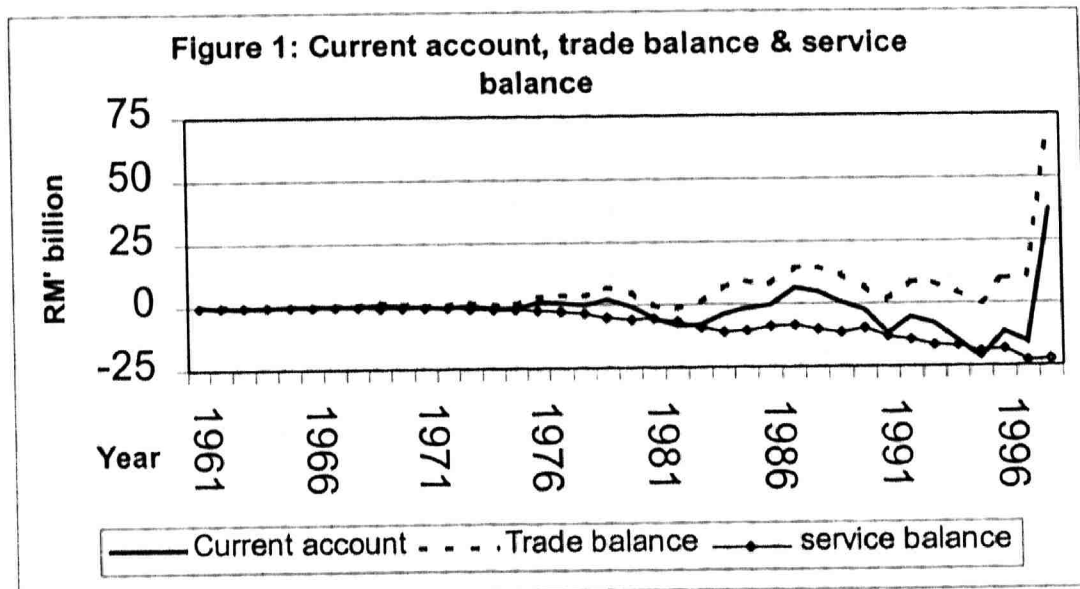


Chapter 2 Malaysian current account

Since independence in 1957, Malaysian current account has undergone tremendous changes. As shown in Figure 1, Malaysia does not encounter serious current account problems prior to the 1980s. However, Malaysia ran into trade deficits in the early 1980s and only managed to register surpluses in 1987. This did not last long and Malaysia was again slump into even much severe trade deficit problems in the 1990s and recorded trade deficits as high as 10.1% of GNP in 1995.



Source: Bank Negara Quarterly Bulletin.

- Mean: $E(Y_t) = \mu$
- Variance: $\text{Var}(Y_t) = E(Y_t - \mu)^2 = \sigma^2$
- Covariance: $\gamma_k = E[(Y_t - \mu)(Y_{t+k} - \mu)]$

Throughout the 1960s and 1970s, Malaysia enjoyed favourable trade balance which was usually large enough to offset the persistent service account deficits as shown in Table 1. This is mainly attributed to favourable commodity prices especially of tin. The tin price increased from £785 per ton in 1959 to £1,413 in 1965. Rubber is the exception as its price declined from 108.08 cents per pound in 1960 to 70.13 cents in 1965 (Lim 1967a). As a result, the current account remained in Malaysia's favour throughout the period.

However, Malaysia frequently ran into current account deficits in the 1980s. This is due to slowdown of demand as a result of worldwide recession in the early 1980s and economy slowdown in the industrial countries in the mid-1980s.

As Malaysian economy picked up in 1987, the current account turned around and registered surpluses. In addition, the turnaround was also attributed to the structural program of the Malaysian government to encourage export-oriented industrialization to pursue export-led growth.

Table 1: The current account (1961 – 1998)

RM' million	Exports	Imports	Trade balance	Balance of services	Net transfer	Current account
1961	3,208	2,697	511	-334	-193	-16
1962	3,232	2,895	337	-310	-194	-167
1963	3,296	3,013	283	-321	-181	-219
1964	3,346	3,074	272	-326	-74	-128
1965	3,752	3,231	521	-341	-58	122
1966	3,808	3,255	553	-407	-106	40
1967	3,679	3,204	475	-351	-142	-18
1968	4,070	3,433	637	-400	-143	94
1969	4,921	3,308	1,613	-702	-180	731
1970	5,020	3,953	1,067	-862	-180	25
1971	4,884	4,198	686	-878	-137	-329
1972	4,736	4,371	365	-906	-157	-698
1973	7,263	5,669	1,594	-1,197	-151	246
1974	10,022	9,482	540	-1,743	-104	-1,307
1975	9,057	8,443	614	-1,722	-79	-1,187
1976	13,330	9,608	3,722	-2,148	-100	1,474
1977	14,854	11,116	3,738	-2,586	-78	1,074
1978	16,932	13,242	3,690	-3,337	-104	249
1979	24,060	17,152	6,908	-4,858	-17	2,033
1980	28,013	22,775	5,238	-5,813	-45	-620
1981	26,900	27,143	-243	-5,312	-78	-5,633
1982	27,946	29,704	-1,758	-6,576	-75	-8,409
1983	31,762	30,760	1,002	-9,098	-21	-8,117
1984	38,452	31,466	6,986	-10,813	-90	-3,917
1985	37,576	28,693	8,883	-10,391	-14	-1,522
1986	34,970	26,592	8,378	-8,790	96	-316
1987	44,733	30,030	14,703	-8,409	348	6,642
1988	54,607	40,083	14,524	-10,180	395	4,739
1989	66,727	54,856	11,871	-11,392	219	698
1990	77,458	70,365	7,093	-9,723	147	-2,483
1991	92,220	90,771	1,449	-13,195	102	-11,644
1992	100,910	92,301	8,609	-14,568	337	-5,622
1993	118,383	110,152	8,231	-16,670	513	-7,926
1994	148,506	144,046	4,460	-17,005	-2,225	-14,770
1995	179,491	179,394	97	-19,229	-2,515	-21,647
1996	193,363	183,275	10,088	-18,371	-2,943	-11,226
1997	217,712	207,439	10,273	-22,748	-3,345	-15,820
1998	281,947	212,939	69,008	-22,338	-9,876	36,794

Source: Bank Negara Quarterly Bulletin.

Subsequently, Malaysian current account was back to deficits again from 1991 to 1997. This was due to the following factors:

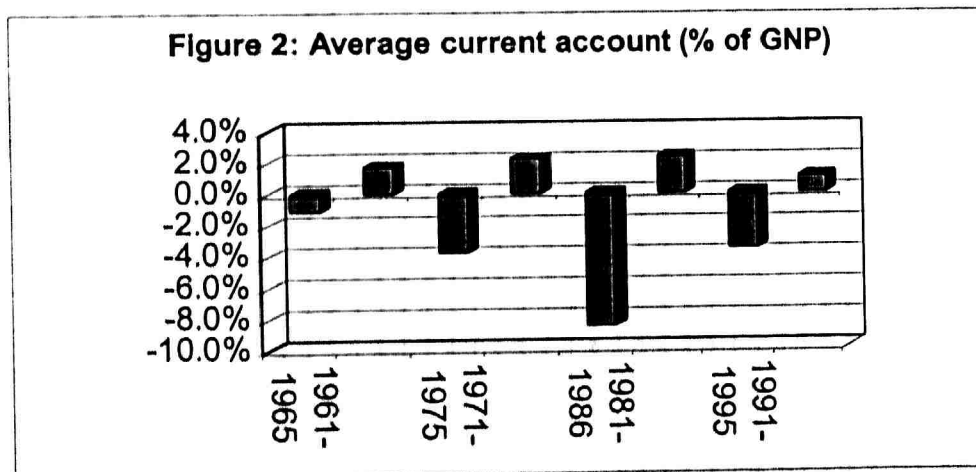
1. High import content of the manufactured exports (which cause the import of intermediate goods to increase).
2. The increase in foreign direct investments (FDIs) (which requires importation of capital goods as Malaysia do not have the capability to produce these goods)
3. The engagement of big infrastructure projects such as the construction of Bakun Dam, KLIA (Sepang International Airport), Bukit Jalil Stadium (for Commonwealth Games) and Cyberjaya. This caused the import bills to escalate.

However, the Malaysian current account made a strong comeback in 1998 with an unprecedented hefty surplus of RM36.794 billion. This was mainly due to the favourable effect of weaker Ringgit Malaysia (RM), the currency of Malaysia, on export earnings and the cutback of some bulky import items of the infrastructure projects. Export grew strongly at 29.5% which outpaced the import growth rate of 2.7%.

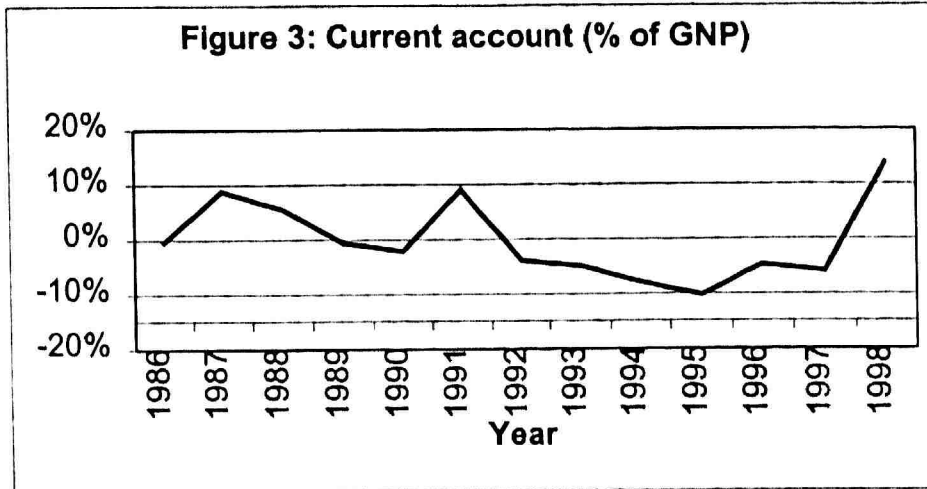
In general, the performance of Malaysian current account was largely dependent on the performance of the merchandise balance. This is owing to the fact that the services account is persistently in deficits and it is growing bigger from time to time. The poor performance of the merchandise account will aggravate the problems and leads Malaysia into current account deficits. This is

shown clearly in the Figure 1 where the rise and fall of the merchandise account will lead to the corresponding rise and fall of the current account.

In addition, from the 5-year average current account balance as a percentage of Gross National Product (GNP), we can observe some interesting pattern. As shown in Figure 2, Malaysian current account is highly cyclical. The most severe current account deficit was recorded in the period of 1981-1985 of 8.5% (on average) of GNP. Even though the deficits in the period of 1991-1995 are less severe, the deficit in 1995 is as high as 10.2% of GNP. This is extraordinary high and indicates the acute savings-investment gap in Malaysian economy, which serve as an indicator of weakness to the currency speculator during the recent economic crisis. Please refer to Figure 3 for the changes in the current account balance from 1986 to 1998.



Source: Bank Negara Quarterly Bulletin and Lin (1993)



Source: Bank Negara Quarterly Bulletin and Lin (1993).