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Economic Reforms in the Aftermath of
Regime Change in Malaysia

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Economic Reforms in the Aftermath of Regime Change in Malaysia

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Abstract

The 14th General Election in May 2018 brought about an unexpected change in political rule in Malaysia for the first time since the country's independence in 1957. In its first year of rule, the new Pakatan Harapan-led government implemented several populist economic policies that were drawn from its election manifesto. While these policies may have moderated populist politics to some extent, they have also weakened the government's fiscal capacity. Ethnic fragmentation and a strengthened opposition alliance have also made it difficult for the new government to implement its ambitious institutional reform agenda. The new government needs to formulate and implement a new growth strategy that overcomes some of the existing structural weakness of the economy.

Keywords: Economic Reform, Institutional Reform, Political Economy

JEL Codes: D70, H00, P16

Economic Reforms in the Aftermath of Regime Change in Malaysia

Cassey Lee

“If we fail or if we break our promises, by all means reject us in the next general election”

Mahathir Mohamad, Buku Harapan (election manifesto), 8 March 2018

“Actually, we did not expect to win, we made a thick manifesto with all kinds of promises ... If we can't fulfil them, we will need a good reason that is acceptable to the people. Or else, if we fail to deliver on our promises, the opposition will use it against us and we may be defeated (in the next general election)”

Mahathir Mohamad, New Straits Times, 14 August 2018

1. Introduction

The 14th general election (GE14) in Malaysia was a historical event in Malaysia. The election brought an end to the political rule of Barisan Nasional (BN) which had ruled the country continuously for 62 years since the country's independence in 1957. In the election, the then opposition coalition Pakatan Harapan (PH) garnered 113 seats of the available 222 parliamentary seats. In a dismal performance, BN won only 79 seats compared to the 133 seats it won in the previous general election in 2013. Even though BN was resoundingly defeated in GE14, the change in political regime caught many by surprise including the leaders of the then opposition coalition Pakatan Harapan (PH).

Any change in political regime will always bring about economic and political reforms. Such reforms could be particularly drastic and deep if the political transition involved the demise of a dominant single party that had ruled for a long period, such as the case of Malaysia. The unexpected nature of the change in regime also has important implications for economic policy-making ex-post GE14. More specifically, electoral promises may have been made that were premised upon assumptions about expected electoral performance. Furthermore, asymmetric information about fiscal capacity may lead to difficulties in fulfilling electoral promises. These and other related issues are studied in this study.

The main goal of this study is to describe, explain, and evaluate economic reforms in Malaysia in the aftermath of GE14. The outline of this study is as follows. Section 2 will review the relevant literature with the view to frame subsequent discussions on regime change and economic reforms. This will lead to a discussion of the nature of political changes in Malaysia in Section 3. The economic reforms that are proposed and carried out by the new Pakatan

Harapan-led government are described in Section 4. Section 5 undertakes a similar analysis of the institutional reforms proposed and implemented by the new government. Section 6 provides an overall assessment of the economic and institutional reforms. Section 7 concludes.

2. Core Concepts and Literature

Economic reforms can be analyzed from three perspectives (Bénassy-Quéré et al., 2019). First, the positive economics perspective examines the effects of such reforms on the economy, e.g. economic growth, poverty eradication, and inflation. Examples include Coudouel and Paternostro (2005, 2006) which examine the distributional impact of various types of reforms. Second, the normative economics perspective seeks to identify the appropriate policy goals and the set of policies that best achieve these goals. One example of this is the growth diagnostic toolkit developed by Hausmann et al. (2008) to analyze and formulate growth strategies. Finally, the political economy perspective studies the political decision-makers' behavior as an endogenous determinant of the reform decisions. The normative (goals) aspect of reforms is indirectly discussed when the concept of reform is examined in Section 2.1 while the positive and political economy aspects are reviewed in Section 2.2. These two aspects are intertwined as the successes and failures of economic reform often depend on political factors.

2.1 The Concepts of Reforms

Reform entails changes in government policies or institutional rules that depart from the status quo and have significant and durable effects on the economy. These elements are present in the following attempts to define reforms:

“I define reform ... as a durable and significant policy change that improves aggregate socioeconomic welfare, consistent also with an objective function that recognizes distributional and environmental considerations.” (Hill, 2013, 109)

“Reform from the perspective of economics refers to changes in government policies or institutional rules because status quo policies and institutions are not working well. Further, reforms refer to alternative policies and institutions that are available that would most likely perform better than the status quo to achieve economic goals.” (Khemani, 2017, 2).

An important aspect of economic reforms is the set of policy instruments to achieve the goals of these policy reforms. Several terms have been used to classify and group some of these policies. Some of these terms overlap in terms of policies. Despite this, it is still useful to discuss these terms as a means to relate to past and existing research and policy initiatives and discussions.

Macroeconomic reform involves a significant change in the use of macroeconomic policies. These policies include fiscal (expenditure and tax), monetary and exchange rate policies. The goal of macroeconomic policies is to stabilize the economy. Policymakers do often adjust their macroeconomic policies in reaction to the business-cycles. What makes these policy changes a “reform” is when these changes represent a fundamental and significant shift in policy orientation.

Trade reform involves policies that enhance economic growth by increasing the openness of the economy. These include policies that liberalize trade and foreign investment regimes. These policies include at border policies (e.g. tariffs) and behind border policies (e.g. non-tariff measures).

Structural reform is a broad term that encompasses several areas. Aside from trade and FDI liberalization, structural reforms encompass reforms in areas such as labor markets, financial sector, product market, agriculture sector, capital account and institutions (Dabla-Norris et al., 2016). Many of these reforms have also been labeled as **microeconomic reform**. A key aspect of these reforms is the focus on micro-level impact on firms through the stimulation of firms to achieve productivity improvements (PC & ANU, 1998). For some, this has been enabled by increasing the role of markets in the economy through market liberalization, deregulation, and privatization (HM Treasury, 2004; Borland, 2014).

Another prominent type of reform is **institutional reform**. Institutions can be broadly defined as “the rules of the game in a society,” or more formally, “humanly devised constraints that shape human interaction” (North, 1990, p.3). Institutional reforms can be thus be described as attempts to change the rules affecting human interactions. Institutional reforms can cover changes in economic institutions (property rights, tax), legal and related enforcement institutions (courts, judiciary, anti-corruption, police) or political institutions (electoral system,

legislature).¹ Both economic and legal reforms are often featured in both structural and microeconomic reforms (Dabla-Norris et al., 2016).

Finally, **public sector reform** is another important type of reform. Such reform is aimed at enhancing the public sector's effectiveness and efficiency. This is achieved by increasing devolution and decentralization, strengthening competitive pressures, transforming workforce structure and size, HRM arrangements, changing budget practices and procedures and introducing results-oriented approaches to budgeting and management (Curristine et al., 2007).

2.2 Political Economy of Reforms

The research literature on the political economy of reforms seeks to examine how political factors shape and determine the outcomes of reforms. Research in this area flourished in the 1990s due to both democratization and the transformation from socialist central planning to market economies amongst Central European countries during this period.

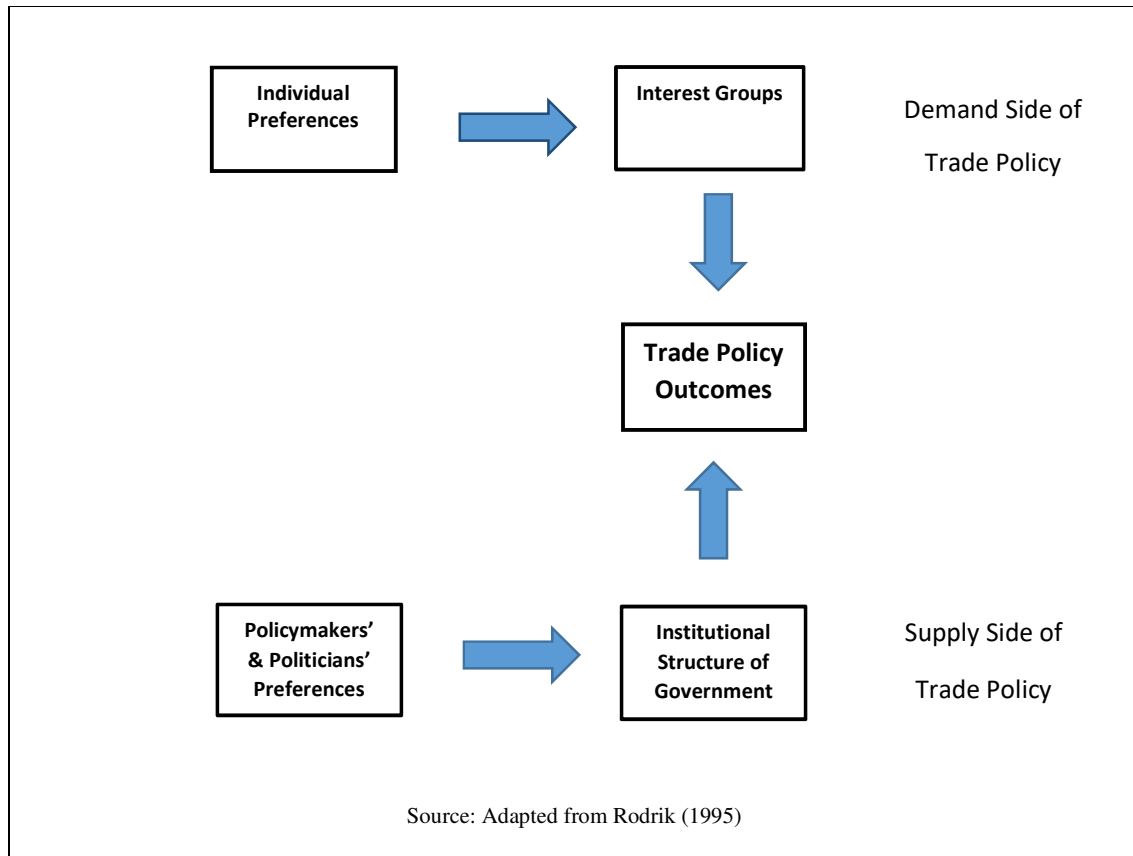
Economic reform is about changing the status quo. Reforms have distributive impacts - there are winners and losers. From a political economy perspective, reforms are driven by interactions between various stakeholders in the economy such as voters (consumers, workers, employees), interest groups (industry lobbies, consumer associations, etc.), policymakers, and politicians. The role that stakeholders play and their influence in the reform process is conditioned by the institutional structure (e.g. democratic vs socialist country, parliamentary vs. presidential system, separation of powers, bureaucratic machinery, etc.).

A simplified framework incorporating these interactions for the case of trade policy reforms is depicted in **Figure 1** (adapted from Rodrik, 1995). In this framework, on the demand-side, "individual preferences are aggregated and channeled, through pressure groups, political parties, or grass-roots movements, into political demands for a particular policy or another" (Rodrik, 1995, p.1459). On the supply-side, the preferences of policymakers and political leaders determine what policies to adopt. These preferences can be shaped by various factors such as political survival, group favoritism, and social welfare maximization. The interactions between the demand side and supply side of policy reforms are shaped by the institutional

¹ Institutions affecting press freedom is another area that is important in democratic societies. This could be subsumed under institutions for governance.

structure of the government. Institutions can be informal such as norms of cooperation (Khemani, 2017).

Figure 1: Political Economy of Trade Policy



The literature on the drivers of reforms can be unpacked by using the above framework. Hill (2013, p.110) listed these drivers as “necessity” (e.g., financial crisis, hyperinflation, political crisis), “triumph of ideas” (e.g. Reaganomics, Washington Consensus), “conjunction of reform-oriented political leadership aided by technocratic advisers”. Economic crisis – whether driven by external and/or internal factors - affects individuals’ (voters’) demand for macroeconomic stabilization. A political crisis can also drive reforms. Much of the literature on economic reforms is based on democratization and its impact on economic reforms (Bunce, 2001; Haggard & Webb, 2004; Rodrik & Wacziarg, 2005). This entails political regime change from authoritarian to democratic rule. The triumph of ideas can inspire and shape visions of

policymakers and politicians. The structure of the electoral system and the relationship between politicians and technocrats is shaped by internal structure of the executive body of the government as well as the relative power of the executive, legislature, bureaucracy (Hill, 2013, p.113).

The drivers of reforms and the perceived distributive effects also affect the implementation of reforms per se as well as the dynamics of reforms in terms of: (i) timing of reforms, (ii) speed of reforms (big bang vs. gradualist), (iii) sustainability of reforms, and (iv) sequencing of reforms.

At the demand side, societies with a lower degree of social cohesion can delay the implementation of policy reforms as the burden of such policy reforms are perceived to be unevenly distributed (Alesina & Drazen, 1991). Divisions within societies can be along the lines of social class (poor, middle class, and rich) or/and ethnicity. Ethnic fragmentation, especially when it interacts with economic inequality, can lead to redistributive conflicts (Khemani, 2017).

In terms of the speed of reforms, Sachs (1994) have argued in favor of the “big-bang” approach as it is futile to seek a social consensus when the public have limited understanding of reforms. Furthermore, on the supply-side, this favors a more autocratic approach to policy reforms. However, such autocratic approaches are seen by some as against democratic values (Przeworski, 1993). Others such as Dewatripont and Roland (1992) have argued that gradualism can be an optimal reform strategy as it allows workers with different abilities to gradually exit at different times and with different levels of compensations thus minimizing the adjustment costs. Comparing both approaches, Wei (1992) noted the big-bang approach could deliver benefits quickly when there is strong public support. However, when there is uncertainty about the losers and gainers from reforms, the gradualist approach may be more politically sustainable because such an approach would reduce resistance to the reforms and build uninterrupted support for them.

The issues of sequencing and speed of reforms are intertwined. The big-bang approach seeks to implement a set of reforms simultaneously while reforms are sequenced in the gradualist approach. The sequencing will depend on the state of the economy. Macroeconomic stabilization via macroeconomic policy reforms is a key priority during an economic crisis. Macroeconomic stability is a necessary condition for reforms in other areas. For these other areas of reforms, the optimal sequence depends on the micro-dynamics of adjustments. For

example, using a two-country general equilibrium model, Asturias et al. (2016) showed that the optimal sequence of reforms requires reforming trade barriers before entry costs and contract enforcement. This is because the transformation of non-exporters into exporters takes time.

Finally, many scholars have pointed out that it is often easier to start reforms than to sustain them. The sustainability of reforms depends on the length of the “honeymoon period” which is positively related to the severity of the economic crisis that triggered the reforms (Williamson, 1994). However, Haggard and Webb (1994) have argued that a severe crisis requires quick responses to prevent rapid economic deterioration. The length of the honeymoon period will also depend on the lag between the initial reforms and the subsequent timing of the flows of benefits. Others have highlighted that weak political opposition would also make it easier for reforms to be implemented and sustained (Joan, 1990). Finally, the sustainability of reforms also depends on the fragmentation of party systems – wide ideological differences may lead to coalition rule with difficulties in finding compromises which can destabilize reform efforts (Haggard and Webb, 1994).

3. Regime Change and Economic Conditions in Malaysia

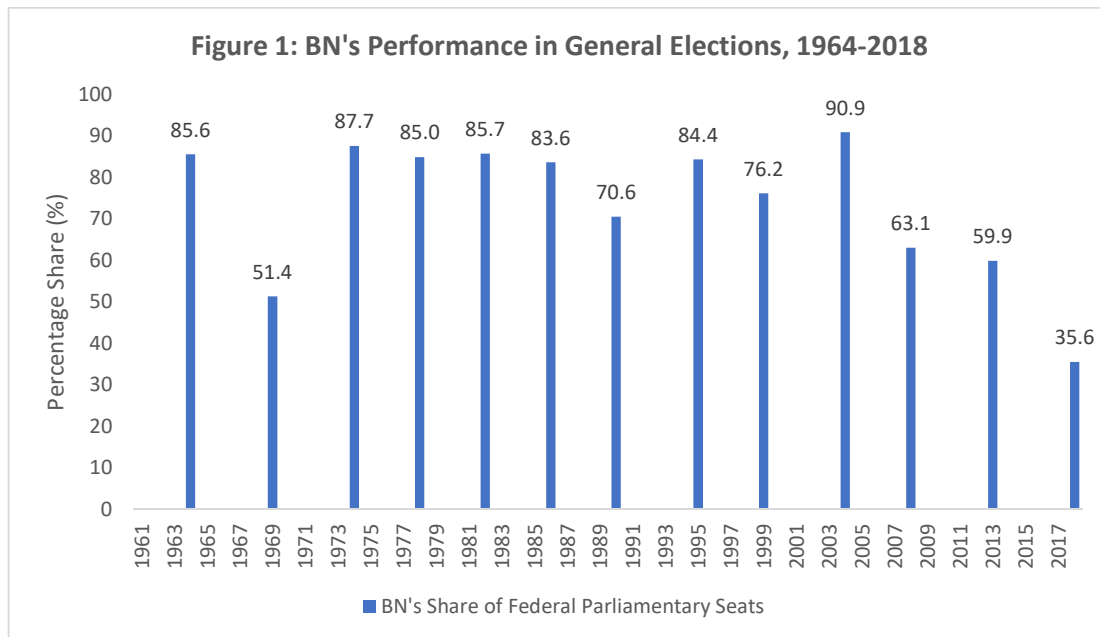
The analysis of economic reforms following a political regime change requires an understanding of the nature of the regime change and the factors (economic and non-economic) that lead to the change. The factors that induced political regime change are important as the new political party that replaces the incumbent party is likely to aim to deliver electoral promises (in the form of election manifesto) related to these factors. As is observed in Malaysia, such election promises significantly influence the economic reform agenda following a change in political regime. These two aspects – nature of regime change and factors driving regime change are discussed in the following sections.

3.1 The Nature of Regime Change in Malaysia

Before the 14th General Election (GE14), the incumbent political coalition, Barisan Nasional (BN) and its predecessor the Alliance had won every general election since the first general election was held in 1955 (two years before Malaysia gained independence).² BN performed

² BN was founded in 1973. Its predecessor the Alliance was formed in 1952 and comprised the three key communal-based political parties, namely, United Malays National Organisation (UMNO), Malaysian Chinese Association (MCA) and Malaysian Indian Congress (MIC). See Saravanamuttu (2016).

relatively well in the country's elections until 2008 (**Figure 1**). In the 12th General Election (GE12), the opposition coalition (Pakatan Rakyat, PR) denied the ruling coalition BN of its two-thirds majority in the Parliament.³ Another significant outcome of the GE12 is the state-level elections which saw the opposition coalition PR wresting control of five of the 13 states in Malaysia. Two of these state – Penang, and Selangor – are amongst the most developed states in Malaysia.⁴ These states provided solid bases for the major two component parties of PR – Democratic Action Party (DAP) in Penang and Parti Keadilan Rakyat (PKR) in Selangor. The states of Kelantan and Kedah came under the control of the Islamic party, Parti Islam SeMalaysia (PAS). In the 13th General Election (GE13) held in 2013, BN was voted back into power with a slight deterioration in the Federal elections. Each of the three component parties of PR – namely, DAP, PKR, and PAS – retained control of their respective base-states. PAS subsequently departed from the PR coalition in 2015 over disagreements on policy issues such as the implementation of the Islamic penal code. Following the departure of PAS, the PR coalition was dissolved, and a new coalition, Pakatan Harapan (PH) was immediately formed by three political parties, namely, PKR, DAP and AMANAH (a splinter party of moderate leaders from PAS).



³ PR is the precursor to Pakatan Harapan (PH).

⁴ Aside from Penang and Selangor, the PH coalition also won the state elections in Kelantan, Kedah and Perak. However, Perak subsequently fell back into BN control after the defection of three state assemblymen.

The 62-year rule of BN in Malaysia finally came to an end in Malaysia in the country's 14th general election (GE14) which was held on 9 May 2018. In the election, the then opposition coalition Pakatan Harapan (PH) garnered 113 seats of the available 222 parliamentary seats. BN's performance was dismal, winning only 79 seats compared to the 133 seats it won in the previous general election in 2013. The results of GE14 was unexpected by almost all political parties and commentators. BN was largely expected to retain power albeit but a slimmer majority. In addition to retaining control over the states of Penang and Selangor, PH won control over five additional states.⁵

Another aspect of the outcome of the GE14 is the asymmetry in the votes for the political coalitions across the different ethnic groups. In the GE14, Malay voters account for 61 percent of total registered voters. In the GE14, estimates of the PH coalition's share of Malay votes in Peninsular Malaysia ranged between 24-31 percent, which is below of that obtained by BN (35-46 percent) and PAS (30-33) (**Table 1**). The informal cooperation between BN and PAS in the post-GE14 period has significant implications for the policy reform orientations of the PH-led government.

**Table 1: Estimates of Percentage Share of Malay Votes
by Political Coalition and Party in GE14 in Peninsular Malaysia**

Analysts	BN	PAS	PH
John Funston	36.6	31.7	31.7
Dah Ikhwan	46.29	28.14	25.47
Merdeka Centre	35-40	30-33	25-30
Ong Kian Ming	44	32	24

Sources:

John Funston: <https://www.newmandala.org/malay-dominance-remains-despite-umnos-rout/>

Dah Ikhwan: <https://dahalmi.wordpress.com/2018/05/22/pru-14-keputusan-dan-analisis-mengikut-kerusi-dan-kaum/>

Merdeka Centre: <https://www.freemalaysiatoday.com/category/nation/2018/06/14/report-95-chinese-but-less-than-30-malays-voted-for-ph/>

Ong Kian Ming: <https://www.malaysiakini.com/news/463053>

⁵ These states included Johor, Kedah, Melaka, Negeri Sembilan, Perak and Sabah.

The literature on the political economy of reforms places importance of the degree of political fragmentation of winning political coalitions (PH) as well as the cohesiveness of the losing (opposition) parties (BN). Thus, an important aspect of the regime change is the structure and dynamics of political coalitions that contested in GE14. Political elites play important roles in regime change and post-election economic reforms (Magaloni, 2006; Reuter and Gandhi, 2010).

In the case of Malaysia, there were significant changes in the opposition political parties and coalition prior to the GE14. In 2017, the Parti Pribumi Bersatu Malaysia (PPBM) – a party founded by the former Malaysian Prime Minister Mahathir Mohamad and comprising primarily elite and splinter/defector members from UMNO – formally joined the PH coalition.⁶ Another UMNO splinter party in Sabah (in East Malaysia) - Parti Warisan Sabah (WARISAN) – also joined the PH coalition. Thus, elite defections (a key feature in the literature on the end of single-party dominance) played an important role in the outcomes of GE-14 (**Figure 2**). Of the 121 parliamentary seats won by PH in the GE14, 31 seats (or 26 percent) came from the three splinter/defector elite parties (**Table 2**). The incumbent BN coalition lost a total of nineteen seats to these party defectors. These party defectors were particularly important for political contestation for Malay votes. The leader of PPBM, Mahathir Mohamad, campaigned aggressively in the four months leading to GE-14. Aside from Mahathir Mohamad and Muhyiddin Yassin, PPBM Vice-President and another former elite member of UMNO also actively mobilized voters (especially Malay voters) to vote against UMNO and BN. Other former UMNO leaders and former members of Mahathir’s cabinet that were not PBM party members such as Rafidah Aziz (former Wanita UMNO chief and former trade minister) and Daim Zainuddin (former UMNO treasurer and former finance minister) were also roped into campaigning for the PH coalition. As will be argued later, Mahathir and members from the splinter coalition parties were to play a significant role in policymaking in the aftermath of GE14.

⁶ Aside from Mahathir Mohamad who was a former president of UMNO and Malaysia’s longest serving Prime Minister from 1981 to 2003, other members of PPBM included Muhyiddin Yassin (former vice-president of UMNO and former Deputy Prime Minister) and Mukhriz Mahathir (former Menteri Besar of the state of Kedah and son of Mahathir Mohamad).

Figure 2: Political Elite Defections and Electoral Outcomes

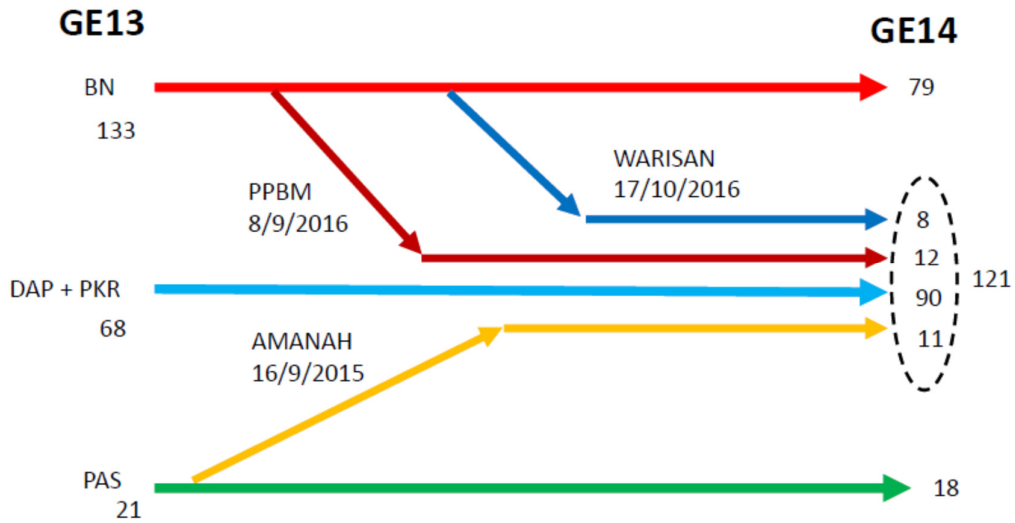


Table 2: Parliamentary Seats Won by Parties in GE-13 and GE-14

		Seats Won in GE-14							
		BN	PKR	DAP	PAS	PBBM	AMANAHA	WARISAN	OTHER
Seats Won in GE-13	BN	78	21	4	5	12	3	7	3
	PKR	0	27	0	0	0	1	1	1
	DAP	0	0	38	0	0	0	0	0
	PAS	1	0	0	13	0	7	0	0
	PBBM	0	0	0	0	0	0	0	0
	AMANAHA	0	0	0	0	0	0	0	0
	WARISAN	0	0	0	0	0	0	0	0
	OTHER	0	0	0	0	0	0	0	0

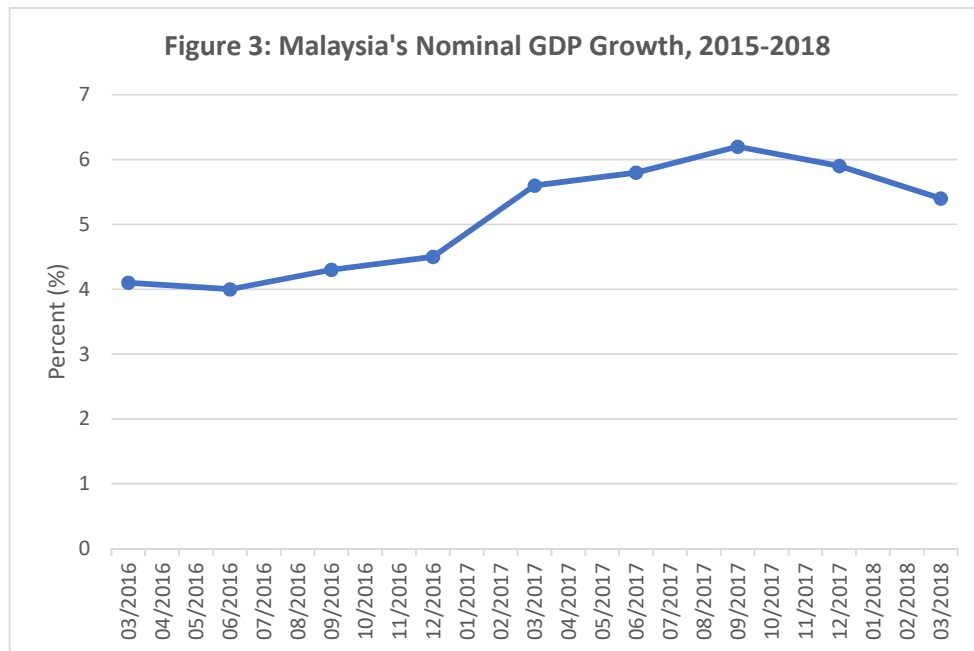
3.2 Economic Factors and Regime Change

Economic conditions can affect electoral outcomes. According to the economic voter hypothesis (or economic voting model), citizens will vote for the incumbent ruling party if the economy is doing well and against it, otherwise (Lewis-Beck and Stegmaier, 2000). Overall,

the empirical literature supports the hypothesis. Economic factors that matter in elections include economic growth, the rate of inflation, and unemployment (Lewis-Beck and Stegmaier, 2000 and Fair, 1996). Higher economic growth, lower inflation, and lower unemployment are positively associated with political support for the incumbent party in elections. The importance of economic factors also means that political parties aspiring to defeat the incumbent ruling party are likely to promise economic reforms in elections. Did Malaysian voters consider economic factors to be important and if yes, what were their key concerns?

In a survey carried out by Merdeka Centre between 28 April 2019 to 8 May 2019, “economic concerns” was regarded as the most issue for voters with some 43 percent of the respondents interviewed indicating this.⁷ This was followed by corruption (21%), preservation of Malay rights/fair treatment of all races (8%) and leadership and governance (8%).

Do the economic indicators support these concerns? In terms of economic growth, the quarterly growth rate for the country’s national income (GDP) exceeded 5 percent (**Figure 3**). Thus, the sharp deterioration in the electoral performance of the incumbent coalition BN took place amidst relatively robust economic growth.



⁷ Merdeka Centre. Malaysia General Elections 14: Prospects and Outcome III, 8 May 2019.

One issue that was consistently highlighted by opposition coalition PH during the election campaign period was the rising cost of living. This was often attributed to the implementation of the Goods and Services Tax (GST) by the BN government. The GST which took effect on 1st April 2015, about three years before the elections. Superimposing the trends in inflation against the timing of GST implementation shows that the inflation rate did increase in the nine months after the implementation of the GST. However, this effect seems to have subsided after this period (**Figure 4**). However, a sharp increase in the inflation rate is observed during the period from the third quarter of 2016 to the first quarter of 2017. This trend of rising inflation coincided with the Malaysian Ringgit's depreciation (**Figure 5**). Even though inflation subsided subsequently, the inflation rate remained above 3.5 percent until GE-14. It is possible that the cumulative effects of inflation (due to ratchet effects) could have affected cost of living.

Finally, the unemployment rate in Malaysia increased from 2.7 percent in the third quarter of 2014 to 3.5 percent in third quarter of 2016 (**Figure 6**). The unemployment rate remained at around 3.3 percent until the first quarter of 2018. The unemployment rate was relatively high in 2018 compared to historical trends in the previous period of 2010-2014.

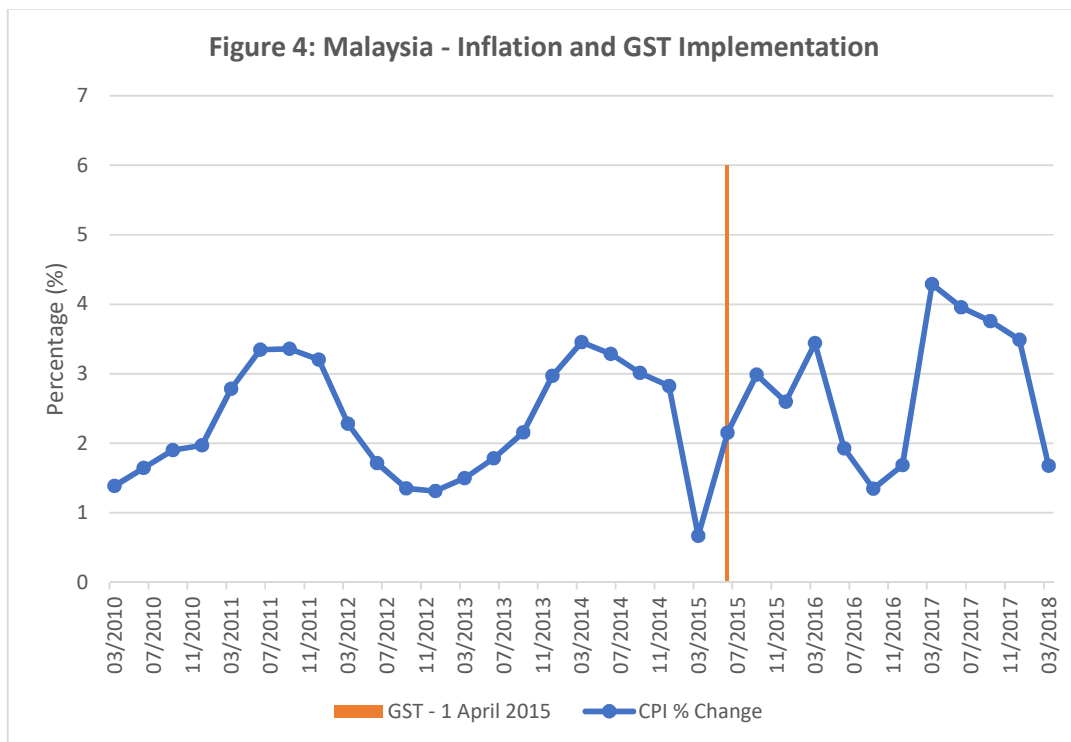


Figure 5: Malaysia - Inflation and Exchange Rate, Q1-2010 - Q1-2018

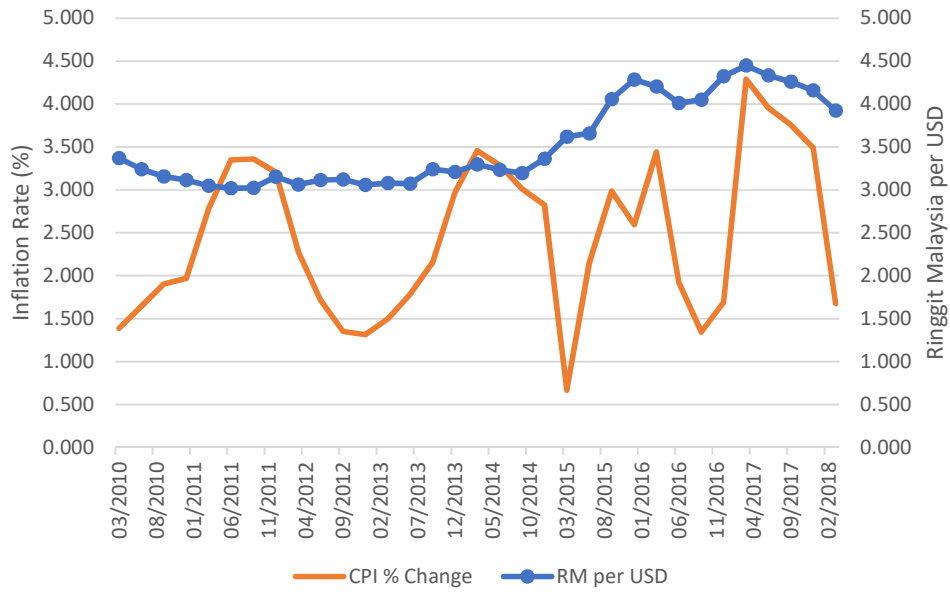
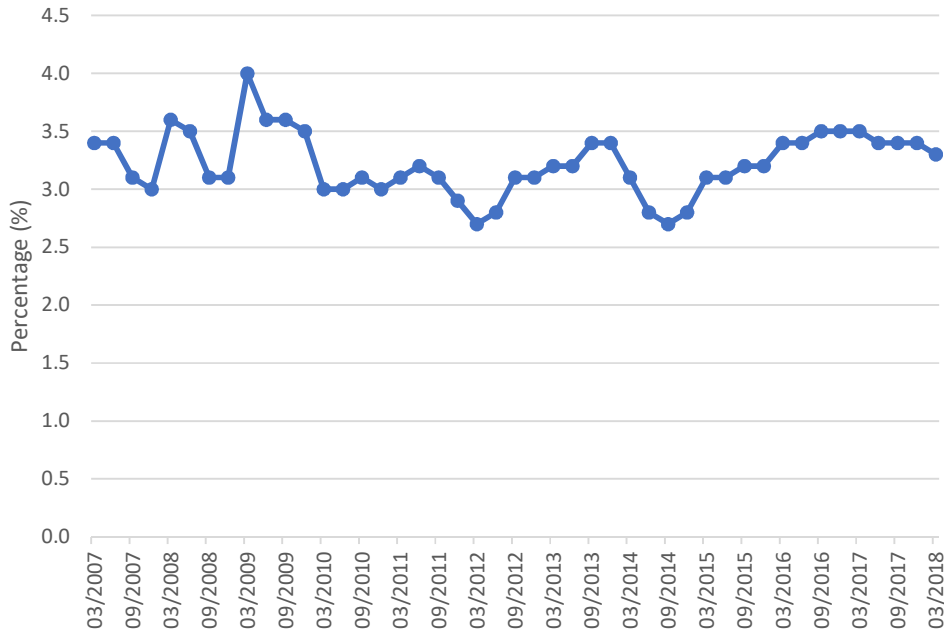


Figure 6: Malaysia - Unemployment rate



The influence of these various economic factors on the outcome of GE14 can be estimated using economic voting model. In an earlier study, Lee (2019) undertook such an estimation using electoral outcomes of GE13 and GE14. In the study, the share of votes obtained by BN in a parliamentary constituency i located in state j and year t can be modeled as follows:

$$V_{it} = \alpha_1 + \alpha_2 GDP_{j,t-1} + \alpha_3 INF_{j,t-1} + \alpha_4 UNEMP_{j,t-1} + \alpha_5 GINI_{j,t-1} + \alpha_6 BUMI_{it} + \alpha_7 EAST_{jt} + \alpha_8 VTURN_{it} + \alpha_9 INCUMBIND_{it} + \alpha_{10} INCUMBPTY_{it} + \alpha_{11} DENSITY_{it} + \alpha_{12} MAHA_{it} + \varepsilon_{it}$$

where GDP is the growth rate of Real GDP per capita (lagged by one year, state), INF the inflation rate (lagged by one year, state), UNEMP the unemployment (lagged by one year, state), GINI the Gini coefficient (lagged by one year, constituency), BUMI the share of Bumiputra voters (constituency), EAST a dummy variable for East Malaysia (Sabah and Sarawak), VTURN voter turnout, INCUMBIND individual incumbency, INCUMBPTY party incumbency, DENSITY population density and MAHA a dummy variable representing Mahathir's visit to a constituency during the election campaign.

Results from the study's estimations are re-produced as **Table 3**. Economic growth is negatively correlated to the vote share of UMNO in GE-14. Inflation is statistically insignificant in GE14. This could be because cumulative effects of inflation could be more important than current inflation rate. Higher unemployment is negatively correlated with BN's vote share in GE-14. Higher inequality, as measured by the Gini coefficient, is negatively correlated with BN's vote share in GE14. Ethnic voting is important in GE14 as higher share of Bumiputra voters is associated with higher BN's vote share. Incumbency – both at the individual and party level – remained important in GE-14.

To summarize the findings of this section, the Malaysian economy was growing at a relatively robust rate and not anywhere near a crisis level. However, the trends in inflation and unemployment do indicate a deterioration in economic conditions. One economic issue that was much emphasized in the electoral campaign of the PH coalition was the alleged financial scandal and abuse surrounding the 1Malaysia Development Berhad (1MDB). **Box Article 1** provides a brief description of the 1MDB financial scandal. The impact of this factor on GE14 is difficult to estimate statistically. However, in a Merdeka Center's survey carried out in June

2018, the top three factors selected by respondents as contributory factors to BN's defeat were the rejection of Najib Razak (40%), GST (22%) and 1MDB (14%).⁸

Table 3: Determinants of BN's Vote Share in GE-14

	GE-14	GE-14 + MAHA	GE-14 + MAHA + PM
VARIABLES	BN Vote Share	BN Vote Share	BN Vote Share
GDP(-1)	-0.168** (0.0672)	-0.172** (0.0679)	0.117* (0.0701)
INF(-1)	-0.266 (0.213)	-0.264 (0.214)	0.393* (0.205)
UNEMP(-1)	-0.164** (0.0650)	-0.168** (0.0656)	0.0510 (0.0667)
GINI	-0.425** (0.178)	-0.430** (0.179)	-0.563*** (0.181)
BUMI	0.128*** (0.0246)	0.129*** (0.0248)	0.399*** (0.0384)
EAST	0.226*** (0.0694)	0.225*** (0.0695)	
VTURN	-1.198*** (0.416)	-1.197*** (0.417)	-2.296*** (0.580)
INCUMBIND BN	-0.0270 (0.0681)	-0.0268 (0.0682)	-0.0153 (0.0765)
INCUMBPTY BN	0.261*** (0.0697)	0.258*** (0.0701)	0.190** (0.0768)
INCUMBIND Non-BN	-0.191*** (0.0490)	-0.189*** (0.0493)	-0.120** (0.0466)
INCUMBPTY Non-BN	-0.205*** (0.0501)	-0.207*** (0.0506)	-0.155*** (0.0478)
DENSITY	-4.64e-05*** (1.17e-05)	-4.59e-05*** (1.18e-05)	-2.49e-05** (1.08e-05)
MAHA		-0.0200 (0.0480)	-0.0248 (0.0411)
Constant	3.156*** (0.486)	3.160*** (0.487)	0.123 (0.573)
Observations	221	221	165
R-squared	0.737	0.737	0.802
Notes: PM – Peninsular Malaysia; Standard errors in parentheses;			
*** p<0.01, ** p<0.05, * p<0.1			

Source: Lee (2019)

⁸ Merdeka Center, Kajiselidik Pemilihan UMNO 2018, 25-28 June 2018.

Box Article 1: The 1MDB Financial Scandal

1Malaysia Development Berhad or 1MDB is a private corporation that is wholly-owned by the Ministry of Finance, Malaysia. It was established in 2009 by converting a state sovereign investment fund, the Terengganu Investment Authority, into a federal entity. The 1MDB was assigned the role of a strategic investment company with the mission “to drive sustainable economic development by forging strategic global partnerships and promoting FDI”. To fulfill its mission, 1MDB invested in two key sectors, namely power (electricity generation) and real estate sectors.

The 1MDB became a controversial issue in Malaysia, mainly because of its financing aspects, allegations of financial abuse and corruption. There was a lack of transparency and the consistency of information on how the borrowings have been utilized. The 1MDB became a political liability for BN in GE14. Critics have linked 1MDB’s financial woes to allegations of corruption and fraud. This has been accompanied by the media’s expose on the lavish lifestyle of ruling-party politicians and their family members.

In the aftermath of GE14, the former prime minister Najib Razak has been investigated for the theft of funds from 1MDB. The trial began on 28 August 2018, and the AG Office is prosecuting Najib Razak for money laundering and abuse of power involving the receipt of illegal transfers amounting to at least RM 2.3 billion ringgit (US\$550.8 million) during the period 2011-2014.

4. Economic Reforms Post GE-14

4.1 Context of Economic Reforms

The change in the ruling government is a unique event in the history of Malaysia. However, there are several factors that should be taken into account when discussing the economic reforms of the new PH-led government. Some of these factors are highlighted in the review of the literature on the political economy of reforms.

First, the electoral victory of the opposition coalition PH in the GE14 was unexpected. This has two implications. The promises contained in the election manifesto of PH were drafted without any expectation that they will be implemented. This implies that some of the election promises are unrealistic. This problem is compounded by information asymmetry in which the PH leaders are unaware of the conditions of the state machinery.

Second, as this the first time that a change in government has occurred in Malaysia, very few of the political leaders that assumed ministerial positions have experiences in running the state machinery (**Table 4**). The exception is Mahathir Mohamad who was Prime Minister from 1981-2003. The two key economic portfolios – Minister of Finance and Minister of Economic Affairs – are helmed by politicians that have state-level executive leadership experiences. The lack of experience of many of the new cabinet ministers in the PH government was also compounded by the fact that the PH coalition (and its predecessor PR) did not form a “shadow cabinet” when they were on the opposition side. Ironically, it was the out-of-power BN that formed the first shadow cabinet in Malaysian history.⁹

Third, the composition of the cabinet in terms of political party membership indicates that this is a more politically diverse and fragmented cabinet than the previous government. In the previous BN-led government, UMNO dominated the cabinet (**Table 5**). All the key ministerial positions were allocated to UMNO politicians in the previous government. Whether the diversity and fragmentation of the PH cabinet have had a positive or negative effect on policy-making is an open question.

⁹ “Malaysia has a shadow Cabinet for the first time”, Straits Times, 27 September 2018.

Table 4: Profile of Key Cabinet Members in the PH-Led Government

Cabinet Portfolio	Office Bearer	Party	Executive Experience in Government Affairs
Prime Minister	Mahathir Mohamad	PPBM	Prime Minister (1981-2003)
Deputy Prime Minister	Wan Azizah Wan Ismail	PKR	-
Minister of Finance	Lim Guan Eng	DAP	Chief Minister of Penang (2008-2018)
Minister of Economic Affairs	Mohamed Azmin Ali	PKR	Menteri Besar of Selangor (2014-2018)
Minister of Defence	Mohamad Sabu	AMANAH	-
Minister of Home Affairs	Muhyiddin Mohd. Yassin	PPBM	Deputy Prime Minister (2009-2015)
Minister of International Trade and Industry	Ignatius Darell Leiking	WARISAN	-
Minister of Education	Maszlee Malik	BERSATU	-
Minister of Water, Land and Natural Resources	Xavier Jayakumar Arulanandam	PKR	-
Minister of Federal Territories	Khalid Abdul Samad	AMANAH	-
Minister of Transport	Anthony Loke Siew Fook	DAP	-
Minister of Agriculture and Agro-based Industry	Salahuddin Ayub	AMANAH	-
Minister of Health	Dzulkefly Ahmad	AMANAH	-
Minister of Tourism, Arts and Culture	Mohammadin Ketapi	WARISAN	-
Minister of Housing and Local Government	Zuraida Kamaruddin	PKR	-
Minister of Foreign Affairs	Saifuddin Abdullah	PKR	Deputy Minister of Higher Education (2009-2013)
Minister of Human Resources	Kula Segaran Murugeson	DAP	-
Minister of Domestic Trade and Consumers Affairs	Saifuddin Nasution Ismail	PKR	-
Minister of Entrepreneurship Development	Mohd. Redzuan Md. Yusof	PPBM	-
Minister of Rural Development	Rina Mohd Harun	PPBM	-
Minister of Works	Baru Bian	PKR	-
Minister of Energy, Science, Technology, Environment, and Climate Change	Yeo Bee Yin	DAP	-
Minister of Primary Industries	Teresa Kok Suh Sim	DAP	Selangor Senior Executive Councillor (Investment, Trade and Industry Committee)
Minister of Youth and Sports	Syed Saddiq Syed Abdul Rahman	PPBM	-
Minister of Communication and Multimedia	Gobind Singh Deo	DAP	-

Table 5: Composition of Cabinet by Political Party Membership

Pakatan Harapan Cabinet (2018-2019)		Barisan Nasional Cabinet (2013-2018)	
Portfolio	Party	Portfolio	Party
Prime Minister	PPBM	Prime Minister	UMNO
Deputy Prime Minister	PKR	Deputy Prime Minister	UMNO
Minister of Finance	DAP	Minister of Finance	UMNO
Minister of Economic Affairs	PKR	Minister in the Prime Minister's Department	Indep
Minister of Defence	AMANAH	Minister of Defence	UMNO
Minister of Home Affairs	PPBM	Minister of Home Affairs	UMNO
Minister of International Trade and Industry	WARISAN	Minister of International Trade and Industry	UMNO
Minister of Education	BERSATU	Minister of Education & Ministry of Higher Education	UMNO
Minister of Water, Land and Natural Resources	PKR	Minister of Natural Resources and Environment	MIC/PBB
Minister of Federal Territories	AMANAH	Minister of Federal Territories	UMNO
Minister of Transport	DAP	Minister of Transport	MCA
Minister of Agriculture and Agro-based Industry	AMANAH	Minister of Agriculture and Agro-based Industry	UMNO
Minister of Health	AMANAH	Minister of Health	MIC
Minister of Tourism, Arts and Culture	WARISAN	Minister of Tourism, Arts and Culture	UMNO
Minister of Housing and Local Government	PKR	Minister of Urban Wellbeing, Housing and Local Government	UMNO
Minister of Foreign Affairs	PKR	Minister of Foreign Affairs	UMNO
Minister of Human Resources	DAP	Minister of Human Resources	SUPP
Minister of Domestic Trade and Consumers Affairs	PKR	Minister of Domestic Trade, Co-operatives and Consumerism	UMNO
Minister of Entrepreneurship Development	PPBM	Minister of Entrepreneurship Development	UMNO
Minister of Rural Development	PPBM	Minister of Rural and Regional Development	UMNO
Minister of Works	PKR	Minister of Works	PBB
Minister of Energy, Science, Technology, Environment and Climate Change	DAP	Minister of Science, Technology and Innovation	UPKO
Minister of Primary Industries	DAP	Minister for Plantation Industries and Commodities	PBB
Minister of Youth and Sports	PPBM	Minister of Youth and Sports	UMNO
Minister of Communication and Multimedia	DAP	Minister of Communication and Multimedia	UMNO

Fourth, the change in government was a peaceful and relatively smooth process without any political violence. As a result, the bureaucracy also remained relatively intact. However, a few key officeholders were replaced – the Chief Secretary and Secretary-General of the Ministry of Finance. A notable change in the bureaucracy is the restructuring of the Economic Planning Unit (EPU) – the agency responsible for medium to long-term economic planning – into the Ministry of Economic Affairs (MEA).¹⁰ In addition to absorbing the EPU, a large number of government agencies were put under MEA (see **Table 6**). These included state development agencies and agencies targeted to support the Bumiputra community.

Table 6: List of Agencies under the Ministry of Economic Affairs

<p><u>Federal Agencies</u></p> <ul style="list-style-type: none"> • Malaysian Government Official Portal • Department of Statistics Malaysia • Halal Development Corporation (HDC) • Bank Pembangunan Malaysia Berhad • Malaysia Petroleum Resources Corporation Berhad (MPRC) • MyHSR Corporation Sdn. Bhd. • Pelaburan Hartanah Berhad • Amanah Raya Berhad <p><u>State Development Agencies</u></p> <ul style="list-style-type: none"> • Johor Petroleum Development Corporation (JPDC) • Perbadanan Kemajuan Ekonomi Negeri Perlis • Perbadanan Kemajuan Negeri Kedah • Penang Development Corporation (PDC) • Perbadanan Kemajuan Negeri Perak • Perbadanan Kemajuan Iktisad Negeri Kelantan • Perbadanan Memajukan Iktisad Negeri Terengganu • Perbadanan Kemajuan Negeri Pahang • Perbadanan Kemajuan Negeri Selangor • Perbadanan Kemajuan Negeri, Negeri Sembilan • Perbadanan Kemajuan Negeri Melaka • Johor Corporation (JCORP) • Sarawak Economic Development Corporation (SEDC) • Sabah Economic Development Corporation (SEDCO) 	<p><u>Agencies to Support Bumiputra Community</u></p> <ul style="list-style-type: none"> • JKP Sdn. Bhd. (Real Estate) • Unit Peneraju Agenda Bumiputera (TERAJU) • Ekuiti Nasional Berhad (EKUINAS) • FELDA Global Ventures Holdings Berhad • Yayasan Amanah Hartanah Bumiputera • Yayasan Ekuiti Nasional • Yayasan Peneraju Pendidikan Bumiputera <p><u>Statutory Board Agencies</u></p> <ul style="list-style-type: none"> • Lembaga Kemajuan Tanah Persekutuan (FELDA) • Lembaga Penyatuan dan Pemulihan Tanah Persekutuan (FELCRA) Berhad • Pihak Berkuasa Kemajuan Pekebun Kecil Perusahaan Getah (RISDA)
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Source: Ministry of Economic Affairs: <https://www.mea.gov.my/en/organisation/link-agencies>

¹⁰ The EPU was previously under the Prime Minister's Office.

Fifth, even though economic issues were important to voters in GE14, the Malaysian economy was not in a crisis mode. Growth was fairly robust and economic concerns amongst citizens revolved mainly around the cost of living (inflation) and corruption (see **Table 7**). It is also interesting to that that there were differences across communities in terms of the importance of the issues. A higher percentage of Malays compared to the Chinese were more concerned about inflation. The reverse was true for corruption. Overall, many of these issues were picked up by the then opposition coalition PH and was incorporated into their election manifesto.

Table 7: Percentage of Respondents Indicating Issues to be Important (%)

Issues	Total	Malay	Chinese	Indian
Inflation	50	54	39	55
Corruption	32	25	48	23
Malay rights / fair treatment of all races	21	18	29	27
Job opportunities	21	23	11	32
Housing	15	15	9	31
Worsening race relations	9	9	9	6
Political instability	9	11	6	2
1MDB case	7	7	9	3

Source: Merdeka Center, “National Public Opinion Survey – Perception towards Economy, Leadership & Current Issues”, 7-14 August 2018

Finally, one of the key constraint to the implementation of economic reforms when PH took over the Federal government in May 2018 was budgetary constraints. One of the earliest messages from the new Pakatan-led government in its early days of taking control of the government machinery was the dire state of the government’s fiscal capacity. On 20 May 2018, ten days after Mahathir Mohamad was sworn in as the new Prime Minister, he announced that the Federal government amounted to more than one trillion Ringgit – a figure higher than expected, much of which was hidden from public.¹¹ A detailed breakdown of the Federal

¹¹ The then new Minister of Finance, Lim Guan Eng, also brought attention to the existence of “red files” on selected projects (such as 1MDB) which had very restricted access status within MOF. See “Guan Eng shocked that Finance Ministry officials blocked from ‘red files’” STAR, 22 June 2018.

Government’s debt and liabilities debt was subsequently released by the Ministry of Finance (MOF). This is summarized in **Table 8**. These constraints on fiscal capacity were to affect the implementation of economic reforms by the PH-led government subsequently.

Table 8: Federal Government Debt and Liabilities

	RM Billion		Share of GDP (%)	
	End-2017	End-June 2018	End-2017	End-June 2018
Federal government debt	686.8	725.2	50.7	50.7
Committed government guarantees	102.1	117.5	7.5	8.2
1MDB (Net Debt)	38.3	38.3	2.8	2.7
Other liabilities (PPP, PFI, and PBLT)	260.1	184.9	19.2	12.9
Total	1,087.3	1,065.9	80.3	74.5

Source: Ministry of Finance, Malaysia

Note: PPP (public-private partnership - project), PFI (public finance initiative – procurement), PBLT (Developer of projects for Royal Malaysia Police)

4.2 Economic Reforms & the Pakatan Harapan’s Election Manifesto

The 150-page election manifesto of the Pakatan Harapan titled “Buku Harapan” (Book of Hope) was, in many respects, the political coalition’s agenda for reforms. The manifesto contained 60 promises grouped into five categories (“pillars”) and five “special commitments” to various communities (**Appendix Table 1**). The Pillar 1 which carries the heading “Reduce the People’s Burden” contains ten promises that underpin PH’s economic reform agenda post-GE14. Based on some of these ten promises under Pillar 1, a specific list of ten actions were promised to be implemented within the first 100 days of the new PH-led government. This is in **Table 9**. Overall, the new government has taken actions to fulfill nine of the ten promises that scheduled to be implemented in the first 100 days. Other actions have also been taken that are part of ten promises under Pillar but do not fall under the 100-days promise category. The impact of a few of these key actions is discussed next.

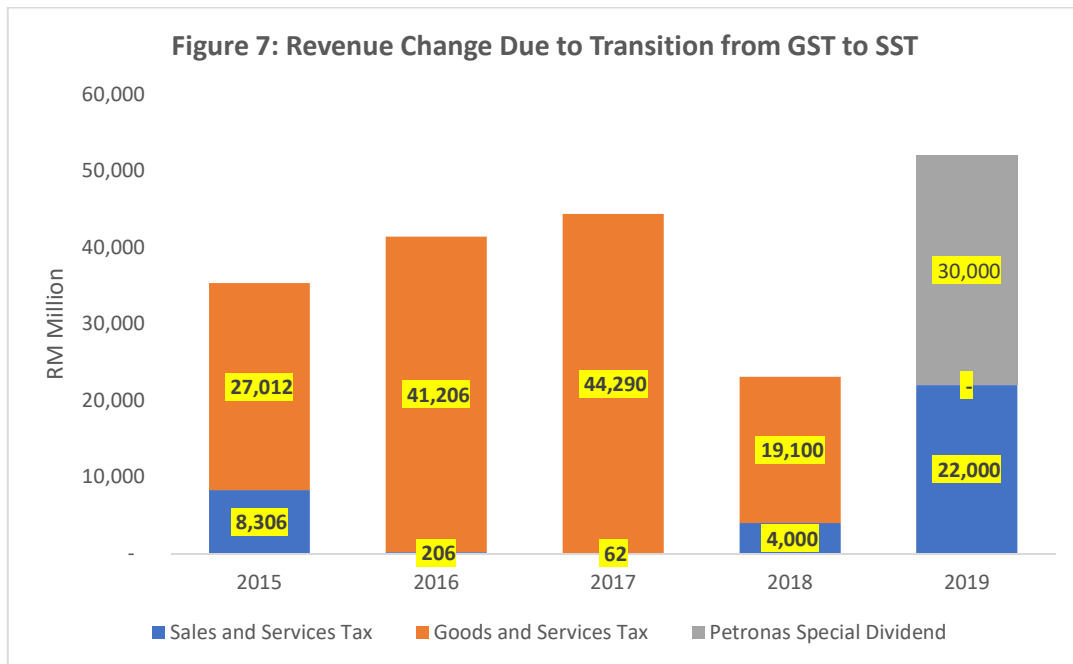
Table 9: Ten Actions to be Implemented within the First 100 Days

Action Item	Implementation Status	Estimated Cost
1. Abolish the GST and take steps to reduce cost of living.	GST has been replaced with SST. The Festive Season Price Control Scheme has been implemented.	The revenue gap between GST and SST is estimated to be around RM22 billion.
2. Stabilise the price of petrol and introduce targeted petrol subsidies.	The RON95 petrol is currently subsidized and price is capped at RM2.08 per litre. There are plans to replace this with direct cash transfer to low-income recipients.	The RON95 subsidy is estimated to cost RM3 billion in 2019.
3. Abolish unnecessary debts that have been imposed on FELDA settlers.	The debts of FELDA settlers have not been abolished. Instead, FELDA will restructure and delay repayment of these debts	In April 2019, the government injected RM6.23 billion into FELDA.
4. Introduce EPF contribution for housewives	This will be implemented in three phases. Phase 1 and Phase 2 began in August 2018 and early 2019. Phase 3 will begin in early 2020.	Phase 1 is estimated to cost the government RM20 million. There are no estimates for Phase 2 & Phase 3.
5. Equalise the minimum wage nationally and start the processes to increase the minimum wage.	The standardised minimum wage of RM1,100 month was implemented on 1 January 2019.	-
6. Postpone the repayment of PTPTN to all graduates whose salaries are below RM4,000 per month and abolish the blacklisting policy.	The blacklisting of defaulters has been abolished but deferment of repayment has not been implemented.	The total loan portfolio of PTPTN is estimated to be RM40 billion with non-performing loans at RM6.4 billion in 2018.
7. Set up Royal Commissions of Inquiry on 1MDB, FELDA, MARA and Tabung Haji, and to reform the governance of these bodies.	No RCIs have been formed.	-
8. Set up a Special Cabinet Committee to properly enforce the Malaysia Agreement 1963.	The special committee has been formed. As at August 2019, 7 of the 21 issues have been resolved.	-
9. Introduce Skim Peduli Sihat with RM500 worth of funding for the B40 group for basic treatments in registered private clinics.	The government has begun piloting two health programs for B40: (i) B40 Health Protection Fund (HPF) for health insurance (ii) Skim Perlindungan Kesihatan (PEKA)	The initial cost are: (i) RM2 billion for HPF and (ii) RM100 million for PEKA
10. Initiate a comprehensive review of all megaprojects that have been awarded to foreign countries.	A number of mega projects have been either canceled, postponed or/and scaled-down	(i) The ECRL project has been scaled down from RM66.6 billion to RM44 billion (ii) The KL-Singapore High Speed Rail, estimated to cost RM110 billion has been deferred by two years to 2020 (iii) The Trans-Sabah Gas Pipeline costing RM10.4 billion has been canceled (iv) The cost of the Mass Rapid Transit 2 (MRT2) project has been reduced from RM22.64 billion to RM17.42 billion.

Sources: Author's compilation based on Buku Harapan, IDEAS (2019a, 2019b) and media reports.

(a) Abolishment of the Goods and Services Tax (GST)

The abolishment of the GST is one of the key promises in the PH’s election manifesto. The GST was zero-rated on 1 June 2018 and was subsequently replaced by the Sales and Services Tax (SST) on 1 September 2018. There has been no systematic evaluation of the impact of the GST removal on the cost of living in Malaysia. The removal of GST did weaken the country’s fiscal capacity significantly. The estimated revenue gap between SST and GST amounted to about RM22 billion in 2019 (or about nine percent of total fiscal revenue) (see **Figure 7**). This revenue gap was temporarily filled by the special dividend of RM30 billion paid by the national oil company PETRONAS. By all accounts, GST is regarded superior to SST and the abolishment of GST was clearly a populist policy by the new government.



(b) Price Stabilization and Control

The new government has also implemented policies to minimize the impact of prices increases (Promise 2, Pillar 1). An allocation of RM150 million for price stabilization was announced in the 2019 Budget. The Festive Season Price Control Scheme (SKHMP) have also been implemented to control the prices of essential goods for seven annual festival seasons.¹²

The new government does recognize that exchange-pass through effects of a weak Ringgit can adversely impact prices. The election manifesto called for action to “revive” the Malaysian Ringgit within three years. This is difficult to implement as the country uses a floating exchange rate regime. Thus far, the country’s central bank, Bank Negara Malaysia, has mainly intervened to stabilize the exchange rate.¹³

Another source of price-related burden is the monopoly supplies for some of the essential goods and services. The national monopoly status of such companies is currently under review. These include (i) Padiberas Nasional Bhd (Bernas) – for rice imports and distribution, (ii) Puspakom - for vehicle inspection services, (iii) Pharmaniaga Bhd – for pharmaceutical supply for public hospitals, and (iv) MyEG Services Bhd – for e-government solutions and services.

(c) Petrol Price and Subsidies

The third 100-day promise calls for the stabilization of the price of petrol and the introduction of targeted petrol subsidies (note: the latter also appears as Promise no.7 under Pillar 1 of the election manifesto). At present, the RON95 petrol is subsidized and the price is capped at RM2.08 per litre. In the 2019 Budget, the original plan was to implement targeted petrol subsidies based on vehicle engine capacity. This would have entailed subsidizing owners of vehicles and motorcycles with engine capacities below 1,500cc and 125cc, respectively. The subsidy rate would be fixed at 30 sen per litre for RON 95 petrol. A cap would also be imposed on total petrol consumption - 100 litres per owner for cars and 40 litres for motorcycles. This policy has since been abandoned. The government is now considering a new strategy to replace the petrol subsidy and price cap. The new strategy entails direct cash transfers to low-income recipients based on data on income/vehicle ownership contained in the Bantuan Sara Hidup (Cost of Living Aid) database. The overall impact of this new policy (which has not been implemented) – in terms of the impact on consumers and government budget - is uncertain.

¹² See <https://www.kpdnhep.gov.my/implementation-of-skhmp/?lang=en>

¹³ “Bank Negara refutes US Treasury claim of Malaysia as potential currency manipulator”, STAR, 29 May 2019.

(d) Abolishment of Tolls

Another policy that the new PH-led government has attempted to implement is the abolishment of tolls. This is an election promise (Promise 6, Pillar 1) even though it is not part of the list of ten 100-day promises. Malaysia has an extensive network of privatized expressways that date back to the privatization era beginning in the early 1980s during Mahathir Mohamad's first term as Prime Minister (Naidu & Lee, 1997). With close to 80 percent of Malaysians expected to live in urban areas by 2020, the abolishment of tolls can have a significant impact on easing the cost of living concerns in the country. However, due to financial constraints, the new government has come to the realization that it is too costly to abolish tolls. One estimate puts the total debt held by 29 toll concessionaires amounted to RM52 billion.¹⁴ Instead of abolishing tolls, the PH government is now planning to selective nationalize expressways and reduce their tolls gradually. In June 2019, the government made offers to acquire four toll highways for a total cost of RM6.2 billion. More recently, the media has reported that the government is assessing a proposal to acquire 15 tolled highways at a total cost of RM42.2 billion.¹⁵

(e) Review of Megaprojects Awarded Under Previous Government

Another 100-day election promise (no.10) that was swiftly implemented was the review of megaprojects that were awarded by the previous government. Though the election promise qualified such projects as "all megaprojects that have been awarded to foreign countries", the exercise went beyond projects awarded to foreign entities. One of the key targeted projects was the East Coast Rail Link (ECRL) – a joint project between the Malaysian government and the China Communications Construction Company Ltd (CCCC), a state-owned enterprise from China. During the GE14 campaign trail, many PH politicians called for the cancellation of the ECRL project. However, the PG government subsequently negotiated to down-size the project from RM66 billion to RM44 billion as the penalty cost (estimated to be RM21.7 billion) was too high.¹⁶ The other mega project that was reviewed was the Kuala Lumpur – Singapore High-Speed Rail (HSR). Similar to the ECRL, the initial stance of the PH government was to scrap the project. This would have incurred a penalty of RM500 million. In the end, the Malaysian government opted to negotiate for a deferment and pay a token compensation of S\$15 million to the Singaporean government (which had already spent S\$250 million up to that

¹⁴ "The truth about the toll abolition pledge", STAR, 25 February 2019.

¹⁵ "Decision on tolled highway takeover only after report tabled to Cabinet", STAR, 26 August 2019.

¹⁶ "PM: ECRL revived to avoid RM21 billion penalty", New Straits Times, 15 April 2019.

point). Other smaller mega projects were either scaled-down (e.g. Mass Rapid Transit 2) or canceled (e.g. The Trans-Sabah Gas Pipeline). Overall, even though fiscal constraints initially motivated the new PH government to cancel the megaprojects, the high-cost of project cancellation penalty pushed the government towards deferring or/and down-sizing the projects.

To summarize, the economic reform policies of the new government focused mainly on meeting some of the key election promises. These key policies fall into two categories. In the first category are policies aimed at pleasing voters such as the abolishment of the GST, price stabilization and control and petrol subsidies. Such policies appear to be populist in nature in so far as they resemble the “implementation of policies receiving support from a significant fraction of the population, but ultimately hurting the economic interests of this majority” (Acemoglu et al, 2012, p.772). However, as Rodrik (2018) cautioned, care should be given to what the ultimate interest of the majority should be. As the Malaysian experience is that of a regime change, short-term populist policies may be required to maintain support for longer-term reforms whose benefits are not only uncertain but will accrue only in the long-term. Furthermore, the multi-ethnic nature of the Malaysian society and the political fragmentation (as evidenced by the asymmetry in votes across the Malays and Chinese) may require economic populism to forestall political populism (Rodrik, 2018, p.199). Reforms related to these issues are examined in the next section.

5. Institutional Reforms Post GE14¹⁷

In the PH’s election manifesto and the many campaign speeches during the elections, the failures of the government under the incumbent coalition Barisan Nasional were often attributed to deep-seated weaknesses in governance. These institutional weaknesses resulted in widespread corruption and financial scandals. As a result, institutional reform became a major priority for the new PH-led government. The PH’s agenda for institutional reforms is encapsulated in its election manifesto as 19 promises under Pillar 2 titled “institutional and

¹⁷ This section draws extensively from the author’s previous work, Lee (2018).

political reform”.¹⁸ Unlike the economic promises under Pillar 1, these were to be implemented within the next five years.¹⁹ **Appendix Table 2** provides a summary of these reforms.²⁰

(a) Executive Reforms

A significant area of institutional reforms involves the executive body (government administration). These proposed reforms were aimed at reducing the concentration of power in the Prime Minister’s Office (PMO) (Promise 12, Pillar 2). They include: a two-term limit for the positions of Prime Minister and Menteri Besar (and Chief Minister), fewer agencies and ministers under PMO, and lower financial allocation to PMO.²¹ The decentralization of fiscal resources away from the PMO has already begun in the 2019 Budget. Another set of reforms involve the fiscal capacity of the government. These involve changing the main sources of tax revenues (from GST to SST), improving the system of fiscal management (asset, debt, and liability), and making the procurement system more transparent. These fiscal reforms will consolidate the liabilities and expenditures of the government in the medium to long-term. The greater transparency in the fiscal system will also improve governance which should lead to less corruption and more productive use of fiscal resources.

(b) Legislative Reforms

With regards to the legislature, the proposed reforms are clearly aimed at enhancing the role and autonomy of the Parliament as well as the quality of the law-making process. These are to be achieved by giving more resources to Parliament (e.g. Parliamentary Services Act) as well as the establishment and greater use of parliamentary select committees (Promise 16, Pillar 2).²² Thus far, the government has announced that it will establish six select committees

¹⁸ After the May elections, an advisory committee – the Institutional Reforms Committee (IRC) – was set-up to provide recommendations on regulatory reforms. The IRC submitted its final report in July 2018 but the report has not been published thus far.

¹⁹ Aside from the manifesto, both the Mid-Term Review of the Eleventh Malaysia Plan (published 11 October 2018) and the 2019 Budget (2 November 2018) have revealed additional information about these reforms.

²⁰ Other areas that also fall under institutional reforms but not covered in this essay include race-relations, human rights, bureaucracy and government linked companies (GLCs). Lack of space prevents treatment of these issues.

²¹ See Joshi (2018) for a more detailed analysis of the reduction in development expenditure allocation to the PMO.

²² A parliamentary select committee is formed by and reports to the parliament. Such a committee comprises selected parliamentarians. The use of parliamentary select committees is not entirely new though they were not extensively used in the previous government. Under the Najib Administration, only two parliamentary select committees were used, namely, the Special Select Committee on Electoral Reform (2011-2012) and the Select Committee on the Lynas Advanced Materials Plant Project (2011-2012).

covering the consideration of bills, budget, home and defence, rights and gender equality, Federal-State relations, and, major public appointments.²³ The goal of using parliamentary select committees for major public appointments for agencies (such as the Elections Commissions (EC) and the Anti-Corruption Commission (MACC)) is to reduce the influence of elected politicians on such agencies. Unfortunately, this has not been implemented as such appointments involve changing in the country's constitution which requires two-third majority approval in the lower house (Dewan Rakyat).²⁴

(c) Judiciary Reforms

Judiciary reforms are aimed primarily at removing the influence of the executive body (politicians) in the selection of judges and on the decisions of the judges (Promise 19, Pillar 2). This is to be achieved by the use of a parliamentary select committee to approve the appointment of members of the Judicial Appointments Commission (which selects, for the prime minister's consideration, judicial candidates for the superior courts). As in the case of EC and MACC, the parliamentary selection committee has not been formally established.

(d) Rule-of-Law / Enforcement Reforms

Enforcement agencies often come under the influence and control of ministries through the appointment process and through funding. The proposed reforms in this area have focused on enhancing the autonomy of these agencies by reducing the influence of elected politicians. One key proposal involves separating the Attorney General's Office (AGO, which is the legal adviser for the executive body) from the Public Prosecution Office (PPO) (Promise 15, Pillar 2). This is aimed at reducing the conflict of interest involving the AGO representing the executive body and prosecuting members of the same body. There are also significant numbers of proposals to give more independence to the Malaysian Anti-Corruption Commission (MACC) (Promise 14, Pillar 2). These include changing the legal status of MACC from a government agency to a commission under the Federal Constitution which reports directly to Parliament. Another class of legal reforms involves encouraging the reporting of corruption through the revision of laws such as the Whistleblower Protection Act, the Witness Protection Act, and the Official Secrets Act.

²³ "Six select committees to be formed soon", Malaysiakini, 16 August 2018.

²⁴ "Dr M: PM decides on key appointments until parliament committees are made legal", EDGE Markets, 11 June 2019.

(e) Electoral Reforms

The electoral system determines how politicians are selected to rule a country. The goal of the PH government's electoral reforms is to improve the electoral system in such a way as to make the procedures of elections fairer (i.e. not biased in favor of certain politicians and political parties) (Promise 17, Pillar 2). This begins with a reform of the agency in charge of running elections, namely, the Elections Commission (EC). The PH's proposal is to make EC more independent by ensuring that its commission members are appointed and monitored by Parliament. Other electoral reform proposals deal with the efficiency of the system (e.g. electoral roll, postal voting) and creating a level playing field for political competition (e.g. political financing).

(f) Reforms of Oppressive Laws

Another area of institutional reform involves abolishing oppressive laws in order to enhance the media's role in providing information to the public (Promise 27, Pillar 2). These are covered by a number of proposed legal reforms to improve access to information (Freedom of Information Act) and enhance the dissemination of information (Printing Presses and Publications Act, Communications and Multimedia Act, Anti-Fake News). A number of laws enacted under the previous BN-led government were aimed at enhancing national security and public order. However, some of these are seen by the PH government to contain elements that render them "oppressive" and limits on the freedom of political participation. Laws that are expected to be either revised or revoked include the Security Offenses (Special Measures) Act 2012 (SOSMA) and the Prevention of Crime (Amendment) Act 2015 (POCA).²⁵ Reforms in this area are not easy. For example, the bill to abolish the Anti-Fake News Act was passed by the lower house (Dewan Rakyat) on 16 August 2018 but subsequently rejected by the BN-controlled upper house (Dewan Negara) on 12 September 2018.

To sum up, the PH government's institutional reforms agenda is ambitious but difficult to implement. This is not unique to Malaysia as not all countries that have attempted to carry out similar reforms have been successful (Andrews, 2013). In the case of Malaysia, this can be attributed to the lack of two-third majority in the Parliament (for constitutional amendments)

²⁵ In a BERNAMA report, the Malaysian Home Minister has indicated that more than 2,000 people have been detained under SOSMA, 475 under POCA and nine under POTA. See: <http://www.theedgemarkets.com/article/muhyiddin-more-2000-detained-under-sosma-475-under-poca-and-9-under-pota>.

and the BN's control over the upper house (Dewan Negara). Even though the BN coalition has been weakened after GE14 by defections (at the individual and party levels) and legal prosecution of leaders (e.g. Najib Razak for corruption), it remains a formidable force especially when it has cooperated with PAS.²⁶ This, together with ethnic political fragmentation, has resulted in the PH government reversing its decision to implement policies such as ratification of the International Convention on the Elimination of All Forms of Racial Discrimination (ICERD) in November 2018 and the Rome Statute of the International Criminal Court (ICC) in April 2019.

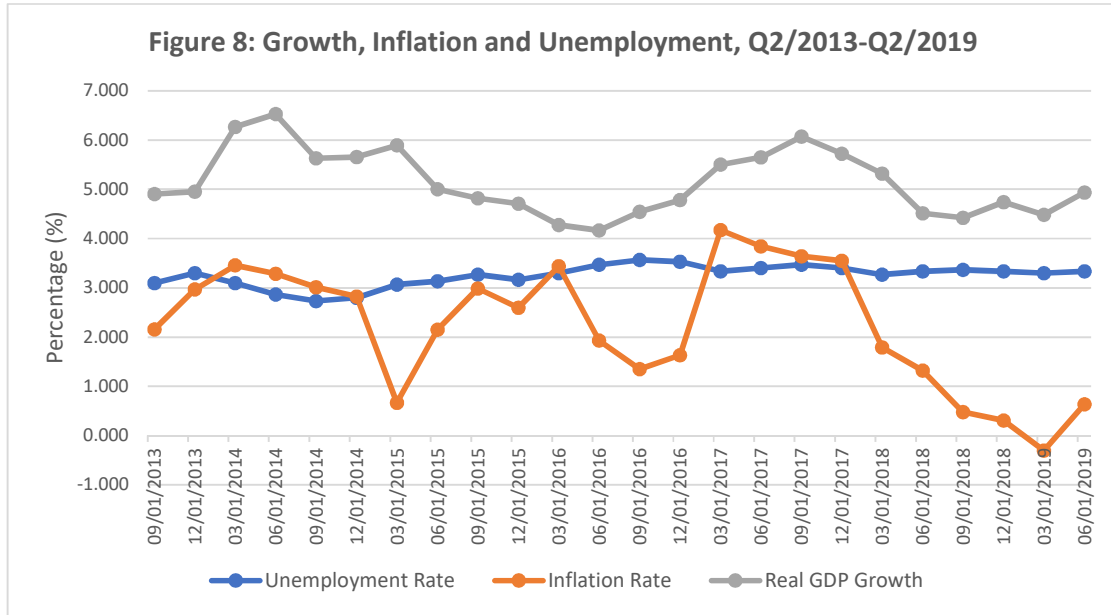
6. Overall Assessment of Reforms

The Malaysia economy has performed relatively well in the first year of the PH-rule (Q2/2018-Q2/2019) (**Figure 8**). Growth remained robust at 4.5-5.0 percent during this period whilst the official inflation rate has remained relatively low at less than one percent. The unemployment rate has remained relatively low and stable during this period. The Malaysian Ringgit has also been stable during this period (**Figure 9**). All these macroeconomic indicators suggest that the political transition has not had any negative impact on the economy. On the flip side, the robust and “business as usual” economic performance may have disappointed the heightened expectations of the voters - that the new PH-led government would bring significant improvements. This has been heightened by the announcement of the populist policies such as the abolishment of the GST, petrol subsidies and price stabilization schemes. The cash transfer payments for B40 has continued under the new government – though the name has been changed from Bantuan Rakyat 1Malaysia (BR1M) to Bantuan Sara Hidup (BSH).

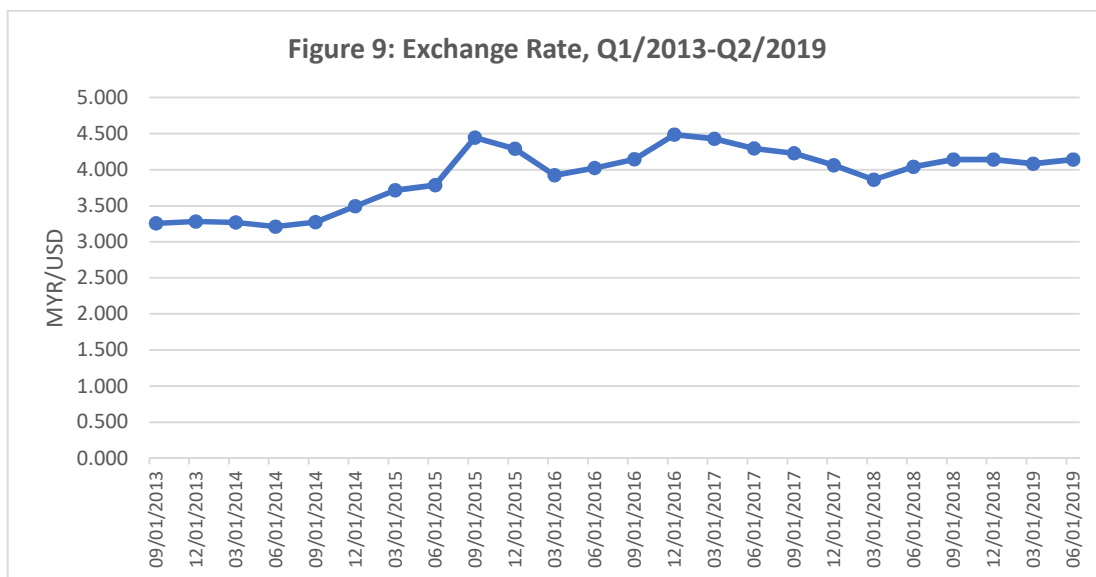
Collectively, these policies have moved the overall policy orientation of the government towards a more welfarist state. This is not necessarily bad especially if populist policies can moderate populist politics and buy time for institutional reforms. The ethnic polarization and strengthened opposition (UMNO-PAS informal alliance) are expected to heighten populist politics further. This has made it more difficult for the new government to implement institutional reforms in the country. Aside from this, there are glaring weaknesses that require further attention. The new government needs to strengthen its revenue base given the weakening of its fiscal capacity following the abolishment of the GST. This had prevented the government from abolishing the expressway tolls. In addition, more attention is needed on

²⁶ This is evidenced by the successive defeat of the PH in four successive by-elections after the GE14.

long-term development issues in areas such as education, human capital and structural transformation (premature deindustrialization and servicification). The decision by the new government not to ratify the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) also signals a need for a new growth strategy that effectively engages the country's economy globally.



Source: CEIC



Source: CEIC

7. Conclusions

The GE14 brought about a change in political regime for the first time since the country's independence. In its first year of rule, the new PH-led government sought to implement populist policies, most of which were derived from its election manifesto. These include the abolishment of the GST, price stabilization and control, and targeted petrol subsidies. The abolishment of the GST, in particular, has weakened the fiscal capacity of the government. Whilst the deferment, downsizing and cancellation of megaprojects have bought some time, the revenue base of the government will need to be strengthened if the welfarist-oriented populist policies are to be continued into the future.

The new PH-led government has also embarked on an ambitious set of institutional reforms. These will have long term effects on the economy and society. However, as the new government's experience indicate, they are extremely difficult to implement. Some of the proposed reforms require a two-thirds majority in the lower house and control of the upper house. In addition, the ethnic polarization and strengthened political opposition (UMNO-PAS informal alliance) make it more difficult to implement some of the proposed institutional reforms.

The "honeymoon" period enjoyed by the new PH-led government is likely to be a short one (2 years?) given that the Malaysian economy was not in a crisis mode prior to and during the election. The new government faces considerable challenges in formulating new growth strategies that will overcome many of the structural weaknesses of the economy. These include education, human capital, foreign labor, and trade policy. The political transition at the party level – the Mahathir-Anwar succession plan – also cast considerable uncertainties on the cohesion of the PH political coalition. This has considerable impact on the sustainability of the new government's reform programs.

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Appendix Table 1: List of Promises in Pakatan Harapan’s Election Manifesto

<p>Pillar 1: Reduce the People’s Burden</p> <ul style="list-style-type: none"> • Promise 1: Abolish GST • Promise 2: Reduce the pressures causing burdensome price increases • Promise 3: Sharing the nation’s wealth in a targeted and equitable way • Promise 4: Increase the number of affordable housing for purchase and rental • Promise 5: Reduce the burdens faced by young people • Promise 6: Abolish Tolls • Promise 7: Provide targeted petrol subsidies • Promise 8: Improving the quality and coverage of public transport • Promise 9: Improve access to and quality of health services • Promise 10: Guarantee people's basic food needs and taking care of the welfare of farmers
<p>Pillar 2: Institutional and Political Reform</p> <ul style="list-style-type: none"> • Promise 11: Restore the dignity of the Malays and Malay institutions • Promise 12: Limit the Prime Minister’s term of office and restructure the Prime Minister’s Department • Promise 13: Resolve 1MDB, FELDA, MARA and Tabung Haji mega scandals • Promise 14: Reform the Malaysian Anti-Corruption Commission (MACC) and strengthen anti-corruption efforts • Promise 15: Separating the Office of Attorney General from Public Prosecutor • Promise 16: Restore the dignity of the Parliament • Promise 17: Ensure transparency and robustness of our election system • Promise 18: Create a political financing mechanism that has integrity • Promise 19: Restore public trust in the judicial and legal institutions • Promise 20: Make the Malaysian Armed Forces and the Royal Malaysia Police a respected and an enviable force • Promise 21: Empowering the public service • Promise 22: Make the governance of our GLCs world class at par with international standards • Promise 23: Ensure government procurement produces the best value for taxpayer’s money • Promise 24: Revive the true spirit of federalism • Promise 25: Strengthen the role and powers of the local authorities • Promise 26: Make our human rights record respected by the world • Promise 27: Abolish oppressive laws • Promise 28: Support a creative young generation that are free from oppression • Promise 29: Enhance the transparency and integrity of the budget and budgeting process
<p>Pillar 3: Spur Sustainable and Equitable Economic Growth</p> <ul style="list-style-type: none"> • Promise 30: Support the economic growth of Bumiputera and all citizens in the country. • Promise 31: Spur investment and simplify business processes and trade • Promise 32: Introduce a tax system that is people-friendly and entrepreneur-friendly • Promise 33: Set up Equal Opportunity Commission • Promise 34: Enhance the income of the majority • Promise 35: Raising the dignity of workers and creating more quality jobs • Promise 36: Implementing EPF scheme for housewives • Promise 37: Ensuring the long-term prosperity of the rakyat/people

<ul style="list-style-type: none"> • Promise 38: Advancing the interests of Orang Asal in Peninsular Malaysia • Promise 39: Balancing economic growth with environmental protection 85
<p>Pillar 4: Return Sabah and Sarawak to the Status Accorded by the Malaysia Agreement 1963</p> <ul style="list-style-type: none"> • Promise 40: Implement the 1963 Malaysia Agreement • Promise 41: To ensure the prosperity of the people of Sabah and Sarawak by enhancing the states' economic growth • Promise 42: Create more employment opportunities for Sabahan and Sarawakian youth • Promise 43: Making Sabah and Sarawak a model of harmonious society • Promise 44: Improving the quality of education and healthcare services • Promise 45: Advancing the interest of the rural and remote populations • Promise 46: Protecting the sovereignty and security of Sabah • Promise 47: Decentralisation of power to Sabah and Sarawak • Promise 48: To return and guarantee the right of customary land of the people of Sabah and Sarawak
<p>Pillar 5: Create a Malaysia That is Inclusive, Moderate and Respected Globally</p> <ul style="list-style-type: none"> • Promise 49: Making government schools the best choice for its people • Promise 50: Restore the authority and independence of public universities and institutes of higher learning • Promise 51: Advance the interests of the disabled • Promise 52: Fight crime and social ills • Promise 53: Promote the integrity of family institution and neighbourliness • Promise 54: Empowering societal institutions, civil society and social entrepreneurship • Promise 55: To increase the space for and diversify the activities of young people • Promise 56: Establishing a Consultative Council for People's Harmony • Promise 57: Malaysia must be known for its integrity, not corruption • Promise 58: Defend and protect the country's borders from external invasion, trafficking and smuggling • Promise 59: To lead efforts to resolve the Rohingya and Palestine crises • Promise 60: To Promote Malaysia's role in international institutions
<p>Special Commitments</p> <ul style="list-style-type: none"> • FELDA Settlers • Indian Community • Women • Youths • Senior Citizens

Source: Pakatan Harapan, Buku Harapan, 2018

Appendix Table2: Pakatan Harapan Government’s Institutional Reform Agenda

Institution	Reforms
Executive (Administration)	<ul style="list-style-type: none"> • Collective cabinet administration system • Prime Minister will not hold other ministerial posts • Lower number of ministers in PM Dept from 10 to 3 • Lower financial allocation to PM Dept from RM17 bil (2018) to RM8 bil (2019) • Reduce number of agencies under PM Dept • Elected politicians and senior government officials to declare assets and income • 2-year term limit for PM, Chief Minister and Menteri Besar • Remove PM’s ability to influence and manipulate key institutions • Publication of directorship and consultancy positions held by MPs • Commissions of Inquiry into 1MDB, FELDA, MARA, Tabung Haji • Reform governance structure for 1MDB, FELDA, MARA, Tabung Haji • Limit the use of private consultants in public sector • Parliamentary committee to receive MOF reports on GLCs regularly • Reform and redesign public services • Production of Green and White papers for policy discussions
Fiscal Capacity	<ul style="list-style-type: none"> • Improve transparency and discipline of government’s financial administration • Adopt accrual accounting • Enact a Fiscal Responsibility Act by 2021 • Fiscal consolidation during 2019-2021 period • Setup a Debt Management Office to review and manage the government’s debt and liabilities • Re-evaluation and rationalisation of infrastructure major projects • Zero-rating of Goods and Services Tax (GST) and implementation of Sales and Services Tax (SST) • Review tax structure with the view to increase tax revenues e.g. gaming industry and property gains • Reform public procurement system and promote open tendering • Enact a new Government Procurement Act in 2019 • Reform Public-Private Partnership Unit to achieve greater transparency and eliminate corruption • More extensive use of IT and online (cashless) systems in procurement
Legislature (Parliament)	<ul style="list-style-type: none"> • Speaker of lower house and president of upper house must retire from partisan politics • Leader of opposition to have minister status • Transparent funding to MPs • Establish select committee system • Chairmanship of PAC to be held by opposition • Reintroduce the Parliamentary Services Act to make parliament more independent • Parliamentary committees to approve appointments to key commissions e.g. MACC, Elections Commission, Judicial Appointment Commission, National Audit Department, Human Rights Commission
Judiciary (Courts)	<ul style="list-style-type: none"> • Parliamentary Select Committee to determine membership of Judicial Appointments Commission • Abolish clauses that prevent court from reviewing government’s decisions and laws

	<ul style="list-style-type: none"> • Introduce new rules that require judges to provide written judgements when their judgments are announced
Enforcement	<ul style="list-style-type: none"> • Separate the Attorney General Office from Public Prosecution Office • Upgrade MACC to a Commission under Federal Constitution • Greater independence for MACC (appointment, tenure, finance) • MACC to be answerable to Parliament directly • Establish Independent Police Complaints and Misconduct Commission • Revise Whistleblower Protection Act 2010 • Revise Witness Protection Act 2009 • Revise Official Secrets Act 1972
Electoral	<ul style="list-style-type: none"> • Improvements in electoral process – electoral roll, postal voting, campaign period, fair access to media, and independent observers • Election Commission to be fully monitored by Parliament • Membership of EC requires Parliamentary approval • Fair ratio in future delimitation exercises • Enact the Political Financing Control Act • Lower voting age from 21 years to 18 years
Federalism	<ul style="list-style-type: none"> • States to have higher number of Senate appointments than Federal government • Further decentralize powers to state e.g. public transport, social services, environmental protection, agriculture • Return at least 10% of income tax revenues generated in a state to that state • Ring-fence 50% of development expenditure to five poorest states • Powers of the Malay Rulers to govern religion and Malay Customs will be returned to the states
Local Government	<ul style="list-style-type: none"> • Amend Local Government Act 1976 to make local government more accountable
Media & Information	<ul style="list-style-type: none"> • Enact Freedom of Information Act • Revoke Sedition Act 1948, , Printing Presses and Publications Act 1984 • Abolish Anti-Fake News Act 2018 • Revise Communications and Multimedia Act 1998 • Improve independence of RTM and BERNAMA • Enable an open government environment
National Security, Public Order and Political Participation	<ul style="list-style-type: none"> • Revise Universities and University Colleges Act 1971 (UCCA) • Revise Peaceful Assembly Act 2012 • Revise Security Offences (Special Measures) Act 2012 (SOSMA) • Revise National Security Council Act 2016 • Revise Prevention of Crime (Amendment) Act 2015 (POCA) • Revise Prevention of Terrorism Act (POTA)

Source: Lee (2019)