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Time for a second wave of reforms

In February, a Sarawak-based oil and gas engineering firm called Serba Dinamik Holdings Bhd had the biggest initial public offering in Malaysia in 19 months at a valuation of RM2 billion.

What may not be as widely known is that the group, whose business is mainly based overseas, began humbly as a participant in state oil company Petroliam Nasional Bhd's vendor development programme in the early 1990s.

It illustrates the nurturing role that the state can play via government-linked companies (GLCs), says political economist Prof Dr Edmund Terence Gomez.

He adds that such programmes help to bridge the gap between big businesses and the small and medium enterprises, cultivating potential champions of tomorrow.

It is a potential answer to the fundamental question of the role of government in business. The point is that the government's involvement in business is not necessarily bad per se, but how that involvement materialises is a crucial consideration.

> "There is also a need to redefine the role of GLCs in the economy." — Lee

One example Gomez highlights is the banking sector consolidation initiated by Bank Negara Malaysia in the aftermath of the Asian financial crisis in the late 1990s, which saw nearly 60 separate banks merge to form 10 anchor banks.

The forced exercise illustrated the state's power to take over private assets via public policies or dictates. Gomez believes that that, in turn, contributed to a decline in private investment after the Asian financial crisis.

"Many of the smaller banks were family-owned enterprises and they were not willing [to merge]," he recalls, adding that in the aftermath of the event, private businessmen in general "are worried about the capacity of the state to expropriate their wealth through this kind of policies".

"When you have a state that is so powerful that it can take over assets via public policies, how will investors react if they fear for their property rights? They will go abroad. They won't invest here," Gomez remarks.

Thus, it is important to draw clear lines of what business areas the government should be in and where it should not. In that vein, what is essential is to have more GLCs be managed professionally, without competing political interests getting in the way of their commercial and social mandates.

In May 2004, the government launched a 10-year initiative called the GLC Transformation Programme, which, among others, revamped sovereign wealth fund Khazanah Nasional Bhd and set higher standards for the management of GLCs.

It was a "defining moment", says Gomez. "They professionalised the GLCs and GLICs (government-linked investment companies) and they also got rid of all the politicians on most of the GLCs, and definitely most of the GLICs."

He adds that a key difference is how the GLICs and GLCs see themselves in their operations — whether they see themselves as the government's hand, which implies subservience to the government, or as a corporate enterprise pursuing their commercially driven mandates.

In a previous interview, Tan Sri Abdul Wahid Omar, group chairman of bumiputera asset manager Permodalan Nasional Bhd, gave a glimpse of such a professional mindset when asked about the crowding-out effect from the extensive GLIC participation in the economy.

"[Just to clarify], we are not the government. We are a government-sponsored fund management company and the RM266 billion [of our assets under management] is the people's money," says Abdul Wahid. "Ownership-wise, it is actually the people's."

That professional mindset, along with the political independence of GLCs, is key to preventing the mismanagement of what is essentially public resources. To be fair, most GLICs and the GLCs they control are in good shape, lending support to national economic growth and public spending.

"In our assessment of the credit implications of the current landscape, we also take into account the support to Malaysia's credit profile that GLICs bring. The GLICs provide a large pool of investable funds that help to underpin one of the region's deepest capital markets and [provide] stable funding for the government's debt," says Anushka Shah, assistant vice-president and analyst at Moody's Investors Service.

That said, a number of GLCs, particularly at the state level, still have room for improvement.

The time is right for further reforms to enhance governance standards and to put in place adequate institutional arrangements to prevent the mismanagement of public resources in GLCs, says Lee Heng Guie, executive director of the Socio-Economic Research Centre.

"The time has come for a second round of transformation, specifically aimed at improving the governance of GLCs," says Lee. "The management of public funds in carrying out nation-building objectives require greater public scrutiny.

"There is also a need to redefine the role of GLCs in the economy, with a view of ensuring that the limited public financial resources are efficiently managed and invested while not crowding out the private sector. The inefficient ones should be restructured or disposed of," he adds.