SPECIAL REPORT

LIBERALISATION:
Follow-through action crucial

The stock market barely reacted to the liberalisation measures unveiled by Prime Minister Datuk Seri Najib Razak last week. Nevertheless, some of the key reforms, such as scrapping the 30% bumiputera equity ownership requirement, were well received.

| BY JENNY NG |

The buzz of previous Invest Malaysia conferences was absent at the fifth instalment held last week in Shangri-la Hotel in Kuala Lumpur despite the watershed announcement by Prime Minister Datuk Seri Najib Tun Razak to further liberalise decades-old affirmative action policies introduced under the New Economic Policy (NEP).

A regular attendee says investors may have been let down previously when expectations were raised under former prime minister Tun Abdullah Ahmad Badawi. Malaysia was oversold in earlier Invest Malaysia conferences, he notes. Furthermore, the ongoing swine flu pandemic and economic downturn may have been contributing factors as well.

Or it could be a sign that Malaysia is increasingly left behind in the race to win investor interest as neighbouring countries liberalise.

It is Najib's first Invest Malaysia conference as prime minister. In his keynote address last Tuesday, he unveiled major changes in stock ownership and property acquisition rules.

The stock market barely reacted, but the liberalisation measures were generally well received by investors and corporate figures present at the conference.

A key reform is the immediate removal of the 30% bumiputera equity ownership requirement for public-listed companies. Other measures include a whittling down of the powerful Foreign Investment Committee (FIC), set up in 1974, to vet and approve foreign investments.

With immediate effect, FIC guidelines covering the acquisition of equity stakes, mergers and takeovers are repealed and the committee will no longer process transactions involving equities nor impose conditions on such deals.

FIC will also no longer process property transactions, except where it involves dilution of bumiputera or government interests for properties valued at above RM20 million. Restrictions on foreign ownership of fund management companies and brokerages were also relaxed.

Najib in his speech said the FIC was no longer an effective instrument to support growth with equity. While the policy was practicable back then, Malaysia faces a completely different scenario today.

"Investment policies creating regulatory uncertainty and that are not in line with international practice will only constrain our growth potential — growth that will allow our distributional objectives to be achieved. Further, the dynamism and complexity of today's economy does not sit well with the blunt 'one-size-fits-all' approach of the FIC," he said.

Najib explained later to the media the two factors which brought about the recent reforms: firstly, the competitive global economic environment and secondly, FIC's failure to expand bumiputera equity ownership.

It is the government's belief that the easing of regulations will significantly enhance Malaysia's value proposition as a place to do business and invest.

"This is 20 years too late but better late than never. The PM is to be congratulated for his bold policy reform, but there's a long way to go still before we can become fully competitive in attracting investments from the cream of MNCs and other preferred investors," says

REUTERS

Najib: The dynamism and complexity of today's economy does not sit well with the blunt 'one-size-fits-all' approach of the FIC

Dr Lim Teck Ghee, CEO of the Centre for Policy Initiatives.

In 2006, Lim, then the director of Asian Strategic Leadership Institute's Centre for Public Policy Studies, was one of the authors of a controversial study on corporate equity distribution, which challenged the government's assertion that bumiputera equity ownership had stagnated at 18.9%.

Lim says many other countries are equally intent on attracting the right quality of capital inflows. In the present scenario of diminishing global and regional FDI flows in the short term, Malaysia will have to work doubly hard to attract investors.

Investors would also consider other factors before investing, namely the extent of government intervention and control, the country's commitment to an open environment for inward and outward FDI, human resources, government policies, key socio-economic policies and the civil service.

"The sad truth is that we have lost a great deal of our competitive edge and our reputation with local and foreign investors mainly due to archaic policies, an obstructionist civil service and the primacy of the Malay agenda. The only solution, if the government does not want to see FDIs dry up further, is to push through structural reforms faster," says Lim, adding that there is still a long road ahead and reform measures are needed in many other areas.

But at least the removal of the 30% bumiputera quota for Malaysian-based companies seeking listing here may compel them to list here rather than in Singapore or elsewhere, an investment banker says.

In the past, companies going for listing or an initial public offering (IPO) will have to meet both the Securities Commission's public spread requirement of 25% and the FIC's 30% bumiputera equity requirement. Effective last Tuesday, Malaysian-based companies going for listing are now required to only offer 50% of the public spread shareholding to bumiputera investors. The public spread of 25% remains.

This means that effectively, only a minimum 12.5% of a company's issued shares must be in bumiputera hands compared with 30% for the last 38 years.

"Generally, when listing requirements make it more onerous for owners to list, they will think twice about listing here. Previously, they may consider listing in Singapore or London. It's a way to retain local guys who want to list," he notes.

The investment banker is also pleased that the 12.5% bumiputera equity requirement is a one-time condition at listing; post-IPO, there will not be any equity condition imposed except in the case of reverse takeover (RTO) and backdoor listing.

"Previously, the company must top up if there's dilution in the bumiputera shareholding," he adds.

Top Glove Corp Bhd's chairman Tan Sri Dr Lim Wee Chai welcomes the changes.

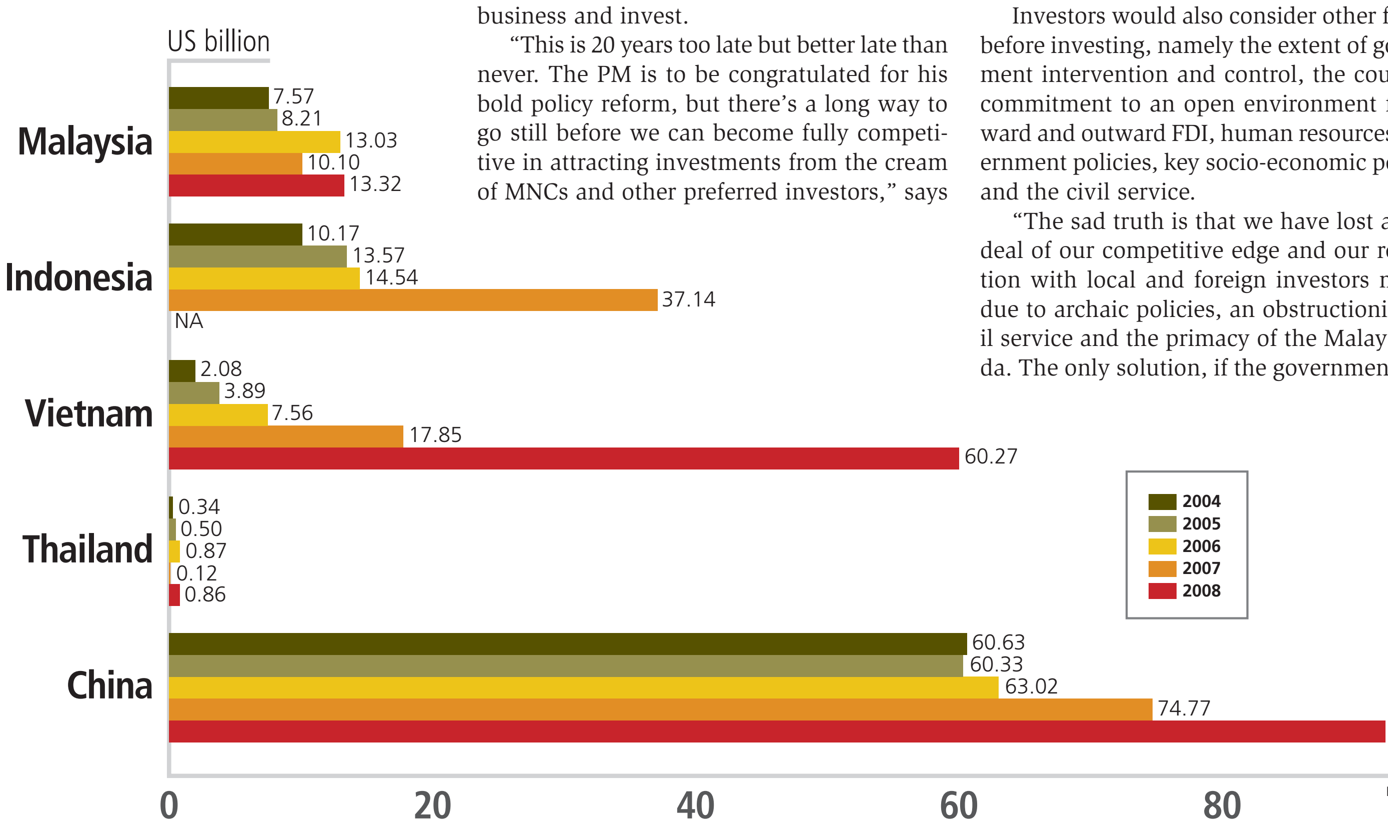
"Sometimes you want to do business, it must be as smooth and efficient as possible. While rules are necessary, make sure they are updated. From time to time, we need to change according to situation. It makes business easier and more efficient but with quality," he tells *The Edge*.

While business owners may be happy with the change, small time non-bumiputera investors, however, may be disappointed to know that their chances of being picked during the balloting process have been diminished under the new regime now that the balloting portion must be shared 50:50 instead of 30:70 as in the past. However, on the basis of the company's entire issued share capital, the minimum bumiputera equity share has come down from 30% to 12.5%.

Certain strategic sectors, however, will continue to be regulated by their respective sector regulators even though they will no longer be subjected to FIC rules. Companies in these sectors will continue to be subject to equity conditions imposed by the regulators. These regulators include Bank Negara Malaysia, the Energy Commission, Commercial Vehicles Licensing Board, National Water Services Commission, and Malaysian Communications and Multimedia Commission.

It is understood that this does not mean that the powers previously held by the FIC are transferred to the sectors' ministries or regulators. The regulators and ministries will still perform their roles as before.

The FDI race



BLOOMBERG

Is Ekuinas a better option?

As the sun sets on the Foreign Investment Committee (FIC), the 35-year-old panel that approves foreign investments in Malaysia, the government is establishing another institution known as Ekuiti Nasional Bhd or Ekuinas to promote genuine bumiputera participation in commercial activities.

Ekuinas is a private equity fund with an initial capital of RM500 million, funded by the government. In time, the fund size will be enlarged to RM10 billion. The fund will invest in high growth sectors, such as education, tourism and oil and gas.

Going forward, Ekuinas will be driven by two key principles: to be market-friendly and underpinned by commercial sense as opposed to the FIC's restrictive policies in the past, and to encourage meaningful and sustained bumiputera participation in commercial activities.

Prime Minister Datuk Seri Najib Tun Razak assured that participation of bumiputera through Ekuinas will be based on merit.

"We need a new instrument but the new instrument must be more market-friendly and in the process, we're embarking on a new philosophy which will help the good and the best bumiputera in business, not just any bumiputera but bumiputera who are willing to help themselves," added Najib, also the finance minister.

Ekuinas will invest in bumiputera entrepreneurs and unlisted companies while encouraging joint ventures between the bumiputera and non-bumiputera business communities. It will also facilitate mergers and acquisitions involving bumiputera-owned companies and other local and foreign entities with ready customer base.

The rationale behind Ekuinas is that the FIC, set up under the New Economic Policy (NEP), had failed to increase bumiputera equity participation. Also, the government finally recognised that FIC's archaic rules have no place in today's intense competition for foreign investments, which would help diversify the Malaysian economy and move it up the value chain.

The government believes this model would work in striking a balance between attracting foreign investors and addressing the need for a more effective instrument for bumiputera participation. The prime minister also maintained that the 30% bumiputera equity shareholding remains a "macro target" and Ekuinas is one of the measures to achieve that target along with other existing institutions, for example, the national unit trust schemes managed by Permodalan Nasional Bhd (PNB).

But is Ekuinas necessarily a better alternative in achieving the objective of fair distribution of wealth, compared to restrictive policies under the NEP? It must not succumb to previous trends of making the rich richer while neglecting those who genuinely need help but lack the connection to the right people.

BIG MONEY
BY **Jenny Ng**

As Ekuinas operates as a private equity fund funded by the government, how transparent will it be and can taxpayers be certain it will not be subject to abuse? Will its investments be made public? Even though it is a "private" equity fund, it should still be accountable to taxpayers who are effectively investors of the fund. The fact that the fund will invest in private companies may be another cause for concern. As such, generous information should be offered regarding these companies and entrepreneurs.

While it may be impractical to require Ekuinas to make public its every move, there has to be a mechanism in place to ensure minimal abuse of power and maximum transparency.

The concern is valid given the government's poor record in transparency when it comes to disclosing and reporting the performance of national investment arms.

PNB's annual report, for example, offers no details of its various investments in properties, fixed income securities and equities in terms of their geographical spread, sectors or returns. Khazanah Nasional Bhd releases its portfolio of listed companies at annual briefings but does not reveal its bottom line. ValueCap Sdn Bhd's financial statements are available on its website but do not offer details of the investments it made. What is available is the fair value of the investments.

Perhaps a leaf ought to be taken from Singapore's Temasek Holdings which discloses its financial statements along with detailed information of its investments by sector, geography and liquidity on its website and also offers information of the companies it invested in, providing details on when the investment arm bought into them, percentage held and the total return on the investment.

If Ekuinas, when it is set up, chooses to remain opaque in how it invests and allocates its funds, then it will no doubt attract criticisms that it is simply a tool to appease those who stand to lose from the liberalisation measures or that it is open to abuse by those in positions of power.

Malaysia is now on the cusp of either continued economic growth and diversification, or decline, if we do not get our investment policies right. While there are many more areas — not just within the economic sphere — where improvement will be needed, removal of restrictive policies that are not market-friendly is welcome indeed but care must be taken not to replace it with something even more onerous. E

In place of the FIC as an instrument to support growth with equity, the government is adopting a new approach via Ekuiti Nasional Bhd or Ekuinas, a private equity fund that will invest jointly with private sector funds in high-growth sectors. The participation of bumiputeras through Ekuinas will be merit-based, in order to promote genuine partnerships driven by commercial sense.

It is hoped that through Ekuinas as well as other institutions and policies, the macro target of 30% bumiputera equity ownership will be achieved. The government hopes that Ekuinas will have a more sustainable approach to capital retention among bumiputeras compared to the policies prescribed under the NEP. According to Najib, out of RM54 billion of equity allocated, only RM2 billion is still held by bumiputeras. Bumiputera equity ownership is currently 19.4%.

Lim, however, expresses concern over the move, which he likens to a political carrot dangled to appease Umno hardliners and possibly open to abuse. He adds that the use of public funds must be justified.

"The PM needs to practise the principles of full disclosure, transparency and accountability so as to avoid future setbacks and deviations to what has been intended. It would be scandalous and unacceptable if the RM10 billion goes mainly to support politically connected bumiputera companies. We do not need another gravy train to run, especially when the country is facing hard economic times," he says.

He is worried that by pouring money and resources into this programme, even greater inequality will be created.

"There are better ways of ensuring fairer distribution of the economic pie. Trying to build up a class of Malay businesses through special treatment has not worked in the past. This approach has also not worked anywhere in the world. But let's say that we succeeded after pouring hundreds of billions of dollars and other resources into this programme; still we will end up with even greater inequality and worse distribution rather than fairer distribution. Therein is the fatal contradiction and flaw in the government's main policy thrust," he adds.

The latest changes will be the second wave of liberalisation under Najib since he came into office in April. In the same month, bumiputera equity requirement was removed from 27 services sub-sectors and other liberalisation measures were announced for the financial sector.

"The devil is in the details and the execution, but surely in view of the time he has had in office, it's all looking very positive. I look forward to more deregulation," says Gerry Ambrose, head of Malaysian operations at Aberdeen Asset Management Sdn Bhd.

Economists, however, emphasised the need for follow-through execution and minimal economic dislocation.

Standard Chartered's economist Alvin Liew writes in a report on July 1 that while the steps taken are "measured and not the big-bang approach", Najib's willingness to tackle long-standing issues in a pragmatic fashion should improve investor confidence.

"But, at the same time, the measured approach taken should ensure no or minimal economic dislocations as the economy undergoes reform," he says.

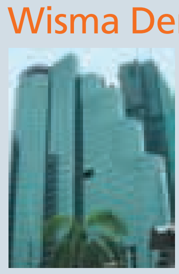
Lee Heng Guie, CIMB Research's head of economics research, notes that dependence on government investment, which is deficit-financed, will be unsustainable over the long term and detrimental to price stability. The liberalisation measures would give a boost to private domestic and foreign investments, accelerating the economic transformation necessary for Malaysia to move up the value chain. However, follow-through execution will be crucial. E

Deals blocked by FIC

Effective June 30, the approval of the Foreign Investment Committee (FIC) will no longer be required for property transactions except where there is a dilution of bumiputera or government interests for properties valued at RM20 million and above.

In the past, attempts by foreigners to acquire properties in Malaysia have been blocked by the FIC, attracting media attention to the country's restrictive investment policies.

Wisma Denmark



In 2006, Great Eastern Life Assurance (M) Bhd entered into a deal to purchase the 32-storey Wisma Denmark and the plot of land adjacent to the building for RM150 million. Kuala Lumpur's civil courts were once located in Wisma Denmark.

The building, located on Jalan Ampang, Kuala Lumpur, was then owned by bumiputera tycoon Tan Sri Ibrahim Mohamed and his family. Ibrahim also developed Menara Promet in Jalan Sultan Ismail.

The FIC rejected Great Eastern's application to buy the building and no reason was given. Great Eastern started its operations in Malaysia in 1908. The company is a wholly owned subsidiary of Singapore's Great Eastern Holdings Ltd, which is owned by the Oversea-Chinese Banking Corp Ltd.

Wisma Denmark was eventually sold to Sunway City Bhd for RM170 million in 2007.

Menara Lion

The building, now known as Menara Citibank and located on Jalan Ampang, could have been known by some other name if Citibank Bhd hadn't appealed against FIC's rejection of its acquisition.

In 1999, Citibank, through Menara Citi Holding Co Sdn Bhd, sealed a deal to buy 50% of Inverfin Sdn Bhd, which still owns Menara Citibank (then Menara Lion), from Amsteel Bhd. Amsteel owned 70% of Inverfin and the rest was held by Pidemco Land Ltd, a member of the Singapore Technologies Group (the stake is now owned by CapitaLand).

Amsteel is the steel-making entity of the Lion Group. The sale was part of the group's restructuring plan to pare down borrowings. The group completed the 50-storey Menara Lion in 1994.

Menara Citi Holding is a unit of US bank Citigroup.

At first, the FIC rejected the deal. Citibank appealed against the decision in 2000 and finally got the approval to purchase 50% of Inverfin a few months later. The 50% stake was sold for RM75.25 million in 2000.

Menara Citibank is going on the block again as Citigroup disposes of assets worldwide to shore up its position after being hit by the subprime crisis. The latest news is that Hap Seng Consolidated Bhd is bidding for the 50% stake. — *By Jenny Ng* E