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INSTITUTE FOR DEMOCRACY AND ECONOMIC AFFAIRS

Government-Linked Companies: Impacts on the Malaysian Economy

Executive Summary

In this policy paper "Government-Linked Companies: Impacts on the Malaysian Economy", Jayant Menon explores the impacts of GLCs on the Malaysian economy while reviewing the Government Transformation Programme and the role of GLCs in the affirmative action policies. The author examines the theory and evidence on the relationship between GLCs and private investment, to determine whether a crowding out effect is a reality or not. Using recent data, the paper finds that GLCs are crowding out the real private investment.

Besides preferential treatment that GLCs receive concerning government procurement, the author argues that they could also enjoy various other benefits, including direct subsidies, concessionary financing, state-backed guarantees, and exemptions from antitrust enforcement or bankruptcy rules. In contrast, private firms may be reluctant to invest in sectors where GLCs are dominant because they perceive the playing field to be skewed against them. This suggests a negative relationship between the share of GLCs in an industry and the rate of investment by private firms.

The author explains that GLCs serve as instruments of government's social policy, given the explicit role that they have been assigned to play in the affirmative action programme, in the past and present, for redistributing wealth towards the Bumiputera.

The paper cautions that GLCs might lead to an increase in inequality in Malaysia due to their designated role in the affirmative action policies. These policies may improve horizontal disparities, but they tend to worsen intra-group and vertical or overall inequality, the paper notes. This poses grim challenges for good governance within a political culture of patronage and where institutions can be manipulated.

The author argues that direct government spending on GLCs will lead to an increase in fiscal deficit which will be augmented by direct subsidies, concessionary financing, state-backed guarantees and the like. There has been a string of government bailouts over the years, resulting in a massive drain on the public purse. Hence, GLCs pose a fiscal burden to the country and result in a more expansionary budgetary position than would otherwise be the case.

The author hopes for a committed and legitimate programme of divestment as the only real solution. Commitment to divestment is admittedly complicated and requires a separate study focusing on much broader issues. But at a minimum, it would seem to require confronting vested interests and addressing the underlying political economy motivations that continue to provide a lifeline for GLCs and allowing them to flourish.

Jayant Menon, is the Lead Economist (Trade and Regional Cooperation) Office of the Chief Economist and Director-General, Economic Research and Regional Cooperation Department Asian Development Bank

Jayant Menon, PhD in International Economics from University of Melbourne is a member of the Asia and the Pacific Policy Society, an adjunct fellow at Crawford School of Public Policy, The Australian National University and Lead Economist at the Office of Regional Economic Integration, Asian Development Bank.

As Lead Economist in the Office for Regional Economic Integration at the Asian Development Bank, he works on trade, international investment and development issues, and leads the Trade Team. He holds adjunct appointments with the ANU Crawford School of Public Policy, University of Nottingham, UK and Cambodian Institute for Cooperation and Peace, and serves on the Advisory Board of the University of Nottingham Campus in Malaysia.