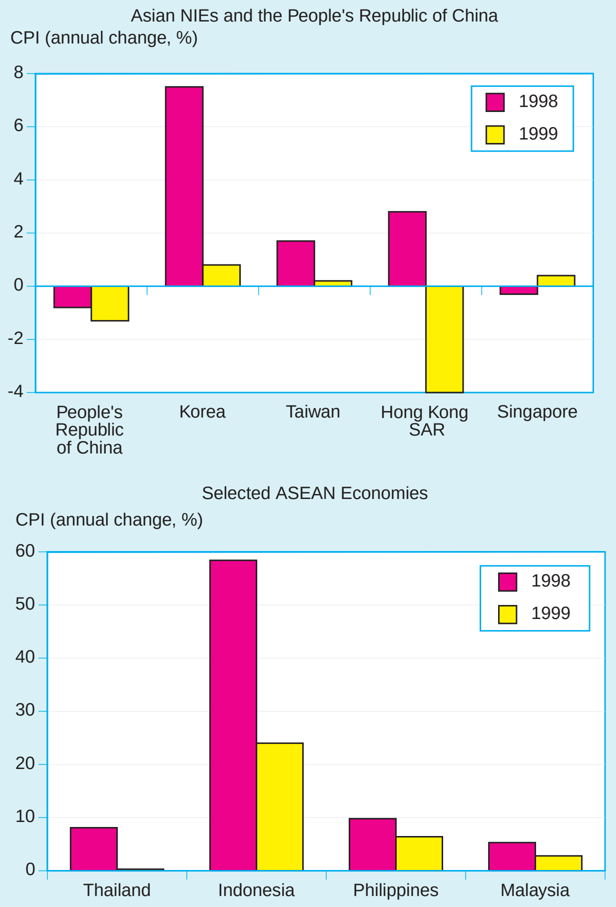
Value added in the **mining** sector contracted by 4% due to lower production of crude oil in line with the National Depletion Policy. Crude oil production was lower at 693,200 barrels per day, 4.4% lower than the level recorded in 1998. Production of natural gas increased by 2.1% in response to higher demand from both domestic and external sources.

On the demand side, strong economic growth was sustained by robust export performance, accelerated public sector expenditure and a revival in private consumption expenditure. Growth in real aggregate **domestic demand** (excluding stocks) increased by 1.6% in 1999, due mainly to the fiscal stimulus measures implemented by the Government and the revival in private sector consumption expenditure. Public sector expenditure recorded a strong positive growth of 14.8% following the speedier implementation of projects under the fiscal stimulus programme, particularly in the second half-year. Of significance, private consumption turned around to record a positive growth beginning from the second quarter. For the year as a whole, private consumption increased in real terms by 2.5% in 1999, following a decline of 10.8% in 1998. The decline in private investment moderated as lower stock levels and higher capacity utilisation rates became evident in several major industries.

Despite the pick-up in economic activities and increase in capacity utilisation in major sectors, inflationary pressures remained subdued in 1999. Inflation as measured by the **Consumer Price Index (CPI, 1994=100)** moderated to 2.8%, from 5.3% in 1998. The monthly inflation rate moderated to 1.6% in November 1999, representing a significant deceleration from the peak of 6.2% in June 1998. The moderation in the CPI was mainly attributable to the absence of imported inflation from abroad, relative stability of ringgit exchange rate and continued excess capacity in some selected industries in the economy. The decline in non-oil commodity prices was another contributory factor. Growth of most components of the CPI moderated in 1999. The exceptions were beverages and tobacco and transport and communication which recorded higher growth, while the clothing and footwear component recorded a decline. Excluding food, inflation for 1999 was lower at 1.6%, compared with 3.1% in 1998.

The **labour market** situation improved in 1999 following the stronger-than-expected growth in the domestic economy. The unemployment rate is estimated to have declined to 3%, well below the full employment level of 4% (1998: 3.2%). The improved employment situation was also reflected in key employment indicators including retrenchment, number of job vacancies and job seekers. The Government's counter-cyclical measures and the special attention given to the social agenda have helped to reduce the severity of the economic downturn and contain the deterioration in the overall employment situation. The counter-cyclical measures contained a programme to protect the lower income groups from the adverse effects of the crisis.

Graph 1.6
Regional Countries: Inflationary Trends



On the external front, the overall **balance of payments** position strengthened further to record a surplus of RM17.8 billion or US$4.7 billion, driven by favourable external trade balance and a larger net inflow of long-term capital. In the trade account, gross exports (in US dollar terms) have increased for five consecutive quarters, while import growth has turned positive since the second quarter of 1999. In US dollar terms, exports of manufactured goods rose by 17.6%, benefiting especially from strong global demand for electronic products such as semi-conductors, personal computers and other information and communications-related components. Following the rebound in exports, imports of intermediate goods in US dollar terms have recorded positive growth since March 1999. Imports of capital goods have turned positive since June 1999 reflecting the recovery in private investment activities in the second half-year. Nevertheless, export growth was stronger (12%) relative to import growth (9%) contributing to a record merchandise surplus of RM83.5 billion (US$22 billion) and another year of a large **current account surplus** of RM47.4 billion (US$12.5 billion) or 16.9% of GNP in 1999.

The balance on the **long-term capital account** increased to RM11.7 billion (US$3.1 billion) due mainly to higher inflows of official long-term capital and foreign direct investment. The net private long-term capital account, however, showed a decline due mainly to higher overseas investments by Malaysians. **The overall balance of payments** recorded a surplus of RM17.8 billion, after adjusting for revaluation losses from ringgit appreciation, increased short-term trade credits, further reduction in short-term external debt of commercial banks and the non-bank private sector and some liquidation and repatriation of portfolio investment by foreign investors, following the expiry of the one-year holding period for portfolio investment. Consequently, the **net international reserves of Bank Negara Malaysia** increased to RM117.2 billion (US$30.9 billion) as at end-1999, from RM99.4 billion (US$26.2 billion) at the end of 1998. This level of reserves was sufficient to finance 5.9 months of retained imports (5.7 months in 1998). In addition, the international reserves were 5.1 times the short-term external debt.

Malaysia's external debt position remained at a manageable level in 1999. **The total external debt** outstanding declined by 1.4% to RM159.7 billion or equivalent to US$42 billion as at end-1999. Consequently, the ratio of external debt to GNP improved to 57% from 60% at end-1998, while the debt service ratio improved to 5.3% from 6.4% in 1998. The moderate increase in medium- and long-term external debt of the public sector (mainly reflecting the receipts from the 10-year US$1 billion Malaysian Global Bond issued by the Federal Government and the US dollar denominated bond issue of US$650 million by Petronas) was offset by the net repayment of long-term external loans by the private sector (the first decline since 1989) and the net decline in outstanding short-term debt. Ample liquidity in the domestic market and lower demand for hedging contracts by exporters and importers led to the decline in short-term external debt of commercial banks. Short-term debt of the non-bank private sector, which accounted for about 6% of total external debt, also declined to RM9 billion or US$2.4 billion. With total short-term debt declining to RM22.8 billion or US$6 billion, the ratio of short-term debt to total debt declined to 14% (from 20% in 1998) while the ratio of short-term debt to international reserves improved to 19.5% (1998: 32.4%).

Macroeconomic policy management in 1999 focused on strengthening the recovery process and on expediting measures to address structural issues, both in the economic and financial sectors. To achieve a broad-based recovery that is sustainable over the medium term, the policy strategy adopted was comprehensive, taking into account the potential upside as well as downside risks.

In early 1999, the Malaysian economy was at an initial stage of recovery after one year of economic contraction. Despite some improvements in external demand in the fourth quarter of 1998, there was considerable uncertainty about the prospects for growth in the major industrial countries. In addition, there was an inventory overhang and excess capacity in selected industries in the domestic economy. In such an environment, the broad thrust of policy was directed at strengthening domestic demand through the fiscal stimulus. In the 1999 Budget, the **overall financial position of the Federal Government** was targeted to record a fiscal deficit of 6.1% in 1999. The pace of implementation of Government's projects was initially slow. At the end of the first quarter, only 3.6% of the total development expenditure allocated for 1999 was spent due to implementation constraints. To address this, the Government took measures to expedite spending, which included streamlining the contract tender process, close monitoring of the implementation of projects through regular submissions of progress reports and ensuring more prompt payments to contractors. As a result, Government spending increased in the second quarter of 1999. By end-1999, the Government had utilised 87.5% of the total development expenditure of RM25.8 billion.

Although it was recognised that the public sector stimulus was critical for the economic recovery, the Government remained committed to maintaining the budget deficit at a level that would not jeopardise public sector policies in the longer term. In line with fiscal prudence, the Government targeted for a balanced position in the current account of the Federal Government and an overall deficit of 6.1% of GNP. The actual outturn of the financial position of the Federal Government was, however, better than expected because of the improved performance of the economy. The current account recorded a large surplus of RM12 billion or 4.3% of GNP. The deficit in the overall account was smaller than budgeted in the 1999 Budget, amounting to RM9.5 billion or 3.4% of GNP. Reflecting the improved financial position of the Federal Government as well as the non-financial public enterprises (NFPEs), the **consolidated public sector account** recovered to record a surplus of RM581 million or 0.2% of GNP. With higher crude oil prices, revenue receipts were higher for PETRONAS.

In terms of Government spending, priority was accorded to projects to address structural and socio-economic issues (education and skills training; health services; low-cost housing; and agriculture and rural development), as well as revival of selected infrastructure projects to increase efficiency of the economy. An important criterion of the stimulus package was that it should result in minimal leakage abroad to ensure no build-up of risks in the balance of payments. In addition, the higher expenditure should be financed largely from domestic sources (69%) to contain the nation's external debt and debt service ratio at a manageable level. The Government raised a global bond issue of US$1 billion at end-May 1999 mainly for the purposes of benchmarking. Meanwhile, Malaysia also had obtained funding from multilateral sources such as World Bank (total amount approved in 1999: US$404 million or RM1.5 billion), Islamic Development Bank (total amount approved: US$99 million or RM376 million) and bilateral sources, including loans under the New Miyazawa Initiative amounting to an equivalent of RM4.8 billion or US$1.3 billion (mainly from Overseas Economic Cooperation Fund and Japan Export-Import Bank which have merged and renamed Japan Bank for International Cooperation). In 1999, the Federal Government had only drawn down RM610 million under the Miyazawa Initiative. The remaining amount would be drawn down over the next 3-5 years. The yen credit line offered as bilateral financial assistance to Malaysia under the Miyazawa Initiative are of maturity periods of 5 to 40 years. Such borrowing from official creditors have not adversely affected the overall debt profile. Overall, total debt of the Federal Government remained at about 40% of GNP, of which external debt was 6.6% of GNP.

In the absence of inflationary pressures, monetary policy was accommodative during the course of 1999 to support the expansionary fiscal stance. The easing of monetary policy and ample liquidity in the banking system following the improvement in the balance of payments provided an environment to reduce interest rates to support the economic expansion. The BNM intervention rate was reduced in three steps of 0.5 percentage points to 5.5% in August 1999. Given the moderation in inflation, the objective of ensuring positive real interest rate was achieved. The maturing of high cost deposits and the consequent reduction in the average cost of funds had provided the banking institutions with greater flexibility in reducing lending rates. To ameliorate the adverse impact of the low interest rate environment on the income earned by retirees on their deposits, BNM issued the Malaysia Savings Bond Series 02 in November 1999, with a coupon rate of 5.75% per annum.

Overall, the Central Bank interacted proactively with the banking institutions to ensure that credit remained available to viable activities to support the economic recovery process. Banks were encouraged to channel resources to sectors that were viable, both for new growth sectors and traditional export sectors. Approvals and disbursements of loans by the banking system increased. In 1999, loan approvals averaged RM8.7 billion a month (1998: monthly average of RM5.4 billion a month), while disbursements recorded an average of RM26.9 billion a month (1998: RM20.9 billion a month). The marginal increase in total outstanding loans of the banking system of 0.3% for 1999 (including loans sold to Danaharta) reflected a number of developments, including high repayments (monthly average of RM28 billion in 1999, as against RM22.5 billion in 1998), write-off of loans and conversion of loans to bonds. Including the write-off of loans, conversion of loans to bonds as well as the holdings of private debt securities (PDS), total financing provided by the banking system increased by 2.8%.

Credit limits on total exposure of banking institutions to the broad property sector and purchase of shares imposed on 1 April 1997 were maintained to ensure that banking institutions would not be excessively exposed to sectors that are susceptible to economic cycles. In 1999, an additional measure was also put in place to contain further overhang of high-end properties through the restriction on the provision of bridging finance to developers for the development of properties exceeding RM250,000. However, financing to end-buyers for the purchase of properties in both the primary and secondary markets was not affected by the prohibition.

In the course of 1999, Bank Negara Malaysia also **intensified structural adjustment efforts in the banking sector**. Recognising the risks of over reliance on the banking system in financing the economy, the development of the bond market was accelerated to reduce pressures on the banking system, while providing borrowers and investors with alternative instruments. In June 1999 the National Bond Market Committee (NBMC) was established to provide the overall policy direction and to rationalise the regulatory framework for the orderly development of the market.

In 1999, Malaysia also accelerated the pace of restructuring of the banking system and corporate sectors. The period of stability accorded by the selective exchange controls and the fixed exchange rate facilitated significant progress in the restructuring of the banking system during the course of 1999. By 31 December 1999, **Danaharta**, the national asset management company set up in June 1998, had acquired and was managing NPLs with loan rights amounting to RM45.5 billion from the financial system, of which RM35.7 billion was from the banking system. The book value of these NPLs amounted to RM34 billion, representing approximately 42% of total NPLs of the banking system. With the removal of these NPLs from the banking sector, the residual NPL level in the banking sector declined to 6.6% based on 6-month classification as at 31 December 1999 (11.1% based on 3-month classification), from the peak of 9%

based on 6-month classification as at 30 November 1998 (14.9% based on 3-month classification). As consideration for the loans acquired, Danaharta has issued RM10.3 billion nominal value bonds up to December 1999.

As at end-1999, Danaharta has achieved a recovery rate of 80.2% on the loans and assets that it has restructured or disposed. On loan disposals, Danaharta has conducted two successful restricted open tenders to dispose of foreign currency loans and papers in August 1999 and December 1999 involving 43 accounts worth US$394.3 million. The recovery rates of both tender exercises were encouraging, with a recovery rate of 55.3% achieved in the first tender exercise and 71% in the subsequent exercise. With the two tender exercises, Danaharta has successfully disposed a total of US$339.8 million of foreign currency loans and papers. Danaharta has also successfully completed its first open tender exercise on 44 properties with a total indicative value of RM122.6 million. A total of 24 bids were successful, raising a total consideration of RM17.8 million. The amount received on the successful bids represented an 8% surplus over the indicative value of RM16.5 million. The remaining 20 properties with an indicative value of RM106.1 million were transferred to Danaharta's asset subsidiary.

Danamodal, the bank recapitalisation agency set up in August 1998 to recapitalise affected banking institutions has injected RM7.1 billion into 10 banking institutions since its inception. Following repayments by five banking institutions, the amount of capital injected has been reduced to RM5.3 billion as at end-January 2000.

While the pace of corporate debt restructuring to contain the growth of NPLs and complement the restructuring of the financial institutions was slow initially, there was significant improvement in the second half-year. The Corporate Debt Restructuring Committee, **CDRC**, established in August 1998, has received 67 applications with debts totalling RM36.3 billion as at 24 February 2000. Of these, 19 restructuring schemes amounting to RM14.1 billion have been completed and are in various stages of implementation, while 10 cases amounting to RM3.3 billion are being resolved by Danaharta. Thirteen cases involving debts worth RM2.8 billion have been rejected/withdrawn and the debt restructuring schemes for the remaining 25 cases amounting to RM16.2 billion are currently being worked out. In addition, CDRC is also actively looking into the restructuring of three industries, namely transportation, telecommunication and steel.

As at end-January 2000, the RWCR of the banking system remained strong at 12.5%, well above the minimum requirement of 8% and higher than the pre-crisis level of 12% as at end-June 1997. The net NPL ratio, based on a 6-month classification, declined to 6.6% as at end-1999 from the peak of 9% as at end-November 1998. In terms of value, net NPLs amounted to RM24.3 billion (end-1998: RM29.3 billion).

The success of Danaharta and Danamodal in achieving their targets ahead of schedule has enabled BNM to move forward to the next stage of further strengthening the banking sector through mergers and consolidation. Under the merger programme, the banking institutions were given the flexibility to form their own merger groups and to select the lead banks to spearhead the merger process. The banking institutions were given until end-January 2000 to submit to BNM their merger groups. On 14 February 2000, BNM approved the formation of 10 domestic banking groups with the anchor banks as Malayan Banking Berhad, Bumiputra-Commerce Bank Berhad, RHB Bank Berhad, Public Bank Berhad, Arab-Malaysian Bank Berhad, Perwira Affin Bank Berhad, Hong Leong Bank Berhad, Multi-Purpose Bank Berhad, Southern Bank Berhad and EON Bank Berhad. This industry-wide merger exercise is expected to be completed by end-December 2000. The industry consolidation is an important step towards creating a resilient, efficient and competitive banking sector. This industry consolidation needs to be complemented with medium- to long-term measures. In this regard, BNM has embarked on the formulation of a long-term financial master plan to chart the future direction of the banking and insurance sectors.

Efforts to restructure the banking sector were complemented by additional prudential measures introduced in 1999 (for details, please refer to Chapter 4).

With regard to the **selective exchange control measures** that were implemented in September 1998, BNM initiated the liberalisation of these regulations given that the objectives of the measures had been achieved. The one-year minimum holding period of portfolio capital was modified effective 15 February 1999 to allow foreign investors to repatriate principal

Box I

Sustainable Growth: Challenges and Responses

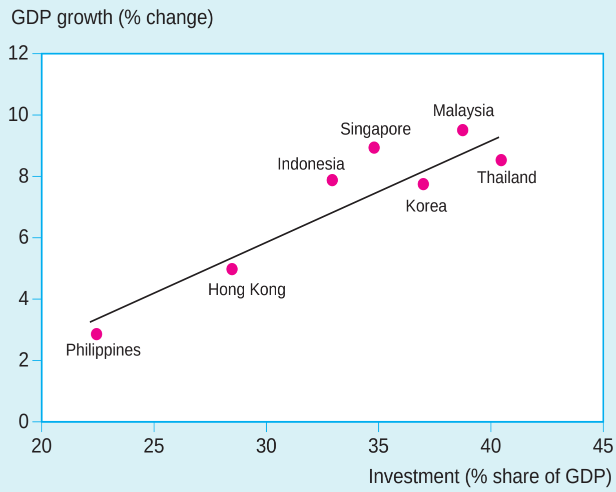
Sustainable economic growth is a situation in which the economy is able to grow at its long-run potential level without experiencing long-term imbalances, particularly price pressures or external imbalances. Essentially, the signs of sustainable growth are a steady rate of growth consistent with low inflation, a manageable balance in the current account, a sustainable fiscal balance with no economy-wide wage pressures and asset price inflation.

In the period following the East Asian financial crisis, the focus of economic policy in Malaysia was to promote economic recovery. To achieve this goal, a comprehensive set of policies consisting of expansionary fiscal and monetary policies, a fixed exchange rate and selective exchange controls and a longer-term programme of restructuring, both for the financial and corporate sector, was implemented. As a result of these policies and strong external demand, Malaysia recorded an expansion of real gross domestic product (GDP) of 5.4% in 1999. With the restoration of growth, the focus of policy has shifted to address medium-term issues of ensuring broad-based and sustainable growth. In a globalised environment of integrated markets and rapid changes in technology, policies that were effective in the past decade may now be less relevant. While the objective of maintaining macroeconomic stability remains unchanged, a paradigm shift is needed to ensure sustainable growth in this new global economy. For Malaysia, this return of focus is particularly timely, given the end of the period of coverage of the Seventh Malaysia Plan (1996-2000) and the work being undertaken to introduce the Eighth Plan. Further, work on the Third Outline Perspective Plan, the Knowledge Economy (K-Economy) Master Plan, the Financial Sector and Capital Markets Master Plans is in progress and industrial policy, as laid out in the Second Industrial Master Plan, 1995-2005 (IMP2), is under review.

Challenges to Sustainable Growth

The development strategy thus far, which has focused on investment- and trade-led growth, has served Malaysia well. In particular, the liberalisation and privatisation programme that was implemented following the economic slowdown in the 1980s saw a structural shift, with manufacturing, especially for exports, becoming the lead sector in the economy. The leap in competitiveness allowed the production for export to be enhanced and was supported by a policy that actively encouraged foreign manufacturers to locate in Malaysia to strengthen the role of the Malaysian private sector to become the engine of growth. As a result, the period between 1987-97 saw the strongest growth in Malaysia's history, with real GDP expanding by a compounded average annual rate of 9.3%. During the same period, real gross fixed capital formation increased by 18.4%. As a result, the share of investment to GDP rose from 22.1% in 1987 to reach 49.1% in 1997. While the rapid increase in investment has provided the base for capacity expansion, the rapid pace of expansion did create some supply-side bottlenecks.

Graph I.1
Growth and Investment-A Regional Comparison



Data for all countries refer to an average for 1990-1996.
Source: International Monetary Fund and Department of Statistics, Malaysia

Firstly, as a consequence of an industrial strategy that focused on non-resource-based industries as the main driver of the development process, there were weak linkages with the rest of the economy. The low level of indigenous capital and intermediate goods manufacturing industries as well as a shortage of labour led to high imports of goods and workers. The consequent impact on the balance of payments was seen in the current account. The surplus that was recorded in 1987 (8.7% of gross national product (GNP)) narrowed and gradually moved to a large deficit equivalent to 10.2% of GNP in 1995, before improving to 4.6% in 1996.

Secondly, the low level of local input in the rest of the value chain was a factor in the low value added contribution of the manufacturing sector given the level of investment. In the case of upstream activities, the lack of research and development resulted in the concentration on assembling components with a relatively low value added content. In the case of downstream activities, manufacturers had limited participation and relied on just a few export destinations. As a result, having moved away from a primary commodity-dominated economy so as to reduce our reliance on uncertain international markets, a large proportion of Malaysia's exports were now manufactured commodities and highly dependent on fewer markets.

There are two main challenges that now face the economy in the post-crisis period. Firstly, investment-driven growth is no longer sufficient to fulfill the development goals envisioned in the longer-term plans. Given the limitations in increasing the supply of other factors of production, investment alone cannot be expected to yield maximum results. Malaysia's incremental capital-output ratio (ICOR), that is, the amount of additional capital required to produce an additional unit of output had been rising throughout this decade. In 1987, the ICOR stood at 2.74 but by 1995, the ICOR had increased to 5.49, implying that while investment had increased, the rate of utilisation of this additional capital stock was lagging. In part, this increase was due to increased capital spending on investments with long gestation periods but which were necessary to ameliorate supply shortages and increase the capacity of the economy. However, it is equally true that efficiency of capital was not as high as it could have been. Additionally, there are limits to the financial resources, both domestic and international, that can be tapped at a reasonable cost to achieve this growth in investment. As such, a more efficient utilisation of resources is the focus for future development and industrial policy. The focus now will be to increase the productivity of labour given that the essential infrastructure has now been put in place.

Secondly, challenges arising from a fast-changing global marketplace also need to be addressed. The events of the last two years have highlighted the risks associated with the reliance on a small range of products or a small group of markets. The electronics industry in particular has been an important element in Malaysia's economic performance over the last decade. However, given the need to diversify the economic structure, new growth areas need to be identified and existing growth areas need to be reviewed to strengthen competitiveness. These include both the higher technology information-communication technology (ICT) sector as well as the resource-based industries. Further, services that support the competitive export structure need to be nurtured. There are also new risks arising from the globalised economy, especially in the case of the financial sector which need to be addressed. Efforts are also being undertaken to promote domestic demand.

Policy Responses to the Challenges

The main components of the policy responses in facing these challenges are to improve competitiveness and efficiency, to manage risks more effectively and to ensure that policy implementation is done in a consistent and efficient manner.

Competitiveness and Efficiency

Competitiveness defines the capacity of industries to provide world class goods and services, both for domestic and external consumption. These goods and services must meet exacting quality standards at reasonable prices. Efficiency is defined as increasing output per unit of input. In this context, this includes improved utilisation of capital, increasing the skill level of the workforce andimproving work processes. Increased efficiency will increase competitiveness while measures that spur competition such as progressive market liberalisation, especially in trade, can contribute to efficiency gains. These, however, need to be achieved in a manner that is not disruptive to the overall functioning of the economy.

- ***Exploring new growth areas***

  Increasing the knowledge content of the economy will be key to moving up the value chain so as to transform Malaysia into a K-economy. The K-economy has been defined as "...one in which the generation and the exploitation of knowledge has come to play the predominant part in the creation of wealth. It is not simply about pushing back the frontiers of knowledge; it is also about the more effective use and exploitation of all types of knowledge in all manner of economic activity."[1] This means not just knowing more but using this knowledge, be it technical, managerial and even networked knowledge to improve design, production, delivery and marketing, effectively. To this end, the Federal Government Budget 2000 has made available, for the first time, funds to identify the key drivers to making the transition to a K-economy.

  A major thrust in development policy will be to identify new growth areas. The services and high-technology manufacturing sectors where knowledge is the key driver have been identified for further development. In these new growth areas, product innovation will be important. The emphasis will also be on productivity-driven growth as much of the essential capital infrastructure is already in place. Identification of these new growth areas will have to correspond with identifying the critical success factors in being able to take advantage of them. This includes the critical role played by industrial clusters, financing, international networks and the education system.

- ***An integrative industrial policy***

  Critical to moving into these new growth areas is a holistic industrial policy. The IMP2 sets out a more integrative approach to industrial development in the use of the cluster-based paradigm. Essentially, instead of industries, eight industrial clusters or groups of related industries have been identified for further development. These clusters are the electrical and electronics industry group, the transportation industry group, the chemicals industry group, the textiles and apparel industry group, the resource-based industry group, the materials and advanced materials industry group and the agro-based and food products industry group.

  Supporting industries are built so as to deepen and widen the industrial base. In the resource-based cluster, for example, the plans include the development of the supporting agricultural base so that supplies of raw materials are maintained. The cluster-based approach also pays attention to the downstream activities such as distribution, packaging and marketing to move industries from original equipment manufacturing (OEM) to higher value-added activities that include indigenous design and branding.

- ***Improving education and human resource development***

  The inadequacy of domestic human resources (HR) is reflected by the estimated 1.2 to 2 million foreign workers who resided in Malaysia in the 1990s. This was partly due to the expansion during the early stage of industrialisation of low skill, labour intensive industries. To address this, the strategy is to improve the skill and productivity level so that higher wages are more than offset by higher output. This will be beneficial both to producers, in that labour costs per unit of output decline despite a higher wage bill, and to workers, in that real wages increase as wage increases are not matched by increases in the price level.

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[1] "Our Competitive Future Building the Knowledge Driven Economy" – White Paper prepared by the UK Department of Trade and Industry, December 1998.

In the case of training and education, the Government accelerated its university-building programme while several new industrial training institutes (ITIs) have been set up. This includes the building of new universities in different parts of the country while upgrading several higher education institutes and training facilities of several large non-financial public enterprises (NFPEs) to full university status and the building of a total of five new ITIs. The private sector has also been encouraged to take on a proactive role in training with the establishment of the Human Resource Development Fund and the introduction of several tax incentives. Between 1996 and 1999, the number of instructors in private higher education institutions increased, on average, by 18.5%. In future, both the private sector and the workers themselves must take on a greater share of the responsibility for training and re-training. In view of the critical importance of human capital to enhance our competitiveness, measures will be taken to reverse the brain drain and to encourage the infusion of talent from abroad.

The education system in Malaysia has performed well thus far. However, in future, a greater premium will be attached to creativity and solution-orientation. The emphasis on a more holistic education has, therefore, become an important part of the curriculum.

While high employment remains a goal of economic policy, high employability is also encouraged to produce a more adaptable labour force. Emphasis is, therefore, given towards constant re-training programmes and the development of a more flexible educational system.

- ***Upgrading the services sector and the knowledge content of traditional economic activity***

As noted earlier, the knowledge content will be an important driver of economic activity. Whereas product innovation will take center stage in the case of the new growth areas, in more traditional areas, equal importance will be place on marketing, product customisation and delivery.

Services, both that are explicitly rendered as well as the intrinsic services embodied in goods, will have an important role. The services sector is the largest part of the productive economy, accounting for 54.2% of real GDP in 1999. However, at the current stage of economic development, the sector is relatively underdeveloped by international standards[2]. Services do more than just support the merchandise sector of the economy but are now seen as necessary inputs into the production process. In the manufacturing sector, only an estimated 25% of the price of goods is for “pure” production costs. The remainder of the payment is for costs linked to services such as product development, storage, distribution, marketing and publicity, financial and insurance services and waste management and disposal systems[3]. The services sector is integral to upgrading the knowledge content in production or shifting to full K-economy status. Services such as transport, design, packaging, marketing and even administrative arrangements are all becoming suffused with a higher knowledge content. For instance, many companies have sites on the worldwide web but relatively few have integrated their links to customers and suppliers and their backroom operations with this new window to the world. Those who are able to do so gain an invaluable competitive edge.

The resource-based industries offer another important avenue to be exploited. Malaysia possesses competitive advantages in this area due to availability of raw materials, a long tradition of research and development, a strong presence in the international market and the strong presence of higher value-added industries that can take advantage of the upstream strengths. The main drawbacks are in product development, design and

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[2] See Box A (pp. 69-73), Annual Report 1995, Bank Negara Malaysia (March 1996) and “Services Sector as an Engine of Growth” by Dr. Zeti Akhtar Aziz (July 1996).

[3] Giarini and Stahel, “The Limits to Certainty: Facing Risks in the New Service Economy” (1989) quoted in “Intermediate Services and Economic Development: The Malaysian Experience” Behuria, Sutanu and Rahul Khullar, Asian Development Bank Occasional Paper (May 1994).

marketing. Attention is, therefore, being directed to equip producers with the necessary knowledge and networks to successfully market their products.

The distribution and logistics system needs to be given prime consideration if all the above developments are to be put in place. The importance of delivering the goods and services consumers want quickly, efficiently and reliably cannot be understated. The widespread containerisation of cargo, more than any other development saw the explosion in global trade and allowed previously untradeable items such as perishable produce to be shipped globally. The new developments in this area will be the improvement in logistics so as to improve multi-modality, that is, greater integration between various modes of transportation. In this regard, an integrated ports policy that hinges on load-centering at Port Klang and the use of an electronic data interchange that brings together the shippers, the port, Customs and insurers has yielded tangible results. While much improvement needs to take place, the increase in the number of mainline operators stopping at Port Klang has been encouraging. Also, faster delivery of services such as banking, brokerage, news, entertainment and even shopping are emerging. As interactive platforms and security systems evolve, internet-based delivery systems can be expected to become more widely accepted as a medium in which transactions are made, making their use more widespread.

- ***Preparing for progressive deregulation and trade liberalisation***

Competition can be an important driver of efficiency and innovation. In general, the Malaysian economy has trended towards greater deregulation with specific rules put in place to ensure safety and fair trade practices. Malaysia's basic philosophy has been to encourage managed competition, particularly in industries where the capital outlay is large, while allowing for progressive entry to foreigners through joint ventures. The gradual deregulation of the telecommunications industry, for example, has culminated with the granting of full access in 1999. However, this deregulation was accompanied with intervention, where necessary. For instance, apart from maintaining its traditional role of ensuring service standards were maintained, the Government intervened directly to expedite connectivity agreements among cellular telephone operators in the mid-1990s.

The other path to increased competition has been trade liberalisation. Malaysia has always been an open economy. Total trade amounted to more than twice gross national product in 1999. Malaysia is a signatory to many major regional and global multilateral free trade agreements. The most important of these are the Uruguay Round agreements including the General Agreement on Trade in Services that formed the World Trade Organisation and the ASEAN Free Trade Area agreement. In addition, bilateral trade agreements have been signed with several developing countries. Local industries have, therefore, been and will be even more progressively subject to international competition.

Risk Management and the Financial Sector

In the new approach towards sustainable growth, the role of the financial system in allocating capital efficiently becomes even more important. It will, therefore, be important to increase the dynamism and efficiency of the sector while ensuring that it is capable of coping with the emerging risks. The critical success factor in achieving these aims is the simultaneous development of both bank and non-bank financial institutions. In the case of banks, the emphasis is being placed not only on capitalisation, but also the implementation of a more innovative and prudent credit culture and improved risk management. While efforts have already moved forward with the initiation of the consolidation programme for domestic banks, further work remains to be done. In the case of non-bank financial institutions, efforts continue to be directed at enhancement of efficiency and the development of the capital markets, in particular, the bond markets, and innovative financiers (e.g. venture capital companies).

Co-ordination of Policies

Due recognition is given to the co-ordination and implementation of policies. Macroeconomic policy, that is fiscal and monetary policies, will continue to play supportive roles to the longer-term developmental policies. The primary aim of macroeconomic policy will be to ensure growth with economic stability. The aim is for high quality growth, led by productivity gains.

Malaysia has always practised prudent fiscal management. This resulted in fiscal surpluses, which provided the stronger base for the implementation of the current counter-cyclical fiscal policy to promote economic recovery. In 1999 and 2000, the Government has increased development spending to provide social services such as health and education to balance the slowdown in private spending. Over the medium term, the conduct of fiscal policy remains unchanged. During periods of strong growth, the Government will aim to achieve a fiscal surplus and allow the private sector to be the main engine of activity. This will reduce competition for resources and prevent imbalances, ensuring stable prices.

The conduct of monetary policy (including exchange rate policy) is mainly targeted at price stability. In this regard, the authorities will implement monetary policy in a flexible manner and adjust these policy responses as circumstances change. Flexible and pragmatic monetary policies will ensure that monetary policy does not become counter-productive to the overall development goals of the nation.

The focus of exchange rate policy will be to ensure that the rate remains consistent with the fundamentals of the Malaysian economy. The peg will not be adjusted in response to any marginal and short-term misalignments that could easily be reversed by subsequent changes in global financial markets. Meanwhile, the overall policy of improving competitiveness will ensure that Malaysia does not depend on the exchange rate to enhance the competitiveness of the economy. The authorities have long maintained that the exchange rate alone cannot guarantee competitiveness but rather it is the fundamental efficiency of the economy that is important. In summary, the overall policy direction in the medium term is to improve efficiency and competitiveness through the use of a market-oriented industrial policy. Macroeconomic policy will play a supportive role to manage emerging risks and ensure the stability of the financial markets while structural reforms continue.

Social and welfare policies such as equitable distribution of wealth and the provision of social safety nets will also continue to receive the attention of economic policy makers to ensure balanced and broad-based growth is achieved.

capital and profits, subject to a graduated levy, depending on when the funds were brought into Malaysia and the duration of the investment. The levy system provided flexibility to investors and was directed at encouraging existing portfolio investors to have a longer-term perspective of their investment in Malaysia. Following the modification, there was a net inflow of funds from non-residents amounting to RM4 billion during the period 15 February 1999 until 31 August 1999. These funds were mainly channelled into the stock market. In response to representation by fund managers to streamline the administrative problems associated with the measures, the Government announced that, effective 21 September 1999, a flat 10% levy on repatriation of profits on portfolio investment would replace the two-tier system.

With improved investor confidence and renewed optimism about the economy, there were continued strong inflows on both the current and capital accounts of the balance of payments. Hence, despite some uncertainty generated by the expiry of the September deadline on repatriation of capital without levy, the net outflows of portfolio funds remained manageable, amounting to about RM8 billion or US$2 billion. In January and February 2000, however, this trend reversed with net inflow amounting to RM8.6 billion or US$2.3 billion in the period January to 8 March 2000.

A number of **tax and non-tax measures** were introduced in Budget 2000 to address longer-term structural issues in the real sector. The crisis has confirmed the need to accelerate efforts to reduce the vulnerability due to over-reliance on exports from the manufacturing sector, particularly electronic products. Recognising that sustained growth with external balance require more balanced and diversified sources of growth for the economy, the new measures included in the Budget (details in Chapter 2) aimed at facilitating the shift towards new growth areas. Within the traditional sectors, policy measures aimed to increase the domestic value added activities to contribute to growth.

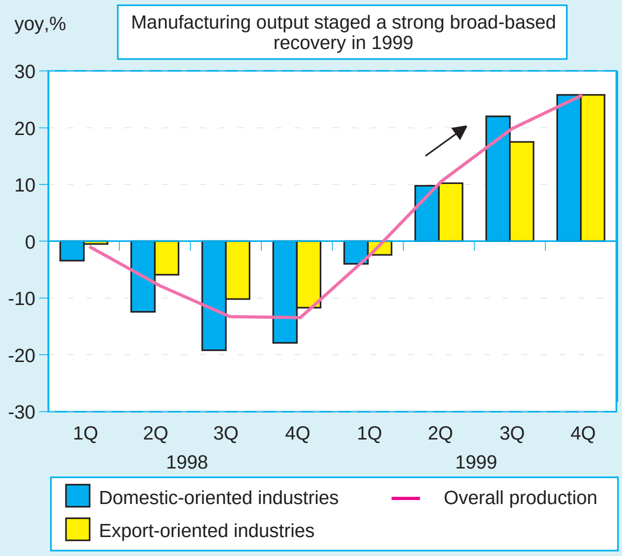
Overall, the downside risks envisaged in early 1999 did not occur. On the external front, the strong external demand following the improvements in the Asian economies and robust growth in the US economy spurred production increases in the export sector. This was underpinned by the early upswing in the global electronics cycle, and moved towards a more broad-based export growth in the latter part of 1999. The favourable external environment, the more stable conditions in the domestic financial markets provided by the selective exchange controls and the fixed exchange rate, as well as expansionary fiscal and monetary policy contributed to significant improvement in business and consumer confidence. Consequently, domestic demand recovered as the private sector responded positively to generate a stronger-than-expected recovery for Malaysia.

Sectoral Review

Manufacturing

The overall output performance of the manufacturing sector recovered strongly in 1999. Manufacturing output as measured by the Industrial Production Index (1993=100) turned around to record a strong positive growth of 12.9% (1998: –10.2%). In terms of level, the manufacturing production index exceeded the pre-recession level to register a record high of 167.8 (1997: 165.6), with the better-than-expected recovery in output of both the export- and domestic-oriented industries. In tandem with the strong pick-up in production activities, value added of the manufacturing sector turned around to record a positive growth of 13.5% (1998: –13.7%). Apart from the marked improvement in external demand, the manufacturing sector also benefited from the Government's pragmatic policy responses aimed at expediting economic recovery and promoting sustainable growth. With the favourable performance of the sector during the year,

Graph 1.7
Output Performance of the Manufacturing Sector



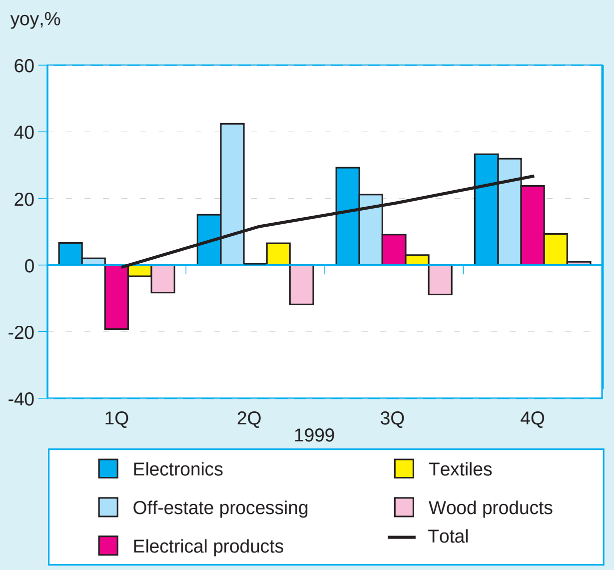
its contribution to GDP growth rose from 27.9% in 1998 to 30.1% in 1999, while its share of total exports and employment rose to 84.6% and 27.1% respectively (1998: 82.9% and 26.5% respectively).

At the initial stage, the turnaround in manufacturing output which began in February 1999 was predominantly export-led, driven mainly by a stronger-than-expected recovery in the electronics industry. Subsequently, as stability returned to financial markets and consumer confidence improved following the implementation of pro-recovery measures by the Government, output growth in the domestic-oriented sector gathered strength during the second quarter of the year. Thereafter, growth in manufacturing production accelerated, recording an annual increase of 22.5% in the second half of the year (first-half: 3.5%). Against the background of an improvement in external and domestic demand conditions, output of both the export- and domestic-oriented industries recorded a growth of 12.9% and 13.1% respectively during the year (1998: –7.3% and –13.4% respectively), thereby contributing to a broad-based recovery in the manufacturing sector.

In the export-oriented sector, growth was spearheaded by the electronics, electrical products and off-estate processing industries.

- The **electronics industry** remained the leading industry with a strong output expansion of 21.2% in 1999 (1998: –4.2%), attributable largely to the increased usage of the Internet and e-commerce, rising demand for communication chips for use in computer modems, networks and cellular phones from major markets in the United States, Europe and Japan, as well as intensified efforts in upgrading facilities to address the Y2K problem. The turnaround of electronic output was in tandem with the recovery in the global semiconductor industry, which expanded by about 18.9% in 1999, the first double-digit growth recorded since 1995.

Graph 1.8
Output Performance of the Export-Oriented Sector



- Output of the **electrical products industry** rebounded to increase marginally by 2.7%, following two consecutive years of decline. This was mainly on account of improved demand for office and computing equipment, consumer durables and air-conditioners from the United States, Japan and the Asia-Pacific region in the latter part of the year. As a group, the **electronics and electrical products industry** registered a substantial increase of 15.6% in output during the year (1998: –7.7%).

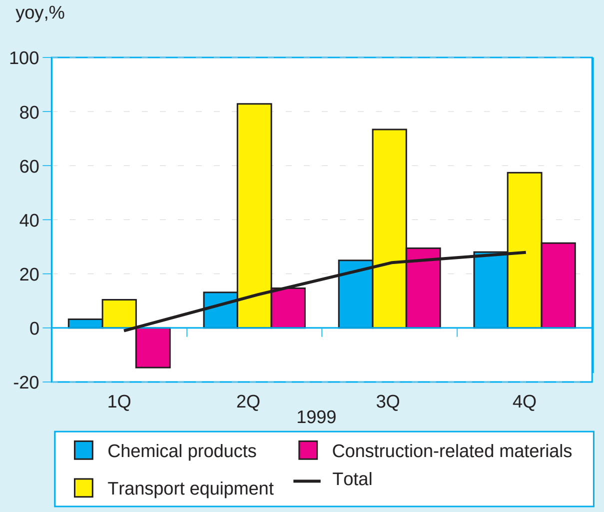
- Output of the **off-estate processing industry** expanded significantly by 24.7% in 1999 (1998: –2.7%), reflecting largely increased palm oil processing activity on account of higher crude palm oil production.

- The **textiles and wearing apparel industry** also performed better with a positive output growth of 4% (1998: –5.3%). Higher expansion of the fibre spinning and weaving, synthetic textiles milling and dyeing, bleaching and finishing activities, as well as improved demand for better-designed and up-market wearing apparel from major overseas buyers such as the United States and Europe contributed to improved output performance.

- On the other hand, production of the **wood and wood products industry** continued to decline for the third consecutive year (–7.3%; 1998: –11.3%). Although production of plywood and particle board improved in response to increased external demand, this was more than offset by the significant contraction in the output of sawn timber as logging activities in the peninsula were disrupted by heavy rain experienced during the year.

In 1999, manufacturing activities of the **domestic-oriented industries** as a group recorded a significant turnaround of 13.1% (1998: –13.4%).

Graph 1.9
Output Performance of the Domestic-Oriented Sector



The impressive output performance reflected mainly increased consumer demand and public investments following the implementation of expansionary fiscal and monetary policies during the year. Growth of the domestic-oriented sector escalated to 23.9% during the second half of the year (first-half: 2.8%), with all industries except the tobacco products industry recording increases in output. Of significance was the strong expansion in the output of the chemical products, transport equipment and construction-related materials industries which together accounted for 61% of total value added of the domestic-oriented sector.

- Output expansion of the **chemicals and chemical products industry** continued throughout the year since its recovery in February. The industry recorded a strong positive growth of 17.1% (1998: –1.8%) as all the sub-sectors, except the soap and cleaning preparation sub-sector, registered higher output growth. In particular, the increased production of resins and plastic products, paints, varnishes and lacquers as well as industrial gases was in response to the strong demand from the electronics, automobile and construction-related materials industries.

- Benefiting from the implementation of the measures to stimulate domestic demand, output of the **transport equipment industry** rebounded significantly to increase by 53.5% in 1999 (1998: –52.2%). During the year, sales of motor vehicles comprising passenger cars and commercial vehicles recorded a strong positive growth of 75.8% to reach a total of 288,547 units, in response to improved domestic demand (1998: 164,116 units). The higher production of motor vehicles created positive spin-off effects on the output of motor vehicle parts and accessories, which turned around to record a strong expansion of 43% in 1999 (1998: –40.1%).

- In tandem with the turnaround in construction activity in the second half of the year, output of the **construction-related materials industries** as a group improved markedly by 14.3% (1998: –27.6%). Higher demand for cement and concrete products, structural clay products as well as iron and steel bars and rods contributed to increased production of the **non-metallic mineral products** and **iron and steel industries**, at 2.6% and 29.5% respectively in 1999 (1998: –26.5% and –29.1% respectively). At the same time, increased exports also supported output growth. This was true especially in the case of ceramic products which benefited from higher external demand particularly from Europe, and selected iron and steel products which gained from the recovery in the ASEAN countries.

- At the same time, the decline in the production of **fabricated metal products** moderated significantly to –1.1% (1998: –17.2%), as output of most of the sub-sectors, including the structural metal products, brass, copper and aluminium as well as tin cans and metal boxes sub-sectors turned around in the second half of the year amidst improved domestic economic activity. In addition, increases in the production of wire and wire products during the year contributed to the improved output performance of the industry.

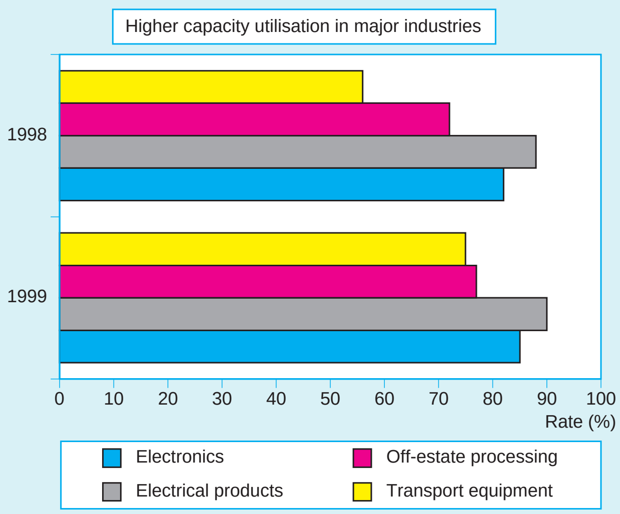
- Output of the **rubber products industry** registered a slower growth of 3.6% in 1999 (1998: 7.8%), as the moderation in the production of gloves amidst intense competition from neighbouring countries more than offset the increase in output of tyres and tubes.

- Reflecting the improvement in domestic consumption, the production of **food products** expanded positively by 5.7% in 1999 (1998: –2.1%), with notable increases in the production of other dairy products, biscuits, rice, flour and sugar. In the **beverages and tobacco products industry group**, the production of beverages turned around to increase by 13.2% in the second half of 1999, while the decline in the output of tobacco products moderated significantly to –9% (first-half 1999: –16.8% and –20.9% respecitively) as domestic demand conditions improved further. In 1999, output of the group recorded a slower decline of –9.4% (1998: –10.4%).

- In 1999, the contraction in the output of the **petroleum products industry** slowed down markedly (–0.3%; 1998: –11.5%), as higher oil prices prompted increases in crude oil refining activities. Production of other petroleum products and coal also rose in the second half of the year. Meanwhile, the improvement in output of the manufacturing sector, especially the electronics and electrical products industry had led to increased demand for paper products, in particular, containers and boxes of paper and paperboard. During the year, the **paper products industry** recorded a positive output expansion of 12.8% (1998: –8.7%).

In response to the strong improvement in demand conditions in the international and domestic markets, most industries, especially those producing electronics and motor vehicles, experienced a rapid drawdown in inventory levels. In line with this development, overall capacity utilisation in the manufacturing sector rose significantly. The electronics (mainly semiconductors), electrical products (mainly radio, television and communication equipment), chemical products (mainly paints), transport equipment (mainly motor vehicles), rubber products and paper products were operating above 90% capacity. Meanwhile, improvement in capacity utilisation was also evident in industries producing basic metals and fabricated metal products.

Graph 1.10
Capacity Utilisation of Selected Industries



For the construction-related materials industry, sustained revival of the construction sector is envisaged to absorb the remaining excess capacity.

While the policy response of the Government to the financial crisis was instrumental in revitalising activities in the manufacturing sector, past policies which were implemented to enhance efficiency and productivity, contributed to the resilience of the manufacturing sector. In particular, factors such as well-diversified export markets, strong focus on product quality and design, increased automation and mechanisation, competitive pricing and reliable delivery had enabled the manufacturing sector to bounce back and attain a steady and robust recovery during the year.

During 1999, the main focus of policies has been to improve labour productivity in the manufacturing sector. Given the already full employment situation, recent measures focus on facilitating the process of moving towards a more capital-intensive and hi-tech manufacturing base. The Government has put in place various special incentives to encourage indigenous technological capability and foreign participation in R&D activity, as well as to encourage training and re-training of workers so as to strengthen the quality and skills of the workforce. For instance, in the 2000 Budget, the Government has allocated a total of RM226.85 million for the Intensification of Research in Priority Areas (IRPA), to be shared between the public research and higher education institutions. At the same time, priority was also given to high-technology industries. A total of RM25.17 million was allocated for programmes that promote science and technology, to encourage the use of new technology, upgrade innovative capabilities and commercialise local technology.

Construction

The contraction of the construction sector moderated markedly in 1999, with value added of the sector declining by 5.6%, compared with a sharp decline of 23% in 1998. The improvement was particularly evident in the second half of the year when value added recorded a positive annual growth of 1.8%. Construction activity was supported mainly by the implementation of infrastructure projects under the fiscal stimulus package as well as housing development in response to strong underlying demand and low interest rates. Reflecting improved sentiments on the economic outlook, the value and volume of property transactions increased sharply by 23.1% and 21.1% respectively during the year

(–47.6% and –32.3% respectively in 1998). However, growth of the construction sector continued to be constrained by the stock overhang of commercial buildings and poor demand for higher-priced residential units, particularly those in the suburban areas. Consequently, credit extended for construction activity by the banking system (including loans sold to Danaharta) declined by RM2.3 billion or 5% in 1999.

Recovery was most evident in the **civil engineering sub-sector**. The BNM Survey of the Construction Sector, 1999 showed that most companies surveyed reported an increase in construction activity in the civil engineering sub-sector in 1999. Growth was supported by higher allocation for infrastructure projects and on-going projects related to power plants, roads, rail, water, port, sewerage and waste disposal. The 1999 Budget allocated RM4 billion for development of infrastructure, particularly for the construction of roads, bridges, rail, ports and civil aviation facilities. The resumption of construction work on the New Pantai Expressway as well as rail projects, including the Express Rail Link and the People-Mover Rapid Transit System, provided further impetus to the growth of the sub-sector.

The **non-residential sub-sector** remained weak during the year, due to the continued excess supply of office and retail space. Nevertheless, with some pick-up in demand, the decline in value added moderated. The improved sentiment in the sub-sector was reflected in the increase in the value and number of commercial property transactions by 26.1% and 31.4% respectively in 1999.

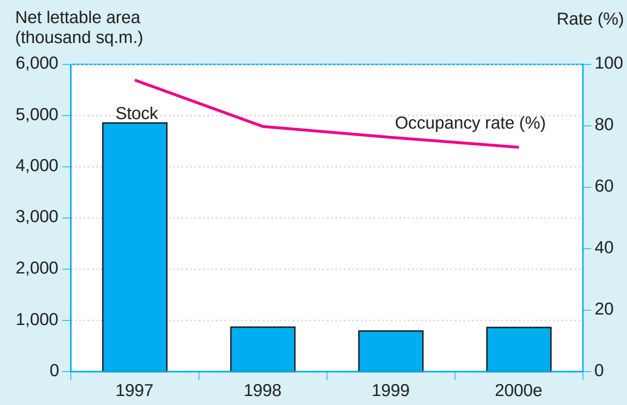
Table 1.5
Supply of Office Space, Retail Space, Condominiums and Apartments in the Klang Valley[1]

	Office Space		Retail Space		Condominiums & Apartments
	Square metres	Occupancy rate (%)	Square metres	Occupancy rate (%)	Units
1991	12,331	96.7	17,502	92.0	13,560
1992	39,825	97.2	58,910	94.2	3,768
1993	332,246	91.5	130,345	97.3	18,232
1994	192,808	94.3	117,340	98.5	9,331
1995	362,851	94.9	341,091	96.1	17,822
1996	296,742	95.5	136,964	92.8	14,568
1997	869,394	94.9	362,574	90.5	5,473
1998	873,346	79.8	395,328	59.5	14,151
1999	795,750	76.2	58,486	76.6	9,547

[1] Refers to Kuala Lumpur & Selangor D.E.

Source: Valuation and Property Services Department

Graph 1.11
Supply of Purpose-Built Office Space in the Klang Valley[1]

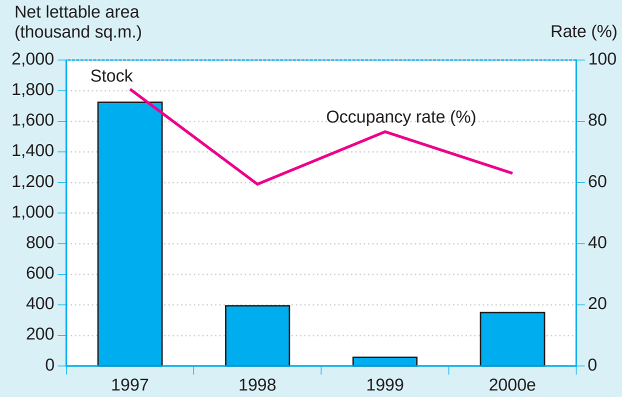


[1] Refers to Kuala Lumpur & Selangor D.E.

In the **purpose-built office space sub-sector**, growth emanated mainly from ongoing projects. A total of 0.8 million square metres of lettable area entered the Klang Valley in 1999, bringing the total supply to 6.5 million square metres at year-end. With the new supply exacerbating the large stock overhang, occupancy rates fell further. The overall occupancy rate for purpose-built office space in the Klang Valley declined from 79.8% in 1998 to 76.2% in 1999. Reflecting the oversupply situation, BNM's estimates showed that the average monthly rental rates of office buildings in the Klang Valley declined further by 4.5% to RM40.60 per square metre (RM3.80 per square foot) in 1999. Compared to the levels in 1997, the average rental rate was lower by 18.5%.

In the **retail space sub-sector**, the delayed completion of several projects resulted in new supply in the Klang Valley totalling 58,500 square metres during 1999, compared with the 205,000 square metres

Graph 1.12
Supply of Retail Space in the Klang Valley[1]



[1] Refers to Kuala Lumpur & Selangor D.E.

scheduled to come on stream. Thus, at 2.2 million square metres at the end of 1999, the total supply of retail space was lower than initially anticipated. With higher demand due to improved business and consumer sentiments and lower new supply, occupancy rates in retail complexes in the Klang Valley improved significantly to 76.6% at end-1999, compared with 59.5% at end-1998. Retail complexes in prime areas of the Klang Valley continued to enjoy relatively high occupancy rates. Meanwhile, retail space under construction remained high at 1.1 million square metres as at end-1999, representing 48% of the existing stock. Many of these projects were those that were near completion and are expected to come on-stream in 2000-2003. The stock overhang of 1.5 million square metres of retail space nationwide as at June 1999 and the expected surge of new supply are expected to influence occupancy rates in the near term.

The number of new **hotels** increased by 6.8% or 97 units, which added 22,662 new rooms to total supply in 1999 (1998: 4% or 54 new hotels with 9,351 rooms), with the bulk of the construction activity carried out prior to 1999. Despite the increase in hotel capacity, the average occupancy rate increased to 53.4% in 1999 from 49.9% in 1998 due to the higher number of tourist arrivals during the year (8 million; 1998: 5.6 million). Latest available data showed that the average occupancy rates for hotels in Penang and Johor Bahru had also increased during the first nine months to 58.7% and 54.6% respectively, compared with 55.7% and 48.8% for the corresponding period of 1998.

Construction activity in the **residential sub-sector** continued to be supported by strong underlying demand, particularly for landed properties in choice locations. Encouraged by lower prices, lower interest rates and improved job opportunities, the value and volume of residential property transactions increased by 32.8% and 27.6% respectively in 1999. Construction activity, especially for low- and medium-cost houses accelerated in the second half of 1999 following the increase in the issue of new developers' licences (+11.7%) in 1999 (1998: –30.3%). Activity in this sub-sector was reflected in the increase in new sales and advertising permits (+13.3%; 1998: –28.3%). The improved performance was also reflected in the number of housing units that were completed by the private sector, which increased by 2.2% to 122,699 units in 1999. On the other hand, a smaller number of units of condominiums and apartments (9,547) were completed in the Klang Valley during the year, compared with 14,151 units in 1998.

Despite the improved performance, the residential sub-sector was still faced with an excess supply situation. As at end-June 1999, the number of unsold units was estimated at 93,599 units, valued at RM14.2 billion. The unsold residential property included 12,021 units of low-cost houses, which were located mainly in the outskirts of towns. New construction activity in the residential sub-sector was, therefore, constrained by the large stock of unsold houses and condominiums. Although more developers' licences were issued during the year, the average size of the projects launched was smaller so that the number of houses approved by the Ministry of Housing and Local Government for construction by private developers declined by 5.7% to 183,041 units during the year. Approvals for low- and medium-cost houses continued to account for the largest share (66%) of total approvals. This reflected that demand was mainly for affordable housing. It also reflected the impact of the BNM guideline, effective 6 January 1999, whereby banking institutions were encouraged to finance development of new residential property and shophouses costing less than RM250,000 each.

Latest available data showed that house prices continued to trend downwards in the first half of 1999. The Malaysian House Price Index declined further by 12% in the first half of 1999 (1998: –9.4%). The decline was broad-based with the price correction being more significant for detached (–13.4%) and semi-detached houses (–10.9%). Following successive price declines since 1996, the high-rise units recorded a smaller decline of 5%. By region, the decline was more pronounced in the Klang Valley (–10.2%), Johor Bahru (–8.7%) and Pulau Pinang (–8.2%) as these areas tended to have a greater supply of higher priced units. In contrast, the Seremban-Sepang and Ipoh-Kinta regions recorded increases in house prices of 1.4% and 7% respectively in the first half of 1999. At the state level, all states experienced lower prices except Kelantan, Perak and Perlis, which registered price increases of 5%, 4.3% and 1% respectively. The decline in house prices was most evident in Selangor (–16.4%), affecting mostly detached houses (–37.7%), followed by semi-detached (–29.6%) and terraced houses (–15.2%). With the strengthening of economic recovery in the second half of the year there were signs of price increases for landed property, particularly terraced houses in selected choice locations in the Klang Valley. Indicators included the high take-up rate of newly launched housing projects as well as higher transaction prices in the secondary market. Price increases were evident in the secondary market for properties in locations such as Bangsar, Bandar Utama and Subang Jaya.

Table 1.6
Home Ownership Campaigns (HOC 1 & 2) - Number and Value of Properties Sold

	Supply		Sales		Sales (% of supply)	
	Units	Value (RMm)	Units	Value (RMm)	Units	Value (RMm)
HOC 1 (12 Dec. '98 - 12 Jan. '99)	53,849	11,778	19,650	3,576	36.5	30.4
HOC 2 (29 Oct. '99 - 7 Dec. '99)	70,135	10,254	17,956	2,795	25.6	27.3

Source: Housing Developers' Association

Meanwhile, house prices in 1999 have remained very attractive to foreigners as they were lower in US dollar terms following the depreciation of the ringgit since 1997. Prices of single-storey and double-storey terraced houses in prime locations were lower by 30-50% in the second quarter of 1999 compared to their pre-crisis levels in the second quarter of 1997. Accordingly, foreign purchases increased significantly. Based on approvals by the Foreign Investment Committee, a total of 1,382 units of residential properties (+18.7%) valued at RM560 million were purchased by foreigners in 1999 (1998: 1,164 units valued at RM434 million). The bulk of the purchases was for condominiums and terraced houses. In the case of commercial property, foreign purchases totalled RM190.9 million (1998: RM44.3 million).

As growth in the construction sector continued to moderate, demand for construction workers declined further, albeit at a marginal rate of –0.7%, to 804,000 workers (1998: –16.8%). However, as the country's employment level increased by 1.7% to 8.7 million workers during the year, the share of construction workers to total employment declined to 9.2% (1998: 9.4%). Nevertheless, skilled foreign workers were in greater demand, resulting in their average daily wages increasing by 6% compared with wages of the other categories of workers, which generally stabilised.

The findings of BNM's Survey of the Construction Sector, 1999 reflected developments in the construction sector in 1999. The performance of the companies surveyed, however, was more favourable, recording a growth of 3.4% in construction activity during 1999. In terms of issues faced, the majority of respondents were still plagued by the problem of excess stocks, declining selling prices and, hence, lower profit margins as well as unfavourable business conditions. Average selling prices of retail and office buildings declined by 20% each while prices of single-storey and double-storey terraced houses declined by 8% and 24% respectively. Meanwhile, one-fifth of the respondents experienced difficulty in obtaining bank financing. Most companies, however, felt that employment conditions were favourable as they continued to rely on the services of foreign labour to fulfill demand in this labour-intensive industry.

During the year, the Government continued with its efforts to revitalise the construction industry in support of economic recovery. To help reduce excess stocks, the Government assisted in the Second Home Ownership Campaign (29 October - 7 December 1999), following the First Home Ownership Campaign (12 December 1998 - 12 January 1999). Incentives offered during the campaign included exemption of stamp duties, and a minimum price discount of 5% for properties costing RM100,000 or less, and 10% for properties costing above RM100,000. Financial institutions also offered incentives such as higher margin of finance (up to 95%), waiver of processing fees and increased loan tenure of up to a maximum of 30 years. Legal fees were also lowered for the Sale and Purchase and loan agreements as well as other charge documents. At the close of the campaign, a total of 17,956 units of residential and commercial properties valued at RM2.8 billion were sold, representing about one-quarter of the total number of units offered for sale.

To assist small- and medium-scale Bumiputera entrepreneurs in the construction sector, a total of RM100 million of the RM300 million Tabung Projek Usahawan Bumiputera, which was established on 10 February 2000, was allocated for the construction sector. This would enable the small- and medium-scale Bumiputera entrepreneurs to have access to financing at a reasonable cost of 5% per annum.

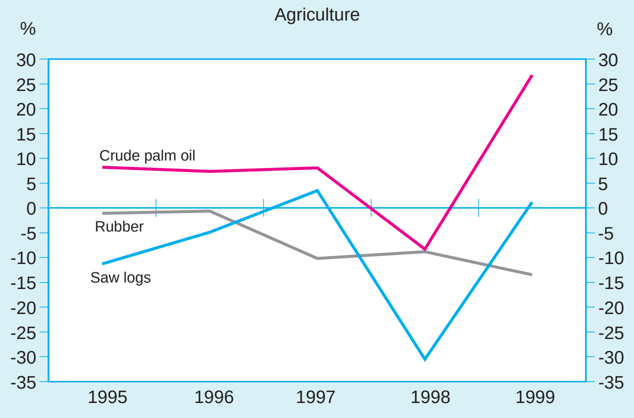
Total loans extended by the banking system to the broad property sector, comprising residential, non-residential, real estate and construction sub-sectors increased by 2.7% or RM4 billion to RM153.6 billion (including loans sold to Cagamas and Danaharta). However, as total loans extended by the banking system increased by only 0.2% in 1999, the share of loans to the broad property sector increased to 36% as at end-1999 (1998: 35.1%). The increase in loans was extended mainly for the purchase of residential property, and for financing real estate activity. Of the total loans extended by the banking system in 1999, purchase of residential property accounted for 14.8%, followed by loans for construction (10%), purchase of non-residential property (6.8%) and real estate activity, 4.3% (1998: 13.2%, 10.6%, 7.3% and 4% respectively). Following the easing of the credit situation, the purchase of housing loans by Cagamas moderated, accounting for 25.6% of total housing loans outstanding (1998: 33.8%).

Reflecting improved sentiments and a pick-up in demand in the latter half-year, the total value of housing loans approved by the various housing credit institutions as a group rose significantly by 106.9% to RM23.5 billion in 1999. In particular, the housing loans approved by the commercial banks and finance companies as a group totalled RM20.6 billion or an increase of 123.5%, accounting for 87.9% of the total value of housing loans approved by the housing credit institutions. However, loans approved by the Malaysia Building Society Berhad, Borneo Housing Mortgage Finance Berhad, Sabah Credit Corporation and Bank Simpanan Nasional declined due to keen competition and the attractive loan packages offered by the banking institutions. In tandem with the higher loan approvals, total housing loans outstanding increased in 1999. Financing of owner-occupied houses costing RM100,000 or less under the prescribed rate provided by the banking system accounted for 30.6% of total financing for residential houses. Effective 1 April 1998, the commercial banks and finance companies had made firm commitments to finance 137,048 and 45,790 of these units respectively as at end-1999.

Agriculture, Forestry and Fishery

Value added in the agriculture, forestry and fishery sector turned around to increase by 3.9% in 1999 (1998: –4.5%) primarily on account of the marked increase in crude palm oil production. The production of saw logs, fish and livestock also increased but this was not sufficient to offset the decline in the production of rubber, cocoa and other agriculture products. Hence, in 1999, the agriculture, forestry and fishery sector accounted for a lower share of GDP (9.3%; 9.4% in 1998), total exports (8.6%; 10.5% in 1998) and employment (16%; 16.3% in 1998).

Graph 1.13
Production Growth Rate



Within the agriculture sector, **crude palm oil** remained the most important growth-generating commodity in 1999, accounting for 31.9% of the sector's value added. Together with processed palm oil, it contributed 52.5% of export earnings from the agriculture sector. Crude palm oil production increased strongly by 26.8% to 10.6 million tonnes in 1999. The surge in production was mainly due to the upturn in the biological yield cycle of the oil palm trees and to a lesser extent, an expansion in mature area, especially in Sarawak.

On a regional basis, production in the peninsula increased by 23.9% to 7.4 million tonnes, while production in Sabah increased by 31.9% to 2.7 million tonnes and Sarawak by 50.7% to 0.5 million tonnes. As returns from oil palm cultivation were more favourable compared with other industrial crops, the total area under oil palm cultivation expanded further by 4.5% to 3.2 million hectares. Total mature area increased by 7% to 2.8 million hectares as at end-1999. Expansion in mature area under oil palm was most rapid in Sarawak (99%), followed by Sabah (6%) and Peninsular Malaysia (2.2%). During the year, Malaysia remained the world's largest producer of crude palm oil, accounting for more than half (53%) of total world production.

During the year, private estates accounted for the largest share of the total oil palm cultivated area at 58.2% or 1.9 million hectares, followed by the organised smallholders under the Federal Land Development Authority, Federal Land Consolidation and Rehabilitation Authority and the Rubber Industry Smallholders Development Authority schemes (26.2% or 0.8 million hectares) and schemes under the state governments and independent smallholders (combined share of 15.6% or 0.5 million hectares).

With the expansion in area planted with oil palm in Sabah, a total of 33 new licences for mills were granted by the Palm Oil Registration and Licensing Authority in the state in 1999. Five new licences were granted in Sarawak while another 11 new licences were issued in the peninsula. As at end-1999, the number of mills in operation was 333 (1998: 325) with an annual capacity to process 61.5 million tonnes of fresh fruit bunches. Reflecting the higher production of crude palm oil, the average rate of capacity utilisation of the mills rose to 92.5% during the year (1998: 75.1%). In the refining sector, domestic processing of crude palm oil increased sharply by 21.7% to 10.3 million tonnes in 1999. During the year, one new refining licence was issued by the Ministry of International Trade and Industry, bringing the total number of refineries in operation to 46 with a total annual capacity to process 12.9 million tonnes of crude palm oil.

Based on existing acreage under oil palm cultivation and expected continued increase in new planting of oil palm, Malaysia's production of crude

Graph 1.14
Oil Palm: Area, Production and Yield

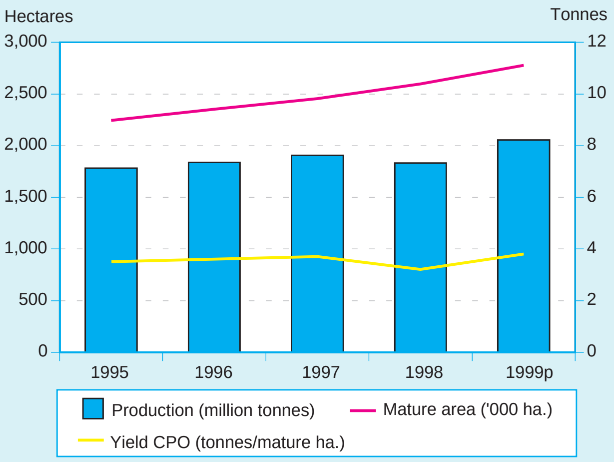


Table 1.7
Oil Palm: Area, Production and Yield

	1998	1999*p*	1998	1999*p*
			Annual change (%)	
Area ('000 hectares)				
Planted	3,078	3,216	9.2	4.5
Mature	2,597	2,780	5.8	7.0
Production ('000 tonnes)				
Crude palm oil	8,320	10,553	–8.3	26.8
Yield (tonnes/mature hectare)				
Crude palm oil	3.2	3.8	–13.5	18.8

p Preliminary

Source: Department of Statistics
PORLA

palm oil will continue to be on a rising trend in the medium and long term. Given the prospect of increasing supply of palm oil, efforts to penetrate new markets as well as R&D to develop new uses of palm oil were further enhanced. During 1999, the Malaysian Palm Oil Promotion Council (MPOPC) held promotional activities in various countries to improve market opportunities and trade. In this regard, MPOPC participated in 20 international exhibitions during the year. Meanwhile, the Palm Oil Research Institute of Malaysia (PORIM) intensified its R&D on new uses of palm oil in both the edible and non-edible products categories. In addition, PORIM continued to undertake research on developing new high-yielding clones and better agronomic practices, including mechanisation of field operations, to increase productivity of the industry. During the year, the Advanced Oleochemical Technology Centre (AOTC) was established to spearhead research in the production and utilisation of palm-based oleochemicals for more value added downstream activities.

Production of **natural rubber** which has been below the one million tonnes production level since 1997, declined further by 13.5% to 766,540 tonnes in 1999. The industry continued to be affected by depressed prices, labour shortages and reduction in cultivated area. During the year, prices for natural rubber fell further due to weak world demand for rubber amidst ample global supplies. Malaysia's RSS 1 price declined by 14.4% to 240 sen per kilogramme. High stocks of rubber, especially latex also led to low farmgate prices for smallholders. The unremunerative level of prices discouraged tapping activity, particularly among the smallholders, which accounted for almost 80% of the country's

Table 1.8
World Elastomer: Production and Consumption

	1998	1999[1]	1999[1]	1998	1999[1]
	'000 tonnes		% share	Annual change (%)	
Production	16,700	12,460	100.0	1.4	0.7
Natural rubber	6,710	4,910	39.4	5.2	–0.6
Thailand	2,216	1,413	11.3	9.0	–14.6
Indonesia	1,714	1,383	11.1	13.9	6.2
Malaysia	886	593	4.8	–8.8	–8.5
India	591	409	3.3	1.9	5.1
The People's Republic of China	450	345	2.8	1.4	2.7
Vietnam	219	177	1.4	9.0	11.3
Sri Lanka	96	75	0.6	–9.4	2.7
Nigeria	93	68	0.5	43.1	–2.9
Others	445	447	3.6	–20.5	44.7
Synthetic rubber	9,990	7,550	60.6	–1.0	1.6
Consumption	16,470	12,380	100.0	–0.2	0.7
Natural rubber	6,590	4,930	39.8	1.4	0.6
Synthetic rubber	9,880	7,450	60.2	–1.2	0.8
Deficit(–)/ surplus(+)	+230	+80			

[1] January - September

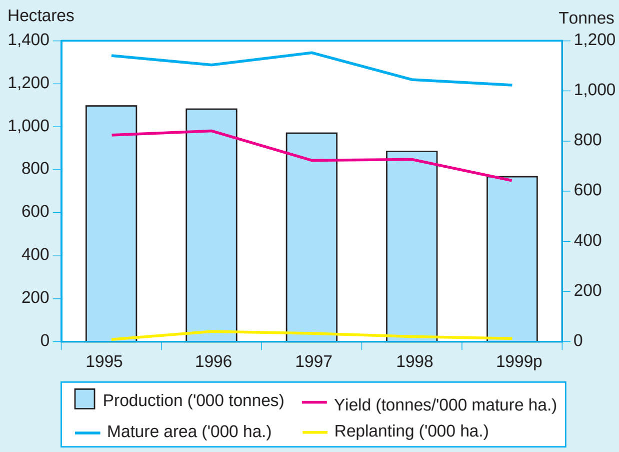
Source: International Rubber Study Group

rubber production. The production of rubber during the year was also affected, to some extent, by the slow rate of replanting over the past decade, contributing to the low level of yields in the smallholder sector.

The prolonged low prices for natural rubber had adversely affected rubber producers, particularly the smallholders. This prompted the Government to introduce in mid-1999, a temporary scheme, whereby the Government purchased rubber directly from the smallholders and rationalised the stock of latex in the country. The scheme was subsequently discontinued in February 2000 when rubber prices improved.

A major problem in the rubber smallholding sector is the low yield. In 1999, a total of 388,000 hectares of rubber cultivated land (26% of total) were due for replanting as the trees were more than 25 years old. During the year, the Rubber Industry Smallholders Development Authority (RISDA) financed the replanting of 13,600 hectares of smallholders' rubber land. To encourage replanting, the Government has, in the 2000 Budget, provided an allocation of RM201 million for replanting purposes, covering 45,000 hectares of

Graph 1.15
Rubber: Area, Production and Yield



rubber cultivated land. In addition, the Government announced in the Budget that it would set up a RM1 billion fund to provide soft loans to RISDA for replanting programmes. In an effort to increase productivity, and given the problem of labour shortages, an allocation of RM80 million was provided in the Budget to encourage rubber smallholders to adopt the low intensity tapping system (LITS). Through LITS, productivity can be increased by 30% compared to the conventional tapping system.

In the international arena, the International Natural Rubber Agreement (INRA) was terminated in October 1999, following the withdrawal of Malaysia and Thailand from the pact. With the termination of INRA, Malaysia and Thailand signed a memorandum of understanding (MoU) with the main purpose of joining efforts and

Table 1.9
Rubber: Area, Production and Yield

	Estates		Smallholdings	
	1998	1999*p*	1998	1999*p*
	'000 hectares			
Planted area	197	192	1,303	1,273
Replanting	3	2	22	14
New planting	1	1	4	2
Production ('000 tonnes)	198	182	687	585
Yield (kg./mature ha.)	1,021	968	670	580

p Preliminary

Source: Department of Statistics
Malaysian Rubber Board
Department of Agriculture, Sarawak
Sabah Rubber Fund Board

sharing resources available in their respective countries to achieve equitable rubber prices for smallholders. At the same time, both countries would develop suitable schemes to minimise stock withholding in order to avoid a market overhang. In addition to co-operation in areas relating to price and trade, the MoU also provided for technical co-operation. Seven broad areas have been identified for technical co-operation, including specification of natural rubber products, exploitation of rubberwood and clone breeding. To avoid a large stock build-up in the international rubber market arising from the release of the International Natural Rubber Organisation's (INRO) rubber stockpile, Malaysia and Thailand had established a US$43 million fund to purchase rubber stocks held by INRO.

Production of **saw logs** turned around to increase by 1.2% to 21.9 million cubic metres in 1999 (1998: –30.5%), due entirely to higher production in Sarawak. Log production in Sarawak accounted for 60% of national production. In response to the recovery in external demand, especially from the Asia-Pacific markets, log production in Sarawak increased strongly by 15.8% to 13.1 million cubic metres. On the other hand, production in Peninsular Malaysia and Sabah declined by 5% and 24% to 4.8 million cubic metres and 4 million cubic metres respectively. During the year, Malaysia's saw log production levels were in line with the Government's forest conservation policy and sustainable forest management as stipulated under the International Tropical Timber Agreement.

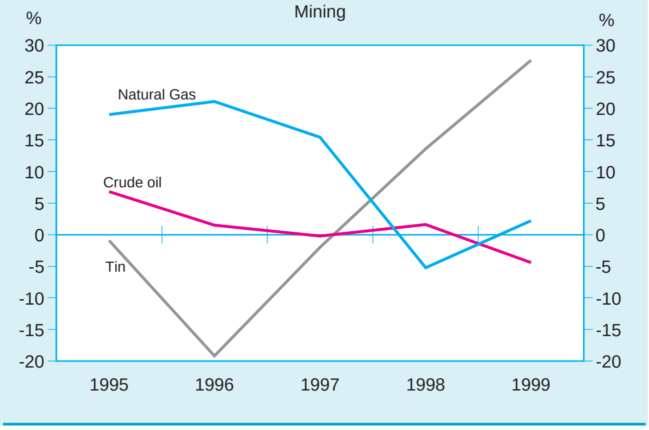
Cocoa production, which had been on a downtrend since 1991, fell by 7.2% to 83,700 tonnes in 1999 (1998: –14.9%) as cultivated area under cocoa declined further following conversion of cocoa cultivated land to other crops, particularly oil palm. Low cocoa prices during the year had also affected production. In addition, rising cost of production as a result of increases in labour costs and prices of agricultural inputs had affected production particularly among the smallholders. In terms of acreage, a total of 1,778 hectares of cocoa cultivated land were converted to other crops during the year. However, in Sabah where production accounted for 70% of the total national output, the total area cultivated with cocoa expanded further by 11.4% during the year. In terms of domestic consumption, demand from cocoa grinders increased further to 110,440 tonnes in 1999 (1998: 100,100 tonnes) in response to higher external demand. As domestic production of cocoa beans was insufficient to meet the demand from the domestic cocoa processing industry, cocoa beans were imported, mainly from Indonesia.

Production in the **fishery** industry increased by 5.1% to 1.4 million tonnes in 1999, reflecting higher production of both marine fish and aquaculture. Marine fish landings, which accounted for almost 90% of total fish production increased by 2.5% to 1.2 million tonnes. As a result of efforts to promote aquaculture activities, production from the sub-sector grew sharply by 28.7% to 172,000 tonnes. During the year, measures were taken to increase fish landings through the construction of a greater number of artificial reefs for breeding fish and through improved fishing technology. With higher production, exports of fish increased by 1.4% to 152,000 tonnes. The main export markets were Thailand, Singapore and Japan. At the same time, imports of fish, mainly from Thailand, declined by 0.6%. During the year, per capita consumption of fish in Malaysia increased to 44 kilogrammes from 43 kilogrammes in 1998.

Mining

Value added in the mining sector contracted by 4% in 1999 (+1.8% in 1998) on account of lower production of crude oil, which accounted for almost 80% of total value added in the sector. On the other hand, natural gas production turned around to grow by 2.1% due to higher domestic and external demand. Tin production also registered a positive growth during the year, in response to favourable prices. In terms of contribution to the economy, the share of the mining sector to GDP growth was lower at 7.3% in 1999 (1998: 8.1%). Its share of total exports was, however, higher at 5.4% (1998: 5.2%) following the sharp increase in prices for crude oil. Meanwhile, the sector's contribution to employment remained unchanged at 0.5% during the year.

Graph 1.16
Production Growth Rate



In 1999, production of **crude oil, including condensates** declined by 4.4% to 693,200 barrels per day (bpd). Excluding condensates, crude oil production was lower by 4% at 614,100 bpd, compared with 639,600 bpd in 1998. The lower level of crude oil production was in line with the National Depletion Policy, which aims to sustain the exploitation of the nation's resources. As at 1 January 1999, Malaysia's crude oil reserves was 3.6 billion barrels and at the current rate of production, this level of reserves could last for another 15 years. Meanwhile, the production of condensates (that is crude oil produced in gas fields) declined by 7.4% to 79,100 bpd (1998: 85,400 bpd) in response to weaker external demand for condensates.

On a regional basis, Peninsular Malaysia accounted for a share of 58% of total production, Sarawak 29% and Sabah 13%. Lower crude oil production was recorded by all regions, namely, Sarawak (–5%), Sabah (–4.3%) and the peninsula (–4.1%). During the year, two new oil fields, one each in the peninsula and Sarawak, commenced operations. In the upstream sector, four new production sharing contracts were signed in 1999. A total of 10 exploration wells and 41 development wells were drilled during the year, while 93,000 line kilometres of seismic data were acquired for exploration and development purposes.

Natural gas production, on the other hand, turned around to increase by 2.1% to 3,802 million standard cubic feet per day (mmscfd) in 1999 following increased domestic demand as well as higher external demand for LNG by Japan and Korea. While the production of associated gas (originating from oil fields) declined by 6.5% in line with the decline in crude oil production, production of gas from gas fields recorded a growth of 3.4%. Based on reserves as at 1 January 1999, it was estimated that Malaysia's gas reserves could be utilised for another 30-45 years.

The production of **tin-in-concentrates** continued to record positive growth for the second consecutive year in 1999 as tin prices remained favourable. The firm tin prices resulted in three new mines commencing operations during the year and also induced higher production from existing mines. As a result, production of tin-in-concentrates increased sharply by 27.6% to 7,350 tonnes in 1999.

Services

Supported by the overall improvement in the economy, the services sector rebounded to grow by 2.9% in 1999 (1998: –0.8%). The recovery was broad-based encompassing stronger growth in final services and a turnaround in the growth of intermediate services. Growth picked up slowly by 0.6% in the first half-year and subsequently accelerated to 5.1% in the second half-year, as the recovery strengthened further. Despite a small decline in its share of GDP to 54.2% (1998: 55.6%), the services sector remained the largest sector in the economy.

Intermediate services, comprising transport, storage and communications; and finance, insurance, real estate and business services expanded by 2.2% in 1999 (1998: –2.3%). Growth emanated mainly from the **transport, storage and communications** sub-sector, particularly transportation services, underscoring the strong increase in international trade.

- For **port services**, the volume of cargo handled by the five major ports in Malaysia increased strongly by 9.5% to 132.9 million

Table 1.10
Growth in the Services Sector in 1987 Prices

	1998	1999*p*	1998	1999*p*
	Annual change (%)		% share of GDP	
Services	**–0.8**	**2.9**	**55.6**	**54.2**
Intermediate services	–2.3	2.2	20.8	20.1
Transport, storage and communication	*0.9*	*3.8*	*8.2*	*8.0*
Finance, insurance, real estate and business services	*–4.3*	*1.2*	*12.6*	*12.1*
Final services	0.1	3.3	34.8	34.1
Electricity, gas and water	*3.0*	*4.9*	*3.4*	*3.4*
Wholesale and retail trade, hotels and restaurants	*–3.1*	*2.1*	*15.7*	*15.2*
Government services[1]	*1.8*	*6.6*	*7.3*	*7.4*
Other services[2]	*3.7*	*2.1*	*8.4*	*8.1*

[1] Include general public services (general public administration, external affairs and public order and safety), defence, health, education and others.
[2] Include imputed rent from owner-occupied dwellings; and community, social and personal services, product of private non-profit services to households and domestic services of household.
p Preliminary

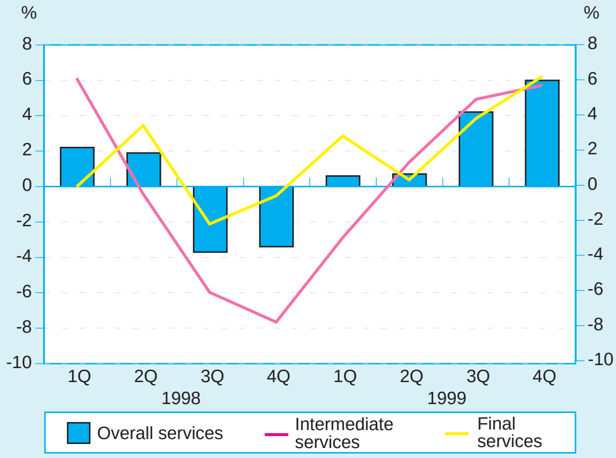
Source: Department of Statistics.

freight weight tonnes (1998: –12.8%), while container throughput surged strongly by 31.7% to a record high of 3.84 million twenty-foot equivalent units (TEUs) in 1999. To meet the increase in container volume, several ports embarked on expansion plans to augment their facilities and services. Westport, for example, began work on the construction of a new 600-metre terminal which would increase the capacity to 1.8 million TEUs annually. Meanwhile, the Kuantan Port Consortium (KPC) has started the construction of 12 new berths to strengthen the port's position as the country's main gateway for the petrochemicals industry. The new berths are expected to raise the port's handling capacity by 9 million tonnes in mixed cargo annually. In the south, the commencement of operations of the Port of Tanjung Pelepas (PTP) at the end of 1999 is expected to enhance port services, particularly in the southern region. The port is envisioned to become an ideal transhipment hub due to its strategic location at the confluence of major international shipping routes.

- In the case of **air transport**, the volume of cargo handled increased marginally by 1.7% in 1999. Growth was affected by diversion of part of the cargo to Singapore due to problems faced by MAS Cargo Advanced Centre since its relocation to KLIA. On the other hand, following the recovery of the Malaysian economy and the efforts taken by MAS to rationalise its flight routes, the number of passengers using the airline increased strongly by 9.1% to 14.8 million passengers. At the same time, MAS was also actively pursuing more code-sharing agreements as a means to increase flight frequencies, capacity and offer a better spread of services to passengers.

- In the **rail transport** segment, lower revenue from cargo and passenger services was recorded in 1999. Revenue declined in the first half-year before increasing in the subsequent half-year, in tandem with the strengthening pace of the economic recovery. The ridership of the Light Rail Transit (LRT) also increased substantially in 1999 due mainly to the opening of the extension route of the Projek Usahasama Transit Ringan Automatik (PUTRA) LRT from Pasar Seni to Gombak in June and the success of the promotion campaign to increase ridership through reduction in fares.

Graph 1.17
Services Sector: Quarterly Annual Growth



- The **communications** sub-sector also benefited from the recovery in domestic demand. The number of telephone (fixed line) subscribers grew by 1.1% in 1999, with increases in both commercial (1.8%) and residential (0.9%) subscribers. At the same time, the increased popularity of mobile phones, particularly the pre-paid service, contributed to a substantial increase in subscriber base.

Value added in the **finance, insurance, real estate and business services** sub-sector recovered to increase by 1.2% in 1999 (1998: –4.3%). The growth in value added of the sub-sector was due in part to improved profitability of financial institutions following measures to strengthen and restructure the banking sector. Meanwhile, the surge in trading activity and higher prices of shares in the Kuala Lumpur Stock Exchange as well as the increase in insurance premium income collections (5.7%) enhanced further the performance of the sub-sector, particularly in the second half-year.

In the **final services** group, comprising utilities; wholesale, retail trade, hotels and restaurants; government services and other services, value added increased by 3.3% in 1999 (1998: 0.1%). Growth emanated mainly from the Government services and utilities sub-sectors.

- Growth in the **Government services** sub-sector was higher at 6.6% in 1999 (1998: 1.8%). The increase reflected mainly higher emoluments arising from the bonus payment and reinstatement of allowances to civil servants as well as the increase in supplies and services provided by the Government.

- With the pick-up in economic activity, particularly in the manufacturing sector, value added in the **utilities** sub-sector expanded by 4.9% in 1999 (1998: 3%). The increase in electricity demand, particularly from the industrial and commercial sectors, led to higher production of electricity, as measured by the Electricity Production Index, which rose by 3.9%. During the year, water consumption increased by 1.5% to 8,754 million litres per day while production increased by 2.4% to 10,382 million litres per day.

- The **wholesale, retail, hotels and restaurants** sub-sector recorded an encouraging growth of 2.1% in 1999 (1998: –3.1%). Following a decline in the first half-year, value added in the sub-sector increased by 5.4% in the second half-year, on account of higher consumer spending and an increase in tourist arrivals. The gradual improvement in consumer confidence was reflected in the Malaysian Institute of Economic Research (MIER) Consumer Sentiments Index, which rose from 84 points in the first quarter of the year to 117.7 points in the fourth quarter. The improved consumer sentiment was mainly on account of the positive wealth effect of the rising equity market, favourable economic outlook and improved employment prospects. Meanwhile, the survey conducted by the Malaysian Retail Association (MRA) showed that retail sales increased by 1% in the first half-year and 6.8% in the third quarter of 1999 (1998: –20%). In the same survey, a stronger growth of 8.7% was expected in the fourth quarter of the year. Reflecting the improvement in the domestic trade sector, the collection of sales tax rose strongly by 16.7% (1998: -37.7%). In the tourism industry, the hosting of international events, in particular the Formula One Grand Prix Championship and the depreciation of ringgit from 1997 onwards had resulted in a significant increase in tourist arrivals, contributing to the favourable performance of the hotels and restaurants sub-sector. During the year, the average hotel occupancy rate rose to 53.4% from 49.9% in 1998.

  The improvement in the wholesale and retail trade sector is corroborated by the results of Bank Negara Malaysia's Annual Survey of the Wholesale and Retail Sector, 1999 which showed a marked increase in sales performance. Sales revenue of the retail sector rose strongly by 10.9% in 1999 (1998: –5.4%) while that of the wholesale sector increased by 1.3% (1998: –4.5%). In the departmental store sub-sector, sales revenue increased by 20.9% in 1999. For the wholesale and retail sector as a whole, sales revenue was higher by 6.6% in 1999 (1998: –5%).

Domestic Demand Conditions

The impact of policy measures to restore consumer and investor confidence was felt in 1999 when domestic demand conditions improved significantly. Growth in real aggregate domestic demand (excluding stocks) turned positive since the third quarter of 1999 due mainly to higher public sector expenditure and revival in private sector consumption. Private investment, however, moderated further in 1999 owing to excess capacity in selected industries. Overall, aggregate domestic demand (excluding stocks) registered a positive growth rate of 1.2% in nominal terms and 1.6% in real terms, a significant turnaround from the decline of 20.3% in nominal terms and 25.2% in real terms recorded in 1998.

Total consumption expenditure increased by 8.4% in nominal terms in 1999, compared with a decline of 7.4% in 1998. In real terms, total consumption spending, which accounted for 68% of total demand, improved by 6.1% (1998: –10.2%). **Public consumption** expenditure, with a share of 23% of total consumption spending, increased significantly by 20% in nominal terms and 20.1% in real terms during the year. While all components of Federal Government consumption expenditure increased, the most pronounced increase was in expenditure on emoluments.

Graph 1.18
Domestic Demand Aggregates

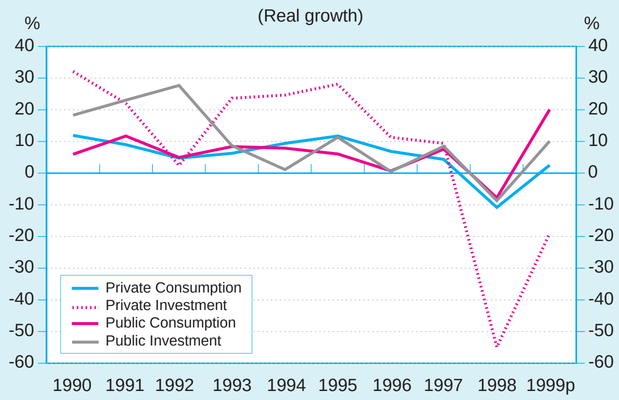


Table 1.11
Quarterly Aggregate Domestic Demand Components at Current and Constant (1987=100) Prices

	1998	1999				
		Q1	Q2	Q3	Q4	Year
	% annual change					
Constant Prices						
Aggregate Domestic Demand (excl. stocks)	–25.2	–9.3	0.2	8.9	7.3	1.6
Total Consumption	–10.2	1.0	6.7	8.1	8.4	6.1
Private Consumption	*–10.8*	*–4.3*	*2.8*	*4.6*	*7.6*	*2.5*
Public Consumption	*–7.8*	*36.0*	*20.8*	*20.2*	*11.0*	*20.1*
Gross Fixed Capital Formation	–42.9	–25.3	–11.2	10.7	5.2	–6.8
Current Prices						
Aggregate Domestic Demand (excl. stocks)	–20.3	–9.2	–0.5	6.2	8.8	1.2
Total Consumption	–7.4	4.7	8.8	8.9	10.9	8.4
Private Consumption	*–7.5*	*–0.4*	*5.6*	*6.5*	*10.8*	*5.6*
Public Consumption	*–7.3*	*37.9*	*21.0*	*18.0*	*10.9*	*20.0*
Gross Fixed Capital Formation	–37.2	–31.3	–17.6	0.2	4.4	–12.7

Private consumption expenditure turned around to record a positive growth of 5.6% in nominal terms and 2.5% in real terms for 1999 (–7.5% and –10.8% respectively in 1998). This reflected the improvement in consumer confidence and consumer spending in an environment of low interest rates and rising wealth following the bullish trend in the stock market and the favourable performance of the export sector. In 1999, the KLSE Composite Index closed the year at 812.3 points, an increase of 38.6%, while export earnings rose by 12.1%. Several major consumption indicators pointed towards an improvement in consumer spending. Sales of passenger cars increased by 79.9% in 1999 to 255,878 units. Imports of consumption goods rose at an annual rate of 21.3% to RM15.5 billion or US$4.1 billion. Improved consumer spending was also indicated by the increases in loans disbursed for consumption credit and general commerce (RM17.1 billion and RM57.7 billion respectively in 1999, from RM11.7 billion and RM35.9 billion respectively recorded in 1998).

Higher budget allocation for development projects by the Government, speedier disbursement of funds and signs of recovery in private investment expenditure in the second half-year led to a slower rate of decline in **gross fixed capital formation**. In 1999, gross fixed capital formation declined at a slower rate of 12.7% in nominal terms and 6.8% in real terms (1998: –37.2% in nominal terms and –42.9% in real terms). With stronger public sector investment activities and a modest recovery in private investment activity especially in the second half-year, gross fixed capital formation posted the first positive growth of 0.2% in nominal terms and 10.7% in real terms in the third quarter of 1999.

Public investment expenditure increased by 3.1% in nominal terms and 10.1% in real terms in 1999. Under the fiscal stimulus programme, allocation for socio-economic projects and selected infrastructure projects were increased. In particular, projects selected were those with greater spill-over effects on the domestic economy and minimal import content. Infrastructure projects funded by the Government included rail, roads, bridges, highways and public utility projects. Capital outlays on the social services sector which accounted for 31% of total development expenditure expanded by 19.9% in 1999. Reflecting the Government's policy of making Malaysia a regional centre of excellence in education as well as promoting a highly skilled labour force to support the strategy of high-technology and productivity-driven growth, allocation for education and training was substantially higher. While several NFPEs increased their capital spending for capacity expansion, particularly PETRONAS and Putrajaya Holdings, other NFPEs particularly Tenaga Nasional Berhad (TNB) and Telekom Malaysia Berhad (Telekom) consolidated their activities to increase the efficiency of their operations. As a result, total investment activities of NFPEs slowed down in 1999. Capacity expansion projects by PETRONAS included the development of several petrochemical complexes in Kertih and Gebeng, central utility facility in Gebeng, and construction of Kuantan Port-Kertih railway link. To provide for the development of the administrative centre in Putrajaya, capital investment by Putrajaya Holdings was also sustained in 1999. Capital expenditure by TNB focused mainly on transmission and distribution projects to ensure reliable and quality supply for its industrial and domestic users. The provision for the construction of the RM2 billion Janamanjung coal-fired plant in Perak accounted for a large part of TNB's capital expenditure in 1999.

Other projects comprised the development of Phase III of the Port Klang Sultan Salahuddin Abdul Aziz Power Station in Kapar and Phase II of the Tenaga Nasional University Complex. Meanwhile, major projects undertaken by Telekom included the development and expansion of the telecommunication network infrastructure, especially to support the development of the Multimedia Super Corridor (MSC).

Latest estimates showed that **private investment** declined at a slower rate of –24.1% in nominal terms and –19% in real terms in 1999 (–50.5% and –55% respectively in 1998) due mainly to the pick-up in activity in the second half-year, following the improvement in consumer and investor sentiment. This trend was also reflected in several indicators of investment activity. Imports of capital goods in US dollar terms, which declined by 40.5% in 1998 and 25.1% in the first half of 1999, turned around to record an increase of 16.7% in the second half of 1999. Sales of commercial vehicles (including 4WD) recovered to 32,669 units or a strong growth of 50.8%, as against a sharp decline of –76.1% in 1998. Loans disbursed by the banking system to the construction and manufacturing sectors were also higher at RM25.6 billion and RM85 billion respectively in 1999, compared with RM21.4 billion and RM68.7 billion in 1998.

The revival of private investment activities differed across sectors. In general, the services, manufacturing and construction sectors continued to experience further consolidation while investment activities were stronger in the agriculture and mining sectors. The 49.3% decline in investment in the services sector reflected mainly lower capital investment in the utilities and finance, insurance and business sub-sectors. The slower rate of investment in the utilities sub-sector was on account of completion of power plant projects by independent power producers. With the completion of LRT II, investment activity in the transport sub-sector was supported mainly by the resumption of construction of the People-Mover Rapid Transit System (Monorail) and Express Rail Link projects. Meanwhile, the property overhang in the supply of office space, hotels and retail space continued to be a drag on the economy, resulting in a substantial reduction in investment in the business sub-sector. Following the continued consolidation of investment activities in the services sector, its share of total private investment declined to 21.1% in 1999 (1998: 31.7%).

Table 1.12
Private Investment by Sector[1]

	1997	1998	1999
	RM billion		
Private investment	89.6	44.3	33.6
Of which:	% share		
Manufacturing	25.7	35.5	36.9
Construction	9.4	15.8	18.9
Services	34.0	31.7	21.1

[1] Estimates

Capital outlay in the construction sector also experienced further adjustment in 1999 due mainly to the deferment and delay in implementation of several privatised road projects as well as commercial buildings. The investment activity in this sector in 1999 was mainly supported by construction activity of low- and medium-cost houses and infrastructure development. The ongoing road projects in 1999 were concentrated in the Klang Valley, such as SPRINT Highway and Elevated Highway. Hence, investment in this sector declined by 9% to account for a share of 18.9% of total private sector investment.

In the manufacturing sector, investment activities were affected by the excess capacity situation faced by selected industries, mainly in the construction-related materials and transport equipment industries. Investment in the manufacturing sector declined by 21% in 1999 (1998: –31.7%). The decline was mainly due to further consolidation in the domestic-oriented industries. Export-oriented industries, particularly the electrical and electronic sector, benefited from the continued strengthening of global demand for electronics and electrical products as well as the stronger expansion of regional trade. New investment activities in the manufacturing sector were mainly sustained by ongoing petrochemical projects approved in 1998 as well as new electrical and electronic projects approved in 1999. Total value of investment approved for electrical and electronic projects exceeded RM7 billion in 1999.

The value of investment approved by the Ministry of International Trade and Industry (MITI) declined to RM16.9 billion in 1999, compared with RM26.4 billion in 1998. Of the total investment approved, four large projects, each with proposed investment exceeding RM1 billion, accounted for approximately 35% of the total investment approved. The electrical and electronic products industry accounted for the largest share of 41.4% of the total value of

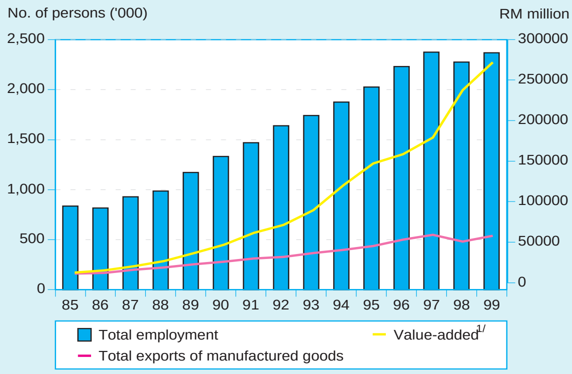
Box II

The Manufacturing Sector in the K-economy - Challenges and Strategies

Introduction

Since Independence, the manufacturing sector has played a progressive role in the economic growth of the country. By 1988, it became the most important source of growth when its share of GDP rose to 21.1%, surpassing for the first time, the traditional mainstay, agriculture. Since then, the sector has been expanding rapidly. During the period 1988-97, both value added and exports of the manufacturing sector grew strongly by 13.9% and 24.3% per year, respectively. Growth, however, was interrupted in 1998 when it contracted by 13.7% before recovering to expand by 13.5% in 1999, with its share of GDP at 30%.

Graph II.1
Trends in the Manufacturing Sector (1985-99)



1/ Value added is based on contribution to real GDP
Source: Department of Statistics
Economic Planning Unit
Bank Negara Malaysia

To a large extent, the impressive growth of the manufacturing sector is attributable to the implementation of deliberate policy measures aimed at achieving an industrialised nation status by the year 2020. Malaysia's industrialisation drive was marked by three distinct phases comprising import substitution (1958-68), selective export-led industrialisation (1969-80) and broad-based export-led industrialisation (1981 onwards). The policy initiatives taken have not only generated employment, expanded exports and further enhanced the value of products, but contributed significantly to the nation's well-being (see Graph II.1 and Chart II.1). An empirical study using the Cobb-Douglas production function in a cointegration model to measure the impact of manufactured and primary exports on GNP per capita for the period 1960-97 suggests that a structural change took place in 1986[1]. The long-run elasticity findings showed that a 1% increase in total primary exports induced a 0.2% increase in GNP per capita during the period 1960-85, but only 0.02% in 1986-97. On the other hand, the long run elasticity of manufactured exports showed that a 1% increase in total manufactured exports resulted in an increase of 1.1% in GNP per capita in 1986-97, significantly higher than the magnitude of 0.2% for the earlier period, 1960-85.

Given the strong positive correlation between the industrialisation process and income per capita, the manufacturing sector needs to be equipped to increase its ability to face the changes that are rapidly shaping the emergence of a new global economic framework. This article, as such, is aimed at identifying the challenges to the manufacturing sector and discussing the strategies to further strengthen the sector.

New Industrialisation Challenges and Strategies

The global landscape for industrial development is fast changing. For a long time, development was viewed as the accretion of both physical

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[1] A predictive failure test was used to test for structural changes. Due to its statistical insignificance, the short-run elasticity of manufactured exports was deleted during the testing-down process. Ceteris paribus, primary exports, in the short-run, though positive in sign, had become insignificant during 1986-97 from a strongly significant position in the earlier period (magnitude of 0.3%).

Chart II.1: Industrial Development and Major Policy Initiatives, 1958-99

Industrialisation Phases	Key Enablers	Annual Growth of Manufactured Exports (RM)
Phase III: 1981-99 Broad-based export-led industrialisation: • Start of promotion of heavy industries: 1981 • Liberalised export-led industrialisation: 1987 onwards	Formation of HICOM (1981) Promotion of Investments Act, 1986 - Active promotion of direct foreign investment *Industrial Master Plan, 1986-95* Liberalisation and deregulation measures - Privatisation - Reinforcement of tax concessions Action Plan for Industrial Technology Development, 1990 Industrial Master Plan II, 1996-2005	**21.9%**
Phase II: 1969-80 *Selective export-led industrialisation*	Investment Incentives Act, 1968 - Export-related incentives - Establishment of free trade zones (FTZs) New Economic Policy, 1970 Industrial Coordination Act, 1975	**17.4%**
Phase I: 1958-68 Import substitution (Domestic market orientation)	Pioneer Industries Ordinance, 1958 - Introduction of 'Pioneer Status' Tariff Advisory Board, 1958 - Promotion of infant industries via tariff protection	**3.7%**

and human capital. Currently, however, there is growing awareness that successful development should not only entail these factors, but also include the closing of the knowledge gap. A new economy in which knowledge is pervasively recognised as a vital source of economic growth, determinant of wealth and basis of competitive advantage is rapidly developing. Thus, the transition from a production-based economy (P-economy) to a knowledge-based economy (K-economy) implies that manufacturers will be faced with a new set of challenges and success is dependent on their ability to leverage knowledge in the best possible way. These key challenges and strategies are as follows:

(i) Advancements in Information and Communications Technology (ICT)

The world is on the verge of the connected society. Essentially, a new global culture and economy of businesses and individuals connected in a high-speed communications fabric that enables digital transmission of data, voice and video to anyone, anywhere, anytime has surfaced. As such, every business today has to compete in two worlds: a physical world of resources and a virtual world made of information. The latter has given rise to the world of electronic commerce, a new locus of value creation.

Those who understand how to master both can create and extract value in the most efficient and effective manner.

The advancing view, supported by the virtual organisation concept, is ‘agile manufacturing’, where a company is able to respond quickly to changing circumstances. This requires highly integrated systems between companies to create a fast, flexible, seamless electronic assembly line. In sum, the implications of the virtual value chain for manufacturers are as follows:

- Unlike physical assets, digital assets are not used up in their consumption. As such, manufacturers that create value with digital assets may be able to reharvest them through a potentially infinite number of transactions, thus changing the competitive dynamics of their industries;

- The virtual value chain redefines economies of scale, allowing small companies to achieve low unit costs for products and services in markets dominated by big companies;

- Businesses can redefine scope of operations by drawing on a single set of digital assets to provide value across many different and disparate markets;

- Transaction costs along the virtual value chain are lower than on the physical value chain, hence, allowing companies to control and track information that would have been too costly to capture and process before.

The biggest change in the age of he connected society will be the enhanced driving force of the consumer, so that expansion of the manufacturing sector increasingly demands a ***shift from supply-side to demand-side strategies*** in order to continuously influence consumer tastes and demands.

Given these developments, Malaysian companies need to urgently take steps to enhance their ICT-based competitive edge in order to take advantage of the opportunities of the connected society. A survey conducted by the Malaysian External Trade Development Corporation (MATRADE) in April 1999 revealed that 68.9% of the companies registered with MATRADE have e-mail facilities and 65.8% have Internet connections. However, only 38.3% have websites or homepage applications and 24.3% have on-line product catalogues whilst only 4.1% indicated that they have strategies to participate in e-commerce. In addition, the Asian Executives Poll of the Far Eastern Economic Review and CNBC Asia (February 2000) which targeted top company executives, showed that only 41.2% of Malaysian executives planned to expand their e-commerce activities, the lowest proportion amongst the 10 Asian countries surveyed (in order of ranking, Philippines, Hong Kong SAR, Taiwan, Australia, Japan, Indonesia, Singapore, Thailand, South Korea and Malaysia). Larger companies that are already shifting critical functions to the Internet would expect others who support their operations, such as, vendors and suppliers to also go on board to be electronically linked. As the number of small- and medium-scale enterprises (SMEs) in Malaysia which serve the larger companies as supporting and ancillary service and product providers begins to increase, there is the urgent need for them to adopt the new electronic medium to expand their electronic operations from purely administrative and inventory keeping to actual day-to-day transactions. Given that the SMEs represent more than 90% of the total manufacturing establishments, it is clear that this sector should not be left behind in the shift to e-business. As of January 2000, only 311 of total domestic SMEs have participated and undertaken on-line business. In a global environment of increased competition, failure on the part of Malaysian manufacturers to create value through the virtual value chain will prove costly in terms of lost opportunities.

The Government has provided a number of incentives to encourage IT-related companies to develop their businesses and to spur a higher usage of computer and technology assets. The Multimedia Super Corridor (MSC) which was established in 1996 to provide a high-powered gateway to the latest multimedia and information technology is also aimed at enhancing manufacturing operations in the areas of design, market intelligence, procurement and production control. Within the Electronic Government flagship of the MSC, a world-class electronic procurement infrastructure is being developed in which the Government will play the role of a single buying entity that will procure products and services electronically from about 30,000 suppliers in the country. In educating the SMEs, the Malaysian Electronic Trading Business Environment (MyBiz) Programme, which was introduced in March 1999 by the Small and Medium Industries Development Corporation (SMIDEC) in collaboration with Hitechniaga Sdn. Bhd., is aimed at enhancing awareness among the business community on the opportunities and benefits of conducting business electronically. The Government will continue to provide the necessary conducive environment for the development of e-commerce with the drawing up of a Malaysian Framework for E-Commerce. The framework will lay down a set of guiding principles and policies leading to the development of a National Masterplan for E-Commerce. Manufacturers, on the other hand, need to begin building the capacity to understand the Internet ecosystem and its manifestations.

(ii) Increased competition and globalisation

As market opening by individual countries continues to be the norm, market borders will increasingly become more porous and technically non-existent. In terms of intra-regional trade, the ASEAN Free Trade Area (AFTA) provides a large potential market of 530 million people with an estimated combined GDP of US$838 billion. On 1 January 2000, duties on 89.7% of the products included in the Common Effective Preferential Tariff Scheme for the six original ASEAN members were lowered to between 0-5%. The ASEAN countries have also agreed to eliminate duties on at least 60% of the products by 1 January 2003. The 1999 BNM's Survey of Manufacturing Companies (SMC)[2] indicated that for the year 2000, only 21.5% of the companies anticipated to increase their export market share resulting from the regional tariff liberalisation. The survey also showed that only 28.8% expected to see product price competitiveness. This implies that Malaysian manufacturers would have to step up their production efficiencies in order to fully gain from the benefits of AFTA.

Increased globalisation implies that the domestic industry and trade entities must be able to compete successfully in the Malaysian market with all foreign competitors, while those exporting abroad must be able to meet the challenges in every export market and compete successfully with others that are also in those markets. Those who fail to adjust risk being marginalised or even eliminated in both domestic and export markets. To enhance the competitive advantage of Malaysian manufacturers, the following needs to be considered:

- ***Higher increase of value added/ downstream activities***

  This includes the following four areas:

  Redefining the value chain: Based on BNM's SMC, the value-added content of the manufacturing sector increased from 32.9% in 1998 to 34.2% in 1999, indicating an increase in downstream activities. The survey, however, showed that the electronics and electrical products industries have relatively lower value-added content due to higher concentration on assembly-type activities and less linkages with domestic suppliers. In contrast, the rubber-, wood- and palm oil-based industries registered relatively higher value-added content. In the K-economy, manufacturers would have to look at the value chain from the position of demand by the customer, examining all the activities the customer performs in using and maintaining a product through its life cycle, from sale to disposal. In the car industry, the traditional manufacturer's view of the value chain is relatively compact: assembling the car,

[2] The results were based on the response from 163 manufacturers. These are preliminary results only.

selling and delivering it and supplying spare parts and upgrades. From the customer's perspective, however, the downstream chain is more complex. It includes financing and leasing, maintenance, servicing, refurbishment and resale.

Innovating value: A five-year study of more than 30 companies around the world in about 30 industries that was conducted by the Harvard Business School (Harvard Business Review, 1998) highlighted a distinct difference in the approach adopted by high growth companies and their less successful competitors in achieving sustained high growth in both revenues and profits. Whilst the approach of less successful companies was dominated by strategies to stay ahead of the competition, the high-growth companies paid little attention to matching or beating their rivals. Instead, high-growth companies sought to make their competitors irrelevant through the strategic approach of value innovation by offering fundamentally new and superior buyer value in existing markets and by enabling a leap in buyer value to create new markets. Essentially, the value innovator does not follow its rivals in offering similar product features, but rather distinguishes factors that engender superior value from all the factors that the industry normally competes on.

The increased brand recognition that comes with value innovation makes imitation costly as the value innovator lowers cost to take advantage of economies of scale. Hence, with value innovation, the focus shifts from restricting output at a high price to a leap in consumer surplus as well as profit and growth for the value innovator. In contrast, in the P-economy, firms with dominant market positions have been associated with two social welfare loss activities. First, to maximise their profits, companies set high prices, which prohibit the mass of customers who, though desiring the product, could not afford it. Second, lacking viable competition, firms with monopolistic positions do not focus on efficiency and hence consume more of society's resources.

Building customer allegiance: In the K-economy, the goal of a manufacturer should not necessarily be to gain the largest share of customers but to gain the strongest relationships with certain target customers. With this, a manufacturer can become the preferred supplier of services throughout the product life span.

Building a customer-based marketing network: As value shifts towards the customer in the K-economy, distribution would become a mainstream activity in the value chain, forcing manufacturers to change from product-based marketing to customer-based marketing. In response to growing competition, businesses are increasingly looking overseas for new opportunities, a trend made easier by the Internet. This in turn brings them into contact with new suppliers, or can bring them new customers. Besides concentrating on the traditional markets, the challenge to Malaysian manufacturers would be to explore the potential of new export markets. In addition, manufacturers should continuously assess the shifts in customers' preferences, as well as new demands. Successful manufacturers will increasingly be characterised by a hands-on involvement with marketing and a focus on identifying and exploiting new products and new channels. According to the BNM's SMC, expenditure on marketing/advertising by Malaysian manufacturers accounted for only 6.1% of their total expenditure in 1999.

- ***Stronger focus on high technology levels***

Further industrial expansion of Malaysia requires expansion in the scientific and technological infrastructure in the manufacturing industries. The transfer of technology from the multinational corporations has been limited and is confined mainly to assembly-line processes. In fostering K-based transformation, focus needs to be placed on absorbing higher levels of technologies.

The impact of these technologies is on long-term cost reductions with simultaneous efficiency and productivity enhancements, and the consequent upgrading of the quality of the industry itself having the trickle-down and spin-off effects on consumers and related industries.

The BNM's SMC showed that only 7.4% of our manufacturers were involved in experimental research. Meanwhile, although 30.7% of respondents were affirmative about undertaking research and development, such expenditure accounted for only about 1.4% of their total expenditure in 1999. A majority of industries were found to be at the low/medium levels of technology, with 62.6% involved in technological support and engineering services, 54.6% in the implementation or installation of new equipment and 45.4% in product innovation or process and prototype development.

Bold steps are being taken to encourage modernisation of the production process of existing industrial units, and the establishment of new industrial units based on the latest technologies. The Government has established a number of funds to provide financing for the acquisition of technology (e.g., Technology Acquisition Fund and Industrial Technical Assistance Fund). In the Budget 2000, the Government also allocated a sum of RM25.2 million for programmes promoting science and technology to encourage the use of new technology and upgrade of innovative capabilities, inventions and commercialisation home grown technology. Furthermore, special allocations were provided to several resource-based agencies to undertake specific research and a RM500 million special fund was announced to support the development of new high technology-based industries. In encouraging companies to undertake high-tech projects that entail high risk, the Budget 2000 announced a full tax exemption incentive for venture capital companies that invest at least 70% of their funds in venture companies in the form of seed capital, start-up or early stage financing (see Table II.1 for the size of selected venture capital funds).

Table II.1: Size of Selected Venture Capital Funds (as at end-1999)

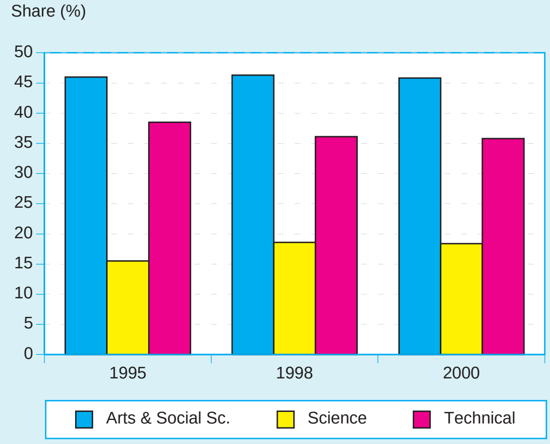
Venture Capital Company / Venture Capital Fund	Amount (RM million)
BNM and two banking institutions (announced in Budget 2000)	300
Government through Bank Industri & Teknologi Malaysia Bhd. (announced in Budget 2000)	200
MSC Venture One Sdn. Bhd.	120

- ***Stronger focus on human resource development***

In the long run, the single greatest K-economy enabler is human capital. Essentially, the K-economy will require a trained labour force that has the capacity and capabilities to optimise the use of new technologies and materials, and to combine them effectively with creativity and innovation. There is, therefore, a need for greater emphasis on creativity and higher order cognitive skills in addition to basic skills, and training in science and technology. In addition, it would be important to meet the training needs of designers and craftsmen who can, in the long-term, create a strong culture of innovation and quality manufacturing. For example, given that the furniture industry is only a step away from producing originally designed pieces, the development of a skilled pool of designers would certainly enable the industry to make greater strides in the export market.

An area of focus is the skilled manpower required to move up the value chain. In 1999, a total of 708 manufacturing projects with total investments of RM16.9 billion were approved by the Government. Of the 65,261 persons that these projects will require, the majority (42%) will comprise skilled workers. While local and tertiary education institutions in Malaysia have expanded to meet the increase in

Graph II.2
Total Intake at Local Institutions of Higher Learning*



* Includes degrees, diplomas, certificates and skills training

Source: Mid-Term Review of the Seventh Malaysia Plan

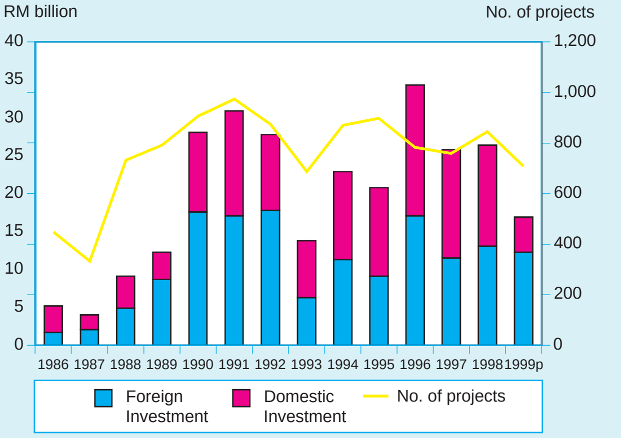
domestic demand and to promote education as an export industry, the general trend continues to favour training in Arts and Social Sciences (see Graph II.2). A World Bank study (1997) highlighted that 80% of firms in Malaysia either did not train or relied exclusively on informal training from co-workers and supervisors, and only 20% provided formal training. Results also showed that formal training improved firm-level productivity. On average, the firms that provided training were 32% more productive than those that did not do so. These firms were also able to pay higher wages out of increased productivity from training. More importantly, the study highlighted that SMEs, which is the group that would most likely benefit from training were under-investing in training.

In order to meet the challenge of producing a skilled labour force, a review of the education policy needs to be undertaken on an ongoing basis. Education needs to continuously raise the general technical competency and increase the 'trainability' of workers for lifelong learning, whilst developing creativity and strategic thinking. Also, core training institutions need to be enhanced to cope with demand for more engineers, technical personnel and technological processes. Training sessions for SMEs, in particular, need to be adapted according to their special needs. SMEs must be required to continuously train and retrain their manpower resources for a wide spectrum of administrative and managerial positions, acquire the entrepreneurial know-how, and also acquire the relevant knowledge and capacity to operate information technology as well as the specialised equipment for their respective industries.

Conclusion

In the K-economy, the manufacturing sector will continue to assume an important role. Nonetheless, in order to operate successfully, manufacturers must be able to adjust to the rapid pace of change. Towards this end, it is important that knowledge is diffused throughout all levels of the firm's value chain. In this era of change, a strong commitment towards the enhancement of knowledge in all aspects of economic activity is needed to achieve a fourth phase of industrial development, namely 'knowledge-based export-led industrialisation' to enable the realisation of industrialised nation status by 2020.

Graph 1.19
Malaysia: Investment Approvals



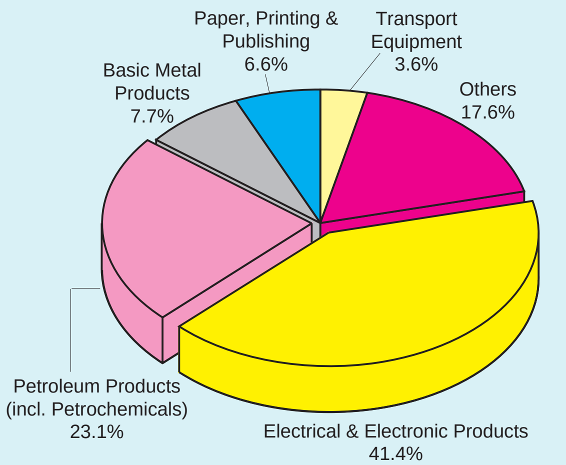
investment approved, followed by petroleum products (including petrochemicals) industry (23.1%), basic metal products (7.7%), paper, printing and publishing (6.6%) and transport equipment (3.6%) industries.

In terms of ownership, approved domestic investment declined to RM4.6 billion (1998: RM13.3 billion) reflecting the ongoing consolidation in domestic investment activities. Meanwhile, foreign investment amounted to RM12.3 billion (1998: RM13.1 billion), reflecting sustained foreign interest in investing in Malaysia. The bulk of the approved investment were for projects in three industries, namely the electrical and electronic products (48.4%), petroleum and petrochemical products (25.7%), and paper, printing and publishing (8.7%) industries. The top five foreign investors in 1999 were the United States (42% of total foreign investment approved in 1999), Japan (8.2%), Pakistan (8%), Singapore (7.4%) and the Netherlands (6.3%). These countries together accounted for 72% of total foreign investment approved by MITI.

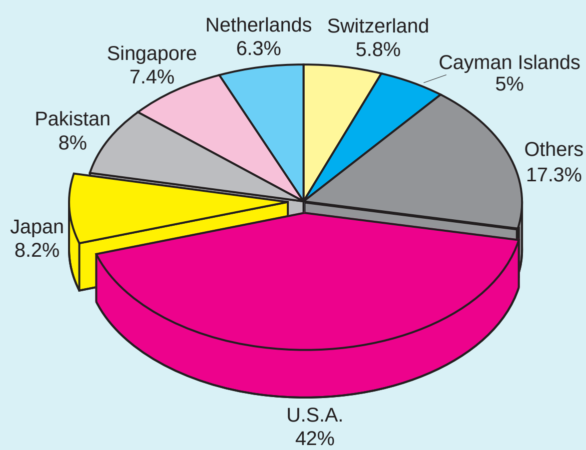
While the major sectors of the economy were still undergoing further consolidation, capital investment in the agriculture and mining sectors increased in 1999. Investment in the mining sector, which accounted for 11.2% of total private investment, increased by 44.2% due mainly to strong expansion in production facilities in the oil and gas sub-sector. The increase in replanted area, especially for oil palm plantations, had contributed to a marginal increase in investment in the agriculture sector in 1999 (10.2% of total investment).

In 1999, the savings-investment gap remained in surplus for the second consecutive year, recording a surplus of RM47.4 billion or 16.9% of GNP in 1999 (1998: RM36.8 billion or 13.7% of GNP). Private savings registered a marginal decline of 0.1% to RM68.6 billion as private consumption recovered in 1999. Nevertheless, the private sector continued to record a bigger resource surplus of RM34.8 billion, as private gross capital formation declined by 23.4% due to the ongoing consolidation of corporate sector activities. Despite higher operating expenditure, public savings increased by 3.8% to RM45.7 billion in 1999 (1998: –22%; RM44 billion), reflecting significantly improved revenue performance of the public sector. The public sector recorded a slightly higher surplus of RM12.6 billion. Overall, **gross national savings (GNS)** increased at a slower rate of 1.4% in 1999 (1998: 7.2% and

Graph 1.20
Approved Manufacturing Investment by Industry, 1999



Graph 1.21
Foreign Participation in Approved Manufacturing Projects by Country, 1999



1997: 11.8%). Consequently, the share of GNS to GNP declined to 40.8% in 1999, from 41.9% recorded in 1998. This rate of savings still remained high by historical standards and in comparison with other countries.

Recognising the need to balance between consumption and savings, the effort of the savings programme in 1999 continued to emphasise on the efficiency of managing household income and expenditure. To achieve this objective, the second edition of the Household Accounts Book for adults and a Pocket Money Book for students were produced in 1999. The main objective of the household accounts book is to encourage households to plan and efficiently manage their income and expenditure and at the same time practise prudent spending habits and avoid wastage. The objective of the students pocket money book is to introduce financial management of personal accounts at a young age and, therefore, introduce a greater awareness in society on financial matters at an early stage.

To strengthen the effort in achieving this objective, the School Finance Club Project was launched in November 1999 by the Minister of Education to establish finance clubs in schools nationwide with participation of the banking industry. To standardise, monitor, guide and streamline the activities of the school finance clubs, Guidebook was produced as part of this exercise. The objective is essentially to outline the relationship between the financial institutions and the schools and the mechanism for the financial institutions to educate the students on banking and financial matters as well as inculcating good expenditure and savings habits and sound management of their personal accounts at a young age. With these mechanisms in place, it is hoped that there will be greater awareness on financial discipline, efficiency and integrity as part of the process of securing a generation that is well informed on these issues in the future.

Table 1.13
Malaysia: Savings-Investment Gap, 1998-99

	1998	1999*p*
	RM million	
Public gross domestic capital formation	31,801	33,126
Public savings	44,027	45,714
Deficit/surplus	12,226	12,588
Private gross domestic capital formation	44,112	33,811
Private savings	68,683	68,604
Deficit/surplus	24,571	34,793
Gross domestic capital formation	75,913	66,937
(as % of GNP)	28.2	23.9
Gross national savings	112,710	114,318
(as % of GNP)	41.9	40.8
Balance on current account	36,797	47,381
(as % of GNP)	13.7	16.9

p Preliminary

Source: Department of Statistics and Bank Negara Malaysia

External Sector

Balance of Payments

The balance of payments position strengthened in 1999 with strong contribution of net exports to GDP and sustained private long-term net capital inflows. Despite the strong recovery in economic growth there was no significant leakage abroad as GDP growth in 1999 was supported by higher productivity and more efficient use of capital invested in previous years. In addition, the surplus in the overall balance of payments was large at RM17.8 billion despite larger outflows of short-term capital. This led to higher BNM external reserves of RM117.2 billion or US$30.9 billion. This level of reserves was sufficient to finance 5.9 months of retained imports and was more than five times larger than the short-term external debt. Malaysia has always ensured that its usable and unencumbered external reserves are adequate to finance the short-term external debt, including the scheduled amortisation of medium- and long-term debts falling due during the following year.

The current account emerged fundamentally stronger in 1999, reflecting an increase in the trade balance that emanated from a stronger export performance, given that imports had begun to increase to service higher export demand. This is in contrast to 1998, when the trade surplus reflected mainly a sharper contraction in imports. The import growth, however, was limited to some extent as the emphasis of the fiscal expansion programme was on projects with low import content. The strength of the external balance was also reflected in a current account surplus that

Table 1.14
Balance of Payments

Item	1999e +	1999e –	1999e Net
	RM million		
Merchandise balance (f.o.b.)	**315,719**	**232,184**	**83,534**
Trade account	*321,181*	*248,870*	*72,311*
Balance on services	**56,057**	**85,000**	**–28,943**
Freight & insurance	4,685	14,416	–9,731
Other transportation	7,258	4,778	2,479
Travel & education	13,326	7,758	5,568
Investment income	7,283	26,073	–18,790
Government transactions n.i.e.	338	385	–46
Other services	23,168	31,590	–8,422
Balance on goods and services	**371,776**	**317,185**	**54,591**
Unrequited transfers	2,732	9,943	–7,210
Balance on current account	**374,508**	**327,127**	**47,381**
% of GNP			**16.9**
Official long-term capital			6,692
Federal Government	4,763	1,840	2,923
Market loans	4,164	1,107	3,057
Project loans	599	733	–134
Non-financial public enterprises	6,080	2,230	3,850
Other assets and liabilities			–81
Private long-term capital			5,025
Balance on long-term capital			11,717
Basic balance			**59,098**
Private short-term capital (net)			–35,958
Errors and omissions			–5,321
Overall balance (surplus +/ deficit –)			**17,819**
Allocation of Special Drawing Rights			–
IMF resources			–
Net change in international reserves of Bank Negara Malaysia (increase – / decrease +)			–17,819
Special Drawing Rights			464
IMF reserve position			–789
Gold and foreign exchange			–17,494
Bank Negara Malaysia international reserves, net [1]			**117,244**

[1] The US dollar equivalent of international reserves as at 31 December 1999 was US$30.9 billion
e Estimate

Source : Bank Negara Malaysia and Department of Statistics

was more than adequate to finance the short-term capital outflows.

The slightly larger balance in the long-term capital account was due to higher inflows of official long-term capital including disbursements under the Miyazawa Initiative. Contrary to market expectations, net inflows of foreign direct investment was higher in 1999, but was partially offset by a significantly larger net outflow of Malaysian investments abroad. Therefore, the surplus balance on long-term capital increased only marginally although net foreign direct investment had increased by 26.8%. Outflows of Malaysian investments abroad doubled to RM6.2 billion from RM3.1 billion in 1998.

The larger outflows of short-term capital in 1999 was due mainly to the improved net external liabilities position of the commercial banks and trade credits to foreign suppliers. Portfolio outflows following the expiration of the 12-month holding period imposed on foreign funds on 1 September 1998 was less than expected. Overall, the large outflows of short-term capital were fully offset by other inflows.

In 1999, the **trade** surplus expanded further, totalling RM72.3 billion, exceeding the previous record of RM58.4 billion set in 1998. In US dollar terms, the surplus amounted to US$19 billion. Overall, the value of Malaysia's total trade increased by 10.8% to RM570 billion and accounted for 203% of GNP compared with 191% in 1998, in tandem with an improved global economic environment and the recovery in the global electronics industry as well as the rebound in domestic demand.

Gross exports (value of exports recorded by the Customs Department) in 1999 increased further by 12.1% to RM321.2 billion (US$84.5 billion). In US

Table 1.15
External Trade

	1998	1999	1998	1999
	RM billion		US$ billion	
Gross exports (f.o.b)	286.6	321.2	73.3	84.5
Annual change (%)	29.7	12.1	–6.9	15.3
Gross imports (c.i.f)	228.1	248.9	58.3	65.5
Annual change (%)	3.3	9.1	–26.2	12.3
Trade balance	**58.4**	**72.3**	**15.0**	**19.0**

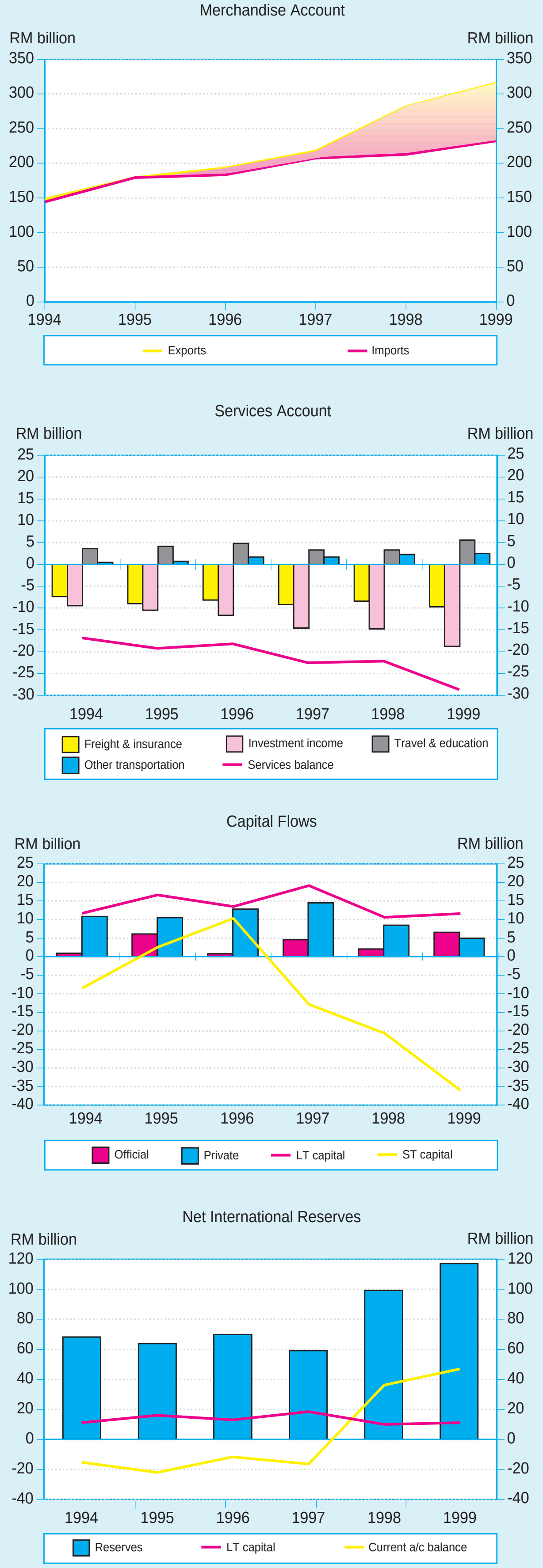
Source: Department of Statistics.

Table 1.16
External Trade: Change in Volume and Prices

	Gross exports	Gross imports	Gross exports	Gross imports
	1998		1999	
	Annual change (%)			
Volume[1]	1.1	–19.9	19.3	12.0
Prices (RM)[1]	30.7	28.9	–4.4	–2.6
Prices (US$)[1]	–6.2	–7.9	–2.7	0.3
Total (RM)	**29.7**	**3.3**	**12.1**	**9.1**

[1] The volume and price estimates for 1999 are preliminary estimates.
Source: Department of Statistics and Bank Negara Malaysia.

Graph 1.22
Malaysia: Balance of Payments

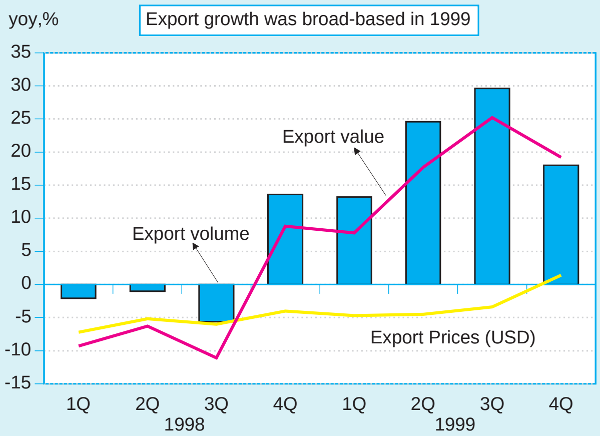


dollar terms, export growth recovered to 15.3% following a moderate decline in 1998. The increase in exports was on account of higher volume. Growth emanated mainly from the strong expansion in manufacturing and mineral exports, while agriculture exports declined. Import growth accelerated to 9.1% to reach RM248.9 billion (US$65.5 billion) in 1999. In US dollar terms, the turnaround in imports was stronger, an increase of 12.3% following a large decline in 1998. This was mostly due to an increase in volume as ringgit prices declined slightly. The decline in prices was marginal as ringgit stabilised. In 1998, the sharp increase in prices was mainly due to the depreciation of the ringgit. The increase in volume in 1999 was due mainly to an increase in demand from the manufacturing sector as a result of the strong export performance. However, the recovery in domestic demand, especially private consumption, and a modest pick-up in investment activities, following improved business and consumer confidence especially in the second half of the year also contributed to the higher import growth.

Reflecting the developments in the trade account, the **merchandise account** posted a record surplus of RM83.5 billion (US$22 billion) in 1999.

Increased demand from the industrial countries and the economic recovery in the region led to a strong rebound in exports of **manufactured goods** in 1999. Total exports of manufactured goods in US dollar terms turned around to register an annual growth of 17.6% to US$71.5 billion in 1999 (1998: –4.6%). In US dollar terms, exports of manufactured goods have exceeded export earnings recorded in the years before the regional crisis (1995-1996: average of US$60.9 billion per year). The higher export receipts were mainly on account of a strong pick-up in volume, while export prices measured in US dollar terms continued

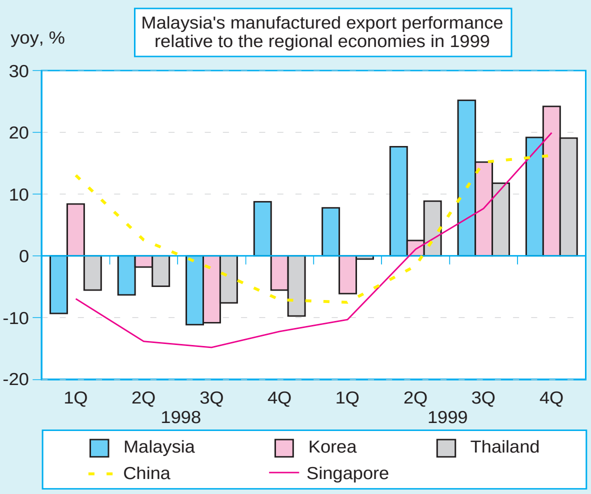
Graph 1.23
Export Performance of Manufactured Goods in 1999



to decline, albeit more moderately. As a result of the improvement in overseas sales, exports of manufactured goods accounted for a higher share of 84.6% of total gross exports in 1999 (1998: 82.9%). In ringgit terms, manufactured exports expanded at a slower rate of 14.3% to RM271.7 million compared with 32.8% in 1998, due to the valuation impact of the exchange rate (1998: US$1=RM3.92; 1999: US$1=RM3.80).

The stability and certainty accorded by the selective exchange controls and fixed exchange rate introduced in September 1998 had facilitated exporters in their costing plans and business operations, thus enabling the Malaysian exporters to retain their export markets. While the Government had implemented policies to provide a more conducive environment for doing business, the track record established by Malaysian

Graph 1.24
Export Performance of Selected Countries in the Region



exporters in the international markets in terms of product quality, design and range as well as reliable delivery had further strengthened the export recovery. Following a modest recovery in the fourth quarter of 1998, Malaysia's manufactured exports continued on an upward trend, similar to developments in Thailand and Korea, with growth accelerating from 12.8% in the first half of 1999 to 22% in the second half (1998: –7.8% and –1.5% respectively).

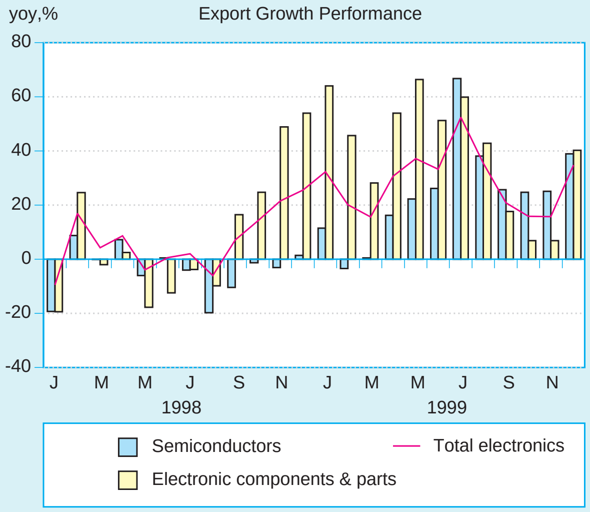
The recovery in export growth was broad-based. Although the electronics industry was a major contributing factor accounting for the growth, exports of the other industries in both the resource- and non-resource based sectors, particularly the electrical products, wood products, furniture and parts as well as chemical products industries also improved, thereby contributing favourably to the growth in manufactured exports.

- Exports of **electronic goods** expanded strongly by 30.4% in 1999 (1998: 1.9%), reflecting the upturn in the global electronics cycle. During the year, exports of both the **semiconductors and electronic equipment sub-sectors** recorded a strong expansion of 23.7% and 36.5% respectively (1998: –4.2% and 8.2% respectively), attributable largely to the more widespread usage of Internet, e-commerce and cellular phones. In addition, intensified efforts to deal with the Y2K problem also boosted demand for computers worldwide. During the year, the United States maintained its position as the largest market for Malaysia's electronic goods, followed by Singapore, Europe, the Asia-Pacific region and Japan.

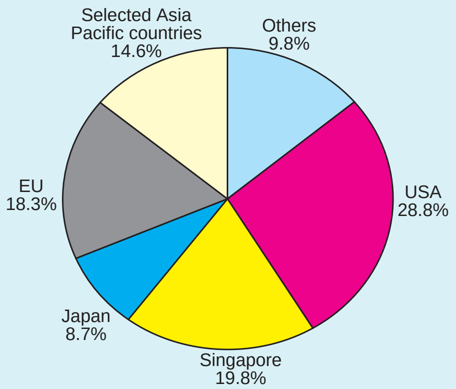
- Exports of the **electrical products industry** rebounded to increase by 8.8% in 1999 (1998: –11.4%), after declining since 1996. The reversal in trend was supported by higher exports to the United States and strengthened demand for consumer durables, air-conditioners and telecommunication products following the economic recovery of major markets in Asia, in particular Japan, Singapore and Hong Kong SAR. As a group, exports of the **electronics and electrical products industries** increased significantly by 24.1% in 1999 (1998: –2.4%), accounting for a higher share of 71.8% of total manufactured exports (1998: 68.1%).

- Following two consecutive years of decline, exports of the **wood products industry** recorded

Graph 1.25
Exports of the Electronics Industry

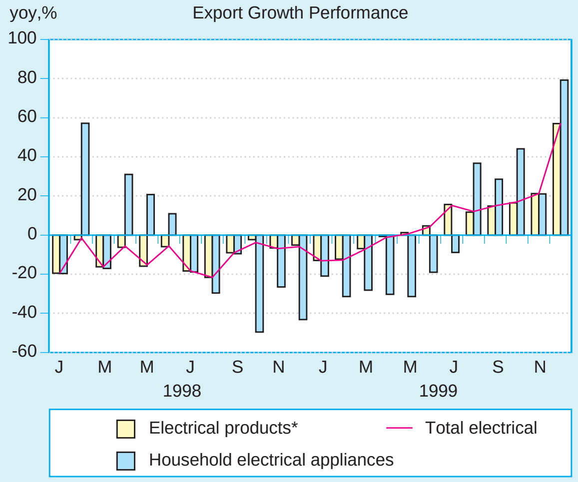


Market Destinations



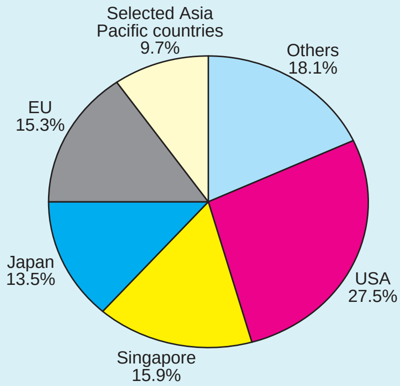
Note: Selected Asia Pacific countries refer to Hong Kong SAR, Taiwan, Korea and Australia

Graph 1.26
Exports of the Electrical Products Industry



* Electrical products refer to consumer electrical products, industrial and commercial electrical products and electrical industrial machinery and equipment

Market Destinations



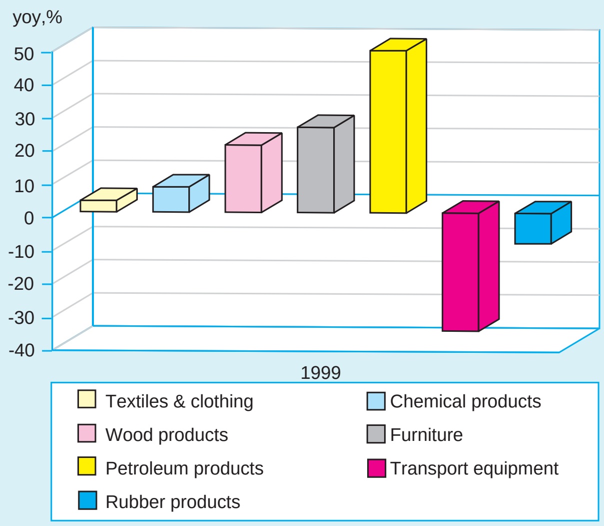
Note: Selected Asia Pacific countries refer to Hong Kong SAR, Taiwan, Korea and Australia.

a strong expansion of 20.3% in 1999 (1998: –34.3%). The recovery in exports was due mainly to the replenishment of plywood stocks in Japan (accounting for almost one-third of total exports of wood products) following the revival of housing starts and sustained demand from the United States and the Asia-Pacific region. In addition, improved export prices of plywood from US$259 per cubic metre in 1998 to US$311 per cubic metre in 1999 also contributed to higher export earnings. Similarly, the turnaround in exports of **furniture and parts** (25.7%; 1998: –7.2%) reflected increased orders from the United States and European Union, as well as the ability of manufacturers to export customized products to meet demand from niche markets in the Middle-Eastern countries.

- Exports of the **chemicals and chemical products** industry recovered to increase by 7.6% in 1999 (1998: –6.6%). The improvement in exports was most evident in the second half of the year due mainly to improved sales of resins and plastic products when the global oversupply situation eased. At the same time, higher exports of organic chemicals, fertilisers as well as perfume materials, essential oils and toiletries to the Asia-Pacific markets and the United States also boosted growth. During the year, the industry maintained its position as the second largest foreign exchange earner, accounting for 4.1% of total manufactured exports. Meanwhile, exports of **petroleum products** increased markedly by 48.9% (1998: –33.4%), reflecting higher crude oil prices and improved industrial demand for both refined and unrefined petroleum products mainly from the Asian countries, in particular, Singapore, Japan, The People's Republic of China and Korea.

- After two consecutive years of decline, exports of the **textiles, clothing and footwear industry**

Graph 1.27
Exports of Other Major Industries



turned around to grow by 3.4% in 1999 (1998: –11%), following increased orders for wearing apparel (accounted for more than half of the total exports of the industry) from the major traditional buyers in the United States and European Union. Since the second quarter of 1999, exports of textiles also picked up in response to higher demand from Taiwan, Hong Kong SAR, Singapore and The People's Republic of China. As export growth was constrained by increased competition from low-cost producers in the region, the industry remained the third largest export earner within the manufacturing sector, having lost its position as the second largest foreign exchange earner to the chemical products industry in 1997.

- On the other hand, exports of the **rubber products industry** declined by 9.1% in 1999 (1998: +3.9%), reflecting lower export earnings from the latex-based products and tyres sub-sectors. During the year, despite increased volume of gloves being exported to the United States and Europe, export earnings continued to decline as a result of persistent weak export prices amidst intense international competition. Meanwhile, the lower exports of tyres were due mainly to reduced overseas sales to cater for increased demand from the domestic automotive industry. Similarly, the **transport equipment industry** registered a contraction in exports (–35.5%; 1998: +17.1%), attributed mainly to lower re-exports of leased aircraft, ships and boats as well as railway vehicles.

- Exports of **iron and steel products** declined by 2.2% in 1999 (1998: +5%), reflecting intense competition among manufacturers in the region who were affected by excess capacity and the imposition of import quotas by the United States. On the other hand, exports of **non-metallic mineral products** rebounded to expand by 10% in 1999 (1998: –13.2%), on account of increased exports of mineral manufactures including ceramic products and tiles, particularly to the European markets. The higher export growth was also attributable to improved external demand for glassware, clay and refractory construction materials during the year.

- Exports of **food products** and **beverages** turned around to grow by 1.4% and 17.4% respectively in 1999 (1998: –10.3% and –11.4% respectively), as demand from the region, especially the ASEAN countries, Korea and Taiwan improved, in tandem with the recovery of these economies.

In terms of market destination, the United States, Singapore, Japan and Europe remained the major trading partners for Malaysia's manufactured goods, accounting for more than two-thirds of the total exports of manufactures. Nevertheless, Malaysian exporters have made considerable progress in penetrating the non-traditional markets in the Asia-Pacific region. The share of manufactured exports to Taiwan, Australia and The People's Republic of China increased from 2.2%, 1.3% and 0.7% respectively in 1991 to 4.7%, 2.2% and 2.1% respectively in 1999.

Besides market diversification, manufacturers have also expanded the range of products exported. The major export items comprised mainly electronics, electrical products, textiles and clothing, chemical products, rubber products, wood products, furniture and parts as well as metal products. However, in line with the momentum gained in globalisation and liberalisation, several industries, especially those which are labour-intensive and highly involved in the production of low- to medium-end products such as the electrical products, textiles and rubber products industries, have faced increased competition from low-cost producing and labour-abundant countries. As a result, the contribution of these industries as a group to the overall export earnings has been declining, from 36.8% of total manufactured exports in 1991 to 31.7% in 1996, before declining further to 23.9% in 1999.

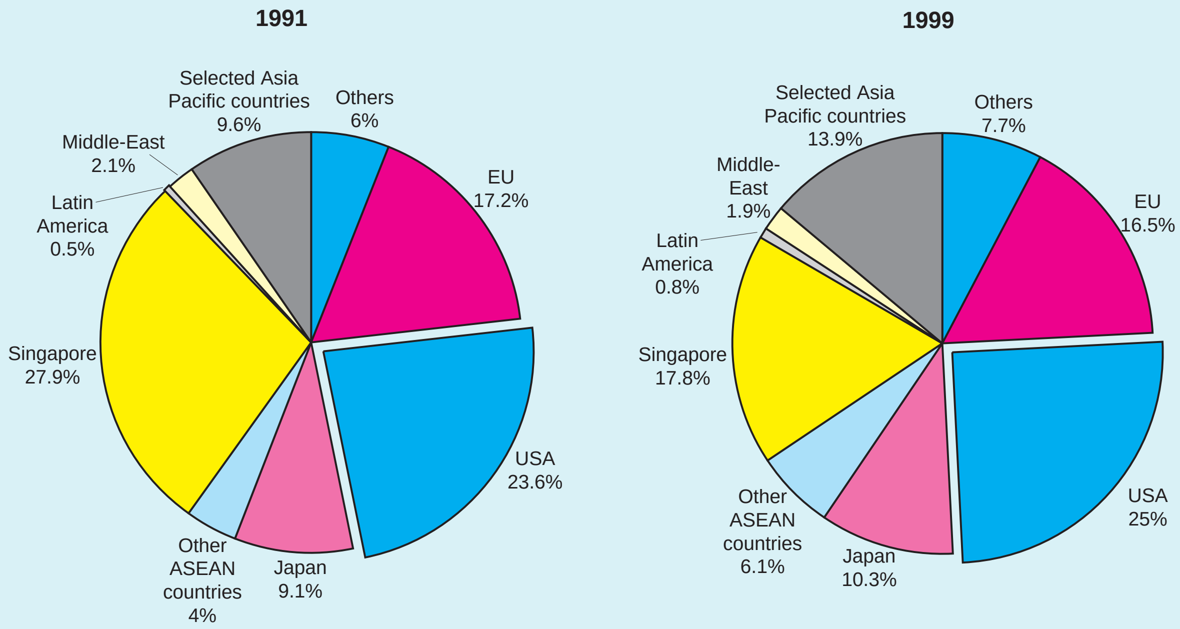
In line with the strategies for industrialisation, Malaysian manufacturers have continuously taken steps to move up the value chain. Several encouraging developments have already taken place in terms of increased exports of higher value-added goods and downstream products. Meanwhile, increased downstream activities in the resource-based sector saw the rapid increase in exports of furniture and parts. During the period 1991-99, exports of these products expanded by an average of 21% per annum, from US$268.7 million in 1991 to US$1.4 billion in 1999. At the same time, manufacturers have also demonstrated their ability to produce customized products to meet demand from niche markets such as the Middle-Eastern countries. To maintain competitiveness in the global market, manufacturers have also moved to producing higher value-added products such as digital video discs and video compact discs in the electrical products industry.

After five consecutive years of growth, export receipts from **commodities** declined by 0.4% to RM44.9 billion in 1999 (1998: +16.8% to RM45.1 billion), due mainly to lower export prices. In United States dollar terms, export earnings from the commodity sector increased by 2.8% to US$11.8 billion. Overall, foreign prices of exports declined by 1.7% as higher prices of crude oil, saw logs and sawn timber were more than offset by the sharp decline in palm oil prices. Export volumes of all major commodities increased, except for rubber and crude oil. As a group, export volume increased by 9.6%.

The contraction in export earnings from the **agriculture** sector in 1999 was due largely to lower proceeds from palm oil, and to a lesser extent, the decline in rubber exports. Nevertheless, exports of saw logs, sawn timber and cocoa turned around to record strong positive growth.

- Exports of **palm oil**, which was the single largest contributor to commodity exports, declined sharply by 18.6% on account of lower export prices. Hence, its contribution to total commodity exports was lower at 32.2% in 1999 (1998: 39.4%). During the year, the export unit value of palm oil fell markedly by 31.8% to RM1,615 per tonne amidst ample global supplies of vegetable oils. Despite the downtrend in prices, crude palm oil production rose substantially during the year, resulting in a corresponding increase in the export volume of palm oil by 19.3% to 9 million tonnes. The increase in exports was in response to higher demand particularly from India (+80.5%) and the European Union (+2%). Demand from India was particularly responsive to prices. Following lower prices, exports to India accounted for 27% of Malaysia's palm oil exports

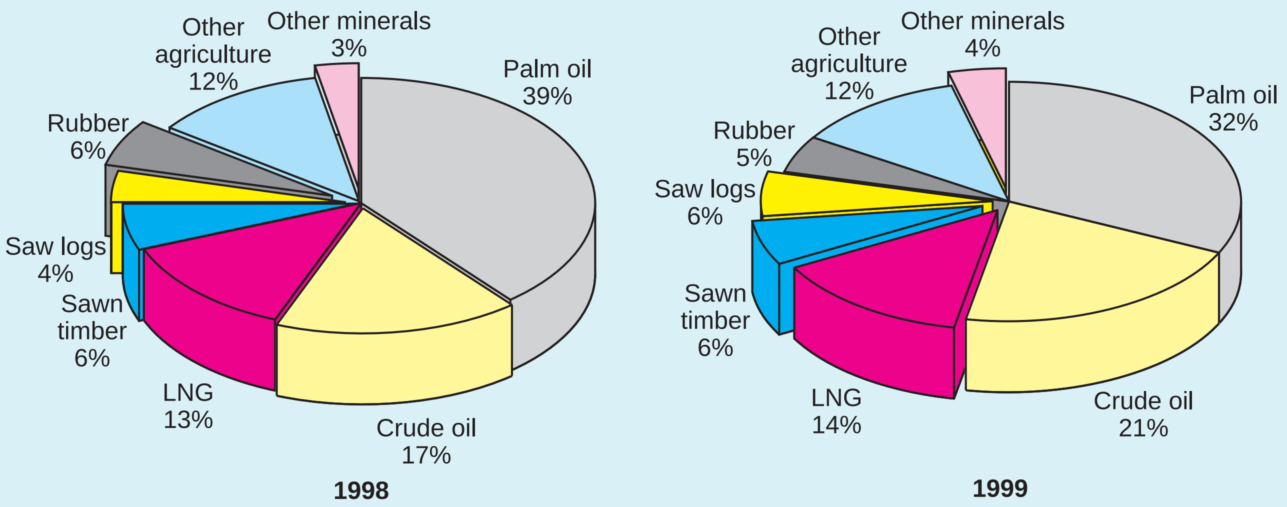
Graph 1.28
Manufactured Exports by Destination



Note: Selected Asia Pacific countries refer to Hong Kong SAR, Taiwan, Korea and Australia.

Graph 1.29
Commodity Exports in 1998-1999

(% share by commodity)



(1998: 18%). On the other hand, demand by Pakistan was slightly lower (–2.5%) while imports by The People's Republic of China fell sharply by 15%, reflecting the reduction in the Republic's import quota for palm oil during the year.

- Export earnings from **rubber** declined further by 17.2% to RM2.3 billion in 1999, the fourth consecutive year of decline, as both prices and external demand remained weak amidst excess global supplies of rubber. In terms of export destination, offtake from the European Union (36% of total rubber exports) in particular, fell by 6% during the year while imports by other buyers remained almost unchanged at the 1998 level.

- Export proceeds from **saw logs** and **sawn timber** turned around to register a sharp increase of 42.7% and 11.1% respectively in response to an improvement in external demand, particularly from the Asia-Pacific markets. The People's Republic of China, which accounted for 25% of Malaysia's total log exports, more than doubled its offtake during the year following increased construction activity in the Republic. Domestic supply constraints due to adverse weather and the Republic's adherence to its forest conservation policy as well as the abolishment of import tariffs on the commodity, encouraged higher exports to China. Meanwhile, Korea, Thailand, The People's Republic of China and Japan accounted for the bulk of the increase in sawn timber exports in 1999.

- Export proceeds from **cocoa**, which mainly consisted of cocoa butter, cocoa beans and cocoa powder, turned positive during the year, growing sharply by 18.6% to RM111.9 million. A higher export volume (+58%) was recorded as external demand improved markedly particularly from the United States, the Netherlands, Singapore, Australia and The People's Republic of China.

Proceeds from **mineral** exports increased in 1999, driven primarily by higher export prices for crude oil and LNG. Export volume increased only marginally.

- Earnings from **crude oil** exports rose sharply by 23.9% to RM9.3 billion in 1999, due entirely to higher export prices as export volume declined during the year. The sharp increase in Malaysia's crude oil prices to an average of US$18.18 per barrel from US$14 per barrel in 1998, was in line with higher international crude oil prices, which had increased substantially on account of tight global supplies following reduced production by OPEC members. On the other hand, the volume of crude oil exports was lower in 1999 due to higher domestic consumption and lower supply as crude oil production was reduced in line with the National Depletion Policy.

- Export receipts from **LNG** were also higher in 1999, increasing by 6.1% on account of increased export volume and higher export prices. The volume of LNG exports expanded

Table 1.17
Gross Exports

	1999				
	RM million	Annual change (%)	% share	US$ million	Annual change (%)
Manufacturing sector	**271,730**	**14.3**	**84.6**	**71,508**	**17.6**
Of which:					
Electronics, electrical machinery and appliances	195,047	20.6	60.7	51,328	24.1
Electronics	144,885	26.9	45.1	38,128	30.4
• Semiconductor	*65,485*	*20.2*	*20.4*	*17,233*	*23.7*
• Electronic equipment & parts	*79,400*	*33.0*	*24.7*	*20,895*	*36.5*
Electrical machinery & appliances	50,162	5.5	15.7	13,201	8.8
• Consumer electrical products	*21,728*	*5.2*	*6.8*	*5,718*	*8.6*
• Industrial & commercial electrical products	*16,498*	*9.5*	*5.2*	*4,342*	*13.0*
• Electrical industrial machinery and equipment	*11,107*	*1.2*	*3.5*	*2,923*	*4.1*
• Household electrical appliances	*829*	*–4.8*	*0.3*	*218*	*–1.9*
Textiles, clothing and footwear	9,467	0.3	3.0	2,491	3.4
Chemicals & chemical products	11,105	4.5	3.5	2,922	7.6
Wood products	6,984	16.8	2.2	1,838	20.3
Manufactures of metal	7,862	–4.8	2.5	2,069	–2.2
Transport equipment	5,114	–36.6	1.6	1,346	–35.5
Rubber products	5,061	–11.8	1.6	1,332	–9.1
Optical and scientific equipment	4,834	1.5	1.5	1,272	4.5
Agricultural sector	**27,673**	**–8.4**	**8.6**	**7,282**	**–5.5**
Of which:					
Palm oil	14,475	–18.6	4.5	3,809	–16.0
Sawn timber	2,807	11.1	0.9	739	14.6
Saw logs	2,663	42.7	0.8	701	47.4
Rubber	2,344	–17.2	0.7	617	–14.7
Minerals	**17,240**	**15.9**	**5.4**	**4,537**	**19.6**
Of which:					
Crude oil	9,306	23.9	2.9	2,449	27.7
LNG	6,349	6.1	2.0	1,671	9.6
Tin	491	1.3	0.2	129	4.7
Other	**4,538**	**18.2**	**1.4**	**1,194**	**21.6**
Total	**321,181**	**12.1**	**100.0**	**84,521**	**15.3**

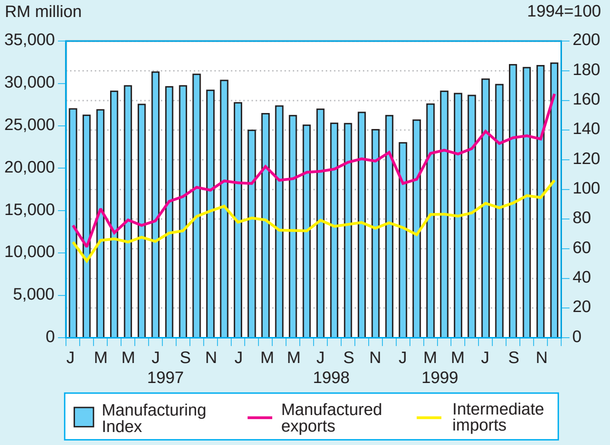
Source: Bank Negara Malaysia and Department of Statistics

by 2.8% (1998: –3.7%), reflecting increased offtake from Malaysia's major buyers, namely Japan and Korea, as economic activity in these economies improved. Meanwhile, the export unit value of LNG recorded an increase of 6.5% in United States dollar terms, in tandem with the increase in crude oil prices.

Gross imports (that is, import payments including cargo, insurance and freight payments or c.i.f.) increased by 9.1% in 1999 in line with output expansion to cater to the recovery in exports and domestic demand. The primary source of the import growth was higher imports of intermediate goods and, to a lesser extent, imports of consumption and dual-use goods. Reflecting the more gradual recovery of private investment and the low import content of public investment, imports of capital goods continued to decline by 6.7%. The significant decline in the first half year was reversed starting in June when a modest recovery in investment fuelled a recovery in imports of capital goods in the second half.

Imports of **intermediate goods** expanded by 13.2% as a result of strong growth in manufacturing production to meet both the higher export and domestic demand.

Graph 1.30
Manufacturing Production, Exports and Intermediate Imports



The main types of goods that contributed to this increase were parts and accessories of capital goods (11.1%) and processed industrial supplies (16.8%), both of which primarily enter into the production of manufactures for export. However, equally important was the strong growth in other types of intermediate imports that were related to the manufacture of goods for the domestic market. In particular, imports of primary fuels and lubricants and parts and accessories of transport equipment contributed significantly to the higher imports of intermediate goods, reflecting the recovery in the motor assembly industry.

The increased imports of parts and accessories of capital goods had a particularly significant impact on import growth, accounting for 4.9 percentage points of the total import growth of 9.1%. This was due mainly to higher imports of thermionic valves and tubes, photocells and parts, items which are crucial inputs for the electronics industry which experienced strong increases in overseas sales orders. These items accounted for about two-thirds of imports of parts and accessories of capital equipment, and 29.3% of total imports, underlining the strength of the industry as the main engine of the recovery.

The weak private investment climate prevailing during the first half of the year accounted for lower imports of **capital goods** by 6.7%. Beginning from the second quarter, the Government launched a concerted programme to speed up the implementation of public sector projects, which resulted in the shortfall in public expenditure narrowing significantly. While most public projects concentrated on infrastructure works that do not have a high import content, higher public investment contributed to the overall recovery in economic activity, especially in the second half of the year. As a result, imports of capital goods turned positive in June 1999 and have since continued to grow strongly.

The primary source of the decline in imports of capital goods continued to be the lower imports of industrial transport equipment. The main cause for this decline was the sharply lower imports of aircraft and ships (–52.4%) as the major transportation companies continued to reduce delivery of new vessels, due partly to the completion of expansion programmes in 1998. On the other hand, imports of commercial vehicles increased by 36.3% while those of trailers and containers increased by 18.8%, in line with the strong recovery in economic activity. In the case of other types of capital goods, higher imports of office equipment (10.3%), construction and mining equipment (39.3%) and agricultural machinery (19.3%) all contributed to the modest 2.5% growth in imports of other capital goods. However, imports of machinery for manufacturing (–7.3%), telecommunication equipment (–17.5%) and machinery for electricity generation and distribution (–10.1%) continued to decline due to the excess capacity in the manufacturing sector and the completion of major utilities expansion programmes.

Imports of **consumption goods** grew strongly by 21.9% as a result of the recovery in private consumption expenditure following improved economic conditions and employment prospects as well as the recovery in share prices. Nevertheless, despite ten consecutive months of positive growth, including nine months of double-digit growth, imports of consumption goods are still below the levels recorded before the onset of the East Asian crisis. Imports of consumption goods have now reached US$425 million in December 1999, lower than the pre-crisis peak of US$461 million in June 1997. Consumption goods accounted for about 6.2% of total imports in 1999, almost unchanged from the pre-crisis level.

The growth in consumption goods imports was due to higher imports of all types of consumer goods, particularly non-durable, durable and semi-durable consumer goods. Some non-durable items that recorded strong growth were medicines (24.6%) and soaps and cosmetics (16.2%). Durable imports which increased significantly included household electrical goods such as washing machines, refrigerators and cookers (151%) and audio and video equipment (46.5%). Semi-durable consumer imports that increased significantly included tapes and records (32%), clothing and footwear (35.8%) and household furnishings such as curtains, cutlery, bed linen, decorative items, mattresses and cushions (16.1%). Similarly, imports of **dual use goods** increased by 29% due to the high imports of passenger motor cars as the import of motor spirit declined due to high oil prices.

Malaysia's trade pattern remained relatively unchanged in 1999, with the major **trade partners** being the United States, Japan, Singapore and the European Union. These four partners alone accounted for 64.9% of Malaysia's total trade. The **United States** maintained a share of 19.9% of the total trade (20.8% in 1998), reflecting the continued strong demand for Malaysian goods. This resulted in a higher trade balance in favour of Malaysia with a bilateral surplus of RM27 billion (RM17.4 billion recorded in 1998). The bulk of the exports made up of manufactured articles, in particular machinery and transport equipment (79.6%). The main commodities imported from the US were also from this category (76.3%), reflecting mainly the importance of the electronics industry.

Japan overtook Singapore and regained its pre-crisis position as the second most important trade partner, accounting for 15.6% of total trade compared with 14.6% in 1998. This was largely due to increased imports (+15.6%) partly on account of valuation impact from a stronger yen. As a result, Japan not only maintained its position as Malaysia's most important source of imports but increased its market share from 19.6% of total imports in 1998 to 20.8% in 1999. However, despite the increase in imports, the trade deficit narrowed marginally to RM14.5

Table 1.18
Gross Imports by End Use

	1999				
	RM million	Annual change (%)	% share	US$ million	Annual change (%)
Capital goods	**33,027**	**-6.7**	**13.3**	**8,691**	**–5.9**
Capital goods (except transport equipment)	29,546	2.5	11.9	7,775	2.8
Industrial machinery	*10,170*	*–7.3*	*4.1*	*2,676*	*–4.0*
Transport equipment	3,482	–47.0	1.4	916	–45.3
Intermediate goods	**182,250**	**13.2**	**73.2**	**47,960**	**17.3**
Food and beverages, mainly for industry	3,998	–4.1	1.6	1,052	–1.2
Industrial supplies, n.e.s.	58,777	16.8	23.6	15,468	20.4
Metals	*14,282*	*20.5*	*5.7*	*3,758*	*24.2*
Fuels and lubricants	5,628	21.7	2.3	1,481	25.2
Parts and accessories of capital goods (except transport equipment)	110,970	11.1	44.6	29,203	15.5
Electronics	74,287	15.7	29.9	19,549	19.1
Parts and accessories of transport equipment	2,878	46.3	1.2	757	43.4
Consumption goods	**15,455**	**21.9**	**6.2**	**4,067**	**21.3**
Food and beverages, mainly for household consumption	6,059	6.6	2.4	1,594	9.7
Transport equipment, non-industrial	91	148.8	0.0	24	152.0
Consumer goods, n.e.s.	9,306	25.8	3.7	2,449	29.6
Consumer durables	*1,710*	*67.3*	*0.7*	*450*	*60.5*
Consumer semi-durables	*3,358*	*25.0*	*1.3*	*884*	*24.9*
Consumer non-durables	*4,238*	*29.9*	*1.7*	*1,115*	*23.7*
Dual use goods	**4,937**	**29.0**	**2.0**	**1,299**	**33.4**
Motor spirit	1,630	–28.8	0.7	429	–26.4
Passenger motor cars	3,307	114.7	1.3	870	122.6
Others	**4,418**	**49.9**	**1.8**	**1,163**	**7.8**
Re-exports	**8,784**	**–19.6**	**3.5**	**2,311**	**–15.9**
Gross Imports	**248,870**	**9.1**	**100.0**	**65,492**	**12.3**

n.e.s: Not elsewhere specified.

Source: Department of Statistics, Malaysia and Bank Negara Malaysia

Table 1.19
Direction of External Trade

	1999				
	Exports		Imports		Trade balance
	RM million	% share	RM million	% share	RM million
Selected South-East-Asian countries	75,467	23.5	58,072	23.3	17,395
Singapore	53,106	16.5	34,817	14.0	18,289
Thailand	10,481	3.3	9,377	3.8	1,104
Indonesia	4,679	1.5	6,677	2.7	–1,998
Philippines	4,929	1.5	6,213	2.5	–1,284
Brunei Darussalam	809	0.3	46	0.0	763
Vietnam	1,463	0.5	943	0.4	520
European Union	50,522	15.7	28,974	11.6	21,548
United Kingdom	12,067	3.8	5,611	2.3	6,456
Germany	7,692	2.4	7,704	3.1	–12
Netherlands	16,233	5.1	1,805	0.7	14,428
Other EU countries	14,531	4.5	13,855	5.6	676
United States	70,391	21.9	43,318	17.4	27,073
Japan	37,289	11.6	51,803	20.8	–14,514
The People's Republic of China	8,808	2.7	8,125	3.3	682
Hong Kong SAR	13,344	4.2	6,250	2.5	7,094
Taiwan	14,600	4.5	13,259	5.3	1,341
South Korea	9,498	3.0	12,974	5.2	–3,476
India	7,745	2.4	2,014	0.8	5,731
Australia	7,711	2.4	5,670	2.3	2,041
Rest of the world	25,808	8.0	18,411	7.4	7,406
Total	**321,181**	**100.0**	**248,870**	**100.0**	**72,311**

Source: Department of Statistics, Malaysia.

billion compared with RM14.6 billion recorded in 1998. Increased exports to Japan contributed significantly, growing by 23.7% during the year, following the recovery in the Japanese economy. The bulk of the exports consisted of machinery and transport equipment (52.3%) and mineral fuels (17.2%). Malaysia's imports from Japan consisted mainly of machinery and transport equipment (67.1%).

Singapore was Malaysia's third most important trade partner, accounting for a share of 15.4% (15.5% in 1998). This was due to a lower proportion of exports bound for Singapore compared with the previous year. Despite this, the trade surplus with Singapore increased to RM18.3 billion compared with RM17.7 billion in 1998. Similarly, trade with the 15 nations of the **European Union** was slightly lower in relative importance from 14.3% of total trade in 1998 to 13.9% in 1999. This was primarily due to the lower proportion of exports bound for the EU, while its importance as a source of imports also declined slightly.

The trade account with several other East Asian countries showed mixed developments, reflecting mainly the domestic economic conditions in both Malaysia and these partners and to some extent, the shift to source imports from lower cost suppliers. By and large, the bilateral trade balances with several developed Asian countries improved. In these cases, the main reason was faster growth in exports to countries that posted strong economic recovery. In particular, exports to South Korea increased by 45.7%, mirroring the strong recovery there. On the other hand, Malaysia's imports from other Asian countries increased, reflecting some shift to source imports from those countries where prices were lower. In particular, the trade deficit with Indonesia and the Philippines widened further due to the larger increase in imports to meet stronger growth in domestic demand in Malaysia.

For the second successive year, the surplus in the merchandise account was more than sufficient to offset the significantly higher deficit in the services account as well as the continued net outflow in the transfers account. In 1999, the net outflow in the **transfers account** remained large at RM7.2 billion, although lower than the record net outflow of RM9.9 billion experienced in 1998. This reflected lower remittances as a consequence of a lower number of foreign workers in the country following the return of nearly half a million foreign workers to their home countries during the recession in 1998. In addition, the unrequited transfers in the previous year were exceptionally large due to the one-off lump sum repatriation by returning workers.

The deficit in the **services account** deteriorated in 1999 as the recovery in domestic economic activity and buoyant external trade transactions resulted in increased demand for imported support services. The services deficit widened by RM6.6 billion to RM28.9 billion or 10.3% of GNP in 1999 (–8.3% of GNP in 1998). However, in US dollar terms, the deficit of US$7.6 billion remained below the pre-crisis level of US$8.1 billion experienced in 1997. In ringgit terms, the deterioration was due entirely to higher gross payments of RM85 billion, representing an annual increase of 19.8%. Gross receipts also recorded a large increase of 15.3% to RM56.1 billion due to higher demand for Malaysia's exported services reflecting the strong recovery in the regional economies. The weaker performance of the services account was again primarily due to large net payments for investment income due to non-residents, freight and insurance as well as other services, particularly management and professional charges. Meanwhile, the travel and other transportation accounts improved significantly, recording larger net surpluses during the year.

Net payments in the **investment income** account increased further by RM4 billion to RM18.8 billion in 1999, affected primarily by higher payments of profits and dividends. The substantial increase in receipts from Malaysian investment overseas was not sufficient to offset higher profits and dividends accruing to foreign direct investors, especially in the electronic and electrical

Graph 1.31
1999: Components of Gross Payments in the Services Account
(% share)

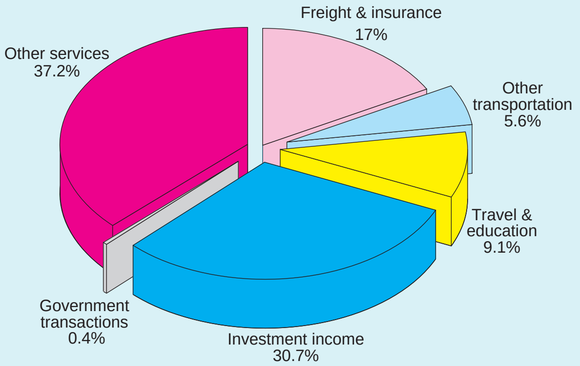


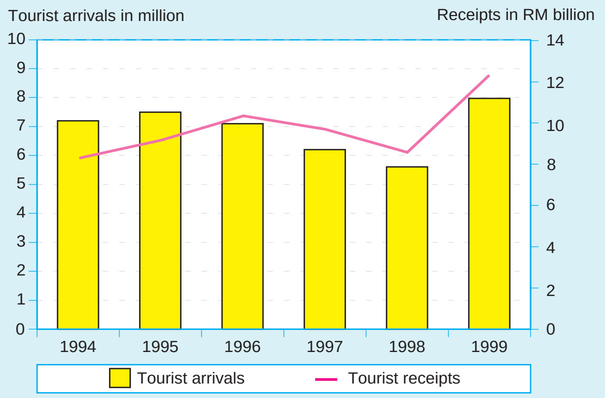
Table 1.20
Services Account

Subsector	1999			
	Net (billion)		Annual change (%)	
	RM	US$	RM	US$
Freight & insurance	–9.7	–2.6	15.4	19.1
Other transportation	2.5	0.7	9.3	12.8
Travel & education	5.6	1.5	81.3	87.1
Investment income	–18.8	–4.9	26.8	30.9
Government transactions n.i.e	…	…	–78.4	–77.8
Other services	–8.4	–2.2	100.1	106.5
Balance on services	**–28.9**	**–7.6**	**29.6**	**33.7**

industries which enjoyed high sales on the back of strong global demand. The interest income component remained in deficit (–RM1.7 billion) for the third consecutive year. However, the deficit has narrowed as the continued large interest payments on the external debt was partially offset by higher returns from the external assets of Bank Negara Malaysia. Meanwhile, higher demand for **other services** in line with the overall improvement in the economy led to a substantially higher net payments position in the **other services** account (–RM8.4 billion). In particular, the restructuring and merger exercises undertaken in both the corporate and financial sectors resulted in higher payments for contract and professional charges as well as salaries and agency fees. The **freight and insurance** account posted a larger deficit of RM9.7 billion (1998: –RM8.4 billion), reflecting higher payments abroad associated with higher trade transactions. The international shipping liners also raised freight rates after two years of consolidation. Nevertheless, higher earnings by major Malaysian shipping companies and the national airline for cargo services helped to reduce the outflow somewhat.

The net surplus in the **travel and education** account increased significantly to RM5.6 billion, benefiting mainly from the marked improvement in tourist receipts. The recovery of the regional economies, intensified promotion of inbound tourism and the hosting of major international conferences and sporting events led to a marked increase in tourist arrivals to 8 million visitors in 1999 compared with 5.6 million visitors a year ago. In particular, the Formula One race event brought in a total of 65,000 foreign visitors contributing more than RM500 million in foreign exchange earnings. Similarly, the number of excursionist arrivals also increased by 12.5% to 6 million. Meanwhile, concerted effort to promote Malaysia as a regional centre for education resulted in an increase in the number of

Graph 1.32
Tourist Arrivals and Tourist Receipts



foreign students pursuing courses in the local universities and colleges. Together, the tourism and educational sectors contributed to a significant increase by 42.6% in travel receipts to an unprecedented level of RM13.3 billion in 1999. On the payments front, the recovery in the economy contributed to an increase in expenditure on travel and education abroad, by 23.2% to RM7.5 billion (US$2 billion). Nevertheless, in terms of US dollars, the outflow was contained below the pre-crisis level of US$2.5 billion in 1997, due largely to active promotion to encourage domestic travel in Malaysia as well as Government measures to increase student intake at local universities and private colleges.

The net surplus in **other transportation** account (comprising mainly passenger fares, charter fees, charges on port and airport-related activities, and bunkers and stores) improved further by 9.3% to RM2.5 billion. This was attributed to improved earnings by Malaysian airline companies from passenger fares and higher receipts from port- and airport-related activities in tandem with improved economic conditions in the regional countries. Reflecting the increase in external trade and positive results of the ongoing effort to promote Port Klang as the main port for Malaysian exporters as well as the regional transhipment hub, throughput handled by Port Klang increased significantly. The container cargo throughput posted a 40% increase to 2.55 million TEUs in 1999, with transhipment cargo accounting for a share of 37.9%. Other major ports also reported increases in cargo handling.

In the **capital account**, the net inflow of long-term capital increased to RM11.7 billion in 1999 (1998: RM10.6 billion), due mainly to higher net inflow of official long-term capital and foreign direct investment. However, the short-term capital account recorded a substantial net outflow for the third successive year, amounting to RM36 billion, due to the reduction in short-term external liabilities of commercial banks and the non-bank private sector, increased trade credits and liquidation and repatriation of portfolio investment by some foreign investors.

The **official long-term capital account** registered a significantly larger net inflow of RM6.7 billion in 1999 (1998: RM2.1 billion) due to both larger borrowings and lower repayments by the Federal Government and the non-financial public enterprises (NFPEs). In contrast to the developments in 1998, the higher net inflow of official long-term capital in 1999 reflected mainly the improvement in access to long-term funds from the international markets. The Federal Government issued a 10-year global bond of US$1 billion in May 1999 and drew down loans offered by the World Bank and bilateral lenders to finance the recovery package and development of infrastructure. The larger borrowings by the NFPEs reflected the higher financing requirements for capital expenditure on both domestic and overseas projects. The new borrowings included the issuance of a 5-year US dollar-denominated bond of US$650 million by PETRONAS as well as loans under the Miyazawa Initiative.

Despite higher net foreign direct investment, **private long-term capital** declined to RM5 billion in 1999 (1998: RM8.5 billion), reflecting mainly a higher net outflow of funds for overseas investment and substantial net repayment of foreign loans by the Malaysian-owned companies. Net **foreign direct investment** increased moderately to RM13.4 billion or 4.8% of GNP (1998: RM10.6 billion or 4% of GNP), with higher inflows of both new investment and reinvestment. The stability and certainty accorded by the selective exchange control rules and the fixed exchange rate together with the Government's commitment to maintain pro-business policies contributed to the continued commitment of several multinational corporations to long-term investment in the country. In addition, higher export earnings on the back of strong external demand also contributed to higher retained earnings in 1999, which accounted for about one-half of net FDI while new equity accounted for a share of 42%. The bulk of the FDI in 1999 continued to be channelled into the manufacturing sector, which accounted for a 47% share, followed by the services sector (27%) and the oil and gas sector (24%). Net external loans from parent and associated companies were substantially lower in 1999 on account of lower new borrowing amidst ample liquidity in the domestic economy and higher interest rates abroad.

In terms of investments in manufacturing projects, the value of proposed foreign investments approved by the Ministry of International Trade and Industry continued to remain significant in 1999, amounting to RM12.3 billion (1998: RM13.1 million). This reflected the confidence and the sustained commitment among the foreign investors, particularly the existing investors in Malaysia, to invest in the country. This was evidenced in the increase in the value of approvals for expansion and diversification projects to RM6.2 billion in 1999 compared with RM3.8 billion in 1998. In terms of sources of investment, the United States of America, Japan, Singapore and the Netherlands had remained as the top investors during the year. Meanwhile, Pakistan has emerged as an important investor in 1999, with the approval to invest in a large project in the paper, printing and publishing sector. Within the oil and gas sector, the United States and the Netherlands continued to remain as major foreign investors in the country.

Gross **overseas investment** increased significantly to RM10.4 billion in 1999 (1998: RM8 billion), due mainly to larger investment by Malaysian companies, particularly the NFPEs, either through acquisitions or joint ventures, in a move to expand their operations worldwide. Reflecting the improved domestic corporate performance in 1999, the liquidation of assets of Malaysian-owned companies abroad and the repayment of loans to parent companies in Malaysia declined during the year. Hence, on a net basis, overseas investment increased significantly to RM6.2 billion (1998: –RM3.1 billion). Based on the Cash BOP Reporting System, the major recipient countries of overseas investment in 1999 were France, which accounted for 24% of the total direct equity investment, followed by Mauritius (16%), Singapore (12%), the United States of America (8%) and the United Kingdom (5%). Investment in France and Mauritius reflected mainly the transfer of funds by PETRONAS to its joint-venture partners in those countries for actual investment in third countries such as Sudan and Iran. Apart from Sudan and Iran, PETRONAS also has interests in exploration ventures in Vietnam, Syria, Pakistan, Turkmenistan, The People's Republic of China, Myanmar, Libya/Tunisia, Algeria and Angola. In addition to the upstream activities, PETRONAS has also formed strategic partnerships with companies in Vietnam, The People's Republic of China, Thailand, Philippines and South Africa to market and distribute LPG and other petroleum products.

Private long-term capital in the form of loans by the resident-controlled companies (RCCs) recorded a significant net repayment of RM2.2 billion in 1999 (1998: +RM1 billion). Gross external borrowings by the RCCs declined in 1999, attributable both to lower investment, especially in the first half-year, as well as higher supply of internally generated funds (due to higher export earnings) to finance capital expenditure. At the same time, the repayment of loans increased significantly during the year, reflecting mainly the maturity of loans committed in the mid-1990s. In addition, some companies took advantage of lower domestic interest rates to restructure their more expensive external debt through refinancing with domestic borrowing, while some companies with foreign exchange earnings opted to repay some foreign loans to reduce their debt servicing burden in view of higher interest rates abroad.

The **short-term capital account** continued to record a substantial net outflow of RM36 billion in 1999, due to a number of factors. Firstly, the outflow reflected both the decline in net external liabilities of the commercial banks due to lower inter-bank borrowings amidst ample liquidity in Malaysia and lower financing requirements for hedging contracts as well as the significant repayment of short-term debt by the non-bank private sector due to rising interest rates abroad. Secondly, the net liquidation and repatriation of portfolio investment by foreign investors following the expiry of the 12-month holding period of portfolio investment from 1 September 1999 amounted to about US$2 billion (RM8 billion). This was, however, significantly lower than earlier market expectation of a significant exodus of funds. Private sector estimates of funds outflow ranged from US$5 billion to US$8 billion. More significantly, some of these foreign funds have since been reinvested in the country in the first two months of 2000. In addition, higher interest rates overseas have prompted an increase in trade credits extended to the foreign importers while the repatriation of export proceeds of some Malaysian exporters, particularly those earned in the later part of the year, have yet to be effected. Exporters are allowed a period of six months from the date of exports to repatriate export earnings to Malaysia.

External Debt

Malaysia's policy of active debt management, guided by prudential safeguards and an efficient debt monitoring system, has enabled the country to keep the overall external debt situation manageable. The nation's **total external debt** outstanding declined further by 1.4% to RM159.7 billion at the end of 1999, reflecting reductions in the short-term debt as well as longer-term private sector external debt. In US dollar terms, the total debt was equivalent to US$42 billion (US$42.6 billion in 1998). The improvement in the debt situation in 1999 was reflected in the decline in the ratio of external debt to GNP and to exports to 57% and 43% respectively. The Federal Government's external debt, although slightly higher in 1999, accounted for only 12% of total external debt, while the NFPEs accounted for a share of 37%. The balance of the debt was private sector debt, with the non-resident controlled companies in Malaysia accounting for a larger share of this debt (54%).

Short-term external debt declined for the second consecutive year, by 29% to RM22.8 billion (US$6 billion) at the end of 1999. Ample liquidity in the domestic banking system, higher external borrowing costs following monetary tightening in the major industrial countries as well as lower financing requirements for hedging contracts resulted in a significant reduction in short-term borrowing by both the commercial banks and the non-bank private sector. Hence, the ratio of short-term debt to total external debt declined to 14% from 20% in 1998. As a share of international reserves, it fell to 19.5% from 32.4% in 1998. Including long-term debt with remaining maturity of less than one year, short-term debt would

Table 1.21
Outstanding External Debt

	1998		1999*p*	
	RM million	US$ million	RM million	US$ million
Total debt	**162,015**	**42,636**	**159,696**	**42,025**
Medium & long-term debt	*129,778*	*34,152*	*136,848*	*36,013*
Short-term debt[1]	*32,237*	*8,483*	*22,848*	*6,013*
As % of GNP				
Total debt	60.2	62.1	57.0	57.0
Medium & long-term debt	48.2	49.8	48.8	48.8
As % of exports of goods and services				
Total debt	49.0	50.6	43.0	43.0
Medium & long-term debt	39.3	40.5	36.8	36.8
Debt service ratio (%)				
Total debt	6.4	6.4	5.3	5.3
Medium & long-term debt	5.7	5.7	4.8	4.8

[1] Refers to bank and non-bank private sector short-term debt.
p Preliminary

amount to RM38 billion (US$10 billion), well below BNM's international reserves of US$30.9 billion as at end-1999.

External borrowing of medium- and long-term loans recorded a slightly lower net inflow of RM5 billion in 1999 (1998: RM5.2 billion). For the first time since 1989, the private sector recorded a net repayment of external loans of RM1.8 billion. However, this was more than offset by higher net external borrowing by the Federal Government and NFPEs totalling RM6.8 billion in 1999, reflecting official borrowing to finance the fiscal deficit and recourse to the international capital markets by Malaysian corporations following an improvement in spreads. Together with an exchange revaluation loss of RM2.1 billion arising from the depreciation of ringgit against the Japanese yen which raised the debt in ringgit terms, the total **medium- and long-term external debt** increased by 5.4% to RM136.8 billion at the end of 1999. In United States dollar terms, the debt amounted to US$36 billion (1998: US$34.2 billion).

In terms of **currency composition**, debt denominated in United States dollars continued to be the largest component of the medium- and long-term external debt, with a share of 72% of debt outstanding at the end of 1999 (74% in 1998). The share of yen-denominated debt increased to 21% (1998:18%), reflecting the drawdown of yen loans under the Miyazawa Initiative as well as an exchange revaluation loss which raised the yen debt in ringgit terms. The remaining 7% of the debt was accounted for by other international currencies, including the French franc, Singapore dollar, Deutsche Mark and pound sterling.

Overall **debt servicing** declined by 8.2% to RM19.5 billion, due both to lower principal repayment and interest payments. In line with higher export growth, the total debt service ratio declined to 5.3% from 6.4% in 1998.

Public sector external debt: The **Federal Government's** external debt increased by 23% to RM18.4 billion at the end of 1999, to account for a larger share of 12% of total external debt. Gross borrowings increased to RM4.8 billion, mainly from the issuance of US$1 billion Global Bond and the drawdown of loans offered by the World Bank and Islamic Development Bank and bilateral lenders especially from Japan under the Miyazawa Initiative (RM610 million). There was no prepayment of Federal

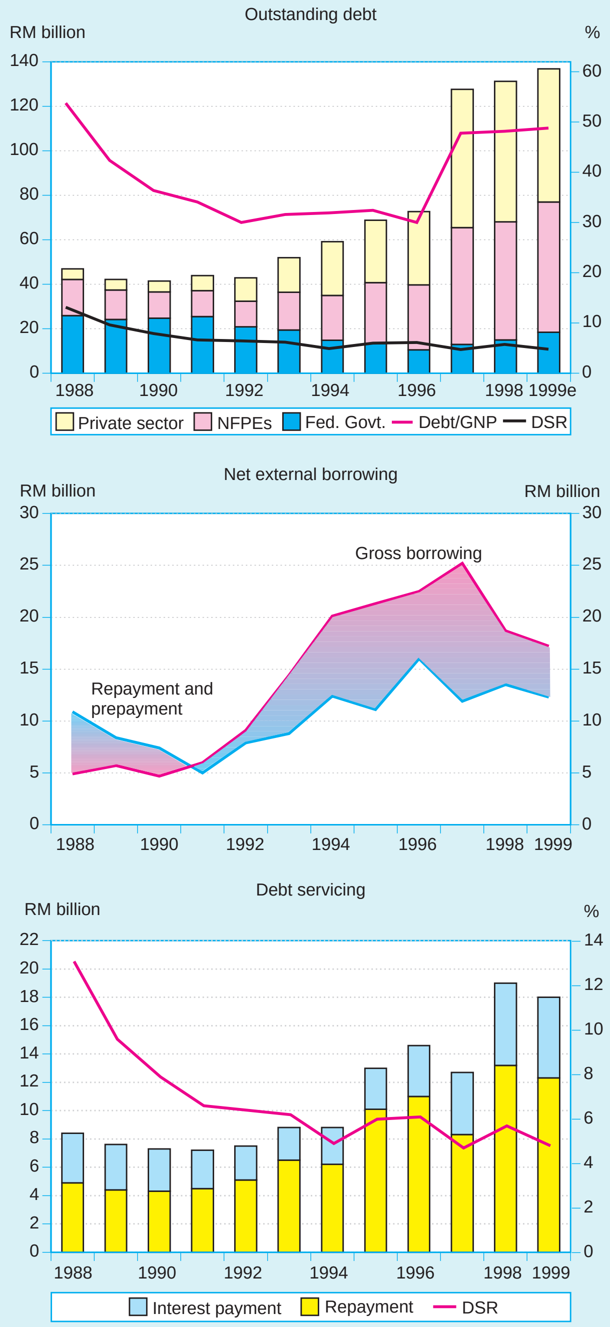
Government loans in 1999 while scheduled repayments totalled RM1.8 billion, including the maturity of a Samurai bond valued at 30 billion yen.

While the funding requirements were primarily met from domestic non-inflationary sources, the Government also tapped the international capital markets in May 1999 to establish market presence and develop an investor base for Malaysian securities, as well as establish a benchmark rate for Malaysian corporations. The 10-year Global Bond with a coupon rate of 8.75% was over subscribed by 300%. With the return of investor confidence and the upgrading of Malaysia's sovereign debt rating, external borrowing costs have declined significantly. Interest rate spreads for Malaysian benchmark securities have narrowed substantially to about 170 basis points at end-1999 (from a peak of about 1200 basis points in September 1998). A large share of loans under the Miyazawa Initiative are for educational projects and infrastructure development. The yen credit lines are offered at concessionary interest rates with maturities of up to 40 years.

The **NFPEs** took advantage of the improvement in access to long-term funds from international capital markets to increase gross borrowing to RM6 billion in 1999 (1998: RM4.7 billion). The new loans were mainly made by PETRONAS and Telekom Malaysia Berhad for funding domestic capital expenditure and investment in projects and joint ventures abroad as well as to refinance the more expensive existing loans. Petronas issued a US$650 million 5-year bond at a coupon rate of 8.875% to finance petrochemical projects. Foreign borrowings to finance overseas projects are naturally hedged, with earnings in foreign currency to service the debt. Loans under the Miyazawa Initiative (RM1.2 billion) were also drawn down by Bank Industri and Bank Pembangunan for promotion of exports and development of infrastructure for transportation. With principal repayments declining substantially to RM2.2 billion, the NFPEs recorded a larger net inflow of new loans of RM3.9 billion (1998: RM361 million). Together with an exchange revaluation loss of RM1.6 billion, the outstanding debt of the NFPEs increased by 10.2% to RM58.6 billion at the end of 1999.

Private sector external debt: The private sector recorded a net repayment of external loans of RM1.8 billion in 1999, reflecting a reduction in new borrowing (RM6.4 billion; RM10 billion in 1998) and significantly higher repayment abroad (RM8.2 billion; RM7 billion in 1998). Demand for external loans was subdued in the face of weak private investment activity, especially in the first half-year, and availability of cheaper sources of domestic funding, including internally generated funds arising from higher export earnings, to finance their capital expenditure. At the same time, higher interest rates abroad induced higher repayments by the private sector. As part of active debt management to reduce the overall debt servicing cost, some companies took the opportunity to restructure their more expensive external debt through refinancing with cheaper domestic bank loans and the issuance of private debt securities. Following these developments,

Graph 1.33
Medium- and Long-Term External Debt



private sector external debt outstanding declined by 3% to RM59.8 billion at end-1999.

Malaysia's framework for external debt management has always been guided by prudential policies designed from a macro perspective to reduce risk exposure to global interest rate shocks, adverse exchange rate movements and shifts in investor sentiment. In the context of these objectives, the debt management strategy will continue to balance the need to ensure that the corporate sector can have access to funding from the most competitive sources to finance productive activities that will generate sufficient foreign earnings to service the debt. In the management of the public debt, the Government will maintain prudence in its recourse to external borrowing to ensure continued long-term access to the international financial markets and low future borrowing costs.

In the management of risk and liquidity exposure, Malaysia already has the experience in practising some simple guidelines which are being put forward to emerging economies on the management of external debt. Corporations are encouraged to raise loans with longer maturity while short-term borrowing by the non-bank private sector to finance long-term investment are not encouraged. Consequently, Malaysia's external debt profile is biased towards the long-end, with about two-thirds of the medium- and long-term debt having remaining maturities of more than three years. Short-term debt forms only a small portion of total external debt. The currency composition of liabilities also corresponds closely with the currency composition of earnings, providing a natural hedge against currency risks. Prudential criteria on managing external loans by both the public and private sectors have helped to reduce Malaysia's vulnerability to external shocks.

International Reserves

The **net international reserves** held by BNM (comprising gold and foreign exchange holdings, IMF reserve position and holdings of Special Drawing Rights (SDR)) increased by RM17.8 billion in 1999 to RM117.2 billion (+US$4.7 billion in 1999 to US$30.9 billion). The level of international reserves is sufficient to cover the short-term external debt by 5.1 times (3.1 times in 1998), and is sufficient to finance 5.9 months of retained imports (5.7 months at end 1998).

The build-up in international reserves reflected the strong trade surplus during 1999. To a lesser extent,

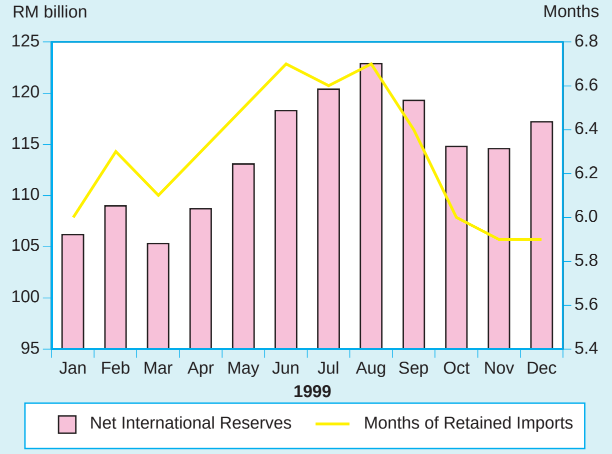
Table 1.22
International Reserves

	As at end		
	1997	1998	1999
	RM million		
Net Reserves	**59,122.8**	**99,424.4**	**117,243.5**
SDR holdings	478.9	793.9	330.3
IMF reserves position	1,622.0	2,379.2	3,168.2
Gold and foreign exchange	57,021.9	96,251.3	113,745.0
	US$ billion		
Gross Reserves	**21.7**	**26.2**	**30.9**
Months of retained imports	**3.4**	**5.7**	**5.9**

the accumulation in reserves also arose from foreign currency borrowing by the Federal Government, the bulk of which was through the issuance of a global bond. The combined trade inflows and borrowings more than offset net repayment by the private sector and the commercial banks, as well as portfolio outflows.

During the period January-August, reserves increased steadily by RM23.4 billion (US$6.2 billion) or a monthly average of RM2.9 billion. During September-November 1999, however, reserves declined by RM8.3 billion following the expiration of the 12-month minimum holding period on foreign portfolio funds on 1 September 1999. The outflow of portfolio funds amounted to US$1.3 billion in September and subsequently moderated to US$0.8 billion in the period October-December 1999. The decline in reserves in October was also attributed to the repayment of external

Graph 1.34
Net International Reserves



loans (US$0.8 billion) by the private sector as part of the corporate debt restructuring process. In December, reserves resumed its uptrend to increase by RM2.7 billion.

Following the 11th general review of quotas, Malaysia's quota with the IMF was raised in January 1999. As a result of the higher quota, there was an increase in the IMF reserve position. Part of the increase in the IMF reserve position, however, came from the decrease in the holdings of SDR. For the year as a whole, the IMF reserve position increased by RM789 million while the holdings of SDR by BNM declined by RM464 million.

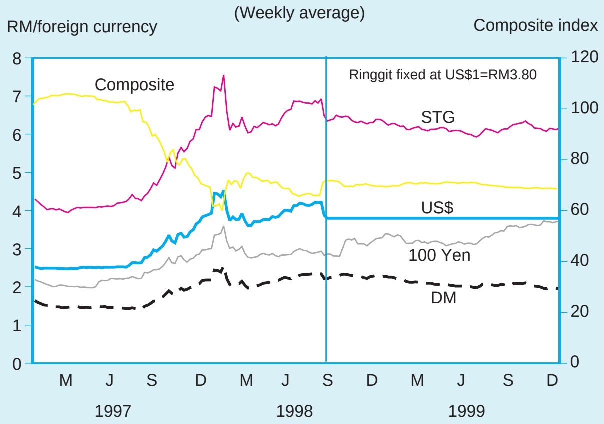
The objective of **reserve management** at BNM is to ensure capital preservation and liquidity of reserves whilst optimising returns. BNM has formulated a customised benchmark to serve as a guide for its investment decisions taking into account the need to ensure safety of reserves and to meet liquidity requirements as well as the level of tolerance for risk in investment decisions. The benchmark portfolio and, hence, BNM's reserves comprises a number of major international currencies, which are held in the form of foreign currency deposits or invested in high investment grade sovereign papers and gold. The composition of foreign currencies in reserves depends on factors such as the country's foreign currency obligations, its trade flows, and the overall assessment of the performance of the currencies concerned. The operational risks of reserve management are closely monitored to ensure full compliance with the investment guidelines.

Exchange Rates

In 1999, **the ringgit remained pegged to the United States** dollar at the rate of RM3.8000. This system of a pegged exchange rate has been effective since 2 September 1998. Under this arrangement, the ringgit exchange rate vis-à-vis other currencies is determined through cross-rates based on the movements of the US dollar against those currencies in the international foreign exchange markets.

The ringgit was relatively stable against most major currencies in 1999. The **volatility of the ringgit** (measured by the standard deviation of the daily rates) against major currencies, with the exception of the Japanese yen, reduced significantly. The standard deviation of the ringgit declined to 0.076 against the Deutsche mark (1998: 0.123) and

Graph 1.35
Exchange Rate of the Malaysian Ringgit against Major Currencies



0.092 against the pound sterling (1998: 0.326). However, the volatility of the ringgit against the yen increased to 0.213 (1998: 0.198).

During the year, the **ringgit appreciated against most major currencies in the world** reflecting the movements of the US dollar in the international foreign exchange markets. In 1999, the strong performance of the US economy supported the performance for the US dollar, leading to an appreciation against the pound sterling and the Euro. The dollar, however, depreciated vis-à-vis the Japanese yen due to the shift in the portfolio preference of global fund managers to yen-denominated assets with the growing investor confidence in the Japanese economic recovery. Following these developments, the ringgit appreciated against the pound sterling (+3.1%) and the Euro (+17.5%), while depreciating against the Japanese yen by 10.7%.

Graph 1.36
Exchange Rate of the Malaysian Ringgit against Selected ASEAN Currencies

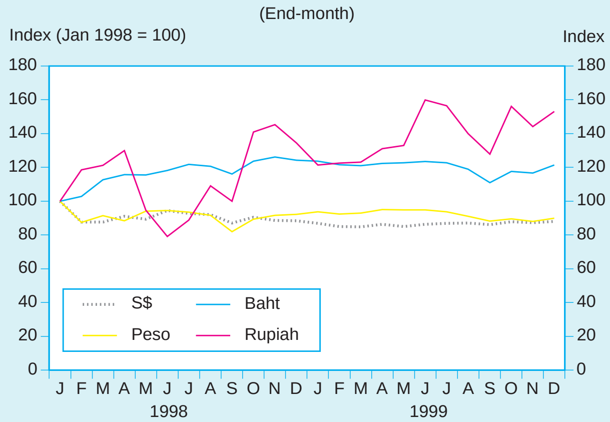


Table 1.23
Movement of the Ringgit

	RM to one unit of foreign currency[1]					Annual change (%)		2 Sept.'98-Dec.'99
	1998		1999			1998	1999	Change (%)
	End-Dec.	Sept. 2 [2]	End-Dec.	Low	High			
Composite	69.57	72.11	68.64	68.53	71.26	–0.2	–1.3	–4.8
SDR	5.3505	5.1177	5.2096	5.0296	5.3819	–1.8	2.7	–1.8
US$	3.8000	3.8000	3.8000	3.8000	3.8000	2.3	0.0	0.0
S$	2.2879	2.1998	2.2809	2.1874	2.2930	1.4	0.3	–3.6
100 Yen	3.3141	2.7742	3.7115	3.0561	3.7442	–9.7	–10.7	–25.3
Pound Sterling	6.3313	6.3708	6.1389	5.8975	6.3694	1.8	3.1	3.8
Deutsche Mark	2.2640	2.1743	1.9599	1.9450	2.3034	–4.0	15.5	10.9
Swiss franc	2.7497	2.6450	2.3836	2.3798	2.7983	–2.7	15.4	11.0
Euro [3]	–	–	3.8333	3.8042	4.5050	–	17.5	–
100 Thai baht	10.3613	9.3713	10.1199	9.1489	10.5337	–20.5	2.4	–7.4
100 Indonesian rupiah	0.0476	0.0354	0.0542	0.0407	0.0575	51.5	–12.2	–34.7
100 Korean won	0.3190	0.2827	0.3355	0.3053	0.3367	–27.7	–4.9	–15.7
100 Philippine peso	9.7064	8.8302	9.4823	9.2356	10.1152	–1.1	2.4	–6.9

[1] US$ rates are the average of buying and selling rates at noon in the Kuala Lumpur Interbank Foreign Exchange Market. Rates for foreign currencies other than US$ are cross rates derived from rates of such foreign currencies against the US$ and the RM/US$ rate.
[2] Ringgit was fixed to US$1 = RM3.8000 on 2 September 1998.
[3] The Euro began to be traded on 4 January 1999 (EUR 1 = RM4.5050). The annual change for 1999 is calculated against the value as at 4 January 1999.

Meanwhile, the **performance of the ringgit against regional currencies was mixed** in 1999. The ringgit appreciated against the Singapore dollar (+0.3%), the Thai baht (+2.4%) and the Philippine peso (+2.4%), while depreciating against the Indonesian rupiah (–12.2%), Korean won (–4.9%) and the Taiwanese dollar (–2.7%). The Indonesian rupiah continued to remain volatile during the year due mostly to domestic economic and political developments. In other parts of the region, the Thai baht remained subdued for the most part of the year, while strong portfolio inflows into Korea resulted in an appreciation of the won.

Since the fixing of the ringgit exchange rate against the US dollar on 2 September 1998, the ringgit has depreciated against regional currencies and the Japanese yen reflecting the movements of the US dollar. During the period between 2 September 1998 and end-December 1999, the ringgit has weakened against regional currencies in the range of 3.6%–34.7% and 25.3% against the Japanese yen. In terms of the composite, the ringgit depreciated by 4.8% during the same period.

Overall, the pegged exchange rate regime has benefited the economy by offering a period of relative stability, which has aided the recovery of economic activity and allowed the acceleration of financial reforms. The peg has introduced a greater degree of stability and predictability in the operations of trade which has helped manufacturers conduct their pricing and investment decisions in an environment of greater certainty. The peg has been sustainable as it is consistent with the underlying fundamentals of the economy. At the same time, consistent macroeconomic policies have further ensured the viability of the regime.

Flow of Funds

For 1999, the economy registered a larger total resource surplus of RM47.4 billion, which accounted for 16.9% of GNP (+RM36.8 billion or 13.7% of GNP in 1998). The larger resource surplus reflected mainly the favourable export performance amidst a moderate increase in imports. The nation's larger net savings was due mainly to the larger net savings of the private sector of RM34.8 billion, while the resource surplus of the public sector remained stable at RM12.6 billion (both the private and the public sectors also registered resource surpluses of RM24.6 billion and RM12.2 billion respectively in 1998). The inter-sectoral flow of funds between the sectors of the economy in 1998 and 1999 is shown in Tables 1.23 and 1.24 respectively.

Despite the higher public consumption and investment expenditure, which were undertaken as part of the fiscal stimulus package to promote economic recovery, the non-financial balance of the public sector continued to register a net resource surplus of RM12.6 billion in 1999 (a net resource surplus of RM12.2 billion in 1998). Together with official foreign borrowings (RM6.7 billion) and net withdrawals of deposits (RM2.2

Table 1.24
Flow of Funds, 1998

Transactions/Sectors	National Accounts	Domestic Economy			Rest of the World	Sum
		Public Sector	Private Sector	Banking System		
	RM billion					
Disposable Income	–259.3	72.5	186.8			0
Consumption	146.6	–28.5	–118.1			0
Investment	76.3	–32.0	–44.3			0
Change in Stocks	–0.4	0.2	0.2			0
Exports of Goods and Services	325.3				–325.3	0
Imports of Goods and Services	–263.3				263.3	0
Net Factor Payment Abroad	–15.3				15.3	0
Net Transfers	–9.9				9.9	0
Non-Financial Balance	0.0	12.2	24.6	0.0	–36.8	0
Foreign Financing						
Corporate Investment			8.5		–8.5	0
Net Foreign Borrowings		2.1	–9.8		7.6	0
Net Change in Foreign Assets						
BNM				–40.3	40.3	0
Banking System				–10.9	10.9	0
Domestic financing						
Change in Credit		–12.3	4.1	8.2		0
Change in Money Supply, M3			–10.7	10.7		0
Net Borrowings from Non-Bank Sector		–2.1	2.1			0
Net Errors and Omissions			–18.8	32.3	–13.5	0
Sum	0	0	0	0	0	

Table 1.25
Flow of Funds, 1999

Transactions/Sectors	National Accounts	Domestic Economy			Rest of the World	Sum
		Public Sector	Private Sector	Banking System		
	RM billion					
Disposable Income	–273.1	79.8	193.3			0
Consumption	158.8	–34.1	–124.7			0
Investment	66.6	–33.0	–33.6			0
Change in Stocks	0.3	–0.2	–0.2			0
Exports of Goods and Services	363.3				–363.3	0
Imports of Goods and Services	–289.3				289.3	0
Net Factor Payment Abroad	–19.4				19.4	0
Net Transfers	–7.2				7.2	0
Non-Financial Balance	0.0	12.6	34.8	0.0	–47.4	0
Foreign Financing						
Corporate Investment			5.0		–5.0	0
Net Foreign Borrowings		6.7	–24.8		18.1	0
Net Change in Foreign Assets						
BNM				–17.8	17.8	0
Banking System				–11.1	11.1	0
Domestic financing						
Change in Credit		2.2	–5.9	3.8		0
Change in Money Supply, M3			–33.1	33.1		0
Net Borrowings from Non-Bank Sector		–21.4	21.4			0
Net Errors and Omissions			2.6	–7.9	5.3	0
Sum	0	0	0	0	0	

billion), a total of RM21.4 billion was extended to the private sector. This largely reflected transfers, in particular by NFPEs to the private sector, mainly in the form of equity participation and purchase of assets.

Meanwhile, the recovery in economic activities enabled the private sector to register higher disposable income of RM193.3 billion in 1999 (RM186.8 billion in 1998). Following a period of higher disposable income and the lower rates of interest, private consumption also increased to RM124.7 billion in 1999 (RM118.1 billion in 1998). Nonetheless, with the continued excess production capacity in the domestic economy, private investment expenditure declined to RM33.6 billion in 1999 (RM44.3 billion in 1998). As a result, the private sector registered a larger net savings-investment surplus of RM34.8 billion (RM24.6 billion in 1998). Together with continued inflows of corporate investment from abroad (+RM5 billion) and net borrowings from the public sector (+RM21.4 billion), the private sector surplus stood at RM61.2 billion.

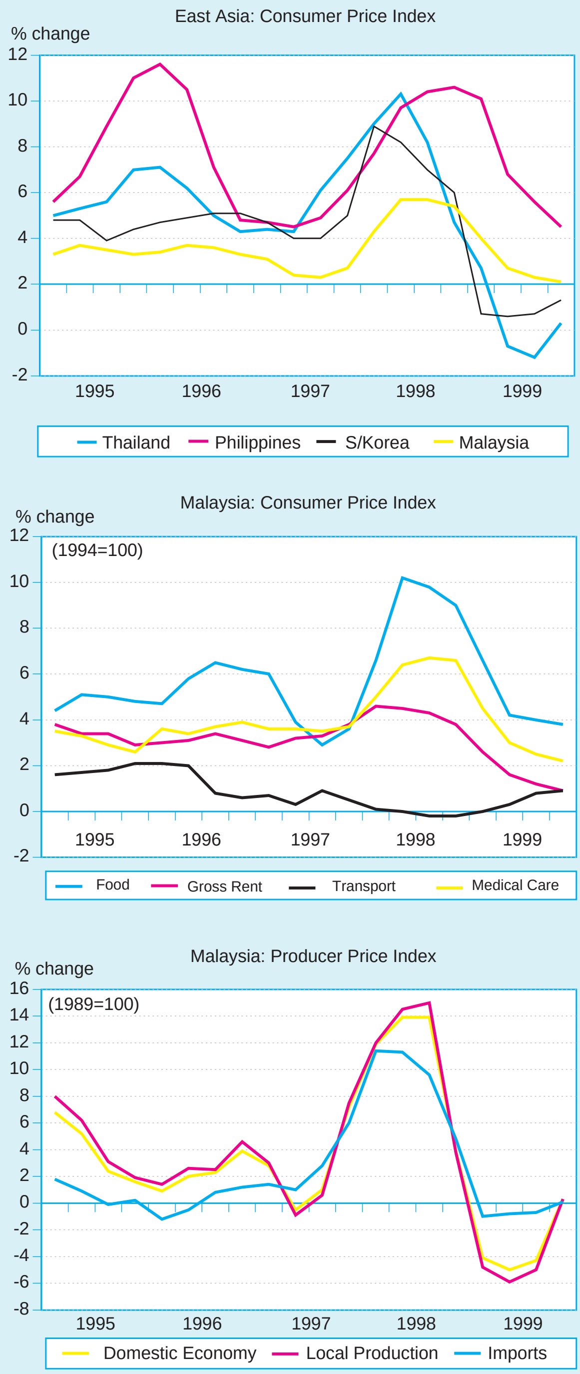
The bulk of the surplus was placed in the form of deposits with the banking system (-RM27.1 billion) and held as currency balances (-RM6.0 billion), which together amounted to RM33.1 billion, as well as net repayment of credit to the banking system (-RM5.9 billion). There was also partial outflow of these funds to abroad. Outflows were mainly in the form of private short-term funds (-RM24.8 billion) as well as reduction in net external liabilities of the banking system (-RM11.1 billion), which together with some net unidentified payments abroad (-RM5.3 billion), amounted to RM41.1 billion. Nonetheless, continued inflows of long-term capital (both official borrowings and corporate investment) together with the large current account surplus, resulted in an accumulation of net international reserves of RM17.8 billion during the year.

Inflation

Inflation moderated in 1999. The relative stability of the ringgit exchange rate, excess capacity in the economy and lower commodity prices led to more moderate price increases in 1999. Inflation as measured by the **Consumer Price Index** (CPI, 1994=100) rose at an annual rate of 2.8% in 1999, lower than the earlier estimate of 3%. The CPI had risen to peak at 6.2% in June 1998 before moderating to record an increase of 5.3% for the year as a whole. Excluding food, growth in CPI was lower and had moderated progressively from 2.8% in January to reach 0.8% in December. For 1999 as a whole, the CPI excluding food rose at an annual rate of 1.6%.

As the ringgit exchange rate against the US dollar was fixed at US$1=RM3.80 effective 2 September 1998, the ringgit appreciated by an average annual rate of 4.8% against the US dollar in the period January-August 1999 and 3.2% for the year as a whole. This marginal appreciation contributed partly to lower consumer prices. In the

Graph 1.37
Inflation: Average Annual Rate of Change



Box III

Towards A Knowledge-Based Economy

Introduction

The rapid development of information technology in recent years has enabled information to be transmitted almost instantaneously to any part of the world. Together with the rapid advancement in technology, this has made the basic production skills increasingly vulnerable to machine substitution. Hence, the need for highly skilled knowledge workers to generate the intangibles that will add value to the product. This is reflected in the shift towards high skill, high technology and service-based growth.

As a small, open economy, Malaysia recognises this global change in which economic growth and success are directly associated with the ability to harvest new ideas and innovation and implement them. To remain competitive, Malaysia needs to transform into a knowledge-driven economy in order to take advantage of the global developments created by the new information and communication technologies. This box article begins by defining the K-economy in simple terms. This is followed by a discussion of the rationale for the transition to the K-economy and the challenges posed by the transition. The article concludes with a discussion of the enabling environment needed for a sustainable K-economy.

K-economy Defined

There is no one standard definition of the K-economy but an acceptable one must place importance on the generation and exploitation of knowledge to create new value in the economy. Indeed, knowledge is information that is put to productive work. Knowledge includes information in any form, know-how and know-why. Knowledge is not only embodied in goods and services, particularly in high technology industries, but also in knowledge as a commodity itself, manifested in forms such as intellectual property rights or in the tacit knowledge of highly mobile key employees. And it involves the way we interact as individuals and as a community. Unlike capital and labour, knowledge is a public good and sharing with others involves zero marginal cost. In addition, technology breakthrough based on knowledge creates technical platforms that support further innovations and drives economic growth.

There are three main aspects of a K-economy that differentiate it from the traditional production-based economy (P-economy).

- Firstly, the K-economy focuses on knowledge as the driver of economic growth, as knowledge can increase the production capacity of the other factors of production and transform them into new products and processes. The K-economy is not confined to information technology (IT). Before the advent of the proliferation of IT, it was knowledge that was embodied in human beings as “human capital” and technology that was embodied in the capital investment undertaken by the Asian economies that brought about the so called Asian miracle. These two types of investments had helped to close the “knowledge gap” between the developed and emerging countries on how to transform inputs into desired outputs. With IT developments, the management of this knowledge gap has become more complex as the globalisation process gains momentum.

- Secondly, K-economy encompasses both qualitative and quantitative changes that transform the structure, mode and the way the economy operates. To compete in a K-economy environment, one needs to focus on the exploitation of intellectual capital, information advantage, a learning culture and more importantly, agile organisations. Knowledge goods and services are customised, less stable and have a shorter life cycle. Moreover, knowledge-based activities will not in most cases generate large volume. Rather,

Chart III.I
Migration to a K-economy

P-economy	K-economy
Structure comprises: manufacturing, agriculture, construction, mining and services sectors.	Merging and blurring of sectors and emergence of K-based sector.
Factors of production: land, labour, capital and decreasing returns to scale.	Intellectual capital, knowledge and increasing returns to scale.
Hierarchical organisations.	Networking and horizontal organisations.
Products: stable and longer life cycle. Output is mass-produced.	Products: less stable and shorter life cycle and customised with K-contents.
Output and resources traded in the market place.	Output and resources traded in the market space through information-based channels.
Competitive advantage: low cost of labour and abundance of raw materials.	Competitive advantage: intellectual capital and exploitation of knowledge.
Based on production work.	Based on K-work and growth of e-commerce.

they will result in the production of intangibles that enhance value through better quality, time saving and increased consumer satisfaction.

- Thirdly, firms in a K-economy focus on investments in intangibles such as human capital, R&D capacity, customers' database, brand names and reputation. As creators of knowledge-based assets, K-firms organise and create intellectual assets, exploit networks and gain access to other clusters of knowledge assets that belong to their suppliers and customers. In this way, the firms will be able to integrate the whole value chain to increase productivity and competitiveness in both domestic and foreign markets.

Rationale for the Transition to the K-Economy

In this era of the Knowledge Revolution we will witness ideas breeding other ideas in a concentric spiral of progress. To remain competitive, Malaysia has to tap the vast opportunities provided by the knowledge revolution. A knowledge-rich and agile environment will facilitate successful competition in an evolving global environment. The ability to shift to this new competitiveness paradigm will enable Malaysia to leapfrog from the industrial era to a post-industrial era that is based on knowledge and R&D. It is clear that in a dynamically evolving environment, a transition to a K-economy where innovation and adaptiveness prevail will be the most prudent and effective strategy for promoting sustainable real economic growth.

There is no doubt that there has been some gains in productivity in certain sectors in Malaysia. Nevertheless, the concern is that the productivity gains have been facilitated by increased sophistication of production equipment that are imported, and this equipment would also be available to competitors. The problem of productivity has been aggravated in recent years by rising wages. Continuous wage increase that exceed productivity growth will erode Malaysia's advantage as a low cost production centre. In other words, in this millennium, low wages will no longer provide the leverage for competitiveness in Malaysia. Low wages in fact encourages brain drain of skilled labour and managerial talent drawn by higher wages elsewhere. Hence, competitiveness does not depend on low wages. Rather, it requires a critical mass of creativity and innovative potential which is backed by adequate financing, educated labour force with the right skills and positive attitude and a supportive infrastructure and regulatory environment.

Currently there are skill gaps in Malaysia. This is the inherent weakness of the present P-economy with a mismatch of skills. Of more concern is that wages in the P-economy will be determined by the competition with other low-cost P-economies, thus setting the ceiling for any increase in wages. Consequently, earnings in such P-jobs are below the wages for K-jobs, thus widening the income gap between these groups of workers.

The advent of IT has also brought changes through the evolvement of global electronic business, in particular e-commerce as the fundamental element of the emerging digital economy. E-commerce calls for a distinct paradigm shift from our traditional way of doing business, and the growth of e-commerce will have an impact on the domestic economy that could far exceed the ringgit value of e-commerce activity. Indeed, Malaysian businesses will have to harness the forces of e-commerce to break into the international market. At the same time, there is a need to develop new areas of growth such as knowledge-intensive services sector. Reliance on accumulation of manufactured goods, and the export of traditional goods will be insufficient to generate growth in the future. Malaysia needs to become a "knowledge-export" platform to secure future economic prosperity. Exports need to be increasingly based on "knowledge content" that have higher value added and that contribute to higher income levels.

Table III.1
Malaysia vis-à-vis Other Economies

Year 1997	K-skills Workforce (as % of total workforce)	R & D/ GDP (%)	K-skills in R & D (per million population)
Countries			
Malaysia	10.7	0.3	87
Singapore	26.4	1.4	2512
Korea	15.1	2.8	2636
Taiwan	15.5	1.9	3340
Japan	22.9	2.8	5677

Source: NITC

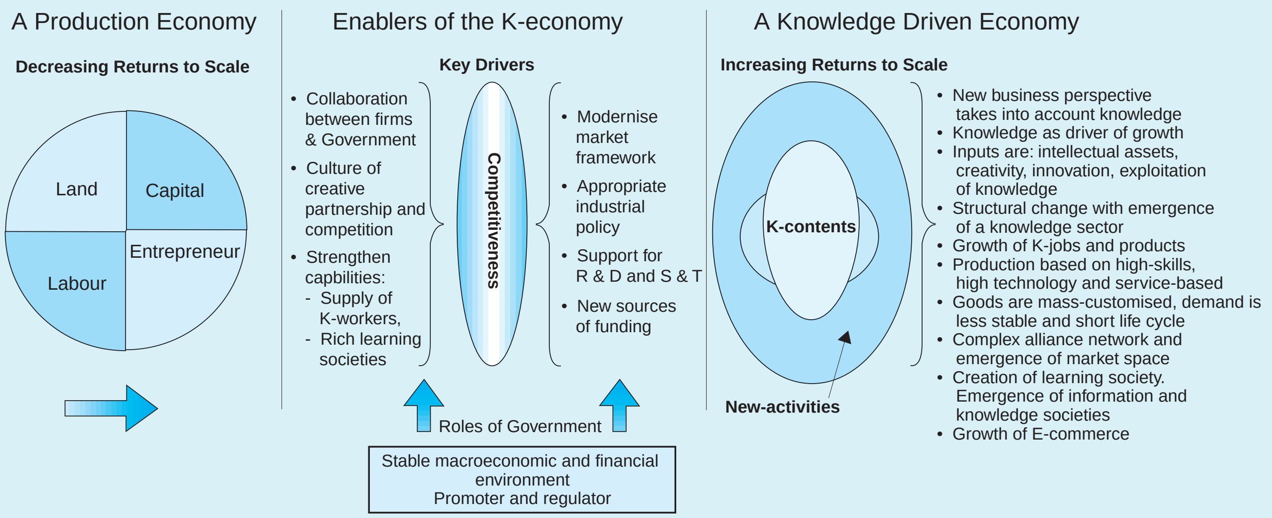
Challenges of the Transition to a K-Economy

In managing the transition to the K-economy, many barriers both cultural and economic will be encountered and many facets of life will be changed. The traditional manner of managing organisations, business models and culture and production process will be challenged in an economy that is knowledge driven. While Malaysia has relatively strong economic fundamentals, it needs to develop the information infrastructure and increase the use of technology. There are also shortages of technical and K-skilled labour and expenditure on R&D needs to increase. A shift towards a knowledge-based economy, therefore, presents significant new challenges to the way the Government, people and organisations think, operate and manage their businesses.

- The first challenge is to design an aggressive and pragmatic architecture that can contribute to building a knowledge rich and agile environment. This is new, and policy makers must realise that if we do not change the way we operate, this will affect the efficiency and success of the migration to the K-economy. Malaysia needs not only to increase the knowledge but also to position itself to increase the exploitation of knowledge. In this endeavour, Malaysian businesses have to close the productivity gap with their competitors and to produce innovative new products and create high value services. Malaysia has, therefore, embarked on the preparation of the K-economy Master Plan to formulate the framework for the successful transformation of the economy. Various aspects such as the pace of transition into the K-economy, the targets and the breakthrough approach will be given careful consideration and study.

- The second challenge is to close the present "gaps" in the economy that obstruct and are a constraint to the transition to a knowledge driven economy. A critical assessment of the possible rigidities in the economy and obstacles in terms of legislation and policies need to be identified. While there are already "pockets" of K-activities in existence, it is important to establish benchmarks for the performance of these "pockets". When compared with the successful K-economies, statistics show that at present Malaysia has a relatively low share of IT skills to labour force, K-skills in R&D per million of population and R&D investment to GDP. Nevertheless, efforts are being directed to increase the levels of K-labour, private investment in the K-sectors, and innovation capabilities.

Chart III.2 The Knowledge Economy: A Route Map



- The K-economy will make new demands on a conducive business environment and adequate human capital with the right motivation, attitudes, high level of skill and educational attainment as well as high entrepreneurial skills to successfully capitalise on opportunities that arise. The policy makers will be challenged to equip people with K-skills such as problem-solving and cognitive skills, as well as providing the appropriate communication infrastructure and adequate financial capital to sustain knowledge organisations.

- There are also risks that need to be taken into consideration in planning the transition to a K-economy. Policy makers and the public at large must realise that a K-economy does not eliminate the risks of volatility and uncertainty that exists in the international environment. Indeed, declining exports and slower global economic performance will also affect the K-based industries and therefore will continue to be vulnerable to external development.

- Besides the demand for the right fundamentals that support the K-economy, there will also be an impact on society and the quality of life. There will be certain barriers to entry into the K-economy and these may widen the disparity between the urban and rural population. For example, the need to ensure rural access to IT equipment and services. Otherwise, it would reduce their chance to actively participate in the new economy. Therefore, one major challenge is to ensure that the K-economy will not increase the disparity in income distribution between the various segments of society and between the urban and rural populations.

- The final challenge is to change the perception or mindset of the population and the investors towards the knowledge-driven economy. The experience of other countries reveals that people do not fully appreciate the potential economic impact of the transition to a knowledge-driven economy. People do not have the perception that “knowledge work” will hold promise for the economy in the future and thus will continue to place undue importance on the traditional tangible sectors.

Setting the Enabling Environment

Lessons learnt from the national K-economy strategies of other countries point to the need to put in place several key ingredients for setting the right environment for a K-economy. These include establishment of efficient and low cost universal telecommunications network, improved productivity and industrial and commercial competitiveness, support for the information services sectors, focus on investments in education and training, life long learning and upgrading of skills, better-informed populace and support for an innovation culture. Malaysia already has in place the enabling environment for the transition including the ICT policies as part of the broader modernisation programme, and the setting up of the Multimedia Super Corridor infrastructure. There are other important enablers for the successful transition to a K-economy. These include the following:

- In the dynamic and agile knowledge-driven economy, new polices will replace old protectionist policies that protect industries against the tide of globalisation and liberalisation. The trend has been to shift towards market-driven, self-regulatory mechanisms that promote competition, stimulate enterprise and create a culture of creative partnerships.

- Strengthening capabilities in all aspects in the economy:

  – Increase the supply of workers with creativity and higher order cognitive skills through provision of incentives for ensuring a brain gain and for establishing responsive educational and training institutes that cater for continuous work-related training and more knowledge-based courses, particularly IT and multimedia.

  – Nurture a pool of entrepreneurs with the vision to turn ideas and exploit knowledge into winning products and processes.

  – Support for R&D and encourage innovative collaboration, technology dissemination and modernisation of infrastructure to support all forms of research. Science and technology policies that emphasise on the need for innovation and dissemination of technology to a wide range of sectors.

  – To maximise the benefit of a shift from the P-economy to a K-economy, focus R&D on resource-based industries where Malaysia can raise value added capacity.

  – Nurture learning communities and a rich learning society whereby people share and disseminate knowledge.

- Modernise the market framework to facilitate the growth of the K-economy. To this end, priority needs to be accorded to the development of a first-rate National Media System which will include the internet and other IT innovations, as these provide the platform of e-commerce and the central economic strategy for the development of the K-economy.

- Availability of new sources of business funding (such as venture capital and high net worth individuals) for knowledge-based firms to fill the gaps in the early stage of investment funding. Effective strategies will also be needed to unlock the bottlenecks for growth of SMEs through enhancing access to finance, technology capability and innovation, while promoting networking and alliances and diffusion of best practices.

Changing Role of Government

The Government has the role of both a promoter and a regulator to lead and facilitate the development of a K-economy. In this new environment, the Government will also need to manage the risks arising from market deregulation and liberalisation that may be required to promote the K-economy. While moving forward towards a K-economy driven growth, it is necessary to manage the consequent risks that may cause instability in the system and markets. Policies will therefore be clearly articulated to provide the right signals to businesses on the direction that the economy is heading and the strategies to get there. As a manager of emerging risks, the Government will deal with any market failures in a trans parent manner to provide a conducive macroeconomic and financial environment to ensure business confidence.

Conclusion

There are both opportunities and challenges that policy makers will face in the transition towards a knowledge-based economy. Knowledge and ideas in the K-economy are infinite economic goods that can generate increasing returns. Indeed, throughout the world, the national focus has shifted to the intangibles of knowledge as an engine of economic growth. We are in uncharted territories and will have much to learn from the experience of other successful K-economies. However, all changes need to be carefully managed. In the transition to a K-economy, the proven contributions from the traditional economic system should also be managed accordingly. Indeed, the two systems should be managed as complements to economic development and prosperity.

prevailing environment of excess capacity in the economy, firms would have passed on the full impact of this appreciation of the ringgit to consumers in order to maintain market share. To a large extent, low inflation in Malaysia's trading partner countries and lower prices for most agricultural commodities further helped ease increases in domestic prices. On a regional basis, the CPI for Peninsular Malaysia, Sabah and Sarawak rose at an annual rate of 2.9%, 2.4% and 1.6% respectively in 1999. During the first two months of 2000, the annual rate of increase in the CPI moderated further to 1.6%.

In early 1999, CPI was at a monthly annual high of 5.2% in January, but moderated progressively to a low of 2.1% in June 1999. Thereafter, it picked up marginally before stabilising again at 2.1% in September and October and reached the year's monthly annual low of 1.6% in November. The CPI rose by 2.5% in December mainly on account of cyclical supply constraints, resulting from adverse weather conditions as well as an increase in demand due to several festivities during the month.

Reflecting cyclical supply shortages, particularly of essential food items, prices of non-durable goods advanced more rapidly at an annual rate of 4.2%, while prices for services rose more moderately at 2.3%. Higher prices for services reflected increased costs of medical and health care; recreation, entertainment, education and cultural services; and miscellaneous services. On the other hand, as a reflection of weak global prices and relatively lower consumer demand, prices of semi-durable and durable goods declined by 0.9% and 0.5% respectively, as consumers had deferred or reduced consumption of these goods or looked towards cheaper substitutes.

In comparing the different components of the overall CPI, the rise in the three sub-indices, that is, beverages and tobacco; food; and medical care and health expenses exceeded the 2.8% annual increase in the overall CPI in 1999. The index for beverages and tobacco rose by 7.9% on account of higher import and excise duties imposed on cigarettes, tobacco products and alcoholic beverages in the 1999 Budget. However, the group's low weight of 3.6% in the overall CPI basket meant that this group contributed only 0.27 percentage points to the rate of inflation in 1999. On the other hand, the food group accounted for 1.78 percentage points of the year's overall inflation rate due to its largest weight of 34.9% in the CPI basket as well as the high increase of 4.6% in food prices in 1999. The higher prices observed for food consumed at home (4.8%) and food away from home (4.3%) reflected mainly shortages in supplies. These shortages led to stronger increases in prices of most domestic as well as imported essential food items, except sugar and oil and fats, while the price of meat declined. The price increase was most pronounced for fish, at 10.8%.

The medical care and health expenses index increased by 3.1%, but the group's weight in the CPI basket is small (1.9%). More moderate price increases, ranging between 2.6% and 0.5% were recorded for the remaining groups, while prices of clothing and footwear declined by 2%. Prices of gross rent, fuel and power; and transport and communication; the other two sub-groups in the CPI basket with large weights (21.1% and 17.9% respectively), increased by 1.6% and 0.5% respectively. Within the transport and communication category, the increase was on account of increases in prices of transport while charges for all items under the communication category remained stable. The increase in transport charges arose from increases in toll rates effective March 1999, bus and taxi fares and other transportation charges. The impact of these increases were mitigated to some extent by stable prices for railway, ship and airline fares.

The **Producer Price Index** (PPI, 1989=100), which measures prices of both intermediate and final goods charged by domestic producers and paid by importers in the country, declined by 3.3% in 1999, compared with an increase of 10.7% in 1998. The decline was on account of lower import prices (–0.6%) as well as lower local production costs (–3.9%). In 1999, producers paid lower prices for most imported commodities, which more than offset the higher prices paid by producers to import beverages and tobacco; chemicals and related products and other miscellaneous manufactured items. In the case of local production, costs declined for most items, particularly animal and vegetable oils and fats, which more than offset higher costs for mineral fuels, lubricants and related materials; beverages and tobacco; chemicals and related products and other miscellaneous manufactured articles. On a monthly basis, the decline in the PPI was evident in all months of the year except in December, when it rose marginally by 1.9%. Significantly higher increases in prices of mineral fuels, lubricants and related materials, a trend observed since July 1999 due mainly to increases in world oil prices, could no longer offset the lower declines in the prices of animal and vegetable oils,

Table 1.26
Inflation Indicators

	Weights	1997	1998	1999
		Annual change (%)		
Consumer Price Index (1994=100)	**100.0**	**2.7**	**5.3**	**2.8**
Of which:				
Food	34.9	4.1	8.9	4.6
Beverages and tobacco	3.6	1.3	4.3	7.9
Clothing and footwear	3.6	–0.5	0.4	–2.0
Gross rent, fuel and power	21.1	3.2	4.4	1.6
Furniture, furnishings and household equipment and operation	5.6	0.1	3.9	1.3
Medical care and health expenses	1.9	3.6	6.2	3.1
Transport and communication	17.9	0.6	–0.1	0.5
Recreation, entertainment, education and cultural services	5.8	0.4	3.3	2.6
Miscellaneous goods and services	5.6	4.6	7.1	1.5
Consumer Price Index (1989=100) by Region				
Peninsular Malaysia	100.0	2.8	5.5	2.9
Sabah	100.0	2.0	4.3	2.4
Sarawak	100.0	1.7	4.2	1.6
Producer Price Index (1989=100)	100.0	2.7	10.7	–3.3
Of which:				
Local Production	79.3	2.5	11.2	–3.9
Imports	20.7	2.8	9.2	–0.6
House Price Index (1990=100)		1.9	–9.4	–12.0[1]
By region:				
Klang Valley		4.4	–14.5	–10.2
Johor Bahru		0.1	–25.3	–8.7
Penang Island		4.3	–12.9	–8.2

[1] January - June.
Source: Department of Statistics
Valuation and Property Services Department

such as palm oil. If prices of animal and vegetable oils and fats are excluded, the adjusted PPI would show an increase of 2.1% in 1999.

As inflationary pressures arose mainly from supply constraints in the food sector, the Government continued with measures to encourage local food production in addition to diversifying sources of imports for food. In the 2000 Budget, the Government announced that paddy production would be increased through productivity gains derived from a more efficient use of agriculture resources. The Government also undertook to provide new land for agricultural activities, especially for vegetable and fruit cultivation and to encourage greater consumption of local produce. As a short-term measure to increase the supply of food and also to contain the price of food, import duties on 43 categories of food products were abolished, while import duties on another 136 categories of food products were rationalised in the 2000 Budget. Meanwhile, the Ministry of Domestic Trade and Consumer Affairs, using the provisions under the Price Control Act 1946 and Control of Supplies Act 1961, continued with various on-going programmes to ensure adequate supplies of essential goods. Contrary to general perceptions, these programmes were not designed to control prices, but to curb unjustified excessive increases in prices. Of significance is the programme where the Ministry monitors 233 essential items by surveying their prices at 34 centres on a weekly basis. Through this programme, the Ministry is able to anticipate problems and take pre-emptive action.

Asset prices showed mixed trends in 1999. Overall, property prices continued to decline, while share prices increased. The **Malaysian House Price Index** (MPHI) indicated a further decline of 12% in the first half of

1999, after declining by 9.4% in 1998. As part of efforts to clear the existing backlog of properties so as to stimulate new economic activities, various measures were taken both to prevent new supply adding onto the backlog as well as to encourage demand for the existing stock of properties. In this context, effective 6 January 1999, banking institutions were not allowed to finance the development of new residential properties and shop houses where the individual units cost more than RM250,000 each. The guideline, however, did not affect financing for projects already commenced and also new applications for financing of existing projects where construction had already started. The guideline also did not affect end financing for the purchase of both residential and non-residential properties, which have been completed and those already under construction. To clear the backlog of houses not sold, a Second Home Ownership Campaign was held from 29 October to 7 December 1999. Sales under this campaign were exempted from stamp duty on the instruments of transfer, while developers and banks provided discounts and lower lending rates respectively. In addition, in the 2000 Budget, the Government also relaxed various terms of the Treasury Housing Loan Scheme for civil servants.

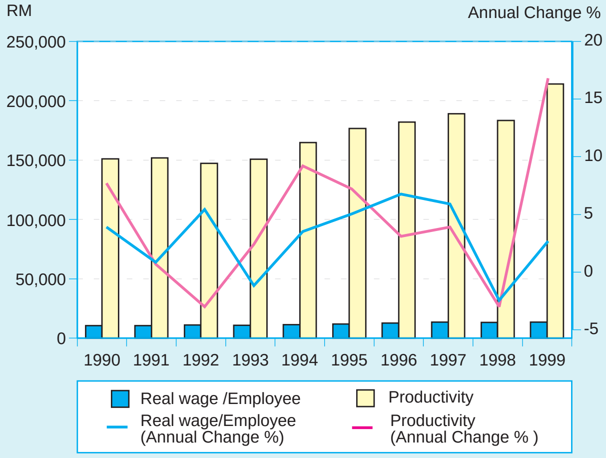
As a result of all these measures, indications are that property prices stabilised in the second half of 1999 but still remained below the pre-crisis levels. In selected choice locations, particularly in the Klang Valley, indications are that property prices increased compared to a year ago. To ensure orderly longer-term planning in the property sector, the Government also established the National Property Information Centre under the Valuation and Property Services Department to set up a database on the property sector. In the stock market, the clear evidence that the economic recovery was gaining momentum led to improved market confidence on the Kuala Lumpur Stock Exchange (KLSE). This was reflected in the strengthened performance of the KLSE, where the KLSE Composite Index gained 226.2 points or 38.6% to end the year at 812.3 points. Compared with the lowest level of 262.7 points on 1 September 1998, the gain was even more significant at 549.6 points or an increase of 209.2%.

Labour Market Developments

The labour market situation improved in 1999 underpinned by the recovery in domestic economic activities. The demand for labour picked up during the year, with the latest estimates showing an increase in employment by 1.7% or 144,000 persons to total 8.7 million workers as at end-1999 (1998: –2.5%). At the same time, the labour force increased at a slower rate of 1.5% to 9 million persons. Consequently, the unemployment rate declined further from 3.2% in 1998 to 3% in 1999, well below the full employment rate of 4%. Although job vacancies were almost three times the number of workers retrenched, wage pressures remained subdued. Overall, labour productivity improved due to rationalisation of operations undertaken during the downturn of the economy. However, unlike the years of high growth during 1995-97, the improvement in wages did not exceed productivity growth.

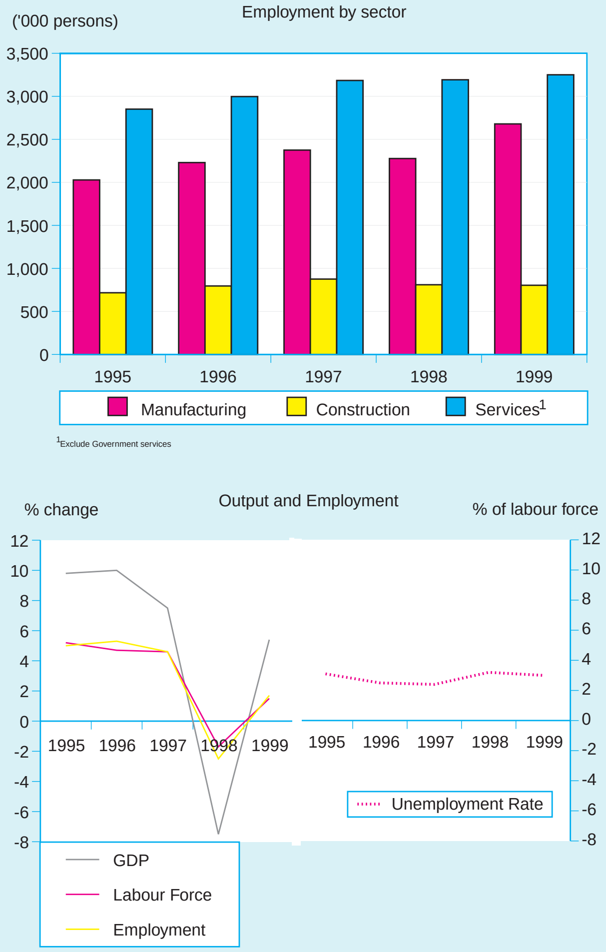
In 1999, the manufacturing sector accounted for the major share of new workers employed (70.8% or 102,000 persons), thus raising its share of total employment to 27.2% from 26.5% in 1998. Within the manufacturing sector, the new jobs created were concentrated mainly in the assembly and labour-intensive industries (such as wood and wood products; electrical machinery; rubber products; and textiles), and to a lesser extent, the crude oil refinery industry. The services sector, which accounted for 47.2% of total employment, recorded a moderate increase in employment by 1.5% or 60,000 workers to 4.1 million persons. The wholesale and retail trade, hotels and restaurants and transport and communication sub-sectors accounted for 21.7% and 11.7% respectively of the increase in employment in the services sector, while the utilities, financial and Government services sub-sectors accounted for about 3% each. More than half of

Graph 1.38
Productivity and Real Wage per Employee in the Manufacturing Sector



Source: Department of Statistics
Bank Negara Malaysia

Graph 1.39
Labour Market Conditions



the increase in total employment in the services sector were provided by the miscellaneous or other services sub-sector. While employment in the finance, insurance and commerce sub-sector remained stable at 420,000 persons, employment in the banking sector declined (–4.5% to 92,360 persons) due partly to the ongoing consolidation exercise, particularly the merger of finance companies. This decline was offset by the increase in employment in business services. Meanwhile, employment in the agriculture and construction sectors continued to decline, albeit at a slower rate of 0.9% and 0.7% respectively (–4.6% and –16.8% respectively in 1998).

With the recovery in both export and domestic activities, demand for labour as reflected by the number of job vacancies reported to the Manpower Department increased during the year. The total number of job vacancies reported throughout the country increased by 45.2% to 108,318 vacancies in 1999 compared with 74,610 in 1998. The number of vacancies could have been higher as it is not compulsory for firms to report job vacancies to the Manpower Department. Job vacancies in the manufacturing sector increased further by 26.9%, accounting for 61.1% of the total number of job vacancies reported in 1999. Of significance, the job vacancies reported in the agriculture sector rose markedly from 5,231 vacancies in 1998 to 24,263 vacancies in 1999, reflecting partly the expansion in agriculture sector activities particularly in Sarawak. However, the number of job vacancies in the services sector declined. This decline prevailed in all the sub-sectors except the finance, insurance, real estate business services and transport, storage and communication sub-sectors. Hence, the services sector's share of total job vacancies declined to 13.6% in 1999 (1998: 20%).

Table 1.27
Job Vacancies and Retrenchment in 1999

	Job Vacancies[1]		Retrenchment	
		Number	% Share	Number
% Share Total	108,318	100.0	37,357	100.0
Agriculture, forestry and fishing	24,263	22.4	3,816	10.2
Mining and quarrying	91	0.1	473	1.3
Manufacturing	66,174	61.1	20,485	54.8
Construction	3,036	2.8	2,869	7.7
Services	14,754	13.6	9,714	26.0
Wholesale and retail trade, hotel and restaurant	*4,864*	*4.5*	*4,320*	*11.6*
Finance, insurance, real estate and business services	*3,595*	*3.3*	*2,789*	*7.5*
Transport, storage and communication	*1,666*	*1.5*	*690*	*1.8*
Electricity, gas and water	*42*	*0.1*	*99*	*0.3*
Social and private services	*–*	*–*	*1,776*	*4.7*
Other services	4,587	4.2	40	0.1

[1] The number of job vacancies could have been under-reported as it is not compulsory for firms to report vacancies to the Manpower Department.

Source: The Ministry of Human Resources
Manpower Department

As selected firms within the agriculture, construction and manufacturing sectors continued to face labour constraints, the Government approved the intake of another 84,150 foreign workers in 1999 to ensure that business expansion is not affected by labour shortages. Nevertheless, Malaysia's dependence on foreign labour was reduced as the number of registered foreign workers continued to decline to 697,219 workers, from 781,548 workers in 1998 (peak of 1.2 million workers in 1997). The number of foreign workers employed in the agriculture sector remained high, increasing by 33.6% to account for 37% of the total foreign workforce (excluding domestic services). In the other major sectors of the economy, the number of foreign workers declined. In terms of origin, 92% of the total foreign workforce were from Indonesia and Bangladesh.

With improving economic and financial conditions, the number of workers retrenched declined during the year. The number of workers retrenched in 1999 declined significantly by 55.5% to 37,357 workers from 83,865 workers in 1998. To some extent, retrenchments were lower because employers were able to implement flexible labour market practices including part-time, flexi-time and pay cuts before resorting to retrenchment. In 1999, about 400 employers implemented pay cuts involving 15,017 workers (August-December 1998: 795 employers involving 22,514 workers). Lower retrenchments were recorded across the board among the major sectors of the economy. In the manufacturing sector, the majority of the workers retrenched were mainly from the fabricated metal, machinery and equipment, chemicals and petroleum products industries, while the wholesale and retail trade, hotel and restaurant sub-sector accounted for the largest share of workers retrenched in the services sector. The main reasons cited for retrenchment were the decline in demand (45%; 1998: 52.2%), closure of company (11%; 1998: 6.4%) and restructuring of companies (12.9%; 1998: 8.1%).

In an environment of excess capacity, wage pressures remained subdued in 1999 despite the pick-up in economic activity. While signs of upward adjustments were observed in the second half-year in the manufacturing sector, real wages rose only moderately for 1999 as a whole:

- The findings of the survey conducted by the Malaysian Employers Federation (MEF) showed that private sector salary increases had slowed down further to 5.9% in 1999, from 6.2% in 1998 and 8.9% in 1997.

- Information collected by the Ministry of Human Resources showed that about 1,195 employers implemented pay cuts involving 37,531 workers in the period August 1998 to end-December 1999.

- The weighted average wage of the three-year collective wage agreements, covering 133,000 workers in the private sector or about 2% of the total workforce in the country, declined by 8.8% in 1999 (1998: +9.6% and 1997: +8.9%). In particular, wages declined significantly by 19.5% in the agriculture sector and 8.5% in the mining sector. The decline was less pronounced in the manufacturing and electricity sectors (–1.1% and –0.8% respectively). The commerce and transport sectors were the only sectors in which wages increased, albeit moderately.

- While most of the indicators on wages pointed to a downward trend in wages, the findings of the Monthly Survey of Manufacturing Industry conducted by DOS showed that wage per employee picked up in the second half-year to increase by 7.5% from a more moderate increase of 3.3% in the first half of 1999 (first half and second half of 1998: 4.8% and 0.7% respectively). Consequently, for the year as a whole, wage per employee increased by 5.5% in 1999, compared with 2.7% in 1998. In real terms, average wages increased by 2.7% in 1999 (1998: –2.4%) compared to the 3.7% increase in labour productivity for the country as a whole.

The number of strikes declined to 11 in 1999 (1998: 12). However, the number of workers involved in strikes doubled to 3,452 workers in 1999 (1998: 1,778 workers), thus raising the number of man-days lost due to industrial actions to 10,555, from 2,685 in 1998. The main causes of strikes were attributable to disputes over terms and conditions of employment (six cases); dismissal, retrenchment and layoffs of workers (one case); and disputes over other issues (four cases). The strikes occurred only in the agriculture and manufacturing sectors. In the agriculture sector, five cases of strikes involving 1,283 workers were recorded, compared with three cases involving only 435 workers in 1998. A higher number of strikes was also recorded in the manufacturing sector with six cases involving 2,169 workers against four cases involving 482 workers a year ago. The 11 strikes that occurred in 1999 were settled mainly through Government intervention and conciliation efforts.

In 1999, the number of workers involved in disputes reported to the Industrial Relations Department declined to 90,278 (1998: 93,530 workers) although the number of industrial disputes increased to 496 cases from 442 cases in 1998. The bulk of the disputes centred on issues relating to terms and conditions of employment (242 cases) and deadlock in the process of collective bargaining (138 cases). On a sectoral basis, the increase in the number of disputes was mainly in the services sector (200 cases), followed by agriculture (73 cases), mining (12 cases) and construction (five cases). The number of industrial disputes in the manufacturing sector declined to 206 cases involving 46,414 workers from 216 cases involving 49,146 workers in 1998.

The supply and demand situation in the labour market over the last two years clearly demonstrate the importance of enhancing the level of productivity. This in turn is influenced by the availability of an adequate supply of workers with appropriate skills and who are willing to move to areas of employment opportunities. Recognising this, the Government introduced several measures during the year, to address the issues of enhancing labour mobility and training. The Ministry of Human Resources had organised labour mobility programmes to increase labour mobility from surplus to deficit areas. In relation to this, work has begun on the implementation of the Electronic Labour Exchange to effectively mobilise workforce and integrate labour market information. The project is expected to be completed by end-2000.

In addition to enhancing labour mobility, the Government also took the lead to promote the use of productivity-linked wages and to encourage training activities through budget allocations as well as through the use of fiscal incentives. The Government launched the implementation of the guidelines on productivity-linked wage system, approved by the National Labour Advisory Council on 1 August 1996. A series of seminars were organised to disseminate information to employers and unions on the implementation of the guidelines. In addition, several fiscal incentives were provided in the 2000 Budget to promote human resource development to enhance productivity of the labour force:

- An allocation of RM14.1 billion was provided to finance education programmes and to develop quality infrastructure for education. With this allocation, the intake of students into local universities is expected to increase to 99,482 students in 2000.

- The Government has also allocated RM1.2 billion to build and equip facilities in existing training institutions.

- Private institutions of higher learning were required to contribute to the Human Resources Development Fund (HRDF). The main aim is to upgrade the quality of the teaching staff. Private institutions of higher learning are given a 95% reimbursement for staff training in the field of medicine, engineering and computer science.

In 1999, the Government continued to emphasise on industrial training to meet the increasing demand for skilled manpower. In this regard, the new intake of trainees in the existing nine Industrial Training Institutes increased further by 22.5% to 3,479 trainees (1998: 2,839 trainees), while the Centre for Instructors and Advance Skill Training (CIAST) provided training for 1,796 new instructors. In addition, the three existing bilateral training centres, namely, the German Malaysian Institute (GMI), Malaysian French Institute (MFI) and British Malaysian Institute (BMI) recruited 1,134 trainees in 1999.

In 1999, a total of 247,785 training places were approved with financial assistance of RM106 million for retraining and skills upgrading of the workers for companies registered with the Human Resources Development Council (HRDC), which administers the HRDF. The HRDF was set up under the Human Resources Development Act 1992, to ensure companies train and retrain and upgrade the skill of their workers through a compulsory contribution of 1% of the monthly wage bills to the Fund. Meanwhile, the Government provided a matching grant of RM2 for each RM1 contributed by small- and medium-scale employers with a workforce of between 10 and 49 people and a paid-up capital of less than RM2.5 million.

Since its inception in 1993, the HRDC has approved a total of 2.3 million training places with total financial assistance of RM706 million. With the onset of the economic crisis, the Government allocated RM5 million for implementing the Training Scheme for Retrenched Workers in May 1998 to retrain retrenched workers. In 1999, 426 participants benefited from this scheme with financial assistance of RM2 million. As at December 1999, 988 participants had benefited from this scheme with financial assistance of RM4.5 million.

During the crisis period, employers facing financial problems were given exemption from contributing to the HRDF. This exemption was extended for the third time, for a period of six months beginning from 11 February to 12 August 1999. The final exemption for the six-month period beginning 12 August 1999 to 11 February 2000 was only extended to the hotel industry and in-bound travel agency sector. The HRDF collection from the levy was higher, amounting to RM83.7 million in 1999 (RM61 million in 1998) despite the exemption given to companies affected by the economic crisis. As at end-December 1999, the number of employers registered with the HRDF rose to 6,352 employers, of which 78% were from the manufacturing sector, while another 22% were from the services sector.

In addition to the existing schemes, the HRDC also plans to introduce four Apprenticeship Schemes in 2000 including apprenticeship schemes for multimodal transport operators, plastic injection moulding, tool and die machining and the wood-based (furniture) industry. As part of an effort to provide quality services, the HRDC will launch the Human Resource Development Network (HRNet) to allow consumers and, in particular, employers registered with the HRDF, to gain direct access to latest information via the internet.

2 Monetary and Fiscal Developments

Monetary Developments

Monetary developments in 1999 reflected the policy measures introduced during the year as well as developments in the domestic real and financial sectors. Monetary policy in 1999 continued to focus on supporting economic recovery while maintaining price stability. Following progressive easing of monetary policy since August 1998 coupled with large trade inflows amid sluggish domestic private investment, liquidity conditions eased in 1999. Consequently, with the absence of inflationary pressures, interbank and lending rates were allowed to ease during the course of the year.

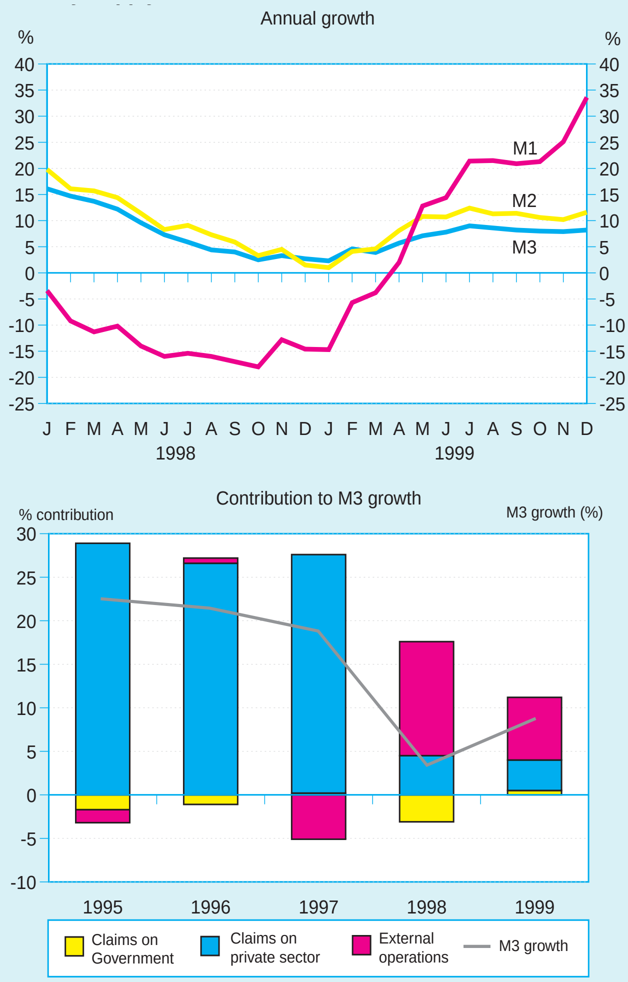
The strong economic performance and large trade surplus as well as the accommodative monetary policy stance resulted in an expansion of all **monetary aggregates** in 1999. Narrow money, M1, which had recorded a sharp decline in the previous year and in the first quarter of 1999, turned around to record a positive growth in April and rose sharply thereafter to 33.6% as at end-December 1999 (end-1998: –14.6%). Similarly, the broader monetary aggregates, M2 and M3, also accelerated, albeit at a slower pace, to record an annual growth rate of 11.6% and 8.2% respectively at the end of 1999 (1998: 1.5% and 2.7% respectively). Overall, the performance of the broad monetary aggregates was consistent with the monetary policy objective of providing adequate liquidity to finance real output expansion while ensuring price stability.

During the year, M3 increased by RM33.1 billion (RM10.6 billion in 1998) to RM434.6 billion at the end of 1999. In terms of components, demand for transaction balances (currency holdings and demand deposits of the private sector) increased significantly by RM18.3 billion during the year (–RM8.9 billion in 1998), reflecting the strengthening momentum in economic and stock market activities. In addition, the private sector also increased their holdings of transaction balances during the year, as the opportunity cost of holding non-interest-bearing deposits became lower with the prevailing low interest rates. To some extent, there was also a shift into higher currency holdings due to Y2K concerns, particularly in December 1999.

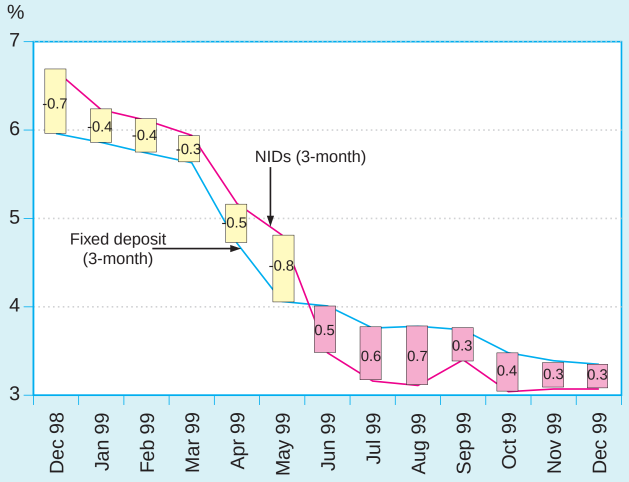
Reflecting the preference for transaction balances, broad quasi-money (private sector holdings of fixed and savings deposits, negotiable instruments of deposits (NIDs) and repurchase agreements (repos) with the banking system) expanded by RM14.7 billion or 4.3% (1998: RM19.6 billion or 6%).

In terms of instruments, fixed deposits, which remained the largest component of broad quasi-money (80.1% of total broad quasi-money as at end-1999) recorded an increase of RM29.9 billion or 11.5% in 1999 (RM14.9 billion or 6.1% in 1998). In contrast, NIDs, which accounted for a share of 1.6% of broad

Graph 2.1
Money Supply



Graph 2.2
Interest Rate Differential: NIDs vs. Fixed Deposits



quasi-money (1998: 7.6%) declined by RM21.9 billion or 79.1%, reflecting to some extent, the shift in private sector holdings from NIDs to fixed deposits to take advantage of the higher fixed deposit rates vis-à-vis NID rates. Amid an environment of excess liquidity, the weighted average rates of NIDs (3-month or lower) declined at a faster rate (–360 basis points) than the weighted average rate of 3-month fixed deposit (–261 basis points) in 1999. Meanwhile, savings deposits also increased by RM7.9 billion or 24.4% (+RM1.3 billion or 4% in 1998) in line with the higher disposable income of the private sector.

In terms of determinants, the primary source of monetary growth emanated mainly from the large increase in the current account surplus of the balance of payments. During the year, net external assets contributed 7.2 percentage points to M3 growth. Net external reserves of BNM increased by RM17.8 billion reflecting mainly the large surplus in the current and capital accounts of the balance of payments.

The other major contributory factor to monetary expansion was the higher claims on the private sector. During the year, it exerted an expansionary impact on monetary growth by RM14.1 billion, contributing about 3.5 percentage points to M3 growth. This reflected higher financing extended to the private sector (RM13.3 billion) and moderate growth in holdings of private securities (RM888 million).

The Government operations also exerted an expansionary impact on money supply in 1999 (RM2.2 billion) due to higher withdrawal of its deposits placed with BNM and the banking system (RM5.1 billion). These withdrawals were mainly to finance Government expenditure and also for domestic loan redemptions. Most of the funds withdrawn were sourced mainly from the surplus funds in 1998 and loan proceeds, including MGS issuance during the year, as well as the Government Global Bond. Nevertheless, holdings of Government securities by banking institutions declined by RM2.9 billion, partially offsetting the expansionary impact from the withdrawal of Government's deposits.

Reflecting the improved economic activity, **total loans outstanding** (including loans sold to Danaharta and Cagamas, write-offs of bad debts and conversion of loans into equity) increased by RM9.1 billion or 2.1% in 1999. Commercial banks and merchant banks

Table 2.1
M3 Determinants

	Outstanding		Change		Annual Growth	
	1998[1]	1999[2]	1998[1]	1999[2]	1998[1]	1999[2]
	RM billion				%	
M3	401.5	434.6	10.6	33.1	2.7	8.2
Of which:						
Net claims on Government	–21.0	–18.8	–12.3	2.2	–140.9	10.3
Claims on private sector[3]	465.3	479.4	17.7	14.1	4.0	3.0
Net external assets	94.6	123.6	51.2	29.0	117.6	30.6
Net other influences	–137.4	–149.6	–45.9	–12.2	–50.2	–8.9

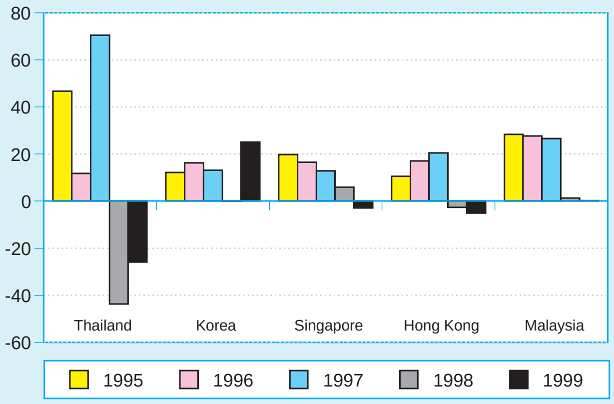
[1] Effective 15 September 1998, following the fixing of the ringgit/United States dollar exchange rate at RM3.80, all foreign currency assets and liabilities have been revalued into ringgit at rates of exchange prevailing on the reporting date. Therefore, part of the increase in the external assets reflected BNM's exchange revaluation gains. The revaluation gains of BNM were also reflected in other influences.
[2] Effective 1 January 1999, all foreign currency assets and liabilities were only revalued at the end of each quarter.
[3] Includes write-offs and loans sold to Danaharta.

recorded an annual increase of 4.8% and 0.3% respectively, while finance companies recorded an annual contraction of 6.4%, partly due to several absorptions of finance companies by the commercial banks that took place in 1999. During the year, the banking institutions increased their holdings of PDS by RM2.9 billion. Including these holdings of PDS, total financing provided by the banking system increased by RM12.1 billion or 2.8% in 1999.

It has been observed that loans have increased with a lag in the initial stage of the economic recovery. Such a phenomenon was apparent in most of the regional economies. Following the crisis and the subsequent restructuring of the banking sector, loan performance in Hong Kong SAR and Singapore declined by 5.1% and 2.9% respectively in 1999 (1998: –2.7% and +5.9% respectively), even though GDP had recovered to increase by 2.9% and 5.4% respectively. In the case of Thailand, the decline was larger at –26% (–43.7% in 1998). In Korea, loans however, increased strongly by 25% in 1999 (–0.1% in 1998) reflecting the strong economic recovery in Korea since the first quarter of 1999.

In Malaysia, total loans outstanding rose moderately in 1999, as the strong loan disbursements were almost matched by the high loan repayments. As such, for 1999, loan disbursements and approvals rather than loans outstanding, provided a better indication of the financing role of the banking system in supporting economic recovery. In this regard, disbursements of loans increased substantially by 28.7% to RM323.2 billion in 1999, with a monthly average of RM26.9 billion compared with RM20.9 billion in 1998. Similarly,

Graph 2.3
Loan Growth: Selected Countries



Source: Datastream.

loans approved rose by 61% to RM104.8 billion or a monthly average of RM8.7 billion (a monthly average of RM5.4 billion in 1998). However, the high disbursements during the year were virtually matched by loan repayments for several reasons:

- In the early part of the year, sluggish economic activity and excess capacity in some industries, as well as uncertainties about the prospects for the economy contributed to slow loan demand. Businesses tended to use their surplus cash to repay their loans and reduce their leverage rather than expand operations.

- During the year, several corporations borrowed to meet short-term working capital needs as opposed to borrowing long-term for new investments in view of the excess capacity. This practice resulted in a high turnover of disbursements and repayments but was not reflected in the level of loans outstanding.

- As the economy recovered during the course of the year, many borrowers took the opportunity to repay their loans following an improvement in business conditions as well as higher earnings of individuals and business enterprises. Meanwhile, a number of corporations refinanced their bank borrowings by raising funds in the PDS market to take advantage of the more competitive interest rates prevailing in the PDS market as well as the ability to borrow long-term on a fixed rate basis.

Consequently, due to the high repayments of loans (+24% to RM335.6 billion or a monthly average of RM28 billion compared with a monthly average of RM22.5 billion in 1998), total loans outstanding did not reflect the actual strength of credit expansion in 1999. Nevertheless, the increased repayment of loans and increased recourse to the PDS market, are positive developments as it reduces risk of potential loan defaults as well as over dependence on the banking system, particularly for long-term financing.

By sector, loans disbursed generally reflected the performance of the various sectors. Loans disbursed were higher to nearly all sectors. Disbursements were lower in the mining and quarrying sector; finance, insurance and business services; and for the purchase of securities. Loans disbursed to the manufacturing sector, which led the economic upswing, was the highest, amounting to RM85 billion

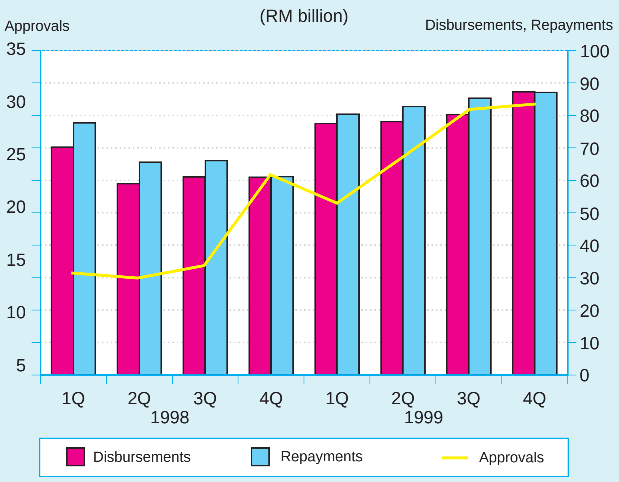
Table 2.2
Banking System: Loans Outstanding by Sector

	As at end		Change	Share of total
	1998	1999	1999	1999
	RM million			%
Agriculture, hunting, forestry and fishing	7,816.2	9,183.8	1,367.5	2.1
Mining and quarrying	1,685.3	1,579.5	–105.9	0.4
Manufacturing	65,133.5	66,074.9	941.4	15.5
Electricity, gas and water	5,854.1	7,087.9	1,233.9	1.7
Wholesale, retail, restaurants and hotels	35,759.9	36,321.7	561.8	8.5
Broad property sector	149,612.7	153,954.0	4,341.3	36.0
Construction	*45,091.7*	*43,108.7*	*–1,983.0*	*10.0*
Purchase of residential property	*56,450.4*	*63,348.5*	*6,898.0*	*14.8*
Purchase of non-residential property	*30,958.5*	*28,978.1*	*–1,980.3*	*6.8*
Real estate	*17,112.1*	*18,518.7*	*1,406.6*	*4.3*
Transport, storage and communication	15,210.9	15,532.0	321.1	3.6
Finance, insurance and business services	38,023.8	33,357.2	–4,666.7	7.8
Consumption credit	49,491.7	50,242.1	750.5	11.8
Purchase of passenger cars	*30,831.7*	*30,029.6*	*–802.0*	*7.0*
Purchase of securities	37,943.5	33,996.2	–3,947.3	8.0
Purchase of transport vehicles	4,504.8	1,966.9	–2,537.9	0.5
Community, social and personal services	6,686.3	7,068.5	382.2	1.7
Others	8,845.0	11,326.6	2,481.6	2.7
Total loans outstanding[1]	**426,567.7**	**427,691.2**	**1,123.5**	**100.0**
Plus: Write-offs and conversions	3,152.4	11,169.9	8,017.5	
Total loans outstanding	**429,720.1**	**438,861.1**	**9,141.0**	
Plus: Holdings of PDS	5,918.3	8,851.2	2,932.8	
Total financing	**435,638.4**	**447,712.3**	**12,073.9**	

[1] Including loans sold to Cagamas and Danaharta.

(1998: RM68.7 billion) accounting for 26.3% of total loans disbursed during the year. A significant share of loans was also disbursed to the wholesale, retail, restaurants and hotels and the broad property sectors with total disbursements of RM57.7 billion and RM57 billion respectively. The bulk of the loans disbursed to the broad property sector were to the construction sector and for the purchase of residential property. The house ownership campaign organised in 1999 contributed to the higher disbursements for residential property, particularly towards the end of the year. Loans disbursed to the agriculture sector were also higher at RM8.2 billion, as the activity in the sector recovered in 1999. Loans disbursed for the purchase of transport vehicles amounted to RM15.6 billion or 4.8% of total loans disbursed. The bulk of these loans were extended for the purchase of passenger cars which increased to RM12.5 billion.

Graph 2.4
Banking System: Loan Approvals, Disbursements and Repayments



In terms of total loans approved, the bulk of the approvals (55.2%) during the year were for the purchase of residential property, for the manufacturing sector, purchase of transport vehicles and for finance, insurance and business services. A total of RM20.6

Table 2.3
Banking System: Total Loans Approved and Disbursed

Sectors	Loans Approved		Loans Disbursed	
	1998	1999	1998	1999
	RM million			
Agriculture, hunting, forestry and fishing	2,236.2	3,448.2	6,147.8	8,227.7
Mining and quarrying	225.6	197.0	1,918.3	1,483.1
Manufacturing	10,347.7	14,012.1	68,693.1	84,975.4
Electricity, gas and water	926.5	2,187.5	3,141.2	6,275.7
Wholesale, retail, restaurants and hotels	4,869.4	7,630.6	35,858.9	57,716.4
Broad property sector	16,608.6	34,840.8	45,735.4	56,975.3
Construction	*5,668.2*	*7,893.6*	*21,390.3*	*25,600.8*
Purchase of residential property	*9,269.6*	*20,649.5*	*14,235.2*	*17,039.3*
Purchase of non-residential property	*1,670.8*	*3,289.1*	*5,876.0*	*6,307.9*
Real estate	*n.a.*	*3,008.6*	*4,223.8*	*8,027.9*
Transport, storage and communication	3,001.3	3,150.0	7,199.7	8,885.5
Finance, insurance and business services	8,752.4[1]	10,587.0	42,562.4	38,894.6
Consumption credit	4,066.6	5,714.2	11,659.0	17,111.9
Purchase of securities	3,998.7	5,276.9	9,833.5	9,655.5
Purchase of transport vehicles	5,876.6	12,619.2	6,097.2	15,637.1
of which: Purchase of Passenger Cars	*n.a.*	*11,055.3*	*n.a.*	*12,510.8*
Community, social and personal services	760.5	2,004.3	3,039.3	5,106.6
Others	3,453.8	3,135.8	9,240.8	12,224.2
Total	**65,123.9**	**104,803.7**	**251,126.5**	**323,169.0**

[1] Includes real estate.

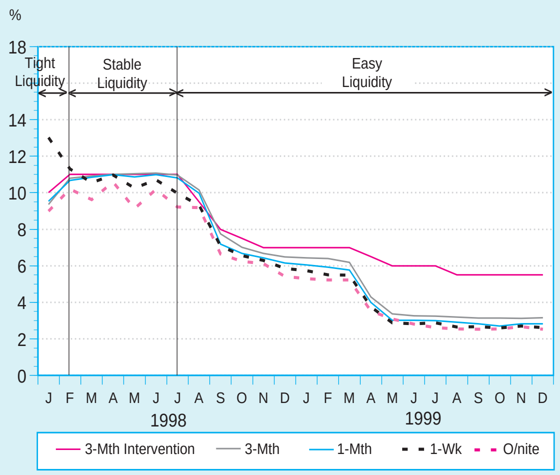
billion of new loans had been approved for the purchase of residential property, which accounted for 19.7% of total loans approved in 1999. Loans approved to the manufacturing sector and for the purchase of transport vehicles amounted to RM14 billion and RM12.6 billion respectively, accounting for 13.4% and 12% respectively of total new approvals during the year. Loan approvals for finance, insurance and business services amounted to RM10.6 billion or a share of 10.1% of total loans approved.

During the year, a total of RM21 billion of NPLs were sold to Danaharta. The bulk of the NPLs sold to Danaharta were loans to the broad property sector (35% of total loans sold), in particular, the construction sub-sector; manufacturing sector (17%); and for the purchase of securities (15.6%). As at the end of 1999, Danaharta had acquired and managed a total of RM34 billion worth of NPLs from the banking system or 42% of total NPLs of the banking system.

Several adjustments were made during the year to ensure the effectiveness of the special funds established by the Government. In tandem with the lower interest rate levels, the funding rates and maximum lending rates for funds administered by Bank Negara Malaysia were reduced. With effect from May 1999, funding rates for the Fund for Small and Medium Industries and the Special Scheme for Low and Medium Cost Houses were reduced from 6% to 4% per annum with the maximum lending rate being concurrently reduced from 8.5% to 6.5% per annum. In the case of the New Entrepreneurs Fund, the funding rate was reduced from 6% to 4% per annum, while the maximum lending rate was reduced from 8% to 6% per annum. Due to its weak performance, the Industrial Adjustment Fund (IAF) and the Special Scheme for Low and Medium Cost Houses (SLMCH) were terminated with effect from 4 August 1999. The allocation under the Rehabilitation Fund for Small and Medium Industries (RFSMI) was also reduced to RM500 million from RM750 million previously. To ensure the effective utilisation of the Government financial resources, the unutilised portions of the IAF and the SLMCH, as well as the RM250 million withdrawn from the RFSMI were channelled into the Fund for Small and Medium Industries which had a higher utilisation rate.

Interest rate movements in 1999 exhibited a downward trend reflecting the easing of monetary policy since August 1998 as well as the excess liquidity in the banking system. The outstanding resource surplus of the banking system increased from RM37 billion at end-1998 to RM71.2 billion at end-1999. With the inflation outlook remaining subdued and given the monetary policy objective to support the economic recovery, the BNM 3-month intervention rate was further

Graph 2.5
Interbank Rates (average for the month)



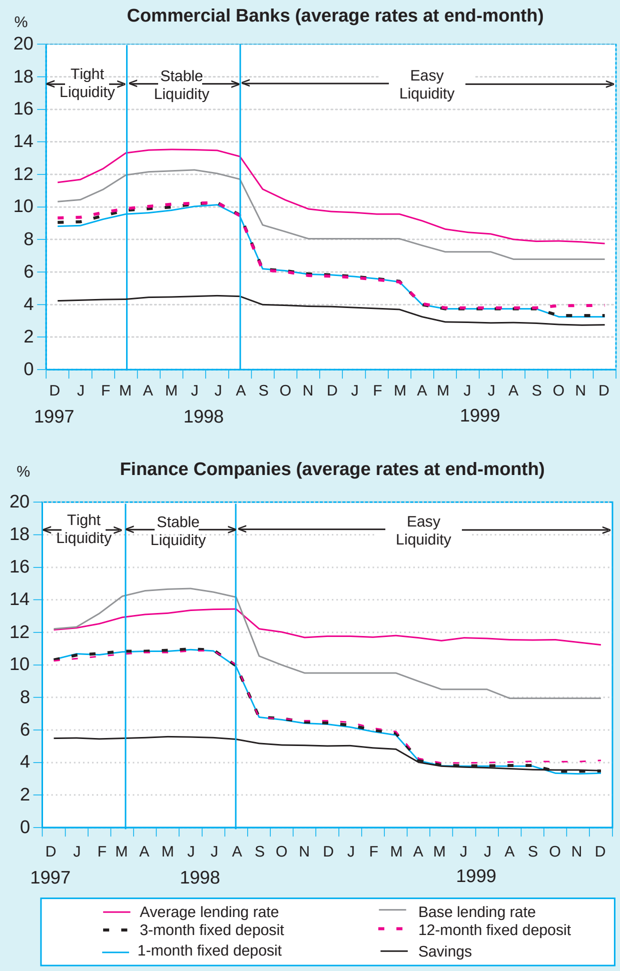
lowered in three steps during the year: from 7% to 6.5% on 5 April, to 6% on 3 May, and to 5.5% on 9 August (see Graph 2.5). These reductions in the policy rate resulted in a reduction of lending rates across the banking industry. However, with the larger amount of excess liquidity in the banking system, the decline in the interbank money market rates was significantly more than the reduction of the intervention rate. On the whole, while the intervention rate fell by 150 basis points in 1999, the 3-month interbank rate fell by 328 basis points from 6.46% at end-1998 to 3.18% at end-1999. To ensure that real interest rates remained positive, BNM conducted operations in the interbank money market to absorb part of the excess liquidity.

Retail interest rates of the banking institutions also trended downward in 1999. During the year, the average base lending rates (BLRs) fell to a historically low level. The average BLR of the commercial banks and finance companies declined in April, May and August in step with the reductions in BNM's intervention rate (see Graph 2.6). For commercial banks, the BLR fell by 40 basis points on each occasion to 7.64% at end-April and to 7.24% at end-May. In August, the commercial banks' BLR fell by another 45 basis points to 6.79% and has since remained unchanged. This level is equivalent to the historical low recorded in November 1994. For the finance companies, their BLR fell by 50 basis points on each occasion to 9% at end-April and 8.50% at end-May. In August, it fell by another 55 basis points to 7.95% and has since remained unchanged, surpassing the historical low of 8.40% recorded in December 1994.

Table 2.4
Changes to BNM Intervention Rate and SRR Ratio

Period		Liquidity	Date	Intervention Rate	SRR Ratio
1997			End-Dec	8.70	13.50
1998	Jan-Feb	Tight	9 Jan 20 Jan 6 Feb	9.00 10.00 11.00	
	Mid-Feb -Jul	Stable	16 Feb 1 Jul		10.00 8.00
	Aug-Dec	Easy	3 Aug 10 Aug 27 Aug 1 Sep 3 Sep 16 Sep 5 Oct 9 Nov	10.50 10.00 9.50 8.00 7.50 7.00	 6.00 4.00
1999	Jan-Dec		5 Apr 3 May 9 Aug	6.50 6.00 5.50	

Graph 2.6
Interest Rates of Banking Institutions



Monetary Measures in 1999

Monetary measures implemented in 1999 reflected the continued accomodative monetary policy stance to strengthen economic recovery while maintaining monetary and financial stability. To build upon the earlier measures introduced in 1998, several measures were introduced in 1999 to stimulate domestic spending as well as to ensure that credit continued to be channelled for productive purposes. These measures were as follows:

- To ensure that there were sufficient funds to finance the economic recovery process, banking institutions with the capacity to lend continued to be encouraged to achieve a minimum annual loan growth of 8% by the end of 1999.

- In view of the need to clear the backlog of properties, **effective 6 January,** banking institutions were **not allowed to finance the development of residential properties and shop houses where the individual unit costs more than RM250,000 each**. In addition, banking institutions were not allowed to provide financing to develop hotels, resorts, office buildings, golf courses, clubs and shopping complexes. This prohibition would be applicable under the following circumstances:

  i) Where applications for credit facilities to finance the development of properties costing above RM250,000 had yet to be approved; and

  ii) Where approval had already been given, banking institutions were only permitted to disburse loans to complete the current phase of development subject to project viability. For subsequent phases, banking institutions were only allowed to finance the construction of properties costing RM250,000 and below.

  However, the guideline would not affect end-financing for the purchase of both residential and non-residential properties which had been fully completed as well as those currently under construction. Banking institutions were in fact encouraged to extend end-financing credit. Similarly, financing for the development of projects that had commenced and new applications to complete existing projects where construction had already commenced would not be affected. The guideline would be applicable only in cases where application for bridging finance facility had yet to be approved by the banking institutions and construction had yet to commence.

- BNM reduced the **3-month intervention rate** by 50 basis points to 6.5% effective **5 April.** The rate was further reduced to 6.0% on **3 May** and to 5.5% on **9 August**. The reduction in the policy rate was to reflect the expectations of lower inflation over the medium term and to allow for further easing of lending rates to support economic activity.

- In tandem with the lower interest rates level, the funding rates and maximum lending rates for **selective funds administered by BNM** were also reduced. With effect from **3 May,** the funding rates for the Fund for Small and Medium Industries (FSMI) and the Special Scheme for Low and Medium Cost Houses (SLMCH) were reduced from 6% to 4% per annum, with the maximum lending rate being concurrently reduced from 8.5% to 6.5% per annum. In the case of New Entrepreneurs Fund (NEF), the funding rate was reduced from 6% to 4% per annum, while the maximum lending rate was reduced from 8% to 6% per annum.

- Due to the low demand for loans under the Industrial Adjustment Fund (IAF) and Special Scheme for Low and Medium Cost Houses (SLMCH), these funds were terminated with effect from **4 August 1999**. In addition, the total allocation under the Rehabilitation Fund for Small and Medium Industries (RFSMI) was reduced from RM750 million to RM500 million. To ensure an effective utilisation of the Government's financial resources, the unutilised portion under the IAF and SLMCH as well as the RM250 million from the RFSMI were reallocated to the Fund for Small and Medium Industries (FSMI), which had a higher utilisation rate.

- Effective **28 July**, the minimum annual income eligibility criterion for **credit cards** was reduced to RM18,000 from the existing RM24,000.
- A total of RM2 billion of **Malaysia Savings Bond Series 02 (BSM 02)** was offered for sale to retirees during the period from 1 November 1999 to 10 November 1999, of which RM1 billion was offered under the Islamic principles. The bonds have a maturity of 2 years with a rate of return of 5.75% per annum, to be paid on a quarterly basis.
- To assist small- and medium-scale Bumiputera entrepreneurs and to provide financing at reasonable cost, Tabung Projek Usahawan Bumiputera (TPUB) with an allocation of RM300 million was established on **10 February 2000.**

The fixed deposits rates of all tenures remained higher than the average rate of inflation of 2.8% throughout 1999. This reflected the policy to maintain positive real rates of return to savers. During the year, the movements of fixed deposit (FD) rates of both commercial banks and finance companies also closely tracked the wholesale interbank rates. Overall, the 3-month FD rates for commercial banks and finance companies declined by 250 and 294 basis points respectively from end-December 1998 to end-December 1999. During the first half of the year, both the interbank rates and the retail FD rates were on a declining trend. However, during the second half-year, in line with the stability in the interbank rates, the FD rates also exhibited greater stability. There was, however, a notable change in the term structure of FD rates in the last quarter of 1999. From being relatively flat for most of the year, the term structure steepened as the longer-term rates increased in October. From a difference of only four basis points between the 1-month and 12-month FD rates of commercial banks at end-September, the differential widened to 71 basis points. The 1-12 month FD rates increased to 3.24–3.95% by end-1999. Similarly, the differential for finance companies also widened to 79 basis points with the 1-12 month FD rates increasing to 3.34–4.13%.

The savings deposit rates for both commercial banks and finance companies also trended downward in 1999, but the decline in the savings rates was smaller than that of the FD rates. For commercial banks, the savings rate declined by 111 basis points from end-December 1998 to end-December 1999. For finance companies, it declined by 151 basis points over the same period.

The interest margins of both the commercial banks and finance companies widened by 91 and 246 basis points respectively during the year. The wider margins were due to the faster reduction of the average cost of funds (ACF) as compared with the average lending rates (ALR). The larger interest margin achieved by finance companies was largely an outcome of a more rapid decline in their ACF as higher-cost deposits and

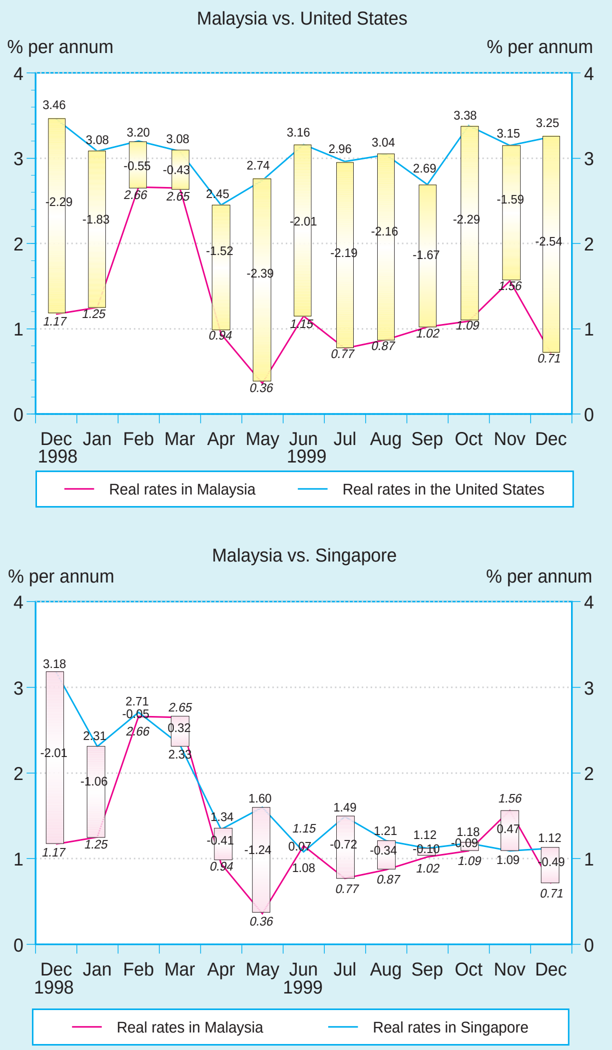
Table 2.5
Interest Rates of Banking Institutions (%)

	As at end	1998	1999	Difference
Commercial Banks	3-Month FD	5.83	3.33	–2.50
	Savings Deposit	3.87	2.76	–1.11
	Base Lending Rate	8.04	6.79	–1.25
Finance Companies	3-Month FD	6.43	3.49	–2.94
	Savings Deposit	5.01	3.50	–1.51
	Base Lending Rate	9.50	7.95	–1.55

Table 2.6
Interest Margins of Banking Institutions (%)

	As at end	1998	1999	Difference
Commercial Banks	Avg. Lending Rate (ALR)	9.72	7.75	–1.97
	Less Avg. Cost of Funds (ACF)	6.17	3.29	–2.88
	Interest Margin	**3.55**	**4.46**	**0.91**
Finance Companies	Avg. Lending Rate (ALR)	11.76	11.23	–0.53
	Less Avg. Cost of Funds (ACF)	7.68	4.69	–2.99
	Interest Margin	**4.08**	**6.54**	**2.46**

Graph 2.7
Real Interest Rate Differentials[1]



[1] Based on the 3-month interbank rates

borrowings matured during the year. Additionally, since the bulk of the finance companies' loans are at fixed rates, their lending rates fell at a slower pace than the predominantly floating lending rates of the commercial banks.

Real interest rate differentials (3-month interbank nominal rates adjusted for inflation) between Malaysia and other countries, notably the United States and Singapore, had generally remained negative during the year. Malaysia's real interest rate differentials with the United States widened towards the end of the year as US nominal interest rates began to edge upwards, while Malaysian nominal interest rates remained largely unchanged. On the other hand, although the interest rate differentials with Singapore remained negative, the gap had narrowed significantly during the year. On a number of occasions, the interest rate differential was in fact positive. The narrowing of the real interest rate differentials with Singapore was primarily reflective of changes in the Consumer Price Index of Singapore, which varied from a deflationary trend in early 1999 to a reversal in the trend in late 1999. The inflation rate in Malaysia, on the other hand, continued to moderate.

Monetary Policy in 1999

In 1999, the basic thrust of monetary policy was to create an environment to support economic recovery and facilitate structural reforms, while preserving price stability. The easing of monetary policy which began in August 1998 was continued into the year. Against an environment of a strengthening financial sector; benign inflationary environment; improving balance of payments position and a more favourable performance of the world economy including the regional economies, monetary policy remained accommodative throughout the year. With the large trade inflows, however, an important task of monetary policy in 1999 was to manage excess liquidity to avoid inflationary pressures. While interest rates were reduced to support economic recovery, Bank Negara Malaysia also ensured a positive real rate of return to depositors.

Following progressive easing of monetary policy since August 1998 through the reduction in the Bank Negara Malaysia policy rate (3-month intervention rate) and the statutory reserve requirement, liquidity conditions eased considerably in early 1999. As the year progressed, the underlying excess liquidity became progressively larger due to large inflows on both the current and capital account of the balance of payments. In managing this excess liquidity, the conduct of monetary policy in 1999 was influenced by several considerations. Firstly, it was important to ensure that the underlying excess liquidity would not reignite inflationary pressures, especially as the economic recovery strengthened and asset prices recovered significantly. In this regard, BNM noted that while consumer spending and asset prices had recovered, they were still below the levels that could potentially trigger inflationary pressures in the near term. Nevertheless, the Bank monitored closely these developments. The second concern was the impact of monetary easing on deposit rates. While a reduction in interest rates was necessary to promote increased consumption and investment activities, it was important to strike an appropriate balance with the need to ensure a positive real rate of return for depositors. Finally, the conduct of monetary policy had to bear in mind that efforts for structural reforms have to be intensified. Too rapid a reduction in interest rates would undermine the positive impact of other measures being implemented to strengthen the banking institutions, thereby impairing the financial restructuring process. Given the overhang of the high-cost deposits incurred by banking institutions during the high interest rate period in 1998, reducing the BNM 3-month intervention rate (the anchor rate for the computation of BLR) too sharply would result in disruptive adjustments in the investment portfolio of the banking institutions.

Taking into account the impact of lower interest rates on the financial system and the economy, BNM opted for a smooth and more gradual easing of interest rates under the pegged exchange rate regime. Interest rates were kept relatively stable in the first quarter of 1999, as BNM assumed a more active role to sterilise the significant trade inflows from abroad. Since April, with prospects of further large trade inflows and improvement in the inflationary outlook, the interbank rates were allowed to ease to reflect the underlying liquidity situation in the system. Consequently, the 3-month interbank rates eased by 29 basis points in the first quarter before declining by 299 basis points for the rest of the year to reach 3.18% at the end of 1999. The intervention rate, on the other hand, was reduced albeit at a slower pace. Amid the improvement in the inflationary outlook and the maturing of some of the high-cost deposits, Bank Negara reduced further the intervention rate in several steps in April, May and August by 50 basis points in each revision to 5.5% to strengthen economic recovery. Thereafter, the intervention rate remained at 5.5% for the rest of the year.

The decision to leave the intervention rate unchanged since August 1999 was based on several factors. Firstly, the effective BLR rate had fallen to the historical low of 6.79%. At that level, the BLR was nearly 550 basis points below its peak in June 1998. Amid the ample liquidity situation, the average lending rate fell to an unprecedented level of 8% by the end of August 1999, before easing further by another 25 basis points to 7.75% at the end of 1999. Secondly, there was ample evidence that the recovery was gaining momentum. Indications were that the rebound in GDP would be stronger than earlier expectations. Concerns on rising non-performing loans (NPLs) had also dissipated, with the NPLs in fact moderating to 7.9% by March (based on six-month classification) and subsequently to 6.6% by the end of 1999 from a peak of 9% at end-November 1998. Thirdly, significant progress had also been made by banks in financing economic recovery. Loan approvals picked up during the period June-December, nearly double the amount recorded in the first five months of 1999, while loans disbursed were one-and-a-half times higher over the same period. Nevertheless, as the high volume of disbursements was mainly for working capital, the amount extended was virtually matched by repayments so that the loans outstanding remained low. To some extent, credit growth was also affected by the conversion of debt into bonds as well as the write-offs of loans by banks. The year also saw increased recourse to financing from the equity and the private debt securities market, as corporations took advantage of the improved market sentiment in the stock market and the underlying low interest rates to refinance their activities on a longer-term basis. On the whole, these favourable developments indicated that monetary easing had adequately supported economic recovery while maintaining price stability. More importantly, it provided an environment in which the cost of bank and corporate restructuring was reduced.

In ensuring stable monetary conditions, BNM absorbed a total of RM28 billion through direct interventions in the money market. During January-August 1999, there was a consistent net inflow of capital. By August, total funds locked in with BNM through direct borrowings reached a peak of RM45 billion. In September, there was a net outflow of portfolio funds (–RM5.2 billion) following the expiration of the 12-month holding period on 1 September. To alleviate the temporary withdrawal of liquidity from the system, funds were released into the system through the maturing of the short-term borrowings by BNM. Reflecting the growing confidence in the market, the outflow of funds moderated significantly in the subsequent months and reverted to a net inflow in January 2000. Since November 1999, BNM resumed its mopping up operations to offset the expansionary operations of the external sector and the Government. Throughout the period of September to December, interbank rates remained relatively steady in the range of 2.52–3.15% for overnight to 3-month money.

On the whole, the extent of the monetary easing, as reflected in the reduction in lending rates, was less pronounced compared with other crisis-affected regional economies. This was due to the recognition by BNM at the onset of the crisis that the pursuance of a very high interest rate regime in a prolonged economic crisis would not only be ineffective in stabilising the foreign exchange market, but would also contribute to undermining the domestic real economy. Consequently, unlike several of the other crisis-affected economies, BNM had not resorted to raising interest rates too sharply during the height of the economic crisis. Furthermore, the Bank was mindful that in complementing the role of fiscal policy to revive the economy, there was a need to avoid overly excessive monetary expansion which could lead to a potential risk of rekindling inflation over the medium term and undermine output growth in the long term.

It is also important to note that the selective exchange controls to some extent allowed interest rates in Malaysia to diverge significantly from the US dollar interest rates. By the end of 1999, interest rate spreads widened against US rates to 2.75 percentage points in favour of the US dollar interest rates from 4 percentage points in favour of Malaysian rates at the end of August 1998 (prior to the imposition of the selective exchange controls).

While the focus of monetary policy was directed at supporting the economic recovery, BNM had also placed high priority on the need to ensure that the low interest rate regime does not unduly affect those who depend on interest from savings as their main source of income. Indeed by April, the fixed deposit rates offered by the commercial banks had fallen to 3.99–4.06% for one- to 12-month maturity (5.82–5.74% at end-1998). In addition to monetary policy ensuring real positive rates of interest to depositors, BNM also introduced other savings instruments to provide alternative investments to deposits, especially for pensioners. In November, BNM launched a second series of Malaysia Savings Bond for subscription by retirees.

Throughout the year, the decisions on monetary policy had also been taken on the basis of what is considered appropriate to preserve financial stability. This was viewed necessary as market confidence and the bank intermediation process hinged critically on the state of the banking system. The conduct of monetary policy was balanced delicately to ensure that monetary easing did not destabilise the financial system and will continue to promote long-term savings. The year saw the imposition of more stringent guidelines aimed at strengthening the banks. These included, among others, guidelines governing the extension of lending to their controlling shareholders and guidelines on future capitalisation of banking institutions by controlling shareholders. This was to avoid a repeat of past practices whereby the capitalisation of banks by the controlling shareholders was made through bank borrowings which consequently exerted pressure on banks to generate large returns to service these loans at the expense of prudent lending. At the same time, complementary measures were also undertaken to reduce the NPLs of banks and facilitate the restructuring of banks and the private sector.

During 1999, there was a change in policy focus from managing the Asian crisis to addressing longer-term issues of strengthening and enhancing the competitiveness of the banking system to support the further transformation of the economy as well as to improve the transmission mechanism of monetary policy. As part of this process, BNM initiated a merger programme for the domestic banking institutions during the year. The Bank also commenced work on the masterplan for the development of the financial sector over the next ten years to enhance the efficiency, effectiveness and stability of the financial system.

Fiscal Operations and Policy

The 1999 Budget formulated in October 1998 during a recession year appropriately focused on the counter-cyclical role of fiscal policy to revitalise economic activities and strengthen the nation's resilience and competitiveness. Various measures were also introduced to further improve the balance of payments; strengthen the financial sector; promote the services and agriculture sectors; and improve governance in the public and private sectors as well as ensure social well-being. Overall, the Budget strategy reinforced the fiscal stimulus adopted in 1998 in line with the plan to revitalise the economy as set out in the National Economic Recovery Plan (NERP). The fiscal stimulus in 1999 via a budget deficit of 6.1% of GNP contributed to the restoration of consumer and investor confidence, particularly in the second half of 1999.

While the Government undertook a stimulative role, fiscal prudence and discipline continued to be maintained to contain the fiscal deficit at a manageable level so as not to jeopardise long-term growth. The level of expenditure, therefore, was managed with the consideration that revenue should be sufficient to finance operating expenditure; fiscal deficit be contained at a sustainable level of about 6% of GNP in 1999; and availability of domestic and external financing without crowding out the private sector. This required restraint in the increase in public sector spending through a tight budgetary control on non-essential and non-productive spending.

Meanwhile, the better-than-expected revenue outturn in 1999, reflecting the strong pick-up in the momentum of economic recovery as the year progressed, provided the Government with increased flexibility in managing its fiscal policy. It enabled the Government to expand its fiscal stimulus to reinvigorate the economy further through increased expenditure during the course of 1999, while containing the budgeted deficit to within 6% of GNP. Consequently, total expenditure (including contingency reserves) was raised from the budgeted RM65.1 billion to RM74.6 billion. The bulk of the increased expenditure was expended on social and economic sectors. The Government also announced the provision of RM600 special payments to each eligible civil servant and pensioners as well as the reinstatement of civil service allowances.

However, in early 1999, implementation of projects was relatively slow, due to the slow disbursement of development expenditure. It was clear that delays in project implementation would impede economic recovery. In response, the Government implemented several measures to accelerate the pace of implementation of projects to ensure that budgetary allocations were utilised to the maximum, with minimal shortfall. The various measures instituted included intensive monitoring of project implementation; submission of monthly reports on the progress of project implementation; as well as changes in procedures relating to tenders and procurement. With these measures, the Government was able to contain its shortfall in development expenditure to 12.5% of total allocation of RM25.8 billion (shortfall of 21.6% in 1998).

Adequate domestic resources to finance the deficit in 1999, due to fiscal surpluses from previous years and the large current account surplus in the balance of payments, reduced the reliance on external sources. In line with prudent debt management policy and ample liquidity in the financial system, the Government borrowed mainly from the domestic bond market, thereby minimising the nation's exposure to foreign exchange and interest rate risks. The bulk of the domestic borrowing was raised through the issuance of Malaysian Government Securities and through non-inflationary sources, especially from the Employees Provident Fund and insurance companies, to avoid crowding out the private sector. The Government also drew down its accumulated realisable assets. Funding through external borrowings was small. Borrowings were mainly from the World Bank and bilateral sources, namely under the Japanese New Miyazawa Initiative. In international capital markets, the Government raised only US$1 billion through a global bond issue, the objective being primarily, to set a benchmark for Malaysian corporations accessing the international markets.

The 2000 Budget presented to Parliament on 29 October 1999 was aimed at strengthening recovery and raising economic growth to a level consistent with Malaysia's growth potential. Hence, the budgetary operations of the Federal Government in 2000 continued to be expansionary to strengthen the foundation of economic growth. Nevertheless, in line with fiscal prudence, the Government would ensure that the current account of the Federal Government would be in surplus or at least balanced, while the overall deficit does not exceed 6% of GNP. In managing the deficit, the over-riding objective was to achieve sustainable growth with price stability and, at the same time, avoid crowding out the private sector access to resources. For the year 2000, priority would continue to be accorded to projects, which would expand the productive base, generate strong domestic demand as well as projects for the social sector. A large share of the 2000 Budget allocation was for infrastructure development, education and skills training, health services and industrial development. Emphasis was also given to low-cost housing, and agriculture and rural development.

However, the Budget was retabled in Parliament on 25 February 2000 following the dissolution of Parliament on 11 November 1999. The revised 2000 Budget retained the original Budget strategies as well as all the tax and non-tax proposals. A number of additional new tax and non-tax proposals were tabled. After taking into account the new tax measures as well as increases in the salaries and housing allowances of civil servants announced in the original 2000 Budget, the overall fiscal deficit of the Federal Government for year 2000 is projected at 4.5% of GNP. This deficit is smaller than the original 2000 Budget (–5% of GNP) reflecting the better revenue collection arising from the projected stronger economic activities in year 2000.

The 1999 Budget contained both tax and non-tax fiscal incentives focused at reviving business activities, while strengthening the financial sector and the balance of payments. On tax policy, the Government continued to modernise and streamline the tax system to enhance its efficiency and responsiveness in tax collection; as well as to ensure that the revenue collection will improve flexibility in fiscal operations by ensuring that revenue collection reflects economic development in the current year. Hence, a major policy change in the tax administration system was the revision in the tax assessment, which would be based on income received in the current year instead of the previous year, with effect from year 2000.

Fiscal incentives were also introduced during the year to reduce the cost of doing business and improve competitiveness. These included the exemption of stamp duty on refinancing instruments for businesses and trade activities; and abolition of excise duty on refrigerators, television sets and air conditioners. Wide-ranging tax incentives and exemptions were also provided to promote tourism and to strengthen the balance of payments through the promotion of exports, encouraging import-substitution and enhancing the capacity of the domestic services sector to export and substitute for imported services. Among others, the measures included group relief incentive for food production, tax incentive for the shipping sector and tax exemption on income earned from selected services such as repair and maintenance of luxury boats and yachts in Langkawi; and sports, cultural and arts activities.

Several fiscal incentives were also announced to strengthen the banking institutions to enhance their resilience to meet growing challenges, increase the capacity to grant new loans and, hence, provide a strong impetus for the revival of economic activities. These included the exemption of stamp duty and the real property gains tax on mergers; the 50% tax exemption for interest-in-suspense; and the provision of a tax credit (50%) for the accumulated losses of the merged entity. Incentives were also provided to life insurance companies and unit trust sectors to encourage further development of these sectors. Meanwhile, selective tax increases were imposed to increase the Government revenue as well as to discourage the consumption of selected goods or activities.

Consolidated Public Sector

The financial position of the consolidated public sector recovered to record a surplus in 1999. This was entirely due to the significant improvement in the performance of the non-financial public enterprises (NFPEs). The favourable performance of the NFPEs was due mainly to the substantially higher revenue receipts reflecting largely the recovery in economic activities as well as the sharp pick-up in petroleum prices, especially in the second half of 1999. During the year, the coverage of the NFPEs was reviewed and expanded from 28 public enterprises to 37, retrospective to 1998. On the other hand, the financial position of the general government, in particular the Federal Government recorded a larger deficit attributable to the implementation of the fiscal stimulus package. In aggregate, the overall account of the consolidated public sector recorded a small surplus of RM581 million or 0.2% of GNP (1998: –RM3.5 billion or –1.3% of GNP). This financial position was significantly better than the earlier projection of a deficit (–RM16.4 billion or –5.8% of GNP) in the Treasury Economic Report 1999/2000 attributable largely to the strong pick-up in economic activity as well as the sharply higher petroleum prices in the latter part of the year.

The general government consolidated position, comprising the Federal Government, 13 state governments, statutory bodies and local governments recorded a smaller current account surplus (RM16.9 billion or 6% of GNP). This was mainly due to higher operating expenditure (+7.7%), amidst moderate increase in revenue receipts (+2%). Increased operating expenditure was channelled to improving the quality of the public services and amenities as well as for higher emoluments and debt servicing. The surplus, as in previous years, was generated mainly by the Federal Government and to a lesser extent, the state governments, while the statutory bodies remained in deficit, attributable to their narrow revenue base. In contrast, several major public enterprises recorded improved performance during the year. The operating surplus of the NFPEs, as a group, was higher (RM31 billion or 11.1% of GNP). Consequently, the consolidated

Table 2.7
Consolidated Public Sector Finance

	1998	1999*p*	2000 Forecast
	RM million		
General government[1]			
Revenue	69,595	71,006	74,917
Operating expenditure	50,179	54,061	61,874
Current account of general government	19,416	16,945	13,043
Current account of NFPEs[2]	23,918	31,006	28,804
Public sector current surplus	**43,334**	**47,951**	**41,847**
(% of GNP)	**16.1**	**17.1**	**14.0**
Net development expenditure	46,827	47,370	49,417
General government	*17,168*	*21,823*	*23,061*
NFPEs[2]	*29,659*	*25,547*	*26,356*
Overall balance	–3,493	**581**	**–7,570**
(% of GNP)	–1.3	**0.2**	**–2.5**
General government	*2,248*	*–4,878*	*–10,018*
NFPEs[2]	*–5,741*	*5,459*	*2,448*

[1] Comprises Federal Government, state governments, statutory authorities and local governments.
[2] Refers to 37 NFPEs.
p Preliminary

Source: Ministry of Finance, state governments and non-financial public enterprises public sector recorded a larger current account surplus of RM48 billion or 17.1% of GNP in 1999.

Public sector development expenditure was marginally higher (+1.2%) in 1999 due to the significantly higher development outlays (+27.1%) of the general government to reinvigorate economic growth and meet the socio-economic objectives of the nation, notwithstanding the lower capital outlays of the NFPEs (–13.9%). The bulk of the general government development outlays were channelled to infrastructure projects; human resource development; as well as agriculture and rural development. In contrast, lower capital outlays of the NFPEs reflected largely the deferment of less essential development projects and sharply lower investment overseas. Declines in investments were recorded by several major public enterprises including Tenaga Nasional Berhad, Telekom Malaysia Berhad and Malaysia Airports Berhad.

Federal Government Finance

The Federal Government recorded a larger fiscal deficit in 1999, reflecting the expansionary fiscal programme to promote economic recovery amid the moderate increase in revenue receipts. The current account continued to remain in surplus (RM12 billion or 4.3% of GNP), while the overall balance recorded a further deficit (–RM9.5 billion or –3.4% of GNP) for the second consecutive year. Nevertheless, the deficit was smaller than budgeted in the 1999 Budget (a deficit of RM16.1 billion or –6.1% of GNP), reflecting the better revenue performance than the original estimate, notwithstanding the upward revision of total expenditure.

In 1999, **Federal revenue** registered a moderate increase of 3.5% or RM2 billion to RM58.7 billion or 20.9% of GNP despite the double-digit decline in income taxes. The better-than-expected revenue collection was attributable to the marked improvement in indirect tax collection in tandem with the recovery in aggregate demand as well as higher receipts from investment income. The higher collections also reflected several revenue enhancing measures announced in the 1999 Budget including increases in taxes/duties on selected goods and gaming activities. Meanwhile, for the second consecutive year, contribution from petroleum-based income was lower (–1.2% to RM11.7 billion) due to decline in receipts of petroleum income tax and royalty which were affected by the marked decline in petroleum prices in 1998 and in the first quarter of 1999. In aggregate, the increase in revenue emanating from indirect taxes (+RM2.8 billion) and non-tax revenue and receipts (+RM2 billion) more than offset the decline in direct taxes (–RM2.8 billion).

Table 2.8
Federal Government Finance

	1998	1999*p*	2000 Revised Budget
	RM million		
Revenue	56,710	58,675	61,822
Operating expenditure	44,584	46,699	54,343
Current account	**12,126**	**11,976**	**7,479**
(% of GNP)	**4.5**	**4.3**	**2.5**
Net development expenditure	17,128	21,463	20,881
Gross development expenditure	*18,103*	*22,615*	*21,881*[3]
Less Loan recoveries	*975*	*1,152*	*1,000*
Overall balance	**–5,002**	**–9,487**	**–13,402**
(% of GNP)	**–1.9**	**–3.4**	**–4.5**
Sources of financing[1]			
Net domestic borrowing	11,040	5,423	–
Gross borrowing	*17,990*	*19,281*	–
Less Repayment	*6,950*	*13,858*	–
Net foreign borrowing	1,819	2,923	–
Gross borrowing	*4,001*	*4,763*	–
Less Repayment	*2,182*	*1,840*	–
Special receipts	1	238	–
Realisable assets[2] and adjustments	–7,858	903	–
Total	**5,002**	**9,487**	**–**

[1] Data for 2000 are not given.
[2] Includes changes in Government's Trust Fund balances. A decline in the accumulated realisable assets is indicated by a positive (+) sign.
[3] Includes shortfall in expenditure.
p Preliminary

Source: Ministry of Finance

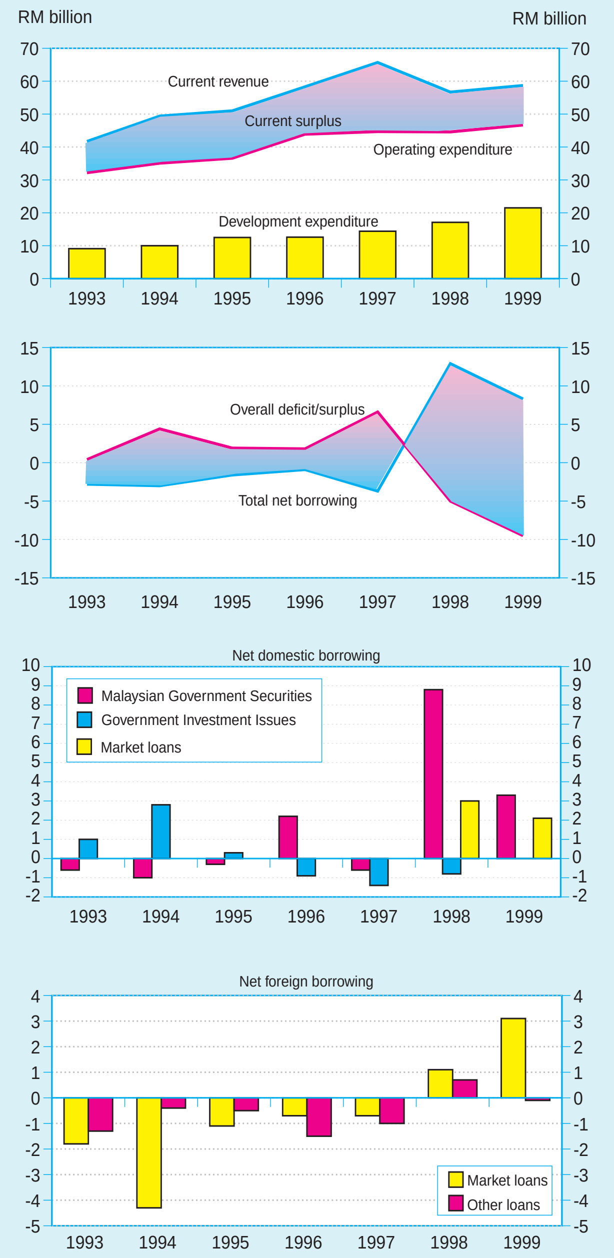
Revenue from **indirect taxes** expanded by 18.1% following a sharp decline of 33.9% in 1998 to account for a higher share of 31% of total revenue (27% in 1998). Reflecting the moderate recovery in aggregate demand as well as higher petroleum prices, especially in the second half-year, most major sources of indirect taxes registered strong performance. The higher demand, in particular for motor vehicles, as well as machinery and spare parts have contributed to the large increases in excise duties (31.7%), import duties (22%) and sales tax (16.7%). Revenue collections were also boosted by the increases in import and excise duties on liquor, tobacco and cigarettes in the

1999 Budget. These measures were expected to result in a revenue gain of RM378 million, which was partially offset by revenue foregone of RM59 million arising from the abolition of excise duties on television sets, air conditioners and refrigerators to enhance competitiveness. Meanwhile, service tax recorded a marginal increase (0.8%) due to increased demand for selected professional services and a miscellany of other services. Reflecting the pick-up in crude petroleum prices during 1999, export duty receipts were higher by 7.6%. Other indirect taxes were also higher (4.5%) attributable to some extent to the increases in the rate of duties or taxes on gaming activities.

Revenue from **direct taxes**, however, declined further by 9.2%, thus reducing its share of total Federal revenue to 46% (53% in 1998). All major categories of direct taxes registered declines except for receipts from stamp duties. The decline was most marked in property gains tax (–27.5%) attributable to both lower property prices and a fall in the number of transactions in 1998 as well as in the first quarter of 1999. Collection from income taxes was also sharply lower due to poor business earnings in 1998 (tax base for 1999) as well as lower crude petroleum prices in 1998. As in the previous year, income tax collections were dampened by the restructuring of tax payments, particularly for companies, due to cash flow problems. It was also affected by the provision of several tax concessions and incentives in the 1999 Budget to stimulate business activities, strengthen the financial sector and the balance of payments, and modernise and increase the efficiency of tax administration system. These measures were estimated to result in revenue foregone of about RM1 billion. These fiscal measures included individual income tax waiver for payees on current year basis; income tax exemption of 50% of the amount in the interest-in-suspense account; tax treatment on actuarial surplus of life insurance companies; income tax exemption on interest income of unit trusts; and tax incentives to promote food production and domestic tourism. In particular, sharp declines were recorded for receipts of petroleum (–29.4%), company (–9%) and individual (–7%) income taxes. Higher receipts, nevertheless, were collected from co-operative income tax (10%). In contrast, collections from stamp duties increased by 31.6% in line with strong recovery in stock market activities in 1999.

Overall, **tax revenue** increased marginally by 0.02%, thereby reducing its share to 77% of the total revenue. Consequently, the ratio of tax receipts to GNP declined to 16.2% (16.8% in 1998), the lowest since 1988.

Graph 2.8
Federal Government Finance



Reflective of the Government's efforts to modernise and streamline the tax administration system, the Inland Revenue Board (IRB) stepped up its efforts to raise productivity and efficiency as well as increase the quality of service to meet new challenges. Measures to increase the compliance rate and expand the tax base included expanding the smart partnership concept with related licensing agencies; increasing education programme and publicity; strengthening enforcement activities; and conducting surveys to minimise tax avoidance or evasion. Meanwhile, skills training was conducted for IRB's officers emphasising on technical competency and customer service orientation. An

Table 2.9
Federal Government Revenue

	1998	1999*p*	1998	1999*p*
	RM million		Annual change (%)	
Tax revenue	**45,336**	**45,346**	**–15.5**	**...**
(% of GNP)	**16.8**	**16.2**		
Direct taxes	30,015	27,246	–1.4	–9.2
Income taxes	28,369	25,159	4.6	–11.3
Companies	*17,294*	*15,742*	*3.6*	*–9.0*
Petroleum	*4,046*	*2,856*	*4.8*	*–29.4*
Individuals	*6,900*	*6,419*	*7.3*	*–7.0*
Co–operative	*129*	*142*	*–9.8*	*10.0*
Real property gains tax	396	287	–24.3	–27.5
Stamp duties	1,190	1,566	–56.2	31.6
Other	60	234	–18.9	289.7
Indirect taxes	15,321	18,100	–33.9	18.1
Export duties	623	670	–40.8	7.6
Import duties	3,868	4,720	–40.7	22.0
Excise duties	3,586	4,723	–40.8	31.7
Sales tax	3,845	4,488	–37.7	16.7
Service tax	1,447	1,459	–1.9	0.8
Other	1,952	2,040	1.6	4.5
Non–tax revenue and receipts	**11,374**	**13,329**	**–6.1**	**17.2**
Total revenue	**56,710**	**58,675**	**–13.7**	**3.5**
(% of GNP)	**21.1**	**20.9**		

p Preliminary

Source: Ministry of Finance

integrated assessment and collection system has been developed to provide for an automated assessment and collection process to facilitate operations of the IRB.

Non-tax revenue increased by 16.5% with higher receipts of investment income mainly from dividends of PETRONAS (RM4.1 billion) and BNM (RM1 billion). However, receipts from licences and permits declined by a further 5.1% with lower collections from levies on foreign workers and petroleum royalties. Similarly, **non-revenue receipts**, which included refunds of expenditure, receipts from Government agencies and revenue from the Federal territories, were substantially higher during the year.

Total Federal Government expenditure increased substantially by 10.6% to RM69.3 billion in 1999 due to the expansionary program to support economic recovery. It also reflected the upward revision in expenditure allocation from RM65.1 billion (including contingency reserves) announced in the 1999 Budget to RM74.6 billion in view of the better-than-expected revenue collection. In the course of the year, the Government undertook several measures to expedite project implementation to ensure that the fiscal stimulus would have maximum impact in generating economic growth. As a result of these measures, the Government's development expenditure shortfall in 1999 was reduced to 12.5%, as against a larger shortfall of 21.6% in 1998.

In line with prudent fiscal management and discipline, the increase in **operating expenditure** was moderate (+4.7%), reflecting continued restraint on less essential spending. During the year, the total wage bill, the largest component of operating expenditure (31%), increased by 3.2%. The higher wage bill reflected the part payment of the one-month bonus announced in the 2000 Budget inclusive of the special payment of RM600 announced in June 1999 to each eligible civil servant. The balance of the bonus payment would be paid in the first three months of 2000. Another contributory factor to the higher wage bill was the reinstatement of the civil service allowances, effective August 1999. The payment for pensions and gratuities was also higher reflecting the special payments to pensioners during the year as well as the higher annual contribution to the Pensions Trust Fund (RM833 million in 1999; RM742 million in 1998). Debt service charges in 1999, which accounted for 17% of operating expenditure were also higher. The higher outlay reflected increased domestic interest payments arising from the higher domestic debt level to finance the economic recovery programme. Foreign interest payments, however, declined reflective of the Government's prudent external debt management policy.

Table 2.10
Federal Government Operating Expenditure by Object

	1998	1999*p*	1998	1999*p*
	RM million		% share	
Emolument[1]	13,984	14,436	31.4	30.9
Supplies and services	5,212	6,074	11.7	13.0
Asset acquisition	434	422	1.0	0.9
Public debt charges	6,928	7,941	15.5	17.0
Pensions and gratuities	3,658	3,792	8.2	8.1
Other grants and transfers[2]	11,972	12,260	26.8	26.3
Other expenditure	2,396	1,774	5.4	3.8
Total	**44,584**	**46,699**	**100.0**	**100.0**

[1] Excludes statutory bodies.
[2] Includes grants and transfers to state governments as well as public agencies and enterprises.
p Preliminary

Source: Ministry of Finance

Table 2.11
Federal Government Development Expenditure by Sector

	1998	1999*p*	1998	1999*p*
	RM million		% share	
Defence and security	1,380	3,122	7.6	13.8
Economic services	9,243	8,970	51.1	39.7
Agriculture and rural development	960	1,089	5.3	4.8
Trade and industry	3,227	2,798	17.8	12.4
Transport	3,062	2,893	16.9	12.8
Public utilities	1,968	1,850	10.9	8.2
Other	26	340	0.2	1.5
Social services	5,783	6,936	31.9	30.6
Education	2,915	3,865	16.1	17.1
Health	716	835	3.9	3.7
Housing	1,030	1,081	5.7	4.7
Other	1,122	1,155	6.2	5.1
General administration	1,697	3,587	9.4	15.9
Total	**18,103**	**22,615**	**100.0**	**100.0**

p Preliminary

Source: Ministry of Finance

Disbursement on supplies and services recorded a sharp increase of 16.5% mainly for repairs and maintenance works as well as professional services to enhance the quality and efficiency of public services. Other transfer items were higher due largely to grants and transfers to other Government agencies for development and maintenance purposes as well as increased allocation to the Higher Education Fund and the National Education Fund. However, grants and transfer payments provided to the state governments and subsidies recorded declines. Meanwhile, disbursements on asset acquisitions and refund of expenditures were lower.

In tandem with the Government's strong commitment to revive economic activities, gross **development expenditure** increased markedly by 24.9% to RM22.6 billion in 1999. Priority was placed on projects that could generate economic activities with minimal leakages in terms of imports. Continued attention was also given to meeting the socio-economic objectives of the nation. The bulk of the expenditure, therefore, was channelled to social and economic programmes to reinvigorate growth as well as to improve the social well-being particularly of the lower income group.

In terms of sectoral distribution, economic services remained the largest component of total development expenditure, although its share declined to 40% (51% in 1998). Reflecting the Government's efforts to complement privatised entities to provide an integrated transportation network, expenditure on transportation remained significant. A large proportion of the expenditure was for infrastructure development, particularly for the construction, upgrading and improvement of roads (including highways) and the development and expansion of rail, port and airport projects. Trade and industry also absorbed a sizeable share of the gross expenditure. This included expenditure for the provision of infrastructure facilities, industrial research and development, development of small- and medium-scale industries and the promotion of tourism. A large proportion of the expenditure was also disbursed to Pengurusan Danaharta Nasional Berhad (RM1 billion), Keretapi Tanah Melayu Berhad (RM132 million), Bank Pembangunan dan Infrastruktur Malaysia Berhad (RM34 million) and Multimedia Development Corporation (RM30 million). Expenditure on public utilities remained high to improve water and electricity supplies. Meanwhile, outlays on agriculture and rural development (including land development) were higher reflecting the Government's commitment to upgrade the standard of living in rural areas.

Capital outlays on the social services sector recorded a further double-digit growth of 19.9% in 1999 to account for 31% of total development expenditure. In particular, investment in education and training was substantially higher to account for the largest share of development expenditure (17%). This reflected the Government's policy of making Malaysia a centre of excellence in education as well as promoting a highly skilled labour force to support the strategy of productivity-driven growth. The expenditure was mainly for the upgrading of educational infrastructure and support facilities as well as curriculum development. This included the construction and upgrading of primary, secondary, vocational and polytechnic schools as well as the development of universities including the Medical Faculty of the International Islamic University in Pahang and University Malaysia Sabah. The higher expenditure on housing was for low-cost public housing projects and housing programmes for the armed forces, police personnel, customs and excise officers and teachers in rural areas, as well as additional allocation to the housing fund for the hardcore poor. Outlays on health and family planning were also higher to provide better quality health care services.

The higher outlays on defence and internal security during the year reflected largely the modernisation

Table 2.12
Public Debt of Federal Government

	Annual change		At end 1999*p*
	1998	1999*p*	
	Nominal value in RM million		
Domestic debt	11,229	5,553	93,750
Treasury bills	0	0	4,320
Government Investment Issues	–750	0	2,000
Malaysian Government Securities	8,750	3,324	78,336
Treasury Housing Loans Fund	189	130	3,955
Market loans	3,040	2,099	5,139
External debt	1,972	3,445	18,369
Market loans	1,220	3,382	11,075
Project loans	752	63	7,294
Total	**13,201**	**8,998**	**112,119**

p Preliminary

Source: Ministry of Finance

programme of the armed forces and police force. This included the purchase of military and operational equipment as well as construction of infrastructure.

Expenditure for general administration was also substantially higher, largely for the construction and maintenance of the new administrative centre at Putrajaya; the computerisation of the Government administration; expenses pertaining to Y2K compliance in the public sector; as well as enhancing the efficiency and effectiveness of the Government administrative machinery.

The financing requirement of the Federal Government remained high in 1999 to finance its fiscal deficit. Nevertheless, the better-than-expected outturn in revenue collection provided the cushion for the Government to revise downward its borrowing programme during the year. The fiscal deficit in 1999 was largely financed by domestic borrowing given the ample domestic liquidity. External borrowing was relatively small. The Government also drew down some of its cumulative realisable assets. Overall, the Federal Government recorded a **total net borrowing** of RM8.3 billion, which was smaller when compared with 1998 (RM12.9 billion), when the Government's borrowing was larger than its financing needs due to the shortfall in expenditure. Nevertheless, the increased borrowings, coupled with a net exchange revaluation loss arising largely from the weakening of ringgit against the Japanese yen led to a moderate increase in the total debt of the Federal Government. The total outstanding debt rose by 8.7% to RM112.1 billion as at end-1999 or 40% of GNP (end-1998: RM103.1 billion or 38% of GNP). Nevertheless, the ratio was much lower when compared with 1986 (111% of GNP), 1990 (83% of GNP) and 1995 (43% of GNP) reflecting the prudent debt management policy.

During the year, net domestic borrowing totalled RM5.4 billion. The domestic borrowing was financed largely from non-inflationary domestic sources as well as the remaining second and third tranches of the US$1.35 billion syndicated loan signed at the end of 1998 with 12 locally-incorporated foreign banks. Gross funds raised through the issuance of Malaysian Government Securities (MGS) amounted to RM10 billion. Part of the new issue was to refinance MGS which matured in 1999 amounting to RM6.7 billion. The Government also drew down the balance of RM2.1 billion from the syndicated loan of US$1.35 billion. However, the Government took advantage of the narrowing of spreads following Malaysia's improved credit ratings, to refinance the syndicated loan to reduce the debt-servicing burden. In November 1999, the Government signed a syndicated loan agreement with 26 banks (including 10 foreign locally-incorporated banks) for a loan of US$1.25 billion and ¥11.6 billion (equivalent to RM5.2 billion) to refinance the syndicated loan.

A Government Investment Issue (GII) worth RM2 billion was raised to refinance the maturing GII during the year. Meanwhile, no net new funds was raised through Treasury bills (TB), while the Treasury Housing Loans Fund recorded a small net borrowing in 1999. As a result, the total domestic debt of the Federal Government increased by 6.3% to RM93.8 billion or 33.4% of GNP at the end of 1999 to account for 84% of the total outstanding debt.

In 1999, the Government floated five issues of MGS worth RM2 billion each, mainly by way of open tender through principal dealers and through private placements. The new issues were for a wide range of maturities of 3, 5, 7, 10 and 15 years so as to provide a benchmark yield curve for the development of the bond market. As in previous years, the longer-dated MGS were mainly offered to institutional investors such as the social security institutions. After adjusting for loan redemptions, total MGS outstanding increased by 4.4% to RM78.3 billion at the end of 1999 to account for a share of 83% of the total domestic debt outstanding. In terms of the ownership structure of MGS holders, the social security and insurance institutions held a higher

Table 2.13
Holdings of Federal Government Domestic Debt

	1998	1999*p*	1998	1999*p*
	Nominal value in RM million		% share	
Treasury bills	**4,320**	**4,320**	**100.0**	**100.0**
Insurance companies	183	41	4.2	1.0
Banking sector	3,678	3,720	85.1	86.1
Other	459	559	10.7	12.9
Government Investment Issues	**2,000**	**2,000**	**100.0**	**100.0**
Insurance companies	132	139	6.6	7.0
Banking sector	1,848	1,858	92.4	92.9
of which:				
Bank Negara Malaysia	*940*	*3*	*47.0*	*0.2*
Other	20	3	1.0	0.1
Malaysian Government Securities	**75,012**	**78,336**	**100.0**	**100.0**
Social security and insurance institutions	52,921	59,929	70.6	76.5
of which:				
Employees Provident Fund	*45,670*	*51,757*	*60.9*	*66.1*
Insurance companies	*5,307*	*6,030*	*7.1*	*7.7*
Banking sector	15,420	12,403	20.6	15.8
Other	6,671	6,004	8.8	7.7

p Preliminary

share of 77% of total outstanding MGS. This reflected the critical role of these institutions in funding economic development as well as implementing the fiscal stimulus package to revive the economy. In particular, the Employees Provident Fund (EPF) while remaining the single largest institutional investor in 1999, increased its holding by five percentage points to 66% through new investment in MGS as well as absorbing the liquidation of MGS, especially by banking institutions. Hence, the share of MGS held by the banking sector declined to 16%. The remaining MGS was held mainly by public enterprises, the non-bank financial institutions and foreign investors.

The balance of the domestic debt was in the form of the domestic foreign currency syndicated loan (6%), TB (5%), the Treasury Housing Loans Fund (4%) and GII (2%). The banking institutions held the bulk of TB (86%) mainly for liquidity purposes and GII (93%), reflecting the growing Islamic banking activities. The insurance companies also held GII (7%) and TB (1%) largely to comply with the statutory requirement to invest in approved Government papers. The main lenders to the Treasury Housing Loans Fund were Cagamas Berhad, the EPF, the National Savings Bank and the commercial banks.

External borrowings were also used by the Government to finance its operations. Net external borrowing of the Federal Government for 1999 recorded a net inflow of RM2.9 billion. Gross external borrowing amounted to RM4.8 billion, reflecting largely the issuance of the US$1 billion Malaysian Global Bond (or RM3.8 billion) and the drawdown of a number of loans secured from multilateral (such as the World Bank and Islamic Development Bank) and bilateral sources especially from Japan under the New Miyazawa Initiative. The issuance of the global bond was mainly aimed at providing a benchmark for Malaysian corporations in international capital markets.

During the year, the Government signed several loan agreements under the New Miyazawa Initiative amounting to an equivalent of RM4.8 billion. In March and April 1999, the Government signed several loan agreements with the Overseas Economic Cooperation Fund (which has merged with Japan Export-Import Bank and is currently known as Japan Bank for International Cooperation or JBIC) totalling ¥65 billion (or equivalent to RM2.1 billion) which was for financing utilities, educational projects and small- and medium-scale industries; and secured a syndicated loan of US$250 million and ¥54 billion (or equivalent to an aggregate of RM2.7 billion) arranged by Citibank North America and guaranteed by the Japan Export-Import Bank (currently known as JBIC) to finance transportation projects. Loan agreements were also signed with the World Bank and Islamic Development Bank (IDB). The Government signed an agreement with the World Bank totalling US$404 million (RM1.5 billion) to finance various projects including education, Y2K compliance and social programmes, while four agreements were signed with the IDB totalling US$99 million (RM376 million) to finance the purchase of health, education and fire equipment.

Meanwhile, one market loan, the Yen Bond 9th series of ¥30 billion raised in 1989, matured during the year. Together with a net exchange revaluation adjustment, the outstanding external debt of Federal Government increased to RM18.4 billion or 6.6% of GNP at the end of 1999 from RM14.9 billion or 5.5% of GNP at the end of 1998.

State Governments

Based on preliminary estimates, the consolidated financial position of the 13 state governments recorded a further overall deficit in 1999, the second consecutive year of deficit. The lower revenue receipts coupled with higher operating expenditure of the state governments led to a smaller consolidated current account surplus (+RM4 billion). Reflecting financial prudence, all states achieved surpluses in their current accounts. However, with most states recording deficits in their overall balance, the consolidated position showed a larger deficit of RM372 million. As total resources including Federal Government loans were more than sufficient to finance the overall deficit, there was a build-up of RM455 million in the accumulated financial assets of the state governments.

During the year, the consolidated state **revenue** fell marginally by 1.9% to RM8.7 billion with most state governments experiencing declines in revenue. The slightly lower revenue collection was attributable to lower Federal grants and transfers on account of the absence of revenue growth grants. As in previous years, the receipts from Federal sources were channelled to assist the states in providing infrastructure and other essential amenities to improve the quality of life and to support the increasing urbanisation in the states. Meanwhile, receipts from state sources were sustained at the previous year's level. This reflected the pick-up in economic activities; the recovery in prices of selected commodities especially crude petroleum; as well as the implementation of several revenue enhancing measures by the state governments to diversify their sources of income. These measures included the 50% increase in the export royalty on high quality logs and the introduction of sales tax on crude palm oil and lottery tickets. Consequently, higher revenue was collected from both direct and indirect taxes, while non-tax revenue recorded a decline. The increased direct tax receipts reflected higher receipts from taxes on lands and mines which emerged as the largest source of state revenue (13.7%). Receipts from forest taxes also remained high and maintained its share of total revenue (13.6%). Meanwhile, the increase in indirect taxes was attributable to higher duties collected from excise and import duties of petroleum products. In contrast, non-tax revenue recorded lower collection mainly on account of declines in receipts from investment income, petroleum royalty, commercial undertakings and government services.

Table 2.14
Consolidated State Government Finance

	1998	1999*p*	2000 *Budget*
	RM million		
Revenue	8,817	8,650	9,475
State sources	*7,064*	*7,067*	*7,544*
Federal grants and transfers	*1,753*	*1,583*	*1,931*
Expenditure	4,546	4,670	4,765
Current account	**4,271**	**3,980**	**4,710**
Net development expenditure	4,357	4,352	4,763
Gross development expenditure	*4,856*	*4,534*	*4,947*
Less Loan recoveries	*499*	*182*	*184*
Overall balance	**–86**	**–372**	**–53**
Sources of financing			
Federal loans	610	827	619
Realisable assets[1]	–524	–455	–566
Total	**86**	**372**	**53**

[1] An increase in the accumulated realisable assets is indicated by a minus (-) sign.
p Preliminary

Source: State governments

Total gross expenditure of the state governments as a group declined by 10% attributable to the lower development expenditure. Reflecting efforts of the state governments to contain spending in line with lower revenue receipts, **operating expenditure** of the state governments rose by 2.7% to RM4.7 billion. The increased expenditure reflected higher emoluments (+4.7%) mainly due to part payment of the one-month bonus including the special payments of RM600 to eligible civil servants announced in the 2000 Federal Budget. Meanwhile, other expenditure was lower following lower revenue receipts. During the year, gross **development expenditure** fell by 6.6% to RM4.5 billion as the state governments consolidated their position in line with reduced resources. Nevertheless, seven states provided for an increase in their capital expenditure. The bulk of the expenditure was channelled to the economic sector, especially infrastructure (road, bridges and public amenities), industrial and commercial investments and agriculture and rural development. The balance was for social programmes, including housing and social and community programmes. After taking into account a smaller loan recovery of RM182 million, net development expenditure declined marginally by 0.1% to RM4.4 billion.

Non-Financial Public Enterprises

During the year, the number of **non-financial public enterprises** (NFPEs) for monitoring and reporting purposes was reviewed and expanded. The objective of the revision was for a more representative coverage of NFPEs to further strengthen the analysis on public sector. In this review exercise, the criteria for determining an enterprise as a NFPE included higher annual sales turnover of at least RM100 million (previously RM50 million) as well as at least 51% equity share by the Government including public sector agencies. Other criteria included enterprises with large borrowing requirements and high capital expenditure or which have large economic impact. Based on these criteria, a total of 19 new enterprises were identified. In addition, the review excluded 10 enterprises from the existing list due to the consolidation of selective enterprises with other NFPEs and some that did not meet the criteria. Hence, as a result of the review, the coverage of NFPEs for monitoring and reporting purposes increased from 28 enterprises to 37 (see table on List of NFPEs), retrospective to 1998.

Based on the revised list, preliminary estimates of the consolidated **financial position** of the 37 NFPEs indicated that the overall financial position of the NFPEs as a group improved significantly to record a surplus of RM7.5 billion or 2.7% of GNP in 1999 after recording a deficit of RM4.5 billion or 1.7% of GNP in 1998. However, if based on the previous coverage of 28 enterprises, the consolidated overall financial position would have shown a larger surplus of RM10 billion or 3.6% of GNP in 1999 (1998: –RM1.9 billion or –0.7% of GNP). This development reflected mainly the large capital outlays of some of the new enterprises.

The better financial outturn in 1999 reflected the strong increase in revenue, while total expenditure was slightly higher with higher operating expenditure, offsetting lower capital spending. It also reflected measures taken by NFPEs in 1998 and 1999 to address the impact of the economic contraction, through measures to improve productivity as well as sales of assets to consolidate financial positions. In particular, Tenaga Nasional Berhad (TNB) completed its internal restructuring with new subsidiary companies established for the generation, transmission and distribution activities to improve operational efficiency and to consolidate its strength. To enhance the competitiveness of the generation sector, TNB has embarked on a programme to divest its thermal generation assets. In 1999, TNB disposed the combined cycle plant in Melaka to a private power generation company. Similarly, PETRONAS continued to diversify its investments related to its core businesses including investment overseas to strengthen its earnings.

The consolidated **revenue** of the NFPEs rose sharply by 18.4% to reach RM88.4 billion (1998: +6.6%). The

Table 2.15 List of NFPEs

(a)	**Existing Enterprises**	
1	Cement Industries (Sabah) Sdn. Bhd.	
2	Keretapi Tanah Melayu Bhd.	
3	Kuching Port Authority	
4	Malaysian Rubber Development Corporation Bhd.	
5	Penang Port Sdn. Bhd.	
6	Perwaja Terengganu Sdn. Bhd.	
7	Petroliam Nasional Bhd.	
8	Sabah Electricity Board	
9	Sabah Energy Corporation	
10	Sabah Port Authority	
11	Sarawak Electricity Supply Corporation	
12	Telekom Malaysia Bhd.	
13	Tenaga Nasional Bhd.	
14	UDA Holdings Sdn. Bhd.	
15	Kumpulan Guthrie Bhd.	
16	Golden Hope Plantation Bhd.	
17	Kontena Nasional Sdn. Bhd.	
18	SEBOR (Sabah) Sdn. Bhd.	
(b)	**New Enterprises**	
1	Klang Port Management Sdn. Bhd.	
2	Rakyat Berjaya Sdn. Bhd.	
3	Central Spectrum (M) Sdn.Bhd.	
4	Antara Steel Mills Sdn. Bhd.	
5	Marconi (Malaysia) Sdn. Bhd.	
6	Pos Malaysia Bhd.	
7	Bintulu Port Sdn. Bhd.	
8	Sergam Bhd.	
9	Kulim (Malaysia) Bhd.	
10	Felda Agricultural Services Sdn. Bhd.	
11	Tabung Haji Plantations Sdn. Bhd.	
12	Perbadanan Pembangunan Ekonomi Sarawak Sdn. Bhd.	
13	Pacific Hardwoods Sdn. Bhd.	
14	Sinora Sdn. Bhd.	
15	Malaysia Airports Bhd.	
16	Gas Malaysia Sdn. Bhd.	
17	Multimedia Development Corporation Sdn. Bhd.	
18	Putrajaya Holdings Sdn. Bhd.	
19	Kelang Container Terminal Sdn. Bhd.	
(c)	**Removed**	
1	Felda Oil Products Sdn. Bhd.	
2	Felda Palm Industries Sdn. Bhd.	
3	Felda Trading Sdn. Bhd.	
4	PERNEC Corporation Sdn. Bhd.	
5	Petronas Carigali Sdn. Bhd.	consolidated into PETRONAS group
6	Petronas Dagangan Bhd.	
7	Petronas Penapisan (Terengganu) Sdn. Bhd.	
8	Malaysia LNG Sdn. Bhd.	
9	Malaysian International Shipping Corporation Bhd.	
10	Tabung Haji Travel Industries Sdn. Bhd.	

Source: Economic Planning Unit

revenue collection was boosted significantly by the higher petroleum prices, which rose from an average of US$14 per barrel in 1998 to average US$18.18 per barrel in 1999. The recovery in economic activities also contributed to the higher revenue collection. Reflecting the tight financial discipline and the restructuring exercises undertaken by selective public enterprises, operating expenditure of the NFPEs increased at a slower pace of 11.8% to RM55.4 billion (1998: +17.8%). The larger outlays reflected the higher cost of supporting increased business activities, while the debt service payment was contained following a smaller accumulation of external debt a year ago and low domestic interest rates.

With the increase in revenue outpacing the growth in operating expenditure, the operating surplus of the NFPEs as a group was substantially higher at RM33 billion or 11.8% of GNP (1998: +9.4% of GNP). The sizeable operating surplus was contributed mainly by the major NFPEs involved in commodities, utilities and commercial services, notably PETRONAS, TNB and Telekom Malaysia Berhad (Telekom). Meanwhile, a small number of small enterprises continued to record losses in 1999.

During the year, the **capital expenditure** of the NFPEs declined by 13.9% to RM25.5 billion (1998: RM29.7 billion). The lower capital expenditure was largely attributable to the sharply lower investment overseas as well as the scaling down or deferring of less essential projects. Most of the enterprises recorded lower investments. Nevertheless, several enterprises including PETRONAS, Putrajaya Holdings Sdn. Bhd. and Sarawak Electricity Supply Corporation (SECSO) increased capital spending for capacity expansion.

Table 2.16
Consolidated NFPEs Finance[1]

	1997	1998	1999*p*
		RM million	
Revenue	70,086	74,715	88,433
Expenditure	42,033	49,529	55,389
Current account	**28,053**	**25,186**	**33,045**
(% of GNP)	**10.5**	**9.4**	**11.8**
Development expenditure	21,341	29,659	25,547
Overall balance	**6,712**	**–4,473**	**7,498**
(% of GNP)	**2.5**	**–1.7**	**2.7**

[1] Refers to 28 NFPEs in 1997 and 37 NFPEs in 1998 and 1999.
p Preliminary

Source: Ministry of Finance and non-financial public enterprises

In 1999, PETRONAS continued to invest in both upstream and downstream activities, including the construction of new gas processing plants and the Centralised Utility Facility projects in Kertih and Gebeng. Other projects undertaken by the company included several petrochemical projects; expansion and upgrading of the University of Technology PETRONAS; construction of the railway link from Kuantan Port to Kertih; as well as continued fleet expansion programme by Malaysian International Shipping Corporation to enhance its capacity to handle the growing volume of international trade. PETRONAS also continued to expand its overseas investments, namely, the acquisition of the 25% stake in the UK-based Premier Oil.

Meanwhile, capital investment of TNB was mainly channelled towards capacity expansion, systems improvement for security purposes as well as to improve reliability and quality of supply to meet the increasing demand for electricity by the commercial and industrial sectors and residential consumers. Major on-going projects included the construction of Phase I and I(A) of the 500kw transmission network, Phase III of the Port Klang Sultan Salahuddin Abdul Aziz Power Station in Kapar and the conversion of power plants including the Melaka, Chenderoh, Paka and Pasir Gudang plants. Other projects included the construction of Phase II of the Tenaga Nasional University Complex and ongoing construction of the RM2 billion TNB Janamanjung coal-fired plant in Perak Darul Ridzuan. Similarly, Telekom also continued to expand and modernise telecommunication infrastructure as well as upgrading the international and local networks. The bulk of the expenditure was expended on developing a range of services and products for the Corporate Information Superhighway (COINS), which is an integral part of the Multimedia Super Corridor (MSC), and the National Information Infrastructure (NII). Telekom continued to diversify its investments overseas, including projects in Ghana, but on a more moderate scale. Capital outlays of Putrajaya Holdings Sdn. Bhd. was mainly for the new administrative centre in Putrajaya, while Malaysia Airports Bhd. and Keretapi Tanah Melayu Bhd. continued to modernise and enhance the quality and efficiency of their services.

The capital outlays of the NFPEs as a group were mainly financed by internally-generated funds and recourse to domestic and external borrowings. In 1999, the outstanding external debt of the public enterprises increased to RM58.6 billion to account for a larger share of 43% of the nation's medium- and long-term external debts. The increase reflected the higher borrowing and, to a smaller extent, a net exchange revaluation loss as a result of the appreciation of the Japanese yen against the ringgit. During the year, PETRONAS issued two bonds, namely the ¥51 billion and US$650 million bonds. The external debt of the NFPEs remained manageable, with debt service ratio (ratio of debt servicing to exports of goods and services) of 1.3% in 1999. Furthermore, most of the loans have been utilised to fund productive investments, including overseas investments, that generate foreign exchange revenue to service the debt. Nevertheless, investment activities and borrowings of the NFPEs would be closely monitored to ensure that their borrowings would not create risks to the economy.

During the year, the Government continued to pursue its privatisation policy. However, projects to be privatised are assessed more critically in terms of the potential impact on the economy, balance of payments, strong domestic linkages and multiplier effects. In 1999, three government agencies were corporatised, namely, the Penang Water Authority, Terengganu Water Department and the Human Resource Department Council. Another 12 existing projects and enterprises were also privatised mainly in the area of land development, while one enterprise was divested.

3 Outlook and Policy

World Economic Outlook

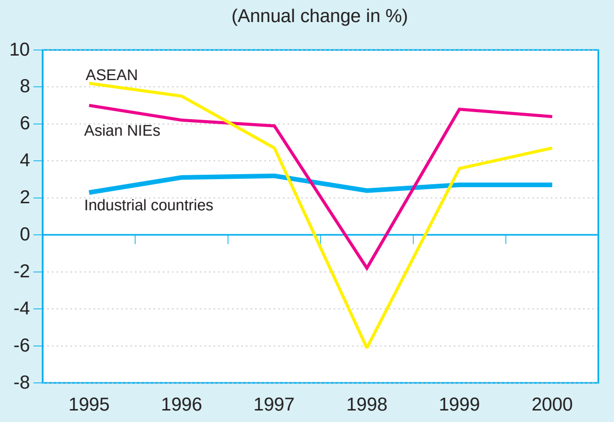
International Environment

In 1999, real GDP growth in the **major industrial countries** as a group expanded further by 2.7%, amidst moderating inflation and improved labour market conditions. The individual countries, however, continued to show divergent growth trends. The expansion in the United States economy remained strong in 1999, growth in the United Kingdom and the euro-11 area moderated, while Japan recorded a slight improvement.

The United States economy entered its eighth year of expansion, underpinned by strong domestic demand driven mainly by the positive wealth effects from a buoyant stock market, and to a lesser extent, due to inventory build-up related to potential Y2K computer problems. Some recovery was seen in the Japanese economy with a modest growth in 1999. Growth was stronger in the first half of the year due to the large fiscal stimulus and housing investment. Growth in the United Kingdom and euro-11 area moderated, affected mainly by the weakness of the economies in the early part of the year. However, economic activity in these countries picked up in the second half of 1999, led by domestic demand in the United Kingdom, while in Germany and the euro-11 area, growth was driven mainly by the external sector. In the **developing countries**, real GDP grew at a faster pace of 3.5% (1998: 3.2%), reflecting mainly an export-led recovery in the East Asian economies, which more than offset slower growth in Africa and the Middle East and virtually no growth in Latin America.

In **year 2000**, growth prospects remain positive for the world economy with moderate growth in the industrial countries and stronger growth in developing countries. Real GDP growth in the major industrial countries as a group is expected to stabilise at 2.7%, as a moderation in the United States' economy is likely to be compensated by higher growth in the euro-11 area, the United Kingdom and Japan. Meanwhile, real GDP of the developing countries as a group is projected to expand by 4.8%, reflecting a turnaround in Latin America and higher growth in Asia, Africa and the Middle East. In line with the favourable growth prospects, growth in the volume of world trade is expected to increase significantly by 6–7% (1998: 3.7%).

Graph 3.1
Real GDP Growth: Industrial Countries, Asian NIEs and ASEAN



Industrial Countries

In the **United States**, the economy is expected to continue with its ninth year of expansion in 2000, albeit at a slightly slower pace of 3.5%. The moderation is based on expectations that the domestic stock market would consolidate gradually during the year, in response to a series of expected monetary tightening. The probability for a sharp stock market correction is somewhat reduced by safeguard mechanisms such as programme trading, circuit breakers and margin requirement. The stock market is also likely to be supported, to some extent, by the continued trend in mergers and acquisitions of internet-related companies, rapid growth in employees' share options and better prospects for corporate earnings in view of the global recovery. The lower stock market and higher financing cost are likely to dampen both consumption and investment. The reduction in wealth effect and higher debt servicing would rein in consumption, which has been the prime source of growth in recent years. However, on the upside, continued productivity growth would help sustain growth at a relatively high level. Nevertheless, significant imbalances in the economy, including the growing current account deficit, high private sector borrowing and negative savings ratio combined with the present high valuation of stock prices accentuate the risks in the economy.

In **Japan**, the economy is expected to pick up further, albeit at a slow pace of 1% in 2000. The gradual improvement in the economy would be aided by the supportive economic policies and favourable external environment. In the early part of the year, growth would arise from the new fiscal stimulus package

Table 3.1
Major Industrial Countries: Key Economic Indicators

	Average 1992-96	1997	1998	1999*e*	2000*f*
	Annual change (%)				
REAL GDP					
Major Industrial Countries	**2.3**	**3.2**	**2.4**	**2.7**	**2.7**
United States	2.8	4.5	4.3	4.1	3.5
Japan	1.7	1.6	–2.5	0.3	1.0
Euro-11 Area	1.4	2.3	2.8	2.1	2.8
Germany	1.2	1.5	2.2	1.5	2.3
United Kingdom	2.4	3.5	2.2	2.0	2.7
INFLATION					
Major Industrial Countries	**2.6**	**2.0**	**1.4**	**1.5**	**1.8**
United States	2.9	2.3	1.6	2.2	2.5
Japan	0.7	1.7	0.7	–0.3	0.0
Euro-11 Area	3.3	1.6	1.1	1.1	1.7
Germany	3.3	1.5	1.0	0.6	1.3
United Kingdom[1]	3.2	2.8	2.7	2.3	2.2
	% of labour force				
UNEMPLOYMENT					
Major Industrial Countries					
United States	6.3	4.9	4.5	4.2	4.2
Japan	2.8	3.4	4.1	4.7	4.7
Euro-11 Area	11.0	11.7	10.9	10.2	9.6
Germany	8.0	9.8	9.3	9.0	8.7
United Kingdom	9.0	5.7	4.7	4.4	4.2
	US$ billion				
CURRENT ACCOUNT BALANCE					
Major Industrial Countries	**15.2**	**–20.3**	**–54.6**	**–193.6**	**209.9**
United States	–100.1	–143.5	–220.6	–321.0	–365.0
Japan	110.2	94.5	120.8	111.0	134.7
Euro-11 Area	27.5	109.2	67.5	40.5	45.3
Germany	–13.9	–1.7	–3.7	–1.1	2.6
United Kingdom	–8.5	10.1	–0.8	–22.0	–22.4

[1] Retail Price Index, excluding mortgage interest
e Estimate
f Forecast

Source: IMF World Economic Outlook, October 1999.
OECD Economic Outlook, December 1999.
Datastream

worth ¥18 trillion (about 3.7% of GDP) and improved export performance. The latest supplementary budget, the largest of the nine packages announced since 1992, focuses mainly on public works and measures to help small businesses. External demand is also likely to remain favourable given the recovery of overseas markets especially in Asia, which accounts for about 35–44% of Japan's total exports. However, the strength of the yen could impinge on Japan's competitiveness and restrain exports to some extent. In the latter part of the year, as the effect of fiscal spending tapers, private sector demand is likely to pick up. Increased profits and stronger balance sheets of corporations, incentives to replace existing capital stocks and a recovery in overseas demand should help to gradually restore business investment. Notwithstanding these favourable developments, the Japanese economy is likely to remain relatively weak during the year due to structural issues associated with excess employment and production capacity as well as the ongoing banking sector reforms.

In the **United Kingdom**, the recovery momentum is expected to continue in 2000 with GDP growth picking up to 2.7%. As the economy gathers pace, growth is likely to be more broad-based, spreading from the services sector to manufacturing and exports. A stronger external demand is anticipated with higher growth in the euro-11 area, which accounts for about one-half of the United Kingdom's total exports. At the same time, domestic demand is likely to remain strong in 2000, supported mainly by easier access to credit and gains in wealth emanating especially from buoyant house prices. The risks to growth would emerge from further monetary tightening. Prospects of higher interest rates would also exert a dampening impact on domestic economic activity as well as a loss in export competitiveness, especially if the euro weakens significantly.

Similarly, growth in **Germany** and the **euro-11 countries** as a whole are expected to pick up to 2.3% and 2.8% respectively in 2000. The higher growth would emanate from increased intra-euro trade and higher exports to non-euro markets due to the weak euro. In Germany, business investment is anticipated to improve gradually with the upturn in foreign demand and favourable monetary conditions. Tax reforms and measures taken to improve labour market rigidities in 1999 are also likely to yield positive results in the course of the year by stimulating private consumption. The German government had adopted a new approach to improve structural unemployment via the reduction in indirect labour costs, a greater resort to active labour market measures and roundtable discussions to reach consensus. Tax reforms to increase family allowances and a reduction in pension contributions from the wage base were also announced in 1999, which should contribute towards increasing overall disposable income. Therefore, growth prospects would not only depend on the performance of the overseas markets and nominal exchange rate of the euro but also on the effectiveness of the tax and labour market policies in addressing structural impediments to growth.

Despite the favourable outlook, there are **a number of potential risks and uncertainties** that could cloud prospects for growth of industrial countries in 2000. These downside risks include the possibility of a sharp correction in the United States' stock market, aggressive monetary tightening in the industrial countries as well as risks associated with a weak recovery of the Japanese economy. In the event that these risks materialise, they could have broad ramifications on the international financial markets and moderate growth in world trade. Given the large imbalances in the United States' economy with the present high valuation of Internet stocks and the large weighting of investors' portfolio in speculative stocks, the economy remains vulnerable to a sudden reversal in investor sentiment. A major stock market correction could undermine confidence and precipitate a cyclical downturn in investment and consumption, in view of the heavy reliance of corporations on equity financing and through the negative wealth effect (above 60% of the household's financial assets are in equities). Given the record high debt levels (share of private sector debt to GDP of 132%), borrowers could also face financial problems should asset prices fall sharply, thus adversely affecting their wealth and income levels. The extent to which a sharp correction of the stock market and its adverse effects could be mitigated by fiscal and monetary policies remains uncertain.

Another risk is the uncertainty over the strength of the economic recovery in Japan. The uncertainties include the deflation situation that could be aggravated by a possible strengthening of the yen, the extent of the impact of corporate and financial restructuring on employment and investment, as well as the limitations of further fiscal stimulus to stimulate the economy.

The risks of monetary tightening in the industrial countries could exert pressures on exchange rates and affect capital flows into emerging economies. Given the stronger economic fundamentals of the emerging economies compared with the situation during the crisis period, these economies are likely to remain resilient despite a gradual tightening of monetary policy in the industrial countries. However, an aggressive tightening cycle could destabilise the global stock markets with consequential adverse impact on growth prospects for the regional economies for 2000.

Inflation in the major industrial countries as a whole is expected to edge upwards to 1.8% in 2000, reflecting higher inflation in almost all the major industrial countries. Despite the downward pressure on prices due to higher productivity growth, retail competition and price transparency through online business, inflationary pressures are likely to emerge due to higher oil prices and tight labour markets. The increase in oil prices is expected to exert a larger impact on inflation in Europe than in the United States. Consumer prices in the United States and euro-11 area are likely to increase further by 2.5% and 1.7% respectively (1999: 2.2% and 1.1% respectively). Meanwhile, Japan is expected to experience zero inflation in year 2000 (1999: –0.3%), attributable to a pick-up in economic activity despite downward price pressures arising from structural disinflation. On the other hand, core inflation in the United Kingdom is expected to remain subdued at 2.2% in 2000, well below the official target of 2.5%. The favourable inflation situation would be partly policy-induced, arising from the prospects of higher interest rates, and partly due to falling prices of goods caused by intense retail competition, which would more than offset price increases in the services and housing sectors.

Growth in the volume of **world trade** is expected to expand strongly by 6–7% (1999: 3.7%), in line with sustained growth in the industrial countries and improving growth performance of the developing countries, in particular in the East Asian and Latin American countries. The current account deficit of the major industrial countries as a group is expected to deteriorate further to US$210 billion in 2000, due largely to the higher deficit in the United States. In the United States, the current account deficit is expected to deteriorate further to US$365 billion in view of the worsening trade balance and rising servicing cost of the growing foreign debt. Despite the improvement in exports to the euro-11 countries, the current account deficit in the United Kingdom is likely to remain virtually unchanged on account of the rapid increase in imports arising from strong domestic demand. In contrast, the current account position in Japan is likely to improve due to resumption in export demand from Asia and increase in net investment income following continued profit repatriation by Japanese corporations abroad.

Similarly, the current account surplus of the euro-11 countries as a whole is likely to increase, arising from the increased intra-euro trade and gains in export competitiveness as a result of the weaker euro.

East Asian Economies

Growth prospects for the regional economies in year 2000 are expected to be favourable as economic recovery gathers momentum and the region moves on to the next phase of recovery. The countries are expected to return to more broad-based and balanced growth, with the impetus to growth gradually shifting from net exports and fiscal stimulus to domestic private demand. At the same time, capital flows are also likely to pick up further although not yet to pre-crisis levels, reflecting improved investor confidence and higher economic activity in the region. Other factors that point to a positive regional outlook include the supportive external environment with the continued strong performance in the global electronics industry and further pick-up in intra-regional trade. The strengthening of domestic demand is expected to reinforce a virtuous upward cycle in regional growth, which would help to mitigate the adverse impact of any shortfall in demand from the industrial countries. In addition, the authorities in the region are expected to continue with growth-supporting policies in year 2000 to ensure a solid and sustained economic recovery. Inflation, although upward-biased, would remain benign in 2000. Given the low inflation scenario and the continued weakness in the corporate and banking sectors, rapid monetary tightening is not likely to take place during the year. Meanwhile, the fiscal balance of the regional countries (especially the crisis countries) are likely to improve during the year, arising from higher tax revenues from increased economic activity and company profitability.

In year 2000, **real GDP** growth in the **Asian Newly Industrialised Economies (NIEs)** as a group is expected to stabilise around 6.3–6.5% (1999: 6.8%), reflecting higher economic growth in all the countries except Korea. After recording an exceptionally strong performance in 1999 (10.2%), real output growth in **Korea** is likely to moderate to a more sustainable pace of 7.2% in year 2000. Growth is likely to be underpinned by increases in private consumption, investment and exports. Meanwhile, in **Taiwan**, real GDP growth is likely to pick up further to 6.5% (1999: 5.7%), led mainly by exports and higher private investment associated with the post-earthquake reconstruction and implementation of other major projects. Private consumption is also expected to strengthen further during the year.

Similarly, the pace of economic activity in **Hong Kong SAR** is expected to strengthen in 2000, with real output growth rising to around 5% (1999: 2.9%), buoyed by exports and a pick-up in domestic demand amidst a moderation in real interest rates. In addition, the prospective entry of The People's Republic of China into the World Trade Organisation is expected to improve overall sentiment and support domestic demand in Hong Kong SAR. In **Singapore**, real GDP growth is expected to be in the upper range of 4.5–6.5% (1999: 5.4%), with impetus to growth emanating from manufacturing exports, especially in the electronics and chemical industries, as well as an increase in private demand. Meanwhile, in **The People's Republic of China**, real output growth is

Table 3.2
East Asia: Selected Key Economic Indicators

	Average 1992-97	1998	1999*e*	2000*f*
	Annual change (%)			
Real GDP				
Asian NIEs	**6.6**	**–1.8**	**6.8**	**6.3 ~ 6.5**
Korea	6.7	–5.8	10.2	7.2
Taiwan	6.6	4.6	5.7	6.5
Singapore	9.2	0.3	5.4	4.5 ~ 6.5
Hong Kong SAR	5.2	–5.1	2.9	5.0
ASEAN[1]	**7.2**	**–6.1**	**3.6**	**4.4 ~ 5.0**
Malaysia	9.2	–7.5	5.4	5.8
Thailand	6.4	–10.4	4.0	4.5
Indonesia	6.9	–13.2	0.2	3.0 ~ 4.0
Philippines	3.8	–0.5	3.2	4.0
Vietnam	8.9	5.8	4.8	5.5 ~ 6.0
The People's Republic of China	11.5	7.8	7.1	7.0
Consumer prices				
Asian NIEs	**4.9**	**4.0**	**–0.4**	**1.7 ~ 1.8**
Korea	5.2	7.5	0.8	3.1
Taiwan	3.2	1.7	0.2	2.0
Singapore	2.1	–0.3	0.4	1.0 ~ 2.0
Hong Kong SAR[2]	8.1	2.8	–4.0	–1.0
ASEAN[1]	6.6	19.9	7.9	4.0 ~ 4.9
Malaysia	3.6	5.3	2.8	3.2
Thailand	5.0	8.1	0.3	2.5 ~ 3.0
Indonesia	8.2	58.4	24.0	5.0 ~ 7.0
Philippines	8.1	9.8	6.4	6.0 ~ 7.0
Vietnam	13.6	7.7	1.3	6.0
The People's Republic of China	12.2	–0.8	–1.4	1.0

[1] Includes Singapore, but excludes Brunei Darussalam, Lao PDR, Myanmar and Cambodia
[2] Refers to composite prices
e Estimates
f Forecast

Sources: IMF World Economic Outlook 1999
National sources

likely to stabilise at around 7% (1999: 7.1%), supported by a new fiscal stimulus, increased foreign direct investments and higher export demand from the industrial countries, which account for about 70% of China's exports.

The combined real GDP growth of the members of the **Association of South-East Asian Nations (ASEAN)** is expected to improve further to 4.4–5% in 2000 (1999: 3.6%), reflecting higher activity in all the countries. In **Thailand**, real GDP growth is expected to pick up to 4.5% (1999: 4%), following a strong expansion in manufactured exports led by electronics and further strengthening in private demand, supported by accommodative monetary and fiscal policies. Similarly, the **Philippine economy** is likely to grow at a faster pace of 4% (1999: 3.2%), supported by strong exports and expansion in the manufacturing sector. Meanwhile, the recovery in **Indonesia** is expected to gather momentum, with real GDP increasing by about 3–4% (1999: 0.2%), supported by a pick-up in exports from both non-oil exports benefiting from the competitive rupiah as well as oil exports arising from higher oil prices. At the same time, recovery in domestic demand is taking place in an environment of lower interest rates.

However, **risks** that could affect growth prospects of the regional countries remain. The main source of risk would emanate from the external environment. Given the strong correlation between the regional bourses and the performance of the Dow Jones, a sharp correction in the United States stock market could trigger a new bout of instability and declines in the regional financial markets. Developments in the stock and foreign currency markets could result through shifts of funds from the emerging markets. In addition, the global trend of higher interest rates, initiated by monetary tightening in the industrial countries could also dampen capital flows to the region. With the region still dependent on exports for growth, a significant slowdown in the United States, which accounts for about 22% of the region's exports, would affect the regional growth performance.

On the **inflation front**, the regional economies are expected to face some upward trend in prices in year 2000 as industries absorb excess capacity and private consumption strengthens with the steady economic recovery. Higher oil and world commodity prices are also contributory factors to inflation during the year. Nevertheless, inflation should remain under control and is not likely to impact growth prospects. Inflation in the **Asian NIEs** as a group is expected to rise to 1.7–1.8% (1999: –0.4%), reflecting higher consumer prices in all economies. In **Korea** and **Taiwan**, consumer prices are expected to increase at a higher rate of 3.1% and 2% respectively (1999: 0.8% and 0.2%), fuelled by rising international prices for raw materials and oil as well as stronger domestic consumption. To some extent, the higher prices would also reflect the low base effect, higher wages in Korea and price increases in Taiwan due to post-earthquake reconstruction. Nevertheless, imported inflation would remain subdued, restrained by the appreciation of their currencies.

Meanwhile, inflation in **Singapore** is expected to remain in the region of 1–2% (1999: 0.4%). The upside risks to inflation emanating from higher disposable income due to the restoration of previously cut wages and an increase in bonuses for civil servants may be somewhat offset by the strengthening of the Singapore dollar and a continuation of tax rebates. Deflationary pressures in **Hong Kong SAR** are likely to subside and inflation is expected to resume marginally in **The People's Republic of China** in 2000. In Hong Kong SAR, the composite consumer price index is expected to decline at a slower rate of 1% (1999: –4%), reflecting continued competition among retailers. In The People's Republic of China, consumer prices are projected to increase by 1% in 2000 (1999: –1.4%), due partly to the effects of recent measures taken to stimulate consumption. The measures included an imposition of a 20% tax on bank interest income, seven interest rate cuts since May 1996 and significant increases in wages of civil servants and low-income workers. Nevertheless, the continued excess supply in agriculture products is likely to restrain price increases.

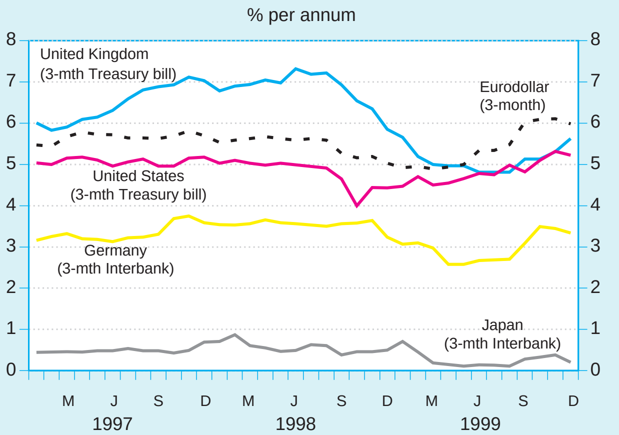
Despite higher price pressures in Thailand and the Philippines, inflation in the **ASEAN** countries as a group is expected to recede further to 4–4.9% in 2000 (1999: 7.9%), due mainly to the significant moderation in price increases in Indonesia. In **Indonesia,** inflation is expected to moderate to 5–7% (1999: 24%) reflecting the base effects, the appreciation of the rupiah and improving efficiency in the distribution network. In contrast, in **Thailand** and **the Philippines**, inflation is expected to rise to 2.5–3% and 6–7% respectively (1999: 0.3% and 6.4% respectively), reflecting the higher oil prices and stronger domestic demand. The reduction in excess capacity in Thailand and the increase in public sector wages in the Philippines are the contributory factors to inflationary conditions during the year.

In line with stronger economic growth, the **external account surpluses** in most of the regional countries are expected to narrow in year 2000. The pick-up in domestic demand is likely to stimulate import growth and lead to lower trade and current account surpluses. Hong Kong SAR, however, is expected to register a stronger current account surplus based on an expected strong export growth.

Interest Rates and Exchange Rates

Monetary policy in the major industrial countries was biased towards easing in the first half of 1999 against a backdrop of an economic slowdown, except for the United States. Both the European Central Bank (ECB) and Bank of Japan reduced their key rates by 50 and 10 basis points respectively, while the Bank of England was more aggressive, cutting interest rates four times during the period with a cumulative reduction of 125 basis points. On the other hand, in the United States, in view of the continued strength of the economy and robust stock market, the Federal Reserve Board embarked on pre-emptive monetary tightening to address inflationary pressures by raising the Federal funds rate by 25 basis points to 5% on 30 June. The move was subsequently accompanied by two further interest rate hikes totalling 50 basis points in the second half of the year. During this period, the Bank of England and the ECB also reversed their earlier monetary easing and raised interest rates by a total of 50 basis points each, prompted by the faster-than-expected economic recovery. Only the Bank of Japan maintained an accommodative monetary stance to facilitate the economic recovery as well as to contain excessive yen strengthening.

Graph 3.2
Industrial Countries : Short-Term Interest Rates



In the first two months of 2000, while Japan maintained its zero interest rate policy, the other major industrial countries continued to pursue monetary tightening due to concerns of overheating in their economies. The Federal Reserve Board and the ECB raised their key rates by 25 basis points each to 5.75% and 3.25% respectively to pre-empt potential inflationary risks. Meanwhile, the Bank of England was more aggressive, raising the key rates by 50 basis points to 6% to rein in the strength of the housing sector. For the remaining part of 2000, monetary policy in the major industrial countries other than Japan is expected to remain biased towards tightening. The extent of the tightening would, however, depend on the strength of the economic growth and on inflationary pressures, including developments in the asset markets. Policy directions would also be influenced somewhat by external factors such as the performance of the exchange rate and the sustainability of the current account. Meanwhile, Japan is expected to maintain an accommodative monetary policy to counter the risk of deflation and to support economic recovery.

In the **foreign exchange** markets, the United States dollar strengthened against all the major currencies in the first two months of 2000 to close at US$1=¥110.19, €1=US$0.9643 and £1=US$1.5786 at end-February. The dollar appreciated by 7.2% against the Japanese yen, 4.3% against the euro and 2.4% against the pound sterling compared with levels at the end of 1999. Against the yen, the dollar reversed its trend to strengthen, largely due to resumption in yen carry trades and to a lesser extent, weaker market sentiment on Japan's economic recovery. The dollar reached a six-month intra-day high of US$1=¥111.73 on 22 February, buoyed by continued expectations on the strength of the economic expansion in the United States.

Against the euro, the dollar strengthened markedly to a range below parity since the second half of January 2000 as European investors continued to diversify into non-euro financial markets. At end-month, market perception of lack of G-7 concern on the level of euro further exacerbated the weakness in the euro. Thereafter, the dollar continued to strengthen to touch an intra-day high of €1=US$0.939 on 28 February, its highest level against the euro since the debut of the euro on 4 January 1999. The euro was affected by uncertainty over the stance of the ECB in their foreign currency intervention and on structural issues such as the rules on corporate take-over in Germany. To some extent, the relative growth momentum between

Box IV

Pegged Exchange Rate Regime – Its Implications on the Malaysian Economy

Introduction

The Asian financial crisis was, to a large extent, a reflection of the shortcomings of the international financial system in coping with the growth in capital flows across borders. Among the many strategic issues highlighted in the aftermath of the crisis was the need to reassess exchange rate policies. The rapid movements in short-term capital, the so-called "hot money", had resulted in conflicts between domestic macroeconomic policy and exchange rate arrangements in many of the South-East Asian economies. As a result, most of the crisis-affected countries that had previously operated under pegged *(de facto* or *de jure)* or banded exchange rate regimes moved to more flexible exchange rate arrangements. On the other hand, Malaysia, which had previously operated under a managed float, adopted a pegged exchange rate arrangement, by pegging the ringgit exchange rate to the United States dollar on 2 September 1998. The ringgit was pegged at a level of RM3.8000 = US$1, which was the rate prevailing in the Kuala Lumpur interbank foreign exchange market at that time. This was also the rate at which the ringgit was, on average, traded during February to June 1998.

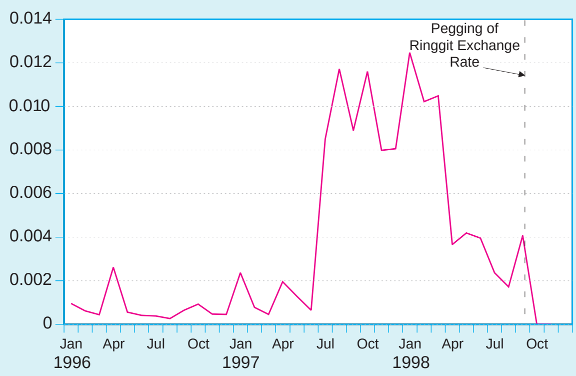
Why Malaysia moved to a pegged exchange rate arrangement

The move to a pegged exchange rate arrangement was to reduce the volatility of the ringgit exchange rate and to promote a stable environment conducive to economic recovery. As shown in Graph IV.1, throughout the crisis period, the ringgit experienced a sharp increase in volatility. The increased volatility was not due to any change in the fundamentals of the economy, but was the outcome of contagion, speculation and the movement of non-resident short-term capital. The resulting uncertainty made pricing and investment decisions of businesses increasingly difficult. The establishment of the pegged exchange rate arrangement aimed to restore some element of predictability within the economy.

For a small, open economy like Malaysia, the exchange rate is a very important price. Movements in the exchange rate can beneficially correct disequilibriums in the balance of payments that are caused by economic fundamentals. However, this becomes more complicated when the changes in the exchange rate are caused not by fundamentals, but by short-term capital flows. The increasing global market integration has led to surges of short-term foreign investment by institutional investors seeking higher returns mostly in the asset markets of emerging economies. By allowing the exchange rate to respond to these surges of inflows and outflows by appreciating and depreciating respectively, the exchange rate will experience greater volatility that will be highly costly to the tradables sector.

The question arises whether allowing the exchange rate to move in response to volatile short-term capital flows is the optimal policy for a trade dependent country like Malaysia. The degree to which different countries can tolerate wide swings in their exchange rates depends on the relative openness of their economies. The more open the economy, the greater would be the adverse economic consequence of any sustained volatility in the exchange rate. Countries like Hong Kong

Graph IV.1
Monthly Standard Deviation of RM/USD Exchange Rate



SAR and Singapore make the maintenance of exchange rate stability the primary focus of their monetary policy because of the crucial role external prices play in determining their economic welfare. Similarly, it is unrealistic to expect Malaysia, with trade accounting for 203% of GNP in 1999, to allow its exchange rate to move erratically in response to short-term flows over a prolonged period.

Benefits of a pegged exchange rate arrangement for the economy

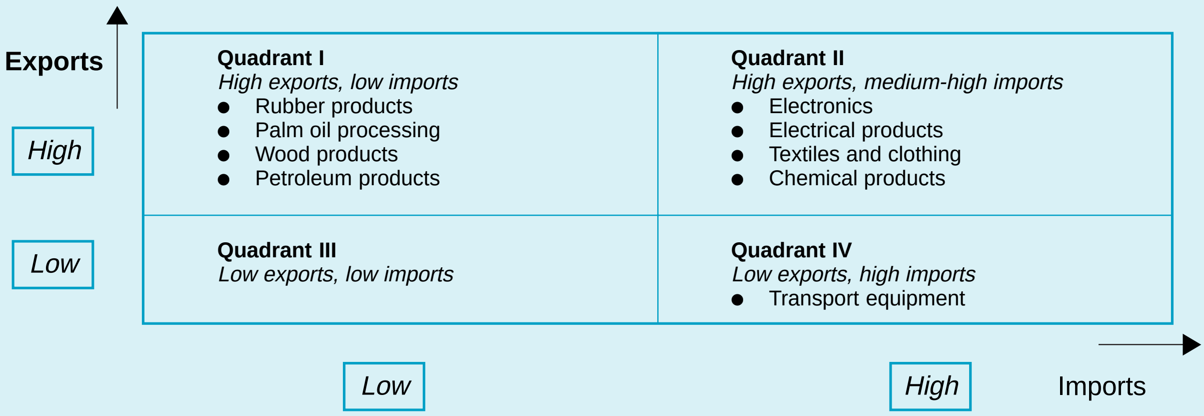
The main benefit of the introduction of the pegged exchange rate regime in Malaysia was relative stability in the foreign exchange market. Economic agents, such as businesses and consumers, base their decisions concerning production, investment and consumption on the information that the price system provides. If these prices become more uncertain, the quality of these decisions will decline and it will be difficult for businesses to generate reliable forecasts of their future earnings. In a volatile environment, the exchange rate becomes less reliable as a mechanism to allocate resources efficiently. Thus, the reduction in exchange rate variability through the pegged system has resulted in efficiency gains to the economy. These welfare gains are more evident for countries such as Malaysia, which trade a large proportion of goods and services with foreign countries.

The pegged exchange rate regime has helped the pricing and investment decisions of companies in Malaysia. During the first three quarters of 1998, the volatility in ringgit movements against the US dollar complicated the process of business planning and cost accounting of exporters, resulting in uncertainties and causing a reduction of new export orders and potential export opportunities. With the pegged exchange rate arrangement in place, Malaysian manufacturers and exporters were able to capitalise on the exchange rate stability to resume normal business activities as external demand began to improve in October 1998. Approximately 85% of Malaysia's trade is settled in US dollars. With this high concentration of settlements in the dollar, the single currency peg has been effective in fostering stability for the majority of the trade sector.

During the crisis, the effective policy responses of the government were always hampered by the instability of the exchange rate. In the initial stages, the response of the Government was directed towards halting the further depreciation of the ringgit as well as limiting the effect on inflation. When the policymakers decided to shift to ease monetary policy following the sharper-than-expected contraction in the real economy, their efforts were constrained by the need to support the exchange rate. For policymakers, the pegging of the exchange rate removed the issue of managing the day-to-day movements of the ringgit exchange rate. Further depreciation of the ringgit was effectively halted and this, along with the selective exchange controls, allowed policymakers to concentrate on rebuilding the other sectors of the economy. Interest rates were reduced, facilitating the use of monetary policy to support fiscal policy in the recovery process. The low interest rates and stable exchange rates also ensured a greater chance of success for efforts to restructure the banking and corporate sectors.

The pegging of the ringgit exchange rate has benefited the external sector due to the subsequent favourable movement of the US dollar. Some improvement in external competitiveness can be seen in the strong performance of the current account of the balance of payments. The trade balance recorded a surplus of RM98.2 billion during the period from September 1998 to end-1999. This improvement in the current account balance has been due to favourable external demand, especially in the electronics sector, the stability of the ringgit exchange rate against a key currency and the improvement in external competitiveness following the pegging of the ringgit.

The effect of the increased competitiveness due to the subsequent appreciation of the regional currencies against the ringgit differs across the various sectors of the economy. Generally, the sectors of the economy that will benefit from both the increased stability in the exchange rate as well as the improved competitiveness are the tradable sectors of the economy. The largest traded sector in the Malaysian economy is the manufacturing sector. However, the degree to which the different industries within the manufacturing sector have benefited vary according to the mixture of import content in their production as well as the share of exports in total production. The following matrix



divides the various industries in the manufacturing sector into four quadrants according to their level of import content and share of exports.

Generally, the industries that are located in Quadrant I, which are the resource-based industries, would benefit the most from the improved competitiveness. To a lesser extent, the high exports, medium-high imports industries (Quadrant II) such as electronics and electrical products, would stand to benefit as well. In contrast, industries in Quadrant IV, such as the transport equipment industry, would benefit the least due to their higher cost of production. Table IV.1 shows the annual growth in exports and volumes of production of the respective industries in the manufacturing sector for 1998 and 1999.

On the whole, the export performance of the various industries reflect what would have been expected, given the distribution of the industries in the matrix above. The resource-based industries such as petroleum and wood products registered two of the three highest growth rates in terms of exports. However, the rubber products industry registered a negative growth in exports in 1999. This was a result of lower export prices for rubber products, particularly the rubber gloves segment. In the non-resource based industries, the high export, medium-high import industries all registered positive growths in their exports for 1999. As expected, the transport equipment sector, which is very import-intensive, registered a decline in export growth of 35.5%.

Table IV.1: Performance of Major Industries in the Manufacturing Sector

	Exports (US$)		Production	
	1998	1999	1998	1999
	Annual growth in %			
Overall Manufacturing Sector	–4.6	17.6	–10.2	12.9
Non-resource based industries				
High export, medium-high import				
Electronics	*1.9*	*30.4*	*–4.2*	*21.2*
Electrical products	*–11.4*	*8.8*	*–14.8*	*2.7*
Textiles and clothing	*–11.0*	*3.4*	*–5.3*	*4.0*
Chemical products	*–6.6*	*7.6*	*–1.8*	*17.1*
Low export, high import				
Transport equipment	*17.1*	*–35.5*	*–52.2*	*53.5*
Resource-based industries				
High export, low import				
Rubber products	*3.9*	*–9.1*	*7.8*	*3.6*
Wood products	*–34.3*	*20.3*	*–11.3*	*–7.3*
Petroleum products	*–33.4*	*48.9*	*–11.5*	*–0.3*

In terms of volumes of production, the non-resource based industries that have experienced a growth in exports have also experienced a growth in production. The exception to this generality is the transport equipment industry. While exports declined for the year, the volume of production for the transport equipment sector increased by 53.3% in 1999, primarily due to a surge in domestic demand.

It is important to note, however, that the pegged exchange rate arrangement only pegs the nominal exchange rate and not the real effective exchange rate. The true measure of competitiveness comes from the real exchange rate, which takes into account the relative inflation performance of the economy as well. Therefore, the benefits derived from the movements of the US dollar against other currencies which has increased our competitiveness, will be insofar as the inflation in Malaysia is lower than that of our competitors. Furthermore, the competitive benefit from an exchange rate is transitory, and true competitiveness can only be obtained by increasing efficiency and enhancing productivity.

Risks of a pegged exchange rate regime

The move to a pegged exchange rate regime also introduces a new set of risks to the economy. The possibility of misalignment of the currency is one of the major risks in a pegged exchange regime. Misalignment is defined as a departure in the existing exchange rate from some measure of a fundamental equilibrium exchange rate. Misalignment can originate from a variety of sources. Changes in relative price levels, trade barriers, preferences of domestic versus foreign goods as well as improvements in the relative productivity of the economy are key factors that affect the fundamental exchange rate over the long run. Apart from these fundamental factors, movements of short-term capital as well as substantial movements in the value of the anchor currency can result in temporary misalignment.

When there is a misalignment in the exchange rate, some form of nominal adjustment has to take place in order to bring the real exchange rate into equilibrium. This nominal adjustment can take place through wage and price changes or through factor mobility. Misalignments can also cause the inefficient allocation of resources in an economy.

The degree of misalignment of an exchange rate needs to be assessed carefully. It is recognised that the “correct” level of an equilibrium exchange rate is difficult to determine due to the dynamic nature of the equilibrium as well as the variety of short-term and long-term factors that influence the rate. Therefore, continuous monitoring of developments in the Malaysian economy as well as in the regional economies is important to ensure that the exchange rate is consistent with the fundamentals. Currently, the issue of misalignment is not a concern given that inflation is expected to remain moderate over the medium term.

In the literature on exchange rates and financial fragility that followed soon after the outbreak of the Asian crisis, the risk of moral hazard behaviour by corporations has been continuously raised. Pegged exchange rate regimes were seen to be equivalent to an implicit guarantee by the Government and hence a source of moral hazard. This guarantee implies that, under a pegged exchange rate regime, companies and investors do not take into account the full risks of their investments, which in turn creates an incentive to take on excessive risk. Apart from promoting unhedged foreign currency borrowing, pegged regimes also skew flows more toward shorter maturities as these regimes are not seen to be credible in the long run. The experience of some Latin American and South-East Asian countries in the 1990s seem to corroborate this hypothesis.

In the Malaysian case, the risk of moral hazard under a pegged exchange rate regime has been contained. Prudential guidelines regarding external borrowing have long been in place even prior to the crisis. BNM’s approval is required for all external borrowings. Approvals are only given for investments that would generate sufficient foreign exchange receipts to service the debt, hence serving as a natural hedge with regards to foreign exchange exposure. Banks, on the other hand, are subject to net open position limits that vary according to the dealing capacity of the individual bank. Regulation and more vigorous supervision of the financial system have ensured that the financial institutions comply with these regulations. These prudential guidelines have limited the external exposure of Malaysian companies and banks, making thems less vulnerable to the effects of the depreciation of the ringgit during the crisis.

However, there is still the risk that there may be companies that have foreign currency exposures, such as exporters and importers, that are not adequately hedged. One of the lessons learnt from the experience of other countries during the crisis was that there should not be too much reliance on the level of the exchange rate. While it may be profitable to cut back on the cost of hedging, such practices reflect poor risk management on the part of the exporters and importers and may result in higher costs in the long run.

Another argument that has been put forward is that the pegged exchange rate regime might reduce the incentive for the corporate sector to restructure. Countries that emerge from recessions due to exchange rate advantages, in which export-oriented companies benefit significantly as a result of the depreciation following a crisis might be adversely affected over the medium term. Because of the exchange rate edge during the crisis period, the corporate sector might not restructure their operations to become efficient and lower unit cost of output. As a result, such countries would be subsequently set back. For those corporations that became much leaner and have reduced their costs of operations through restructuring, they have greater potential to prosper. There is a need for new investments in technology and to identify new growth areas, in order to gain the competitive edge in the global market. While Malaysian companies may be enjoying some benefits due to the movements in the regional countries' nominal exchange rates, it is recognised that this may not be a permanent phenomenon. Progress will have to be made to restructure in order to gain greater competitiveness.

Implications of a pegged exchange rate regime on monetary policy

A pegged exchange rate regime has implications for the conduct of monetary policy. Generally, domestic monetary policy has to follow the monetary policy of the country to which the currency is pegged. However, in the case of Malaysia, the pegged exchange rate regime was instituted against the backdrop of selective exchange controls. The selective exchange controls, which reduced the degree of the free-flow of capital, have granted the authorities some degree of independence in monetary policy. In this environment, Malaysia has the latitude to set its own level of interest rates in order to achieve domestic objectives.

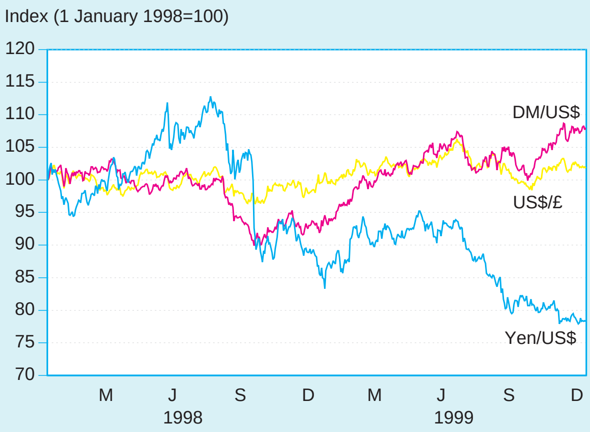
Another implication of a pegged exchange rate arrangement on monetary policy is that in an environment of capital inflows, BNM has to conduct sterilisation operations by absorbing the excess liquidity. In an environment of capital outflows, however, the reverse will be the case. Thus, the liquidity operations of BNM has to adjust in order to preserve the objectives of monetary policy.

Under a pegged exchange rate regime, the burden of adjustment to external shocks will fall on the international reserves of the country. The volatility in exchange rates will be substituted by volatility in the level of reserves. Due to BNM's intervention operations in order to maintain the peg in the face of capital flows, the level of reserves will experience corresponding changes. An adequate level of reserves is therefore important for promoting confidence in the sustainability of a pegged regime.

Conclusion

A large amount of literature on exchange rates have concluded that there is no one exchange rate regime that is appropriate for all countries. The differences among countries in levels of economic and financial development as well as in other aspects of economic situation will determine the suitability of a particular exchange rate arrangement. The pegged regime has functioned efficiently for Malaysia in providing a stable environment against which the revival of economic activity and the acceleration of financial reforms have taken place. The stability has been welcomed by manufacturers as it has allowed them to conduct their operations in an environment of greater predictability. This has contributed to the overall economic recovery process.

Graph 3.3
Movement of the US Dollar against Major Currencies



the United States economy and the euro-11 reinforced the weakness of the euro.

Against the sterling, the dollar fell initially to reach an intra-day low of £1=US$1.6578 on 21 January 2000, dampened by expectations of more aggressive monetary tightening in the United Kingdom relative to the other major economies. Nevertheless, the gains were reversed thereafter as the dollar strengthened since end-January to reach a seven-month high of £1=US$1.5786 on 29 February, as a result of spillover effects from the cross currency trading of euro/dollar and sterling/euro. However, relative to other currencies, the dollar had traded in a narrow range against the pound sterling as both the tightening cycle in the United States and the United Kingdom were perceived to be in line with minimal overshooting. For the remaining part of the year, the major currencies are likely to be influenced by a number of factors, such as portfolio adjustments in response to interest differentials and asset market valuations as well as the fundamental strength of the major economies during the monetary tightening cycle.

Malaysian Economy in 2000

Growth in the Malaysian economy is expected to be sustained in year 2000, while the external sector will continue to strengthen. Against the more favourable external environment and strengthening domestic economy, the forecast for GDP growth for 2000 has been revised upwards to 5.8%, from the earlier estimate of 5%. Given the strong recovery in the regional economies and the generally favourable world economic outlook for 2000, export growth is expected to be sustained at a high level. Other assumptions for growth in 2000 include an expansionary fiscal policy supported by an accommodative monetary policy. The external sector is expected to remain strong although the current account will narrow in line with higher output growth.

All domestic demand components are expected to record positive growth in 2000. In particular, **private consumption** is estimated to increase by 9.5% to become the main driver of growth. Measures to promote consumption under the 2000 Budget together with strong export performance will increase the disposable income of Malaysians, thereby strengthening consumer sentiments and expenditure. Consumption-related measures under the 2000 Budget include a one percentage point across-the-board reduction in personal income tax rates, higher tax relief and salary adjustments for civil servants and pensioners and another round of tariff reductions on 305 items. The fiscal stimulus will also support growth in consumption. The bulk of the net development expenditure of the public sector will continue to be spent on small- and medium-size projects, educational infrastructure and low-cost housing. These areas have strong linkages with other sectors in the economy and will, therefore, enhance the multiplier impact on private consumption. In addition, the broad-based recovery in exports of manufactured goods, saw logs and crude oil will support further improvement in capacity utilisation and generate more employment opportunities. Thus, these developments are expected to raise private consumption to exceed pre-crisis levels in real terms.

Table 3.3
Contribution of Demand Components to Real GDP Growth

	1999*p*	2000*f*
	(% contribution)	
Aggregate Domestic Demand	**1.6**	**6.2**
Private Consumption	1.1	4.1
Private Investment	–3.3	0.6
Public Consumption	2.3	0.0
Public Investment	1.3	1.3
Net Exports	**3.8**	**–0.4**
Exports of Goods & Non-factor Services	14.0	11.4
Imports of Goods & Non-factor Services	10.2	11.8
Gross Domestic Product	**5.4**	**5.8**
Aggregate Consumption	3.4	4.2
Aggregate Investment	–2.1	1.9

p Preliminary
f Forecast

Source: Department of Statistics and Bank Negara Malaysia

Table 3.4
GNP by Expenditure Components
(in 1987 prices)

	1999*p*	2000*f*
	Annual change (%)	
Real aggregate domestic demand[1]	**1.6**	**7.3**
ı Consumption	6.1	7.4
ı Investment	–6.8	7.2
Aggregate private demand[1]	**–3.5**	**8.3**
ı Consumption	2.5	9.5
ı Investment	–19.0	4.5
Aggregate public demand[1]	**14.8**	**5.2**
ı Consumption	20.1	0.2
ı Investment	10.1	10.0

[1] Exclude stocks
p Preliminary
f Forecast

Source: Department of Statistics and Bank Negara Malaysia

Private investment, which had remained subdued in 1999 owing to excess capacity in several sectors in the economy, is now projected to turn around to register a positive growth of 4.5% in 2000 (–19% in 1999). Companies are expected to expand capacity in 2000 in response to the steady rise in consumer demand underpinned by strong economic recovery, improved employment opportunities, favourable export prospects and higher commodity prices. Ample liquidity conditions due to large surpluses in the current and long-term capital accounts of the balance of payments and a low inflation environment will enable interest rates to remain supportive of private investment. Private sector investments are expected to be channelled into new growth areas and promoted sectors such as education and skills training, venture-type projects, medium- and low-cost housing, and agriculture and rural development. While public sector expenditure continues to provide a stimulus, the Government will gradually scale down its fiscal spending given the recovery in private expenditure. Consequently, growth in **public sector expenditure** is expected to moderate from 14.8% in 1999 to 5.2% in 2000. Overall, **real aggregate domestic demand** is expected to strengthen further by 7.3% in 2000 (1999: 1.6%) due mainly to stronger recovery in private sector expenditure.

On the **supply** side, growth is expected to be more broad-based, led by the manufacturing and services sectors. The construction, agriculture and mining sectors are also expected to contribute to growth, although at relatively moderate rates.

Table 3.5
Real GDP Growth (in 1987 prices)

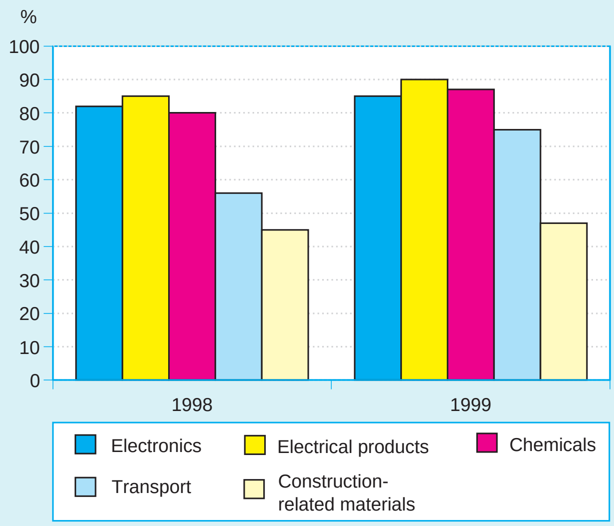
	1999*p*	2000*f*
	Annual growth (%)	
Real GDP	5.4	5.8
Agriculture	3.9	2.0
Mining	–4.0	2.1
Manufacturing	13.5	10.0
Construction	–5.6	5.0
Services	2.9	5.4

p Preliminary
f Forecast

Source: Department of Statistics and Bank Negara Malaysia

Prospects for the **manufacturing sector** remain favourable in 2000. Expected sustained external and domestic demand will support further expansion of value added by 10%. In January 2000, the industrial production index of the manufacturing sector increased by 37.4%. During the year, a broad-based expansion is expected to continue, with the export- and domestic-oriented industries recording further increases in output, at 10% and 9.6% respectively. Among the export-oriented industries, the electronics industry, in particular, is expected to maintain a strong output growth, supported by more widespread usage of the internet, e-commerce and mobile phones and other telecommunications equipment worldwide. At the same time, the production of electrical products is envisaged to increase amidst sustained improvement in demand especially from the US, Japan and the Asia Pacific region. Moreover, the introduction of new products such as flat screen televisions, digital video disc and

Graph 3.4
Capacity Utilisation of Selected Industries in the Manufacturing Sector



video compact disc players would also contribute to growth. In the domestic-oriented sector, the expected strengthening in domestic consumption and pick-up in construction sector activity augur well for output performance of the transport equipment and construction-related materials industries. Meanwhile, the production of chemical products is expected to increase, in tandem with favourable developments in the electronics, transport equipment and construction-related materials industries. The expected expansion of output in the manufacturing sector is envisaged to lead to higher capacity utilisation in the sector. Currently, capacity utilisation has risen to an average of 85% for export-oriented industries and 78% for domestic-oriented industries.

With the improved outlook for the economy, value added in the **services sector** is expected to increase by 5.4%. Growth will emanate from the intermediate and final services sub-sectors. For the intermediate services sub-sector, growth is expected to be sustained by buoyant activity in the manufacturing sector based on the expectation of continued growth in both the external and domestic sectors. In particular, demand for transport, storage and communications services is expected to pick up strongly, reflecting mainly a strong increase in external trade. Activity in the finance sub-sector is also expected to increase, reflecting the projected higher loan growth and the favourable outlook in the equity market. Meanwhile, the return of consumer confidence and the expected increase in tourist arrivals from 8 million in 1999 to 8.5 million in 2000, are expected to contribute to higher growth in the wholesale, retail trade, restaurants and hotels sub-sector. Similarly, value added in the utilities sub-sector is projected to increase further in response to expected higher demand from the industrial and commercial sectors.

In the **agriculture sector,** growth is expected to moderate to 2% in 2000, due mainly to the slower increase of 2.7% in crude palm oil production as yields will be affected by the downturn in the biological yield cycle of the oil palm trees. While rubber production is projected to decline further during the year, the production of saw logs is forecast to increase by 3.3% in response to expected higher external demand, especially from Japan, The People's Republic of China and Korea.

Value added in the **mining sector** is expected to turn around to record a positive growth of 2.1%, attributable mainly to higher gas production (9.3%) as crude oil production is expected to increase marginally by 0.4%. The projected increase in natural gas production was premised on expectations of higher domestic and external demand, in addition to the commencement of operations of a new gas field during the year. Crude oil production will be maintained at about the level in 1999, at 694,000 barrels per day (bpd) (1999: 693,200 bpd), in line with the National Depletion Policy.

Following two years of adjustments, the **construction sector** is expected to turn around to grow by 5%. Growth will emanate mainly from development of residential and civil engineering projects. In the residential sector, construction of low- and medium-cost houses is expected to remain strong, underpinned by strong underlying demand and low interest rates. At the same time, the increase in new developers' licences issued and loans approved by the housing credit institutions during 1999 will pave the way for new construction activity in 2000. The civil engineering sub-sector will benefit from the Government's continued efforts to improve infrastructure development, particularly for the construction, upgrading and improvement of roads and highways. On the other hand, construction of new commercial buildings is expected to remain subdued in view of excess supply and the guideline prohibiting banking institutions from financing the development of new hotels, resorts, office buildings, golf courses, clubs and shopping complexes effective 6 January 1999. Hence, activity will be supported mainly by ongoing projects. Reflecting the prospects of a recovery in the construction sector, BNM's 1999 Survey of the Construction Sector showed that construction activity of the companies surveyed is expected to pick up by 17.8%.

Generally there is greater optimism that **downside risks** to growth prospects for 2000 are limited. The main area of vulnerability for the region is the downturn in the US economy arising from a sharp correction in the United States stock market. However, pre-emptive measures taken by the Federal Reserve Board to rein in aggregate demand emerging from the wealth effect of the strong performance of the equity markets have so far successfully avoided this development. Interest rates have been gradually raised in four steps of 0.25 percentage points since June 1999 to ensure a soft landing. The Federal Reserve Board has also clearly indicated that further increases in interest rates are likely to manage the inflationary expectations and to deflate the emerging asset bubble. Notwithstanding this development, the Federal Reserve Board is likely to reduce interest rates in the event of a major correction in the United States stock market so as to manage the systemic risks emerging from a downturn in economic activities. This is based on the track record of the Federal Reserve Board in using monetary policy to prevent an over-adjustment if share prices experience a major correction. In 1987, the Federal Reserve Board responded promptly after the stock market crash on 19 October by injecting liquidity into the system to prevent the economy from spiralling downwards abruptly. Similarly, in 1998, the Federal Reserve Board was quick to arrange financing support in response to emerging systemic risks to the US economy arising from the collapse of the hedge fund, Long-Term Capital Management, following the Russian debt moratorium in August 1998.

Another area of concern is the uncertainty over the sustainability of the current upswing in the electronics industry although there is increasing evidence that the upward trend in the electronic cycle is expected to continue beyond 2000. While there is concern about the over-reliance of the manufacturing sector on the electronics industry (accounting for more than half of total manufactured exports and one-fifth of manufacturing value added), the relatively well diversified product mix exported by the Malaysian electronic manufacturers would help to mitigate any undesirable effects arising from the cyclical nature of the electronics industry. Moreover, both the multinationals and domestic manufacturers have built a strong foundation for the industry in terms of capital investment, input sourcing and product marketing channels. These developments, complemented by adequate infrastructure and the availability of skilled labour, would continue to provide strength to the electronics manufacturers and exporters to build on existing capabilities as well as enhance their competitiveness in niche products/ markets with growth potential.

On the domestic front, the current ringgit peg against the US dollar has often been cited as a possible source of instability, contributing to loss of competitiveness. The main concern of market participants at this point is that ringgit is undervalued and the external liquidity generated from the strong balance of payments position would contribute to inflationary pressures. An appreciation in the real effective exchange rate arising from an increase in domestic inflation would undermine external competitiveness of the economy. However, a closer look at the fiscal position, the savings-investment gap as well as the potential output gap indicates that inflationary pressures are likely to remain subdued in 2000. With the momentum in the domestic economic activity increasing, the output gap will narrow and this may result in some inflationary pressures in 2000. However, while excess capacity is declining, it is likely to remain significant in several industries. The increase in inflation, is therefore projected to edge up slightly to 3.2% from 2.8% in 1999, largely reflecting the structural constraints in the food sector. While the labour market situation is expected to tighten with the unemployment rate remaining low at 2.9% in 2000, wage pressures are expected to remain subdued because of the expectation of greater labour mobility from surplus to deficit areas. In addition, given the competitive environment, the increases in wage costs are expected to be commensurate with productivity improvements, hence mitigating the potential for the build-up of inflationary pressures.

Notwithstanding the mildly expansionary public sector spending programme, the fiscal position is not expected to be a source of inflationary pressures. Based on the revised 2000 Budget announced on 25 February 2000, the current account of the Federal Government is expected to remain in surplus notwithstanding the 10% salary adjustment for civil servants and pensioners. With higher revenue collection, the current account is expected to record a surplus of RM7.5 billion or 2.5% of GNP. While net development expenditure is expected to remain high at RM20.9 billion, this amount is marginally lower than in 1999 (RM21.5 billion). Overall, the fiscal deficit of the Federal Government is expected to amount to RM13.4 billion or 4.5% of GNP, well below the 6% cap set earlier. As the recovery process strengthens to allow the private sector to resume its role as the engine of growth, there will be fiscal consolidation, enabling the Government to revert to

Table 3.6
Federal Government Finance

	1999*p*	2000*f*
	(RM billion)	
Revenue	58.7	61.8
Operating expenditure	46.7	54.3
Current account	**12.0**	**7.5**
(% of GNP)	**(4.3)**	**(2.5)**
Net development expenditure	21.5	20.9
Overall account	**–9.5**	**–13.4**
(% of GNP)	**(–3.4)**	**(–4.5)**

p Preliminary
f Forecast

Source: Ministry of Finance

a surplus position. Given ample liquidity in the banking system, a large proportion of the fiscal deficit would continue to be financed from non-inflationary domestic sources. As a result, the Federal Government's external debt would be maintained at low levels (5.4% of GNP in 2000), due mainly to drawdown of loans committed earlier under both bilateral and multilateral programmes. Private sector activities are not likely to be crowded out given that liquidity generated from the surplus in the current account of the balance of payments in 2000 is expected to be sustained.

Despite the projected stronger growth in imports, the **current account of the balance of payments** is expected to remain in surplus in 2000 due to several factors. The projected import growth is expected to emanate mainly from higher imports of intermediate goods, which are necessary inputs for the production of manufactured goods for exports. Imports of capital goods are expected to register a marginal increase, as the import content of investment activity is likely to be low in the immediate term because of high capital outlay in the pre-crisis period, particularly in infrastructure projects. Generally, the increases in imports would be mainly for capital imports in projects with shorter gestation period that are likely to directly generate export earnings, for example, expansion in the higher value-added electronics sector. The fiscal stimulus package has also targeted those activities with low import content such as basic infrastructure, education and low-cost housing. Moreover, the new growth is anticipated to be supported by more efficient use of existing resources. Consequently, the current account of the balance of payments is expected to remain strong in 2000, recording another surplus of RM42.6 billion or 14.2% of GNP.

In the merchandise account, **exports of manufactured goods** in US dollar terms are projected to increase by 14% in 2000, arising from expected sustained demand from the industrial countries and a stronger economic performance in the region. During the year, growth is expected to emanate mainly from the electronics, electrical products, wood products, furniture and parts and chemical products industries. With its high contribution to total manufactured exports, the electronics industry is envisaged to remain an important impetus for growth. Exports of the electronics industry is projected to be sustained at a double-digit expansion, underpinned mainly by increased usage of the internet, e-commerce and increasing demand for communication chips for use in computer modems and cellular

Table 3.7
Balance of Payments

	1999*e*	2000*f*	1999*e*	2000*f*
	RM billion		US$ billion	
Merchandise	83.5	83.4	22.0	21.9
Services	–28.9	–32.9	–7.6	–8.7
Transfers	–7.2	–7.9	–1.9	–2.1
Balance on current account	**47.4**	**42.6**	**12.5**	**11.2**
(% of GNP)	*16.9*	*14.2*	*16.9*	*14.2*
Long-term capital	11.7	7.9	3.1	2.1
Basic balance	**59.1**	**50.5**	**15.6**	**13.3**
Short-term capital	–36.0		–9.5	
Errors & Omissions	–5.3		–1.4	
Overall balance	**17.8**		**4.7**	
BNM international reserves	**117.2**		**30.9**	
Months of imports	*5.9*		*5.9*	
Reserves/ST debt	*5.1*		*5.1*	

e Estimates
f Forecast

Source: Department of Statistics and Bank Negara Malaysia

phones. The favourable growth forecast is in line with the projection of the Semiconductor Industry Association that sales of the global semiconductor industry is expected to grow by 21% in 2000 (1999: 18.9%). Reflecting the favourable external demand prospects, export volume is expected to expand by 13.3%, while US dollar export prices are expected to turn around to record a marginal growth of 0.4% in 2000.

Total export earnings from the commodity sector is forecast to decline by 8.5% to RM41.1 billion in 2000 due mainly to lower export earnings from palm oil. Overall, the outlook for **commodity prices** in 2000 is somewhat mixed. While prospects for crude oil, timber and rubber are favourable, further declines in crude palm oil prices are expected. The overall commodity export unit value is forecast to decline by 3.8% during the year. However, excluding crude palm oil prices, the overall commodity price index is expected to increase by 5.5%. During the year, crude palm oil prices are expected to average RM1,250 per tonne (1999: RM1,615 per tonne) as the current situation of ample global supplies of vegetable oils is expected to remain. In particular, the large carry-over of palm oil stocks from 1999 is expected to weigh down on palm oil prices during 2000. On the other hand, the price outlook for saw logs and sawn timber is expected to be more favourable with prices expected to increase further on expectations of increased external demand,

Table 3.8
Exports and Imports

	1999	2000*f*	1999	2000*f*
	RM billion		US$ billion	
Gross exports	**321.2**	**356.2**	**84.5**	**93.7**
(% change)	**12.1**	**10.9**	**15.3**	**10.9**
Manufactures	271.7	309.9	71.5	81.5
(% change)	14.3	14.0	17.6	14.0
Minerals	17.2	17.1	4.5	4.5
(% change)	15.9	–0.6	19.6	–0.6
– Crude oil	9.3	9.1	2.4	2.4
(% change)	23.9	–1.8	27.7	–1.8
– Production ('000 bpd)	693.2	694.0	693.2	694.0
– Unit value (US$/bbl)	18.18	20.00	18.18	20.00
Agriculture	27.7	24.0	7.3	6.3
(% change)	–8.4	–13.4	–5.5	–13.4
Gross imports	**248.9**	**286.0**	**65.5**	**75.3**
(% change)	**9.1**	**14.9**	**12.3**	**14.9**
ı Capital goods	33.0	33.6	8.7	8.8
(% change)	–8.9	1.8	–5.9	1.8
ı Intermediate goods	182.2	215.1	48.0	56.6
(% change)	13.2	18.0	17.3	18.0
ı Consumption goods	15.5	16.5	4.1	4.4
(% change)	17.8	7.0	21.3	7.0
ı Dual-use goods	4.9	5.2	1.3	1.4
(% change)	29.0	5.3	33.4	5.3

f Forecast

Source: Department of Statistics and Bank Negara Malaysia

particularly from the Asia-Pacific markets amidst tight global supplies of tropical wood. Meanwhile, rubber prices are expected to increase moderately as global demand improves. In the minerals sector**, crude oil prices are forecast to average US$20 per barrel** (1999: US$18.18 per barrel). Prices recorded during January-February 2000, averaging US$26 per barrel, are not expected to be sustained as global production of crude oil is expected to increase in the face of rising global demand and declining inventories. Developments in crude oil prices would be influenced largely by OPEC's production.

With **merchandise imports** expected to increase only at a slightly faster rate, the surplus in the merchandise account is expected to be sustained at about the same level as in 1999 (RM83.4 billion), more than adequate to finance the net payments for services imported. Higher net outflows in investment income, freight and insurance as well as other services accounts are expected to contribute to the higher deficit in the **services account** (–RM32.9 billion or 11% of GNP). The projected larger outflow in investment income is due to the strong export performance by the electronics industry as well as other export-oriented industries. Higher imports are also expected to lead to higher payments for freight and insurance. However, the travel and other transportation accounts are expected to post improved performances with expected net inflows of RM6.7 billion and RM3 billion respectively, contributed mainly by the tourism sector. Net transfer payments are expected to increase to RM7.9 billion.

In the **capital account**, the Federal Government is expected to record a net repayment in 2000 due to both lower borrowings as well as higher repayment of loans. The NFPEs, however, are expected to continue to record a larger net borrowing in 2000 due to increased borrowings to finance capital expenditure, domestically as well as abroad. Gross inflows of direct foreign investment are expected to increase moderately in 2000. Overall, the basic balance, comprising the current account and the long-term capital account is projected to record a surplus of about RM50.5 billion or US$13.3 billion.

The total **external debt** outstanding is expected to decline by 1% to RM158.8 billion by end-December 2000, equivalent to 53% of GNP. The decline in medium- and long-term debt is attributable to lower borrowings by the banks and the non-bank private sector as well as the Government. This development reflects the reduced recourse to external borrowing in the wake of higher interest rates abroad and the ample liquidity and more favourable terms offered in the domestic market. Despite higher principal repayments and interest payments, the debt service ratio is expected to stabilise at 5.6% given the sustained strong export growth.

In a global environment that is increasingly more competitive, the **management of the Malaysian economy** in the year 2000 will face new challenges. While the objective of maintaining macroeconomic stability and sustained growth with low inflation remains unchanged, the globalised financial markets, new technological developments and the advent of even larger and more influential multinationals, require that Malaysia adopt new strategies to sustain growth. Economic management in 2000 will focus on developing new areas of growth and improving competitiveness in traditional growth sectors. At the same time, focus is also directed at continued restructuring of banks, corporations and industries to increase resilience while improving

Table 3.9
External Debt of Malaysia

	1999*p*			2000*f*		
	RM billion	US$ billion	% share	RM billion	US$ billion	% share
Medium & long-term	**136.8**	**36.0**	**86**	**137.9**	**36.3**	**87**
Public sector	**77.0**	**20.3**	**48**	**79.6**	**21.0**	**50**
Federal Government	*18.4*	*4.8*	*12*	*16.1*	*4.2*	*10*
NFPEs	*58.6*	*15.4*	*37*	*63.6*	*16.7*	*40*
Private sector	**59.8**	**15.7**	**37**	**58.3**	**15.3**	**37**
Short-term	**22.8**	**6.0**	**14**	**20.8**	**5.5**	**13**
Non-bank private sector	*9.0*	*2.4*	*6*	*7.0*	*1.8*	*4*
Banking institutions	*13.8*	*3.6*	*9*	*13.8*	*3.6*	*9*
Total External Debt	**159.7**	**42.0**	**100**	**158.8**	**41.8**	**100**
% of GNP						
Total debt	57.0			53.0		
Medium & long-term debt	48.8			46.0		
Short-term debt	8.2			7.0		
Debt service ratio						
Total debt	5.3			5.6		
Medium & long-term debt	4.8			5.3		

p Preliminary
f Forecast

Source: Ministry of Finance and Bank Negara Malaysia

competitiveness. Similarly, macroeconomic policies will also be directed at managing emerging risks. Such risks, should they occur, will be associated with the sharp correction of major stock markets and a sudden fall in export demand. In the strategy to ensure sustainable growth, an investment-driven growth may be less relevant. In the past, investment-driven growth had benefited the economy by building capacity for future growth. The Government's policy is to target for quality investments to strengthen competitiveness and value added, and accelerate technology and skills development. In addition, small- and medium-size enterprises (SMEs) with specialised technology and strong linkages with the domestic economy will continue to be promoted.

In the recent past, a significant portion of domestic investment was channelled into the property sector. Given the excess capacity in this sector, more efforts are required to ensure that the resource surplus (savings exceeding investments) generated from the favourable balance of payments position are channelled to fund productive investments. This is particularly important to ensure that in a low interest rate environment, the strong growth in liquidity does not create excessive or speculative investments in the asset markets.

A major focus of policy is to ensure that there will be an increase in access to funding for productive investments. This is critical to ensure that excess liquidity in the system is utilised efficiently to raise the potential output of the economy in the medium term. In the drive to promote productive investments, policy initiatives are directed at promoting investments in the SME sector. In particular, BNM is reviewing policies which are aimed at increasing banks' participation in financing the growth of SMEs. In this respect, the Credit Guarantee Corporation would be reorganised to enhance its efficiency and effectiveness to ensure financing for SMEs. At the same time, the new emphasis on growth emanating from IT-related industries would mean that appropriate financing vehicles need to be developed to finance the higher risk ventures. While traditional bank financing would extend to cover some part of the investment in this area, more innovative and flexible non-bank financing is required. In this regard, the Government has taken several steps to enhance venture capital financing to accelerate the development of high-technology SMEs. Over and above the amounts being allocated by the Government and BNM, additional venture capital funding will need to be secured, should demand for venture capital funds become large during the course of 2000.

While promoting new growth areas, it is also necessary to review the strategies in the main sectors of agriculture, manufacturing and services, to address the risks and other areas of vulnerabilities that could emerge in view of rapid technological change. The new strategies should aim at alleviating structural impediments in the economy in order to remain competitive. While the strategic shift towards high technology-based industries in the manufacturing sector will continue to be promoted, the Government has also identified and encouraged new growth industries in the main sectors which are low in import content, high in value added and have high interlinkages with other industries and sectors of the economy. In particular, there is greater emphasis on revitalising the agriculture sector given that the phsyical infrastructure is already in place. The development of the agriculture sector is to focus more on the efficient utilisation of resources. Bold steps are being taken to encourage modernisation of the production process of existing industrial units, and the establishment of new industrial units using the latest technologies. In this regard, the Government has established various funds to provide financing for the acquisition of technology.

The Government also recognises the vulnerability of over-reliance on a narrow base of exports from the manufacturing sector, particularly the electronics industry. While electronics will remain important, the Government is promoting the development of resource-based industries with high growth potential within the wood-based, rubber-based and palm oil-based industries. At the same time, emphasis will be given to the promotion of new industries such as the composites and petroleum-based industries. Besides manufacturing and traditional commodities, the Government will continue to focus on the promotion of Malaysia as a regional centre for education services and tourism.

In all sectors, adjustments will be made to move from a production-based economy towards greater dependence on knowledge and information technology or knowledge-based economy. Accordingly, renewed emphasis is being directed at education and human resource management. In order to enhance labour productivity, the present education system would be reviewed to move to more creativity and solution-orientation than the present system. While high employment remains an important goal in economic policy, the Government would encourage high labour mobility. In this regard, restrictive and inflexible market practices in the labour market are being reviewed to produce a more adaptable labour force in the country.

In 2000, attention will also be given to the assessment of the most appropriate manner in which Malaysia can continue to integrate with the global economy but at the same time ensure stability in the domestic economy. In this regard, strengthening the financial sector remains a central policy objective. Measures in 2000 will build upon those effected since 1998. Corporate and bank restructuring will continue to be emphasised in 2000.

It is expected that Pengurusan Danaharta Nasional Berhad (Danaharta) would progress further in the restructuring of the banking and corporate sectors. Danaharta is currently in the midst of its secondary carve-out of non-performing loans (NPLs) from the financial system, having completed the primary carve-out involving a total of RM39.3 billion on 30 June 1999, six months ahead of the original schedule. The secondary carve-out, which comprises incidental and common loan accounts, is expected to be completed by 31 March 2000. In terms of loan workout targets, Danaharta expects to conclude workout proposals with the largest 20% of its borrowers, or transfer them for asset management workouts (i.e. sale of business or collateral) by 30 June 2000. These borrowers represent 85% of the total value of NPLs acquired by Danaharta during the primary carve-out period. In addition, Danaharta will hold further tenders for its foreign loan assets. The tenders will offer non-ringgit loans and marketable securities extended to or issued by foreign companies. Danaharta will also embark on the sale of businesses of companies that fall under Special Administration. With regard to foreclosed properties, the second sale by open tender will be launched at end-March 2000. Danaharta plans to hold these sales on a quarterly basis. Properties which are unsold will be transferred to its subsidiary, which will be entrusted to undertake value enhancement measures before selling them eventually in the open market.

Since its inception in August 1998, Danamodal Nasional Berhad (Danamodal) has injected funds totalling RM7.1 billion into 10 banking institutions. The improved confidence in the banking system and stronger economic performance has enabled five of the recapitalised banking institutions to repay Danamodal. In all of the exits to date, the “first-loss principle” has essentially been applied. In line with BNM’s policy on consolidation of the banking industry, Danamodal is in negotiations with various parties to divest its investments of RM5.3 billion in the remaining five recapitalised banking institutions. The divestments are expected to be achieved within the planned time frame.

Box V

Potential Output Revisited

Malaysia's recovery from the financial crisis in the region was stronger than expected. After five consecutive quarters of output contraction, Malaysia recorded the first positive growth in the second quarter of 1999. Since then, output expansion has strengthened, with economic activity in the final quarter of 1999 rebounding to end-1997 levels. The quick and strong recovery in the economy has prompted many analysts to question if the current growth in output is sustainable. Of more concern is whether actual growth is within the potential output growth. Potential output is defined as that level of output in the economy at which there are no inflationary pressures or external imbalances. The sustainability of growth involves both a demand and a supply dimension. This article focuses on the supply dimension of whether actual output growth is in line with potential output growth and whether the output gap that emerged during the economic contraction in 1998 has narrowed.

As in the previous study of potential output published in the 1997 Annual Report, the post-crisis potential output was estimated based on the single equation production function:

$$Y_t = f(KCU_t, L_t)$$

where KCU represents the utilised level of capital stock (capital stock, K, multiplied by the capacity utilisation rate) and L represents the labour force in employment. Based on quarterly data for the period 1991 to 1999, the short-term and long run elasticities for capital and labour were derived. KCU and L were then substituted with K and L* to derive potential output from the relationship, where L* represents the potential employment, that is, the labour force that is consistent with the "natural" or "long run" rate of unemployment[1].

[1] In this case, the "natural" or "long-run" unemployment rate is not an explicitly defined Non-Accelerating Inflation Rate of Unemployment (NAIRU), but is a rate that has been cyclically adjusted. The cyclical natural rate should be the same as NAIRU if the economy operates at the NAIRU over the course of the cycle.

The estimates from the previous study are not strictly comparable to the present study as the data used differs in terms of the period of time covered and the frequency of the data. The earlier study was based on annual data for 1970 to 1995 while the present study used quarterly data for 1991 to 1999. Nevertheless, there are some similarities in trends between the studies.

Firstly, in both studies the absolute value of the error-correction factor indicated that there was a stable long run relationship between output and the main factors of production, namely capital and labour. Secondly, the long run elasticity of labour was much higher than for capital. This implies that output has been relatively more responsive to labour than capital. Thirdly, the elasticity of capital was low in both studies. While low elasticity might imply an inefficient use of capital or that capital was being channelled into activities where returns were low, it could also be explained by the significant investment in infrastructure projects which have long gestation periods spanning over a decade. During the period 1993 to 1997, Malaysia made significant investments in improving the infrastructure in the country, as evidenced by the high ratio of investments to GDP averaging 46% over the period and therefore the return would be realised only after a time period.

The similarities in the findings of the two studies indicate that the production structure of the economy has remained largely unchanged in the sense that there have been no significant changes in the allocation of resources. Generally, companies gained higher output either through recruiting more labour or increasing the work shifts. The study shows that the efficiency of capital has declined. Hence, the improvement in efficiency in the utilisation of capital needs to be given greater priority.

Pre-crisis Period (1992-1997)

The period 1992-95 was characterised by high growth. Actual GDP expanded by 9.5% during this

Table V.1: Compound growth rate of actual output and potential output (1992-1999)

	Actual Output (GDP)	Potential Output
	(growth rate in %)	
1992-1995	9.5	7.2
1996-1997	8.8	9.0
1998-1999	–1.3	–1.5

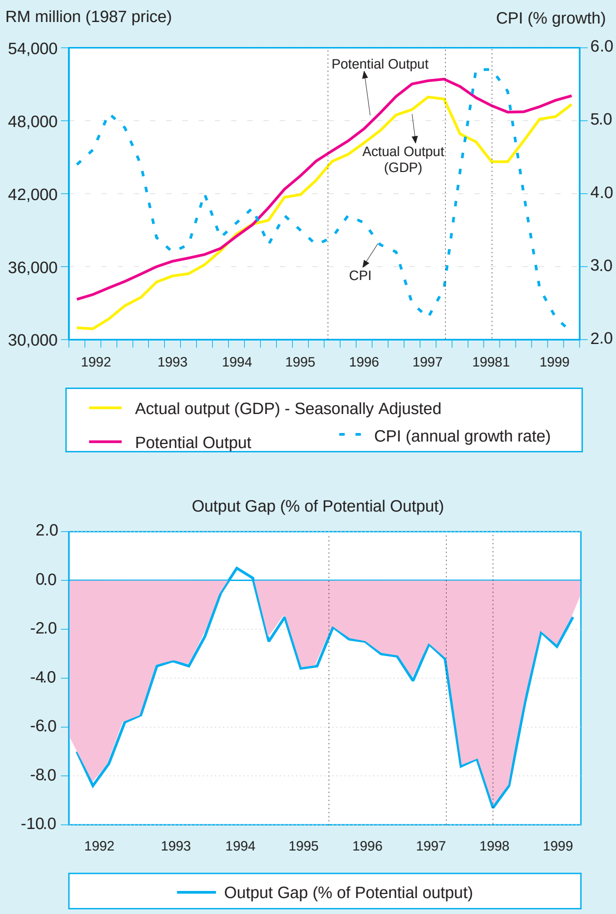
period, significantly higher than the growth rate of potential output of 7.2%. However, inflation rate as measured by Consumer Price Index (CPI) was well contained below 4% for the period 1993-95 due mainly to macroeconomic measures and the recourse to imported inputs as reflected in the widening of the current account deficit. The negative output gap narrowed gradually as actual output growth was above the trend growth of potential output. Beginning from the third quarter of 1994, there were signs of over-utilisation of production factors as actual output was above potential output. While the rate of inflation moderated, the current account deficit widened.

Following deliberate policies to contain aggregate demand in order to reduce the current account deficit in the balance of payments, actual output began to expand at a slower pace in 1996 and 1997, compared with trend growth of potential output. During this period, GDP increased by 8.8% while potential output expanded at a faster rate of 9%. The high investment rate coupled with the significant increase in potential new entrants to the labour force (population age of 20–24 years) contributed to the expansion of potential output during this period. Actual output expanded at a slower rate as bulk of the investments was in infrastructure projects. Consequently, the negative output gap began to widen. The inflation rate moderated from 3.7% in the second quarter of 1996 to 2.3% in the third quarter of 1997, before increasing subsequently due to the depreciation of ringgit.

Crisis and Post-crisis Period (1998-99)

The output gap began to widen significantly since the first quarter of 1998, when the GDP registered its first contraction of 3.1% on an annual basis. The impact of ringgit depreciation also began to have its adverse implications on the economy as manifested partly in the acceleration of inflation and the contraction of output. At the height of the recession in the third quarter of 1998, the output gap was the largest at 9.3% of potential output. However, the economic performance has improved since September 1998, after the introduction of selective exchange controls and the fixing of ringgit at RM3.80=US$1 to provide stability, enabling the authorities to implement growth-oriented policies and undertake structural reforms. The success of these measures was significantly aided by the recovery in export demand. Since the fourth quarter, actual output expanded at a faster pace compared with potential output, thus, narrowing the negative output gap. GDP recorded the first double-digit growth of 10.6% in the fourth quarter of 1999, closing the output gap to 1.5% of potential output. Potential output has trended upwards again since the first quarter of 1999 due mainly to higher investments by the public sector, some pick-up in private investment and increases in employment.

Graph V.1
Actual Output vs Potential Output



Conclusion

The findings indicate that the output gap is narrowing and potential output is back on its growth path. With the closing of the output gap in the near-to-medium term, high growth with low inflation can be sustained through measures to raise efficiency both in terms of technology and the use of capital and labour. The Government's current and long-term strategies in transforming the economy to a knowledge-based economy, as well as developing new growth areas based on information, communication and technology would raise potential output. The commitment to sound macroeconomic policies will provide the environment for the narrowing of the gap between actual output and potential output without creating economic imbalances in the economy.

The consolidation exercise of the banking institutions is expected to be completed by end-December 2000. It is recognised that continued change in the financial sector will take place given the expected changes that are likely to occur in both the external and domestic environment. Such changes will involve both the deregulation and liberalisation of the financial sector. At the same time, it is also recognised that financial sector deregulation and liberalisation that is too rapid can be destablising. Malaysia's approach to financial liberalisation is, therefore, one that is gradual and progressive to ensure that the country fully benefits from the liberalisation and that the reforms have the best chance of success without undermining stability. Presently, the focus is to prepare for greater liberalisation through the following steps:

- Strengthen the financial sector and deepen the capital markets in order to benefit from liberalisation and reduce risks.

- Ensure adequate prudential regulation for banks to manage risks and adapt to imposition of best practices in line with international standards.

- Strengthen institutions so that existing firms will be able to compete on a stronger foundation with new entrants into the markets.

BNM has adopted a proactive approach to prepare the industry to meet increased competition. A blueprint for the further development of the domestic banking sector would be presented in the Master Plan for the Malaysian Banking Sector, which is currently being developed by BNM and slated for implementation this year. Hence, the development and liberalisation of financial markets in this context would ensure that the financial sector remains effective in providing the financial requirements to realise the new strategies and to ensure sustainable growth with price stability.

While strategies to develop a more competitive banking sector are being undertaken, measures are also being implemented to ensure that in the process banking institutions are not detracted from their lending activities in 2000. In the merger exercise, procedures have been established to allow acquirer banks to influence lending practices of acquiree institutions. Lending by banking institutions would be monitored by the Steering Committee which will be set up by each banking group to co-ordinate the merger activities and monitor the level of loan activities within the group. In addition, banks will ensure that their operation staff and those involved in loan approvals and processing are separated from the merger team.

Overall, the indicators point toward a favourable economic and financial outlook for Malaysia in the year 2000. Macroeconomic management would continue to be flexible and pragmatic to respond promptly to changing conditions. BNM will continue to be vigilant of risks of inflationary pressures and new risks that could undermine the medium-term growth potential. In order to face the challenges in an increasingly competitive global environment, public sector structural adjustment policies will continue to aim at nurturing a more competitive environment so that private sector activities will resume their role in the growth process beyond 2000.

Monetary Policy in 2000

Monetary policy in 2000 will continue to meet the objective of strengthening the economic recovery while maintaining price stability. As a matter of policy, monetary policy would continue to aim at influencing inflationary expectations by a prudent management of excess liquidity arising from the continued strong balance of payments position. The exchange rate peg would be sustained as long as it is supported by consistent economic fundamentals.

The stance of monetary policy is determined by developments in the international environment and the domestic economy. On the international front, the monetary environment in 2000 is expected to be different from that in 1999. The benign inflation situation in 1999 would likely give way to greater concern about international inflationary pressures, especially in the United States. Interest rates have been raised both in US and Europe in the later part of 1999 and monetary policy in these countries is likely to maintain a tightening bias in 2000. However, Japan is likely to maintain its easy monetary policy. If the current round of oil price hikes are sustained, then the danger of higher inflation in the major industrial and regional economies would be greatly increased. The tightening of monetary policy and the resulting slower growth in the industrial countries would have an impact on the export-led growth of the regional countries.

On the domestic front, factors that are expected to influence monetary policy in 2000 include the inflation outlook, strong capital inflows under the pegged exchange rate regime and the availability of adequate financing to support the economic recovery. GDP growth is forecast to strengthen further in 2000, with continued reduction in excess capacity. The international outlook is vulnerable to the bias towards monetary tightening and a sharper than expected correction in the US stock prices. Both these developments would impact US aggregate demand and their import growth. On the domestic front, private investments have only recently shown signs of recovery, while excess capacity continues to exist in several sub-sectors. Against these uncertainties, fiscal policy would remain counter-cyclical to ensure that the recovery will strengthen further. Inflation, however, is expected to edge up only slightly, but can be maintained at relatively low levels. Under these circumstances, monetary policy in 2000 would remain accommodative to complement fiscal policy in strengthening the economic recovery given the absence of inflationary trends.

This accommodative monetary policy stance, however, would only be sustainable as long as there is no danger of inflation in the domestic economy. Inflationary pressures would carry additional risks to Malaysia, apart from the inefficiencies associated with higher inflation. It is recognised that inflation would contribute to a misalignment of the exchange rate and result in a loss of international competitiveness. Under a pegged regime, the exchange rate does not adjust in response to capital flows or changes in domestic aggregate demand but rather domestic prices would adjust upwards affecting the competitive position in regional and international markets.

In this regard, the monetary policy stance would be pre-emptive to contain inflation and maintain an environment of monetary stability. The assessment is therefore that the exchange rate peg would remain consistent with macroeconomic fundamentals over the medium term. This overall outcome would be achieved through close monitoring of all relevant indicators. In an economy recovering from a recession, some of the most important lead indicators would be inventories, excess capacity and productivity levels. These indicators and other price, wage and employment indicators as well as external factors would be monitored closely in the management of monetary policy to ensure subdued inflationary expectations.

Looking ahead, there are several challenges to monetary management in 2000. Efforts to ensure that inflation remains low need to monitor closely developments in asset prices. Higher incomes, easy liquidity conditions and low interest rates amidst slow demand for financing of private investment could still pose an inflationary threat if it leads to speculative activities in the asset markets. Excessive increases in asset prices could result in higher consumer prices if the positive wealth effects of higher equity and property prices led to excessive consumption spending. Asset prices, however, are not an objective of monetary policy. Asset price increases should reflect strengthening fundamentals. Credit-driven increases in asset prices should be avoided to prevent a repeat of earlier experiences. Of concern is that sharp increase in asset prices could also create an illusion of strengthening balance sheets which would reduce the urgency to restructure to become more competitive.

A further challenge to monetary management is managing the continued inflows, reflecting the performance in both the current and capital accounts in the balance of payments. BNM has intervened in the foreign exchange market to absorb the surplus foreign currency to maintain the currency peg. This has resulted in additional liquidity within the banking system, exerting downward pressures on interest rates. BNM has conducted sterilisation operations to absorb the liquidity from the money market. These sterilisation operations have been largely conducted through direct borrowings from the market.

Given that the balance of payments is expected to remain strong in 2000, the challenge to monetary policy in 2000 would focus on the effective management of excess liquidity. While a large amount of surplus funds have already been absorbed, under the current interest rate developments in Malaysia and abroad, further sterilisation of inflows would not create new risks. In addition, BNM has sufficient instruments to manage the liquidity. In the near term, BNM would continue to absorb the excess liquidity. BNM would also continue to recycle Government deposits placed with BNM to influence the liquidity situation in the banking system. The issuance of BNM bills has been particularly important in 2000 with the issuance of RM3.5 billion of these bills in February. The statutory reserve requirement also remains an option should the need arise. Managing the liquidity will remain important to ensure that the excess liquidity would not exert inflationary pressures and undermine the sustainability of the recovery process.

The accommodative monetary policy is aimed at providing an environment in which there is access to financing for productive and viable investments to support a higher level of economic activity. The balance sheet problems that may have constrained bank lending in the past have been addressed through the mechanism of Danamodal, Danaharta and the CDRC. As the banking institutions' balance sheets have improved and as NPLs have been on a declining trend, loan disbursement is expected to expand further in 2000. Drawing from past lessons, BNM would monitor closely lending activities to ensure prudent lending and avoidance of concentration and over-exposure to any particular sector.

On the exchange rate front, the focus of policy would be to ensure that the ringgit exchange rate remains consistent with the fundamentals of the Malaysian economy. The peg would not be adjusted in response to any marginal and short-term misalignments that could easily be reversed by subsequent changes in the major international currencies. The purpose for fixing the exchange rate is to provide an environment of stable domestic financial markets to facilitate economic recovery. It is, therefore, not the intention to adjust the rate frequently. Currently, there are no compelling reasons to warrant an adjustment of the peg. The medium term outlook suggests that domestic inflation would remain subdued and the threat of misalignment remains small. Nevertheless, BNM will monitor developments on both the external and internal front, that may have implications for the ringgit's exchange rate, and will respond accordingly in a highly transparent manner to ensure that the ringgit is at an appropriate rate.

As in the past, monetary policy would be implemented in a flexible and pragmatic manner. While the objective of low inflation would remain unchanged, the strategies to achieve this objective would need to be adjusted to changing circumstances and domestic and global developments. In terms of instruments, BNM would continue to work towards conducting monetary policy through more market-based instruments. The development of the bond market would enhance this process. At the same time, current measures to strengthen and improve risk management in the banking system would set a sound framework for more effective monetary policy.

4 The Financial Sector

Sources and Uses of Funds of the Financial System

The improved economic activity in 1999 was reflected in the total assets of the financial system which rose by 6.9% to RM1,171 billion at the end of 1999 (a decline of 1.7% in 1998). This was attributable to the increase in the assets of both the non-bank financial intermediaries (NBFIs) (11.6%) and the banking system (4.8%). The banking system recorded a significant turnaround in the growth of its assets, compared with a decline of RM45.3 billion or 5.6% in 1998. Nevertheless, given the increased pace of growth of the assets of the NBFIs, the banking system's share of the financial system assets declined marginally from 70% at the end of 1998 to 68.6% at the end of 1999. Within the banking system, the assets of the commercial banks (including Islamic banks) registered an increase of 5.2% compared with a decline of 5.4% in 1998, reflecting mainly the increase in deposit placements with other domestic financial institutions. The total assets of the finance companies declined further but at a moderate rate, reflecting the more favourable economic environment. The decline in assets of the finance companies reflected the constraint in their lending activities arising from the merger and other restructuring exercises undertaken in the industry, as well as the absorption of eight finance companies by the parent commercial banks.

Table 4.1
Assets of the Financial System

	Annual change 1998	Annual change 1999*p*	As at end-1999*p*	As at end-1999*p*
	RM billion			% share
Banking system	**145.3**	**37.2**	**803.9**	**68.6**
Bank Negara Malaysia	15.8	22.3	147.0	12.6
Commercial banks[1]	–26.3	24.0	483.2	41.3
Finance companies	–28.8	–7.7	115.9	9.9
Merchant banks	–5.1	0.0	39.2	3.3
Discount houses	–1.0	–1.4	18.6	1.6
Non-bank financial intermediaries	**26.5**	**38.1**	**367.1**	**31.4**
Provident, pension and insurance funds	24.0	30.0	243.6	20.8
Employees Provident Fund	*16.2*	*20.0*	*168.6*	*14.4*
Other provident & pension funds	*3.4*	*3.5*	*28.5*	*2.4*
Life insurance funds	*3.1*	*5.5*	*32.3*	*2.8*
General insurance funds	*1.4*	*1.0*	*14.2*	*1.2*
Development finance institutions[2]	4.4	2.6	22.4	1.9
Savings institutions[3]	–0.3	1.8	20.9	1.8
Other financial intermediaries[4]	–1.7	3.7	80.3	6.9
Total	**-18.8**	**75.2**	**1,171.0**	**100.0**

1 Includes Bank Islam Malaysia Berhad and Bank Muamalat Malaysia Berhad (since 1999).
2 Includes Malaysian Industrial Development Finance Berhad,Bank Pertanian Malaysia, Borneo Development Corporation, Sabah Development Bank Berhad, Sabah Credit Corporation, Export - Import Bank Malaysia Berhad, Bank Pembangunan dan Infrastruktur Malaysia Berhad and Bank Industri Malaysia Berhad (Renamed "Bank Industri dan Teknologi Malaysia Berhad" as of 28 February 2000).
3 Includes National Savings Bank, Bank Kerjasama Rakyat and co-operative societies.
4 Includes unit trusts (ASN, ASB, ASW 2020 and ASM Mara), building societies, Pilgrims Fund Board, Credit Guarantee Corporation, Cagamas Berhad, leasing companies, factoring companies and venture capital companies.
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For the NBFIs, total assets rose faster by 11.6% in 1999, compared with a growth of 8.8% in 1998. Consequently, their share of total financial system assets increased further from 30% at the end of 1998 to 31.4% at the end of 1999. The higher growth was principally supported by strong expansion in the assets of the provident, pension and insurance funds (14%), which accounted for 78.7% of the increase in the total assets of the NBFIs. Total assets of the development finance institutions also continued to grow, albeit at a slower rate of 13.2% (28.8% in 1998). The growth was due mainly to the increase in loans extended by Bank Pembangunan dan Infrastruktur Malaysia Berhad, following the large increase in its paid-up capital to RM1 billion to enable the bank to undertake financing of infrastructure projects.

Concomitant with the improved economic activity, large trade surplus, and general rise in income and business profits during the year, deposits mobilised by the financial institutions recorded a stronger increase of 10.9% in 1999 (2.2% in 1998). As a result, deposits continued to be the main source of funds for the financial system, accounting for 47.9% of total sources of funds at the end of 1999 (46.1% in 1998). The

Table 4.2
Sources and Uses of Funds of the Financial System

	Annual change		As at end-1999*p*	
	1998	1999*p*		
	RM billion			% share
Sources:				
Capital and reserves	–3.0	6.3	109.6	9.4
Currency	–4.0	9.9	30.5	2.6
Deposits[1]	10.7	55.3	560.6	47.9
Borrowings	–24.0	–0.2	8.5	0.7
Funds from other financial institutions[1]	–83.5	1.6	72.7	6.2
Insurance and provident funds	19.3	25.3	213.0	18.2
Other liabilities	65.9	–23.1	176.1	15.0
Total	**-18.8**	**75.2**	**1,171.0**	**100.0**
Uses:				
Currency	–0.8	4.6	7.9	0.7
Deposits with other financial institutions	–67.2	28.8	180.6	15.4
Bills	–11.1	6.1	16.4	1.4
Treasury	*–0.1*	*–0.1*	*3.7*	*0.3*
Commercial	*–10.9*	*6.2*	*12.8*	*1.1*
Loans and advances	–1.3	–12.5	471.9	40.3
Securities	17.5	14.9	239.5	20.5
Malaysian Government	*5.5*	*3.6*	*75.1*	*6.4*
Foreign	*0.0*	*0.3*	*1.5*	*0.1*
Corporate	*12.8*	*11.7*	*156.8*	*13.4*
Others	*–0.7*	*–0.7*	*6.1*	*0.5*
Gold and foreign exchange reserves	39.2	17.5	113.8	9.7
Other assets	4.8	15.8	140.9	12.0

[1] Effective 1998, the statutory reserves of banking institutions have been reclassified as "Funds from other financial institutions" rather than "Deposits". In this regard, data from prior years have also been revised accordingly.
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banking institutions (comprising commercial banks, finance companies, merchant banks and discount houses) accounted for 83.1% of total deposits mobilised by the financial system (86% in 1998). Among the banking institutions, the significant growth of deposits placed with the commercial banks more than offset the decline in deposits mobilised by the finance companies and merchant banks.

The non-financial private sector (comprising individuals and business enterprises) accounted for the bulk (62.6%) of the outstanding deposits with the financial institutions. The faster growth in deposits of this group with the financial system (5.4%, compared with 3.7% in 1998) reflected improved incomes as economic expansion and stock market activities gathered momentum in 1999. Fixed deposits continued to account for the bulk of deposits placed by the non-financial private sector, accounting for 95.1% of the increase in total deposits of the sector (118.4% in 1998). By maturity, fixed deposits continued to be concentrated in shorter-end maturities. At the same time, both demand and savings deposits also registered significant increases of 28% and 20.8% respectively.

Contractual savings with provident funds and contributions to insurance funds remained as major sources of funds for the financial system, expanding by 13.5% (11.4% in 1998), to account for 18.2% of the outstanding total funds of the financial system. With the exception of borrowings and other liabilities, other sources of funds also registered increases. Capital and reserves of the financial system increased by 6.1% (–2.9% in 1998), consonant with healthier business profits and gains from investments in the stock market recorded during the year. Funds obtained from other financial institutions registered a small increase in 1999, compared with a large reduction in 1998 which was due to the reduction in the statutory reserve requirement from 13.5% to 4%.

Table 4.3
Non-Financial Private Sector Deposits[1] with the Financial System[2]

	Annual change		As at end-1999*p*	
	1998	1999*p*		
	RM billion			% share
Deposits[3] with:				
Commercial banks	5.0	21.5	250.1	71.2
Finance companies	4.0	–7.3	59.0	16.8
Merchant banks	–0.5	–0.4	10.9	3.1
Discount houses	0.0	0.2	3.9	1.1
National Savings Bank	0.6	0.9	8.0	2.3
Others	2.7	3.1	19.1	5.4
Total	**11.9**	**18.0**	**351.1**	**100.0**
Demand deposits	–5.2	9.0	41.2	11.7
Fixed deposits	14.0	17.1	239.1	68.1
Savings deposits	2.3	9.0	52.5	14.9
NIDs[4]	0.1	–15.5	2.9	0.8
Repos[5]	0.6	–1.6	15.5	4.4
Fixed deposits				
Of which:				
Up to 1 year	19.6	18.9	220.8	62.9
More than 1 year	–5.5	–1.7	18.2	5.2

[1] Refers to deposits of business enterprises (excluding NFPEs) and individuals.
[2] Excludes provident, pension and insurance funds, and other financial intermediaries.
[3] Refers to demand, savings and fixed deposits, negotiable instruments of deposit and repos.
[4] Refers to negotiable instruments of deposit.
[5] Refers to repurchase agreements.
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Table 4.4
Direction of Credit[1] to Non-Financial Private Sector

	Annual change 1998	Annual change 1999*p*	As at end-1999*p*	As at end-1999*p*
	RM billion			% share
Loans and advances	–12.3	–8.0	438.9	73.7
Agriculture	*0.1*	*1.2*	*10.2*	*1.7*
Mining & quarrying	*0.4*	*–0.3*	*1.4*	*0.2*
Manufacturing	*–0.7*	*–1.5*	*56.0*	*9.4*
Housing	*6.2*	*5.7*	*71.1*	*11.9*
Construction[2]	*1.0*	*–7.3*	*85.5*	*14.4*
Business services	*0.3*	*10.9*	*20.8*	*3.5*
General commerce	*–15.5*	*0.2*	*17.7*	*3.0*
Transport & storage	*1.8*	*0.2*	*14.2*	*2.4*
Purchase of shares	*–7.2*	*–5.3*	*23.2*	*3.9*
Consumption credit	*–5.5*	*–0.5*	*50.7*	*8.5*
Others	*6.8*	*–11.3*	*88.1*	*14.8*
Investment in corporate securities	12.8	11.7	156.8	26.3
Total	**0.5**	**3.7**	**595.7**	**100.0**

[1] Excludes credit to non-financial public enterprises.
[2] Includes loans for real estate.
p Preliminary

Total loans and advances extended by the financial system contracted by RM12.5 billion (–RM1.3 billion in 1998). However, including loans sold to Danaharta and Cagamas during the year, total loans and advances outstanding would register an increase of RM5.2 billion in 1999. Loans and advances (excluding loans sold to Cagamas and Danaharta) extended to the non-financial private sector registered a smaller decline of RM8 billion, compared with a decline of RM12.3 billion in 1998. Large declines were recorded for loans and advances extended for the purchase of shares (–18.7%) and to the construction sector (–7.9%). Meanwhile, loans and advances extended to the agriculture sector increased by 13.5% (0.7% in 1998).

On the other hand, investment in corporate securities by the financial system continued to register a significant increase of 8.1% (9.7% in 1998). In particular, there were marked increases in investment in corporate securities by the Employees Provident Fund (RM8.9 billion), life and general insurance funds (RM5.2 billion) and unit trust funds (RM5.1 billion). The continued strong growth was in line with the improved stock market performance during the year. Deposits placed with other financial institutions increased by 18.9%, reflecting mainly the increase in placements of deposits by the banking system with BNM. Meanwhile, gross holdings of gold and foreign exchange reserves of BNM increased significantly by RM17.5 billion to RM113.8 billion, reflecting mainly Malaysia's sustained large current account surplus in the balance of payments in 1999.

Management of the Banking System

The year 1999 was clearly a year of recovery and consolidation for the banking system. This was evidenced by the marked improvement in the performance of the banking sector which registered preliminary unaudited pre-tax profit of RM5.3 billion for the calendar year 1999 compared with a pre-tax loss of RM5.7 billion in the previous year. At the same time, further industry consolidation through the merger process took place, resolving some of the problems associated with smaller and weaker banking institutions which became apparent during the financial crisis. The thrust of banking policies during the year aimed at further enhancing the financial intermediation activities of the banking institutions to provide the required financing to support economic recovery. A number of measures were also implemented to address structural imbalances in the banking system and to lay the foundation for a more resilient, efficient and competitive banking system that would also contribute towards macroeconomic stability.

A strong, efficient and stable banking system is a prime pre-requisite for a sustainable economic recovery, since only a viable and resilient banking system can allocate and mobilise domestic resources efficiently and effectively within the economy. Any disruption to the functioning of the intermediation process would adversely negate the economic recovery process. Against this backdrop, a comprehensive restructuring plan was implemented during the second half of 1998, as described in the 1998 Annual Report, to address weaknesses emanating from high incidence of non-performing loans (NPLs), capital deficiencies in the banking system as well as the distressed corporate sector. Taking advantage of the period of stability in the domestic environment following the imposition of the selective exchange controls in September 1998, the restructuring efforts were accelerated to address weaknesses within the banking sector. At the same time, reductions in interest rates to support recovery also eased the burden of high corporate debts which facilitated the restructuring process in both the corporate and banking sectors.

The banking system as a whole remained relatively resilient throughout the last two years given the strong conditions prior to the crisis. Nonetheless, given the magnitude of its impact, some banking institutions suffered substantial losses arising primarily from high levels of NPLs which rapidly eroded their capital. In order to prevent further deterioration in the financial health of these banking institutions, BNM assumed control over the operations of four banking institutions, namely Kewangan Bersatu Berhad, MBf Finance Berhad, Sabah Finance Berhad and Sime Merchant Bankers Berhad. The move also aimed to pre-emptively contain any possibility of a systemic failure in the system. With the exception of MBf Finance Berhad, the control over the operations and management of the three ailing banking institutions still remain under BNM. The three banking institutions have also been restricted from engaging in new lending activities so as to preserve their balance sheets and various schemes have been worked out to address problems relating to these institutions. As part of the rescue operations, Kewangan Bersatu Berhad and Sabah Finance Berhad will be absorbed by Mayban Finance Berhad and Multi-Purpose Bank Berhad respectively. The purchase of assets and assumption of liabilities of these weak institutions by stronger entities will ensure that the operations and services of the former will not be disrupted. Meanwhile, resolution of Sime Merchant Bankers Berhad was achieved via an open tender exercise conducted towards end-1998. The weak capital position of MBf Finance Berhad was resolved through capital injection amounting to RM2.3 billion in the form of tier-1 capital by Danamodal Nasional Berhad (Danamodal). Danamodal has also appointed its nominees to oversee its investment as well as to enhance the effectiveness of the Board and management of MBf Finance Berhad.

In addition, two of the larger domestic commercial banks, namely Bank Bumiputra Malaysia Berhad and Sime Bank Berhad, also incurred large losses as a result of substantial provisions arising from high NPLs. Given the size and the potential impact of these institutions on the overall system stability and depositors' confidence, these two institutions were merged with stronger commercial banks. Bank Bumiputra Malaysia Berhad was absorbed by Bank of Commerce (M) Berhad and Sime Bank Berhad was taken over by RHB Bank Berhad. To ensure that the mergers would not weaken the strength of the acquiring banks, the distressed assets of the weaker institutions were removed to subsidiaries of Pengurusan Danaharta Nasional Berhad (Danaharta) that were specifically set up to manage the distressed assets of these banks prior to the merger and for a subsequent period which ranging from 12 to 18 months from the date of their mergers. The two mergers involving Sime Bank Berhad and Bank Bumiputra Malaysia Berhad were successfully completed on 30 June 1999 and 30 September 1999 respectively.

Following the accelerated implementation of the restructuring plan, together with lower interest rates and improved liquidity conditions, the strains on the banking sector began to subside. The removal of NPLs by Danaharta and recapitalisation by Danamodal placed the banking sector in a better position to undertake the intermediation function more effectively. Furthermore, the success of Danaharta and Danamodal in achieving their targets six months ahead of schedule has enabled the banking sector to play its rightful role in supporting economic activities.

The ample liquidity in the banking system and low interest rates means that borrowers have greater and easier access to financing and are less burdened by high debt servicing cost. Nevertheless, as in any economy recovering from a recession, demand for large-scale and capital investment-related financing has been slow as several industries were experiencing excess capacity. Until the economy is operating close to its full capacity, most of the financing needs during this period are focused on working capital requirements, leaving a large proportion of approved and committed facilities largely unutilised. The rate of loan repayments has also been high as businesses optimise their resources by utilising surplus cash to ease their dependence on bank borrowings and reduce their leverage. The high rate of loan repayments in turn reflects the higher turnover in economic activities which have increased the capacity of borrowers to repay their loans. Such repayment in itself while benefiting businesses in reducing their leverage, was also instrumental in enhancing the stability of the banking sector as it improved the quality of assets of banking institutions, thus resulting in healthier balance sheets.

On the prudential front, BNM recognised that injection of capital funded by short-term borrowings would result in a high incidence of double leveraging in the banking system which could increase the vulnerability of the banking system. The mismatch between long-term capital investments and short-term funding may exert undue pressure on the banking institutions to generate the necessary returns in the short run to enable the shareholders to service their debts at the expense of long term risks. To contain such imprudent practices, BNM now requires that any new capital injection by shareholders of banking institutions must be funded through non-debt sources or very long-term debt instruments. Banking institutions are also no longer allowed to lend to their shareholders with controlling and/or influential interest to minimise occurrence of connected lending within the banking institution.

This new measure effectively complements the existing rules of prohibiting banking institutions from lending to their directors and officers. This prohibition is aimed at curtailing any potential misuse and irregular practices by the shareholders, being owners of the institutions themselves in steering credit decisions related to themselves or parties related to them.

The crisis has also highlighted the weaknesses in the management of some banking institutions. Given the nature of banking operations in assuming and managing risks, the strength and effectiveness of its management would undoubtedly affect the strength of the banking institution itself. Indeed, the first line of defence against unsound banking institutions is competent banking management. Thus, to ensure that the banking institutions continue to be managed by competent management, equipped with a high degree of integrity and professionalism, the suitability of the chief executive officers and directors of banking institutions will now be reviewed once every two years.

During the recent financial crisis, it was evident that a fragmented banking sector is highly vulnerable to shocks and can pose systemic risks to the banking sector. Growing competition and strong pressures emerging from the external front to further liberalise the banking sector has also clearly shown that the domestic banking sector can no longer remain protected. The financial liberalisation envisaged under the ASEAN Framework Agreement on Services and the General Agreement on Trade in Service, to gradually remove barriers to entry and access among the ASEAN countries and among the WTO (World Trade Organisation) Members, has highlighted the crucial need for the domestic banking sector to gear itself and be able to meet the challenges and competition arising from increasing globalisation and technological advancements. Furthermore, in the global market, rapid consolidation of banking institutions is now taking place to take advantage of economies of scale and tap potential synergies.

The banking crisis in the mid-1980s had clearly highlighted the vulnerabilities of the weaker banking institutions which were not adequately capitalised to withstand shocks. Against this backdrop, BNM has always recognised the importance of and the need for consolidation in the banking sector in order to attain the critical mass to meet the demands of the changing domestic economic structure, future challenges from globalisation and liberalisation as well as to contribute towards sustainable economic growth. During the economic boom in the late 1980s and early 1990s, calls for rationalisation and consolidation were often ignored. The buoyant economic growth during that period has led to significant improvements in the performance of the banking system. While some were simply satisfied with the returns earned on their investments and did not realise the urgency for further strengthening and consolidation, others had resorted to short-term funding for their capital expansion. Voluntary mergers were not forthcoming. Since the mid-80s crisis, only two market-oriented mergers were successfully implemented, between Kwong Yik Bank Berhad and DCB Bank Berhad and between Chung Khiaw Bank (Malaysia) Berhad and United Overseas Bank (Malaysia) Berhad.

The sooner the domestic banking sector in Malaysia undergoes a consolidation and rationalisation exercise, the more well-placed will the domestic banking sector be to meet future challenges. In this regard, the merger programme for the finance company industry initiated in 1998 was extended to the domestic banking sector as a whole in 1999. Specifically, all domestic banking institutions were given the flexibility to form their own merger groups and choose their own leader in each group to lead the merger process and revert to BNM by end-January 2000. In response to this approach, approval was granted for the formation of 10 banking groups to be led by Malayan Banking Berhad, RHB Bank Berhad, Public Bank Berhad, Bumiputra-Commerce Bank Berhad, Multi-Purpose Bank Berhad, Hong Leong Bank Berhad, Perwira Affin Bank Berhad, Arab-Malaysian Bank Berhad, Southern Bank Berhad and EON Bank Berhad, each with minimum shareholders' funds of RM2 billion and asset base of at least RM25 billion. With the formation of these 10 banking groups, the number of domestic banking institutions would be reduced substantially from the current 54 to 29 banking institutions. The consolidation exercise would enable the banking groups to reap maximum synergy and enhance their profitability and efficiency. To ensure that the industry consolidation exercise is not delayed, BNM has set the target date of end-December 2000 for the completion of the entire consolidation exercise.

Prudential regulation of banking institutions is necessary as these institutions serve as the intermediaries for the productive mobilisation and distribution of capital within the economy and the prime channels of monetary policy. In order to maintain the safety and soundness of the financial system as well as the position of the banking system to thrive within a dynamic and competitive environment, prudential regulations will continue to be emphasised. In this regard, additional prudential regulations will be introduced in the near future. These include measures to inculcate sound and effective credit risk management, refining the existing risk-based capital adequacy framework, developing a system of prompt corrective measures as well as limiting the Government's financial safety net so that it will not contribute to excessive risk-taking and not undermine market discipline.

The recent experience showed that there is a tendency for bankers as well as corporate players to forget the lessons learned from the crisis in the mid-1980s. Despite the costly experience in the previous recession stemming from imprudent and excessive exposures to the property sector, similar over-concentration was also observed during the recent crisis. In the pursuit of high returns in the property market, substantial amount of resources was channeled to finance various real estate activities. Such decisions were often induced by the wrong assumption that collateral value alone is sufficient to demonstrate creditworthiness and repayment capacity of the borrowers. This imprudent lending practice, on the part of the banking institutions, and the over-optimistic expectations of the property developer, had contributed to a large overhang in certain segments of the property market, in particular, the high-end residential properties and shophouses as well as commercial properties. Therefore, to contain further accumulation in the supply of high-end residential and commercial properties and to clear the abundant stock of unsold properties created by the recession, financing restriction was imposed on the provision of bridging finance for the development of residential properties and shophouses valued in excess of RM250,000 per unit as well as commercial properties. This prohibition is aimed at preventing further downward adjustments in the different segments of the property market. At the same time, two home ownership campaigns were organised during the year at the national level to reduce the overhang of properties in the market. The two campaigns were extremely successful with a total of RM6.4 billion worth of properties sold during the campaign periods. The lending restriction to the high-end property market is also expected to free up resources to other sectors of the economy, including for the development of affordable residential properties where demand has remained high even during the crisis. Moving forward, it is imperative for the banking institutions to remember that property booms are often fueled by the easy and excessive credit and oversupply can result. Given the long cycles in property prices, the challenge is to ensure that the next generation of credit officers and managers do not repeat the same mistake in the future. In this regard, BNM has issued a consultative paper to the banking industry on "Minimum Standards on Credit Risk Management" in November 1999, which outlines the minimum principles which banking institutions should observe in their credit operations. These minimum standards aim to develop and enhance credit risk management standards in the banking sector.

The crisis has also highlighted the losses suffered by the banking institutions due to weak internal and risk management controls. The mismatch between the risk profile of a banking institution's portfolio vis-à-vis the minimum capital requirement led to an overstatement of the banking institution's capability in absorbing potential shocks. Generally, these banking institutions would also be the ones experiencing higher levels of NPLs and capital deficiencies. Such observation also highlighted the deficiencies of the present capital adequacy framework which classifies the assets of banking institutions into five broad risk weight categories, without taking into consideration the risk profile of the loan exposures and the inherent strength or weakness of the banking institutions in managing credit risk. Preliminary studies are currently being conducted to refine the capital adequacy framework to reflect capital charges which commensurate with the risk profile and strength of risk management of banking institutions.

The setting up of Danamodal to address the recapitalisation of weak banking institutions during the crisis has also shown that timely supervisory intervention is critical to minimise capital erosion and subsequent potential financial costs to the Government. On a larger scale, it would also ward off the contagion effect of a bank-specific crisis from becoming endemic, which would have adversely affected the stability of the banking system as a whole. In this regard, a system of prompt corrective measures is being developed and would be introduced to act as a first line of action against banking institutions which are found to be operating in a manner that would potentially threaten their future solvency. The measures would comprise a set of actions that would automatically be instituted if certain transparent prudential indicators as specified by BNM were triggered. This would ensure that capital can be conserved and that further build-up of risks in an ailing or potentially ailing institution can be avoided. While this is not a pre-emptive measure to prevent an institution from failing, it would certainly act as a damage control instrument to minimise capital erosion by allowing BNM to undertake the necessary course of action to contain and rectify the problems.

The concept of disassociating non-supervised entities from banking groups would be introduced primarily to ensure that the obligation of the Government in assuring the safety of deposits would not be extended to other non-supervised institutions of a financial group. In the past, instances have emerged in which the failure of a non-bank entity had affected the confidence of the public in the banking entity within the same financial group. To minimise the occurrence of such events in the future, a bank holding company would have to be set up separately to hold only banking institutions and subsidiaries which are supervised by BNM and the Securities Commission. The harmonisation of holding companies that merely hold investments in supervised entities across all banking groups would also facilitate the implementation of prudential regulations on bank holding companies in the future.

As a developing nation, Malaysia requires a strong and efficient banking system that is resilient and capable of supporting the financing needs of the economy in its next phase of development so that the nation can continue to achieve a strong and sustainable growth in the future. The development of a resilient, efficient and competitive banking sector however, cannot be achieved within a short period of time. It requires considerable effort and commitment as well as a comprehensive set of policies which need to be nurtured and implemented over time. The merger and consolidation exercise is only one of the necessary pre-conditions to create strong, efficient and competitive domestic banking institutions and cannot on its own be expected to fully realise these objectives. This needs to be supplemented and complemented with other measures which would need to be introduced over the medium and longer-term.

In this regard, BNM has embarked on a comprehensive masterplan for the Malaysian financial system that focuses on building the foundation and charting the strategic direction of the banking sector for the next 10 years. The masterplan will provide a clear and common long-term vision for the development of a resilient, efficient and competitive banking sector which is able to operate effectively in an environment of emerging new technological advances and more sophisticated consumer demands. The objective of the masterplan is not only to ensure that the banking sector continues to be able to meet the needs of the changing domestic environment but also to play a catalytic role in the transformation of the economy. Within this broad objective, the main thrust will be to develop a core of strong and forward looking domestic banking institutions which will form an integral part of the Malaysian banking system. The masterplan will identify key issues for the Malaysian banking sector as well as formulate strategies and action plans that need to be pursued over the medium to long term to increase the resilience, competitiveness and dynamism of the banking institutions in the context of the impending challenges of a globalised and liberalised environment. In doing so, a more holistic assessment of the banking sector will be undertaken to ensure that reforms are co-ordinated and objective-oriented. The masterplan will also identify the optimal regulatory and supervisory framework to be adopted by BNM to achieve these objectives.

The years ahead will undoubtedly witness significant changes within the banking sector. A major pre-requisite to be able to adjust and adapt to this changing environment is the development of a sound and strong financial system and institutions. In this regard, BNM has and will continue to consciously develop a modern and sophisticated financial system which will effectively mobilise and allocate resources for productive use in tandem with the rapid transformation of the economy. For the banking institutions, in rising to this challenge, greater focus on improving efficiency and competitiveness needs to be accorded. The impetus to the improvements would rely on innovation, flexibility, skill enhancements, customer-orientation, product development and the need to pay close attention to the return on equity and consolidation of the banking sector. In this context, the importance of achieving critical size would assume greater significance in order for banking institutions to be able to reap the gains from economies of scale and reduce costs and excess capacity, as well as enable higher spending on information technology to remain efficient and competitive. Larger institutions that are well-capitalised and well-managed would be able to position themselves to meet the challenges of an increasingly liberalised operating environment and market driven approach that are unfolding across the globe. A core of strong, efficient, resilient and competitive banking institutions would not only be able to withstand future shocks, thereby minimising the adverse implications on macroeconomic stability, but would also enhance the payments system infrastructure and market surveillance mechanism to monitor capital flows and other sources of risk in the banking system and the economy as a whole. The merger programme is an important step towards accomplishing this objective.

Banking Measures in 1999

Abolishment of the Two-Tier Regulatory System (TTRS): The Two-Tier Regulatory System (TTRS) for banking institutions was abolished on 10 April 1999. As a result, incentives that were previously accorded to Tier-I banking institutions were made available to all institutions, subject to the approval of BNM. The blanket approval previously granted to all Tier-I domestic banks to open new branch offices was withdrawn.

The TTRS, with its emphasis on absolute capital size as one of the pre-requisites for the attainment of Tier-I status, led banking institutions to embark on over-zealous capital expansion program funded by shareholders' borrowings. As a result, significant pressures were exerted on the management of these banking institutions to aggressively increase their loan portfolio in order to generate the requisite returns to meet debt servicing obligations of their shareholders. This, in turn, contributed to poor credit decisions in a number of banking institutions which subsequently affected their asset quality, particularly during the economic downturn.

Approval for Increases in Capital Funds: Arising from lessons learnt under the TTRS, BNM, with effect from 14 April 1999, requires future capitalisation of banking institutions by controlling shareholders to come from non-obligatory sources of financing such as equity, internally generated funds and very long-term debt (preferably by way of bond issue) of at least 10 years maturity. Banking institutions which seek BNM's approval to issue new capital (ordinary shares, preference shares, hybrid capital and subordinated term loans) will have to provide BNM a statement from their controlling shareholders participating in the capital injection on the degree of leverage they will incur in raising the funds to be injected into the banking institution.

Prohibition on Lending to Controlling and/or Influential Shareholders: With effect from 4 August 1999, BNM's guideline on 'Prohibition of loans to its directors, staff and their interested corporations' (BNM/GP6) was expanded to also prohibit the granting of credit facilities to shareholders with controlling and/or influential interest in the banking institution and to any related companies of the shareholder, any firm in which the shareholder has interest as a partner, manager, agent or guarantor and any person for whom the shareholder is a guarantor. Existing credit facilities granted to controlling/influential shareholders and their related parties would be allowed until their maturity or the next review date. An individual or legal entity shall be deemed to be a controlling shareholder of a banking institution if it fulfils either one of the following criteria:- a) controls more than 50% of the voting rights; b) holds more than 50% of the issued share capital; c) controls the composition of the board of directors; d) has the power to appoint or remove all or a majority of the directors; or e) controls the controlling shareholder of the banking institution. Influential interest is defined as:- a) if the person, together with other parties which he controls or acts in concert with, holds 20% or more interest in the voting rights of the banking institution; or b) if the person has the power to appoint at least one person to the board of directors.

Amendments to the New Liquidity Framework: On 30 September 1999, BNM extended the transitional period for banking institutions to cross over to the new liquidity framework by another year to 31 December 2000.

The extension of the transitional period is to accommodate the integration efforts of the merger programme among banking institutions.

Cagamas Berhad Bonds - Liquid Asset Status: With effect from 1 April 1999, holdings of bonds issued by Cagamas Berhad to finance the purchase of commercial and industrial property loans can be classified as liquid assets for purposes of meeting banking institutions' liquid asset ratio requirement under the old liquidity framework.

In 1997, Cagamas Berhad expanded its housing loan securitisation scheme to encompass commercial and industrial property loans. Unlike bonds issued to finance housing loans, bonds issued to finance the purchase of commercial and industrial property loans initially did not qualify as liquid assets. This had led to a disparity in pricing among bonds issued by Cagamas Berhad. As at 31 December 1999, total outstanding bonds issued by Cagamas Berhad for this purpose amounted to RM699 million. To streamline incentives given to Cagamas for its loan securitisation activity and to remove the disparity in the pricing among Cagamas bonds, all bonds issued by Cagamas Berhad have been designated as liquid assets under the old liquidity framework.

Investment in "BB" Rated Private Debt Securities: With effect from 19 July 1999, banking institutions are allowed to invest and trade in corporate bonds rated "BB" and above. Previously, banking institutions were only allowed to hold bonds rated at least "BBB".

The economic downturn has caused the rating of a number of corporate bonds held by banking institutions to be downgraded to below BBB rating. Relaxation of the above requirement would allow banking institutions to continue holding these bonds which have been downgraded to BB, rather than to subject them to mandatory disposal when market sentiment on these bonds is already poor.

Disposal of Shares Acquired in Debt-Equity Conversion Scheme: With effect from 2 March 1999, pursuant to section 66(3) of the Banking and Financial Institutions Act 1989 (BAFIA), banking institutions may hold shares acquired from debt-equity conversion schemes for a period of up to five years from the date the shares are acquired. Previous guideline on debt-equity schemes required banking institutions to dispose the shares not later than six months after the published audited results of the investee company show an operational profit.

The restructuring exercise in the banking sector has resulted in banking institutions holding substantial amount of shares from debt-equity conversion schemes. The extension of the holding period to five years is to avoid unnecessary capital losses for the banking institutions which may be incurred if banking institutions are forced to pre-maturely sell the shares before allowing them to appreciate to their full potential value.

Accounting Treatment for Bonds Acquired Under Debt to Bond Conversion: On 19 July 1999, BNM had prescribed the accounting treatment to be adopted by banking institutions for debt restructuring schemes where book debts have been converted into bonds issued by the borrower. Bonds received are recognised at its fair value (i.e. present value) on inception. Where the fair value of the bonds is lower than the net book value of the original debt (the outstanding amount of the debt, net of specific provision and interest-in-suspense), the losses should be charged to the profit and loss account in the current accounting period. When the fair value is higher than the net book value, the gain should not be recognised as income, but transferred to the "Provision for diminution in value" account and netted off from "Investment/Dealing securities" account in the balance sheet. The unrealised gain can only be recognised as income upon disposal or redemption of the bonds by the issuer. Where unconditional forgiveness of debt is involved in the restructuring scheme, the amount forgiven should be written off from the loan outstanding.

In line with the existing treatment on private debt securities(PDS), bonds treated as investment securities will be stated at cost less provision for any permanent diminution in value. Only bonds that are either guaranteed by the Government or by other banking institutions or bonds that have been otherwise permitted by BNM, may be stated at cost adjusted for amortisation of premium or accretion of discount. Bonds treated as dealing securities will be stated at the lower of cost and market value.

In view of the numerous debt restructuring schemes participated by banking institutions as a result of the economic downturn, the accounting treatment has been recommended in order to bring consistency in treatment and encourage the prudent recognition of income.

Extension of Permissible Activity for Finance Companies and Discount Houses to Facilitate Corporate Debt Restructuring Schemes: With effect from 1 March 1999, finance companies are permitted to hold unsecured debt securities issued by the borrower pursuant to a debt restructuring exercise with respect to the portion of debt for which the finance companies have been lenders. This permissible investment has been gazetted under the Banking and Financial Institutions (Credit Facility Without Security) (Licensed Finance Company) Order 1999 pursuant to Section 60(2) of the BAFIA.

With effect from 22 October 1999, discount houses are allowed to invest in equity-linked debt securities, whether redeemable or irredeemable, with remaining maturity of more than 10 years that are issued pursuant to a debt restructuring scheme. The exercise is subject to the condition that if any such investments are convertible into shares, the discount houses must dispose them before conversion date; or redeem for cash on maturity; or line up buyers prior to conversion date so as to dispose of the shares obtained from the conversion on conversion date. This additional permissible investment has been gazetted under the Banking and Financial Institutions (Investment Business of Discount Houses) Order 1999.

Companies undertaking corporate debt restructuring schemes normally offer a combination of debt and equity instruments. Nevertheless, the schemes cannot be implemented without the consent of the majority of creditors, especially if finance companies and discount houses are also involved as lenders. This relaxation will provide the finance companies and discount houses greater operational flexibility to participate in debt restructuring schemes to enhance recoverability of distressed debts.

Progress of Banking Sector Restructuring

As at 31 December 1999, Danaharta acquired and is managing NPLs with loan rights amounting to RM45.5 billion from the financial system, of which RM35.7 billion was the loan rights acquired from the banking system. The book value of the loans removed from the banking system amounted to RM34 billion, representing approximately 42% of NPLs in the banking system. The removal of these NPLs from the banking sector has reduced the residual NPL level to 6.6% (based on 6-month classification) as at end-December 1999, from the peak of 9% (based on 6-month classification) as at end-November 1998. The overall weighted average discount rate for the acquired NPLs was about 56%. A total of RM10.3 billion nominal value zero-coupon bonds have been issued up to end-December 1999 as consideration for the loan acquisitions. This is considerably lower than the total financing requirement of RM15 billion budgeted earlier. Danaharta has also embarked on the secondary carve out of NPLs in October 1999. With the bulk of the NPLs successfully removed during the primary phase, the amount of NPLs to be acquired under the secondary phase is expected to be minimal. The secondary carve-out will focus on common borrowers whose other accounts are already in Danaharta's portfolio, loans of borrowers with a total gross value exceeding RM50 million, unsecured loans granted to public listed companies or loans from banking institutions with net NPL ratio in excess of 10%.

Danaharta has now entered into the loan and asset management stage. As at 31 December 1999, a total of RM17.6 billion of the loans and assets under its management has been restructured or disposed, with an average recovery rate of 80.2%. Danaharta has also conducted two successful restricted open tenders to dispose of foreign currency loans and papers in August 1999 and December 1999 involving 43 accounts worth US$394.25 million. Under the initial tender exercise, Danaharta achieved a recovery rate of 55.3% on 13 of the accounts, whilst a 71% recovery was achieved on 25 accounts in the second tender exercise. With these two tender exercises, Danaharta has successfully disposed of foreign currency assets with principal value of US$339.8 million.

On the asset management front, Danaharta has conducted its first open tender exercise involving foreclosed properties in December 1999. Out of the 44 properties opened for the tender with indicative value of RM122.6 million, 24 bids were successful raising total consideration of RM17.8 million. The amount received on the successful bids represented an 8% surplus over the indicative value of RM16.5

million. The remaining 20 properties with an indicative value of RM106.1 million were transferred to an asset subsidiary of Danaharta at the minimum bid price. This would allow Danaharta the opportunity to manage and enhance the value of the properties for future disposal.

In the case of recapitalisation exercise by Danamodal, total capital injection into the initial 10 banking institutions has declined to RM5.3 billion as at end-December 1999 following repayments by five banking institutions. The recapitalisation by Danamodal has helped to strengthen the RWCR position of these institutions from 9.9% as at end-September 1998 to 12.3% as at end-December 1999.

On the corporate debt restructuring exercise, Corporate Debt Restructuring Committee (CDRC), as at 29 February 2000, has successfully completed the restructuring of 19 cases with debts amounting to RM14.1 billion, whilst 10 cases have been referred to Danaharta. Reflecting the improved conditions of the corporate sector, there has not been many new applications submitted to CDRC since late 1999. CDRC expects to complete the debt restructuring of 26 cases involving debts amounting to RM16.4 billion currently outstanding by the third quarter of 2000. Apart from corporate restructuring, CDRC is also actively looking into the restructuring of the transportation, telecommunication and steel industries involving nine companies (of which four companies are currently under CDRC) to ensure that the restructured companies operating within the industry would become feasible and viable. The scope of the industry restructuring would differ depending on the nature and extent of structural inefficiencies within the industry.

Performance of the Banking System

Profitability

Two and a half years after the onset of the financial crisis which plagued the Asian region, the Malaysian banking system has turned around to record a pre-tax profit of RM5.3 billion for calendar year 1999, from a pre-tax loss of RM5.7 billion in 1998 (which was largely contributed by exceptionally large losses of three banking institutions). With the improvement in profitability, the banking system was again able to provide a positive return on assets of 0.8% and a return on equity of 11.5% for the year. Although still considerably lower than the levels enjoyed during the pre-crisis period, the encouraging improvement clearly indicates that the banking system is on the path towards recovery and has been able to do so within a respectably short period of time.

On a quarterly basis, the banking system continued to experience its fourth consecutive quarter of losses up to 31 March 1999. The losses recorded by the banking system in the first quarter of 1999, which was lower than the average quarterly loss recorded in the preceding three quarters, were due to exceptionally large losses recorded by one banking group as well as by two other commercial banks and one finance company. After experiencing a pre-tax loss totalling RM8.5 billion during the 12-month period ended 31 March 1999, the performance of the banking system began to take a turn for the better and it began generating profits beginning from the second quarter of 1999 in line with the turnaround in overall economic growth. The banking system rebounded strongly from the crisis to achieve an aggregate pre-tax profit of

Table 4.5
Banking System: Income and Expenditure

	For the calendar year			
	1998	1999*p*	Annual change	
	RM million			%
Interest income net of interest-in-suspense	60,749	38,653	–22,096	–36.4
(Interest-in-suspense)	*4,983*	*3,406*	*–1,577*	*–31.6*
Less: Interest expense	45,893	24,233	–21,660	–47.2
Net interest income	14,856	14,420	–436	–2.9
Add: Non-interest income	6,017	6,767	750	12.5
Less: Staff Cost	3,905	3,508	–397	–10.2
Overheads	5,304	4,870	–434	–8.2
Profit before provisions	11,664	12,809	1,145	9.8
Less: Loan loss provisions	17,396	7,543	–9,853	–56.6
Pre-tax profit	–5,732	5,266	10,998	
(excluding 3 institutions)[1]	-1,258	3,992	5,250	
Of which:				
Commercial banks	–2,687	6,428	9,115	
Finance companies	–2,388	–996	1,392	
Merchant banks	–657	–166	491	
Return on assets (%)	–0.9	0.8		
(excluding 3 institutions)[1]	*–0.2*	*0.7*		
Return on equity (%)	–12.3	11.5		
(excluding 3 institutions)[1]	*–2.8*	*9.0*		

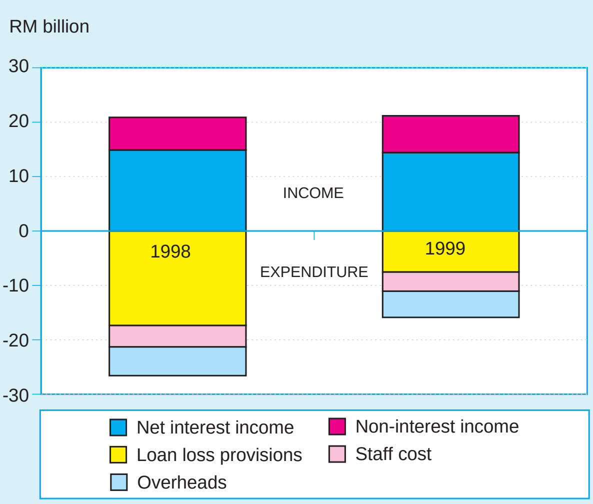
[1] Excluding three banking institutions that made exceptional loss in 1998.
p Preliminary

RM7.4 billion during the last three quarters of 1999. Generally, most banking institutions turned profitable again in the last three quarters of 1999, whilst those that were still incurring losses (15 banking institutions) were registering lower losses as compared with the preceding three quarters.

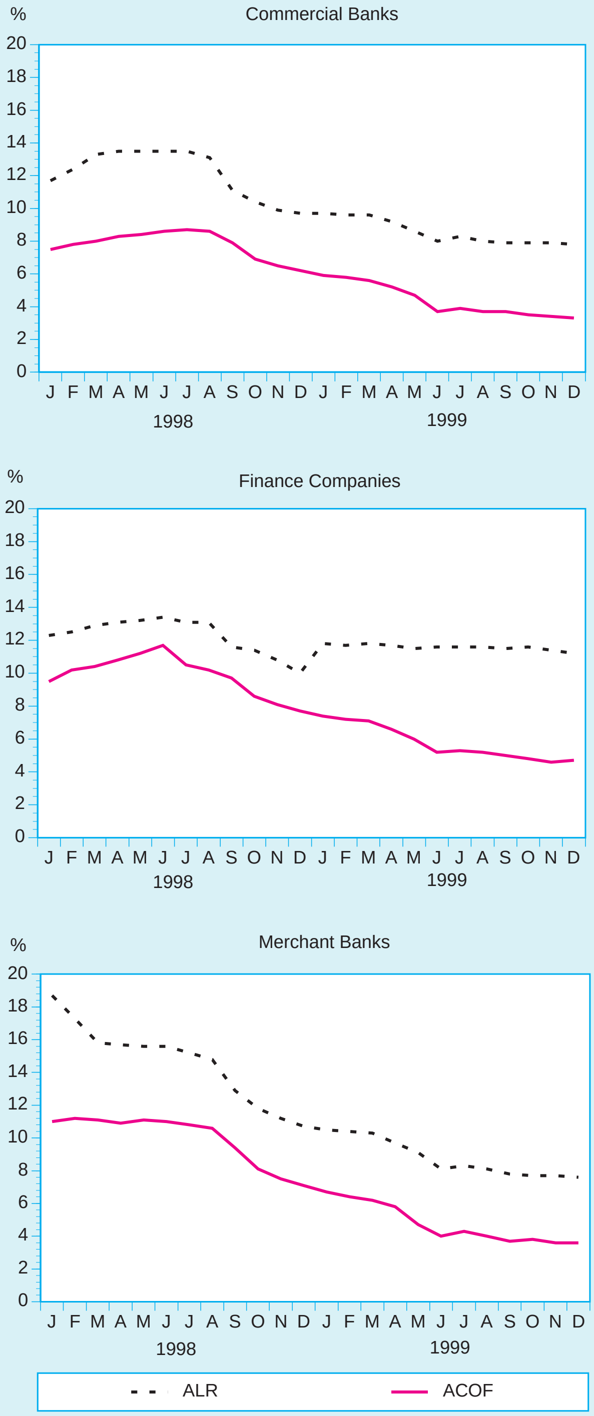
The higher profitability recorded in 1999 was largely due to significantly lower bad debt provisioning that had to be set aside against NPLs. During the year, the banking system charged RM7.5 billion for loan loss provisions, 56.6% less than the amount provided in the previous year (1998: RM17.4 billion). The lower loan loss provisioning for 1999 was as a result of lower additional specific provisions required for the year, as well as significant write-back of provisions already made previously. The improved profitability position of the banking system was attained even after charging RM399 million to their profit and loss account for losses incurred as a result of sale of loans to Danaharta, leaving a total of RM1.4 billion still to be amortised.

However, at the operating level, the banking system still recorded a decline in net interest income of RM436 million (–2.9%) although it was much lower than the decline of 11.1% recorded in 1998 as interest-in-suspense charged in 1999 dropped by 31.6%. Nevertheless, net interest income continued to decline in 1999, due to the negative growth in total outstanding loans (excluding loans sold to Danaharta) while the average net interest margin of the banking system for the year remained virtually unchanged at 3.7 percentage points.

Graph 4.1
Banking System: Profitability



Graph 4.2
Average Lending Rates and Average Cost of Funds



Note: ALR includes interest which have been suspended and penalty interest on NPLs. ACOF excludes the cost of overheads, statutory reserve and liquid asset requirements.

In reviewing the interest rate trends throughout 1998 and 1999, the banking system experienced a decline in net interest margin between June 1998 and March 1999 before it gradually widened from the second quarter of 1999 onwards. There was a rapid decline in deposit rates due to excess liquidity in the market coupled with lower lending rates which were brought down by a series of downward base lending rate adjustments, as a result of progressive reductions of the statutory reserve requirement and lowering of the intervention rate. The gross unadjusted interest rate margin (difference between average gross lending rates and average cost of funds) of the commercial banks declined to a low of 3.2 percentage points in September 1998 due to the locked-in deposit funds, before gradually improving to 4.5 percentage points in the final quarter of 1999 when interest rates level stabilised. The finance company industry, which suffered severe interest margin contraction throughout 1998 when deposit rates rose on the back of fixed rate loans, gained the most from the low interest rate environment when it saw tremendous improvement in net interest margin, from 2.1 percentage points in 1998 to 4.3 percentage points in 1999.

Table 4.6
Banking system: Loan Activity

	For the year		Annual growth
	1998	1999	
	RM million		%
Loan approvals	65,124	104,804	60.9
Loan disbursements	251,127	323,169	28.7
Loan repayments	270,546	335,587	24.0
	As at end-		Annual growth
	1998	1999	
	RM million		%
Adjusted total financing[1]	435,638	447,712	2.8

[1] Adjusted for loans sold to Danaharta, bad debts written off during the year, private debt securities held and loans converted into equity and other assets.

The non-interest income of the banking system increased by RM750 million or 12.5% in 1999. This was mainly due to gains from the sale of investment securities, as well as higher dividend income received from investment securities, in tandem with the general improvement in the stock market and better performance of the corporate sector. The improved pre-tax profit position of the banking system was also aided by lower staff cost incurred during the year (–10.2%) as a result of a 4.4% reduction in the number of employees in the banking sector, as well as a decline in overheads (–8.2%).

Loan Activity

Amidst an improving economic environment and greater economic activities, the banking system continued to play its intermediation function by providing financing to support the increased demand. New loans approved in the banking system increased by nearly two-fold in 1999 to RM104.8 billion, as compared to RM65.1 billion in 1998. Disbursements of approved credit facilities also improved by 28.7%, from RM251.1 billion in 1998 to RM323.2 billion in 1999. However, loan repayments increased by 24%, from RM270.5 billion in 1998 to RM335.6 billion in 1999. The encouraging rate of turnover of loans clearly reflected the improvement in the business environment brought about by a low interest rate environment, ample liquidity situation and rising investor's confidence, which translated into a strong GDP growth of 5.4% for the overall Malaysian economy in 1999.

For the year 1999, the banking system directed the largest proportion of new financing to the manufacturing sector and for the purchase of residential properties. Over 33% of new loans approved in the banking system were channelled to these two sectors. More importantly, loans approved for the purchase of residential properties costing RM250,000 and below accounted for about 74% of new loans approved for the purchase of residential properties. The finance, insurance and business services sector also benefited from the increase in loan approvals, accounting for over 10.1% of total new loans approved in 1999.

In terms of loan disbursements, the manufacturing sector alone accounted for 26.3% of total loans disbursed in 1999. The bulk of loans was also disbursed to the wholesale, retail, restaurants and hotels, and finance, insurance and business services sectors, totalling over 29.9% of loan disbursements in 1999. Although loans disbursed to the broad property sector accounted for 17.6% of total loan disbursements in 1999, 74.8% of these loans were channelled to the construction sector and financing for the purchase of residential properties.

Despite the strong improvement recorded in loan approvals and loan disbursements in 1999, this was not translated into a significant increase in the amount of total outstanding loans due to several developments, namely, the large amount of loans sold to Danaharta, bad debts written off during the year, and loans converted into private debt securities, equity and other assets. If these items were added back, including the banking institutions' holdings of private debt securities (PDS), the adjusted total financing provided by the banking system would have increased by 2.8% from 1998 to 1999. The strong increase in loan disbursements in 1999 was also offset by higher loan repayments which grew by 24% from 1998 to 1999.

During the financial crisis, a great deal of attention was focused on the growth in bank lending because of its importance in the economic recovery process. However, it needs to be recognised that the outstanding loan figures do not reflect the growth in new loans due to the various adjustments mentioned earlier, and that it would not be entirely appropriate to link directly the outstanding loans with the supply of funds into the economy.

Loan growth is a function of both the demand and supply of credit. The provision of credit by banking institutions should be measured against their willingness to provide new financing or allow further drawdown of existing approved credit facilities. Therefore, a more accurate barometer of banking institution's supply of credit to the economy should be the amount of new loans approved and disbursements of approved credit facilities. From the analysis of the credit performance in terms of loan approvals and loan disbursements, there was clearly no evidence of constraints on the supply of credit into the economy.

In terms of demand for credit, most businesses were hesitant to expand their operations especially during the early months of 1999 given the uncertainties in the outlook of the economy. With the existing excess capacity in the economy, most businesses scaled down their operations to meet the underlying demands. Therefore, many credit facilities were left unutilised, as indicated by the large amount of undrawn credit facilities in the banking system, totalling RM113.1 billion as at end-1999. It was also noted that most businesses chose to use their surplus cash reserves to repay their loans to reduce their leverage positions, as observed in the higher loan repayments recorded by banking institutions in 1999. With such high levels of repayments, the outstanding loans of several institutions registered a flat, marginal or even negative growth although financial resources were actually channelled to meet the increase in demand for financing.

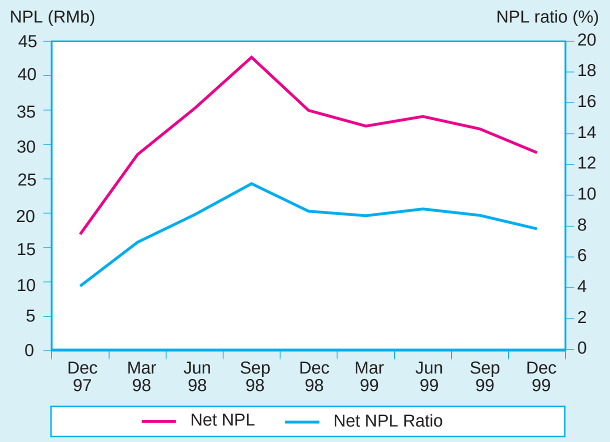
In summary, an increase in the turnover of loans is a better reflection and indication of economic activity, rather than outstanding loans. A higher rate of turnover in loans, measured by loan disbursements and loan repayments, can be expected to result in the generation of increased economic activities and overall GDP growth.

Asset Quality

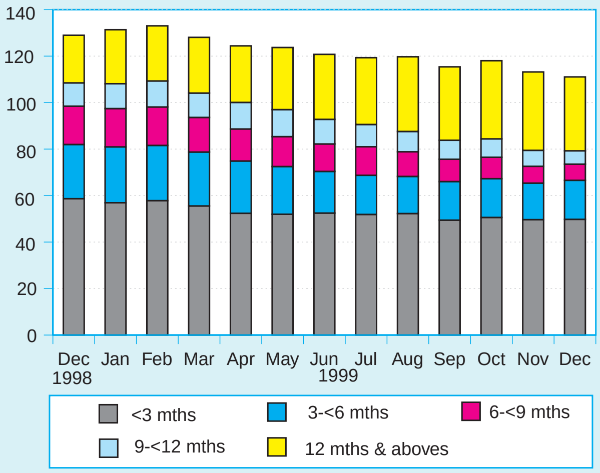
The asset quality of the banking system improved in 1999, after being adversely affected by the financial crisis the previous year. NPLs net of provisions of the banking system declined from 9% to 7.8% of total loans or from RM34.9 billion to RM29.7 billion. Net NPLs of the banking system for the year 1999 peaked in January and since July, have been trending downwards. Even if loans sold to Danaharta are added back, NPLs in the banking system have trended downwards since August 1999. The sale of NPLs to Danaharta had kept NPLs in the banking system at manageable levels and relieved the banking institutions from the burden of managing high levels of NPLs. Three significant sales to Danaharta were made in December 1998 (RM12.1 billion), March 1999 (RM7.8 billion) and December 1999 (RM4.4 billion). As at 31 December 1999, a total of RM34 billion NPLs had been sold to Danaharta, of which RM21 billion was sold in 1999.

Of the remaining loans outstanding with the banking institutions, the amount of loans which were in arrears had declined in 1999. Customers who were previously deferring the servicing of their loans as a result of high interest rates and lower economic activity, were able to service them again. Overall, total loans that were in arrears experienced a decreasing trend throughout the year in line with the stronger economic growth. Total loans that were in arrears for more than one month declined by RM17.9 billion or 13.9% in 1999. However, total loans which had been in arrears for a period of more than twelve months increased in 1999, in part due to the migration of doubtful or sub-standard

Graph 4.3
Banking System: Net Non-performing Loans



Graph 4.4
Banking System: Ageing Profile of Loans in Arrears (excludes loans sold to Danaharta)



loans as well as the longer time period needed to recover bad loans. Some of the loans in the more than 12 months category also consisted of loans which were undergoing restructuring under the CDRC. Around 8% or RM31.3 billion of total loans in the banking system have been restructured or rescheduled.

Both commercial banks and merchant banks experienced similar trends in the ageing profile of their loans as a result of loan concentration to similar sectors of the economy, namely the manufacturing, construction and financing, insurance and business services sectors. These sectors were adversely affected during the financial crisis and took a longer time to recover, the result of which was evident in the increase in NPLs in the construction and financing, insurance and business services sectors. Total loans in arrears of the finance companies reflected a different pattern as a more significant portion of their loans were directed mainly to the real estate sector and for the purchase of transport vehicles and securities. As the economy picked up towards the end of 1999, customers were able to service their loans for the purchase of transport vehicles while the bullish trend in the Kuala Lumpur Stock Exchange boosted the servicing of share financing loans. NPLs in the real estate sector also declined as a result of loans being sold to Danaharta. Hence, a much better turnaround was observed for finance companies.

Despite the decrease in NPLs, the loan loss provisions (interest-in-suspense, specific provisions and general provisions) of the banking system did not decline, but increased slightly from RM33.1 billion as at end-1998 to RM33.2 billion as at end-1999 due to increases in interest-in-suspense outstanding which was offset by similar declines in general provisions, and the excess general provisions being transferred to specific provisions. Interest-in-suspense outstanding increased by RM619.4 million in line with continued suspense of interest on the NPLs of the banking system. The increase in interest-in-suspense, however, was not as much as that in 1998 (RM12.2 billion), hence, banking institutions were still able to record an increase of RM5.3 billion in their pre-tax profit. The drop in general provisions by RM553.7 million was in line with the reduction in the loan base of the banking system which shrank by 5%. Specific provisions outstanding of the banking system remained relatively stable.

In terms of the performance of different banking institutions, both commercial and merchant banks were found to experience a slight decline in their specific provisions outstanding as a result of increases in their collateral value, which increased by RM3.2 billion and RM488.8 million respectively to RM33.2 billion and RM3.2 billion in 1999. However, the situation was reversed for the finance companies. Although NPLs had declined slightly, straight line amortisation policy on vehicle loans resulted in declining collateral values and hence, increased level of provisions. Collateral value of

Graph 4.5
Ageing Profile of Loans in Arrears: By Type of Institution

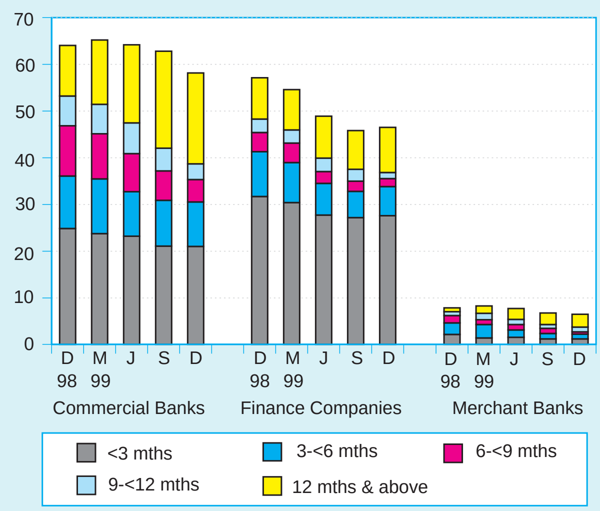


Table 4.7
Banking System: Non-performing Loans and Loan Loss Provisions

	As at end-			
	1998	1999		
	Actual[1]	Actual[1]	Classification 3-month	Classification 6-month
	RM million			
Commercial banks				
General provisions	6,540.4	6,376.3	6,419.5	5,033.8
Interest-in-suspense	4,081.9	4,845.4	4,934.7	4,397.2
Specific provisions	12,688.5	11,317.0	11,492.9	10,179.4
Non-performing loans	37,253.5	35,561.5	41,184.8	30,402.3
Net NPL ratio (%)[2]	*7.3*	*7.0*	*9.0*	*5.7*
Total provisions / NPL (%)	*62.6*	*63.4*	*55.5*	*64.5*
Finance companies				
General provisions	1,823.5	1,442.1	1,211.1	1,258.8
Interest-in-suspense	2,193.1	2,031.3	2,091.7	2,010.1
Specific provisions	3,606.5	5,187.5	4,893.7	5,194.3
Non-performing loans	17,901.3	14,415.2	19,073.4	13,570.6
Net NPL ratio (%)[2]	*14.0*	*9.8*	*16.4*	*8.6*
Total provisions / NPL (%)	*42.6*	*60.1*	*43.0*	*62.4*
Merchant banks				
General provisions	423.6	415.4	406.7	407.6
Interest-in-suspense	463.6	481.2	520.6	441.0
Specific provisions	1,320.9	1,083.6	997.6	879.9
Non-performing loans	4,122.1	3,764.5	5,582.7	3,487.5
Net NPL ratio (%)[2]	*11.5*	*12.7*	*23.4*	*12.3*
Total provisions / NPL (%)	*53.6*	*52.6*	*34.5*	*49.6*
Banking system				
General provisions	8,787.5	8,233.8	8,037.3	6,700.3
Interest-in-suspense	6,738.6	7,358.0	7,547.1	6,848.3
Specific provisions	17,615.9	17,588.1	17,384.2	16,253.5
Non-performing loans	59,276.9	53,741.2	65,840.9	47,460.3
Net NPL ratio (%)[2]	*9.0*	*7.8*	*11.1*	*6.6*
Total provisions / NPL (%)	*55.9*	*61.7*	*50.1*	*62.8*

[1] Loans classified as NPL based on individual banking institution's NPL classification policy i.e. 3-month or 6-month classification.
[2] Net NPL ratio = (NPL less IIS less SP) / (Gross loans less IIS less SP) x 100%

NPLs of finance companies dropped by RM5.7 billion to RM14 billion in 1999.

The combined effect of decreasing NPLs and slight increase in loan loss provisions resulted in an increase in the loan loss coverage ratio of the banking system from 55.9% to 61.7% in 1999. Including the value of collateral, the total loan loss coverage of the banking system amounted to 155.2% of NPLs as at 31 December 1999.

Non-Performing Loans by Sector

In general, the level of NPLs associated with most economic sectors declined in 1999 due mainly to the sale of NPLs to Danaharta. Loans to the manufacturing and construction sectors and for share financing formed the most significant portion of loans acquired by Danaharta.

The level of NPLs for the purchase of securities in the banking system recorded a healthy decline of 35.8% in 1999, due mainly to sales to Danaharta. The gross NPL ratio for the purchase of securities fell from 23.2% as at end-1998 to 19.2% as at end-1999. Even if NPLs sold to Danaharta are added back, NPLs for the purchase of securities declined by 2.6% in absolute terms. Loans to this sector also shrank significantly not only due to recoveries but also due to lower utilisation of such facilities.

Given the high exposure of the banking system to the broad property sector, NPLs to this sector continued to account for the largest portion of total NPLs in the banking system. The construction sector accounted for 40.6% of total NPLs to the broad property sector. Of this, 39.6% was attributable to loans for the construction of commercial complexes and infrastructure projects. Nevertheless, sales to Danaharta contained the level of NPLs at manageable levels.

In line with the Government's call to promote house ownership, the banking system continued to channel a significant portion of total loans for the purchase of residential properties. During 1999, loans for the purchase of residential properties (excluding loans sold to Danaharta) increased significantly by RM6.4 billion or 11.4%. Nevertheless, the NPL ratio of such loans remained relatively low at 7.9% of total loans to this sector. In addition, NPLs to this sector accounted for only 9.2% of total NPLs in the banking system, although loans to this sector (excluding loans sold to Danaharta) constituted 16% of the total loan portfolio in the banking system.

NPLs to the manufacturing sector accounted for 16.1% of total NPLs in the banking system as at 31 December 1999. Nevertheless, about 60% of NPLs to the manufacturing sector had outstanding balances of RM5 million and below and were channelled to the small- and medium-sized industries, and thus were not eligible for sale to Danaharta. To assist these smaller borrowers, the Government has established the

Table 4.8
Banking System: Non-performing Loans by Sectors

	As at end-					
	NPLs by sector (Excluding loans sold to Danaharta)		As percent of total loans to sector			
			Excluding loans sold to Danaharta		Including loans sold to Danaharta	
	1998	1999	1998	1999	1998	1999
	RM million		(%)		(%)	
Agriculture, hunting, forestry & fishing	818	704	10.6	8.1	11.7	12.2
Mining & quarrying	259	232	15.5	16.4	16.1	20.6
Manufacturing	9,018	8,678	14.3	14.3	16.6	19.5
Electricity, gas & water supply	52	104	0.9	1.5	1.1	2.1
Wholesale & retail, restaurants & hotels	3,912	4,428	11.1	12.8	12.6	16.1
Wholesale trade	*2,051*	*2,057*	*11.0*	*11.3*	*12.4*	*14.6*
Retail trade	*1,119*	*1,333*	*10.9*	*12.6*	*12.3*	*15.1*
Restaurants and hotels	*742*	*1,038*	*12.1*	*17.6*	*13.6*	*22.6*
Broad property sector	20,830	19,814	14.3	13.9	16.1	19.0
Construction	*8,053*	*8,051*	*18.7*	*21.5*	*21.8*	*29.9*
Purchase of residential property	*4,102*	*4,932*	*7.3*	*7.9*	*7.3*	*8.0*
Purchase of non-residential property	*3,880*	*3,755*	*12.9*	*13.8*	*15.6*	*18.2*
Real estate	*4,796*	*3,076*	*28.9*	*20.6*	*30.7*	*32.6*
Transport, storage & communication	2,701	2,091	18.0	15.1	19.2	17.0
Finance, insurance & business services	4,591	4,274	12.4	14.0	13.9	19.1
Consumption credit	7,585	7,019	14.1	13.6	14.1	14.2
Personal uses	*2,076*	*2,052*	*15.4*	*15.3*	*15.6*	*17.3*
Credit cards	*750*	*352*	*17.4*	*6.4*	*17.4*	*6.4*
Purchase of consumer durable goods	*150*	*191*	*18.1*	*21.0*	*19.4*	*22.8*
*Purchase of transport vehicles**	*4,609*	*4,424*	*13.0*	*13.8*	*13.0*	*14.0*
Purchase of securities	7,524	4,827	23.2	19.2	34.2	37.4
Community, social & personal services	882	769	13.2	11.1	13.4	12.7
Others	1,105	801	12.6	8.1	13.2	19.1
Total	**59,277**	**53,741**	**14.3**	**13.7**	**16.8**	**19.1**

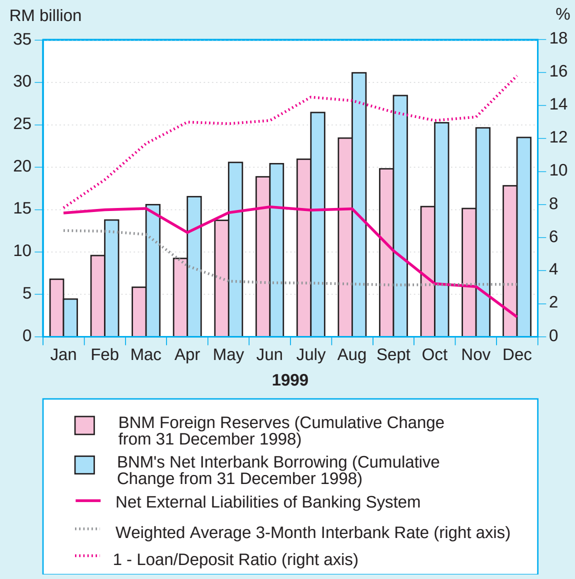
* Includes commercial vehicles

Rehabilitation Fund for Small and Medium Industries and Bumiputera Entrepreneur Project Fund to restructure their loans and ensure that these borrowers continued to have access to financing and remain viable in the longer run.

Liquidity Management

The strong export performance during 1999 resulted in a large trade surplus of RM72.3 billion and a substantial increase in the net external reserves of BNM of RM17.8 billion. With the consequent increase in liquidity from the inflow of reserves, total deposits of the banking system expanded by 4% or RM17.2 billion. As a result, the weighted average 3-month interbank rate eased from 6.43% per annum in January 1999 to 3.15% per annum as at end-1999. The excess liquidity situation necessitated BNM to mop up the excess liquidity through borrowing in the interbank market. Between December 1998 and December 1999, BNM's net interbank borrowings increased from RM18.3 billion to RM41.8 billion (+RM23.5 billion). Moreover, BNM had reduced its intervention rate three times during the year, in March (7%6.5% per annum), May (6.56% per annum) and August (6%5.5% per annum). The move had resulted in the maximum BLR for commercial banks to ease from 8.04% per annum

Graph 4.6
Liquidity of the Banking System

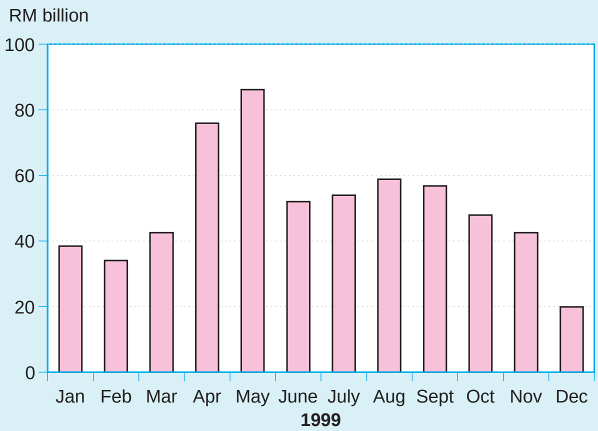


in January 1999 to 6.79% per annum since August 1999, and for the finance companies from 9.5% per annum to 7.95% per annum. This assisted in supporting economic activities and expediting recovery.

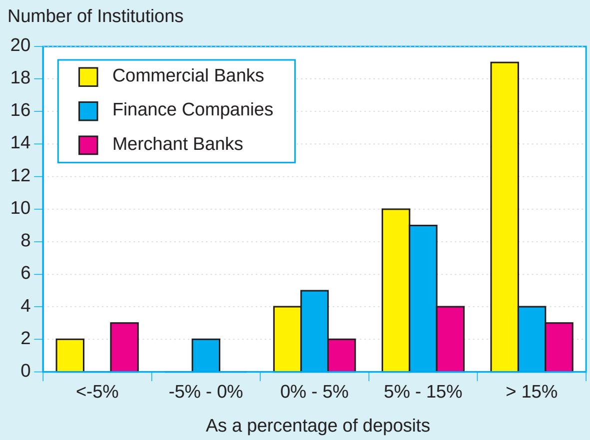
The exchange control policy introduced on 1 September 1998, with the minimum holding period requiring foreign portfolio capital to remain in Malaysia for at least 12 months, had stabilised short-term capital flows and contributed significantly to the stability of the financial markets. On 15 February 1999, the one-year minimum holding period was relaxed, where the principal capital and profits were allowed to be repatriated subject to a graduated levy depending on when the funds were brought into Malaysia and the duration of investment. In September 1999, following the expiry of the one-year minimum holding period, there was a net outflow of portfolio funds of RM5.2 billion, of which a substantial proportion were deposits by non-residents. Subsequently the outflow moderated to RM3.1 billion during the period from October to December 1999. Nevertheless, during the same period, net external liabilities of the banking system experienced a further decline of RM8 billion. This was mainly due to the reduction in foreign currency interbank borrowing by the banking system arising from the US dollar interest rate hike which coincidentally occurred in September 1999. The impact on the banking system liquidity was, however, easily offset by the continuous inflow of export proceeds and some easing of BNM's borrowing in the interbank market.

The activities of Danaharta in removing NPLs from the banking system played a pivotal role in improving the liquidity of banking institutions in 1999. Non-liquefiable NPLs were replaced by Danaharta bonds

Graph 4.7
Banking System: Liquidity Surplus to Meet Withdrawal Obligation of up to One Week in 1999



Graph 4.8
Banking System: Profile of Potential Liquidity Surplus/ Shortfall up to One Month Ahead as at 31 December 1999



which can be discounted or sold under repo with BNM to yield liquidity for the affected banking institutions.

In terms of managing liquidity to meet withdrawal obligations, the banking system as a whole was able to maintain sufficient liquidity, including a buffer stock of liquefiable assets to meet any unexpected requirement. As at 31 December 1999, the banking system had a cumulative liquidity surplus of RM19.9 billion to meet estimated liquidity demands of up to one week and a surplus of RM24.6 billion for demands of up to one month. The amount for December was much lower than the amount normally maintained throughout 1999, partly due to the festive seasons as well as the withdrawal of deposit placements, following the expiry of capital outflow moratorium and US interest rate hikes since September 1999.

In terms of the liquidity position by type of institutions, there was notable difference in the liquidity profile, with merchant banks and finance companies maintaining somewhat lower levels of liquidity surplus due to their smaller deposit base. About 73.1% of banking institutions forecasted surpluses to meet excessive withdrawal based on the past one year historical data (commercial banks: 82.9%, finance companies: 65% and merchant banks: 58.3%), for at least one month ahead as at 31 December 1999, compared to 77.3% as at 31 December 1998.

Interest Rate Risk

The interest rate exposure profile of Malaysian banking institutions is typically signified by a negative gap (net liability) position in the shorter term and a positive gap (net asset) position for tenures above one year. This is because for most banking institutions, their main source of funding comes from their deposits which normally have a maturity of less than one year. The positive gap positions in the longer term tenures arise from holdings of fixed rate debt securities and long term government papers for liquidity and investment purposes. As for finance companies, their positive gap positions were due to their fixed rate loan activities such as hire purchase, block discounting and lease financing.

In terms of the amount of risk, the main source of banking institutions interest rate risk comes from positive gap positions in the 3- to 10-year maturity. Exposures in these tenures have a duration weighted net position of RM1.4 billion for commercial banks, RM0.9 billion for finance companies and RM132 million for merchant banks. (Duration weighted net position indicates the potential loss in the economic value of banking institutions' on- and off-balance sheet positions for a one percentage point increase in interest rate). This 3- to 10-year tenure accounted for 74% of the approximated total duration weighted net position of the banking system. The lack of sufficient medium- to long-term fixed rate funding instruments in the market has constrained the ability of banking institutions in hedging their interest rate risks arising from net asset positions in the longer-term tenures. For commercial banks and merchant banks, exposure to holdings of fixed rate debt securities (amounting to RM25.9 billion) attributed to this phenomenon, while for finance companies, fixed rate loans amounting to RM16.5 billion

Graph 4.9
Banking System: Net Interest Rate Position Mismatches as at end 1999

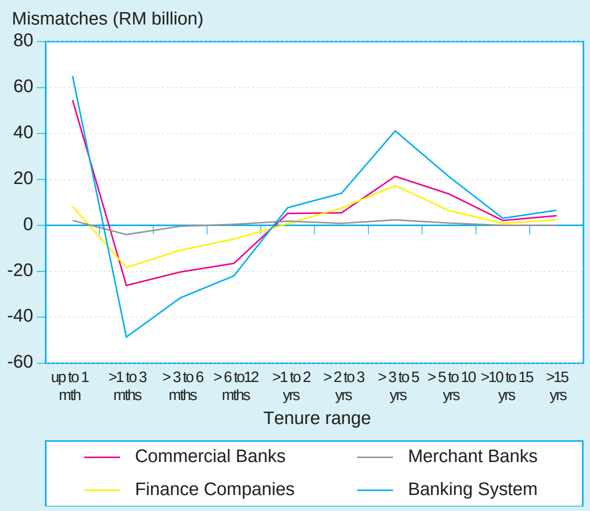


Table 4.9
Banking System: Impact of 1% Rise in Interest Rate on Solvency and Balance Sheet

	Duration Weighted Net Position		
		As a Percentage of	
	(RM million)	Capital Base (%)	Balance Sheet Size (%)
Commercial Banks*	–1,929	–4.5	–0.4
Finance Companies	–1,265	–12.9	–1.1
Merchant Banks	–174	–5.3	–0.4

* Includes Bank Islam Malaysia Bhd. and Bank Muamalat Malaysia Bhd.

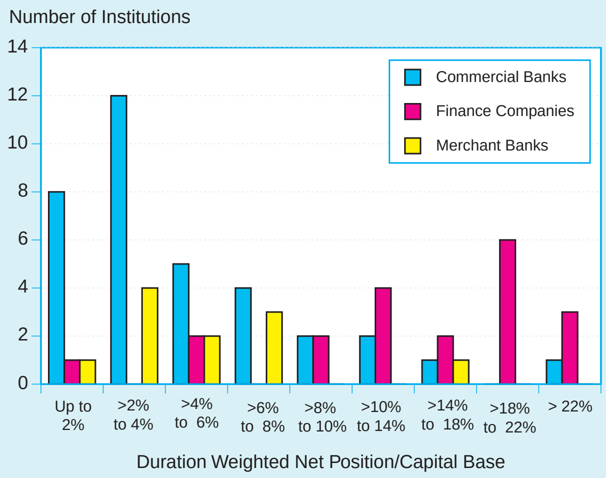
accounted for a larger portion of the positive gap position in this tenure. Most banking institutions' interest rate exposure is in ringgit. Non-ringgit interest rate risk accounted for less than 8% of the banking system's interest rate risk.

In measuring the ability of banking institutions to absorb the potential losses that the mismatches produced, the total approximated duration weighted net position is divided by capital base and total assets respectively.

Interest rate position mismatches have the greatest impact on the solvency and balance sheets of finance companies. A one percentage point rise in interest rates can erode finance companies' capital base by 15.9%. The higher impact reflects the inherent risk of finance company business as approximately 53% of its lending activities are in long-term fixed rate products such as hire purchase, block discounting, leasing and some fixed rate mortgages. The impact of interest rate position mismatches on the solvency of commercial banks and merchant banks is 3.5 times lesser. A one percentage point increase in interest rates would only impact the capital base of commercial banks and merchant banks by 4.5% and 4.3% respectively. Similarly, in terms of sensitivity of the banking institutions' balance sheets to movements in interest rates, finance companies exhibit the highest degree of sensitivity where 1.1% of the balance sheet value would move with every one percentage point change in interest rates. This is 2.8 times more sensitive compared to commercial banks and merchant banks which recorded a sensitivity of 0.4% each.

In reviewing the distribution of banking institutions according to the duration weighted net position as a percentage of capital base, approximately 11% of commercial banks and 1% of merchant banks would

Graph 4.10
Banking System: Distribution by Duration Weighted Net Position as a Percentage of Capital Base as at end 1999



suffer an erosion in economic value of more than 10% of their capital base for a one percentage point increase in interest rates. However, on the same basis, 75% of finance companies would suffer an erosion of more than 10% of their capital base for the same magnitude of change in interest rates.

Equity Risk

As at end 1999, the banking system's exposure to equity was not significant, amounting to RM711 million or 0.1% of total assets. Commercial banks recorded the highest equity position amounting to RM293 million followed by merchant banks at RM244 million and RM174 million for finance companies. Relative to the size of their capital base, merchant banks seemed to have the highest equity exposure at 6.0% compared to commercial banks (0.7%) and finance companies (2.2%). Merchant banks have significantly higher equity exposure as a percentage of their capital base due to their operations in underwriting of equities which amounted to approximately 56% of their total equity exposure at end-1999.

Table 4.10
Banking System: Equity Exposure

	Equity Position (RM million)	Equity/Capital Base (%)	Potential Equity Loss/ Capital Base (%)
Commercial Banks	293	0.7	0.1
Finance Companies	174	2.2	0.4
Merchant Banks	244	6.0	1.2

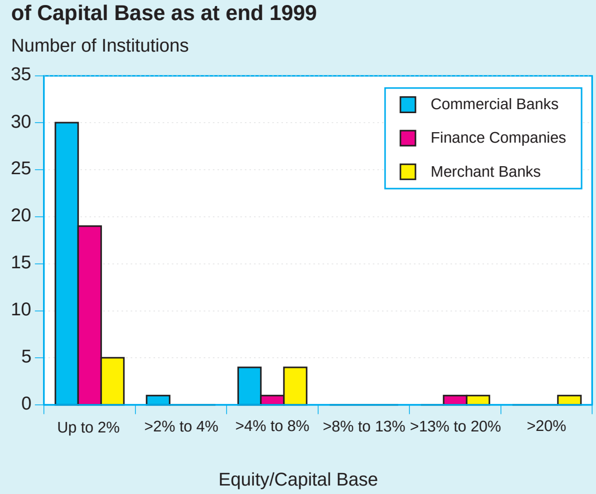
Based on a 10-day volatility of the Kuala Lumpur Composite Index for the period between January 1999 to December 1999, an estimated potential loss of 20% in equity value was possible. Based on such potential loss yardstick, the equity risk faced by the banking system was not significant. Merchant banks had the potential to suffer the highest erosion in capital at 1.2% followed by finance companies at 0.4%, and commercial banks at 0.1%.

Most banking institutions had less than 2% of their capital base exposed to the equities market. Nevertheless, one merchant bank had equity position amounting to more than 20% of its capital base due to the erosion in their capital base arising from the impact of the recent financial crisis.

Foreign Currency Risk

The banking system's net open foreign currency position increased steadily throughout the year. The net open foreign currency position rose from a net short (liability) foreign currency position of RM20.3 million at end January 1999 to a net long (asset) foreign currency position of RM2.3 billion at end-December 1999. This was due to the reduction in net foreign currency liability position by approximately RM8.2 billion to result in a net asset position of RM4 billion as at end-December 1999. The major component driving this increase was the reduction of foreign currency borrowing from the inter-bank market from a high of RM28.3 billion at end-January 1999 to RM19.6 billion at end-December 1999. This gradual reduction in foreign currency borrowing was due to

Graph 4.11
Banking System: Distribution by Equity as a Percentage of Capital Base as at end 1999



Box VI

The Financial Sector in a Globalised Economy

Introduction

In the changing operating environment, the Malaysian financial system must evolve to play its appropriate role in the next stage of the country's economic development. The challenge to the financial system in Malaysia is in terms of its ability to position itself not only to support, but also to act as a catalyst in transforming the economy, particularly, as Malaysia evolves towards becoming a higher value-added and knowledge-based economy (K-economy). The challenges that confront the financial system include meeting the financing needs of these new economic activities and increasingly sophisticated customers, increasing competition, enhancing risk management processes, and changes in the scope of banking business. In addition, the forces of liberalisation and globalisation, together with the rapid advancement of technology, pose additional challenges to the domestic financial system. The ability of the financial system to meet these challenges would be critical in ensuring the prospects for sustainable economic growth. In the context of these challenges, this box article will discuss the implications for the domestic financial system and the broad areas that need to be addressed to enhance the role of the financial system in supporting the changes in the real economy while continuing to strengthen in order to manage new risks in the more globalised financial system. Addressing these issues involves changes by the financial services industry themselves as well as the regulatory authorities.

Challenges in a Dynamic Operating Environment

Financing the New Economy

One of the biggest challenges facing the Malaysian economy amid the rapid transformation of the global economy and emergence of lower cost competitors is to formulate new strategies to support future growth, and to strengthen the structure and improve the efficiency of the economy. The current strategy of moving towards higher value-added economic activities to sustain economic growth is also being reinforced further by the fast pace of development in information and communications technology (ICT). In this connection, while efforts are being directed to further diversify the economic base, strengthen the competitiveness of industry and enhancing productivity-driven growth, the scope of economic transformation needs to take account of global developments in ICT and the increasing role of knowledge-based activities.

The challenge facing the financial system, is to recognise this economic transformation and adapt and adjust to meet the **changing requirements for financing in these new areas of economic activity** in an effective and efficient manner. In particular, the new areas of growth in the K-economy have different characteristics which may limit their access to the traditional form of bank-based financing. These characteristics reflect the nature of these new activities which rely on intangible assets such as knowledge, skills, human capital, while the innovative and "path-breaking" nature of their products lack track record and require long lead time from investment to fruition. Given the characteristics of these new areas of economic activity, their financing needs are in some cases better met by non-bank forms of financing, such as the bond market and venture capital.

Impact and Challenges of Globalisation

The rapid intensification of globalisation in recent years has significantly affected the structure and operations of financial institutions. The global trend towards deregulation and liberalisation in the financial system has led to the blurring of traditional demarcation lines separating the activities of the different groups of financial institutions and removed barriers to competition. As a result, the range of activities that can be undertaken by different groups of financial institutions is converging. Financial institutions worldwide are also undertaking consolidation and mergers, driven primarily by the desire to increase global presence as well as to maximise economies of scale and the scope of activities. Competition can be expected to intensify with the expansion of e-banking activities. The Federal Deposit Insurance Corporation estimates that the number of financial institutions with transactional websites in the US will increase by more than 50% by the end of 2000.

Technological advances in telecommunications, information processing and computing have been a key factor in integrating financial markets, and in enabling the design of innovative and complex financial instruments that have helped to improve risk management and shifted risks to those who are better able to manage them. Consequently, economic agents have become more willing to assume greater risk, while short-term capital funds have flowed rapidly and in large amounts between developed economies and emerging economies since the late 1980s. The integration of financial markets, and the rapid expansion of innovative financial instruments have brought new challenges and transformed the global financial landscape, as reflected in the changes in the relative significance of players in financial markets, nature of financial instruments and volume of activity in the markets.

The above developments will undoubtedly present increased challenges to the financial institutions in Malaysia. In particular, the globalisation process brought about by the trend towards greater liberalisation of domestic financial systems would further reduce the barriers to entry to the domestic financial markets, and as a result, further **intensify competition** in these markets over time. The momentum for liberalisation of the domestic financial system can be expected to pick up as multilateral and plurilateral forums such as the WTO and ASEAN bring about more open financial markets. Domestic financial institutions therefore have to equip themselves to be able to operate competitively in a more liberal and globalised market.

Another important challenge of globalisation is the **management of international capital flows**. Globalisation has made it possible for large amounts of funds to be moved around at a very rapid pace. Short-term capital flows, and new financial products and instruments, while bringing benefits, also bring increased risks, both for the macro economy and financial institutions. In particular, large amounts of short-term capital inflows can complicate the management of macroeconomic policy, as they could increase inflationary pressures or cause significant appreciation of the exchange rate. Similarly, the reversal of the flows could, as was the experience during the Asian crisis, lead to severe macroeconomic implications. These flows are by nature highly volatile and sensitive to market perception of the appropriateness of macroeconomic policies. Therefore, globalisation has increased countries' vulnerability to swings in market sentiments. In such an operating environment, speculative positions against a currency quickly become self-fulfilling and even fundamentally strong economies are adversely affected. The problem is more acute for a small open economy like Malaysia where the volume of international capital flows is huge relative to the size of the domestic financial markets. Given the small size and the stage of development of the domestic financial markets, such flows can result in sharp movements in interest rates, exchange rates and asset prices.

In this environment, financial institutions have to be increasingly vigilant in monitoring and managing market risks. This is because adverse movements and excessive volatility in market prices such as interest rates, currencies and equities could adversely affect an institution's financial condition and pose risks to national financial systems. The Malaysian financial sector needs to take steps to enhance risk management at all levels, namely the national level and the individual institution level. This is crucial to ensure that the benefits of globalisation can be enjoyed, while keeping the associated risks at a prudent and manageable level.

Nevertheless, given the global nature of the problem caused by short-term capital flows, efforts by individual economies to promote financial stability by maintaining sound macroeconomic policy and a strong financial system are not sufficient. There is a need for simultaneous efforts to be pursued at the international level to promote stability in the international financial system and minimise the risks of destabilisation associated with capital flows. In particular, there is a need to enhance transparency and disclosure, as well as regulate the activities of large market players, particularly highly leveraged institutions so as to reduce their ability to cause instability in the global financial markets. Co-operation at the international level, involving the developed and developing countries as well as the private sector, would help to ensure that the international financial system is more stable and not prone to frequent instability and crisis, thereby ensuring the prospects for sustained prosperity.

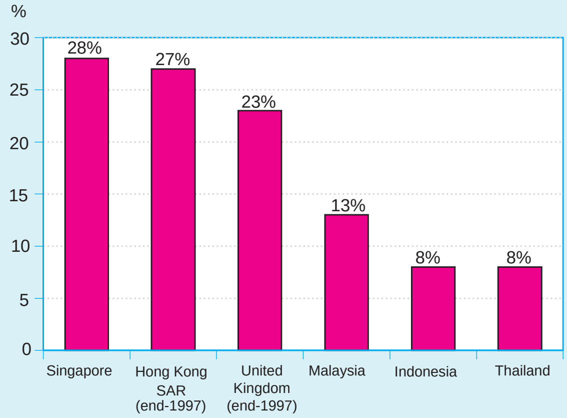
Financial Sector as a New Area of Growth

Efforts to increase the effectiveness, efficiency and competitiveness of the domestic financial sector to meet the challenges of globalisation as well as the financing needs of the economy would present opportunities to develop the financial sector as a growth sector, in line with the vision of promoting services as a source of new growth. In particular, this would result in an increase in the financial sector's contribution to the nation's gross domestic product (GDP). The contribution of the broad financial sector to GDP at 13% in Malaysia is low (Graph VI.1) suggesting that there is scope and opportunity for the sector to increase its contribution. In addition, a progressive and well-developed financial sector would also help to reduce the demand for financial services from abroad, and thus assist in reducing the services deficit of the balance of payments.

Response to Challenges

The further development of the financial system is an area of priority in the national agenda, and resources have been committed to draw up the Master Plans for the development of the financial sector over the next ten years. The Government will formulate the blue-print for the development of the financial sector, including the necessary regulatory framework to ensure a resilient, sound and stable financial sector. The focus on strengthening the financial sector will form the foundation on which further development will take place to develop an efficient and competitive financial sector. On the part of the financial institutions, there is a need to continually enhance their ability to meet the new requirements of customers and the economy, as well as maintain competitiveness by increasing efficiency and effectiveness.

Graph VI.1
Broad Financial Sector as a Share of GDP (at end-1998)



Strengthening the Financial System

The recent economic and financial crisis has heightened the need for developing more diversified forms of financing in the economy and to reduce over-reliance on the banking system. The crisis also demonstrated the vulnerability of the banking institutions, particularly the finance companies, given the fragmented nature of the industry, and the inadequate risk management processes of the banking institutions. Measures were therefore undertaken to address the rising non-performing loans and erosion of capital, as well as providing a platform to restructure corporate debt. In addition, a merger programme for the finance companies was also introduced. At the same time, steps were taken to further strengthen the regulatory and supervisory framework, including the refinement of the capital adequacy framework, greater information disclosure and initiatives to improve risk management of banking institutions.

(a) Regulation and risk management

Given the changes brought about by the globalisation process and advances in technology, efforts to ensure the soundness and stability of the financial system will have to be intensified. Appropriate standards of prudential supervision would need to be maintained to ensure that the benefits of increasing competition and sophistication could be reaped without compromising safety and stability in the financial system. In this regard, BNM will balance between over-regulation, which could limit innovation and inhibit growth and development of the financial system, and under-regulation, which could, on the other hand, undermine the soundness of the system.

In this context, new modalities in bank regulation have to be explored. There has been a global trend towards a market-driven approach as the foundation for the regulatory framework to reap the benefits of competition. Under the market-driven approach, the market is entrusted to allocate risks and resources, while the main task of the supervisor is to contain excessive risk-taking activities, minimise the effect of moral hazard and protect consumers' interests. Under this arrangement, the prudential regulatory and supervisory framework is complemented by the requirement for greater disclosure, transparency and market discipline among market participants.

In the design of the regulatory framework, BNM will strive to balance the elements of protective and preventive regulations. By definition, protective bank regulation is designed to provide support given that the playing field is not level. Meanwhile, preventive bank regulation is designed to curb excess risk-taking by banks and, thereby, reduce the prospect of liquidity and solvency problems. In the market-driven approach, regulation will provide a framework within which competition is allowed to generate a more competitive banking environment without increasing systemic risks, and causing economic and social dislocation. Towards this end, less emphasis will be placed on micro managing, while according greater adherence to a consistent and transparent supervisory philosophy.

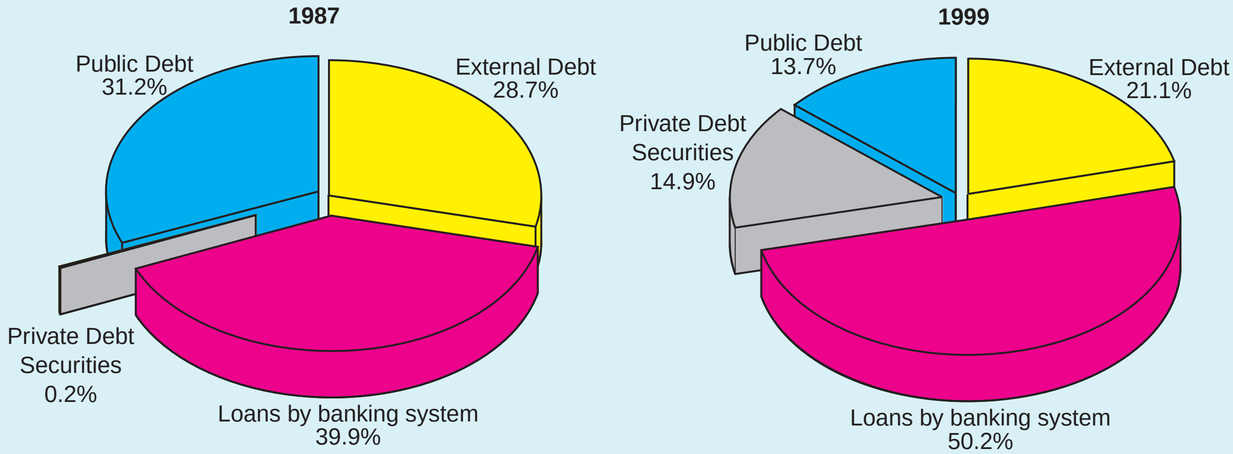
In addition to the role of the authorities, the market-driven approach will also have wide implications on the role of the financial institutions in ensuring the resilience of the banking sector. The accountability, transparency and appropriate skills level of Board members and management will be of paramount importance to promote this development. Bank management will be under greater scrutiny, and needs to be responsive to market requirements to stay competitive. Banking institutions will increasingly have to focus on improving their efficiency and competitiveness. The impetus for these improvements would depend on the banking institutions' capacity for innovation, flexibility, skill enhancement, customer-orientation and product development. Equally important is the need to pay closer attention to the return on equity. In this operating environment, the banking institutions would also have to increase their risk management capability and improve corporate governance. Adequate internal control and systems need to be in place to ensure that there is no excessive risk-taking that could result in adverse consequences. Towards this end, guidelines will be issued to inculcate sound and effective credit risk as well as to set the minimum standards on risk management practices for derivatives. Best practices have also been outlined in order to govern the role of management and employees of banking institutions to ensure that they exhibit high standards of competency, experience and integrity.

(b) Broadening and deepening financial markets

Traditionally, much of the financing for the Malaysian economy is intermediated through the banking system as reflected by the high ratio of bank credit (excluding loans securitised by Cagamas and sold to or managed by Danaharta) to GDP of 126% at the end of 1999 (138.7% at the end of 1998) as well as the high ratio of bank loans to net funds raised in the capital market of 263.0% during 1997. This suggests the potential for developing alternative sources of financing to meet the financing needs of the economy, which would also help diversify risks in the economy. In this regard, there is a need to further deepen and broaden the financial system in terms of financial products and markets.

As there is already a well-functioning and active equity market in Malaysia, efforts have been stepped up to further develop private debt securities as well as to encourage secondary trading in the Government securities markets. The development of an active private debt securities market would enhance the capability of the domestic capital market to accommodate large and more complex funding arrangements and diversify financing away from the banking sector. The bond market would allow companies to obtain long-term fixed rate financing at a lower cost relative to bank credit. This is because intermediation would be minimised, and as risks are diversified among a large pool of investors and liquidity risks for investors

Graph VI.2
Financing of the Economy



are reduced, investors are prepared to accept a lower return.

The commencement of trading of the Malaysian Exchange of Securities Dealing & Automated Quotation Bhd. (MESDAQ), a stock exchange targeted specifically at growth and technology companies, is also a significant step in providing an alternative source of financing**, and would also serve as an exit mechanism for venture capital companies**. At the same time, the Government recognises that the venture capital industry has an important role to play in providing equity capital to finance high-risk investments to support the emergence of a knowledge-based economy**, and has granted the industry tax incentives.** Other alternative sources of finance such as "business angel" investment and "specialist seed capital" firms would complement venture capital financing and would also have to be promoted.

The development of non-bank based sources of financing bode well for the development of a K-economy. Given the different nature of the business, alternative sources of financing for high-risk investments are required. In the case of venture capital, it allows investors to share more fully in the rewards to a successful venture and it helps firms avoid the cash flow problems associated with debt finance. Equally important is the development of instruments that enable the unbundling of risks so that such risks will be borne and managed by those who are best able to do so, so that the risk tolerance of the economy increases and financing would be available at reasonable cost.

Liberalisation

The Government recognises that gradual and progressive liberalisation of the financial system would contribute towards creating a more efficient, competitive and market-driven financial sector, thus enabling the sector to play a more efficient and effective role in the economy. It is clear that the protection of the domestic economy, including the financial system, is not a permanent option in a global economy. Protective measures if maintained for too long would erode competitiveness and prospects of economic growth in the longer term. In addition, the circumvention of regulatory obstacles will reduce the effectiveness of protection. Such circumvention would be difficult to detect with new technology and the emergence of e-transactions.

The Malaysian financial sector already has significant foreign presence**.** In the banking sector, there are 13 commercial banks that are wholly foreign-owned, with foreigners in the aggregate, accounting for about 30% of total assets of commercial banks. Similarly, foreign presence also features significantly in the insurance industry, with foreign market share amounting to 74% of life insurance premiums and 35% of general insurance premiums. Thus far, Malaysia has adopted a gradual and progressive approach to liberalisation where liberalisation is undertaken at a pace that is consistent with the prevailing conditions, infrastructrure and regulatory framework and the needs of the economy, taking into consideration the need to ensure that liberalisation does not marginalise the domestic financial institutions.

The strengthening of the financial system is a necessary first step in the liberalisation process. At the same time, the forces of globalisation and the momentum of multilateral fora to open up financial markets would place greater urgency on banking institutions to focus efforts to enhance their competitiveness. In this context, the measures taken thus far to strengthen the banking system and the present merger process in the banking industry would help the institutions to achieve critical size. This would enable such institutions to reap the gains from economies of scale, reduce costs and excess capacity, as well as afford higher spending on information technology and risk management systems.

New Sources of Growth for the Financial Sector

As competition increases, intermediation margins would narrow and reduce traditional interest incomes of the banking institutions. This trend will intensify as capital markets develop further and the process of disintermediation lead more corporations to access the capital markets directly for financing. In order to meet these challenges, the domestic banking institutions must seek new sources of income. In this regard, non-interest based activities represent a significant source of potential growth for the domestic banking sector, given that only 29% of the earnings of the banking institutions in Malaysia are accounted for by non-interest income, compared to approximately 50% for British banks. These activities include traditional fee-based activities such as equity underwriting and guarantee as well as consultancy.

The financial system would also have to play a role in developing products and solutions that can meet the changing and more sophisticated needs of new areas of economic activity. In this operating environment, bank customers will no longer be satisfied with the traditional “bread and butter” products and banking institutions need to strive to bring the right products and solutions that anticipate the needs of their customers. In addition, the development of alternative sources of financing, such as a vibrant capital market, is a vital complement to the role of the banking institutions. In this regard, technology would enable the financial institutions to further enhance their services, tap new opportunities and develop new products. For instance, those with the capacity and the necessary skills would be in a position to provide other services such as document handling and transmission services relating to trade financing. The broadening and deepening of the financial markets would also stimulate the growth of the financial sector, particularly in the form of increased activities, and hence fee-income, for a multitude of financial institutions, including, investment banks and securities and research houses, as well as support services such as rating agencies and consultancy firms.

New Technology

Investment in new technology is important to enable the financial institutions to enhance their effectiveness, efficiency and ability to provide value-added services, while also being better able to meet the financing needs of the new economy. This need to invest in new technology is continual and is primarily the result of the rapid pace of IT innovation which has resulted in an acceleration of “creative destruction”, with capital shifting from failing technology into new, cutting-edge technology. Financial institutions which fail to invest in the latter would soon find themselves increasingly disadvantaged to compete, as they would lack the ability to develop innovative products, while efficiency deteriorates and delivery costs increase. Over time, efficiency of the financial system and economy would be affected.

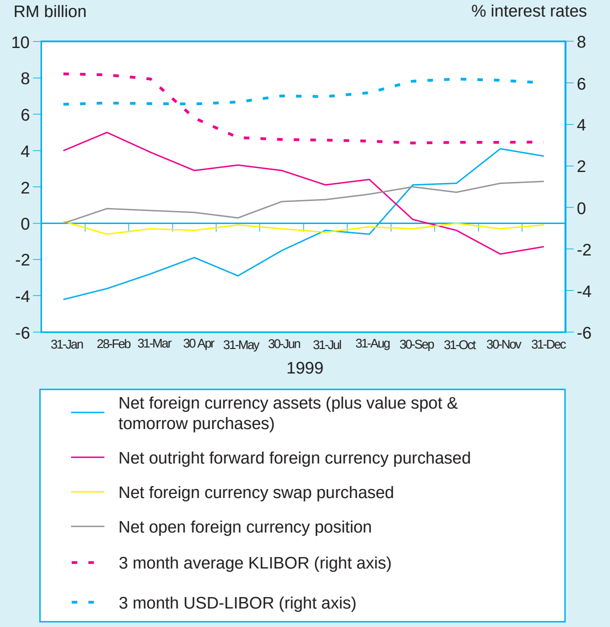
Human Capital

A necessary complement to the above efforts is the development of human capital. In particular, the transition to a truly knowledge-based financial sector which is more competitive, effective and better able to manage risks would require further developments in a number of key areas. *Firstly*, **commitment of management teams:** the management of financial institutions need to be vibrant and innovative in adding value to the traditional financial activities, and in exploring new avenues to enhance services. In this regard, an environment conducive for innovation and creativity must be promoted. The importance of management support is reflected by the results of a recent MORI poll, which revealed that 91% and 65% of companies surveyed in the US and Europe respectively had a board member in charge of e-business. *Secondly*, **human and intellectual capital:** knowledge-based financial activities such as e-banking and on-line share trading will require financial services employees to be technologically competent and able to think, assimilate and apply information and knowledge. In addition, in marketing the multitude of new financial products, financial services employees must have a thorough understanding of these products and the associated risks so that customers obtain the benefits of these products with a full understanding of the risks involved. *Thirdly*, **knowledge infrastructure:** this would allow ideas and knowledge to be transmitted, shared and built within and across companies and countries. The infrastructure will consist of physical networks and, possibly, their interconnections with knowledge or 'thought' centres such as universities, and business centres globally.

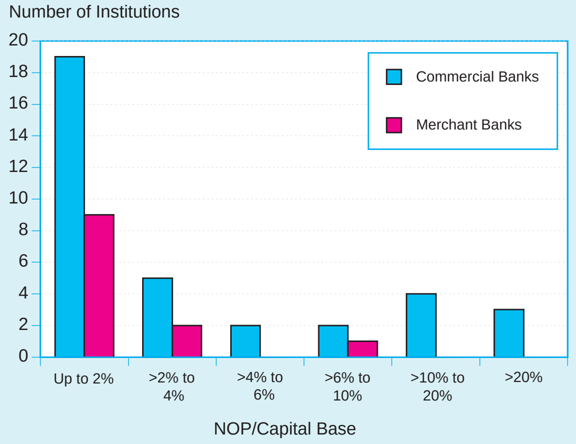
Conclusion

Given the important role of the financial sector in the economy, it is clear that meeting the above challenges would require efforts on the part of both the Government and the financial industry. The Government would focus on creating a conducive regulatory and supervisory framework that encourages efficiency and competition while maintaining the soundness of the financial system. Ultimately, it is in the interest of the financial institutions themselves to continually enhance their resilience, efficiency and competitiveness. The ability of the financial system to assume higher risks while remaining efficient, competitive and resilient in the face of these challenges would ensure its continued prosperity.

Graph 4.12
Banking System: Foreign Currency Exposure



Graph 4.13
Banking System: Distribution by Net Open Foreign Currency Position as a Percentage of Capital Base as at end 1999



the declining attraction of US dollar (US$) borrowings as opposed to ringgit borrowings as the weighted average 3-month KLIBOR rate fell from 6.43% per annum at end-January 1999 to 3.15% per annum at end-December 1999. In contrast, the 3-month US$ LIBOR interest rate rose from 4.97% per annum at end-January 1999 to 6.00% per annum at end-December 1999.

During the year, the outstanding amount of gross forward foreign exchange contracts purchased by the banking system declined from RM11.1 billion as at end-January 1999 to RM7.3 billion as at end-December 1999 despite the consistent improvement in gross exports. In contrast, the outstanding amount of gross forward foreign exchange contracts sold by the banking system increased from RM7 billion as at end-January 1999 to RM8.5 billion as at end-December 1999. This reversed the banking system's position from being a net purchaser of forward foreign exchange contracts in January 1999 with a net outstanding balance of RM4 billion to a net seller of forward foreign exchange contracts (from October 1999 onwards) with a net outstanding balance of RM1.3 billion as at end 1999. This change in position was due to the shift in interest rate differential from favouring the ringgit to favouring the US$. With the ringgit-US$ exchange rate pegged at RM3.8, exporters were becoming less attracted to the increasing forward discount rate caused by the falling ringgit interest rates. The 3-month average KLIBOR fell by 2.83 percentage points from 6.19% per annum at end-March 1999 to 3.36% per annum at end-May 1999, while the 3-month US$-LIBOR rate rose from 5.52% per annum at end-August 1999 to 6.08% per annum in September 1999. As a result, importers were buying US$ forward contracts to take advantage of the forward discount rate which contributed to the increase of RM1.5 billion for the year.

Table 4.11
Banking System: Foreign Currency Exposure

	Net Open Foreign Currency Position (NOP) (RM million)	NOP/Capital Base (%)
Commercial Banks	2,217	5.1
Merchant Banks	92	2.3

Nevertheless, despite the size of foreign exchange activity, the commercial banks and merchant banks normally hedged their positions and maintained their net exposure within a manageable range. As at end-December 1999 commercial banks' net open foreign currency position as a percentage of their capital base stood at 5.1% compared to 2.3% for merchant banks. All merchant banks and 80% of commercial banks had net open foreign currency positions not exceeding 10% of their capital base. A number of commercial banks, however, were maintaining significant long foreign currency positions partly to take advantage of the favourable interest rate differentials which existed between domestic ringgit interest rates and US$ interest rates towards the second half of 1999.

Table 4.12
Banking System: Constituents of Capital

	As at end-		Annual change	
	1998	1999		
	RM million		RM million	(%)
Tier-1 capital	42,102	43,829	1,728	4.1
Tier-2 capital	18,302	15,008	–3,294	–18.0
Total capital	60,403	58,837	–1,566	–2.6
Less:				
Investment in subsidiaries and holdings of other banking institutions' capital	4,665	4,892	227	4.9
Capital base	55,739	53,945	–1,793	–3.2
Risk assets:				
0%	87,976	121,707	33,731	38.3
10%	26,160	21,735	–4,426	–16.9
20%	109,742	103,670	–6,072	–5.5
50%	62,452	67,828	5,376	8.6
100%	414,994	381,813	–33,181	–8.0
Total risk-weighted assets	470,785	438,634	–32,151	–6.8
Risk-weighted capital ratio (%)				
Banking system	11.8	12.3	0.5	
Commercial banks	11.7	12.5	0.8	
Finance companies	11.1	10.4	–0.7	
Merchant banks	15.2	14.6	–0.6	

Capital Strength

In consonance with the recovery of the Malaysian economy, total Tier-1 capital of the banking system increased by RM1.7 billion (4.1%) to RM43.8 billion as at end-1999. The increase was due to better overall profitability of the banking system and the conversion of some banking institutions' Exchangeable Subordinated Capital Loan of RM2.6 billion to either ordinary or preference shares. The year, however, saw a reduction in the paid-up capital of finance companies due mainly to the absorption of eight finance companies by their parent banks. Tier-2 capital funds showed a significant decline as a result of conversion and repayment of Exchangeable Subordinated Capital Loan totalling RM4.5 billion. Overall, capital base declined by 3.2% or RM1.8 billion.

Total risk-weighted assets of the banking system declined by 6.8% or RM32.2 billion to RM 438.6 billion as at end-1999, due mainly to negative loan growth of the banking system. This contraction of credit contributed in large part to the decrease of RM33.2 billion or 8.0% in assets of the 100% risk-weight category. Similarly, risk-weighted assets in the 10% category fell significantly by RM4.4 billion or 16.9% as banking institutions reduced the holdings of Cagamas papers. On the other hand, assets in the 0% and 50% risk-weight category increased for the year to RM121.7 billion and RM67.8 billion respectively due mainly to inter-bank placement with BNM and the expansion in home financing.

On the whole, the RWCR of the banking system showed an increase of 0.5 percentage points to 12.3% as at end-1999. The commercial banks showed an improvement in their RWCR from their end-1998 position to 12.5%. Finance companies and merchant banks, however, experienced a decline in their RWCR ratio due to overall losses for the year 1999.

Islamic Banking

Sources and Uses of Funds

The strong and early economic recovery had positive spillover effects on the Islamic banking system which was also affected by the economic crisis. The total assets of the Islamic banking sector continued to increase strongly by RM14.1 billion or 65.3% to RM35.8 billion as at end-1999. The growth was contributed mainly by a sharp increase in trading and investment securities held by the banking institutions (121.8% or RM11.2 billion) and holding of cash and short-term funds (123.8% or RM3.5 billion). The Islamic banks recorded the highest asset growth of 97.5%, although the commercial banks still have the largest market share of assets in Islamic banking of 44.2%. The share of Islamic banking assets in the banking system rose to 5.4% from 3.4% in 1998.

During the year, a major portion of funds in the Islamic banking sector continued to be sourced from deposits placed with the banking institutions, which recorded a growth of 50.6% (RM8.3 billion) to RM24.7 billion, accounting for 69.2% of the total resources of the Islamic banking sector. As in previous years, the commercial banks and the Islamic banks accounted for the bulk of the increase in these deposits, mobilising 81% of total deposits in the Islamic banking sector. In terms of types of customers, the deposits were held mainly by the domestic non-financial private sector, comprising individuals and business enterprises, which constituted about 59.8% of total deposits. Investment

Table 4.13
Islamic Banking: Key Data

	As at end-		Annual Change (%)	
	1998	1999	1998	1999
Number of financial institutions	49	52	–5.8	6.1
Commercial banks	25	22	4.2	–12.0
Finance companies	18	16	–18.2	–11.1
Merchant banks	5	5	–	0.0
Islamic banks	1	2	–	100.0
Discount houses	–	7	–	–
Total assets (RM million)	21,632	35,754	21.0	65.3
Commercial banks	11,835	15,812	30.4	33.6
Finance companies	3,321	4,704	13.6	41.6
Merchant banks	778	1,407	14.9	80.8
Islamic banks	5,698	11,253	9.5	97.5
Discount houses	–	2,578	–	–
Total deposits (RM million)	16,432	24,739	59.1	50.6
Commercial banks	9,108	10,366	63.9	13.8
Finance companies	2,677	2,642	123.1	–1.3
Merchant banks	607	909	73.9	49.8
Islamic banks	4,040	9,713	25.3	140.4
Discount houses	–	1,109.0	–	–
Total financing (RM million)	10,943	14,007	1.8	28.0
Commercial banks	4,764	5,203	1.2	9.2
Finance companies	2,108	2,996	–3.7	42.1
Merchant banks	421	778	–16.3	84.8
Islamic banks	3,650	5,030	8.9	37.8
Discount houses	–	–	–	–
Financing-deposits ratio (%)	66.6	56.6	–37.5	–15.0
Commercial banks	52.3	50.2	–32.4	–4.0
Finance companies	78.7	113.4	–103.8	44.0
Merchant banks	69.4	85.6	–74.8	23.4
Islamic banks	90.3	51.8	–13.6	–42.7
Discount houses	0.0	0.0	0.0	0.0
Number of branches	90	128	n.a	2.4
Commercial banks	7	6	n.a	–14.3
Finance companies	3	2	n.a	–33.3
Islamic banks	80	120	n.a	50.0
Number of counters	2,391	2,095	n.a	–21.5
Commercial banks	1,619	1,370	n.a	–15.4
Finance companies	766	719	n.a	–6.1
Merchant banks	6	6	n.a	–

deposits continued to account for the bulk of deposits placed in Islamic banking, accounting for 65.6% of the increase in total deposits. In terms of maturity profile, investment deposits remained concentrated in the shorter-end maturities. Notably, current deposits recorded a growth of 79.9% in 1999 thereby constituting 22.2% of total Islamic banking deposits, as compared with a decline of 8.2% in 1998.

The shareholders' funds of the Islamic bank and the Islamic banking capital fund of the conventional banking institutions also improved during the year, increasing by RM589 million to RM2.2 billion as at end-1999. The increase was contributed by the new capital injection into the second Islamic bank and the Islamic banking fund of the discount houses as well as the higher amount of retained profits. In terms of profitability, the Islamic banking sector recorded an impressive pre-tax profit of RM352 million for the financial year ended 1999, higher by 137.8% than the pre-tax profit of RM148 million recorded for the financial year ended 1998. The improved profit was largely due to higher financing income and lower financing loss provisions made by the banking institutions in 1999. The lower financing loss provisions charged during the year were largely due to higher write-backs and recoveries.

The Islamic funds mobilised were utilised mainly for financing activities, while the remaining funds were largely placed as deposits with other banking institutions, in particular in the form of Mudharabah inter-bank investment, and invested in Islamic securities. In 1999, total financing extended by the Islamic banking sector continued to expand by RM3.1 billion or 28%. However, the growth in financing was much lower than the growth in deposits (50.6%). As a result, the financing-deposits ratio declined from 66.6% as at end-1998 to 56.6% as at end-1999.

The exposure of Islamic banking to the broad property sector remained significant at 42.6% of total

Table 4.14
Islamic Banking: Sources and Uses of Funds

	Annual change		As at end-1999	
	1998	1999		
	RM million			% share
Sources:				
Capital and reserves	220	589	2,191	6.13
Deposits	5,647	8,307	24,739	69.19
Amount due to financial institutions	691	3,220	6,498	18.17
Other liabilities	–1,451	2,006	2,326	6.51
Total	5,108	14,121	35,754	100.00
Uses:				
Loans, financing and advances	584	2,872	13,333	37.29
Investment securities	1,752	3,357	6,844	19.14
Dealing securities	1,381	2,808	4,381	12.25
Amount due from financial institutions	1,084	1,822	4,062	11.36
Other assets	308	3,263	7,134	19.95

Table 4.15
Islamic Banking: Deposits by Type and Institutions

	Annual change				As at end-1999
	1998		1999		
	RM million	%	RM million	%	RM million
Current deposits	–273	–8.2	2,434	79.9	5,480
Commercial banks	–134	–6.2	1,288	63.6	3,313
Islamic banks	–139	–12.0	1,146	112.2	2,167
Savings deposits	225	12.4	349	17.1	2,395
Commercial banks	171	20.0	–107	–10.4	917
Finance companies	47	36.4	108	61.4	284
Islamic banks	7	0.8	348	41.1	1,194
Investment deposits	5,180	108.9	5,428	65.8	16,472
Commercial banks	3,217	150.3	470	8.8	5,828
Finance companies	1,439	138.2	–123	–5.0	2,357
Merchant banks	258	73.9	302	49.8	909
Islamic banks	266	21.7	4,779	320.7	6,269
Discount houses	–	–	1,109	–	1,109
Other deposits	970	223.0	–1,014	–72.1	391
Commercial banks	296	73.1	–393	–56.1	308
Finance companies	–9	–30.0	–21	–98.6	–
Merchant banks	–	–	–	–	–
Islamic banks	683	•	–600	–	83
Discount houses	–	–	–	–	–

financing, followed by the manufacturing sector which accounted for 9% of total financing. The growth in the broad property sector was driven mainly by the rapid growth in house financing which increased by RM1.1 billion. The high demand for house financing was due mainly to the fixed-rate nature of Islamic financing as well as the competitiveness of its financing rate, which provided the borrowers with an opportunity to lock

Table 4.16
Islamic Banking: Direction of Lending

	Annual change		As at end-1999
	1998	1999	
	RM million		
Agriculture	–22	319	491
Mining & quarrying	–4	5	74
Manufacturing	15	–46	1,252
Electricity	–66	188	221
Real estate & construction	–431	270	2,132
Housing	675	1,142	3,841
General commerce	104	–1	627
Transport and storage	0	270	990
Finance, insurance & business services	151	444	901
Purchase of stocks & shares	–275	–108	745
Consumption credit	314	–69	878
Others	–270	650	1,855
Total	**194**	**3,064**	**14,007**

Table 4.17
Islamic Banking: Non-performing Financing and Financing Loss Provision

	As at end-	
	1998	1999
	RM million	
Islamic banking		
General provisions	170	238
Income-in-suspense	224	373
Specific provisions	61	110
Non-performing financing (NPF)	1,451	1,585
Net NPF ratio (%)	10.94	8.15
Total provisions/ NPF (%)	31.36	45.49

their cost of financing over the long term. Bai' Bithaman Ajil or deferred payment sale remained the most popular mode of Islamic financing with a share of 58.7% of total financing as at the end of 1999.

Asset Quality

The asset quality of Islamic financing improved in 1999 in line with the improved economic conditions. With the economy recovering, the ability of borrowers to service their debts had improved significantly. This was evident in the decline in the non-performing financing (NPF) ratio from 10.9% in 1998 to 8.2% in 1999. Total provisions set aside on these NPF amounted to 45.5% of NPF.

In terms of NPF by sector, as at end-December 1999, the broad property sector accounted for 49.0% of total NPF. A major proportion of NPF to the broad property sector originated from the real estate and construction sectors, which accounted for 60.3% of total broad property sector NPF.

Developments

An important event in Islamic banking during 1999 was the setting-up of the second Islamic bank in Malaysia, namely Bank Muamalat Malaysia Berhad (BMMB). The establishment of BMMB arose from the merger between Bank Bumiputra Malaysia Berhad (BBMB) and Bank of Commerce (M) Berhad (BOCB). Under the merger arrangement, the Islamic banking assets and liabilities of BBMB, BOCB and BBMB Kewangan Berhad (BBMBK) were transferred to BMMB, while the conventional operations of

BBMB, BOCB and BBMBK were transferred to BOCB. In addition, BMMB was given 40 branches of BBMB and BBMBK in various locations throughout Malaysia with a staff workforce of 1,000. The bank commenced operations on 1 October 1999. The setting-up of the second Islamic bank is expected to play a key role towards fostering an active and progressive Islamic banking system.

BNM also allowed full-fledged Islamic banking branches operated by banking institutions participating in the Islamic Banking Scheme (SPI banks) to accept conventional deposit placements, facilitate withdrawal of conventional deposits and receive payments for conventional loans from customers of conventional branches. The move is to enable customers of the same banking institution to perform their banking transactions with all branches, although the approval is subject to the condition that the full-fledged Islamic branches implement adequate mechanisms to ensure proper segregation between the conventional and Islamic funds.

One of the requirements to be met by the SPI banks by end-1999 was the attainment of a minimum target of 5% market share in terms of deposits and financing granted by their respective banking institutions. Nevertheless, taking cognizance of the financial crisis and the merger exercise currently being carried out by the domestic banking institutions, BNM has decided to defer the compliance deadline to end-2000. Notwithstanding the deferment, 10 SPI banks, all of which are domestic banks, managed to surpass the 5% target in terms of deposits and financing at end-1999. In terms of financing, three commercial banks, five finance companies and two merchant banks met the target, while seven commercial banks, two finance companies and one merchant bank reached the 5% minimum market share for deposits. It is expected that once the merger exercise has been completed, the SPI banks will channel more resources and efforts towards meeting the 5% target.

The first term of the National Syariah Advisory Council for Islamic Banking and Takaful (the Council) ended on 30 April 1999. Among the decisions made by the Council were as follows:

(i) Banking institutions are allowed to charge compensation on the default financing;

(ii) Women and non-Muslim lawyers could attest to all Islamic financial documents;

(iii) Pledging an asset for more than one contract is allowed subject to the following:
   (a) permission from the first chargee;
   (b) sufficient value to cover all contracts; and
   (c) no “dharar” (harmful) to any party to the contract;

(iv) Cross default clause is allowed to be incorporated in the Islamic banking agreement in order to ensure justice;

(v) For Islamic hire purchase, only the concept of Al-Ijarah Thumma Al-Bai’ (Lease and then purchase) will be applied; and

(vi) All banking institutions would be compensated under the RENTAS system for extending overnight financing to other banking institutions, and the amount of compensation is based on the overnight average rate of return of Islamic banks and SPI banking institutions.

For the second term of the Council, BNM has re-appointed four Council members, and appointed two new Council members.

Other Financial Institutions

Discount Houses

The discount houses experienced a further contraction in activities, with total resources declining by RM1.4 billion or 7.1% to RM18.6 billion at end-1999 (–RM970.2 million or –4.6% in 1998). Nevertheless, the environment of ample liquidity and low interest rates enabled the discount houses to achieve a higher level of profitability in 1999 as income earned on investments exceeded the cost of funds appropriated by the discount houses.

The decline in the industry’s total resources was due to lower interbank borrowings (–RM2.9 billion or –30.3%). Lending by banking institutions to discount houses had declined due, to some extent, to changes in liquidity requirements under the New Liquidity Framework introduced by BNM, as well as the consolidation of the banking system, which saw several mergers and absorptions taking place in 1999. In addition, interest rates on interbank borrowings were higher than interest rates on fixed deposits throughout the year, which made such borrowings a relatively more expensive source of funding for discount houses.

Table 4.18
Discount Houses: Sources and Uses of Funds

	Annual change		As at end-1999
	1998	1999	
	RM million		
Sources:			
Approved capital funds	157	549	1,596
Deposits	–4,274	933	10,095
Interbank borrowings	2,977	–2,873	6,596
Others	169	–24	272
Total	**-970**	**-1415**	**18,559**
Uses:			
Investments in securities	911	–2,388	16,051
Government debt securites	653	–333	631
MGS held	644	–363	591
Private debt securities	3	–1,512	10,362
Bankers acceptances	–169	–1,096	3,185
Negotiable instruments of deposit	544	38	947
Cagamas debt securities	–211	206	452
Others	91	309	474
Interbank placements	–1,231	828	1,819
Others	–650	145	689

Nevertheless, total deposits mobilised by discount houses increased by 10.2%, reflecting mainly an increase in deposits by non-bank entities. In terms of type of deposits, fixed deposits increased by RM1.4 billion or 23.6% (+RM660.6 million or 12.4% in 1998) mainly due to higher deposits by non-bank financial institutions (+RM906.2 million) and business enterprises (+RM539.4 million). As the economy recovered, many corporations had surplus liquidity and the discount houses were able to tap some of these funds by offering higher rates than those offered by banking institutions. Meanwhile, call money placed with discount houses declined by RM401.4 million or 14.6% (–RM4.8 billion or –63.6% in 1998), mainly as a result of lower placements by commercial banks (–RM674.5 million) and finance companies (–RM456.8 million). The decline was partially offset by higher deposits from non-bank financial institutions (+RM426.9 million) and business enterprises (+RM314.1 million).

Following the contraction in total resources, total investment of discount houses declined by 13% in 1999 (5.2% in 1998). The bulk of the decline was due to lower investments in private debt securities, bankers acceptances and Malaysian Government Securities. On the other hand, investments in negotiable instruments of deposits increased marginally.

During the year, the fee-based activities of the discount houses, however, increased. The industry as a whole arranged, lead-managed and co-managed the issuance of private debt securities (PDS) amounting to RM1.9 billion (RM180 million in 1998). Meanwhile, the total amount underwritten by the discount houses increased to RM585.6 million (RM508 million in 1998), representing a total of 15 PDS issues (seven issues in 1998). As in the previous year, there were only three discount houses appointed as principal dealers in 1999. However, following the annual review of the Principal Dealer System by BNM at the end of 1999, the number of discount houses appointed as principal dealers has been reduced to two, effective January 2000.

National Savings Bank

During the year, the National Savings Bank (NSB) reviewed its corporate mission to be a total financial services provider following the banking sector merger programme, which involved NSB's associate company, BSN Commercial Malaysia Berhad and its subsidiary companies, BSN Finance Berhad and BSN Merchant Bank Berhad. Following the review, the decision was taken to focus on its core business of retail banking with an emphasis on personal finance, catering for the total financial requirements of individuals and households.

Total resources of the NSB increased by RM594 million or 7.2% to RM8.8 billion at end-1999 (+RM697.9 million or 9.2% in 1998). The increase was due mainly to higher deposits, although the number of active account holders declined marginally from 8.7 million at the end of 1998 to 8.5 million at the end of 1999. By type of deposits, the main source of increase was fixed deposits, GIRO and Sistem Perbankan Islam (SPI) deposits. Fixed deposits rose by 29.8% reflecting mainly an increase in placements by corporate clients from RM1.2 billion to RM1.8 billion. Fixed deposits by individuals also increased by RM124.8 million. GIRO deposits turned around to increase by 7.7% in 1999 (a decline of 3.5% in 1998). Of significance was that SPI deposits more than doubled, partly attributable to higher returns relative to fixed deposits.

During the year, fixed deposits remained the most popular deposit scheme, accounting for 44.8% of total deposits outstanding at the end of 1999, followed by GIRO deposits with a share of 34.5%. On the other hand, savings deposits continued to decline by 5.3% in 1999 reflecting, to some extent, a shift from savings to fixed deposits to take advantage of relatively higher interest rates. Savings rates were in the range of

1.50–3.75% while fixed deposit rates were in the range of 3.20–3.75%. Meanwhile, the number of Premium Savings Certificates sold during the year declined by 7% to 482,200 certificates. However, the value of these new certificates exceeded the value of certificates redeemed during the year. Thus, the outstanding amount of Premium Savings Certificates stood at RM556 million at the end of 1999 (RM543.6 million at end-1998). In 1999, NSB introduced a new deposit scheme, namely the Children's Higher Education Savings Scheme (CHESS).

As at the end of 1999, the bulk of funds mobilised by NSB was invested in securities (34.6%), deposits with financial institutions (25.4%) and loans (21.5%). As in previous years, the bulk of investment in securities was in Malaysian Government Securities (MGS), which accounted for 29.6% of the total investment as at end-1999. The investment in MGS continued to decline to RM904.9 million at end-1999 primarily due to redemption to meet cash needs to prepare for potential withdrawals in conjunction with the rollover to year 2000. The statutory requirement for minimum holdings of Government securities (comprising MGS, Government promissory notes, Government guaranteed bonds and Cagamas bonds) by NSB stood at 30% of total investments as at end-1999. Despite redemption of MGS, NSB exceeded this minimum requirement by 17.8 percentage points. Other investments as at end-1999 included trustee stocks (RM845.3 million), Government guaranteed bonds (RM378.3 million), non-trustee stocks (RM250 million), Government promissory notes (RM158.3 million) and unquoted shares (RM145.1 million).

Table 4.19
National Savings Bank

	Annual change		As at end-1999*p*
	1998	1999*p*	
	RM million		
Deposit[1]	717	1,024	7,681
Savings	–136	–77	1,373
Fixed	897	789	3,438
Save-As-You-Earn	–5	–1	16
GIRO	–90	189	2,650
Sistem Perbankan Islam(SPI)	52	124	205
Premium Savings Certificates	–41	12	556
Investments (book value)	–114	–899	3,060
Malaysian Government Securities	–193	–288	905
Other investments	80	–612	2,155
Deposit with financial institutions	568	994	2,244
Gross loans	185	–198	2,008
Net loans (less provision for doubtful debts, bad debts and interest in suspense)	162	–210	1,901
Number of NSB branches[2]	–20	–9	426
Number of post offices with NSB facilities	–1	0	641
Number of account holders ('000)	–204	–156	8,518

[1] Includes interest credited
[2] Includes mini-branches and sub-branches
p Preliminary

Lending operations of NSB contracted in 1999. Total loans outstanding declined by RM198.4 million or 9% (+RM185.3 million or 9.2% in 1998) to RM2 billion as at end-1999. The lower volume of loans outstanding was mainly the result of a decline of RM205.6 million in loans extended for the purchase of passenger cars. Nevertheless, loans extended for the purchase of residential property, which accounted for the largest share of total loans outstanding (51.6%), increased by RM30.6 million. The moderate increase relative to that of banking institutions reflected greater competition. Although NSB's average lending rate for housing loans was lower in 1999, at 8.5% (9.5% in 1998), it was less competitive than the housing loan packages offered by some banking institutions which were lower than the average base lending rate of the banking system.

The bulk of loans continued to be extended to individuals, amounting to RM1.7 billion or 85.7% of total loans outstanding. Of this portion, RM1 billion or 58.9% was granted for the purchase of houses and RM0.5 billion or 31.6% was utilised for hire-purchase financing. While corporate loans increased by RM35 million or 33.9% (–RM4.8 million or –4.4% in 1998), subordinate loans declined by RM25 million. As at end-1999, provisions for doubtful debts and non-performing loans (NPLs) amounted to 4.3% (3.4% in 1998) and 8.2% (9.1% in 1998) respectively of NSB's total loans outstanding. The NPLs were mainly related to hire purchase and credit card loans.

Deposits placed with financial institutions increased by RM994 million to RM2.2 billion at end-1999, accounting for a higher share of 25.4% of total assets (15.2% as at end-1998).

In 1999, several branches of NSB were merged, reducing the total number of branches and sub-branches from 435 to 426 at the end of 1999. Savings account facilities were provided in 626 permanent and 15 mobile post offices. Meanwhile, the total number of Automated Teller Machines increased by 10 to 597 as at end-1999.

Provident and Pension Funds

Total resources of the 14 **provident and pension funds (PPF)** surveyed by Bank Negara Malaysia continued to grow in 1999, by 13.5% or RM23.5 billion (1998: +12.7%). As at end-1999, the total resources of the PPF amounted to RM197.1 billion, the bulk (85.5%) of which were the resources of the Employees Provident Fund (EPF). The significant growth in the resources of the PPF was largely due to the growth of accumulated contributions in contributors' accounts. Accumulated contributions grew by 12.2% or RM18.9 billion during the year (1998: +11.3%), reflecting mainly the higher net contributions and dividends credited during the year.

Net contributions to the PPF during 1999 was higher by 22.9%, amounting to RM9.8 billion. This reflected higher gross contributions of RM17.5 billion and lower withdrawals of RM7.7 billion. The increase in gross contributions was due to higher income levels of the contributors amidst strong economic performance and the increase in the number of contributors. The total number of contributors increased by 3.0% to 18.4 million persons at the end of 1999. Meanwhile, the lower withdrawals in 1999 reflected mainly the unusually large amount of withdrawals under the Age 55 Withdrawal Scheme in the previous year.

Another factor contributing to the higher accumulated contributions in 1999 was the higher amount of dividends credited to the accounts of contributors amounting to RM10.4 billion. This was attributed to the higher investment income during the year of RM12.1 billion.

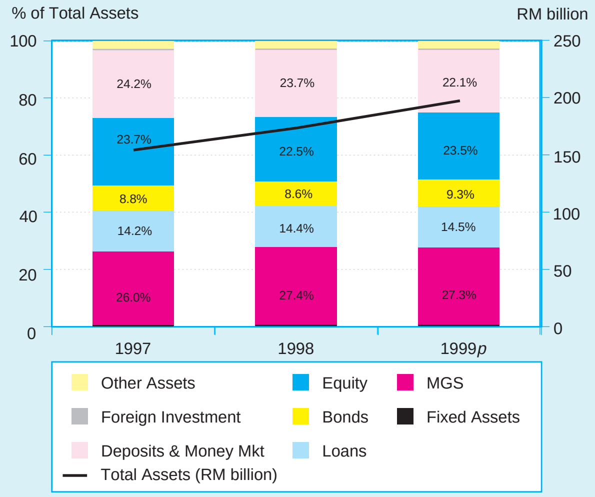
Table 4.20
Provident and Pension Funds: Selected Indicators

	1997	1998	1999p
	RM million		
As at end			Number of
Contributors ('000)	16,788	17,833	18,366
Of which: EPF	*8,275*	*9,158*	*9,532*
: SOCSO	*8,253*	*8,429*	*8,598*
Accumulated Contributions	139,246	155,034	173,944
Assets	154,082	173,597	197,096
Of which: Investments in MGS	*40,021*	*47,481*	*53,775*
During the year			
Gross Contributions	16,888	17,097	17,511
Withdrawals	6,378	9,104	7,683
Net Contributions	10,510	7,994	9,828
Dividends Credited	8,179	9,110	10,376
Investment Income	10,223	11,131	12,140

p Preliminary

Source: Employees Provident Fund, Pension Trust Fund, Social Security Organisation, Armed Forces Fund, Malaysian Estates Staff Provident Fund, Teachers Provident Fund and eight other private provident and pension funds.

Graph 4.14
Provident and Pension Funds: Assets



p Preliminary

In terms of the **composition of assets** of the PPF, there was some shift from the holdings of deposits and money market papers to corporate bonds and equities. The share of deposits and money market papers declined to 22.1% (1998: 23.7%) while the share of corporate bonds and equities increased to 9.3% and 23.5% respectively (1998: 8.6% and 22.5% respectively). The shift reflected the preference for higher return assets in an environment of robust economic growth. Meanwhile, the share of investments in Malaysian Government Securities and loans remained relatively unchanged at 27.3% and 14.5% respectively (1998: 27.4% and 14.4% respectively).

Several measures were announced in the Budget 2000 that affected the PPF industry. Firstly, it was proposed that income tax relief up to RM1,000 be given on annuity premiums for annuities purchased under the EPF annuity scheme. This was to support the EPF's effort to promote its annuity scheme. The EPF annuity scheme, which is expected to be launched in June 2000, will provide contributors with an option of receiving a monthly income upon retirement, instead of withdrawing their savings in a lump sum. Secondly, it was announced that civil servants who had been emplaced in the pension scheme would be allowed to withdraw the balance of their contributions with EPF before reaching the age of 55, while the Government's contribution would be transferred to the Pension Trust Fund. This measure was aimed at enhancing purchasing power as well as increasing demand and economic activity. Thirdly, a Children's Education Withdrawal Scheme was proposed to ease the burden of EPF contributors in educating their children. The scheme would allow contributors to withdraw a portion of their EPF contributions for the purpose of tertiary education of their children. In addition, it was announced that EPF contributors would be allowed to make withdrawals for the purchase of computers.

Pilgrims Fund Board

The activities of the Pilgrims Fund Board continued to expand in 1999, although like other financial institutions, it faced challenges, arising from the weak performance of the KLSE in the early part of 1999 and low returns from deposits placed with domestic banking institutions. Total resources mobilised by the Board amounted to RM8.6 billion at the end of 1999, representing an increase of RM1.3 billion or 17.3% (+RM1.2 billion or 18.9% in 1998). The increase in resources was due mainly to the expansion of its operations and the subsequent increase in the number of depositors by 8.9% to 3,748,208 at the end of 1999 compared with 3,440,971 in the previous year. At the same time, the number of Muslims registered with the Board to perform the pilgrimage was higher at 34,926 (29,404 in 1998).

Total depositors' balance, including bonuses credited, rose by RM1.2 billion or 18.1% (+RM1.1 billion or 18.5% in 1998) to RM8 billion, accounting for 93% of the total resources mobilised at the end of 1999 (92.4% at the end of 1998). During the year, new deposits placed with the Board was higher by 15.9%, at RM3.4 billion, while withdrawals rose by 16.2% to RM2.7 billion, resulting in a net increase of RM681 million in total deposits outstanding. The bonus rate remained at 8% per annum in 1999, while the value of bonuses credited to depositor's accounts was higher at RM539.8 million (1998: RM459.2 million).

As at end-1999, the bulk of the Board's funds were invested in corporate securities. Investments in corporate securities rose by RM384.4 million or 11% (+RM499.3 million or 16.8% in 1998) to RM3.9 billion, accounting for 45.1% of total assets in 1999. Of these investments, 73.5% was in quoted shares and 26.5% in unquoted shares. Investments in short-term instruments turned around to increase by RM443.7 million or 24.2% (–RM197 million or –9.7% in 1998) to RM2.3 billion at the end of 1999, accounting for a higher share of 26.6% of total assets. Despite the increase in investments in corporate securities, gross dividends received by the Board declined by 41% to RM147 million in 1999, reflective of lower dividend rates offered by the companies in which the Board had invested. During the year, income earned from other investments was slightly higher, amounting to RM471.1 million (RM466.6 million in 1998).

Industrial Finance Institutions

Total assets of the industrial finance institutions increased by RM2.5 billion or 16.7% in 1999 compared with RM4.5 billion or 43% in 1998. The stronger asset growth in 1998 was primarily due to the transfer of the Export Credit Refinancing Scheme from Bank Negara Malaysia to the Export-Import Bank of Malaysia Berhad in January 1998.

The growth in total assets in 1999 was mainly in the form of loans which accounted for 63.4% of the increase.

Table 4.21
Industrial Finance Institutions: Changes in Direction of Lending

Sector	Year					
	1997/96		1998/97		1999/98	
	RM million	%	RM million	%	RM million	%
Transport & storage	–25.96	–2.36	125.77	8.04	995.29	62.37
Real estate & construction	568.80	51.61	61.83	3.95	838.17	52.53
Mining & quarrying	7.73	0.70	3.82	0.24	9.69	0.61
Manufacturing	214.29	19.44	1,334.22	85.28	–0.77	–0.05
General commerce	19.00	1.72	29.06	1.86	–24.76	–1.55
Agriculture	22.75	2.06	–32.33	–2.07	–13.43	–0.84
Others	295.56	26.82	42.06	2.69	–208.47	–13.06
Total	**1,102.17**	**100.00**	**1,564.43**	**100.00**	**1,595.72**	**100.00**

The increase was funded mainly by capital funds and borrowings. Industrial finance institutions have traditionally relied heavily on capital funds and borrowings to fund their asset growth as they are not licensed to mobilise deposits from the public. Established primarily to promote development programmes in the agricultural, industrial and international trade and export sectors, these institutions are able to access low-cost resources from the Government and foreign institutions including the Japan Bank of International Cooperation (the merged entity of the Overseas Economic Cooperation Fund of Japan and the Japan Export-Import Bank) and the Islamic Development Bank, Jeddah.

Capital funds of the industrial finance institutions increased by 68.6% as at end-1999 to RM3.1 billion accounting for half of the total increase in liabilities in 1999. This was due mainly to the increase in capital funds of Bank Pembangunan dan Infrastruktur Malaysia Berhad from RM105.5 million to RM1 billion (+RM894.5 million) and Bank Industri Malaysia Berhad[1] from RM320.5 million to RM670.5 million (+RM350 million). Bank Pembangunan dan Infrastruktur Malaysia Berhad underwent capital restructuring at the end of 1998 in which 65% (RM488.6 million) of its total Government loans was converted into paid-up capital. Subsequently, in 1999, a bonus issue was declared based on the enlarged capital, increasing its paid-up capital to RM650 million. In addition, a cash injection of RM350 million by the Government had further increased its paid-up capital to RM1 billion as at end-1999. Similarly, Bank Industri Malaysia Berhad also converted its Government loans amounting to RM350 million into paid-up capital, raising the amount to RM670.5 million as at end-1999.

The other major source of funding of the industrial finance institutions in 1999 was borrowings which increased by 10.8% to account for 44.9% of the increase in total liabilities. Borrowings by these institutions included borrowings from related corporations (22.8%), the Government and Bank Negara Malaysia (40.2%) as well as foreign institutions such as the Japan Bank of International Cooperation and the Islamic Development Bank, Jeddah (24.6%). Borrowings from non-Government entities increased by 28% to RM8.8 billion in 1999, while borrowings from the Government fell by 22.5%. The decline in borrowing from Government was due to the partial conversion of the Government loans into share capital of the industrial finance institutions.

[1] Renamed "Bank Industri dan Teknologi Malaysia Berhad" as of 28 February 2000.

Loans extended by the industrial finance institutions increased by 20.8% (RM1.6 billion) in 1999. The increase was attributed solely to Bank Pembangunan dan Infrastruktur Malaysia Berhad's building up of infrastructure loan portfolio since October 1998 when it was entrusted to finance the nation's major infrastructure projects. Excluding Bank Pembangunan dan Infrastruktur Malaysia Berhad, loans extended by the industrial finance institutions declined by RM362.1 million in 1999.

In terms of distribution by economic sector, transport and storage accounted for the largest share (62.3%) of the increase in loans, compared with 8% in the previous year while the real estate and construction sector accounted for 52.5% of the increase in loans. In contrast, loans to the manufacturing sector declined by RM0.8 million in 1999. Despite the decline in loans to the manufacturing sector, the exposure of the industrial finance institutions to this sector remained high at 37%.

Overview of the Financial Markets

Developments in the financial markets were mixed in 1999. While trading volumes in the stock, bond and interest rate futures markets was higher, trading in the money, foreign exchange and stock index futures markets registered lower volumes.

Trading volume in the money market was lower by 24% in 1999, amounting to RM1.39 trillion. This reflected the lower trading volume in interbank deposits, which more than offset the higher trading in money market papers. The lower trading in interbank deposits was an outcome of the ample liquidity situation and the subdued loan growth, which led to the reduced reliance on the interbank market for funding needs. Meanwhile, trading volume in all money market papers was higher, except for bankers acceptances and negotiable instruments of deposits. This reflected the shift in investments from lower-yielding shorter-tenure papers to the higher-yielding longer-tenure papers. A notable amendment to the privileges given to the principal dealers (PDs) in 1999 was that PDs are now allowed to net off the actual holdings of excess specified securities from their eligible liabilities base.

In the interbank foreign exchange (forex) market, the average daily volume of interbank forex transactions was lower by 61.3% in 1999, amounting to RM1.4 billion. The sharp decline followed the imposition of the selective exchange controls along with the pegging of the ringgit exchange rate to the US dollar (US$) in September 1998. Following the controls, the offshore ringgit market, which previously contributed to the large volumes in the interbank forex market, was effectively eliminated. Trading activity in the ringgit was subsequently restricted to genuine trade-related transactions as well as for portfolio flows. This was evidenced by the shift in the composition of the major buyers of the US$ for the ringgit from offshore financial institutions to domestic enterprises. Activity continued to be dominated by transactions of the US$ against the ringgit, reflecting the importance of the US$ as a vehicle currency as well as the high US$ concentration of trade settlements and external debt.

Funds raised in the capital market were marginally lower in 1999 amounting to RM17.2 billion (1998: RM17.8 billion). This reflected the lower funds raised by the public sector, while funds raised by the private sector were higher. The amount raised by the public sector was lower because of the better-than-expected revenue collection and the availability of surplus funds from the preceding year. Meanwhile, the funds raised by the private sector were higher, following improved sentiment in the capital market as the economic recovery gained momentum. The higher funds raised by the private sector were driven mainly by the higher amount of funds raised through equity issues, which was more than three times the amount raised in 1998. Despite the marginally lower overall net funds raised, the capital market continued to be the main domestic source of financing for the economy in 1999.

In the equity market, sentiment on the Kuala Lumpur Stock Exchange (KLSE) was generally bullish in 1999, with the benchmark KLSE Composite Index (KLSE CI) rising by 38.6% to end the year at 812.33 points. Similarly, market capitalisation and trading volume was higher (47.6% and 46.1% respectively). The positive market sentiment was driven mainly by the strong economic performance and improved corporate earnings. The more favourable outlook on the Malaysian economy, as evidenced by a series of sovereign credit ratings upgrade and the impending reinstatement of Malaysia into the Morgan Stanley Capital International (MSCI) indices, further encouraged market confidence. The year also witnessed the commencement of trading operations on Malaysian Exchange of Securities Dealing and Automated Quotation (MESDAQ), Malaysia's exchange for growth and technology companies, with the listing of a technology hardware company.

The size of the ringgit bond market continued to expand in 1999 growing by 28.1% to RM201.5 billion. This was driven mainly by the higher issuance of private debt securities (PDS) for corporate debt restructuring schemes. As a result of the strong growth in PDS, the outstanding amount of PDS rose to a level that nearly matched that of Malaysian Government Securities. Trading activity for ringgit bonds was also sharply higher in 1999, amounting to RM155.9 billion or more than three times the amount traded in 1998. Consequently, the market's liquidity, as measured by the ratio of trading volume to amount outstanding, improved significantly, rising to 77.4% from 28.9% in 1998. These developments reflected the growing maturity of the domestic bond market which would augur well for the Government's aim of developing a deep and liquid ringgit bond market.

In the futures market, while trading in the KLSE CI Futures contracts declined significantly by 43%, the 3-month Kuala Lumpur Interbank Offered Rate (KLIBOR) futures contract was more actively traded. The decline in stock index futures trading was due mainly to the lack of foreign participation, while the higher trading in interest rate futures was attributed mainly to the improved liquidity situation in the underlying cash market and the revival of the market maker scheme.

As in previous years, efforts continued to be focused on developing the financial markets. Specifically, measures to improve corporate governance and minority shareholder protection were introduced, notably, the Finance Committee Report on Corporate Governance and the new Malaysian Code on Take-Overs and Mergers. Measures were taken to enhance transparency, such as the requirement for public limited companies (PLCs) to file financial statements on a quarterly basis. The year also marked the commencement of Phase 2 of a three-phase programme to move from merit-based regulation to disclosure-based regulation, with the amendments to the Guidelines on Issue/Offer of Securities.

A strategic initiative to develop a Capital Market Master Plan was also initiated in 1999, to chart the strategic positioning and future direction of the capital market for the next ten years. To provide the policy direction and to rationalise the regulatory framework for the development of the bond market, the National Bond Market Committee (NBMC) was established in June 1999. It was also announced that the Securities Commission (SC) would be the single

Table 4.22
Money Market*

	1998		1999	
	Volume (RM billion)	Annual change (%)	Volume (RM billion)	Annual change (%)
Total Money Market Transactions	**1,837.7**	**-1.2**	**1,412.6**	**-23.1**
Interbank Deposits	**1,650.7**	**-1.4**	**1,189.3**	**-28.0**
Money Market Papers	**187.0**	**0.0**	**223.3**	**19.4**
Bankers Acceptances (BAs)	79.3	–6.9	67.9	–14.4
Negotiable Instruments of Deposits (NIDs)	43.1	–23.6	27.2	–36.9
Malaysian Government Securities (MGS)	33.1	166.9	63.8	92.7
Khazanah Bonds	5.0	–	16.1	222.0
Treasury Bills	6.7	55.8	8.9	32.8
Bank Negara Bills	0.0	–	0.0	–
Cagamas Bonds	4.5	21.6	12.9	186.7
Cagamas Notes	15.3	21.4	26.5	73.2

* All data are sourced from money market brokers, except for MGS, Khazanah bonds and Cagamas papers which are sourced from Bond Information and Dissemination System (BIDS).

regulatory authority for the supervision and regulation of the corporate bond market to rationalise the regulatory framework.

Money Market

The volume of funds traded in the money market declined in 1999 by 23% to RM1,413 billion (see Table 4.22). Although, the volume of trade in money market papers increased by 19.4%, this was more than offset by the 28% decline in the volume of trade in interbank deposits. **Trading in interbank deposits** declined to RM1,189 billion in 1999 from RM1,651 billion in 1998, an outcome of the continued ample liquidity situation in the banking system which led to the reduced reliance on the interbank market for funding needs. The reduced recourse to the interbank market for funds was also a result of the subdued loan growth during the year. By tenure of deposits, the volume of trade declined across all tenures except for deposits of 2-month and 12-month maturities. As a significant proportion of the funds was placed at longer tenures, there was a dampening effect on the overall volume of transactions given that the pace of turnover of longer-term funds is slower thereby, leading to a lower volume of trade. In an environment of ample liquidity, a marked increase in the volume of trades in 12-month deposits reflected market perception that interest rates might have bottomed out. In 1999, the volume of trades in the 12-month tenure increased by RM550 million (36.7 times the volume in 1998).

Trading in money market instruments increased by 19.4% to RM223 billion in 1999 (RM187 billion in 1998) reflecting higher trading volumes in all papers except bankers acceptances (BAs) and negotiable instrument of deposits (NIDs). Lower trading volumes in the latter two instruments was due to the lower issuance of both papers. Total NIDs outstanding in 1999 fell by 51.2% to RM27.3 billion, while total BAs outstanding fell by 20% to RM14.8 billion. There was a notable increase in the trading volume of longer-tenured papers such as Malaysian Government Securities (MGS), Khazanah bonds, Cagamas bonds and notes. This was attributable to the shift in investments from the lower-yielding interbank money market deposits into the higher-yielding money market papers. In addition, the lower net issuance of bonds in 1999 as compared with the previous year also contributed to the increased demand for these instruments. The net issuance of MGS was only RM3.3 billion in 1999 (RM8.8 billion in 1998), while Cagamas bonds recorded a larger net redemption of RM2 billion (a net redemption of RM1.7 billion in 1998). There was only a marginally larger net nominal issuance of Khazanah bonds of RM4.1 billion in 1999 (RM3.9 billion in 1998).

A notable development in 1999 was the significantly higher trading volume in the **Islamic interbank money market** increasing from RM158 billion in 1998 to RM436 billion in 1999. Trading was higher for interbank deposits (+197%) which more than offset the reduction in the trading of Islamic papers (–14%). There was a marked increase in Skim Perbankan Islam (SPI) deposits, especially in the first half of the year, to take advantage of the higher rates offered by the Islamic deposits relative to the rates on conventional deposits. Although the relatively more favourable returns on Islamic fixed deposits declined in the second half-year, especially for 1-month deposits, which reversed its

Graph 4.15
Share of Total Volume Traded

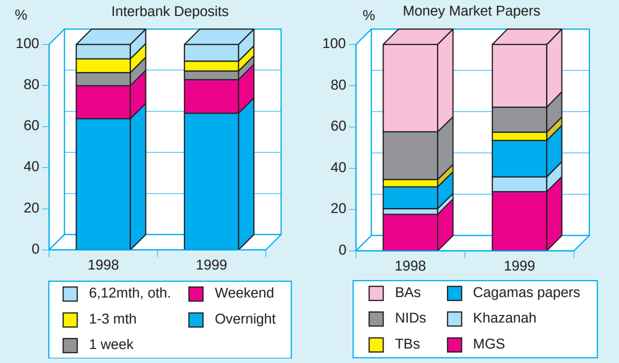


Table 4.23
Islamic Interbank Money Market*

	1998		1999	
	Volume (RM billion)	Annual change (%)	Volume (RM billion)	Annual change (%)
Total IIMM Transactions	**158.1**	**28.1**	**435.7**	**175.6**
Interbank Deposits	**142.0**	**36.9**	**421.9**	**197.1**
Islamic Papers	**16.1**	**-18.3**	**13.8**	**-14.3**
Green Bankers Acceptances (Green BAs)	9.7	–15.7	12.6	29.9
Islamic Acceptance Bills (IABs)	6.4	–22.0	1.2	–81.3

* Volume traded through money market brokers

trend, Islamic fixed deposits of other maturities continued to offer higher rates than conventional fixed deposits of similar maturities. Since the increase in deposits was required to be invested in other Islamic products, this resulted in a marked increase in the trading volume of Islamic interbank deposits. In addition, the increased trading volume of interbank deposits could also be attributed to the participation of discount houses in SPI. In 1999, discount houses were for the first time allowed to participate in the Islamic banking scheme. This is particularly significant as discount houses are active market makers specialising at the shorter-end of the money market. An analysis of the trading volume by maturity indicated that there was a significant increase of about 240% in the trading of overnight and weekend deposits. Meanwhile, trading in Islamic money market papers declined due to the large decline in the trading of Islamic Acceptance Bills (IABs), which was only partially offset by the increase in Green Bankers Acceptances (Green BAs). However, the overall decline in the trading of Islamic money market papers was in line with the decline in the total outstanding issues of all types of BAs.

As part of the annual review of principal dealers (PDs) system, 12 financial institutions (16 in 1999) have been appointed as principal dealers in the year 2000. One notable amendment was made to the privileges given to the PDs. Previously, for the purpose of calculation of their statutory reserve requirement, PDs were allowed to net off from their eligible liabilities (EL) base, 50% of their sales or purchases (whichever is lower) of specified instruments (MGS, Treasury Bills, Cagamas papers and Khazanah bonds) in the secondary market. With the recent amendment, PDs are now allowed to net off their actual holdings of excess specified securities from their EL base. In addition, as part of their new responsibility, each PD is now required to maintain a minimum market share of 2.5% of the total specified securities traded by the industry every month.

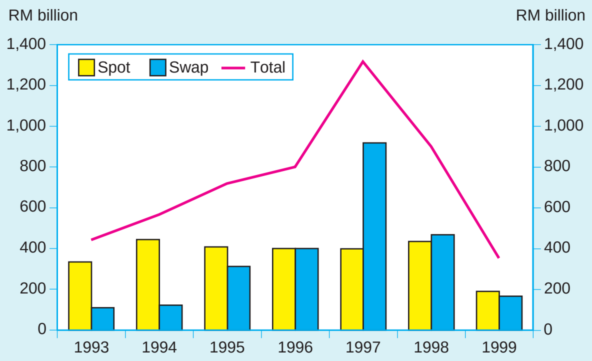
Foreign Exchange Market

The average daily volume of interbank foreign exchange transactions (spot and swap transactions) effected through the eight foreign exchange brokers in the Kuala Lumpur foreign exchange market declined by 61.3% during the year, from RM3.7 billion in 1998 to RM1.4 billion in 1999. The decline followed the imposition of the selective exchange controls and the pegging of the exchange rate to the United States dollar in September 1998.

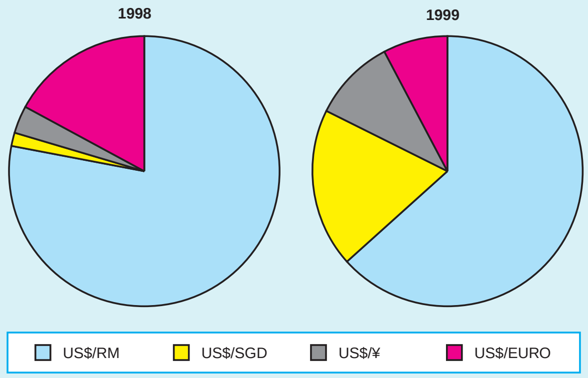
Following the controls, the offshore ringgit market, which previously contributed to the large volumes in the interbank foreign exchange market, had effectively been eliminated. The trading activity in the ringgit was essentially restricted to trade-related transactions as well as for portfolio flows. The larger volumes of trading in 1997 and 1998 were largely due to the significant growth of the swap market and the larger volume of big transactions, both of which reflected the speculative activity.

Activity in the foreign exchange market in 1999 continued to be dominated by transactions of the United States dollar against the ringgit, although its share of total transactions declined to 63.2% from 77.9% in 1998. The continued dominance of US$/RM trades reflected the significance of the US$ as a vehicle currency in the interbank foreign

Graph 4.16
Volume of Interbank Transactions in the Kuala Lumpur Foreign Exchange Market



Graph 4.17
Interbank Transactions in the Kuala Lumpur Foreign Exchange Market by Currency



exchange market as well as the high concentration of trade settlement and external debt in United States dollar. Most notably, trades involving the United States dollar against the Singapore dollar increased by about 3.6 times to account for 19% of the total volume of transactions.

With the introduction of the exchange controls, there has been a shift in the composition of the major buyers of the United States dollar for the ringgit, both in the spot and swap markets. In the past two years, offshore financial institutions dominated the US$/RM market. However, in 1999, the major buyers were domestic enterprises. Swap transactions accounted for 46.6% of total transactions in 1999 (1998: 51.8% and 1997: 69.7%). The lower volume of swap transactions in 1998 and 1999 compared to 1997 was primarily due to the August 1997 restrictions on non-trade related swaps.

Funds Raised in the Capital Market

Funds raised in the capital market were marginally lower in 1999 amounting to RM17.2 billion compared with RM17.8 billion in 1998. This reflected the lower funds raised by the public sector, as funds raised by the private sector were higher in 1999 compared with 1998. The amount of net funds raised by the **public sector** in 1999 was lower at RM6.3 billion, due to the better-than-expected outturn in revenue collection and the availability of surplus funds from the preceding year, when the public sector had raised gross funds of RM9.8 billion. Meanwhile, the net funds raised by the **private sector** was higher at RM10.9 billion (1998: RM8 billion), following improved sentiment in the capital market as the economic recovery gained momentum. Despite the lower overall net funds raised, the capital market continued to be the main domestic source of financing for the economy in 1999. The ratio of net funds raised in the capital market to the net loans extended by the banking system (excluding loans sold to Cagamas but including loans sold to Danaharta) rose from 3.18 in 1998 to 4.72 in 1999.

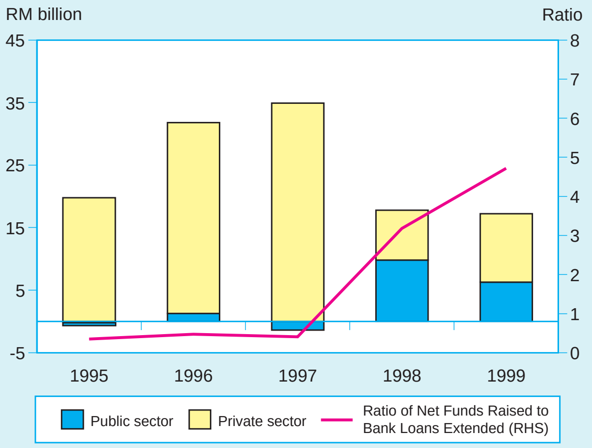
The lower net funds raised by the **public sector** (RM6.3 billion) was primarily due to the smaller issuance of Malaysian Government Securities (MGS). There were five new issues of MGS in 1999 totalling RM10 billion (compared with six issues totalling RM15 billion in 1998). Nevertheless, MGS continued to account for the bulk (67%) of the gross funds raised by the public sector during 1999. In addition to MGS, the Government also issued a single Government Investment Issue (GII) of RM2 billion to replace the last remaining GII issue in the market upon its maturity. There were also four new issues of zero-coupon Government-guaranteed Khazanah Murabahah bonds in 1999, which raised funds totalling RM2.6 billion (1998: RM2.7 billion). The issuance of these Khazanah bonds was a continuation of Khazanah Nasional Berhad's programme of providing a benchmark yield curve for the ringgit bond market since 1997. The year also saw the raising of RM377 million through the

Table 4.24
Funds Raised in the Capital Market

	1998	1999*p*
	RM million	
By Public Sector		
Government Securities, gross	14,950	10,000
Less Redemptions	6,200	6,676
Equals Net Federal Receipts	8,750	3,324
Khazanah Bonds	2,732	2,598
Govt. Investment Issues (net)	–750	0
Malaysia Savings Bond (net)	–928	375
Net Funds Raised by the Public Sector	9,804	6,297
By Private Sector		
Shares/Warrants	1,788	6,087
Private Debt Securities[1], gross	14,152	17,553
Less Redemptions	7,977	12,750
Equals Net Issues	6,175	4,804
Net Funds Raised by the Private Sector	7,963	10,891
Net Funds Raised in the Capital Market	17,767	17,188
Net Issues of Short-term Securities[2]	185	–607
Total	17,951	16,581

[1] Excludes debt securities issued by banking institutions.
[2] Refers to Commercial Papers and Cagamas Notes only.
p Preliminary

Graph 4.18
Total Net Funds Raised in the Capital Market By the Public and Private Sectors



issuance of the 2-year Malaysia Savings Bonds Series 2, which was aimed at ameliorating the adverse impact of the low interest rate environment on the income earned by retirees on their deposits with financial institutions.

In the case of the **private sector**, the higher net funds of RM10.9 billion raised by the private sector was driven mainly by the higher amount of funds raised through equity issues, which at RM6.1 billion, was more than three times the amount raised in 1998 (RM1.8 billion). The equity issues more than offset the lower amount of private debt securities (PDS) issued (RM4.8 billion; 1998: RM6.2 billion), emerging as the main mobiliser of funds for the private sector in the capital market in 1999. The share of funds raised by the private sector through the issuance of equity securities increased from 22.5% in 1998 to 55.9% in 1999.

In the **equity market**, the bulk of the RM6.1 billion raised was through rights issues (RM4.3 billion), which were significantly higher than the amount of RM0.7 billion raised in 1998. Of the total rights issues, RM2.4 billion, or more than half, was raised by a single firm for the purpose of financing acquisitions. Other forms of equity issuance, namely initial public offers (IPOs), special issues and private placements, also recorded higher amounts. Of significance, no IPO was undersubscribed in 1999 compared with a 56.8% undersubscription in 1998.

In the **PDS market**, the net funds raised of RM4.8 billion was marginally lower despite a higher value of new PDS issues of RM17.6 billion (1998: RM14.2 billion). This was due to the much larger amount of redemptions, which was at a record level of RM12.7 billion in 1999 (1998: RM8 billion). The significantly higher PDS redemptions in 1999 was due partly to the maturity of PDS issued in 1994 and 1996. Specifically, the bulk (57%) of the PDS which matured in 1999 were 5-year corporate bonds issued in 1994 (RM4.3 billion or 78% of corporate bonds issued in 1994) and 3-year Cagamas bonds issued in 1996 (RM3 billion or 63% of Cagamas bonds issued in 1996). In addition to the large scheduled redemptions, the PDS redemptions were also due to 11 early redemptions in 1999 by seven PDS issuers, totalling RM2.4 billion (1998: five early redemptions totalling RM805 million). Straight bonds accounted for 54.5% of the RM17.6 billion gross funds raised (1998: 72.3%), asset-backed Cagamas bonds, 25.2% (1998: 23.5%), Islamic bonds, 9.9% (1998: 2.4%), convertible bonds, 7.2% (1998: 0.7%), and bonds with warrants, 3.2% (1998: 1.1%).

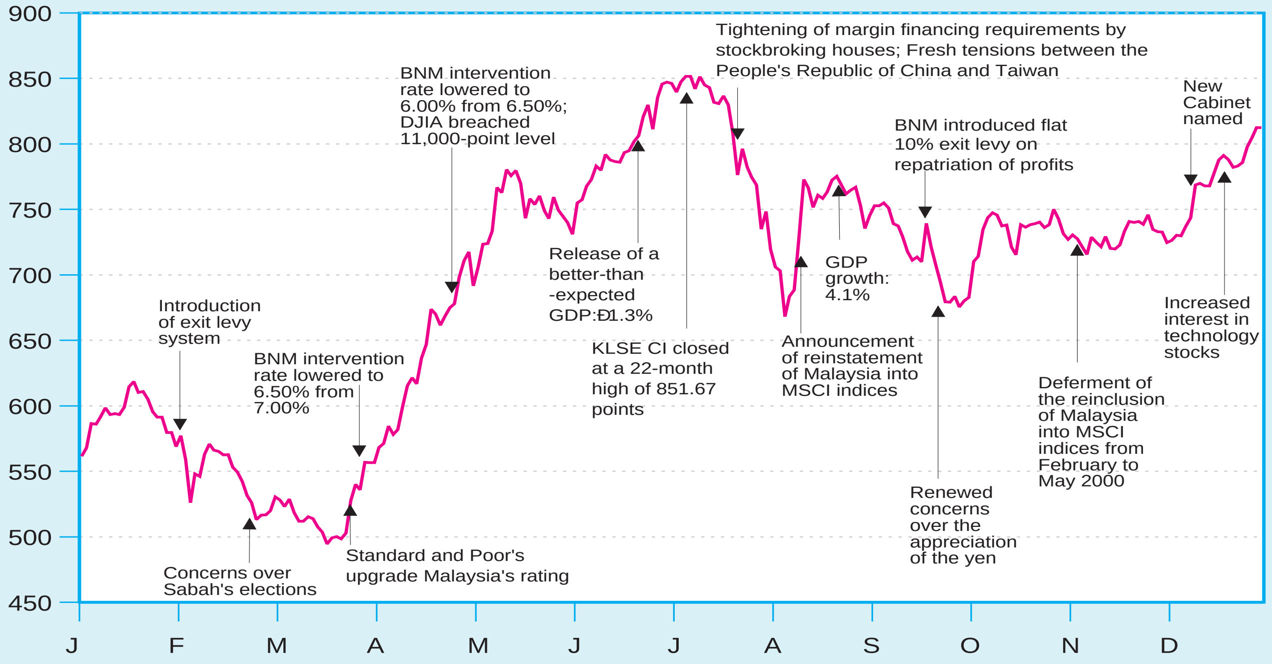
The larger amount of PDS issued and the early PDS redemptions in 1999 were attributed partly to corporate debt restructuring. Indeed, the largest PDS issue in 1999 (accounting for 39.7% of the gross funds raised from PDS issues) was for a debt restructuring scheme. As for Cagamas bonds, there was a net redemption of RM2 billion (1998: –RM1.7 billion), reflecting the larger amount of redemption of RM6.5 billion during the year, compared with RM4.4 billion in new funds raised. In terms of utilisation, 41.7% of the gross PDS funds raised was channelled to the transport, storage and communications sector, while

Table 4.25
New Issues of Private Debt Securities by Sector (RM million)

	1998	1999*p*
Agriculture, hunting, forestry & fishing	0.0	0.0
Mining & quarrying	0.0	0.0
Manufacturing	125.0	524.5
Electricity, gas & water supply	529.0	523.8
Wholesale & retail trade, restaurants & hotels	0.0	170.0
Construction	0.0	1,729.0
Purchase of residential property	1,000.0	0.0
Purchase of non-residential property	0.0	0.0
Real estate	370.0	875.8
Transport, storage & communication	1,103.3	7,316.9
Financing, insurance & business services	11,024.5	5,169.6
Purchase of securities	0.0	1,238.4
Others	0.0	5.0
Total	**14,151.8**	**17,553.0**

p Preliminary

Graph 4.19
Performance of the KLSE CI in 1999



29.5% was channelled to the finance, insurance and business services sector.

Equity Market

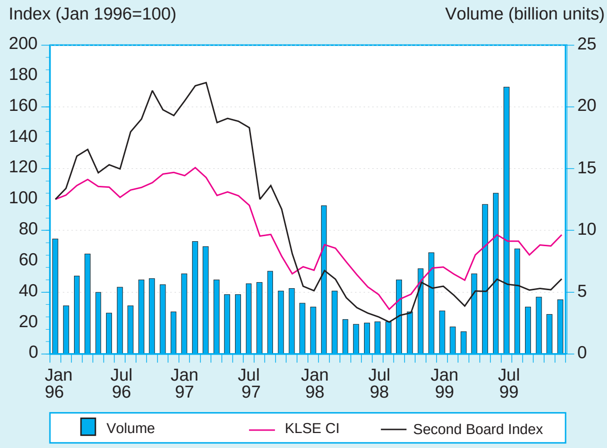
Market sentiment on the Kuala Lumpur Stock Exchange (KLSE) was generally bullish in 1999, with the benchmark **KLSE Composite Index (KLSE CI)** ending the year higher at 812.33 points. This was an increase of 38.6% from a year ago. Similarly, market capitalisation increased by 47.6% to reach RM553 billion. The positive market sentiment was driven by the strong economic performance, improved corporate earnings, considerable progress in bank restructuring and the low interest rate environment. The mix of policies and measures introduced by the Government and the KLSE provided a conducive environment for businesses and investments. Market confidence was further encouraged by the more favourable outlook on the Malaysian economy, as evidenced by a series of upgrading of Malaysia's sovereign ratings by a number of international credit rating agencies, the possible reinstatement of Malaysia into the Morgan Stanley Capital International (MSCI) indices, as well as the economic and stock market recovery in the region.

Consistent with the performance of the KLSE CI, all other KLSE indices, except the Mining and Plantation indices, closed the year higher. The Finance index was the top performer, rising by 75.7%. The rise in the Finance index reflected investors' positive response to the significant progress in bank restructuring. In contrast, the Plantation and Mining indices declined by 8.4% and 4.5% respectively. The former was due mainly to the decline in crude palm oil prices (–29.6%) while the latter was in line with the negative growth of the mining industry (–4%). The Second Board index also underperformed the KLSE CI, rising by 14%. This reflected investors' interest in larger capitalised companies.

The KLSE CI in 1999 was on an uptrend for the most part of the year, interspersed by brief periods of decline. It went through four discernible phases. The KLSE CI began the year with a short period on the rise before pressures emerged in the last week of January to dampen the uptrend, and this continued into the end of March. It reached the lowest point of the year (494.57 points) on 24 March. Sentiment turned around in April, with the KLSE CI rising steadily for more than three months to reach a peak of 851.67 points on 9 July. The rising momentum was halted by a brief period of decline from mid-July to early-August, when the KLSE CI fell to 668.21 points. The KLSE CI subsequently recovered, turning bullish again to close the year at 812.33 points.

The KLSE CI started off the year on a positive note on news of a trade surplus for November 1998 and the exchange control relaxation which allowed the repatriation of profits arising from contra transactions. The price increases was shortlived, however, as market sentiment began to weaken by the end of January, and deteriorated further until the end of March. Following the announcement on 4 February 1999, on the introduction of the levy on the early repatriation of capital (previously repatriation of capital within the 12-month holding period was not allowed), the market fell as stocks were sold based on the misperception that only profits repatriated before 15 February would be exempted from levy. Further clarification on the exit levy, however, produced an almost immediate recovery. Nevertheless, the subsequent announcement of a further decline in the Industrial Production Index (IPI) and the concerns over the Sabah elections dampened market sentiment.

Graph 4.20
Kuala Lumpur Stock Exchange Composite Index, Second Board Index and KLSE Trading Volume



Source: Kuala Lumpur Stock Exchange

Table 4.26
Kuala Lumpur Stock Exchange: Selected Indicators

	1998	1999*p*
Price Indices		
Composite	586.13	812.33
EMAS	146.94	206.39
Second Board	158.37	180.57
Total Turnover		
Volume (billion units)	58.3	85.2
Value (RM billion)	115.2	185.3
Average Daily Turnover		
Volume (million units)	236.9	343.4
Value (RM million)	468.2	747.0
Market Capitalisation (RM billion)	374.5	552.7
Market Capitalisation/GDP (%)	131.7	184.4
Total No. of Companies Listed	736	757
Main Board	454	474
Second Board	282	283
Market Liquidity:		
Turnover Value/Average Market Capitalisation (%)	34.6	40.3
Turnover Volume/Number of Listed Securities (%)	37.1	49.4
Market Concentration:		
10 Most Highly Capitalised Stocks/ Market Capitalisation (%)	35.5	33.9
Average Paid-Up Capital of Stockbroking Firms (RM million)	91.9	103.2

p Preliminary

Source: Kuala Lumpur Stock Exchange

The KLSE CI rebounded strongly from April to mid-July against a backdrop of improving prospects for economic recovery. The Index rose continuously for three months from April to June by 34.2%, 10.1% and 9.2% respectively. The rise was due partly to the improved views on Malaysia, expressed by a number of major international credit rating agencies and security houses. In addition, market sentiment was also aided by the reduction in the BNM 3-month intervention rate, positive growth in the IPI (3.1% in February; the first upturn in 12 months), the moderation in the CPI (from 3.8% in February to 3% in March) and the smaller-than-expected GDP contraction for the first quarter 1999 (–1.3%). On the external front, the rise of the Dow Jones Industrial Average (DJIA) index, which breached the 11,000-point level on 4 May also helped to boost regional markets, including the KLSE.

The strong rally was interrupted in mid-July, as selling interest prevailed and pushed prices lower. Selling by foreign funds became more prominent as they locked in profits. The falling prices resulted in recurring margin calls by stockbrokers and financial institutions and prompted forced selling, thus reinforcing the sell down. Sentiment was also affected by concerns over the rise in US interest rates, tensions between The People's Republic of China and Taiwan and the strengthening of the Japanese yen.

The sharp decline of the KLSE CI reversed on 9 August amidst several positive developments. These included the MSCI's announcement that Malaysia would

Key Capital Market Measures in 1999

Capital market measures introduced in 1999 were aimed mainly at promoting a more efficient, transparent, innovative and competitive capital market that has the highest standards of integrity and systemic stability. The key measures were as follows:

Improving Corporate Governance and Minority Shareholder Protection

- The new Malaysian **Code on Take-Overs and Mergers** 1998 came into force on **1 January** to enhance transparency and to protect minority interests. The new Code contained, among others, provisions to ensure that minority shareholders were given relevant information necessary to make an informed decision and provisions imposing criminal liability on parties that provide false or misleading information.

- The Finance Committee **Report on Corporate Governance** was released on **25 March**. The Report contained 70 principal recommendations to enhance corporate governance standards and covered three broad areas, namely, the development of the Malaysian Code on Corporate Governance, reform of laws, regulations and rules, and training and education. An Implementation Project Team had been established and entrusted with the task to lead and oversee the implementation of the recommendations in the Report.

- Effective **1 April**, **restrictions** were placed **on the number of directorships** that may be held by directors of public listed companies (PLCs) to address the corporate governance issues arising from multiple directorships, e.g. insufficient time and effort devoted to the boards they represent. The restrictions stipulated that a director of a PLC should not hold more than 25 directorships in companies, of which the number of directorships held in PLCs should not be more than 10.

Enhancing Transparency

- Effective **18 June**, listed companies were required to present their financial statements in accordance with **accounting standards** issued by the Malaysian Accounting Standards Board (MASB). This was to enhance the quality of information disclosed in financial statements and to ensure that accounting standards issued by MASB were complied with.

- With effect from **31 July**, PLCs were required to **file financial statements** with the KLSE **on a quarterly basis**. The aim was to strengthen corporate accountability and disclosure as well as to aid investors in making informed investment decisions.

Strengthening the Stockbroking Industry

- Effective **28 May**, the **Capital Adequacy Requirements** (CAR) were introduced to ensure that the liquid capital of a stockbroking company (SBC) would be sufficient to cover its total measured risks. CAR is a risk-based financial monitoring tool with separately identifiable measures for the specific risks associated with a SBC's business.

- The KLSE issued standards for the **treatment of interest on non-performing accounts** and **provision for bad and doubtful debts** in the financial statements of SBCs, effective **1 July**. The objective was to ensure consistency in the recognition of interest income and the provision for bad and doubtful debts.

- The KLSE introduced **new Memorandum & Articles (M&A) and Rules**, with effect from **1 July**. The new M&A and Rules incorporated enhanced measures to strengthen the stockbroking industry and to achieve greater clarity and transparency in the business conduct of SBCs.

Strengthening the Financial Position of PLCs

- On **30 April**, the Securities Commission (SC) announced that **revisions** were made to the **requirements for KLSE Main and Second Board listings, reverse take-overs and back-door listings** to strengthen the financial position of PLCs. These revisions included more stringent profit track records, higher minimum issued and paid-up capital for companies seeking listing on the KLSE, a standard requirement for a moratorium on the disposal of shares by the promoters of all Second Board applicants and Main Board applicants involved in certain activities, as well as additional criteria for the listing of property development, construction and trading/retailing companies.

Facilitating Capital Raising

- On **30 April**, listed companies were allowed to issue and list **new equity warrants** with attractive exercise prices to replace existing equity warrants. This was to ease the capital raising problems of listed companies by enabling them to have access to more flexible avenues for capital raising.

Facilitating the Move Towards Disclosure-Based Regulation (DBR)

- On **30 December**, the SC announced that the "Policies and Guidelines on Issue/Offer of Securities" (Issues Guidelines) were amended to further facilitate the progressive move towards **DBR**[1]. It marked the commencement of Phase 2 of a three-phase implementation programme to move from merit-based regulation[2] to regulation based on disclosure. The focus of the revisions was generally on the liberalisation of the requirements on pricing of securities, valuation of assets and utilisation of proceeds.

Encouraging the Consolidation of Stockbroking Companies

- In the 2000 Budget proposals, **tax incentives** were granted to encourage the consolidation of SBCs. These were as follows:

  – SBCs engaged in merger exercises would be given stamp duty and real property gains tax exemptions on all instruments related to mergers completed between 30 October 1999 to 31 December 2000.

  – The acquiring SBCs would also be given tax credits (calculated as a sum equivalent to half of the losses suffered by the acquired entity multiplied by the income tax rate). The tax credit could only be claimed against tax payable for two years of assessment immediately following the year in which the merger was completed.

Enhancing Infrastructure and Other Measures

- The Institutional Settlement Service (ISS) was launched on 15 July to facilitate the settlement of trades of investors directly with the clearing house. The ISS allows resident custodian banks and institutional investors to participate directly in the clearing and settlement process.

- The integrated electronic system for share applications was inaugurated on 26 August for an initial public offering. The system marked the beginning of an easier share application process since it reduced the need for form-filling and queuing as it provided investors with the option to use automated teller machines.

- The KLSE Link, which is an internet-based electronic document management system, was launched on 8 October to enhance the content, consistency and timeliness of corporate announcements;

- The KLSE Syariah Index was launched on 17 April to cater to investors seeking to invest in instruments which were in line with Syariah principles;

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[1] Under DBR, the SC regulates the quality of information disclosed in offerings of securities and investors determine the investment merits of the offerings.

[2] Under merit-based regulation, the investment merits of offerings of securities are assessed and determined by the SC.

- KLSE strengthened its suspension policy in order to ensure continuous trading and proper functioning of the stock market. Effective 14 June, PLCs were no longer allowed to suspend trading by merely submitting requests without detailed justification and, the periods of suspension generally should not be longer than three market days.

- The regulation of depository receipts was put in place on 3 May to enhance foreign interest in Malaysian shares. Following that, sponsored American Depository Receipts (ADR)/Global Depository Receipts (GDR) programmes were allowed to continue to operate for Malaysian listed companies.

Further Developing the Capital Market

- A **Capital Market Master Plan** would be developed to chart the strategic positioning and future direction of the Malaysian capital market for the next 10 years. Among others, it would address the weaknesses in the capital market highlighted during the crisis, provide a strategic road map to facilitate future business development and assist in the creation of a resilient and competitive capital market.

- The **National Bond Market Committee (NBMC)** was established to provide the policy direction and to rationalise the regulatory framework for the development of the bond market as well as to recommend appropriate implementation strategies to address impediments to the development of the bond market. Chaired by the Secretary-General of Treasury, the NBMC included representatives from BNM, SC, Economic Planning Unit (EPU), Registrar of Companies (ROC) and KLSE. Three working groups were established, namely, the Legal and Regulatory Reform Committee, the Product and Institutional Development Committee and the Infrastructure and Operations Working Group. It was also announced that the SC would be the **single regulatory authority** for the supervision and regulation of the corporate bond market to rationalise the regulatory framework.

- To enhance the development of the bond market, it was proposed in the 2000 Budget that the transfer of assets for the purpose of **asset securitisation** would be **exempted from stamp duty and real property gains tax**, effective 30 October 1999 until 31 December 2000.

- In the 2000 Budget proposals, **unit trusts** sponsored by the Federal and State Governments were given income **tax exemptions** for 2000 and 2001 in order to assist the Government sponsored unit trusts to play a bigger role in mobilising savings and to enhance the stability of the stock market.

be reinstated into its MSCI indices in February 2000. The KLSE CI recovered by 15.7% in four days. This development was shortlived, however, as profit-taking and the non-committal attitude of investors ahead of 1 September led the KLSE CI to trend lower. Sentiment, nevertheless, recovered somewhat, following the announcements by BNM of the small amount of portfolio outflows (US$456 million for the period 1-3 September), allaying the earlier fears of a large outflow of portfolio funds from 1 September. The introduction of the flat 10% levy system by BNM on 21 September was also well received by investors. Sentiment, however, remained weak due to the strengthening of the Japanese yen and the re-emergence of fears over the possibility of an interest rate hike in the US.

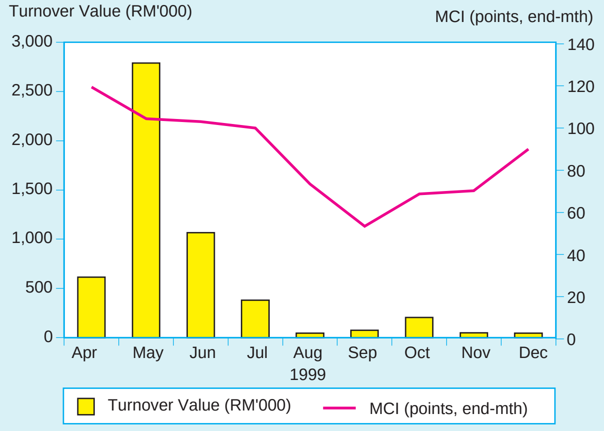
Sentiment began to improve from October, influenced mainly by expectations of a pro-growth Budget. The decision to delay the reinstatement of Malaysia into the MSCI indices from February to May 2000 did, however, dampen sentiment temporarily. Following the favourable response to the new Cabinet line up and the rising interest in technology stocks, sentiment turned bullish in December, with the KLSE CI rising by 10.6%.

In comparison with the performance of the other stock markets in the region, the increase in the KLSE CI (38.6%) was lower than the Korea Composite Index (82.8%), Singapore ST Index (74.8%) and Jakarta Official Index (70.1%), but was higher than the Thailand SET Index (35.4%). In terms of ranking, the KLSE ranked eighth in the Asia-Pacific region and second in ASEAN.

Reflecting the overall positive market sentiment, trading volume on the KLSE was 46.1% higher in

1999, amounting to 85.2 billion units or an average daily volume of 343 million units (1998: 58.3 billion units and 237 million units respectively). In terms of transacted value, the turnover was 60.8% higher at RM185.3 billion (1998: RM115.2 billion). The bulk of the trading (62.4%) was in April to July when market sentiment was most bullish. Trading remained centred on the trading/services (24.4% of total trade) and finance (12.9%) sectors on the Main Board. Of significance was the higher trading volume in the Loans/TSR sector (17.1% of total trade; 1998: 10.8%). This was attributed partly to the decision by the SC to allow the issuance and listing of new warrants to replace the existing warrants. Market liquidity (measured by the ratio of units traded to the number of units of securities listed) increased to 49.4% in 1999 from 37.1% in 1998. Similarly, the ratio of trading value to average market capitalisation rose to 40.3% in 1999 (1998: 34.6%).

Graph 4.22
Malaysian Exchange of Securities Dealing and Automated Quotation: Trading and MESDAQ Composite Index (MCI)

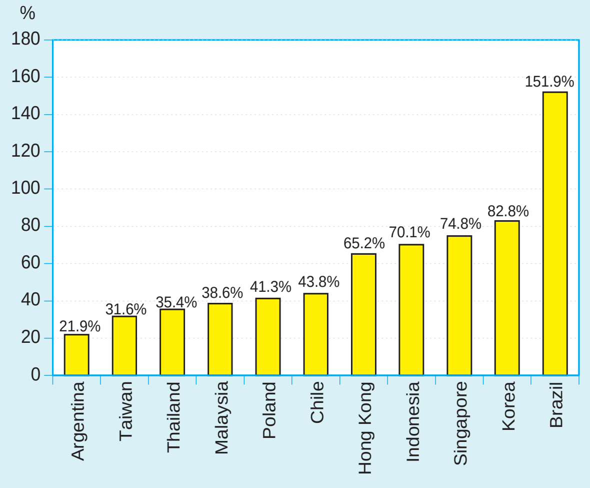


Source: Malaysian Exchange of Securities Dealing and Automated Quotation

Several **measures** were introduced during the year, to further develop the capital market. The key measures are contained in the box, *Key Capital Market Measures in 1999*.

The year 1999 was an important year for **MESDAQ**, Malaysia's exchange for growth and technology companies. The highlight of the year was the commencement of trading operations on 30 April 1999 with the listing of a technology hardware company on the exchange. The MESDAQ Composite Index (MCI) declined initially and rebounded in the last quarter of 1999, broadly in line with the KLSE CI, to close at 89.94 points at end-1999. Trading volume on MESDAQ amounted to RM5.3 million, with the bulk of the trading (53%) concentrated in May. In addition to the single listing, two companies applied for listing in 1999, one of which was involved in smart-card technology while the other was a pharmaceutical company.

Graph 4.21
Performance of Selected Regional & Emerging Stock Market Indices (% change from 1998 to 1999)



Source: International Federation of Stock Exchanges (FIBV)

During the year, MESDAQ also introduced Malaysia's first electronic prospectus and launched the Malaysian Enterprise Network (MEnet). The electronic prospectus was introduced with the first listing on 30 April, and was intended to reduce the cost of IPOs and at the same time extend the reach of prospectuses by leveraging on internet technology. As it turned out, the prospectus for the maiden listing at MESDAQ attracted 64,000 on-line hits with approximately 2,000 copies downloaded. Another development in financial information dissemination during the year was the launch of the MEnet on 16 April. The MEnet is an internet-based bulletin board sponsored by MESDAQ, where Malaysian private limited companies could efficiently and cost-effectively profile themselves to potential investors. As at end-1999, 20 companies and 16 investors had registered with MEnet.

As at end-1999, MESDAQ had 13 stockbroking companies as members, the same number as when trading commenced on 30 April. Seven of these stockbroking companies were market-makers. An open trading system is expected to be implemented by end-2000 to replace the existing trading system, the MESDAQ Quotation

Table 4.27
Outstanding Amount of Ringgit Bonds

	1998		1999p		Change (RM mil)
	RM mil	% Share	RM mil	% Share	
Malaysian Government Securities	75,012	47.7	78,336	38.9	3,324
Government Investment Issues	2,000	1.3	2,000	1.0	–
Khazanah Bonds	4,850	3.1	8,980	4.5	4,130
Malaysia Savings Bonds	4	0.0	379	0.2	375
Danaharta Bonds	2,601	1.7	10,344	5.1	7,743
Danamodal Bonds	11,000	7.0	11,000	5.5	–
Cagamas Bonds	15,064	9.6	13,019	6.5	–2,045
Other Private Debt Securities	46,737	29.7	77,413	38.4	30,676
Total	157,268	100.0	201,470	100.0	44,202

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System (MQS). The move, from the current proprietary platform and network to an open trading architecture which utilises internet-based technologies and standards, would increase the trading system's flexibility and would allow MESDAQ to respond rapidly to the impending borderless marketplace that is being opened up by electronic commerce and the increasing connectivity of issuers and investors worldwide. Meanwhile, as in past years, various roadshows and presentations were also organised for potential issuers, the investment community, the media and the general public, in an effort to market MESDAQ as well as the MEnet.

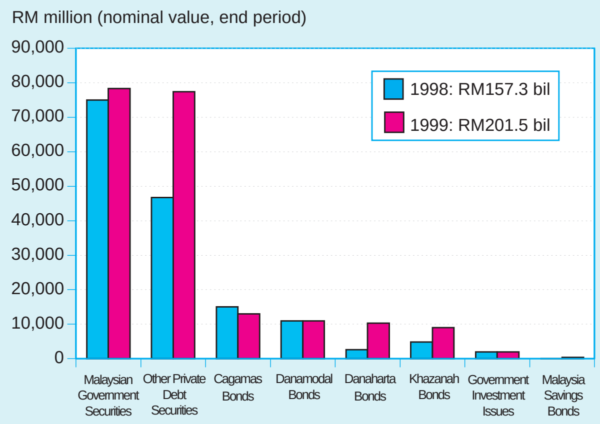
Bond Market

The **size** of the ringgit bond market, comprising public debt securities[2] and private debt securities[3] (PDS), increased by 28.1% during the year, from RM157.3 billion at the end of 1998 to RM201.5 billion at the end of 1999. The growth was driven mainly by the higher issuance of PDS for corporate debt restructuring and the purchase of non-performing loans.

The increase in the size of the bond market reflected mainly the rise in the outstanding amount of other PDS[4] (+RM30.7 billion or 65.6%) and bonds issued by the national asset management company, Pengurusan Danaharta Nasional Berhad (+RM7.7 billion or 298%). Malaysian Government Securities (MGS) continued to account for the largest portion of the total bonds outstanding, although its share fell significantly to 38.9% from 47.7% in the previous year. Most notably, the share of other PDS had risen to a level (38.4%) that nearly matched that of MGS, reflecting the considerable expansion of other PDS in 1999. This development is a positive step towards achieving the Government's aim of developing a deep and liquid PDS market.

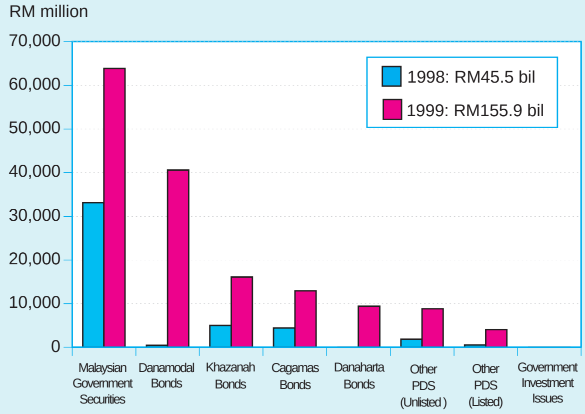
Trading activity in the secondary market for ringgit bonds was sharply higher in 1999. Trading volume amounted to RM155.9 billion, more than three times the amount traded in 1998 (RM45.5 billion). Similarly, the bond market's liquidity, as measured by the ratio of trading volume to amount outstanding, had also

Graph 4.23
Size of the Ringgit Bond Market: Amount Outstanding



[2] Public debt securities refers to Malaysian Government Securities, Government Investment Issues, Khazanah bonds and Malaysia Savings Bonds.
[3] Private debt securities refers to Cagamas bonds, Danamodal bonds, Danaharta bonds and other PDS.
[4] Listed and unlisted private bonds other than those issued by Cagamas, Danaharta and Danamodal.

Graph 4.24
Trading of Ringgit Bonds



Source: Bond Information and Dissemination System

improved significantly, rising from 28.9% in 1998 to 77.4% in 1999. This development reflects the growing maturity of the domestic bond market and augurs well for the development of a deep and liquid bond market. The ample liquidity situation in the banking system, the decline in interest rates, the improved credit risk profiles of corporate bonds, the higher yields offered relative to short-term interbank money market deposits and the recovery in economic activity, were among the contributory factors to the higher trading activity.

As in previous years, trading was focused on the over-the-counter segment of the bond market (97.4%), particularly MGS. Trading of MGS was higher at RM63.8 billion (1998: RM33.1 billion) and continued to account for the largest share of total trading volume. Nevertheless, its share of total transactions at 41% was significantly lower than the 72.8% recorded in 1998. This decline in the share of MGS, reflected the significantly higher trading of the bonds issued by the special purpose vehicle established to recapitalise banking institutions, Danamodal Nasional Berhad (Danamodal). The trading volume of Danamodal bonds amounted to RM40.6 billion in 1999 compared with RM476 million traded in the last three months of 1998[5]. As a result, its share of total trading volume rose from a mere 1% in 1998 to 26.1% in 1999, making it the second most actively traded bond after MGS, taking the place of Khazanah bonds. Danamodal bonds were also the most liquid instrument in the bond market in 1999 (liquidity ratio: 369.4%).

[5] Danamodal bonds were issued on 21 October 1998.

The number of **ratings** of new issues (including short-term debt securities) conducted by the two domestic rating agencies, Rating Agency Malaysia Berhad (RAM) and Malaysia Rating Corporation Berhad (MARC), was significantly higher in 1999. During the year, RAM completed 46 rating exercises valued at RM35.2 billion (1998: six exercises totalling RM934 million). Of these, 42 were long-term issues while four were short-term. Similarly for MARC, new issue ratings numbered 22 compared with seven issues in the preceding year, while the total value of debt rated was RM8.3 billion (RM2.5 billion in 1998). Thirteen of the ratings were long-term issues and nine were short-term issues.

Several measures were introduced during the year, to further develop the ringgit bond market. The key measures are contained in the box, *Key Capital Market Measures in 1999*.

Unit Trust Industry

The **unit trust industry** continued to expand in 1999, as reflected in the growth of five indicators of the unit trust industry (Table 4.29), namely the number of unit trust management companies, number of funds launched, number of units in circulation, number of accounts, as well as the net asset value (NAV). Contributing to the expansion of the industry in 1999 was the 13.5% increase in the number of funds, with the launching of 12 funds during the year (six and nine funds launched in 1997 and 1998 respectively), bringing the number of unit trust funds to 101. One unit trust management company was also established in 1999 (the same number as in 1997 and 1998), bringing the number of such

Table 4.28
Trading of Ringgit Bonds

	1998		1999	
	RM mil	% Share	RM mil	% Share
Malaysian Government Securities	33,085	72.8	63,838	41.0
Government Investment Issues	3	0.0	0	0.0
Khazanah Bonds	5,013	11.0	16,098	10.3
Danaharta Bonds	15	0.0	9,410	6.0
Danamodal Bonds	476	1.0	40,635	26.1
Cagamas Bonds	4,463	9.8	12,944	8.3
Other PDS (Unlisted)	1,886	4.1	8,856	5.7
Other PDS (Listed)	536	1.2	4,094	2.6
Total	**45,475**	**100.0**	**155,876**	**100.0**

Source: Bond Information & Dissemination System

Table 4.29
Unit Trust Industry: Selected Indicators

	1998			1999			1998	1999
	Govt. Sponsored Funds	Private Funds	Total	Govt. Sponsored Funds	Private Funds	Total	Growth (%)	
No. of Unit Trust Management Companies	10	22	32	10	23	33	3.2	3.1
No. of Unit Trust Funds*	28	61	89	29	72	101	11.3	13.5
Units in Circulation (billion)	35.5	11.0	46.5	37.1	15.5	52.6	3.0	13.0
No. of Accounts (million)	7.7	0.8	8.6	7.9	1.0	8.9	3.5	3.5
Net Asset Value (NAV) (RM billion)	32.3	6.4	38.7	32.2	11.1	43.3	15.3	11.8
Ratio of NAV to KLSE Market Capitalisation (%)	8.6	1.7	10.3	5.8	2.0	7.8		

* Refers to funds already launched.

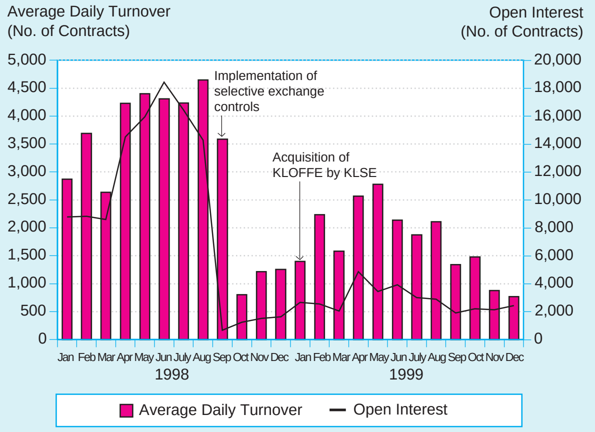
Source: Securities Commission Malaysia

companies to 33. The increase in the number of funds launched and the units in circulation, as well as the strong performance of the KLSE during the year, were among the factors contributing to the 11.8% growth (1998: +15.3%) in the NAV of the unit trust industry, to total RM43.3 billion at end-1999. However, due to the faster growth of the KLSE market capitalisation in 1999 (+47.6%; –0.3% in 1998), the ratio of the unit trust industry's NAV to the KLSE market capitalisation was lower at 7.8% in 1999 (1998: 10.3%).

Futures Market

On 4 January 1999, the KLSE acquired KLOFFE Capital Sdn. Bhd., in line with the global trend towards the consolidation of domestic exchanges. The acquisition would enable the **Kuala Lumpur Options and Financial Futures Exchange (KLOFFE)** to gain access to the infrastructure and operation system of the KLSE, thus providing a comprehensive base to enhance the development of the products offered by KLOFFE. The performance of the **Kuala Lumpur Stock Exchange Composite Index Futures (KLSE CI Futures)**, the only futures product on KLOFFE, was somewhat discouraging in 1999. Trading in the KLSE CI Futures contracts declined significantly by 43% to 436,678 contracts (771,244 contracts in 1998). The lack of interest in the KLSE CI Futures contracts was due mainly to the lower foreign participation since the implementation of the selective exchange controls in September 1998.

Graph 4.25
Kuala Lumpur Options and Financial Futures Exchange: Average Daily Turnover and Open Interest

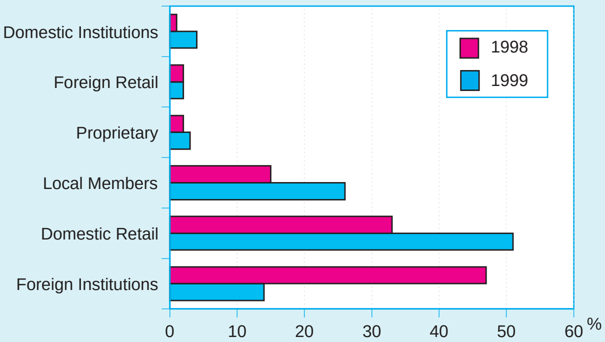


Source: Kuala Lumpur Options and Financial Futures Exchange

During the year, the KLSE CI Futures **prices** tracked the movement of the underlying KLSE CI closely. The KLSE CI Futures started off the year at 582 points, then dipped to a low of 490 points in March, before rebounding to an intraday high of 908.5 points in July. It ended the year at 810 points. The volatility of the KLSE CI Futures reduced markedly, as compared to a year ago. The 20-day moving volatility of the KLSE CI Futures was within a band of 18% to 55% (25% to 215% in 1998) while the underlying KLSE CI was traded within a lower range of 16% to 48%.

In terms of **trading** activities, however, the recovery and the improved market sentiment of the KLSE did not spill over to the futures market. Total trading activity was lower, amounting to 436,678 contracts (1998: 771,224 contracts). On average, trading volume amounted to 1,761 contracts per day (1998: 3,135 contracts) or 43.8% lower than in the previous year. The decline in trading activity was due mainly to the lack of foreign participation. Nevertheless, the open

Graph 4.26
Kuala Lumpur Options and Financial Futures Exchange: Market Demography



Source: Kuala Lumpur Options and Financial Futures Exchange

interest, which is the number of unsettled positions, increased from 1,650 contracts at the end of 1998 to 2,432 contracts at the end of 1999. The Derivatives Liquidity Ratio (DLR), representing the ratio of the turnover value of the futures contracts to the turnover value of the component stocks, stood at 27.9% at the end of the year (24.3% in the previous year). The DLR of less than 100% implied that investors' exposures in the underlying market were not fully covered by its futures contracts, leaving room for further improvement in the turnover value of the KLSE CI Futures contracts.

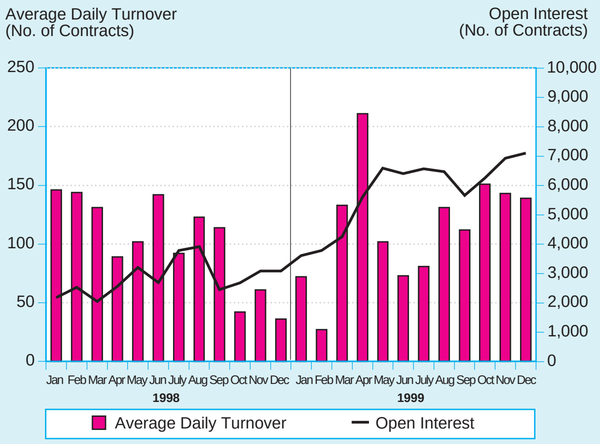
In terms of monthly activity, trading was most active in April and May, with the daily trading volume averaging 2,570 contracts in April and 2,780 contracts in May. In addition, month-end open interest was at its highest in April at 4,878 contracts. This was the period when the market sentiment in the underlying KLSE CI turned bullish, responding to a series of positive news, such as the reduction of the BNM intervention rate, the upgrading of Malaysia's outlook by international credit rating agencies and the overall positive sentiment in the region. In contrast, trading activity declined noticeably in the last quarter, averaging 879 contracts per day in November and 767 contracts per day in December. The lower trading activity reflected market concerns surrounding the general elections and the Y2K issue.

Market **demography** of KLOFFE changed markedly in 1999. Domestic retailers emerged as the major players, accounting for 51% of the total trade (1998: 33%), followed by local members (26%; 1998: 15%). The number of local members increased in 1999 to 61 (1998: 49), reflecting the growing awareness in futures trading. In the past, the market demography of futures trading had been characterised by the dominance of foreign institutions, which accounted for more than 45% of the total trade in the period from 1996 to August 1998. In 1999, the participation of foreign institutions fell significantly to 14% of the total trade (47% in 1998), following their reduced interest in KLOFFE since the selective exchange controls were introduced. However, there was renewed foreign interest in the second half of 1999 when stock market developments reflected the stronger-than-expected recovery in economic growth. The participation of foreign institutions increased from 8% of total trade in the fourth quarter of 1998 to 14% in the third quarter of 1999 and rose further to 18% in the last quarter of 1999. Recognising the need to increase the participation of domestic institutions so that KLOFFE would have a more balanced participation among domestic players, the Futures Industry Act (FIA) was amended to allow domestic fund managers to participate in the futures industry. Consequently, the share of domestic institutions, although small, improved from 1% in 1998 to 4% in 1999.

In 1999, the **3-month Kuala Lumpur Interbank Offered Rate (KLIBOR) futures** contract was more actively traded on the Commodity and Monetary Exchange of Malaysia (COMMEX). KLIBOR futures recorded both a higher turnover during the year (daily average of 115 contracts; 102 in 1998) and a record high open interest position at the end of the year (7,107 contracts; 3,092 in 1998).

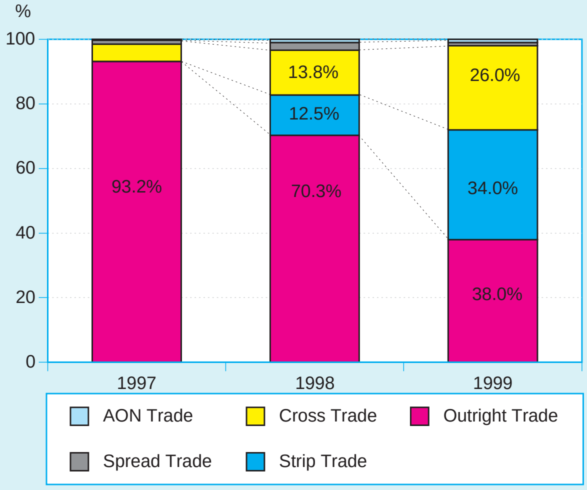
The higher **trading activity** was due mainly to the improved liquidity situation in the underlying cash market and the revival of the market maker

Graph 4.27
KLIBOR Futures: Average Daily Turnover & Open Interest



Source: Commodity and Monetary Exchange of Malaysia

Graph 4.28
KLIBOR Futures: Types of Trade



Source: Commodity and Monetary Exchange of Malaysia

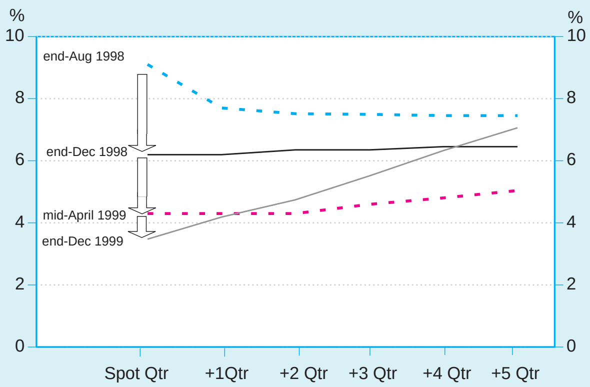
scheme in August 1999. The decline in interest rates during the year could also have increased the demand for hedging against interest rate movements, especially in April when the 3-month KLIBOR declined from 6.3% to 4%. This was reflected in the surge of the average daily turnover to 211 contracts in April (highest monthly turnover during the year) and the increase in open interest position by 1,348 contracts (the highest monthly increase in open interest position ever recorded). The year ended with 7,107 open interest contracts, more than double the number of contracts at the end of 1998. In terms of the types of trades, interest continued to shift from outright trades to strip and cross trades. The share of outright trades fell sharply from 70.3% of total transactions in 1998 to 38% in 1999, while the share of strip and cross trades rose to 34% (1998: 12.5%) and 26% (1998: 13.8%) respectively.

The implied yield curve in 1999, changed from a flat line at the end of 1998 to an upward sloping curve at the end of 1999, with lower implied yields on shorter-term contracts and higher implied yields on longer-term contracts. The implied yield on the spot-month contract declined to 3.48% at the end of 1999 (end-1998: 6.2%), while implied yields on longer-dated contracts were on a declining trend in the first five months, before trending upwards until the end of the year. The implied yield on the 18-month contract, for example, ended the year higher at 7.06% (end-1998: 6.46%). The steepening of the yield curve reflected the market's expectation of higher interest rates in the future. This was partly due to the anticipation of a pick-up in economic activity and loan demand in year 2000 and beyond.

In an effort to boost trading in the KLIBOR futures market, a market maker scheme was re-introduced on 16 August 1999. The revival of the scheme came one year after it was terminated in July 1998 as a result of the financial crisis. Essentially, a market maker scheme requires market makers to make two-way quotes so as to provide liquidity to the market. The scheme started with five market makers but ended the year with four, due to an impending merger of two market makers. Since the launch of the market maker scheme, there was an increase in market turnover, the bulk of which was contributed by the market makers (49–69% of total turnover in the last four months of 1999). Meanwhile, the number of local members of COMMEX increased in 1999 to 52 (1998: 47), reflecting the increased awareness and interest in futures trading following promotional and educational campaigns by COMMEX.

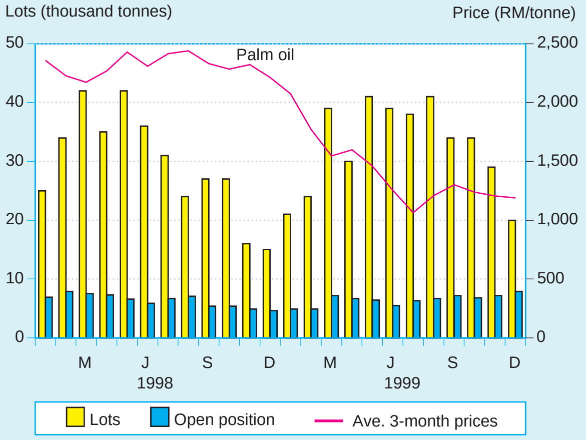
Trading of crude palm oil (CPO) futures contracts on the Commodity and Monetary Exchange of Malaysia turned around to increase by 10.2% to 389,933 contracts or equivalent to 9.7 million tonnes in 1999 (1998: –27% or 353,680 contracts or equivalent to 8.8 million tonnes), primarily on account of the marked increase in Malaysia's CPO production. On a daily basis, the average volume traded was 1,559 lots, compared with 1,443 lots in 1998. Total open positions also increased during the year, from 4,597 lots at end-

Graph 4.29
KLIBOR Futures: Implied Yield



Source: Commodity and Monetary Exchange of Malaysia

Graph 4.30
Futures Trading on the COMMEX



December 1998 to 7,854 lots at the end of December 1999. Foreign participation remained low during the year, although non-residents were allowed since mid-September 1998 to trade in any Malaysian futures market without any restriction on the repatriation of funds as it was exempted from the 12-month holding period and the payment of levy. Foreign participants accounted for 12% of the total volume traded in 1999, compared with 25% in recent years prior to the crisis.

The strong CPO futures prices in 1998 continued briefly in early 1999 with the 3-month price for the commodity staying above the RM2,000 per tonne level in January and trading at a premium over its major competitor, soyabean oil. However, prices fell below the RM2,000 level in February and declined further thereafter, to close at RM1,190 per tonne in December. The downtrend in prices was on account of the sharp increase in Malaysia's CPO production during the year as well as strong competition from the bumper soyabean harvests in the United States and Latin America. With the price decline, CPO was traded at a discount against soyabean oil from May onwards. During the year, the price range for the 3-month futures contract widened to RM1,240 from RM500 in 1998, with the highest price recorded at RM2,203 per tonne.

5 External Relations

Overview

As the crisis-affected economies recovered and stability returned to the world financial markets, discussions at regional and international meetings during the course of 1999 veered away from crisis management towards sustaining the recovery process and the reform of the international financial architecture (IFA). However, limited progress has been achieved with respect to the fundamental IFA issues. Progress has only been in terms of recognition of the need to address some issues to prevent future crises. So far, there is no consensus on implementation plans for areas agreed upon.

Positive developments in 1999 included the recognition by the international community that reforms are necessary to improve the transparency of market players, particularly the highly leveraged institutions. Similarly, there is a consensus on the need for a mechanism to avoid excessive risk-taking by market participants, including measures to ensure that private investors and market players assume a fair share of the costs of crisis management and resolution. The global community has acknowledged the importance of orderly capital account liberalisation and there is growing support for the use of temporary controls as prudential safeguards against financial market excesses. Recognition by important segments of the international community, including the International Monetary Fund (IMF), was gained on the merits of selective and temporary capital controls as a prudential safeguard against volatile and disruptive capital flows. However, the IMF has not explicitly recommended the use of such measures to address financial crises, and has remained silent on whether such prudential safeguards are useful to reduce the vulnerability of small emerging market economies.

The year also witnessed the formation of two new fora for deliberations on the IFA issues, namely the Financial Stability Forum and the Group of 20. The latter provide for a closer dialogue between the industrialised and large developing countries. A number of new initiatives were also launched during the year. These included the establishment of the Contingent Credit Line by the IMF, designed for crisis prevention. Meanwhile, in addressing the need to strengthen surveillance on the financial sector, the IMF and World Bank have launched a pilot project on a Financial Sector Assessment Programme. The transformation of the Interim Committee of the IMF into the International Monetary and Financial Committee (IMFC) represented a step in the process to reform the IMF and accord the IMFC with more decision-making authority.

Notwithstanding these developments, the return of stability to financial markets has also given rise to concern that complacency may set in and dissipate the momentum for reforms in the international financial architecture. While there is a consensus on the need for reforms, progress remains slow in terms of practical proposals for implementation. Although the international community agreed on the need for symmetry in the call for greater transparency in both the public and private sectors, no measure has been made to require greater disclosure by private sector entities. Similarly, progress has yet to be made with respect to greater involvement of the private sector in crisis management and resolution. At the same time, there remains much outstanding work on the new financial architecture. Work needs to be expedited on mechanisms for ensuring orderly capital flows so that the full benefits of globalisation can be realised.

Bank Negara Malaysia (BNM) has continued to participate actively in various international, regional and bilateral fora in pushing for the reform of the international financial architecture. Apart from highlighting the views and interests of emerging countries, BNM's participation also sought to foster support for greater independence of domestic policy actions and for countries to be given the opportunity to implement non-conventional policies when exceptional circumstances required an alternative approach. Much work was also done to forge an ASEAN common position on the reform of the international financial architecture that was adopted at the Informal ASEAN Finance Ministers Meeting on 30 April 1999.

In recognition of the Bank's positive commitment to be an integral part of the international community, BNM was officially admitted as a shareholding member of the Bank for International Settlements (BIS) on 24 December 1999. As a shareholding member of the BIS, it is envisaged that BNM will participate more actively in the activities of the BIS.

International Relations

International Monetary Fund

The Interim Committee of the IMF met on two occasions in 1999, namely the 52nd and 53rd meetings in Washington, D.C. on 27 April and 26 September 1999 respectively. As in 1998, efforts to reform and strengthen the international financial architecture remained at the centre of discussions of the Committee. The Committee's deliberations included a review of efforts to prevent crises and ensure their orderly resolution, measures to further strengthen IMF surveillance, and increase transparency of national government policies, the private sector and the IMF. The Committee also discussed issues relating to the choice of an appropriate exchange rate, capital flows and country experiences with the use and liberalisation of capital controls. Reflecting the international community's commitment to fight poverty, the Interim Committee convened, for the first time, a Joint Meeting with the Development Committee of the World Bank on 26 September 1999 to discuss the enhancement of the Heavily Indebted Poor Countries (HIPC) Initiative.

In the area of crisis prevention, the IMF established the Contingent Credit Line (CCL). Through the CCL, the IMF provides short-term financing, if the need arises, to assist members in addressing the exceptional balance of payments financing needs that can arise from a sudden and disruptive loss of market confidence due to contagion. This refers essentially to circumstances that are largely beyond the member's control and stem primarily from adverse developments in international capital markets consequent upon developments in other countries. Eligible member countries would, however, need to have in place, prior to the crisis, sound and sustainable policies; adherence to internationally accepted standards; and constructive involvement of the private sector. The last criterion is to ensure that the private sector shares the burden in crisis management and resolution. In addition, the IMF is also working with member countries to put in place data monitoring mechanisms as part of the effort to avoid future crises and ensure their orderly resolution. These included the establishment of systems for high frequency monitoring of private external liabilities, maintaining adequate foreign exchange liquidity and effective communication with private capital markets.

In order to further strengthen IMF surveillance, the Committee felt that assessments of the implementation of the Basel Core Principles should be embedded into the regular IMF surveillance activities. In this regard, the IMF and World Bank have launched a pilot Financial Sector Assessment Programme (FSAP), designed to identify financial system strengths and vulnerabilities, so that appropriate policy responses can be developed. The FSAP is aimed at promoting a more effective dialogue with national authorities. It would also aim to provide the IMF and World Bank with a common platform for financial sector policy advice and technical assistance to member countries. The scope of the FSAP generally included an assessment of the macroeconomic environment; financial institutions' structure; financial markets; review and assessment of systemic risks in the payment systems, and risk management procedures. The FSAP would be conducted on a 5-year cycle on a voluntary basis. The FSAP report would feed into the Financial System Stability Assessment (FSSA), which would become a regular part of Article IV Consultations. The Interim Committee encouraged member countries to participate in the FSAP programme.

During the year, the Committee continued to urge for greater transparency of national government policies, as well as of private sector reporting and of the international financial institutions, including the IMF. New initiatives to improve the transparency of member economies include the adoption of the "Code of Good Practices on Transparency in Monetary and Financial Policies: Declaration of Principles" to be used as a guide for members to increase transparency in the conduct of these policies. Meanwhile, the Special Data Dissemination Standard (SDDS) was expanded further to require subscribing members to include additional data on international reserves. The IMF is also in the process of establishing a separate category for data on external debt and international investment positions.

In the IMF, the initiative to enhance its own transparency included a pilot project for the voluntary public release of Article IV staff reports, which contained the assessment of IMF staff on member economies. Greater IMF transparency would also be in the form of the release of the concluding statements on the IMF Executive Board's deliberations on decisions regarding the use of IMF resources by a country as well as the release of Public Information Notices (PINs) on the IMF Executive Board's discussions on policy issues. Public access to the IMF's archives would also be expanded.

During discussions on the choice of an appropriate exchange rate, the Committee noted that global capital mobility has increased the requirements for policy adaptability and institutional preparedness for maintaining a fixed exchange rate. The Committee emphasised that countries should be able to choose an exchange rate regime that is suitable for their specific circumstances and longer-term strategy. In this regard, the Committee agreed that IMF programmes and surveillance should focus on the consistency of macroeconomic and other policies and institutional arrangements with the chosen exchange rate regime. In addressing the issue of sudden reversals in capital flows, the Committee highlighted the need to address sources of economic vulnerabilities and urged the IMF to review efforts to eliminate any regulatory bias in favour of short-term interbank credit lines and to identify arrangements to assure continuing private sector financing in times of crisis. On the use of controls to manage capital flows, the Committee encouraged the IMF to build upon its study of individual countries' use and liberalisation of controls, with particular attention to the relationship between capital account liberalisation and financial sector stability. The IMF and World Bank were requested to develop a set of best practices in public debt management to help countries reduce vulnerability. The IMF has initiated a survey on capital flows associated with foreign exchange markets.

In order to provide faster, broader and deeper debt relief with the central goal of reducing poverty in the poorest countries in the world, the Interim Committee endorsed the new Poverty Reduction and Growth Facility (PRGF). The PRGF replaced the IMF's Enhanced Structural Adjustment Facility and incorporated efforts on poverty reduction as part of a new growth-oriented strategy among low-income members to ensure that debt relief will result in poverty reduction. To finance the IMF's participation in the HIPC Initiative, the Committee endorsed the one-time off-market transactions of up to 14 million ounces of gold by the IMF, in addition to bilateral contributions from member countries.

In the area of institutional reforms in the IMF, the Committee agreed that the IMF should enhance the modus operandi of its institutional mechanism and its co-operation with other institutions. There was a consensus on a proposal to transform the Interim Committee into the International Monetary and Financial Committee and to strengthen its role as the advisory committee of the IMF Board of Governors. This was in line with on-going proposals to reform the IMF, which included a move to accord more decision-making authority to the Committee, as opposed to an advisory role. However, progress in terms of fundamental reforms in the IMF, for example, to make the IMF more accountable for its policy prescriptions, is yet to be seen. Despite the call from various quarters, a review by an independent panel of the performance of the IMF in managing the Asian crisis has not been conducted. Such a review was undertaken after the Mexican crisis. Following the Asian crisis, another review would be important to draw lessons not only on the appropriate policy stance in crisis management and resolution, but also on the institutional arrangements for more effective implementation of these policies.

Financial Stability Forum

Deliberations on reforming the international financial architecture continued in 1999, with the establishment of two new fora, namely the Financial Stability Forum and the Group of 20 (G-20). A number of large developing countries and emerging market economies were invited to participate in the deliberations of the G-20 and in the Working Groups of the Financial Stability Forum. Established by G-7 Finance Ministers and Central Bank Governors on 22 February 1999, the **Financial Stability Forum (FSF)** was designed to facilitate the exchange of information and the co-ordination of issues on international financial stability between national authorities, international regulatory and expert groups and international institutions. The membership of the FSF comprised the G-10 countries, the financial centres such as Hong Kong SAR and Singapore, as well as representatives from international financial institutions and regulatory groups. The scope of activities of the Forum was to evaluate the vulnerabilities affecting the stability of the international financial system and identify and administer the actions needed to deal with these vulnerabilities. To address the wide-ranging issues on financial stability, the FSF formed three ad-hoc Working Groups in May 1999 to study three areas, namely, highly leveraged institutions, capital flows and offshore financial centres.

The Deputy Governor of Bank Negara Malaysia is a member of the FSF Working Group on Capital Flows. In participating in the Working Group, Malaysia shared its experience in managing volatile capital flows. Malaysia also presented its views on the role of capital controls as a prudential measure to ensure financial stability and emphasised the need for the working group to not only consider the issues associated with debt, but also non-debt flows.

The Terms of Reference of the **Working Group on Highly Leveraged Institutions (HLIs)** were to recommend actions to reduce the destabilising potential of HLIs in financial markets. To date, the Group had focused its discussions on addressing the effects arising from the activities of HLIs on the dynamics and integrity of financial markets. A study group to assess the impact of HLIs' activities on small- and medium- sized economies was established by the Group. Based on these discussions and studies, the Group focused on developing recommendations for improving risk management practices, enhancing both institutional disclosure and market transparency and strengthening the infrastructure and functioning of markets.

The **Working Group on Capital Flows** focused its attention on measures that would help reduce volatility of capital flows in borrower and creditor countries and the risks associated with excessive short-term external indebtedness to financial systems. In this regard, Malaysia emphasised the importance of also considering non-debt related flows. A risk management framework was adopted, emphasising the resulting stocks of assets and liabilities of capital flows and the associated risks. Recommendations would focus on the assessment and management of risks on an economy-wide basis through prudent debt and liquidity management by the public sector, the management of various risk exposures and their inter-relationship by banks and corporations, and the improvement of data reporting systems required for sound risk management. The Group also examined distortions that could bias capital flows and increase volatility. The Group examined the costs and benefits of controls on inflows as a preventive risk management tool in the context of implementing sound policies that contribute to internal and external stability.

The **Working Group on Offshore Financial Centres (OFCs)** examined the impact on global financial stability of the use made by market participants of OFCs and the OFCs' progress in conforming with cross-border information exchange agreements and enforcing international prudential standards. The group has reviewed activities of OFCs, and problems that emerged given the prevailing weaknesses in cross-border co-operation, financial supervision, and transparency. In this regard, the Group focused on relevant international standards for implementation by OFCs and the development of recommendations on mechanisms for evaluating and enhancing compliance in the implementation of these standards.

Since its establishment, the FSF has met twice, on 14 April 1999 and 15 September 1999. The working groups have also drawn on work by other private and public sector fora, and have been in consultation with private sector participants and supervisory authorities as well. The Final Reports of the Working Groups are expected to be submitted to the FSF in March 2000.

FSF
Objective: to address issues affecting international financial system stability

Members: Australia, Canada, France, Germany, Hong Kong SAR, Italy, Japan, Netherlands, Singapore, the United Kingdom and the United States.

Institutional members: IMF, World Bank, BIS, Organisation for Economic Co-operation and Development, Basel Committee on Banking Supervision, International Organisation of Securities Commission, International Association of Insurance Supervisors, Committee on Global Financial System, and Committee on Payment and Settlements System.

Working Group on Highly Leveraged Institutions	Working Group on Capital Flows	Working Group on Offshore Financial Centres
Members: Australia, Canada, France, Germany, Hong Kong SAR, Japan, Netherlands UK, US, IMF.	Members: Brazil, Canada, Chile, France, Germany, Italy, Japan, **Malaysia**, South Africa, UK, US, BIS, IMF and World Bank.	Members: Canada, France, Germany, Italy, Japan, Singapore, Switzerland, Thailand, UK, US, OECD.

Group of 20

The **Group of 20** or **G-20** was established on 25 September 1999 to provide a new mechanism for informal dialogue within the framework of the Bretton Woods institutional system. The role of the new Group is to broaden the discussions on key economic and financial policy issues among systemically significant economies and promote co-operation to achieve stable and sustainable world economic growth. Membership of G-20 includes systemically significant developed countries and a number of emerging market economies. The IMF and World Bank also participate in the Group's discussions.

G-20

Objective: forum for informal dialogue on key economic and financial policy issues among systematically significant economies and promote co-operation to achieve stable and sustainable world economic growth that benefits all.

Members: Argentina, Australia, Brazil, Canada, The People's Republic of China, France, Germany, India, Indonesia, Italy, Japan, Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the United Kingdom, the United States, the European Union, IMF and World Bank

At its inaugural meeting on 15-16 December 1999 in Berlin, Germany, it was agreed that the immediate attention of the Group would be to reduce countries' vulnerabilities to international financial crises. The task, to be carried out by the G-20 Deputies, is to focus on four main areas, namely, a complete stock taking of member nations' progress in reducing vulnerability to crises; an assessment by member nations on their compliance with international codes and standards in financial sector policy and transparency; the completion of Reports on Observance of Standards and Codes (Transparency Reports) and Financial System Stability Assessment by the IMF; and an assessment of various exchange rate arrangements and their role in minimising the impact of financial crises.

Regional Relations

ASEAN Finance Ministers' Meeting

Co-operation under the ASEAN Finance Ministers process was further strengthened in 1999 in the aftermath of the financial crisis of 1997-98. The Finance Ministers met on three occasions during the year, namely at the **Third ASEAN Finance Ministers' Meeting (AFMM)** on 19-20 March 1999 in Hanoi, Vietnam, the **Informal AFMM** in Manila, the Philippines, on 30 April 1999 and again at the **Special AFMM** on 25 November 1999 in Manila. The latter was in conjunction with the Third Informal ASEAN Summit on 27-28 November 1999. The meetings provided an opportunity for ASEAN Finance Ministers to review the economic and financial situation in their respective economies, as well as to exchange views on regional and global developments and the near term outlook. Ministers also discussed issues related to the International Financial Architecture.

Members of ASEAN are Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam.

An important move forward in ASEAN co-operation was the adoption of an "ASEAN Position on the Reform of the International Financial Architecture" at the Informal AFMM. Under the Joint Position, ASEAN agreed to adopt a pro-active approach in international discussions on the reform of the international financial architecture. This was considered essential to ensure that such reforms were a joint effort of both industrial and developing countries, and took due cognisance of individual countries' circumstances. ASEAN Finance Ministers agreed that there was a need to strengthen domestic financial systems to avoid future crises, and that a strengthening of regional support mechanisms was important to assist members in times of need. The Ministers emphasised that greater transparency and disclosure of the public sector should be matched by the private sector, including international credit rating agencies, due to their influence on the market. ASEAN Finance Ministers also stressed the importance of an orderly and well-sequenced approach to capital account liberalisation to ensure that countries were adequately prepared to face the challenges of globalisation. Ministers reiterated that stable exchange rates were important for international trade and payments, and that there was no single exchange rate regime that was appropriate for all countries. With regard to short-term capital flows, ASEAN Finance

Ministers emphasised the need for an effective, globally agreed mechanism to promote closer and more co-ordinated monitoring of short-term capital flows. The recent crisis also highlighted the need for an adequate mechanism to protect the most vulnerable segments of society. In this connection, ASEAN Finance Ministers considered it important to reconcile the objectives of greater economic stability with those of improving the standards of living and the attenuation of the effects of crises on the poor and most vulnerable. The Ministers also considered it timely for a review of the roles of the International Financial Institutions (IFIs). Such a review was essential to ensure greater co-ordination of activities and to ensure that IFIs have the capacity and capability to effectively manage and resolve crises.

At the Special AFMM on 25 November 1999, the ASEAN Finance Ministers reiterated their commitment to persevere with reforms to ensure sustainable recovery. At the same time, the Ministers emphasised the importance for the G-7 (Group of Seven) industrialised nations to pursue policies that were conducive to global financial stability and sustained global growth. The Ministers approved a Work Programme on specific activities to implement the commitments in the area of finance co-operation outlined in the Hanoi Plan of Action adopted by the ASEAN Leaders in December 1998. The Work Programme was designed to promote economic recovery and strengthen the region's competitiveness in order to meet the challenges ahead. Among the major activities, Malaysia will lead in the projects in relation to the greater use of ASEAN currencies and to study the feasibility of establishing an ASEAN currency and exchange rate system as a long-term objective of ASEAN co-operation. With regard to the latter, the IMF had agreed to ASEAN's request and prepared a concept paper on a common ASEAN currency, which was tabled for discussion at the Fifth Meeting of the ASEAN Central Bank Forum in November 1999. The IMF study highlighted the preconditions, costs and benefits of a common currency arrangement. Given the different stages of development in the ASEAN economies, it was agreed that the IMF study should examine in greater detail the implications of a single ASEAN currency. The ASEAN Finance Ministers also agreed on the objectives, principles and elements of the Terms of Understanding for the establishment of the ASEAN Surveillance Process. In particular, the scope of the surveillance activities would include the monitoring and analysis of macroeconomic developments within the region, as well as other specific areas, including structural and sectoral issues, that would be of interest to ASEAN members.

Manila Framework

The Manila Framework continued to meet twice in 1999 to discuss issues relating to regional surveillance, policy options in crisis management and the reform of the international financial system. During the **Fourth Meeting of the Manila Framework** held in Melbourne, Australia on 26-27 March 1999, discussions were focused on the efficacy of IMF programmes in Asia. In particular, the meeting assessed the various approaches in the use of monetary policy in an environment of large and sudden movements in short-term capital flows. The meeting noted that the general conditions under which higher interest rates would work were not yet understood and required further study. Participants agreed that constraints on capital inflows could act as a buffer against adverse effects of volatile capital movements in countries where the banking system was still developing. While recognising that controls can work under certain circumstances, the meeting felt that the use of controls should be market based, specific, temporary and in conjunction with other appropriate domestic policy adjustments. In the discussion on international financial reforms, the meeting focused on the impact of large institutional investors, including highly leveraged institutions on foreign exchange markets, the role of the private sector in forestalling and resolving crises, and transparency. It was noted that the stabilisation of global financial markets and the implementation of supportive fiscal and monetary policies were important in contributing to the economic recovery in the crisis-affected economies.

The Manila Framework is a regional surveillance process to complement the IMF's global surveillance. Its members comprise finance and central bank deputies from Australia, Brunei Darussalam, Canada, The People's Republic of China, Hong Kong SAR, Indonesia, Japan, Korea, Malaysia, New Zealand, the Philippines, Singapore, Thailand and the United States.

By the time of the **Fifth Meeting of the Manila Framework** on 30-31 August in Singapore, the performance of most of the regional economies had improved significantly. To ensure sustained, broad-based recovery, it was emphasised that progress in bank restructuring should be reinforced by further progress in corporate restructuring. On reforms of the international financial architecture, there was broad support for better disclosure by highly leveraged institutions and better risk management by the creditors and counterparties of such institutions. The Meeting agreed that capital account liberalisation needs to be carefully sequenced within a framework of sound financial supervision and prudential regulation. It should be supported by adequate reporting and surveillance requirements for capital flows. There was also consensus that the choice of an appropriate exchange rate regime should depend on each economy's circumstances and institutional structure. The Meeting agreed that it was important to achieve greater progress to involve the private sector in the prevention and resolution of financial crises.

The Manila Framework meeting in Singapore included, for the first time, the Bank for International Settlements (BIS). This is in addition to the regular participation of officials from the IMF, World Bank and Asian Development Bank (ADB). The participation of the BIS reflects the increased emphasis on financial sector surveillance and provides an avenue for the views of the Manila Framework on the international financial architecture issues to be communicated to the Financial Stability Forum chaired by the General Manager of the BIS.

Asia-Europe Co-operation

The Asia-Europe Vision Group, established under the **Asia-Europe Meeting (ASEM)** process, completed and presented its report to the ASEM Foreign Ministers on 29 March 1999. The report, "For a Better Tomorrow: Asia-Europe Partnership in the 21st Century", envisioned a broad scope of Asia-Europe co-operation encompassing issues on sustaining economic partnership; environmental challenge; educational, cultural and societal exchanges; political and security co-operation; and the ASEM process. A number of areas were identified under the theme of economic partnership. These included liberalisation and open markets. The report recommended that ASEM partners set a goal of free trade in goods and services by the year 2025 by adopting a strategic framework for the progressive freeing of trade in goods and services among Asia and Europe.

On co-operation for financial stability, the major economic players were urged to undertake closer macroeconomic policy co-ordination. The Vision Group focused on the need for Asia and Europe to work together in order to achieve a co-ordinated response matching rapid globalisation. In enhancing Asia-Europe trade and investment, the Vision Group recommended that the ASEM Leaders establish Asia-Europe Business Advisory Councils to institute high-level dialogue to promote Asia-Europe investment. The conclusions and recommendations of the Vision Group's report will be presented to the ASEM Leaders' Summit in Seoul in October 2000.

The Asia-Europe Meeting (ASEM) process emanated from the meeting of Leaders of Asia and Europe held on 1-2 March 1996, to facilitate economic and financial co-operation between the two continents. Members of ASEM are Brunei Darussalam, The People's Republic of China, Indonesia, Japan, Korea, Malaysia, the Philippines, Singapore, Thailand, Vietnam, Belgium, Denmark, Germany, Greece, Spain, France, Ireland, Italy, Luxembourg, Netherlands, Austria, Portugal, Finland, Sweden, the United Kingdom and the European Commission.

The ASEM Finance Officials met in Washington, D.C. on 26 April 1999 in a follow-up to the Second ASEM Finance Ministers' Meeting in Frankfurt, Germany on 15-16 January 1999. Among the agreements reached by the Ministers was that, in the field of financial sector supervision, there was a need for technical assistance to align the current supervisory and legal systems to internationally agreed standards. Member countries were encouraged to submit their request for technical assistance to the European Commission, which would forward them for discussion by the ASEM Finance Officials in April 2000. Malaysia has been a recipient of grants and technical assistance under the ASEM Trust Fund. In the area of strengthening the financial system, BNM is presently undertaking projects on the study of international practices regarding depositor protection and deposit insurance schemes, and on the development of early warning systems, financed by the ASEM Trust Fund.

Asia-Pacific Economic Co-operation

As the chair of the Asia-Pacific Economic Co-operation (APEC) Finance Ministers Process from May 1998 to May 1999, Malaysia hosted the Eighth APEC Finance Working Group Meeting on 23-24 March 1999 in Kuala Lumpur and subsequently chaired the APEC Finance and Central Bank Deputies Meeting in Washington, D.C. on 29 April 1999. Malaysia hosted the Sixth APEC

Finance Ministers meeting in Langkawi on 15-16 May 1999, which heralded the inaugural participation of the Finance Ministers of Peru, Russia and Vietnam into the forum. New Zealand assumed the chair of the APEC Finance Ministers Process and hosted the Deputies meeting in Wellington, New Zealand on 26-27 August 1999 and the APEC Leaders Summit in Auckland, New Zealand on 13 September 1999.

Since the meeting in Kananaskis, Canada in May 1998, the economic climate had improved markedly. Nonetheless, the meeting in Langkawi accorded the opportunity for Finance Ministers to take stock of the economic and financial situation in the region, explore ways to further strengthen economic fundamentals to accelerate the recovery process, and to meet the longer-term challenges. Malaysia, together with the World Bank, presented a background paper on the experience of the crisis-affected economies in East Asia and Latin America, and the lessons from the crisis for a discussion on mitigating the impact of the crisis on the poor. In addition, APEC Finance Ministers discussed the issue of appropriate exchange rate regimes and concluded that any regime adopted must be supported by consistent policies and robust financial systems. The importance of peer surveillance, restructuring of the financial and corporate sectors, as well as the need for a stronger international financial architecture was also stressed by Ministers. In the discussion on the international financial architecture, there was general agreement on the need for greater transparency and disclosure by market participants and the need to involve emerging market economies in discussions on the reform process. Ministers noted that the approach to capital account liberalisation should be properly sequenced, taking into account the specific circumstances of individual countries. Social issues are also an important element in the new architecture and crisis resolution procedures should take into account the social impact.

Members of APEC are Australia, Brunei Darussalam, Canada, Chile, The People's Republic of China, Hong Kong SAR, Indonesia, Japan, Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, the Philippines, Russian Federation, Singapore, Taiwan, Thailand, the United States and Vietnam.

In the area of finance, various on-going initiatives under the APEC Finance Ministers process were discussed. These included efforts to strengthen financial market supervision; pension fund reform; supporting the development of credit rating agencies and strengthening information disclosure standards; and development of the domestic bond market. Ministers also reviewed the development of a Voluntary Action Plan for Supporting Freer and Stable Capital Flows to enable economies to benefit from and minimise the risks of capital account liberalisation. Malaysia led and presented the results of the initiatives on Strengthening Corporate Governance in the APEC Region and on a Survey on the Adequacy of the Bank Supervisory Regimes in APEC Economies. Ministers approved recommendations contained in the report on governance and urged member economies to take early and comprehensive implementation of reforms to enhance corporate governance. Meanwhile, the results of the survey on adequacy of bank supervisory regimes showed that member economies have achieved a high degree of compliance with the requirements of the Basle Core Principles for Effective Banking Supervision. The Ministers also agreed on the need to expedite the development of the domestic bond market.

During the Meeting of APEC Finance and Central Bank Deputies in Wellington, New Zealand on 26-27 August 1999, the discussions focused on the proper sequence and timing for liberalising capital accounts, ways to further improve IMF surveillance and programmes, a review of the status and progress in implementing international standards, as well as options to involve the private sector in the resolution and containment of crises. In addition, the meeting discussed the applicability of debt standstills to Asia. Deputies also considered measures to promote APEC co-operation via members' efforts to strengthen financial markets.

The work programme of APEC Finance Ministers was endorsed by The APEC Leaders' Summit on 13 September 1999 in Auckland, New Zealand. The APEC Leaders encouraged the Finance Ministers to continue with their efforts to strengthen domestic financial markets and secure the foundation for the return of capital to the region. Towards this objective, the APEC Leaders stressed that there should be enhanced supervision of financial markets, development of domestic bond markets based on an APEC Compendium of Sound Practices published in early September 1999 and development and application of agreed corporate governance principles. APEC Leaders also tasked the Finance Ministers to develop uniform banking standards that will allow greater transparency and accountability among international banks and thereby reduce high-risk lending, especially for speculative purposes.

G-15

The **Ninth Summit of the Heads of State and Government of the Group of Fifteen Developing Countries (G-15)** was held on 10-12 February 1999 in Montego Bay, Jamaica, with Sri Lanka joining as the 17th member of the Group. Noting the slow progress being made in the reform of the international financial system, the Leaders called for concrete steps in a number of areas. These included the need for an appropriate mechanism and rules to monitor and supervise the operations of large financial market players, including hedge funds and currency speculators; and the inclusion of social safety nets as an integral part of development policies and programmes, at both the micro and macro levels. The Leaders reiterated that liberalisation of the capital account should be carried out in an orderly, gradual and well-sequenced manner. In addition, the reform process should be a consultative process involving both the developed and developing countries.

> G-15 comprises Algeria, Argentina, Brazil, Chile, Egypt, India, Indonesia, Jamaica, Kenya, Malaysia, Mexico, Nigeria, Peru, Senegal, Sri Lanka, Venezuela and Zimbabwe.

D-8 Summit

Economic co-operation among the Islamic countries was further enhanced in 1999. At the **Second D-8 Summit** on 1-2 March 1999, Leaders held discussions on a diverse range of issues and programmes of co-operation. On financial issues, D-8 Leaders expressed concern over the lack of progress in the reform of the international financial architecture, that was needed to guard against possible recurrence of crises as well as new threats of instability and protectionism. Leaders noted that such reforms should be a global effort, involving the developing as well as developed countries so that the diverse experiences, problems and circumstances of countries at different stages of development are taken into account. The Leaders supported the call for greater transparency and disclosure, and noted that it should apply equally to both the public and private sectors. On globalisation, mindful of the risks of destabilisation and increased inequality between developed and developing countries, the Leaders stressed the need to address all aspects of globalisation, including the establishment of appropriate safeguards to minimise the risks and to ensure that benefits of globalisation are shared by all.

> D-8 is a forum of functional co-operation, which exploits the element of comparative advantage, complementarity, economies of scale and a commonality of interest, so that real benefits can accrue to the D-8 member countries. D-8 members are Bangladesh, Egypt, Indonesia, Iran, Malaysia, Nigeria, Pakistan and Turkey.

With respect to the D-8 programme of co-operation, Malaysia has agreed to organise activities to enhance the capacity of an existing re-takaful company to meet the needs of D-8 countries. In this connection, Malaysia has convened a workshop to draw up the modus operandi and formulate the appropriate strategies to promote takaful and re-takaful activities on 31 May to 1 June 1999 in Kuala Lumpur. Subsequently, a Conference on Takaful was held on 2-3 June 1999 and a Seminar on Islamic Banking and Finance was also organised on 2-4 June 1999 with participation from all D-8 countries.

Central Banking Fora

ASEAN Central Bank Forum

An important area of central banking co-operation was the meeting of the **ASEAN Central Bank Forum (ACBF)**. **The Fifth ACBF** was held in Hanoi, Vietnam on 3 November 1999. In discussing the current economic and financial developments, there was a general commitment by members to persevere with structural reforms to ensure the pace of recovery is sustainable. During the meeting, the IMF made a presentation on its latest initiative to expand IMF surveillance to include the financial sector. The absence of ASEAN involvement in the new and voluntary IMF Financial Sector Assessment Programme signalled the ASEAN economies' commitment to focus their efforts on economic recovery and restructuring.

> The ACBF was established in 1997 to facilitate frank and open exchange of views between ASEAN central banks and monetary authorities on monetary policy and general macroeconomic and financial matters and to highlight policy issues that might require the attention of the ASEAN Finance Ministers.

The meeting also discussed the IMF study on the concept of an ASEAN currency arrangement. The study highlighted the preconditions as well as the costs and benefits of such an arrangement. While members recognised that a single currency would improve fiscal discipline, there was concern over the loss of monetary autonomy. Members also highlighted that given the diversity, different stages of development, and macro and microeconomic as well as institutional differences in the ASEAN economies, more work was needed to fully assess the costs and benefits of a single ASEAN currency. The meeting agreed that the study needed to examine more deeply the benefits of a common currency for ASEAN.

The Fifth ACBF also discussed the future of the **ASEAN Swap Arrangement (ASA)**, an ASEAN financial arrangement which was first established under a Memorandum of Understanding signed on 5 August 1977 by the central banks of Indonesia, Malaysia, Philippines, Thailand and the Monetary Authority of Singapore. The objective of the ASA is to provide short-term liquidity to member countries facing a temporary balance of payments need. Under the present arrangement, the total credit available under the ASA is US$200 million, with each participating central bank or monetary authority being eligible to draw a maximum of US$80 million. It was agreed that the agreement be renewed for another one year period, pending a comprehensive review of the facility to identify and rectify its shortcomings, as well as to explore the benefits and feasibility of alternative arrangements. The Eighth Supplementary Agreement to the Memorandum of Understanding on the ASA was signed on 27 January 2000.

SEACEN

The Annual Conference of Governors of **South-East Asian Central Banks (SEACEN)** represents one of the earliest fora on regional surveillance. In addition to reviewing economic and financial developments, the Governors also reviewed the progress of activities of the SEACEN Centre and approved its budget and proposed programme for the new operating year. During the Thirty-Fourth Conference in Seoul, Korea, on 20-21 May 1999, the discussions among Governors focused on the lessons drawn from the recent crisis and the importance of closer international co-operation in building a new international financial architecture. Governors also considered it important for the SEACEN Research and Training Centre to strengthen and expand its training for financial supervisors to support ongoing efforts to strengthen the financial sector in SEACEN countries. The Governors agreed to a strategic review of the future role of the SEACEN Centre to ensure that it would effectively meet the changing needs of its membership, given the significant changes that had taken place in the recent period.

During their Thirty-Fifth Conference in Kuala Lumpur on 27-28 January 2000, SEACEN Governors discussed the preliminary report on the Strategic Review. The final report, which will be completed by May/June 2000, would set the future direction of the SEACEN Centre to effectively achieve its objectives in meeting the research and training needs of the regional central banks.

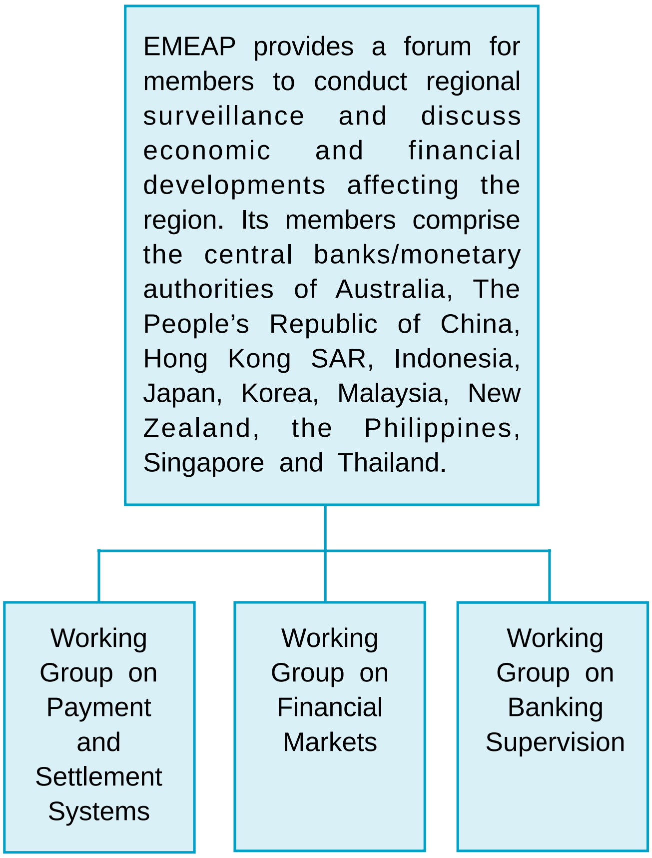
SEACEN was established to promote greater understanding of monetary, banking and economic development matters which are of interest to its member central banks and monetary authorities, through conferences and activities of its research and training centre. SEACEN members comprise the central banks and monetary authorities of Indonesia, Korea, Malaysia, Mongolia, Myanmar, Nepal, the Philippines, Singapore, Sri Lanka, Taiwan and Thailand.

In considering options to further enhance the role of the SEACEN Centre as a world-class centre for co-operation in research and training in central banking polices and operations, Governors encouraged the Centre to expand its collaborative training programmes through strategic alliances with other international and bilateral agencies. To further enhance SEACEN co-operation, the Governors agreed to expand the membership of the Board of Directors of the SEACEN Centre to include two additional members from other SEACEN central banks on a rotation basis.

In their deliberations on economic and financial matters, SEACEN Governors noted that the crisis-affected SEACEN economies recovered sooner than expected in 1999. The recovery was expected to be sustained in the year 2000 with stronger economic fundamentals in the medium term. While inflation would not be an issue despite higher GDP growth, Governors noted the need to be cautious and to persevere with policies to achieve growth with price stability while continuing with efforts aimed at strengthening the financial sector. The Governors emphasised the need for an orderly liberalisation of the capital account as part of the reform process. It was recognised that developments in the capital markets need to be monitored closely in view of the potentially destabilising implications. Governors also agreed to exchange views and assess the efficacy of inflation targeting in the conduct of monetary policy, given the different structure of the economies in the region.

EMEAP

During the year, BNM continued to actively pursue close co-operation with central banks and monetary authorities in the Asia-Pacific region through the **Executives' Meeting of East Asia and Pacific Central Banks (EMEAP)**. As with the previous year, three meetings were held (two at the Deputies' level and one at the Governors' level) during 1999. The Seventeenth EMEAP Deputies' Meeting was held in Melbourne, Australia, on 25 March 1999. This was followed by the Fourth EMEAP Governors' Meeting in Hong Kong SAR on 9 July 1999, and the Eighteenth EMEAP Deputies' Meeting in Tokyo, Japan, on 29 October 1999. The Nineteenth EMEAP Deputies' Meeting was held in Hong Kong SAR on 18 March 2000.



In general, the EMEAP meetings provided the opportunity for members to conduct regional surveillance and take stock of the progress of activities in the three working groups. BNM hosted the back-to-back meetings of the three working groups on 4-5 March 1999 in Kuala Lumpur.

Common themes in the EMEAP meetings convened in 1999 were deliberations on financial policy options during a crisis and the reform of the international financial architecture (IFA). In particular, at the Seventeenth EMEAP Deputies' Meeting, members discussed and agreed on a common position on the role of monetary policy in a crisis, as well as ways to better manage capital flows to avoid undue volatility. With regard to the former, it was agreed that the prescription of higher interest rates during the Asian crisis was not only ineffective, but also aggravated problems in the corporate and financial sectors. The meeting noted that more research was needed to identify the conditions where higher interest rates would work in restoring confidence. With reference to the latter, the meeting agreed that the use of capital controls might be beneficial in specific and exceptional circumstances. However, preference was for such controls to be market-based, specific, temporary, and in conjunction with appropriate domestic policies. Deputies also agreed that greater involvement by the private sector in resolving crises would help to attenuate the problem of moral hazard. Moreover, the role of Highly Leveraged Institutions (HLIs) in the recent crisis prompted calls for greater transparency from both the private and public sectors, including some form of regulation for the HLIs.

The discussion on IFA reforms at the Fourth EMEAP Governors' Meeting on 9 July 1999 also included a discussion of reform efforts in other fora such as the G-7 and the Financial Stability Forum (FSF). The meeting agreed on a common view which included the need for the private sector to match public sector transparency, the need for international co-operation to address the potentially destabilising impact of the activities of the HLIs on the financial systems of the small- and medium-sized open economies, and the importance of emerging market economies' involvement in the process of reforming the IFA. The EMEAP's views on these issues were conveyed to the IMF and the FSF. These issues were also discussed by EMEAP Governors with Mr. Andrew Crockett, General Manager of the BIS, at a special session on 10 July 1999. Mr. Crockett stressed that while the international financial system will remain market-based and that the global surveillance function will remain with the IMF, other aspects needed to be changed.

The EMEAP Governors also addressed issues pertaining to the preparedness of members in the face of the Year 2000 (Y2K) problem. Members were advised to prepare for possible liquidity shortages and upward pressure on interest rates as financial institutions and the general public demand more liquid funds in preparing for contingencies in the new Millennium. Members exchanged information and shared plans on managing year-end financial operations to cope with any Y2K problem.

At the Eighteenth Deputies' Meeting in Tokyo on 29 October 1999, EMEAP Deputies agreed on a study on exchange rate regimes to be initiated by the Bank of Japan. The study, when completed, would be submitted to other international organisations, such as the IMF.

A new initiative under the EMEAP Working Group on Financial Markets was the establishment of a forum among EMEAP members to enable an informal, and where appropriate, technical dialogue on developments in foreign exchange markets. The first Regional Foreign Exchange Markets Monitoring Meeting was held on 2 March 2000 in Hong Kong SAR. Meanwhile, the Working Group on Banking Supervision introduced the Six Guidance Notes regarding the definition, classification and disclosure of problem loans. The objective of the Guidance Notes is to try to facilitate the alignment of practices and standards in respect of problem loans by EMEAP members. While adoption of the Guidance Notes is not compulsory, members were encouraged to work towards these common standards.

Technical Assistance and Information Exchange

As part of the Bank's policy to share its expertise with interested parties, BNM continued to provide technical assistance to foreign public and private sector institutions in 1999. The assistance was in the form of training and attachment programmes, study visits, and briefings on various aspects of central banking in Malaysia. During the year, the Bank received 48 foreign delegations for study visits. The delegations were from the central banks, government agencies and private sector organisations of Bahrain, Brazil, Brunei Darussalam, Fiji, India, Indonesia, Kingdom of Lesotho, Lao PDR, Namibia, Papua New Guinea, Peoples' Republic of China, Republic of Djibouti, Republic of Guinea, Saudi Arabia, Sri Lanka, Sudan, Thailand, Vietnam, and Zimbabwe. Briefings to the study groups covered various aspects of central banking, including money market operations, the development of Islamic banking in Malaysia and policy initiatives in response to the Asian crisis. In addition, BNM participated in the Malaysian technical assistance programme to the Kyrgyz Republic. The programme, under the Special Joint Malaysian-Kyrgyz Commission, was in its second phase of monitoring the implementation of recommendations contained in an earlier joint study. The recommendations covered all aspects of economic development policies for the Kyrgyz Republic, including the principles to guide monetary policy formulation.

A team of officers from The Reserve Bank of India and Bank of Thailand visited BNM to study Malaysia's bank supervision and payment systems respectively. In addition, briefings on the latest developments in the Malaysian economic and financial system were conducted for delegations from Finland, France, Japan, Singapore, the United Kingdom and the United States of America. The Bank also offered 10 places at the Central Banking Course conducted by the Bank's Human Resource Development Centre to foreign participants under the Malaysian Technical Co-operation Programme. The participants were from the central banks of Benin, Brazil, Ghana, Indonesia, Jamaica, Namibia, Sri Lanka and Vietnam.

6 Organisation and Personnel

Staff and Organisation

The Board of Directors extends its deepest appreciation to all Bank staff for their continuous hard work, dedication and commitment in the year 1999. The Board also hopes that as we progress towards the next millennium, all Bank staff would continuously strive to work harder so as to realise the Bank's vision in further developing the financial system and the economy.

Developments in Human Resource Management

In line with the Bank's Recognition Programme which was approved in 1999, the Bank gave away prizes to winners of the various formal awards under this programme during the Bank's annual dinner held on 20 November 1999. Winners were selected for six of the eight awards, namely Excellent Performance, Teamwork, Quality Service, Innovation, Sports/Social and Academic Achievement. There were no winners for the Leadership and Occupational Safety & Health awards. In the year 2000, the Bank intends to enhance the culture of recognition by encouraging and facilitating the habit of giving recognition at the departmental and individual levels.

It has been the Bank's Mission to develop and maintain a committed workforce that is highly competent, proactive and sensitive to the changing needs of the industry. In line with the said Mission, the Bank has approved the detailed implementation approach of the Succession Planning programme, aimed at building a group of qualified people to lead the future direction of the organisation. For a start, the Bank will be implementing the programme on key positions.

In the area of human resource development, the Bank continued with the programmes to improve staff performance, productivity and competency. Apart from technical programmes in banking, finance, statistics and economics, the Bank had also provided training in primary skills, computer literacy and occupational safety and health. Recognising the need to enhance the supervisory skills of new managers, a programme on "Managing Others" was introduced in 1999. The programme, which focused on people skills, was specially designed for new managers to enable them to manage their staff more effectively. The number of induction programmes conducted for new recruits increased significantly to cater for the large intake of new recruits in 1999. The number of training man-days totalled 12,881 for the year as compared to 12,982 man-days in 1998.

In recognising the efforts and contribution of staff from line departments to staff training, a Bank's faculty gathering was organised for the first time by the Human Resource Development Centre. The faculty gathering was held specially as an acknowledgement of the efforts of staff from the various departments who had participated in the task of enhancing the quality of the Bank's manpower. The gathering served to not only encourage present trainers to continue to share their invaluable knowledge and experiences with others but also to encourage other staff to contribute to training and thereby promoting a learning organisation within the Bank.

Awards

The Board congratulates the four Assistant Governors, Dato' Mohamad Daud bin Haji Dol Moin on being conferred the Darjah Dato Paduka Tuanku Jaafar (DPTJ) on the occasion of the birthday of His Royal Highness, Tuanku Yang di-Pertuan Besar Negeri Sembilan on 19 July 1999, Dato' Huang Sin Cheng on being conferred the Darjah Setia Pangkuan Negeri (DSPN) on the occasion of the birthday of His Excellency, the Yang di-Pertua Negeri Pulau Pinang on 10 July 1999, Datuk Dr. Awang Adek Hussin on being conferred the Darjah Mulia Seri Melaka (DMSM) on the occasion of the birthday of His Excellency, the Yang di-Pertua Negeri Melaka on 16 October 1999 and the Johan Setia Mahkota (JSM) on the occasion of the birthday of His Majesty, the Yang di-Pertuan Agong on 5 June 1999 and Encik Mohd Razif bin Abdul Kadir on being conferred the Pingat Mahkota Perak (PMP) on the birthday of His Royal Highness, the Sultan of Perak on 19 April 1999.

The Board extends its congratulations to Encik Che Sab bin Ahmad on being conferred the Bintang Cemerlang Negeri (BCN), Encik Tan Ewe Lee, the Pingat Jasa Kebaktian and Puan Azlina binti Haji Omar, the Pingat Jasa Masyarakat (PJM) on the occasion of the birthday of His Excellency, the Yang di-Pertua Negeri Pulau Pinang on 10 July 1999 and Encik Sa Wai @ Boon Chock on being conferred the Ahli Mangku Negara (AMN) on the birthday of His Majesty, the Yang di-Pertuan Agong on 5 June 1999.

The Board would also like to congratulate all 13 staff who received the long service awards upon the completion of 20 and 30 years of dedicated service in the Bank.

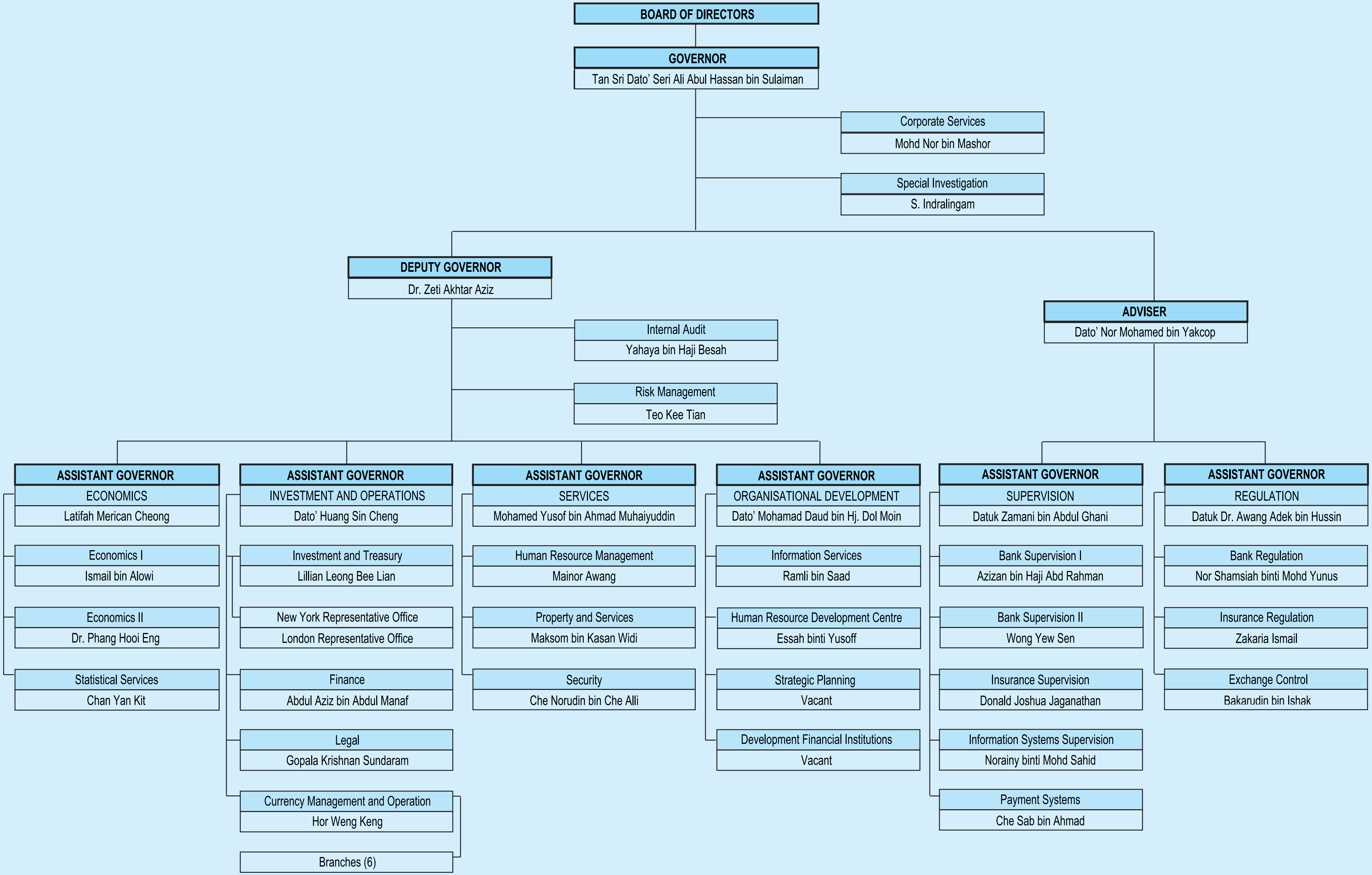
Retirement

The Board wishes to place on record its appreciation and gratitude to the 18 retirees who have rendered loyal and dedicated service to the Bank. The staff who retired from the services of the Bank in 1999 were Puan Chin Soon Ling, Encik Long Kim Swee (Bank Supervision II Department), Encik Mohd Halid bin Ahmad (Payment Systems Department), Encik Md Radzi bin Haji Kechik, Encik Godfrey Jambu, Encik Cheong Swee Kong @ Chong Swee Kong (Exchange Control Department), Encik Ng Tee Tee, Encik Ismi bin Saari (Currency Management and Operation Department), Cik Zawiah binti Ismail (Statistical Services Department), Encik Mohd Shukri bin Abdullah (Kota Kinabalu Branch), Encik Kamarul Bahrin bin Alias, Encik Khalid bin Ahmad (Security Department), Encik Usop bin Roslie, Encik Ismail bin Paie (Kuching Branch), Encik Joachim Wong Tet Sin (Pulau Pinang Branch), Encik Marimuthu s/o Ratnasamy (Johor Bahru Branch), Encik Mohd Ikram bin Ahmad (Finance Department) and Encik Sedana Omar bin Md Yusof (Corporate Services Department).

Manpower

As at the end of 1999, the Bank had a total staff complement of 1,764, representing staff in the Head Office, six branches, two representative offices in London and New York and the Human Resource Development Centre in Petaling Jaya.

BANK NEGARA MALAYSIA
ORGANISATION STRUCTURE



Annual Accounts

CERTIFICATE OF THE AUDITOR GENERAL ON THE ACCOUNTS OF BANK NEGARA MALAYSIA FOR THE YEAR ENDED 31 DECEMBER 1999

I have audited the Balance Sheet of Bank Negara Malaysia as at 31 December 1999 and Profit and Loss Appropriation Account for the year then ended. These financial statements are the responsibility of the Bank Negara Malaysia's management. My responsibility is to express an opinion on these financial statements based on my audit.

2. I conducted my audit in accordance with the Audit Act 1957, in conformity with the International Standards on Auditing. These standards require that I plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used as well as evaluating the overall financial statement presentation.

3. In my opinion, the financial statements give a true and fair view of the state of financial affairs of Bank Negara Malaysia as at 31 December 1999 and of the results of its operations for the year then ended.

(DATUK DR. HADENAN BIN ABDUL JALIL)
AUDITOR GENERAL

KUALA LUMPUR

STATEMENT BY DIRECTORS

We, Tan Sri Dato' Seri Ali Abul Hassan bin Sulaiman and Datuk Oh Siew Nam, being the Chairman and one of the Directors of Bank Negara Malaysia, do hereby state that in the opinion of the Board, the accompanying Balance Sheet and Profit and Loss Appropriation Account together with the Notes thereto, are drawn up so as to give a true and fair view of the state of affairs of Bank Negara Malaysia as at 31 December 1999 and of the results of operations for the year ended on that date.

On behalf of the Board,

TAN SRI DATO' SERI ALI ABUL HASSAN BIN SULAIMAN
CHAIRMAN

15 MARCH 2000
KUALA LUMPUR

On behalf of the Board,

DATUK OH SIEW NAM
DIRECTOR

15 MARCH 2000
KUALA LUMPUR

DECLARATION BY THE OFFICER PRIMARILY RESPONSIBLE FOR THE ACCOUNTS OF BANK NEGARA MALAYSIA

I, Abdul Aziz Abdul Manaf, being the officer primarily responsible for the accounts of Bank Negara Malaysia, do solemnly and sincerely declare that the accompanying Balance Sheet and Profit and Loss Appropriation Account together with the Notes thereto, are to the best of my knowledge and belief, correct and I make this solemn declaration conscientiously believing the same to be true, and by virtue of the provisions of the Statutory Declarations Act, 1960.

Subscribed and solemnly declared)
by the abovenamed at Kuala Lumpur)
this 15th day of March 2000.)

Before me,

Balance Sheet as at 31 December 1999

LIABILITIES		Note	1999 R M	1998 R M
Authorised Capital	RM200,000,000			
Paid-up Capital		2	100,000,000	100,000,000
General Reserve Fund		3	4,992,598,550	3,580,341,905
Other Reserves		4	27,407,427,022	28,342,866,826
Currency in Circulation			30,483,108,998	20,547,397,698
Deposits:				
Commercial Banks, Finance Companies and Merchant Banks			61,343,596,073	34,650,553,608
Federal Government			18,513,468,828	25,281,306,084
Others		5	2,049,180,270	9,079,320,115
Bank Negara Bills/Bonds			378,819,900	3,760,100
Allocation of Special Drawing Rights		6	724,385,851	743,978,271
Other Liabilities			1,055,028,275	2,380,298,386
			147,047,613,767	124,709,822,993

Profit and Loss Appropriation Account for the Year Ended 31 December 1999

	1999 R M	1998 R M
Transfer to General Reserve Fund	753,934,360	367,909,804
Amount Payable to Federal Government	500,000,000	1,000,000,000
	1,253,934,360	1,367,909,804

Notes on the following pages form part of these accounts.

ASSETS	Note	1999 RM	1998 RM
Gold and Foreign Exchange		113,765,926,146	96,264,938,326
International Monetary Fund Reserve Position		3,168,224,524	2,379,240,022
Holdings of Special Drawing Rights		330,338,578	793,875,612
Malaysian Government Papers	7	94,380,064	1,072,364,460
Deposits with Financial Institutions		2,134,841,000	2,512,101,000
Loans and Advances		7,029,644,859	5,773,389,590
Deferred Expenditure	8	2,282,883,663	2,853,604,578
Other Assets	9	18,241,374,933	13,060,309,405
		147,047,613,767	124,709,822,993

	1999 RM	1998 RM
Net Profit	1,253,934,360	1,367,909,804
	1,253,934,360	1,367,909,804

Notes To The Accounts - 31 December 1999

1. Accounting Policies

(a) Gold, Securities and Investments
Gold, securities and investments are stated at cost and provisions have been made for diminution in value as at 31 December 1999.

(b) Foreign Currency Translation
Assets and liabilities in foreign currencies have been revalued into ringgit at rates of exchange ruling on the balance sheet date. Transactions in foreign currencies during the year have been translated into ringgit at rates of exchange ruling on value dates.

The US dollar equivalent of the International Reserves comprising Gold and Foreign Exchange, International Monetary Fund Reserve Position and Holdings of Special Drawing Rights as at 31 December 1999 was US$30,859.1 million.

2. Paid-up Capital
The entire issued and paid-up capital of RM100 million is owned by the Government of Malaysia.

3. General Reserve Fund

	1999	1998
	RM	RM
As at 1 January	3,580,341,905	3,212,432,101
Net Profit	753,934,360	367,909,804
Transfer	658,322,285	–
As at 31 December	4,992,598,550	3,580,341,905

4. Other Reserves
Other reserves comprise the Exchange Rate Fluctuation Reserve, the Investment Fluctuation Reserve and the Contingency Reserve.

5. Deposits - Others
A substantial part of these deposits comprises deposits from Federal Statutory Authorities.

6. Allocation of Special Drawing Rights
International Monetary Fund (IMF) member countries are allocated Special Drawing Rights (SDR) in proportion to their subscriptions to the IMF. The allocation represents a dormant liability of the Bank to the IMF, against which assets are received in SDR from the IMF. The net cumulative of the allocation in SDR amounted to SDR139,048,000.

7. Malaysian Government Papers

	1999 RM	1998 RM
Malaysian Government Securities	91,210,064	132,549,460
Government Investment Certificates	3,170,000	939,815,000
	94,380,064	1,072,364,460

8. Deferred Expenditure

This represents the net deficiency arising from foreign exchange transactions in 1993. The Government has undertaken to make good this deficiency as and when required to do so by the Bank. The amount outstanding is being amortised over a period of 10 years, beginning from 1994.

9. Other Assets

Other assets include investments in shares and bonds of RM15,845,184,391 acquired under section 30(1)(j) and section 30(1)(oo)(i) of the Central Bank of Malaysia Act 1958 (Revised-1994).

10. Contingent Liabilities

Total contingent liabilities as at 31 December 1999 amounted to RM4,510,538,680, which represents the obligation of the Bank to pay in full, in SDR or other convertible currencies, the amount of Malaysia's quota in the IMF under the Articles of Agreement.

Annex

Contents

Exchange Control Policies

Malaysia continues to implement the selective exchange control policies introduced since 1 September 1998, albeit with some major modifications to enhance their effectiveness and overcome administrative difficulties. Among the major changes introduced in 1999 were the following:

(a) 15 February 1999
Introduction of the Levy System
- The rule requiring non-residents to hold their principal sum for portfolio investments for at least 12 months in Malaysia was relaxed. Capital and profits of the portfolio investments were allowed to be repatriated at any time, subject only to payment of the appropriate levy of between 10% and 30%.

(b) 21 September 1999
Standardising the Levy System
- On 21 September 1999, the rate of levy was standardised to only 10% of profits repatriated.

(c) 15 May 1999
Simplification of Travellers' Declaration Form (TDF)
- Resident and non-resident travellers continue to be required to declare whether they are carrying currencies within the limits permitted, but need to state the exact amounts only if they exceed the permitted limit.

The exchange control policies of Malaysia are applied uniformly to transactions with all countries except Israel and the Federal Republic of Yugoslavia (Serbia and Montenegro) for which special restrictions apply. The exchange control policies, in general, are aimed at monitoring the settlement of payments and receipts as well as encouraging the use of the country's financial resources for productive purposes in Malaysia. For monitoring and compilation of balance of payments statistics, residents are required to complete statistical forms, Form P or Form R, for each payment and receipt of more than RM10,000 vis-a-vis non-residents.

The following are the main exchange control requirements:

I Current Account Transactions

(a) Payment for the Import of Goods and Services
- There are no restrictions on payments, irrespective of amount, to non-residents for the import of goods and services. All payments for the import of goods and services, however, must be made in foreign currency.

(b) Export Proceeds
- All export proceeds are required to be repatriated back to Malaysia in accordance to the payment schedule specified in the sales contract, which in any case should not exceed six months from the date of export.
- The export proceeds must be received in foreign currency and must be sold for ringgit or retained in approved foreign currency accounts with onshore commercial banks, up to an aggregate overnight limit of between US$1 million and US$10 million.

(c) Import and Export of Currency by Travellers

- All travellers are required to complete a Travellers Declaration Form at the Immigration checkpoint or carry a valid Travellers Declaration Pass upon their exit or arrival at Malaysia, irrespective of the amount carried.

- Resident and non-resident travellers are allowed to carry ringgit notes up to RM1,000 on person or in their baggage, upon arrival at or departure from Malaysia. The limit includes the demonetised RM1,000 and RM500 notes.

- A resident traveller is freely allowed to take out foreign currency notes, including traveller's cheques, up to the equivalent of RM10,000 per person.

- A non-resident traveller is also allowed to take out foreign currency notes, including traveller's cheques, up to the amount brought into Malaysia.

- Resident and non-resident travellers are allowed to bring in any amount of foreign currency notes, including traveller's cheques, upon their arrival in Malaysia.

- Prior permission of the Controller of Foreign Exchange (the Controller) is required for:
  - a traveller to export or import ringgit notes, or to export foreign currency exceeding the permitted limits; and
  - any person other than a traveller to export or import foreign currency or ringgit notes irrespective of amount.

I Capital Account Transactions

(a) Foreign Direct Investment

- Foreign direct investors are freely allowed to repatriate their investment, including capital, profits and dividends, without being subject to any levy.

(b) Investment Abroad by Residents

- Residents are required to seek prior approval from the Controller to remit funds in excess of RM10,000 for overseas investment purposes.

(c) External Credit Facilities from Non-Residents

Credit Facilities in Foreign Currency

- Residents are freely permitted to obtain credit facilities in foreign currency up to the equivalent of RM5 million. Any amount exceeding the permitted limit would require the prior approval of the Controller.

- There is also no restriction for repayment of credit facilities obtained from non-residents as long as such credit facilities have been obtained in accordance to the relevant exchange control rules.

Credit Facilities in Ringgit

- Residents are not allowed to obtain credit facilities in ringgit from non-residents without the prior approval of the Controller.

(d) Extension of Credit Facilities to Non-Residents

Credit Facilities in Foreign Currency

- Commercial banks are freely allowed to extend credit facilities in foreign currency to non-residents for purposes other than financing the acquisition or development of immovable property in Malaysia.

Credit Facilities in Ringgit

- Commercial banks participating in the Institutional Settlement Services provided by SCAN are allowed to extend intra-day overdraft facility of up to RM200 million and overnight limit up to RM5 million in aggregate to non-resident stockbrokers using the ISS.

- Banking institutions and other non-bank residents are allowed to extend credit facilities in ringgit to non-residents who are working in Malaysia to finance up to 60% of the purchase price or construction cost of a residential property in Malaysia for their own accommodation.

- In addition, banking institutions are also allowed to extend credit facilities in ringgit up to the aggregate of RM200,000 to a non-resident for purposes other than to finance the acquisition or development of immovable property in Malaysia. Prior approval of the Controller is required for the extension of credit facilities exceeding the limit.

- Resident stockbroking companies are allowed to extend margin financing facilities to non-resident clients for the purchase of shares listed on the Kuala Lumpur Stock Exchange (KLSE), subject to the compliance with the rules imposed by the KLSE.

(e) Portfolio Capital

- Non-resident portfolio investors are encouraged to hold their investments over a long term in Malaysia. The rule requiring non-residents to hold their principal sum for portfolio investment for at least 12 months in Malaysia was relaxed on 15 February 1999. Capital and profits of the portfolio investments were allowed to be repatriated at any time, subject only to payment of the appropriate levy of between 10% and 30%:

- For Funds brought into Malaysia before 15 February 1999
  - Principal repatriated within the one-year holding period was subject to a levy payment of between 10% and 30%, depending on the duration of holding the funds in Malaysia.
  - There was no levy imposed on the repatriation of profits.

- For Funds brought into Malaysia on or after 15 February 1999
  - Principal amount repatriated is not subject to levy.
  - However, profits repatriated are subject to two-tier levy:
    - Profits made and repatriated within one year are subject to a levy of 30%.
    - Profits made and repatriated after one year are subject to a levy of 10%.

- On 21 September 1999, the rate of levy was standardised to only 10% of profits repatriated.

- No levy is imposed on the repatriation of proceeds from the sale of investments in immovable property (for both principal capital and profits).

III Credit Facilities in Ringgit to Non-Resident Controlled Companies

- Non-Resident Controlled Companies (NRCCs) operating in Malaysia are freely permitted to obtain from domestic sources:
  - Credit facilities of up to RM10 million per corporate group;
  - Any amount of forward exchange contracts for trade purposes, performance guarantees and short-term trade financing facilities; and
  - Any amount of guarantees to secure the repayment of borrowings, subject to the submission of information on the guarantees to the Controller.

- Of the total amount of credit facilities obtained from banking institutions, at least 60% must be from Malaysian-owned banking institutions.

- For borrowing in excess of RM10 million in the aggregate, NRCCs are required to obtain prior approval. The NRCCs are also required to ensure that the ratio between their domestic borrowing and eligible capital funds is less than three times.

IV Foreign Currency Accounts of Residents

- Resident exporters are permitted to open foreign currency accounts with onshore commercial banks to retain export proceeds in foreign currency of between US$1 million and US$10 million, depending on their export receipts:

Aggregate Overnight Limit	**Average Monthly Export Receipts**
US$10 million	Exceeding RM20 million
US$5 million	Exceeding RM10 million, up to RM20 million
US$3 million	Between RM5 million and RM10 million
US$1 million	Less than RM5 million

- Resident companies with domestic credit facilities are permitted to open foreign currency accounts to retain foreign currency receivables, other than export proceeds, up to aggregate overnight limits of:
  - US$0.5 million with commercial banks in Malaysia; and
  - US$0.5 million with Labuan offshore banks.

- Resident companies with no domestic credit facilities are permitted to open foreign currency accounts with onshore commercial banks to retain foreign currency receivables other than export proceeds with no overnight limit specified by Bank Negara Malaysia.

- Resident individuals are also allowed to open foreign currency accounts solely to facilitate education and employment overseas up to an aggregate overnight limit of US$100,000 with commercial banks in Malaysia, US$100,000 with Labuan offshore banks and US$50,000 with overseas banks.

V Foreign Currency Accounts of Non-Residents

- Commercial banks and merchant banks are freely allowed to open foreign currency accounts for non-residents.

- There are no restrictions on the inflow and outflow of funds through the foreign currency accounts of non-residents.

VI External Accounts of Non-Residents

- Banking institutions are freely allowed to open accounts in ringgit known as External Accounts (or Special External Accounts for those opened on or after 15 February 1999) for non-residents.

- With effect from 21 September 1999, the sources of funds of the External Accounts may be from the sale of ringgit instruments, securities or other assets in Malaysia, obtained using funds already in Malaysia before 15 February 1999; salaries, wages, rental, commissions, interests or dividends.

- The uses of funds in the External Accounts are restricted to the following purposes:
  - Purchase of immovable property in Malaysia;

- Placement of deposits;
- Payment of administrative and statutory expenses in Malaysia;
- Payment for goods and services used in Malaysia; and
- Granting of loans and advances to staff in Malaysia according to the terms and condition of services.

- For the Special External Accounts, the source of funds may be from:
  - Sale of ringgit instruments, securities or other assets in Malaysia, irrespective of the source of funding for the purchases;
  - Salaries, wages, rental, commissions, interests, profits or dividends;
  - Sale of foreign currency to an authorised dealer in Malaysia; and
  - Transfer from External Accounts of the same account holders.

- The funds in the Special External Accounts may be used for the same purposes as those in External Accounts. In addition, the funds in the Special External Accounts may be used to purchase ringgit securities.

- Prior approval is required for transfer of funds between External Accounts and between Special External Accounts of different account holders and for uses of funds other than the permitted purposes.

- There are no restrictions on the operations of the External Accounts of non-residents working in Malaysia, embassies, consulates, high commissions, supranational or international organisations recognised by the Malaysian Government.

VII Designated External Accounts

- Commercial banks are allowed to open ringgit accounts known as Designated External Account (DEA) for non-residents, solely for the purpose of facilitating trading at the Commodity and Monetary Exchange of Malaysia and the Kuala Lumpur Options and Financial Futures Exchange. Funds in the DEA are not subject to a levy on repatriation.

VIII Special Status Granted to Selected Companies

(a) Offshore Entities in Labuan International Offshore Financial Centre

- Entities setup in Labuan International Offshore Financial Centre (IOFC) are declared as non-residents for exchange control purposes. Offshore entities in Labuan IOFC are freely allowed to deal in foreign currency with non-residents.

- Licensed Offshore Banks in Labuan are permitted to receive payments in ringgit from residents arising from fees, commissions, dividends, or interest from the deposit of funds.

- Offshore Insurance Entities in Labuan are also permitted to use their ringgit accounts for the payment of claims and to receive insurance premiums arising from the reinsurance of domestic insurance business.

- All offshore entities are freely allowed to maintain ringgit accounts with onshore banks to facilitate defraying of statutory and administrative expenses in Malaysia.

(b) Multimedia Super Corridor Companies

- Companies operating in Multimedia Super Corridor (MSC) are given exemption from exchange controls upon the companies being awarded the MSC status. They are only required to submit statistics for monitoring purposes.

(c) Approved Operational Headquarters

- Approved Operational Headquarters (OHQs) are allowed to open foreign currency accounts with commercial banks in Malaysia to retain export proceeds up to a maximum aggregate overnight limit of US$10 million, irrespective of the amount of export receipts.

- OHQs are also allowed to open foreign currency accounts with commercial banks in Malaysia, Labuan offshore banks or overseas banks for crediting foreign currency receivables, other than export proceeds, with no restriction on overnight limit.

- OHQs are permitted to obtain any amount of foreign currency credit facilities from commercial banks in Malaysia, and from any non-residents for their own use or to on-lend to their related companies overseas.

(d) Approved International Procurement Centres

- Approved International Procurement Centres (IPCs) are allowed to retain any amount of export proceeds in foreign currency accounts maintained with onshore commercial banks.

- IPCS are also allowed to enter into forward exchange contracts wtih onshore commercial banks to hedge exchange risk based on the projected volume of trade.

Funds Administered/Funded by Bank Negara Malaysia: Fund Utilisation

Funds	Date Established	Fund Allocation (RM m)	Number of Applications Approved: Total as at end 1998	Number of Applications Approved: Total as at end 1999	Number of Applications Approved: Annual Change	Amount Approved (RM m): Total as at end 1998	Amount Approved (RM m): Total as at end 1999	Amount Approved (RM m): Annual Change	Outstanding as at end 1999 (RM m)
New Entrepreneurs Fund	12-Dec-89	1,250[1]	2,186	2,527	341	1,064	1,214	150	681
Ship Financing Facility	30-Oct-92	600	32	34	2	547	549	2	495
Fund for Food	04-Jan-93	700	1,689	2,365	676	493	638	145	355
Bumiputera Industrial Fund	04-Jan-93	100	101	99	–2[2]	99	98	–1[2]	75
Fund for Small and Medium Industries	02-Jan-98	1,850[1]	873	4,216	3,343	882	3,019	2,137	1,634
Rehabilitation Fund for Small and Medium Industries	23-Nov-98	500	1	282	281	0.1	251	250.9	148

Terminated Funds	Date Established	Date Terminated	Fund Allocation (RM m)	Number of Applications Approved: Total as at end 1998	Number of Applications Approved: Total as at end 1999	Number of Applications Approved: Annual Change	Amount Approved (RM m): Total as at end 1998	Amount Approved (RM m): Total as at end 1999	Amount Approved (RM m): Annual Change	Outstanding as at end 1999 (RM m)
Enterprise Rehabilitation Fund	06-Feb-88	01-Jan-91	500	761	763	2[3]	870	880	10[3]	126
Abandoned Housing Projects Fund	18-Jun-90	29-Feb-92	600	74	74	0	331	331	0	84
Fund to Accelerate the Construction of Low-Cost Houses	29-Oct-93	31-Oct-95	500	58	54	–4[2]	379	358	–21[2]	0
Special Fund for Tourism	10-Mar-90	31-Dec-97	200[1]	211	200	–11[2]	239	219	–20[2]	82
Special Scheme for Low and Medium Cost-Houses	01-May-98	04-Aug-99	1,000[4]	33	136	103	241	937	696	250

[1] Revolving funds.
[2] Approval withdrawn by bank/applicant.
[3] Due to additional funding requirements.
[4] Initial allocation was RM2 billion. It was reduced to RM1 billion in 1999.

Bilateral Payments Arrangements (BPA) Between Bank Negara Malaysia and Central Banks of Other Countries

Central Bank of	Model	Date of Agreement	Total Trade Between Partner Countries (RM million)	
			1987	1999
Pakistan	POCPA	6 Aug.1992	468.5	2,164.0
Myanmar	POCPA	21 Jan.1994	53.9	1,108.4
Iraq	POCPA	28 Feb.1993 28 Feb.1995 28 Feb.1996	131.9	63.8
Iran	POCPA Iranian	8 Feb.1994 8 Aug.1988	46	521.1
Bosnia Herzegovina	POCPA Iranian	13 Nov.1996 13 Nov.1996	n.a	0.7
Algeria	POCPA ALADI	14 June 1992 31 Jan.1992	3.8	104.1
Albania	ALADI	24 Jan.1994	0.2	2.6
Argentina	ALADI	3 Dec.1993	104.9	1,043.9
Chile	ALADI	21 June 1991	120.9	686.4
Lao PDR	ALADI	16 April 1994	0.1	5.2
Mexico	ALADI	24 Sep.1990	37.6	1,340.9
Peru	ALADI	13 Nov.1991	5.4	129.8
Romania	ALADI	20 May 1991	14.8	66.2
Seychelles	ALADI	21 Sep.1992	1.1	19.5
Tunisia	ALADI	25 Nov.1992	3.5	95.8
Turkmenistan	ALADI	30 May 1994	n.a	7.2
Uzbekistan	ALADI	28 June 1993	n.a	14.4
Venezuela	ALADI	3 Aug.1990	6.5	56.2
Vietnam	ALADI	29 Mar.1993	43.5	2,405.8
Zimbabwe	ALADI	7 June 1991	15.1	34.3

Central Bank of	Model	Date of Agreement	Total Trade Between Partner Countries (RM million)	
			1987	1999
Sudan	Revolving Credit POCPA (Counter Trade)	4 Jan.1992 16 Apr.1992 16 Sep.1992 18 Dec.1993 11 Oct.1996 23 July 1999	21.5	113.4
Botswana	Iranian	6 June 1991	n.a	n.a.
Fiji	Iranian	12 Oct.1991	67.8	67.0
Mozambique	Iranian	27 Apr.1991	46.8	10.4
Cuba	POCPA	26 Mar.1998	8.3	1.5
Philippines	ALADI	11 July 1998	1,185.8	11,141.9

Note:

ALADI Model : Each central bank pays its own exporter in the domestic currency and settles, on a periodic basis (not exceeding 90 days), the net difference with the other central banks in US dollar.

Iranian Model : Each central bank guarantees payments of its own importers.

Palm Oil Credit and Payments Arrangement (POCPA) : Created to promote the export of Malaysian palm oil to other developing countries. The importation is on a deferred payment basis.

Revolving Credit : The importation of goods is limited to the credit limit agreed by both parties on a deferred payment basis.

n.a. not available

Source: Bank Negara Malaysia and Department of Statistics

Licensed Banking Institutions (as at 31 December 1999)

Commercial Banks

1. ABN AMRO Bank Berhad
2. Arab-Malaysian Bank Berhad
3. Ban Hin Lee Bank Berhad
4. Bangkok Bank Berhad
5. Bank of America Malaysia Berhad
6. Bank of Tokyo-Mitsubishi (Malaysia) Berhad
7. Bank Utama (Malaysia) Berhad
8. BSN Commercial Bank (Malaysia) Berhad
9. Bumiputra-Commerce Bank Berhad*
10. Citibank Berhad
11. Deutsche Bank (Malaysia) Berhad
12. EON Bank Berhad
13. Hock Hua Bank Berhad
14. Hong Leong Bank Berhad
15. HSBC Bank Malaysia Berhad
16. International Bank Malaysia Berhad
17. Malayan Banking Berhad
18. Multi-Purpose Bank Berhad
19. OCBC Bank (Malaysia) Berhad
20. Oriental Bank Berhad
21. Overseas Union Bank (Malaysia) Berhad
22. Perwira Affin Bank Berhad
23. PhileoAllied Bank (Malaysia) Berhad
24. Public Bank Berhad
25. RHB Bank Berhad
26. Sabah Bank Berhad
27. Southern Bank Berhad
28. Standard Chartered Bank Malaysia Berhad
29. The Bank of Nova Scotia Berhad
30. The Chase Manhattan Bank (M) Berhad
31. The Pacific Bank Berhad
32. United Overseas Bank (Malaysia) Berhad
33. Wah Tat Bank Berhad

Islamic Banks

1. Bank Islam Malaysia Berhad
2. Bank Muamalat Malaysia Berhad*

* Formerly known as Bank of Commerce Berhad (BOC). On 1 October 1999, BOC was renamed Bumiputra-Commerce Bank Berhad following its absorption of the conventional assets and liabilities of Bank Bumiputra Malaysia Berhad (BBMB). BBMB remains involved exclusively in the Islamic banking sector under the name of Bank Muamalat Malaysia Berhad.

Finance Companies

1. Advance Finance Berhad
2. Affin Finance Berhad*
3. Arab-Malaysian Finance Berhad
4. Asia Commercial Finance (M) Berhad
5. Bolton Finance Berhad
6. BSN Finance Berhad
7. Bumiputra-Commerce Finance Berhad
8. Cempaka Finance Berhad
9. City Finance Berhad
10. Credit Corporation (Malaysia) Berhad
11. Delta Finance Berhad
12. EON Finance Berhad
13. Hong Leong Finance Berhad
14. Interfinance Berhad
15. Kewangan Bersatu Berhad
16. Mayban Finance Berhad
17. MBf Finance Berhad
18. Perdana Finance Berhad
19. Perkasa Finance Berhad
20. Public Finance Berhad
21. Sabah Finance Berhad
22. SimeFinance Berhad
23. United Merchant Finance Berhad

* Merged with Asia Commercial Finance (M) Berhad and ceased to be a licensed finance company with effect from 1 January 2000.

Merchant Banks

1. Amanah Merchant Bank Berhad
2. Arab-Malaysian Merchant Bank Berhad
3. Aseambankers Malaysia Berhad
4. BSN Merchant Bank Berhad
5. Bumiputra Merchant Bankers Berhad
6. Commerce International Merchant Bankers Berhad
7. Malaysian International Merchant Bankers Berhad
8. Perdana Merchant Bankers Berhad
9. Perwira Affin Merchant Bank Berhad
10. RHB Sakura Merchant Bankers Berhad
11. Sime Merchant Bankers Berhad
12. Utama Merchant Bank Berhad

Credit Guarantee Corporation Malaysia Berhad

The Credit Guarantee Corporation Malaysia Berhad (CGC) was incorporated in July 1972 to provide guarantee cover to the banks for designated loans to small-scale enterprises (SSEs). The various schemes to promote access to institutional credit for SSEs undertaken by CGC includes the Small Entreprenuers Fund, the New Principal Guarantee Scheme and the Flexible Guarantee Scheme which was introduced on 1 March 1999.

Small Entreprenuers Fund (SEF)

In collaboration with the Ministry of Entrepreneur Development, CGC launched the SEF in 1998. The SEF offers small loans ranging from RM2,000 to RM20,000 (increased to RM50,000 in 1999) to the smaller entrepreneurs. The SEF replaced the previous Loan Fund for Hawkers and Petty Traders (launched in 1992) and the Association Special Loan Scheme (also launched in 1992), both managed by CGC, which were wound down in 1998. Each SEF loan is fully funded by the CGC and features bi-weekly repayments which incorporate a service charge to the borrower at the rate of 6% per annum. CGC also provides 100% guarantee on the first RM20,000 loan amount and 80% guarantee on the remaining loan balance. These loans are channelled through 16 participating financial institutions which would carry out the necessary credit assessment although credit decisions ultimately rest with CGC which bears the credit risks.

In view of the overwhelming demand for SEF loans, the total allocation for SEF was gradually increased from RM90 million to RM540 million by July 1999. As at end-1999, a total of 26,836 applications for loans amounting to RM296.6 million had been approved under the SEF scheme, of which RM233.2 million (78.6%) was extended to Bumiputera borrowers. However, the number of loan applications in hand and being processed by CGC as at end-1999 amounted to RM247.6 million. If these applications were approved, the SEF fund would have been fully utilised. Since 1 January 2000, CGC has stopped receiving new applications as future operations of the SEF fund will be taken over by Tabung Ekonomi Kumpulan Usaha Negeri (TEKUN).

Guarantee Schemes

CGC continues to provide guarantee cover for loans to SSEs and small and medium-scale industries (SMIs) granted by the commercial banks and finance companies through its main guarantee scheme, namely, the New Principal Guarantee Scheme (NPGS). In 1999, a total of 8,261 applications for loans amounting to RM1.9 billion were guaranteed by CGC. These represented an increase of 204.7% in terms of number of accounts guaranteed and 269.0% in terms of amount of loans guaranteed over the previous year, mainly due to better economic conditions. By sector, 80.6% of the loans extended in 1999 was channelled to general businesses while 17.9% was extended to SMIs in the manufacturing sector. Total guarantee cover issued during 1999 amounted to RM1.1 billion, of which 25.2% (RM276.9 million) was granted to Bumiputera borrowers.

The Flexible Guarantee Scheme (FGS) offers guarantee cover for loans extended under the four funds administered by Bank Negara Malaysia, that is, the Fund for SMIs, the Rehabilitation Fund for SMIs, the New Entrepreneurs Fund and the Fund for Food. The maximum guarantee cover for the unsecured portion is capped at RM2.5 million for the manufacturing sector, RM0.75 million for the priority sectors identified by CGC, and RM0.5 million for the other sectors. There is, however, no capping of guarantee cover for the secured portion of the loan. The annual guarantee fee under the scheme, which is to be borne by the lending institution, ranges from 0.5% to 1.5% depending on whether the guarantee cover is for the secured or unsecured portion of the loan. The FGS is meant to facilitate greater utilisation of the above-mentioned funds and is made available through the participating financial institutions under the four funds. As at end-1999, a total of 1,073 loans valued at RM302.9 million were guaranteed by CGC under the FGS, the majority of which were under the Fund for SMIs (832 loans valued at RM226.8 million).

Other than the above guarantee schemes, CGC also manages the SPTF Guarantee Scheme which provides guarantee cover for loans granted under Syariah principle.

Other Schemes

Apart from the SEF, CGC also assists the Ministry of Entrepreneur Development in managing two other schemes, that is, the Small Entrepreneurs Financing Fund (SEFF) and the Franchise Financing Scheme (FFS). The SEFF provides financing for small borrowers requiring loans ranging from RM10,000 to RM50,000 while the FFS is aimed at assisting franchisees under the Ministry's Franchise Programme. In November 1999, CGC merged the SEFF programme into the SEF programme.

The CGC is also involved in the Youth Economic Development Program which was introduced to encourage Malaysian youths to venture into business and other productive economic activities. The programme is jointly promoted with the Ministry of Youth and Sports and BSN Commercial Bank (Malaysia) Berhad.

Bank Lending under the NPGS

	Amount approved		
	1998	1999	Annual change (%)
	RM million		
General business	388.5	1,534.3	294.9
Of which:			
Building and construction	39.8	222.8	459.8
General commerce and sundry retail trade	236.1	902.2	282.1
Transport and repairs	38.2	115.0	201.0
Small scale industries	115.2	340.9	195.8
Of which:			
Food, drinks and tobacco	4.1	25.0	509.8
Timber products and furniture	20.4	59.8	193.0
Textiles and clothing	8.6	22.3	159.3
Building materials	2.8	11.7	317.9
Printing and publishing	3.2	16.2	406.3
Agriculture	11.1	24.8	123.4
Of which:			
Padi cultivation and marketing	–	0.1	100.0
Livestocks and poultry farming	1.1	3.9	254.5
Fisheries	0.5	8.9	1,680.0
Mining and quarrying	1.1	3.7	236.4
Of which:			
Other minerals	0.5	0.8	60.0
Total	**515.9**	**1,903.7**	**269.0**

Source: The Credit Guarantee Corporation Malaysia Berhad (CGC)

Key Economic and Financial Statistics

Table A.1
Gross Domestic Product by Industrial Origin (in Constant 1987 Prices)

	1995	1996	1997	1998	1999*p*	1995	1996	1997	1998	1999*p*
	RM million					Annual change (%)				
Agriculture, forestry and fishery	17,115	17,889	17,962	17,157	17,821	–2.5	4.5	0.4	–4.5	3.9
Mining and quarrying	13,643	14,040	14,454	14,719	14,124	22.9	2.9	3.0	1.8	–4.0
Manufacturing	45,174	53,387	58,956	50,899	57,761	11.4	18.2	10.4	–13.7	13.5
Construction	7,411	8,610	9,522	7,333	6,922	21.1	16.2	10.6	–23.0	–5.6
Services	85,348	92,963	102,200	101,346	104,264	10.2	8.9	9.9	–0.8	2.9
GDP in purchasers' value	**166,625**	**183,292**	**197,120**	**182,331**	**192,220**	**9.8**	**10.0**	**7.5**	**-7.5**	**5.4**

p Preliminary

Source: Department of Statistics

Table A.2
Growth in Manufacturing Production (1993=100)

	1996	**1997**	**1998**	**1999**	**1997**	**1998**	**1999**
	Index				**Annual change (%)**		
Export-oriented industry	**145.0**	**160.0**	**148.4**	**167.5**	**10.3**	**–7.3**	**12.9**
Electrical machinery, apparatus, appliances and supplies	159.9	181.6	167.6	193.9	13.6	–7.7	15.6
Radio and television sets	*161.7*	*150.1*	*156.0*	*155.5*	*–7.2*	*3.9*	*–0.3*
Semiconductors	*163.3*	*200.5*	*192.1*	*232.8*	*22.8*	*–4.2*	*21.2*
Cables and wires	*142.3*	*157.1*	*110.7*	*126.9*	*10.4*	*–29.4*	*14.6*
Manuf. of office, computing and accounting machinery	*170.8*	*186.3*	*177.9*	*199.9*	*9.1*	*–4.5*	*12.4*
Manuf. of refrigerating, exhaust, ventilating and air-conditioning machinery	*143.1*	*142.1*	*73.2*	*71.5*	*–0.7*	*–48.5*	*–2.2*
(Electronics)	163.3	200.5	192.1	232.8	22.8	–4.2	21.2
(Electrical)	154.6	151.9	129.5	133.0	–1.7	–14.8	2.7
Textiles and wearing apparel	114.9	121.0	114.6	119.2	5.3	–5.3	4.0
Wood and wood products	123.1	121.1	107.4	99.6	–1.6	–11.3	–7.3
Off-estate processing	125.3	137.6	133.9	167.0	9.8	–2.7	24.7
Domestic-oriented industry	**150.1**	**172.0**	**148.9**	**168.4**	**14.6**	**–13.4**	**13.1**
Chemicals and chemical products	150.5	187.3	183.8	215.3	24.5	–1.8	17.1
Construction-related products	154.2	171.6	124.3	142.0	11.3	–27.6	14.3
Non-metallic mineral products	*156.2*	*172.0*	*126.4*	*129.7*	*10.1*	*–26.5*	*2.6*
Basic iron & steel and non-ferrous metal	*151.6*	*171.5*	*121.6*	*157.4*	*13.1*	*–29.1*	*29.5*
Transport equipment	199.5	228.0	109.1	167.4	14.3	–52.2	53.5
Food products	118.8	123.3	120.7	127.6	3.8	–2.1	5.7
Beverages	147.5	147.2	129.9	126.6	–0.2	–11.9	–2.6
Tobacco products	108.3	129.8	118.0	99.8	19.9	–9.1	–15.5
Rubber products	145.0	149.9	161.7	167.5	3.4	7.8	3.6
Petroleum productds	144.2	157.1	139.1	138.7	8.9	–11.5	–0.3
Fabricated metal products	157.1	175.8	145.6	144.0	11.9	–17.2	–1.1
Paper products	121.0	136.7	124.8	140.8	13.0	–8.7	12.8
Total	**147.3**	**165.6**	**148.6**	**167.8**	**12.4**	**–10.2**	**12.9**

Source: Department of Statistics

Table A.3
Manufacturing Production: Selected Indicators

	1998	1999	1998	1999
	Output		**Annual change (%)**	
Integrated circuits (million units)	11,622	14,878	–7.5	28.0
Semiconductors (million units)	8,951	9,959	20.4	11.3
Television sets ('000 units)	8,035	7,611	3.4	–5.3
Room air-conditioners ('000 units)	1,293	1,147	–38.9	–11.3
Household refrigerators ('000 units)	206	194	–17.3	–5.8
Vehicles assembled ('000 units)	418	572	–52.6	36.8
Passenger cars	*149*	*258*	*–58.8*	*73.2*
Commercial vehicles	*20*	*45*	*–78.9*	*125.0*
Motorcycles & scooters	*249*	*269*	*–41.3*	*8.0*
Pneumatic tyres ('000 units)	13,567	13,553	–1.1	–0.1
Rubber gloves (million pairs)	10,612	10,899	19.0	2.7
Plywood ('000 cu.metre)	3,673	3,701	–18.6	0.8
Veneer sheets ('000 cu.metre)	1,142	1,255	–9.7	9.9
Liquefied petroleum gas ('000 tonnes)	1,410	1,573	4.2	11.6
Kerosene & gasoline ('000 tonnes)	4,576	5,057	–1.3	10.5
Diesel and gas oil ('000 tonnes)	5,974	5,861	–12.0	–1.9
Fuel oil ('000 tonnes)	2,390	1,798	–24.2	–24.8
Cement ('000 tonnes)	10,397	10,105	–17.9	–2.8
Iron and steel bars and rods ('000 tonnes)	1,903	2,271	–43.6	19.3

Source: Department of Statistics

Table A.4
Production: Primary Commodities

		1995	1996	1997	1998	1999*p*	1995	1996	1997	1998	1999*p*
		Volume					Annual change in %				
Crude palm oil	('000 tonnes)	7,811	8,386	9,069	8,320	10,553	8.2	7.4	8.1	–8.3	26.8
Rubber	('000 tonnes)	1,089	1,082	971	886	767	–1.1	–0.6	–10.2	-8.8	–13.5
Saw logs	('000 cu. metres)	31,642	30,094	31,162	21,672	21,941	–11.3	–4.9	3.5	–30.5	1.2
Cocoa	('000 tonnes)	131	120	106	90	84	–26.0	–8.4	–11.6	–14.9	–7.2
Crude oil	('000 bpd)	705	716	714	725	693	6.8	1.5	–0.2	1.6	–4.4
Natural gas	(mmscfd)	2,810	3,402	3,926	3,722	3,802	19.0	21.1	15.4	–5.2	2.1
Tin-in-concentrates	('000 tonnes)	6.4	5.2	5.1	5.8	7.4	–0.9	–19.2	–2.0	13.6	27.6

p Preliminary

Source: PORLA
Department of Statistics
Forestry Departments (Peninsular Malaysia, Sabah & Sarawak)
Malaysian Cocoa Board
PETRONAS
Department of Mines

Table A.5
Selected Indicators for the Services Sector

	1995	1996	1997	1998	1999*e*
	Annual change (%)				
Insurance premiums	21.6	20.0	14.4	–0.6	5.7
KLSE turnover					
Value	–45.5	159.3	–11.8	–71.8	46.1
Volume	–43.6	95.8	9.5	–19.9	60.8
KL office rentals (RM per sq m)	48.1	50.5	49.8	42.5	40.6
KL office occupancy rate (%)	95	95	98	82	77
Tourist arrivals	3.8	–4.4	–13.0	–10.6	42.9
Hotel occupancy rate (%)	65.3	65.5	58.0	49.9	53.4
Cargo throughput at major ports[1]	17.4	14.0	12.5	–12.8	9.5
Container cargo throughput at major ports[1]	19.4	19.4	17.1	4.0	31.7
Electricity Production Index	14.1	12.8	14.2	3.4	3.8
Water supply	8.9	2.0	2.0	1.5	2.4

[1] Include Port Klang, Penang Port, Johor Port, Bintulu Port and Sabah Port.
e Estimate

Source: Kuala Lumpur Stock Exchange (KLSE)
Department of Statistics
Valuation and Property Services Department, Ministry of Finance
Malaysia Tourism Promotion Board (Tourism Malaysia)
Various port operators
Public Works Department

Table A.6
GNP by Demand Aggregates

	1995	1996	1997	1998	1999*p*	2000*f*
	Current Prices (RM million)					
Consumption	134,140	144,972	158,329	146,552	158,804	176,780
Private consumption	*106,613*	*116,794*	*127,650*	*118,098*	*124,672*	*140,883*
Public consumption	*27,527*	*28,178*	*30,679*	*28,454*	*34,132*	*35,897*
Investment	96,967	107,825	121,384	76,275	66,597	71,770
Private investment	*69,424*	*79,388*	*89,561*	*44,322*	*33,639*	*35,320*
Public investment	*27,543*	*28,437*	*31,823*	*31,953*	*32,958*	*36,450*
Change in stocks	120	–2,579	–446	–362	340	819
Exports of goods and non-factor services	209,323	232,358	262,714	325,325	363,278	402,867
Imports of goods and non-factor services	218,077	228,843	260,092	263,318	289,336	330,481
GDP at purchasers' value	222,472	253,733	281,888	284,473	299,683	321,755
Net factor payments abroad	–10,377	–11,801	–15,095	–15,336	–19,351	–21,903
GNP at purchasers' value	212,095	241,931	266,793	269,138	280,332	299,852
	Constant Prices[1] (RM million)					
Consumption	102,663	108,442	113,809	102,185	108,398	116,392
Private consumption	*81,981*	*87,609*	*91,386*	*81,520*	*83,584*	*91,526*
Public consumption	*20,682*	*20,833*	*22,423*	*20,665*	*24,814*	*24,866*
Investment	81,895	88,624	96,744	55,258	51,520	55,246
Private investment	*58,633*	*65,251*	*71,381*	*32,109*	*26,023*	*27,188*
Public investment	*23,262*	*23,373*	*25,363*	*23,149*	*25,497*	*28,058*
Change in stocks	90	–1,900	–323	–235	218	521
Exports of goods and non-factor services	161,856	176,792	186,378	185,979	211,563	233,450
Imports of goods and non-factor services	179,878	188,666	199,488	160,857	179,479	202,173
GDP at purchasers' value	166,625	183,292	197,120	182,331	192,220	203,436
Net factor payments abroad	–11,422	–13,188	–14,416	–9,465	–11,919	–13,331
GNP at purchasers' value	155,204	170,104	182,705	172,866	180,301	190,105

[1] At constant 1987 prices
p Preliminary
f Forecast

Source: Department of Statistics and Bank Negara Malaysia

Table A.7
Selected Private Investment Indicators

	1995	1996	1997	1998	1999
	Annual change (%)				
Imports of capital goods (US$)[1]	n.a.	-6.8	6.7	–40.5	–5.9
Sales of commercial vehicles[2]	43.6	48.7	8.4	–76.1	50.8
Applications for manufacturing investment to MITI					
No. of projects	9.6	–16.8	–8.6	–14.5	2.9
Total capital investment	10.3	56.7	–18.8	–44.7	–25.8
Foreign capital invesment	*11.8*	*32.9*	*–18.4*	*–12.2*	*–28.4*
Local capital invesment	*8.9*	*79.8*	*–19.1*	*–68.2*	*–20.7*
Approved manufacturing investment by MITI					
No. of projects	3.2	–12.9	–2.9	11.2	–16.1
Total capital investment	–9.1	64.2	–24.6	2.1	–35.9
Foreign capital invesment	*–19.4*	*86.5*	*–32.7*	*13.9*	*–6.1*
Local capital invesment	*1.0*	*46.7*	*–16.6*	*–7.4*	*–65.2*
Loans disbursed by the banking system					
For manufacturing	*n.a*	*n.a*	*n.a*	*–0.8*	*23.7*
For construction	*n.a*	*n.a*	*n.a*	*–31.6*	*19.7*
Loans approved by the banking system					
For manufacturing	*n.a*	*n.a*	*n.a*	*–68.4*	*35.4*
For construction	*n.a*	*n.a*	*n.a*	*–77.7*	*39.3*
Capital expenditure by sector[3]					
Manufacturing	*16.0*	*–4.1*	*44.3*	*41.4*	*–44.6*
Construction	*72.9*	*–3.4*	*18.5*	*78.7*	*–80.2*
Others (Services, etc.)	*39.1*	*–1.9*	*170.7*	*4.4*	*–44.4*

[1] Beginning 1995, the data is compiled based on Broad Economic Categories classification. Prior to 1995, the data was compiled based on Economic and Social Commission for Asia-Pacific (ESCAP) classification.
[2] Include four-wheel drive vehicles for commercial use.
[3] Business Expectations Survey by the Department of Statistics. Beginning second half of 1997, the number of companies surveyed increased from 220 to 270.
n.a. Not available

Source: Department of Statistics
Malaysian Automotive Association (MAA)
Ministry of International Trade and Industry (MITI)
Bank Negara Malaysia

Table A.8
Selected Private Consumption Indicators

	1995	1996	1997	1998	1999
	Annual change (%)				
Imports of consumption goods (US$)[1]	n.a.	5.4	–0.7	–32.9	21.3
Sales of passenger cars[2]	49.5	22.8	12.3	–54.8	79.9
Prices of primary commodities					
Rubber	*34.5*	*–11.1*	*–20.7*	*0.7*	*–14.4*
Crude palm oil	*14.7*	*–19.1*	*15.9*	*72.3*	*–38.5*
Tax collection					
Sales tax	*17.9*	*12.4*	*12.7*	*–37.7*	*16.3*
Services tax	*23.2*	*21.1*	*19.8*	*–1.9*	*3.6*
Loans disbursed by the banking system					
For consumption credit (excl. passenger cars)	*n.a.*	*n.a.*	*n.a.*	*–18.7*	*46.8*
For wholesale, retail, restaurants & hotels	*n.a.*	*n.a.*	*n.a.*	*15.0*	*61.0*
Stock market indicators					
Market capitalisation of KLSE	*11.2*	*42.6*	*–53.4*	*–0.3*	*47.6*
Kuala Lumpur Composite Index	*2.5*	*24.4*	*–52.0*	*–1.4*	*38.6*

[1] Beginning 1995, the data is compiled based on Broad Economic Categories classification. Prior to 1995, the data was compiled based on Economic and Social Commission for Asia-Pacific (ESCAP) classification.
[2] Include four-wheel drive vehicles for passenger use.
n.a. Not available

Source: Department of Statistics
Royal Customs and Excise Department
Palm Oil Registration and Licensing Authority (PORLA)
Malaysian Rubber Exchange and Licensing Board (MRELB)
Malaysian Automotive Association (MAA)
Kuala Lumpur Stock Exchange (KLSE)

Table A.9
Savings-Investment Gap

	1995	1996	1997	1998	1999*p*	2000*f*
	RM million					
Public gross domestic capital formation	27,577	27,757	31,706	31,801	33,126	36,866
Public savings	32,765	39,761	56,435	44,027	45,714	41,261
Deficit (–) / surplus	5,188	12,004	24,729	12,226	12,588	4,395
Private gross domestic capital formation	69,510	77,489	89,232	44,112	33,811	35,723
Private savings	42,676	54,255	48,684	68,683	68,604	73,925
Deficit (–) / surplus	–26,834	–23,234	–40,548	24,571	34,793	38,202
Gross domestic capital formation	97,087	105,246	120,938	75,913	66,937	72,589
(as % of GNP)	45.8	43.5	45.3	28.2	23.9	24.2
Gross national savings	75,441	94,016	105,119	112,710	114,318	115,186
(as % of GNP)	35.6	38.9	39.4	41.9	40.8	38.4
Balance on current account	–21,646	–11,230	–15,819	36,797	47,381	42,597
(as % of GNP)	–10.2	–4.6	–5.9	13.7	16.9	14.2

p Preliminary
f Forecast

Source: Department of Statistics and Bank Negara Malaysia

Table A.10
Balance of Payments

Item	1995 +	1995 -	1995 Net	1996 +	1996 -	1996 Net
	RM million					
Merchandise balance (f.o.b.)[1]	**179,491**	**179,394**	**97**	**193,363**	**183,275**	**10,088**
Trade account	*184,987*	*194,345*	*–9,358*	*197,026*	*197,280*	*–254*
Balance on services	**35,778**	**55,007**	**–19,229**	**45,089**	**63,460**	**–18,371**
Freight and insurance	2,552	11,580	–9,028	2,797	11,000	–8,203
Other transportation	4,434	3,697	737	5,617	3,892	1,725
Travel and education	9,939	5,796	4,143	11,264	6,463	4,801
Investment income[2]	6,280	16,618	–10,338	6,362	17,991	–11,629
Government transactions n.i.e.[3]	319	342	–23	333	360	–27
Other services	12,254	16,974	–4,720	18,716	23,754	–5,038
Balance on goods and services	**215,269**	**234,401**	**–19,132**	**238,452**	**246,735**	**–8,283**
Unrequited transfers	1,843	4,358	–2,515	2,020	4,963	–2,943
Balance on current account	**217,112**	**238,759**	**–21,647**	**240,472**	**251,698**	**–11,226**
% of GNP			**–10.2**			**–4.6**
Official long-term capital			6,147			748
Federal Government	419	2,052	–1,633	748	2,927	–2,179
Market loans	0	1,091	–1,091	342	1,017	–675
Project loans	419	961	–542	406	1,910	–1,504
Non-financial public enterprises	9,952	2,184	7,768	8,128	5,284	2,844
Other assets and liabilities[4]			12			83
Private long-term capital			10,464			12,777
Balance on long-term capital			16,611			13,525
Basic balance			**–5,036**			**2,299**
Private short-term capital			2,529			10,317
Errors and omissions			–1,896			–6,371
Overall balance (surplus + / deficit –)			**–4,403**			**6,245**
Allocation of Special Drawing Rights			–			–
IMF resources			–			–
Net change in international reserves of Bank Negara Malaysia (increase – / decrease +)[5]			4,403			–6,245
Special Drawing Rights			–41			–37
IMF reserve position			–701			–15
Gold and foreign exchange			5,145			–6,193
Bank Negara Malaysia international reserves, net			**63,770**			**70,015**
(Reserves as months of retained imports)			4.1			4.4

[1] Adjusted for valuation and coverage to the balance of payments basis. Imports include military goods which are not included in trade data.
[2] Include undistributed earnings of foreign direct investment companies.The counterpart of these earnings is shown as an inflow of direct reinvestment capital under "Private long-term capital".
[3] Include transactions of foreign military and diplomatic establishments.
[4] Refer to changes in overseas assets of the Government and statutory authorities and subscriptions to international institutions and commodity arrangements.
[5] Accumulation of reserves is indicated as a minus(-) sign.
[6] In 1997, the foreign exchange gain on the balance sheet date was not recognised in the Bank's account in view of volatility of the exchange rate during the year.
[7] Arising from the fixing of the ringgit/US dollar exchange rate in September 1998, all assets and liabilities in foreign currencies have been revalued into ringgit at rates of exchange ruling on the balance sheet date and the cumulative gain/loss has been reflected accordingly in the Bank's current year account. The US dollar equivalent of international reserves as at 31 December 1999 was US$30.9 billion.
e Estimate

Source : Department of Statistics and Bank Negara Malaysia.

1997			1998			1999*e*		
+	-	Net	+	-	Net	+	-	Net
RM million								
217,712	**207,439**	**10,273**	**281,947**	**212,939**	**69,008**	**315,719**	**232,184**	**83,534**
220,891	*220,936*	*–45*	*286,563*	*228,124*	*58,439*	*321,181*	*248,870*	*72,311*
51,316	**74,064**	**–22,748**	**48,605**	**70,943**	**–22,338**	**56,057**	**85,000**	**–28,943**
3,178	12,340	–9,162	4,129	12,564	-8,435	4,685	14,416	–9,731
6,222	4,475	1,747	6,547	4,279	2,268	7,258	4,778	2,479
10,523	7,271	3,252	9,342	6,272	3,070	13,326	7,758	5,568
6,443	21,082	–14,639	5,308	20,125	–14,817	7,283	26,073	–18,790
308	458	–150	331	546	–215	338	385	–46
24,642	28,438	–3,796	22,948	27,157	–4,209	23,168	31,590	–8,422
269,028	**281,503**	**–12,475**	**330,552**	**283,882**	**46,670**	**371,776**	**317,185**	**54,591**
2,779	6,124	–3,345	2,945	12,821	–9,876	2,732	9,943	–7,210
271,807	**287,627**	**–15,820**	**333,497**	**296,703**	**36,794**	**374,508**	**327,127**	**47,381**
		–5.9			**13.7**			**16.9**
		4,645			2,137			6,692
462	2,145	–1,683	4,001	2,182	1,819	4,763	1,840	2,923
0	697	–697	2,435	1,324	1,111	4,164	1,107	3,057
462	1,448	–986	1,566	858	708	599	733	–134
9,372	3,006	6,366	4,705	4,344	361	6,080	2,230	3,850
		–38			–43			–81
		14,450			8,490			5,025
		19,095			10,627			11,717
		3,275			**47,421**			**59,098**
		–12,913			–20,633			–35,958
		–1,254			13,513			–5,321
		–10,892			**40,301**			**17,819**
		–			–			–
		–			–			–
		10,892			–40,301			–17,819
		–51			–315			464
		117			–757			–789
		10,826			–39,229			–17,494
		59,123[6]			**99,424**[7]			**117,244**[7]
		3.4			5.7			5.9

Table A.11
Direction of External Trade[1]

	1995			1996		
	Exports	Imports	Trade balance	Exports	Imports	Trade balance
	RM million					
Singapore	37,584.4	24,079.9	13,504.5	40,290.3	26,344.6	13,945.7
Thailand	7,258.0	5,131.5	2,126.5	8,069.2	6,521.7	1,547.5
Indonesia	2,441.2	3,057.3	–616.1	3,065.3	3,584.2	–518.9
Phillippines	1,692.2	1,153.5	538.7	2,011.1	2,360.2	–349.1
Brunei Darussalam	742.8	10.3	732.5	818.0	11.6	806.4
Vietnam[2]	672.8	315.6	357.2	812.8	378.3	434.5
Selected Southeast Asian Countries	50,391.4	33,748.1	16,643.3	55,066.7	39,200.6	15,866.1
Japan	23,449.0	53,088.8	–29,639.8	26,377.8	48,397.8	–22,020.0
The People's Republic of China	4,904.4	4,298.3	606.1	4,734.2	4,718.5	15.7
Hong Kong SAR	9,899.3	4,193.7	5,705.6	11,588.1	4,577.5	7,010.6
Taiwan, ROC	5,813.3	9,913.7	–4,100.4	8,074.4	9,822.8	–1,748.4
South Korea	5,162.0	7,965.3	–2,803.3	5,998.7	10,235.3	–4,236.6
India	2,084.1	1,377.9	706.2	3,033.5	1,849.8	1,183.7
Other Far Eastern countries[3]	3,250.5	449.8	2,800.7	3,524.5	310.6	3,213.9
Australia	2,824.6	5,259.4	–2,434.8	3,058.3	5,559.8	–2,501.5
New Zealand	487.9	800.9	–313.0	604.8	918.7	–313.9
United States	38,278.5	31,413.0	6,865.5	35,821.9	30,495.8	5,326.1
Canada	1,504.7	1,034.0	470.7	1,367.8	1,191.1	176.7
United Kingdom	7,483.5	5,479.6	2,003.9	6,778.0	5,139.3	1,638.7
Germany	5,926.6	8,612.6	–2,686.0	5,978.9	8,434.7	–2,455.7
Netherlands	4,505.3	1,313.3	3,192.0	5,848.9	1,737.9	4,110.9
France	1,852.5	5,917.5	–4,065.0	1,603.3	3,961.1	–2,357.8
Italy	1,418.1	2,462.5	–1,044.4	1,535.1	2,740.1	–1,205.0
Belgium	1,967.6	1,110.3	857.3	2,135.6	1,157.4	978.1
Luxembourg	21.4	43.3	–21.9	17.1	15.4	1.8
Denmark	336.0	275.4	60.6	327.7	366.5	–38.8
Ireland	818.7	1,372.5	–553.8	852.0	1,786.8	–934.8
Greece	137.1	28.9	108.2	145.8	48.3	97.5
Spain	923.0	657.7	265.3	827.5	575.9	251.6
Portugal	140.0	114.5	25.5	129.0	103.0	26.1
Austria[4]	155.3	288.1	–132.8	152.3	298.1	–145.8
Finland[4]	155.4	646.0	–490.6	254.2	494.3	–240.1
Sweden[4]	433.1	1,638.0	–1,204.9	412.6	1,559.7	–1,147.2
European Union (EU)	26,273.6	29,960.2	–3,686.6	26,998.2	28,418.6	–1,420.4
Other West European countries[5]	923.7	4,012.8	–3,089.1	1,483.4	6,836.0	–5,352.6
Russia	250.0	439.0	–189.0	284.6	667.9	–383.3
Other Central and East European countries[6]	394.4	496.0	–101.6	458.4	740.1	–281.7
Rest of the world	9,095.1	5,893.6	3,201.5	8,550.8	3,338.9	5,211.9
Total	184,986.5	194,344.5	–9,358.0	197,026.1	197,279.8	–253.7

[1] Exports are valued on the f.o.b. basis and imports on the c.i.f. basis.
[2] Viet Nam became a member of ASEAN on 28 July 1995.
[3] Include Cambodia, Laos, Macau, Mongolia, Myanmar and North Korea.
[4] Finland and Sweden became members of the European Union on 1 January 1995 , while Austria became one on 1 March 1995.
[5] Include Gibraltar, Greenland, Iceland, Malta, Monaco, Norway, Switzerland and Turkey.
[6] Include Albania, Bulgaria, the Czech Republic, Hungary, Poland, Romania, Slovakia, countries of the former Yugoslavia and other member countries of the Commonwealth of Independent States.

Source: Department of Statistics, Malaysia

1997			1998			1999		
Exports	Imports	Trade balance	Exports	Imports	Trade balance	Exports	Imports	Trade balance
RM million								
44,352.1	28,994.1	15,358.0	48,688.9	30,943.8	17,745.0	53,105.9	34,817.2	18,288.7
7,925.1	8,680.2	–755.1	9,058.9	8,831.7	227.2	10,480.9	9,376.6	1,104.3
3,464.1	4,129.3	–665.2	3,932.2	5,777.8	–1,845.6	4,678.8	6,676.6	–1,997.8
3,301.0	2,632.8	668.2	4,521.2	5,385.6	–864.5	4,929.2	6,212.7	–1,283.5
763.5	64.8	698.6	907.0	14.9	892.1	808.8	45.7	763.1
910.7	456.5	454.2	1,469.9	538.1	931.9	1,463.1	942.7	520.3
60,716.5	44,957.8	15,758.7	68,578.0	51,491.9	17,086.1	75,466.8	58,071.7	17,395.1
27,483.9	48,497.6	–21,013.7	30,236.9	44,854.5	–14,617.6	37,289.0	51,803.1	–14,514.2
5,256.7	6,274.1	–1,017.4	7,764.0	7,250.1	513.9	8,807.7	8,125.3	682.4
12,181.0	5,398.7	6,782.3	13,299.5	5,943.2	7,356.4	13,343.5	6,249.9	7,093.7
9,484.0	10,574.7	–1,090.7	11,797.9	11,646.5	151.3	14,599.7	13,258.7	1,341.0
7,049.1	11,352.4	–4,303.3	6,516.5	13,126.4	–6,609.9	9,497.9	12,973.9	–3,476.1
3,305.7	2,137.4	1,168.3	6,743.8	1,829.9	4,913.8	7,745.1	2,014.1	5,731.0
1,345.2	215.8	1,129.5	1,334.3	284.4	1,049.9	2,094.3	269.3	1,825.0
3,797.0	5,490.4	–1,693.4	6,617.4	4,996.5	1,620.9	7,711.3	5,670.3	2,041.0
564.7	1,079.8	-515.1	820.0	985.2	–165.2	1,151.0	1,052.3	98.6
41,124.0	37,102.7	4,021.3	62,129.6	44,762.4	17,367.2	70,391.1	43,317.8	27,073.3
1,627.0	1,723.6	–96.6	2,144.9	1,466.3	678.6	2,387.0	1,449.1	937.9
7,293.5	5,812.1	1,481.4	10,328.4	5,067.0	5,261.4	12,066.6	5,611.0	6,455.6
6,368.4	9,715.5	–3,347.2	8,654.9	9,018.8	–363.9	7,691.8	7,703.9	–12.1
8,699.8	2,157.7	6,542.1	13,437.4	2,001.0	11,436.4	16,232.7	1,804.5	14,428.2
2,101.0	4,257.6	–2,156.6	3,036.4	3,273.5	–237.1	3,230.9	4,150.0	–919.1
1,393.4	3,161.3	–1,768.0	2,090.1	2,121.2	–31.2	1,963.3	2,026.7	–63.4
2,406.5	1,240.3	1,166.3	3,376.4	1,174.0	2,202.4	3,431.3	1,194.3	2,236.9
23.7	25.3	–1.7	34.9	8.9	26.0	32.0	9.3	22.7
416.3	373.5	42.8	594.8	440.8	154.0	523.7	334.4	189.3
1,082.5	1,234.2	–151.6	1,740.8	1,435.2	305.7	2,413.3	3,258.7	–845.3
152.4	22.7	129.7	346.9	21.1	325.8	269.3	31.6	237.8
871.3	564.7	306.6	1,272.3	524.2	748.1	1,265.3	487.6	777.6
119.7	67.0	52.7	197.4	77.1	120.3	179.4	77.2	102.3
135.1	244.7	–109.6	214.2	240.6	–26.4	248.8	296.7	–47.9
369.2	810.0	–440.9	448.1	384.2	63.9	283.7	415.3	–131.6
510.8	1,564.7	–1,053.9	659.2	1,283.8	–624.6	689.5	1,572.8	–883.3
31,943.7	31,251.5	692.3	46,432.3	27,071.5	19,360.8	50,521.7	28,974.0	21,547.6
1,222.2	3,587.6	–2,365.4	2,200.8	2,878.6	–677.9	2,094.0	4,038.3	–1,944.3
250.3	1,045.4	–795.1	338.2	500.5	–162.3	264.7	1,098.3	–833.6
494.4	808.5	–314.1	970.7	459.5	511.2	943.9	624.6	319.3
13,045.0	9,437.6	3,607.4	18,831.0	8,761.9	10,069.1	16,872.6	9,879.2	6,993.4
220,890.5	220,935.5	–45.0	286,563.1	228,124.4	58,438.7	321,181.3	248,870.0	72,311.3

Table A.12
Principal Markets for Manufactured Exports

Country	1995		1996		1997		1998		1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
ASEAN	**40,878**	**27.8**	**45,388**	**28.6**	**50,869**	**28.4**	**58,299**	**24.5**	**65,004**	**23.9**
Singapore	32,818	22.3	35,686	22.5	39,340	22.0	43,567	18.3	48,390	17.8
Thailand	4,292	2.9	4,746	3.0	5,439	3.0	7,190	3.0	8,396	3.1
Indonesia	1,933	1.3	2,527	1.6	2,745	1.5	2,793	1.2	3,415	1.3
Philippines	1,291	0.9	1,831	1.2	2,794	1.6	4,017	1.7	4,170	1.5
Brunei Darussalam	543	0.4	599	0.4	551	0.3	731	0.3	633	0.2
EU	**21,840**	**14.8**	**22,920**	**14.5**	**27,799**	**15.5**	**39,737**	**16.7**	**44,837**	**16.5**
United Kingdom	6,839	4.6	6,186	3.9	6,686	3.7	9,590	4.0	11,438	4.2
Germany	5,277	3.6	5,430	3.4	5,826	3.3	7,861	3.3	6,955	2.6
Netherlands	2,953	2.0	4,446	2.8	7,363	4.1	10,673	4.5	13,880	5.1
Others	6,771	4.6	6,858	4.3	7,925	4.4	11,614	4.9	12,564	4.6
United States	36,713	24.9	34,410	21.7	39,495	22.1	60,118	25.3	68,058	25.0
Japan	15,202	10.3	17,515	11.0	18,279	10.2	21,509	9.1	28,027	10.3
Hong Kong SAR	9,149	6.2	10,448	6.6	11,176	6.2	12,339	5.2	13,395	4.9
Taiwan	4,439	3.0	6,643	4.2	7,655	4.3	9,943	4.2	12,835	4.7
Korea	2,662	1.8	2,855	1.8	2,950	1.6	3,237	1.4	5,481	2.0
The People's Republic of China	2,348	1.6	2,746	1.7	2,777	1.6	4,415	1.9	5,660	2.1
Australia	1,900	1.3	2,400	1.5	3,058	1.7	5,465	2.3	5,924	2.2
Canada	1,384	0.9	1,280	0.8	1,501	0.8	1,993	0.8	2,262	0.8
West Asian countries	2,767	1.9	2,858	1.8	3,158	1.8	5,050	2.1	5,042	1.9
Latin American countries	1,965	1.3	1,776	1.1	2,431	1.4	3,130	1.3	2,242	0.8
Rest of the World	6,046	4.1	7,299	4.6	7,797	4.4	12,413	5.2	12,964	4.9
Total	**147,253**	**100.0**	**158,540**	**100.0**	**178,945**	**100.0**	**237,649**	**100.0**	**271,730**	**100.0**

Source: Department of Statistics and Bank Negara Malaysia

Table A.13
Principal Export Markets for Electronics

Country	1995		1996		1997		1998		1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
United States	18,159	32.0	16,357	25.3	21,365	26.4	35,320	30.9	41,660	28.8
Singapore	14,578	25.7	17,555	27.2	21,170	26.2	24,335	21.3	28,621	19.8
Taiwan	2,150	3.8	4,056	6.3	4,395	5.4	5,902	5.2	9,153	6.3
Japan	4,670	8.2	5,547	8.6	6,156	7.6	8,264	7.2	12,621	8.7
Hong Kong SAR	2,788	4.9	3,963	6.1	4,490	5.6	4,403	3.9	6,506	4.5
Others	14,435	25.4	17,155	26.5	23,201	28.7	35,949	31.5	46,324	31.9
Total	**56,780**	**100.0**	**64,633**	**100.0**	**80,776**	**100.0**	**114,175**	**100.0**	**144,885**	**100.0**

Source: Department of Statistics and Bank Negara Malaysia

Table A.14
Principal Export Markets for Electrical Products

Country	1995		1996		1997		1998		1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
United States	9,445	23.6	9,145	23.1	8,918	23.3	12,252	25.8	13,817	27.5
Singapore	9,165	22.9	8,323	21.0	7,867	20.6	7,801	16.4	7,958	15.9
Japan	4,894	12.2	5,320	13.4	5,140	13.4	6,472	13.6	6,778	13.5
Hong Kong SAR	2,786	7.0	2,599	6.6	2,223	5.8	2,472	5.2	2,263	4.5
Germany	1,618	4.0	1,757	4.4	1,545	4.0	1,868	3.9	1,662	3.3
United Kingdom	1,067	2.7	1,053	2.7	1,067	2.8	1,270	2.7	1,542	3.1
Others	10,993	27.5	11,443	28.9	11,490	30.0	15,424	32.4	16,142	32.2
Total	**39,968**	**100.0**	**39,639**	**100.0**	**38,249**	**100.0**	**47,558**	**100.0**	**50,162**	**100.0**

Source: Department of Statistics and Bank Negara Malaysia

Table A.15
Principal Export Markets for Textiles, Clothing and Footwear

Country	1995		1996		1997		1998		1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
United States	1,693	26.0	1,662	23.9	1,885	24.8	2,877	30.5	2,882	30.4
Hong Kong SAR	801	12.3	1,071	15.4	1,009	13.2	1,084	11.5	785	8.3
Singapore	763	11.7	774	11.1	734	9.6	683	7.2	763	8.1
United Kingdom	498	7.6	494	7.1	527	6.9	610	6.5	655	6.9
Japan	383	5.9	433	6.2	487	6.4	455	4.8	535	5.7
Germany	352	5.4	365	5.2	314	4.1	420	4.4	371	3.9
Taiwan	239	3.7	346	5.0	547	7.2	587	6.2	525	5.5
Others	1,790	27.5	1,817	26.1	2,113	27.7	2,726	28.9	2,951	31.2
Total	**6,519**	**100.0**	**6,963**	**100.0**	**7,616**	**100.0**	**9,442**	**100.0**	**9,467**	**100.0**

Source: Department of Statistics and Bank Negara Malaysia

Table A.16
Principal Export Markets for Wood Products

Country	1995		1996		1997		1998		1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
Japan	1,405	28.4	2,105	34.6	2,092	32.2	1,574	26.3	2,450	35.1
The People's Republic of China	1,148	23.2	1,241	20.4	949	14.6	741	12.4	725	10.4
Taiwan	384	7.8	476	7.8	533	8.2	468	7.8	499	7.1
Hong Kong SAR	380	7.7	474	7.8	685	10.6	818	13.7	525	7.5
Singapore	367	7.4	399	6.6	433	6.7	366	6.1	364	5.2
Others	1,270	25.6	1,391	22.9	1,798	27.7	2,014	33.7	2,420	34.7
Total	**4,954**	**100.0**	**6,086**	**100.0**	**6,490**	**100.0**	**5,982**	**100.0**	**6,984**	**100.0**

Source : Department of Statistics and Bank Negara Malaysia

Table A.17
Principal Export Markets for Chemicals and Chemical Products

Country	1995		1996		1997		1998		1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
Singapore	834	13.3	901	13.4	1,024	12.6	1,266	11.9	1,454	13.1
Hong Kong SAR	627	10.0	648	9.7	783	9.6	1,086	10.2	993	8.9
Japan	607	9.7	610	9.1	792	9.7	971	9.1	1,199	10.8
Korea	492	7.9	587	8.7	553	6.8	447	4.2	453	4.1
United States	523	8.4	554	8.3	769	9.5	1,029	9.7	922	8.3
Taiwan	281	4.5	381	5.7	635	7.8	543	5.1	409	3.7
Thailand	385	6.2	357	5.3	376	4.6	516	4.9	680	6.1
Indonesia	251	4.0	353	5.3	449	5.5	344	3.2	617	5.6
Australia	185	3.0	242	3.6	239	2.9	336	3.2	352	3.2
Others	2,072	33.1	2,077	31.0	2,517	30.9	4,090	38.5	4,026	36.2
Total	**6,257**	**100.0**	**6,710**	**100.0**	**8,137**	**100.0**	**10,627**	**100.0**	**11,105**	**100.0**

Source : Department of Statistics and Bank Negara Malaysia

Table A.18
Principal Export Markets for Manufactures of Metal

Country	1995		1996		1997		1998		1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
Singapore	1,513	32.5	1,719	34.4	1,789	31.6	2,298	27.8	2,155	27.4
United States	357	7.7	414	8.3	418	7.4	682	8.3	633	8.1
Japan	392	8.4	387	7.7	514	9.1	566	6.9	667	8.5
Korea	221	4.7	338	6.8	324	5.7	294	3.6	279	3.5
Thailand	355	7.6	312	6.2	293	5.2	384	4.6	458	5.8
Indonesia	267	5.7	258	5.2	237	4.2	279	3.4	314	4.0
Taiwan	217	4.7	248	5.0	304	5.4	742	9.0	390	5.0
Others	1,334	28.7	1,322	26.5	1,782	31.4	3,010	36.4	2,966	37.7
Total	**4,656**	**100.0**	**4,998**	**100.0**	**5,661**	**100.0**	**8,255**	**100.0**	**7,862**	**100.0**

Source : Department of Statistics and Bank Negara Malaysia

Table A.19
Export Prices for Major Commodities

	1995	1996	1997	1998	1999	1995	1996	1997	1998	1999
						Annual change in %				
Palm oil (RM/tonne)	1,561.9	1,288.4	1,424.9	2,366.4	1,614.7	23.3	-17.5	10.6	66.1	-31.8
Rubber (sen/kg)	398.5	358.0	291.7	286.0	238.2	38.5	-10.2	-18.5	-1.9	-16.7
Saw logs (RM/cu. metre)	292.2	326.7	366.8	344.4	395.2	-3.3	11.8	12.3	-6.1	14.8
Sawn timber (RM/cu. metre)	879.4	832.5	904.9	941.4	995.9	-3.5	-5.3	8.7	4.0	5.8
Crude oil (RM/tonne)	349.7	412.2	445.3	416.9	525.0	1.8	17.9	8.0	-6.4	25.9

Source: Department of Statistics

Table A.20
Crude Oil Prices: International Comparison

	1995	1996	1997	1998	1999
	(US$/barrel)				
Tapis Blend	18.28	22.00	21.11	14.20	18.60
North Sea Brent	17.20	20.76	19.40	13.09	18.22
West Texas Intermediate	18.43	22.12	20.63	14.37	19.15

Source: PETRONAS

Table A.21
Principal Export Markets for Palm Oil

	1995	1996	1997	1998	1999	1995	1996	1997	1998	1999
	'000 tonnes					% share				
India	748.8	991.9	974.6	1,330.8	2,402.4	11.3	13.5	12.8	17.7	26.8
West Asia	865.2	1,099.0	937.6	862.5	1,123.5	13.0	15.0	12.4	11.5	12.5
Pakistan	1,024.8	1,119.6	1,097.4	1,054.0	1,028.1	15.4	15.3	14.5	14.0	11.5
European Union	640.2	857.4	717.2	1,003.4	1,020.8	9.6	11.7	9.4	13.4	11.4
Netherlands	*267.2*	*421.4*	*347.0*	*616.6*	*637.7*	*4.0*	*5.8*	*4.6*	*8.2*	*7.1*
Italy	*61.2*	*130.1*	*62.8*	*102.1*	*99.9*	*0.9*	*1.8*	*0.8*	*1.4*	*1.1*
Sweden	*53.9*	*71.8*	*63.2*	*68.3*	*66.7*	*0.8*	*1.0*	*0.8*	*0.9*	*0.7*
United Kingdom	*79.9*	*67.2*	*60.6*	*56.4*	*39.1*	*1.2*	*0.9*	*0.8*	*0.8*	*0.4*
Others	*178.0*	*166.9*	*183.6*	*160.0*	*177.4*	*2.7*	*2.3*	*2.4*	*2.1*	*2.0*
The People's Republic of China	1,102.3	934.5	1,102.5	920.7	782.7	16.6	12.8	14.5	12.3	8.7
Singapore	441.9	346.2	392.1	400.1	468.1	6.6	4.7	5.2	5.3	5.2
Japan	316.7	361.8	344.1	334.1	356.4	4.8	4.9	4.5	4.4	4.0
Korea	156.7	190.8	185.7	137.8	190.0	2.4	2.6	2.4	1.8	2.1
Myanmar	204.7	189.0	179.0	206.4	144.6	3.1	2.6	2.4	2.7	1.6
Others	1,154.3	1,231.9	1,661.1	1,263.1	1,447.8	17.2	16.8	21.9	16.9	16.2
Total	**6,655.6**	**7,322.1**	**7,591.3**	**7,512.9**	**8,964.4**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Department of Statistics

Table A.22
Principal Export Markets for Rubber

	1995	1996	1997	1998	1999	1995	1996	1997	1998	1999
	'000 tonnes					% share				
European Union	329	298	315	379	356	32.5	30.4	30.9	38.3	36.2
Germany	*69*	*73*	*76*	*92*	*100*	*6.8*	*7.4*	*7.5*	*9.3*	*10.2*
United Kingdom	*47*	*46*	*47*	*60*	*51*	*4.6*	*4.7*	*4.6*	*6.1*	*5.2*
Belgium	*41*	*35*	*44*	*57*	*48*	*4.0*	*3.6*	*4.3*	*5.8*	*4.8*
Italy	*48*	*42*	*43*	*39*	*36*	*4.7*	*4.3*	*4.2*	*3.9*	*3.6*
Netherlands	*51*	*30*	*22*	*25*	*17*	*5.0*	*3.1*	*2.2*	*2.5*	*1.7*
Others	*73*	*71*	*83*	*106*	*104*	*7.2*	*7.3*	*8.2*	*10.7*	*10.7*
United States	125	123	130	112	111	12.3	12.6	12.8	11.3	11.3
Korea	111	98	87	77	84	11.0	10.0	8.5	7.8	8.5
The People's Republic of China	40	80	52	41	66	3.9	8.2	5.1	4.1	6.7
Turkey	41	34	32	29	26	4.0	3.5	3.1	2.9	2.6
Japan	52	44	52	32	25	5.1	4.5	5.1	3.2	2.5
Others	315	303	350	319	316	31.1	30.9	34.4	32.3	32.2
Total	**1,013**	**980**	**1,018**	**989**	**984**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Department of Statistics

Table A.23
Principal Export Markets for Saw Logs

	1995	1996	1997	1998	1999	1995	1996	1997	1998	1999
	'000 cubic metres					% share				
Japan	4,060	3,613	2,856	2,222	2,280	52.4	51.7	44.7	41.0	33.8
The People's Republic of China	540	341	431	744	1,680	7.0	4.9	6.7	13.7	25.0
Taiwan	1,233	1,172	1,216	968	919	15.9	16.8	19.0	17.9	13.7
India	321	318	688	741	838	4.1	4.6	10.8	13.7	12.4
Hong Kong SAR	375	478	519	389	440	4.8	6.8	8.1	7.2	6.5
Korea	678	496	370	234	393	8.8	7.1	5.8	4.3	5.8
Thailand	304	358	209	90	95	3.9	5.1	3.3	1.7	1.4
Others	235	209	107	30	93	3.0	3.0	1.7	0.6	1.4
Total	**7,746**	**6,985**	**6,396**	**5,418**	**6,738**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Department of Statistics

Table A.24
Principal Export Markets for Sawn Timber

	1996	1997	1998	1999	1996	1997	1998	1999
	'000 cubic metres				% share			
Thailand	1,206	730	360	491	35.7	23.8	13.4	17.4
Netherlands	233	222	269	273	6.9	7.2	10.0	9.7
Singapore	353	332	260	247	10.4	10.8	9.7	8.8
Japan	339	360	217	245	10.0	11.7	8.1	8.7
Taiwan	231	233	273	213	6.8	7.6	10.2	7.6
Korea	288	232	103	159	8.5	7.6	3.8	5.6
The People's Republic of China	76	68	125	150	2.3	2.2	4.6	5.3
Hong Kong SAR	97	108	139	143	2.9	3.5	5.2	5.1
United Arab Emirates	56	66	85	78	1.7	2.2	3.2	2.8
Belgium	64	71	82	71	1.9	2.3	3.0	2.5
Republic of Yemen	81	44	106	70	2.4	1.4	4.0	2.5
United Kingdom	59	52	65	69	1.8	1.7	2.4	2.5
Germany	30	35	31	39	0.9	1.2	1.2	1.4
Others	266	514	568	570	7.8	16.8	21.2	20.1
Total	**3,379**	**3,067**	**2,683**	**2,818**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Department of Statistics

Table A.25
Principal Export Markets for Crude Oil

	1996	1997	1998	1999	1996	1997	1998	1999
	'000 tonnes				% share			
Korea	2,022	2,393	2,328	2,540	11.6	15.1	12.9	14.3
India	863	1,050	1,958	2,387	4.9	6.6	10.9	13.5
Thailand	4,913	3,735	3,206	2,306	28.1	23.5	17.8	13.0
Australia	307	321	1,089	2,087	1.8	2.0	6.0	11.8
Japan	3,929	2,722	2,108	2,004	22.5	17.1	11.7	11.3
Indonesia	683	882	2,127	1,658	3.9	5.6	11.8	9.4
United States	285	535	926	1,143	1.6	3.4	5.1	6.4
Myanmar	335	564	636	633	1.9	3.6	3.5	3.6
Singapore	2,264	1,829	1,094	626	12.9	11.5	6.1	3.5
New Zealand	587	332	459	603	3.4	2.1	2.5	3.4
The Philippines	437	547	617	553	2.5	3.4	3.4	3.1
Sri Lanka	305	296	366	353	1.7	1.9	2.0	2.0
Taiwan	248	244	252	244	1.4	1.5	1.4	1.4
Others	317	421	849	588	1.8	2.7	4.7	3.3
Total	**17,495**	**15,872**	**18,013**	**17,725**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Department of Statistics

Table A.26
External Debt and Debt Servicing

	1995	1996	1997	1998	1999*p*
	RM million				
Medium and long-term					
Gross borrowing	**21,310**	**22,485**	**25,235**	**18,699**	**17,221**
Federal Government	*442*	*749*	*462*	*4,001*	*4,763*
NFPEs	*9,952*	*8,128*	*9,371*	*4,705*	*6,080*
Private sector	*10,916*	*13,608*	*15,402*	9,993	6,378
Repayment and prepayment	**11,155**	**15,958**	**11,862**	**13,520**	**12,266**
Federal Government	*2,077*	*2,926*	*2,143*	*2,181*	*1,840*
NFPEs	*2,184*	*5,284*	*3,006*	*4,344*	*2,230*
Private sector	*6,894*	*7,748*	*6,713*	6,995	8,196
Net borrowing	**10,155**	**6,527**	**13,373**	**5,179**	**4,954**
Federal Government	*–1,635*	*–2,177*	*–1,681*	*1,819*	*2,923*
NFPEs	*7,768*	*2,844*	*6,365*	*361*	*3,850*
Private sector	*4,022*	*5,860*	*8,689*	2,998	–1,818
Outstanding debt	**68,811**	**72,682**	**127,500**	**129,778**	**136,848**
Federal Government	*13,331*	*10,470*	*12,952*	*14,924*	*18,369*
NFPEs	*27,400*	*29,239*	*52,467*	*53,231*	*58,641*
Private sector	*28,080*	*32,973*	*62,081*	61,623	59,838
% GNP	*32.4*	*30.0*	*47.8*	*48.2*	*48.8*
% exports of goods and services	*32.0*	*30.5*	*47.4*	*39.3*	*36.8*
Annual growth (%)	*15.9*	*5.6*	*75.4*	1.8	5.4
Currency composition (% share)	**100**	**100**	**100**	**100**	**100**
U.S. Dollar	*65*	*72*	*76*	*74*	*72*
Japanese yen	*22*	*16*	*15*	*18*	*21*
Other	*13*	*12*	*9*	8	7
Short-term					
Outstanding debt	**16,204**	**25,151**	**43,257**	**32,237**	**22,848**
Banking	*11,293*	*17,053*	*32,276*	*20,339*	*13,848*
Non-bank private sector	*4,911*	*8,098*	*10,981*	*11,898*	*9,000*
Total external debt	**85,015**	**97,833**	**170,757**	**162,015**	**159,696**
% GNP	*40.1*	*40.4*	*64.0*	*60.2*	*57.0*
% exports of goods and services	*39.5*	*41.0*	*63.5*	*49.0*	*43.0*
Annual Growth (%)	*15.5*	*15.1*	*74.5*	–5.1	–1.4
Total servicing (including short-term interest payment)	**14,115**	**16,262**	**14,718**	**21,298**	**19,545**
of which:					
Medium and long-term					
Repayment (excluding prepayment)	**10,133**	**11,019**	**8,322**	**13,152**	**12,266**
Federal Government	*2,077*	*1,792*	*1,232*	*2,181*	*1,840*
NFPEs	*1,570*	*2,442*	*1,447*	*4,344*	*2,230*
Private sector	*6,486*	*6,785*	*5,642*	6,626	8,196
Interest payment	**2,876**	**3,603**	**4,378**	**5,807**	**5,666**
Federal Government	*886*	*751*	*637*	*1,031*	*883*
NFPEs	*1,074*	*1,392*	*1,862*	*2,823*	*2,727*
Private sector	*916*	*1,460*	*1,879*	1,953	2,056
Debt service ratio (% exports of goods and services)					
Total debt	6.6	6.8	5.5	6.4	5.3
Medium and long-term debt	6.0	6.1	4.7	5.7	4.8
Federal Government	*1.4*	*1.1*	*0.7*	*1.0*	*0.7*
NFPEs	*1.2*	*1.6*	*1.2*	*2.2*	*1.3*
Private sector	*3.4*	*3.5*	*2.8*	*2.5*	*2.8*

p Preliminary

Source: Ministry of Finance and Bank Negara Malaysia.

Table A.27
Gross Malaysian Investment Overseas by Country[1]

Countries	1995	1996	1997	1998	1999
	RM million				
Singapore	2,185	1,806	1,783	2,081	1,634
France	17	99	90	206	1,230
United States	544	1,416	1,334	1,650	1,017
Belgium	7	18	2	21	849
Mauritius	–	15	18	211	790
United Kingdom	793	1,308	1,716	812	568
Indonesia	328	414	648	192	380
The People's Republic of China	331	514	327	75	201
Pakistan	6	4	5	5	192
Bermuda	21	23	–	99	173
Hong Kong SAR	816	769	936	162	160
Japan	93	641	149	64	158
Virgin Islands (British)	8	183	17	227	149
Vietnam	102	129	142	61	142
Cayman Islands	206	1	–	34	122
Australia	592	471	505	115	104
Netherlands	143	21	109	266	104
India	14	17	35	30	101
Thailand	89	129	133	537	97
Philippines	646	375	299	103	94
Switzerland	89	62	186	13	85
Myanmar	–	17	8	83	79
Turkmenistan	–	–	–	16	62
Spain	–	15	3	1	43
South Africa	68	1,183	147	42	33
Germany	12	18	110	13	32
Taiwan, ROC	40	112	100	74	25
United Arab Emirates	11	5	7	8	20
Other	775	950	1,649	1,212	1,724
- of which Labuan[2]	*194*	*318*	*824*	*876*	*1,432*
Total	**7,936**	**10,715**	**10,458**	**8,413**	**10,368**

[1] Refers to direct equity investment, purchase of real estate abroad and extension of loans to non-residents. Does not include retained earnings overseas.
[2] Labuan IOFC is treated as a non-resident for exchange control purposes.

Source: Cash BOP Reporting System, Bank Negara Malaysia.

Table A.28
Consumer Price Index (1994=100)

	Weights	1995	1996	1997	1998	1999
		Annual change (%)				
Total	100.0	3.4	3.5	2.7	5.3	2.8
Of which:						
Food	34.9	4.9	5.7	4.1	8.9	4.6
Beverages and tobacco	3.6	2.3	2.2	1.3	4.3	7.9
Clothing and footwear	3.6	0.0	–0.7	–0.5	0.4	–2.0
Gross rent, fuel and power	21.1	3.4	3.2	3.2	4.4	1.6
Furniture, furnishings and household equipment and operation	5.6	2.8	1.1	0.1	3.9	1.3
Medical care and health expenses	1.9	3.1	3.7	3.6	6.2	3.1
Transport and communication	17.9	1.8	1.4	0.6	–0.1	0.5
Recreation, entertainment, education and cultural services	5.8	2.5	3.3	0.4	3.3	2.6
Miscellaneous goods and services	5.6	4.2	2.5	4.6	7.1	1.5
Peninsular Malaysia	100.0	3.7	3.8	2.8	5.5	2.9
Sabah	100.0	2.8	2.8	2.0	4.3	2.4
Sarawak	100.0	2.2	2.2	1.7	4.2	1.6
Durable goods	10.0	1.9	1.4	–0.7	0.4	–0.5
Semi-durable goods	5.5	0.2	1.2	–0.3	1.4	–0.9
Non-durable goods	41.2	4.1	4.0	2.6	6.9	4.2
Services	43.3	3.6	3.7	3.8	5.2	2.3

Source: Department of Statistics

Table A.29
Consumer Price Index for Food

	Weights	1995	1996	1997	1998	1999
		Annual change (%)				
Food	34.9	4.9	5.7	4.1	8.9	4.6
Of which:						
Food at home	25.1	5.3	6.0	3.7	9.1	4.8
Rice, bread and other cereals	5.5	1.4	7.4	3.6	6.9	4.2
Meat	3.8	0.8	4.7	3.4	8.1	–0.3
Fish	4.9	12.1	11.7	7.2	9.1	10.8
Milk and eggs	2.3	–0.4	4.0	1.6	4.7	3.7
Oils and fats	0.7	11.2	0.2	–0.7	5.2	1.7
Fruits and vegetables	5.4	8.7	3.0	2.6	14.1	3.5
Sugar	0.6	0.7	0.8	0.3	19.3	1.4
Coffee and tea	0.8	4.6	0.5	0.8	10.1	3.6
Other foods	1.1	2.7	4.4	0.7	4.2	4.4
Food away from home	9.8	3.7	5.2	5.3	8.4	4.3

Source: Department of Statistics

Table A.30
Producer Price Index (1989=100)

	Weights	1995	1996	1997	1998	1999
		Annual change (%)				
Domestic Economy	100.0	3.9	2.3	2.7	10.7	–3.3
Of which:						
Food and live animals	14.9	2.4	5.5	2.3	8.5	–2.3
Beverages and tobacco	2.1	2.3	0.5	0.1	1.5	10.2
Crude materials	18.0	7.0	–1.5	–4.9	3.0	–2.7
Mineral fuels, lubricants and related materials	18.8	–0.3	12.5	7.0	–2.6	14.2
Animal and vegetable oils and fats	8.5	26.0	–5.8	12.9	63.8	–29.4
Chemicals and related products	4.4	2.2	1.0	1.2	4.7	1.5
Manufactured goods	10.8	–0.1	0.8	0.1	6.8	–0.9
Machinery and transport equipment	18.3	–1.8	0.5	3.4	5.9	–0.5
Miscellaneous manufactured articles	3.6	2.3	3.4	–1.2	5.4	1.4
Commodities and other transactions	0.6	–0.4	0.3	–0.5	2.1	–0.9
Local Production	79.3	4.8	2.8	2.5	11.2	–3.9
Imports	20.7	0.7	0.1	2.8	9.2	–0.6

Source: Department of Statistics

Table A.31
House Price Indicators (MHPI, 1990=100)

	1995	1996	1997	1998	1999 1st half
	Annual change (%)				
Total	18.4	12.9	1.9	–9.4	–12.0
By type					
Terraced	13.1	10.2	10.0	–4.8	–7.8
Semi-Detached	9.8	8.1	2.9	–8.1	–10.9
Detached	15.7	14.1	4.3	–13.6	–13.4
High-Rise Unit	4.2	–1.0	–4.8	–6.2	–5.0
By region					
Klang Valley	15.9	15.7	4.4	–14.5	–10.2
Johor Bahru	16.6	14.3	0.1	–25.3	–8.7
Penang Island	11.2	4.3	4.3	–12.9	–8.2
Seremban-Sepang	11.4	18.6	7.8	–4.9	1.4
Ipoh-Kinta	6.7	6.8	5.0	–4.2	7.0

Source: Valuation and Property Services Department

Table A.32
Average Monthly Rentals and Occupancy Rates for Office and Retail Space in the Klang Valley[1]

	Office Space			Retail Space		
	Monthly Rental		Occupancy Rate	Monthly Rental		Occupancy Rate
	RM/sq.m	% change	%	RM/sq.m	% change	%
1996	50.5	8.1	95.5	122.0	0.0	92.8
1997	49.8	–1.3	94.9	136.1	11.6	90.5
1998	42.5	–14.7	79.8	94.0	–30.9	59.5
1999	40.6	–4.5	76.2	91.8	–2.3	76.6

[1] Refers to Kuala Lumpur & Selangor D.E.

Source : BNM, Valuation & Property Services Department

Table A.33
Wages in Private Sector[1]

Sector	No. of wage agreements		No. of workers involved		Average wages (Weighted increase in %)	
	1998	1999	1998	1999	1998	1999
Manufacturing	146	134	37,283	27,596	8.0	–1.1
Transport	37	31	42,385	4,989	6.1	2.1
Commerce	52	17	50,444	10,054	13.8	3.1
Services	23	30	4,260	3,452	10.1	–1.7
Agriculture	11	30	6,665	54,231	8.9	–19.5
Electricity	1	8	152	31,116	10.0	–0.8
Mining	4	6	160	524	10.6	–8.5
Construction	–	2	–	88	–	0.0
Others	10	10	1,173	956	6.0	–1.6
Total	**284**	**268**	**142,522**	**133,006**	**9.6**	**–8.8**

[1] Based on collective wage agreements in the private sector which are of 3-year duration.
– No collective wage agreements were concluded.

Source: Industrial Courts
Bank Negara Malaysia

Table A.34
Labour Market Indicators

	1995	1996	1997	1998	1999
Labour force ('000)	8,257	8,641	9,038	8,881	9,010
(annual change in %)	5.2	4.7	4.6	–1.7	1.5
Employment (annual change in %)	5.0	5.3	4.6	–2.5	1.7
Unemployment rate (% of labour force)	3.1	2.5	2.4	3.2	3.0
Labour productivity growth (GDP/Employment)	4.6	4.4	2.8	–5.1	3.7
Average real wages in manufacturing sector (annual change in %)	5.1	6.8	5.9	–2.4	2.7
Employment by sector ('000)					
Agriculture, forestry & fishing	1,493	1,492	1,468	1,401	1,389
Mining	41	41	42	42	42
Manufacturing	2,028	2,230	2,375	2,277	2,379
Construction	717	796	876	810	804
Electricity, gas and water	67	71	69	70	72
Wholesale & retail trade, hotels and restaurants	1,324	1,376	1,451	1,437	1,449
Finance, insurance, real estate and business services	373	392	429	418	420
Transport, storage and communication	395	410	434	435	442
Government services	870	871	873	875	877
Other services	693	748	802	832	867
Total	**7,999**	**8,426**	**8,817**	**8,597**	**8,741**
Services	3,721	3,868	4,057	4,067	4,127

Source: Economic Planning Unit
Department of Statistics
Bank Negara Malaysia

Table A.35
Broad Money (M3)

	Annual change					As at end 1999
	1995	1996	1997	1998	1999	
	RM million					(RM million)
Broad money (M3)[1]	49,619	57,759	61,102	10,650	33,097	434,556
(Annual growth in %)	(22.3)	(21.2)	(18.5)	(2.7)	(8.2)	(8.2)
Currency[2]	1,529	1,525	2,339	–3,176	5,995	23,978
Demand deposits	4,548	6,209	80	–5,743	12,354	48,899
Broad quasi money	43,541	50,025	58,683	19,570	14,747	361,680
Fixed deposits	*31,172*	*41,586*	*46,138*	*14,909*	*29,883*	*289,884*
Savings deposits	*1,294*	*6,061*	*–3,711*	*1,259*	*7,927*	*40,451*
NIDs	*9,408*	*–2,047*	*10,117*	*974*	*–21,864*	*5,769*
Repos	*1,667*	*2,572*	*3,837*	*1,052*	*–2,563*	*18,680*
Foreign currency deposits[3]	*n.a*	*1,853*	*2,302*	*1,376*	*1,365*	*6,896*
Factors Affecting M3						
Net lending to Government	–3,852	–2,858	510	–12,290	2,166	–18,849
Lending to Government	229	2,521	1,856	5,194	–2,892	22,337
Less: Government deposits	4,081	5,380	1,346	17,485	–5,059	41,186
Private sector credit[4]	64,154	72,383	90,360	17,696	14,139	479,422
Net external assets[5]	–3,256	1,521	–16,788	51,156	28,959	123,599
Other influences	–7,427	–13,286	–12,980	–45,912	–12,167	–149,615

[1] Excludes interplacements among banking institutions.
[2] Excludes holdings by banking system.
[3] Prior to December 1996, foreign currency deposits were subsumed under its respective category of deposits.
[4] Includes write-offs and loans sold to Danaharta.
[5] BNM net of banking system.
n.a. Not available

Table A.36
Money Supply: Annual Change and Growth Rates

	M3[5]													
			M2[3]										Deposits (incl. NIDs and repos) with other banking inst.[4]	
					M1[1]						Narrow quasi money[2]			
	Total		Total		Total		Currency		Demand deposits					
	RM m	%	RM m	%	RM m	%	RM m	%	RM m	%	RM m	%	RM m	%
1995	49,619	22.3	38,508	24.0	5,453	11.7	1,557	9.8	3,896	12.8	33,055	29.0	11,111	17.9
1996	57,759	21.2	39,335	19.8	8,661	16.7	1,552	8.9	7,109	20.6	30,674	20.9	18,424	25.2
1997	61,102	18.5	54,009	22.7	2,780	4.6	2,402	12.6	377	0.9	51,229	28.8	7,093	7.8
1998	10,650	2.7	4,255	1.5	–9,230	–14.6	–3,188	–14.9	–6,043	–14.4	13,485	5.9	6,395	6.5
1999	33,097	8.2	34,436	11.6	18,184	33.6	6,627	36.3	11,557	32.2	16,253	6.7	–1,339	–1.3

[1] Currency in circulation and demand deposits of the private sector.
[2] Comprising savings and fixed deposits of the private sector placed with Bank Negara and commercial banks, net NIDs and repos by commercial banks.
[3] M1 plus narrow quasi money.
[4] Comprising savings and fixed deposits of the private sector placed with the finance companies, merchant banks, discount houses and Bank Islam, net NIDs issued by the relevant banking institutions and repos; excludes interplacements among these financial institutions and with commercial banks.
[5] M2 plus deposits (including NIDs and repos) with other banking institutions.

Table A.37
Interest Rates

	Average rates at end-year				Average rates at end-month in 1999											
	1995	1996	1997	1998	Jan.	Feb.	Mar.	Apr.	May	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.
	% per annum															
3-month interbank	6.76	7.39	8.70	6.46	6.40	6.42	5.70	3.80	3.30	3.30	3.27	3.20	3.17	3.15	3.18	3.18
Commercial banks																
Fixed deposit:																
3–month	6.64	7.21	9.06	5.83	5.72	5.59	5.44	4.00	3.75	3.75	3.75	3.75	3.75	3.33	3.33	3.33
12–month	6.89	7.26	9.33	5.74	5.66	5.54	5.40	4.06	3.80	3.80	3.79	3.79	3.79	3.93	3.93	3.95
Savings deposit	3.70	4.10	4.23	3.87	3.81	3.76	3.70	3.24	2.93	2.92	2.87	2.89	2.85	2.78	2.74	2.76
Base lending rate (BLR)	8.03	9.18	10.33	8.04	8.04	8.04	8.04	7.64	7.24	7.24	7.24	6.79	6.79	6.79	6.79	6.79
Finance companies																
Fixed deposit:																
3–month	6.79	7.32	10.32	6.43	6.30	6.00	5.80	4.16	3.83	3.80	3.80	3.81	3.81	3.47	3.46	3.49
12–month	6.98	7.36	10.25	6.57	6.47	6.13	5.90	4.26	3.97	3.97	3.99	4.04	4.08	4.05	4.06	4.13
Savings deposit	4.70	5.02	5.49	5.01	5.04	4.90	4.82	4.01	3.77	3.72	3.69	3.62	3.57	3.54	3.54	3.50
Base lending rate (BLR)	9.38	10.65	12.22	9.50	9.50	9.50	9.50	9.00	8.50	8.50	8.50	7.95	7.95	7.95	7.95	7.95
Treasury bills (91 days)	5.92	6.39	6.76	5.31	5.56	5.32	5.40	3.44	2.60	2.73	2.75	2.80	2.82	2.68	2.81	2.71
Government securities (1 year)	6.70	6.70	7.01	5.79	5.95	5.64	5.32	3.63	3.05	2.85	3.33	3.74	3.51	3.31	3.43	3.37
Government securities (5 years)	6.50	6.55	7.75	6.66	6.61	6.38	6.10	5.50	5.40	5.29	5.52	5.83	5.33	5.16	5.21	5.21

Table A.38
Consolidated Public Sector Finance

	1995	1996	1997	1998	1999*p*
	RM million				
General government					
Revenue	62,272	70,944	81,527	69,595	71,006
% growth	*1.9*	*13.9*	*14.9*	*–14.6*	*2.0*
Operating expenditure	41,394	50,463	51,884	50,179	54,061
% growth	*2.1*	*21.9*	*2.8*	*–3.3*	*7.7*
Current account	20,878	20,481	29,643	19,416	16,945
NFPEs					
Revenue	48,335	57,380	69,713	73,447	86,395
% growth	*11.6*	*18.7*	*21.5*	*5.4*	*17.6*
Operating expenditure	32,342	37,032	42,033	49,529	55,389
% growth	*13.4*	*14.5*	*13.5*	*17.8*	*11.8*
Current account	15,993	20,348	27,680	23,918	31,006
Public sector current account	**36,871**	**40,829**	**57,323**	**43,334**	**47,951**
(% of GNP)	***17.4***	***16.9***	***21.5***	***16.1***	***17.1***
Net development expenditure	29,801	30,818	39,992	46,827	47,370
% growth	*3.6*	*3.4*	*29.8*	*17.1*	*1.2*
General government	16,171	15,306	18,651	17,168	21,823
% growth	*28.8*	*–5.3*	*21.9*	*–8.0*	*27.1*
NFPEs	13,630	15,512	21,341	29,659	25,547
% growth	*–15.8*	*13.8*	*37.6*	*39.0*	*–13.9*
Overall balance	**7,070**	**10,011**	**17,331**	**–3,493**	**581**
(% of GNP)	***3.3***	***4.1***	***6.5***	***–1.3***	***0.2***
General government	4,707	5,175	10,992	2,248	–4,878
NFPEs	2,363	4,836	6,339	–5,741	5,459

p Preliminary

Source: Ministry of Finance, state governments and non-financial public enterprises.

Table A.39
Major Industrial Countries: Key Economic Indicators

	1995	1996	1997	1998	1999*e*	2000*f*
	Annual change (%)					
REAL GDP						
Major Industrial Countries	**2.3**	**3.1**	**3.2**	**2.4**	**2.7**	**2.7**
United States	2.7	3.7	4.5	4.3	4.1	3.5
Japan	1.5	5.0	1.6	–2.5	0.3	1.0
Euro-11 Area	2.3	1.4	2.3	2.8	2.1	2.8
Germany	1.7	0.8	1.5	2.2	1.5	2.3
United Kingdom	2.8	2.6	3.5	2.2	2.0	2.7
INFLATION						
Major Industrial Countries	**2.3**	**2.2**	**2.0**	**1.4**	**1.5**	**1.8**
United States	2.8	2.9	2.3	1.6	2.2	2.5
Japan	–0.1	0.1	1.7	0.7	–0.3	0.0
Euro-11 Area	2.8	2.3	1.6	1.1	1.1	1.7
Germany	1.7	1.2	1.5	1.0	0.6	1.3
United Kingdom[1]	2.8	3.0	2.8	2.7	2.3	2.2
	% of labour force					
UNEMPLOYMENT						
Major Industrial Countries						
United States	5.6	5.4	4.9	4.5	4.2	4.2
Japan	3.1	3.4	3.4	4.1	4.7	4.7
Euro-11 Area	11.4	11.7	11.7	10.9	10.2	9.6
Germany	8.1	8.8	9.8	9.3	9.0	8.7
United Kingdom	8.1	7.4	5.7	4.7	4.4	4.2
	% of GDP					
CURRENT ACCOUNT BALANCE						
Major Industrial Countries						
United States	–1.5	–1.7	–1.7	–2.5	–3.6	–3.9
Japan	2.1	1.4	2.3	3.2	2.4	2.9
Euro-11 Area	0.8	1.2	1.7	1.3	0.8	0.7
Germany	–0.8	–0.2	–0.1	–0.2	0.0	0.1
United Kingdom	–0.5	–0.1	0.8	0.0	–1.5	–1.5
FISCAL BALANCE						
Major Industrial Countries						
United States	–1.9	–0.9	0.4	1.3	1.6	2.0
Japan	–3.6	–4.2	–3.4	–5.3	–7.3	–7.1
Euro-11 Area	–5.2	–4.2	–2.5	–2.1	–1.8	–1.2
Germany	–3.2	–3.4	–2.6	–2.0	–1.9	–1.1
United Kingdom	–5.8	–4.4	–2.1	0.3	–0.4	–0.6

[1] Refers to retail price index excluding mortgage interest
e Estimate
f Forecast

Source: IMF World Economic Outlook, October 1999
OECD Economic Outlook, December 1999
Datastream

Table A.40
East Asia: Key Economic Indicators

	1995	1996	1997	1998	1999*e*	2000*f*
Real GDP	Annual change (%)					
Asian NIEs	**7.0**	**6.2**	**5.9**	**–1.8**	**6.8**	**6.3~6.5**
Korea	8.9	6.8	5.0	–5.8	10.2	7.2
Taiwan	6.4	6.1	6.7	4.6	5.7	6.5
Singapore	8.1	7.6	8.9	0.3	5.4	4.5~6.5
Hong Kong SAR	3.9	4.5	5.0	–5.1	2.9	5.0
ASEAN[1]	**8.2**	**7.5**	**4.7**	**–6.1**	**3.6**	**4.4~5.0**
Malaysia	9.8	10.0	7.5	–7.5	5.4	5.8
Thailand	8.8	5.9	–1.8	–10.4	4.0	4.5
Indonesia	8.2	7.8	4.7	–13.2	0.2	3.0~4.0
Philippines	4.7	5.8	5.2	–0.5	3.2	4.0
Vietnam	9.5	9.3	8.8	5.8	4.8	5.5~6.0
The People's Republic of China	10.5	9.6	8.8	7.8	7.1	7.0
Consumer prices						
Asian NIEs	**5.0**	**4.3**	**3.4**	**4.0**	**–0.4**	**1.7~1.8**
Korea	4.5	4.9	4.5	7.5	0.8	3.1
Taiwan	3.7	3.1	0.9	1.7	0.2	2.0
Singapore	1.7	1.4	2.0	–0.3	0.4	1.0~2.0
Hong Kong SAR[2]	9.0	6.3	5.9	2.8	–4.0	–1.0
ASEAN[1]	**7.2**	**6.1**	**4.8**	**19.9**	**7.9**	**4.0~4.9**
Malaysia	3.4	3.5	2.7	5.3	2.8	3.2
Thailand	5.8	5.6	5.6	8.1	0.3	2.5~3.0
Indonesia	9.4	8.0	6.2	58.4	24.0	5.0~7.0
Philippines	8.0	9.1	5.9	9.8	6.4	6.0~7.0
Vietnam	17.0	5.8	3.2	7.7	1.3	6.0
The People's Republic of China	16.9	8.3	2.8	–0.8	–1.4	1.0
Current account balance	US$ billion					
Asian NIEs	**–**	**–**	**7.7**	**63.9**	**–**	**–**
Korea	–8.5	–23.0	–8.2	40.6	25.0	11.5
Taiwan	5.5	10.9	7.1	3.4	5.9	5.2
Singapore	14.4	14.5	15.0	17.6	12.8[6]	n.a.
Hong Kong SAR[3]	n.a.	n.a.	–6.2	2.3	n.a.	n.a.
ASEAN[1]	–	–	–	–	–	–
Malaysia	–8.6	–4.5	–5.6	9.4	12.5	11.2
Thailand	–13.5	–14.2	–3.1	14.3	11.3	7.9
Indonesia	–6.8	–7.7	–5.0	4.1	5.4	4.2
Philippines	–3.3	–3.9	–4.4	1.1	6.4[4]	5.1
Vietnam	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
The People's Republic of China	16.2	72.4	29.7[5]	29.3	n.a.	n.a.
Current account balance	% of GDP					
Korea	–1.7	–4.4	–1.7	9.4	n.a.	n.a.
Taiwan	2.1	4.0	2.7	1.3	2.1	1.6
Singapore	17.3	15.9	15.7	20.9	20.2[6]	n.a.
Hong Kong SAR[3]	n.a.	n.a.	–3.6	1.4	n.a.	n.a.
Malaysia	–9.7	–4.4	–5.6	12.9	15.8	13.2
Thailand	–8.0	–7.9	–2.0	11.4	9.1	6.0
Indonesia	–3.3	–3.4	–2.3	4.1	3.8	2.5
Philippines	–4.3	–4.6	–5.1	1.6	8.0[6]	6.3
Vietnam	–10.1	–10.3	–6.5	–4.3	–3.0	–2.8
The People's Republic of China	2.3	8.8	3.3[5]	3.0	1.3	1.1

Table A.40
East Asia: Key Economic Indicators (continued)

	1995	1996	1997	1998	1999*e*	2000*f*
Fiscal balance[7]	% of GDP					
Korea	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Taiwan	–0.4	–0.1	–0.3	1.9	0.7	n.a.
Singapore	6.2	6.0	1.1	2.4	1.9	1.5
Hong Kong SAR	–0.3	2.2	6.6	–1.8	–3.0	n.a.
Malaysia	0.8	0.7	2.4	–1.8	–3.2	–4.2
Thailand	3.0	2.3	–0.7	–2.5	–2.9	n.a.
Indonesia	2.2	1.4	1.3	–2.6	–3.4	–5.0
Philippines	0.6	0.3	0.1	–1.9	–3.7	–1.9
Vietnam	–1.6	–1.5	–1.5	n.a.	n.a.	n.a.
The People's Republic of China	–1.0	–0.8	–0.8	–1.2	n.a.	n.a.
Unemployment	% of labour force					
Korea	2.0	2.0	2.6	6.8	6.3	4.0
Taiwan	1.8	2.6	2.7	2.7	2.9	2.9
Singapore	2.7	3.0	2.4	3.2	4.6	n.a.
Hong Kong SAR	3.2	2.8	2.2	4.7	6.1	n.a.
Malaysia	3.1	2.5	2.4	3.2	3.0	2.9
Thailand	1.2	1.1	0.9	3.5	4.1	n.a.
Indonesia	7.2	4.9	4.6	5.5	6.3	n.a.
Philippines	9.5	8.6	8.7	10.1	9.7	n.a.
Vietnam	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
The People's Republic of China[8]	2.9	3.0	3.1	3.1	3.3	3.5
Gross national savings	% of GNP					
Korea	35.5	33.8	33.5	33.5	n.a.	n.a.
Taiwan[9]	27.1	26.8	26.5	26.1	26.2	25.7
Singapore	50.3	51.2	51.8	52.0	n.a.	n.a.
Hong Kong SAR	32.4	30.7	31.9	32.0	n.a.	n.a.
Malaysia	35.6	38.9	39.4	41.9	40.8	38.4
Thailand[9]	33.4	33.6	32.4	34.3	31.9	30.2
Indonesia	25.9	26.9	26.8	27.7	25.0	24.0
Philippines	17.5	18.5	18.8	21.0	18.8	n.a.
Vietnam[10]	16.1	17.8	21.5	24.6	22.0	23.0
The People's Republic of China	41.5	40.2	38.9	39.0	n.a.	n.a.

1 Includes Singapore, but excludes Brunei Darussalam, Lao PDR, Myanmar and Cambodia
2 Refers to composite prices
3 Refers to balance of goods and services. The first set of Balance of Payments statistics was released in April 1999 for the reference year of 1997
4 January-November
5 Statistics methods changed significantly since that year
6 1st three quarters
7 Central government balance
8 Registered rates only
9 As % of GDP
10 Gross domestic savings as % of GDP
e Estimates
f Forecast
n.a. Not available

Sources: ADB, Asian Development Outlook 1999
IMF, International Financial Statistics
IMF, World Economic Outlook, October 1999
National sources

Table A.41
World Trade[1]

	1995	1996	1997	1998	1999[2]
	Annual change (%)				
World trade	**9.4**	**6.8**	**9.9**	**3.6**	**3.7**
	% share of world trade				
United States	**13.7**	**14.0**	**14.3**	**15.0**	**15.3**
Japan	**7.6**	**7.2**	**6.7**	**6.1**	**6.2**
European Union	**37.8**	**33.7**	**34.8**	**36.4**	**37.5**
Germany	9.2	8.8	8.7	9.1	8.9
United Kingdom	4.8	4.9	5.2	5.3	4.9
Asia[3]	**18.1**	**18.2**	**18.1**	**16.7**	**17.0**
People's Republic of China	3.7	3.9	4.0	4.0	4.0
India	0.7	0.7	0.7	0.7	0.7
Asian NIEs	**8.7**	**8.5**	**8.4**	**7.5**	**5.9**
Hong Kong SAR	2.2	2.1	2.2	2.0	2.2
Korea	2.3	2.3	2.2	1.9	2.0
Singapore	2.0	2.0	1.9	1.7	1.7
Taiwan	2.2	2.1	2.1	2.0	0.0
ASEAN[4]	**6.3**	**6.5**	**6.3**	**5.4**	**5.4**
Indonesia	0.8	0.9	0.9	0.7	0.7
Malaysia	1.6	1.6	1.6	1.3	1.3
Phillipines	0.5	0.6	0.6	0.6	0.6
Thailand	1.2	1.2	1.1	0.9	0.9
Vietnam	0.2	0.2	0.2	0.2	0.2
Latin America[5]	**4.8**	**5.1**	**5.4**	**5.6**	**5.4**
Argentina	0.4	0.4	0.5	0.5	0.4
Brazil	1.0	1.0	1.1	1.1	0.9
Chile	0.3	0.3	0.3	0.3	0.3
Mexico	1.4	1.6	1.8	2.0	2.1
Emerging Markets					
South Africa	0.5	0.5	0.5	0.5	0.5
Russia	1.3	1.4	1.3	1.1	1.1

[1] Refers to trade in goods.
[2] Refers to first half, except for world trade data, which is a forecast.
3/ Excludes Japan.
[4] Includes Singapore, but excludes Brunei Darussalam, Lao PDR, Myanmar and Cambodia.
[5] Latin America refers to Western Hemisphere.

Source : IMF World Economic Outlook, October 1999
IMF Direction of Trade Statistics

Table A.42
Sources and Uses of Funds of the Financial System

	1995	1996	1997	1998	1999*p*
	(Outstanding in RM million)				
Sources of Funds:					
Capital, reserves and profit	78,696.4	109,427.6	106,323.6	103,278.3	109,615.0
Currency	18,913.2	21,065.6	24,532.3	20,547.4	30,483.1
Demand deposits	46,155.8	56,231.9	57,672.4	65,110.8	74,972.6
Other deposits[1] (of which):	290,224.5	355,979.8	436,995.6	440,211.2	485,656.8
Public sector	*41,420.7*	*35,937.0*	*37,444.1*	*39,314.3*	*45,243.3*
Other financial institutions[2]	*71,422.8*	*81,541.6*	*103,823.9*	*90,319.3*	*117,269.1*
Private sector	*171,804.3*	*233,134.1*	*287,729.2*	*302,564.1*	*316,146.7*
Foreign	*5,576.7*	*5,367.1*	*7,998.4*	*8,013.5*	*6,997.7*
Borrowings	6,322.4	8,365.8	32,683.5	8,652.3	8,486.4
Funds from other financial institutions	78,122.3	99,169.7	154,602.0	71,077.6	72,720.5
Domestic[2]	*61,695.0*	*77,218.5*	*113,986.0*	*45,171.9*	*52,074.8*
Foreign	*16,427.3*	*21,951.2*	*40,616.0*	*25,905.7*	*20,645.8*
Insurance, provident and pension funds	127,055.4	146,888.5	168,451.1	187,734.3	212,988.2
Other liabilities	102,074.0	121,913.9	133,277.0	199,150.6	176,054.4
Total Liabilities	**747,564.0**	**919,042.8**	**1,114,537.4**	**1,095,762.5**	**1,170,977.1**
Uses of Funds:					
Currency	1,929.3	2,804.6	4,046.0	3,283.3	7,886.1
Deposits with other financial institutions	139,216.6	146,612.2	219,083.8	151,851.9	180,620.7
Domestic	*130,830.7*	*139,228.4*	*200,922.3*	*136,798.3*	*165,222.6*
Foreign	*8,385.9*	*7,383.8*	*18,161.5*	*15,053.6*	*15,398.2*
Bills	16,391.6	16,312.6	21,433.2	10,360.3	16,432.9
Treasury	*3,887.4*	*1,916.8*	*3,912.3*	*3,786.1*	*3,677.0*
Commercial	*12,504.2*	*14,395.8*	*17,521.0*	*6,574.2*	*12,755.8*
Loans and advances	305,751.1	384,261.1	485,615.7	484,333.2	471,857.6
Public sector	*4,582.0*	*3,966.3*	*2,661.9*	*5,566.6*	*4,417.7*
Other financial institutions	*26,069.8*	*13,615.5*	*20,615.6*	*28,995.5*	*25,717.4*
Private sector	*274,075.1*	*364,697.2*	*459,250.0*	*446,939.1*	*438,923.2*
Foreign	*1,024.2*	*1,982.1*	*3,088.2*	*2,832.1*	*2,799.4*
Securities	160,280.7	202,520.6	207,091.7	224,597.7	239,505.7
Malaysian government	*61,532.8*	*67,626.9*	*66,090.7*	*71,543.0*	*75,149.7*
Foreign	*92.8*	*491.4*	*1,289.6*	*1,253.2*	*1,507.5*
Corporate	*53,575.6*	*124,458.0*	*132,211.6*	*145,006.5*	*156,752.2*
Others	*45,079.5*	*9,944.3*	*7,499.8*	*6,806.7*	*6,096.3*
Gold and forex reserves	61,681.9	67,864.6	57,032.1	96,264.9	113,765.9
Other assets	62,312.8	98,667.2	120,234.9	125,071.1	140,908.2
Total Assets	**747,564.0**	**919,042.8**	**1,114,537.4**	**1,095,762.5**	**1,170,977.1**

1 Equal savings, fixed and other (NIF, LPHT, etc.) deposits + NIDs + repos.
2 Effective 1998, the statutory reserves of banking institutions have been reclassified as "Funds from other financial institutions" rather than "Other deposits from other financial institutions". In this regard, data for prior years have also been revised accordingly.
p Preliminary

Table A.43
Commercial Banks: Sources and Uses of Funds

	As at end									
	Dec. 1995		Dec. 1996		Dec. 1997		Dec. 1998		Dec. 1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
Sources										
Capital and reserves	19,387.7	6.6	25,867.4	7.2	38,390.2*	8.0	37,271.6*	8.2	38,824.8*	8.2
Debentures and notes	1,949.0	0.7	3,576.3	1.0	1,877.8	0.4	1,267.3	0.3	1,703.5	0.4
Deposits[1]	196,851.0	67.4	243,968.7	68.1	300,558.1	62.6	307,439.6	67.8	329,953.3	70.0
(of which:										
NIDs issued	*24,541.3*	*8.4*	*27,467.1*	*7.7*	*39,660.6*	*8.3*	*36,858.4*	*8.1*	*12,804.1*	*2.7*
Repos)	*9,612.0*	*3.3*	*11,818.1*	*3.3*	*15,060.9*	*3.1*	*15,633.5*	*3.4*	*15,361.5*	*3.3*
Amount due to										
financial institutions	28,349.9	9.7	34,532.1	9.6	79,586.2	16.6	40,632.8	9.0	35,455.2	7.5
Domestic	*13,249.4*	*4.5*	*13,060.8*	*3.6*	*43,490.0*	*9.1*	*18,190.6*	*4.0*	*18,814.1*	*4.0*
Foreign	*15,100.5*	*5.2*	*21,471.3*	*6.0*	*36,096.1*	*7.5*	*22,442.3*	*4.9*	*16,641.1*	*3.5*
Bankers acceptances	15,781.1	5.4	19,580.5	5.5	23,115.4	4.8	18,497.5	4.1	14,802.5	3.1
Others	29,893.2	10.2	30,562.8	8.5	36,720.4	7.6	48,383.1	10.7	50,730.4	10.8
TOTAL	**292,211.9**	**100.0**	**358,087.8**	**100.0**	**480,248.1**	**100.0**	**453,492.0**	**100.0**	**471,469.8**	**100.0**
Uses										
Cash[2]	1,589.7	0.5	2,363.2	0.7	4,547.7	0.9	2,825.8	0.6	6,239.7	1.3
Reserve with BNM	18,518.8	6.3	27,972.9	7.8	37,131.0	7.7	10,624.4	2.3	10,209.6	2.2
Amount due from										
financial institutions	45,257.3	15.5	37,949.9	10.6	63,744.5	13.3	57,971.9	12.8	76,914.4	16.3
Domestic	36,908.9	12.6	30,104.5	8.4	48,804.3	10.2	45,212.0	10.0	64,054.9	13.6
Foreign	8,348.4	2.9	7,845.4	2.2	14,940.1	3.1	12,759.9	2.8	12,859.4	2.7
Investments	7,633.5	2.6	8,773.0	2.4	14,073.0	2.9	20,354.9	4.5	19,084.8	4.0
(of which:										
Stocks and shares	*3,251.1*	*1.1*	*4,276.2*	*1.2*	*3,714.8*	*0.8*	*4,507.4*	*1.0*	*5,670.2*	*1.2*
Debentures	*864.6*	*0.3*	*821.0*	*0.2*	*2,992.4*	*0.6*	*7,505.6*	*1.7*	*4,536.8*	*1.0*
Fixed assets	*2,989.6*	*1.0*	*3,505.8*	*1.0*	*6,521.4*	*1.4*	*7,264.0*	*1.6*	*7,791.2*	*1.7*
Foreign investments)	*528.2*	*0.2*	*170.0*	*…*	*844.4*	*0.2*	*1,077.9*	*0.2*	*1,086.7*	*0.2*
Placement with										
discount houses	1,829.2	0.6	3,849.4	1.1	6,037.0	1.3	1,342.0	0.3	701.6	0.1
Marketable securities	36,962.6	12.6	50,960.1	14.2	61,871.1	12.9	60,314.5	13.3	59,744.0	12.7
(of which:										
Treasury bills	*2,301.4*	*0.8*	*1,789.4*	*0.5*	*3,775.2*	*0.8*	*3,611.9*	*0.8*	*2,973.0*	*0.6*
MGS	*6,462.3*	*2.2*	*7,726.1*	*2.2*	*8,900.4*	*1.9*	*9,967.2*	*2.2*	*7,786.2*	*1.7*
NIDs held	*12,528.2*	*4.3*	*20,776.6*	*5.8*	*24,394.7*	*5.1*	*21,059.0*	*4.6*	*12,907.2*	*2.7*
Cagamas bonds)	*4,898.5*	*1.7*	*8,301.7*	*2.3*	*12,487.6*	*2.6*	*13,098.0*	*2.9*	*10,766.5*	*2.3*
Loans[3]										
(incl. trade bills)	175,007.4	59.9	217,820.6	60.8	276,285.3	57.5	285,676.3	63.0	282,264.6	59.9
Others	5,413.4	1.9	8,398.7	2.3	16,558.6	3.4	14,382.3	3.2	16,311.3	3.5
TOTAL	**292,211.9**	**100.0**	**358,087.8**	**100.0**	**480,248.1**	**100.0**	**453,492.0**	**100.0**	**471,469.8**	**100.0**

1 Includes NIDs issued and repos.
2 Includes balances with BNM.
3 Excludes housing loans sold to Cagamas Berhad.
* Includes current unaudited unadjusted profit (If excludes, the figure would be for the year 1997: RM33,714.5 million; 1998: RM35,405.6 million 1999: RM35,400.7 million).

Table A.44
Commercial Banks: Commitments and Contingencies

	As at end			
	1998		1999	
	RM million	% share	RM million	% share
Assets sold with recourse and commitments with drawdown	14,909	5.8	12,110	4.7
Credit extension commitments	119,115	46.3	131,833	51.1
Direct credit substitutes	19,042	7.4	17,204	6.7
Foreign exchange related contracts	59,079	22.9	49,290	19.1
Interest rate related contracts	5,930	2.3	12,816	5.0
Trade-related contingencies	7,947	3.1	6,802	2.6
Transaction-related contingencies	17,646	6.9	17,777	6.9
Underwriting obligations	1,219	0.5	2,202	0.9
Others	12,627	4.9	8,110	3.1
TOTAL	**257,514**	**100.0**	**258,146**	**100.0**

Table A.45
Finance Companies: Sources and Uses of Funds

	As at end									
	Dec. 1995		Dec. 1996		Dec. 1997		Dec. 1998		Dec. 1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
Sources										
Capital and reserves	4,516.7	4.9	6,844.1	5.7	9,431.2*	6.2	7,723.3*	6.2	6,317.8*	5.5
Debentures and notes	332.4	0.4	531.0	0.4	872.2	0.6	742.2	0.6	669.6	0.6
Deposits[1]	69,963.1	76.1	90,842.0	75.9	107,350.8	70.4	98,627.2	79.8	91,354.2	78.8
(of which:										
NIDs issued	*8,711.0*	*9.5*	*14,973.8*	*12.5*	*18,751.9*	*12.3*	*12,843.8*	*10.4*	*8,158.5*	*7.0*
Repos)	*1,869.8*	*2.0*	*3,001.0*	*2.5*	*7,877.3*	*5.2*	*2,891.2*	*2.3*	*525.9*	*0.5*
Amount due to financial institutions	8,908.1	9.7	12,868.8	10.8	25,479.1	16.7	5,243.0	4.2	4,468.4	3.9
Domestic	*8,908.1*	*9.7*	*12,868.8*	*10.8*	*25,479.1*	*16.7*	*5,243.0*	*4.2*	*4,468.4*	*3.9*
Foreign	…	…	…	…	…	…	…	…	…	…
Others	8,172.1	8.9	8,524.2	7.1	9,253.5	6.1	11,263.6	9.1	13,062.6	11.3
TOTAL	**91,892.4**	**100.0**	**119,610.1**	**100.0**	**152,386.8**	**100.0**	**123,599.3**	**100.0**	**115,872.6**	**100.0**
Uses										
Cash[2]	159.6	0.2	164.3	0.1	208.7	0.1	181.7	0.1	780.4	0.7
Reserve with BNM	7,640.2	8.3	12,050.4	10.1	16,043.1	10.5	3,475.2	2.8	3,174.2	2.7
Amount due from financial institutions	7,548.9	8.2	6,445.4	5.4	5,676.9	3.7	7,529.4	6.1	10,334.5	8.9
Domestic	*7,548.9*	*8.2*	*6,445.4*	*5.4*	*5,676.9*	*3.7*	*7,529.4*	*6.1*	*10,334.5*	*8.9*
Foreign	…	…	…	…	…	…	…	…	…	…
Investments	*968.2*	*1.1*	*1,241.3*	*1.0*	*3,191.7*	*2.1*	*5,128.8*	*4.1*	*3,148.5*	*2.7*
(of which:										
Stocks and shares	*282.0*	*0.3*	*281.7*	*0.2*	*436.4*	*0.3*	*315.4*	*0.3*	*399.1*	*0.3*
Debentures	*70.3*	*0.1*	*767.9*	*0.6*	*1,227.2*	*0.8*	*3,134.8*	*2.5*	*1,080.5*	*0.9*
Fixed assets	*615.9*	*0.7*	*827.9*	*0.7*	*1,528.1*	*1.0*	*1,678.6*	*1.4*	*1,668.9*	*1.4*
Foreign investments)	…	…	…	…	…	…	…	…	…	…
Placement with discount houses	735.1	0.8	1,152.4	1.0	2,051.8	1.3	1,006.1	0.8	407.3	0.4
Marketable securities	10,650.8	11.6	14,888.6	12.4	18,312.6	12.0	13,990.6	11.3	17,634.2	15.2
(of which:										
Treasury bills	*119.3*	*0.1*	*22.2*	…	*46.4*	…	*42.8*	…	*338.3*	*0.3*
MGS	*1,768.2*	*1.9*	*2,806.5*	*2.3*	*3,250.9*	*2.1*	*3,602.9*	*2.9*	*3,980.6*	*3.4*
NIDs held	*2,686.6*	*2.9*	*4,451.1*	*3.7*	*7,665.3*	*5.0*	*5,473.1*	*4.4*	*4,749.9*	*4.1*
Cagamas bonds)	*2,704.6*	*2.9*	*2,959.6*	*2.5*	*2,795.8*	*1.8*	*1,778.5*	*1.4*	*1,586.4*	*1.4*
Loans[3] (incl. trade bills)	62,752.0	68.3	82,496.7	69.0	102,528.1	67.3	86,553.9	70.0	75,378.3	65.1
Others	1,437.6	1.6	1,171.0	1.0	4,373.9	2.9	5,733.6	4.6	5,015.3	4.3
TOTAL	**91,892.4**	**100.0**	**119,610.1**	**100.0**	**152,386.8**	**100.0**	**123,599.3**	**100.0**	**115,872.6**	**100.0**

[1] Includes NIDs issued and repos.
[2] Includes balances with BNM.
[3] Excludes housing loans sold to Cagamas Berhad.
* Includes current unaudited unadjusted profit (If excludes, the figure would be for the year 1997: RM8,813.3 million; 1998: RM7,606.4 million; 1999:RM5,361.7 million).

Table A.46
Finance Companies: Commitments and Contingencies

	As at end			
	1998		1999	
	RM million	% share	RM million	% share
Assets sold with recourse and commitments with drawdown	5,393	31.6	5,536	31.8
Credit extension commitments	9,579	56.2	9,926	57.0
Direct credit substitutes	1,211	7.1	969	5.6
Foreign exchange related contracts	…	…	…	…
Interest rate related contracts	510	3.0	667	3.8
Trade-related contingencies	…	…	…	…
Transaction-related contingencies	12	0.1	19	0.1
Underwriting obligations	10	0.1	…	…
Others	325	1.9	306	1.8
TOTAL	**17,039**	**100.0**	**17,423**	**100.0**

Table A.47
Merchant Banks: Sources and Uses of Funds

	As at end									
	Dec. 1995		Dec. 1996		Dec. 1997		Dec. 1998		Dec. 1999	
	RM million	% share	RM million	% share	RM million	% share	RM million	% share	RM million	% share
Sources										
Capital and reserves	1,615.6	6.0	2,783.4	8.2	4,233.1*	9.6	3,951.1*	10.1	3,619.6*	9.2
Debentures and notes	113.8	0.4	183.8	0.5	150.0	0.3	150.0	0.4	150.0	0.4
Deposits[1]	16,093.3	59.5	23,530.7	69.2	26,389.7	59.6	26,337.0	67.1	25,873.7	66.0
(of which:										
NIDs issued	*3,380.7*	*12.5*	*6,000.8*	*17.6*	*6,553.0*	*14.8*	*6,242.2*	*15.9*	*6,352.3*	*16.2*
Repos)	*2,664.0*	*9.8*	*2,373.9*	*7.0*	*3,933.8*	*8.9*	*3,283.9*	*8.4*	*3,198.9*	*8.2*
Amount due to financial institutions	5,841.3	21.6	5,198.3	15.3	10,771.7	24.3	4,853.7	12.4	5,897.3	15.1
Domestic	*5,811.3*	*21.5*	*5,157.3*	*15.2*	*9,650.7*	*21.8*	*4,288.4*	*10.9*	*5,376.7*	*13.7*
Foreign	*30.0*	*0.1*	*41.0*	*0.1*	*1,121.0*	*2.5*	*565.3*	*1.4*	*520.6*	*1.3*
Bankers acceptances	676.2	2.5	566.6	1.7	612.4	1.4	275.9	0.7	207.6	0.5
Others	2,721.6	10.1	1,742.1	5.1	2,143.1	4.8	3,660.2	9.3	3,436.0	8.8
TOTAL	**27,061.8**	**100.0**	**34,004.9**	**100.0**	**44,300.0**	**100.0**	**39,227.8**	**100.0**	**39,184.1**	**100.0**
Uses										
Cash[2]	4.3	…	6.5	…	2.3	…	5.6	…	4.7	…
Reserve with BNM	1,546.2	5.7	2,643.3	7.8	3,466.4	7.8	852.8	2.2	833.7	2.1
Amount due from financial institutions	4,968.7	18.4	4,452.8	13.1	6,163.5	13.9	3,191.8	8.1	5,263.5	13.4
Domestic	*4,968.4*	*18.4*	*4,413.1*	*13.0*	*5,761.0*	*13.0*	*2,807.7*	*7.2*	*4,786.6*	*12.2*
Foreign	*0.3*	*...*	*39.7*	*0.1*	*402.5*	*0.9*	*384.0*	*1.0*	*476.9*	*1.2*
Investments	579.9	2.1	741.7	2.2	970.6	2.2	2,861.5	7.3	1,495.1	3.8
(of which:										
Stocks and shares	*319.6*	*1.2*	*310.9*	*0.9*	*450.0*	*1.0*	*387.6*	*1.0*	*390.2*	*1.0*
Debentures	*188.3*	*0.7*	*337.4*	*1.0*	*319.7*	*0.7*	*2,244.6*	*5.7*	*871.6*	*2.2*
Fixed assets	*71.9*	*0.3*	*93.3*	*0.3*	*166.6*	*0.4*	*186.8*	*0.5*	*190.9*	*0.5*
Foreign investments)	*0.1*	*...*	*0.1*	*...*	*34.3*	*0.1*	*42.4*	*0.1*	*42.4*	*0.1*
Placement with discount houses	117.0	0.4	296.0	0.9	38.0	0.1	…	…	10.0	…
Marketable securities	5,132.9	19.0	6,500.1	19.1	9,467.5	21.4	8,671.5	22.1	11,364.6	29.0
(of which:										
Treasury bills	*78.2*	*0.3*	*40.7*	*0.1*	*57.4*	*0.1*	*131.4*	*0.3*	*351.2*	*0.9*
MGS	*316.6*	*1.2*	*633.3*	*1.9*	*592.9*	*1.3*	*907.4*	*2.3*	*595.7*	*1.5*
NIDs held	*2,894.8*	*10.7*	*3,502.5*	*10.3*	*5,078.4*	*11.5*	*4,844.4*	*12.3*	*4,868.6*	*12.4*
Cagamas Bonds)	*1,211.8*	*4.5*	*1,834.8*	*5.4*	*1,520.3*	*3.4*	*1,260.2*	*3.2*	*786.7*	*2.0*
Loans[3] (incl. trade bills)	14,141.2	52.3	18,888.2	55.5	23,052.0	52.0	22,191.5	56.6	18,870.7	48.2
Others	571.6	2.1	476.3	1.4	1,139.7	2.6	1,453.2	3.7	1,341.6	3.4
TOTAL	**27,061.8**	**100.0**	**34,004.9**	**100.0**	**44,300.0**	**100.0**	**39,227.8**	**100.0**	**39,184.1**	**100.0**

[1] Includes NIDs issued and repos.
[2] Includes balances with BNM.
[3] Excludes housing loans sold to Cagamas Berhad.
* Includes current unaudited unadjusted profit (If excludes, the figure would be for the year 1997: RM3,852.1 million; 1998: RM3,883.8 million 1999: RM3,180.1 million).

Table A.48
Merchant Banks: Commitments and Contingencies

	As at end			
	1998		1999	
	RM million	% share	RM million	% share
Assets sold with recourse and commitments with drawdown	167	0.9	302	1.4
Credit extension commitments	7,092	36.5	4,968	23.1
Direct credit substitutes	3,157	16.3	4,311	20.1
Foreign exchange related contracts	1,673	8.6	708	3.3
Interest rate related contracts	5,003	25.8	9,373	43.7
Trade-related contingencies	1	…	…	…
Transaction-related contingencies	1,215	6.3	1,015	4.7
Underwriting obligations	635	3.3	717	3.3
Others	476	2.5	76	0.4
TOTAL	**19,420**	**100.0**	**21,469**	**100.0**

Table A.49
Commercial Banks: Income and Expenditure

	For the financial year			For the calendar year		
	1995	1996	1997	1997	1998	1999*p*
	RM million					
Interest income net of interest-in-suspense	17,161.7	23,503.0	29,154.1	33,555.2	43,335.6	27,567.9
(Interest-in-suspense)	*334.1*	*495.9*	*66.8*	*141.8*	*3,076.4*	*2,164.3*
Less: Interest expense	10,113.3	14,057.4	18,272.8	21,749.9	31,155.2	17,190.6
Net interest income	7,048.4	9,445.6	10,881.3	11,805.3	12,180.3	10,377.3
Add: Non-interest income	2,991.8	3,230.8	4,149.1	3,899.1	5,038.5	5,235.4
Less: Loan loss provisions	874.7	1,269.1	3,231.0	4,022.2	13,237.1	2,961.7
Staff cost	2,260.4	2,579.7	2,889.7	3,007.8	3,027.0	2,789.1
Overheads	2,064.1	2,658.0	2,730.9	2,957.1	3,641.6	3,434.1
Pre-tax profit	4,841.0	6,169.6	6,178.8	5,717.2	–2,686.9	6,427.7

p Preliminary

Table A.50
Finance Companies: Income and Expenditure

	For the financial year			For the calendar year		
	1995	1996	1997	1997	1998	1999*p*
	RM million					
Interest income net of interest-in-suspense	6,748.9	9,377.1	12,006.5	13,158.8	13,525.2	8,933.1
(Interest-in-suspense)	*177.8*	*123.7*	*353.0*	*335.9*	*1,426.7*	*817.1*
Less: Interest expense	3,741.2	5,774.2	8,056.5	9,050.6	11,585.9	5,446.1
Net interest income	3,007.7	3,602.9	3,950.0	4,108.2	1,939.4	3,487.0
Add: Non-interest income	308.4	390.5	386.7	511.6	669.5	842.9
Less: Loan loss provisions	554.3	645.8	1,543.8	1,295.4	2,878.0	3,556.1
Staff cost	572.1	667.2	785.6	821.7	745.0	585.5
Overheads	741.9	843.0	1,380.6	1,228.5	1,374.0	1,184.6
Pre-tax profit	1,447.8	1,837.4	626.7	1,274.3	–2,388.1	–996.3

p Preliminary

Table A.51
Merchant Banks: Income and Expenditure

	For the financial year			For the calendar year		
	1995	1996	1997	1997	1998	1999*p*
	RM million					
Interest income net of interest-in-suspense	1,361.4	1,967.8	2,566.3	3,410.8	3,888.2	2,152.2
(Interest-in-suspense)	*11.0*	*45.8*	*25.3*	*42.1*	*479.9*	*425.0*
Less: Interest expense	1,025.9	1,488.9	1,936.3	2,611.3	3,152.3	1,596.4
Net interest income	335.5	478.9	630.0	799.5	736.0	555.8
Add: Non-interest income	502.0	552.7	540.1	532.1	309.3	689.0
Less: Loan loss provisions	54.7	97.4	206.6	307.5	1,280.3	1,025.1
Staff cost	109.9	128.2	143.7	163.4	133.6	133.8
Overheads	92.9	99.4	205.0	197.5	288.1	251.5
Pre-tax profit	580.0	706.6	614.8	663.2	–656.8	–165.6

p Preliminary

Table A.52
Commercial Banks: Lending Guidelines to the Priority Sectors

	1996 Lending Guidelines (performance as at compliance date of end-March 1998)		1998 / 1999 Lending Guidelines[1] (performance as at end-1999)	
	Target	Achieved	Target[2]	Achieved
Loans to Bumiputera Community[3]				
Total outstanding loans (RM billion)	53.0	76.6	72.9	80.0
Total outstanding loans (%)	30.0	43.4	30.0	33.4
Non-compliance (no. of institutions)		9		19
Housing Loan Commitments[3]				
Total houses (units)	100,000	107,747	108,434	137,048
Non-compliance (no. of institutions)		4		19
Loans under NPGS				
Total guarantee cover (RM million)	1,000.0	2,341.1		
Non-compliance (no. of institutions)		9		
Of which: for Bumiputera Cos.			–	–
Total guarantee cover (RM million)	500.0	585.6		
Non-compliance (no. of institutions)		16		
Loans of RM500,000 and below to SMEs[3,4]				
Total loans approved (RM million)			1,064.7	1,984.3
Non-compliance (no. of institutions)				6
Of which: for Bumiputera SMEs	–	–		
Total loans approved (RM million)			571.0	511.4
Non-compliance (no. of institutions)				18
Loans of RM5 million and below to SMEs				
Total loans approved (RM million)			1,043.0	2,052.3
Non-compliance (no. of institutions)				11
Of which: for Bumiputera SMEs	–	–		
Total loans approved (RM million)			521.5	527.9
Non-compliance (no. of institutions)				27

[1] The 1996 Guideline on Loans Under the New Principal Guarantee Scheme (NPGS) expired on 31 March 1998 and was replaced by the 1998 Guideline on Loans of RM500,000 and below to SMEs. The latter guideline expired on 30 June 1999 and was replaced by the 1999 Guideline on Loans to SMEs. Under the 1999 Guideline, the maximum loan size per borrower was increased from RM500,000 to RM5 million. The size of eligible companies was also increased from shareholders' funds or net assets of RM2.5 million to RM10 million. The 1999 Guideline expires on 31 December 2000.

[2] Compliance dates for the 1998 / 1999 Lending Guidelines are as follows:

Loans to Bumiputera Community	end-March 2000
Housing Loan Commitments	end-March 2000
Loans of RM500,000 and below to SMEs	end-June 1999
Loans of RM5 million and below to SMEs	end-December 2000

[3] Targets under the 1998 guidelines differ from those reported in the 1998 BNM Annual Report due to the banking institutions' merger exercise.

[4] Achievements shown are as at compliance date of end-June 1999.

Table A.53
Finance Companies: Lending Guidelines to the Priority Sectors

	1996 Lending Guidelines (performance as at compliance date of end-March 1998)		1998 / 1999 Lending Guidelines[1] (performance as at end-1999)	
	Target	Achieved	Target[2]	Achieved
Loans to Bumiputera Community[3]				
Total outstanding loans (RM billion)	19.4	36.1	22.4	29.4
Total outstanding loans (%)	30.0	55.8	30.0	39.5
Non-compliance (no. of institutions)		9		6
Housing Loan Commitments[3]				
Total houses (units)	40,000	43,431	35,167	45,790
Non-compliance (no. of institutions)		5		14
Loans under NPGS				
Total guarantee cover (RM million)	240.0	1,216.1		
Non-compliance (no. of institutions)		8		
Of which: for Bumiputera Cos.			–	–
Total guarantee cover (RM million)	120.0	278.7		
Non-compliance (no. of institutions)		8		
Loans of RM500,000 and below to SMEs[3,4]				
Total loans approved (RM million)			211.5	336.2
Non-compliance (no. of institutions)				14
Of which: for Bumiputera SMEs	–	–		
Total loans approved (RM million)			114.6	110.1
Non-compliance (no. of institutions)				15
Loans of RM5 million and below to SMEs				
Total loans approved (RM million)			197.0	144.1
Non-compliance (no. of institutions)				14
Of which: for Bumiputera SMEs	–	–		
Total loans approved (RM million)			98.5	46.3
Non-compliance (no. of institutions)				16

[1] The 1996 Guideline on Loans Under the New Principal Guarantee Scheme (NPGS) expired on 31 March 1998 and was replaced by the 1998 Guideline on Loans of RM500,000 and below to SMEs. The latter guideline expired on 30 June 1999 and was replaced by the 1999 Guideline on Loans to SMEs. Under the 1999 Guideline, the maximum loan size per borrower was increased from RM500,000 to RM5 million. The size of eligible companies was also increased from shareholders' funds or net assets of RM2.5 million to RM10 million. The 1999 Guideline expires on 31 December 2000.

[2] Compliance dates for the 1998 / 1999 Lending Guidelines are as follows:

Loans to Bumiputera Community	end-March 2000
Housing Loan Commitments	end-March 2000
Loans of RM500,000 and below to SMEs	end-June 1999
Loans of RM5 million and below to SMEs	end-December 2000

[3] Targets under the 1998 guidelines differ from those reported in the 1998 BNM Annual Report due to the banking institutions merger exercise.

[4] Achievements shown are as at compliance date of end-June 1999.

Table A.54
Commercial Banks: Direction of Lending

Loans by Sectors	As at end			
	1998		1999*	
	RM million	% share	RM million	% share
Agriculture, hunting, forestry and fishing	6,187.3	2.0	7,520.5	2.3
Mining and quarrying	1,212.0	0.4	1,218.9	0.4
Manufacturing	58,366.9	18.8	60,279.7	18.8
Electricity, gas and water	5,057.5	1.6	6,190.8	1.9
Wholesale, retail, restaurants and hotels	30,836.4	9.9	31,415.4	9.8
Wholesale trade	*17,355.0*	*5.6*	*17,514.8*	*5.5*
Retail trade	*8,660.9*	*2.8*	*9,114.4*	*2.8*
Restaurants and hotels	*4,820.5*	*1.6*	*4,786.2*	*1.5*
Broad property sector	111,018.2	35.8	116,646.4	36.3
Construction	*32,005.6*	*10.3*	*30,966.5*	*9.6*
Purchase of residential property	*43,436.9*	*14.0*	*49,872.2*	*15.5*
Purchase of non-residential property	*23,650.8*	*7.6*	*22,548.7*	*7.0*
Real estate	*11,924.9*	*3.8*	*13,259.1*	*4.1*
Transport, storage and communication	11,647.5	3.8	11,924.2	3.7
Finance, insurance and business services	31,076.1	10.0	28,933.0	9.0
Financial services	*24,001.2*	*7.7*	*20,348.6*	*6.3*
Insurance	*172.3*	*0.1*	*258.4*	*0.1*
Business services	*6,902.6*	*2.2*	*8,325.9*	*2.6*
Consumption credit	17,206.8	5.5	19,423.7	6.0
Personal uses	*12,190.7*	*3.9*	*12,704.1*	*4.0*
Credit cards	*3,310.7*	*1.1*	*4,369.8*	*1.4*
Purchase of consumer durables	*541.5*	*0.2*	*799.1*	*0.2*
Purchase of passenger cars	*1,163.9*	*0.4*	*1,550.7*	*0.5*
Purchase of securities	24,669.2	8.0	23,056.9	7.2
Purchase of transport vehicles	206.7	0.1	130.7	0.0
Community, social and personal services	4,836.0	1.6	5,613.4	1.7
Others	7,970.9	2.6	8,855.2	2.8
Total loans outstanding[1]	**310,291.4**	**100.0**	**321,208.9**	**100.0**

[1] Including loans sold to Cagamas and Danaharta.
* Including Bank Muamalat Malaysia Berhad.

Table A.55
Finance Companies: Direction of Lending

Loans by Sectors	As at end			
	1998		1999	
	RM million	% share	RM million	% share
Agriculture, hunting, forestry and fishing	927.7	1.0	795.3	0.9
Mining and quarrying	327.0	0.4	252.3	0.3
Manufacturing	4,052.7	4.4	3,133.0	3.7
Electricity, gas and water	71.4	0.1	74.4	0.1
Wholesale, retail, restaurants and hotels	3,609.6	3.9	3,567.7	4.2
Wholesale trade	*1,272.7*	*1.4*	*1,197.6*	*1.4*
Retail trade	*1,498.9*	*1.6*	*1,562.7*	*1.8*
Restaurants and hotels	*838.0*	*0.9*	*807.4*	*1.0*
Broad property sector	30,915.4	33.2	29,948.1	35.4
Construction	*8,048.0*	*8.6*	*7,596.2*	*9.0*
Purchase of residential property	*12,908.1*	*13.9*	*13,371.8*	*15.8*
Purchase of non-residential property	*6,547.0*	*7.0*	*5,682.8*	*6.7*
Real estate	*3,412.3*	*3.7*	*3,297.2*	*3.9*
Transport, storage and communication	2,480.2	2.7	2,334.7	2.8
Finance, insurance and business services	3,053.9	3.3	2,561.4	3.0
Financial services	*1,496.3*	*1.6*	*1,005.6*	*1.2*
Insurance	*16.8*	*0.0*	*25.3*	*0.0*
Business services	*1,540.7*	*1.7*	*1,530.5*	*1.8*
Consumption credit	32,160.5	34.6	30,707.8	36.3
Personal uses	*1,199.4*	*1.3*	*1,004.7*	*1.2*
Credit cards	*1,002.3*	*1.1*	*1,097.2*	*1.3*
Purchase of consumer durables	*298.3*	*0.3*	*136.2*	*0.2*
Purchase of passenger cars	*29,660.5*	*31.9*	*28,469.7*	*33.7*
Purchase of securities	9,176.3	9.9	7,676.2	9.1
Purchase of transport vehicles	4,282.0	4.6	1,836.0	2.2
Community, social and personal services	1,356.7	1.5	983.6	1.2
Others	658.5	0.7	682.4	0.8
Total loans outstanding[1]	**93,072.1**	**100.0**	**84,552.9**	**100.0**

[1]Including loans sold to Cagamas and Danaharta.

Table A.56
Merchant Banks: Direction of Lending

Loans by Sectors	As at end 1998 RM million	1998 % share	1999 RM million	1999 % share
Agriculture, hunting, forestry and fishing	701.2	3.0	868.0	4.0
Mining and quarrying	146.3	0.6	108.2	0.5
Manufacturing	2,713.9	11.7	2,662.2	12.1
Electricity, gas and water	725.2	3.1	822.8	3.8
Wholesale, retail, restaurants and hotels	1,313.9	5.7	1,338.6	6.1
Wholesale trade	*446.7*	*1.9*	*350.5*	*1.6*
Retail trade	*273.2*	*1.2*	*295.1*	*1.3*
Restaurants and hotels	*594.0*	*2.6*	*693.0*	*3.2*
Broad property sector	7,679.2	33.1	7,359.5	33.6
Construction	*5,038.0*	*21.7*	*4,546.0*	*20.7*
Purchase of residential property	*105.5*	*0.5*	*104.5*	*0.5*
Purchase of non-residential property	*760.7*	*3.3*	*746.6*	*3.4*
Real estate	*1,774.9*	*7.6*	*1,962.4*	*8.9*
Transport, storage and communication	1,083.2	4.7	1,273.1	5.8
Finance, insurance and business services	3,893.8	16.8	1,862.7	8.5
Financial services	*3,142.2*	*13.5*	*1,123.5*	*5.1*
Insurance	*90.1*	*0.4*	*91.9*	*0.4*
Business services	*661.6*	*2.9*	*647.3*	*3.0*
Consumption credit	124.3	0.5	110.6	0.5
Personal uses	*116.9*	*0.5*	*101.3*	*0.5*
Credit cards	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of consumer durables	*0.2*	*0.0*	*0.1*	*0.0*
Purchase of passenger cars	*7.2*	*0.0*	*9.2*	*0.0*
Purchase of securities	4,098.0	17.7	3,263.2	14.9
Purchase of transport vehicles	16.1	0.1	0.2	0.0
Community, social and personal services	493.5	2.1	471.4	2.1
Others	215.6	0.9	1,789.0	8.2
Total loans outstanding[1]	**23,204.2**	**100.0**	**21,929.4**	**100.0**

[1]Including loans sold to Cagamas and Danaharta.

Table A.57
Commercial Banks: Non-performing Loans by Sector

	As at end			
	1998		1999	
	RM million	% of total loans to the sector	RM million	% of total loans to the sector
Agriculture, hunting, forestry and fishing	568	9.2	547	7.6
Mining and quarrying	166	13.9	162	15.0
Manufacturing	7,220	12.8	7,171	13.0
Electricity, gas and water	39	0.8	33	0.5
Community, social and personal services	543	11.3	566	10.4
Broad property sector	13,216	12.2	13,463	12.3
Real estate	*2,595*	*22.1*	*2,107*	*18.2*
Construction	*5,221*	*17.1*	*5,210*	*19.4*
Purchase of residential property	*3,002*	*10.0*	*3,694*	*9.5*
Purchase of non-residential property	*2,398*	*10.4*	*2,451*	*11.5*
Wholesale, retail, restaurants and hotels	3,138	10.4	3,788	12.7
Transport, storage and communication	1,501	13.1	1,298	12.7
Finance, insurance and business services	3,131	10.3	3,078	11.5
Purchase of securities	4,130	21.3	2,039	13.3
Consumption credit	2,581	14.9	2,771	14.4
Credit cards	*554*	*16.7*	*289*	*6.6*
Personal uses	*1,766*	*14.5*	*1,866*	*15.1*
Purchase of consumer durables	*72*	*13.6*	*164*	*21.2*
Purchase of transport vehicles[1]	*189*	*13.8*	*451*	*26.8*
Others	1,020	12.9	646	8.6
Total	**37,254**	**12.5**	**35,561**	**12.1**

[1] Includes commercial vehicles.

Table A.58
Finance Companies: Non-performing Loans by Sector

	As at end			
	1998		1999	
	RM million	% of total loans to the sector	RM million	% of total loans to the sector
Agriculture, hunting, forestry and fishing	172	18.5	117	14.9
Mining and quarrying	57	17.5	70	27.8
Manufacturing	1,242	30.8	1,032	33.5
Electricity, gas and water	13	18.0	17	22.6
Community, social and personal services	233	17.2	193	19.6
Broad property sector	6,161	20.4	4,979	18.1
Real estate	*1,904*	*58.8*	*550*	*32.2*
Construction	*1,722*	*22.6*	*1,989*	*28.5*
Purchase of residential property	*1,099*	*15.1*	*1,212*	*15.5*
Purchase of non-residential property	*1,435*	*22.3*	*1,228*	*22.5*
Wholesale, retail, restaurants and hotels	621	17.2	546	15.4
Transport, storage and communication	996	40.2	564	24.2
Finance, insurance and business services	989	32.6	841	37.7
Purchase of securities	2,419	26.7	1,730	24.8
Consumption credit	4,927	13.5	4,241	13.1
Credit cards	*196*	*19.6*	*63*	*5.7*
Personal uses	*237*	*19.9*	*179*	*18.0*
Purchase of consumer durables	*78*	*26.2*	*26*	*19.4*
Purchase of transport vehicles[1]	*4,416*	*13.0*	*3,973*	*13.1*
Others	71	10.7	85	12.5
Total	**17,901**	**19.4**	**14,415**	**17.8**

[1] Includes commercial vehicles.

Table A.59
Merchant Banks: Non-performing Loans by Sector

	As at end			
	1998		1999	
	RM million	% of total loans to the sector	RM million	% of total loans to the sector
Agriculture, hunting, forestry and fishing	77	12.7	40	5.3
Mining and quarrying	36	24.5	0	0.0
Manufacturing	555	21.0	476	20.3
Electricity, gas and water	0	0.0	54	6.8
Community, social and personal services	106	21.5	10	2.3
Broad property sector	1,454	20.4	1,372	24.1
Real estate	*297*	*18.4*	*418*	*25.5*
Construction	*1,110*	*22.6*	*852*	*23.6*
Purchase of residential property	*0*	*0.5*	*26*	*24.8*
Purchase of non-residential property	*46*	*9.4*	*76*	*22.4*
Wholesale, retail, restaurants and hotels	153	12.3	93	7.8
Transport, storage and communication	204	18.8	229	18.2
Finance, insurance and business services	471	12.3	354	22.2
Purchase of securities	974	24.6	1,059	36.5
Consumption credit	78	55.2	7	14.3
Credit cards	–	–	–	–
Personal uses	*73*	*62.4*	*7*	*18.0*
Purchase of consumer durables	…	…	…	…
Purchase of transport vehicles[1]	*5*	*19.6*	*0*	*0.6*
Others	*14*	*6.5*	*71*	*4.0*
Total	**4,122**	**18.6**	**3,764**	**19.9**

[1] Includes commercial vehicles.

Table A.60
Commercial Banks: Loans Sold to Danaharta

	As at end 1998			As at end 1999		
	Non-Performing Loans	Performing Loans	Total Loans	Non-Performing Loans	Performing Loans	Total Loans
	RM million					
Agriculture, hunting, forestry and fishing	8.9	0.0	8.9	277.8	77.9	355.8
Mining and quarrying	11.7	0.0	11.7	66.9	62.8	129.7
Manufacturing	1,720.3	115.1	1,835.4	3,842.6	1,216.3	5,058.9
Electricity, gas and water supply	14.0	0.0	14.0	22.4	1.5	23.9
Wholesale, retail, restaurants and hotels	517.5	56.1	573.6	1,286.9	255.5	1,542.4
Wholesale trade	*321.5*	*28.1*	*349.6*	*715.3*	*163.8*	*879.1*
Retail trade	*132.8*	*28.0*	*160.8*	*266.2*	*83.6*	*349.8*
Restaurants and hotels	*63.2*	*0.0*	*63.2*	*305.4*	*8.0*	*313.4*
Broad property sector	2,124.7	158.9	2,283.6	5,579.1	1,313.0	6,892.1
Construction	*1,355.2*	*77.4*	*1,432.6*	*3,475.0*	*517.3*	*3,992.3*
Purchase of residential property	*11.7*	*57.8*	*69.5*	*65.9*	*72.7*	*138.5*
Purchase of non-residential property	*585.8*	*10.4*	*596.2*	*919.2*	*159.4*	*1,078.6*
Real estate	*171.9*	*13.3*	*185.2*	*1,119.0*	*563.7*	*1,682.7*
Transport, storage and communication	225.7	2.0	227.8	533.3	1,147.7	1,681.0
Fin, ins, real estate & buss. services	608.4	198.0	806.4	1,506.2	621.7	2,127.9
Financial services	*213.4*	*0.0*	*213.4*	*950.0*	*19.8*	*969.9*
Insurance	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Business services	*395.0*	*198.0*	*593.0*	*556.2*	*601.9*	*1,158.0*
Consumption credit	33.8	28.5	62.3	291.0	64.7	355.7
Personal uses	*20.7*	*28.5*	*49.2*	*268.4*	*60.8*	*329.2*
Credit cards	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of consumer durable goods	*13.1*	*0.0*	*13.1*	*22.6*	*3.9*	*26.5*
Purchase of passenger cars	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of securities	5,236.3	6.0	5,242.3	6,779.7	855.1	7,634.8
Purchase of transport vehicles	0.0	0.0	0.0	0.2	0.0	0.2
Community, social and personal services	10.3	4.6	14.8	110.3	43.2	153.6
Others	59.9	4.5	64.3	1,342.2	0.0	1,342.2
TOTAL	**10,571.5**	**573.7**	**11,145.2**	**21,638.7**	**5,659.4**	**27,298.1**

Table A.61
Finance Companies: Loans Sold to Danaharta

	As at end 1998			As at end 1999		
	Non-Performing Loans	Performing Loans	Total Loans	Non-Performing Loans	Performing Loans	Total Loans
	RM million					
Agriculture, hunting, forestry and fishing	0.0	0.0	0.0	7.8	0.0	7.8
Mining and quarrying	0.0	0.0	0.0	0.0	0.0	0.0
Manufacturing	13.0	13.0	26.0	42.2	13.0	55.2
Electricity, gas and water supply	0.0	0.0	0.0	0.0	0.0	0.0
Wholesale, retail, restaurants and hotels	6.0	0.0	6.0	6.0	6.4	12.4
Wholesale trade	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Retail trade	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Restaurants and hotels	*6.0*	*0.0*	*6.0*	*6.0*	*6.4*	*12.4*
Broad property sector	609.6	113.9	723.6	2,357.9	134.9	2,492.7
Construction	*330.6*	*95.4*	*426.0*	*531.6*	*95.4*	*627.0*
Purchase of residential property	*0.0*	*0.0*	*0.0*	*38.8*	*0.0*	*38.8*
Purchase of non-residential property	*104.9*	*18.5*	*123.4*	*217.8*	*18.5*	*236.3*
Real estate	*174.2*	*0.0*	*174.2*	*1,569.6*	*20.9*	*1,590.6*
Transport, storage and communication	0.0	0.0	0.0	0.3	0.0	0.3
Fin, ins, real estate & buss. services	19.2	0.0	19.2	330.3	0.0	330.3
Financial services	*0.0*	*0.0*	*0.0*	*225.5*	*0.0*	*225.5*
Insurance	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Business services	*19.2*	*0.0*	*19.2*	*104.8*	*0.0*	*104.8*
Consumption credit	10.8	0.0	10.8	10.8	0.0	10.8
Personal uses	*10.8*	*0.0*	*10.8*	*10.8*	*0.0*	*10.8*
Credit cards	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of consumer durable goods	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of passenger cars	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of securities	104.4	0.0	104.4	699.7	0.0	699.7
Purchase of transport vehicles	0.0	0.0	0.0	43.7	0.0	43.7
Community, social and personal services	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	3.5	0.0	3.5
TOTAL	**763.1**	**126.9**	**890.0**	**3,502.2**	**154.3**	**3,656.5**

Table A.62
Merchant Banks: Loans Sold to Danaharta

	As at end 1998			As at end 1999		
	Non-Performing Loans	Performing Loans	Total Loans	Non-Performing Loans	Performing Loans	Total Loans
	RM million					
Agriculture, hunting, forestry and fishing	89.5	0.0	89.5	128.8	0.0	128.8
Mining and quarrying	0.0	0.0	0.0	25.2	0.0	25.2
Manufacturing	34.6	37.1	71.7	271.4	50.9	322.3
Electricity, gas and water supply	0.0	0.0	0.0	20.5	0.0	20.5
Wholesale, retail, restaurants and hotels	69.0	0.0	69.0	141.6	0.0	141.6
Wholesale trade	*0.0*	*0.0*	*0.0*	*8.2*	*0.0*	*8.2*
Retail trade	*32.1*	*0.0*	*32.1*	*59.5*	*0.0*	*59.5*
Restaurants and hotels	*36.9*	*0.0*	*36.9*	*73.9*	*0.0*	*73.9*
Broad property sector	473.8	78.8	552.6	1,403.6	272.1	1,675.7
Construction	*107.3*	*17.0*	*124.3*	*776.3*	*166.4*	*942.7*
Purchase of residential property	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of non-residential property	*259.9*	*11.9*	*271.8*	*351.3*	*55.9*	*407.2*
Real estate	*106.6*	*49.8*	*156.5*	*275.9*	*49.8*	*325.8*
Transport, storage and communication	0.0	0.0	0.0	12.0	0.0	12.0
Fin, ins, real estate & buss. services	81.5	0.0	81.5	269.8	0.0	269.8
Financial services	*51.3*	*0.0*	*51.3*	*98.4*	*0.0*	*98.4*
Insurance	*30.2*	*0.0*	*30.2*	*66.8*	*0.0*	*66.8*
Business services	*0.0*	*0.0*	*0.0*	*104.6*	*0.0*	*104.6*
Consumption credit	0.0	0.0	0.0	64.0	0.0	64.0
Personal uses	*0.0*	*0.0*	*0.0*	*64.0*	*0.0*	*64.0*
Credit cards	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of consumer durable goods	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of passenger cars	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Purchase of securities	129.0	12.6	141.7	349.1	15.2	364.3
Purchase of transport vehicles	0.0	0.0	0.0	0.0	0.0	0.0
Community, social and personal services	0.0	0.0	0.0	15.0	0.0	15.0
Others	0.0	0.0	0.0	19.4	0.0	19.4
TOTAL	**877.5**	**128.5**	**1,005.9**	**2,720.4**	**338.2**	**3,058.6**

Table A.63
Banking System: Selected Indicators

	Commercial banks		Finance companies		Merchant banks		Banking system	
	As at calendar year end							
	Dec. 1998	Dec. 1999	Dec. 1998	Dec. 1999	Dec. 1998	Dec. 1999	Dec. 1998	Dec. 1999
Pre-tax profit/Average assets (%)	–0.6	1.4	–1.7	–0.8	–1.6	–0.4	–0.9	0.8
Pre-tax profit/Average shareholders' funds (%)	–7.8	18.0	–29.1	–15.3	–17.0	–4.7	–12.3	11.5
Pre-tax profit per employee (RM'000)	–37.8	92.2	–102.8	–48.5	–260.1	–69.8	–59.2	56.8
Cost[1] incurred per ringgit of revenue earned[2] (sen)	38.7	39.9	81.2	40.9	40.3	31.0	44.1	39.5
Cost[1] incurred per ringgit of net interest income[2] (sen)	54.7	60.0	109.3	50.8	57.3	69.3	62.0	58.1
Overheads to staff cost ratio (%)	120.3	123.2	184.4	202.3	215.6	187.9	135.8	138.8
Staff cost per employee (RM'000)	42.6	40.0	32.1	28.5	52.9	56.4	40.3	37.9
Loan[3]-deposit[4] ratio (%)	92.9	85.5	87.8	82.5	84.3	72.9	91.2	84.2
Loan[3] per branch (RM million)	169.0	159.7	78.8	78.5	1,008.7	857.8	140.3	137.0
Deposit per branch (RM million)	150.9	170.8	75.4	86.1	764.1	741.9	126.2	145.8

[1] Excluding bad debt provisions.
[2] Including interest-in-suspense.
[3] Excluding housing loans sold to Cagamas Berhad.
[4] Including NIDs and repos.

Table A.64
Banking System: Key Data

	As at end				
	1995	1996	1997	1998	1999
Number of					
- Commercial banks	37	37	35	35	33
- Finance companies	40	40	39	33	23
- Merchant banks	12	12	12	12	12
Risk-weighted capital ratio (%)					
- Commercial banks	11.1	10.8	10.3	11.7	12.5
- Finance companies	9.7	9.8	10.3	11.1	10.5
- Merchant banks	11.9	11.7	13.3	15.2	14.6
Branch network					
- Commercial banks	1,433	1,569	1,671	1,690	1,767
- Finance companies	988	1,096	1,144	1,099	960
- Merchant banks	17	24	24	22	22
ATM network					
- Commercial banks	2,230	2,326	2,528	2,647	3,317
- Finance companies	402	525	622	662	587
Persons served per office					
- Commercial banks	14,024	13,492	12,966	13,124	12,854
- Finance companies	20,341	19,314	18,939	20,182	23,659
Number of employees					
- Commercial banks	64,461	68,068	73,709	71,124	69,714
- Finance companies	24,593	26,322	27,937	23,227	20,543
- Merchant banks	2,334	2,592	2,802	2,525	2,373

Table A.65
Industrial Finance Institutions[1]: Sources and Uses of Funds

	1995	1996	1997	1998	1999
	RM million				
Sources:					
Shareholders' equity	1,598.38	2,252.10	2,804.64	2,757.01	3,618.42
Issued & Paid-up Capital	*803.89*	*1,272.99*	*1,613.55*	*1,813.54*	*3,058.07*
Reserves	*694.51*	*882.80*	*990.59*	*1,136.82*	*510.52*
Current profits	*99.98*	*96.31*	*200.50*	*–193.35*	*49.83*
Borrowings	4,719.42	5,302.40	6,655.41	10,463.79	11,593.97
Government	*1,799.13*	*2,078.20*	*2,567.40*	*3,579.83*	*2,776.32*
Other	*2,920.29*	*3,224.20*	*4,088.01*	*6,883.96*	*8,817.65*
Other	859.45	1,067.18	1,084.90	1,862.22	2,385.93
Total	**7,177.25**	**8,621.68**	**10,544.95**	**15,083.02**	**17,598.32**
Uses :					
Deposits	1,459.73	1,210.61	1,117.10	2,974.47	3,067.52
Investments	1,033.18	1,435.74	1,755.18	2,167.55	2,296.76
Quoted	*70.90*	*59.30*	*67.67*	*52.56*	*47.73*
Unquoted	*962.28*	*1,376.44*	*1,687.51*	*2,114.99*	*2,249.03*
Loans	3,887.45	4,989.65	6,091.82	7,656.24	9,251.97
Fixed assets	213.16	269.67	417.20	429.98	510.04
Other	583.73	716.01	1,163.65	1,854.78	2,472.03
Total	**7,177.25**	**8,621.68**	**10,544.95**	**15,083.02**	**17,598.32**

[1] Consist of Sabah Development Bank Berhad, Malaysian Industrial Development Finance Berhad, Malaysian Industrial Estates Berhad, Bank Pembangunan & Infrastruktur Malaysia Berhad, Bank Industri Malaysia Berhad, Export-Import Bank of Malaysia Berhad, Borneo Development Corporation (Sabah) Sendirian Berhad and Borneo Development Corporation (Sarawak) Sendirian Berhad.

Table A.66
Industrial Finance Institutions[1]: Direction of Lending

	1995	1996	1997	1998	1999
	RM million				
Manufacturing	1,756.57	1,872.08	2,086.37	3,420.59	3,419.82
Agriculture	94.50	112.27	135.02	102.69	89.26
Property	895.75	1,579.22	2,148.02	2,209.84	3,048.02
Real estate	*491.05*	*755.16*	*1,060.92*	*1,080.83*	*1,136.93*
Construction	*362.49*	*783.41*	*1,046.85*	*1,090.79*	*1,872.17*
Housing	*42.21*	*40.65*	*40.25*	*38.22*	*38.92*
General commerce	161.04	265.74	284.73	313.80	289.04
Transport and storage	241.41	241.52	215.57	341.33	1,336.62
Other	738.18	918.82	1,222.11	1,267.99	1,069.21
Total	**3,887.45**	**4,989.65**	**6,091.82**	**7,656.24**	**9,251.97**

[1] Consist of Sabah Development Bank Berhad, Malaysian Industrial Development Finance Berhad, Malaysian Industrial Estates Berhad, Bank Pembangunan & Infrastruktur Malaysia Berhad, Bank Industri Malaysia Berhad, Export–Import Bank of Malaysia Berhad, Borneo Development Corporation (Sabah) Sendirian Berhad and Borneo Development Corporation (Sarawak) Sendirian Berhad.

Table A.67
Malaysia Export Credit Insurance Berhad (MECIB)

Year of Establishment	1978					
Objectives	Promoting Malaysian exports through the provision of export credit insurance facilities to exporters to cover against commercial and non-commercial risks and issuing guarantees for banks and financial institutions to facilitate access to export finance. Since the end of 1995, MECIB has also diversified into domestic credit insurance business to provide cover to local SMIs for their domestic sales.					
	1997	1998	1999	1997	1998	1999
	Business Coverage (RM million)			**Income (RM '000)**		
I. Export Coverage						
Short-term Policies						
Comprehensive policies (export declared)	383.0	484.0	719.0	1,879.1	2,299.4	3,749.6
Banker's comprehensive policies (export declared)	4.7	0.2	–	96.9	4.8	–
Bankers' Export Finance Insurance Policy (guaranteed value)	50.4	106.9	100.8	647.4	1,022.3	659.2
Confirming bank policy (letter of credit value)	19.2	83.6	75.6	548.1	101.5	844.1
Sub-total	457.3	674.7	895.4	3,171.5	3,428.0	5,252.9
Medium and Long-term Policies						
Buyer credit guarantee (amount guaranteed)	368.7	375.5	627.4	11,306.9	–	15,672.6
Supplier credit guarantee (amount guaranteed)	47.5	38.3	–	–	–	–
Bond indemnity support (face value insured)	2.9	2.4	34.9	47.9	10.8	1,529.9
Sub-total	419.1	416.2	662.3	11,354.8	10.8	17,202.5
Total Export Insurance Coverage	**876.4**	**1090.9**	**1557.7**	**14,526.3**	**3,438.8**	**22,455.4**
I. Domestic Sales Coverages						
Domestic credit insurance (sales declared)	53.0	118.4	159.2	268.0	621.0	918.6
Specific policies (amount covered)	27.0	–	36.7	84.9	41.4	277.6
Domestic bonds (face value insured)	1.4	–	0.6	20.1	–	7.8
Specific bond (face value insured)	–	0.5	–	–	6.8	–
Comprehensive services rendered policies (amount covered)	–	10.0	10.0	–	2.9	–
Total Domestic Insurance Coverage	**81.4**	**128.9**	**206.5**	**373.0**	**672.1**	**1,204.0**
Total Insurance Coverage	**957.8**	**1,219.8**	**1,764.2**	**14,899.3**	**4,110.9**	**23,659.4**
Total Income	**–**	**–**	**–**	**25,546.0**	**14,035.3**	**33,031.0**

Source: MECIB

Table A.68
Housing Credit Institutions

	Year of establishment	Objective	Average lending rate for housing loans (%)		No. of branches	
			1998	1999	1998	1999
Commercial banks	-		9.0 - 14.8	5.5 - 10.5	1,690	1,888
Finance companies	-		9.0 - 17.2	5.5 - 12.0	1,099	960
Treasury Housing Loans Division	1970	To provide housing loans to Government employees	4.0	4.0	-	-
Malaysia Building Society Berhad	1950	To be the nation's single largest provider of property finance and to contribute to the continuous growth of the nation	10.4	9.2	20	22
Borneo Housing Mortgage Finance Berhad	1958	To provide housing loans mainly to Sabah and Sarawak State Government employees	10.0 - 10.8	8.0 - 8.8	2	2
Sabah Credit Corporation	1955	To improve the social economic development of Sabah through loans mainly to the property, agriculture and business sectors	8.0 - 11.0	8.0 - 11.0	11	11
Bank Rakyat	1954	A co-operative society which collects deposits and provides conventional banking facilities as well as according to Syariah principles	10.0 - 13.3	7.5 - 10.8	74	80
Bank Simpanan Nasional	1974	To promote and mobilise savings particularly from small savers and to inculcate the habit of thrift and savings	9.5	8.5	448	439

Table A.69
Housing Credit Outstanding

	1998	1999 *p*	1998	1999 *p*	1998	1999 *p*
	RM million		Annual change (%)		Share (%)	
Commercial banks	43,436.9	49,871.8	14.6	14.8	57	59
Finance companies	12,908.1	13,371.8	0.2	3.6	17	16
Treasury Housing Loans Division	15,794.2	16,774.0	4.2	6.2	21	20
Malaysia Building Society Berhad	1,436.2	1,294.6	–9.5	–9.9	2	2
Borneo Housing Mortgage Finance Berhad	532.7	590.0	10.9	10.8	1	1
Sabah Credit Corporation	269.3	259.0	1.5	–3.8	…	…
Bank Rakyat	716.9	888.0	54.2	23.9	1	1
Bank Simpanan Nasional	1,005.6	1,036.2	31.5	3.0	1	1
Total	**76,099.9**	**84,085.4**	**9.5**	**10.5**	**100**	**100**

p Preliminary
… Negligible

Table A.70
Approved Housing Loans

	1998	1999 *p*	1998	1999 *p*	1998	1999 *p*
	RM million		Annual change (%)		Share (%)	
Commercial banks	7,768.6	17,951.9	–55.2	131.1	68	77
Finance companies	1,467.2	2,688.5	–52.0	83.2	13	11
Treasury Housing Loans Division	1,673.5	2,396.3	40.7	43.2	15	10
Malaysia Building Society Berhad	70.6	56.9	–55.8	–19.4	1	…
Borneo Housing Mortgage Finance Berhad	121.2	99.2	152.0	–18.2	1	…
Sabah Credit Corporation	17.3	17.2	–60.0	–0.6	…	…
Bank Rakyat	53.2	159.7	–68.7	200.2	…	1
Bank Simpanan Nasional	177.0	111.8	–56.0	–36.8	2	1
Total	**11,348.6**	**23,481.5**	**–49.4**	**106.9**	**100**	**100**

p Preliminary
… Negligible

Table A.71
Agriculture Credit Institutions

	Annual change				As at end 1999	
	1998		1999			
	RM million	%	RM million	%	RM million	% share
Credit for Agriculture						
Banking System	178.4	2.3	1,367.6	17.5	9,183.8	65.4
Commercial Banks	*269.7*	*4.6*	*1,333.2*	*21.5*	*7,520.5*	*53.5*
Finance Companies	*–388.0*	*–29.5*	*–132.4*	*–14.3*	*795.3*	*5.7*
Merchant Banks	*296.8*	*73.4*	*166.8*	*23.8*	*868.0*	*6.2*
Development Agencies	–333.6	–9.1	–584.9	–17.5	2,764.2	19.7
FELDA	*–284.0*	*–8.0*	*–573.1*	*–17.5*	*2,696.1*	*19.2*
Sabah Development Bank	*–49.6*	*–38.3*	*–11.8*	*–14.8*	*68.1*	*0.5*
Rural Credit Institutions	–116.4	–5.4	68.5	3.4	2,101.7	15.0
Bank Pertanian Malaysia	*–123.0*	*–6.1*	*51.2*	*2.7*	*1,934.8*	*13.8*
Bank Rakyat	*4.6*	*11.1*	*17.6*	*38.4*	*63.3*	*0.5*
Farmers' organisations, farmers' co-operatives and agro-based co-operative societies and others	*2.0*	*1.9*	*–0.3*	*–0.3*	*103.6*	*0.7*
Total	**–271.5**	**–2.0**	**851.2**	**6.4**	**14,049.7**	**100.0**
Total resources of the Rural Credit Institutions						
Bank Pertanian Malaysia	–64.5	–1.3	18.4	0.4	4,793.1	36.0
Bank Rakyat	517.3	9.2	1,216.9	19.8	7,349.1	55.2
Farmers' organisations, farmers' co-operatives and agro-based co-operative societies and others	26.2	2.4	55.7	5.0	1,171.0	8.8
Total	**479.0**	**4.1**	**1,291.0**	**10.7**	**13,313.2**	**100.0**

Interest Rates	1998	1999
Bank Pertanian Malaysia		
Commercial loans for agricultural purposes	0% to 4% + prevailing BLR (10.0% at end-December)	0% to 4% + prevailing BLR (7.95 % at end-December)
Fixed deposits	6.20%	3.75% - 3.80%
Savings deposits	4.65%	4.62%
Bank Rakyat		
Commercial loans for agricultural purposes	12.50% minimum	9.50% minimum
Fixed deposits	6.84% - 7.03%	3.60% - 4.30%
Savings deposits	4.00%	3.26%
Branches and Membership		
Bank Pertanian Malaysia	143 branches	143 branches
Bank Rakyat	74 branches with 178,466 members	80 branches with 253,024 members
Farmers' organisations	282 with 651,965 members	282 with 661,303 members
Agro-based co-operatives societies	591 with 94,720 members	579 with 94,046 members

Source: Various agencies

Table A.72
Urban Credit Co-operative Societies[1]

	Annual change 1998	Annual change 1999	As at end 1999	Annual change (%)	% share
	Number				
Total co-operative societies	23	42	957	4.6	100.0
Deposit-taking co-operatives	*–6*	*1*	*12*	*9.6*	*1.3*
Other credit co-operatives	*29*	*41*	*945*	*4.5*	*98.7*
	('000)				
Total members	–547	279	1,514	22.6	100.0
Deposit-taking co-operatives	*–28*	*190*	*313*	*155.1*	*20.7*
Other credit co-operatives	*–519*	*89*	*1,201*	*8.0*	*79.3*
	RM million			Annual change (%)	% share
Sources of funds					
Share subscriptions	–513.9	–432.0	1,213.2	–26.3	33.1
Reserves	–1,124.8	–407.3	298.9	–57.7	8.1
Borrowings	61.6	–142.7	678.3	–17.4	18.5
Sundry creditors	–397.6	–98.0	57.5	–63.0	1.6
Savings and deposits	79.7	25.5	337.8	8.2	9.2
Surplus	–81.7	1,058.3	1,082.3	4,419.2	29.5
Total	**–1,976.7**	**3.8**	**3,668.0**	**–0.1**	**100.0**
Uses of funds					
Investments	–1,149.6	105.0	1,520.7	7.4	41.5
Shares	*–728.4*	*–239.5*	*828.9*	*–22.4*	*22.6*
Fixed and savings deposits	*–136.5*	*71.7*	*339.2*	*26.8*	*9.2*
Real estates	*–296.3*	*188.5*	*188.7*	*–*	*5.1*
Other	*11.6*	*84.3*	*163.9*	*105.4*	*4.6*
Loans to members	–476.9	22.1	1,350.5[2]	1.7	36.8
Fixed assets	–173.3	151.8	567.7	36.5	15.5
Other assets	–310.2	–33.1	111.8	–22.9	3.0
Cash and bank balances	–75.8	0.7	103.7	0.7	2.8
Other	209.1	–242.7	13.6	–94.7	0.4

[1] Urban credit co-operative societies which comprise employees credit societies, thrift and loan societies and thrift and investment societies, were established primarily to provide consumer credit and serve as an investment channel for members.
[2] Refers to total loans outstanding.

Source: Department of Co-operative Development Malaysia

As at the end of 1999, 247 leasing companies and 21 factoring companies had registered with Bank Negara Malaysia (BNM). However, only 144 leasing companies and 17 factoring companies submitted statistics pertaining to their operations to BNM. Total assets of the 144 leasing companies and 17 factoring companies amounted to RM14.8 billion and RM1 billion respectively at the end of 1999. Nevertheless, of the 144 leasing companies, only 45 were pure leasing companies, while of the 17 factoring companies, only 13 were pure factoring companies. The remaining companies only undertook leasing and factoring business as part of their overall business activities.

Table A.73
Leasing Companies[1]: Sources and Uses of Funds

	As at end				
	1995	1996	1997	1998	1999
	RM million				
Sources					
Capital and reserves	430	569	802	677	654
Borrowings from financial institutions	2,779	3,449	4,061	3,071	1,898
Inter-company borrowings	841	2,102	1,739	1,416	1,296
Others	2,039	2,294	2,767	2,364	2,400
Total	**6,089**	**8,414**	**9,369**	**7,528**	**6,248**
Uses					
Cash and bank balances	20	48	144	266	266
Investments	161	351	484	341	308
Receivables	4,851	5,544	5,261	3,820	3,056
Leasing	*3,013*	*3,150*	*3,067*	*2,101*	*1,537*
Factoring	*187*	*171*	*90*	*11*	*4*
Hire purchase	*1,536*	*2,016*	*1,843*	*1,431*	*1,261*
Others	*115*	*207*	*261*	*277*	*254*
Others	1,057	2,471	3,480	3,101	2,618

[1] Statistics shown are for pure leasing companies only.

Table A.74
Leasing Companies[1]: Income and Expenditure

	During the period				
	1995	1996	1997	1998	1999
	RM million				
Income					
Income from	477	611	615	491	329
Leasing	*323*	*380*	*393*	*316*	*225*
Factoring	*16*	*20*	*12*	*5*	*1*
Hire purchase	*136*	*208*	*200*	*169*	*102*
Others	*2*	*3*	*10*	*1*	*1*
Others	120	233	470	418	265
Total	**597**	**844**	**1,085**	**909**	**594**
Expenditure					
Interest paid	273	434	586	620	289
Financial institutions	*240*	*388*	*529*	*566*	*253*
Block discounting	*33*	*46*	*57*	*54*	*36*
Bad debts written off & provision	29	35	100	705	195
Others	145	192	218	283	183
Total	**447**	**661**	**904**	**1,608**	**667**
Pre-tax Profit	**150**	**183**	**181**	**–699**	**–73**

[1] Statistics shown are for pure leasing companies only.

Table A.75
Leasing Companies[1]: Financing by Sector

	During the period				
	1995	1996	1997	1998	1999
	RM million				
Sector					
Agriculture	66	48	50	12	8
Mining and quarrying	37	69	54	4	0
Manufacturing	457	449	406	96	111
Electricity	3	2	3	2	3
General commerce	155	181	164	43	27
Property sector	214	206	195	17	29
Construction	*191*	*190*	*184*	*15*	*24*
Real estate	*22*	*15*	*9*	*2*	*5*
Residential property	*1*	*1*	*2*	*...*	*...*
Transport	184	215	167	74	16
Business, insurance and other services	211	274	216	62	35
Consumption credit	0	...	1	1	0
Others	183	114	128	36	83
Total	**1,510**	**1,558**	**1,384**	**347**	**312**

[1] Statistics shown are for pure leasing companies only.

Table A.76
Factoring Companies[1]: Sources and Uses of Funds

	As at end				
	1995	1996	1997	1998	1999
	RM million				
Sources					
Capital and reserves	70	92	101	85	89
Borrowings from financial institutions	384	437	596	345	247
Inter-company borrowings	227	354	349	245	256
Others	445	528	675	470	385
Total	**1,126**	**1,411**	**1,721**	**1,145**	**977**
Uses					
Cash and bank balances	12	30	19	31	30
Investments	4	7	10	8	5
Receivables	1,066	1,275	1,664	1,053	928
Leasing	*1*	*...*	*...*	*...*	*0*
Factoring	*1,006*	*1,186*	*1,459*	*824*	*808*
Hire purchase	*1*	*7*	*19*	*28*	*2*
Others	*58*	*82*	*186*	*201*	*118*
Others	44	99	28	53	14

[1] Statistics shown are for pure factoring companies only.

Table A.77
Factoring Companies[1]: Income and Expenditure

	1995	1996	1997	1998	1999
	During the period				
	RM million				
Income					
Income from	82	110	150	105	47
Leasing	*0*	*0*	*0*	*0*	*0*
Factoring	*73*	*98*	*129*	*76*	*38*
Hire purchase	*...*	*...*	*1*	*4*	*...*
Others	*9*	*12*	*20*	*25*	*9*
Others	16	30	39	37	15
Total	**98**	**140**	**189**	**142**	**62**
Expenditure					
Interest paid	34	58	74	88	42
Financial institutions	*34*	*58*	*74*	*88*	*42*
Block discounting	*0*	*0*	*0*	*0*	*0*
Bad debts written off & provision	8	11	15	86	202
Others	24	30	34	26	41
Total	**66**	**99**	**123**	**200**	**285**
Pre-tax Profit	**32**	**41**	**66**	**–58**	**–223**

[1] Statistics shown are for pure factoring companies only.

Table A.78
Factoring Companies[1]: Financing by Sector

	1995	1996	1997	1998	1999
	During the period				
	RM million				
Sector					
Agriculture	1	1	1	1	...
Mining and quarrying	3	2	3	0	0
Manufacturing	139	183	171	69	71
Electricity	1	5	6	2	3
General commerce	216	198	259	149	133
Property sector	259	308	374	231	222
Construction	*251*	*298*	*363*	*218*	*174*
Real estate	*0*	*10*	*11*	*13*	*48*
Residential property	*8*	*0*	*0*	*0*	*0*
Transport	14	14	16	10	6
Business, insurance and other services	86	60	161	62	86
Consumption credit	31	32	33	30	23
Others	132	57	67	27	23
Total	**882**	**860**	**1,091**	**581**	**567**

[1] Statistics shown are for pure factoring companies only.

Table A.79
Venture Capital Companies

	1998	1999
	As at end	
No. of venture capital companies	27	30
No. of investee companies invested in	277	270
	RM million	
Cumulative investments made	1,448.6	1,446.2
Sources		
Shareholders' funds	755.2	728.3
Liabilities	963.4	1,000.7
Total	**1,718.6**	**1,729.0**
Uses		
Investments in investee companies [1]	892.0	923.5
Other assets	826.6	805.5
Total	**1,718.6**	**1,729.0**
	During the year	
No. of investee companies invested in	79	41
	RM million	
Profit before tax	–62.1	60.3
Investments during the year	**199.7**	**91.9**
By sector		
Manufacturing	*142.8*	*33.2*
of which:		
- IT based products	*4.1*	*–0.1*
- Electrical and electronic products	*16.5*	*1.3*
Telecommunication services	*–*	*10.3*
Others	*56.9*	*48.3*
By type		
Seed [2]	*15.6*	*4.1*
Start-up [3]	*15.8*	*7.3*
Other early-stage [4]	*23.6*	*3.8*
Expansion/growth [5]	*28.6*	*12.1*
Bridge/mezzanine/recapitalisation/pre-IPO [6]	*54.4*	*26.1*
Management buy-out [7]	*14.6*	*0.9*
Management buy-in [8]	*–*	*5.5*
Turnaround [9]	*11.1*	*1.2*
Cashing-out (secondary purchase) [10]	*8.4*	*1.2*
Others	*27.5*	*29.6*

[1] *After revaluation, liquidation and others.*
[2] *Stage where financing is provided for research and for developing an initial concept or prototype. Before a business has reached the start-up phase .*
[3] *Financing provided to companies for product development and initial marketing. Companies may be in the process of being set up or may have been in business for a short time but have not sold their product commercially.*
[4] *Financing provided to companies that have completed the product development stage and require further funds to initiate commercial manufacturing and sales.*
[5] *Refers to the period during the growth and expansion stage of a company, when the company is breaking even or trading profitably. Financing is required for additional working capital to increase production capacity, marketing and product development.*
[6] *Financing made available to companies or its shareholders in the period of transition from being privately owned to being publicly qouted or for subsequent capital/corporate exercise.*
[7] *Financing provided to enable current operating management and investors to acquire an existing product line or business.*
[8] *Financing provided to enable a manager or group of managers from outside the company to buy into an investee company with the support of private equity investors.*
[9] *Financing made available to existing businesses which have experienced operational and financial difficulties, with a view to re-establishing prosperity.*
[10] *Purchase of existing shares in a company from another private equity investment organisation or from another shareholder.*

Table A.79
Venture Capital Companies (continued)

	List of venture capital companies surveyed	Year of establishment	Type of fund
1.	Citicorp Capital Sdn. Bhd.	1985	Open
2.	S.B. Venture Capital Corporation Sdn. Bhd.	1989	Open
3.	Mezzanine Capital (M) Sdn. Bhd.	1990	Open
4.	BI Walden Ventures Sdn. Bhd.	1990	Closed
5.	BI Walden Ventures Kedua Sdn. Bhd.	1992	Closed
6.	BI Walden Ventures Ketiga Sdn. Bhd.	1999	Closed
7.	PNB NJI Holdings Sdn. Bhd.	1991	Closed
8.	PNB NJI Holdings (II) Sdn. Bhd.	1995	Closed
9.	Perbadanan Usahawan Nasional Bhd.	1991	Open
10.	Public Bank Venture Capital Sdn. Bhd.	1991	Open
11.	MBf Equity Partners Sdn. Bhd.	1991	Closed
12.	Malaysian Ventures (II) Sdn. Bhd.	1991	Closed
13.	Mayban Ventures Sdn. Bhd.	1992	Open
14.	Malaysian Technology Development Corporation Sdn. Bhd.	1992	Open
15.	MTDC Private Equity Management Sdn. Bhd.	1998	Open
16.	Malaysian Technology Development (Johor) Sdn. Bhd. (Regional)	1994	Open
17.	Malaysian Technology Development (Penang) Sdn. Bhd. (Regional)	1994	Open
18.	Malaysian Technology Venture One Sdn. Bhd.	1993	Closed
19.	Malaysian Technology Venture Two Sdn. Bhd.	1994	Closed
20.	Malaysian Technology Venture II (Agr.) Sdn. Bhd.	1995	Closed
21.	Malaysian Technology Venture III Sdn. Bhd.	1997	Closed
22.	Sumber Modal Satu Sdn. Bhd.	1995	Closed
23.	East Malaysia Growth Corporation Sdn. Bhd.	1995	Closed
24.	Ekuiti Teroka Malaysia Sdn. Bhd.	1994	Closed
25.	Amanah Ventures Sdn. Bhd.	1995	Open
26.	Gemrusa Capital Sdn. Bhd.	2000	Closed
27.	Pica (M) Corp. Bhd.	1982	Open
28.	PFM Capital Holdings Sdn. Bhd.	1977	Open
29.	MSC Venture One Sdn. Bhd.	1999	Closed
30.	Commerce Asset Ventures Sdn. Bhd.	1997	Open

Table A.80
Export-Import Bank of Malaysia Berhad (Exim Bank)

Year of Establishment	1995			
Objective	Establishing an institutional support mechanism to facilitate the exports of manufactured goods and diversification of exports by providing medium-and long-term credit to Malaysian exporters and investors, as well as foreign buyers of Malaysian goods. Effective January 1998, the Export Credit Refinancing facility was transferred from Bank Negara Malaysia to Exim Bank.			
Facility	**Loans / Guarantee Approved**		**Operating Income**	
	1998	1999	1998	1999
	RM million		RM million	
Buyer Credit Facility	3.8	269.8	19.1	32.7
Overseas Investment Credit Facility	27.5	109.9	14.0	12.8
Supplier Credit Facility	274.6	210.8	3.1	3.8
Guarantee	0.0	28.5	0.1	1.0
Export of Services Financing Facility	5.0	0.0	0.1	0.1
Export Credit Refinancing	929.0	995.5	94.4	39.7
Others	0.0	0.0	4.4	4.8
Total	**1,239.9**	**1,614.5**	**135.2**	**94.9**

Source: Exim Bank

Table A.81
Funds Raised in the Capital Market

Sector	1995	1996	1997	1998	1999*p*
	RM million				
By Public Sector					
Malaysian Government Securities (MGS)	2,000.0	6,000.0	3,000.0	14,950.0	10,000.0
MGS Advanced Subscriptions	0.0	–	0.0	0.0	0.0
Khazanah Bonds (KB)	–	–	794.4	2,731.9	2,598.2
Government Investment Issues (GII)	750.0	–	0.0	0.0	2,000.0
Malaysia Savings Bonds (MSB)	–	–	0.0	0.0	377.2
New Issue of Government Securities	2,750.0	6,000.0	3,794.4	17,681.9	14,975.4
Less: Redemptions					
MGS	2,250.0	3,809.0	3,648.0	6,200.0	6,676.0
KB	–	–	0.0	0.0	0.0
GII	500.0	900.0	1,400.0	750.0	2,000.0
MSB	37.8	34.0	154.8	928.2	2.1
Less: Government Holdings	–2.6	–74.1	–1.2	0.0	0.0
Net Funds Raised by the Public Sector	**–35.2**	**1,331.1**	**–1,407.2**	**9,803.7**	**6,297.3**
By Private Sector					
Shares/Warrants					
Ordinary Shares[1]					
Initial Public Offers	4,175.0	4,099.2	4,781.0	684.7	999.5
Rights Issues	5,240.2	5,268.5	8,524.9	722.0	4,346.9
Private Placements/Restricted Offers-for-Sale	1,146.9	4,554.4	3,233.6	320.1	518.6
Special Issues	875.5	2,002.3	1,818.8	61.0	208.0
Preference Shares	–	–	0.0	0.0	0.0
Warrants	–	–	–	–	13.5
New Issue of Shares/Warrants	11,437.6	15,924.4	18,358.3	1,787.8	6,086.5
Private Debt Securities[2]					
Straight Bonds	3,929.9	2,675.4	4,209.0	10,238.0	9,570.0
Bonds with Warrants	3,607.7	5,563.7	2,950.3	150.0	555.0
Convertible Bonds	863.1	1,794.6	2,018.9	98.8	1,269.2
Islamic Bonds	800.0	2,350.0	5,249.7	345.0	1,734.0
Cagamas Bonds	3,022.0	4,665.0	5,169.0	3,320.0	4,425.0
New Issue of Private Debt Securities	12,222.7	17,048.7	19,596.9	14,151.8	17,553.2
Less: Redemptions					
Cagamas Bonds	2,635.0	750.0	1,640.0	5,012.0	6,470.0
Other Private Debt Securities[3]	1,249.1	1,765.0	1,368.5	2,964.5	6,279.5
Net Issue of Private Debt Securities	8,338.6	14,533.7	16,588.4	6,175.3	4,803.7
Net Funds Raised by the Private Sector	**19,776.2**	**30,458.1**	**34,946.7**	**7,963.1**	**10,890.2**
Net Funds Raised in the Capital Market	**19,741.0**	**31,789.2**	**33,539.5**	**17,766.8**	**17,187.4**
Short-Term Securities					
Commercial Papers	20,216.5	35,980.0	55,993.7	70,045.0	61,598.6
Cagamas Notes	3,395.0	5,790.0	13,890.0	16,845.0	20,625.0
New Issue of short-term securities	23,611.5	41,770.0	69,883.7	86,890.0	82,223.6
Less: Redemptions					
Commercial Papers	18,993.7	31,776.0	53,632.8	71,370.5	62,396.0
Cagamas Notes	1,945.0	5,290.0	11,700.0	15,335.0	20,435.0
Net Issue of Short-Term Securities	2,672.8	4,704.0	4,550.9	184.5	–607.4
Total	**22,413.8**	**36,493.2**	**38,090.4**	**17,951.3**	**16,580.0**

[1] Exclude funds raised by the exercise of Employee Share Options Schemes, Transferable Subscription Rights, Warrants and Irredeemable Convertible Unsecured Loan Stocks.
[2] Exclude bonds issued by the banking institutions.
[3] Include all straight bonds, bonds with warrants, convertible bonds and Islamic bonds.
p Preliminary

Table A.82
Kuala Lumpur Stock Exchange: Selected Indicators

	1995	1996	1997	1998	1999*p*
Indices					
Composite	*995.2*	*1,238.0*	*594.4*	*586.1*	*812.3*
EMAS	*279.5*	*347.7*	*151.2*	*146.9*	*206.4*
Second Board	*298.7*	*576.3*	*162.9*	*158.4*	*180.6*
Trading Volume (mil. units)	33,979.0	66,461.0	72,798.7	58,287.1	85,156.6
Main Board	*30,862.0*	*47,351.0*	*62,278.3*	*52,061.1*	*79,981.0*
Second Board	*3,078.0*	*19,039.0*	*10,497.3*	*6,226.0*	*5,175.6*
Average Daily	*139.8*	*268.0*	*293.5*	*236.9*	*343.4*
Trading Volume (RM mil)	178,859.0	463,265.0	408,558.0	115,180.7	185,249.5
Main Board	*157,908.0*	*278,138.0*	*299,595.6*	*100,610.4*	*171,500.6*
Second Board	*20,877.0*	*185,061.0*	*108,958.4*	*14,570.3*	*13,748.9*
Average Daily	*736.0*	*1,868.0*	*1,647.0*	*468.2*	*747.0*
No. of Listed Companies	529	621	708	736.0	757.0
Main Board	*369*	*413*	*444*	*454.0*	*474.0*
Second Board	*160*	*208*	*264*	*282.0*	*283.0*
Market Capitalisation (RM bil)	565.6	806.8	375.8	374.5	552.7
Main Board	*542.8*	*746.0*	*354.2*	*353.4*	*527.6*
Second Board	*22.7*	*60.8*	*21.6*	*21.1*	*25.1*
Market Capitalisation / GDP (%)	254.2%	318.0%	133.3%	131.6%	184.4%

p Preliminary

Source: Kuala Lumpur Stock Exchange

Table A.83
Ringgit Debt Securities[1]: Amount Outstanding

As at end	Malaysian Government Securities	Government Investment Issues	Khazanah Bonds	Malaysia Savings Bonds	Danaharta Bonds	Danamodal Bonds	Cagamas Bonds	Other Private Debt Securities[2]	Total
	RM million (nominal value)								
1995	64,719	5,050	–	1,131	–	–	9,312	22,701	102,913
1996	66,910	4,150	–	1,092	–	–	13,227	33,528	118,907
1997	66,262	2,750	1,000	918	–	–	16,756	46,594	134,281
1998	75,012	2,000	4,850	4	2,601	11,000	15,064	46,737	157,268
1999*p*	78,336	2,000	8,980	379	10,344	11,000	13,019	77,413	201,470

[1] Refer to debt securities with an original maturity period of more than one year.
[2] Exclude debt securities issued by the banking institutions. Private debt securities are assumed to be redeemed or converted at maturity.
p Preliminary

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