Chapter Five

FINDINGS AND ANALYSIS

Macroeconomic Performance

The selective capital control imposed on September 1, 1998 was meant to insulate the economy against currency manipulations as well as to provide a breathing space to restoring economic stability. The previous chapter deliberates on the rationale for adopting selective capital controls. In order to evaluate the impact of these control measures and other corrective actions, a quarterly review of various macro-economic indicators were monitored throughout the period after the imposition of selective capital controls.

This chapter examines the major economic indicators over a five-year period (1995-1999), on a quarterly basis. These indicators include the **GDP growth**, the **Balance of Payments**, the **Current Account Balances**, the **Balance of Trade**, the **Capital Account**, the **International Reserves**, the **KLSE indices**, the **Inflation Rate** (Consumer Price Index) and **the Unemployment Rate**.

Each of these indicators will be discussed and analyzed to provide us with an in-depth insight and understanding of the impact of selective capital control on the Malaysian economic performance. These indicators do not represent the complete list but suffice to reflect and provide a good indication of the overall status of a country's economy.

The GDP growth

The Gross Domestic Product is the total national income/output of a country. When it is calculated by adding up the total expenditure for each component of final output, the result is called GDP expenditure-based, when it is calculated by adding up all the incomes generated by the act of production, it is called GDP income-based.

Malaysia adopts the GDP expenditure-based method. Here, total expenditures on final output is the sum of four broad categories of expenditure: consumption, investment, government spending and net exports.

GDP is measured at the purchaser value and GDP growth is derived by using the percentage of annual change at 1987 constant price. GDP growth is an important indicator of economic growth. By definition, recession ensues when GDP records a negative growth for two successive quarters. Once in recession, a country must record a positive GDP growth successively for two quarters to render it out of recession. Because of this definition all the data obtained in this study are computed on a quarterly basis.

It can be seen in table 1 that GDP growth for 1995 was 10.3% in the first quarter, 12.2% in the second quarter, 8.0% and 9.2% in the third and fourth quarter respectively. Hence average GDP in 1995 was about 9.9%. In 1996, the GDP growth was 12.2% in the first quarter, 8.8% in the second quarter, 9.7% in the third quarter and 9.5% in the fourth quarter making the average GDP growth in 1996 at about 9.8%.

In 1997, the GDP growth in the first and second quarter was 8.6% and 8.4% respectively. However in the third and fourth of 1997 GDP growth decelerated to 7.7% and 5.6% respectively. The average GDP growth in 1997 was reduced to 7.6% as compare to the preceding year.

In summary GDP growth was fairly stable and strong during the period just before the crisis. The full impact of the currency crisis was felt in 1998, where GDP registered a negative growth of -3.1% in the first quarter and –5.2% in the second quarter. The biggest contraction of -10.9% was recorded in the third quarter before stabilizing at –10.3% in the last quarter of 1998.

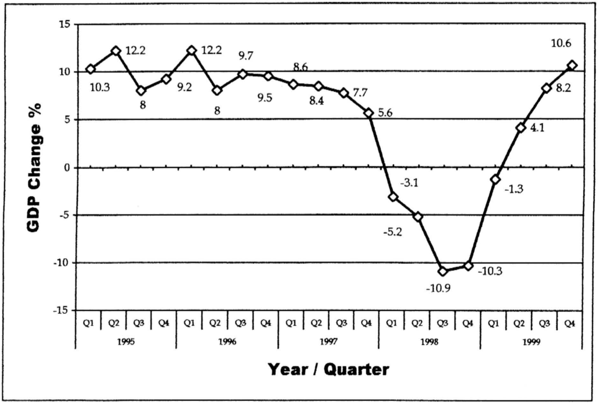
•

Table 1 : GDP at Purchaser value : 1995 - 1999

Year	GDP Annual Change (%) @ 1987 Constant Price			
	Q_1	Q_2	Q_3	Q_4
1995	10.3	12.2	8.0	9.2
1996	12.2	8.8	9.7	9.5
1997	8.6	8.4	7.7	5.6
1998	-3.1	-5.2	-10.9	-10.3
1999	-1.3	4.1	8.2	10.6

Source : Department of Statistic

Figure 1 : GDP at Purchaser Value : 1995 - 1999



Source : Derived from Table 1

From the data, it was obvious that by the end of the second quarter of 1998 Malaysia had already plunged into a recession. This trend went on throughout 1998 till the first quarter of 1999 where GDP growth was –1.3%. However, in the second quarter of 1999, GDP began to register a positive growth of 4.1%. This is also true for the third quarter (8.2%) and fourth quarter (10.6%). By the end of the fourth quarter of 1999, Malaysia was already out of the recession with GDP growth back at the pre-crisis level.

Hence, It can be deduced that the imposition of selective capital controls on 1 September 1998 has managed to reduce the severity of a recession and subsequently restored the GDP growth as evident in the second quarter of 1999 onwards.

Figure 1 shows a line graph of the GDP growth derives from table 1. Here, the direction and movement of the GDP growth throughout 1995 to 1999 is seen more clearly.

Balance of Payment

The balance of payments records the transactions between countries. The balance of payments accounts are normally divided into **two** broad parts. One part deals with payments of goods and services, interest, and transfers. This is known as the **current account**. The other part records transaction in assets and is, accordingly, known as the **capital account** (textbook economics). In table 2, it can be seen that for 1995, Malaysia had a deficit in its balance of payment account in the first, third and fourth quarter of –RM3.9 billion, -RM1.9 billion and –RM1.5 billion respectively. Though the second quarter showed a surplus of about RM2.9 billion, the overall balance of payment in 1995 was a deficit of –RM4.4 billion.

This implied that international trade during the 1995 period was not in Malaysia's favor. In 1996, the BOP for the first, second, third and fourth quarter was RM0.05 billion, RM3.0 billion, RM1.0 billion and RM2.2 billion respectively, making an overall surplus of about RM6.2 billion in 1996.

In 1997, though the first quarter registered a positive BOP of –RM2.1 billion, subsequently i.e. the second, third and fourth quarter recorded a negative balance of payment account of –RM1.5 billion, -RM8.8 billion and –RM2.8 billion respectively. Hence, overall in 1997, Malaysia posted a deficit BOP of about -RM10 billion. This huge deficit could be attributed to the financial crisis, with the loss of investor's confidence and capital outflow.

In 1998, the first quarter still recorded a negative balance of –RM1.9 billion but subsequently, the second, third and fourth quarter showed a positive balance of RM0.9 billion, RM23.3 billion and RM18 billion respectively. The huge surplus in the balance of payment seen in the third quarter could be due to the depreciation of ringgit. This trend continued in the fourth quarter after the imposition of capital control. Hence, the overall balance of payment for 1998 was about RM40 billion.

In 1999, the first, second and third quarter recorded a positive balance of payment of about RM5.8 billion, RM13.0 billion and RM1.0 billion respectively. In the fourth quarter there was a negative BOP of about –RM2.0 billion. However, 1999 still registered a BOP surplus of about RM17.8 billion.

Figure 2 shows a line graph of the BOP derives from table 2.

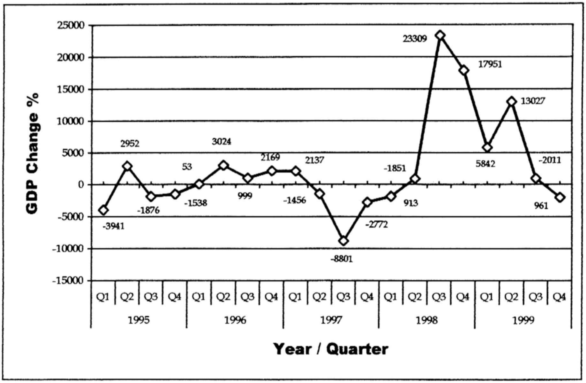
It would be interesting to know which of the components in the BOP account that contributed to its deficit or surplus. This can be readily seen under the section on current account and capital account.

Table 2 : Balance of Payment : 1995 - 1999

Year	Balance of Payment			
	Q1	Q2	Q3	Q4
1995	-3,941	2,952	-1,876	-1,538
1996	53	3,024	999	2,169
1997	2,137	-1,456	-8,801	-2,772
1998	-1,851	913	23,309	17,951
1999	5,842	13,027	961	-2,011

BNM : MSB Feb 1999
Oct 1998

Figure 2 : Balance of Payment : 1995 - 1999



Source : Derived from Table 2

Current Account

The current account records transaction arising from trade in goods and services, from accruing to capital owned by one country and invested in another, or from transfers by residents of one country to residents of another. The current account is divided into two main sections.

The first of these, variously called visible account, the trade account, and the merchandise account, records payment and receipts arising from the import and export of tangible goods. The second part, the invisible account, records payments arising out of trade in services, payments for the use of capital, and transfer to persons. In short, the combination of trade balance and invisible balance gave an overall current account balance. However, in this section, the current account balances refers to the combination of both trade and invisible balances.

In table 3, it can be seen that in 1995, there was a current account deficit of -RM4.2 billion in the first quarter, -RM7.8 billion in the second quarter, -RM0.6 billion in the third quarter and –RM3.4 billion in the fourth quarter. Hence in 1995, Malaysia's current account deficit was about, -RM16.0 billion. If we looked back at the BOP account we could conclude that the BOP deficit in 1995 was mainly due to the deficit in current account.

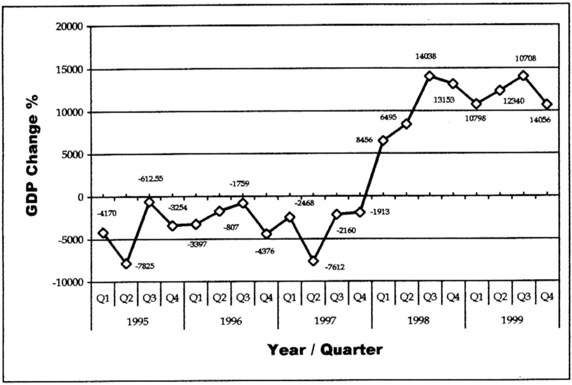
In 1996, there was a deficit of -RM3.3 billion, -RM1.8 billion, -RM2.8 billion and –RM4.4 billion in the first, second, third and fourth quarter respectively, making the total deficit in 1996 of about -RM12.3 billion. However, the surplus BOP registered in 1996 was due to the surplus contributed by the capital account. In 1997, the first and second quarter registered a deficit in current account of –RM2.5 billion and –RM7.6 billion respectively. However, the third and fourth quarter though still showed a negative current account balance of –RM2.2 billion and –RM1.9 billion respectively, the deficit was reduced. This shows that the currency crisis has resulted in the reduction of imports of goods and services.

Table 3 : Current Account Balance

Year	RM (Mil)			
	Q_1	Q_2	Q_3	Q_4
1995	-4,170	-7,825	-612.55	-3,397
1996	-3,254	-1,759	-2,807	-4,376
1997	-2,468	-7,612	-2,160	-1,913
1998	6,495	8,456	14,038	13,153
1999	10,798	12,340	14,056	10,708

BNM : MSB 02/99 QSB

Figure 3 : Current Account Balance



Source : Derived from Table 3

In 1998, the first quarter shows a surplus of RM6.5 billion, while the second, third and fourth quarter shows a surplus of RM8.5 billion, RM14.0 billion and RM13.2 billion respectively making a current account surplus for 1998 at about RM42.2 billion. 1999 above saw a huge current account surplus of RM10.8 billion in the first quarter, RM12.3 billion in the second quarter while the third and fourth quarters surplus was RM14.1 billion and RM10.7 billion respectively. Hence, the total current account surplus for 1999 was RM47.9 billion.

The Balance of Trade

As mentioned earlier, the trade account is a part of the current account which records payment and receipts arising from the imports and export of tangible goods.

In table 2, it can be seen that the balance of trade for 1995, for all the four quarters were negative i.e about –RM1.7 billion in the first quarter, about –RM3.9 billion in the second quarter while the third and fourth quarter was about –RM2.8 billion and about RM1.0 billion respectively making the total deficit of about –RM9.4 billion. This means that throughout 1995 the importation of goods exceeded its exports.

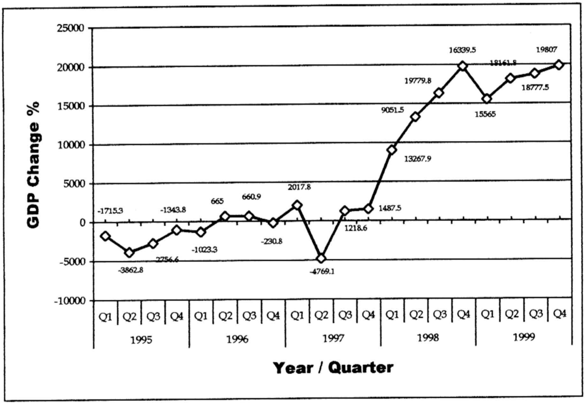
In 1996, the negative trade balance of - RM1.35 billion in the first quarter and - RM0.23 billion in the fourth quarter indicating more imports than exports. But, for the second quarter and the third quarter of 1996 exports exceeds imports with a positive trade balance of RM0.66 billion and RM0.67 billion respectively. However, if taken on an annual basis, there was a negative trade balance of about - RM0.25 billion in 1996.

Table 4 : Balance of Trade : 1995 - 1999

Year	Balance of Trade (RM Mil)			
	Q_1	Q_2	Q_3	Q_4
1995	-1,715.3	-3,862.8	-2,756.6	-1,023.3
1996	-1,343.8	660.9	665.0	-230.8
1997	2,017.8	-4,769.1	1,218.6	1,487.5
1998	9,051.5	13,267.9	16,339.5	19,779.8
1999	15,565.0	18,161.8	18,777.5	19,807.0

Source : Department of Statistics

Figure 4 : Balance of Trade : 1995 – 1999



Source : Derived from Table 4

For 1997, positive trade balance of RM2.0 billion was seen in the first quarter, RM1.2 billion in the third quarter and RM1.5 billion in the fourth quarter. In the second quarter, there was a negative trade balance of about - RM4.77 billion. On the whole, in 1997, Malaysia recorded a slightly negative trade balance of about - RM0.045 billion. This is understandable as the importation of goods and consumer spending has declined further as a consequence of the currency crisis.

In 1998, the balance of trade recorded a positive trade balance of RM9.0 billion in the first quarter, RM13.3 billion in the second quarters RM16.3 billion in the third quarter and RM19.8 in the fourth quarter.

Hence, in 1998, there was an overall surplus of trade balance of about RM49.4 billion. In 1999, a positive trade balance was also observed throughout the year. In the first quarter the surplus was RM15.6 billion, while the second, third and fourth quarter were RM18.2 billion, RM18.8 billion and RM19.8 billion respectively, making the overall surplus of about RM72.4 billion.

The huge positive trade balance seen in 1998 and 1999 could be attributed to the decline in importation of goods as a result of depreciated ringgit as well as the higher earnings in foreign exchange from the export of goods.

Hence, it can be seen from the data obtained that the pegging of ringgit USD together with the selective capital controls has resulted in a higher export value and earnings, at the same time allowing for the increase in positive trade balances.

Figure 2 is a line graph presentation of the balance of trade derives from table 2.

Capital Account

As mentioned earlier, the other major component in the balance of payments is the capital account, which records transactions related to the international movements of ownership of financial assets. It is important to notice right away that the capital account does not relate to imports and exports of physical capital: trade in such things as machine tools or construction equipment is part of the **visible trade account**. Rather, the capital account of the balance of payments relates only to cross-border movements in financial instruments, such as ownership of company shares, bank loans, or government securities.

Malaysia Purchases of foreign investments (which then become assets to Malaysia) are called a **capital outflow**. When foreign exchange is used to buy the foreign investment, they are entered as a debit (negative) item in the Malaysia payments accounts. Foreign investment in the Malaysia (which, thereby, increases Malaysia liabilities to foreigners) is called a capital inflow. It earns foreign exchange and so is entered as a credit (positive) item.

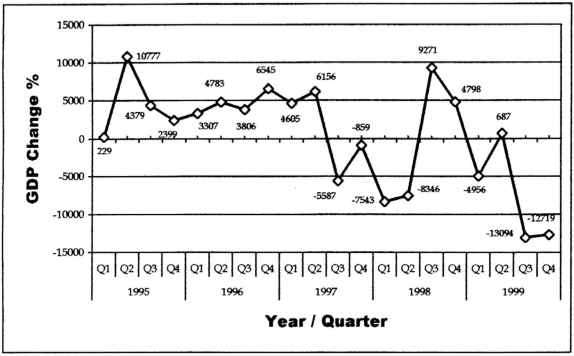
The capital account is often divided into two categories that distinguish between movements of short-term and long-term capital. Short-term capital is money that is held in the form of highly liquid assets, such as bank accounts and short-term Treasury bills. Long-term capital represents funds coming into Malaysia (a credit item) or leaving Malaysia (a debit item) to be invested in less liquid assets, such as long-term bonds, or in physical capital, such as a new semi-conductor plant.

The two major subdivisions of the long-term part of the capital account are direct investment and portfolio investment. Direct investment relates to changes in non-resident ownership of domestic firms and resident ownership of foreign firms. One form of direct investment, called Greenfield investment, is the building of a factory in Malaysia by a foreign firm - for example, the Motorola factory in Singe Way.

Table 5 : Capital Account

Year	Capital A/C RM (Mil)			
	Q_1	Q_2	Q_3	Q_4
1995	229	10,777	4,379	2,399
1996	3,307	4,783	3,806	6,545
1997	4,605	6,156	-5,587	-859
1998	-8,346	-7,543	9,271	4,798
1999	-4,956	687	-13,094	-12,719

Figure 5 : Capital Account



Source : Derived from Table 5

Another form of direct investment, called Brownfield investment, is a takeover, in which a controlling interest in a firm, previously controlled by residents, is acquired by foreigners. Portfolio investment, on the other hand, is the investment in bonds or a minority holding of shares that does not involve legal control.

From table 5, in 1995 the capital account recorded a positive balance of RM0.23 billion in the first quarter, RM10.8 billion in the second quarter, RM4.4 billion in the third quarter and RM2.4 billion in the fourth quarter. Hence, in 1995 the net capital inflow is about RM17.78 billion.

In 1996 the capital account again recorded a positive balance for all the quarters i.e. about RM3.3 billion in the first quarter, RM4.8 billion in the second quarter, RM3.8 billion in the third quarter and RM6.5 billion in the fourth quarter. The total out capital inflow in 1996 was RM18.4 billion, higher than the one recorded in 1995.

In 1997, Malaysia again attracted a net capital inflow of RM4.6 billion in the first quarter and RM6.2 billion in the second quarter. However, during the currency crisis capital began to flow out of Malaysia as recorded in the third quarter - RM5.6 billion and - RM0.86 billion in the fourth quarter of 1997. The net capital outflow continued in the first quarter and second quarter of 1998 with a value of - RM8.35 billion and - RM7.54 billion respectively. However, in the third quarter of 1998 there was a net capital inflow of RM9.3 billion. The inflow could be attributed to the imposition of selective capital control the trading of ringgit was deemed illegal and cannot be traded outside Malaysia. The net capital inflow of RM4.8 billion was also seen in the fourth quarter of 1998. Taking the whole of 1998, there was a net capital outflow or - RM1.82 billion.

In 1999, the first quarter saw a net capital outflow of RM4.96 billion but in the second quarter there was a net capital inflow of about RM0.69 billion. However, in the third quarter and fourth quarter there was a huge capital outflow of - RM13.1 billion and - RM12.7 billion respectively.

This huge capital outflow happened after the one year expiry period imposed under the selective capital control. Hence in 1999, the net capital outflow was about - RM30.1 billion. However, that capital flight is expected and is not worrisome as Malaysia current account balance for 1999 was in exceed of RM47.9 billion and can easily offset the capital account deficit for 1999.

International Reserves

Government often accumulate and hold foreign exchange reserves, just as individual maintain saving accounts. Malaysia had a steady reserves in 1995 and 1996. In 1995, the reserves were RM64.3 billion in the first quarter, about RM67.3 billion in the second quarter, about RM64.0 billion in the third quarter and about RM63.9 billion by the fourth quarter. For 1996, the reserves ranges were about RM63.8 billion in the first quarter, qhile the reserves for the second and third quarter were about RM66.8 billion and RM67.8 billion respectively. By the fourth quarter the reserves were at about RM70.0 billion. It can be seen that in 1995 and 1996, Malaysia had a steady reserves that could support about 3 ½ months its imports. In 1997, the reserves in the first and second quarter were steady at RM72.2 billion and RM70.7 billion respectively.

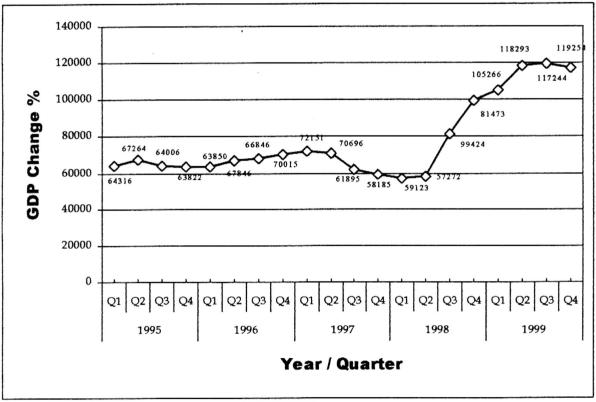
However, in the third and fourth quarter, reserves fell to about RM61.9 billion and RM59.1 billion respectively. The loss in reserves in the second half of 1997 was attributed to supporting the depreciating ringgit during the currency crisis. The reserves slipped further to about RM57.3 billion and RM58.2 billion in the first and second quarter of 1998 respectively.

Table 6 : International Reserves : 1995 – 1999

Year	International Reserves [RM (MIL)]			
	Q1	Q2	Q3	Q4
1995	64,316	67,264	64,006	63,850
1996	63,822	66,846	67,846	70,015
1997	72,151	70,696	61,895	59,123
1998	57,272	58,185	81,473	99,424
1999	105,266	118,293	119,254	117,244

BNM : MSB 02/99 (P103)

Figure 6 : International Reserves : 1995 – 1999



Source : Derived from Table 6

However, by the third quarter of 1998, the reserves has increased to about RM81.5 billion and by the end of the fourth quarter of the same year, the reserves were at about RM99.4 billion. In 1999, reserves in the first quarter was about RM105.3 billion while reserves in the second and third quarter were about RM118.3 billion and RM119.3 billion respectively.

By the end of the fourth quarter of 1999, Malaysia's reserves was about RM117.2 billion equivalent to 5.9 months of retained imports.

The increase in reserves was in accordance to the positive trade balances that were recorded during the same period. Hence, it can be deduced that the imposition of selective capital control has not only helped to reduce the further decline of reserves but has helped to increase.

Kuala Lumpur Stock Exchange (KLSE) Composite Index

The KLSE there are about 800 companies hotel composite in the KLSE. The composite index (index) is derived from 100 selected stocks listed in the main board of the KLSE. The index indicates the performance of the KLSE. In table 7, the index in 1995 is about 984.1 points in the first quarter, 1,026.6 points in the second quarter, 1000.6 points in the third quarter and 995.2 points in the fourth quarter. In 1996, the index was above 1,100 points for all the quarters i.e. 1,149.1 points in the first quarter 1,136.3 points in the second quarter, 1,135.3 points in the third quarter and 1,237.9 points in the fourth quarter.

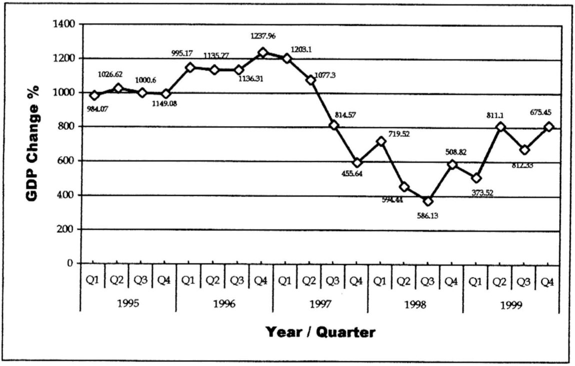
In 1997, the index remained high at 1,203.1 points in the first quarter and stood at 1,077.3 points in the second quarter. However, in the third quarter it slipped to 814.4 points and reduced further to 594.4 points in the fourth quarter. The sudden fall in the KLSE in the third and fourth quarter of 1997 which continued throughout 1998 was due to a major sell out of stock during the currency crisis and also in anticipation of depreciation of the ringgit by foreign portfolio managers.

Table 7 : KLSE Indices

Year	KLSE Indices			
	Q_1	Q_2	Q_3	Q_4
1995	984.07	1,026.62	1,000.6	995.17
1996	1,149.08	1,136.31	1,135.27	1,237.96
1997	1,203.1	1,077.3	814.57	594.44
1998	719.52	455.64	373.52	586.13
1999	508.82	811.1	675.45	812.33

Note : *All indices are end of period closing price.*
BNB : *MSD*
QB

Figure 7 : KLSE Indices



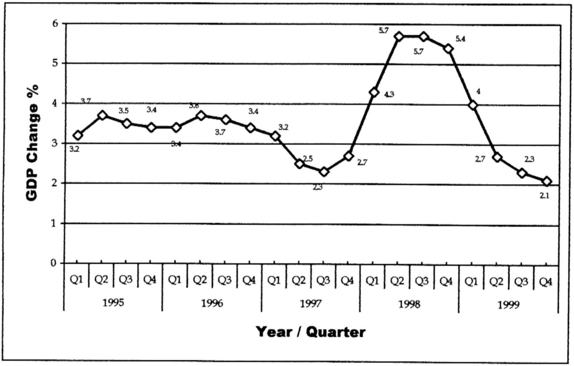
Source : Derived from Table 7

Table 8 : CPI

CPI / Year	CPI			
	Q_1	Q_2	Q_3	Q_4
1995	3.2	3.7	3.5	3.4
1996	3.4	3.7	3.6	3.4
1997	3.2	2.5	2.3	2.7
1998	4.3	5.7	5.7	5.4
1999	4.0	2.7	2.3	2.1

Source : QEB, MSB, BNM

Figure 8 : CPI



Source : Derived from Table 8

However, after the imposition of capital control on 1st. September 1998, the index increased to 586.1 points in the fourth quarter as compared to 373.5 points in the third quarter of 1998.

In 1998 , the index was 508.8 points in the first quarter and, 811.1 points in the second quarter. In the third quarter it dropped to 675.5 points but climbed up to 812.3 points in the fourth quarter.

The fall in the composite index to 675.5 points in the third quarter as compared to 811.1 points in the second quarter of 1999 could be due the low market sentiment resulting from the outflow of capital after the one year holding position as required under the selective capital control policy. However, the low market sentiment was just temporary as the index bounced back to 812.3 points in the fourth quarter of 1999.

Hence, from table 7, it can be deduced that the imposition of selective capital control has managed to arrest a further decline of the composite index, stop a major sell out of stocks as well as gaining back market confidence especially among long-term investors both domestic and abroad.

Inflation

In Malaysia the rate of inflation (CPI,1994=100) is measured using the consumer Price Index . Inflation is the rate of change of the price level, so the same forces that cause the price level to adjust upwards will also tend to raise inflation. From table 8, it can be seen that in 1995, Malaysia's inflation rate is fairly stable ranging from 3.2% in the first quarter, 3.7% in the second quarter, 3.5% in the third quarter and 3.4% in the fourth quarter.

Taking all the quarters, it can be derived that the average inflation rate in 1995 was 3.5%. In 1996, the inflation rate was 3.4% in the first quarter, 3.7% in the second quarter, 3.6% in the third quarter and 3.4% in the fourth quarter giving an average of 3.5% in 1996.

The inflation rate in 1997 was 3.2% in the first quarter, 2.5% in the second quarter, 2.3% in the third quarter and 2.7% in the fourth quarter giving an average of 2.7% for 1997. In 1998, where the full impact of the financial crisis was felt, the inflation rate went up to 4.3% in the first quarter, 5.7% in the second quarter, 5.7% in the third quarter. However, after the imposition of capital control and the pegging of ringgit to USD, the inflation rate in the fourth quarter of 1998 went down slightly 5.4%. In 1999, the inflation rate improves further to 4.0% in the first quarter, 2.7% in the second quarter, 2.3% in the third quarter and 2.1% in the fourth quarter. Hence from the data recorded, the government intervention to contain the crisis such as the selective capital control, pegging of the ringgit and a low interest rate regime has managed to stabilized the inflation rate to the pre-crisis level. We would expect the inflation rate to go up if the IMF solution of tight monetary and fiscal policy was adopted.

Figure 8 is a line graph presentation of the inflation rate which was derived from table 8.

Unemployment

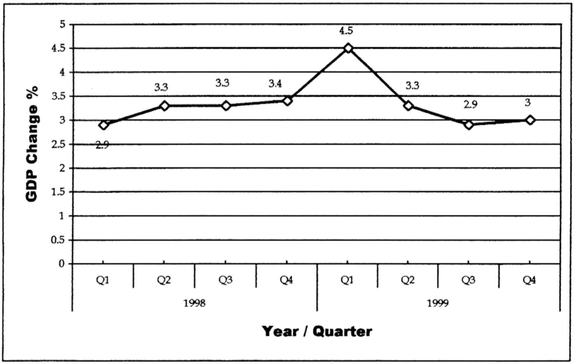
Many people are concerned about such issues as inflation, unemployment, recession and competitive. Firms are concerned about how inflations, recessions, and foreign competition affect their profits and, perhaps, even their survival.

Table 9 : Unemployment

Year	Unemployment				Annual
	Q1	Q2	Q3	Q4	
1995	n/a	n/a	n/a	n/a	3.1
1996	n/a	n/a	n/a	n/a	2.5
1997	n/a	n/a	n/a	n/a	2.4
1998	2.9	3.3	3.3	3.4	3.4
1999	4.5	3.3	2.9	3.0	n/a

Source : BNM

Figure 9 : Unemployment



Source : Derived from Table 9

Governments worry about how to prevent recessions, reduce inflation, increase competitiveness, and increase employment. Adults of working age are anxious to avoid the unemployment that comes with recessions and to obtain rising real incomes. Pensioners are keen to protect themselves against the hazards of inflations, which can lower the value of their savings.

High unemployment is associated with recessions, so when GDP falls below its potential level unemployment rises. Conversely, when output is above potential GDP, firms are running above normal capacity and unemployment tends to be low. A downturn is economic activity causes an increased in unemployment.

In table 9, the unemployment rate an annual basis for 1995 is 3.1%, 1996 is 2.5% and 1997 is 2.4%. At the height of the crisis in 1998, unemployment rate shot up to 3.4%. The first quarter of 1999 saw the unemployment rate to be at its peak of 4.5%. This is understandable as most companies affected by the currency crisis had to downsize their operations. In fact those companies which were seriously affected had to close down and retrenched their workers.

However, with the Malaysia government intervention, the unemployment rate in the second quarter of 1999 falls to 3.3%, while in the third quarter it slips further to 2.9% and stabilizing at 3.0% in the fourth quarter.

The Malaysian economy recorded a strong performance in the fourth quarter of 1999 as evident from the above data. Economic activity has returned to end 1997 levels. For the year as a whole, the real GDP rebounded to 5.4% compared with a contraction of 7.5% in 1998. Growth continued to be supported by stronger external demand, higher Government spending and further improvement in domestic demand. (BNM. Quarter Bulletin, 1999).

Political stability and the Government's commitment to restructuring, together with sound and pragmatic economic and financial policies, contributed to further improvement in investor and consumer confidence. This was reflected in the upgrading of Malaysia's sovereign ratings by a number of international credit rating agencies in late 1999 and early 2000. The liberalisation of the exchange control rule on one-year holding of portfolio investment did not lead to higher outflows of short-term capital. The net outflow of portfolio funds moderated to RM3.2 billion during the fourth quarter (RM5.2 billion in the third quarter). Nevertheless, some of these foreign funds have been reinvested in the country as reflected in the recent increase in net inflow of RM6.9 billion. As at 24 February 2000, the net international reserves of BNM increased significantly to RM128.6 billion (US$33.8 billion; US$30.9 billion at end-1999), sufficient to finance 6.4 months of retained imports. (BNM, 1999)

On the domestic front, the strong recovery in consumer confidence led to significant turnaround in many of the domestic-oriented industries. Aggregate domestic demand improved further during the fourth quarter as indicated in higher sales of new passenger cars and increased imports of consumption goods and loan approvals for consumption credit.

Fiscal expenditure also increased, mainly to fund the economic and social programme to strengthen economic recovery. Several key private investment indicators, such as higher imports of capital goods and higher disbursement for manufacturing ad construction sectors, also showed signs of modest recovery in private investment activity. (BNM, 1999)

The restructuring of the banking sector continued to show further progress. The RWCR of the banking system is stronger than the pre-crisis levels (12.5%), while the NPLs continued to decline (6.6%), thus providing the banking system with a comfortable cushion to absorb any potential shocks to the economy.

In a move to consolidate the domestic banking system, BNM has granted approval for the formation of 10 banking groups. The merger programme is a necessary precondition to create strong, efficient and competitive domestic banking institutions. In addition, BNM will continue to implement appropriate policies to further increase the resilience and competitiveness of the banking institutions. (BNM.1999)

Overall, strong economic growth during the fourth quarter was achieved in an environment of low inflation, favourable labour market conditions, continued large trade surplus, strong international reserves and relatively low external debt. (BNM.1999)

Hence, the selective capital control, the pegging of ringgit with an expansionary monetary and fiscal policy adopted by the Malaysian government had managed to stop the further increase of unemployment and put back the economy on a firmer footing.

If Malaysia were to adopt the IMF prescription, more business and corporate failures with a resultant increase in unemployment would be expected. Hence, Malaysia's policy prescription has managed to restore its economy at the sametime maintaining social peace and order of the country.
Countries such as Thailand, Indonesia and South Korea which adopted the IMF recipe had a high unemployment rate due to corporate failures. The high unemployment has also affected the political and social stability resulting in both political turmoil and social unrest.