

# Malaysia: Potholes on the Road to 2020

2014 was a year of tragedy for Malaysia with twin airline disasters. However, this should not detract from the country's substantial achievements over the past half-century. Since 2009, the government has pursued economic and political reforms meant to propel the country into developed nation status by 2020 while gradually increasing democratic freedoms. Although considerable progress has been made on the economic front, backlash from conservative groups have stalled some political reforms.

## Truly Asia

Located at the geographical centre of the region, Malaysia is the fulcrum between maritime and mainland Southeast Asia. Like Singapore, the Malaysian government has pursued investor-friendly policies for much of its recent history, although these have had to be balanced with domestic socio-economic goals in the form of affirmative action policies. The latter remains a controversial matter and efforts to roll back such policies have encountered substantial resistance.

The country's ruling coalition, Barisan Nasional ("BN") — for the most part made up of a collection of ethnic-based political parties — has never lost control over the government in the 57 years since independence. The BN's lengthy and uninterrupted rule has provided investors with the comfort of political stability. The cumulative result has been decades of steady growth, barely interrupted by regional and global crises. By the 1990s, Malaysia had emerged as a major centre for electronics production and high-tech manufacturing. On a per capita basis, Malaysia's GDP is second only to Singapore in Southeast Asia.

Now firmly established as an upper-middle income country, Malaysia is attempting to move further up the value-chain to focus on knowledge-based and innovation-driven industries. Soon after taking office in 2009, Prime Minister Najib Razak announced a raft of ambitious economic and political reforms which were meant to improve government finances, steer the country out of the middle-income trap and increase democratic freedoms.

Economic Reform Goals in Figures <sup>1</sup>	
<b>3.3 million</b>	new jobs
<b>USD444 billion</b>	investments
<b>USD15,000</b>	per capita GNI by 2020
<b>12</b>	National Key Economic Areas
<b>6</b>	Strategic Reform Initiatives

<sup>1</sup> Source: Pemandu, Overview of the Economic Transformation Programme, [http://etp.pemandu.gov.my/About\\_ETP/@-Overview\\_of\\_ETP.aspx](http://etp.pemandu.gov.my/About_ETP/@-Overview_of_ETP.aspx)

## Clear Agenda, Clouded Implementation

More than five years after Najib assumed office, the implementation of these reforms has been eclipsed by a series of unfortunate events. It would seem that he could do little right in 2014. Two major aviation disasters involving the national carrier, including the mysterious and still unsolved disappearance of MH370, brought the Najib administration under intense international scrutiny over the handling of these mishaps. On the domestic front, the continuation of a painful but necessary subsidy rationalization program hurt wallets and Najib's approval rating — by October 2014 this had dropped to 48%. In December 2014, the country experienced its worst floods in recent history while Najib was photographed playing golf with President Obama in Hawaii.

More difficult times lie ahead. The government is expected to push ahead with reforms to address structural weaknesses in the Malaysian economy. In 2015, this will take place through the introduction of a long-awaited goods and services tax ("GST") in April. The 6% tax is expected to boost government revenues by MYR10 billion, compared to the current tax system, helping to reduce the fiscal deficit — a major goal of the Najib administration. While observers and market analysts have welcomed the implementation of the GST for its contribution to fiscal consolidation efforts, the population as a whole is markedly less happy satisfied about the move. Lower-to-middle income households are expected to pay the most GST as a percentage of earnings, placing further strain on household budgets and dampening consumption.

The former is no small matter. At almost 87% of GDP, household debt levels in Malaysia are the highest in the region and indeed, in Asia. Debt levels have increased by almost 50% since 2008, when household debt stood at 60% of GDP.

Meanwhile, the drop in global oil prices proved to be a double-edged sword for the Malaysian economy. While low oil prices presented the government with an opportunity to slash fuel subsidies — which it duly seized in December 2014 — it also derives a third of the national budget from Petronas, the national oil and gas company and largest taxpayer. Low oil prices could hamper efforts to reduce the budget deficit in the oil-producing country.

There is also the matter of the government-owned and Najib-linked "strategic development company," 1MDB and its debts of MYR42 billion (around USD12 billion). 1MDB's exact position in relation to government finances is unclear; the government claims that it guarantees only 14% of the company's debt but the investment community believes that there is an implicit guarantee on 1MDB's debts, in which case it could strain Malaysia's debt position.

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Like many of its neighbours, corruption remains a challenge in Malaysia although the country's ranking on several corruption indexes has improved slightly in recent years. Najib has made commendable efforts to eliminate corruption but some policies — notably the award of government procurement and public work contracts without competitive bidding or open tenders — remains unchanged and open to abuse. Open tenders are mandatory only for contracts worth more than MYR30-50 billion.

### Moving Away from the Middle

While progress has been made in the matter of subsidy reduction and the gradual liberalisation of various sub-sectors of the economy, political reforms have stuttered along in the face of opposition from Najib's own party, United Malays National Organisation ("UMNO") — the dominant party within BN — and right-wing Malay groups. An earlier promise to repeal the Sedition Act, — an archaic law which was used frequently in 2013 and 2014 to arrest and bring charges against critics of the government, — was dropped in the face of overwhelming opposition from UMNO. An internal poll found that 85% of party divisions opposed the plan to repeal the act, a wish that Najib duly granted at the party's general assembly in November.

Although the BN can still boast of unbroken rule over Malaysia, the coalition's position is under threat. In the 2013 general elections, the coalition clocked its poorest performance ever with only 46% of the popular vote. This delivered a stunning blow to Najib's leadership of UMNO. Having steered the country in a more progressive direction prior to 2013, he was seen as the cause of the party's decline and the weakest leader the party and BN have ever had. As the leader of BN and UMNO, Najib was blamed for their poor showing in the 2013 elections despite the fact that he has been consistently more popular than the party and coalition he leads.

Since the 2013 elections, Najib has found himself in a considerably weaker position compared to the pre-election period. Criticism of his administration's policies has come from not just the opposition but also members of his own party, including the formidable former Prime Minister Mahathir Mohamed, who helped engineer Najib's ascendancy within UMNO in the late 2000s. Within UMNO, divisions between the liberal elite and its conservative factions have come to the fore. This rift places Najib and his allies on one side of the fence, facing his deputy and other likeminded politicians who favour *Ketuanan Melayu*, or Malay sovereignty, over Najib's own unity-promoting programme, 1Malaysia.

The increasing prominence of the *Ketuanan Melayu* narrative parallels a rise in religious fundamentalism in Malaysia. Recent years have seen a number of disquieting developments including a ban on the use of the word "Allah" by non-Muslims, attacks on churches and a foiled Islamic State plot to attack several sites in the country. The shift towards religious fundamentalism has not gone unopposed by more liberal segments of society but the contest for the country's future is likely to be a long-drawn and ongoing one.

### Steering the ASEAN Economic Community Beyond 2015

It is against this backdrop that Malaysia has taken the chairmanship of ASEAN, a position it will hold for the rest of 2015. As well as other initiatives, Malaysia's responsibilities in this role include overseeing the process of regional economic integration through the ASEAN Economic Community ("AEC"). Of equal importance is the country's task of formulating the ten-year roadmap for the ASEAN Community post-2015. In this leading role, Malaysia has the opportunity to set the pace of regional economic integration but also the unenviable task of balancing the competing interests of member states.

Najib may be short on domestic support but he is adept on the international stage, having successfully upgraded bilateral ties with both the U.S. and China to comprehensive partnerships during the past two years. One proposal which he has put forward to ensure the success of the AEC and the wider ASEAN Community is to further empower the Jakarta-based ASEAN Secretariat by having member states increase funding and staffing levels at the secretariat. While Malaysia may be willing to commit additional funds and support to the secretariat, convincing other ASEAN states — particularly the grouping's poorer members — of this will be an uphill climb.



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