Plenary 2

The Rapidly Developing Economies

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Challenges in Rapidly Developing Economies – The Malaysian Experience
Agenda

• The Malaysian Experience
• Main Success Factors
• Challenges Faced
• Meeting the Challenges
The Malaysian economy has undergone profound structural changes.

In 1957 - agriculture, forestry & fishing = 40% of GDP.

By 1987 - manufacturing played a more dominant role.

Going forward - focusing on enhancing value-add of productive activities.

In 1957 - agriculture, forestry & fishing = 40% of GDP.
Malaysia’s GDP growth has been relatively robust since the 1960s

- GDP grown by average 6.3% per annum in this period
- GNP per capita grew 18 times since independence → from US$200 in 1957 to US$3,600.8 in 2002
- By 2002, unemployment fell to 3.5% (1970: 7.7%), and incidence of poverty fell to 4.5% (1970: 52.4%)

Average annual real GDP growth

Source: Bank Negara Malaysia
High savings rates enabled strong economic growth with relative stable price

Malaysia has a relatively high savings rate

Gross national savings in 2001 (% of GDP)

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This has helped keep inflation low

Average annual CPI growth in Malaysia

- 1963-1972: 1.6%
- 1973-1982: 7.0%
- 1983-1992: 2.7%
- 1993-2002: 3.0%

Inflation pushed up by global oil price shocks

Source: IMF

Source: Bank Negara Malaysia
Social progress to ensure “growth with equity”

- New Economic Policy (NEP) introduced in 1970 aimed at:
  - Promoting national unity
  - Restructuring society
  - Eradicating poverty
  - Equitable distribution of wealth
  - Public sector to play major role

- Targets:
  - No deprivation of economic benefits to any ethnic group / sector of society
  - Employment patterns at all levels to reflect racial composition of the population

Population below national poverty line

<table>
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<th>Year</th>
<th>% of population</th>
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<td>1970</td>
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<td>1980</td>
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<td>1990</td>
<td>17.1</td>
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<td>2000</td>
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Source: Economic Planning Unit, Malaysia
Diversifying the economy by pursuing industrialisation

- First Industrial Master Plan (IMP) outlined industrial strategy and established framework of developmental strategies to be undertaken from 1986-1995
  - To create a more broad-based manufacturing sector
  - To promote an export-led industrialisation strategy
Malaysia now has a widely-diversified production structure and range of exports

- Manufacturing accounts for 28% of GDP in 2002 (1960: 8%)
- In 2002, Electrical & Electronic goods comprise 51% of exports

Composition of GDP by sector

Source: Bank Negara Malaysia
“Malaysia Inc” policy to promote private sector as main engine of growth

- Privatisation of major govt entities:
  - Telecom services transferred from Telecom Dept. to Telekom PLC, which was successfully listed on the KLSE in 1990
  - National Electricity Board was corporatised and privatised in 1990; listed on KLSE in 1992

- Capital market provided efficient access to funding and facilitated social agenda on wealth creation

Private sector investment as % of total investment

Source: EPU
The capital market has been a key driver of growth over the years

Funds raised in the capital market (RM bil)
- New government issues
- New equity issues
- New corporate bond issues
- Nominal GDP (RHS)
Financial sector development

- The corporate sector increasingly turning to the capital market for funding needs
- In doing so, they reduce their over-dependence on the banking sector
- Ratio of the size of the capital market (equities and bonds) to banking sector assets is now 100% (at end-2002)

Sources: Respective central banks, World Federation of Exchanges, Bank for Intl Settlements
Development of a knowledge-based economy is important going forward

- New Development Policy (NDP) announced in 1991:
  - Led to formation of Multimedia Super Corridor in 1996
  - Formed the basis of “Vision 2020”
- 8th Malaysia Plan (5-year plan)
  - Achieving sustainable growth with resilience to meet challenges of globalisation and liberalisation
  - Facilitate devt of knowledge-based economy to raise value-added of all economic sectors
  - Priority to increase supply of quality manpower, enhance R&D
Snapshot of economic development since 1957

- 1957: Independence
- 1951: Employees Provident Fund set up
- 1956: Federal Land Development Authority (FELDA) set up
- 1959: Malaysia's Central Bank established
- 1960: Stock Exchange formed
- 1971: National Equity Corporation set up
- 1978: National Agriculture Policy formulated
- 1984: Industrial Master Plan introduced
- 1986: Industrial Master Plan introduced; Privatisation Master Plan implemented
- 1991: New Development Policy introduced; Privatisation Master Plan implemented
- 1997-98: East Asian financial crisis
- 2001: Capital Market, Financial Sector Master Plans introduced
- 2001: Capital controls fully removed

Real GNP/Capita (LHS) and KLCI (RHS)
The Malaysian Economy – Main success factors

**STABLE POLITICAL CLIMATE**
- Strong ruling coalition

**PLANNING & IMPLEMENTATION**
- National Agriculture Policy
- Industrial Masterplans
- Privatisation Masterplan
- National Economic Recovery Plan
- Capital Market Masterplan
- Outline Perspective Plans
- 1st – 8th Malaysia Plans
MAIN SUCCESS FACTORS
- Key Policies and Key Enablers

- Well Planned Structural Changes to Economy
  - National Agricultural Policy (Federal Land Development Authority)
  - Development of Manufacturing Sector (Malaysian Industrial Development Authority)
  - Development of Knowledge Based Economy (Multi-media Super Corridor)

- Mobilisation of Savings to Fund Development
  - Compulsory Savings (Employees Provident Fund)
  - Voluntary Savings & Investments (National Equity Corporation, Pilgrim Savings Fund Board)

- Development of Private Sector as Main Engine of Growth
  - Privatisation Masterplan (Economic Planning Unit)
  - Regional Development (State Economic Development Corporations)
MAIN SUCCESS FACTORS
- Key Policies and Key Enablers (Con’td)

Capital Market as Key Driver of Growth

- Access to Cheaper Funds (Kuala Lumpur Stock Exchange)
- Capital Market Masterplan (Securities Commission)

Economic Growth with Equity

- New Economic Policy (Foreign Investment Committee)
- Distribution of Wealth (National Equity Corporation, Bumiputra Participation Unit)
Challenges Faced

• National Savings Rate is too high at 39.7% and is stifling domestic consumption.

• The Statutory Pension Fund grew to RM203.7 Billion by 2003 (40% of the Exchanges’ Market Capitalisation) has created liquidity in the Capital Market.

• The Government’s hand in the economy is still strong. The Privatisation Masterplan has resulted in 7 out of the Top 10 largest firms being Government-linked, and 34% of total market capitalisation of the Exchange (or more than half of Malaysia’s GDP)!

• The Industrial Masterplan was too successful, now more than 51% of Malaysia’s exports are electronic and electrical goods, accounting for more than the exports of oil and gas, palm-oil, timber, pepper and other exports combined!!.
Move Challenges!

The Asian Financial Crisis of 1997/98 highlighted the vulnerability of the Malaysian Financial sector e.g.

• The export boom internationalised the Ringgit, exposing it to manipulative attacks.

• Mismatch of borrowings to income by corporate sector.

• Exposure to short term capital flows without shareholder value and corporate governance.

• Unconsolidated markets and intermediaries.
Meeting the Challenges

- Liberalisation of credit to encourage domestic consumption.
  - Savings rate has stopped growing and declined to 35%
- Review of Pension Funds Industry still on-going.
  - Other provident funds being promoted.
- Government Linked Companies are being re-vamped.
  - New CEOs with performance incentives, more independent boards,
Meeting the Challenges (Cont’d)

- Government Linked Companies are being re-vamped.
  (Cont’d)
  - Government looking at reducing its shareholding in the GLCs.

- The 9th Malaysia Plan will push for a more knowledge-based economy.
  - This will reduce over-dependence on export of E & E goods
Recovery from the Financial Crisis

  - Protecting the Malaysian Ringgit from attacks.
  - Capital controls, Ringgit-peg.
  - Danaharta, the National Asset Management Company, handled non-performing loans.
  - Recapitalisation of weakened banks through Danamodal.
  - Revamp of Corporate Governance values, launch of Code of Ethics.
Recovery from the Financial Crisis (Con’td)

• After recovery, launch of Capital Market Masterplan and Financial Sector Masterplan.
  - Improving Corporate Governance and Investor Protection
  - Developing the Bond Market to reduce mismatch of borrowings to Income.
  - Consolidating, demutualising and listing the Malaysian Exchanges.
  - Consolidating and strengthening the intermediaries.
  - Improving areas to Capital Market by introduction of REITS etc.
A wide range of initiatives already completed or actively in progress

- Disclosure-Based Regulation
- Corporate governance reforms
- Enforcement
- Market-based regulation
- Training & education
- Consolidation & demutualisation of market institutions
- Bond market development & asset securitisation
- Islamic capital market
- E-commerce
- Stockbroking consolidation & Universal Brokers

Capital Market Masterplan
Corporate Governance

Capital Market Masterplan (2001)
- Holistic framework for longer-term market development, also covering corporate governance

Shareholder activism
- Minority Shareholder Watchdog Group
- Enhanced legal provisions for recourse

Professional management of companies
- Mandatory accreditation programme for directors
- Regulatory reforms to encourage participation of non-executive directors
- Change in management in some companies

Malaysian Code on Corporate Governance (2000)
- Principles and best practices
- Statement of extent of compliance with Code required by revised KLSE Listing Rules (2001)

Malaysian Accounting Standards Board
- Frameworks for accounting standard setting, compliance and enforcement are internationally benchmarked

Audit Quality
- Guidelines on Internal Audit function released July 2002

Enhanced Enforcement Focus
- Increased emphasis on enforcing accountability of principal officers/controlling stakeholders

Transparency & disclosure
- Quarterly reporting (1999)
- Enhanced disclosure in prospectuses

Investor Protection

Report on Corporate Governance (1999)
- Some 70 recommendations for improving CG practices
Bond market development has been significant...

- **Enhanced efficiency of issuance process**
  - Revised issuance framework → regulatory requirements streamlined

- **Broadened participation**
  - Reduced minimum investment in government bonds from 20% to 10% for insurance co.s
  - Introduction of guidelines for UBs to deal directly in unlisted PDS

- **Asset-backed securitisation framework**
  - Exemption on stamp duty and real property gains tax on transactions
Bond market development has been significant, broadening the sources of financing.

Funds raised in the Malaysian capital market

- Government Securities
- Private Debt Securities
- Equity
- Total funds raised as a % of GDP

In 2004

- Private Debt Securities: 39%
- Government Debt Securities: 54%
- Equity: 7%

Source: Bank Negara Malaysia
New funds raised in the capital market (1995 – 2002)

- New public sector debt issues
- New private sector debt issues
- New equity issues

New funds raised in the capital market in 2002

- Public sector debt: 28%
- Private sector debt: 53%
- Equity: 19%

Proportion of corporate debt over total funds raised has doubled to 53%, from 25% in 1992

...helping co.s raise funds amid challenging conditions
Thank you