

HIS ECONOMIC LEGACY

Lasting Achievements

In *his own* words, *Mahathir* diagnosed Malaysia's problems and treated them. But he also *created problems that will be hard for his successors to solve*

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By S. Jayasankaran/KUALA LUMPUR

MAHATHIR MOHAMAD'S economic legacy is a chequered one. But its hallmark has been his pragmatic response to crises, even if it meant sharp shifts in strategy or gambling on unpopular policies. Maybe he was simply thinking like a doctor. "I think my medical training has helped me," he once declared. "You diagnose the problem and you treat its symptoms."

In 1985, for example, Malaysia fell into recession amid low global commodity prices, high unemployment and a record budget deficit. Mahathir responded by relaxing a 15-year-old affirmative-action policy that aided ethnic Malays—once a cornerstone of his own Malay nationalist ideology—in favour of opening up the economy to foreign investors. It worked: From 198X-97, more than \$52 billion in foreign direct investment—more than 10 times the amount in the previous decade—flowed into Malaysia, helping to underpin a decade of unprecedented prosperity.

Then in 1998, faced with a tumbling ringgit in the wake of the Asian financial crisis, Mahathir—who had embraced the global capitalist system in the 1990s—unplugged Malaysia from world financial markets. Against the advice of his central bankers, he banned offshore ringgit trading, imposed capital controls to limit currency movements and pegged the ringgit to the U.S. dollar. The radical moves sparked criticism, but eventually helped to stabilize the economy.

Such bold steps won Mahathir, now 78, admirers. To them, he was the decisive, blunt-spoken problem-solver, and the great modernizer.

Over his 22 years in power, Malaysia evolved a huge, multiethnic middle class—more than 60% of households now have cars, TVs and basic amenities—which has helped to consolidate economic and political stability. "It may be Dr. Mahathir's lasting achievement," says Musa Hitam, a former deputy premier. "For these people, the differences aren't ethnic but class ones: the second car, the mortgage. They have a stake in the economy and no one wants to rock the boat."

Indeed, by many economic measures, the national well-being has improved. Per-capita incomes have tripled since Mahathir came to power—to 14,877 ringgit (\$3,915) in 2002 from 4,630 ringgit in 1982. And the poverty rate has dropped to 5% of all households from more than 35% in 1982.

Mahathir also spotted trends faster than most. In 1984, for example, he saw that tourism was a potential money-spinner and backed projects to attract visitors. Tourism has now topped oil and gas receipts in terms of annual foreign-

exchange earnings and visitors have jumped seven-fold to 14 million in 2002 from 2 million in 1985.

Mahathir's most astute trend-spotting may be manifested in the Multimedia Super Corridor, a hard-wired hi-tech zone south of Kuala Lumpur that he wants developed into Malaysia's version of Silicon Valley. Still in its early stages, the MSC has attracted a steady influx of local start-ups and foreign multinationals.

But Malaysia's progress isn't all Mahathir's doing. In 1981, he inherited control of a reasonably vibrant economy with well-established government institutions. His predecessors had actually done better in some respects. "Between 1961 and 1981, Malaysia's real GDP grew 7% annually," says Tan Teng Boo, the chief executive of icapital.biz, an investment advisory firm. "Over the next 20 years, the figure dropped to 6.2%."

MAHATHIR'S HALLMARK HAS BEEN HIS PRAGMATIC RESPONSE TO CRISES, EVEN IF IT MEANT SHARP SHIFTS IN STRATEGY OR UNPOPULAR POLICIES

Even the popular notion that Mahathir transformed Malaysia from a sleepy rubber- and tin-producer into an industrial hub is misleading: In 1981, the country already possessed a significant industrial base, with manufacturing accounting for 19% of GDP. The figure today is close to 33%, primarily due to the deluge of foreign direct investment after Mahathir opened up the economy.

But global events also pushed the change: Japanese, Korean and Taiwanese manufacturers relocated their factories to Southeast Asia after the Plaza Accord in 1985 boosted the yen's value against the dollar. That helped make Malaysia the 17th largest trading nation by 1995 and explains why Mahathir is so closely associated with its industrialization.

In fact, much of Mahathir's own industrialization strategy failed. Early on, the premier promoted the creation of state-backed, capital-intensive heavy industries, including steel, cement and car making, funded largely by low-interest yen borrowings from Japanese aid agencies. Today, state-owned Perwaja Steel is insolvent and burdened with more than 10 billion ringgit in government-guaranteed debt,

while two thirds of Malaysia's cement plants were bought by foreign companies after the Asian Crisis rendered them unprofitable.

Now, only car making survives. And the profitability of national car-maker Proton depends on steep tariffs that make foreign cars much more costly. But Malaysia's home-made cars will face tough competition after 2005, when most tariffs on regional goods are to be lifted under a pact to create a Southeast Asian free-trade area.

The amount of money lost in Malaysia through waste, corruption and mismanagement over the last 20 years would have severely stretched less resource-endowed countries. Based on published data, the REVIEW estimates that between 1980 and 1997, at least 25 billion ringgit was squandered through financial misadventures. These include the central bank's disastrous foray into currency speculation in the mid-1990s, a failed attempt to corner the world tin market, the Perwaja fiasco and bailouts of state-owned banks. Moreover, the government's own estimates indicate that it will have to spend an additional 20 billion ringgit renationalizing services—such as urban light-rail transit systems and the national airline—that were privatized but went bust after the 1997 financial crisis.

LONELY ROAD:

“A balance sheet for the Mahathir era suggests that he has much to answer for,” says University Malaya economist K. S. Jomo, referring to those financial excesses. (See also K.S. Jomo's commentary on page 25.)

With the economy, as with much else, Mahathir did it his way

Even Malaysia's 1985-86 recession was partly self-induced. During the 1980s, the government overspent with an expansionary fiscal policy, which was then exacerbated by its commitment to heavy industry and the yen's 70% appreciation against the dollar following the Plaza Accord. The soaring yen hugely increased, in ringgit terms, Kuala Lumpur's debt to Japanese aid agencies.

Another-hallmark of the Mahathir era was an extensive privatization programme, which featured billions of dollars in sales of state assets and the awarding of huge infrastructure projects to the private sector. Begun in 1984, privatization unlocked new wealth for private investors and businesses, created many jobs, deepened the stockmarket through new listings and spawned a new class of entrepreneurs.

But it came at a great cost. To create a class of Malay entrepreneurs, the government routinely dished out awards to politically favoured individuals and companies without competitive bidding. The Renong group, once the investment arm of Mahathir's political party, for example, received 15 privatization awards in the late 1980s and early 1990s, including the 6.4 billion ringgit North-South Highway.

Instead of fostering transparency and good corporate governance, privatization came to be identified with cronyism. “No competition meant there was no benchmark to see how fat the actual award was.” acknowledges a Malay businessman. And, he says, it has created a problem for the future: “People who lived off this easy money can never compete and may have to resort to shady deals. It's one legacy that will take time to remove because many people are used to it.” ■