

BTI 2014 | Malaysia Country Report

	scale	score	rank	trend
Status Index	1-10	6.35	# 43 of 129	
Political Transformation	1-10	5.23	# 71 of 129	➔
Economic Transformation	1-10	7.46	# 22 of 129	➔
Management Index	1-10	5.65	# 43 of 129	

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2014. It covers the period from 31 January 2011 to 31 January 2013. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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Key Indicators

Population	M	29.2	HDI	0.769	GDP p.c.	\$	17142.6
Pop. growth ¹	% p.a.	1.7	HDI rank of 187	64	Gini Index		46.2
Life expectancy	years	74.7	UN Education Index	0.731	Poverty ³	%	2.3
Urban population	%	73.4	Gender inequality ²	0.256	Aid per capita	\$	0.7

Sources: The World Bank, World Development Indicators 2013 | UNDP, Human Development Report 2013. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$2 a day.

Executive Summary

From 2011 to 2013, Malaysia experienced solid macroeconomic development, with foreign direct investment (FDI) flows reaching a record level in 2012. However, political reforms oriented toward liberal democracy remained stalled, with most current policies geared toward general elections to be held in 2013. In his national day speech in 2011, Prime Minister Najib Tun Razak promised to expand civil liberties and implement democratic reforms. According to him, the changes were designed to accommodate and realize a modern and functioning democracy, necessary to maintain racial harmony. Subsequently, the Internal Security Act (ISA) was repealed, the Peaceful Assembly Act 2012 implemented and the abolishment of the Sedition Act announced. However, these reforms have to be considered as pure “window dressing.” The Peaceful Assembly Act 2012 is regarded by observers as more restrictive than the regulations it replaces, and contravenes international human rights standards. The ISA was replaced with the Security Offences (Special Measures) 2012 Act (SOSMA), which added new limits to previously unrestricted activities, while broadening police arrest and surveillance powers in new and innovative ways. The government’s authoritarian tendencies were evident on several occasions during the period under review. In July 2011, police forces cracked down on a demonstration (the Bersih 2.0 rally) organized by the Coalition for Clean and Fair Elections (Bersih) in Kuala Lumpur. More than 1,600 people were temporarily arrested, and police forces fired tear gas and water cannons at the 20,000 protesters. Ten months later, police forces again cracked down on a demonstration organized by Bersih (Bersih 3.0 rally), this time arresting more than 500 people. With general elections to be held in 2013, the government rejected demands for effective electoral reforms. For instance, the problem of “phantom voters,” or voters registered in apartment blocks in closely contested constituencies, continues to undermine the electoral process, raising doubts with regard to the government’s commitment to accept free and fair elections. Malaysia’s economic transformation from 2011 to 2013 showed more positive signs than did its political development. The government achieved several of its aims as formulated under the New Economic Model (NEM). The goals of the NEM are to allow Malaysia to double its per capita income from

the present \$7,000 to \$15,000 by 2020, while becoming more competitive, market-driven and investor-friendly. Much of this growth is expected to come from the private sector. Consequently, Malaysia's economy remained resilient during the period under review, mainly because of a rapid expansion of domestic demand. The overall GDP growth rate for 2012 was 5.1%, with 2013 growth forecast by the government to be 5.6%. GDP per capita (on a purchasing power parity basis) increased in 2011 to \$15,600, a level higher than before the global financial crisis. The inflation rate (based on average consumer prices) eased significantly, reaching a two-year low of 1.2% in December 2012, one of the lowest rates in the region. The level of investor confidence in Malaysia was reflected in the surge of FDI inflows. In 2011, FDI increased by 12.3% compared to 2010. However, the structural fiscal deficit remains high, and threatens to undermine the country's growth. The country's current model, which relies on using oil-related revenue to sustain a large budget deficit and fund widespread subsidies, social transfers and grand infrastructure projects, is vulnerable to external economic shocks.

History and Characteristics of Transformation

The federation of Malaysia was established in 1963, combining the territories of Malaya, Singapore, Sabah and Sarawak. Two years later, in 1965, Singapore was expelled from the federation. Today, Malaysia consists of 13 states and three federal territories. It is a constitutional monarchy based on the British Westminster model, a legacy of British colonialism. At the federal level, there is a bicameral legislature. The House of Representatives (the lower house) is composed of members elected every five years in a first-past-the-post election from single-member constituencies. The Senate (upper house) consists of 70 members, 26 of which are indirectly elected by the states, while the other 44 are appointed by the king. Executive power lies with the prime minister and the cabinet. Each of the 13 states has its own legislature.

Politically and officially, the country's population is divided into two categories: Bumiputera and non-Bumiputera. The Bumiputera group is made up of Malays and other indigenous peoples, while the non-Bumiputera group consists mainly of Chinese and Indians. This divide is evident in every facet of Malaysian life, from politics to food to university admissions.

Most of the Chinese and Indians originally came to Malaysia during colonial times, when the British actively recruited them to open up the economy. After independence, the British left political power largely in the hands of the indigenous Malays. The Malay leaders then forged a political alliance with the major Chinese and Indian parties. This set a pattern in which the office of the prime minister was to be occupied by a Malay from the United Malays National Organization (UMNO). The current president of UMNO, Najib Tun Razak, is Malaysia's sixth prime minister. He is the eldest son of Abdul Razak, who was the second prime minister of Malaysia. However, the alliance system collapsed in May 1969 when emergency rule was declared and the constitution suspended after race riots broke out between the Malays and the Chinese in the wake of a bitterly fought election. Once the constitution was reinstated in 1971, new

legislation was passed ensuring Malay political supremacy, which in turn allowed the UMNO to enhance its powers and aggressively promote its main supporters, the Malay population. A New Economic Policy (NEP) was promulgated, providing extensive benefits to the Bumiputera (i.e., Malay) community through quotas, bank loans, scholarships, special licenses and so on. The government justified the affirmative action character of the NEP, claiming that the wide economic gap between the Malay and the non-Malay (i.e., Chinese) threatened racial harmony and had prompted the May 1969 riots. Although the NEP discriminated against the non-Bumiputera, the UMNO-led government was careful to allow a free market economy to develop. The government gave the non-Bumiputera a free hand in the economy, as long as quotas and shares were allocated to Malays. This strategy, which emphasized growth with ethnic distribution through significant foreign direct investment in the 1970s and 1980s, was so successful that Malaysia became one of the “Asian Tiger” economies.

Although the NEP officially ended in 1991, economic policies since that time have changed little in character. They continue to include special rights for the Bumiputera, while at the same time promote rapid economic growth to ensure that all ethnic groups receive their share of the economic pie.

The government has been headed by the UMNO since independence, while the ruling coalition, the Barisan Nasional (BN), has won every general election. Before 2008, the BN regularly achieved more than a two-thirds majority in parliament, allowing it to amend the constitution at will and giving the executive the leeway to pursue policies without significant opposition. Having successfully managed the economy, the government has been able to proclaim that, by 2020, Malaysia will be a fully developed and industrialized country. Today, Malaysia is generally regarded as a success story among developing countries in the sense of maintaining a stable and growing economy. However, the polity has become significantly unstable in the past years, mainly due to increasing ethno-religious conflicts.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The Malaysian state is strong and faces virtually no challenges to its monopoly on the use of force throughout the country. During the period under review, Malaysia's territorial dispute with China, the Philippines, Brunei, Vietnam and Taiwan in the South China Sea intensified. Malaysia claims 12 features in the Spratly Islands where vast reserves of natural resources are suspected. As of the time of writing, Malaysia was occupying six of these features. To reinforce and defend its claims, Malaysia maintains a military presence on the Ardasier Reef, the Mariveles Reef, the Swallow Reef and Investigator Shoal. Two claimed features, Amboyna Cay and Barque Canada Reef, are currently occupied by Vietnam and one claimed feature, Commodore Reef, is occupied by the Philippines. In July 2011, Malaysia, together with the other Southeast Asian countries, agreed with China to a preliminary set of guidelines in the dispute. In August 2012, Malaysia and China bilaterally agreed that any territorial dispute or conflict in the South China Sea should be resolved peacefully via discussions. In addition, territorial conflicts with Thailand in the southern area of the Gulf of Siam remain active. Malaysia's territorial dispute with the Philippines over the northern part of Sabah on the island of Borneo is unresolved. The Philippines' claim to the territory stems from the sultan of Brunei's act ceding Sabah to the sultanate of Sulu in the 17th century. The Sulu lands now belong to the Philippines. In 1798, the territory was leased to the British North Borneo Company and brought under direct British control in 1946. Malaysia contends that the territory was purchased by the British North Borneo Company and is therefore a part of Malaysia. The final border with Indonesia on the island of Borneo is still unresolved. These conflicts, however, did not interfere with state affairs during the review period.

All Malaysian citizens accept the nation-state as legitimate, and all individuals and groups enjoy the right to acquire full citizenship rights without discrimination. However, the Malay majority population and the Islam religion shape the character of the Malaysian state. Ethnic Malays dominate the country's key political

Question
Score

Monopoly on the
use of force

10

State identity

9

institutions, such as the parliament, the bureaucracy and the armed forces. The head of state, the Yang di-Pertuan Agong, is also a distinguished Malay institution. This Malay predominance draws criticism from Indians and Chinese, who make up about 30% of the population and report feeling like second-class citizens. In addition, indigenous groups in Sabah and Sarawak have repeatedly voiced discontent with Malay dominance. In a survey released by the Merdeka Center in June 2011, data indicated that only 39% of the respondents primarily identify themselves as Malaysian. Similarly, 41% primarily identify themselves as a follower of a religion. Almost half of the respondents (44%) felt that ethnic unity in the country was superficial. This feeling was very common among young Chinese participants. Nine percent of respondents said that ethnic relations have worsened in the country as compared to 2006.

The Malaysian Constitution defines the state as a secular order. However, Islam has considerable influence on the Malaysian legal system and the country's political institutions. Although Malaysian law is mainly based on the common law legal system, state Shari'ah courts operate alongside civil courts in civil matters. Though the Shari'ah courts have jurisdiction only over matters involving Muslims, they remain highly influential in general, because their decisions frequently affect non-Muslims on matters such as child custody, for example. In March 2011, a Christian lawyer failed in her attempt to be allowed to practice in the Shari'ah courts. During the period under review, several court decisions were the source of considerable controversy. On 11 October 2012, a high court rejected a request to declare unconstitutional a Shari'ah law that prohibits "wearing women's attire" or "posing as a woman" in Negeri Sembilan. The suit was filed by four Muslim transgender women who had been arrested under the law. The court justified its ruling by noting that the complainants were Muslim and had been born male. In addition, the Selangor and Kuala Lumpur state religious departments detained 88 Muslims suspected of khalwat (close proximity to a member of the opposite sex) in February 2011. Furthermore, Islam also plays an important role in the political institutions. The government continues to present itself as the preserver of Malay and Muslim rights. The opposition parties disagree with regard to the application of hudud laws (a branch of fixed punishment under Shari'ah law), a difference they say they would implement should they take over the federal administration.

The Malaysian state has a differentiated administrative structure throughout the country, providing all basic public services. The highly trained and professional administration, which is dominated by ethnic Malays, implements the policies of the elected government. The state is able to fulfill its proper jurisdictional function and enforce the law throughout the country. The country's transport network is diverse and developed, with a particularly extensive road network. Malaysia has six international airports. Improving the rural basic infrastructure and the urban public transport were two of the National Key Results Areas (NKRAs) for the government

No interference of religious dogmas

6

Basic administration

9

during the period under review. However, infrastructure in the states of Sabah and Sarawak remains underdeveloped compared to peninsular Malaysia. Although 100% of the population has access to a water source, only 96% has access to sanitation, mainly due to a significantly lower share in Sabah and Sarawak. In addition, numerous rural communities in Sabah and Sarawak are still without electricity services.

2 | Political Participation

Malaysia has established universal suffrage and regularly holds general elections. Opposition parties are able to run in the country's elections and political posts are generally filled according to the electoral outcome. Despite this fact, elections cannot be considered free and fair. The ruling coalition, the Barisan Nasional (BN), frequently uses repressive laws to restrict the opposition and control the media. Cases of gerrymandering, the use of government resources to ensure consistent victories, and electoral fraud such as the manipulation of voter registration lists reflect an undemocratic strain within the BN government. These undemocratic attitudes were clearly displayed in the Sarawak state elections in April 2011. Opposition parties accused the ruling BN of vote-buying in constituencies such as Bukit Assek and Bawang Assan. In addition, NGOs criticized the allocation of postal voters to certain constituencies. A BN member party retained the seat in Senadin thanks to more than 1,000 postal votes, resulting in a majority of just 58 votes over the oppositional Democratic Action Party (DAP). The Election Commission's inactivity with respect to these forms of electoral fraud led to several large demonstrations organized by the Coalition for Clean and Fair Elections (Bersih) in the capital Kuala Lumpur during the period under review. In early April 2012, a Parliamentary Select Committee (PSC) on Electoral Reforms released a report containing 22 recommendations for improving the electoral system. The House of Representatives (Dewan Rakyat) passed the report without debate on April 3. However, opposition groups rejected the report. In July 2012, the government announced that overseas voting would be implemented in the next general elections (which were held in June 2013). Overseas voters have asked the Election Commission to ensure the integrity of their ballots. During the period under review, opposition accused the government of granting citizenship to illegal immigrants in the state of Sabah. In August 2012, a royal commission of inquiry on illegal immigrants in Sabah was formed to investigate the problem.

Despite being elected in unfair elections, rulers in principle have the effective power to govern as far as potential veto-holders such as the military, the clergy, landowners, business elites or external actors are concerned. Nonetheless, the importance of ethnic and religious politics in Malaysia makes it difficult for elected political representatives to implement profound policy changes. Racist groups such as

Free and fair elections

5

Effective power to govern

2

Perkasa, an organization formed by Ibrahim Ali in the aftermath of the 2008 general elections, put constant pressure on the federal government to maintain the special rights of the Malay population and to strengthen Malay supremacy throughout the country.

Association and assembly rights are severely limited. In December 2011, the government passed the Peaceful Assembly Act 2012. The act replaced Section 27 of the Police Act, which means police permits for mass assemblies will no longer be required. Instead, organizers must notify the officer in charge of the police district, who outlines restrictions and conditions, at least 10 days before the gathering date. Organizers must be at least 21 of age and participants under the age of 15 are not allowed in an assembly. Neither the Human Rights Commission of Malaysia (SUHAKAM) nor civil society groups were meaningfully consulted in the drafting of the bill. A group of independent U.N. human rights experts warned that the bill gives wide-ranging authority and power to law enforcement officials. Furthermore, the act is seen as more restrictive than preexisting regulations, and contravenes international human rights standards. During the period under review, hundreds of individuals were arrested while seeking to exercise their assembly rights. In July 2011, police forces cracked down on a demonstration (Bersih 2.0 rally) organized by the Coalition for Clean and Fair Elections (Bersih) in Kuala Lumpur. More than 1,600 people were arrested, and police forces fired tear gas and water cannons at the 20,000 protesters. Ten months later, police forces again cracked down on a demonstration organized by Bersih (Bersih 3.0 rally), this time arresting more than 500 people. Between 80,000 and 100,000 people gathered in the city center of Kuala Lumpur for the event. Federal laws such as the Societies Act ensure that organizations critical of the government can be banned or refused registration. Malaysian trade unions are strictly controlled according to the Trade Unions Act and the Industrial Relations Act.

Association /
assembly rights
4

The freedom of expression is severely limited in Malaysia. Public debate is vulnerable to distortion and manipulation through government intervention. Laws such as the Official Secrets Act (OSA) and the Sedition Act restrict the freedoms of information and speech. All mainstream media are indirectly controlled by the government through companies such as Media Prima Berhad or Utusan Melayu Berhad. Although two opposition-led state governments, Selangor and Penang, passed freedom of information acts in April and November 2011, no such act exists on the federal level. During the period under review, serious limitations on the freedoms of expression and of the press were evident. In April 2011, UMNO-owned newspaper Utusan Malaysia suspended journalist Hata Wahari, who had accused the newspaper of failing to provide the public with objective news coverage. In December 2012 and January 2013, Utusan Malaysia lost two defamation lawsuits against opposition leaders Karpal Singh and Anwar Ibrahim. On 4 July 2012, blogger Syed Abdullah Hussein Al-Attas was arrested under the Official Secrets Act for criticizing the sultan of Johor. The same month, the Kuala Lumpur High Court ruled

Freedom of
expression
5

that the September 2010 arrest of cartoonist Zulkiflee Anwar Haque, a critic of the government, was lawful under the Sedition Act. The Press Freedom Index 2011 – 2012, published by Reporters Without Borders, ranked Malaysia at 122nd place, up from 141st place in 2010. In a landmark ruling in October 2012, the Kuala Lumpur High Court rejected the government’s decision not to grant political news website Malaysiakini a publishing permit. The website is known for content often highly critical of the government. The same month, the government announced that the Sedition Act would be replaced by the National Harmony Act in 2013.

3 | Rule of Law

The constitution provides a structure for the separation of powers in Malaysia. However, the executive has an ongoing monopoly on power, and frequently influences the two other branches of government. Nevertheless, several high-profile judicial review cases indicated that the government’s influence on the judiciary decreased during the period under review. On 9 January 2012, opposition leader Anwar Ibrahim was acquitted by the Kuala Lumpur High Court of sodomizing his 23-year-old former aide, Mohd Saiful Bukhari Azlan. Six months later, the court rejected the government’s decision to declare the opposition group Coalition for Clean and Fair Elections (Bersih) unlawful. In addition, Arifin Zakaria was appointed as new chief justice of the federal court in September 2011. His nomination was welcomed by the Malaysian Bar Council. In a speech in November 2011, the new chief justice urged the government to maintain a clear separation of powers between the judiciary and the executive in order to uphold the rule of law.

Separation of powers

5

The judiciary is institutionally differentiated and has the ability to interpret and review existing laws, legislation and policies. Channels of appeal are in place, and the court administration functions reasonably well. Though judicial decisions and doctrines are not free from the influence of political decision makers, several court decisions during the period under review indicated that the influence of the prime minister’s office was decreasing. After a two-year trial, opposition leader Anwar Ibrahim was acquitted of sodomy charges in January 2012. In December 2011 and June 2012, the Penang High Court ordered UMNO-owned newspaper Utusan Malaysia to pay damages to Penang’s Chief Minister Guan Eng, a member of the oppositional Democratic Action Party (DAP), for publishing defamatory articles about him. On 21 January 2013, the Kuala Lumpur High Court ruled in favor of opposition leader Anwar Ibrahim in his defamation suit against Utusan Malaysia. One week earlier, Chief Justice Arifin Zakaria reaffirmed the judiciary’s commitment to upholding its independence.

Independent judiciary

5

Officeholders who break the law and engage in corrupt activities are both prosecuted under established laws and are the subject of adverse publicity, but often slip through political, legal or procedural loopholes. Though the Malaysian Anti-Corruption

Prosecution of office abuse

6

Commission (MACC) is criticized of being inactive with regard to the prosecution of BN officeholders, several corruption cases were exposed during the period under review. In October 2011, the Auditor-General's Report 2010 revealed that the government-linked National Feedlot Corporation (a project initiated by the government under the Ninth Malaysia Plan with the aim of developing the local cattle industry) was given a soft loan of MYR 250 million and 5,000 acres of land in Gemas, but failed to meet its goal of meeting 40% of the country's demand for beef. The corporation's chairman was the husband of then-Minister of Women, Family and Community Development Shahrizat Abdul Jalil. On 11 March 2012, her husband was charged with using government funds to buy apartments and pay for overseas trips. The same day, Sharizat Abdul Jalil announced that she would step down from her ministerial post. The project was approved in 2008 by the chairman of the High Impact Investment Project Committee, Najib Tun Razak, who is now the prime minister. In June 2012, the MACC opened an investigation of a government-owned public transport company (Syarikat Prasarana Negara Berhad) over the award of a contract for the Ampang Light Rail Transit (LRT) extension project. The opposition accused Prime Minister Najib of intervening in the contract award process. The same month, the government denied allegations of corruption in its \$1.25 billion purchase of two Scorpene submarines, produced by French shipbuilder DCN, in 2002. In September 2012, Amnesty International called on the Malaysian authorities to end all forms of harassment and intimidation targeted at Suara Rakyat Malaysia (Suaram), a human rights group that had successfully petitioned for a French judicial review in the Scorpene case. Corruption allegations against the government parties emerged at the end of 2012 when investigation papers submitted to the attorney general by the MACC showed that a sum of MYR 40 million, discovered being smuggled into Malaysia from Hong Kong by a Sabah businessman, was intended as a political contribution to the state Umno. These high-profile corruption cases have raised questions as to the government's commitment to tackling corruption effectively.

Civil rights are constitutionally guaranteed but are nevertheless occasionally violated under the Malaysian state. Mechanisms and institutions to prosecute, punish and redress violations of civil rights are partly in place, but often prove to be ineffective. The Malaysian authorities' attitude toward civil liberties remains ambivalent, with recent implemented reforms having something of the character of window dressing. In April 2012, the government replaced the Internal Security Act (ISA), which had allowed the state to keep people perpetually incarcerated by enabling detention orders to be renewed every two years, with the Security Offences (Special Measures) 2012 Act (SOSMA). Under the SOSMA, police can detain individuals for only 28 days (compared to 60 under the ISA), and the home minister lost the power to place individuals under detention without trial for two years. However, opposition groups, the Malaysian Bar Council and international human rights watchdogs criticized the reform as insufficient. With the possibility of detaining suspects for 28 days without judicial oversight and the definition of who may be arrested remaining very broad,

Civil rights

6

the SOMSA fails to protect citizens' basic constitutional rights adequately. Furthermore, the bill added limits to previously unrestricted activities, and broadened police arrest and surveillance powers in new and innovative ways. As of the time of writing, approximately 45 suspects were still being held under the provisions of the ISA. On 9 April 2012, the government tabled amendments to the Universities and University Colleges Act (UUCA) to allow university students to engage in political activities. However, students who hold positions in political parties will be barred from campus elections, among other new restrictions. On two occasions during the period under review, police forces came under heavy criticism. In July 2011, police forces cracked down on a demonstration (Bersih 2.0 rally) organized by the Coalition for Clean and Fair Elections (Bersih) in Kuala Lumpur. More than 1,600 people were arrested, and police forces fired tear gas and water cannons at the 20,000 protesters. Ten months later, police forces again cracked down on a Bersih demonstration (Bersih 3.0 rally), and arresting more than 500 people. Between 80,000 and 100,000 people gathered in the city center of Kuala Lumpur for that event. Federal laws such as the Official Secrets Act (OSA), which automatically classifies all government documents as secret, and the Sedition Act, which criminalizes speech with seditious tendency without specifying the definition of seditious, provide the government with broad legal cover to take action against its critics, thereby leading to violations of civil rights on a massive scale. On 11 July 2012, the government announced it would repeal the Sedition Act and replace it with the National Harmony Act. Details of the new legislation were not provided, however. The civil rights of followers of nonmainstream religious groups remain unprotected. Shi'ites and other groups viewed by the Muslim mainstream as heretic cannot count on the state to guarantee their basic rights as citizens.

4 | Stability of Democratic Institutions

Although Malaysia's system of checks and balances is weak, its key institutions are stable. The executive's dominant position negatively affects the country's horizontal and vertical separation of powers. The prime minister and the cabinet make all key political decisions, with the parliament clearly subordinated to these institutions. The intensity of parliamentary debate has increased since the last general elections, but opposition parliamentarians' rights are frequently violated. The judiciary too is subject to interference by the executive.

At present, the Barisan National (BN) government is not committed to democratic institutions. During the period under review, the United Malays National Organization (UMNO)-dominated government revised or abolished repressive laws such as the ISA. However, these laws were replaced by regulations that are to some extent even more restrictive. The government's reform agenda must be seen as paying only lip service with regard to the establishment of democratic institutions. The

Performance of
democratic
institutions
3

Commitment to
democratic
institutions
2

government's commitment to democracy and democratic institutions thus remains dubious. Moreover, the current Malaysian government makes no secret of the fact that it considers liberal democracy to be unsuitable for Malaysia because of its multiracial and multiconfessional population.

5 | Political and Social Integration

The Malaysian party system is fundamentally established and rooted in society. Two major blocs, the Barisan Nasional (BN) and Pakatan Rakyat, compete for votes. The ruling coalition, the BN, is comprised of 13 parties, each of which represents an ethnic group or a region. Historically, the Malaysian Chinese Association (MCA) and the Malaysian Indian Congress (MIC), along with the largest party, the United Malays United Organization (UMNO), have formed the backbone of the BN. After losing votes in the last general election, the MIC and especially the MCA have been unable to regain the support of their respective ethnic groups. Despite harsh attacks against the opposition parties in their general assembly in October 2012, MCA politicians failed to demonstrate how they could preserve the interests of the Chinese population by remaining within the government coalition. The attacks only deepened polarization between the two major blocs. Opposition parties are similarly divided along ethnic lines and are therefore influenced by ethnic and religious divisions. After the last general election in March 2008, Parti Keadilan Rakyat (PKR), the secular Democratic Action Party (DAP) and the Islamist Parti Islam Malaysia (PAS) formed a political coalition called Pakatan Rakyat (PR). The Sarawak National Party (SNAP), which joined the PR in April 2010, left the coalition on 6 May 2011. Factions of the PAS that favored the idea of opening talks with UMNO over a possible Malay-Muslim unity government became increasingly isolated during the period under review. However, frictions within the opposition coalition emerged in November 2012, largely over the question of who should be prime minister if PR wins in the upcoming polls.

Party system

7

There is a range of interest groups in Malaysia, but important social interests such as indigenous groups are underrepresented. In addition, particular strong interests dominate, and there is a risk of polarization. The spectrum of interest groups ranges from social movements, such as vocal environment groups and community organizations providing assistance to the poor at a local level, to professional associations such as the Malaysian Bar Council. However, civic groups can act only within the narrow limits set by the Malaysian authorities. In practice this means they cannot broach issues of race or religion, and cannot criticize the government. Though most civic groups promote the ideals of a multiracial and open society, they are strongly organized along ethnic and religious lines. On 26 January 2013, the government lifted its four-year ban against Hindu non-governmental organization (NGO) Hindraf (Hindu Rights Action Force). During the period under review,

Interest groups

5

environmental groups who protested against rare earth mining company Lynas in Pahang and the opposition group Bersih were the most prolific and active organizations. Environmental groups in particular successfully intensified their efforts to raise awareness for environmental concerns among the Malaysian population. In November 2012, environmental group Himpunan Hijau organized a so-called Green Walk, a 14-day cross-country march held as a protest against the Lynas Advanced Materials Plant (LAMP) in Gebeng, a rare-earth mining factory. In addition, protests against the government's long-term plans to build 12 massive hydroelectric dams on the island of Borneo intensified. On 27 September 2012, at least 200 people blocked the access road to the Murum dam in Sarawak. Historically, employers' associations and trade unions such as the Malaysian Trade Union Congress (MTUC) umbrella organization have no political weight.

Malaysians have an ambivalent relation to democratic norms. According to data provided by the Asian Barometer Survey, 86.9% of Malaysians express a desire for democracy, and 81.1% of Malaysians believe that democracy is the most suitable form of government for the country. In addition, 58.8% of Malaysians feel no attachment to any form of authoritarian rule. However, less than half of Malaysians surveyed support the rule of law, judicial independence or a system of checks and balances. Furthermore, the majority of Malaysians are attached to procedures associated with authoritarian governance. According to the survey, 84.3% of Malaysians feel that the relationship between the government and people is similar to that between a parent and a child. In addition, more than 80% of the people support the system of government in Malaysia. Only 30% of the participants believe that the political system should be replaced by another system.

Approval of
democracy
n/a

There is a fairly low level of communal trust within the Malaysian population. Social and cultural barriers divide the major ethnic and religious groups. Although the number of autonomous, self-organized groups, associations and organizations continued to grow during the period under review, 68.4% of Malaysians lack membership in any form of societal association, according to data provided by the Asian Barometer Survey. In addition, the data show that involvement in associations largely fails to foster trust in fellow citizens in Malaysia. Data provided by the Merdeka Center show that many Malaysians feel that ethnic unity in the country is superficial (44%). Accordingly, stores of social capital are notably low in Malaysian society.

Social capital
5

II. Economic Transformation

6 | Level of Socioeconomic Development

Question
Score

Socioeconomic
barriers
7

Poverty and inequality are limited and only marginally structurally ingrained in Malaysia. The country's level of development permits freedom of choice for all citizens. Key indicators show a high level of human development according to UNDP reports. The country's score in the 2011 UNDP's Human Development Index was 0.761. The score was above the average of 0.741 for countries in the high human development group and above the average of 0.671 for countries in East Asia and the Pacific. Malaysia was ranked 61st overall. Between 1980 and 2011, Malaysia's HDI value increased from 0.559 to 0.761, an increase of 36.0%, or an average annual increase of about 1.0%. Life expectancy at birth was 74.2 years. According to World Bank data from 2009, 2.3% of Malaysians lived below the poverty threshold of \$2 per day. Although the government's New Economic Model (NEM) explicitly aims at reducing disparities of wealth between the poorest and richest segments of the population, the gap between the rich and the poor did not decrease during the period under review. With a Gini Index value of 46.2, Malaysia retained Asia's second-highest gap between the rich and poor. With regard to inequality between the genders, Malaysia performed better. In 2011, the country had a Gender Inequality Index value of 0.286, earning a rank of 43rd out of 146 countries. However, only 14% of parliamentary seats are held by women. In addition, the female labor-market participation rate is 44.4%, as compared to 79.2% for men, according to UNDP data for 2011. The female literacy rate is 94.6%, slightly higher than the male rate of 90.3%. Income disparities and development imbalances among the country's various regions were not reduced during the period under review. The World Bank estimated that 40% of the population of the state of Sabah was living under the national poverty threshold. Poverty is particularly widespread in the rural parts of the state. In sum, problems associated with poverty and rural development remain in Malaysia.

Economic indicators		2009	2010	2011	2012
GDP	\$ M	202251.4	246822.6	287934.4	303526.2
GDP growth	%	-1.5	7.2	5.1	5.6
Inflation (CPI)	%	0.6	1.7	3.2	1.7
Unemployment	%	3.7	3.4	-	-

Economic indicators		2009	2010	2011	2012
Foreign direct investment	% of GDP	0.1	3.7	4.2	-
Export growth	%	-10.9	11.3	4.2	0.1
Import growth	%	-12.7	15.6	6.2	4.5
Current account balance	\$ M	31801.0	26998.1	33508.3	18637.9
Public debt	% of GDP	52.8	53.7	54.5	55.5
External debt	\$ M	69784.3	85126.5	94467.9	-
Total debt service	\$ M	12125.7	13359.8	10856.4	-
Cash surplus or deficit	% of GDP	-6.1	-5.2	-4.8	-4.5
Tax revenue	% of GDP	14.9	13.8	15.3	16.2
Government consumption	% of GDP	13.0	12.2	13.0	13.5
Public expnd. on edu.	% of GDP	6.0	5.1	-	-
Public expnd. on health	% of GDP	2.6	2.4	1.6	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	2.0	1.6	1.7	1.5

Sources: The World Bank, World Development Indicators 2013 | International Monetary Fund (IMF), World Economic Outlook 2013 | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database 2013.

7 | Organization of the Market and Competition

Market competition has a strong institutional framework in Malaysia, but the rules for market competition are not always uniform for all market participants. The informal sector is small. However, administered prices play an important role in some sectors. The government continued to control prices for rice, sugar, gasoline, liquefied petroleum gas and diesel during the period under review. The only subsidy reform measure in the 2013 budget was a cut in sugar subsidies by MYR 0.20 a kilogram. However, the cut fell below the MYR 0.34 per kilogram increase in sugar subsidies implemented in January 2012, thus leaving subsidies at the same level or even higher than in September 2011. In addition, this reduction may be offset by the government's decision to stabilize cooking oil prices. During the period under review, the government did not abolish its policy of favoring Bumiputera companies for small government contracts. For example, 47% of the project value of the Sungai Buloh-Kajang mass rapid transit (MRT) line has been offered to Bumiputera companies, exceeding the initial goal of 43%. In 2012, the government announced the liberalization of an additional six services subsectors, including legal services,

Market-based
competition

8

medical specialist services, dental specialist services, international schools, private universities and telecommunications, by allowing majority ownership without Bumiputera equity participation. However, no guidelines were created for the sectors that have been liberalized, and no clear information is available to potential investors in these subsectors. According to the World Bank's Doing Business Index 2013, Malaysia took further steps toward a more competitive market economy during the period under review. Malaysia was ranked 12th out of 185 economies, rising from 18th place in 2012. The results showed a trend of improving competitiveness which began in 2008. Malaysia is ranked first overall in the World Bank's getting credit category, and fourth overall in terms of investor protection. The country improved its competitiveness in five areas of business in particular: getting electricity, registering property, paying taxes, trading across borders, and dealing with construction permits.

Competition laws designed to prevent monopolistic structures and conduct exist, but are enforced inconsistently. On 1 January 2012, the Competition Act 2010 came into force. The act was intended to prevent large companies from engaging in monopolistic or cartel-like activities. The act applied to any commercial activity within or outside Malaysia, including government-linked companies (GLC), and was enforced by the Malaysian Competition Commission (MyCC). The anti-monopoly law prohibited three matters: horizontal agreements, vertical agreements and abuse of dominance. Previously, no law against monopolies or the formation of monopolies and oligopolies has existed. However, cartels are still not criminalized in Malaysia, and the MyCC remained relatively inactive. During the period under review, complaints focusing on the government's policy restricting domestic shipping between Malaysian ports to Malaysian-owned ships emerged. This protectionist policy has led to excessive shipping costs and higher costs for goods, especially for people in Sabah and Sarawak. In addition, in some sectors such as electric supply, big companies have a virtual monopoly.

Anti-monopoly
policy

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Foreign trade is liberalized in principle, but significant exceptions remain, including differentiated tariffs and privileged treatment for domestic industries. During the period under review, the government liberalized an additional six services subsectors by allowing majority ownership without requiring participation by Bumiputera equity holders. However, these liberalized subsectors had no Bumiputera market participants, and other Bumiputera equity quotas and protectionist policies shielding key enterprises constitute high barriers for foreign investors. Since 2009, Malaysia has at least most-favored nation (MFN) treatment with its trading partners while providing tariff preferences to China, Japan, Pakistan, the Republic of Korea and other ASEAN countries. The simple average applied MFN tariff rate was approximately 8.0%, or 10.9% for agricultural products and 7.6% for nonagricultural products. Major trading partners for agricultural products include China, Singapore and the European Union; for nonagricultural products, China, Singapore and the United States are the largest partners. On March 2012, Malaysia and Australia

Liberalization of
foreign trade

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concluded negotiations on the Malaysia-Australia Free Trade Agreement (MAFTA). According to the agreement, Australia will eliminate 100% of its import tariffs when the treaty goes into force on 1 January 2013, while Malaysia will progressively reduce or eliminate import tariffs on 99% of its tariff lines by 2020. Along with Australia, Malaysia has signed FTAs with Japan, Pakistan, New Zealand, India and China. Malaysia and the European Union held their sixth round of FTA negotiations from 8 February to 11 February 2012.

Malaysia's banking system and capital market are differentiated and oriented to international standards, with functional banking supervision. Capital markets are open to domestic and foreign capital and banks remained well capitalized during the period under review. In 2011, the bank capital-to-assets ratio was 8.9%. The risk-weighted and core capital ratios stood at 14.8% and 13.0% respectively as of September 2012. Both numbers were above levels required by national authorities and Basel III standards, though lower than the 15.1% and 13.2% levels seen in early 2012. Asset quality improved further during the period under review, with the ratio of nonperforming loans declining to 2.2% in August 2012, an improvement as compared to the 2.7% ratio at the end of 2011. Furthermore, interbank rates were stable from 2011 to 2013. In July 2012, rating agency Moody's described the Malaysian banking system as "stable." The overall Malaysian financial system is made up of conventional and Islamic financial institutions. In February 2012, there were 16 Islamic banks operating in the country. However, a de facto lack of supervision in the banking sector became evident when research and advocacy organization Global Financial Integrity (GFI) revealed in December 2012 that close to MYR 200 billion in illicit financial flows was siphoned out of Malaysia in 2010.

Banking system
8

8 | Currency and Price Stability

Inflation and foreign exchange policies are treated in concert with other economic policy goals and have an adequate framework in Malaysia. During the period under review, the inflation rate (based on average consumer prices) eased significantly, reaching a two-year low of 1.2% in December 2012; this was in line with consensus estimates for a level of 1.7% and was one of the lowest rates in the region. In 2011, the rate was at 3.2%. Prices of food, alcoholic beverages and health care in particular rose at the end of 2012. In mid-2011, the government froze its Subsidy Rationalization Programs (SRP) in an attempt to keep the retail prices of fuel, essential food items and energy stable. The government is expected to cut subsidies in 2013 after the general elections. Consequently, the inflation rate is expected to increase in 2013, with forecasts predicting a rate of 3%. Throughout the period, the inflation rate remained within the comfort zone of the independent central bank (Bank Negara Malaysia). Since July 2011, benchmark interest rates have remained at 3%. The ringgit was stable during the period under review. The real effective exchange

Anti-inflation /
forex policy
9

rate (setting 2000=100) increased from 104.8 in 2009 to 109.2 in 2011. However, the ringgit performed well relative to the U.S. dollar, reaching the level of 3.10 to the dollar in January 2013, up from 2.99 to the dollar in February 2012.

The government's fiscal and debt policies generally promote macroeconomic stability, despite inconsistencies within the country's spectrum of institutional safeguards. In 2012, the budget deficit was at 4.5% of GDP. At MYR 42.3 billion, this deficit was below the government's original target of MYR 43 billion. In 2011, the deficit stood at 4.8% of GDP. Furthermore, overall public debt was the equivalent of 53.8% of GDP. However, the government declared that this rate was within the manageable range. The government successfully increased its revenues during the period under review. From 2012 to 2011, federal government revenues grew by 11.8%. Higher revenues were largely generated by firm oil prices and greater efforts in tax collection. The country's total reserves totaled \$131.8 billion in 2011. However, higher revenues were largely absorbed by additional government consumption. On 10 January 2012, the government launched its 1Malaysia People's Aid (Bantuan Rakyat 1Malaysia; BR1M) program. This offers payments of MYR 500 to households with a monthly income of MYR 3,000 or less. Eight months later, the ruling coalition announced a second round to the program. Eligibility was extended to single individuals aged 21 and above who earned less than MYR 2,000 a month. These persons would get a one-off payment of MYR 250. With general elections to be held in 2013, the program was widely seen as an attempt to provide "election goodies" so as to generate support for the government coalition among the poor.

Macrostability
7

9 | Private Property

Rights and regulations governing the acquisition, benefits, use and sale of property are generally well defined, but problems with implementation or enforcement under the rule of law occasionally emerge. The Heritage Foundation's 2013 Index of Economic Freedom praised Malaysia for improving the protection of property rights. In April 2012, amendments to the Copyright Act 1987 came into force. The new regulations included a system of voluntary registration of copyright works and the registration of a royalty collection body. In line with these amendments, Malaysia acceded to the World Intellectual Property Organization (WIPO) Copyright & Performances and Phonograms Treaties in December 2012. However, corporate lawsuits continue to face lengthy delays. In addition, the relocation of local residents and indigenous populations creates ongoing conflicts between the state government, developers and the population. In September 2011, the Federal Court dismissed an appeal by five native landowners who were suing the state government of Sarawak over the loss of their land due to the Bakun dam project. However, the legal status of large plots of native land remained unsettled during the period under review. On 27

Property rights
9

September 2012, at least 200 people blocked the access road to the Murum dam in Sarawak. The construction of the Murum dam will require the forced relocation of about 1,500 people.

Private companies are institutionally viewed as important engines of economic production and are given legal safeguards in Malaysia. The revenues of Malaysia's state-owned companies and government-linked companies (GLC) constitute 17.4% of the country's GDP. The government intensified the privatization process during the period under review. Under the New Economic Model (NEM), 33 companies have been identified as ready for divestment either through a listing, pare-down or outright sale. In 2011, 11 divestments were completed. High-profile divestments included Felda, car producer Proton, EON Capital, highway operator PLUS and Pharmaniaga. However, the privatization of state companies does not fully conform to market principles, mainly because the privatization of projects requires Bumiputera participation. The public sector continues to play a considerable economic role.

The World Bank's Doing Business Index 2013 ranked Malaysia 12th in the world and emphasized that the country is among the world's most business-friendly countries. As part of its reforms, Malaysia cut the number of days it takes to register property transfers by introducing a new caseload management system at the land registry.

10 | Welfare Regime

In principle, social safety nets are well developed, but do not cover all risks for all strata of the population. A part of the population is still at risk of poverty in Malaysia with no state-funded unemployment benefits or individual retirement funding mechanism in place. Several social-security programs provide benefits for various groups of workers. Government employees receive the best benefits, while employees in the small informal sector receive virtually nothing. The Employees Provident Fund (EPF) is the primary social-security institution, covering more than half of the workers in the private sector as of the year 2000. From 1 January 2012, employee's contribution share is 11% of their monthly salary, while employers contribute 13%. The 1% increase from the earlier 12% level benefited 5.3 million workers, comprising 92% of EPF's active members. For employees who receive wages or salaries exceeding MYR 5,000, the employee's contribution of 11% remained, while the employer's contribution was 12%. These rates are valid for employees below 55 years of age. Nevertheless, Malaysia is still dependent on informal community assistance and a large number of NGOs in the social-security sector. This informal community assistance is needed due to the low public expenditure on health (2.4% of GDP in 2010). Malaysia has a widespread system of

Private enterprise
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Social safety nets
7

health care. A universal health care system coexists with a growing private health care sector.

Equality of opportunity has largely been achieved, though discrimination against women and ethnic groups persists. Although women's civil liberties are protected by law in Malaysia, traditional practices continue to distinguish between genders. In 2011, the country had a Gender Inequality Index value of 0.286, earning it a rank of 43rd out of 146 countries. However, only 14% of parliamentary seats are held by women. In addition, the female labor market participation rate is 44.4%, as compared to 79.2% for men, according to UNDP data for 2011. The female literacy rate is 94.6%, slightly higher than the male rate of 90.3%. Women's higher level of education is indicated by the female to male enrollment ratio (129% at the tertiary level). Due to continuing affirmative action policies for Bumiputera, Chinese and Indian citizens face explicit disadvantages when seeking employment in public offices, the state bureaucracy, public enterprises and the armed forces.

Equal opportunity

7

11 | Economic Performance

Malaysia's economic performance was good during the period under review. The country's economy remained resilient, mainly because of a rapid expansion of domestic demand, while external demand (and export-oriented industries) stagnated due to continuing global uncertainty and weakening demand from advanced economies and China. With the introduction of minimum wages in May 2012, the government strengthened domestic demand further. Private-sector workers in peninsular Malaysia receive a minimum salary of MYR 900 a month, while workers in the states of Sabah and Sarawak receive MYR 100 less. Some argued that the high level of the minimum wage in the states of Sabah and Sarawak could hurt small businesses in these states. Nevertheless, Malaysia's economy performed well. The overall GDP growth rate for 2012 was 5.1%, with 2013 growth forecast by the government to be 5.6%. GDP per capita (on a purchasing power parity basis) increased in 2011 to \$15,600, a level higher than before the global financial crisis. The inflation rate (based on average consumer prices) eased significantly, reaching a two-year low of 1.2% in December 2012, one of the lowest rates in the region. For 2012, overall inflation is expected to total 1.7%, a rate expected to rise slightly in 2013 to 2.5%. The current account balance in Malaysia was positive in 2011, at \$32.99 billion. In November 2012, the unemployment rate stood at 2.9%, up from its record low of 2.7% in August 2012. In addition, consumer confidence is holding up, and is expected to remain largely intact. The level of investor confidence in Malaysia was reflected in the surge of foreign direct investments (FDI) inflows. In 2011, FDI increased by 12.3% compared to 2010, reaching the overall mark of \$11.97 billion, as compared to \$9.1 billion in 2010, according to the United Nations Conference on Trade and Development (UNCTAD) 2012 World Investment Report. The

Output strength

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manufacturing sector accounted for the largest share of FDI. However, the budget deficit remained at 4.5% of GDP in 2011. In addition, government spending on subsidies in 2012 exceeded the original budgeted amount for the third consecutive year, with one-fifth of the government's revenues and operating expenditures committed to subsidies.

12 | Sustainability

Environmental concerns are taken into account by Malaysian policymakers, but are occasionally subordinated to efforts to promote growth. Environmental regulation and incentives are partly in place, but enforcement is at times deficient. Deforestation and climate change are the nation's primary environmental problems. The Environmental Performance Index (EPI) ranked Malaysia 25th worldwide in 2012, the best ranking for the country so far. Within the Asia-Pacific region, Malaysia was ranked at third place. Improvements were largely made with regard to air pollution measurements and a higher level of biodiversity. However, the problems associated with uncontrolled hillside development in Malaysia became evident on 21 May 2011 when a massive landslide killed 16 people in Hulu Langat. In November 2012, environmental group Himpunan Hijau organized a so-called Green Walk, a 14-day cross-country march in protest of the Lynas Advanced Materials Plant (LAMP) in Gebeng, a rare-earth mining factory. Opponents of the company fear the factory would release dangerous chemicals to which local residents would be exposed. However, the Malaysian Court of Appeal dismissed an appeal against an earlier decision to grant Lynas a temporary operating license on 19 December 2012. During the period under review, protests against the government's long-term plans to build 12 massive hydroelectric dams on the island of Borneo persisted. On 27 September 2012, at least 200 people blocked the access road to the Murum dam in Sarawak. The construction of the Murum dam will require the forced relocation of about 1,500 people.

Environmental
policy
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In principle, education policy ensures a nationwide system of sound education and training. The research and technology sector is fairly advanced. Public expenditure on education, totaling 5.8% of GDP in 2009, can be considered high, even with reference to international standards. Malaysia has 24 universities and 65 private institutes for higher education. These universities, university colleges and polytechnics nationwide produced 184,581 graduates in 2011. However, the Malaysian educational system continues to demonstrate several shortcomings. Gross enrollment ratios at the secondary and tertiary levels are low by international standards (68.3% and 40.2%). Consequently, the World Economic Forum's Global Competitiveness Report 2012 – 2013, which ranked Malaysia 25th out of 144 countries, identified an inadequately educated workforce as one of the most problematic factors for doing business in the country. In particular, a low level of

Education policy /
R&D
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technological readiness could significantly undermine Malaysia's efforts to become a knowledge-based economy. Expenditure on R&D amounted to 0.64% of GDP in 2006. Among Asian countries, Malaysia is ranked sixth behind Japan, China, South Korea, Taiwan and Singapore. The overall literacy rate stood at 92.5% during the period under review. In January 2013, the government launched the National Education Blueprint (2013 – 2025) to transform the national education system to a level comparable with that of developed nations within the next 13 years. One of the program's key points is to ensure that every child is proficient in English. In order to reach this goal, 70,000 English teachers are to be given training to improve language proficiency. This policy can be seen as an attempt to revoke the decision made in 2009 when the government abolished its policy of teaching sciences and mathematics in English. The program's progress is monitored and evaluated by the Education Performance and Delivery Unit (Padu).

Transformation Management

I. Level of Difficulty

The Malaysian government faces only moderate structural constraints with respect to its capacity to govern. With only 2.3% of the population living below \$2 a day in 2009, infrastructure development and poverty are not serious constraints on the Najib administration. Moreover, the country has not been exposed to natural disasters or pandemics. Nevertheless, the educational system's output of high-skilled workers is insufficient and regional disparities in economic development, especially on the island of Borneo, must be addressed by the government. Less than 70% of the Malaysian workforce has completed a secondary level education. Wage growth has been muted and Malaysia is still seen as a "low-cost" country. The low-cost production model has been supported by inflows of low-skilled foreign workers. Though the New Economic Model (NEM) recognizes the need to develop a higher-quality workforce, the majority of jobs in Malaysia, especially in the private sector, are still low-skilled. In addition, women are underrepresented in engineering, architecture and other traditionally non-female fields. Corruption, a weak civil society and significant ethnic and religious heterogeneity continue to be structural constraints. During the period under review, ethnic and religious tensions remained, a factor that today represents the country's most severe structural constraint.

Structural
constraints

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Civil society traditions remain fairly weak in Malaysia, and are mostly found in urban areas. Though new NGOs have emerged in the last two decades, the country's voluntary organizations remain plagued by scarce organizational resources. However, civil society has become stronger and awareness has risen during the period under review. Protests by environmental groups took place in Manjung, Perak, because of a MYR 4 billion iron ore hub and jetty project; in Pengerang, Johor, against a Petronas Refinery and Petrochemical Integrated Development project; and in Sarawak regarding the construction of the Murum and Baram dams. As another sign of increasing vibrancy within civil society, non-governmental organizations protested against the government in the People's Uprising Rally (KL 112 rally) in Kuala Lumpur on 12 January 2013. More than 50,000 people attended the demonstration. In general, two different civil society cultures have emerged within the growing circle of NGOs. On the one hand, a group of liberal organizations has intensified activities such as monitoring human rights or observing the government's

Civil society
traditions

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reform agenda, especially with regard to environmental issues. On the other hand, a more welfare-oriented culture has also gained strength, with a particular focus on informal community assistance for the poor at the local level. However, right-wing Malay Muslim organizations such as Perkasa deepened civil society's polarization along ethnic lines. More broadly, data provided by the Asian Barometer Survey indicates that Malaysians' involvement in associations largely fails to foster trust in fellow citizens.

There have been few outbreaks of violence in Malaysia in recent times. However, society is polarized along ethnic and religious lines. Since independence, the political elite have managed ethnic and religious cleavages by forming a multiracial ruling coalition that has included the three largest race-based parties. Though this bargain led to a political spectrum split along religious and ethnic lines, it helped stabilize a divided Malaysian society and inhibited the outbreak of major violent conflict for three decades. However, ethnic and religious relations remained tense during the period under review. In March 2011, a lot of 5,100 Malay-language Bibles were stamped with "For Christians Only" on the cover; and in May, the *Utusan Malaysia* newspaper concocted stories about an alleged plot by Christian priests to establish some kind of Christian state in Malaysia. In August 2011, officials from the Selangor Islamic Department (JAIS) raided an annual Thanksgiving dinner without a search warrant because of an alleged attempt to proselytize Muslims. Twelve Muslims present at the dinner were provided counseling in order to restore their faith and belief in Islam. On 22 October 2011, the right-wing Malay Muslim group Perkasa organized a rally in Kuala Lumpur to fight the challenge of Christianization in Malaysia. In January 2013, Perkasa leader Ibrahim Ali called on Muslims to burn Malay-language Bibles that contained the words "Allah" or other religious Arabic scripts. A survey published by the Merdeka Center in August 2011 revealed deterioration in the country's ethnic and religious relations. The share of Malaysians who felt that ethnic relations in the country were good had fallen from 78% in February 2006 to 66% in May 2011. The number of people who felt that ethnic unity was superficial rose from 29% to 44%. These developments served as a contradiction to Prime Minister Najib's *1Malaysia* program, which stresses national unity and ethnic tolerance. So far, *1Malaysia* has not fostered unity among Malaysians, and it is questionable whether the program can become anything more than a slogan.

Conflict intensity

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II. Management Performance

14 | Steering Capability

The Malaysian government claims to be setting strategic priorities. Nonetheless, the political leadership has shown inconsistency between its policies and its stated aims. Furthermore, the government's long-term strategic aims do not include a further democratization of the public sphere or the extension of democratic norms. Two key strategic regime priorities are contained in the Government Transformation Plan (GTP) and the Economic Transformation Plan (ETP): improving the efficiency of the public service and improving the competitiveness of the economy, including increasing private investment so as to meet the stated target of achieving high-income country status by 2020. The ETP focuses in particular on a Human Capital Strategic Reform Initiative aimed at upgrading and improving skills within the workforce, the inclusion of women in the labor market, and the creation of a minimum wage. A minimum wage was in fact introduced during the period under review, indicating that some of the goals stated in the GTP and the ETP have begun to materialize, demonstrating the strategic capacity of the government to prioritize and organize its policy measures. However, women are still underrepresented in the labor market, and inefficiency in the bureaucracy remains. The majority of jobs in Malaysia, especially in the private sector, are still low-skilled. In addition, the long-awaited introduction of a goods and services tax (GST) has yet to be implemented. The postponement of the tax until after the elections in 2013 is sign of a government shift in focus toward short-term interests with the aim of silencing public criticism, instead of adhering to its long-term aim of consolidating the country's budget.

A number of new economic policies were implemented during the period under review. Under the New Economic Model (NEM), 33 companies have been identified as ready for divestment either through a listing, pare-down or outright sale. Eleven divestments were completed in 2011. High-profile divestments included Felda, car producer Proton, EON Capital, highway operator PLUS and Pharmaniaga. In addition, amendments to the Copyright Act 1987 came into force in April 2012. The new regulations included a system of voluntary registration of copyright works and the creation of a royalty collection body. In line with these amendments, Malaysia acceded to the World Intellectual Property Organization (WIPO) Copyright & Performances and Phonograms Treaties in December 2012. In January 2012, the government launched a program aimed at assisting the country's poorest residents. Under this 1Malaysia People's Aid (Bantuan Rakyat 1Malaysia, BR1M) program, households with a monthly income of MYR 3,000 or less receive payments of MYR 500. Eight months later, the ruling coalition announced a second program round. This

Question
Score

Prioritization
5

Implementation
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time, eligibility was extended to single individuals aged 21 and above who earn less than MYR 2,000 a month. These persons were made eligible for a single-time MYR 250. The cabinet under Prime Minister Najib improved environment policies with the aim of lessening air pollution. Although the government abolished several restrictive laws during the period under review, the executive has not sought structural or qualitative changes in the political system in such a way as to facilitate democratic transformation. In December 2011, the government passed the Peaceful Assembly Act. However, the act is seen as more restrictive than preexisting regulations, and contravenes international human rights standards. In April 2012, the government replaced the Internal Security Act (ISA), which allowed the state to keep people perpetually incarcerated by enabling detention orders to be renewed every two years, with the Security Offences (Special Measures) 2012 Act (SOSMA). However, opposition groups, the Malaysian Bar Council, and international human rights watchdogs criticized the reform as insufficient. With the possibility of detaining suspects for 28 days without judicial oversight and a very broad definition of who may be arrested, the SOMSA fails to adequately protect citizens' basic constitutional rights. Furthermore, the bill imposed limits on previously unrestricted activities, while broadening police arrest and surveillance powers in new and innovative ways.

The Najib administration has demonstrated a desire to respond to mistakes and failures with change. The government shows a considerable degree of flexibility and learning capability with reference to market reforms. However, the political leadership continues to refrain from the implementation of democratic reforms. Moreover, it shows a low degree of political will to learn from past mistakes so as to facilitate democratic changes. A populist style of politics on the part of the Najib administration continued during the period under review. The government's 1Malaysia People's Aid program (Bantuan Rakyat 1Malaysia/BR1M), which offers payments to the poor, is widely seen as an attempt to offer "election goodies" so as to generate support for the government coalition among the poor, rather than being an effective tool to fight poverty. The creation of the Performance Management & Delivery Unit (PEMANDU) in 2009 in order to oversee implementation and assess the progress of the ETP and GTP can be seen as an important step toward good practices aimed at facilitating economic growth. However, coordination between the various government evaluation units – for example, between the Education Delivery Unit (EDU) and PEMANDU – will be critical so as to avoid duplication of implementation efforts and dilution of reform effectiveness. The government's executive-centered decision-making process did not change during the period under review. Prime Minister Najib, often presenting himself as a reformer, did not demonstrate a willingness to abandon authoritarian practices on the part of the ruling government. In sum, the government's reform projects cannot be considered as proof of its learning process or of its commitment to democratic norms.

Policy learning
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15 | Resource Efficiency

The Malaysian government makes efficient use of most available human, financial and organizational resources. The government's administrative personnel are generally seen as professional. However, the reach of competitive recruiting systems is limited due to the Bumiputera quota system. This negatively impacts the functioning of the administrative system at the lower levels of the Malaysian bureaucracy. More broadly, the government's affirmative action policy establishing a Bumiputera quota for virtually all of its economic activities remains worrisome. Separately, the federal government budget deficit in 2012 stood at 4.5%. Although the government reduced subsidies during the period under review, subsidies for fuel, food and energy were distributed, thus burdening the budget. For 2013, official federal government debt is forecast to rise as a proportion of GDP from 51.8% to 53.7%. In addition, operating expenditures were up 18% in the first half of 2012 and were expected to increase by 11% for the year as a whole, thereby exceeding the original budget allocation by 11.5% due to the government's increased spending on wages, pensions and transfers. In sum, the budget deficit and the Bumiputera quota system restrict the government's efficient use of assets.

Efficient use of assets

7

The government coordinates conflicting interests and objectives under the leadership of Prime Minister Najib. Under his hierarchical leadership, the cabinet effectively handled major conflicts over economic or social policies in such a way as to achieve policy coherence. Najib's approval ratings were relatively good in 2011 and 2012, although still lower than those of his predecessor as prime minister, Abdullah Badawi, shortly before he fared badly in the 2008 general elections. Approval ratings for the UMNO party were comparatively low. The other coalition partners, especially the MIC and the MCA, remain weakened due to their leadership changes during the period under review. The weakness of his alliance parties has to be a concern for Prime Minister Najib. The continuation of the government's affirmative action policy has weakened the MIC and the MCA further, as the ethnic Chinese and Indian minorities feel they are being put at a disadvantage. Therefore, Prime Minister Najib has to ensure that trade-offs between policy goals are well balanced, and do not serve as additional burdens to the BN member parties. Compared to other countries in the region, the government's ability to coordinate conflicting objectives and interests continues to be fairly effective, however.

Policy coordination

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The government has identified corruption as an important problem within state structures, although levels of corruption in the civil service are probably the lowest in the region after Singapore. Although institutions enabling auditing of state spending are in place, political connections continue to be the strongest criterion in awarding large state contracts and infrastructure projects. The government's corruption-fighting reforms have been somewhat ambivalent, however. In October

Anti-corruption policy

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2011, the Auditor-General's Report 2010 revealed that the government-linked National Feedlot Corporation was misusing government money. Consequently, the chairman was charged with using government funds to buy apartments and pay for overseas trips in March 2012. However, the Whistleblower Protection Act, introduced in December 2010, does not protect whistleblowers effectively. Opposition politician Rafizi Ramli, who provided information in the National Feedlot Corporation case, was prosecuted for violating the Banking & Financial Institutions (BAFIA) Act as a result of revealing confidential banking details. Although the government is planning under the second Government Transformation Program (GTP) to tackle corruption by adding a corporate liability provision into the Malaysian Anti-Corruption Act (MACC) (thus bringing the statute on par with the U.K. Bribery Act or the U.S. Foreign Corrupt Practice Act), there is widespread public feeling that the political and economic elites use public resources at will and can avoid prosecution. In addition, party financing regulations are insufficient. As a government-controlled body, the Election Commission (EC) is not willing to check party financing and campaign expenses closely. Candidates have to publish an account of their election expenses from nomination until polling day, but the EC does not analyze these accounts. The EC has no authority to inspect party financing or to prosecute legal violations. Parties are not required by law to file a statement of their income or expenditures during elections, although they spend an exorbitant amount of money to muster support.

16 | Consensus-Building

In principle, all major political and social actors agree on the goal of a market-based economy. The exceptions to this include some environmental groups, who criticize the fact that environmentally compatible growth tends to be subordinated to growth efforts, as well as fundamentalist Muslim groups such as Perkasa. During the period under review, Perkasa put constant pressure on the government to retain the Bumiputera affirmative action policy. With Perkasa gaining support among the Malay Muslim majority population, the organization has posed a growing challenge to the government's reform policies. Nevertheless, there is no politically or economically relevant actor with the power to derail either the reform process or the expansion of the market economy. With regard to liberal democracy, however, no such consensus is shared by political and social actors. The ruling coalition has tried to present itself as reformist and open to democratic practices. However, implemented reforms such as the Peaceful Assembly Act 2012 and the Security Offences (Special Measures) Act 2012, which replaced the Internal Security Act (ISA), have not facilitated democratic transformation.

Consensus on goals

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With the Barisan Nasional (BN) continuing to control a parliamentary majority on the federal level, reformers have had no power to bring forward democratic reforms. The government has shown no intention of enabling democratic transformation, and the idea is further rejected by fundamentalist Islamists who want to create an Islamic state. Nonetheless, the four state governments led by opposition parties have started to implement democratic reforms on the state level, despite federal government attempts to undermine the process. The military poses no threat to potential democratic transformation, as the armed forces are effectively subordinated to the civilian rulers.

Anti-democratic
actors

5

Given the ethnic and religious heterogeneity of Malaysian society, with its significant ethno-religious cleavages, the government has been more or less successful in managing social differences in the past. However, while cleavage-based conflicts did not escalate, ethnic and religious tensions remained during the period under review. In March 2011, a lot of 5,100 Malay-language Bible were stamped with “For Christians Only” on the cover, and in August, officials from the Selangor Islamic Department (JAIS) raided an annual Thanksgiving dinner without a search warrant because of an alleged attempt to proselytize Muslims. Twelve Muslims present at the dinner were provided counseling in order to restore their faith and belief in Islam. On 22 October 2011, right-wing Malay Muslim group Perkasa organized a rally in Kuala Lumpur to fight the challenge of Christianization in Malaysia. These events exemplified the tense relationship between the Malay/Muslim majority and the ethnic Chinese and Indian minorities. The government’s 1Malaysia campaign, aimed at creating unity among Malaysian citizens, did little to overcome the country’s ethnic and religious division, and must be seen primarily as a slogan that differs little from earlier campaigns. Hopes among ethnic minorities that government programs would shift to a need and merit basis with the introduction of the New Economic Model (NEM) and the ongoing high-profile divestments have not been realized. In contrast, politicians within the government and the opposition voiced fears that only Bumiputera companies would profit from the divestments, thereby deepening ethnic and religious cleavages further. Regional and economic disparities within the Malaysian state persist, and continue to deepen the center-periphery cleavage between eastern and western Malaysia.

Cleavage /
conflict
management

6

The political leadership recognizes and accommodates the interests of civil society actors only as long as they are not perceived to interfere with government policies. Laws pertaining to NGOs and other civil society groups continue to limit the space within which civic activity can take place. In April 2012, a Parliamentary Select Committee (PSC) on Electoral Reforms, formed in the aftermath of the 2011 Bersih rally, released a report with 22 recommendations for improving the electoral system. Although the recommendations were widely seen as insufficient – for example, the problem of “phantom voters,” or voters registered in apartment blocks in closely contested constituencies, was not addressed – the report can be seen as a direct

Civil society
participation

5

reaction on the part of the political leadership to the protests led by civil society groups. In addition, the government's decision to lift its four-year ban against Hindu NGO Hindraf (Hindu Rights Action Force) on 26 January 2013 can be seen as a positive sign. However, Malaysian civil society in general plays a marginal role in terms of agenda setting, policy formulation, policy implementation and performance monitoring.

The effects of the 13 May 1969 race riots remain visible in Malaysian society today, as the Bumiputera affirmative action policies implemented at the time are partially still in place. Discontent with these policies is clearly visible among the ethnic Indian and Chinese minorities. This is true even within the ruling coalition, largely due to the fact that the Malaysian Chinese Association (MCA) and the Malaysian Indian Congress (MIC) have both lost significant support within their own ethnic communities, and fear they will make a weak showing in the upcoming general elections. These concerns stand in sharp contrast to the United Malays National Organization (UMNO), which continued to be the dominant force within the ruling Barisan Nasional (BN) coalition. The government's 1Malaysia campaign, aimed at creating unity among Malaysian citizens, cannot be seen as an effective tool to overcome the country's ethnic and religious division. As a result, tension between the Malay Muslim majority and the non-Malay, non-Muslim minorities persists.

Reconciliation
n/a

17 | International Cooperation

The political leadership tries to use international assistance to further its own development agenda, but has demonstrated difficulties in devising a consistent long-term strategy able to integrate this support effectively. The Najib administration works with bilateral and multilateral international donors such as the World Bank, the IMF and the Asian Development Bank (ADB). Nevertheless, the government limits the influence of international aid by approving only those policies that suit the government's own ideological preferences. The Government Transformation Program (GTP) and the Economic Transformation Program (ETP) offer distinct roadmaps aimed at achieving the government's goal of attaining high-income country status, and of promoting inclusive and sustainable growth. Consequently, the government is working closely with the World Bank to monitor the program's successes. An international panel reviews the ETP, and publishes annual reports. However, the Malaysian government blocks every attempt by international donors or organizations to facilitate any deepening of democracy or civil rights in the country.

Effective use of
support
7

The Malaysian government is considered by the international community to be a credible and reliable partner. Prime Minister Najib has solidified Malaysia's position in the world community with his pro-Western stand. The political leadership remains fully engaged with the World Bank, the IMF, the ADB and other international institutions such as the WTO. During the period under review, Malaysia acceded to

Credibility
9

the World Intellectual Property Organization (WIPO) Copyright & Performances and Phonograms Treaties in December 2012. However, Malaysia was internationally criticized due to a high level of illicit financial outflows. According to Global Financial Integrity (GFI), close to MYR 200 billion in illicit funds was siphoned out of Malaysia in 2010, putting the country second only to China in terms of global capital flight. Prime Minister Najib has disputed these figures.

The political leadership actively and successfully builds and expands upon cooperative neighborly and international relationships. The government promotes both regional and international cooperation. In November 2012, together with nine ASEAN states, Malaysia adopted a human rights declaration at the 21st ASEAN summit in Phnom Penh. In March 2012, Malaysia and Australia concluded negotiations on the Malaysia-Australia Free Trade Agreement (MAFTA). The same year, Malaysia successfully brokered peace talks between the Moro Islamic Liberation Front (MILF) and the Filipino government, thereby helping to end one of the region's longest-lasting conflicts. In February 2012, Malaysia and Thailand identified six potential areas in which they could enhance economic cooperation. To further improve bilateral relations between Malaysia and Indonesia, the two countries agreed to hold joint patrols to monitor the border on Borneo in September 2012. However, Malaysia's territorial dispute with China, the Philippines, Brunei, Vietnam and Taiwan in the South China Sea intensified during the period under review. Malaysia claims 12 features in the Spratly Islands, where vast reserves of natural resources are suspected.

Regional
cooperation
10

Strategic Outlook

During the period of review, the ruling Barisan National (BN) coalition, and especially its Malaysian Chinese Association (MCA) member party, was unable to regain public support lost in recent years. The degree of democratic transformation in Malaysia has remained minimal. The Najib administration has shown no intention of facilitating democratic transformation, although the government did implement reforms such as the abolishment of the Internal Security Act (ISA). These reforms were widely seen as window dressing obscuring an underlying lack of change. Public demands for democratic reforms did not lessen during the period under review, and as of the time of writing, it appeared that the ruling coalition ran the risk of losing power in the 2013 general elections. Opposition parties gained momentum at the beginning of 2013, with the opposition's strength becoming evident in the People's Uprising Rally (KL 112 rally) against the government in Kuala Lumpur on 12 January 2013. Consequently, a new transformation strategy aimed at enhancing democratic reforms and economic growth should focus on three key elements. First, the government has to guarantee a free and fair electoral process. With a highly competitive general election expected, irregularities or even electoral fraud could destabilize the country. Although a Parliamentary Select Committee (PSC) on Electoral Reforms released a report with 22 recommendations for improving the electoral system in April 2012, the opposition rejected the report as insufficient. The problem of "phantom voters," or voters registered in apartment blocks in closely contested constituencies, threatens to undermine the electoral process. In addition, the government has to guarantee the integrity of overseas votes. Second, the Malaysian government has to address the persistent religious and ethnic tensions. Between 2011 and 2013, the already-low level of social capital further declined. Ethnic Chinese and ethnic Indians in particular feel a strong sense that they face disadvantages, and no longer seem willing to accept their inferior standing within the Malaysian polity. More than half of the Chinese population is dissatisfied with the government, and the main Chinese party allied with the ruling BN coalition lost 13 of 19 seats it contested in local Sarawak elections in 2011. At the same time, members of the Malay Muslim majority population fear that ending the Bumiputera affirmative action policy would endanger their economic position. Therefore, the government should continue its path of reducing the preferential politics and special rights accorded to the Bumiputeras. The continuation of reform to the Bumiputera policies should be given the highest priority in order to ease the country's ethnic tensions and promote a more competitive economy. Third, the sustainability of Malaysia's favorable near-term economic outlook into the medium term hinges on improving employment quality. With a significant portion of investment taking place in the oil and gas sector, and oil revenues supporting public investments, Malaysia's near-term outlook owes much to commodities. These investments bring risks associated with the potential for external economic shocks. Only if it develops a high-skilled and well-educated workforce will Malaysia be able to attract foreign investors in other sectors, thus increasing private-sector investment. In order to achieve these goals, more women have to be incorporated into the job market, and the first steps toward making the education system more competitive have to be taken.

