Paper Title

Heterodux Economic Policies in Malaysia. Economics Rational, Stock Market and A Corporate Mess

Mohamed Aslam
Applied Economics Department
Faculty of Economics and Administration
University of Malaya
50603 Kuala Lumpur
MALAYSIA
Tel: 603-79673605/4, Fax: 603-79677252
E-mail: g2mohd@umcsd.um.edu.my
maslam@um.edu.my

Heterodox Economic Policies in Malaysia. Economics Rational, Stock Market and A Corporate Mess

Mohamed Aslam[1]

INTRODUCTION

The policies of capital control, exchange control and fixed exchange rate which were introduced by the Malaysian government in September 1998 can be regarded as a heterodux policies. The idea of these measures emerged since the policy package prescribed to Indonesia, South Korea and Thailand by the International Monetary Fund (IMF) failed to contain the impact of the financial crisis. Actually, Malaysia had implemented orthodox economic policies before September 1998, however the policies were incompatible to accommodate the impact of the financial crisis; in fact, it subsequently drove the economy into a deep crisis. Based on economic arguments, capital and exchange controls (CEC) are used to curb the high swing of portfolio capital outflow and volatile exchange rate, therefore enable the government to manage economic recovery more effectively. In other words, the measures will increase the autonomy of monetary policy and allow the government to run expansionary economic policies. Liquidity in the banking system will be stabilised or increased thereafter. Supplemented with the government's directive to the banking sector to increase loans to the business sector, this may delay failure of businesses. The main purpose of the fixed exchange rate is to direct price stability mainly in export sectors and this will speed up economic recovery. Some argue that the measures were politically motivated. The economic crisis had eroded wealth and increased the debt of certain firms which were closely linked to the ruling coalition. The intention of the policies is to delay a downfall of heavily debted firms and provide opportunities to the firms to undertake extensive restructuring or allow the pengurusan Danaharta Nasional Berhad (Danaharta) a state asset managament company and Corporate and Debt Restructuring Agency (CDRC) to manage the company's debt and conduct restructuring exercises. Another argument is that, the measures will decrease the value of the company's assets (shareholders) by depressing the company's stock price, thereby providing an incentive to other firms to buy and control the indebted firm. This paper tries to discuss the heterodox policies from the perspectives of politics and economics.

SECTION I
ECONOMICS RATIONAL

Before the capital control was announced, Malaysians had moved up to RM32 billion into Singapore at the height of the financial crisis (SBT, 3 July 1999). The amount of RM in circulation in the country then was only RM20 billion. Local investors contributed to the panic and loss of confidence as a result of the funds pull-out by foreign investors. Local investors had also contributed to the exodus of funds during the onset of the financial crisis two years ago. With the implementation of selective exchange controls on September 1, 1998 all ringgit savings overseas had been brought back. The exchange controls also meant that Malaysians could not invest overseas unless they borrowed in foreign currencies.

Malaysia imposed capital control on the outflow of portfolio investment on 2 September 1998[2]. Long-term flows and FDI were not regulated. A "twelve-month rule" was imposed

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[1] Lecturer, Applied Economics Department, Faculty of Economics and Administration, University of Malaya, 50603 Kuala Lumpur, Malaysia. E-mail: g2mohd@umcsd.um.edu.my or maslam@um.edu.my.

[2] Some people, mainly from the financial sector argued that such a measure is not effective in restoring economic or market confidence. The question is now, do they understand the purpose and mechanic of the capital and exchange controls, and why these measures are introduced during the country facing an economic instability? If Malaysia had a policy of capital control (either control on capital inflow or outflow) and a stringent exchange control before 1997, would the economy have

prohibiting the repatriation of portfolio funds for 12 months. The “12 month rule” was subsequently replaced (for new funds) with a levy. The levy was reduced to 10 percent and applied only to dividends repatriated (Mahathir, 2000). The 10 percent levy has been lifted up for portfolio capital that has been invested (stay) in one year (Ministry of Finance, 2000). The government has also imposed an exchange control to disallow non-residents from holding the ringgit either in the form of hard currency or in bank accounts in offshore markets[3]. The ringgit is fully convertible for commercial transaction purposes as long as they are undertaken through Malaysian banks in Malaysia.

In international finance, capital control is not a new issue. Industrialised countries have used capital controls to soften the pressure on the exchange rate since the Gold Standard. Under the Bretton Woods System[4] capital control was an integral part in the system in ensuring the stability of the exchange rate. The maintenance of capital controls had been authorized in the Articles of Agreement negotiated at Bretton Woods in order to reconcile exchange rate stability with other goals: in the short run, concerted programs of postwar reconstruction; in the long run, the pursuit of full employment (Eichengreen B, 1996:188). After the collapse of the fixed exchange rate regime under Bretton Woods, the floating exchange rate gained much attention and capital control on international capital flows was eliminated gradually.

Capital account convertibility means lifting up any form of control or restriction on international capital transactions (financial and real assets) and freeing currency transactions. There are many forms of capital restriction from direct control of inflow or outflow to indirect control of capital inflow or outflow. This broad definition suggests that it will be difficult to generalize about capital controls because they can take on many forms and may be applied for various purposes (Bakker, 1996). Controls may take on the form of taxes, price or quantity controls, or outright prohibition on international trade in assets. Example of controls: Chile requires non-interest-bearing reserves against certain capital inflows; Switzerland limits interest payments to foreign owners of claims; France and Japan – they prohibit residents from purchasing foreign securities except through domestic financial institutions. Other examples of forms of capital control include rationing foreign access to the new issue market and limiting domestic financial institutions foreign currency tradings (including swap)(Cooper R, 1999).

The major cause of the recent Asian financial crisis is the cross-border movement of portfolio investment (bonds and equity). The introduction of capital control is designed to eliminate or limit the impact of the capital movement on the economy. Portfolio capital is different as compared to long-term loans and foreign direct investment (FDI) in terms of its contribution to economic development, impact on prices and the exchange rate. The most outstanding feature of foreign portfolio investment (FPI) as opposed to FDI and long-term external loans, is that the FPI (“hot money”) can reverse in a very short time. When the FPI finds its way into

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fallen into the currency-cum-financial crises? Besides China, Singapore and Taiwan also have a policy of capital control and this is the reason (partly) why those countries have escaped from the impact of the crises. For instance, the Singaporean government does not allow foreigners to invest in her equity and derivative markets in Singapore dollar, hence speculation on the currency is eliminated generally. In other words, the government demads that its currency be determined by economic fundamentals.

[3] There were regulations on exchange or restrictions on capital movement before the Asian crisis and even before the economy received a massive capital inflow since 1990 (refer to Bank Negara Annual Report 1990, 1993, 1994 and 1998).

[4] The founding fathers of the Bretton Woods System, Harry Dexter White and John Maynard Keynes, encouraged economic liberalization yet also suggested that restrictions on international financial transactions should be placed (Eichengreen. Barry, 1998).

the banking system and pushes up domestic expenditures and increases the current account deficit, its reversal can affect the domestic economy through a decrease in asset prices, a jump in interest rates, liquidity problems in the banking sector, or a depreciation of the currency (Corbo and Hernandez, 1996). Furthermore, if the central bank does not react quickly enough and the stock of international reserves is low, then the reversal may cause a balance of payments crisis.

As the Asian pre-crisis experience illustrates, the FPI can cause inflation of asset prices (including consumer prices) and provoke interest rate hikes. These matters stimulate a "chain-reaction" and "herd behaviour" in the asset market. Due to the expectation of an increase in future returns on investment, domestic investors further pour their money or savings in the market, consequently a "bubble" will be created in the market[5]. If future expectation of making profits falls, then foreign (domestic) investors will leave the market by selling their stock holdings and buying foreign currency. Stock prices will fall and, depending on the exchange rate system, either a loss of international reserves and an increase in domestic interest rates, or a depreciation of the exchange rate, or both will occur. If interest rates, asset prices, or exchange rates fluctuate too widely it can be very damaging for the economy because (i) high interest rates will increase corporate failure (non-performing loans of banks may accelerate) and, (ii) appreciation of currency value will decrease export competitiveness or profitabilities of exporting and import-competing sectors, and increase the cost of imports resulting in a deterioration of the current accounts of the balance of payments. Another impact of the FPI, is that it may induce a diversion of resource allocation (loans) in the banking system from the productive to the unproductive sector[6]. In other words, resources might move from the tradable to non-tradable sectors, and the shifting could harm real economic growth in the long run, which is exactly what happened in Malaysia prior to the Asian crisis.

Although, the main objective of the capital control is to help stabilise the exchange rate and international payments system, it would also have the effect of delaying any fall in international reserve. International reserve is a part of the monetary base. A fall in the reserve means monetary aggregates will be unstable and might create illiquidity in the financial system. The monetary base or high-powered money (M^B) consists of domestic credit (D) plus international (foreign exchange) reserves (R) or net foreign assets held by the central bank, as given by the equation $M^B = D + R$. A change either in international reserves and domestic credit will influence the monetary base. D is a 'control variable', which means that a government can control expansion (or accumulation) of domestic credit through the interest rate policy or credit rationing. But R is an 'exogenous variable', that is, it depends on external sector positions (balance of payments account) as represented by the equation $R= CA + KA$[7], where CA=current account and KA=capital account. R is equal to a

[5] The inflow of portfolio capital or foreign capital in the stock market is not exactly induced by the interest rate differential. Basically, investment in the market is based on the expectation of higher return on investment by betting on prices (arbitrage). In Malaysia, bond and derivative markets are less developed. The only possibility inflow of foreign funds is in the equity (stock) market. (There is foreign short-term capital inflow into the country based on the interest rate differential, i.e investment in fixed deposits in commercial banks).

[6] There is no evidence of foreign portfolio capital encouraging resource allocation and increasing efficiency in the banking or financial system. Efficiency in the financial sector is based on the development of new financial instruments (capital or money markets), technology and financial deregulation. The other question that needs to be considered is how long does the foreign portfolio fund stay in an economy.

[7] It also can be written as $\Delta CA + \Delta KA = \Delta R$. Foreign exchange or international reserve (R) is also regarded as a net foreign asset (F). In the flexible exchange rate, the equation is read as $CA=-KA$, that is, the deficit of current account is offset by the surplus of KA, which means the central bank is out of the foreign exchange market. Whereas in the fixed exhange rate regime, the central bank will

net demand on domestic securities by foreign resident. Capital account comprises of foreign loans (long-term and short-term) (FL), foreign direct investment (FDI) and foreign portfolio investment (FPI). To simplify the matter, we decompose the KA into two groups, non-speculative capital F_{NS} consisting of FL and FDI and speculative capital F_S which is FPI. We can rewrite the equation and read as CA + [FDI + FL + FPI] = R. If we assume that a deficit in CA is offset by F_{NS}, thus F will be equal to F_S. So it must be true that $M^B = D + F_S$. Assuming that domestic credit (D) remains unchanged, a change in F_S will affect a change in M^B. Therefore the monetary base is entirely influenced by the FPI[8]. Control of the F_s allows the government to manage the monetary sector more effectively. This is done by delaying a fall in international reserves through the outflow of F_s and allowing the accumulation of international reserves through the current account and non-speculative capital. Therefore, Bank Negara Malaysia (BNM) will have greater freedom in implementing monetary policies without worrying about the accumulation of reserves from the speculative market. Secondly, the policy of capital control will permit the economy to re-build international reserves via other components of balance of payments, i.e trade and long-term capital accounts. Since the outbreak of the financial crisis in July 1997, the Malaysian economy had run losses in international reserves particularly from the outflow of portfolio capital. Thirdly, capital control can avoid a liquidity or credit crunch in the economy. The reason as mentioned above is the delay in a fall in international reserves.

The main objective of Malaysia's exchange control was to regain control of the ringgit from speculators and manipulators in the international foreign exchange market (Mahathir, 2000). This was done by (a) 'freezing' the external ringgit accounts of non-residents in Malaysia and (b) enforcing the withdrawal of about RM20-25 billion held in bank accounts from abroad and transfering it into the country's banking system. Non-residents were not allowed to sell or lend the ringgit to other non-residents but could invest their funds freely in the country. Thus, currency traders were unable to shortsell the ringgit and change its exchange rate. Therefore, only the government could determine the exchange rate.

The exchange control also assists in the effectiveness of the capital control by alleviating speculation on the RM in the international foreign currency market. Those controls allow the BNM to embrace the monetary sector firmly. The measures will also reduce sterilization costs to the bank. A combination of capital control and exchange control to some extent will increase the degree of independence of the monetary policy[9]. Before the capital control, the statutory reserve requirement (SRR) was 13.5%, currently the rate is below 4%. The low SRR policy has injected about RM80 billion into the banking system. This expansionary

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loose control of its money supply, thus money supply becomes an endogenous factor. An increase in reserve represents an increase in the stock of net foreign assets owned by residents.

[8] In Malaysia, the main factor influencing money supply (and exchange rate stability) in pre-crisis period and during the crisis is the short-term capital (FPI) (see Bank Negara Annual Report 1993 and 1994). Available data suggests that from 1993 to 1996 the accumulation of international reserve come largely from short-term capital.

[9] In a pure fixed exchange rate, the central bank will loose control of money supply as argued in the Mundell-Fleming model. Experiences of countries show that the Mundel-Fleming prepositions do not work practically. Capital flows play a crucial role in the balance of payment crisis in two ways. Swings in international capital flows can create both a balance of payments problem and if the exchange rate is not defended it can accelerate devaluation under the fixed exchange rates if there is a policy of free capital mobility. With regards to the flexible exchange rate, there is no country in the world that has fully adopted the exchange rate system purely. Most of the countries with the flexible exchange rate regime frequently intervene in foreign exchange markets to realign (or stabilise) the exchange rate to the desired level. There are two main questions which should be examined by a country before making a decision in selecting an exchange rate policy. Which factor may influence most of the exchange rate movements, fundamental or non-fundamental? Can the financial market (and foreign currency market) be trusted in not causing a deterioration of the currency value (or the exchange rate)? Policy makers wishing to avoid exchange rate fluctuation and retain scope for independent monetary policy must implement another option, that is, to restrict capital flows (Neely, 1999).

monetary policy has increased money supply (M3) from RM401.5 billion in 1998 to RM458.5 billion in 2000, a 12.4 percent increase. Total deposits (demand, saving and fixed) have increased from RM232.9 billion in 1998 to RM282.1 billion in 1999 before recorded at RM302 billion in 2000. Liquidity in the banking system has expanded, however, loans extended by banks to the private sector are not impressive. Loans to the private sector in 1997 was RM406.9 billion, in 1998 it declined to RM397.2 billion and marginally increased to RM398.3 billion in 2000. On the other hand, the capital and exchange controls have allow the government to tap extra liquidity caused by the measure to deal with the economic recession more effectively. The government budget has expanded as indicated by the value of treasury bills that have been issued. The government had issued the bill value of RM15 billion in 1998, RM10 billion in 1999 and RM16.4 billion in 2000.

Based on the experiences of developing countries, capital controls on outflow may not stimulate or encourage the inflow of foreign short-term capital, but the control may also not hinder the inflow of long-term capital. Since capital controls was imposed, the net outflow of foreign portfolio funds from September 1998 to September 1999 was about RM1.3 billion. The total net outflow of the capital was about RM3.33 billion from year 1999 to 2000. Whereas, FDI is still coming into the Malaysian economy. In 1998, total FDI into the economy was about US$2.7 billion and increased to US$3.5 billion in 1999, and is expected to record about US$6.7 billion in the year 2000. In 1997, the inflow of FDI was US$7.3 billion compared to US$6.5 billion in 1996. The international reserves have increased from US$21.7 billion in 1997 to US$26.2 billion in 1998, to US$30.9 billion in 1999 before declining to US$30.3 billion as at November 15, 2000. The decrease in foreign reserves is not only attributed to the outflow of portfolio funds but also due to the repayment of foreign debt, particularly short-term debt. The foreign short-term debt has been reduced from RM43.3 billion in 1997 to RM17.6 billion in 2000

SECTION II

Since the currency cum financial crisis broke in 1997, the government has introduced many policies, in the form of macro as well as micro policies, to reflate the economy, particularly to place the private sector including financial institutions on the right track. The main impact of the economic crisis on Malaysia is failure of the corporate sector (and also the banking system). Restructuring exercises have been encouraged and in certain cases even enforced. The immediate problem of the private sector is debt. This paper tries to present exercises has been taken by the private firms in removal of the debt and stay competitive in business (market). However, due to resource constraits and undisclosed information either from the government or companies on the issue of debt and restructuring exercises, thus the presentation on the issue is limited. This section is divided into 8 sub-sections, as follows:. An Overview: Corporate Performance; Stock Market Performance; CDRC; Danaharta; Bail-out; Corporate Restructuring Cases; and Bank Consolidation.

An Overview: Corporate Performance

The Malaysian private (corporate) sector is struggling to settle its debt. The debt has been estimated at more than RM60 billion since the Asian financial crisis struck in 1997. The percentage of listed firms on the Kuala Lumpur Stock Exchange (KLSE) that cannot cover interest expenses has increased from 5.6 percent in 1996 to 17.1 percent in 1997, to 34.3 percent in 1998 but in 1999 it declined to 26.3 percent. In the years 2000-2002 its estimated about 16 percent of the listed companies will not be able to cover interest payment (Goad, GP, 1999). Furthermore, about 80 percent of Malaysian companies did not perform well in 2000 (Barrock, L, 2001a).

The most affected and badly hurt in the private sector are companies dealing in construction and infrastructure as well as property and banking (finance). Shares prices of those firms (with the exception of the finance counter) fell sharply and the prices discounted more than 50 percent. For instance, share prices (closing price as at 29 March 2001) of some construction firms or developers such as Arab-Malaysian Development fell to RM0.21; Damasara Bhd-RM0.28 sen; Metroplex-RM0.26, Sri Hartamas-RM0.41; Sateras-RM0.23; Mycom-RM0.12), Innovest-RM0.10; MUI Properties-RM0.33, Hong Leong Properties-RM0.50; Taiping Consolidated-RM0.21; KLIH-RM0.49, Menang-RM0.13; Selangor Dredging-RM0.37, Land and General-RM0.27 and Promet RM0.29.

Virtually all large developers are struggling to climb out from the debt crisis. As for the case of Metroplex Bhd, it has a huge net debt of RM1.12 billion (inclusive of the RM310 million) as at end of July 2000. Its fixed assets are valued at about RM1.7 billion (comprising mainly its integrated Putra Place project in KL (that included Legend Hotel, theMall shopping complex) and Wisma Equity as well as its hotels in Cherating and in the Philippines). Theoretically it should be able to cover the debt, but the firm reluctant to unload some of the assets (The Sun, 8 January 2001). Mycom is caught more than RM1.8 billion debt. It has two unfinished projects (stopped), the RM900.6 million Duta Grand Hyatt hotel and RM699.2 million retail project Duta Plaza in central Kuala Lumpur. Mycom sought the government's help in September 1998 after it defaulted on its debt and the Sabah government scrapped Olympia's (subsidiary of Mycom) lottery licence (The Sun, 5 January 2001). Failling to pay the debt, Mycom dragged its bankers Sime Bank Bhd, MBf Finance Bhd and Arab-Malaysian Bank Bhd into debt woes. Non-performing loans of the banks rose thereafter. Taiping Consolidated Berhad (TaipingCon) which secured a project from Keretapi Tanah Melayu (KTM, owns 30% of the project) to build the Sentul Raya (residential and commercial centre) project costs about RM2.5 billion, has abandoned the project due to the economic crisis. YTL interested in the project and invested and directly controlled 51% of TaipingCon in early 2001 and the Sentul Raya project has resumed. There are many cases of companies which are unable to continue developing construction projects which will be elaborated below. The failure of construction and property firms in developing land and property has affected and increased the NPL of the banking system, since many of those firms are powerless to meet loan obligations.

Although the Malaysian economy has expanded about 7% in 2000, its real estate market remains in a slump. Given the slow down of the property market, a large volume of commercial and residential units are still unsold. In 2000, unsold residential units were about RM6.6 billion, whereas RM21.8 billion commercial space remained unsold (shopping complexes-RM10.2 billion, retail lots-RM2.1 billion, industrial-RM1.1 billion and office space RM8.4 billion). The government has liberalised regulation on foreign ownership in the property sector to ease the overhanging of properties. Before the liberalisation, foreigners were not allowed to own more than 30 percent of any housing project, and they were barred from owing properties worth under RM250,000 each. Foreigners were also not allowed to have majority control of commercial space-offices, shopping malls and hotels.

Many companies either public listed or privately owned have undertaken restructuring exercises. Most of the restructuring exercise involved debt restructuring. There are a few actions that have been taken by companies for debt settlement such as selling part of the company's asset, debt-equity swap (either in the form of right issue, warrant or bonds), or asking the government to bail it out. There are companies which sought help from the Corporate Debt Restructuring Committee (CDRC) and Pengurusan Danaharta Nasional (Danaharta) to restructure its debt. However, there are companies which have protracted debt restructuring exercises. This is due to the unwillingness of the companies to restructure their assets or dispose of their assets. Many of them are still counting on a vibrant stock market to resolve their debt woes. Furthermore, many companies have banked on their merchant bankers' financial wizardry to shift their debts around instead of unloading assets in the much-improved environment.

The capital and exchange controls (CEC) implemented by the government is a sound economic policy. The CEC and supplemented reclassification of non-performing loans (NPLs) from 3-months to 6-months along with the regime of low interest rates will provide time and funds for the companies in distress to restructure. The CEC policy has accumulated liquidity in the financial system. Total deposits (demand, saving and fixed) has increased from RM232.9 billion in 1998 to RM282.2 billion in 1999 and RM302 billion in 2000 (Table 1). Money supply growth in year 2000 is about 6.6 percent. Since the banking sector is stuck with large non-performing loans (NPLs), they are reluctant to provide financial facilities to the private sector, mainly which companies have a huge debt. In 1999 and 2000, the growth of loan was less than 2 percent in contrast to the growth of deposits. Loans to the private sector in 1997 which was RM406.9 billion declined to RM397.2 billion in 1998 and increased marginally in 2000 to RM398.3 billion. However, loans in the form of debt papers (securities) accelerated from RM40.7 billion in 1997 to RM54.5 billion in 1998 to RM72.2 billion in 2000. The increment is largely related to the conversion of loan to bonds (medium/long-term).

TABLE 1
Malaysia: Monetary Aggregate (selected components) (RMbil)

Year	Currency	Demand Deposits	Saving Deposits	Fixed Deposits
1990	10.1	14.2	13.4	30.0
1995	17.5	34.4	23.5	96.4
1997	21.4	41.9	26.8	156.5
1998	18.2	35.9	27.8	169.2
1999	24.8	48.7	35.2	198.3
2000	22.3	56.5	40.5	205.0

Source: Bank Negara Malaysia, monthly bulletin.

I argue that CEC is a pronounce measure. However, the fixed exchange rate even its has stimulated economic recovery from the exports channel[10], concurrently its accelarated foreign debt servicing. In other words, the fixed exhange rate has driven private companies (and financial institutions) in distress but only for the companies whice have borrowed money denominated in the US dollar. The value of the US dollar against RM is now very much higher than the pre-crisis level, subsequently it has created difficulties to the borrower in servicing the loans. This is one of the weaknesses of the fixed exchange rate in the case of Malaysia.

The impact of the financial crisis has driven the corporate sector to undertake immediate and extensive restructuring exercises and implant corporate governance and strenghten accounting and auditing procudures. The KLSE has introduced a new ruling that require listed companies to regularise their financial conditions. The ultimatum may force insolvent and debt-ridden listed companies to seriously consider how to turn themselves around, and help investors focus on companies with sound fundamentals. At the same time, it may also further reduce the declining premiums that rescuers with assets or cash are willing to pay for listed vehicles. It is estimated that at least 80 of the 796 listed companies could be suspended at least, if not delisted, if they fail to "regularise" their financial conditions by the KLSE's earliest deadline of February 23 2002. These companies have a deficit in their shareholders' funds or have had special administrators appointed by bad debt agency Danaharta (BT, 2 February 2001). Among the companies affected is Dewina Bhd, a food manufacturer, partly owned by the son and brother of Deputy Prime Minister Abdullah Ahmad Badawi. Dewina's total debts are about RM25 million and the company will place

[10] Indirectly, the fixed exchange rate has accumulated international reserve to finance foreign loan repayments, overseas investment by the local private companies as well as outflow of portfolio funds. Decline in international reserves since early 2001, was largely due to servicing of foreign debt and outflow of portfolio fund.

out 1.9 million new shares to unidentified shareholders to raise cash. One of the biggest contracts Dewina secured was in 1996 in the privatisation exercise to supply food to the armed forces for 15 years.

Despite the government's encouragement and establishing institutions dealing in debt restructuring cases, corporate restructuring in Malaysia is still premature. Danaharta has a wide range of power to force restructuring. But restructruing seems to be very slow. The slower the debt restructuring, the higher the risk of corporate insolvency and bank failure. Government may not allowed big firms to fail such as Renong. Renong, Lion Group and MRCB, which altogether have total debts of about RM43 billion equivalent to almost 8 percent of total loans from the banks and if these companies collapse the banks (creditors) will be in hazardous. On the other hand. writing off that amount of debt may start a bank run. This is one of the main reasons for the enforcement of merger programs in banking institutions. On top of that, the establishment of Danamodal Nasional (Danamodal) and deployment of about RM11 billion to recapitalise and rehabilitate the banking system is crucial. The financial system has to be fixed and be strong.

Stock Market Performance

The CEC's policy has been blamed for the gloomy performance of the KLSE. The main factor influencing stock market prices is not quite clear. In general, non-fundamental factors such as news (rumours), politics and speculation are major factors which reflect the movement of share prices. There are fundamental factors related to the company itself that "may" play a role in determining the share price of the company, i.e. the company's assets, company's debt, profitibility and corporate governance. But this is true during the slump period and not during the bull run (before financial crisis 1997). Factors of nepotism, croynism, corporate governance and weak financial regulation and supervision have emerged during the financial crisis and not before the crisis. Therefore, people who believe that the CEC policy caused the depression of stock prices is incorrect.

Since the CEC policy took place in September 1998, the Kuala Lumpur Composite Index (KLCI) shot up almost 300 percent in early year 2000[11]. Although the KLSE Composite Index closed at 657 points in late March 2001, 394 points higher than the 263 level, it sank on September 1, 1998. We do not deny that there are listed companies which market quote their shares at very low prices. There are sixty-eight companies listed on the KLSE- 39 on the main board and 29 on the second board which have been of less interest among investors (for instance, Amsteel Bhd, WTK, Muhibbah, Berjaya Land, Metroplex, Mycom, Olympia, Sriwani, Idris, Mbf Capital). All of these firms have a huge debt. However, looking at the big picture, 68 make up less than 10% of the 799 counters trading on the KLSE (The Star, 4 January 2001). Even rights issues and warrants are also no longer a safe bet. The dismal performance of the KLSE is not because of the CEC policy.

How about the Initial Public Offering (IPO)? Depression of the KLSE reflected the weak demand on IPO issued since 1998. In 2000, about 38 new IPO were issued and two-thirds of the companies which went public, ended their share prices below their IPO prices. In 1999 about 21 IPO suffered from undersubscription. The uncertainty and undersubscriptions of the IPO drove underwriters in dilemma, and they live 'dangerously'. Not only do they have to worry about mopping up undersubscribed shares, they also have to worry about the potential negative impact on their counters if they are saddled with the unsold shares. The central bank of Malaysia, Bank Negara Malaysia (BNM), imposed a limit on financial institutions for

[11] Before Morgan Stantely Capital International Indexes (MSCI) reinstated Malaysia in her indices in June 2000 circulated around 600-990 points from late 1998 to early 2001. MSCI has dropped Malaysia from the indexes in 1998 when it imposed capital controls.

share financing, i.e it can make up 20 percent of total loans. Currently bank lending for the share financing was only 7 percent. This is also not a reason that pushed down the KLSE.

However, there is an argument that the CEC policy is used to oppress the share prices, whereby the value of the company's assets will fall thereafter. Hence, the strong company will invest or increase its stake and finally control the company. Also there is no validity to this argument. After the country currency, ringgit (RM) attacked, the stock price fell sharply below 300 points (in 1997) before capital control was imposed. That was a right time for investors to buy shares but the condition of the market locally and regionally provided disincentive to invest. There is a "contagion effect" in stock bourse around the globe and this contagion is a global phenomena. In late 1997, the government had permitted companies to buy back their shares. This was mainly to push or stimulate investors to re-invest in the market. But not all companies listed on the KLSE bought back their shares. Furthermore, the companies which had bought and accumulated their shares were unable to manipulate share prices. As Table 2 show, there is no indication that companies which buy back shares manipulate their share prices, since the closing price on 29 March 2001 is much lower than the highest price purchased. Cash rich company, YTL groups spent more than RM340 million to buy back their shares but the closing price was much lower than the highest purchased price. The same goes to other firms as listed in the Table 2.

TABLE 2
Major Companies Buyback Shares Since 1999 to 29 March 2001 (selected)

Company	Shares Repurchased (Mil)	% of Share Capital	Highest Price Purchased (RM)	Lowest Price Purchased (RM)	Share Price on 29 Mar. 2001 (RM)
Ancom Bhd	0.99	n.a	1.60	1.41	1.49
Berjaya Sports Toto[b]	13.30	2.31[a]	9.70	4.28	3.56
CCM	3.36	0.90[a]	2.90	1.85	1.98
Choo Bee Metal Industries Bhd	2.05	n.a	1.33	1.28	1.14
Commerce Asset-Holding Bhd	7.85	n.a	7.25	7.05	6.50
Hap Seng Cons	20.21	3.13[a]	2.97	1.92	1.95
Jaya Tiasa Hlg	11.14	2.51[a]	4.44	2.84	2.58
MPI	10.96	5.22[a]	36.75	5.60	12.00
IOI Corp	10.83	1.27[a]	2.69	2.01	2.42
OSK Holdings Bhd	10.90	n.a	1.90	1.63	1.60
OYL Industries	4.72	3.30[a]	13.30	7.90	12.50
Paragon Union	1.75	0.88[a]	1.18	0.91	1.04
Phileo Allied	5.90	n.a	2.06	1.95	1.65
YTL Power Int.	47.68	2.74[a]	3.10	2.23	2.50
YTL Corp	52.02	3.52[a]	5.10	4.02	3.62
YTL Cement	5.45	3.68[a]	3.18	2.27	2.75
WTK Holdings	0.55	0.33[a]	4.90	4.52	4.54

Note: a: as at January 31, 2001, cited in Gabriel, A (2001), b: the company has a huge debt RM1.01 billion.
*Source: Gabriel, Anita (2001), "Shares Buybacks", **The Edge**, February 5, pp:54-55., The Edge, various issues.*

The other major and controversial factor and related to the performance of the KLSE is that of Malaysian shares under Clob International. The Malaysian government ceased operation of Clob on Malaysian shares on 15 September 1998. This move is in line with CEC's measures. It is a puzzle since Malaysia never recognized shares traded under Clob since 1990, so why was it that prior to the capital controls the Malaysian government did not prohibit or disallow such activities from taking place. There are about 112 counters of KLSE traded in Clob with investors about 172,417. It is estimated that shares trapped in Clob are about 11 billion units and its value is about RM18.8 billion (based on closing price as at February 25, 2000).

It is not quite clear, the release of shares under Clob could trigger or contribute to the downtrend of shares prices on the KLSE. On the day the government terminated Malaysian shares traded on Clob International, the KLCI sunk 389.08 points (15 September 1998). However, the price of shares at the KLSE shot up to 995.52 points on 15 February 2000, Most of the shares trapped in Clob are not from a heavyweight counter such as Tenaga Nasional Berhad, Telekom and Petronas Dagang, however Mayban's share in Clob is only 5% of the total shares. The companies with the top 10 largest percentage held by Clob investors are Westmont Land Bhd (63.35%), Idris Hydraulic Bhd (55.3%), Sateras Resources Bhd (54.73%), Construction and Supplies House Bhd (52.73%), Hexza Holdings Bhd (51.98%), MBf holding Bhd (44.6%), Sri Hartamas Bhd (43.1%), Golden Plus Bhd (40.98%), Asian Pac Holdings Bhd (38.83) and Mulpha International Bhd (53.37%). Most of these companies face a huge debt and most of their shares are selling at discount price.

The move to release shares from the Clob and migrate it to the KLSE involved politics and the matter was really in a mess. More than 6 companies or parties had offered proposals to resolve the Clob impasse. Among them were Effective Capital Sdn Bhd (ECSB), Bintang Melewar Sdn Bhd (BMSB), United Engineers (M) Bhd (UEM), Securities Investors Association of Singapore, Ms Tai Sim Yew, Collective Custodial Services Asia Pte Ltd amd Postmicro Sdn Bhd. The proposal by BMSB[12] (owned by the royal family state of Negri Sembilan) wa the one most favoured by Clob investors. But the KLSE favoured the proposal by ECSB[13], since Akhbar Khan, owner of ECSB was associated to Finance Minister, Tun Daim Zainuddin. Since KLSE had a word on the matter and the KLSE was under the jurisdiction of the Finance Ministry, ECSB won the tender on 26 May 2000. 93 percent of the total investors accepted ESCB's solution.. ECSB imposed 1.5% fees on shares based on the closing price on 15 February 2000. KLCI's composite index on 15 February 2000 was 995.52 points. However, shares prices fell since March 2000. This affected the welfare of Clob investors as they were loosing their money since share prices had fallen more than 60%. In February 1999, the government had liberalised the capital control with the creation of the exit levy system. Investments in portfolios before 15 February 1999 which had stayed less than one year would be charged with 30 percent levy, whereas for investment more than one year, the charges were according to the sliding scale as determined by the BNM. Since the share under Clob is more than one and half years, the Clob investors were not subjected to exit levy. It seems that the exit levy was restructured in such a way so that there was no need to charge the investors.

Selling Assets

With regards to the companies indebtedness, the government has liberalised foreign investment further in order to ease the companies debt. Foreigners now are allowed to hold more than 50 percent of equity in key industries such as telecommunications, hotel, shipping, forwarding and insurance companies (Table 4)[14]. For instance, Malaysia sold 30% (RM400 million) of Westport of Port Klang to Hutchison Whampoa owned by Li Ka-shing in

[12] The company charged a fee of 1 percent as at closing price on December 30, 1999 (KLCI index about 740 points. BMSB summited their proposal before December 31, 1999 (date of submission of proposal) but the proposal was dismissed by the KLSE on grounds of incomplete and does not meet with its procedure. BMSB requested to KLSE to circulate their offer to Clob investors but had been turn down. Implicitly KLSE urged investors to accept ECSB plan. ECSB is the only party that submitted a complete proposal that fully complied with KLSE rules and procedures as at 31 December 1999.

[13] In the first proposal, ECSB charged a fee of 2 % but in the modified plan they charged 1.5% fee based on the closing price on Feb 15, 2000. Share prices on 15 Feb 2000 were much higher than the settled price on 30 December 1999.

[14] In the manufacturing sector, foreigners are allowed to hold 100% equity interest for 5 years from the commencement of the projects, after which the company needs to restructure its equity to be held 49% by Malaysians including at least 30% Bumiputra. Foreign parties may be allowed to hold more than 30% equity interest in companies involved in projects encouraged by the government or provide direct benefit to the growth and development of the country.

2000. Maersk-Sealand, a Danish shipping firm bought 30% stake in Port of Tanjung Pelepas in Southern Johor. Lion Group sold 50% (RM200 million) of its equity in its corporate headquarters of 50 storeys (Menara Lion) to Citicorp, now known as Citibank Tower. Amsteel Corporation sold 31.57% interest in Malaysian British Assurance Bhd to Alliance AG, a German insurer company. British Telecom (BT) bought 33.3% (RM1.8 billion) stake in Maxis from Binariang, however BTele intends to sell the whole stake since its caught with a huge debt. Blue Circle bought 50% of Pan-Malaysian Cement Works (RM1.2 billion) from Associated Pan-Malaysian Cement and 65% of Kedah Cement Holdings (RM701.4 million) from Hicom Holdings and Bolton, and in January 2001 Lafarge SA of France bought Blue Circle for RM13.6 billion, indirectly the Lafarge controlled 52.3% in Malayan Cement Holdings Bhd (Malayan Cement control 77% of Kedah Cement Holdings Bhd). National Power (British) bought 20% (RM570 million) of Malakoff from Malaysian Resources Corporation Berhad (MRCB). Prudential (Britain) bought 21% (RM220.5 million) of Berjaya Prudential from Berjaya Capital, and Vivendi (France) bought 30% (RM91 million) of Intan Utilities from Berjaya Group. The Government of Singapore Investment Corporation (GIC) has bought a 25 percent stake in Sunway City for RM180 million, 48 percent in Sunway Pyramid mall for RM182 million and 70 percent stake in Menara Shahzan Insas for RM133 million (Toh, E, 2001). As shown in Table 2, since 1998 Malaysia disposed its assets to foreign firms whereby the disposals were soaring than prior to financial crisis. In 1995, Malaysians purchased firms abroad about RM1.12 billion, this increased to RM9.64 billion in 1996. In post currency attack, Malaysians sold their interest either in foreign or domestic firms (Table 4).

TABLE 3
Foreign Ownership Liberalisation

Sectors	Existing rule	Relaxation
Non-licensed manufacturing companies	30%	>30%*
Telecommunications	30%	61%**
Hotel operators	51%	51%***
Shipping agencies	49%	70%
Forwarding Agencies	30%	49%
Insurance companies	49%	51%
MSC status companies	-	100%

Notes: * in line witi MITI new relaxation on manufacturing companies
** the foreign equity should be reduced after 5 years
*** initially foreign interests are allowed to hold 100% equity interests for 5 years from the commencement of the project, after which the company needs to restructure its equity to be held 49% by Malaysians including at least 30% Bumiputra

Source: The Sun (August 1, 2000).

TABLE 4
Malaysia: Cross-border M&A Sales (RM million)

Year	*1988*	*1989*	*1990*	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*
As seller	20	701	86	128	46	518	443	98	768	651	1096	1101
As purchaser	-	27	144	149	148	774	812	1122	9635	894	1059	1292

Source: The Edge (2000), FDI inflows hit record high in region, October 9, pp: 72.

However, in certain cases, the government had rejected the proposal of selling local assets to foreigners. The classic example is in the case of Singapore Telecommunication (SingTel) which intended to invest RM2.4 billion in Time Engineering (TE) and two of its subsidiaries, Time dotCom and Time Online. But the plan was disapproved by the government on grounds for national security since the TE is the sole owner of fibre optic cables in the country. The second case, unwillingness of the government to sell MAS shares (which was owned by Tan Sri Tajuddin Ramli) to a few interested international airlines.

Corporate Debt Restructuring Committee (CDRC)

CDRC was set up in 1998 as a non-statutory body to assist companies in debt restructuring. Table 5 (and 6) show debt restructuring cases supervised by CDRC. It received 75 applications for restructuring in 2000. It resolved 33 cases worth RM25.3 billion and 12 cases worth RM16 billion remain outstanding. The CDRC has helped 33 companies to restructure debts totaling RM25.48 billion. Out of the 33 companies, 20 are in investment holding with debts of RM19.77 billion, seven in property and construction (RM3.62 billion debts), five in finance and services (RM1.66 billion) and one in manufacturing (RM425 million). Sixteen of them are listed on the main board of the Kuala Lumpur Stock Exchange and nine are on the second board, while eight are private companies (The Sun, 26 February 2001). About RM7.94 billion or 32.35% of the 33 companies corporate debts were settled in "cash payments", RM4.6 billion or 16.97% in bonds, and RM3.99 billion of 16.27% in notes.

Most of the debt restructuring cases either under CDRC or without CDRC, converted loans into bonds or right issues (new shares) or warrants (debt-equity swap). Debt securities and new shares from these restructuring exercises increased or expanded the capital market (Table 7). However this is not fresh capital. Implicitly, the public has been blind about the amount of funds which have been raised in the capital market. On the other hand, in the banks balance sheet, assets (excluding fresh assets) are not increased, and remain the same. However, the NPLs have been reduced because part of the NPL has turned to perfoming loans.

The company which issues a bond now needs an assurance. The government formed the National Financial Guarantee Insurer (NFGI) (The Sun, January 12, 2001) in January 2001 to ensure bonds which have been issued will not become junk bond. The paid-up capital of NFGI is RM500 million[15]. The shareholder of the NFGI is the Ministry of Finance (Inc) 30%, Amanah Capital 20%, Malaysian National Reinsurance Bhd 5 % and the remaining 45% is likely to be held by selected insurance companies and financial institutions 5% each). The NFGI acts as a safeguard to firms issuing bonds.

TABLE 5

CDRC: Company Debt Restructuring Cases (RM mil)

Subject	1998	1999	2000
Application received (accumulative)	(36)	(66)	(75)
Total Debts	11,028.15	24,624.62	11,556.98
Withdrawn/ Rejected Cases	-	3,504.35 (15)	4,855.28 (6)
Transferred to Danaharta	-	2,764.70 (8)	1,813.54 (1)
Completed Cases	344.50 (2)	11,089.28 (11)	13,698.63 (20)
Cases Outstanding	10,683.65 (34)	16,651.13 (28)	12,093.40 (12)

Note: figure in parenthesis is the number of applications/cases

Source: CDRC website.

Pengurusan Danaharta Nasional Berhad (Danaharta)

Established in 1998 to remove non-performing loans, rehabilitate the banking and corporate sector, and assist in debt restructuring. There are 86 companies from 56 groups of companies under the special administration of Danaharta. In particular, those companies are stockbroking (11), investment (10), properties/developers (14), manufacturers (24), trading (3), services (2), group/holding-broad business (2), retailers/wholesalers (1) and non-specified (6).

[15] The NFGI aim to enhance bond rating and promote the growth of private debt securities and the bond market.

In the year 2000 Danaharta received 2,835 accounts relating to 2,507 borrowers with a total gross value of RM47.49 billion (NPL) in which RM38.17 billion was from the banking system (representing 42.2% of total NPLs in the banking system) and RM8.60 billion from non-banking and offshore institutions. Of this total, Danaharta is managing RM27.1 billion of NPLs in respect of the Sime Bank Group (RM15.7 billion) and the Bank Bumiputra Malaysia Berhad (BBMB) Group (RM11.4 billion).

In return for the NPLs, Danaharta had issued bonds amounting to RM11.14 billion (15 bonds from 20 November 1998 to 31 March 2000). The maturity date of bonds are 2003 (2), 2004 (10) and 2005 (3). The bonds are guaranteed by the government. Danaharta will issue another RM4 billion bond (total bond issued will be RM15 billion). Danaharta bonds are zero-coupon bonds, therefore interest payments do not need to be made to the financial institutions which receive them.

TABLE 6

CDRC: DEBT RESTRUCTURING CASE BY COMPANY

Company	Debt	Proposal
Setegap Berhad	RM95.5 mil (creditors-21 banks)	Not available
Trans Capital Holding Berhad	RM185.6 mil	Right issue – 79,288,500 new shares
Chase Perdana Berhad (MRCB)	RM279.9 mil	Right issue- 147,366,501 new ordinary shares
Sistem Televisyen Bhd (TV3) (MRCB)	RM500 million	Not available
Mycom Group (including Olympia Industries Bhd, Mycom Capital Ltd)	RM1.5 bil (Foreign loan – US$47 mil)	Right issue- 116,285,131 new ordinary shares
Renong	RM28 billion	Not available
Park May Berhad (Renong, 51%)	RM146 mil	20% of outstanding loan converted into right issue and 80% of the loan converted into Redeemable Convertible Bonds.
Putra (owned by Renong 100%)	RM2 billion	Sold to government
Lien Hoe Corporation Berhad	RM212.062 mil	40% of the debt converted into Redeemable Secured Bonds and issued Right issue 254.252 million
Nam Fatt	RM312.3 mil	Loan converted into Redeemable Secured Bonds
Changai Corporation Berhad and Pembangunan Bandar Mutiara Sdn. Bhd	RM115 mil.	RM3.26 mil of the loan converted into right issue
Tongkah Holdings Berhad	RM1.189 bil	Issued a bond RM462.699 mil Issued Irredeemable convertible unsecured loan stocks, RM161.996 mil
Gadek Berhad (DRB-Hicom)	RM750 mil (Creditor-CIMB)	Not available
Naluri Bhd (Tan Sri Tajuddin Ramli)	RM950.1 mil (of which RM888.2 mil is from Naluri and the rest from its subsidiaries)	Sold entire stake in Malaysia Airlines System (MAS) 29.09% to the Malaysian government, for RM1.79 bil cash.
Lion Group (including Amsteel Corporation, Lion Corporation, Posim) (Datuk William Cheng)	RM10 bil	Not available
Idris Hydraulic (M) Bhd. (Datuk Annuar Senawi)	RM782 million	Disposed Sagisan Timber concession in sabah for RM150 millon. Disposed stake in Prime Utilities Bhd for RM150 million

Source: CDRC press release, newspapers.

Danaharta has recovered RM12.03 billion from the non-performing loan portfolio of RM47.49 billion, while another RM11.77 billion is expected to be recovered by the year 2001. This leaves another RM12 billion remaining unrealised with another RM12.40 billion being "unrestructured". Half of the amount recovered was in hard cash amounting to RM6.4 billion, while the rest are in the form of rehabilitated loans, securities and properties. With the RM11.77 billion expected to be recouped by year 2001, this would bring its total realisable recovery of bad loans from the financial system to RM23.8 billion, or two-thirds of the RM35.83 billion of the loans outstanding as at December 31,2000.

Most of the NPLs are related to the property sector (29.9%), purchase of shares (16.9%) followed by financing, insurance and business services (15.0%), manufacturing 13.1% etc. Most of the NPLs are in the form of restructured loans (67.1%), 21.2% more than 1 year maturity and 11.7% below one year. Major borrowers are private limited companies 59%; public companies 15%; non-resident 19% and resident 7%. In respect to collateral, property makes up about 47%, shares 20% and unsecured portfolios 37%. 1,536 properties are valued at RM17 billion. Danaharta sold 325 or 72 per cent of the 449 properties (excluding hotel and leisure properties) with a total indicative value of RM985.93 million through four property tenders. This is about 5% of its total gross NPL property portfolio. Total outstanding unsold properties value at RM16 billion. RM20.21 billion of the gross value of NPLs in Danaharta's portfolio are secured by properties, Since Danaharta has sold about 5.0 percent of its total gross NPL property portfolio, how much time will it need to get rid of the other RM16 billion. Prices of the properties being tendered are still unattractive. In some cases, the properties belong to uncooperative borrowers-meaning Danaharta has no physical control of the properties.

TABLE 7

Malaysia: Funds Raised in the Capital Market (RMbil)

Sector	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
PUBLIC SECTOR										
MGS	*3.5*	*3.8*	*1.6*	*2.2*	*2.0*	*6.0*	*3.0*	*15.0*	*10.0*	*16.4*
Total New Issues of Debt Securities	*3.8*	*4.3*	*3.7*	*5.5*	*6.0*	*6.0*	*3.8*	*17.7*	*15.0*	*20.0*
Net Funds Raised By Public Sector	**3.2**	**1.5**	**1.2**	**1.8**	**-0.04**	**1.3**	**-1.4**	**9.8**	**6.3**	**13.7**
PRIVATE SECTOR										
Shares/Warrants										
Initial Public Offering	*1.7*	*5.4*	*0.9*	*3.0*	*4.2*	*4.1*	*4.8*	*0.7*	*1.0*	*1.0*
Rights Issues	*2.2*	*3.4*	*1.2*	*3.4*	*5.2*	*5.3*	*8.5*	*0.7*	*4.3*	*4.0*
Private Placement/ Restricted Offer-for- sale	-	*0.03*	*0.7*	*0.8*	*1.1*	*4.6*	*3.2*	*0.3*	*0.5*	*0.9*
Special Issues	*0.5*	*0.3*	*0.7*	*1.2*	*0.9*	*2.0*	*1.8*	*0.06*	*0.2*	*0.1*
New Issues of Shares/Warrants	4.4	9.2	3.4	8.5	11.4	15.9	18.4	1.8	6.1	6.0
Debt Securities										
Straight Bonds	*0.6*	*1.2*	*2.1*	*1.0*	*3.9*	*2.7*	*4.2*	*10.2*	*9.6*	*12.9*
Bonds with Warrant	*0.2*	*0.5*	*1.1*	*2.9*	*3.8*	*5.6*	*3.0*	*0.2*	*0.6*	-
Convertible Bonds	*1.1*	*0.6*	*0.2*	*1.3*	*0.9*	*1.8*	*2.0*	*0.1*	*1.3*	*1.7*
Islamic Bonds	*0.4*	*0.03*	-	*0.3*	*0.8*	*2.4*	*5.2*	*0.3*	*1.7*	*7.7*
Cagamas Bonds	-	*2.1*	*1.7*	*4.8*	*3.0*	*4.7*	*5.2*	*3.3*	*4.4*	*8.5*
New Issues of Debt Securities	2.1	4.4	5.0	10.3	12.2	17.0	19.6	14.2	17.6	30.8
Net Funds Raised By The Private Sector	**6.3**	**12.5**	**7.1**	**17.5**	**19.8**	**30.5**	**35.0**	**8.0**	**10.9**	**26.6**
Net Funds raised in the Capital Market	**9.4**	**14.0**	**8.3**	**19.3**	**19.7**	**31.8**	**33.5**	**17.8**	**17.2**	**40.2**

Source: Bank Negara Malaysia, Monthly Bulletin.

Under Pengurusan Danaharta Nasional Berhad (Danaharta), Bill 2000 (amendment) which was passed by Parliament on 17 July 2000, Danaharta has total rights as a charge over property collateral. It can replace and appoint administrators to companies so long as the company has given a security of any amount, even an insignificant amount, and even when only 2% of the company's shares are assigned to the corporation, or even if the company is still healthy and does not want external interference. In addition, the amendment allows Danaharta to sell off any asset given to it as security even without the owner's consent. Its decisions are final and cannot be challenged in a court of law. It does not have to explain or account for its actions. No injunctions can also be taken against it and any injuction already taken will become void. Any civil action for damages appears futile under the amendments. It is not difficult to understand why Danaharta and its officials need to protect themselves from any blame (Gratias, AD, 2000). Why the Danaharta is not exercise it power? It seem there is a "invisible hand" behind certain action of Danaharta. In the case disposal of property, Danaharta is less transparent in terms disclosure of the owner and value of property. Market respone of the property tender offer by Danaharta is less impressive since most the property priced above the current market rate.

Bail-out

In general most companies which have a political link have been bailed out if they fail in business. Some of companies which have been bailed out are involved in construction, transportation, heavy industry and public utilities. Prior to the implementation of capital controls there were a few bail-out cases. The first case was that of Bakun Dam (costs about RM20 billion) which was run by Ekran Bhd in 1993 (controlled by Tan Sri Ting Pek Khiing, close to ruling government). Ekran Bhd sub-contracted RM13.6 billion enginering and construction to a Swedish-Brazilan consortium comprising Asea Brown Boveri and Companhia Brasileira de Projectos Obras. Disputes between the consortium and Ekran Bhd in 1997 emerged, and in late 1997 Ekran Bhd terminated the contract. In November 1997, the government took over the project (Tenaga Nasional Berhad) and paid nearly RM1 billion as compensation to Ekran Bhd. The Bakun Dam project has been revived and resumed in a smaller scale in contrast to the earlier proposal with an estimate cost of RM13.5 billion. Eventhough Ekran Bhd had failed in the dam project, it has not stop them from receiving new projects from the government; the latest project that Ekran Bhd has been awarded is the RM120 million naval base project in Sabah.

A debt-laden RM1.6 billion shipping firm, Konsortium Perkapalan Berhad (KPB) which was owned 72% by Mirzan Mahathir has been saved by the state oil company through Malaysian International Shipping Companies (MISC) state-control shipping firm. Petronas has a stake of 50% in MISC. Petronas comes directly under the Prime Minister's Department. The rescue package involved almost RM2 billion. In the deal Petronas acquired the entire stake of shipping assets of KPB. Petronas paid in cash, and Mirzan was free from the debt[16].

The government bought back Indah Water Konsortium (IWK) from Prime Utilities Berhad (PUB) (owned by Berjaya Group) in June 2000. The company incurred a loss of about RM700 million despite receiving soft loans and grants of about RM925 million from the government. For the takeover, the Ministry of Finance (MOF) paid RM192.54 million to PUB. IWK, a national sewerage company had been privatised by PUB in 1994 without a tender bet.

In early 2001, the government took over the light rail transit (LRT) operations in Kuala Lumpur which were handled by Sistem Transit Aliran Ringan Sdn Bhd (STAR) and Projek Usahasama Transit Aliran Ringan Automatik Sdn Bhd (Putra). The government issued RM6 billion of 5 to 15 year bonds with an interest rate of 5.8% to 7.2% for the purpose. STAR is owned by a local consortium owned by the Employees Provident Fund (EPF), national pilgrim fund Lembaga Urusan Tabung Haji (LUTH), armed forces fund Lembaga Tabung Angkatan Tentera and civil servant pension fund Kumpulan Wang Amanah Pencen (KWAP),

[16] Prime Minister Mahathir Mohamed and Mirzan denied received money from Petronas and dismissed the matter as a bail-out (Haggard, S, 2000:170).

Shell Malaysia and Sabah Retirement Fund. Putra is 100% owned by Renong Berhad[17]. The immediate problem of Star and Putra is their heavy debt burden. Both of the operators have been unable to meet payments on interest on loans taken from Commerce International Merchant Bankers Bhd and RHB Bank Bhd. Bail-out by the government will enable the owners to repay the loans.. If the government had not bailed out both companies, the country's bad loans would be increased to 13.9 percent of total loans of RM411 billion (SBT, 21 Feb 2001). However, the operation of the LRT was leased to the same companies. Giving back the operations to the same management may not guarantee they will do it better the second time around. To allow the LRT to be operated by the same companies that have suffered losses even since they started is a moral hazard. It has been argued that the operators know the business better than others.

KL Monorail System Sdn Bhd has also received helped from the government. Aside from the RM300 million loan provided by the government to the concessionare, the government also extended the concession from a 30 years (original concession) period to 40 years for the KL Monorail System Sdn Bhd (KL Monorail). The cost of the project was RM2.1 billion but reduced to RM1.7 billion as a result of utilising Malaysian technology for the train. The project was revived in June 1999 after the government extended RM300 million (infrastructure loan RM610 million and shareholders' equity RM260 million). KL Monorail formely knowns as KL PRT Sdn Bhd is owned by Berjaya Group Bhd[18].

Express rail Link Sdn Bhd (ERL) which operates the Kuala Lumpur city-KL International Airport was launched in 1995 but shelved during the Asian financial crises. It was re-started in 1998 and is scheduled for completion in April 2002. Total investment is about RM2.5 billion in which the government has funded RM1 billion, while RM500 million has been raised from the shareholders and the rest of the money has been borrowed. The major shareholders are the national pilgrimage fund, Lembaga Urusan Tabung Haji (LUTH), subsidiary TH Technologies Sdn Bhd and YTL Corp Bhd[19]. LUTH holds a 60% stake and YTL the remaining 40%.

The Malaysian Airline System (MAS) case triggered public concern on how the public fund is used to bail-out a person well connected to the government. MAS suffered RM1 billion losses in the last two years and incurred debts of RM9.4 billion. Finance Minister Tun Daim Zainuddin[20] defended the government's decision to buy back 20.09% of MAS shares from Tan Sri Tajudin Ramli's Naluri Berhad at RM8.00 a share of about RM1.79 billion in cash[21].

[17] Keretapi Tanah Melayu (KTM) will be privatised. The privatisation will be handled by a consortium led by Marak Unggul (owned by Renong Bhd) with a 59% share, DRB-Hicom 25%, Bolton Properties 20% and Jasa Meta 5%.

[18] Road Builder Holdings Bhd (RBH) plan to secure the New Pantai Expressway (NPE) project from Berjaya Land. The cost of the project is RM983 million. The highway is scheduled to be completed by year 2002, but to date only 15% of the highway is complete. The highway is a 30 year toll concession. The project started in 1996 but stalled in 1998 due to the economic crisis. NPE had also received a soft loan of RM250 million from the government.

[19] Another shareholder of ERL was Abrar Corporation Bhd, but it sold the entire stake of 20% to LUTH to reduce their group debt which was more than RM200 million.

[20] Tun Daim said the purchase should not be seen as a bailout. The sale price is what Tajudin paid when he first bought MAS in 1994. Tun Daim also said the government was willing to pay RM8 because the company's real value was much higher than the market price (The Sun, 23 December 2000). Tun Daim also indicated that the government will retain the golden share but did not say if the government is willing to dilute its veto power. Foreign airlines such Qantas Airways, SwissAir, KLM Royal Dutch Airlines and Luftansa are interested to buy MAS, but since they will not be given a veto status, those are airlines not interested.

[21] Brunei Investment Agency disposed of 70 million shares in the Malaysian Airline System Bhd on December 1, 2000 at RM4 a share before the government purchased MAS shares from Naluri. The state corporation had bought MAS shares, thereafter. The Employees Provident Fund (EPF), the second largest shareholder in MAS after Naluri Bhd, increased its stake in the airline. EPF currently owns 12.1% of MAS from 6.41% as at June 1998. The fund bought about 5.3 million MAS shares on the open market in October 2000, and spent about RM16.2 million. The purchase price ranging RM3.04-RM3.12 (BT, 9 November 2000). Bank Simpanan Nasional Bhd (National Saving Bank-BSN) has accumulated 17.14 million MAS shares representing a 2.15 percent stake

On the purchase date, MAS share was trading at about RM3.62 on the KLSE. The purchase of 29.09 percent of MAS from Tan Sri Tajuddin Ramli by the government to help him repay his company's debt, telecoms-based Technology Resources Industries (TRI). TRI has total group borrowings of over RM3.7 billion. Naluri (formerly known as Malaysian Helicopter Services Bhd) which controlled MAS is a subsidiary of TRI. Naluri gains from the sale of MAS shares about RM865 million after paid off its debt. The gains may be used to reduce the TRI debt.

Debt-ridden Malaysian auto group DRB-Hicom[22] (this company is also politically connected to UMNO) has also received state funds to ease the burden of debt. The group has debts totalling RM5.06 billion[23]. Petronas has bought 25.8 percent stake in Perusahan Otomobil Nasional Bhd (Proton) from DRB-Hicom. The purchase cost RM981.02 million (140.15 million shares). DRB-Hicom is also in negotiation with LUTH to sell 85% stake in the second national air carrier Air Asia Sdn Bhd to LUTH. Air Asia losing money since it began operations in 1996. Eventhough the LUTH has used the air carrier for pilgrimage purposes since five years ago, financially there is no concrete justification or reason why the fund should buy the air carrier. It is learnt that DRB-Hicom had also approached the Sarawak Economic Development Corporation, Angsana Vacation Sdn Bhd, and Lufthansa Air for the matter. DRB-Hicom had planned to sell Hicom to Kedah State Economic Development Corporation, but Kedah's state government has abandoned the deal.

Another case of an expensive bail-out is the debt-laden and loss-making National Steel Corporation (NSC) in Philippines which is owned by Tan Sri Halim Saad (TSHS) through his company, Hottick Investment Ltd based in Hong Kong. Hottick invested more than RM4 billion in the loss-making steel company, NSC in 1997. TSHS owns 82.5% in NSC. Prior to TSHS's involvement in the NSC fiasco, the NSC was owned by Wing Teck Holdings (WTK) which was associated to politician Joseph Chong of the ruling government. The investment was made by borrowing money from Malaysian banks, i.e. Malayan Banking Berhad and RHB Bank each extended RM925 million while Bank Bumiputra Malaysia Berhad (BBMB) and Commerce Asset-Holding Berhad lent RM658 million and RM578 millon respectively. The loans were given without a collateral (Lopez,L, 1999). Besides the fact that NSC owns Malaysian bank, it also owns about 14 billion peso (RM1.4 billion) from Philippines banks. Danaharta rescued TSHA by seizing NSC shares from Hottick of about RM3 billion. Since both companies are not in Malaysia's jurisdiction, it is impossible for Danaharta to recover the loans made by the Malaysian banks. In other words, the shares seized are worthless, and it seem that the loans from Malaysian may have been write off. Loans from the banks taken by the Danaharta directly rescued TSHS and indirectly saved WTK. Since NSC is a loss-making firm and has a huge debt, and since TSHS is himself saddled with a huge debt (will be elaborated below) why he so eager to invest in the firm?. Malaysian government to save whom? Why not let TSHS go bankrupt? Is it to expensive for the government to let him down?. It seems that the Malaysian government is bailing-out a person or company at the expense or welfare of her people.

Corporate Restructuring Cases

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in MAS. BSN had spent about RM66 million for the stake. Kumpulan Wang Amanah Pencen (KWAP) has increased its equity in MAS by 72.12 million shares to 154.29 million shares.

[22] Diversified Resources Berhad (DRB), the parent of Hicom merged with Hicom, Gadek Berhad and Gadek Capital in a share-swap and formed DRB-Hicom in 2000.

[23] As in the case of Ekran Bhd, Renong and UEM, despite DRB-Hicom faced a huge debt, the government still awarded it another national project. Recently, DRB-Hicom was awarded a project of infrastructure work of electrified double tracks between Rawang-Ipoh; its learnt that the company also tried to secure a contract from the government to build roads and the Kajang-Seremban Highway interchange and the company was named as one of the contractors in the Bakun Dam project.

In this section we offer two cases of companies[24] which have a huge debt that are on going debt restructuring exercises and are closely connected to United Malay National Organisation (UMNO). The companies are conglomerate Renong Berhad (Renong) and Malaysian Resources Corporation Berhad (MRCB). The corporate and debt restructuring of Renong is very much more complicated than other firms including MRCB. Forms of debt restructure involve debt-equity swap, conversion of debt (bonds) into new bonds with new maturity date and coupon rate, disposal of part of the company's asset to other companies within the group (swap deal) or sell to other companies closely related to the government or sell to the government directly. In the process of restructuring, top management of the companies remain the same persons except in the MRCB case[25]. If the government bails out those companies and firms associated to them, it either does that through the government coffer (tax payers money) or by instructing public fund institutions particularly, EPF[26], KWAP, LUTH or Petronas to buy the companies..

Renong and UEM

Renong Berhad (Renong) and United Engineers Malaysia Berhad (UEM), which are controlled by Tan Sri Halim Saad (TSHS), are saddled with huge debts. Renong is indebted about RM28 billion which represents 5% of all loans in the banking system, UEM, the country's biggest construction and road company has RM17.3 billion in debt. UEM holds around 32.6% in Renong and Renong owns a 38.5% stake in UEM.

Renong and UEM immediate problem is solving a mounted debt. Except for the group banking and cement operations, almost all of its businesses which include hotels, telecommunications, consultancy work, contruction and transportation are losing money. Most of the group debt, is settled by its cash cow subsidiary, Projek Lebuhraya Utara Selatan (Plus). UEM has already used Plus to wipe off Renong's short-term debts of RM5.3 billion[27] (the government has also extended the Plus concession to 12 more years). In return, Renong has promised to sell its assets over the next seven years to repay Plus. Under the proposed deal announced, UEM will take over RM5.4 billion worth of assets of Renong's (The Star, 19 January 2001)[28]. The assets include the entire equity of Fleet Group Sdn Bhd, which UEM will buy for RM2.9bil upon completion of Fleet's revamp. Renong said the price for Fleet was arrived at after taking into consideration the latter's assets, which include shares and warrants in Time Engineering Bhd (47%), Faber Group Bhd (60%), Commerce Asset-Holding Bhd (12%), and Camerlin Group Bhd (3%). The other Renong assets to be acquired are its 50.1% stake in Park May for RM16 million, a 38.6% stake in Crest Petroleum Bhd for RM74.52million, and 80% stake in Amra Resources Sdn Bhd (the holding company for Prolink Development Sdn Bhd) for RM1.29billion. Renong's wholly-owned subsidiary Hatibudi Nominees (Tempatan) Sdn Bhd also sold to UEM its 1.7% equity interest in Time Engineering Bhd for RM47.43 million. In reducing the debt UEM has

[24] Both companies received many government privatisation projects, mainly Renong or UEM. Besides Renong and UEM, the government privatisation project is also extended to other firms that are connected to the ruling government, for instance, DRB-Hicom, YTL, Berjaya, company associated to Tan Sri Wan Azmi, Tan Sri Ting Phek King.

[25] Eventhough top management has changed in MRCB, still the new persons engaged with UMNO ally to Prime Minister group.

[26] Employees Provident Fund (EPF) is a major holder of the government treasury bills. The government to date had issued the bills valued RM89.31 billion, and EPF hold about RM60.4 billion, followed by banks about RM13.1 billion, insurance companies about RM6.8 billion and Socso RM2.2 billion.

[27] In March 1999 Renong and the CDRC proposed an RM8.41 billion bond issue to repay debts of Renong and its associate UEM. The deal requires Renong to raise RM8.75 billion to repay Plus by 2006, when the bonds are mature. However, the amount of bonds was reduced to RM5.4 billion after Renong sold monorail operator Putra to the government.

[28] In early April 2001, Renong has postponed the deal since it has not yet received approval from the Securities Commission (SC).

sold Stadium Merdeka, Stadium Negara and Changkat Pavillion to Permodalan Nasional Berhad (PNB)[29]. The cost of acquisition was expected to be more than RM800 million.

A toll road concessionaire Expressway Lingkaran Tengah Sdn Bhd (Elite)(RM1.34 billion), which manages a 36 mile road linking Kuala Lumpur to Kuala Lumpur International Airports (KLIA) and is owned by UEM and is also stuck with a a serious cash flow problems and its debt amounts RM1.1 bilion. In August 1999, Elite defaulted on loans of RM940 million and was unable to pay RM21.3 million in interest (Barrock, L, 2001b). Elite announced issuing 13 years RM1.86 billion Islamic bonds to repay the debt. What is actually happening is that Elite is just transferring its debt from one creditor to another creditor. In the initial contract, Elite planned to operate and collect toll on its highway till 2018, but due to the debt matter the concession has been extended to 2030. The longer concession period means that the company has the option to seek refinancing at some point. The toll collection depend on performance of the KLIA. The volume of traffic to and from KLIA makes up only 27 per cent of total traffic volume on Elite and it is a questionable ability of Elite to redeem the bond .

Time Enginerring Bhd (TE), another firm under Renong is also struggling to reduce the company's debt of about RM5 billion. Renong holds a 46.8% stake in TE while TE owns a 21% stake in Renong. TSHS took an unlisted TE subsidiary, Time Telecommunications Holdings, renamed it Time dotCom (TDC) and transfered it to its parent company. In order to reduce the groups debt TSHS plans to list TDC on KLSE's, main board.Time dotCom had made an offer of 575 million shares at RM3.30 a piece to the Malaysian public and institutions. The IPO will make RM1.9 billion. Before the listing, TE sold a 30% stake (RM2.1 billion) in Time dotCom to Khazanah Nasional Bhd (KNB). The IPO and investment from KNB will raise RM4.875 billion[30] for TE and with this amount of money Renong hope to slash its RM24 billion to RM20 billion (excluding Putra case). Unfortunately, the IPO was unsuccessful. TDC IPO was 75% undersubscribed and the company's stock plunged 26% on its first day of trading on Monday, 12 March 2001. On Thursday, 15 March 2001, TDC stock closed at RM2.17, 34% below its RM3.30 IPO price. The unsubscribed shares affect the underwiter led by CIMB Merchant Bankers (controlled by Renong), and this will drive the banks and its associates in debt burden if the excess of the TDC shares are not mopped up from the market. The state agencies, KWAP, EPF and Danaharta have intervened in the market and acquired a combined 17.2% (433.2 million million shares, about RM1.43 billion) equity stake in TDC. Even KWAP was assumed as a sub-underwiter, basically what has happened is a bail-out[31]. The share is now valued at RM967 million, a paper loss of about RM463 million to the entities (at RM2.23 per share, a closing price as on 27 March 2001) (Utusan Konsumer, 2001). A total of about 47.2% of TDC is now owned by the government entities including KNB, while Renong acquired 46% of TDC.

In 1997 parties linked to TSHS sold some RM2.3 million (32.2%) of Renong shares to UEM in an off-market transaction. This deal raised the anger of UEM investors and finally in 1998 TSHS agreed to buyback the shares at RM3.24 per share and this cost him about RM3.2 billion. TSHS stressed he will honour the put option deal, but until now he is still delaying the purchase. As been reported that he has paid RM100 million so far. Is TSHS able to pay for the repurchase or will he be bailed out again or he may request for a waiver from the industry regulator. Industry observers say giving TSHS a waiver could set a bad precedent, especially since this purchase may be followed with a much bigger acquisition of the UEM block (BT, 20 October 2000).The wider implications of the TSHS move has fueled speculation that the deal could be part of a bigger exercise and might even lead to Renong being taken privately.

[29] The government has granted the land (13.08 ha) to UEM in exchange of the development of the RM800 million National Sports Complex in Bukit Jalil in 1994.
[30] Including sale of 21.56% (RM875 million) in Renong to TSHS.
[31] Some estimate that 95% of TDC IPO's exercise was sub-underwritten (Barrock,L 2001c)

MRCB

Malaysia Resources Corporation Bhd (MRCB), a power and media group had borrowed about RM1.5 billion. About 30% of its debt which is denominated in US dollars, was supposed to be repaid in two tranches in July 1999 and December 2000. The repayments were postponed several times.

MRCB fell into debt troubles when it acquired RM1.5 billion for a 27% stake in Rashid Hussain Bhd (RHB), which controls the country's third-largest banking group RHB Capital Bhd, by borrowing US$250 million in the offshore market. The purchase was signed in 1997. MRCB plunged into losses in 1998 due to the RHB loss of RM938 million from its banking units. RHB incurred additional debt when its Vision City real estate project in Kuala Lumpur stalled during the economic crisis. Also stalled was its KL Sentral project, a RM1.3 billion rail transportation hub with hotels, condominiums and offices (Yong, 2001). MRCB is expected to refinance its debt of RM516 million into long-term loans. The company has also signed RM920 million Islamic bond financing for the ongoing work in KL Sentral and for the next phase of its integrated property and city rail link project in Kuala Lumpur which is to be undertaken by it subsidiary Kuala Lumpur Sentral Sdn Bhd. The refinancing gives MRCB time to work out measures to sell some of its media and property assets in order to raise cash to repay its creditors.

MRCB has disposed its property and construction assets to industrial gas producer, Sitt Tatt Bhd and real estate group Chase Perdana. The deal included swapping fixed assets for marketable securities, without losing control of the assets. Sitt Tatt and Chase Perdana both listed companies and are controlled by MRCB. MRCB plans to sell an office tower that houses its corporate office, and a shopping mall outside of Kuala Lumpur for RM 275 million (Yong, 2001). In July 2000, it sold its 22.7% stake in Malakoff Bhd, the country's second power producer, to Malaysian Mining Corporation for RM744 million cash. MRCB also plan to sell its Port Dickson Power. MRCB has also received RM700 million for the sale of two hotels to LUTH. The group has managed to reduce its debts from RM1.51 billion in 1999 to RM516 million by selling non-care assets (The Sun, 28 February 2001).

MRCB's newspaper arm, New Straits Times Press (NSTP) is also in debt of RM1.35 billion. The NSTP short-term loans (borrowing) stand at RM1.07 billion with some RM800 million in unsecured loans. The company will be refinancing its loans and rationalising its assets in a bid to improve its financial position. The decision on debt restructuring has not been finalised yet. However, the NSTP group has sold it subsidiary Berita Publishing to Kadir Jasin, a former editor of News Straits Times.

Sistem Televisyen (M) Bhd (TV3) (MRCB ownes about 49.7%) accumulated debts of almost RM600 million, including foreign borrowings. TV3 has negative shareholders funds of RM337.5 million as at August 31, 2000. It has to undertake a restructuirng exercise, otherwise it will be delisted by the KLSE based on new regulations. To strenghten the group's financial position, MRCB has sold 21.1 % to Simpletech Sdn controlled by Mohd Ibrahim Mohd Nor, a former managing director of Padi Beras Nasional Berhad. TV3's restructuring proposal includes a capital reduction exercise, a debt-to-equity swap and RM125 million bond and warrant issue to cover an aggregate debt of RM714.62 million.

Bank Consolidation

The economic downturn resulted in the banking sector recording a pre-tax loss of RM2.3 billion in 1998 as compared to pre-tax profit of RM7.7 billion in 1997. The banking sectors large pre-tax loss was also due to large losses recorded by two commercial banks, Bank Bumiputra Malaysian Berhad and Sime Bank Group and one finance company Malaysian

Borneo Finance (MBf). This was mainly due to huge loan loss provisions made on rising non-performing loans (NPLs), as more and more companies found it difficult to service their loan obligations. The actual NPLs (combination of 3-month and 6-month NPL classification) of financial institutions rose by RM34.2 billion or 8.3% of total loans in 1998, while on a 3-month classification basis, NPLs grew by RM48.8 billion. NPL ratio rose from 4.7% in 1997 to 13.2% in 1998. Gross NPLs arising out of loans to the broad property sector accounted for 35% of total NPLs in 1998 while the NPL ratio for the purchase of securities rose from 6.5% in 1997 to 23.2% in 1998. Following the injection of capital by Danamodal Nasional Bhd[32] (Danamodal), the decline in total loans and removal of NPLs by Danaharta, the risk-weighted capital of the sector rose to 11.8% in 1998.

Concerned with the non-removal or servicing of the NPL of RM34 billion and stuck with the short-term debt of about RM30 billion, the government implemented the consolidation of banking institutions. Initially, the plan was to form 6 groups of banks, but was then changed to 10 groups banks of after a wide protest from Chinese bankers[33]. Other reasons for the reverse decision are; unhappiness over the selection of anchor banks[34], dissatisfaction over the terms and conditions imposed by anchor banks and political reasons (unhappiness of the Chinese business community). The merger program should have been completed by December 2000. However, the deadline of the merger proposal has been extended since some parties have not reached an agreement between the anchor bank and their associate, for instance, in the case of Utama Bank, MBf and PhileoAllied Bank.

Eventhough the merger or banking consolidation programme is said to be market driven, it is actually an enforcement upon the 54 financial institutions to merge (to date 50 of the 54 banking institution have been consolidated into 10 banking groups. Equivalent to 94 per cent of the total assets of the domestic banking sector). The government intended to reduce the number of banks and create a strong bank in order to compete with foreign banks. Indeed, the programme is to create a “big bank”, instill market power to banks (creating a supplier market rather than a buyer market), and form a type of cartel or oligopolistic competition in the industry. The price of funds, i.e. the interest rate will be determined by the banks themselves rather than by the market forces. Furthermore the state participation in the sector will be increase. The creation of a few banks that are “big” in terms of assets does not reflect the spirit of financial liberalisation, indeed the government turning back it planning in liberalising the sector as instituted by former Finance Minister, Anwar Ibrahim.

It is believed that BNM will push another round of consolidation in terms of restructuring shareholders in the banking system and the number of banks. There is speculation that the banks will be further reduced to 6 or below in future. Section 46 of the Banking and Financial Institution Act 1989 (Bafia) states that shareholdings in banks should not be more than 10 percent of any one individual and 20 percent for any one corporation. It is estimated that up to RM10 billion worth of shares may have to be divested by controlling shareholders to comply with the above mentioned ruling (Sakran,S, 2001). Who will gain from this divestification? Implementation of the rules will affect a few big names and institutions in the banking sector, namely, Tan Sri Teh Hong Piow (Public Bank), Tan Sri Azman Hashim/AMMB Holdings (Arab-Malaysian Bank), Tan Sri Rashid Hussain/RHB Capital (RHB Bank), Tan Sri Quek Leng Chan/Hong Leong Bhd (Hong Leong Bank Bhd), DRB-Hicom/Edaran Otomobil Nasional Bhd (EOB Bank Bhd), Datuk Tan Teong Hean

[32] Danamodal had Injected RM7.59 billion to recapitalise 10 financial institutions. Only four banking institutions remained indebted to Danamodal. They are MBf Finance Bhd, RHB Bank Bhd, Arab-Malaysian Bank Bhd and Oriental Bank Bhd. The outstanding amount owing is RM14.4 billion.

[33] Banks consolidation received a strong support from within the ruling UMNO, to make sure that trusted members of the party control all 10 anchor banks (Shari, M. 2001).

[34] The 10 anchor banks in the merger include Maybank, Bumiputra-Commerce bank Bhd, RHB Bank Bhd, Public Bank Bhd, Hong Leong Bank Bhd, Perwira Affin Bank Bhd, Southern Bank Bhd, EON Bank Bhd, Multi-Purpose Bank Bhd, and Arab-Malaysian Bank Bhd.

(Southern Bank Bhd) and Affin Holdings/Lembaga Tabung Angkatan Tentera (Affin Bank). Since the rule was established more than 12 years ago, why is it now that BNM is proceeding with it.

The Bafia rule maybe one of the reasons why the Ministry of Finance (MOF) rejected the proposal of Tan Sri Rashid Hussian (TSRH) to pay RM1.38 billion (38% premium) to buy RM1 billion RHB Bank Irredeemable Non-Cumulative Preference Shares (INCPS) held by Danamodal which was issued in 1999.[35] There are a few reasons (speculative) regarding the matter: the government blocked the purchase of the shares to keep RHB from issuing more bonds to finance its existing debts. TSRH had a debt of about RM2.29 billion in 2000. On the other hand, as has been argued, passing the debt from the taxpayers to the market investors is an entirely acceptable move, especially given RHB Bank's position as an anchor bank (RHB bank is the third largest bank in the country after Maybank and Bumiputra-Commerce Bank). It seems that the government wants to hold on to the stake at the expense of the taxpayers. The move may be a ploy to wrest control of Malaysia's third-largest bank from a who is businessman out of favour with the ruling party UMNO. The move by MOF is not fair to TSRH since the government (BNM) had requested the RHB Bank to take over the troubled Sime Bank in 1999[36]. RHB Bank never required any recapitalisation from Danamodal and the sole purpose of the RM1 billion INCPS was for the rescue of Sime Bank. MRCB supported the move by MOF.

TSRH has 23.9 percent stake in RHB Bhd. RHB Bhd in turn has a 55.4% stake in RHB Capital , which has a 70% stake in RHB Bank. TSRH controls 7.6% of RHB Bank through a 55.4% stake in RHB Capital. If the INCPS is redeemed, this will dilute RHB Capital's stake in the bank to 56%. RHB Bank could save about RM70 million a year. This amount will be transferred to its parent company RHB Capital in the form of a higher dividend. As long as the preferences shares are there in RHB Bank, there is less dividend that can be remitted upwards (Shanmugam M, 2001). This exercise will leave investors with a smaller exposure to the growth potential of RHB Bank. MRCB which owns 22.7 percent in RHB Bhd is against the move. Also, the MRCB has stressed that TSRH should concentrate and settle his debt of RM2.29 billion. MRCB has emphasized that the scheme which was presented did not provide details as to how TSRH will reduce his debt. Since MRCB is in the process of reducing debts, the move by TSRH will distort their plan. Some people believe that the move is to thwart RHB's chairman, TSRH. TSRH was once close to the ruling party (Datuk Seri Anwar Ibrahim and Datuk Seri Dr Mahathir). In 2000, MRCB had reorganised the top management and several associates of Finance Minister Daim Zainuddin had been brought into the company.

The government has also planned to consolidate stockbroking firms by creating the so called Universal Stockbrokers. The move is also due to the indebtedness of 11 stockbroking companies of about RM2.81 billion. All the 11 companies are now under Danaharta for debt restructuring exercises. The number of stockbroking companies and proposals received by the SC as at December 31, 2000, 54 companies has decided to merge.

CONCLUSION

[35] If the restructuring agency, Danamodal keeps and converts the INCPS shares, then MOF will control RHB Bank through a 30% stake held by Khazanah Nasional, plus 14% held by Danamodal. Danamodal is a temporary institution and its role will end after the recapitalisation of the banking sector is over.

[36] In February 1999, Commerec Asset-Holding Bhd (CAHB), the parent company of Bank of Commerce (M) Bhd, owned by Renong and MRCB, has acquired Bank Bumiputra Malaysia Bhd, a state commercial bank. The acquisition costs RM1.53 billion in which RM1.02 billion paid in new shares issued by CAHB and the balance paid in cash. The purchase represented a 28 percent discount from BBMB net tangible assets of RM2.2 billion (The Star, 15 February 1999).

The effectiveness of capital control in Malaysia's case relies on the exchange control. Without the exchange control, the capital control (and the fixed exchange rate) would have been ineffective in restoring monetary policy independence. Eventhough the government received a lot of criticism mainly from portfolio investors who stated that the capital (and exchange) control could harm the investment, nevertheless the CEC policy has promoted and stimulated economic recovery. Although the CEC policy has directly hurt incentives to invest in portfolio instruments but it is not in foreign direct investment (FDI). There are other reasons why FDI is diverted from the country, among them are China's economy and the recession in Japan.

The CEC policy and expansionary monetary policy have expanded liquidity in the financial system, however, banks remain sceptical in providing or extending banking facilities to fragile or indebted companies. Due to the experience from the effect of the economic crisis, banks are hesitant to provide loans to weak companies just to avoid facing another height of non-performing loans. As can be noticed, the 1997 economic crisis has struck many large corporations and most of the companies are closely associated to members of UMNO. Since banks are reluctant to provide loan (or refinance) to the companies[37] indebt, and the companies themselves barely undergo extensive "market-based" debt-restructuring, the government (including public fund entities) has been asked to step in to help those sick firms (selected) by issuing guaranteed bonds or by paying cash. Implicitly, the bonds financed by taxpayers and this has creates unhappiness in the society. The ruling party is practising the "economics of corrupt democracy".

The government fund should be used in promoting economic recovery and employment as well as to eradicate poverty in the agricultural sector. The government has abused the CEC policy in helping a few people that are close to them. Malaysia may face another phase of economic crisis from the slowdown of United States of America (USA) economy. USA is Malaysia's main trade partner after Japan. Malaysia has missed an opportunity to stabilise and promote sustainable economic growth.

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[37] Companies which have received financial assistance from the government are largely involved in privatisation projects. Besides extending a soft loan to the companies to start a project the government has to bail out them if they fail. What kind of privatisation is this? It seems that privatisation was implemented in 1984/5 now on brink of failure. In the early stages of the privatisation policy, the success of the policy was related to the heavy inflow of FDI-expansion of the manufacturing sector which needed large public investment in infrastructure (some of the intrastructure in the country is not yet need). The privatisation and corporatisation policies had created a group of "new rich" which are closely related to the ruling government (party). The creation of new wealth which is accumulated among a few people at the expense of socio-economic development is against the principle of the New Economic Policy (NEP). In the new Outline Perspective Plan 3 (OPP3) which was unveiled by Prime Minister Dr Mahathir in early April 2001, the government has stressed on poverty eradication. OPP3 is to eradicate poverty or re-accumulate/re-build a losses of cronies which are affected from the economic crisis. I am very sceptical that the OPP3 is to eradicate poverty for people in income below the poverty line.

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