

Najib's NEM to dismantle subsidy regime
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Malaysia is considering proposals to end its subsidy regime and phase in a new goods and services tax as it begins dismantling a four-decade race-based economic system that has deterred foreign investment.

The economic regime adopted after race riots in 1969 has given a wide array of economic benefits to the 55 percent Malay population, but investors complain it has led to a patronage-ridden economy that has resulted in foreign investment increasingly moving to Indonesia and Thailand.

NONEThe cabinet has seen the reform proposals, which will be reviewed again before Prime Minister Najib Razak presents them at the "Invest Malaysia" conference this month, a government source who has seen the plans told Reuters.

"The proposal cites political implications for some of the measures and calls for the government to make some tough decisions," said the source, who could not be named because of the controversial nature of many of the policies.

An aide to Najib declined to comment, saying the plans, which will be open to public discussion before taking effect in June, would be unveiled only at the end of this month.

The government last weekend abandoned politically sensitive plans to introduce a goods and services tax just weeks after scrapping petrol price increases aimed at cutting its subsidy bill, and an electricity price hike. It cited a need to "engage with the public" as reason for the delay.

The government will end budget crippling price controls and subsidies, mainly for fuel, food and power "with minimal exceptions", according to the reform plans, drawn up by a government advisory body.

"The savings should then be allocated to widen the social safety net for the bottom 40 percent of households," the source said.

The shift mirrors the opposition's policy of targeting benefits at the poor regardless of race, although as the majority of poor are Malays, it may have little change on outcomes or on the wider system of preferences enjoyed by Malays.

The reform plans also call for reductions in personal and company tax rates, although the levels were not specified.

Najib has already rolled back elements of the Malay affirmative action policy, relaxing a rule that companies must offer stakes to indigenous ethnic Malays.

Policy flip-flops

A series of policy flip-flops in recent years have dogged Malaysia's reform efforts and the country has seen net foreign direct investment outflows to the tune of RM26.1 billion over

the past two years.

Malaysia attracted 31 percent of the total foreign direct investment that went to Malaysia, Indonesia and Thailand in 2008 versus half of that total in the 1990-2000 period, according to UN data.

Foreign ownership Malaysian shares dropped to 20.4 percent of market capitalisation at the end of 2009 from 26.2 percent at the end of 2007, according to official data.

Malaysia will seek to position itself in high growth industries under the new reform proposals, aiming to achieve per capita gross national income of \$17,000 by 2020, which would make it a developed nation by World Bank standards.

Countries such as South Korea and Singapore have already made that leap.

Without a radical reshaping of its economy and a move away from low-value added electronics exports and labour intensive commodities industries, Malaysia risks losing ground to the likes of China and Vietnam and not making it to developed nation status, a recent World Bank report said.

It is unclear how far the proposals will go in reshaping Malaysia's social system, blamed by some political analysts and economists for fostering graft and an uncompetitive economy.

"If the government wants to do it right, you will have to rope in everyone including the opposition," said Shaharuddin Badaruddin, associate professor at Universiti Teknologi Mara in Kuala Lumpur.

"This is the biggest difficulty now for the government in terms of implementing economic reform politics."

Polarised political system

Malaysia's political system has been polarised by the trial on sodomy charges of opposition leader Anwar Ibrahim, who says they are part of a political conspiracy.

The current system gives majority Malays a range of benefits, from cheap loans and discounts on property to preferential access to education and preferential equity in companies.

The government has repeatedly sought to reassure Malays, its core voter base, their rights would not be eroded even as it tries to woo back ethnic Chinese and Indian voters who deserted the coalition in droves in the 2008 general election.

The report said a backlash against the proposed reforms could come from industries that have enjoyed protection from competition as well as from politicians whose constituents did badly out of the planned changes.

The blueprint offered no details on cutting the budget deficit other than through "prudent spending", although a higher growth target of 6.5 percent annually would boost tax revenues.

The economy shrank by 1.7 percent last year.

Under its 2010 budget, the government had planned to reduce subsidies by RM3.6 billion this year by altering its petrol subsidy regime from May, a measure that will now not likely happen until after elections, due by 2013, but which political analysts say could come in early 2011.

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