## Undiscovered Pearl: The case of Malaysia's bullish policies implementation.

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**23 April 2004**

**The Malaysian economy has been turned upside down during the past ten years. As one of the most rapidly growing economies in the Asian region, it was heavily bombarded by the Asian Economic Crisis of 1997-98. Malaysia and its economy were created from a dream and this was shattered by the crisis. Proven by history, it stood up and regained stability due to its bullish and highly debated macroeconomic policies. This essay will argue that besides the criticisms by a number of highly influential economic analysts and economic organisations, Malaysia's macroeconomic policies were effective in stimulating a rapid economic recovery from the Asian Economic Crisis of 1997-98. This essay will describe the effects of the crisis on the Malaysian economy and its financial status. Equally important, it will discuss the recent economic recovery in Malaysia with particular emphasis on the methodology and schemes of the major stimuli.**

**The Asian Economic Crisis of 1997-98 had left a great impact on the whole Asian region. In the case of Malaysia, it caused great distress to the Malaysian government and its economic policy makers. Since gaining independence, Malaysia showed rapid development and economic growth from an agricultural based economy to a technologically advanced manufacturing based economy (Meesok, Lee, Liu, Khatri, Tamirisa, Moore and Krysl, 2001). However with the depreciation of the Thai Baht in mid-1997, a ripple effect of financial, currency and economic plunge changed the image of the Malaysian economy. An increase of large portfolio outflows and economic vulnerability caused a major decline of market confidence, equity and property values. The decline created tremendous pressure on the value of the ringgit (Okposin Hamid and Boon, 1999). This was worsened by the activities of money traders, which consequently caused the ringgit to devalue by almost 100 percent. As an illustration of the intensity of the devaluation, Malaysia's wealth decreased by half and its economic growth stopped during the financial crisis period (Okposin, Abdul Hamid and Boon, 1999). The string of events eventually amplified the level of inflation, which affected the financial stability of the Malaysian people and thus triggering a great stir in Malaysian politics (Mohammad, 1999). With an already severe scenario at hand, Malaysia and its government were faced with another problem, the instability of politics. In order to manage and survive these problems, especially the economy, the Malaysian government imposed its new macroeconomic policies, which consisted of its version of capital control and financial and corporate reforms.**

**One of the major stimuli in Malaysian economic recovery from the Asian Economic Crisis of 1997-98 was its version of capital controls. According to most literature, capital control is a method imposed by a government to its economy to totally separate it from the rest of the world. However, Malaysia had formulated its capital controls without total separation. Malaysia's capital controls were laid by several methodology and schemes aimed at restricting portfolio outflows and eliminating the offshore ringgit market. It was imposed by limiting the withdrawal of funds invested in Malaysia for at least a year by portfolio investors. The government also made the trading of ringgit, international borrowing and lending in ringgit, and trade settlements in ringgit to be illegal outside of Malaysia (Meesok, Lee, Liu, Khatri, Tamirisa, Moore and Krysl, 2001). In addition, a comprehensive restriction in exporting and importing of ringgit banknotes was also implemented. Circumvention of the controls was limited due to the design of the control. The design was selective in focusing on only the offshore ringgit market and portfolio flows. Neither current account transactions nor direct foreign investments were affected (Meesok, Lee, Liu, Khatri, Tamirisa, Moore and Krysl, 2001). These are the main differences between conventional capital controls and the Malaysian version of capital controls. However, many economic analysts did not consider these differences and set prejudgement in criticising the implementation of the controls (Mohammad, 1999).**

**A relatively fast and strong recovery was achieved by the implementation of Malaysia's capital controls regardless of criticisms made by international economic analysts and organisations. Initially, the International Monetary Fund (IMF) had lodged a solution for Malaysia to overcome its problems and condemned the Malaysian government for its implementation of its own macroeconomic policies (Mohammad, 1999). Despite the external pressure, the Malaysian government decided that it was wise to implement its policies on capital controls. This action, subsequently, stimulated an impressive economic recovery. Portfolio outflows and offshore ringgit markets were restricted and eliminated without neither creating a non-deliverable forward market nor a black market (Meesok, Lee, Liu, Khatri, Tamirisa, Moore and Krysl, 2001). Starting from mid-1999, portfolio inflows increased and the market sentiment turned bullish in response to monetary easing and the upgrading of Malaysia's outlook and credit ratings. This remarkable and surprising recovery affected the IMF significantly on its credibility and optimistic approach towards assisting economies in stress (Business Asia, April 2004). The Malaysian economy recovered relatively and significantly faster compared to other IMF-prescribed economies (Mohammad, August 1999). According to Mahathir Mohammad, the then Malaysian prime minister, in his article "Case Study for a Country under Economic Stress",**

**In the same article, Mohammad mentioned that the international financial community in itself was flawed and that putting Malaysia's fate in it will cost her sovereignty. In this case the government implemented the self-help approach. The decision was proven to be most effective in the case of Malaysian financial and economic crisis of 1997-98.**

> "3. Currency control as imposed by Malaysia is not generally understood by the international financial community. Their criticisms are therefore based more on their text-book models than on proper examination of what Malaysia has done. To understand the measures we took it is necessary to look at the root cause of the financial turmoil which undermined the economy of the country. "

**However the recovery was not based on only one stimulus. The Malaysian government also implemented financial and corporate reforms together with capital controls. The methodologies of these reforms are to craft a competitive market and to stabilise the ringgit. It was done by the mergence of Malaysia based companies and local companies focusing on banks and financial companies and pegging of ringgit to the US dollar on a RM3.80 exchange rate (Nyland, Smith, Smyth and Vicziany, 2001). Capital controls have helped to keep the stability of the economy whilst the reforms have made Malaysia a competitive market with a stable exchange rate of its currency. The problem of the outflow of investments was contained thus helping the economy to stay strong. Malaysia's unconventional response to the crisis suggests that it has developed a new level of confidence in its ability to adopt and sustain innovative policies even when these strategies challenge the international financial community (Nyland, Smith, Smyth and Vicziany, 2001). George Soros's, a highly influential investment analyst, criticism of the Malaysian government and its actions as "a menace to its own economy" was later to be proven wrong. This can be seen from his action of investing in Malaysian sovereign bonds in 2001. The US projected that imposing capital control and corporate and financial reforms would send Malaysia into poverty and chaos. However, after analysing current developments, US State Department official, James Kelly, heralded Malaysia as a beacon of stability (Business Asia, April 2004).**
**In conclusion, Malaysia dealt with the Asian Economic Crisis of 1997-98 effectively and was able to maintain stability and growth of its economy. A new approach of its capital controls and financial and corporate reforms have helped to achieve the successful recovery. Critisms and prejudgements towards the Malaysian government and its macroeconomic policies were proven to be irrelevant and that the implementation was a success. With this experience, Malaysia is prepared to face future economic challenges. Malaysia's macroeconomic policies have provided the international society with an experience, which will be useful for case studies in the management of a country's economy facing crisis.**

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