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## **REVISITING PRIVATISATION IN MALAYSIA: THE IMPORTANCE OF INSTITUTIONAL PROCESS**

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### **ABSTRACT**

*This paper argues that institutional process are essential to the execution of economic policy. In the absence of adequate institutional processes, well-intentioned economic policies may not be implemented in the manner expected by theory. The case of privatisation in Malaysia is used as an example to illustrate why institutional processes must be put into place in order to achieve the full benefit of economic policies. Economic theory suggests that privatisation, rather than state-ownership of enterprises, leads to greater economic efficiency. However, this is only the case if privatisation initiatives are carried out in a manner that consistent with good institutional practice. This paper suggests that there is a prima facie case for establishing transparent institutions in order to gain from the proper implementation of economic policy.*

**Keywords:** privatisation policy, institutional process, Malaysian economic policy implementation

### **INTRODUCTION**

The microeconomic foundations of economies ensure that macroeconomic objectives are achieved. Stated differently, macroeconomic goals can only be achieved if there are robust institutions ensuring that microeconomic policies are designed, executed and monitored in accordance with the principles of transparency and good governance. Institutional strategies are not usually given a place of prominence in debates on national economic growth. Indeed, the importance of institutions is usually given a back seat and labelled as a 'soft' issue. In fact, as this paper will argue, the lack of a clear institutional framework may possibly have robbed Malaysia's privatisation drive of its full effectiveness.

The privatisation initiative in Malaysia was introduced at the correct juncture in the country's development. It is undeniable that the basis for privatisation was in keeping with current economic thinking. The rationale for privatisation is based

on the premise that governments should restrict themselves to governing and not venture into running businesses. There are several reasons for this argument, including the undesirability of a large bureaucracy, the inefficiencies of centralised planning and the crowding-out of private investment. The implementation of privatisation could be undertaken in such a manner as to undermine the benefits that would otherwise accrue. The proper conduct of privatisation requires that efficiency and transparency should be considered in the implementation process. Otherwise, the outcomes might not be efficient and there will be an associated welfare loss.

The implementation of privatisation requires that proper institutions be established in order to avoid practices that will result in inefficiencies and welfare losses. The implementation of privatisation in Malaysia may well have suffered from the lack of a well-defined institutional framework. Had such a framework been established prior to the execution of privatisation, many of the flaws in the implementation phase could have been avoided. The absence of any consideration for institutions that could have overseen the execution of privatisation led to the inappropriate implementation.

This paper will be organised as follows. The second section will consider the increasing importance that has been attached to institutions, and areas in need of attention within the process of institutional reform. The third section will discuss how the government planned for privatisation. We argue that privatisation was a part of the country's planning process but that institutional elements were ignored. The section that follows will highlight the practice of privatisation in Malaysia, demonstrating the incidence of disregard for institutional processes. The improper execution of privatisation in the health care industry will be discussed in this context. The fifth section will discuss the issues of institutional reform in the case of the telecommunications sector. We will highlight the need to establish an independent body to oversee institutional reform. Finally, some concluding remarks are offered.

## **ESTABLISHING INSTITUTIONAL REFORM**

There is a recognition that textbook principles of microeconomics take the presence of institutions for granted. Rodrik (1999) admitted in his research, that "the broader point that markets need to be supported by non-market institutions in order to perform well took a while to sink in". Indeed, for long much of neoclassical economic theory has historically paid scant attention to the role of institutions.<sup>1</sup> Rodrik (1999) draws from general equilibrium theory to note that the Arrow-Debreu model "seems to require no assistance from non-market institutions".

In fact, the interest in institutions has motivated empirical work on institutions and their contribution to the improvement of aggregate incomes (Acemoglu, Johnson & Robinson, 2001; Easterly & Levine, 2003). Various institutions are considered necessary for economic growth, such as property rights, regulatory institutions, institutions for macroeconomic stabilisation, institutions for social insurance and institutions for conflict management (Rodrik, 1999). Rodrik (1999) emphatically states that participatory political regimes deliver higher-quality growth.

Good microeconomic policy would seek to ensure competition. Indeed, one of the principal objectives in undertaking privatisation would be to ensure that the government does not crowd out the market and that privatisation increases competition in the provision of goods and services. The purpose of any regulatory agency is to ensure that competition is protected. It then follows that particular suppliers of goods and services should not receive any specific protection. The intention of any regulatory agency would be to ensure that competition is allowed to prevail in the market without distortion or intervention, either from an external source (such as the government) or from within (more powerful firms in the market).

The overall principle at stake is competition. Regulatory bodies must ensure that competition, rather than specific competitors, is protected.<sup>2</sup> With this idea forming the backdrop to policy-making, the overall welfare of society must be given due consideration rather than the interests of particular sectors or groups. Broadly, the intention of any microeconomic policy (and by extension, of any regulatory body), should be to safeguard the principle of attaining the highest possible welfare for the economy as a whole.

There are often various issues at stake and these matters go beyond the ambit of competition or efficiency. Among such issues is the safeguarding of health and safety standards. It is equally important to overcome income inequalities and regional disparities. It is not always appropriate for the government to intervene, but it is also not always appropriate to leave matters to be resolved by the market itself. This again creates a strong argument for a relevant regulatory agency that could make independent assessments of the private sector and the government. Such an agency could make recommendations on policy design and provide ex-ante evaluation prior to policy implementation. As expected, the agency would follow up with an ex-post evaluation at a reasonable period after the introduction of the policy measure in question.

Having argued that there are a number of considerations that need to be taken into account in devising policy, we note that it is essential to determine the significance and risk associated with certain events. These factors call for an

independent agency that could advise the government and the public at large on the efficiency and welfare outcomes of policy devices. Clearly, this proposal hinges on the need for institutional reform, particularly in a country like Malaysia.<sup>3</sup>

We would argue that good regulation would be achieved if the following criteria were to be satisfied:<sup>4</sup>

i. Transparency.

It should be clear how a certain policy was decided up. Further, the processes entailed by this policy should be open to all stakeholders. Finally, information should be made available to concerned parties without undue restriction.

ii. Costs and benefits.

The cost and benefit considerations underlying any policy initiative should be made clear. The costs and benefits accruing to alternative policies should be clearly laid out to all stakeholders.

iii. Performance criteria.

There should be clear criteria for judging performance, which should be used to judge the effectiveness of the policy as well as the parties involved in the delivery of the policy. This will enable the clear and fair audit of policy initiatives and effectively assess the performance of agents/agencies involved in implementing the policies.

iv. Process and organisational flow.

The manner of instituting policies and the institutions and processes involved should be clearly linked, showing the interdependences between agents, their lines of connection and responsibilities.

Two critical points must be seriously considered in formulating good regulation. First, the entire process should be transparent. Second, the regulatory process should work towards achieving efficiency or an adequate balance of competing government goals, as the case may be. While the question of balance in the presence of competing goals is problematic, we argue that transparency in addition to defensible structures and processes ensure that acceptable solutions may be derived.

In discussing the form that a stylised policy development process could take, Dee (2006) noted the necessity of several stages. Dee's scheme started with problem identification, extended to agency review, and resulted in a consultation process

with stakeholders in the economy. This is followed by a report that is prepared by the concerned agency and submitted to the relevant Minister. The Minister would then discuss the matter, before legislation and regulation processed are tabled.

The policy process in Malaysia deeply lacks some of the elements of 'good' regulation that we have been describing. While the practice of privatisation was, in essence and in principle, appropriate for Malaysia, execution was flawed due to a lack of the right institutions. The fundamental flaw, as we shall discover in subsequent sections, was the absence of appropriate institutions to guarantee that privatisation was carried out efficiently and effectively. Indeed, even the central documents that were released prior to privatisation exercise listed the goals, but were largely silent on the institutions necessary for the successful implementation of privatisation.

Transparency is the most pressing issue that must be accommodated within the institutional structure of policy process in Malaysia. This would have to be incorporated at all levels of the policy process, starting with problem identification, going through cost-benefit analysis (CBA) calculations and reaching the point of describing the projected outcomes from alternative scenarios. Obviously, there should be transparency in the implementation of the policy process, which would imply transparency in public procurement, open discussions of shortcomings in implementation and clear admissions of failure in the delivery of the policies.

The second area that demands attention is the assessment and review process. Presently, there is no clear process through which assessments and evaluations are carried out. Private consultants are engaged on occasion, but the process is otherwise executed internally. In both cases, the independence of the assessment process comes under question. It would be preferable to have an independent body that could conduct CBA studies, design policies and review outcomes once the proposed policies have been implemented. A possible model for such a body the Australian Productivity Commission. It is still possible to consider the opinions of private consultants and internal assessments, and such comparisons should indeed be discussed in parliament. Without doubt, discussions based on views from various sources would add to the richness of debate and allow the parliament to make better-informed decisions.

Finally, it is necessary to institute an agency that could monitor and report on the organisational aspects of the policy process. The ministries for their respective policy implementation would monitor those aspects that are related to the implementation of a policy. The function of monitoring would ensure the followings:

- i. Routines in policy executing follow recommended flows and organisational structures;
- ii. Lines of responsibility are adhered to;
- iii. Implementation flaws are detected and improvement are advised on; and
- iv. Recommended procedures and standards are followed.

Since claims of mismanagement and poor governance can arise, it follows that an independent monitoring agency should be established. This monitoring agency will observe the implementation of policies and observe non-compliance with suggested guidelines; it will also recommend how inefficiencies in the operation of policy implementation could be improved.

In institutional terms, the limiting factors to the Malaysian policy process come from three possible sources:

- i. Inadequate exposure to regulatory best practice;
- ii. Vested interests that impede good regulatory practice; and
- iii. Rent-seeking behaviour by the government.

The first issue corresponds to the economic culture that prevails in Malaysia and is symptomatic of most developing countries: there is no definite agreement on what constitutes good regulatory practice. Essentially, this relates to a poor theoretical understanding of what constitutes best practice, particularly with regard to institutional structures that must be established and maintained to ensure that policy process seek to achieve the highest possible social welfare for the economy, viewed as a whole.

The second constraint arises due to vested interests that, in their attempt to achieve their own goals, disrupt the efficient functioning of good regulatory practice. Here, we assume that the government itself does not actively support events that are detrimental to the efficient functioning of institutional processes and agencies, but is rather obstructed by firms and individuals who attempt to violate good practices for their own gains. In effect, this is caused by firms and individuals, without government complicity, who attempt to induce corruption or use personal influence and power so that institutional processes are made malleable to achieve individual gains.

Finally, the possibility of the government using its own offices in order to obtain rent would be the most difficult to contain. Indeed, one often reads reports of this practice occurring in developing countries, particularly after a change in regime. Transparency is most important in this category, yet is typically absent. It has been alleged that the primary problem with the privatisation exercise in Malaysia was largely due to the government overlooking this source of difficulty.

## **PLANNING FOR PRIVATISATION**

The privatisation wave in Malaysia had its beginnings in 1983, when then Prime Minister Mahathir Mohamad publicised his government's intention to embark on a privatisation policy. This was followed by the publication of Privatisation Guidelines by the Economic Planning Unit (EPU) of the Prime Minister's Department in 1985. These guidelines constituted the official document on privatisation. In February 1991, the Privatisation Masterplan (PMP) was announced. This plan set out the country's privatisation policies.

In formulating its privatisation policy, the government aimed to achieve the following objectives:

- i. To relieve the financial and administrative burden of the government;
- ii. To improve efficiency and increase productivity;
- iii. To facilitate economic growth;
- iv. To reduce the size and presence of the public sector in the economy; and
- v. To assist in meeting the national development policy targets.

In tandem with the PMP, the government introduced the Privatisation Action Plan (PAP),<sup>5</sup> a two-year rolling plan to assist in implementation. The PAP was reviewed annually with a view to identify measures to expedite the implementation of the programme and to determine the entities to be privatised in the following two years. The PAP was guided by a study undertaken by private consultants who were commissioned by the government to review the advisability of privatising government-owned entities (GOEs).

The government at that time, did institute a plan for privatisation. The PMP did define its objectives clearly; it also identified the activities that were to be privatised. The PMP did rank the priority by which projects were to be privatised, indicating those that were of national importance. The PAP outlined an implementation pathway (as mentioned, implementation did not refer to institutional processes and regulatory frameworks). The PAP was instead, concerned with the different categories of activities to be privatised<sup>6</sup> and the methods for restructuring non-profitable companies. This document also outlined the stages in the implementation of privatisation.<sup>7</sup>

The execution of privatisation would have achieved more efficiency if there were an institutional structure that ensured the conduct of transparency. Transparency, in this context, would have been broad-ranging enough to encompass other considerations. We have identified transparency, disclosure of costs and benefits, performance criteria, process and organisational flow as elements of good regulation. The PMP or PAP should have addressed these issues explicitly. As we



shall see in the following section, the failure to do so led to the flawed implementation of several privatisation projects.

Arguably, the most crucial of the elements suggested is transparency. Other aspects would have been achieved if transparency had been emphasised, because insistence on transparency would require disclosure on CBA, methods of evaluation, and a clear description of the agents involved. On a macro level, the privatisation of particular projects should be defended through CBA results. This should be followed by the enunciation of a clear set of goals and the proposed evaluatory framework. On a more micro level, an adequate institutional process would require transparency in the selection and award of contracts to the selected companies. Execution of the privatisation plan was because it did not explicitly accommodate institutional processes.

## **PRIVATISATION OF HEALTH SUPPORT SERVICES**

The government has long been the provider for health services in Malaysia. In the pre-privatisation era, the government engaged itself in the entire gamut of health care, from public health to preventive medicines and including curative and rehabilitative care. The first slivers of privatisation occurred in the early 1990s, when the government decided to privatise non-medical services only, excluding core medical functions and services. In 1994, the Ministry of Health divested its pharmaceutical store and services, which was followed by the outsourcing of hospital support services in 1996 and the privatisation of health examination of foreign workers in 1997.

The privatisation of the health support services in Malaysia was part of the larger attempt to launch privatisation in the health sector and to liberalise the sector.<sup>8</sup> The objective, ostensibly, was to improve economic efficiency in the health sector. These developments also coincided with the Ministry of Health's plan to privatise clinical waste management services since public hospitals did not appear to have adequate facilities. Two developments were wrestling for the attention of the government: the increasing costs of providing medical care, and the burden of providing a wide range of services for the public in connection with administrative, support, medical and preventive services. The government's responses to these problems were twofold. First, it decided to concentrate on its core health services and privatise other activities within the health sector. Second, the government was convinced that it would continue maintaining its commitment to civil servants and the deprived. In consonance with these views, the government chose to privatise non-core activities and to liberalise the health sector. The latter implied that the private sector was encouraged to provide health

care (which would lead to the opening of private hospitals) to cater to those who could afford more expensive health care and medical treatment.

Consequently, in 1993, the government began to privatise the health support services (HSS), calling for open tenders in July 1993. Thirty-one companies (both local and foreign) participated in the tender process, with the EPU and the Privatisation Task Force (PTF) overseeing the process. Before contracts were awarded, three private companies submitted their respective proposals to the EPU on the basis of recommendations made by their consultants. Several meetings were held between EPU, the Ministry of Health and the three companies before reaching an agreement on the mode of privatisation. The three companies—Faber Medi-Serve Sdn. Bhd., Radicare (M) Sdn. Bhd. and Pantai Medivest Sdn. Bhd.—discussed the formulation of the Concession Agreement (Noorul, unpublished) and were allocated regions over which they had control over the market. Faber Medi-Serve was given the Northern Zone of Malaysia and East Malaysia, Radicare had responsibility over the Central and Eastern Zones and Pantai was required to cover the Southern Zone. This process of allocation had the effect made the three companies monopolies in their allocated regions. Two striking observations must be made about the companies that were selected to provide the HSS. None of the firms had a background on the provision of the services that they were supposed to provide. Furthermore, all three companies had to undergo a restructuring process subsequent to the 1998 economic crisis due to mismanagement.

The following are some of the key areas that were privatised by the Ministry of Health:

- i. Supply of pharmaceutical services;
- ii. Supply of hospital support services;
- iii. Monitoring and consultancy services; and
- iv. Monitoring and supervision of foreign workers health certification.

The supply of pharmaceutical services was contracted to Pharmaniaga Logistics, a private limited company. Pharmaniaga received a concession period of 15 years, the strength length of most other services contracted to private companies. It was agreed that the government would make purchases from Pharmaniaga at an agreed price that would be re-negotiated every two years. No single body would act as a regulatory authority. Instead, the purchase of pharmaceutical products, services pricing and other arrangements were regulated jointly by the National Pharmaceutical Bureau, the Ministry of Health and the Price Committee.

The supply of hospital support services was contracted to two private limited companies, Pantai Medivest and Faber Mediserve. The concession period for these companies was 15 years, with the government purchasing the supply of hospital support services at an agreed price named in the Concession Agreement. It was decided that Kawalselia, the Fee Review Committee and the Ministry of Health act together to regulate the purchase, price and quality of the services provided. The supply of monitoring and consultancy services was contracted out to SIHAT for a concession period of 5 years. For hospital support services, the agencies were involved in regulation with the exception of the Fee Committee, which was not involved in the supply of monitoring and consultancy services. The financing mechanism was similar to that adopted for the supply of hospital support services, with payments being made by the government based on services provided at the agreed rate. No single body acted as a regulatory authority. The monitoring and supervision of the health certification of foreign workers was privatised to FOMEMA and regulated by the Disease Control Division and the Ministry of Health. Financing in this case was borne entirely by foreign workers.

The concession agreement that was extended to the firms involved in privatisation covered important elements relating to scope of service, quality and the like. For instance, indicators listed the expected technical requirements and performance standards. The Master Agreed Procedures (MAP) listed the practices and procedures to be followed. A hospital-specific implementation plan was designed to ensure that technical requirements, performance indicators, and required practices and procedures were operationalised in hospitals. A quality assurance programme was instituted to ensure that key performance indicators were satisfied. In all these respects, there is no doubt that the government tried to safeguard the operational efficiency and quality of service offered in the hospitals. There were other areas in which the privatisation process had room for improvement and are still in need of correction because they hinder economic efficiency within the system.

It is necessary to outline the regulatory framework as conceived and implemented by the government before delving into a critical analysis of the regulatory system used in the privatisation of HSS. As mentioned, the concession agreement was collectively determined with the participation of the companies that were awarded the contracts. The efficacy of such a practice is questionable. The supervisory system that was devised is equally questionable.

The Ministry of Health (MoH) established Kawalselia (or the regulatory unit) with the express intention of supervising and monitoring the activities of concessionaires to ensure that their services were in accordance with the requirements stipulated in the Concession Agreement (CA). Kawalselia was responsible for monitoring the activities of contractors, providing technical

advice and approving consumables and procedures. On the other hand, SIHAT (or the Hospital System for the Monitoring of Standards) directly monitors the performance of contractors and advises the MoH as to whether contractors are fulfilling their obligations as stipulated in the Concession Agreement. SIHAT acts as an independent inspector and auditor of standards, providing input for Kawalselia and hospital directors in all hospitals where contractors have been hired.

First, the manner in which Kawalselia and SIHAT were instituted is subject to criticism. Kawalselia was operational in 1998, about a year after the privatisation of HSS. It is unacceptable that there was no institutional structure in place prior to the launching of privatisation. Even more objectionable is the fact that Kawalselia, the regulatory unit, had only eight staff members and was insufficiently equipped to supervise its purported objective, the privatisation of HSS. Another supervisory and audit company was formed in order to correct this deficiency in the functioning of Kawalselia. This company, SIHAT, was meant to act as an external monitoring and evaluation agency. SIHAT was expected to monitor and supervise the contractors, and to use their input to provide advisory services to the Engineering Services Division of the MoH. Two observations arise from this arrangement. First, the MoH did not seem to anticipate the need for a regulatory unit while the privatisation initiative was being implemented. Second, it is questionable to appoint a regulatory company that lacks the essential capabilities required to perform the designated function. Finally, the appointment of an advisory company (SIHAT, in this case) to oversee another company (i.e., Kawalselia) promotes an overlap in function, which creates more friction and unnecessarily raises regulatory costs.

As we can see, the government and the Ministry of Health in particular, lacked a clear understanding of institutional structures and regulatory reform during the privatisation efforts. There is no doubt that privatisation was, in theory, a necessary step in the development of health services in the country, but the manner in which the privatisation initiative was exercised raises serious questions on the efficacy of institutional strategies undertaken by the government. In fact, the manner in which the microeconomic reform was carried out indicated a lack of understanding of institutional reform. To undertake privatisation without the necessary institutional infrastructure weakened the potential gains of privatisation. To invite privatisation bids from firms with no prior experience in a particular sector raises questions about the selection of such concessionaries. If there was a specific reason why firms without an industry track record were entrusted with the privatisation effort, then a transparent display of selection criteria should have been made public. Equally, the government should have publicised the standing of other bidding firms and explained why some firms were chosen over others. Clearly, well-designed institutional policy and

appropriate institutional structures and processes should have been developed ahead of the privatisation effort and thereafter followed in order to maximise social welfare.

Lopez's (2005) study on the privatisation of HSS revealed that contractors did not have well-trained staff for clinical waste management. The hospitals also experienced problems with waste separation. Problems of a different sort were experienced in the case of cleaning services because staff members were incapable of following guidelines and procedures, particularly when handling hazardous and potentially risky situations. Another problem is that planned preventive maintenance is not conducted in a scheduled manner and the monitoring of equipment does not follow prescribed guidelines. Finally, Lopez (2005) noted that SIHAT based its evaluation on complaints from hospital staff. This is an inadequate system because the hospital staff is not aware of the conditions that contractors are expected to satisfy or of the nature of the contracts. Further, HSS contractors are known to develop relationships with hospital staff in order to influence their judgements.

Several comments must be made on institutional arrangements in the context of the privatisation of HSS. First, the scenario that has been painted regarding the privatisation of HSS clearly suggests that there is a need for a regulatory authority with overarching control over public agencies (public hospitals, in this case). Second, this regulatory agency must be independent in order to remain effective, and it should be free from the intervention of its respective ministers. While final decisions should be made at the discretion of ministers, the counsel received from independent regulatory bodies should be transparent and free from government interference. The absence of such a body could prevent some of the inconsistencies found in the HSS case, such as the ad hoc appointment of audit companies lacking requisite expertise, inadequate evaluating systems and the absence of transparency. An independent authority would have noted that the fee review process outlined in the CA had not been revised since the onset of the agreement. This authority would also have drawn attention to the fact that HSS costs are increasing (exceeding RM700 million at present) and would have ensured that contractors were appointed on a transparent basis. These factors decidedly point to the urgent need of independent regulatory bodies in the health sector.

## **REFORMING REGULATION**

### **Preliminary Efforts at Reform: The Telecommunications Industry**

The privatisation of the telecommunications industry is an interesting case for study because it has historically been very much under the wings of the government. Secondly, the privatisation of telecommunications involved institutional reform, albeit in an inadequate manner. The first move in telecommunications reform was to permit the private sector to supply telecommunications equipment (such as telephones and teleprinters), an activity that had been entirely within the province of Jabatan Telekomunikasi Malaysia (JTM) or the Malaysian Telecommunications Department. The private sector was allowed to participate in this line of activity because JTM was unable to meet the demand for such equipment, and the government thought that the inclusion of the private sector was a way of overcoming the problem of excess demand. This move was the start of a series of efforts to liberalise the telecommunications sector. With the privatisation of terminal equipment in 1983, VANS were liberalised in 1984, which was quickly followed by the liberalisation of the radio paging and mobile cellular markets in 1985 and 1988, respectively.

The liberalisation of pockets of the telecommunications sector ultimately led to the takeover of JTM by Syarikat Telekom Malaysia Berhad (STM) in 1987. A public listing of STM took place in 1999, and STM was renamed Telekom Malaysia Berhad (TMB). Despite this privatisation bid, the government continues to hold substantial shares (no less than 60%) in TMB's equity. Liberalisation has required entry into the fixed line and cellular services markets. The fixed line market has been more or less immune to penetration since the costs of building a fixed line are prohibitively high new entrants. While at least five licenses have been issued to new entrants into the fixed line market, it seems inconceivable that TMB's market share in this area will be contested to any significant degree.

The situation is quite different in the cellular phone services market since the barriers to entry are less stringent. The first cellular phone license was issued to NMT450 in 1984, followed by one to STM Cellular Communications in 1988. STM sold its shares in the latter company, after which the company was called Celcom Sdn Bhd. The leading competitors in the cellular market include TMB, Mobikom, Celcom, Maxis, DiGi and TIME dotCom. Similarly, the internet service provider (ISP) market has been liberalised following the initial internet service that was first provided by MIMOS, a government-owned research institute. Other licensees in the market include TMB, TIME, Maxis and Celcom. Several other companies, such as Mutiara and Prismanet, have licenses to offer ISP services. With this brief overview of the telecommunications industry, we now proceed to an examination of the regulatory framework.

Until 1987, the telecommunications sector was regulated by the Ministry of Energy, Telecommunications and Posts (METP). While METP assumed responsibility over the granting of licenses, JTM continued to provide telecommunications services. Thus, JTM acted on instructions received from METP. The Telecommunications Act of 1950 made JTM the regulatory authority for this sector. With the passing of the Telecommunications Service (Successor Company) Act of 1985, STM was provided with the authority to take over telecommunications services from JTM.

The National Telecommunications Policy (NTP) (Ministry of Energy, Telecommunications and Posts, 1994), which was released in 1994, is an important benchmark in the development of the regulatory framework for the sector. The NTP was aimed at covering broad policy directions governing the sector for the period 1994–2020. The main thrust of the NTP was to "encourage competition in the telecommunications sector in order to achieve efficiency and to provide excellent and quality service" (NTP, 1994). This proclaimed interest in encouraging competition was not the sole or overriding objective of the NTP. In fact, the government retained the right to intervene, and the NTP expressly endows the government with authority to determine the number of competitors in the sector. There seems to be a contradiction between the idea that competition is the primary objective and the government's function as an arbitrator that is "empowered to determine the number of competitors that are economically viable for certain telecommunication systems/services" (NTP, 1994). The problem arising here is the question of the government's independence and impartiality in determining the number of competitors, and how this function will be tempered by other potentially conflicting objectives. In terms of our framework, it is undesirable for the government to play a dual role. It would be more desirable for the government to establish an independent agency that could be answerable to the parliament.

There have been claims that the government has acted in the interests of government-linked companies (GLCs) rather than in the interest of optimising social welfare. Decisions such as this should be transparent and made solely in the interests of efficiency and productivity, but recent claims of improper interference in decision-making casts aspersions on the government ability to play the dual role of decision-maker and final arbitrator.<sup>9</sup> There are several pertinent points that need to be raised at this juncture. First, we must bear in mind that the government has a responsibility to all its citizens and all stakeholders, rather than to the interests of particular stakeholders. We have argued that overall social welfare is the central concern, which means that overall welfare should stand ahead of the welfare of GLCs.

The lack of distinction between the government's role as a decision-maker and arbitrator resurfaces in the Communications and Multimedia Act 1998 (CMA). MTEP was restructured in 1998 into the Ministry of Energy, Communications and Multimedia (MECM). The Malaysian Communications and Multimedia Commission (MCMC) were founded during this restructuring. Subsequent to the passing of the CMA, the MCMC is the regulatory authority for the telecommunications sector. The independence of this body is questionable because it seems to be unduly influenced by the government. Government's representation in the MCMC is overwhelmingly heavy; although there is only one member on the Commission who is a government representative, all other members are appointed by the Minister responsible for this portfolio. The appointment process was not transparent, and public input was not part of the process preceding appointment. The independence of any regulatory structure is of utmost importance. While final decisions will be made by the relevant minister, any regulatory body must constitute of members who do not seem to be unduly influenced by the government. Additionally, any advice proffered by a regulatory body should be made available to the public, even if it is to be eventually rejected by the government. This is essential in terms of our criteria for good institutional support, since transparency cannot be dispensed with. A careful examination of the MCMC will clearly indicate that these criteria are not abided with in spirit, even though the form of required institutional fabric seems to have been prepared.

The CMA bestows extensive powers upon the Minister in matters relating to regulatory policies.<sup>10</sup> The Minister of Energy, Communications and Multimedia acts on recommendations made by the MCMC and in turn directs the latter. The MCMC is a middle-level organisation that liaisons with industry forums and also interacts with the appeal tribunal. The Minister does not deal with industry operators directly, but only through mediation of the MCMC. The MCMC makes recommendations to the Minister and also has the responsibility of administering license applications, renewals and their issuance. Yet, the Minister has the final say in matters pertaining to licenses. This organisational structure leaves no doubt that the Ministry is the highest authority in industry regulation. There is no independent body that can receive appeals or arbitrate disputes when industry participants wish to contest a decision made by the Ministry or when there is a difference of opinion between competing firms. Similarly, there is a need for a regulatory body that can assess the operations of the various institutions under the government's umbrella, in addition to assessing the efficiency and welfare consequences of the government's decisions. One of the crucial responsibilities that an appropriate institutional structure must maintain is the conduct of feasibility studies on decisions, with a clear exhibition of associated costs and benefits, as well as opening these results for public discussion. This is completely



absent in the Malaysian context, and the MCMC is equally subject to these shortcomings.

There is no doubt that there is room for public participation through the conduct of public inquiries. This is provided under the Communications and Multimedia Act (CMA) 1998. The MCMC has utilised provisions under the CMA to conduct public enquires, receive opinions from private operators and receive public feedback on the MCMC's discussion papers. Indeed, there is room for public participation within the regulatory structure that has been laid out, but the extent to which this feedback is incorporated within policy decisions is questionable because no independent agency exists to arbitrate between differing views. It cannot be denied that the regulatory structure as officially designed has channels for receiving public participation, but questions remain as to the extent that opposing views can be assimilated within the policy process. With the centralisation of powers in the hands of the government, there is a true need for an independent agency to evaluate the validity of differing views. Such an agency is not quite achievable under the present framework. Although MCMC is a statutory body with its own funding arrangements, the fact that it takes directives from the Minister of Energy, Communications and Multimedia must certainly restrict its capabilities.

The CMA 1998 provides some regulatory framework despite its limitations. Indeed, this is not available in all areas of public policy. In this restricted sense, it is commendable that the CMA has distinguished four central areas for regulatory attention: consumer protection, economic regulation, technical regulation and social regulation. Perhaps the most significant regulatory objective that the CMA has undertaken is one that ensures an efficient communications and multimedia industry. The CMA proposes to do this by incorporating provisions against anti-competitive behaviour. The MCMC has taken steps to ensure that the CMA's objective of establishing a competitive environment is achieved. Towards this end, it is significant that the MCMC has published guidelines on procedures and processes for addressing anti-competitive conduct. The importance of the MCMC's actions stands in stark contrast against the absence of any national policy or comprehensive legislation on anti-competitive practices. In this sense, the MCMC's recognition of the significance of competition policy and law and the dire need to address these issues is laudable. At the risk of digressing, it should be noted that attempts to improve the institutional infrastructure in Malaysia will require the institution of competition law and policy in all areas of commerce, rather than confining these issues to the communications and multimedia industries.

The CMA 1998 is comprehensive in its coverage because it addresses crucial aspects of consumer protection, such as service quality, rate regulation and

universal service provision. However, the practice of rate regulation leaves much to be desired. While the CMA provides for a market-based approach to the setting of rates, it also permits the Minister to decide on tariffs. The provision of ministerial intervention overturns the attempt to set prices based on market signals, which disrupts attempts at achieving social welfare maximisation. Another interesting commitment that the CMA undertakes is to improve on the service quality and consumer needs. The act is dedicated to forming a Consumer Forum that addresses reasonable consumer demands.

Other areas of regulation that the CMA is concerned with include technical regulation and social regulation. The question of social regulation relates to the social values that are considered to be at the core Malaysian culture, primarily relating to offensive content. Although the CMA does not allow for the direct interference of the Minister in this matter, there is no doubt that his indirect control will be at play since he is involved in the issuance of licenses. Technical regulation in the context of the CMA 1998 refers to spectrum assignment, numbering and electronic addressing and technical standards. The MCMC has an important role to play in these matters. While all of these steps are in the right direction, increased shareholder participation would be preferable, so that information is publicly disseminated and the government's influence is moderated. The last issue is perhaps the most sensitive and pressing.

### **Institutional Reform: What Needs to be Done**

The improprieties that can be observed in the execution of privatisation indicate the importance of regulatory reform in Malaysia (Gomez and Jomo, 1999). From the discussion on reform in telecommunications, we observe that wider-ranging institutional reforms are necessary. One of the key features of any institutional reform in Malaysia should include the establishment of a body that can contribute to this process. The flaws and the improprieties committed in the Malaysian privatisation experience should provide lessons on the areas for action. Some of the features that the organisation should incorporate include the following:

- i. Conducting studies on policy issues, especially those addressing the costs and benefits of policy actions. This is to ensure that intended government initiatives are supported by strong arguments and reliable statistical evidence.
- ii. Providing an avenue for public complaints and investigations. In the event of accusations of impropriety, this organisation can have the mandate to conduct independent inquiries.
- iii. Providing an avenue for promoting public awareness. This organisation can inform and disseminate information to the public on the cost-

effectiveness and community benefits of projects. At the same time, the public will be invited to give their input and feedback. This will act as a counterbalance to vested interests trying lobby their views, and will also ensure that the larger interests of the community are served.

- iv. Acting to promote the government-community interface. An organisation such as this is meant to ensure that larger interests of the economy are served, and that communicating intentions and objections is a part of this process.

The Australian Productivity Commission (PC) is a good example of an organisation that fulfils the requirements of the above-mentioned features<sup>11</sup>. Like the PC, a similar organisation can be established in Malaysia. The organisation should be independent and free to research the justifications for policies suggested by the government. The organisation should also have the freedom to investigate the performance of policies that have been undertaken.

The proposed organisation may not have judicial or executive powers, but it should have a mandate to play an advisory role in structural reform. For instance, the organisation would conduct investigations in instances where preliminary evidence indicates improper conduct in the delivery of policies. The organisation can report its results to the parliament or make recommendations to the government on the basis of its findings. Similarly, this organisation, as a result of its studies, may find merit in introducing competition law and policy in the country. These suggestions can be made to the government.

## CONCLUSION

The primary rationale for privatisation is based on the argument that privatisation increases efficiency. Thus, it is implied that welfare will be maximised with privatisation. Privatisation is undertaken to reduce government involvement in business, which is done to avoid the crowding-out of private sector investments and to reduce the costs of government intervention in business. However, the privatisation record in Malaysia shows that the government involved itself in business in different ways: it continued to intervene, but perhaps less directly.

If the government had deliberated more careful on drawing an institutional framework that emphasised efficiency, transparency and good governance, it is possible that cronyism could have been curtailed. The Malaysian experience demonstrates the importance of *soft* issues, such as institutional reform, because 'hard' outcomes are compromised when such issues are ignored. Although there was a need for privatisation, it should have been preceded by the establishment of appropriate institutional mechanisms.

It is not possible to calculate the income stream losses arising from the irregular execution of privatisation, which was caused by lack of information. There is no doubt that vested interests and the practice of crony capitalism would have effectively prevented the economy from achieving the highest possible level of welfare maximisation. If Malaysia has done well and achieved significant levels of growth, then it is very well possible that Malaysia might have done even better if it had planned for its institutional mechanisms and processes. The privatisation experience is one example of how such an opportunity was lost.

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## NOTES

- <sup>1</sup> Rodrik (1999) emphatically observes, "institutions do not figure prominently in the training of economists."
- <sup>2</sup> See Dee (2006) for an account of the institutional basis of microeconomic reform.
- <sup>3</sup> This is discussed in greater detail in Nambiar (2006).
- <sup>4</sup> See Dee (2006) for a discussion of these criteria.
- <sup>5</sup> The Privatisation Action Plan is the outline that proposes how the PMP will be implemented. The PAP is a component of the PMP (<http://www.epu.my/Bi/publi/Private/part6.htm>)
- <sup>6</sup> The six categories of activities were: (i) flagships, (ii) easily privatisable Government majority-owned entities, (iii) restructuring candidates, (iv) services, (v) minority or listed holdings, and (vi) new projects.
- <sup>7</sup> The three stages of implementation were: (a) commercialisation, (b) corporatisation, and (c) divestiture.
- <sup>8</sup> For a detailed treatment of the privatisation of the healthcare sector, see Chan, C. K. (1996, 1997), Chan, C. K., Noorul, A. M., & Dzulkifli, A. R. (1997), and Jomo, K. S. (1995).
- <sup>9</sup> The institutional considerations arising from the privatisation of the telecommunications industry and thereafter are to be found in Nambiar (2006).
- <sup>10</sup> See Lee, C. (2004) for a discussion of the regulatory aspects of the telecommunications industry in Malaysia within the context of competition policy.
- <sup>11</sup> For a discussion on the features and role of the Australian Productivity Commission, see Wonder (2006).

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