Mahathir sets new course for Malaysia in first 100 days

Prepared by Asia House Research and Advisory practice

The defeat of incumbent Malaysian Prime Minister Najib Razak in the Malaysian general election on May 9 by Mahathir Bin Mohamad was unexpected and unprecedented in Malaysian history. Najib's United Malay National Organisation (UMNO) party and its Barisan Nasional Alliance has dominated Malaysian politics since independence in 1957. Mahathir's Pakatan Harapan (PH) alliance won 135 seats of 222 in the parliament.

An opposition win seemed unlikely for several reasons – an unfavourable electoral system, a hostile campaigning environment, fragmentation of the PH alliance, and an apparent lack of a mass movement for change. However, the PH alliance prevailed under the leadership of the 93-year-old Mahathir, a UMNO Prime Minister from 1981-2003, who came out of retirement for the election. The other prominent figure in the PH alliance is Anwar Ibrahim, Mahathir's former Deputy Prime Minister (1993-1998) until he was removed from his post and jailed by Mahathir on what he claims were politically-motivated charges. After a twenty-year rivalry the two figures buried the hatchet to oust Najib from power.

The new government is widely seen both domestically and internationally as a welcome change after years of dissatisfaction in Malaysian politics, and a government mired in corruption and debt.

On Tuesday, 21 August, Mahathir returned from meetings with President Xi Jinping and other key figures in China, the main purpose of which was to renegotiate the terms of at least US$23 billion of Chinese-financed infrastructure projects settled under the previous government. Speaking at a joint press conference with Premier Li, Mahathir maintained a strong political line saying that "free trade should also be fair trade" and defending "poor countries… unable to compete with rich countries" against a "new version of colonialism". However, the outcome of the visit suggests friendly relations will continue with two-way increases in trade and investment promised.

Mahathir's return from his China visit with a strengthened relationship with China and a set of trade deals under his belt is a solid win to wrap up his first 100 days. Progress has also been made in other areas, and although the new government has both immediate and long-term challenges, the outlook for Malaysia is the brightest it has been for several years.

Policy promises and the 100 days plan

Mahathir made several major policy promises during the campaign, which the PH alliance promoted as "10 promises in 100 days". Mahathir recently admitted that they may have overpromised during the campaign on the assumption that they would not gain power.

However, the new administration has made progress on several fronts and recent polls reported a 71 percent approval rating. It remains to be seen how long this elation lasts; the swell of popular support that resulted in the alliance's victory may also be a public awakening from disillusionment and the beginning of a new environment of public scrutiny.

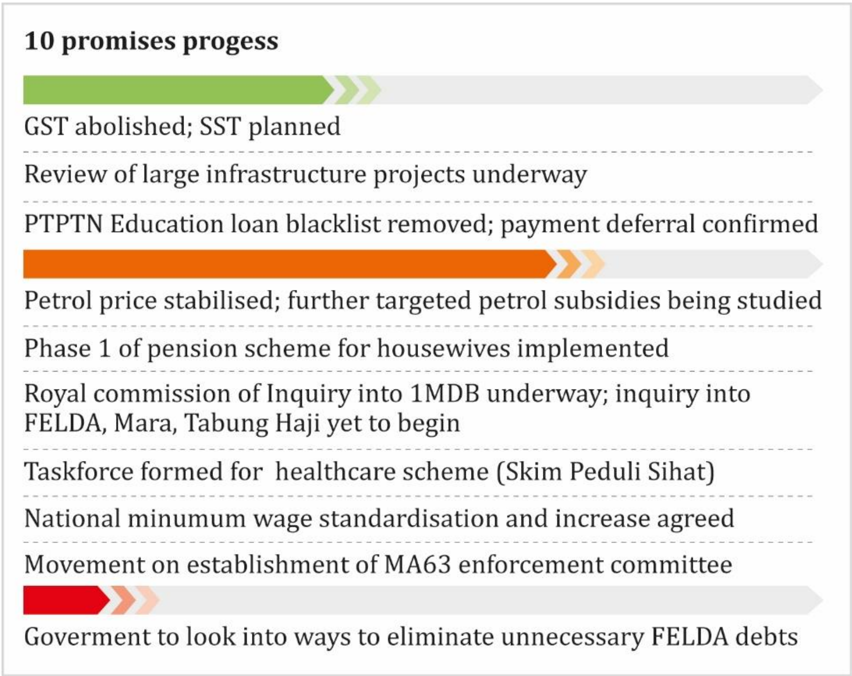
There are several immediate obstacles that stand in the way of the government's plans. Proposed corruption investigations rely on the investigative capacity and cooperation of foreign jurisdictions and the review of infrastructure projects relies on the continued tolerance of China.

Of greater concern, the true state of the nation's finances – debt in excess of RM1 trillion (80.3 percent of GDP) – was not realised until the new government took power. Furthermore, while Mahathir and Anwar are old political hands, much of the cabinet is made up of less experienced new ministers, who will rely on their teams, some of whom may still be attached to the former government.

A hole in the budget?

Seven of the PH alliance's targeted policies were aimed at reducing the cost of living for lower income groups. They may also have a general positive impact on the domestic economy, putting money in the hands of workers, housewives and small businesses. For now, consumer confidence is positive, and there has been a spike in the purchase of homes and locally made cars.

While certainly a noble aim, the newly realised scale of the debt burden, as well as the complexity of many of the issues has caused a rethink of some of the measures and their timelines.



Green = underway, amber = some progress, red = no progress so far

Some targeted fuel subsidies have been implemented, and a more detailed subsidy system is being studied. The government is also looking into the best ways to eliminate the debt burden for land settlers under the government's FELDA scheme.

The implementation of an increased and standardised minimum wage will be introduced gradually in order to retain competitiveness. Meanwhile, a taskforce has been established to lay the groundwork for a national healthcare scheme (Skim Peduli Sihat). A clearer picture on these policies will come to light in the November budget for 2019.

Mahathir has been a long-term opponent of the goods and services tax (GST) for its impact on living costs. The move to eliminate GST may exacerbate the debt burden, and so far, the trickle-down benefit for consumers has been patchy. Furthermore, GST forced many businesses to legally register their income; an element of transparency that may be lost as firms sink back into opacity.

To fill the revenue gap, a sales and services tax (SST) will be re-implemented – at 10 percent for sales and six percent for services. Finance minister Lim Guan Eng expects the SST to generate RM4 billion. The impact on consumers is unclear as the tax is implemented at the point of sale from the manufacturer, so prices will rely on retailers' calculations. Some analysts have noted than in hindsight, a more pragmatic approach may have been to reduce GST from six percent to two or three percent.

Of greater impact is Mahathir's plan to restructure the country's debt. Much of Malaysia's debt is expensive to service, and conversations with Japan and China will be important. Japan is already considering a credit request, and discussions with China are underway.

The government says that there will be enough money. Given the focus on lower-income groups, if the money is not forthcoming it seems unlikely that Mahathir will turn to the general public, potentially leaving the private sector to pick up the bill.

Addressing corruption – a long time coming, a long road ahead

Mahathir's victory represents a welcome change from what seemed to be a polity veering towards kleptocracy. The 1MDB scandal has dominated the global view of Malaysia for the past few years, keeping the electorate frustrated and investors cautious.

In his first 100 days, Mahathir has come good on his promise to clean up public life by overseeing a proactive investigation. Scalps have already been taken including the high-profile arrest of Najib and several other 1MDB officials; over 400 bank accounts have also been frozen.

The government is also keen to plug the hole in the nation's finances by clawing back public funds that went missing. However, it will be a long road ahead, investigating a complex web of transactions and relying on the interest and cooperation of foreign jurisdictions.

The United States' SEC may already be primed for involvement. The SEC settled a lawsuit in March for US$60 million with a movie production company linked to 1MDB that – somewhat ironically – produced "Wolf of Wall Street". Singapore and Indonesia are also cooperating.

In addition to the 1MDB scandal, there are other nodes of suspicion. Government-linked companies (GLCs) have been told that they have strayed away from their original mandate of increasing domestic involvement in the economy and have rather focused on enriching themselves. Analysts expect some divestment of successful GLCs, coupled with more government support, if less direct intervention.

It is not yet clear if the new government's commitment to tackling corruption will extend beyond the alliance's political opponents. Furthermore, institutional reform and cultural change are long-term projects. In the short-term, while the high-profile arrests will assuage the domestic audience, a tightening of government tender and procurement processes would be a positive sign to international partners and investors.

Infrastructure projects – anti-corruption or anti-China?

At the geopolitical level, much has been made of the proposed review of major infrastructure deals mired in corruption allegations and anxiety over foreign dependence. Projects worth a total of US$50 billion, mostly financed by Singaporean and Chinese money, are under review.

The RM40 billion Klang Valley mass rapid transit line 3 (MRT3) and two gas pipeline deals may be cancelled outright, the kick-off of the Kuala Lumpur to Singapore high-speed rail link has been deferred and works on the East Coast Rail Link have been suspended.

While Singapore may be more inclined to forgive and forget, given the symbiotic relationship between the neighbours, there is always a collective intake of breath when a country dares to challenge China.

In a recent interview, PH alliance leader Anwar Ibrahim maintained that both suspicions of corruption and strategic overreliance on China were driving the review. Observers have noted that several of the projects were questionable deals for Malaysia, lop-sided in favour of foreign lenders, suppliers and labour. This narrative also helps placate jitters in the investment community about further reviews.

As mentioned above, conversations between Malaysia and China over the past few days seem to have been positive. Mahathir has tried ease the concerns of Chinese businesses too. Speaking at the China Entrepreneur Club Leader Forum he said that the project suspensions are about cost, not the source of financing, laying blame on the previous government.

Mahathir's experience as an elder statesman will help in these matters. He is a familiar face in Beijing with regular visits when he was previously PM. Ultimately, both sides are looking for cordial and productive relations, especially given Malaysia's position on the geo-strategically important Straits of Malacca.

Furthermore, the review will not inevitably be the death-knell of all the projects, given the public appetite and economic need for better infrastructure. Investors expect some projects to be retendered, especially more strategic projects such as the KL-Singapore high-speed rail link.

A (more) federal Malaysia?

One promise has (perhaps) been overlooked among the more high-profile policy headlines. The government has set up a cabinet committee to properly enforce the Malaysia Agreement 1963 (MA63), as some terms of the agreement, which governs the federal structure of Malaysia, have been eroded. The pledge won the alliance votes outside peninsular Malaysia and will bolster the self-governing powers of Sarawak and Sabah including their decision-making power on investments.

This policy exists in the context of a more ethnically diverse approach by Mahathir. The new cabinet contains more ethnic Chinese and East Malaysians, including the first ethnic Chinese finance minister, Lim Guan Eng.

Malaysia outlook

The domestic policy agenda proposes a broad challenge for the new government which will test their ability to balance the books while funding welfare and the need for continued infrastructure development. The infrastructure review and the corruption investigations present opportunities to balance the books, while also repairing Malaysia's image on the world stage with investors – especially if followed by broader institutional reform.

This need for improved governance and reform has been echoed by the report of the Council of Eminent Persons, set up by Mahathir in May. At a press conference on Monday August 20, council member Daim Zainuddin said the council recommended institutional reform in several areas, including parliament, the judiciary, the concentration of executive power, legislation, and human rights.

However, the new government will also need to focus on enhancing the economy's attractiveness to FDI, on which its success is dependent. Alongside building consumer-centric industries to export to its ASEAN neighbours, areas of focus include improving processes for employing foreign labour, foreign exchange control liberalisation, and increasing the supply of the skilled and technical workforce.

Mahathir will be seeking to reposition Malaysia internationally, which may have downstream implications for ASEAN's global role. He is already carefully engaging China, and there are indications of a revival of his 'Look East' policy of the 1980s and 1990s in which Japan played a major role with investment and technology transfer. The relationship with ASEAN will also be important, though Mahathir may take a harder stance towards Singapore. He also has a reputation for being prickly with the west, but the US in particular will be important in balancing China's influence in the region, a power which has grown significantly since Mahathir was last in power.

In contrast to his first 22-year stint as PM, the Mahathir 2.0 era will likely only last a couple of years before the 93-year-old hands over to Anwar Ibrahim, currently leader of the PH alliance. But this transfer of power is on the distant horizon in comparison to what the government has on its plate now.

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