

CHAPTER 5

EFFECTIVENESS OF THE RECOVERY MEASURES

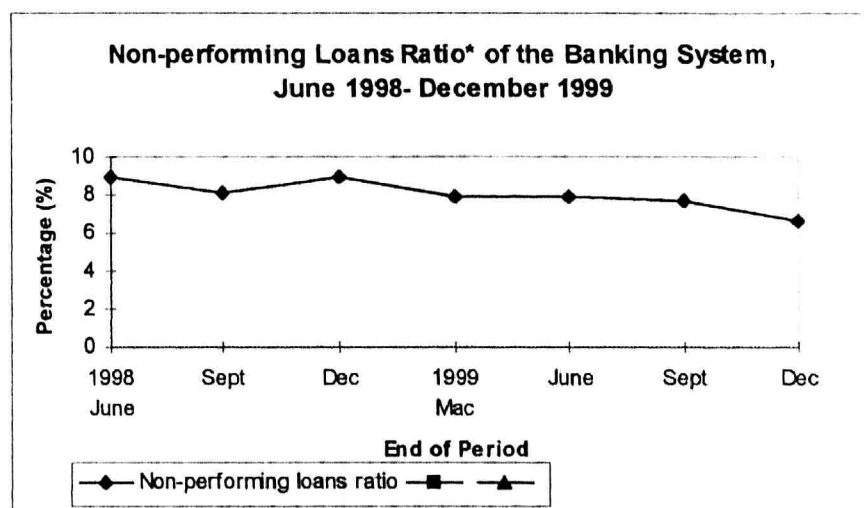
This chapter analyzes the effect of the recovery measures on the banking system. The recovery measures (which discussed in Chapter 4) undertaken by the banking system was to relieve banks from the shadow of bad loans, to recapitalize the banking sector and to create liquidity in the banking system which will encourage credit growth. Effectiveness of the recovery measures which have been implemented since September 1998 are to be discussed below.

5.1 Non-performing Loans (NPLs)

From June 1998 to end 1999, Danaharta has acquired and managed RM59.1 billion of NPLs from the banking system (Danaharta Annual Report, 1998 & 1999). This has reduced the NPL ratio of the banking system (based on the 6-months classification), by 25.8% between June 1998 and December 1999. This downward trend of the NPL ratio in the banking system is depicted in Chart 5.1 in page 50. The 25.8% drop in NPL ratio of the banking system was mainly contributed by the 21.9% and 37% decline in NPL ratio respectively for commercial banks and finance companies. However, the NPL ratio of merchant banks recorded an increase of 35.2% in the same corresponding period, as shown in Table 5.1 in page 50.

80.4% of the total RM59.1 billion NPLs acquired and managed by Danaharta between June 1998 and December 1999 was concentrated in the 4 main sectors as tabulated in the Table 5.2 in page 51, with breakdown of 32.1% from the BPS, 19.1% from purchase of shares and unit trust funds and 15.4% from the manufacturing sector.

Chart 5.1



Note: *the non-performing loans ratio is based on the 6-months classification

Source: Bank Negara Malaysia Monthly Statistical Bulletin, December 1999

Table 5.1: Non-performing loans ratio* of the Banking System

| NPL Ratio Period | Banking System | Commercial Banks | Finance Companies | Merchant Banks |
|---------------------|-------------------|---------------------|----------------------|-------------------|
| June | 8.9 | 7.3 | 13.6 | 9.1 |
| September | 8.1 | 7.6 | 9.2 | 8.3 |
| December | 9.0 | 5.9 | 11.9 | 10.9 |
| March | 7.9 | 6.4 | 12.3 | 11.2 |
| June | 7.9 | 6.4 | 11.8 | 13.8 |
| September | 7.7 | 6.7 | 10.5 | 13.3 |
| December | 6.6 | 5.7 | 8.6 | 12.3 |

Note: * The NPL ratio based on the six months classification

Source: BNM Monthly Statistical, December 1999

In terms of asset quality, NPLs in the purchase of shares recorded 58% improvement between September 1998 and December 1999 as compared to the BPS and Manufacturing sectors which only demonstrated a slight improvement in their asset qualities in the same corresponding period (Table 5.3, page 51).

Table 5.2: Total NPLs by sectors Acquired and Managed by Danaharta

| End of Sector | 1998 (RM billion / %) | 1999 (RM billion / %) | Total (RM billion / %) |
|---|----------------------------------|----------------------------------|-----------------------------------|
| Broad Property Sector* | 5.5 (27.7) | 13.5 (29.7) | 19.0 (32.1) |
| Purchase of Shares | 3.3 (16.8) | 8.0 (17.6) | 11.3 (19.1) |
| Manufacturing | 3.1 (15.7) | 6.0 (13.2) | 9.1 (15.4) |
| Financing, Insurance & Business Services | 2.0 (10.0) | 6.2 (13.6) | 8.2 (13.8) |
| Total | 19.7 (100.0) | 45.5 (100.0) | 59.1 (100.0) |

Source: Danaharta Annual Report, 1998 & 1999

Table 5.3: Banking System- NPLs by Sector (RM million)

| End of Sector | June 1998 | Sept 1998 | Dec 1998 | Mar 1999 | June 1999 | Sept 1999 | Dec 1999 |
|---|----------------------|----------------------|---------------------|---------------------|----------------------|----------------------|---------------------|
| Broad Property | 18,151.2 | 22,390.7 | 20,821.2 | 20,414.4 | 21,902.4 | 20,969.7 | 19,864.0 |
| Construction | 6,804.8 | 8,545.2 | 6,942.6 | 8,477.1 | 10,141.6 | 8,890.3 | 8,051.3 |
| Residential | 4,085.2 | 4,615.4 | 4,101.8 | 4,459.7 | 4,660.1 | 4,883.3 | 4,931.6 |
| Non-residential | 3,414.1 | 4,471.5 | 3,879.6 | 4,165.2 | 3,795.9 | 3,873.2 | 3,805.4 |
| Real estate | 3,874.1 | 4,637.0 | 4,796.1 | 3,312.4 | 3,294.8 | 3,322.9 | 3,075.7 |
| Purchase of shares | 8,483.4 | 11,276.9 | 5,609.8 | 6,371.3 | 5,970.8 | 5,609.8 | 4,746.4 |
| Manufacturing | 7,179.8 | 9,351.2 | 9,017.7 | 9,265.7 | 9,528.7 | 9,002.7 | 8,678.4 |
| Financing, Insurance & Business Services | 3,176.1 | 4,181.9 | 4,320.0 | 4,872.6 | 4,772.7 | 4,508.8 | 4,041.7 |

Source: BNM Monthly Statistical Bulletin, December 1999

In addition, the CDRC has resolved the debts of 16 companies totalling RM13.1 billion, leaving it with some RM16.9 billion worth of debt of 29 companies in the final stages of restructuring as at December, 1999 (Table 5.4, page 52). This enable the companies repay their loans and reduced NPLs of the banking system.

Table 5.4: Status of CDRC Cases (as at December 31, 1999)

| Status | No. Of cases | % of total | Total Debts | % of total |
|-----------------------------------|---------------------|-------------------|--------------------|-------------------|
| Resolved | 16 | 25.8 | 13,092.22 | 38.3 |
| Outstanding | 29 | 46.8 | 16,853.84 | 49.3 |
| Withdrawn/ trasferred/rejected | 17 | 27.4 | 4,258.79 | 12.5 |
| Total | 62 | 100 | 34,204.85 | 100 |

Source: *The Star*, 19 January 2000

5.2 Profitability

After 15 months of expansionary monetary policy, some of the domestic banks are reclassified back to the black. As at 30 September 1999, Arab-Malaysian Merchant Bank (AMMB), RHB Bank and Southern Bank recorded a pre-tax profit compared to a pre-tax loss in the previous year as highlighted in Table 5.5 below.

Table 5.5: Pre-tax Profits for Financial Quarter Ended September 30, 1999

| Pre-tax Profits (RM million) | September 30, 1999 | September 30, 1998 |
|-------------------------------------|---------------------------|---------------------------|
| Malayan Banking | 403 | - |
| Public Bank | 268 | 28 |
| AMMB Holdings | 162 | (150) |
| Commerce Assets Holdings | 177 | 119 |
| RHB Capital | 203 | (39.4) |
| Southern Bank | 10.4 | (23.8) |
| Hong Leong Bank | 86 | 61 |

Source: *The Star*, November 30 1999

The banking system as a whole also recorded a pre-tax profit of RM5.3 billion as at December 1999 compared to a pre-tax loss of RM2.3 billion in 1998 (*The Star*, 30 March 2000). The profitability was mainly due to lower provisions for NPLs. Total outstanding loans provision reduced by RM320 million between December 1998 and December 1999 (Table 5.6, page 53).

Table 5.6: Banking System-Outstanding Loan Provisions (RM million)

| End of | Interest-in-suspense | Specific provisions | General provisions | Total |
|-----------|----------------------|---------------------|--------------------|--------|
| 1998 June | 4,689 | 12,300 | 8,726 | 25,715 |
| Sept. | 5,438 | 14,099 | 7,024 | 26,561 |
| Dec. | 6,336 | 16,444 | 7,963 | 30,743 |
| 1999 June | 6,236 | 15,953 | 6,926 | 29,115 |
| Sept | 6,532 | 16,939 | 6,947 | 30,418 |
| Dec | 6,915 | 16,527 | 6,981 | 30,423 |

Note: The loan provisions based on the six months classification

Source: BNM Monthly Statistical Bulletin, 1999

5.3 Capital Strength

The purpose of the incorporation of Danamodal is to recapitalize the banking system. As at June 1999, Danamodal has injected a total of RM6.4 billion to the banking institutions in the form of Subordinated Capital Loans (ESCLs). As a result, the risk-weighted capital ratio¹⁰ (RWCR) of the banking system has improved by 0.7% basis points from 11.8% to 12.5% between December 1998 and December 1999 as reflected in Table 5.7 in page 54. The RWCR is well above the minimum requirement of 8% which provides the banking system with a sufficient cushion to absorb any potential shocks to the economy.

¹⁰ Risk Weighted Capital Ratio (RWCR) refers to the ratio of capital base to risk-weighted assets.

Capital Base refers to total capital (Tier 1 Capital + Tier 2 Capital) after deducting investment in subsidiaries and holdings of other banking institutions' capital.

Assets by Risk Weights refer to the value of the assets (both on and off balance sheet) against their allocated risk-weights. Five risk-weights are used-0%, 10%, 20%, 50% and 100%.

Tier 1 Capital refers to paid-up capital, non-cumulative perpetual preference shares, share premium, statutory reserve fund, general reserve fund, retained profits, surplus / loss arising from sale of fixed and long-term investments as well as minority interests.

Tier 2 Capital refers to hybrid capital instruments, minority interest arising from preference shares, subordinated term debt, revaluation reserves and general provisions for bad and doubtful debts.

Table 5.7: Bank System - Constituents of Capital

| End of | 1998 (RM million) | 1999 (RM million) | Changes (RM million) | Changes (%) |
|---|-------------------------|-------------------------|----------------------------|----------------|
| Tier-1 Capital | 41,941 | 43,829 | 1,888 | 4.5 |
| Tier-2 Capital | 18,298 | 15,008 | -3,290 | -18.0 |
| Total Capital | 60,239 | 58,837 | -1,402 | -2.3 |
| Asset by Risk Weight: | | | | |
| 0% | 87,929 | 121,707 | 33,778 | 38.4 |
| 10% | 26,160 | 21,735 | -4,425 | -16.9 |
| 20% | 109,770 | 103,670 | -6,100 | -5.6 |
| 50% | 62,452 | 67,828 | 5,376 | 8.6 |
| 100% | 415,057 | 381,813 | 33,244 | 8.0 |
| Total risk-weighted asset | 470,853 | 438,643 | -32,210 | -6.8 |
| Risk Weighted Capital Ratio Banking System | 11.8% | 12.5% | 0.7 | 5.9 |

Source: BNM Monthly Statistical Bulletin, December 1999

In line with the pre-tax profit of banking system, the Tier-1 Capital increased by RM2 billion (4.5%) to RM44 billion between December 1998 and December 1999 (Table 5.7 above). However, the Tier-2 Capital reduced by RM3 billion (18.0%) due to the lower provision in NPLs. The reduction in Tier-2 capital which outpaced the increase in Tier-1 capital has attributed to the 2.3% drop in the total capital between December 1998 and December 1999.

Banking system's total risk-weighted assets improved by 6.8% as at December 1999. This was mainly due to the negative loans growth of 4.8% and the RM19 billion of NPLs acquired by Danaharta.

5.4 Lending Growth

After 15 months of implementation of the expansionary monetary policy, the money supply M1, M2 and M3 increased substantially by 39.7%, 15.6% and 12.1%

respectively between September 1998 and December 1999 as shown in Table 5.8 as below. The increase in money supply had encouraged credit growth in the banking sector.

Table 5.8: Monetary Aggregates: M1, M2 and M3 (RM million)

| End of Period | M1 | M2 | M3 |
|----------------|------------------|------------------|------------------|
| September 1998 | 51,769.2 | 286,080.8 | 387,742.2 |
| December 1999 | 72,318.2 | 330,708.2 | 434,556.3 |
| Changes | 20,549.0 (39.7%) | 44,627.4 (15.6%) | 46,814.1 (12.1%) |

Source: BNM Monthly Statistical Bulletin, December 1999

Bank's intervention rate was further reduced from 8% as at September 3, 1998 to 5.5% as at August 9, 1999 (Table 5.9 below). With the reduction in intervention rate, base lending rate of commercial banks and finance companies were subsequently reduced accordingly from 8.04% and 9.50% to 6.79% and 7.95% respectively as shown in Table 5.10 in page 56.

Table 5.9: Changes to BNM Intervention Rate

| Year | Date | Intervention Rate (%) |
|------|--------|-----------------------|
| 1998 | 3 Aug | 10.50 |
| | 10 Aug | 10.00 |
| | 27 Aug | 9.50 |
| | 3 Sept | 8.00 |
| | 5 Oct | 7.50 |
| | 9 Nov | 7.00 |
| 1999 | 5 Apr | 6.50 |
| | 3 May | 6.00 |
| | 9 Aug | 5.50 |

Source: BNM Statistical Monthly Bulletin, December 1999

Table 5.10: Interest Rates of Banking Institutions (Percentage %)

| | | End 1998 | End 1999 | Change |
|-------------------|----------------------|-----------------|-----------------|---------------|
| Commercial Banks | Base Lending Rate | 8.04 | 6.79 | 1.25 |
| | Average Lending Rate | 9.72 | 7.75 | 1.97 |
| Finance Companies | Base Lending Rate | 9.50 | 7.95 | 1.55 |
| | Average Lending Rate | 11.76 | 11.23 | 0.53 |
| Merchant Banks | Base Lending Rate | - | - | - |
| | Average Lending Rate | 10.71 | 7.59 | 3.12 |

Source: BNM Monthly Statistical Bulletin, December 1999

The encouraging environment in terms of lower interest rate had boost credit growth in terms of new loans approved. Total new loans approved by the banking system recorded approximately two-fold increase to RM104.8 billion in 1999 as compared to RM65.1 billion in 1998 (BNM Annual Report, 1999).

On the other hand, loans repayments which increased by 24% (from RM270.5 billion in 1998 to RM335.6 billion in December 1999) outpaced the disbursement of approved credit facilities which recorded an increase of 28.7% (from RM251.1 billion in 1998 to RM323.2 billion in December 1999); has resulted a contraction in total loans and advances by RM 12.5 billion (BNM Annual Report, 1999).