

RAMON V. NAVARATNAM

Malaysia's Economic Challenges

A Critical Analysis
of the Malaysian Economy,
Governance and Society



ASEAN ACADEMIC PRESS

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ACADEMIC PUSHTAKA PERDANA
London



1006103

Introduction

THIS book discusses the challenges and prospects that lie ahead as Malaysia marches towards Vision 2020 and beyond. It traces the evolution of Malaysia's socioeconomic policies and developments, as they unfolded in real time, over the critical period between 1995 and 2001. It covers the period before, during and after the Asian financial crisis of 1997 right up to the end of 2001.

These impressive years of rapid economic development since Malaysia's Independence in 1957 have given the country the reputation of being one of the most successful and advanced developing countries in the world. Also, in recent years, Malaysia has earned the distinction of being the most modern and progressive Muslim country.

However, all these accolades were brought to an end when Malaysia and other Asian countries suffered serious recessions in 1998 (recessions that were caused mainly by currency attacks initiated by highly leveraged and speculative unregulated hedge funds and vicious currency speculators). These unfettered hedge funds were allowed to operate without proper management; they were like irresponsible financial cowboys who inflicted chaos and much damage to the Asian financial markets and thus destroyed much of their hard-earned wealth!

Most western analysts and particularly the cynical western mass media attributed the Asian financial crisis to cronyism, corruption and nepotism. These criticisms persisted with a vengeance, until the scandals of the Long-Term Capital Management (LTCM) hedge fund, the collapse of Enron Corp. and other major business scandals, shook corporate America and forced these critics to reluctantly examine their own sophisticated backyards first, before throwing stones so brazenly at Asian glass houses!

This book then covers the unorthodox policies adopted by Malaysia (such as foreign exchange controls) to recover from the recession and to avoid the social and political upheavals that some other countries had to endure because, unlike Malaysia, they faithfully followed the IMF's simplistic cookie-cutter economic prescriptions.

In this book, the commendations and criticism of many Malaysian government policies have been made in good faith. The candid comments are intended to encourage more open debate and discussion in Malaysia where, as in most developing countries, the tradition of honest professional commentary is not sufficiently strong, although it is admittedly growing.

However, the main value of this book is that it includes my most significant analysis of some controversial internal socioeconomic public-policy issues, and the public responses to these policies, as they actually occurred on an ongoing basis. Thus the real thinking and the sense of feel for and the spirit behind these major public-policy changes of that time have been carefully captured. All these developments reflect the intellectual arguments, the concerns and doubts, the uncertainties and the public debate, at the very time of policy formulation and execution.

Hopefully, an honest assessment of these vital socioeconomic developments that took place in the political context of the period between 1995 and 2001 will provide reliable background material and valuable insights into the thinking behind the policies at that time, so that public debate would be stimulated even further, to enhance policy planning and implementation.

Such appreciation will thus enable policymakers, economic planners and researchers to have a better understanding of important socioeconomic developments and to experience "genuine empathy" for the Malaysian economy, during those challenging times of the country's hazardous march to realise the aspirations and goals of Vision 2020, i.e., to become a developed nation by the year 2020.

Thus the progress to achieving developed-nation status by 2020 could be strengthened and even hastened. Also, economic planners in other developing countries may be able to learn from our pitfalls and the success of the Malaysian model of socioeconomic development and aim to do better.

In Part I, "Managing the Malaysian Economy: Challenges and Prospects (1995-1997)", I have taken a critical look at socioeconomic developments in Malaysia from 1995 to 1997 by commenting on public policies that were introduced even before 1995, but which have had a strong bearing on policy developments that emerged before the onset of the Asian financial crisis in July 1997. (The Malaysian economy, which had enjoyed spectacular growth for nine consecutive years, was jolted from its euphoria in July 1997, when the vicious contagion effect arising from the *de facto* devaluation of the Thai baht sent East Asian currencies and stock markets nosediving to lows the likes of which had never been seen before.) Here, I argue how Malaysia's unique economic model worked well to advance its progress to a higher level, compared to most of the other developing countries and to introduce reforms that are essential to strengthening the economy.

In Part II, "Strengthening the Malaysian Economy: Policy Changes and Reforms (1997-1998)", I have highlighted critical economic developments during and after the Asian financial crisis of 1997 and the policy measures that were taken to expedite economic recovery.

It was a period of struggle and painful recovery with considerable uncertainty as to whether the introduction of unorthodox economic, fiscal and monetary policies would actually work, given the severe criticism of foreign analysts and investors. Malaysia had defied the IMF and the soothsayers of doom, both at home and especially cynics abroad, who had doubts as to whether Malaysia had taken the right decision. However, as the record shows, Malaysia has been proved right! But there must be more healing in the economy.

Part III, "Healing the Wounded Tiger: How the Turmoil is Reshaping Malaysia (1998-1999)", looks at the Malaysian economy after the country began to recover from the severe beating it took from the Asian financial crisis and as Malaysia moved into the 21st century.

The healing of economic and societal wounds were not easy. Having been called a "Tiger Economy" because of its rapid economic growth and its unprecedented success in "social engineering", it was time to lick its wounds and consolidate its recovery. Indeed, Malaysia had to ensure that there was rapid "healing" of the economy, if Malaysia's economic recovery was to be sustained via policy reforms.

In Part IV, "Malaysia's Economic Recovery: Policy Reforms for Economic Sustainability (1999-2000)", I have provided considerable analysis of the policy measures that were thought to be necessary to unwind some of the earlier strategies that were meant to stimulate economic recovery and not necessarily longer-term sustainability.

Such issues as exchange controls and the continuing currency peg are reviewed for their future relevance. Fresh ideas are introduced on how to sustain the remarkable recovery that was achieved, despite opposition from orthodox critics.

Longer-term policy issues like national unity, globalisation, higher productivity and strengthening national resilience, are critically examined and questioned. Recommendations are made to overcome structural problems so as to sustain the economy, especially in the light of new global realities.

I conclude my analysis with Part V, "Malaysia's Economic Sustainability: Confronting New Challenges Amidst Global Realities (2000-2001)", by further questioning the sustainability of Malaysia's economic success as the nation moved into the 21st century.

Increasing international competition, the serious challenges of globalisation and from the Asean Free-Trade Area (AFTA) and the threats and opportunities posed by the emerging giant economy of China, are brought into sharper focus as the Malaysian economy confronts the sharp edges of greater global competition. Also, the impact of the September 11, 2001 terrorist attacks on the U.S. and the activities of international terrorists and their root causes are examined to seek solutions from an economic point of view.

Malaysian Prime Minister Dr Mahathir Mohamad has undoubtedly led Malaysia impressively into the 21st century. With him at the helm, Malaysia is today a modern developing nation that is moving steadily towards industrialised-nation status by the year 2020. With his deep convictions and charismatic leadership, Dr Mahathir has won many economic and political battles in his more than 20 remarkable years as premier of Malaysia.

However, questions are now being raised about the future direction of the Malaysian economy, despite the impressive achievements of the Malaysian economic model. The affirmative-action policies, i.e., the New Economic Policy (NEP), are reviewed in the context of the growing impact of global realities and the need for more liberalisation and the ongoing preparation for the transfer of leadership to Deputy Prime Minister Abdullah Ahmad Badawi in October 2003. The PM designate has already reinforced Dr Mahathir's call for a major shift in the "mindset" of all Malaysians to face the challenges of an increasingly globalised economy.

This book therefore analyses the major socioeconomic developments between 1995 and 2001 and all the challenges and responses over this critical period. We will face more challenges in the future.

However, I am confident that Malaysia and Malaysians will face up to the new challenges and opportunities that confront Malaysia in the spirit of the country's proven track record and continuing sound political and pragmatic economic management.

I believe that Abdullah Ahmad Badawi will build upon the outstanding economic achievements of Dr Mahathir, and enable Malaysia to become an industrialised nation by the year 2020.

This book is a compilation of five previously-published books on Malaysian economic development (as well as on international developments): *Managing the Malaysian Economy: Challenges and Prospects* (1997); *Strengthening the Malaysian Economy: Policy Changes and*

Reforms (1998); *Healing the Wounded Tiger: How the Turmoil is Reshaping Malaysia* (1999); *Malaysia's Economic Recovery: Policy Reforms for Economic Sustainability* (2000); and *Malaysia's Economic Sustainability: Confronting New Challenges Amidst Global Realities* (2002). What I have attempted is to put into a single succinctly written package a broad-ranging overview of the Malaysian economy between 1995 and 2001.

Throughout these commentaries, readers will observe Malaysia's special brand of pragmatic and innovative approaches to economic management—which I have called “*Malaysianomics*”. Malaysia has not followed any one school of economic thought or any single management model, but have been open to all that is best for the country.

Hopefully, those interested in the evolution of the Malaysian economy and its domestic and foreign policies would find this book relevant. It will also be of interest to anyone wishing to use the Malaysian experience as a case study of the impact of globalisation on developing economies.

Ramon V. Navaratnam

May 2003

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