REVISITING THE AFTERMATH OF THE 1997 ASIAN FINANCIAL CRISIS: AN EXAMINATION OF THE ROLE OF THE DANAHARTA IN ADDRESSING THE NON-PERFORMING LOANS IN THE PROPERTY SECTOR IN MALAYSIA

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ABSTRACT

During the 1997 Asian Financial Crisis, non–performing loans in the property sector accounted for more than 30 percent. It was alarmingly high for one sector and was said to have had a crippling effect on the banking sector. Many properties were auctioned off with subsequent detrimental effects on the property industry.

This paper discusses the problem of non-performing loans in the property sector in Malaysia during the 1997 Asian Financial Crisis. It evaluates the role of the national asset management company, Danaharta, solely set up to stabilise the banking and the property industries. Evidence from the central bank will be used to assess the effectiveness of Danaharta in handling the non –performing loans. It also discusses how the non-performing loans were negotiated with the banks, how the loan was restructured, and the economics of such transactions. Finally, it evaluates the impact of Danaharta in managing the non-performing loans in the property sector in Malaysia.

Keywords: non-performing loans, asset management company, asset disposal, asset recovery

1. INTRODUCTION

The Malaysian property market was at its peak in the third quarter of 1997. Speculation was rife and the market players were capitalizing on the flourishing market situation. When the 1997 Asian Financial Crisis hit Malaysia in the third quarter of the year, many were taken by surprise and slow to respond accordingly. The reality sunk in the following year when unprecedented levels of NPLs plagued the financial system, followed by a credit crunch which almost crippled the property industry. The property market which was previously booming was hit badly with a high number of unsold housing units, falling prices and rents.

The financial crisis caused systemic distress in the Malaysian financial system. As most of the banks were heavily burdened with non-performing loans in the property sector, the Malaysian government quickly intervened with four measures to address the non-performing loans that threatened the stability of the economy. The measures taken were the formation of the National Asset Management Company, Danaharta, to address the NPL; the consolidation of financial institutions to increase the resilience of the banking industry; the establishment of the Corporate Debt Restructuring Committee to address deterioration of the corporate sector and a special purpose vehicle; and Danamodal to provide capital injection to the banking industry and address the capital erosion in the banking industry.

The focus of this paper is on Danaharta, the national asset management company. This paper attempts to evaluate the role of the national asset management company, Danaharta, solely set up to stabilise the banking and the property industry. Evidence from the central bank will be used to assess the effectiveness of Danaharta in handling the non –performing loans. It also discusses how the non-performing loans were negotiated with the banks, how the loans were restructured and the economics of such transactions. Lastly, the paper evaluates the impact that Danaharta addressing the non-performing loans (NPLs) had on the economy at large and in the property industry in Malaysia.

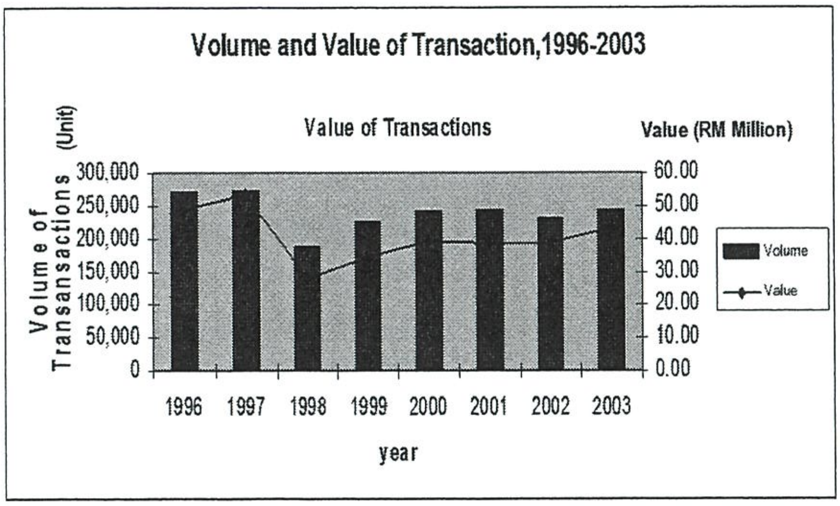
2. BACKGROUND

In the 1990s, Malaysia was categorised by the World Bank as one of the East Asian Economic Miracles, a reference made to high performing East Asian economies (World Bank, 1993). It showed an exceptional record of high and sustained economic growth for more than two decades. In 1990s, the real GDP grew at an average rate of over 8 percent. It achieved a remarkably high physical and human capital accumulation as well as rapid technological improvement. With a comparatively cheap and ready supply of skilled workers and up to date technology, Malaysia became a popular foreign investment destination. Foreign direct investment, in 1996 accounted for 59.60 percent (RM20,411.80 million) of the capital investments (MIDA, 1998). There were high inflows of foreign funds. In the banking sector a high interest rate was maintained to attract foreign investors looking for high rate of return. Against this background, Malaysia received a reasonably large inflow of foreign funds.

Unlike developed economies, the Malaysian economy has been highly dependent on the banking sector for financing most of its economic activities, while other avenues for raising funds like bonds and other financial derivatives are neglected (Mahani, 2000; Fung, 2004). It was also highly dependent on the property market in one form or another. Substantial amounts of bank loans were channelled to the property sector, causing property prices to spiral up. Noland (1999) argued that this was because alternative forms of investments were not well developed. In 1997 when the East Asian economies were hit by the financial crisis, it brought about panic and uncertainty. There were rapid reversals of capital inflows, property prices fell and the resulted in the crippling of the property market. In 1998, the GDP experienced a negative growth.

2.1 The Malaysian Property Market Before the Crisis

The year 1996 and 1997 was a boom period for the Malaysian property market. Against the backdrop of high economic growth, rising levels of income, market optimism and easy availability of credit, there were vigorous investments in certain property sub-sectors.



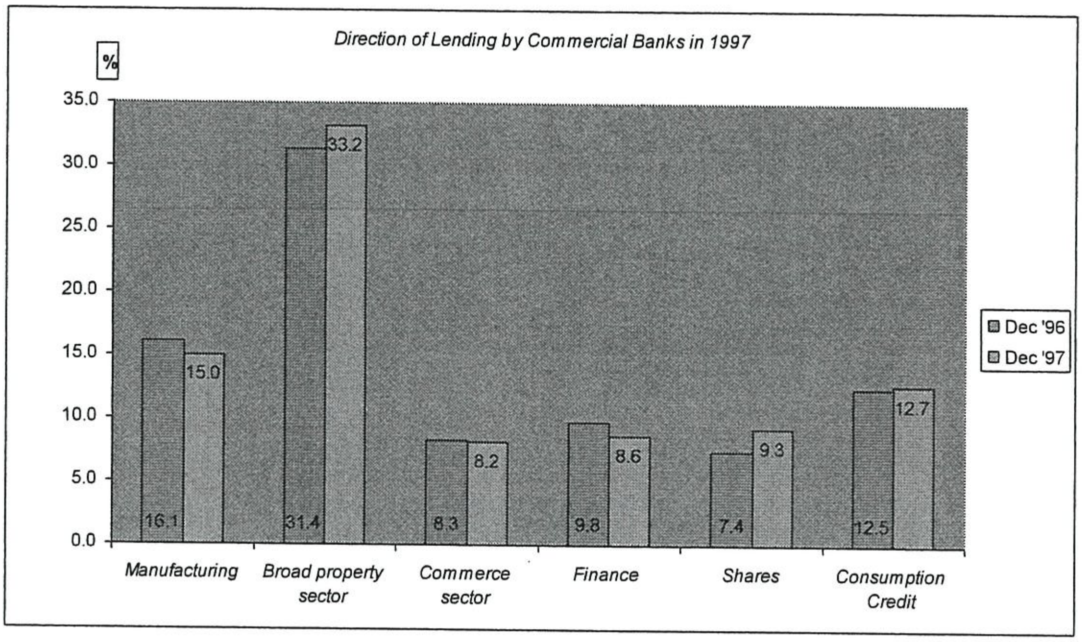
Source: Valuation and Property Services Department (VPSD), Property Market Report, various years

Figure 1: Volume and Value of Property Transaction, 1996-2003

As can be seen from Figure 1, the property market peaked in 1997. The volume and value of transaction were the highest during this year. Speculative development and buying were widespread. The market optimism caused an oversupply in commercial, hotel and condominium sub-sectors. The incoming supply of retail space in shopping complexes in the Klang Valley for the following three years was one and a half times more than the existing supply during the year (VPSD, 1998). Overbuilding was also apparent in the residential sector. These speculative activities supported by the readily available credit fuelled the inflationary trend. The prices of residential property in major towns increased by 20 to 25 percent per annum in the 1994 to 1996 period, compared to only 4.5 to 6.4 percent during the 1992 to 1993 period.

2.2 Property Finance

Loans to the property sector comprise the largest slice of the commercial banks advances. As shown in Figure 2, in 1997 broad property sector housing consumed the most credit, while other sectors like the manufacturing and services that propelled the economy were not allocated as many funds as the property sector. This raised the question of whether the funds were properly allocated and channelled for macroeconomic growth and stability. Growth in such sectors contributes to job creation and ensures that the standard of living, employment and wages do not stagnate.



Source: Bank Negara Report, 1997

Figure 2: Direction of Lending

As at the end of 1997, loans to the broad property sector made up more than a third of their total loans. Such large flow of funds not only caused distortion to the economy but also distortion in the property prices.

2.3 Non Performing Loans in the Property Sector

This financial crisis triggered a deflationary impact on the property market. As these loans were collateralised with the real estate at over–inflated prices, the banks suffered significant erosion of value of their collateral. The over-exposure to the property sector caused the banks to be badly hit. During this time the ability to pay back the loan by the borrowers was also reduced. Borrowers could not easily trade off their properties to pay off the loan as banks had tightened up their lending policy. Subsequently, potential buyers had great difficulties financing their purchase. Incidence of arrears and non-performing loans were high.

By August 1998, the net NPL ratio for the banking system had reached 11.4 percent. This is above the normal tolerable level of NPLs that the banks can absorb. It was projected to reach 15 percent by the end of 1998. Given the worrying state of affairs, the government resolved that the net NPL ratio had to be brought down to a single digit as soon as possible.

Table 1 shows the level of NPLs in broad real estate sector. At the end of 1997, the total NPLs was RM24 billion, of which RM4.82 billion (36.5 percent) was from the property sector. The NPLs further increased in 1998 to RM59.2 billion and the portion channelled to the broad property sector increased to RM28.3 billion or 35.5 percent. The level of NPLs attributable to the broad property sector continued to move upward in relation to its proportion to total loans.

Table 1: Non-Performing Loans (NPLs) in the Broad Real Estate Sector 1997 to 2004

	1997	1998	1999	2000	2001	2002	2003	2004
Total Loan (RM Billion)	421,205	413,638	427,691	454,212	470,434	439,032	473,979	502,522
Total NPL (RM Billion)	24,044	59,263	53,740	52,714.9	66,616.6	62,315.8	56,894.8	52,057.1
% of NPL	**5.70839**	**14.3273**	**12.5651**	**11.6058**	**14.1607**	**14.1939**	**12.0037**	**10.3592**
NPL in BPS	8,767	20,831	18,949.8	20,874	27,347.5	26,817.5	25,775.7	30,773.3
% of NPL in BPS	**36.4623**	**35.1501**	**35.262**	**39.5979**	**41.0521**	**43.0348**	**45.3041**	**59.1145**

Source: Bank Negara Malaysia (1997)
*[*1] NPL: non performing loans*
*[*2] BPS: broad real estate sector*

3. LITERATURE REVIEW

Many studies have established the significant link between NPLs and the real economy. The increase in NPLs results in the malfunctioning of the banking sector. This affects a banks soundness, distorts actual economic performance, and threatens to impede economic development. At the pinnacle of high NPLs severity, banks are unwilling to give new loans, which creates a credit crunch that ultimately leads to a financial crisis.

The financial crises is also a confidence crises. As market confidence erodes, panic situations deepen. Deposits outflow and asset values decline. In the property market, studies have shown that the decline in confidence manifests by the decline in formerly robust real estate markets. This is evidenced by falling in occupancy of office and retail spaces, rents and values, foreclosures, and a growing inventory of unsold properties (Cooke & Foley, 2000). As a result, restoring confidence becomes a critical part of the solution (Mahani, 2002).

In many East Asian countries, the economy is highly dependent on the property industry. A substantial proportion of bank credit is channeled to the property sector. Thus, as property values dropped, much of the banks' capital eroded. It has been established in many studies that the deflation of asset values contributed to non-performing loans (NPLs).

Studies show (Fung, 2004, Kliengebel, 2000) that many economies addressed the issue of NPLs by removing them from normal banking operations through the establishment of asset management companies (AMC). Hanohan and Klingebel (2000) identified two types of AMCs; the public asset management companies, and the private management companies, which are usually the banks own asset management unit managing their own non-performing assets. Studies have shown however that in comparison to other banks, public AMCs were able to more rapidly and efficiently recover assets and cash through legal actions, disposal of loans, and the sales of equity positions in exchange for NPLs.

The advocates of public AMCs argued that Governments can manage acquired NPLs effectively through their special powers and enabling them to maximise value. This is done by swapping debt for equity, playing an active role in managing and turning the borrowers' company around or foreclosing on non-performing collateral (Haggard, 2000). On the other hand, the opponents of public AMCs argued that they may succumb to political pressure especially in cases where they hold a large portion of the corporate claims and may lead to a bailout. This is costly to the taxpayers.

In bank based models, NPAs are transferred to a specialised bank departments or workout units or to a separate special purpose organisation affiliated with bad banks. The assets are no longer reflected in the bank's book. The creation of bank based AMCs may or may not involve some government financial assistance. The advocates of bank based AMCs argued that it gives the bank the incentives to workout the NPLs, and avoid future losses by lending prudently and strict monitoring. This type of AMC does not involve public funds.

The asset management companies manifest in many forms. The first model is the rapid asset disposition agency, where its role is to try to dispose of the banks' asset within a short time frame, usually at fire-sale losses. The advantage is that the assets are liquefied and the capital can be turned around. Second, is the ware-housing model, where the agency takes over NPLs and warehouses them until the market recovers before commencing asset disposal. The third is an asset management company, where the agency acquires and restructures viable NPLs and liquidate NPLs of non–viable borrowers, manages assets to make it financially viable and attractive to new investors, with the aim of maximising recovery value. According to Klingebiel (2000) for emerging markets, restructuring agencies offer a larger scope of political interference. A rapid asset disposition agency is better suited.

In the transfers of NPLs to the public AMCs there is always the issue of pricing. It is often argued that the purchase price and disposal price is depressed which is at substantial cost to the banking industry. Banks are concerned over the implications on the value management of their own assets. Thus many banks are likely to oppose the acquisition of NPLs by public AMCs. In most cases transfers of NPLs to an AMC government is intended to lower NPLs of banks rather than remove overall NPLs, which allows the bank to focus on its lending business.

4. RESEARCH METHODOLOGY

In order to assess the impact of NPLs carved out by Danaharta from the banking system, as well as its contribution to the property industry, the following analysis, measurements and indicators were used:

i. Credit growth
Analysis on credit growth is carried out to detect any positive changes after the NPLs have been carved out by Danaharta.

ii. Correlation analysis between credit growth and the NPLs carved out by Danaharta
A correlation analysis is carried out to establish the relationship between credit growth and the carved NPLs.

iii. Restoration of confidence
Earlier studies establish that credit growth contributes to the regeneration of economic activities and ultimately restore confidence. There are two dimensions of confidence: the business confidence and consumer confidence. Having established the credit growth in the previous analysis, the following analysis is carried out to see whether business and consumers' confidence was restored.

   a. Business confidence can be seen from the opening and the expansion of office spaces. Data on office space occupancy is studied to see any positive movements in the occupancy levels after the NPLs were carved out from the banking sectors. Correlation analysis is then carried on the credit growth and office space occupancy.

   b. Consumers' confidence can be seen from the willingness of consumers to make major capital commitments. Data on residential purchase is taken as an indicator of consumers' confidence. Changes in residential transactions are analysed and correlation analysis is carried out to establish the relationship between consumers' confidence and credit growth.

iv. Property Market Recovery
Data on volume and price of property transactions were analysed to detect movements in the property market and correction analysis is carried out to establish relationships between credit growth and market recovery.

Interviews with the former Danaharta management personnel and its client banks were carried out to get an insight on the workings of the asset management companies, how prices were negotiated, loan restructured and the empowerment through the Danaharta Act.

5. DANAHARTA, THE NATIONAL ASSET MANAGEMENT COMPANY

To address the alarmingly high NPLs in the banking sector, in June 1998, the Malaysian government incorporated an asset management company, Danaharta, under the companies Act, 1965 to relieve the banks of the pressure of NPLs and enable them to concentrate on their lending operations during the period of financial instability. Danaharta was given a mission to re-energise the banking sector by carving out NPLs and maximising the recovery values of acquired NPLs. The setting up of Danaharta was financed through the issuance of RM3.2 billion in government guaranteed bonds, RM2.0 billion in loans from government agencies and the issuance of RM8.22 billion in zero coupon bonds to selling financial institutions. The total sum was RM13.22 billion. Danaharta was operational up until 2005.

To ensure its effective execution of removing NPLs from the banking sector, Danaharta was given three special powers under the Pengurusan Danaharta Nasional Berhad Act 1998. First, is the statutory vesting, where Danaharta was allowed to take over from the selling banking institution, with the same right as the creditors, thus enabling Danaharta to acquire assets with the certainty of titles. The second power is pertaining the right to appoint special administrators to take over and manage the company without having to go through the court. The third power is pertaining to foreclosure of properties, where Danaharta do not have to go through court process.

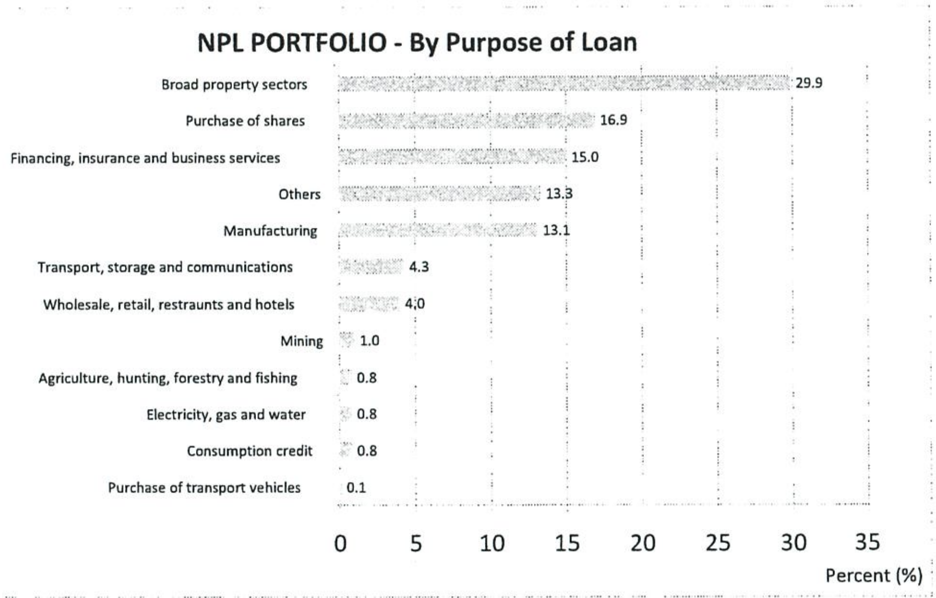
5.1 Acquisition of NPLs

Danaharta did not attempt to remove all NPLs from the banking sector. It merely relieved the banks of their NPLs to enable them to stabilise and continue their operations. The NPLs that remained in the banks were at a tolerable level. Danaharta's removal of NPLs comprised of acquiring and managing NPLs. Acquired NPLs refers to those NPLs which Danaharta purchased from the banks, while managed NPLs refers to those accounts belonging to banks, SIME bank and BBMB banks, where Danaharta managed the loans on behalf of the government and central banks.

Danaharta carried out two major exercises in carving out the NPLs. The primary carve out was from September 1998 to June 1999. In this first exercise, accounts worth RM5 million and above were acquired. The NPLs were both secured and non secured loans. All securities associated with the loans were transferred to Danaharta. By June 1999, Danaharta's NPLs portfolio was RM39.33 billion, out of which RM17.79 were acquired NPLs and a total of 21.54 billions were managed NPLs, taking out 34% of banking system NPL (Danaharta, 2000)

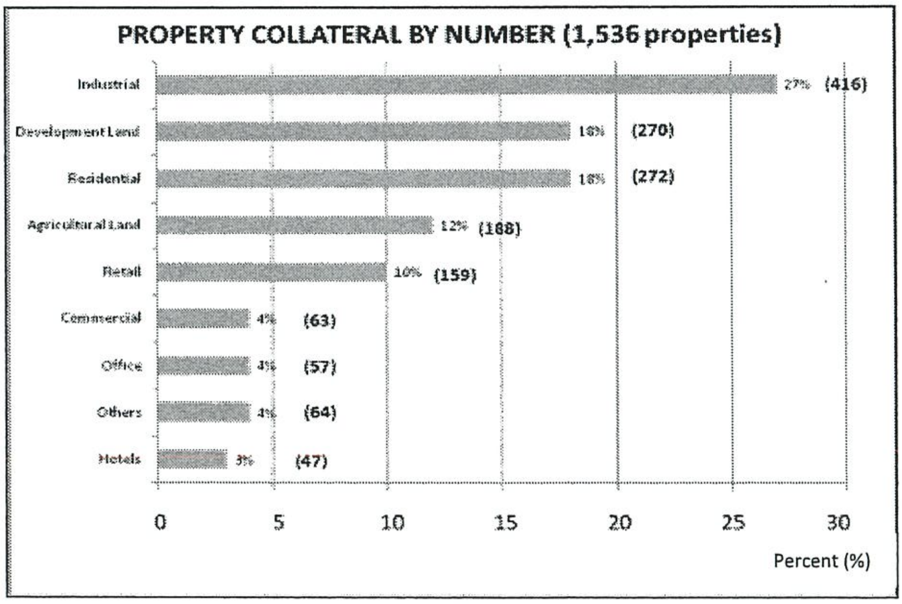
The secondary carve out was from 1 July 1999 to 31 March 2000. During this time Danaharta was very selective. It only acquired loans of borrowers with total value of RM50 millions and above. The secondary carve out raised Danaharta's NPLs portfolio to RM47.68 billion of which RM19.71 billion was acquired assets and RM27.97 billion was managed assets.

About 43% of Danaharta's RM47.49 billion NPLs portfolio was secured by property, comprising 1,536 properties with a total estimated value of RM17 billion. Of these, almost one third are property related loans. Figure 3 shows the NPL profile by purpose of loans. Most of the property related loans were a result of indiscriminate investment in the property market during the boom in the mid 1990s. Property developers and non property developers alike jumped onto the bandwagon to capitalise on the booming market. With the high composition of property in the NPL portfolio, there were concerns from many quarters on the likelihood of Danaharta ending owning and ware housing all of the property assets backing its NPLs.



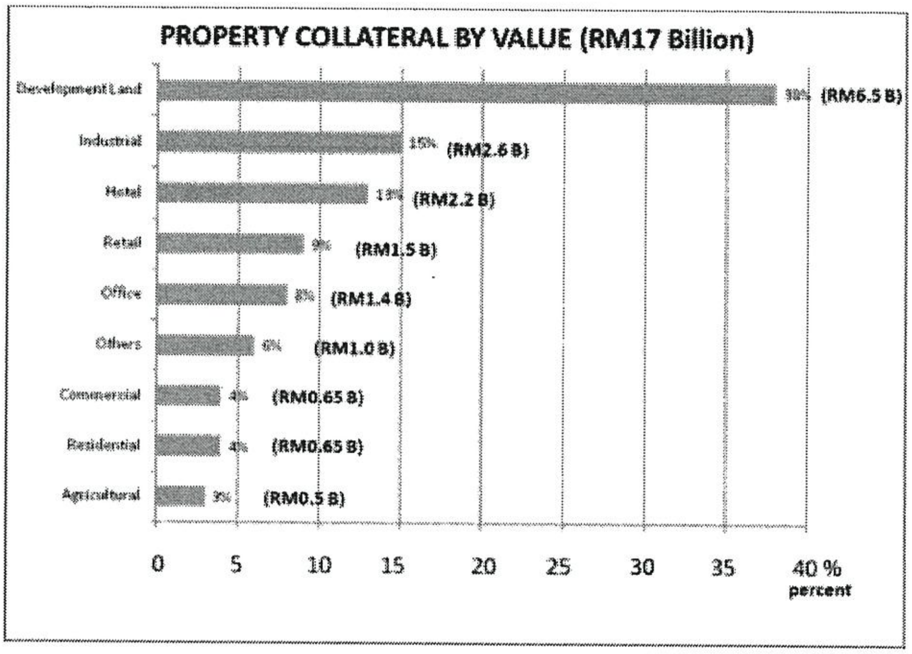
Source: Danaharta (1999)

Figure 3: NPL Portfolio –By Purpose of Loan



Source: Danaharta (1999)

Figure 4: Property Collateral by Number



Source: Danaharta (2000)

Figure 5: Property Collateral by Value

5.2 Acquisition Price

The financial institutions were encouraged to sell their NPLs to Danaharta. For loans that were backed by property collateral, the price paid was the fair value of the underlying property collateral. The fair market value was set at 95% of the market value of the property at the acquisition date, as determined by an independent licensed valuer. As at that time, it was a thin market and the banks were concerned of undervaluation. However, this did not appear to be so as the prices fetched through sales were within the range of the indicative value, i.e. the value set by the independent licensed valuer.

For NPLs backed by quoted shares, the price paid depended on size of the stake in the company that were pledged as collateral. The larger the stake, the higher the control and therefore the higher the price.

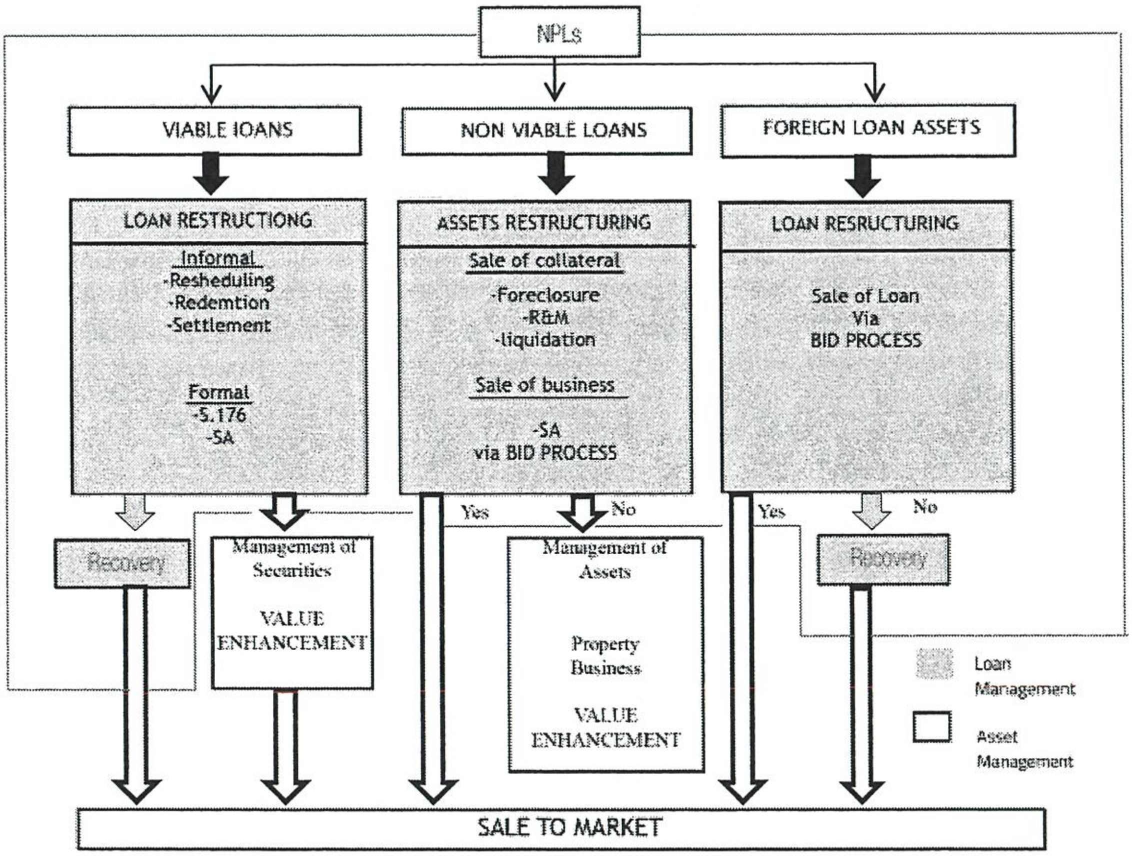
In all cases where the fair value was found to be higher than or equal to the loan amount outstanding, Danaharta's purchase price was equal to the full amount outstanding. Where the fair value was less than the loan amount outstanding, but higher than or equal to the principal amount outstanding, the purchase price was the fair market value. However, in cases where the fair value was lower than the principal amount outstanding, the purchase price would be equal to the principal amount outstanding. For unsecured loans, Danaharta's purchase price was equal to 10 percent of the principal amount outstanding. On average the NPLs were purchased at an average discounts of 54.6 percent. The total purchase price for all the acquired NPLs was RM8.94 billion. The acquisition was paid in cash and bonds.

There was no compulsion for financial institutions to sell their NPLs to Danaharta. This is evidenced by the period up to December 1999 (Danaharta 2000). Offers from Danaharta to purchase RM7.290 billion in book value of NPLs had been rejected by the selling banks. This represented 27.7% of the total NPL (acquired and rejected) of RM26.39 billion. The same happened in the corresponding period of 2001 where RM8.03 billion was rejected by banks representing 28.5% of the total NPL. Loans were bought only if the selling financial institutions felt that the price offered was fair and agreed to do so.

To encourage the financial institutions to sell their NPLs, incentives were offered which included offers to share profits earned from asset recoveries with the financial institution on an 80:20 (Bank:Danaharta) ratio, allowing financial institutions to amortise the shortfall arising from the sale of NPLs for a period of up to five years. Banks that chose not to sell their NPLs to Danaharta had to immediately write down 80% of Danaharta's valuation. This would impact negatively on the profit and loss account.

5.3 Recovery Strategy

As mentioned above it was Danaharta's mission to maximize the recovery value of the acquired NPL. Except for the foreign loans, where Danaharta's legislative bypasses did not work outside Malaysian jurisdiction, it did not dispose the NPLs outright. Danaharta resolve its non-performing assets/loans in a variety of methods. The recovery strategy is contingent upon the best recovery value that it can reap in each. Figure 6 describes the strategy adopted by Danaharta in the recovery of loans.



Source: Danaharta Final Report, 2005

Figure 6: Recovery Strategy

Danaharta tried to turn the assets around and dispose them after value enhancement efforts had been taken. This involved assessing the viability of each of the NPLs acquired and deciding on the appropriate strategy. The NPLs were catergorised into viable loans, non-viable loans, and foreign loans. Viability was evaluated from two aspects, the company and industry viability.

If both the borrower's company and the industry in which it operated were deemed viable, Danaharta would adopt a soft approach. This involved the special administrator preparing a workout proposal which was then given to an Independent Advisor for evaluation, taking into account all creditors and shareholders. Upon approval from Danaharta, with the consent from secured creditors, the workout proposal was implemented. Loans were then restructured by either rescheduling the payments or additional working capital was given. In doing so, Danaharta enhanced the recovery value. The appointment of Special Administrators helped to preserve the value of the company's asset and allowed it to remain as an on-going concern, without which lenders might have to liquidate and weakened the companies and erased their value.

Under the soft approach, borrowers also had the option to choose quick settlements of loans, where they were given 12 months to do so, or borrowers and creditors could voluntarily formulate schemes to restructure loans. This was done under the purview of a special committee who acted as advisors, known as the Corporate Debt Restructuring Committee.

A hard approach would be adopted if the borrower's business was deemed non-viable. It involved the sale of borrower's business and assets. The borrower's business was put up for sale if it was no longer viable but the industry where it belonged remained so. However, in the case where both the company and the industry were not viable, the underlying assets were put up for sale.

As at 31 December 2004, 1298 properties were foreclosed with a total consideration of RM 2.2 billion. The Danaharta Act 1998 allowed Danaharta to sell underlying collateral which were either auction, tender or private contract via a private treaty. In comparison, the financial institutions which were only allowed to sell foreclosed properties via public auction. The flexibility for Danaharta enhanced the chances of selling the properties.

5.4 Recovery

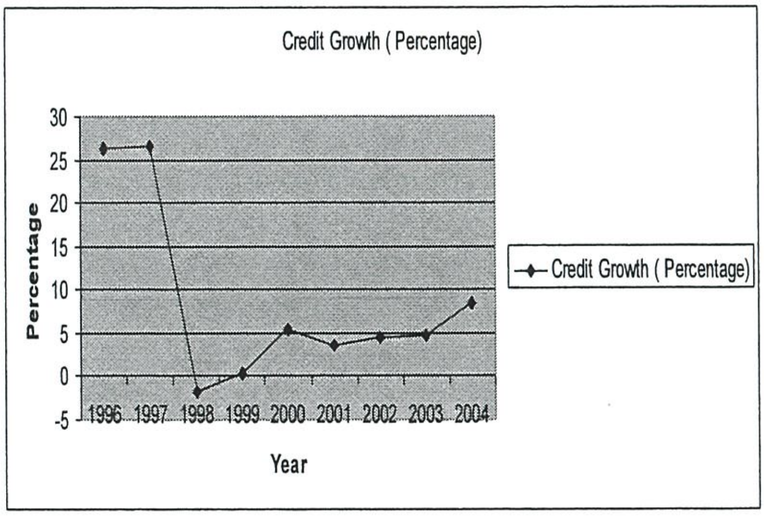
As at 30 September 2005, the total NPLs recovered was RM29.03 billion. This is equivalent to a 55 percent recovery rate. This recovery rate was considered an achievement when compared to similar agencies in the region which achieved between 20 to 50 percent. The total recovery proceeds were distributed to Government and 38 other financial institutions.

When Danaharta ceased operations on 31 December 2005 the residual recovery assets at that time was RM3.66 billion. It reverted to the control of Ministry of Finance Incorporated (MOF Inc.) who subsequently appointed a wholly owned subsidiary, PROKHAS Sdn. Bhd. to act as a collection agent for the residual recovery assets.

6. FINDINGS

By July 1998, the NPLs in the banking sector made up 14 percent of the outstanding loans which was far beyond the tolerable range of 2-3 percent. Credit growth contracted by 1.8 percent. Banks tightened their lending and switched their attention to rehabilitating the NPLs in their books. Danaharta's role was to remove the NPLs pressure from the banking sector and to allow them to concentrate on their lending operations. This was intended to ensure that the real sector of the economy continued to receive financing and generate economic activities. The question is did Danaharta make an impact in stabilising the economy?

By the end of the primary carve out in June 1999 about 34 percent of the total NPLs were removed from the banking sector. This meant that 66 percent was still in the banking system. Although only 34 percent was removed, as shown in Figure 7, credit growth of 0.3 percent was detected in 1999 and 5.4 in the following year 2000. From the year 2001 to 2004 the annual credit growth was between 3.6 to 8.5 percent. This indicates the 34 percent removal of NPLs from the banking system managed to relieve significant pressure from the banks, enabling them to continue their lending operations. Correlation analysis carried out between the carved loans and credit growth shows a strong correlation, with a coefficient of 0.86.

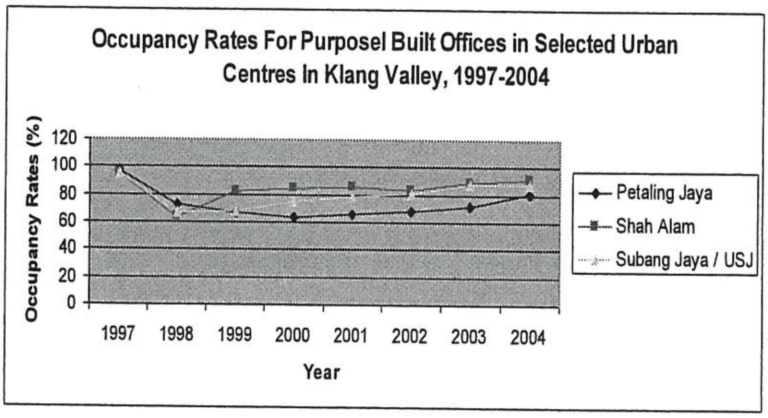


Source: Bank Negara Report, various years

Figure 7 Credit Growth 1996 - 2004

However, in spite of Danaharta's effort to remove from the banking sector, the share of NPLs in banking system and the broad property sector reduced marginally in 1999 until 2001, but went on the increase to a higher level than 1998. This can be explained by the fact that Malaysia like one East Asian Countries, its economy is highly dependent on the property industry. As can be seen from Table 1 above, by the year 2004, 43.9 per cent of total loans were directed to the property sector. As the property prices plunged in 1998 and did not recover quickly, many property loans become non-performing.

The property market was in turmoil in 1998. As shown in Figures 8, 9 and 10, occupancy rates for purpose built offices in selected urban centres in the Klang Valley dropped dramatically. The volumes of residential transactions reduced substantially and the property prices plunged in 1998. However the situation improved in the year 1999 and subsequent years that followed. The improved occupancy rates for purpose built offices meant that new businesses were opening up or existing businesses were expanding. This can be translated into business confidence. Correlation analysis carried out between credit growth and occupancy rates in selected Klang Valley urban centres show a strong correlation with a coefficient correlation of 0.73.



Source: Property Market Report (1997-2004)

Figure 8: Occupancy Rates For Purposed Built Offices in Selected Urban Centres In Klang Valley, 1997-2004

Table 2 shows the result of correlation analysis in respect of carved out loan and credit growth; correlation of credit growth and the property industry performance.

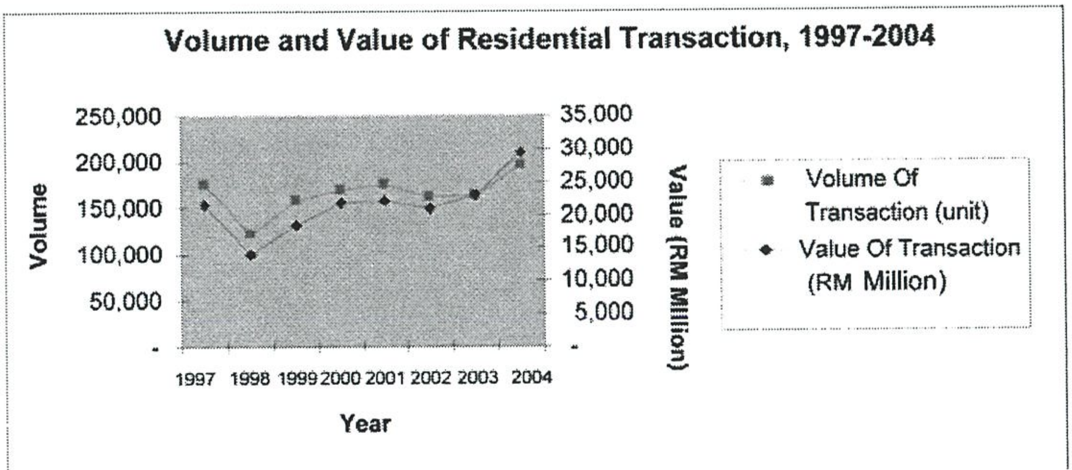
Table 2: Correlation Analysis, Carved out Loans, Credit Growth and Property Industry Performance

Carved out NPLs By Danaharta and Credit Growth		
Carved Out Loan Period	1998-2003	0.86
Credit Growth Period	1999-2004	
Credit Growth and Business Confidence		
Credit Growth	1998-2003	0.73
Occupancy Rates of Purpose Built Occupancy	1999-2004	
Credit Growth and Consumers Confidence		
Credit Growth	1998-2003	0.55
Volume of Residential Transaction	1999-2004	
Credit Growth	1998-	1.0
Value of Residential Transaction	1999-2004	
Credit Growth	1998-2003	0.88
House Price	1999-2004	

Note: Correlation between credit growth and volume of residential transactions is given a one year lag time to reflect the time taken for credit growth to impact on the property market activities.

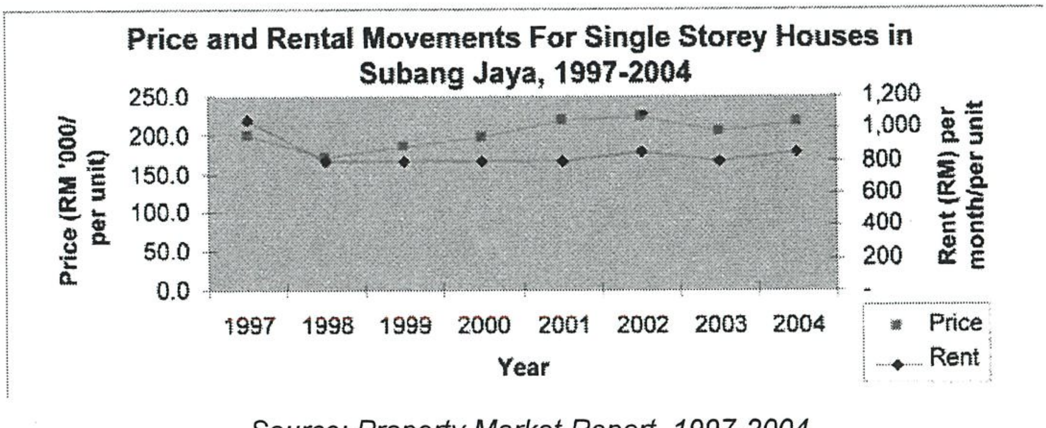
The credit growth not only restored business confidence but also consumers' confidence. This can be seen from the increased volume and value of residential transactions as well as increases in the house prices, shown in Figures 9, and 10. It meant consumers were confident to commit to big capital expenditure, a condition that exists only when there is job security. The correlation between credit growth and the volume and value of residential transactions shows a moderate correlation with volume of transaction (correlation coefficient of 55) and a perfect correlation with value of transaction (correlation coefficient of 1).

The house prices also increased. There is also a positive strong correlation between credit growth and house price. These findings, in line with previous studies that revealed credit growth and an increase in house prices, are somewhat related.



Source: Property Market Report, 1997-2004

Figure 9: Volume and Value of Residential Transactions, 1997-2004



Source: Property Market Report, 1997-2004

Figure 10: House Price and Rental Movements for Single Storey Houses In Subang Jaya

Danaharta's strategy in restructuring or rehabilitating viable loans was equally important. It averted large corporations from liquidation and loss of employment for its workers. In essence, big corporations were given the chance to get out of the red. Danaharta's approach in disposing the non-performing asset is to be commended. It had managed to prevent the property from being sold at fire-sale losses which would have created a panic situation in the industry. Finally, its recovery rate of 55 percent is above the recovery rates of NPLs in the other East Asian economies.

7. CONCLUSION

By 1999, the Malaysian economy was showing signs of recovery. The GDP grew by 5.4 percent. Other economic indicators also showed signs of recovery with inflation and unemployment rates low at 2.8 percent and 3 percent respectively. Even though the total NPLs initially removed from the banking system was only 34 percent, it was enough to help the banks continue their lending operations. Credit growth improved from 1999 onwards.

The most important contribution by Danaharta was the restoration of public confidence in the economy. The restructuring and rehabilitating of viable loans meant that defaulting corporations did not have to liquidate their businesses. Danaharta's move to not rapidly dispose its assets immediately, prevented a property market panic situation and the further falling of property prices. Danaharta was instrumental in the return of broader economic stability and growth in Malaysia.

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