

MAY 2018

BRIEF ON MALAYSIAN ELECTION



Malaysia's Opposition Coalition, Pakatan Harapan (PH), led by 93 year-old former Prime Minister Tun Dr Mahathir has won the General Election held on 9 May 2018. This is the first time since independence in 1957 that Malaysia will be led by a party other than the UMNO-led coalition. This is a considerable achievement for PH as there appears to have been a substantive campaign by the BN led incumbent government to prevent PH from campaigning fully by not giving opposition time on state-run television, for example, as well as such actions as a mid-week voting day, difficult postal voting conditions, electoral gerrymandering and more.

But reports of crowds of 10-25 thousand attending the opposition rallies, organized in large part by social media, appears to have circumnavigated the government's efforts to dilute the opposition message, and those rallies have been backed up by high turn out rates at the voting booth – this appears to have been key to PH's victory.

The Election Commission announced the results at 2am and the overall result of was confirmed by the Chief Secretary of State who also announced that Malaysia will have two public holidays on 10-11 May to make way for the swearing in ceremony and the formation of a new cabinet of ministers. BN has said it will "respect the will of the people", with PM Najib attending a press conference as scheduled and conceding defeat.

PH NOW THE GOVERNMENT

Pakatan Harapan has won 121 parliamentary seats (112 are needed to form the government), BN 79 and PAS 18. Eight former ministers and 19 deputies have lost their seats. Pakatan Harapan/DAP/PKR have also kept control of Penang, Selangor, and won in Melaka, Kedah, Johor and Negri Sembilan states. The win in Johor and Negri Sembilan is especially noteworthy given these have been the stronghold of UMNO (the key component party in BN) and has a huge proportion of Federal Land Development Authority (FELDA) settlements that historically has been aligned to UMNO/BN. BN has been reduced to two state

governments; Perlis and Pahang. The Islamic Party (PAS) has kept control of Kelantan and won Terengganu. Perak and Sabah are hung states and Sarawak held only parliamentary elections.

One downside is that PH's narrow margin of victory will likely leave it vulnerable to defections and it will also have to negotiate with the other parties to form a coalition. That said, defections can work both ways – some BN MPs may also switch sides to PH.

Mahathir helms an unwieldy four-party coalition that includes Malaysia's largest ethnic Chinese party, and he plans to step aside once de facto opposition leader Anwar Ibrahim gets out of jail (Mahathir said he would seek a pardon for Anwar). "I have to manage four presidents of four different parties," Mahathir has said. "It's going to be a headache." Mahathir has pledged to set term limits for prime minister and reduce its power, while promising to scrap the GST within 100 days in power. It's uncertain whether the outcome will fundamentally reshape race relations in Malaysia. Najib's party BN had long staked its legitimacy on providing preferential treatment for the bumiputera, or "sons of the soil," which include ethnic Malays and indigenous groups.

The market consensus view was for a straightforward victory for PM Najib and BN. An opposition victory is viewed with caution given its populist tilt with promises of the abolishment of GST, and the return of subsidies which, if implemented, could widen the fiscal deficit and weaken the

ringgit. Hence the sentiment for the short term is likely to be risk-off and indeed the MSCI-based Malaysia ETF fell 6% in overnight trading in the US while the ringgit also sold off when results first came through before recovering slightly. This indicates the sell off may have run its course for the short term.

POLICY IMPLICATION

The Central Bank meeting will still be held today, 10 May. This election result is likely to be negative for economic growth in the short term as policy uncertainty may dampen private sector investment and the political transition may disrupt public sector spending. This will likely support Bank Negara Malaysia leaving its policy rate unchanged in the near term.

The fiscal consolidation agenda could be at risk – while PH in its manifesto pledges to keep the budget balanced, risks such as the removal of GST and return to fuel subsidies could be negatives for the credit rating agencies. Indeed, Moody's has published a negative note on the Malaysia economy citing the lack of clarity in Mahathir's policies and pointing out the return of subsidies would be credit negative.

Election pledges could raise fiscal deficit by around 0.4% of GDP if implemented in mid-August (100 days after elections) with a possible knock-on impact on sovereign ratings given Malaysia's relatively high debt for an A-rated economy.



There are also unanswered questions over whether Mahathir will break the new links with China (he has already mentioned he will “review projects”) as well as new question marks on relations and planned projects with Singapore. Mahathir was known in the past for his sour relationships with Singapore. The PH coalition may consider reviewing the High Speed Rail link agreements between KL and Singapore as promised during the election campaign.

SHORT-TERM UNCERTAINTY, LONG-TERM GAIN

However, there is a train of thought that this is positive for the long term. Although there is likely to be a period of adjustment, PH’s commitment to good governance and it does have governing experience in various states, while of course Dr Mahathir was prime minister for 22 years. There is also no lack of next generation leaders who are young, smart and very capable in Malaysia.

In summary then, there is likely to be

a short-lived period of uncertainty in the markets, offset by the KL bourse being closed until next Monday. Medium term, more political maneuvering is likely given the un-declared status of opposition figure Anwar Ibrahim while in the long-term, this result increases the chances that Malaysia will undertake economic reforms that are needed to raise growth rates. There is, however, much to fix. Government institutions appear weakened by decades of weakened governing, electoral gerrymandering and interference in the judiciary. This will take time.



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