

*From the Desk of...***Hans Vriens**

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What path now for Malaysia?

Hans Vriens, veteran advisor on public policy in Asia, shares his views on Malaysia's widely-expected general election next year and asks; is this a country moving forwards, or backwards?

After winning two by-elections recently Barisan National (BN), the coalition that has governed Malaysia since independence in 1957, seems to be gearing-up for general elections in the first half of next year. It was the best result for BN in by-elections since Najib Abdul Razak became prime minister shortly after the disastrous general elections in 2008. In these general elections BN lost its two-thirds majority for the very first time to a resurgent opposition coalition led by Anwar Ibrahim.

The increasingly confident prime minister wants his own electoral mandate. The budget Najib presented last month made this clear as well. Instead of focusing on badly needed reforms to make Malaysia more competitive the budget was big on pump-priming. The 33-minister strong Najib administration has allocated close to RM100 billion (USD35 billion) in new grandiose projects ranging from the construction of a 100-storey tower to RM47 billion mass-rail transit network and the building of the usual new highways and power plants.

It felt like the good old days of Prime Minister Mahathir Mohamad were back. During his 22-year undisputed reign that ended in 2003 Dr. Mahathir launched numerous ill-advised grandiose projects he thought would transform Malaysia into a developed country by 2020. One example is the national car, the Proton, which still continues to bleed money and cost vastly more in opportunity cost. As a result of the high tariff walls that had to be erected to protect the Proton, Malaysia failed to build a successful car industry, while free-trading Thailand became the hub of car manufacturing

in Southeast Asia, thanks to Toyota, Ford and Nissan. Thailand these days is even exporting Japanese cars to Japan. Dr Mahathir's decision to direct the ethnically Malay ruling party UMNO into business in a major way changed the nature of the party, from one led by school teachers whose dues financed the party to a party of cronies who used their party links to steer multi-billion dollar contracts to their companies.

The Mahathir days are indeed back, judging from Najib's budget. His strangely named Economic Transformation Programme (ETP) envisions a revival of foreign direct investments and promises to create three million new jobs over the next ten years. By that time, according to the ETP, Malaysia will have achieved developed economy status. He is dreaming. And he knows it.

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The ETP raises three questions: Can Malaysia afford it? What happened to the political reforms Najib announced earlier in the year? And especially, will he honour the promise to transform Malaysia into a society based on merit instead of race? The ethnic Malays have enjoyed many privileges since 1971, officially to allow them to catch up with the economically more successful Chinese thirty per cent of the population. In reality the so-called New Economic Policy (NEP) created an apartheid style society, where everything is determined by race instead of merit, from access to universities to entrance into the civil service. Virtually all the 1.2 million civil servants in Malaysia are ethnically Malay after 40 years of NEP.

Many ethnic Chinese, who can afford it, send their children to universities overseas. An ethnic Indian underclass could neither enter university nor the civil service. The NEP, which demanded that Malays own 30 per cent of companies, made a small number of politically-connected Bumiputra or Malay businessman very wealthy. This small group form the real beneficiaries. These cronies are the ones who are staunchly opposed to the erosion of Malay privileges. They even established a Malay rights movement, Perkasa, to defend themselves, and Perkasa can count on the support of Dr. Mahathir. They will not allow Najib to tinker with the race-based policies.

Can Malaysia afford carrying on like before? Not for much longer. The golden days of Malaysia as a petro state will soon be over. In 2014 Malaysia will become a net importer of oil and gas. Oil products are subsidised to keep the Proton-driving Malaysian middle class happy. Najib has postponed further cuts in subsidies. This is unsustainable. The government already runs a budget deficit of 7.4% of GDP. It may not be Greece yet, but worse is to come. Forty per cent of the national budget comes from the oil and gas sector.

At the same time Malaysia's other engine of economic growth, direct investment from overseas into factories - producing electronics in Penang and call centres in Kuala Lumpur - has come to a crashing halt. Last year Malaysia was even a net exporter of capital. Malaysian companies have also figured out there are better growth opportunities overseas. In the meantime many multinationals have relocated

their factories and offices to China, India, Vietnam and the Philippines. The Malaysian workforce is poorly educated and expensive compared to their neighbouring countries. Many Malay students seem to prefer Malay or Islamic Studies over engineering. Islamic Studies may be good enough to become a civil servant but it doesn't really prepare you for a globalised world. An earlier move to change the medium of education from English to Malay has also put Malaysia at a distinct disadvantage compared to India and the Philippines. The World Bank has warned about the dismal state of the state-run education system. As a result of all this Malaysia has fallen off the investment map.

Prime Minister Najib may be able to pump enough money into the economy to win back the two-thirds majority for the ruling coalition if he feels confident enough to call a snap election in the next few months. However, this will not solve any of the structural problems Malaysia is facing. The UMNO inward-looking political class is devoid of ideas - beyond playing the Malay supremacist card - and obsessed with protecting its own financial privileges. It cannot see the elephant in the room. One only has to look at Eastern Europe in the eighties to see how the people reacted when governments were forced to put their financial houses in order and slash subsidies. Najib's and UMNO's inability to push through necessary reforms now does not bode well for the future. Malaysia seems destined to remain trapped in a middle income trap. ■

About Hans Vriens and The Insight Bureau

Hans Vriens is one of the leading independent advisors on public policy in the Asia Pacific region, with almost 20 years of experience following the political shifts taking place across a number of key countries. Based in Singapore, he has been counsel to chief executives and board members on market entry strategy, regulatory affairs and managing sensitive issues across Asia. He has particularly strong experience in Southeast Asia, China and India. Hans frequently provides background briefings to visiting executives to help them understand political, economic, cultural and business developments in the region. He is able to provide unique and frank analysis thanks to the many research and consultancy projects he has led for leading multinationals and governments around Asia over recent years. <http://www.insightbureau.com/HansVriens.html>

The Insight Bureau provides speaker placements and briefings as a service that helps achieve a better understanding of the world in which we do business and to ultimately help senior executives to make better business decisions. The Insight Bureau represents Hans Vriens for speeches and briefings.

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