# CHAPTER 2

# THE DEVELOPMENT OF PUBLIC SECTOR PRIVATISATION: THE MALAYSIAN AND SINGAPOREAN EXPERIENCES

## 2.0 Introduction

Privatisation is the process of change of ownership and control. Differences in approach and outcomes are the prime reasons for this special evaluation study, namely, to provide a more comprehensive understanding of privatisation, and guidance on how the privatisation should be managed. The objective of this chapter is to provide an understanding of how privatisation has led to new ownership structures in Malaysian and Singaporean companies. This chapter begins with a discussion of the development of privatisation in the world. The discussion is then followed with a description of the process of introducing and transforming the public sector in Malaysia and Singapore to private companies, but which the government still owns and controls. In discussing the success and failure factors of privatisation in the two countries, the importance of government involvement is highlighted – not only in the efficiency of its involvement in state ownership enterprises, but also in its participation, which is more equitable.

## 2.1 Privatisation in Malaysian Public Sector Enterprises

### 2.1.1 Introduction

The Malaysian Government was among the first developing countries that embarked on privatisation programmes in Asia. A number of factors and events led to the creation and expansion of the public enterprises in Malaysia. This part will briefly explain the problems associated with the expansion of the public sector, including the reasons for the reversal of this policy. An overview of the privatisation programme in Malaysia is also presented.

### 2.1.2 New Economic Policy

The main objective of the New Economic Policy (NEP) was to achieve national unity by 'eradicating poverty' irrespective of race and 'restructuring society' to achieve inter-ethnic economic parity between the predominant Malays (Bumiputra) and the predominant Chinese. This policy was announced in 1971 under the Second Malaysia Plan (SMP).[2] Two major objectives of NEP were: (i) to eradicate poverty regardless of race and (ii) restructure society by eliminating the identification of race with economic function. However, the ultimate objective was to redistribute wealth more equally among the Malaysian society.[3] The Government aims to achieve the goals of the NEP on the basis of economic growth. The attention given to eradicating poverty had broad support for the NEP. It seemed that the NEP had responded well to the problems of poverty, unemployment, and inter-ethnic economic imbalances that emerged before May 1969.

The NEP will lead to a different ownership structure in Malaysian listed companies. Its objective is to make sure that Bumiputras hold at least 30% of the equity stake, and that the structure of ownership in public listed companies will be changed with Bumiputra involvement in companies. The Government, through GLCs led by Khazanah aims to achieve NEP targets by ensuring that the Bumiputras, especially the Malays, will not be left

[2] The Second Malaysian Plan (SMP) carried out in 1971-1975.
[3] In restructuring of society, a part of the objective was to provide the Bumiputra a largerportionof the economy, which was hitherto dominated by the Chinese (Jayasankaran and Hiebert, 1997).

out and that they are able to compete with others such as the foreigners and the economically powerful Chinese.

As mentioned earlier, the major objective for introducing the NEP was to balance wealth between the ethnic Malays and others, especially the Chinese, therefore, this policy aims to create a much larger Malay business community. According to Permodalan Nasional Bhd (PNB) or the National Equity Corporation, in 1972, 62 percent of corporate assets were owned by foreigners, 34 percent by non-Malays, and 4 percent by Bumiputras (Jomo, 1993). The purpose of setting up the NEP was to target an equity ownership level of 30 percent for foreigners, 40 percent for non-Malays, and 30 percent for Bumiputras, to be reached by 1990. To achieve the NEP objectives, the Government increased state intervention, public sector expenditure, and ensured economic growth based on export-oriented industrialisation.

The main feature that was highlighted in the NEP as ‘restructure society’ was to expand the Malay ownership of equity. Since the 1950s, efforts had been made to encourage Malay participation in the ‘modern’ industrial and commercial sectors of the economy, mainly dominated by foreign and non-Malay entrepreneurs, through the establishment of the Rural Industrial Development Authority (RIDA). However, such efforts failed to increase the ethnic composition of the ownership and control of economy (Jomo, 1993).

PNB, one of the GLICs was conceived as a pivotal instrument of the Government's New Economic Policy to promote share ownership in the corporate sector among the Bumiputra, and develop opportunities for suitable Bumiputra professionals to participate in the creation and management of wealth. Prior to the establishment of PNB, efforts to increase Bumiputra ownership in the corporate sector were not sufficient as shares allocated to individuals were seldom retained. Research indicated that when Bumiputra shareholders sold their shares, the profits generated were consumed and not reinvested. Consequently, wealth distribution mechanisms, such as Amanah Saham Nasional (ASN) and Amanah Saham Bumiputra (ASB), were introduced providing opportunities for the Bumiputra to invest their money in various portfolio investments. The dividends paid by the ASN, and later the Amanah Saham Bumiputra (ASB), have been in the range of 12% to 18% per annum. The average annual returns on investments offered by the ASN and ASB have been extremely high compared to the commercial bank's average fixed deposit rate of 3.5% per annum over the corresponding period, that is, during the NEP decades (Malaysian Business, 2006).

Through PNB, substantial shares acquired in major Malaysian corporations from funds provided by Yayasan Pelaburan Bumiputra or Bumiputra Investment Foundation were transferred to a trust fund and sold to the Bumiputra in the form of smaller units. By employing this innovative investment model, PNB ensures that these shares are retained, resulting in the cultivation of widespread saving habits, and the development of entrepreneurship and investment skills of the Bumiputra. With funds under management totalling about RM150 billion, the PNB Group is the country's leading investment institution with a diversified portfolio of interests that include unit trusts, institution property trust, property management and asset management(Malaysian Business, 2006).

The restructuring policy involved state intervention to increase Malay ownership of the economic activities by developing large public enterprises, ostensibly on behalf of the Malays. The Government also tried to endorse Malay businesspersons through budget allocations to existing agencies relevant to promoting business activities by the Malays, such as institutions that include MARA (Majlis Amanah Rakyat) and the Council of Trust for Indigenous People. Various other public enterprises such as PERNAS (Perbadanan Nasional Berhad) and UDA (Urban Development Authority) were established to achieve the policy objectives. Regional development authorities like MADA (Muda Agriculture Development Authority) and KADA (Kemubu Agriculture Development Authority) were also set up. In addition, a State Economic Development Corporation (SEDC) was set up in every state (Jomo, 1990). These public corporations are either wholly owned by the Government or joint ventures mainly involving foreign partners, and have become large business entities involved in various activities.

### 2.1.3 Growth of Public Enterprises in Malaysia

Public enterprises in Malaysia evolved with the changing nature of the State and the dominant interest groups. Before the 1950s, these enterprises were largely limited to infrastructure and utility provisions, in the form of government departments and agencies as well as statutory bodies. Public enterprises with the redistributive objectives were also set up in the early and mid-1950s. Some of these institutions include the Rural Industrial Development Authority (RIDA), the Rubber Replanting Fund Board, and the Federal Land Development Authority (FELDA) (Jomo, 1993).

From the late 1950s, after Independence, other public enterprises were set up to promote new economic activities, especially import-substituting manufacturing. Some of these institutions included the Federal Industrial Development Authority (FIDA) and the various state economic development corporations (SEDCs). By 1957, the year of Independence, there was already 29 public enterprises in Peninsular Malaysia. In the next 12 years, up to 1969, 54 more public enterprises were established. In the following four years (1969-1972), 67 new public enterprises were set up. Between 1972 and the early 1980s, the establishment of public enterprises gained greater momentum as such enterprises were profile rated in Malaysia (Mohamed, 1995).

After Independence, SOEs grew speedily due to Government involvement in business activities. The public sector ventured into commercial and industrial enterprises. At the time, the "government-in-business" strategy was implemented and was manifested mainly in the following forms (Mohamed, 1995):

1. By establishing new companies with the Government as sole owner.
2. By setting up joint-venture companies with private entrepreneurs as part owners.
3. By buying a portion of public-traded shares of existing companies.

With its commitment to the New Economic Policy (NEP) objectives, the Government became directly involved in many economic activities. Up until the 1980s, the Government continued to invest in various new economic activities. However, the Government prioritised its investment in capital-intensive heavy industries in the early 1980s. By 1979, the Government had shares in 557 companies. All but 10 were private limited companies, i.e.

their shares were not traded on Bursa Malaysia (Mohamed, 1995). Although different sectors were involved, the highest number of public enterprises was found to be in the manufacturing and service sectors. By the end of the 2005, there were 1,253 public enterprises. Table **2.1** shows the growth of public enterprises from 1970 to 2005.

**Table 2.1: Number of Public Sector Enterprises in Malaysia**

| Industry | 1970 | 1975 | 1980 | 1985 | 1992 | 2000 | 2005 |
|---|---|---|---|---|---|---|---|
| Agriculture | 10 | 38 | 83 | 127 | 146 | 157 | 162 |
| Building & Construction | 9 | 33 | 65 | 121 | 121 | 125 | 129 |
| Extractive Industries | 3 | 6 | 25 | 30 | 32 | 39 | 43 |
| Finance | 17 | 50 | 78 | 116 | 137 | 142 | 150 |
| Manufacturing | 40 | 132 | 212 | 289 | 315 | 321 | 336 |
| Services | 13 | 76 | 148 | 258 | 321 | 334 | 339 |
| Transport | 17 | 27 | 45 | 63 | 68 | 74 | 78 |
| Others | 0 | 0 | 0 | 6 | 9 | 12 | 16 |
| Total | 109 | 362 | 656 | 1010 | 1149 | 1204 | 1253 |

Source: Economic Plan Unit, 2007

### 2.1.4 Performance of State-Owned Enterprises (SOEs)

In the early 1970s and 1980s, public sector investment increased substantially when the government was implementing NEP. In spite of the Government's extreme investments, the rapid expansion of the public sector under the NEP led to a bloated bureaucracy, inferior services, inefficiency, low productivity, high costs, and limited innovation. Gomez and Jomo (1997) acknowledged a number of factors contributing to the poor performance of public enterprises. The inefficiencies of the managers and lack of objective evaluation of the enterprises are among the factors that have been recognised.

Managers of public enterprises in Malaysia are expected to maximize several, often conflicting objectives. In addition to efficiency and productivity, they are also expected to fulfil certain social goals that are usually associated with NEP. Such mixed objectives tend to undermine the efficient and profitable operations of these entities. Another factor is that these organisations lack proper systems or criteria to evaluate and prioritise the objectives. Furthermore, very little monitoring was exercised by their government financiers, especially when funds were readily available before the fiscal and debt crisis of the mid-1980s (Jomo and Ng 1996).

Consequently, public enterprises in Malaysia lacked a competitive spirit, which then affected the profitability of these companies. This, in turn, led to poor performance of many public enterprises. The poor financial performance and wastage of investment resources increased the fiscal burden of the Government and reduced economic growth. For example, in 1984 the Minister of Public Enterprises only reported the annual returns of 269 out of a total of

900 public enterprises and their accumulated losses amounted to RM137.3 million (Arif and Abu Bakar 1999).

From 1980, the country's attention was more on foreign loans to find a way out of the recession. Malaysia's public sector foreign debt grew from RM4.9 billion in 1980 to RM28.5 billion in 1987. Total public sector borrowings, including loans from domestic agencies increased from RM26.5 billion in 1980 to RM100.6 billion in 1986 (Jomo, 1990). In 1983, two-thirds of total government debt expenditure on public enterprises was attributed to only 27 out of over 1,000 public enterprises (Khoo KJ, 1992). By 1987, public enterprises accounted for more than one third of the public sector's outstanding debt and more than 30 percent of total debt servicing (Jomo, 1990).

### 2.1.5 "Malaysia Incorporated"

To improve relations between the private and public sectors, the "Malaysia Incorporated" concept was introduced. This policy reversal associated with NEP woes was also in response to the criticisms and complaints by the business community against the NEP that included impositions by the Government (Ariff and Semudram, 1987). Another important factor was that the NEP inter-ethnic economic redistribution mainly benefited the Bumiputra middle and upper income groups rather than the Bumiputra poor. Thus, it was anticipated that further continuation of NEP policies would widen the gap between lower income and high income Bumiputras (Mohamed, 1995).

"Malaysia Incorporated" was launched in 1983. This term was adapted from a pejorative term "Japan Incorporated", which emerged in the industrial West in the face of what it considered as 'unfair' competition from the more strongly state-backed Japanese business interests (Lee, 1995). The essence of this idea was that Malaysia would be run as a single business corporation with the private sector helping the country's growth and expansion. At the same time, the public sector would provide the support vital for the success of the corporation.

In Malaysia, the slogan has come to refer to efforts to curtail and rectify 'excesses' associated with the over-zealous implementation of the NEP, especially by Malay bureaucratic elements, and resented by the mainly Chinese business interests (Jomo, 1993a). The policy seemed to have diminished significantly by the mid-1980s.

### 2.1.6 Privatisation in Malaysia

Privatisation, spearheaded by the British and the US Governments in the early 1980s, became a fashionable economic policy around the world. Among the developing countries, Malaysia was one of the first to start its privatisation programme (Mohamed,1995). Privatisation in Malaysia was officially inaugurated in March 1983 with the pronouncement of the "Malaysian Incorporated" concept on 25 February 1983. The two main reasons in favour of privatisation are:

1. Growing disillusionment with the performance of SOEs.
2. Reassessment of the role of the NEP.

### 2.1.7 Privatisation Master Plan

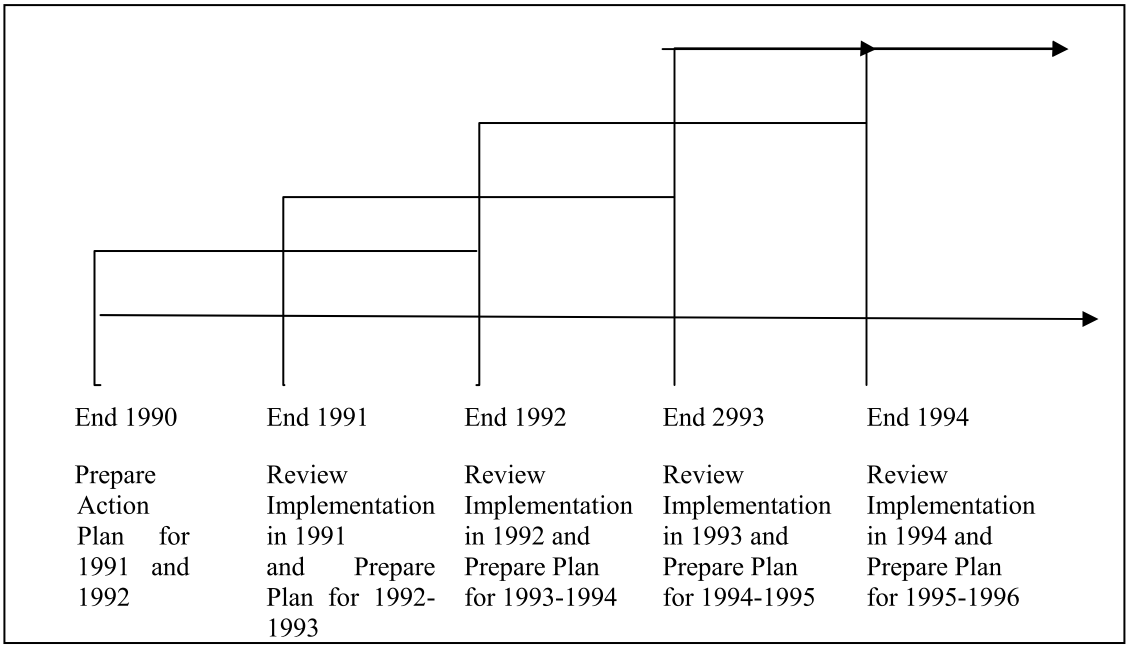
Since the formation of the privatisation policy in 1983, the Government has published statements from time to time to explain to the public the intention and content of the policy and to inform them of the latest developments.

In February 1991, the Malaysian Government published the “Privatisation Master Plan”. The main purpose of this document was to explain to the public that this master plan has been drawn up by the Government to provide guidelines concerning the implementation of the privatisation policy. This can be regarded as one of the four major documents issued in 1991 outlining the Malaysian economic development policy for the foreseeable future. The other three being “Vision 2020”, Outline Perspective Plan 1991-2000, and the Sixth Malaysia Plan 1991-1995.

### 2.1.8 Privatisation Action Plan

To achieve policy objectives, the Government formulated a Privatisation Action Plan (PAP). This is to ensure that privatisation efforts are channelled to appropriate priority areas. The PAP consists of a two-year “rolling plan” which is to be reviewed at the end of each year to identity the targets for privatisation and for preparation of the eventual privatisation the following year. This yearly review is to take stock of the progress being made to determine the entities to be privatised in the next two years. A rolling action plan is illustrated in Figure 2.1.

**Figure 2.1: Rolling Privatisation Action Plan in Malaysia**

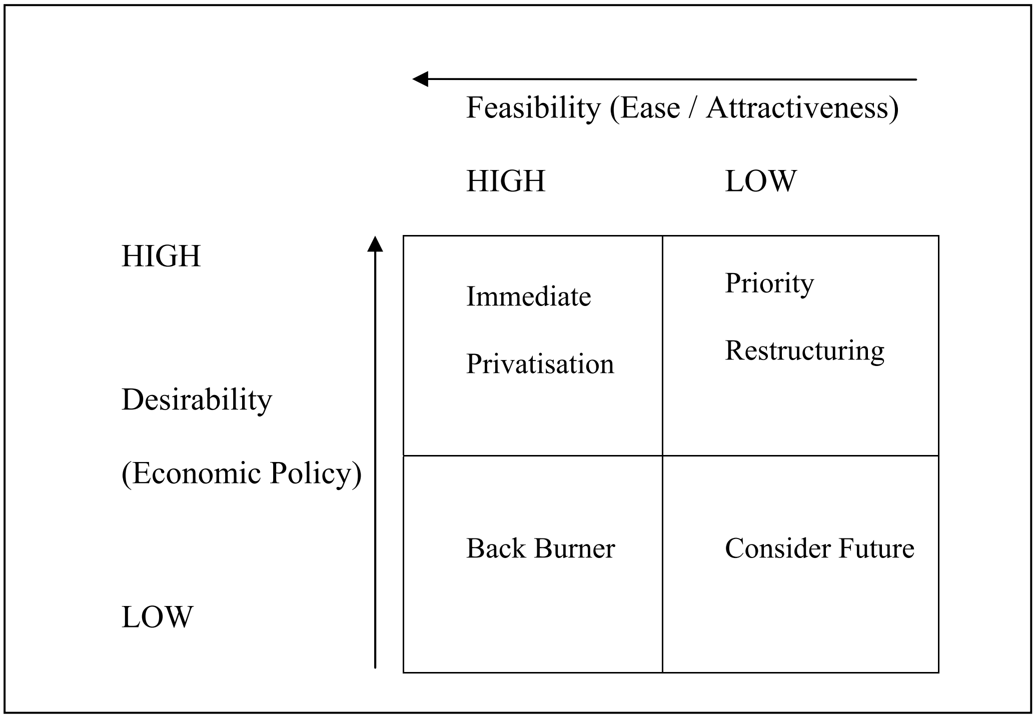



Source: Economic Planning Unit, 1991.

A number of factors were taken into consideration in order to prepare the PAP. The most important criteria in determining priorities are the feasibility and desirability of the SOEs. Feasibility is determined by two factors, the ease of privatisation, and the attractiveness of the company to the private sector. The attractiveness is determined primarily by its competitive market position, growth potential, and financial profile. The desirability seems to be defined by the Government perception of private sector superiority.

A combination of the two is portrayed through a privatisation grid in Figure 2.2.

**Figure 2.2: Privatisation Grid**




*Source: Economic Planning Unit, 1991.*

The SOEs are evaluated based on the feasibility and desirability criteria. The privatisation grid distinguishes four categories. Immediate privatisation candidates are the ones in high rank – easily privatised and attractive to the private sector (feasibility) and are of high priority (desirability). Priority restructuring are the candidates that rank high in terms of objectives, but are either difficult to privatise or unattractive in the present form. Back-burner candidates are feasible for privatisation, but the benefits of privatisation are less evident. "Consider future" category consists of the entities that are both low in desirability and feasibility.

The PAP identifies six different categories of entities for privatisation requiring different treatments. They are:

(i) **Flagships** are SOEs that are of national importance in terms of size and complexity, and, thus, merit special treatment. Flagship companies include organisations such as Tenaga Nasional Bhd and Telekom Malaysia Berhad.

(ii) **Easily Privatisable**are mainly government companies (government majority owned entities) already operating in competitive environments like the private entities and often have commercialised operations.

(iii)**Restructuring Candidates** are unprofitable companies operating in competitive commercial environments that need financial and operating restructuring. However, the Government needs to minimise pre-privatisation restructuring, which usually involves financial injections.

(iv)**Services** refer to organisations previously protected from commercial competition, such as training, health services, veterinary services, and research companies that are to be deregulated and privatised in the interest of consumers.

(v) **Listed and Minority Holdings** are those that are to be given low priority since the private sector in these entities are already substantial.

(vi)**New Projects** usually involve infrastructure that isto be privatised by way of BOT (build, operate and transfer) or BO (build and operate).

For implementation purposes, the PAP distinguishes between those *ready* for privatisation from those requiring privatisation. Most flagships require preparatory work, as they are still either a government department or a statutory body.

### 2.1.9 Method of Privatisation

Privatisation in Malaysia, as in most of the other countries, has primarily involved divestment of SOEs by using various methods. In some cases, public enterprises had been corporatized before divestment through public listing. Under this process, the status of the enterprises would be changed to a public limited company, with the Government still retaining ownership. This helped to ascertain the public enterprises' financial position to introduce managerial reforms and to make the company more "marketable" for launch in the stock market (Jomo, 1991).

Between the launch of the privatisation programme in 1983 and 2005, 376 projects were privatised. The methods of implementing and the total number of privatisations are given in Table 2.2. Of all the modes, the most common is Sales of Equity, 29.26 percent followed by Sales of Assets, 18.35 percent. The other two common methods are "Build-Operate-Transfer" and "Build-Operate-Own": 13.56 percent and 9.84 percent, respectively.

**Table 2.2: Malaysian Privatisation Project Including Methods 1983-2005**

| Method | 1983-90 | 1991-95 | 1996-2000 | 2001-2005 | Total |
|---|---|---|---|---|---|
| Sale of Equity | 4 | 94 | 11 | 1 | 110 |
| Sale of Assets | 3 | 33 | 32 | 1 | 69 |
| Build,Operate, Transfer | 9 | 21 | 15 | 6 | 51 |
| Build, Operate, Own | 1 | 18 | 13 | 5 | 37 |
| Corporatisation | 1 | 13 | 9 | 10 | 33 |
| Management Contract | 5 | 9 | 11 | 6 | 31 |
| Lease of Assets | 2 | 6 | 3 | 1 | 12 |
| Management Buy Out | 2 | 5 | 7 | 0 | 14 |
| Build-Transfer | 0 | 5 | 0 | 2 | 7 |
| Sale of Assets and Leasing | 2 | 0 | 0 | 1 | 3 |
| Public Listing | 7 | 0 | 0 | 3 | 10 |
| TOTAL | 9 | 204 | 101 | 35 | 376 |

*Source: Mohamed 1995, 1995, Seventh Malaysia 1996-2000, Eighth Malaysia Plan 2001-2005 and Ninth Malaysia Plan 2006-2010*

### 2.1.10 Achievements

Privatisation has played a fundamental role in reform programmes aimed at achieving higher levels of microeconomic efficiency and fostering sustained economic growth in both the developed and developing countries. In Malaysia, 56 privatised companies were listed on Bursa Malaysia by the end of 2006. The listing of the privatised companies on Bursa Malaysia contributed RM260 billion or 34 percent of the total market capitalisation, as at 30 December 2005, as shown in Table 2.3.

**Table 2.3: Paid-Up Capital and Market Capitalisation of Malaysian Listed Privatised Companies as at 30 December 2005**

| | Number of Companies | Paid-Up Capital (RM million) | Market Capitalisation (RM million) |
|---|---|---|---|
| Listed Privatised Companies | 56 | 36,032 | 260,000 |
| Total Companies Listed | 1049 | 283,717 | 755,555 |
| Percent of Listed Privatised Companies | 5.3 | 12.9 | 34 |

Source: Ninth Malaysia Plan 2006-2010

The privatisation programme reduced the financial and administrative burden of the Government, as shown in Table 2.4. During the planning period (2001-2005), the government continued to benefit from the privatisation programme in terms of savings in capital expenditure amounting to RM28.6 billion, of which 81.5 percent was from the electricity, gas, and water sector, followed by the construction sector at RM3.7 billion or 12.8 per cent. The Government also benefited in terms of proceeds from the concessionaires through the sale of assets and equity, generating RM21.7 million and RM40.5 million, respectively, as shown below. A total of 6,249 employees were transferred to the private sector, reducing the government administrative burden as well as generating savings in operating expenditure.

**Table 2.4: Proceeds, Savings, and Reduction in Malaysian Public Sector Employment**

| Item | 1983-2000 | 2001-2005 | Total |
|---|---|---|---|
| **Proceeds (RM million)** | | | |
| Sale of Assets | 1,514.8 | 21.7 | 1,536.5 |
| Sale of Equity | 4,299.7 | 40.5 | 4,940.2 |
| **Savings (RM million)** | | | |
| Capital Expenditure[1] | 125,356.9 | 28,603.9 | 153,960.8 |
| Operating Expenditure | 7,620.2 | 126.9 | 7,747.1 |
| **Number of Public Sector Employees Transferred** | 106,971 | 6,249 | 113,220 |

*Source: Economic Planning Unit, 2006*
*Note:[1] based on estimated project cost*

Concerning Bumiputra participation, the policy requiring at least 30 percent equity of Bumiputra entrepreneurs in privatised projects continued to be strictly implemented. Based on the overall equity ownership of the 35 companies approved to implement privatised projects during the planning period, Bumiputras had a controlling interest in 24 companies. However, in terms of par value of the shares, Bumiputras only owned 17.2 per cent of the equity, as shown in Table 2.5. This was largely due to the higher level of the paid-up capital held by the Government in some of these companies.

**Table 2.5: Equity Ownership of Privatised Entities upon Malaysian Privatisation, 2001-2005**

| Equity Ownership | Par Value | |
|---|---|---|
| | RM million | % of Total |
| Government | 309.3 | 74.7 |
| Bumiputra | 71.3 | 17.2 |
| Non-Bumiputra | 21.4 | 5.2 |
| Foreign | 12.1 | 2.9 |
| Total | 414.1 | 100.0 |

*Source: Economic Planning Unit, 2006*

Meanwhile, Bumiputra equity ownership reflected an increase from 32.7 per cent upon privatisation to 51.7 per cent at the end of 2005, as shown in Table 2.6. In absolute terms, Bumiputra ownership of the share capital at par value increased from RM5.5 billion upon privatisation to RM14.9 billion in 2005.

**Table 2.6: Equity Ownership of Privatised Entities in Malaysia**

| Equity Ownership | Upon Privatisation Par value RM million | % of Total | December 2005 Par value RM million | % of Total |
|---|---|---|---|---|
| Government | 8,584.40 | 50.70 | 9,013.80 | 31.20 |
| Bumiputra | 5,535.60 | 32.70 | 14,901.50 | 51.70 |
| Non-Bumiputra | 1,510.50 | 8.90 | 2,573.00 | 8.90 |
| Foreign | 1,303.40 | 7.70 | 2,368.50 | 8.20 |
| Total | 16,933.90 | 100.00 | 28,856.80 | 100.00 |

*Source: Economic Planning Unit, 2006*

### 2.1.11 The Financial Crisis

It is widely believed that the so-called "Asian Financial Crisis" was triggered in July 1997 by the speculative attacks on the Thai Baht, due to concerns of a decline of exports and fall in asset prices in Thailand (Wiwattanakantang, 1999). This resulted in investor perception of similar risks in other economies of the region. However, many economists are still divided on what really triggered the financial crisis.

The general erosion in investor confidence and the deterioration in market sentiments, in turn, triggered a sudden and massive reversal of short-term capital flows and a series of downward adjustments in regional currencies and stock markets, including Malaysia. The Malaysian currency (Ringgit) lost about 40 percent of its value within a year. Bursa Malaysia, known as the Kuala Lumpur Stock Exchange (KLSE) Composite Index, declined by 44.9 percent during the period between 1st July 1997 and 31st December 1997 (Okposin and Cheng, 2000).

The Malaysian economic growth, in terms of Gross Domestic Product (GDP) contracted. The impact of the crisis became evident towards the end of 1997, when the real GDP began to slow down and registered a negative growth beginning the first quarter of 1998(Economic Planning Unit, 1999). Private investment also contracted, mainly due to uncertainties arising from volatile exchange rates, a decline in both domestic and foreign demand, existence of excess capacity and the tight liquidity position encountered since the beginning of the financial crisis. The growth in private consumption and investment were far below what had been anticipated. The output of all sectors was also severely affected, with agriculture and construction sectors experiencing a contraction during 1996-1998 (Economic Planning Unit, 1999).

The impact of the economic downturn on share prices and corporate performance also severely affected the share of Bumiputra ownership in the corporate sector in 1998, which fell below the 1995 level. Reflecting the overall effects of the slowdown in the business activities of all Malaysians, the share of Chinese ownership also declined, while the Indian share remained at the 1995 level (Okposin etal., 2000).

The financial crisis affected the whole economy and disrupted the achievement of socio-economic targets, with the incidence of poverty increasing in 1998 after a sustained period of decline and the limited progress achieved in terms of equity and employment restructuring (Economic Planning Unit, 1999). With the deepening of the crisis, the real sectors of the economy came under pressure. The decline in output was evident in all major sectors including the privatised companies, due to the weaker demand from domestic and external markets. This is highlighted when performance of the privatised companies are analysed.

The introduction of the New Economic Policy (NEP) by Malaysian Government in 1970 was to encourage rapid economic growth in all sectors of the national economy, promote private entrepreneurship – especially among representatives of poor communities – and support small and medium-sized businesses. It was also intended to attract foreign investment, especially in modern technologies, by offering cheap and well-trained labour. Another unique aspect of this NEP was that the government made major efforts to redistribute wealth. The NEP recognized the need for radical social change and aimed to improve living conditions, economic power, and access to education and social benefits for the Malays and indigenous people. These groups, called Bumiputra (sons of the soil), received privileged access to public services, were granted land rights and preference in education and training, and benefited from job quotas in the public sector. This programme was successful, and

Malaysia achieved impressive economic growth, especially during the late 1970s, and throughout the 1980s.

In Malaysia, privatisation has played a fundamental role in reform programmes aimed at achieving higher levels of microeconomic efficiency and fostering sustained economic growth in both the developed and developing countries. The Malaysian government introduced two privatisations–Privatisation Master Plan and Privatisation Action Plan – to make sure that the objectives of privatisation in Malaysia could be achieved. This programme reduced the financial and administrative burden of the Government in handling state-owned enterprises.

The introduction of a 20-year programme by the Malaysian government called the New Economic Policy (NEP in 1970) was intended to encourage rapid economic growth in all sectors of the national economy, promote private entrepreneurship – especially among representatives of poor communities – and support small and medium-sized businesses. The NEP recognized the need for radical social change and aimed to improve living conditions, economic power, and access to education and social benefits for the Malays and indigenous people. As a result, this programme was successful, and Malaysia achieved impressive economic growth, especially during the late 1970s, and throughout the 1980s until 1997.

Table 2.7: A Summary of unique features of Malaysian Privatisation Experience

| **Malaysia: Experience in Privatisation** |
|---|
| 1. The introduction of NEP increase Bumiputra owned equity of private entities from 4 percent in 1972 to 20% (2005)<br>2. "Malaysia Incroporate" (1983) was launched for Malaysian can run as single business corporation with private sector helping the country's growth and expansion and lead Malaysia to become developed country in 2020 (Vision 2020)<br>3. The introduction of GLCs lead by Khazanah will handling and controlling companies to perform better and at same time to economic growth.<br>4. The appointed of senior civil servants and politicians as CEO in GLCs is make sure that Bumiputra hold at least 30% of of the equity stake and compare with other non-Bumi and foreigners. |

## 2.2 Privatisation in Singaporean Public Sector Enterprises

### 2.2.1 Introduction

Privatisation reflects a worldwide interest in reducing the direct involvement of governments in economic development by enhancing the scope of private ownership. The appeal of privatisation embraces both the desire for less government intervention and a belief in the superior economic performance of the private sector.

At first, there were in doubt when Singapore became an independent nation in 1965 since just a small country with 650 square kilometres and lack of resources. But the Singapore economy performed remarkably well starting 1970. Its double-digit growth rates were impressive by comparison with other developing nations, especially during the oil crisis and world recession in the 1970s (Low, 1995). Singapore always cited as an economic model for other developing countries to emulate. It has a successful public housing programme for low-income families. It has solved its unemployment problem within a decade of becoming independent. It is now an international financial centre and has the busiest seaport in the world. Its Changi International Airport has been acclaimed as one of the best. The performance of its national carrier, Singapore Airlines, has become the envy of other international airlines. To the surprise of many economic observers, these achievements have been made possible through the efficient management of public sector enterprises (Low, 1995).

Privatisation was the long-term government policy that ultimately could have the most effect on the structure of the economy and the lives of Singaporeans. At one level, privatisation represented the government's decision, articulated in the 1986 Report of the Economic Committee, that the economy had sufficiently matured for the private sector to become the primary engine. Since government-owned enterprises had "been successful in their respective areas of endeavour and should continue to be so", the government no longer needed to continue running them (Alten, 1995).

In 1987, a government-appointed committee, the Private Sector Investment Committee, issued a report recommending the sale of shares in 41 of the approximately 500 state-backed companies, ranging from Singapore Airlines (SIA) to the national lottery, while retaining more than half the value of the share. SIA shares subsequently went public, although the government retained control. The sale of four statutory boards, including the telecommunications monopoly, was also recommended in the proposed ten-year divestment plan (Yin, 2008).

Through privatisation, the state was changing its role from that of direct provider of social and business amenities to that of director and overseer of a much wider range of private, social, and business institutions. The strategy was not without problems, however. One of the most difficult questions was what effect privatisation would have on the management of the divested companies and on the statutory boards. Since the government had absorbed the "best and brightest" into the civil service, there was a critical shortage of private-sector top-level entrepreneurial talent. Moreover, even if the plan was carried out fully, the government would still maintain control in many areas of industry and services because more than half the value of shares of state companies would remain under government control, a partial divestment at best.

Following that, Lawrence (1987) suggested that Singapore needed less government control of the economy, which could come about through the government restraining itself from absorbing new investment opportunities and encouraging local private entrepreneurs to undertake the new investment. In time, this would likely produce a more vibrant economy.

### 2.2.2 Government Linked Companies in Singapore

Government companies are enterprises incorporated under the Companies Act, just like any private sector company. They are owned by the Government through holding companies, whose main function is to exercise overall control over the subsidiary companies, which may be wholly owned or are joint ventures with the private sector. Statutory boards may also establish subsidiaries in the legal form of limited companies as joint ventures with the private sector. This is similar to the holding company approach adopted by other developing countries, such as Nigeria, where the Government establishes holding companies to pursue its objectives through the activities of subsidiaries and associated companies (Lee 1991).

In the late 1960s, the Singapore government created GLCs and statutory boards to spearhead development in various sectors of the economy. The stated rationale for this strategy was to compensate for the lack of private sector funds or expertise. Pioneer GLCs included the Keppel, Sembawang, and Jurong Shipyards, which spurred the development of Singapore as a major shipbuilding and ship repair centre; the Development Bank of Singapore, which was set up to provide development financing; and Neptune Orient Lines, which was formed to leverage on the island's strategic location. Some GLCs were set up for strategic reasons, notably Chartered Industries and Allied Ordnance in the defence industry. Many of these early companies were joint ventures with foreign investors.

For example, the Singapore Refining Company, which provided the catalyst for the growth of the oil refining industry, was a joint venture with Caltex and British Petroleum, while the Petrochemical Corporation of Singapore, which launched Singapore's entry into the petrochemicals industry, was a joint venture with Shell and a Japanese consortium. In 1974, the government (through the Ministry of Finance) established a limited holding company, Temasek Holdings, to manage its investments in GLCs. At that time, 36 companies were transferred to Temasek's control.[4]Since then, rapid economic growth has afforded GLCs the scope and opportunities to expand and diversify their operations. The 1980s and 1990s also saw the corporatisation of a number of statutory boards into GLCs.[5](*Refer Figure 2.3 and 2.3 on GLCs corporate structure and Temasek Holding group structure*)

Today, the total number of GLCs is estimated to be in the hundreds. Temasek Holdings directly holds 22 first-tier GLCs, all of which have subsidiaries or associate companies, which, in turn, often have third-tier subsidiaries, and so on. The companies are involved in a wide range of sectors, including finance, telecommunications, transport and logistics, property, infrastructure and engineering, and utilities. Temasek Holdings and its subsidiaries are registered companies under the Companies Act, subject to all the same requirements as private businesses. Many of its companies are listed on the Singapore Exchange. According to Temasek, the major listed companies account for more than 20 percent of the total market capitalisation.[6]

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[4]*Two other holding companies were set up around the same time: MND Holdings (owned by the Ministry of National Development) and Sheng-Li Holdings (owned by the Ministry of Defence). MND Holdings was subsequently taken over by the Ministry of Finance and the bulk of its GLCs transferred toTemasek. Sheng-Li Holdings (now Singapore Technologies) is responsible for defence-related GLCs.*

[5]*For example, the Telecommunications Authority of Singapore was converted to Singapore Telecommunications in 1992, the Public Utilities Board's electricity sector functions were spun off to create Singapore Power in 1995, and the Port Authority of Singapore was converted into the PSA Corporation in 1997.*

[6]*The listed first-tier companies are DBS Bank, Keppel Corporation, Neptune Orient Lines, SembCorp Industries, Singapore Airlines, SMRT Corporation, and Singapore Telecommunications. See http://www.temasekholdings.com.sg/.*

According to the government, GLCs operate fully as for-profit commercial entities, on the same basis as private sector companies: They are expected to provide commercial returns commensurate with the risks taken; they are subject to the same regulations and market forces as private entrepreneurs; and they do not receive any subsidies or preferential treatment from the government. In an early survey of public enterprises in Singapore, Lee (1976) concludes that "government control is in fact very loose" and that the government "normally does not interfere with the management of the companies directly". Furthermore, he notes that GLCs appear to receive few, if any, special privileges by virtue of their government ownership:

The main advantage of government ownership appears to be the positive signal it sends to the markets Low (1991, p. 65) cited: "Being linked to Government is of course useful. It gives the company credibility and nobody will think you are an unreliable operation. But the company has to justify itself and earn its keep by marketing the right products at the right time as no favours are given or expected."

Indeed, many GLCs have consistently posted a strong financial performance. However, the rapid growth of GLCs – both in size and in number – has led to concerns that they are encroaching into too many industries, effectively crowding out the private sector, and hindering the development of a critical mass of thriving local enterprises. Among small- and medium-sized private enterprises in particular, GLCs are still perceived to have unfair advantages in terms of access to funds, tenders, and opportunities (Ang and Ding 2005 and Lin 2000). Other critics argue that GLCs are less efficient than private sector companies are, due to their institutional relationship with the government, the market structure in which they operate, or the management systems applied within them (Majmudar 1996, Yeh and Chiu 1996, Ramirez 2000 and Tian, 20000. For example, GLC managers are usually appointed from the ranks of senior civil servants and military officers; and, while they are generally of a high calibre and promoted based on their performance they have also been criticised for being too risk-averse and lacking sufficient entrepreneurial drive.[7]

There have also been charges that certain GLC investments have been more politically motivated than commercially. In addition, being linked to the government may sometimes be a barrier rather than an advantage; in recent years, some countries have been reluctant to allow Singaporean GLCs to invest in sectors considered nationally strategic.[8]

**2.2.3 Performance of Government Companies**

Industrial development was further stimulated by the Government's active participation. In order to provide financial assistance to the industrialists, the Government set up the Development Bank of Singapore (DBS Bank) as a joint venture with private sector investors. The Government-owned Trade Development Board (TDM) assists manufacturers to export their products.

[7] *In recent years, some of the large GLCs saw management shake-ups, with new senior executives brought in from the private sector and some from abroad. A number of these foreign executives subsequently left before completing their contracts. The government has put this down to coincidence, maintaining that it does not play a direct role in recruitment decisions made by the GLCs' boards.*

[8] *In 1999–2000, Singapore Telecommunications was defeated in takeover attempts in Hong Kong SAR and Malaysia largely for this reason.*

The Government is also directly involved in competing with the private sector. Through the three major holding companies (Temasek Holdings, Sheng-Li Holdings, and MND Holdings), the Government has equity shares in a few hundred companies in all sectors of the economy. All these companies are managed as private limited liabilities companies except that they are wholly or partially owned by one of these holding companies that are directly accountable to the Ministries of France, Defence, and National Development, respectively.

The holding companies are supervised by a special Directorship and Consultancy Appointments Council (DCAD) chaired by the Minister for Finance. Details of the operations of these holding companies are seldom publicly disclosed except during Parliamentary debates. For example, in August 1986, in a written reply to an enquiry by a Member of Parliament, the Minister for Finance disclosed that in spite of the prevailing depressed economic conditions during that time, the three government holding companies had performed well.

Their consolidated profits rose from S$226 million in 1984 to S$361 million in 1985. The average rate of return on capital was 85 per cent in 1985 compared to 57 per cent in 1984. These three holding companies had equity interest in 57 companies engaged in a wide range of business activities in manufacturing, petrochemicals, trading, shipbuilding, transportation, properties, construction, and financial services. Among the three, Temasek Holdings had the largest profits amounting to S$213 million. Though MND Holdings had only S$69 million in profits, the return was S$2.20 per dollar invested. Sheng-Li Holdings' profits were S$79 million or a return of 61 cents per dollar invested (Singapore Planning Unit 1989).

### 2.2.4 Divesting Government Companies

During the initial years of economic development of Singapore, it was essential for the Government to set the pace and take the lead in the desired direction. The Government had to decide on the type of economic system that would bring about a higher standard of living for its people. Active and direct participation in economic activities helped the system to move in the right direction at a faster pace. This is understandable given the actual conditions at the time of its independence in 1965. The Government had to create a sense of nationhood in an immigrant population of diverse cultures and languages. However, as the economy matures, there are other means to ensure that the momentum is sustained and that the same objectives are achieved. The role of the Government should be to provide a conducive business environment and to create opportunities for productive investments. It should provide the framework, set the major policies, but let individual entrepreneurs weigh their risks, choose their options, and earn their rewards. Except for special reasons, such as national security, the Government should rely on the private sector initiative and enterprise to generate growth.

The Committee has also recommended some order of priorities for privatisation. The major companies under the three priority lists are summarised in Tables 2.7 to 2.9.

**Table 2.8: Major Companies Recommended for Listing on the Singapore Stock Exchange**

| Name of Company | Shareholders' fund (S$ million) | Govt. holding (%) As of 1988 | Govt. holding (%) As of 2000 | % Target |
|---|---|---|---|---|
| Jurong Shipyard | 160 | 43 | Nil | Nil |
| Singapore National Printers | 12 | 100 | 51 | 51 |
| Singapore Offshore Petroleum Services | 26 | 33 | 33 | Nil |
| Singapore Pools | 52 | 100 | 100 | Nil |
| Yaohan Singapore | 13 | 15 | Nil | Nil |
| Resource Development Corporation | 83 | 100 | 30 | 30 |
| Changi International Airport Services | 48 | 70 | 70 | 21 |
| Container Warehousing & Transportation | 10 | 40 | 40 | 51 |
| DBS Land | 623 | 100 | 48 | 51 |
| DBS Finance | 97 | 100 | 100 | 51 |
| Keppel Insurance | 22 | 60 | 60 | 51 |
| Sembawang Maritime | 24 | 100 | 31 | 51 |
| Shing Loong Finance | 23 | 100 | 71 | 51 |
| Singapore Airport Terminal Services | 283 | 100 | 100 | 51 |

(*Source:* Singapore Planning, 2002)

**Table 2.9: Major Companies Recommended for Reduction in Singaporean Government Holdings**

| Name of Company | Shareholders fund (S$ million) | Govt. holding (%) As of 1988 | Govt. holding (%) As of 2000 | % Target |
|---|---|---|---|---|
| DBS Bank | 1,947 | 48 | 44 | 30 |
| Keppel Corporation | 364 | 68 | 48 | 30 |
| Neptune Orient Lines | 177 | 62 | 39 | 30 |
| Sembawang Shipyard | 242 | 74 | 54 | 30 |
| Singapore Airlines | 4,338 | 63 | 56 | 30 |
| INDECO | 22 | 100 | 67 | 51 |

(*Source:* Singapore Planning, 2002)

**Table 2.10: Major Companies Recommended for Total Privatisation in Singapore**

| Name of Company | Shareholders fund (S$ million) | Govt. holding (%) As of 1988 | Govt. holding (%) As of 2000 | % Target |
|---|---|---|---|---|
| Acma Electrical Industries | 30 | 22 | 22 | Nil |
| Chemical Industries | 36 | 23 | Nil | Nil |
| Intraco | 148 | 27 | 10 | Nil |
| National Iron & Steel Mills | 236 | 19 | Nil | Nil |
| UIC | 335 | 11 | Nil | Nil |
| Hitachi Electronics Devices | 53 | 30 | Nil | Nil |
| Singapore Airport Duty Free Emporium | 14 | 20 | Nil | Nil |
| Van Ommeran Terminal | 48 | 34 | Nil | Nil |
| Construction Technology | 27 | 100 | 100 | Nil |
| GATX Terminals | 22 | 59 | 50 | Nil |
| Singapore Airport Bus Services | 8 | 31 | 31 | Nil |
| EPB Publishers | 3 | 100 | Nil | Nil |

(*Source:* Singapore Planning, 2002)

One of the major issues deliberated by the Committee was the question of succession. Government participation is dominant in the major companies such as Singapore Airlines, Keppel, and Neptune Orient Lines. It is unlikely that any single group of investors would want to be involved so extensively. Besides, the good performance of these companies should not decline due to lack of direction and support. The Committee has recommended that new directors from the private sector should be phased into the boards of Government companies so that they may be entrusted with the leadership after the civil servants have been phased out.

As Jurong Town Corporation, Port of Singapore Authority, Public Utilities Board, Singapore Broadcasting Corporation and Telecoms are natural monopolies, which provide essential services, privatisation can only be implemented after some major issues are examined and safeguards formulated. These issues include possible conflict of interests between shareholders and consumers and foreign ownership versus local ownership of the monopolies. The Committee has recommended that if statutory boards were to be privatised then the ownership should be as widely distributed as possible. As a result of the comprehensive deliberation and specific recommendations of the Committee, one can expect many Government companies to be privatised and to seek listing on the stock exchange in the coming years.

One major Government divestment was that of the very successful Singapore Airlines (SIA). In terms of magnitude, it was one of the largest Government companies. The divestment was done by Temasek Holdings, which reduced its holding to 63 per cent in 1988. However, even after privatisation, the Board of Directors of SIA was still Government-appointed. The flotation exercise was one of the grand events in SIA's history. It immediately became the local stock exchange's premier blue chip stock.

Table 2.11: A Summary of unique features of Singaporean Privatisation Experience

| Singapore: Experience in Privatisation |
| --- |
| 1. The introduction of GLCs in Singapore boost economic growth and lead to Singapore become the first developed country in ASEAN.<br>2. Singaporean GLCs controlling more than 50% equity stake in Singaporean Stock Market compared to Malaysian only 30%<br>3. GLCs appointed experience senior executives from private sectors and foreigners to manage GLCs after Asian financial crisis compared to Malaysian GLCs which still appoint civil servants and politician as their CEOs of company |

### 2.3 Chapter Summary

The objective of this chapter is to provide an understanding of how privatisation has led to new ownership structures in Malaysian and Singaporean companies. The development of privatisation throughout the world started in the early 1950s and became more important in the early 1970s. Governments will also take part in their public sector enterprises, even when the privatisation is a partial privatisation. In this thesis, this chapter briefly discusses the process of introducing and transforming the public sector to private whereby the government still owns and controls companies in Malaysia and Singapore. In Malaysia, the government introduced the NEP to achieve national unity through inter-ethnic economic parity between Bumiputras (especially the Malays) and others, especially the Chinese. Thus, the NEP has led to different ownership structures in Malaysian listed companies as a result of the 30% Bumiputra equity ownership requirement for public listed companies. The master plan, laid out by the government, called the Privatisation Master Plan, together with the action plan "Privatisation Action Plan", became the guidelines in implementing the privatisation policy and at the same time to achieve a developed country status by 2020 ("Vision2020").

Meanwhile, when Singapore jump-started its industrialisation in the late 1960s, the government created GLCs to boost the economy to try to be the first developed country in ASEAN. With Temasek Holding as the leader, holding more than half of the equity in state-owned enterprises, Singapore has become a more successful country than its neighbours, especially Malaysia. In the beginning, GLCs in Singapore were not as efficient compared to private companies for several reasons. One of the reasons was that the GLCs managers were usually appointed from senior civil servants and military officers who were seen to be too risk averse and lacking sufficient entrepreneurial drive. The government then changed its policy by hiring senior executives from the private sector and foreigners to manage the GLCs. With their experience and knowledge, GLCs in Singapore became more efficient and profitable compared to the private sector and now control more than 50% of the Singapore Stock Market (SGX).