

Scandal-hit Malaysia risks lost decade

Malaysian Insider

Oct 16, 2015

Meet Malaysia, the new Brazil.

Nearly felled by the Asian financial crisis in the late 1990s, the Southeast Asian nation recovered to become a global commodities juggernaut, known for its stable government and investor-friendly policies.

Now, with its prime minister enveloped by a multi-million dollar funding scandal, Malaysia risks being infected with the kind of economic malaise that has struck its emerging market counterpart in South America.

Prime Minister Datuk Seri Najib Razak, 62, has denied any wrongdoing. But as investigations continue and opponents like previous prime minister Tun Dr Mahathir Mohamad call for his resignation, the danger is the leadership stays in fire-fighting mode.

The economy is already hit by a slowdown in prices for oil and natural gas, and Najib is expected to make bigger handouts to the poor in the 2016 Budget to be announced on October 23. Could Malaysia slide into a "lost decade"?

"Malaysia risks not just being left behind, but falling off the radar all together, especially with foreign investors," said Jim Walker, managing director at Hong Kong-based Asianomics and former chief economist at CLSA Asia-Pacific Markets.

People are definitely shying away from Malaysia," he said, and the politics of Malaysia is "by far the biggest threat".

Foreign investors are noticing. They pulled US\$4.6 billion from stocks and bonds last quarter and sent the currency to a 17-year low.

While the ringgit has since recovered alongside emerging market currencies it's still down about 15% this year, the worst performer in the Asia Pacific region. Approved foreign direct investment fell about 42% in the first half of 2015 to RM21.3 billion.

"The reforms are not taking place because Najib is preoccupied," said Datuk Saifuddin Abdullah (pic, below), a former deputy minister in Najib's government and ex-member of his Umno supreme council, who has now joined an opposition party.

"It's maintenance mode" for companies as they wait for an end to political uncertainty, he said.

A decade-long commodities boom improved the budget position and the lives of many Malaysians, with per capita gross domestic product more than doubling and the poverty rate falling to 1%. But as that benefit wanes – growth has slowed from a peak of 7.4% in 2010 to about 5% now – the government is falling back on strategies like

state-led spending as foreign companies hold back on new investments.

Half a world away, Brazil is an example of how that doesn't always work. President Dilma Rousseff increased spending at the end of her first term as growth began to slow, a move that helped fuel inflation and contributed to swelling debt.

The emerging market that was the darling of international investors is now seeing its leader fight for her political survival amid a graft scandal engulfing state-run oil giant Petroleo Brasileiro SA (Petrobras). As a result, Latin America's biggest economy is heading for its deepest recession in at least a quarter century.

For Najib, shoring up the economy and confidence is key as he also fends off criticism of his leadership amid a scandal over nearly US\$700 million that appeared in his bank accounts before the general election in 2013, a ballot where his coalition lost the popular vote for the first time while keeping power.

Najib acknowledged the money reached his accounts but said it was political donations from the Middle East rather than public funds, an initial conclusion that was announced by the Malaysian Anti-Corruption Commission too.

The government is also embroiled in claims of financial irregularities at state investment company 1Malaysia Development Bhd (1MDB), whose advisory board is chaired by Najib and which nearly defaulted this year after amassing RM42 billion of debt.

1MDB didn't respond to an e-mail and calls seeking comment. It said this month the attorney-general had not found evidence of wrongdoing.

Parliament resumes

Political pressure on Najib may increase as Parliament resumes Monday, with results of more 1MDB probes expected in the next three months.

Dr Mahathir has led calls for a parliamentary vote of no confidence in Najib, though the prime minister has the support of many of the ruling party's divisional chiefs and the opposition remains fragmented after the Pakatan Rakyat split this year.

"It's the uncertainty with the investigation analogous to what we see in Brazil which adds to volatility," said Edwin Gutierrez, who helps oversee US\$13 billion as the head of emerging-market sovereign debt at Aberdeen Asset Management Plc in London, comparing 1MDB to the probe at Petrobras.

Perched on the lower end of peninsular Southeast Asia, Malaysia straddles some of the world's busiest waterways and is a conduit for trade between Europe and Asian economic powers like Japan and China.

Bigger in area than all but four US states, Malaysia is a net oil and gas exporter and the world's second-largest producer of palm oil.

Ringgit peg

The Malay-dominated party now headed by Najib has been in power since independence in 1957, the main actor in one of the longest-ruling coalitions in the world. Past prime ministers have steered it through a series of crises, including the pegging of the ringgit during the Mahathir era.

There are differences with Brazil: Malaysia's estimated budget deficit is a third of Brazil's as a percentage of GDP, while inflation is forecast at 2% to 3% this year compared with the Latin American nation's 9.5%.

Still, both leaders have become entangled in state companies. Rousseff chaired Petrobras's board from 2003 to 2010 and has said she was unaware of corruption while at the company, while Najib chairs the advisory board at 1MDB, but has said he wouldn't tolerate the misuse of 1MDB funds.

Political distraction

Bank Negara Malaysia governor Tan Sri Zeti Akhtar Aziz has acknowledged the impact of the scandals.

"People are distracted now because our country rarely has political developments of this nature," she said in an interview.

Najib's office didn't respond to an e-mail and calls seeking comment.

Since 2013, when ethnic Chinese voters deserted his coalition, Najib has moved to shore up his Malay base via the retention of socio-economic privileges for the majority group.

Such policies have led to concerns about the potential for racial tensions in the moderate Islamic state. He's also ordered state investment funds to give stocks a RM20 billion boost, and get government-linked companies to build more hospitals.

"Malaysia has run out of ideas," said William Case, who teaches international political economy at City University of Hong Kong.

"There are state interventions when they should be freeing up markets and embracing more openness and transparency. I don't see any obvious drivers at this stage to lift it to the next stage of development."

Sales tax

The scandal has overshadowed Najib's achievements. He fended off opposition to introduce an unpopular goods and services tax (GST) in April in an effort to widen the tax base and limit a reliance on oil revenue.

In 2010, he unveiled an economic transformation plan, and announced key areas he would focus on to help make Malaysia a high-income nation.

"Early in his tenure, I had great hopes with all the reforms that looked quite promising," Case said. "But all of that has fallen by the way in the socio-political pressures."

The government isn't addressing longstanding concerns, according to the Federation of Malaysian Manufacturers.

Also, the Malaysian International Chamber of Commerce & Industry said some recommendations it tabled as part of a five-year government strategy known as the 11th Malaysia Plan were similar to what it submitted in 2000.

'Same old'

"Same-old same-old worked when you have high commodity prices, if there are no overwhelming financial or political scandals waiting to bury you in a huge tsunami," Penang chief minister Lim Guan Eng said.

Addressing investors last month in New York, Najib said Malaysia remains a good place to do business.

Not everyone is convinced. The economy is "holed below the waterline," said Andrew Harding, a law professor at the National University of Singapore.

"The country needs deep-rooted reform," he said. "We might be at the beginning of a lost decade." – Bloomberg, October 14, 2015.

Copyright © 2015 Edge Insider Sdn Bhd

Source:

<http://www.themalaysianinsider.com/malaysia/article/scandal-hit-malaysia-risks-lost-decade>