A speculative attack was the cause for the Asian financial crisis in 1997, in which Malaysia itself was caught in this crisis. Asian countries suffered heavily as a result of the financial crisis in which none of them managed to completely evade from the crisis. Later, severe economic problems; a number of the multinational companies and enterprises had gone bankrupt and this increased the unemployment rate. In order to overcome this problem, the Malaysian government had taken several steps which involved the usage of internal and external resources in order to overcome this financial crisis and bring the economy back to its normal value. The financial crisis was worsened due to wrong policy responses, anti-market rhetoric, panic, and excessive risk-taking which damaged the balance sheets of banks and corporate sectors. The financial crisis affected the economy, society and politics in Malaysia, which made it hard to recover from the slump in just a few years. A few recovery plans were implemented by the Malaysian government; reengineering the financial systems, corporate sectors, capital controls as well as short to medium term outlook. Ten years after the financial crisis of 1997-1998, Malaysia’s economy was at its strongest, and had greater economic flexibility that enabled the shift to new areas of growth and thus sustained the
developmental momentum. This scenario showed that the recovery plans geared towards battling the crisis was successful, as Malaysia stands strong in the eyes of the world.

**Keywords:** Financial Crisis, Speculative, Financial System, Financial Institution

1. Introduction

The financial crisis was first felt in Thailand on July 2, 1997, in which later spread to Malaysia, Indonesia, Philippine and Singapore; not forgetting Hong Kong, Taiwan, Korea, Japan and China. None of the countries in East Asia were spared from the impact of the financial crisis. A year later, the financial crisis had spread its wrath to Russia and Latin America, in which it causing a sharp depreciation in their currency values and collapsing the stock market. This had caused a decline in exports, and resulted in a slowdown of economic growth, as well as an alarming rate of unemployment. Moreover, the East Asian region itself was also suffering from internal economic problems which caused a lot of companies and enterprises to file the bankruptcy. The governments concerned had no effective means of mitigating the impact of the financial crisis (Yu & Xu, 2000).

The Malaysian government had resorted to public borrowing, which means the government had to find economic sources from borrowing or public debt, essentially through internal or external sources of money, capital, manpower, expertise and so forth. The internal sources of the Malaysian government in public borrowing were from the Central Bank as well as Financial and Commercial Banks. Moreover, the Malaysian government had introduced Danaharta, Danamodal, Merger of Financial Institutions, Corporate Debt Restructuring Committee, and Bond Market in order to overcome the financial crisis internally. However, the internal sources were not enough to overcome the impact of financial crisis and this forced the Malaysian government to resort to external borrowing.


According to Zubair Hadan (2003), the Malaysian economy had largely been in a good condition since independence. In recent years, it had enjoyed full employment, considerable stability in the price level, and high growth, with the average rate being 8.7 % during the time period of 1990-1997. Malaysia, even with its small mass, was ranked as the 35th top country in 1997 with...
reference to the size of both the aggregate and per capita GNP. It essentially was a trading country, in which exports and imports played a major role in the progress of the economy. Thus, the economy was highly open, and was much susceptible to external disturbances. The foreign capital had continuously supplemented domestic savings in order to sustain high investment rates, to bring forward growth. Malaysia wanted to retain the advantage of its achievements in economic stability, but it was no easy task, especially because of the international economic policies had assumed political overtones. The high performance of the Malaysian economy that was maintained over the decades, without markets or technology or even the core capital being local, cannot be undermined. However, in 1997 the financial crisis came to light, and essentially being a short-term phenomenon, it caused the crash of the Malaysian economy.

Among the factors that caused the financial crisis in Malaysia were speculative attacks, deficiencies in risk management, form of corporate governance and equity markets, and the legal infrastructure (Colin & Fancis, 2003). The Malaysian economic was vulnerable due to the unsustainable pace of economic growth and over-valued exchange rates. The relationship between firms, government and banks in Malaysia in the financial crisis period cannot be describe as good compared to other Asian countries. There was no clear policy on directed lending to big firms, and to that extent one cannot say that the financial constraints on big firms were weak. The government came out with a high growth policy based on a high ratio of investments to gross domestic product complemented with the promotion and support of certain mega projects, which led to implicit assumptions by lenders that the government would not let those projects fail, which was helped by lending decisions by bankers based on not only a project’s cash flow but also on collateral and implied government support. The over-investment was fueled by an aggregated demand to outstrip aggregated supply, with a consequently persistent external deficit. Moreover, it had also led to a poorer cash flow and more problems of loans.

Later on, the deficiencies in risk management caused by the financial crisis had also affected the Asian region, including Malaysia; with huge mismatches between the asset and liabilities of enterprises, leading them to assume excessive liquidity, interest rate and currency risks. The currency mismatches had also happened in Malaysia, with the exchange control regime requiring approvals for foreign currency borrowing. Several prominent corporations were allowed to raise foreign currency loans, although they only had ringgit cash flows. Due to the sharp ringgit depreciation, these corporations were faced with massive foreign exchange losses or insolvencies because of their currency mismatches and inabilities to hedge exposures. Moreover, the banking system in Malaysia was very risky and this caused bad macroeconomics.
It was an explosive mix for any corporate entity which had over-borrowed and assumed too much maturity period or currency mismatches. The high risk nature of banking in distinction to fund management had risen from its high gearing and massive asset liability mismatches, and in particular, from its tendency to borrow for a short period and lend for even longer. The over-dependence on banks in Asia was caused by their over-protection, as well as by the over-regulation of capital markets, and had also affected the Malaysian financial system. This had caused the under-development of non-banking financial institutions, capital markets, and risk management products, risk intermediaries, trading and market-making, which had functioned under inconsistent macroeconomic policies (Colin & Fancis, 2003).

The form of corporate governance and equity market was another factor that caused the financial crisis to occur in the Asian region. Asia was characterized by a concentrated shareholdings system. Non-competitive product markets and weak legal protection as well as governance by large shareholders rather than managers had reduced opportunities for managements to specialize, poor diversification of investments, and increased risks of expropriation of outside shareholders by insiders. The concentrated shareholding had resulted in a less-developed equity market. In Malaysia, the equity market was very sizeable (Colin & Fancis, 2003). The news of the outbreak of the regional crisis of corporate governance breakdowns, and the weak responses to these regulators had led to a huge stock market sell-down. The problem was compounded by new rules on scrip delivery which was imposed to check the sell-down, even though these rules were scrapped later on. However, the initiatives taken to facilitate the development of suitable mechanisms for improved corporate governance were taken only much later, and doubts persisted on issues related to enforcement.

Lastly, the legal infrastructure system in Asia, and more specifically Malaysia, was plagued by inadequate reliance on markets due to its weak infrastructure in private contracting, which in turn was attributed to poor laws or weak enforcement of those laws. The investment decisions were based on the relationship model rather than on market prices, whereas contracts needed not manage the supply of capital relative to investment opportunities, which were limited. In order to protect their interest, foreign lenders to Asian corporations and banks invariably made short-term loans; relying on the threat of not rolling over the loans to ensure borrowers serviced the latter. When the Asian economic crisis occurred, a majority of the lenders took back their loans and this caused the capital to outflow without any control. This was considered to be a rational response by the lenders in taking their time and going to courts to enforce their rights; given the poor laws and weak enforcement (Colin & Fancis, 2003).
2. Impact on the economic, society and politics

Malaysia faced the financial crisis on July 1997, and several impacts or consequences were observed, especially on the economic, social, and political aspects in Malaysia, and these are explained below.

2.1 Impact on the Economic

The financial crisis had an impact on the economy of Malaysia. During the financial crisis, the value of the ringgit had declined. Previously, in April 1997, the ringgit was equivalent to 2.42 of the U.S. dollar, whereas later on the value of the ringgit against the dollar depreciated by almost 50 per cent, hitting a high of RM 4.88 to the U.S. dollar on January 7, 1998 (Mohamed Ariff & Syarisa Yanti, 1999). Besides that, the composite index (CI) of the Kuala Lumpur Stock Exchange (KLSE), which was the third largest stock exchange in the region after Tokyo and Hong Kong, fell precipitously from 1,077.3 points in June 1997 to 262.7 points on September 1, 1997 (Syarisa Yanti, 2002). Between July 1997 and mid-January 1998, approximately U.S. $225 billion of share values were wiped off and between July 1, 1997 and September 1, 1998, market capitalization in the KLSE fell by about 76 per cent to RM 181.5 billion. In the end, Malaysia experienced the biggest stock market plunge among the Asian countries amid the crisis. The financial crisis had also caused the real sector of the economy to feel the negative effects of the crisis. Weak stock prices, the property market slump, and the net contraction impact of the ringgit depreciation together led to a negative wealth effect, which resulted in a general contraction of domestic demand. Consequently, domestic-oriented industries, such as the construction and services sectors, were severely hit by the economic crisis. Meanwhile, the increase in non-performing loans (NPLs) of the financial sector was reflected in a sharp downturn in borrowing and financing, bringing about tight liquidity (Syarisa Yanti, 2002).

Other than that, in the foreign direct investment (FDI) levels, as measured by the value of applications received in the manufacturing sector and applications for investment incentives from the hotel, tourism, and agriculture sectors by the Malaysian Industrial Authority (MIDA), it displayed a declining trend over the period January until December 1998. Thus, it can be concluded from the information above that the investors tried to reduce their investment in order to avoid any lost during the time of crisis. The public sector itself had its share of impacts from the financial crisis. In the public sector, a decrease in both expenditure and investment was initially expected, following the government’s intention of reducing the budget for operating expenses by 18 per cent, as well as cancelling or postponing several mega-projects (Syarisa Yanti, 2002). Other than that, the ministers accepted a
10 percent pay cut, while the salaries of senior civil servants were slashed by 10 percent in order to reduce the government’s expenditure. Salary increases for higher categories of civil servants were also frozen (Ching, 1999). This was part of the government’s effort to reduce the government’s expenditure in order to stabilize the economy.

Another impact from the crisis was the declining of imports of luxury goods, as domestic demand slowed due to the depreciation of the ringgit. Nevertheless, exports especially in the resource-based sector had increased, and displayed a continued uptrend in ringgit terms. However, when converted into U.S. dollar terms, most of the major export categories displayed a downward trend. In October 1997, the government forecasted a growth rate of 7 per cent for 1998, but subsequently adjusted it downward to four until five per cent in December 1997, and again to two until three per cent in March 1998 (Mohamed Ariff & Syarisa Yanti, 1999). Thus, this showed that the economic growth was not stable because of the financial crisis.

2.2 Impact on Society

For Malaysia, the social issues that assumed primary importance in the post-crisis scenario were raising unemployment, inflation and poverty levels, as well as reduced access to quality education and health benefits (Ching, 1999).

2.2.1 Inflation

Amidst the financial crisis, the inflation rate increased from 2.7 per cent in 1997 to 5.3 percent in 1998 (Syarisa Yanti, 2002). The increase in food prices was the main reason for the rise in the inflation rate, as food items accounted for 34.9 per cent of the weight in the overall Consumer Price Index (CPI) basket. Increase in the prices of controlled imported essential items such as sugar, cooking oil and flour was roughly 20.0 per cent. Among the non-food sub-groups, the price increase for miscellaneous goods and services and medical care and health expenses, had together accounted for 7.5 per cent of the weight in the consumer basket. The second largest sub-group, accounting for 21.1 per cent of the weight in the CPI basket, was for gross rent, fuel, and power. Prices of clothing and footwear registered a marginal increase of 0.4 per cent. Prices of transport and communication, the third largest subgroup, accounting for 17.9 per cent of the weight in the consumer price basket, declined by 0.1 per cent (Syarisa Yanti, 2002). The higher rate of inflation caused rising unemployment rates, lower wages, and reduced real incomes.
2.2.2 Unemployment

The financial crisis resulted in higher rates of unemployment. Prior to the onset of the financial crisis, Malaysia had suffered from a labour shortage, which caused the presence of well over a million migrant workers (Ching, 1999). During the financial crisis, between January and December 1998, the total number of workers retrenched was 83,865. Based on data collected from January to September 1998, almost 88.1 per cent, or 52,834 of workers were retrenched. Data compiled by the Ministry of Human Resource showed that more employers adopted alternative measures, such as pay cuts, temporary layoffs, and voluntary layoffs, before resorting to permanent layoffs during the period of August until December. According to Syarisa Yanti (2002), of those retrenched between 1 January and 26 July 1998, 43,967 persons, or 89 per cent, were Malaysian nationals, while the remaining 11 per cent consisted of foreign nationals.

2.2.3 Impact on Poverty and Income Distribution

Based on the findings of the Household Income and Expenditure Survey 1997, it can be concluded that the incidences of poverty cases in Malaysia declined until 1997. This decline was in both urban and rural areas. Similarly, the survey also indicated that the incidences of hardcore poverty cases had declined. However, when the financial crisis took place, the real household income fell given the rise of inflation in 1998. Assuming a 6 percent increase in the inflation rate, the report had also estimated that the incidence of poverty including citizens and non-citizens in 1998 had increased by 399,100 households (8 per cent of total), up from 346,000 households (6.8 per cent of total) in 1997 (Syarisa Yanti, 2002). Meanwhile, the incidence of hard-core poverty was estimated to have increased from 1.4 per cent in 1997 to 1.7 per cent, or 82,900 households, in 1998.

In terms of income distribution, the rapid economic growth experienced by the country during the booming period of 1990 until 1997 increased the disparity in income distribution, with growth benefiting the top 20 per cent of the population (mainly urban households) more than the bottom 40 per cent (mainly rural households). In 1998, the household income in urban areas and of the top 20 per cent of households fell slightly. Concurrently, incomes from the agricultural sector grew at a faster rate than 1997, owing it to higher prices for palm oil and increased production of food crops in response to higher import costs. Thus, the mean income of the bottom 40 per cent of households, especially in the rural areas, remained stable, due to their ability to diversify their sources of income. Consequently, the urban-rural income imbalance and overall income inequality improved slightly in 1998, thereby reducing the widening gap experienced from 1996 until 1997.
2.2.4 Health

In Malaysia, the provision of health care is primarily the responsibility of the public sector. However, during the crisis, private sector hospitals and clinics recorded a drop of 15 until 50 per cent in demand, mainly due to the higher net costs associated with attending private clinics and hospitals. Following the crisis, a 30 per cent rise in the cost of imported drugs, which accounted for 60 per cent of all drugs used in the country was recorded. Based on reports of increased patient loads of about 18 until 20 per cent experienced by government hospitals, it was safe to conclude that a proportion of private sector patients transferred their patronage to the public health care system. This placed additional pressure on the public health care system as well as on the already limited resources of the government. In addition, in the public sector, there was no real threat to the budget allocation for the health sector even at the initial stages of the crisis, when the government was still pursuing its fiscal austerity policies. The budget allocation for the health sector in fact increased slightly from 6.3 per cent in the national budget of 1997 to 6.6 percent in 1998 (Syarisa Yanti, 2002). Although there was an increase in the overall government budget allocation, allocations for public health and medical treatment declined.

2.2.5 Education

Education has always been the backbone of Malaysia’s developmental strategy. The government is committed to develop this sector, whereby it continuously receives high budgetary allocations for operational and developmental expenditure. However, the economic crisis disrupted the pattern of government expenditure on education, at least in the short-term. Initially, the government announced a cutback of its expenditure by 2 per cent as part of its strategy to handle the crisis; however, in December 1997, this cutback was increased by an additional 18 per cent.

Other than that, the fall in the value of the ringgit meant that many families could go longer afford to send their children abroad for higher education. There was anecdotal evidence that a number of those already enrolled in universities abroad had to drop out. For example, according to the British Council survey, the number of Malaysian students enrolled in British universities had fallen by over 44 per cent in 1998, to 2,127 compared to 3,821 in 1997. At the same time, the government encouraged students to stay in Malaysia for advanced studies, but Malaysian universities simply did not have the capacity to absorb all of them. In 1998, 64 per cent of students applying for university places were turned down in which there were 112,000 applications received for the 40,222 places that were available (Ching, 1999).
2.3 Impact on Political System

Politics was not spared from the impacts of the financial crisis. Although Malaysia did not experience the far reaching political change like those which occurred in Indonesia, in as Malaysia had no change in the constitutional structure and coalition, it did not mean that the political system had not faced any problem. During this time period, the dominant party, which was United Malay National Organization (UMNO), had also faced some turbulence. The factor that brought instability to the party was the incipient split between the deputy president of UMNO, Anwar Ibrahim and the president, Tun Mahathir Mohammad which came to light after the crisis began. This split, which many observers believed had started in 1993 when Anwar Ibrahim overwhelmingly defeated Ghafar Baba for the deputy presidency of the part. This had greatly unnerved Mahathir who was then the president (Lee & Tham, 2007). Mahathir later saw Anwar as a threat and confessed that they were not meant to get along politically.

During the crisis, Anwar and his supporters tried to challenge Mahathir’s authority in two ways. Firstly, Anwar’s supporters made the remark that Mahathir’s time was up and used words such as like corruption, cronyism, and nepotism to make Mahathir step down as the president of UMNO (Lee & Tham, 2007). Secondly, was the championing of Anwar by the accepting international Monetary Fund (IMF) loans (Lee & Tham, 2007). However, Mahathir rejected the loan from the IMF. Due to action by by Anwar, Mahathir responded by having Anwar convicted of the sodomy and corruption (Lee & Tham, 2007). The charge of sodomy was successful enough that it resulted in Anwar’s resignation. The expulsion of Anwar Ibrahim as the deputy prime minister in 1998 was the catalyst for enhanced activism. There was increased momentum in the campaign for greater transparency, more political freedom, and abolition of the internal Security Act, which permitted detention without trial (Colin & Francis, 2003, p.69). Anwar retaliated by taking to the streets before with his supporters, with the message of reformation, and from this Anwar won much sympathy in Western countries with his message of reformation (Lee & Tham, 2007). Thus, the dispute between Mahathir and Anwar caused instability in the political arena especially during the time of crisis.


According to Samuel (2001), there were several actions taken by the Malaysian government to overcome the financial crisis during 1997/1998, such as using the extent of the current recovery, restructuring in the financial and
corporate sectors, the role of selective capital controls, and the short to medium term outlook.

3.1 Extent of Economic Revitalization

In 1998, Malaysia’s current account surplus was RM34 billion or 13% of the GNP (Gross National Product). Strong external sectors were reflected in the improved international reserves position such as in August 1998, in which Malaysia had reserves of US20.2 billion, and these had increased to US31.7 billion in July 1999. Besides that, the level of interest rates had also decreased significantly. For example, in June 1999, the base-lending rate was 7.24% as compared to an all time high of 12.27% in June 1998. It meant that the crisis had not recorded a higher impact in the inflation rates in Malaysia. The consumer price index (CPI) increased from 2.7% in 1997 to a high of 6.2% in June 1998.

3.2 Financial and Corporate Sector Restructuring

The next plan involved two phases of the reform process, which was stabilization and reformation. In terms of the reformation process, several agencies were established to face the financial crisis such as Danaharta which had objective to purchase the non-performing loans (NPLs) and Danamodal to recapitalize financial institutions in the stabilization phase. The reformation phase consisted of corporate sector restructuring (Corporate Debt Restructuring Committee), merger of financial institutions, and the development of the bond market.

Danaharta

Danaharta, an asset management company, was established in June 1998. Its main objectives were to remove NPLs from the balance sheets of financial institutions at fair market value and to maximize their recovery value. This will free the financial institutions from their debts that had prevented them from carrying out their intermediation functions. Danaharta successfully completed the first phase of its mandate; to deal with NPLs. Later, Danaharta had acquired a total of RM 23.1 billion NPLs, amounting to 31.8% of the total NPLs in the banking system.

Danamodal

Danamodal had injected RM6.4 billion into 10 financial institutions. As a result, the capital adequacy ratio of the banking system increased to 12.7%. The capital injection was accompanied by absorption of losses by shareholders through reduced shareholding in the institutions, change in the composition of the boards of directors and/or change in the management. Danamodal had also appointed their representatives in the recapitalized institutions to
ensure that these institutions were managed prudently and efficiently as well as to institute changes that will strengthen the institutions. Danamodal’s influence on the recapitalization of financial institutions accelerated the institutional merger process.

**Merger of Financial Institutions**
The plan to merge 58 financial institutions into 6 groups, announced on 29 July, was an important component of financial sector restructuring. This initiative was consistent with the earlier plan of financial institutional mergers, which was announced at the beginning of the crisis. Currently, the merger timetable was accelerated, and the restructuring was more comprehensive. The 6 banking groups had merchant banking and securities trading, in addition to commercial banking and financial company activities. There was an overall agreement that bank mergers were necessary as it would prepare the domestic banks for the eventual opening of the financial services.

**Corporate Debt Restructuring Committee (CDRC)**
The CDRC had shown some progress, but restructuring of the corporate sector remained slow. The CDRC sought to assist companies to restructure without governmental support. Progress had been slow because the process needed the agreement of all creditors. Banks, in particular, had been reluctant to settle without full repayment. Negotiations had therefore been long because even disagreement from one creditor would jeopardize the whole process.

**Bond Market**
As Malaysia was expected to resume its growth after the crisis, it was important to develop an environment where capital can be mobilized to finance long-term investment and to provide a better match between risks and returns. Thus, the development of a bond market was viewed as a priority because it served as an alternative source of raising capital. In view of the importance of this issue, the Malaysian government had established a committee to expedite the development of the bond market.

**3.3 Selective Capital Controls (SCC)**
The SCC was a measure to deal with a situation of extreme uncertainty. Its primary objectives were to bring stability in the exchange rate, and regain control of monetary policy. It had helped to lower interest rates, and support a fiscal stimulus such as liquidity in which it fueled the domestic economy. It had also provided a shield for carrying out reforms, particularly banks’ recapitalization. Moreover, contrary to some expectations, FDI had continued to flow in. Critics had predicted that Malaysia would use SCC to relate the economy, and bail out companies.
3.4 Outlook for the Malaysian Economy

The return to growth came from external sectors, which was a result from the strong US economy, as well as the recovery by Asian economies. Thus, even if there was a threat of potential weaknesses from the US economy, the revived Asian economies were most likely to counter balance any slack of export demands from the US market. Furthermore, the intra-regional trade forms a substantial portion of the Malaysian export and the recent recovery of the Japanese and other Asian economies would benefit Malaysia. The performance of Malaysia’s external sector shows that Malaysia’s exports were very competitive. The rate of Malaysia’s export growth was very much higher than the other East Asian economies.

3.5 National Economic Action Council (NEAC)

This was one of the approaches that were taken by the Malaysia government in order to overcome the financial crisis. The NEAC was establishing 1998 as a consultative body to deal with the immediate issues of tackling the Asian Financial Crisis in 1997. It had been instrumental in turning the economy around through pre-emptive strategies to counter the adverse impacts. Some of NEAC’s objectives were to stabilize the ringgit, restore market confidence, maintain financial stability, strengthen economic fundamentals, continue socioeconomic agenda and restore sectors badly affected by the crisis (Mahathir, 2003).

3.6 National Economic Recovery Plan (NERP)

This was another approach that was taken by the government in facing the financial crisis of 1997/1998. The National Economic Recovery Plan provided the opportunity for economic fundamentals to reassert themselves. Allowing for the lagged impact of the measures, Gross Domestic Product expanded by 4.1% in the second quarter of 1999. The easier monetary policy led to a considerable easing of the liquidity crunch. From the macro perspective, a more important development was the improvement in both consumer and business sentiments (Mahathir, 1999).

3.7 World Bank

There are various external resources that can be used s a tool to help countries in crisis such as International Monetary Fund (IMF) and World Bank. Countries such as Thailand, Indonesia and South Korea viewed IMF as their final way to resolve their financial problem. This was because they had no other way out, although they all knew about the consequences of relying on IMF; such as they must follow the conditions given by IMF, and IMF will take over
the decision making on their finance over the years, until they were able to pay back the loans to the IMF (Khor, 1998). However, Malaysia had thought out of the box and had its own solutions. Malaysia preferred to use World Bank as their external resource rather than IMF which could be damaging in the future. Malaysia had collaborated with World Bank in order to maintain the economy of this country. For example, World Bank had launched several missions to enhance Malaysia’s economy. A World Bank mission visited Malaysia in August 1999 to update the information on the Strategic Policy Review process. A previous mission in May updated progress in financial and corporate sector restructuring, identified outstanding and emerging issues related to restructuring, and discussed the corporate and financial restructuring aspects of the current Country Assistance Strategy.

The Malaysia Country Assistance Strategy (CAS) was approved by the World Bank in March 1999 following a series of consultations with government officials and a broad spectrum of organizations representing the civil society. The CAS outlined a number of performance triggers that would guide the Bank's lending programme in the coming years. The mission found that the government authorities acted quickly to establish an institutional framework for financial and corporate restructuring, and progress was noteworthy. The CAS outlined a base case programme of investment loans focusing largely on the social sectors. Financial sector restructuring loans were not anticipated under this base case scenario. Nonetheless, a robust programme of analytical work, policy advice, selective technical assistance, and country dialogue was envisaged in the CAS, particularly in the areas of financial and corporate restructuring, medium-term competitiveness and social issues. Both the impact of the crisis and medium-term challenges were analyzed in detail in a Malaysia Structural Policy Review, which served as an instrument for the Government and the Bank to monitor Malaysia’s performance over the CAS period (Malaysia, 2000).

Another World Bank mission was launched in March/April 2000 for a Strategic Policy Review monitoring mission, in which it helped to gauge the progress in the financial and corporate sector reform. In August 1999, the Inclusive Financial System (IFC) organized a mini-seminar in Kuala Lumpur with Malaysia’s private firms. The IFC subsequently received requests to consider participating in several high technology ventures, two corporate restructuring proposals, and a recycling project. Malaysia had a well-developed financial market, and local currency financing was preferred by many companies. In this context, IFC's strategy was to;

i. Support the rapidly evolving high-tech sector through nontraditional sources of financing in Malaysia, such as venture capital.
ii. Support financial institutions that provide assistance to Small and Medium Enterprises (SMEs) including leasing and venture capital funds.

iii. Provide direct support to SMEs.

The World Bank assisted the Malaysian government through several channels. The Education Sector Support Project provided funding to a continuous core program in basic education, and supported polytechnic education to provide skilled technicians for the medium-term economic recovery, as well as efficiency improvements through further staff development and institutional strengthening. Implementation was done on schedule. The on-going Social Sector Support Project assisted the Government in ameliorating the adverse impacts of the economic crisis on the poor and vulnerable through maintaining their welfare and access to essential social services; particularly for those groups located in the poorest districts.

3.8 Miyazawa Funds

Under the new Miyazawa Initiative, Japan had set up a short term financing facility worth US$2.5 billion for Malaysia. The facility served as a standby for the government should the need arise and was aimed at supporting credit-extending schemes intended to promote economic activities in Malaysia, such as trade financing, and small-and medium scale enterprise credit line.


Ten years after the economic crisis of Asia, countries that were affected by the crisis had been recovering by embracing the free market and globalization. Asia was one of the most dynamic regions in the global economy. Malaysia’s economy and financial system was at the strongest position after a decade of the financial crisis. Malaysia had greater economic flexibility to shift to new areas of growth, and thus, sustained the developmental momentum. Economic growth was achieved with pricing stability, low unemployment and strong external balances. The level of savings remained high at 37 per cent as a percentage to the GDP, while the level of external reserves remained strong at US$91 billion. Malaysia had taken the advantage of globalization to strengthen its economic and financial relationships with the major trading blocs across the globe (Economic outlook, 2007). In 2006, the total value of the external trade exceeded RM1 trillion (US$294 billion) for the first time in history. Foreign direct investment was also sustained, particularly in new areas of growth. The private sector continued to prosper as the catalyst for the economic growth for the fifth consecutive year, while the public sector played a supporting role. In terms of economic growth in Malaysia, after the economic crisis, GDP per capita at current prices had increased to about US$ 6,000 in
2006, whereas it expanded to 7.3 per cent in the fourth quarter of 2007, with the overall GDP exceeding 6.3 per cent in the year (Economic Outlook, 2007).

Aside from that, Malaysia continued to attract both domestic and foreign investments from the traditional sectors, while new sectors were also gaining importance. On the other hand, the servicing sector such as information technology, shared services and outsourcing, health and medical, tourism, financial services, and Islamic finance had also shown an increase in their market share. On the back of the public sector, pay was increased effective July 2007, and during the year-end festivities, domestic demand was sustained in the second half of 2007. Private consumption had grown strongly despite the rise in the cost of living, benefiting from the higher income and firm commodity prices (Malaysian economy, 2007). Other than that, Malaysia’s growth momentum had increased in the fourth quarter of 2007 to 7.3 per cent, from 6.3 per cent in the third quarter. The increase in public investment was due to the impact of the Ninth Malaysia Plan (RMK9), which gained momentum in the second half of the year. On the supply side, the manufacturing sector was adversely affected by the decrease in the electronics market and the external demand in general. However, the slower growth in manufacturing was largely maintained by the strong expansion in the services sector. The growth in servicing was helped by strong domestic demand, solidness of household spending and tourist money. Improved business and financial activities had also led to an expansion in services (Malaysian economy, 2007).

The construction sector’s growth was helped favourably by the implementation of projects under RMK9, which gathered momentum since the beginning of the year. The construction sector growth was maintained at 4.7 per cent in the fourth quarter, picking up from 4.0 per cent in the first half of 2007. The finance, insurance and business services sub-sector had also expanded to 9.8% in the fourth quarter due to the strong demand for loans and insurance (Malaysian economy, 2007). Other than that, inflation had decreased dramatically, when it fell to a low of 1.4 per cent in June 2007 due to the reduction of oil price hike in 2006, and the stronger Ringgit. The engine of growth for 2007 was private consumption and government spending. Domestic demand was also the main engine of growth, given the uncertainty in external demands. Although private consumption and government spending had also contributed to the growth in 2007, the private sector was growing modestly (Malaysian economy, 2007). In terms of private investment, 11.6 per cent share of GDP had continued to expand moderately, given the business confidence. During the year 2007, the total trade had surpassed the RM1 trillion marks or two consecutive years, growing by 3.7 per cent to a record RM1.11 trillion (Malaysian economy, 2007).
Besides that, Malaysia’s private debts securities market, including the conventional market, became the second largest market in Asia. The economic and financial linkages between Asia and the Middle East had grown stronger. Meanwhile, world trade had expanded at the average of 10 per cent over the period of 2001 until 2005. Asia’s trade with the Middle East increased on the average of 24 per cent (Economic outlook, 2007). In addition, starting in 2007, the creation of the development corridors such as the Iskandar Development Region (WPI), Northern Corridor Economic Region (NCER) and Eastern Corridor Economic Region (ECER) had capitalized on the momentum created by the sustained economic growth (Malaysian economy, 2007). Those development corridors were now in the first phase of its implementation which started in 2007.

Malaysia had sustained its political stability throughout the year after ten years of the financial crisis. This was because there were strong linkages between political stability and economic development. The political situation in Malaysia was stable during Tun Dr. Mahathir Mohamed’s rule. However, in 2008, Dato’ Seri Abdullah Ahmad Badawi was indirectly threatened by the opposition leader, Anwar Ibrahim, who add planned to overthrow the government with parliamentary defections after he returned to Parliament in a by-election at Permatang Pauh (Malaysian’s independence day clouded by politics, 2008). In the social aspect, Malaysia can take pride in the progress and development of the country that has been achieved. The hard work, tolerance and the consensus of multi-ethnicity, cultural and religious Malaysia’s population had turned diversity into an asset which brought stability and prosperity to the country.

5. Conclusion

As a conclusion, this paper has discussed the financial crisis that affected the Asian countries. To overcome this crisis, the government had taken several steps such as the establishment of Danaharta and Danamodal. Ten years after the financial crisis, the countries that were most affected by it were recovering well. In the period of 2006 to 2007, the Malaysian economy was stronger due to the state demand. Growth was achieved by low inflation climate and low unemployment rate. Improving and maintaining economic freedom was the only reliable way to generate positive cycle of economic growth and prosperity. Thus, Malaysians should be proud of the government’s initiatives for the successful financial packages for our country.
References


