

Malaysia suffers today because it didn't in 1990s – William Pesek

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AUGUST 11 – Malaysia's ongoing currency crash has many causes: a worsening global outlook, plunging commodity prices and, of course, the political scandal enveloping Prime Minister Datuk Seri Najib Razak. But the real culprit is the year 1997.

The conventional wisdom is that Malaysia's then-leader Tun Dr Mahathir Mohamad saved the country from the worst ravages of the Asian financial crisis when he imposed capital controls, pegged the ringgit and waged verbal war against speculators. It's true that Malaysia avoided much of the chaos that toppled economies in Indonesia, South Korea and Thailand. But events today show why, 18 years later, Malaysia may wind up the biggest loser in the region.

Malaysia's neighbours recovered by improving transparency, strengthening their financial systems, and limiting collusion between public and private sectors. Such urgency never swept Malaysia, where the ruling coalition has held power for almost six decades.

Improvements in Malaysian corporate governance have been slow and uneven. Hopes for an end to 46 years of affirmative action – which benefits the Malay majority while sapping productivity and repelling foreign investors – have been for naught. Efforts to weed out corruption and ween the economy off energy exports have been tepid.

Today's economic troubles are the product of that complacency. Had the Malaysian government worked harder to strengthen economic fundamentals and win the trust of global investors, Najib's scandal might not be sending the ringgit to its lowest level in 17 years. Had officials in Putrajaya, the country's administrative capital, done more to internationalise Malaysia's business culture, foreign investors wouldn't now be rushing for the door. The FTSE Bursa Malaysia KLCI Index has fallen more than 11 per cent from its April 21 peak, while official foreign-exchange reserves dropped below \$100 billion for the first time since 2010.

As has been well reported, Najib faces questions about US\$700 million (RM2.6 billion) that allegedly moved through government agencies and state-linked companies to accounts bearing his name. (Najib denies it, while Malaysia's anti-graft commission says it was a “donation.”) But foreign investors' mistrust of the Malaysian government traces back to policies pursued over the past 18 years.

Perhaps the most notorious was Dr Mahathir's September 1998 decision to sack Deputy Prime Minister and Finance Minister Datuk Seri Anwar Ibrahim. After months of sparring with Anwar over post-crisis reforms, Mahathir fired him and named himself finance minister, an awkward centralization of power that persists today and enabled Najib to create and oversee scandal-plagued state investment company 1Malaysia Development Bhd. And when Najib recently fired Deputy Prime Minister Tan Sri Muhyiddin Yassin, who was demanding answers from the prime minister, it seemed like history repeating itself. Just as in 1997 and 1998, the government is more concerned with closing ranks than retooling the economy.

Indonesia, Korea and Thailand are also having their share of troubles as China wobbles and the Federal Reserve prepares to hike interest rates. But Malaysia's accelerating capital flight is particularly worrisome.

Malaysia's central bank appears to be struggling to slow the ringgit's 18 per cent plunge over the past 12 months. The currency is now the lowest since Anwar's departure in September 1998. That makes for an inauspicious economic bookend: Dr Mahathir is now among those suggesting Malaysia peg the ringgit anew.

There's certainly less stigma attached to such policies than there once was. In 1998, the International Monetary Fund called Malaysia's peg a "retrograde step." By December 2002, the IMF was terming it a "stability anchor." And the IMF notably didn't slap Greece for imposing capital controls, the way it did Mahathir in the late 1990s.

But the mere mention of another peg suggests Malaysia's political establishment is still more concerned with the symptoms of the country's problems than the underlying causes. The ringgit isn't sliding because speculators like George Soros (who Mahathir blamed in 1997) are attacking it. Malaysian assets are suffering because the government failed to do basic economic maintenance — in part because it avoided the worst of 1997 and 1998, in ways Bangkok, Jakarta and Seoul couldn't.

As that dawns on investors, the pressure to sell will intensify. Overseas ownership of Malaysian government and corporate debt fell 2.4 per cent in July as a sense of crisis began to permeate the air.

Malaysia isn't about to collapse. With its moderate growth and the highly-respected Tan Sri Zeti Akhtar Aziz helming the central bank, meltdown risks are limited. But Malaysian officials are wrong to argue that the ringgit's slide doesn't reflect underlying fundamentals. It does indeed, and that's the real problem — one that can be traced back to 1997.

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