



Managing the Malaysian Economy

Overview

When Budget 2001 was formulated last year, the outlook of the global economy was still uncertain, particularly with respect to the magnitude and duration of the United States (US) economic slowdown. The expectation then was for an early recovery commencing from the fourth quarter of 2000. However, towards the end of 2000, global economic activity further slowed down, particularly in the US. Since the second quarter of this year, it became increasingly evident that the slowdown has not only become more protracted and severe but the contagion has also spread to other economies. The recent attack on the US has made the prospect of an early recovery even more uncertain.

The Malaysian economy had recovered from the 1997 Asian financial crisis and was on the path of stronger growth. Real Gross Domestic Product (GDP) growth, which turned positive since the second quarter of 1999, had continued to grow strongly for seven consecutive quarters. Against this background and premised on the assumption of an early global economic recovery, the main strategic thrusts of Budget 2001 were focussed on stimulating domestic growth and enhancing competitiveness as well as improving the quality of life of Malaysians in line with the nation's agenda of a caring society.

Stimulating Economic Growth

Fiscal Policy

The expansion in domestic aggregate demand in 2001 was expected to be broad-based driven

by both the private and public sectors. The slower performance of the private sector reflecting the impact from the unfavourable external sector, however, necessitated further stimulus measures by the public sector to support domestic demand. In this regard, Budget 2001 allocation for both operating and development expenditure amounted to RM91,050 million, against an expenditure of RM84,500 million in 2000, an increase of 7.8%. During the course of the year and in response to the greater-than-expected slowdown in the global economy and the resultant deterioration in the nation's export performance, the Government announced a pre-emptive package in March 2001 aimed at further stimulating domestic demand. Under this package, the Government expenditure was further increased by RM3 billion to supplement the expansionary stance taken during Budget 2001 announced in October 2000.

The fiscal stimulus to increase domestic demand also comprised both tax and non-tax measures. As a means to increase disposable income and encourage consumption, higher tax rebates were given. The rebate for individuals was increased from RM110 to RM350 and from RM60 to RM350 for wives. The rebate would benefit 1.25 million taxpayers and place some RM434 million in the hands of taxpayers. Measures to stimulate domestic demand also included the reduction of employees' contribution to the Employees Provident Fund (EPF) and the removal of tax on credit cards to encourage spending. To augment sales of automobiles, civil servants are allowed to apply for car loans once in every five years instead of seven years. To encourage the sales of properties, exemptions were given to

stamp duty for the sales and purchase, transfer and loan agreements while for civil servants, processing fees were exempted for purchases of completed properties up to the end of 2001. At the same time, the housing loan eligibility of civil servants was increased. Additional critical allowances were also given to doctors and nurses, headmasters and principals while incentive and meal allowances were given or increased for the personnel of the Armed Forces and Police.

Monetary Policy

The thrust of monetary policy in 2001 continues to focus on complementing the fiscal stimulus in supporting economic activities. Given the less favourable external environment, in particular the slowdown of the US and Japanese economies at the beginning of the year, the pursuit of an easier monetary stance is necessary to mitigate the slack in external demand. The policy stance has been facilitated by the low inflationary environment as well as the global easing of interest rates. The ample liquidity in the banking system helped to maintain low interest rates to ensure the financing of economic activities at reasonable costs. Despite the low interest rates, depositors continue to enjoy positive real rates of return on savings.

The banking sector expanded their financing activities through loans and private debt securities (PDS) financing, which grew by 4% in the first eight months of the year. Lending was broad-based, with loans extended for the purchase of residential property, manufacturing sector, wholesale trade and the purchase of passenger cars. Meanwhile, measures continue to be taken to improve the financing of small- and medium-enterprises (SMEs), an important mainstay of the economy.

In the foreign exchange market, the ringgit, which is pegged to the US dollar since September 1998, remained relatively strong against most major and regional currencies in tandem with the strong US dollar in the first seven months of 2001. By virtue of the peg, the ringgit mirrors the movements of the US dollar. As such, the ringgit has since 11 September, depreciated by between 0.2% to 3% against major and regional

currencies, following the weakening of the US dollar. Nevertheless, the ringgit peg will be closely monitored against both domestic and external developments to ensure that it remains consistent with macroeconomic fundamentals. Meanwhile, the ringgit peg continues to provide an environment of stability and predictability to facilitate economic activities.

Capital Market

The equity market remains generally lacklustre in 2001, in line with other major and regional markets on concerns of the global economic slowdown. In July and August, the equity market began to improve, but the uptrend was eventually affected by the September attacks on the US and the subsequent fall in stock prices worldwide. The bond market, however, continues to grow in 2001, reflecting its increasing significance as an alternative to financing by the banking system. In this regard, the Securities Commission (SC), as the sole regulator of the bond market, continues to undertake measures to promote the bond market, in particular Islamic debt issues and asset-backed securities. The issuance of Islamic PDS has been rising, reflecting its growing acceptance to account for 37% of total new PDS issues approved by SC in the first half of 2001 (2000: 25%). The issuance of asset-backed securities, however, has yet to pick up. In addition, further amendments were made to the Securities Commission Act, aimed at establishing an efficient regulatory regime for capital raising and in tandem with developing the capital market as the preferred fund-raising centre for domestic companies.

Knowledge-based Economy

Recognising that technology, skills and innovation are the main drivers to enhance future growth, Budget 2001 further reinforced the strategy to transform the economy from a production-based to a knowledge-based economy. The knowledge-based economy or K-based economy presents a strategy to generate and exploit knowledge to create new value in the economy, thereby contributing to increasing total factor productivity and raising the long-term growth potential. To enable the transition to the new economy and

address present challenges, the Government commissioned the Knowledge-based Economy Master Plan in 2000. The Master Plan, recently completed, is holistic in approach and outlines the key strategies to transform the economy to be highly competitive and resilient.

Measures to expedite Malaysia's transition into a K-based economy focussed on efforts to attract the best brains into the country to create a world-class workforce and enhancing computer literacy and information and communications technologies (ICT) through the greater use of computers. Towards this end, Malaysians who are abroad and with the required expertise were given incentives to return, in particular through the granting of permanent status to spouse and children and tax exemptions on personal effects and income remitted into the country. By mid-September 2001, of the 356 applications received from professionals working overseas, 122 were approved in the areas of finance, industries, ICT and medicine.

With regard to enhancing computer literacy, of the 4,400 schools identified to be equipped with computer laboratories, 50 projects have been completed, 1,354 are under various stages of construction and the rest are under the planning stage. To enhance accessibility to computers in line with the one-computer-per-family policy, amendments to the EPF Act were made, allowing withdrawals for the purchase of computers. By end-August, EPF has approved 467,832 applications totalling RM1,555 million. Government employees also took advantage of the more flexible loan facility, which permits the purchase of computers once in every five years from just once, previously.

Developing ICT Industries and Venture Capital

The development of the Multimedia Super Corridor (MSC) marked the beginning of initiatives towards the development of a K-based economy. In order to promote the development of world-class ICT companies, various incentives have been provided to attract ICT companies to the MSC. As at September, 563 companies have been awarded MSC-status, of which 48 are world-class companies, exceeding the target of 500 and

ahead of the scheduled timeframe of 2003. These companies have, thus far, invested RM6 billion while their exports have increased more than six times from USD19 million in 1997 to USD127 million in 2000 and increasing further to an estimated USD260 million this year. In addition, these companies have also expended a sum of 26% of their total expenditure on research and development (R&D). In terms of employment generation, a total of 11,911 workers were employed, of which 82.6% or 9,842 were knowledge-workers in 2000. The number is expected to increase to 14,438 and 12,169 workers, respectively in 2001.

Further progress in fostering synergy has been made with the addition of an eighth MSC flagship application on Technopreneur Development. The network of incubators set up via this flagship is expected to provide the necessary impetus to the development of technopreneurship.

New high-technology and knowledge-based as well as idea-based startups for SMEs require different and more creative modes of funding. Collateral-based traditional bank lending may not be forthcoming for activities based on promising ideas or intangible collaterals. Venture capital financing provides a viable alternative to traditional lending as it provides seed capital for early startups and acts as business angels for high-risk growth sectors. To close the financing gap, the Government announced the establishment of a venture capital fund totalling RM500 million in Budget 2001. The fund has been channelled to a newly-formed Government company, namely the Malaysian Venture Capital Management Berhad (MAVCAP) in the form of interest-free soft loans for a period of 10 years. MAVCAP will implement the Government's strategic mandate to drive the development and empowerment of innopreneurs and technopreneurs to create wealth in the K-based economy as well as development of the venture capital industry. MAVCAP is expected to launch its financing facilities to the market in October 2001. MAVCAP is negotiating to secure a RM1.9 billion soft loan from Japan as a source of additional funding. A significant portion of this funding would be utilised for debt ventures such as project-based loans, guarantee to banks and export finance for the ICT industry and high-

KNOWLEDGE-BASED ECONOMY : THE WAY FORWARD

Introduction

The world is fast becoming a single borderless global marketplace which is expedited by rapid advancements in information and communications technologies (ICT). The global economy is characterised by high-technology diffusion, information accessibility, capital mobility and the increasingly sophisticated demands of consumers. As such, competing in the current environment is becoming more and more knowledge-driven. Growth and wealth creation of economies are increasingly propelled by the knowledge, skills and creativity of the workforce, as evident from the experience of highly productive countries.

In the case of Malaysia, the imperative to develop into a knowledge-based (K-based) economy is crucial as a strategy to sustain high growth and to remain competitive in order to achieve Vision 2020. The nation's move to a K-based economy is influenced by challenges from increasing globalisation as well as concerns about intense competition for foreign direct investment from relatively labour-surplus and low-waged economies in the region and elsewhere. The move towards a K-based economy is part of a wider plan to become a fully developed and knowledge-rich nation by 2020.

Understanding the Knowledge-based Economy

A K-based economy is one in which knowledge, creativity and innovation play an increasing and important role in generating and sustaining growth. While traditional factors of production will continue to remain important, knowledge will be the key factor in driving growth through the creation of value added and enhancing productivity and competitiveness. The nucleus of the K-based economy is human capital with its capacity to create, innovate and commercialise knowledge, while ICT will be a key enabling tool to facilitate the transformation to a K-based economy. In a broad sense, all sectors of the economy will become K-based through productivity-driven strategies to enhance the application of knowledge *vis-à-vis* input-driven strategies involving increased inputs of capital or labour.

The K-based economy essentially comprises two important types of knowledge industries: the first being industries with knowledge as the major product and the second being industries managing, processing and disseminating information. The first category includes industries such as software, biotechnology and information technology (IT) hardware and occupations such as engineers, scientists, programmers and designers, whose major output is research that translates into new products and services. The second category comprises industries such as telecommunications, banking, insurance, law, medicine, education and the government services. Occupations in this category include managers, bankers, accountants, doctors and teachers. These industries are typically required to handle and manage information effectively, rather than breakthrough knowledge creation.

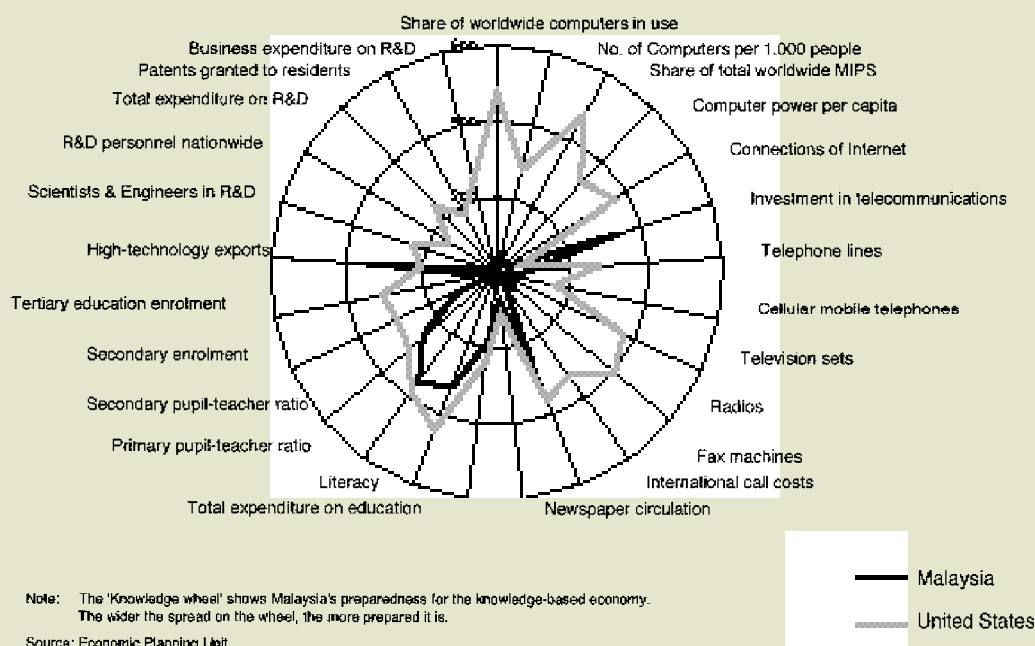
Current Status

Malaysia started to lay down the foundation for the K-based economy in the mid-1990s. Among others, measures taken include the launching of the Multimedia Super Corridor (MSC), which represents the first phase of the K-based economy agenda. Meanwhile, continuous efforts have been taken to enhance several key areas to effect the transformation towards the K-based economy. These include human resource development, science and technology (S&T), R&D, infrastructure

and infostructure as well as incentives and financing. At the same time, with the comprehensive world-class infrastructure and infostructure in place, MSC offers an excellent and conducive ICT environment to spearhead the development of a K-based economy, in particular in attracting knowledge workers and high technology industries. To date, MSC has attracted a total of 563 companies, including 48 world-class companies. In addition, MSC promotes several flagship applications, including electronic government, smart schools, multipurpose card and telehealth as well as the new technopreneur development flagship.

In assessing Malaysia's readiness to become a K-based economy, the United Nations Human Development Report 2001's Technology Achievement Index (TAI) places Malaysia among the world's potential technology leaders, ranking 30 among 72 countries. The index defined potential technology leaders as countries that have invested in high levels of human skills and have diffused old technologies widely, but with little innovations. The Knowledge-based Economy Development Index (KDI) ranked Malaysia in 17th position among developing and developed countries. The KDI, developed by the Economic Planning Unit, indicated that Malaysia fared better in terms of telecommunications infrastructure and literacy level but has to intensify efforts to improve higher education enrollment, R&D and computer usage, in particular Internet connectivity.

KNOWLEDGE WHEEL: MALAYSIA AND UNITED STATES, 2000



Knowledge-based Economy Master Plan

The Government embarked on the project to develop a Knowledge-based Economy Master Plan following its announcement in Budget 2000 on the need for a paradigm shift from a production-based economy to a K-based economy. Further initiatives to promote the development to a K-based economy were introduced in Budget 2001. Among others, they included tax incentives to enhance the usage of ICT, withdrawals from EPF for the purchase of computers and the establishment of the Malaysia Venture Capital Management (MAVCAP) in the Ministry of Finance to manage an additional RM500 million venture capital fund, aimed at promoting the financing of start-ups of high technology industries.

The Knowledge-based Economy Master Plan outlines seven strategic thrusts, comprising 155 recommendations to expedite the development towards the K-based economy. The seven strategic thrusts with the main salient features are as follows:

- i. Cultivating and securing the necessary human resources
 - Enhancing human resource development to build the knowledge-human resources. The emphasis is on education, training and retraining and life-long learning, in particular computer literacy.
 - Brain gain programme which is aimed at attracting global talent and encouraging Malaysian experts to return.
- ii. Establishing the institutions to drive the K-based economy
 - Setting up institutions to drive the development of the K-based economy. In this regard, a National K-based Economy Development Council is proposed to champion and mobilise efforts as well as monitor the progress towards the development of the K-based economy.
- iii. Ensuring the necessary infostructure and infrastructure
 - Improving the communications and multimedia infrastructure, such as the availability of computers, integrated high-bandwidth and connectivity to the Internet, computer labs and English language learning centres.
 - Enhancing infostructure such as networks, local content, incentives and legislation to create an enabling environment infrastructure.
- iv. Building S&T capacity
 - Increasing S&T capacity in terms of expanding the supply of manpower and fostering the appreciation of science in schools and tertiary education, aimed at developing innovative and creative capabilities.
 - Enhancing R&D in terms of increased expenditure and forging greater collaboration between research institutions, universities and industries to create and commercialise knowledge and technology.
- v. Private sector spearheading the K-based economy
 - The private sector will continue to be the engine of growth in the K-based economy.
 - Promoting greater use of e-commerce, in particular among the small- and medium-industries and enterprises.
 - Harnessing the entrepreneurial skills of the private sector to promote new economic activities.

vi. Developing the K-based civil service

- The civil service will continue to facilitate the development of the K-based economy in terms of providing leadership, strategising and drawing up policies, implementing programmes, regulating the economy and fostering collaboration between the public and private sectors.
- Emphasis will be given to the development of human resources in the civil service, in particular the instilling of a culture of innovation, improving English language capabilities and enhancing the absorption and application of ICT.

vii. Bridging the knowledge and digital divides

- Ensuring the K-based economy does not widen disparities between various segments of Malaysian society.
- Empowering the *rakyat* with knowledge through providing access to education.
- Enhancing the affordability of computers and Internet access.
- Addressing the digital gap among races, rural-urban areas, gender and disadvantaged groups.

Conclusion

The K-based economy is an imperative that Malaysia cannot afford to ignore in order to achieve sustainable economic growth and remain globally competitive. The experience of developed countries further attest to growth and wealth being increasingly driven by knowledge. Although measures have and continue to be taken in progressing towards the K-based economy, more concerted and accelerated efforts need to be instituted, particularly in human resource development, S&T, R&D, infrastructure, infostructure and the digital divide in order to leapfrog to the K-based economy.

growth sectors. Requirements for these lending facilities would be flexible and less conditional and the provision of hard collateral is not necessary.

The Government has also established the Venture Capital Fund for Technology Acquisition (VCTA), totalling RM190 million to finance activities related to venture capital and technology acquisition. The fund is channelled through a newly-formed Government company, namely Kumpulan Modal Perdana Sdn. Bhd. (KMPSB) in the form of interest-free soft loans for a period of 10 years. KMPSB will be involved in the formulation of a master plan and the management of programmes for investment linkages in high-technology industries. It will also play a role in the investment of high-growth and high-technology startups and be involved in the expansion of companies and identification of investment opportunities for Malaysia as well as suitable technologies abroad to be transferred to Malaysia.

To facilitate ICT companies to tap funds in the capital market, the listing requirements of the Malaysian Exchange of Securities Dealing and Automated Quotation (MESDAQ) were further liberalised. The requirement that 70% of listing proceeds be used in Malaysia was replaced. Under the new requirements, applicants are required to provide proof that benefit accrues to Malaysia if more than 50% of the listing proceeds is utilised outside Malaysia. As at end-August 2001, there were four companies listed on MESDAQ, with seven more companies approved for listing.

Enhancing the Nation's Competitiveness

Strengthening the Financial System

The Government continues with efforts to strengthen the financial system with a view to

creating a more competitive, strong and resilient financial sector. The Capital Market Master Plan and the Financial Sector Master Plan were launched on 22 February and 1 March 2001, respectively. Both the master plans chart the strategic directions of the capital market and financial sectors over the next 10 years, aimed at enhancing their efficiency, resilience and competitiveness in an increasingly globalised and integrated environment. The master plans encompass a change programme to be implemented in phases.

In line with the objective to enhance domestic capacity to develop a core of strong domestic institutions, further progress was achieved in the restructuring of the financial sector. The bank merger programme was successfully implemented with 52 out of the 54 domestic banking institutions consolidated into 10 banking groups, resulting in 98% of total assets of the domestic banking sector rationalised and consolidated by end-September 2001. The two remaining banking institutions are expected to finalise their merger negotiations soon.

The capital position of the banking system continues to remain strong with the new capital fund requirement increased to RM2,000 million for domestic banking groups and RM300 million for the locally-incorporated foreign banks. As at end-August 2001, nine banking groups and eight foreign banking institutions have complied with this requirement. The risk-weighted capital ratio (RWCR) increased to 12.6% as at end-August 2001 (end-2000: 12.3%), well exceeding the Basle minimum requirement of 8%. Non-performing loans (NPLs) ratio on a 6-month classification, which was 6.3% as at end 2000, have risen to 8.3% at end-August, following the slowing down in economic activities and the reclassification of NPLs previously given indulgence. The level is, however, still below the peak of 9% experienced during the financial crisis.

In order to further strengthen the capital market, efforts were undertaken to consolidate the stockbroking industry. As at end-August 2001, seven stockbroking companies had entered into agreements to acquire or merge with three other companies. In addition, as a measure to forge better communication with investors and to counteract misperceptions especially by foreign

investors, the Kuala Lumpur Stock Exchange (KLSE) has set up an international communications team to disseminate accurate, timely and effective information on the equity market. In the light of improvements in the equity market, the 10% exit levy on repatriations of portfolio profits within one year was withdrawn on 2 May 2001. With this, the remaining capital control restriction on portfolio investment was completely removed.

Developing Strategic Partnerships

Establishing strategic partnerships with international and global players in the services sector, particularly in ports, airports, telecommunications and ICT, are critical to ensuring sustained competitiveness and resilience within the context of a borderless market. Strategic alliances and partnerships are important in bringing about higher technological and managerial skills via technology transfers and investment in human capital by foreign partners. Smart partnerships also broaden domestic markets with increased access to international markets provided by marketing links of global network players. During the year, a number of discussions were held to identify strategic partners for the Malaysian airport operator as well as the national air carrier. In this respect, Schipol International B.V. of Holland has entered into a Memorandum of Understanding to acquire an equity stake in Malaysian Airport Holding Berhad (MAHB). Malaysia Airlines (MAS) has also brought on board foreign management expertise to spearhead efforts at turning around its operations. With regard to West Port of Port Klang, the country's leading port is expected to derive synergistic benefits from the 30% stake held by Hutchinson Whampoa. Similarly, the Tanjung Pelepas Port (PTP) in Johore, which sold 30% of its equity to Maersk Sealand, is expected to benefit from the increase in cargo handling.

Improving Corporate Governance

Efforts towards enhancing transparency and accountability continue to be undertaken in order to further improve investor confidence. By July, 29 or 41% out of the 70 recommendations on corporate governance proposed by the Finance

Committee on Corporate Governance have been implemented. To ensure smooth and effective execution, an Implementation Project Team comprising representatives from the Ministry of Finance, BNM, the Registrar of Companies and KLSE was set up. Legislation, rules and regulations are being reviewed and updated on a continuous basis to further improve corporate governance.

In addition, the KLSE listing requirements were revamped on 22 January to address, among others, the issue of corporate governance. In particular, the requirements on the reporting of extent of compliance with the Malaysian Code on Corporate Governance, disclosure by directors on the state of internal controls, independence of the board of directors as well as mandatory accreditation were emphasised. Directors of public listed companies are also required to attend prescribed training programmes as a prerequisite to continued listing, aimed at enhancing the competency and professionalism of company directors. Meanwhile, a Minority Shareholders Watchdog Group, comprising EPF, Lembaga Tabung Angkatan Tentera, Lembaga Tabung Haji, Social Security Organisation (SOC SO) and Permodalan Nasional Berhad (PNB), has been set up, aimed at encouraging proactive shareholders participation in public listed companies.

Eliminating Bureaucratic Delays

The Government continues to step up efforts to eliminate bureaucratic delays as a measure to accelerate project implementation and completion in order to sustain economic growth as well as improve delivery of public goods and services. In this context, a task force in the Ministry of Finance was established to closely monitor the progress, identify and troubleshoot problem areas in order to ensure smooth implementation of all the measures announced in Budget 2001. A Flying Squad was also formed in the Ministry to ensure both public sector development and privatised projects proceed as scheduled.

To further reduce red tape and in line with the need to empower ministries and agencies with bigger financial authority, tender boards at the ministerial and departmental levels can now approve tenders of up to RM50 million for works

and RM30 million for supplies and services. The tender boards are also allowed to approve restricted tenders of up to RM5 million. For quotations, authority has been delegated to ministries to approve up to RM200,000. For statutory authorities, the ceiling for the approval of tender awards for all supplies, services and works has been increased to RM100 million, while for restricted tenders, they have been given authority of up to RM10 million.

In order to accelerate project implementation as well as reduce processes, the Government appointed project management consultants (PMCs) to supervise public sector projects. Projects were also awarded on turnkey and design-and-build basis to shorten processing time as well as expedite project completion.

In terms of expediting payments, all ministries and agencies are required to make payments up to 50% of the value claimed within 14 days and full payment within 30 days upon receipt of full documentation as per contract requirement. For projects undertaken through PMCs, the latter are allowed to submit claims for payment direct to the Accountant General's office, for which payment will be made within 10 days. To facilitate early project startups, all contractors implementing government projects are given advance payments of 15%, while for those implementing small projects under the pre-emptive package, advance payments of up to 75% are allowed.

The Government also implemented the two-year budgeting process for the 2002-2003 Budget, with a view to improving the efficiency in the preparation and examination of the annual budget. The two-year system will facilitate efficient planning for fund utilisation and programme implementation while enabling greater efforts to be directed towards project monitoring and evaluation.

Continuing the Agenda for Caring Society

As in previous years, Budget 2001 incorporated a policy on caring society as a national agenda in line with the Government's empathy to the needs of the less fortunate. In this respect, the

CORPORATE GOVERNANCE : AN UPDATE

Introduction

The importance of good corporate governance is increasingly recognised worldwide, particularly in the context of enhancing investor confidence. Investment inflows are generally drawn to countries with credible corporate governance practices. In light of the keen competition for investment, the adherence to good corporate governance practices is an imperative that cannot be ignored. Even within the country, good corporate governance practices will help boost the confidence of domestic investors and ultimately induce more stable sources of financing for industries and the capital market. A recent survey on emerging markets also indicated the strong correlation between corporate governance and price performance of stocks.

Efforts to address corporate governance in Malaysia began way before the Asian financial crisis, although the crisis provided the impetus to accelerate corporate governance reforms. A high level Finance Committee was established in 1998, comprising both government and industry representatives. The committee was tasked with establishing a framework for corporate governance and setting best practices for the industry.

Understanding Corporate Governance

There is no one standard definition of corporate governance. The Finance Committee Report defines "Corporate governance as the process and structure used to manage the business and affairs of the company towards enhancing business prosperity and corporate accountability, with the ultimate objective of realising long-term shareholder value, whilst taking into account the interests of other stakeholders".

Corporate governance is premised on the principles of transparency, accountability, fairness and responsibility, which are universal in their application. The implementation of corporate governance is usually a combination of regulation by the appropriate authorities and self-regulation by the market. It is, however, observed that statutory regulation alone cannot promote effective governance. Corporate governance initiatives tend to win most support when driven from the bottom up *vis-à-vis* from the top down.

Finance Committee Report on Corporate Governance

The Finance Committee on Corporate Governance released the Report on Corporate Governance in March 1999, comprising 70 recommendations. The thrust of reform efforts is focussed on strengthening the influence of minority shareholders, enhancing the role of boards of public listed companies (PLCs), strengthening regulatory enforcement and promoting high standards of corporate governance through training and education. The key recommendations of the Finance Committee Report centred on effecting legal reforms alongside the introduction of a Malaysian Code on Corporate Governance as well as facilitating training and education at all levels and promoting active participation of minority shareholders.

An Implementation Project Team (IPT) was also formed and tasked to lead and oversee the implementation of the recommendations of the Report. The progress of the IPT is monitored by the Finance Committee to ensure the necessary balance between public and private sector interests in addressing the various implementation issues. Significant progress has been made in the implementation of the Report's recommendations, particularly in respect of disclosure requirements as well as enhanced standards of corporate governance and investor protection.

■ Malaysian Code on Corporate Governance

The Malaysian Code on Corporate Governance was released in March 2000. The code essentially aims at setting out best practices in corporate governance. Although compliance to the code is voluntary, it is coupled with a requirement in the Listing Requirements of the Kuala Lumpur Stock Exchange (KLSE), which mandates disclosure of the extent of compliance with principles and best practices.

■ Legal and Regulatory Reforms

Effective 1 July 2000, amendments to the securities legislation were made to enhance primary market disclosures. The amendments have effectively delineated and streamlined the responsibilities of the Securities Commission and the Registrar of Companies with regard to prospectuses, thus resulting in greater legal and regulatory certainty in the area of public offerings of securities.

Further changes have been recommended to the securities and company laws. Among the intended changes include the requirement for auditors to report suspected breaches of securities laws, the codification of key duties of directors and provisions to curb a controlling shareholder's right to vote in cases involving related party transactions. The implementation of these measures is currently under way.

The revamped Kuala Lumpur Stock Exchange (KLSE) Listing Requirements, released on 22 January 2001 are primarily aimed at enhancing standards of corporate governance and investor protection. New provisions have been introduced with existing provisions strengthened in areas relating to disclosure, internal controls, continuing listing obligations, financial reporting and protection of minority shareholders.

■ Minority Shareholder Watchdog Group

A Minority Shareholder Watchdog Group has been set up to encourage proactive shareholder participation in PLCs. It comprises the Employees Provident Fund (EPF), Armed Forces Fund, Pilgrims Fund Board, Social Security Organisation (SOCSO) and Permodalan Nasional Berhad (PNB), representing the largest institutional funds in the country. The Watchdog Group, which is intended to harness the ability of large, albeit minority institutional investors to monitor and institute change where necessary in the companies they have invested, is expected to be fully operational in the near future.

■ Training and Education

Amendments were made to the KLSE Listing Requirements to introduce the mandatory accreditation of directors of PLCs as a prerequisite to continued listing. As a measure to enhance standards of competency and professionalism amongst company directors, directors of PLCs are required to attend a prescribed training programme. In this regard, the Malaysian Institute of Corporate Governance (MICG) is currently undertaking on-going training and education for directors as well as company secretaries, auditors and investors on corporate governance.

■ Capital Market Master Plan

The Capital Market Master Plan (CMP), which was released in February 2001, comprehensively charts the strategic positioning of the Malaysian capital market over the next 10 years. Of the 152 recommendations in the CMP, there are 10 recommendations related directly to corporate governance. The CMP builds on the Finance Committee Report's recommendations and further develops the corporate governance reform agenda in a number of key areas relating to the disclosure of timely and accurate corporate information, accountability of company directors, financial controllers and management as well as strengthening the role of auditors, encouraging greater institutional investor

participation in corporate governance and promoting shareholder activism. The CMP further reinforces the corporate governance agenda as a strategic thrust to further enhance investor confidence as well as developing an efficient and competitive capital market.

Conclusion

It is imperative to move forward in addressing corporate governance issues, particularly in the light of investors being driven more by sentiment and perception, rather than fundamentals. This is even more pertinent given the increasing integration and dynamism of global financial markets, where large flows of funds can be easily transferred across the globe within seconds, facilitated by technology advancements. Although notable progress has been achieved in corporate governance, companies need to institute measures to continuously innovate and adapt their corporate governance practices in order to meet new challenges and seize opportunities. The Government, on its part, is committed towards the enhancement of corporate governance. Measures have and will continue to be taken to further accelerate the corporate governance agenda towards developing the Malaysian capital market as the preferred fund raising centre for Malaysian companies as well as in attracting foreign investment.

Government has intensified efforts to ensure a more equitable distribution of wealth and benefits, and avoid marginalisation of the disadvantaged groups. Thus, higher allocations have been channelled towards programmes aimed at increasing the incomes of the poor, enhancing rural accessibility to public utilities and amenities, upgrading rural health facilities and services as well as improving opportunities for better education and employment prospects.

In recognition of the contributory role of women in development, the Government has established the Ministry of Women and Family Development. With the formation of the Ministry, issues and problems specific to women, including children and family, will be given greater focus and attention. Since its establishment, a significant achievement was the amendment of Article 8(2) of the Federal Constitution to include the word 'gender' so that there would no longer be any law or policy which discriminates against women. The Ministry also launched the Women Against Violence or WAVE campaign in July 2001, which is targetted to eliminate all forms of violence, especially violence against women. Efforts will continue to be undertaken to further the participation and involvement of women in the social and economic development of the country as well as develop Malaysia into a nation of

character, built by families that are resilient, ethical, healthy, knowledgeable and harmonious.

Attack on the US - - - Managing Uncertainties

Following the attack on the US, the outlook of the global economy becomes increasingly uncertain. The attack has not only altered the prospects for an early recovery, but also increased the risk of the US economy entering into a recession. The US being the largest economy in the world and accounting for about one-fifth of world output and exports, the contagion on the economies of major industrialised countries and the rest of the world would be significant.

Even before the attack, there was increased evidence of a more protracted slowdown of the world economy, primarily on account of the sharper decline in output growth in the three main economic blocks, namely the US, Japan and the euro area. The decline in the US manufacturing output continued to worsen, its equity market became increasingly volatile, while the unemployment rate edged upwards and business sentiment deteriorated. At the same time, Japan, the second largest economy, has not shown any sign of recovery. Depressed consumer demand,

weak external sector and a lacklustre pace of financial and corporate sector restructuring have pointed towards a contraction in Japan's output growth. The outlook for the euro area became more pessimistic with Germany, its largest economy, experiencing a stronger downturn, particularly in its industrial sector. The rigidities in the labour market and constraints in the European Central Bank (ECB) monetary policy also contributed to the greater pessimism.

In the aftermath of the attack, the US equity market was badly affected with the Dow Jones declining by 684.8 points when it reopened on 17 September to close below 9,000 points, the largest one-day fall ever recorded. There were also heavy sell-offs across major bourses and financial markets. On the day of the attack, stock prices worldwide fell sharply lower, with among others, the DAX index plunging by 8.5% in its biggest one-day fall and the FTSE index by 5.7%, marking its largest single-day fall since 1987. The Nikkei index, which had already fallen to a 17-year low of 10,196 points on 10 September, declined further by 5.7% to a new low of 9,610.1 points on 11 September. Other regional bourses, such as the Hang Seng and the STI also declined by 8.9% and 7.4%, respectively. Similarly, indices of the Taiwan, Thailand and Kuala Lumpur stock markets, which reopened on 13 September, fell by between 3.8% and 6.7%.

The US dollar has shown signs of greater pressures as investors liquidate into other 'safe haven' currencies. The dollar has been depreciating against the euro and yen since July this year, triggered by changing market perceptions that the US stance on a strong dollar policy had softened as well as the weakening investor sentiment, as reflected by the decline in the US stock market. Since the attack, the dollar has further weakened, declining by 2.4% and 2.5% against the yen and euro, respectively as at 27 September.

In response to these adverse developments, the US Administration has put in place a series of measures to arrest the slide in investor sentiment and consumer confidence as well as to contain any further decline in the equity markets. The US Fed has injected liquidity into the financial system and undertook a further cut in interest

rates. The US Congress has approved USD40 billion fiscal allocations for reconstruction, relief work and security. A bail-out package of USD15 billion has also been approved for the airlines.

In response to the US move, other monetary authorities have also taken measures to contain and ease the immediate adverse impact on their economies. In this regard, a coordinated action by major central banks has also been taken to reduce interest rates to improve confidence. The ECB has reduced the repo rate by 50 basis points to 3.75% while the Bank of Japan (BOJ) reduced the discount rate by 15 basis points to 0.10%. In addition, with the US dollar depreciating broadly against all major currencies, there are expectations of joint foreign exchange intervention by the G7 authorities, particularly should excessive volatility occur.

In addition to the impact on global equity and financial markets as well as the real economy, the September 11 attack has also clouded efforts in international financial cooperation. The international community's attention has now been diverted to address issues pertaining to security, combatting terrorism as well as immediate recovery measures to counter the deterioration in the global economic environment. Several major international meetings, such as the World Bank and International Monetary Fund (IMF) Meetings as well as the Commonwealth meetings at the level of Finance Ministers and Heads of Governments have either been cancelled or postponed. In the light of these developments, progress on important international financial issues of concern for developing countries could face a setback, such as efforts in reforming the international financial architecture, enhancing support for least developed countries (LDCs) through debt relief and leveraging trade for development, combatting money laundering, strengthening corporate governance as well as other initiatives in the pipeline. The turn of events has cast further uncertainty over future efforts to deliberate on collaborative initiatives, including the possibility of depriving developing countries the opportunity of putting forth issues of concern, particularly relating to the multilateral trading system at the upcoming Fourth World Trade Organisation (WTO) Ministerial Conference scheduled in November 2001 in Doha, Qatar. The impact of such delays could have far-reaching implications for developing countries.

Malaysia, being an open economy, where trade accounts for more than 200% of GDP, was also adversely affected by these external developments. The growth forecast of the Malaysian economy, which was revised downwards to 5-6% for 2001 in March from the Budget 2001 estimate of 7.5%, is being further adjusted to 1-2%, following primarily the recent developments in the US.

Notwithstanding this, the strong fundamentals of the Malaysian economy continue to provide sufficient policy flexibility to implement growth-supporting measures to stimulate domestic economic activities without jeopardising the sustainability of the nation's potential growth prospects in the medium- and long-term. The nation's current account in the balance of payments continues to register strong surpluses since 1998. The external reserves has stabilized at a higher level and is sufficient to finance 4.6 months of retained imports and is 6.2 times short-term liabilities, while external debt remains low and inflation subdued.

In response to the adverse developments in the external sector and with a view to minimising its immediate adverse spillover effects, the Government announced another stimulus package of RM4.3 billion on 25 September 2001. Apart from adding further stimulus to domestic economic activities, the package also aims to cushion the implications on the poor and other less advantaged segments of the society from the impact of the economic slowdown, generating business and income opportunities for small enterprises as well as providing skills training. The largest allocation of RM1 billion is provided for small projects in rural and selected urban areas including, among others, the construction and upgrading of roads, bridges, water and electricity supply, and community-based projects. In addition, computer laboratories will be constructed in 2,000 more schools, while maintenance works on government buildings and facilities will be stepped up. The package also provides for the doubling of current rates of welfare payments, monthly allowance for degree and diploma holders to learn IT, mathematics and languages as well as the promotion of tourism.

Monetary policy continues to be accommodative to reinforce fiscal stimulus to sustain economic growth. The adoption of an easier monetary stance will continue to be monitored against domestic and external developments. Following the cuts

in interest rates in the US, BNM reduced its 3-month intervention rate on 20 September by 50 basis points to 5%. The reduction marks the first cut by BNM in more than two years, and is in line with the action taken by several other central banks, following the worsening external environment. It is also aimed at enhancing domestic business sentiment and consumer confidence to support economic activities.

On the medium-term impact, the prospects remain uncertain as events continue to unfold. For Malaysia, the difficulties in the external environment have emerged at the time when the nation is just at its first year of the Third Outline Perspective Plan (OPP3), 2001-2010 and the Eighth Malaysia Plan, 2001-2005. To achieve the long-term objective of Vision 2020 of attaining a developed nation status, both Plans projected an average GDP growth of 7.5% per annum. The slower growth of 1-2% this year and moderate recovery of 4-5% anticipated next year, however, would necessitate greater efforts at accelerating growth in the subsequent years to recoup lost ground during the first two years of the Plans. Given the strong foundation already in place for the economy, the prospects of accelerating GDP growth remain plausible. The Asian financial crisis has shown that despite experiencing the worst-ever recession with the economy contracting by 7.4% in 1998, Malaysia was able to recover strongly in the following years, with growth rates of 6.1% and 8.3% in 1999 and 2000, respectively, thereby achieving the growth target of 7.5 % of the Second Outline Perspective Plan (OPP2).

Conclusion

The recent development in the US has led to greater uncertainties. As events continue to unfold, the prospect of an early recovery in the US and the global economy, generally, has become increasingly difficult. In the light of this, the Government will constantly monitor and assess developments in the external sector and their impact on the economy. Further measures primarily premised on promoting growth through strengthening resilience and enhancing competitiveness will be put in place to contain and minimise any immediate adverse spillover effects on the economy and, thus, avoiding further slide in the nation's growth. With the strong economic fundamentals coupled with flexible and pragmatic policy responses, the nation will be able to return to its stronger growth path.