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Putting the 12th Malaysia Plan under microscope

THE 12th Malaysia Five Year Plan tabled in the Dewan Rakyat by the Prime Minister is replete with claims of its policies and programs being “game changers”, “catalysts for....”, “enablers” ,etc However, our scrutiny of the document together with the speech by Datuk Seri Ismail Sabri, leaves us deeply disappointed as we fail to discern specific policies that qualify that description.

We call the attention of the government, policy makers and other stake players and holders to the following three key longstanding stalled issues that necessitate rethinking and an entirely different set of policy initiatives if the Plan is to meet its goals of a high-income country with inclusive and sustainable growth. Our concerns are echoed in part by the Leader of the Opposition, Datuk Seri Anwar Ibrahim, and a host of other respected commentators.

To compound matters, the disclosure by the Federation of Freight Forwarders (FMFF) of the government’s attempt to enforce a drastic restructuring of the freight forwarding industry has been a distraction that has met strong opposition. The proposal to require existing non-Bumiputera firms in the industry to divest 51 percent of equity has been described as tantamount to a robbery and classic “Umno-ism”. Yet other observers have pointed out the negative vibes this announcement sends to firms in other sectors. If implemented, most if not all independent and credible quarters agree that this will be a contributing factor to further damage the investment climate as well as disrupt the supply chain’s efficiency and productivity which the economy can ill afford.

In our judgement, the government proposal overturns the solemn undertaking given by Tun Razak that the 30 percent target would not entail takeover of existing assets but would be achieved via growth when he presented the New Economy Policy (NEP) in Parliament. It must also be recalled that the BN Cabinet rejected the initial version of the Industrial Coordination Act which attempted to put in place a regime in which 30 percent of equity in each limited company be made available to Bumiputera investors. We believe the MOF proposal is not only a regressive policy change but also that it is contrary to Article 153 of the Federal Constitution and is likely to be litigated.

We next take up the contentious issue of how the 30 percent equity ownership target is measured. We do so in order to highlight how deeply flawed numbers have come to determine policies that are not in the best interests of the nation. The resulting policy distortions have created a number of negative outcomes that include rent seeking, crony capitalism, widening income disparities in the Bumiputera community and ethnic tensions.

Corporate equity

The 12th Plan errs by suggesting that the 30% target has yet to be attained. This is a debatable contention as the Plan fails to elaborate on how the calculations were done. No reference has been made to research studies that report findings that contradict the official estimates; no credible statistics provided.

It is appropriate to begin with a focus on the nature of this target and the manner in which it is calculated. To set the record straight and once and for all, it is important that we go back to the origins of this target and the manner in which the baseline estimates were calculated.

The baseline numbers of corporate equity used in the formulation of the NEP were calculated by classifying share ownership in both publicly listed and privately owned limited companies. Ethnicity was used as a determining factor; no entities were excluded.

The use of the totality of corporations was in line with the recommended approach advocated in the United Nations " System of National Accounts" (SNA). The ownership structure of each corporate entity was compiled by taking account of the ethnicity of shareholders. This identification was determined by using the name of each shareholder to assign ethnicity. In brief, the resulting count was that of the number of shares as no ringgit share values were determined.

One reason for this was the non-standard nature of the accounting returns that had been filed by the registered corporations. This was the best that could be done given the nature of the available data and the time constraints under which the Department of Statistics was then operating.

It was further understood that the baseline numbers would be further refined at a later date via a primary collection of data. Indeed, the Department of Statistics did launch the Ownership Survey of Companies with that objective in mind; the survey incorporated a section containing a standardized balance sheet.

The comprehensive data collected provided a basis for using balance sheet values to determine equity, which in turn could be subdivided by ethnicity. The tragedy was that the Economic Planning Unit chose not to tread that path and stuck to the older base numbers. The data from the Ownership Survey of Companies was classified as "sensitive" and not released. This is an omission that can be easily rectified to provide a truer, less politically exploited, picture and understanding of company ownership in Malaysia

The current methodology employed by the government produces a result indicating a shortfall in what has been achieved. The absence of actions to correct the basis for calculating the value of equity holdings has reduced the credibility of the statistics released. These deeply flawed numbers should not under any circumstances underpin important policy making.

Professionally researched empirical studies yield an outcome showing that Bumiputera holdings of corporate equity appropriately valued exceed 30%. This previously was confirmed by an analysis of traded shares in the stock exchange.

It is this aspect of the NEP that needs correction via an adoption of valuations based on a more defensible set of principles. Asset values need to be calculated based on concepts that take account of commercial accounting concepts that happen to be aligned to the SNA.

The re-evaluation can be easily accomplished at a minimum cost as the needed data exists in the files of the Companies Commission of Malaysia. Furthermore, the data is available on an annual basis and can thus be used to track progress or lack thereof at regular intervals. A transparent and timely availability of ownership data would remove a key contributor to policy manipulation and ethnic tensions.

Credible data is a fundamental requirement to support evidence-based policies. Greater transparency in the collection and dissemination of data on equity holdings will contribute to an improved investment climate vitally needed in the aftermath of the Covid-19 pandemic.

Failure to introduce the reforms listed above will continue to impact on race relations and policy distortions. These distortions are likely to potentially lower growth and would run counter to the twin goals of achieving a restructuring of the economy and promoting sustainable growth.

Finally, and perhaps most importantly, there is one reality for any economy that our policy makers and legislators must not forget. The Plan speaks of a decline in the equity held by Bumiputeras resulting from a disposal of shares allocated to them. No account however is taken of the fact that trading of shares is a normal activity. Proceeds from such sales are often invested in other assets e.g. real estate, financial instruments etc. Additionally, many of the elite appear to have transferred their new found wealth off-shore. This is confirmed by the large outward flows recorded in the Balance of Payments together with the consistently large errors and omissions item. If further affirmation is needed, one has only to look at the estimates of capital flight which places Malaysia as the second largest source of capital flowing out of an economy. The time has come to measure wealth in its totality rather than place a component represented by equity capital on a pedestal.

GLCs and Re-energizing the Private Sector

Our initial draft had identified GLCs as a key sector to reform. Not only is the role that government linked companies (GLCs) play in the Malaysian economy widespread and pervasive but among countries in the world, we rank with the highest in terms of SOE presence among largest firms. The negative economic impacts of such a dominant and dominating presence of GLC in the Malaysian economy are well known and need little elaboration.

Since then, we are encouraged that former PM Tan Sri Muhyiddin in his recent address to Parliament has called for a review of GLCs (and GLICs) and voiced the view that they should not be competing with the private sector.

However this opinion is nothing new. In fact it is too little too late. Initially established to facilitate Bumiputera participation in the modern economy, GLCs have over the past 30 years proliferated to take over and control not only the commanding heights of the economy but also to encroach into the mid and lower tiers. GLCs today constitute over 40% of the share market capitalization of all publicly listed companies and can be considered to be the elephant in the room that has stifled growth, crowded out private enterprise including Bumiputras, and contributed to poor governance practices. Moreover, there is every indication that they are among the main sources, if not the main source, responsible for the growing income disparity in the country, in particular that pertaining to the Bumiputera community.

With its influence over, and links to, the national and state bureaucracy, quite apart from its role in facilitating clientelism, collusion and nepotism of the political elite, GLCs have introduced severe distortions to the market in the products and services provided and have generally raised the costs of doing business whilst not improving economic efficiency at national, state and even local levels.

Earlier Plans had failed to address the out-of-control proliferation of GLCs as well as its other pernicious economic and governance impacts. The most recent round of political appointees to GLC high positions, despite public dismay and widespread condemnation of the practice, gives little confidence that any review will be taken seriously or will result in any reforms.

Hence it is crucial for Parliament in its deliberations on the 12 Plan to not delay any further with implementing policy reform proposals, in particular, the dismantling of rent-seeking and patronage components, that can restore GLCs to an appropriate position and place in the economy as commercial and competitive entities shorn of unnecessary and inflated government privilege or other functions that provide openings for politically driven patronage and misuse of public funds. Such a reform agenda contained in the 12 Plan should include an appropriate divestment programme of the numerous GLCs that have little or no justification for their existence and stand in the way of the private sector's development.

Revitalizing our Private Sector and SMEs

In tandem with a GLC reform programme, there needs to be put in place a revitalization programme for the private sector, especially directed at small and medium sized enterprises.

It is clear now that Malaysia has lost its competitive edge in attracting multinational corporations. The exodus of many established corporations to Bangladesh, Indonesia, Vietnam, the Philippines and other countries is indicative of this trend. New FDI flows into the country have slowed even in terms of feel good dubious figures touted by MITI. According to the latest data, foreign direct investment (FDI) in Malaysia registered a net inflow of RM14. 6 billion in 2020 as compared to RM32. 4 billion in the previous year. This contraction by 54.8 percent is only partly a result of global economic uncertainties due to the pandemic situation. These corporations as well as the local businesses have also found the price of doing business rising given the negative impact of the regulatory environment. The regulatory regime in place has grown, is stifling and is at the same time subject to uncertainties generated by frequent policy changes as has happened, for example, with the MM2H program for foreigners.

Meanwhile there is every likelihood that a significant proportion of the present number of 900,000 SMEs - if stronger corrective measures are not taken by the Government - will close shop or cut back on operations as a result of the ongoing pandemic crisis which the Plan has failed to adequately address. That this prospect will considerably worsen the poverty and unemployment problems for the country is clear from this profile data

SMEs

● make up one million or 98.5% of all business establishments

●provide two-thirds of all employment

●contribute 40% to the national GDP, and

●are located in all states, all sectors and range in size from micro-enterprises to small and medium.

SMEs are not just a pillar of the economy. They also play a key role in social stability and social cohesion. This vital contribution of SMEs to national unity and harmony has either been ignored or has not been properly acknowledged in Plan documents.

Here it is necessary to remind policy makers and legislators that SMEs are the main source of multiracial partnerships and inter-ethnic linkages, relationships and interaction at many levels, including ownership, labour force and in other spheres. Also not generally known is that 20% of SMEs are owned by women thus contributing to gender equality.

Reviving the SME segment of the economy in the short and medium-term future should be amongst the highest policy priorities of the government in the 12th Plan.

The above difficulties facing the private sector, together with the monopolistic policies favoring the GLCs and the GLICs, and the resultant rising price of doing business needs to be addressed in any clear-sighted and pragmatic plan. Unfortunately despite these stark past and new policy failures, the Plan document is largely silent or evasive. Should the Government fail to take corrective measures in the new Plan we fear that this heavy baggage will be carried forward.

Urgent game changer reforms

The third backward step we have discerned applies not just to a single sector. It relates to a wide range of sectors in which earlier policy reform measures were clearly identified and agreed to by a previous government and where these reform measures have either been ignored, stalled or discontinued.

To recall, thirty years ago at the National Economic Consultative Council (NECC) deliberations to propose the successor to the NEP, no quantitative targets were set in the final report as it was the consensus of the 150 members drawn from political, economic and social sectors and all communities that what was important was not the contentious numerical targets but the necessary capacity building to build and sustain businesses. The 9th Malaysia Plan 1991 to 1995 in fact did not specify such ownership targets.

Likewise ten years ago in 2010 the New Economic Model drawn up for the 10th Plan by one of the most credible and qualified economic teams recruited to chart the country's socio-economic future eschewed the continuation of a regressive NEP policy which was originally intended to be discontinued after 1990.

Further it identified the following urgent policy imperatives to ensure the nation's ability to meet the multiple challenges from internal and external factors. These included

●Refocusing from quantity to quality-driven growth. Mere accumulation of capital and labor quantities in the past has been insufficient for sustained long-term growth. To boost productivity, Malaysia needed to refocus on quality investment in physical and human capital.

●Relying more on private sector initiative as the primary engine of growth. This involves rolling back the government's role in some areas, promoting competition and exposing all commercial entities and activities (including GLCs) without exception to the same rules of the game.

●Making decisions bottom-up rather than top-down. Bottom-up approaches involving decentralized and participative processes that rest on local autonomy and accountability would lead to more accountable and less rent-seeking and crony-driven outcomes

●Redressing unbalanced regional growth. Growth accelerates if economic activity is geographically concentrated rather than spread out. Ripple effects would also come from more effective poverty alleviation and equitable income distribution outcomes and more inclusive and sustainable growth.

●Welcoming foreign talent including from the Malaysian diaspora whilst retaining local talent. As Malaysia improves the pool of talent domestically, foreign skilled labor can fill the gap in the meantime and can generate positive spill-over effects

●Prioritizing the education sector which is a key laggard in the economic transformation of the country. In particular the public higher education sector has not been able to produce the skilled human capital despite being provided with consistently large budget allocations during the past 20 years

●Rightsizing the bloated public sector and rectifying its siloed and ineffective sectors that have impeded investment and productivity

What was unprecedented about the NEM is not only its acknowledgement that falling FDIs and competitiveness, compounded by the brain drain and decline in standards of governance as evidenced by pervasive corruption, rent-seeking and patronage, have put Malaysia behind many of our neighbours in the region. It was also the recognition that the NEP had become a time warp and millstone holding back the development of the country. Hence the need to not simply shift to a higher skilled, more competitive and private sector driven economic ideology but also of the necessity and urgency of deep structural reforms for the country to move out of the middle income trap and reach its true potential.

When drawn up and approved by the Government of Prime Minister Najib Razak, the NEM with its paradigm changing principles and change strategies had the strong support of not only business and professional elites and the country's movers and shakers but also legislators in Parliament. However it needed to be accompanied by actionable policies and a multi-year commitment to implement them. This has not happened.

Today as the current Parliament sits to deliberate and finetune the 12th Plan package presented, we urge legislators from both sides of the policy divide - and this includes legislators from the period of the adoption of the NEM - not to return to a NEP clone mindset but to use the NEM instead as a reference text to select, support and not marginalize the real game changers that the nation needs or we will risk a further falling back in our economic prosperity and standing among nations.

Conclusion

We believe that the Plan, if implemented as currently presented, is likely to act as a self-inflicted wound that will adversely alter the trajectory for Malaysia's socio- economic growth and heighten the likelihood of our country becoming further entrapped as a middle-income economy, with a clear risk of going backward in our development and prosperity.

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