

Abstract

This paper attempts to develop an early warning system to predict currency crises that will allow managers not to be caught off-guard when a currency crisis hits the country. It is hoped that with an effective early warning system, managers will have adequate time to construct appropriate marketing and business strategies to counter the negative impact of a currency crisis.

This research project examines the macroeconomic data generated by Bank Negara and the Ministry of Finance to see if correlations exist between macroeconomic measures and devaluation prospects as cited in the literature and whether these can be used in the construction of an early warning system predictor. Further a model of the early warning system is proposed. The proposed model has 3 components. The first component is to track economic performance particularly current account sustainability. The second component is to track investor expectations and the third component is to track vulnerability to triggering events.

It was found that the selected macroeconomic factors alone could not precisely indicate that the current account deficit was unsustainable and thereby leading to the probability of a crisis.