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Abstract

The article reports on the political uncertainty faced by Malaysia after the ruling Barisan Nasional party suffered its worst result in general elections on March 8, 2008. The country's short- and long-term political ratings remain unchanged for the time being, but may be subject to downward revisions if political conflict continues. Barisan Nasional lost in four states based on the general election result.

POLITICAL OUTLOOK

Early Polls Result In Political Instability

BMI View: Malaysia is facing a period of political uncertainty after the ruling Barisan Nasional (National Front) suffered its worst ever result in general elections held on March 8. Our short- and long-term (74.2) political ratings remain unchanged for the time being, but may be subject to downward revisions if political in-fighting escalates.

Prime Minister Abdullah Ahmad Badawi was sworn in for a second term on March 10, ignoring calls for his resignation after his Barisan Nasional coalition – which has ruled Malaysia since independence in 1957 – recorded its worst ever election result in general elections recently. After winning 90% of the vote and 12 of the 13 states in 2004, the National Front was only able to capture 62% this time around, losing four states in the process. Protest votes from ethnic Chinese and Indians – which cost Barian Nasional Abdullah's home state of Penang to the Chinese-backed Democratic Action Party (DAP) – were widely expected, but it was the opposition Islamist party Parti Islam SeMalaysia (PAS) that really delivered the telling blow.

Ethnic tensions have flared in recent months, and racial inequality was expected to be the cornerstone of the opposition's challenge to Barisan Nasional's dominance. However, voter dissatisfaction with Abdullah's administration evidently runs deeper than just distress over ethnic disparities, with PAS claiming shock victories in the northern states of Kedah and Perak as voters expressed their growing unrest with the government. PAS also retained control of its northeastern stronghold of Kelantan, and in a joint effort with DAP and the People's Justice Party (Parti Keadilan), wrested power from the National Front in Selangor and won almost all the seats in the federal territory of Kuala Lumpur.

This has set the stage for opposition parties – which have frequently complained that the electorate is gerrymandered in favour of rural Malays, that the pro-government mainstream press gives too little coverage to opposition statements and that campaigning rules favour the incumbents – to push for political reform, but if they are to successfully do so, the disparate parties must work together. Former premier Anwar Ibrahim, the *de facto* leader of Parti Keadilan, which emerged as the largest opposition party in the new federal parliament with 31 seats, has assumed the mantle of uniting the opposition parties, but he will face a tough time in doing so. Opposition parties have a history of distrusting each other, and diverging ideologies and policies will make the task that much more difficult.

This has opened the path for a period of political instability in Malaysia, as Barisan Nasional regroup from the shock election result and opposition parties attempt to forge a workable partnership. Abdullah has shrugged off calls for his resignation, but the general consensus is that his standing within his party has been fatally damaged. The United Malays' National Organisation (UNMO), the dominant party within the Barisan Nasional coalition, holds party elections later in the year, and it is looking increasingly likely that Abdullah will be replaced by Deputy Prime Minister Najib Razak when these take place.

Meanwhile, opposition parties have threatened to review the multi-billion-dollar development corridors, set up by Abdullah as the centrepiece of his economic programme, in the states now under their control. This is the first sign that the results of March's poll could result in a fragmented government.

DATA & FORECASTS

	2006	2007e	Latest Period		2008f	2009f
Population, mn [8]	26.11	26.57	-	-	26.99	27.45
Nominal GDP, US$bn [9]	156.20	181.80	-	-	200.30	217.50
GDP per capita, US$ [9]	5,980	6,841	-	-	7,421	7,922
Real GDP growth, % change y-o-y [1,10]	5.9	6.3	7.3	Q407	5.5	5.6
Industrial production index, % y-o-y, ave [10]	5.0	3.9	5.7	Dec	6.0	5.6
Fiscal revenue, MYRbn [2,11]	115.6	134.8	-	-	148.2	162.8
Fiscal expenditure, MYRbn [3,11]	134.0	155.4	-	-	169.4	184.6
Budget balance, % of GDP [4,9]	-3.2	-3.3	-	-	-3.2	-3.0
Consumer prices, % y-o-y, ave [5,9]	3.6	2.0	2.3	Jan	2.4	2.8
Lending rate, %, eop [6,8]	6.80	6.30	-	-	6.20	6.20
Exchange rate MYR/US$, eop [8]	3.53	3.30	3.17	7-Mar	3.10	2.90
Imports, US$bn [7,12]	137.30	144.44	43.30	Jan	154.84	171.56
Exports, US$bn [7,12]	160.84	165.83	53.00	Jan	170.80	181.91
Trade balance, US$bn [12]	21.65	21.25	9.70	Jan	13.88	7.89
Current account, US$bn [12]	26.74	28.85	-	-	21.24	18.75
Current account, % of GDP [9]	17.12	15.87	-	-	10.60	8.62
Forex reserves (- gold), US$bn [8]	82.24	93.50	113.86	15-Feb	107.64	120.06
Import cover, months g&s [9]	7.5	8.3	-	-	8.3	8.3
Foreign debt, US$bn [11]	53.4	54.2	-	-	56.9	59.8
Foreign debt, % of GDP [9]	34.2	29.8	-	-	28.4	27.5

Notes: e/f = BMI estimates/forecasts; 1 The Oxford Economic Forecasting model is used when generating forecasts.; 2 Federal Government, Total Revenue & Grants; 3 Federal Government, Total Expenditure & Loans Minus Repayments; 4 Federal Government; 5 Chain-weighted index (2000 = 100), sourcing from IMF and Bank Negara Malaysia; 6 Modes of the range of rates quoted for the base lending rate. Beginning in January 1996, weighted average base lending rate charged by commercial banks; 7 Free on board; Sources: 8 IMF; 9 BMI calculation; 10 Statistics Department, Malaysia; 11 Bank Negara Malaysia; 12 IMF, Statistical Department, Malaysia.

BMI View: While **Bank Negara Malaysia** (BNM) had been seeking to cut interest rates in 2008 to ensure that the recent surge in domestic demand stays well supported, mounting inflationary pressures are now likely to force the central bank to adopt a far more cautious approach to monetary policy. Consumer price inflation (CPI) dipped slightly from December's 10-month high of 2.4% y-o-y, slowing to 2.3% in January. Nonetheless, inflation pressures remain as global food and fuel costs continue to climb significantly higher. We are forecasting annual average CPI to rise by 2.4% in 2008, up from 2.0% in 2007, but recognise that risks remain firmly to the upside. With BNM seemingly hamstrung to raise interest rates in order to curb inflation, we are expecting further currency appreciation towards our end of 2008 ringgit forecast of MYR3.10/US$.