

## **Of cronies, sweetheart deals, IPPs and Francis Yeoh**

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YTL group's Francis Yeoh has got himself into quite a bit of a pickle over some statement on cronyism he made at a talk on going global. He denies he is a crony and that the crony way is not how business is done in Malaysia. But is that the truth? Let Tiger dig to unearth the bare truth with his claws.

Who is a crony really? Tiger, without any reference to a dictionary, thinks its a cosy relationship with the powers that be so as to obtain an advantage over others and get what is commonly known as a sweetheart deal, that is an uncommonly good deal which no government in its right mind will give you.

And crony capitalism defines a situation where this is rampant – that is a cosy relationship between the state and businessmen for the benefit of the businessmen primarily and often the state leaders too.

Just to be sure Tiger looked it up. Merriam-Webster defined a crony as “a friend of someone powerful (such as a politician) who is unfairly given special treatment or favours.” And Investopedia (Tiger's favourite site for business terms) defined crony capitalism as a capitalist society based on the close relationships between businessmen and the state.

In Tiger's books his definition is not significantly different from the dictionary definitions – just a matter of phraseology and an emphasis here and an emphasis there – nothing anyone will tear their hair out over discussing differences

Now that we are clear on what we mean by crony and crony capitalism. Let's dig in. This is going to be a long dig so be prepared to stay with it – it will show things up quite clearly as we unearth the truth.

There are two parts to it. Is there crony capitalism in Malaysia? And the second part is this: Is Francis Yeoh a crony? If you have not already, read how he became caught up in the crony controversy here. And read herehow he got whacked by Utusan Malaysia for it.

Let's try and answer the second part first and it will be easier to answer the first part after that. And let Tiger take you back in time to the early nineties and a major blackout in Malaysia when there was power outage across the land.

We Tigers never noticed it of course because it's always dark in the jungle at night except for the moon now and then and the question of whether the jungle was close enough to be affected by haze through which starlight seldom penetrates.

Back to the story, this prompted then prime minister Dr Mahathir Mohamad to launch perhaps his most expensive (to the Malaysian that is) privatisation plan – to privatise the generation of electricity, alleging that our electricity utility Tenaga Nasional Bhd or TNB was inefficient, hence the blackout.

TNB had by then been producing electricity without problems for many decades and was able to raise funding for its power stations without government support. It was considered to be quite efficient.

There were allegations that the blackout happened because TNB was not allowed to plant up, hence reducing the reserve production margin it was supposed to maintain for eventualities.

In fact, in an interview with The Star in 2006, former TNB executive chairman Ani Arope alleged that TNB had been ready to plant up following the 1992 blackout, but that it was prevented from doing so by none other than the Economic Planning Unit (EPU) under the prime minister's department.

TNB was ordered to surrender the land it had acquired to the government, and not long after the government announced plans to privatise power plants.

Ani also alleged in the interview that it had no negotiations with the IPPs. TNB had to deal with the EPU, who gave TNB the terms and asked management to agree. Ani refused to agree.

In the interview, Ani also said that the pricing and terms of the PPAs "was all fixed up". "They said you just take it and I refused to sign the contracts. And then I was put out to pasture," he was quoted as saying.

Later, the government did put in the checks and balances to ensure that IPPs do not continue earning ludicrous profits from their PPAs, but the damage had already

been done. The IPPs created overnight billionaires and many of them continue to profit at TNB's expense even today.

Recall that among the first-generation of IPPs was YTL Power International, often said to be the richest IPP. It was a lucrative deal for YTL Power, with the pricing of power based on at least an internal rate of return (IRR – the correct way of calculating returns on investments) of a high 16% at least.

If the project is structured such that equity is 20% and the rest 80% financed by debt and if we assume an interest rate of say 7.5% (it's much lower now), then calculations show that the return on equity is at least 50%. In two years, you recover your equity investment!

And the risk is minimal – the person who supplies the power plant will guarantee the performance and TNB will guarantee take up of the power or pay a capacity charge. What a wonderful sweetheart deal and this is confirmed by no less than the TNB executive chairman at the time!

If there is still doubt, here is more evidence. The table shows YTL Power's power businesses. The TNB contract has a profit margin of 14.1% while other power businesses are less than half that at 6.2%.

Yes, Francis Yeoh now takes pride in the fact that most of YTL Power's business is overseas but it was Malaysia that provided him the base and Malaysia where his business it still most profitable.

Did Francis Yeoh know Mahathir? Yes and by most accounts very well. Then, we can assume that he was indeed a crony – certainly not the only crony, because every IPP owner subsequently was also one and many more besides but a very major one nevertheless. This bit of crony capitalism catapulted his family into billionaire status.

It was recently reported that the same YTL Power has won the Project 4A award for a new power plant as part of a consortium linked to the Sultan of Johor with Tenaga Nasional taking a 20% stake via direct negotiations. And so cronyism marches forward and onward.

The model that YTL Power pioneered with the connivance of the EPU under Mahathir was copied by those following him, the other cronies, if you will but no one else got as good a deal as he did.

Even now, the IPP project is a sure and easy path to massive riches, selectively handed out to connected businessmen who carefully cultivate the politicians who dish them out. One can safely say that anyone who gets an IPP contract is a crony – that makes for a fair number of cronies in this sector alone.

And if the entire IPP sector is owned by cronies would it not be fair to say that crony capitalism is not only alive in Malaysia but well and thriving? That answers the first the question this article was examining.

To summarise: Yes, cronyism is part of doing business in Malaysia and Francis Yeoh is a crony. But to be fair to him he is just one of many and it is not easy to do business in Malaysia unless you are a crony.

Although he denies having said that, he is right when he said that in developed countries he does not need to toady up to prime ministers and other leaders before and after he gets a project. Which implies that he has to here.

This Tiger has always maintained that IPPs are actually unnecessary and merely add another layer of costs to the ultimate consumers of electricity. The best way is for Tenaga Nasional to own and run the plants – its been doing it for many decades before privatisation.

So long as the staff of Tenaga Nasional are kept clean, honest and efficient and paid a good salary for their work, this will provide the lowest cost of electricity to consumers.

Why? Simply because you don't need to provide an IRR of 12-16% for meddling middlemen cronies who become multi-millionaires and billionaires on the back of these needless contracts.

GRRRRR!

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