

Dr M, Pak Lah and the economy

COMMENT
BY WONG SULONG

ONE of the things that infuriates former Prime Minister Tun Dr Mahathir Mohamad is the claim that he had spent all the money when he handed over power to Datuk Seri Abdullah Ahmad Badawi.

The Tun hotly disputes this and says the country has plenty of funds and the present Government could implement some of the mega projects approved under his administration. As examples, he said the Government could use funds in Petronas and the Employees Provident Fund.

I am not quite sure if anyone had specifically accused the Tun of leaving his successor with a bankrupt Treasury. Certainly, there were comments made by a number of economists and analysts that when Pak Lah took over the reins of Government at the end of October 2003, as much as 75% of the funds allocated under the 8th Malaysia Plan (2000-05) had already been spent or committed.

To appreciate the controversy, we need to go back to a bit of economic history.

When the 8MP was unveiled, Malaysia was just emerging from the throes of the Asian financial crisis. The economy was still weak, and investor confidence fragile.

The Government under Dr Mahathir felt it was imperative that it bolstered the sluggish economy through pump priming, meaning spending more money to lift the economy since the private sector was holding back its investments.

The strategy worked and, as a result, the economy was nursed back to reasonable health.

But there was a cost. Pump priming was implemented at the expense of a growing budget deficit, meaning government expenditure was higher than revenue.

The state of the Government's finances is similar to the finances of an ordinary family - only many, many times larger and more complex.

Say, a family's monthly income is RM8,000, and the total spending of that family is RM10,000. The deficit is RM2,000.

Now, this is tolerable if the deficit is temporary (say, a couple of months) and the family can call on its savings to make up for the shortfall. But if the family continues to incur a deficit and resort to debt to make up for the shortfall, sooner or later that family will be in deep financial trouble.

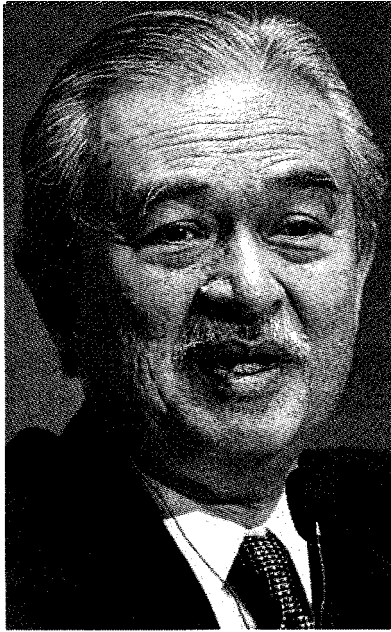
It's the same with a country.

When Abdullah took over, the Government's budget deficit was a matter of concern.

According to Treasury figures, the budget deficit was RM20.25bil in 2002 and RM20.93bil in 2003. This was equivalent to 5.6% and 5.3% of Gross Domestic Product (GDP) respectively.

A rule of thumb among international financial circles is that a 5% budget deficit to GDP is a warning sign.

A government that continuously chalks up budget deficits above 5% would be seen as profligate, and confidence in that government's economic management would erode, and could lead to a massive capital flight.



Abdullah: Is building upon the success of his predecessor

Therefore, when Abdullah took over the administration he was confronted with an unenviable choice: take the populist approach and continue with budget deficit financing or impose fiscal restraint and upset vested economic interests.

Abdullah chose fiscal restraint. As he said, it was the most difficult choice he had to make as Prime Minister.

Fiscal restraint means cutting off or postponing projects that are either wasteful, not a priority or could be deferred until a later stage when the Government's finances are stronger.

In doing so, Abdullah had endured a lot of anger and criticism from vested-interest groups, who had been too reliant on government contracts for their prosperity, many of whom are from his Umno party.

The Government's policy of fiscal discipline is yielding results. According to the Treasury's Economic Report, the budget deficit has been reduced to 4.3% of GDP in 2004, 3.8% in 2005 and is expected to fall further to 3.5% in 2006.

Had the Government allowed the budget deficit to grow, the Government and national debt rating could be downgraded to junk bond status.

Can you tolerate a scenario where Malaysia goes to the international capital markets for a loan and is being charged 7% or 8% higher than Thailand or Indonesia?

In my view, the Government must strive for a balanced or surplus budget.

What about Dr Mahathir's argument that the Government should tap the funds in Petronas and EPF? He suggests these funds are lying idle. "It's like keeping money under the pillow," he said.

I think it's unwise to look towards Petronas and the EPF whenever the Government faces a financial shortfall.

It must be clear: Petronas and EPF money are not there for the Government's taking.

They belong to the people. The nation's oil resources are vested in Petronas by law. It has done a great job managing our oil and gas resources as well as its huge profits, although some say it should provide more information about its accounts.

Petronas is a well-managed corpora-



Dr Mahathir: Did a great job getting Malaysia out of the financial crisis

tion with an impressive record at home and abroad. It is a great national asset.

Petronas contributes to nation building by paying royalties, taxes and dividends to the Government as well as its various activities. These come up to billions of ringgit annually.

Our oil and gas resources are finite, and Petronas must manage its reserves (oil and profits) prudently to serve the nation well into the future.

The EPF was set up as a national pension fund before Independence and is 100% funded from deductions from the salaries of employees and contributions from employers. The money belongs to EPF members. They are the ones who would suffer for any losses incurred by the EPF - and there had been some horrendous losses in the past.

The Government has always tapped EPF money to fund national development. Most EPF funds are invested in government bonds and securities, which incidentally, carry an interest rate of between 3% and 3.5% when the EPF is paying out 5% to its contributors.

Last June, the Government announced a RM2.5bil plan to build new homes and accommodation for the police. The funding would come from the EPF and the Pension Fund. These institutions will get a guaranteed return from the Government that is higher than the yield from government securities.

Therefore, leave Petronas and the EPF alone, and let the professionals do their job.

Dr Mahathir did a great job getting Malaysia out of the Asian financial crisis and nursing it back to reasonable health. Pak Lah is building upon the success of his predecessor, but faced with a new set of challenges and a vastly changed global economic landscape, he has little choice but to re-orientate the nation's economic priorities.

The 9th Malaysia Plan targets a healthy annual growth rate of 6%. There is new money for the Government to spend because of increased revenues. A sum of RM200bil is allocated for development under the Plan, a good deal more than under the 8th Plan. Malaysians must get behind Pak Lah's Government to ensure the 9th Plan is successfully implemented for the benefit of all.