Chapter 5

Malaysia Country Report

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November 2014

This chapter should be cited as
Mohammad, S. (2014), 'Malaysia Country Report', in Zen, F. and M. Regan (eds.), *Financing ASEAN Connectivity*, ERIA Research Project Report FY2013, No.15.Jakarta: ERIA, pp.167-218.

CHAPTER 5

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Introduction

As a country, Malaysia represents one of the success stories in the ASEAN in terms of its top-down political commitment to the five-year economic plans. For one, a sizeable government budget is allocated every year for its infrastructure activities. Malaysia is now an upper middle-income country served in most parts by good quality roads and expressways and a system of communication comparable to that of any developed, high-income country in the world. Many of its indicators on infrastructure have reached world-class standards, although there are still disparities in terms of total coverage and quality of infrastructure especially between West Peninsular Malaysia and its eastern counterpart states of Sabah and Sarawak.

For years, Malaysia had not relied much on external sources of infrastructure financing since the government for many years had always managed to source funds internally. However, this also meant that government expenditure has increased tremendously over the years as population, urbanisation, and economic growth continue to put increasing demands on infrastructure.

Since the 1980s, the government has considered the privatisation option—i.e., inviting the private sector as its partner in public-private partnership (PPP) projects—in its attempt to reduce government's burden in sourcing. The PPP model allows a speedier development, making it possible for more projects to be launched within a given window of time than if government funding is the only source of financing. Over the years, the public has also allowed the PPP

model to continue and even shared some of the public infrastructure costs such as in the form of passage fees paid for toll roads.

In the more recent years, however, higher costs of living have led to greater public scrutiny on the way the provision of public services are being met by the government. Hence, new models of financing need to consider not only issues of resource mobilisation and efficiency *per se* but accountability, social justice, and development that supports an inclusive growth and empowers the marginalised as well.

This paper reviews the various government plans and budget allocations for infrastructure in the last 10 years, the financing modes as well as the PPP projects involved. Finally, it looks at Islamic financing—i.e., the use of *sukuk* or the Islamic bond—as a new mode of fundraising from the capital market, leveraging on Malaysia as a platform to attract highly liquid global sources in search of shariah-compliant investment instruments. This liquidity might come from Islamic investors from various parts of the world, including the Gulf. The paper recommends that the ASEAN Connectivity Coordinating Committee (ACCC) and other relevant agencies explore this new method of financing for projects that promote ASEAN connectivity.

Country Overview

Malaysia has a land area of 330,803 sq. km, and population of 28.9 million (see Annex Table 5.11 and Table 5.12). Administratively, it has 11 states and two federal territories (Putrajaya and Kuala Lumpur) in Peninsular Malaysia or West Malaysia. Meanwhile, East Malaysia is separated from the west by the South China Sea and composed of two states (Sabah and Sarawak) and the island of Labuan, a federal territory (Figures 5.1-5.3).

Figure 5.1: Map of Malaysia

Source: http://www.malaysiamap.org/.

Figure 5.2: Peninsular Malaysia

Source: http://www.map-library.com/maps/maps-of-asia/maps-of-malaysia/detailed-road-map-of-west-malaysia.jpg.

Figure 5.3: Sabah and Sarawak

Source: http://travelmalaysiaguide.com/images/Maps/borneo-malaysia-map.jpg.

The Malaysian economy is expected to grow at 4.9 percent in 2014, after declining growth in 2013 at 4.7 percent down from 5.6 percent in 2012. In 2012, domestic demand recorded the highest rate of expansion over the recent years. Following the exceptional growth in capital spending in 2012, the upward trend in public and private investment is expected to remain strong. Private investment, specifically, will be driven by the continued capacity expansion of domestic-oriented firms, ongoing implementation of projects with long gestation periods, and gradual improvement in external demand. Private consumption is projected to grow at a more moderate rate but will continue to be supported by sustained income growth and healthy labour market conditions.

Public sector spending is also projected to see lower growth, as the government consolidates its fiscal position and as the private sector's role gains greater significance.

Financial Position

The federal government revenue in 2013 is expected to increase to RM208.65 billion due to, among others, higher tax revenue of RM159.20 billion. According to the Ministry of Finance, the government aims to continue to safeguard the people's wellbeing while it works to make its public sector service delivery more nimble and responsive in a private sector-led economy. Operating expenditure is projected to decline marginally to RM201.92 billion due to prudent spending. Development expenditure will be allocated a lower sum of RM47.750 billion as well (or 19.1% of the total 2013 expenditure) (Table 5.1).

The economic services sector is allocated the largest slice (62.9%) of the total development expenditure in 2013 at RM30 billion (Figure 5.11 and Table 5.5). Meanwhile, the social services sector is allocated RM11.1 billion, with the education and training sub-sector getting the largest allocation of RM6.5 billion so as to meet the growing demand for a talented, highly skilled, creative and innovative workforce.

The security sector will be provided RM4.6 billion, of which RM3.9 billion is for the defence sub-sector and RM644 million for internal security. The RM2 billion given to the general administration sector is expected to be spent on continued improvements in public service delivery, promotion of higher information technology (IT) usage in the civil service, and repair and maintenance of government facilities nationwide.

Table 5.1: Federal Government Revenue

	RM (million)			% Change		
	2011	**2012[1]**	**2013[2]**	**2011**	**2012[1]**	**2013[2]**
Revenue	185,419	207,246	208,650	16.1	11.8	0.7
Operating Expenditure	182,594	202,617	201,917	20.4	11.0	-0.3
Current Balance	2,825	4,629	6,733			
Gross Development Expenditure	46,416	49,822	47,750	-12.1	7.3	-4.2
Less: Loan Recovery	1,082	2,895	1,024	-11.6	3.5	-0.4
Net Development Expenditure	45,334	46,927	46,726			
Overall Balance	-42,509	-42,297	-39,993			
% of GDP	-4.8	-4.5	-4.0			

Note: [1] Revised Estimate
[2] Budget Estimates excluding 2013 tax measures
Source: Economic Report 2012-2013.

Table 5.2: Federal Government's Development Expenditure by Sector, 2011 - 2013

	RM (million)			% Change		
	2011	**2012[1]**	**2013[2]**	**2011**	**2012[1]**	**2013[2]**
Economic Services of which:	28,156	30,362	30,041	7.8	7.8	-1.1
Agriculture and rural development	1128	1,901	3,297	-61.4	68.6	73.4
Trade and Industry	83,64	5,491	3,297	19.7	-34.3	38.0
Transport	10,140	10,073	9,416	17.0	-0.7	-6.5
Social Services of which:	12,607	13,643	11,113	-39.3	8.2	-18.5
Education and training	7,735	8,557	6,491	-35.8	10.6	-24.1
Health	2,207	1,948	1,919	-41.6	-11.7	-1.5
Housing	762	738	,643	-42.9	-3.2	-12.8
Security	**4,569**	**4,394**	**4,592**	**15.1**	**-3.8**	**4.5**
General Administration	**1,085**	**1,424**	**2,005**	**-43.4**	**31.2**	**40.8**
Total	**46,416**	**49,822**	**47,750**	**-12.1**	**7.3**	**-4.2**
% of GDP	**5.3**	**5.3**	**4.8**			

Note: [1] Revised Estimate
[2] Budget Estimates excluding 2013 tax measures
Total may not add up due to rounding
Source: *Economic Report 2012-2013.*

Ever since the 1998 Asian financial crisis, the federal government's budget has been in deficit. Such deficit, in fact, has increased partly due to the government's initiatives to revive the economy.

As one of the top 20 trading nations in the world, Malaysia is highly dependent on international trade. Thus, global shocks such as the 9/11 attack in 2001 and global crisis of 2008 and 2009 all the more challenged the government's attempts to reduce the fiscal deficit.

The last three years have shown some small success. Deficit as a percentage of GDP is expected to drop from 4.8 percent in 2011 to 4.0 percent in 2013.

Infrastructure Development in Malaysia

West Malaysia is served by major highways that are of world-class standards. North-South Expressway is the longest expressway in Malaysia, running through the whole north-to-south length of the Peninsula. It is about 775 km long from Bukit Kayu Hitam located north of Malaysia, to Johor Bahru on the southern end. Its presence contributed significantly to the development of major sectors of the economy such as manufacturing, transportation, domestic tourism and other services industry such as retailing and banking. It likewise helped connect Malaysia with its neighbouring ASEAN countries Thailand and Singapore.

Another project that bolstered regional connectivity is the Kuala Lumpur International Airport (KLIA). The international airport was moved from its old location in Subang to Sepang at the cost of about RM10 billion (US$3.5 billion). The project was commenced in 1998 via the PPP scheme. Once KLIA was completed, a low-cost carriage terminal (LCCT) by Air Asia was built in 2006. The success and smooth operation of both KLIA and LCCT stimulated not only the Malaysian economy but the regional economy as well.

Since the mid-1990s, the government has been investing significantly in urban transport infrastructure, particularly to restructure the public transport system in the Klang Valley. Among the earlier initiatives were the introduction of the KTM Komuter (KTM), a commuter train service, in 1995; two light transit systems (previously known as the Star LRT) in 1996; and the Kelana Jaya Line (previously known as Putra LRT) in 1998. Subsequently, a high-speed train connecting KLIA and Kuala Lumpur City Centre and operated by Express Rail Link Sdn Bhd (ERL) was launched in 2002. In addition, the KL Monorail System commenced operations in 2003, covering central business districts in the city centre while the RapidKL bus service was introduced in 2004 to provide a comprehensive bus network in the Klang Valley. Currently, all these services, except for KTM and the ERL, are owned

by Syarikat Prasarana Negara Bhd (Prasarana) and operated by Rangkaian Pengangkutan Integrasi Deras Sdn Bhd (RapidKL).

Despite these initiatives, the modal share of public transport in the Klang Valley has declined from 20 percent in 1997 to 12 percent in 2008 due to the population's growing affluence, easy access to vehicle financing and an inefficient public transport system. In 2010, about 83 percent of 7.2 million trips (6 million trips) were made through private transport, mostly involving single-occupancy vehicles. In contrast, average daily ridership on both the urban rail and RapidKL buses grew marginally by 2.6 percent compared with the 7.5-percent increase in private vehicle ownership in the Klang Valley in 2010.

The number of cars in the Klang Valley is expected to reach 7 million by 2020, unless there is a marked shift towards public transport. In addition, a comparison of the public transport modal share in the Klang Valley with other cities such as Tokyo, London, Hong Kong, and Beijing suggests that there is much scope for improvement. The situation warrants concerted and intensified efforts to further increase the modal share of public transport to 50 percent and to place Kuala Lumpur among the top 20 liveable cities by 2020, as outlined in the Greater Kuala Lumpur National Key Economic Area (NKEA). *(Malaysia Economic Report 2011-2012 pp. 58 – 6)*

Recent Initiatives

The government introduced several new initiatives to improve the quality of urban public transport (UPT) service—a common public concern—in the Klang Valley. Thus, the UPT National Key Result Area (NKRA) was launched in 2009 to provide an efficient, reliable and integrated UPT system with adequate facilities and connectivity for the people. Other initiatives pertain to the rail and bus services, the support infrastructure as well as the establishment of the Land Public Transport Commission (or SPAD), which looks into the following modes of transport:

Rail System

- KTM Komuter
- Light Rail Transit
- Monorail
- My Rapid Transit

Bus Services

- RapidKL
- Bus Expressway Transit

Supporting Infrastructure and Systems

- Integrated Transport Terminals
- Bus Stops and Train Stations
- Integrated Ticketing System

Government Agenda (Economic Transformation Programme)

The Economic Transformation Programme (ETP) is the government's economic agenda as a response to national economic challenges. There are four common foundations for the ETP:

1. Malaysia, People First, Performance Now

The 1Malaysia concept aims for national unity while respecting the values of different communities. It is anchored on the principle of fairness and equity—meaning that opportunities and growth will be shared equitably. Meanwhile, People First is an approach to planning and delivery. Performance now, as the title implies, reflects the government's resolve towards delivery and results.

2. Government Transformation Programme

The Government Transformation Programme (GTP) was introduced in 2010 to transform the government's effectiveness in the delivery of services and to sharpen accountability for outcomes. It features six NKRAs: reducing crime, fighting corruption, improving student outcomes, raising living standards of low-income households, improving rural basic infrastructure and improving urban public transport. The next section below details the progress of this programme.

3. New Economic Model

The government established an independent National Economic Advisory Council (NEAC) to develop recommendations on the design of a new economic model. The council's report in April 2010 analysed the challenges and opportunities facing the Malaysian economy and recommends eight strategic reform initiatives.

4. 10th Malaysia Plan

The 10th Malaysia Plan, which outlines the government's development plan for the next five years, aims to focus on economic growth, promoting inclusive socio-economic development, developing and retaining talent, building an environment that enhances quality of life and transforming government. It identifies the 12 NKEAs that will receive prioritised policy and investment.

Infrastructure Development and the GTP

As the year 2020 comes closer, the lesser time is there left for Malaysia to become a developed, high-income nation. Specifically, it has less than a decade left to raise its status to the level of a developed nation. While urban towns and cities have good roads and other infrastructure development, there are still pockets across the country, especially in big states such as Sarawak, where infrastructure is still below developed-country standards.

Fortunately, Malaysia has already embarked on a plan to effect its transformation. At the heart of the plan is the GTP, an ambitious, broad-based

programme of change to fundamentally transform the government into an efficient and people-centred institution. Currently, infrastructure development is covered by the GTP.

Of the programme's six NKRAs, those that relate to infrastructure are:

A. Improving Rural Development

B. Improving Urban Public Transport

5. The First Phase (GTP 1.0, Pre-2013)

The first phase of the GTP (GTP 1.0) started in 2010. The GTP 1.0 aimed to arrest the decline in the NKRAs and to change mindsets in support of the transformation. It also helped the government measure the effectiveness of its targeted approach, and understand how best to achieve its overall targets. Quantifiable National Key Performance Indicators (NKPIs) of GTP 1.0 were established to determine the success of each initiative.

6. Gtp 1.0 Accomplishment (Pre 2013)

Improving Rural Basic Infrastructure

About 4.5 million Malaysians now enjoy the benefits from the GTP 1.0 programme. The GTP 1.0 had focused on basic infrastructure such as road and clean water (although other infrastructure needs such as housing remain a concern). Despite a budget cut of RM3 billion, GTP 1.0's achievements are rather impressive, as described in the section below.

Increasing Access to Paved or Gravel Roads. One test of the programme's success is to look at the percentage of Malaysians living within 5 km of a paved, gravel road and lateritic road. Results show that by the end of 2012, about 3,147 km of roads was completed. The following statistics show the percentages of Malaysians benefiting from the pave roads:

- 98.6 percent of Peninsular Malaysia’s rural population
- 87.0 percent of Sabah’s rural population
- 86.0 percent of Sarawak’s rural population

The key performance indicator (KPI) for 2011 was to complete the construction of 905 km of road—which was surpassed as 1,013 km of roads were completed.

Increasing Access to Clean or Treated Water. Access to clean water is a top priority in Malaysia's rural basic infrastructure plans. By end of 2012, GTP 1.0 is expected to give 310,742 homes access to clean or treated water. The geographic breakdown of the current access to clean water or treated water is as follows:

- 99 percent of Peninsular Malaysia's rural population
- 79 percent of Sabah's rural population
- 90 percent of Sarawak's rural population

Ensuring 24-hour Access to Electricity. Twenty-four-hour access to electricity, a necessity for improving the quality of life of rural Malaysians, is also a main contributor to the industry and to economic growth. By year of 2012, the rural basic infrastructure initiatives will ensure that an additional 93,712 houses will have 24-hour power access.

Geographically, the breakdown is as follows:

- 99.8 percent of Peninsular Malaysia's rural population
- 88.7 percent of Sabah's rural population
- 82.7 percent of Sarawak's rural population

In 2011, the government's target of 26,882 homes was surpassed as it was able to get 27,004 homes attached to the power grid.

Building and Restoring Houses for the Rural Poor. The rural basic infrastructure NKRA includes programmes for those living in dire poverty. Among these is to provide financial aid to the rural poor. As resources were limited, the government had to ascertain that only qualified poor households received this support. Thus, over the past three years, 50,000 homes in rural areas received the government's housing assistance. In 2011, a total of 14,365 homes were build and restore, surpassing the target of 9,146 homes.

Improving Urban Public Transport (UPT)

The GTP 1.0 was also successful in improving accessibility and connectivity in urban public transport. Currently, the NKRA is on track in the Greater Kuala Lumpur/Klang Valley and is also addressing the city's traffic congestion problem.

Initiatives covering four core transport categories—i.e., Bus, Rail, Integration and Network—were implemented in the past three years.

Increasing Capacity of Inter- and Intra-City Trains. In 2011, GTP 1.0 introduced 35 four-car sets for the Kelana Jaya LRT line to increase the daily passenger capacity from 254,745 (the previous year's figure) to 258,156 passengers. It effectively allowed 18 percent (or 10.4 million) more commuters to travel through the line. Statistics shows a ridership of about 44,170 passengers during peak periods.

Four six-car sets from Malaysia's other train service provider, Keretapi Tanah Melayu Bhd (KTMB) started operations in March 2012, helping to alleviate the traffic during rush hours by increasing the ridership by an additional 32,000 persons. Rail usage presently accounts for about 40 percent of the daily public transport ridership.

Enhancing the Bus Experience. To encourage the use of buses as a form of public transport, 1,102 bus stops were upgraded in Sepang, Subang Jaya, Ampang Jaya, Selayang, Shah Alam, etc. in 2011. In the Klang Valley, 470 RapidKL buses were introduced. Thus, 4.04 million more passengers were recorded to have used the service in 2012 compared to the preceding year. In addition, the design and planning of 306 new bus stops are currently under way.

Refurbishing and Re-Designating Pudu Sentral. The 35-year-old Puduraya Terminal was redesigned to provide passengers a better and hassle-free travel experience. The Terianl, renamed to Pudu Central, is an air-conditioned bus terminal with 50 ticket counters and officially opened on 16 April 2011.

Introducing Terminal Bersepadu Selatan. To avoid congestion of public transport in the city centre, the Integrated Transport Terminal Bandar Tasik Selatan (ITT BTS), or *Terminal Bersepadu Selatan*, began its full operations on 1 March 2011. The RM570-million ITT BTS consists of 55 bus platforms,

150 taxi bays, 1,000 parking bays and 1,800 seats for the public, all within its air-conditioned waiting halls. Its facilities boast of a computerised ticketing system, restaurants, and retail outlets. An electronic bus schedule of arrivals and departures allows travellers to obtain real-time updates on travel times.

7. Enhancing Change (GTP 2.0)

Following the successes achieved in GTP 1.0, the second phase known simply as GTP 2.0 started in 2013. This next phase aims to further expand and enhance the GTP 1.0 initiatives that proved to be effective, as well as to introduce new initiatives.

Improving Rural Development (Plan after 2012)

The two main areas of focus under GTP 2.0's rural development component are:

- To complete the infrastructure work begun in GTP 1.0; and
- To enhance the rural economy and ensure that rural residents enjoy the same opportunities as those in the urban area.

The aim here is for rural folks to have better incomes and access to the markets, enough to encourage the new generation of Malaysians to stay and develop their own villages. This is part of the effort to transform Malaysia into a high-income nation.

Completing the Development of Rural Basic Infrastructure. The government is committed to follow through the initiatives started in GTP 1.0 and deliver on its initial promises to the rural people. In addition, a new component—namely, the maintenance of infrastructure—will also be included in GTP 2.0.

The targets under this second phase are summarised in Figures 5.4 to 5.6:

Figure 5.4: Improved Roads

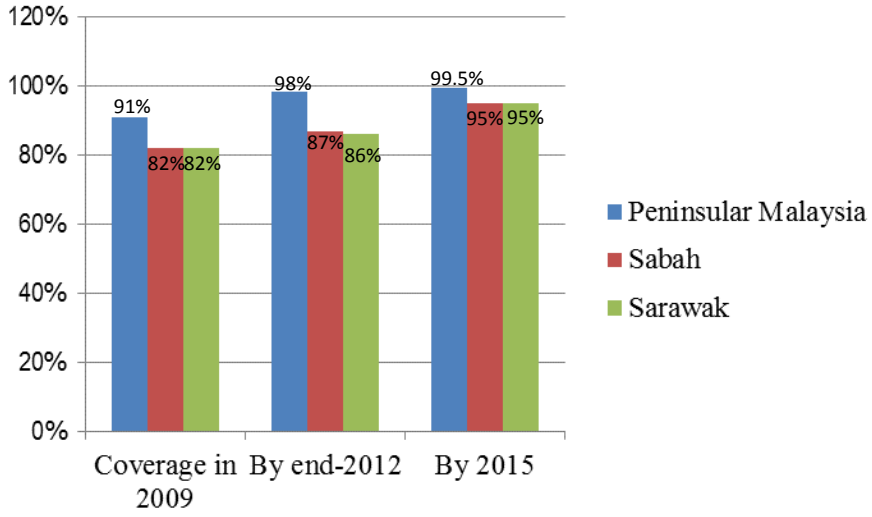


Figure 5.5: Access to Clean or Treated Water

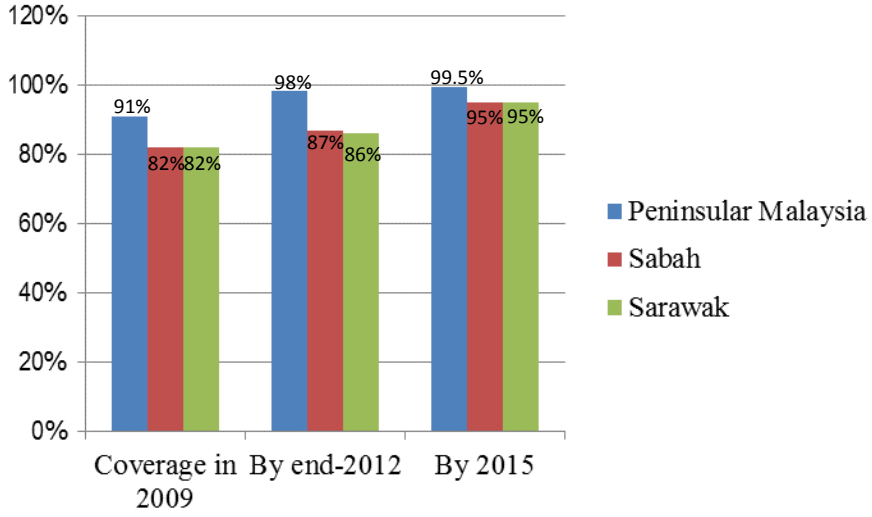
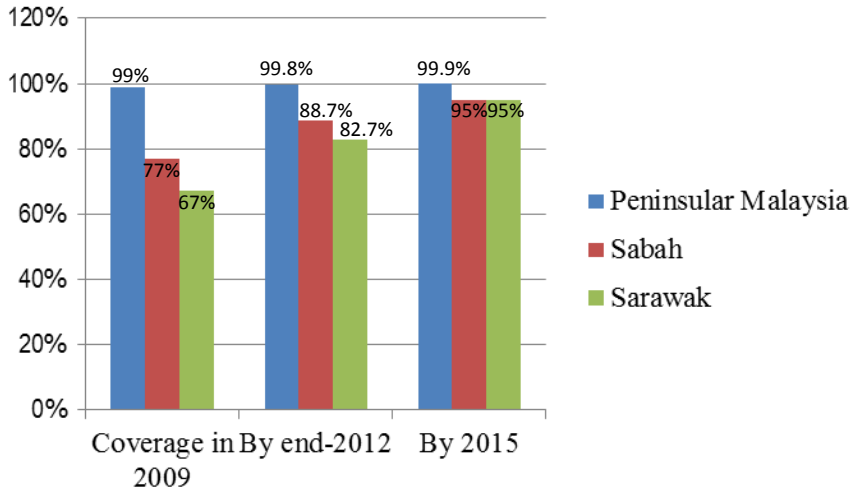


Figure 5.6: 24-hour Electricity



Under GTP 2.0, supporting initiatives will be introduced to maintain and ensure satisfactory delivery of the utilities. These include:

- Upgrading the existing water supply distribution and treatment system so as to ensure that the expansion of water delivery will not overly tax the existing supply;
- Implementing the rural electrification programme so as, among others, to connect schools in rural areas to the main grid and to reduce their dependence on diesel generators, thereby lessening their fuel cost and stabilising their supply of electricity;
- Using hybrid systems to deliver electricity to rural households;
- Monitoring and maintaining roads and power generators in rural areas.

Improving Urban Public Transport

In urban public transport, the GTP will focus on the Greater Kuala Lumpur/Klang Valley area. However, a "watching brief" mechanism will be rolled out to monitor those initiatives implemented in other cities, particularly in key economic corridors.

Enhancing the Bus System. Three initiatives in the Greater Kuala Lumpur /Klang Valley region aim to enhance the bus system:

- A systematic bus network will consider the number of operators per route and require that all stage buses stop at dedicated Inter-Urban Transport Terminals (IUTT) located at the periphery of the central business district. Other sub-initiatives include:
  - Establishing city-bus service within the central business district
  - Reorganising the stage bus and feed bus network
  - Monitoring bus lanes and stage bus drivers.
- Implementing the Bus Rapid Transit (BRT) to provide express service around the entire Klang Valley area. Three projects are in the offing:
  - Kuala Lumpur – Ampang route: 69,000 passengers (pax) daily
  - Kuala Lumpur – Puchong route: 52,000 pax daily
  - Kuala Lumpur – Melawati route: 79,000 pax daily
- Enhancing bus stops by labelling and indexing; and establishing the minimum number of bus stops, either by building new bus stops or upgrading existing ones.

Enhancing the Rail System. The rail system is touted as the most-utilised mode of public transport in the country. Under GTP 2.0, initiatives aim to enhance the entire rail system serving the Greater Kuala Lumpur/Klang Valley area—namely, the inter-city KTM Komuter trains, the inter-city RapidKL Light Rail Transit, and KL Monorail. These are:

- Rolling out rehabilitation programmes, power upgrades of KTMB's networks as well as upgrade of the communication and electrification system to increase the reliability and efficiency of the KTM;
- Extending the Kelana Jaya and Ampang LRT lines;
- Increasing the KL Monorail's capacity.

Transforming Malaysia's Taxi System. The second phase of GTP aspires to upgrade the services provided by taxi providers in Malaysia, especially in urban areas. In particular, the NKRA intends to at least be on a par with the best in other ASEAN countries. The initiatives include:

- Implementing a centralised taxi service system so as to enhance the enforcement and monitoring capabilities of industry regulators and taxi operators.

- Introducing a new business model aimed at lowering the operating costs incurred by taxi drivers. The SPAD, which regulates the taxi industry, will reach out to owners of repair and maintenance facilities in Greater Kuala Lumpur/Klang Valley and ask them to devise attractive packages that draw on economies of scale. In addition, it will also coordinate with car manufacturers to look at leasing options that can reduce the amount of down payment for car loans upon renewal of vehicle permits.

8. The Future and Beyond (GTP 3.0)

The third instalment, GTP 3.0, will be the final phase to be launched in 2015. It will factor in feedback on the impediments brought about by the two previous phases and aim to establish new innovative governance structures that are people-centred.

Factors Contributing to Infrastructure Development

- **Sustained economic growth over the past years.** Malaysia recorded an annual GDP growth average of 6.2 percent over the period 1990-2005. Although growth had been at a much lower trajectory after the 1998 Asian financial crisis, infrastructure development continued. In addition, both rapid urbanisation and high population growth sparked the demand for basic infrastructure.

- **Privatisation and fiscal position.** In the early 1980s, privatisation and private sector-led growth took place when fiscal deficits as well as inefficiencies of state-owned enterprises and government agencies handling the infrastructure services such as ports, electricity, telecommunications and highways became an issue. A change in policy stance emphasised privatisation and enabled some infrastructure development (e.g., in the telecommunications industry) to be commercialised.

- **Development of PPPs.** The PPP as a new business model enables the private sector to participate and can reduce the government's burden in raising funds for infrastructure projects. Such made it possible for the government to complete the more high-cost infrastructure. The establishment of the PPP Unit (the *Unit Kerjasama Awam Swasta*, or UKAS) in Malaysia, which monitors and supervises Public-Private Partnerships, has worked to ensure efficiencies in infrastructure development

- **Domestic financing capabilities.** In the first half of the decades 1970s, 1980s and 1990s, gross capital formation generally exceeded savings as mirrored in the current account deficits. During the 1990-2005 period, the country's gross national savings averaged 34.5 percent of GDP while gross capital formation averaged 31.4 percent, giving rise to a positive savings-investment gap of 3.1 percent of GDP in current prices, which enabled the banking and capital market to tap into this domestic savings and channel such into investments that funded infrastructure development.

- **Dynamic involvement by government-linked companies and agencies.** In Malaysia, more than 40 government-linked companies and agencies operated and participated in various phases of infrastructure projects ranging from project identification, building and construction, operation and maintenance, and investment as an equity or bondholder.

- **National initiatives.** Government plays an important role in promoting the participation of various stakeholders, especially government-linked companies and agencies, in their national agenda. Its robust and comprehensive plans contribute significantly to infrastructure development.

Malaysian Role in Promoting MPAC Initiative

The Master Plan on ASEAN Connectivity (MPAC) was developed and created so as to achieve connectivity among ASEAN member countries. This strategic document covers the initiatives to be undertaken from year 2011 until their completion in 2015. Participating member countries are assigned to

each project and required to ensure these projects' completion. Table 5.3 shows the list of projects directly coordinated and monitored by Malaysia.

Table 5.3: Malaysian role in MPAC project

Project	Malaysian Role	Current Status	Remarks
Singapore Kunming Rail Link (SKRL) Missing Links	Coordinating Country (Ministry of Transport Malaysia)	Seeking technical assistance and funding	Target Completion Date: December 2015
Melaka – Pekanbaru Power Interconnection Indonesia-Malaysia-Thailand Growth Triangle (IMT-GT)	Coordinating and Implementing Country (Tenaga Nasional Bhd)	Seeking financial resources for the whole project. Detailed Terms of Reference (TOR) prepared for the undersea submarine cable survey. Contract to be awarded soon and survey would be completed by the end of first quarter of 2012.	Target Completion Date: December 2015
West Kalimantan – Sarawak Power Interconnection BIMP – EAGA	Implementing Body (Sarawak Energy Bhd)	Term Sheet for a Power Exchange Agreement (PEA) between Sarawak Energy Bhd (SEB) and PT PLN Persero (PLN) for the export of bulk electricity from Sarawak to West Kalimantan was signed in Jakarta in July 2011.	Budget Estimated Total Project Cost: US$ 161 million. Malaysia: US$ 41 million, Indonesia: US$ 120 million Funding Partner(s): Asian Development Bank (ADB).

Source: website www.asean.org on ASEAN Connectivity: Project Information Sheet 2012

Sources of Infrastructure Financing in Malaysia

National Source

The government plays a prominent role in ensuring the development of infrastructure. One of the sources of funds for infrastructure projects is the

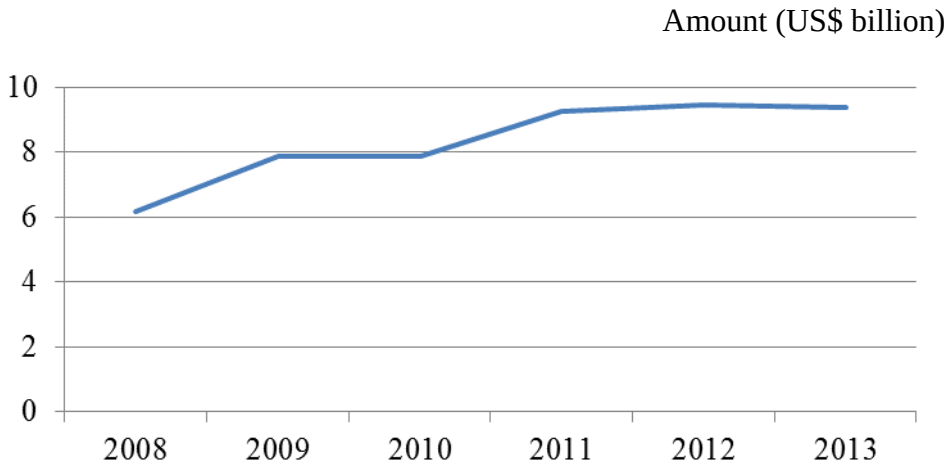
national budget. Thus, Malaysia's annual budget covers both its operating and development expenditure, including those on infrastructure as this has always been the government's focus in its attempt to make Malaysia a developed nation by 2020. Table 5.4 and Figure 5.7 show the trend in the budget allocated for infrastructure development:

Table 5.4: Budget Allocation for Infrastructure Development

Year	Amount (US$ billion)	% growth
2009	7.88	27.51
2010	7.89	0.13
2011	9.25	17.24
2012	9.44	2.05
2013	9.38	-0.63

Source: Ministry of Finance.

Figure 5.7: Budget Allocation Trend



Source: Ministry of Finance.

The budget allocation from the federal government had an increasing trend until 2013, where it slightly dipped at only 0.63 percent. The next sub-topics discuss the details of the infrastructure budget for the recent years.

9. Malaysian Budget 2012

In Malaysia's 2012 budget, rural infrastructure development is the government's third area of focus (Malaysian Government Budget, 2011, as gleaned from the following details:

1) The government will implement several measures in the Rural Transformation Programme (RTP) that complement the national transformation initiatives as follows:

   - The government will establish Rural Transformation Centres (RTCs) to offer integrated services including collecting, processing and distributing agricultural products; banking and insurance, business advisory services; training and skills; as well as providing clinics and retail space. For a start, the existing National Agrobusiness Terminal (TEMAN) in Wakaf Che Yeh, Kelantan and Gopeng, Perak will be developed as RTC pilot projects. In addition, four more RTCs will be developed in Kedah, Johor, Sabah, and Sarawak;

   - Bank Simpanan Nasional, which is a community bank as well as commercial bank, will provide RM100 million as soft loans at an interest of 4 percent. This loan instrument meant as a financing scheme will be given a stamp duty exemption and will form the Professional Services Fund to encourage professionals such as lawyers, doctors, and accountants to set up firms in small towns;

   - The amount of RM110 million will be allocated to implement the Rural Mega Leap Programme covering 6,500 ha in 11 agropolitan projects nationwide for the cultivation of commodity and cash crops as well as fish caged culture. Also, the Rubber Industry Smallholders Development Authority (RISDA) will be given an allocation of RM140 million to implement new planting and rubber re-planting programmes that will benefit 20,000 smallholders.

2) RM5 billion will be allocated to strengthen the development of rural basic infrastructure in a more comprehensive manner. From the total, RM1.8 billion will be for the Rural Road Programme and Village-Link Road Project involving 2,749 km of roads that will benefit 1.76 million rural households. In addition, RM2.1 billion will be assigned to expand the supply of clean water to 200,000 houses while RM1.1 billion will be for the provision of electricity supply to 39,000 houses in the rural areas, particularly in Sabah and Sarawak.

3) The amount of RM500 million will be allocated to continue the upgrade of basic infrastructure under Projek Penyelenggaraan Infrastruktur Awam (PIA) and Projek Infrastruktur Asas (PIAS), particularly in the rural areas, where it will provide opportunities to 29,000 Class F contractors.

4) To cover the cost of an additional 20,000 water tanks for rainwater harvesting for 100,000 people living in the interiors of Sarawak, RM102 million is set aside for water supply reticulation projects. Another RM50 million will be used to expand the programme to Sabah.

5) The amount of RM400 million is meant for the upgrade of the water supply infrastructure in selected Federal Land Development Authority (FELDA) areas, particularly in Pahang, Kedah, Kelantan, and Terengganu.

6) Bank Simpanan Nasional will provide RM50 million for systems development, training of agents and operational costs so as to provide rural folks greater access to banking services. Financial services to be provided by appointed agents in rural areas include saving and withdrawal transactions, bills payment as well as purchase of premium savings certificates.

7) From 1 January 2012, an additional RM150 million will be allocated to the Public Transport Development Fund of the SME Bank. The fund is a special financing facility that offers soft loans to stage, mini and school bus operators at an interest rate of 4 percent. The loan can be used for purchasing or refurbishing buses.

8) The RM90 million is for the provision of basic necessities that include the extension of the clean water supply project as well as income-generating programmes for 190,000 individuals in the Orang Asli area. An additional RM 20 million is for the home relocation of those affected by the landslide at Sungai Ruil, Cameron Highland.

10. Malaysian Budget 2013

In 2013, a total of RM4.5 billion is allocated for various development projects in rural areas such as:

1) Development of 441 km of rural roads and village link roads to benefit 220,000 villagers (RM1.2 billion).

2) Rural utility infrastructure projects for the provision of water supply to 24,000 houses and electricity supply to 19,000 houses (RM1.6 billion).

3) *Program Desa Lestari* involving 29 villages nationwide and benefiting 38,000 villagers (RM137 million).

4) Economic development programmes and water supply projects for the Orang Asli community (RM88 million).

5) A total of 40,000 water tanks for rainwater harvesting, particularly in the interiors of Sabah and Sarawak (RM100 million).

Public-Private Partnership in Malaysia

Malaysia's privatisation policy was launched in 1983, when the Special Task Force in the Economic Planning Unit (EPU) of the Prime Minister's Department was established to coordinate the implementation of the policy. In 1991, the government published the Privatisation Master Plan and renamed the Special Task Force into the Privatisation Section of the EPU. In 2009, the Privatisation Section was transferred to a new dedicated agency known as the Public-Private Partnership Unit or UKAS (Unit Kerjasama Awam Swasta, formerly known as 3PU).

To allow privatisation to take place, the government passed the following:

- The Federal Roads Act (Revised 1989)
- Tolls (Road and Bridges) Act 1965 (Revised 1989)
- Port Authorities Act 1963 (Revised 1992)

To facilitate the privatisation process, the government ratified the following:

- Abattoirs (Privatisation) Act 1993
- Sewerage Services Act 1993
- Highway Authority Malaysia (Incorporation) Act 1980
- Ports (Privatisation) Act 1990
- Water Services Industry Act 2006
- National Water Services Commission Act 2006
- Street, Drainage and Building Act 1974

- Town and Country Planning Act 1976
- Local Government Act 1976
- Control of Padi and Rice Act 1994.

The following guidelines and key publications on PPP were released (UKAS website[1]:

- Malaysian Incorporated Policy 1983
- Privatisation Policy 1983
- Guidelines on Privatisation 1985
- Privatisation Master-plan 1991
- Private Finance Initiative under the
- Ninth Malaysia Plan 2006
- Procurement Guidelines for the Implementation of Projects under the Private Finance Initiative (PFI), Treasury letter, 14 September 2006
- Guidelines on Public Private Partnership 2009
- Private Finance Initiative under the 10th Malaysia Plan.

11. Unit Kerjasama Awam Swasta (UKAS)

The establishment of UKAS has facilitated the government's evaluation of PPP projects and processing of potential project proposals for the Cabinet's final decision. It is responsible for monitoring the implementation of PPP projects and acts as secretariat for the government's projects in the five economic corridors (i.e., the East Coast Economic Region, Iskandar Malaysia, Sarawak Corridor for Renewable Energy, Sabah Development Corridor, North Corridor Economic Region). It also oversees the Facilitation Fund from the national budget. Before final decisions are made, UKAS negotiates the terms and conditions in PPP agreements.

[1] http://www.ukas.gov.my/en/latar-belakang;jsessionid=48158A2D18481435552682B243424832

12. Parties Involved in PPP (see Annex C)

- Special Purpose Vehicles created specifically for the project
- Debt Investor
- Construction Contractor
- Facilities Management Operator
- Ministry/Related Agencies and Users

13. Achievements in PPP Implementation

Table 5.5 describes the achievements in PPP projects from 1983 to 2012. The impact can be gleaned by comparing the data from year 1983 to 2010 and data from year 1983 to 2012. The total number of projects signed from year 2010 to 2012 increased by 15.40 percent in two years. New projects did not affect jobs in the government's payroll at all. The capital expenditure increased by 6.61 percent in two years with no proceeds from sales of government equity and assets. The market capitalisation increased by 12.34 percent.

Table 5.5: PPP Achievements

	1983 - 2010	1983 - 2012	%growth
Total Projects Signed:	513	592	15.40
Existing projects	348	542	55.75
New projects	165[1]	50[2]	
Jobs eliminated from government payroll	113487	113,487	0.00
Savings:			
Capital expenditure (RM billion)	163.8	174.62	6.61
Operating expenditure (RM billion)	9.00	9.25	2.78
Proceeds from sales of government equity and assets (RM billion)	6.5	6.5	0.00
Market capitalisation (RM billion)	208.3	234.0	12.34
% of total Bursa Malaysia Capitalisation	*16.30%*	*15.97%*	*-2.02*

Note: 1 From 1983 to 2010
2 From 2011 to 2012

Sources: UKAS (www.ukas.gov.my).

Table 5.6 shows the implemented projects by economic sectors from 1983 to 2010. Infrastructure projects would mostly be in the electricity, gas, water, government services, other services, construction, and transport and communications, all of which account for over 55 percent of all PPP projects.

Table 5.6: Implemented PPP Projects by Economic Sectors, 1983-2010

Sector	% of total
Agriculture and Forestry	6.2
Electricity, Gas and Water	8.2
Wholesale, Retail Trade, Accommodation and Restaurant	11.1
Finance, Real Estate and Business Services	10.7
Government Services	7.4
Other Services	9.2
Mining and Quarrying	3.9
Manufacturing	13.6
Construction	16.6
Transport, Storage and Communications	13.1
Total	100.0

Source: Malaysia Economic Report 2011-2012.

ASEAN Infrastructure Fund – Strengthening Integration

While ASEAN faces large infrastructure deficits, it also holds significant regional savings. In this context, the proposal to mobilise ASEAN savings towards regional infrastructure development was first suggested by Malaysia at the 10th ASEAN Finance Meeting in Cambodia in 2006. Thus, the ASEAN Infrastructure Fund (AIF) was created. Malaysia has since chaired a series of High-Level Task Force Meetings composed of ASEAN senior finance officials to explore the best framework and mechanism for the AIF.

In September 2011, nine ASEAN member states and the Asian Development Bank (ADB) reached a consensus to provide equity contributions in three tranches amounting to US$485.2 million for the AIF. Of this total, Malaysia contributed US$150 million (Table 5.7). The equity contribution will be augmented with hybrid capital after four to five years of operation. Once the AIF has established a credible track record, bonds will be issued.

Table 5.7: Equity Contribution for ASEAN Infrastructure Fund, in US$ million

Shareholder	1st tranche (2012)	2nd tranche (2013)	3rd tranche (2014)	Total
Brunei Darussalam	3.4	3.3	3.3	10.0
Cambodia*	0.1	-	-	0.1
Indonesia	40.0	40.0	40.0	120.0
Lao PDR*	0.1	-	-	0.1
Malaysia	50.0	50.0	50.0	150.0
Philippines	5.0	5.0	5.0	15.0
Singapore	5.0	5.0	5.0	15.0
Thailand	5.0	5.0	5.0	15.0
Vietnam	3.4	3.3	3.4	10.0
ADB	50.0	50.0	50.0	150.0
Grand Total				**485.2**

Note :* One-time payment
Source: Economic report 2012-2013 pp. 47.

Bond issuance is an important feature of the AIF's business model, as it is designed to tap the region's substantial foreign exchange reserves while maintaining reserve eligibility based on the AIF's expected high investment-grade credit rating and sufficient liquidity. To operationalise the funds, the ASEAN Infrastructure Fund Limited was incorporated on 24 April 2012 in Labuan, Malaysia under the Labuan Companies Act 1990. The primary aim of the company is to provide loans to ASEAN member states for financing infrastructure projects in transport, telecommunications, and utilities sectors.

During its initial years of operation, the AIF focused only on sovereign projects, including those within public-private partnerships scheme.

Parallel to this development, Malaysia's leadership role as co-chair of the AIF Board of Directors along with Indonesia, reflects its commitments towards promoting regional economic growth and integration. Malaysia's profile and reputation as a progressive and proactive ASEAN member was reinforced by its role in the establishment of the AIF and by the fact it is the largest shareholder, along with the ADB (Malaysian Economic Report, 2013).

Islamic Infrastructure Financing

Project finance is a method of raising long-term financing for major projects based on lending against the cash flow generated by the project alone. This refers to the fact that project sponsors or creditors are repaid or earn a return solely from the revenue that is generated by the sale of the project's output. Project finance depends on a detailed evaluation of a project's construction; operating and revenue risks; and the allocation of such risks among investors.

As an effective alternative to conventional direct financing, Islamic infrastructure financing became popular in some countries. In Islamic finance, taking or receiving interest (*Riba*) in loan transaction is prohibited. Risks in any transaction must be shared between at least two parties so that the provider of capital and the entrepreneur share the business risk in return for a share in profit. Besides riba, other prohibitions include speculative behaviour and extreme uncertainty or risk (*Gharar*) and gambling (*Maysir*); thus, Islamic financing requires contractual obligations and clear disclosure of information. Islamic finance follows a set of rules—the *shariah*—and to be shariah compliant, investments must not violate the rules of shariah, as well as not be involved in generally non-ethical investments—i.e., those relating to businesses in alcohol, pork-related products, conventional financial services, entertainment (gambling and casinos, pornography), weapons, and defence.

14. Sukuk and its Role in Project Financing

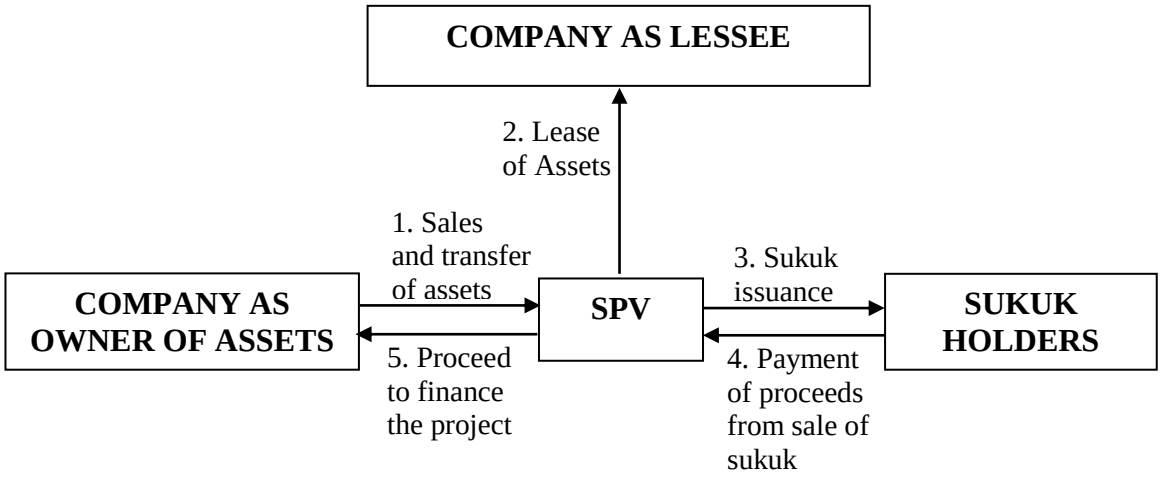
Sukuk (Islamic bond) is a fixed-income certificate that is permissible within the provisions of Islamic Law known as Shari'a, as they are raised during

trading in or construction of specific identifiable assets. The certificate is structured in such a way that it generates returns to investors.

There are differences and similarities between sukuk and conventional bonds. A conventional bond is a contractual debt obligation whereby the issuer is contractually obliged to pay bondholders according to the agreed interest and period. This differs with sukuk. That is, sukuk holders each hold an undivided beneficial ownership of the underlying assets and are entitled to share the profits realised from the sukuk assets. However, both conventional bond and sukuk are marketable and can be traded in financial markets as well as easily rated by ratings agencies.

Sukuk is fast becoming an alternative and attractive source of financing in many countries, especially Malaysia and the Middle East, for the government's development projects. For example, Islamic Development Bank (IDB) has issued RM400 million (US$120 million) sukuk in local currency in Malaysia during 2008 to finance toll roads in Malaysia (IDB, 2012). How sukuk plays its role in project financing is best explained in Figure 5.8:

Figure 5.8: Basic Transaction Structure of Sukuk al Ijarah



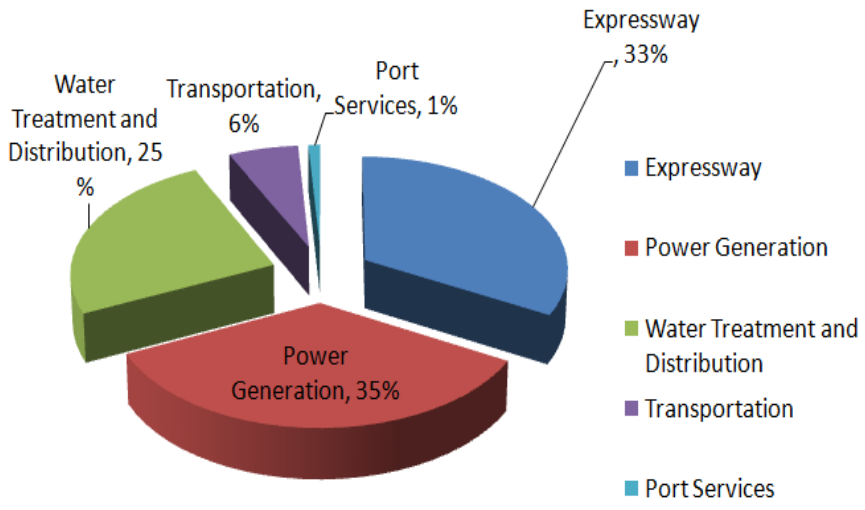
The illustration shows an example of how sukuk is used to finance a project. The company as owner of the asset makes a sale and transfer of such assets to the special purpose vehicle (SPV), which was established by the company as lessee. Then, SPVs will issue sukuk to investors in exchange for the periodic

distribution amount (profit) as well as the dissolution amount upon redemption. The SPV then gives sukuk's proceeds to the company as lessee in exchange for utilisation of the assets. The proceeds from the sukuk issuance will be used to finance the project.

Islamic Fundraising for Infrastructure Projects in Malaysia from 2000 to 2009

The following lists the specific projects funded by Islamic bonds since 2000, followed by a more detailed description on select Islamic PPP projects. Figure 5.9 also shows the breakdown of financing by sector. As we can see there are quite diverse sectors involved showing large utilisation of sukuk. As typical PPP projects, power sector dominates the amount of project size, followed by expressway and water treatment.

Figure 5.9: Islamic Fundraising by Subsector



Power Generation

- Total Issuance : RM36.7 billion (19 issuers)
- Tenure : between five and 20 years
- Examples:-

i Malakoff – RM7.9 billion (20 years) Musharakah (AA3)

ii Jimah Energy RM4.8 billion (20 years) Istina' (AA3)

iii Mukah Power RM950 million (22 years) Mudharabah (AA3)

iv Kapar Energy RM3.4 billion (15 years) BBA (AA+)

Water Treatment & Distribution

- Total Issuance : RM25.7 billion (5 issuers)
- Tenure : between 10 and 20 years
- Examples:-
    i. Pengurusan Air SPV Bhd RM20 billion (10 years) Ijarah/Musyarakah (AAA)
    ii. Syarikat Bekalan Air Selangor RM3 billion (20 years) BBA (AA-)
    iii. Puncak Niaga RM 1.02 billion (10 years) Murabahah (AA)

Transportation

- Total Issuance : RM6 billion (1 issuer)
- Tenure : between 15 and 20 years
- Examples:-
    i. Syarikat Prasarana Negara – RM4 billion (20 years) Ijarah MTN (Government guarantee)
    ii. Syarikat Prasana Negara RM2 billion (15 years)

Expressways

- Total Issuance : RM34.6 billion (20 sukuk issuers)
- Tenure : between four and 29 years
- Examples:-
    i. PLUS SPV – RM4 billion (18 years) – Musharakah (AA1)

ii. Projek Lintasan Shah Alam – RM415 million (29 years) – Mudharabah (A3)

iii. KESAS – RM100 million (4 years) – Murabahah (AA3)

iv. Penang Bridged – RM695 million (13 years) – Istisna' (AA2)

v. SPRINT – RM510 million (20 years) – BBA (A2)

Port Services

- Total Issuance : RM0.98 billion (2 issuers)
- Tenure : Between 14 and 15 years
- Examples:-

i Kuching Port Authority – RM180 million (14 years) BBA (AAA)

ii Westports – RM800 million (15 years) – Musyarakah (AA+)

15. Description of Select Islamic PPP Projects

PLUS (Projek Lebuhraya Utara Selatan). The PLUS programme involves RM11 billion worth of GG sukuk issuances and RM19.6 billion of AAA issuances, both on a bought deal and on private placement bases. The non-government guarantee component could be increased to RM23.35 billion.

The issuances were through PLUS Malaysia Sdn Bhd in year 2012, a jointly owned special purpose company of UEM Group Bhd and the Employees Provident Fund (EPF). The entity was set up to acquire the business and undertakings, including the assets and liabilities of PLUS Expressways Bhd via the issuance of the GG Sukuk and AAA Sukuk Musharakah.

PRASARANA. Syarikat Prasarana Negara Bhd (Prasarana), the Malaysian public infrastructure company wholly-owned by the Ministry of Finance, successfully issued RM2 billion Government-Guaranteed Sukuk Al-Ijarah, under its RM4 billion nominal value sukuk programme arranged in 2009. Proceeds will be used to partly finance the Kelana Jaya and Ampang LRT Line Extension Project and other infrastructure improvement initiatives by Prasarana. This is the first sukuk issuance by the company that tapped the Islamic capital market.

The company is responsible for facilitating, undertaking and expediting public infrastructure projects approved by the government and, together with its group of companies, is also an asset owner and operator of several public transport systems such as Ampang and Kelana Jaya lines, KL Monorail system, bus operations in Klang Valley and Penang, as well as the cable car services in Langkawi.

DANAINFRA. DanaInfra Nasional Bhd's total issue of current exchange-traded bonds and sukuk (ETBS) for the first phase of the MRT Kajang-Sungai Buloh line is worth RM1.5 billion, of which RM300 million is allotted for retail investors. The balance of RM1.2 billion will be for institutional investors.

DanaInfra first issued its 10-year RM300 million retail sukuk on 8 February 2013. Its proceeds are intended to partially fund the Klang Valley's mass rapid transit (MRT). Its minimum required investment of RM1,000 made it possible for small investors to take part, particularly as this is for a national infrastructure project. This first retail sukuk, which was guaranteed by the Malaysian government, would most likely encourage others to issue retail private debt securities such as conventional bonds and Malaysian Government Securities (MGS) to the public as well.

The government had also announced that incentives will be given to companies that issue bonds and sukuk. These incentives include double tax deductions for a period of four years for additional expenses incurred in such issuances.

AXIATA Celcom Transmission (M) Sdn Bhd. Axiata Bhd issued RM5 billion nominal value Murabahah Sukuk on 15 June 2012. All proceeds from the sukuk programme were intended for the refinancing of the issuer's existing debt, payment of fees and expenses (if any) related to the refinancing of the debt, payment of fees and expenses related to the sukuk programme, funding of capital expenditures and working capital, and other corporate and funding purposes provided that such utilisation will be shariah compliant.

Why Islamic Project Financing?

In recent years, many sukuk fundraising were meant to finance an infrastructure development. The PPP model—where the government has

allowed the private sector to participate either through the involvement of government-linked companies (GLCs) or through creation of SPVs—is clearly visible here. In this model, even though the interest in infrastructure development is of the public, the way the fund is raised is very much with the private sector's involvement.

In Malaysia, total sukuk issuances have now surpassed that of bonds, indicating that it is more attractive to raise funds through sukuk rather than conventional ways. Islamic instruments, specifically sukuk or Islamic bonds, are increasingly becoming the preferred financing option in view of the benefits derived from sukuk financing.

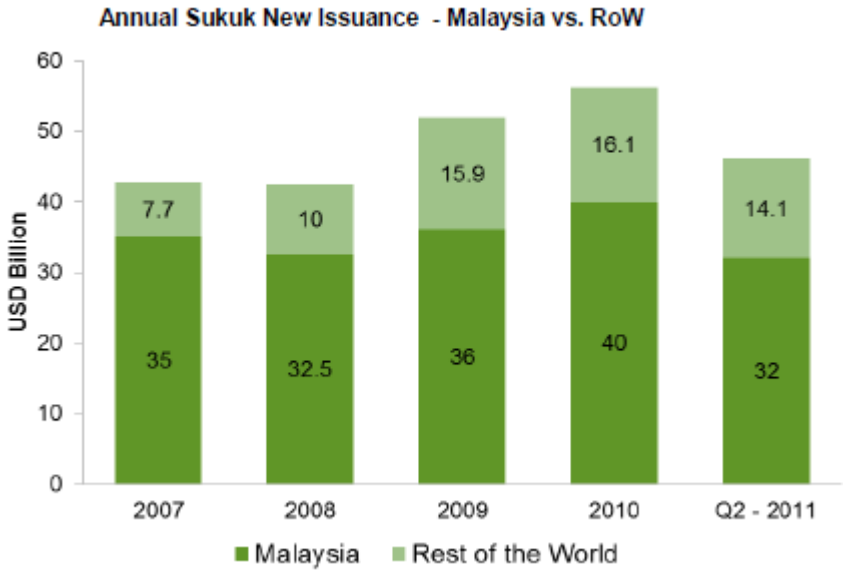
Below are some factors that explain why sukuk is attractive as an option in infrastructure financing:

1) Lower cost of funds
   - No stamp duty imposed
   - Better yield given the greater demand from a wider investor base and lower cost of funds
   - Ability of the Malaysian capital market to attached large liquidity
2) Tax incentives (for both issuers and investors)
   - Tax deduction for issuers
   - Tax neutrality for SPVs
3) Flexibility
   - An array of shariah contracts to cater to varying investors' risk appetites
4) Diverse investor base
   - Larger investor base, both local and global players
5) Greater transparency
   - Obligation of full disclosure to investors
   - Prohibition of excessive leveraging
6) Enhanced security for investors
   - Collateralised or backed by assets
7) Supportive regulatory and legal framework
   - Strong regulations by Bank Negara Malaysia (Bank NM) and Securities Commission Malaysia (SC)
   - Robust legal framework that support Islamic Capital Market
   - Framework that provide issuers and investors' protection

Malaysia as a Leading Global Sukuk Market

- Malaysia's Islamic Financial System boasts of assets valued at RM1.416 trillion (EUR 351.68 billion). Malaysia is the global leader in the sukuk market as it accounts for 62.7 percent share of the outstanding sukuk globally in 2011. It is number one on terms of industry asset size and activity, and it continues to be a market leader until now. The successful of sukuk issuance is influenced by increasing infrastructure spending and strong infrastructure pipeline supply.

Figure 5.10: Annual Sukuk New Issues – Malaysia vs. Rest of the World



Source: KFH Research Ltd. and Kuwait Finance House (2013)

Conclusions

Enhancing ASEAN Connectivity through New Modes of Financing: Exploring Islamic Finance

Malaysia can be considered as leading the ASEAN in the use of the PPP model in infrastructure financing. It started back in the 1980s, when agencies that were responsible for many of the infrastructure development were

privatised. This enabled the development of major infrastructure projects, including major highways across the country, airports such as the KLIA, and communications facilities.

In recent years, another option on project financing has emerged: The Islamic project financing, particularly the use of sukuk, for Malaysia's infrastructure activities. As a world leader on Islamic finance, Malaysia is poised to leverage on current conditions and further to enhance the use of sukuk for its infrastructure development. As the sukuk market is already established in Malaysia—i.e., around 63 percent of the global outstanding sukuk were issued in Malaysia—the cost of funds raised through Islamic financing is cheaper than the conventional way. Thus, at least in Malaysia, it makes more business sense to raise funds through sukuk issues than through bonds.

How does the ASEAN benefit from Malaysia's role as world leader in Islamic finance? How can issues of ASEAN connectivity be resolved through Islamic financing? Certainly, some Malaysian success stories in project financing can be replicated in other ASEAN member states. Other ASEAN countries can issue their own sovereign sukuk so as to raise funds for infrastructure financing.

How viable is this options when markets are not familiar with Islamic finance and sukuk? This question needs to be analysed from the issuers and investors' perspective.

On the issuers' perspective, countries need to be ready in terms of the legal environment before they issue sukuk. This includes taxation laws. To be able to make Islamic financing attractive or at least not penalising, countries need to have tax neutrality. A few countries have undergone tax reforms to allow for tax neutrality before issuing sukuk and be more involved in Islamic finance. Countries such as Singapore, Thailand, and Indonesia are rather well ahead in terms of the infrastructure to support the Islamic finance industry and have either issued sukuk and other Islamic instruments or are well on their way to devising and reforming laws to make it possible to issue sukuk.

For the Cambodia-Lao PDR-Myanmar-Viet Nam (CLMV) countries, without the proper legal infrastructure, issuing sukuk would be rather costly. However, a viable option is for sukuk to be issued from Malaysia as a fundraising activity for projects in CLMV through a special purpose vehicle so as to

leverage on Malaysia's leading position in Islamic finance and take advantage of the associated benefits.

Would sukuk raised in CLMV be attractive to global investors? According to an interview with Noripah Kamso, a leading Islamic finance practitioner (2 August 2013 at CIMB, Kuala Lumpur), the Asian region represents a far more attractive venue to invest compared to some of the developed regions such as Europe. In principle, it is possible to raise bonds or even sukuk in these CLMV countries. However, the credit ratings of these countries could be an issue. Without significant historical experience in bond or sukuk issuance, these countries will not be highly rated enough to be attractive to investors.

Meanwhile, a bond issue would not be any better than a sukuk issue in terms of investor attraction and credit rating. However, assuming there are already elements of trust and credibility pervading among parties involved, it may be worthwhile to find a way to structure the sukuk so as to attract Islamic investors across the globe who are always on the lookout for new shariah-compliant products. Currently in the Islamic finance space, demand outstrips supply. Such global demand, coupled with Malaysia's position as leader in Islamic Finance, is reason enough for other ASEAN countries to also consider Islamic financing as another way to fund infrastructure activities.

Developments and trends in the global and ASEAN markets suggest some factors that can support the growth of Islamic project financing. These include:

- ASEAN as part of a fast-growing Asian economy;
- Ability to attract liquidity from Asian and Gulf Cooperation Council (GCC) Islamic and non-Islamic investors;
- Growing global interest on sukuk as a financing instrument and on wealth management tools for corporate and retail investors;
- Malaysia is the world’s leading Islamic finance hub with the most comprehensive market infrastructure;
- Nearby Singapore is an upcoming Islamic finance “hot spot”;

- Large Muslim population and a supportive market coming from Indonesia;

Challenges: Islamic Financing as a PPP Mode for Infrastructure Financing in ASEAN Countries

- Markets' unfamiliarity with Islamic finance, especially in non-Muslim countries (Note: In the case of sukuk, investors are usually corporations and institutions, and global sukuk can be structured to attract sophisticated global investors familiar with the instrument);
- Laws of the land that are not friendly to sukuk and Islamic contracts. This will take time before the country becomes legally ready to issue sukuk. (This can be resolved though by using other countries such as Malaysia or Singapore as country of domicile or issuing country.);
- If a country has no record in bond or sukuk issuance or does not possess good country ratings, sukuk issued may be given poor credit ratings, thus reducing its credibility as well as the takeup rate by investors;
- Persistent and wrong perception that Islamic finance and sukuk are only for Muslims and that a predominantly Muslim country will tend to prevent a Muslim-minority country from looking at Islamic financing as a viable option.

Recommendations

The ASEAN member countries can look at Malaysia and learn from its success stories on the PPP model as well as the more recent modes of Islamic financing, particularly the use of sukuk as a tool to fund infrastructure projects. Financing agencies such as the ADB may also replicate the success of the Islamic Development Bank on sukuk issuance for many of its infrastructure projects.

Countries in the ASEAN may further consider leveraging on the comprehensive and complete Islamic finance market in Malaysia, where an established legal and regulatory framework as well as the human capital and

other infrastructure had been developed over the past 30 years. Sovereign sukuk of neighbouring ASEAN countries can be issued using Malaysia as a platform, thus enhancing ASEAN connectivity. Islamic financing instruments—sukuk, in particular—should not be viewed as a financing tool for Muslim countries or Muslim investors only. It is worthwhile for other ASEAN countries to explore sukuk's usefulness for their own infrastructure projects.

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Annex A: Area, Population, and Age Structure

Table 5.A1: Area

Area	Sq. Km.
Peninsular Malaysia	132,631
Sabah & Labuan	73,722
Sarawak	124,450
TOTAL	330,803

Table 5.A2: Population

Number (Mid-year)[1/]	Unit	2008	2009	2010	2011	2012
	mil	27.5	27.9	28.3	28.6	28.9
Growth	% p.a.	1.3	1.3	1.3	1.1	1.1
Density	per sq.km	84.4	85.0	85.0	86.3	87.2

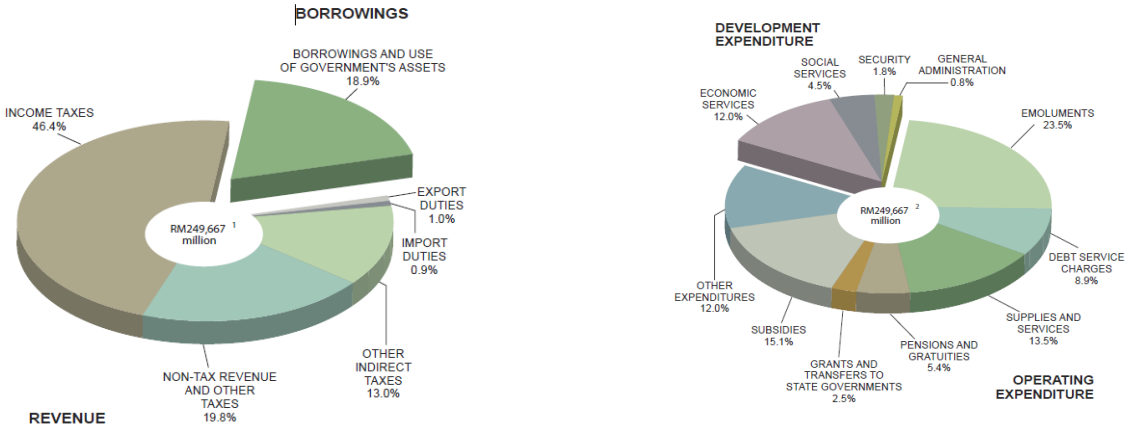
Table 5.A3: Population Age Structure

Age group	2008		2009		2010		2011		2012	
	mil	% of Total	mil	% of Total	mil	% of Total	mil	% of Total	mil	% of Total
0 - 14	7.8	28.2	7.7	27.7	7.7	27.2	7.7	27.1	7.6	27
15 - 64	18.5	67.3	18.9	67.7	19.2	68.1	19.5	69.1	19.8	70.1
65 & above	1.2	4.5	1.3	4.6	1.3	4.7	1.4	4.9	1.4	5.1

Source: Department of Statistics, Malaysia.

Annex B: National Budget 2013

Figure 5.B1: Government Revenue and Expenditure 2013 (Budgeted)



Note: [1]Include revenue, borrowings, and use of government assets, [2] Excludes contingency reserves
Source: Ministry of Finance.

Annex C: PPP in Malaysia

Figure 5.C1: PPP Structure

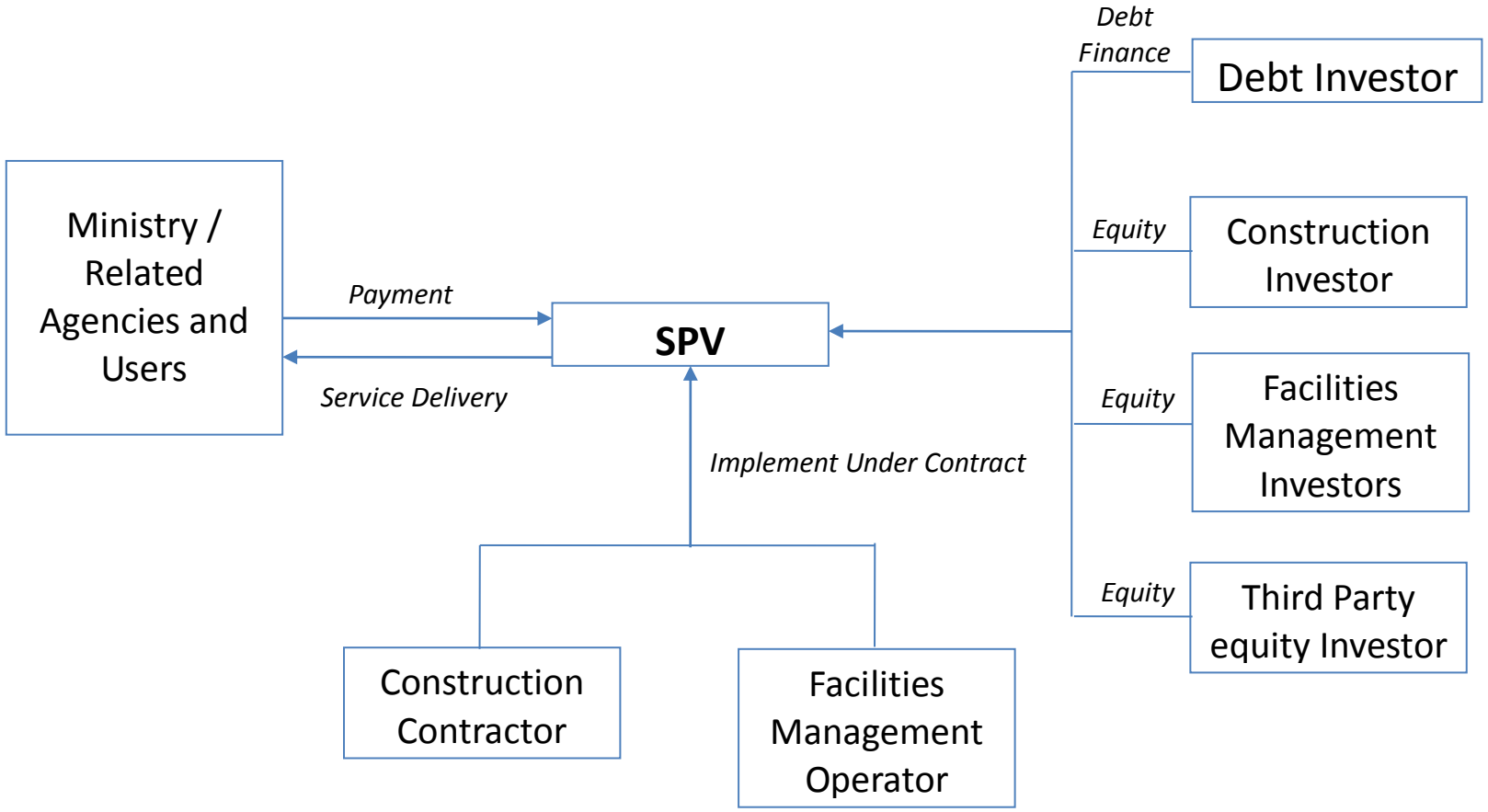


Table 5.C.1: Comparison: Privatisation, PPP, and Conventional Methods of Procurement of Public Services

Privatisation	PPP	Conventional
• Funding via private financial resources without implicit or explicit public sector guarantee. • No impact on the level of public sector expenditure. • Risks are entirely borne by the private sector. • Government acts as regulator. • Long duration of relationship with private contractors. • Applicable for projects with high commercial viability.	• Funding via private financial resources without public sector's explicit guarantee. • Impact on public budget spreads over the duration of the concession. • Risks are allocated to parties that can manage them most efficiently • Public sector's involvement is through enforcement of pre-agreed KPIs. • Long duration of relationship with private contractors. • Applicable for projects with commercial viability.	• Procurements are funded directly via public budget. • Immediate impact on public sector financial position. • Risks are entirely borne by public sector. • Extensive public sector involvement at all stages of project life. • Relationship with private contractor is short term. • Applicable for projects with high socio-economic returns and those justified on strategic considerations.

Source: UKAS, 2009, p. 7 (www.ukas.gov.my).

Table 5.C.2: Sample PPP Projects in Malaysia

Here are more detailed descriptions on three of Malaysia's PPP projects that have been implemented successfully.

PPP Project	Project description
North South Expressway	The North South Expressway (NSE) is Malaysia's ultra-modern highway that spans across Peninsular Malaysia, from the border with Thailand in the north to the border with Singapore in the south. The 973-km highway was completed in 1988. The NSE is operated by the concessionaire, Projek Lebuhraya Utara Selatan Malaysia Bhd or PLUS. It is implemented via the Build-Operate-Transfer (BOT) mode of PPP. The concession period is for 48 years.
SMART Tunnel	The Stormwater Management and Road Tunnel (SMART Tunnel) project is a special project that combines a system of traffic dispersal (to reduce congestion in downtown Kuala Lumpur) and a flood-mitigation initiative (to reduce the occurrences of flash flood in Kuala Lumpur). The project was awarded to a joint venture between MMC Corporation and Gamuda Bhd and was completed in 2007. The tunnel component of the project, built at a cost of RM1.9 billion, will be recovered by the concessionaire via collection of toll fees for a period of 40 years.
Putrajaya	Putrajaya has been Malaysia's new administrative capital since 1999. It is situated 25 km south of Kuala Lumpur. The project is undertaken by Putrajaya Holdings, a company with PETRONAS (the National Petroleum Corporation of Malaysia), Khazanah Nasional Bhd (a Malaysian government investment arm), and Kumpulan Wang Amanah Negara as shareholders. The project was implemented via the Build-Lease-Transfer (BLT) mode of PPP. The development, covering an area of 4,930 ha, includes modern buildings for government offices, residential, and commercial facilities that would cater to a population of 500,000.

Figure 5.C.2: Sector Distribution of PPP Projects 1983-2012 (% of total)

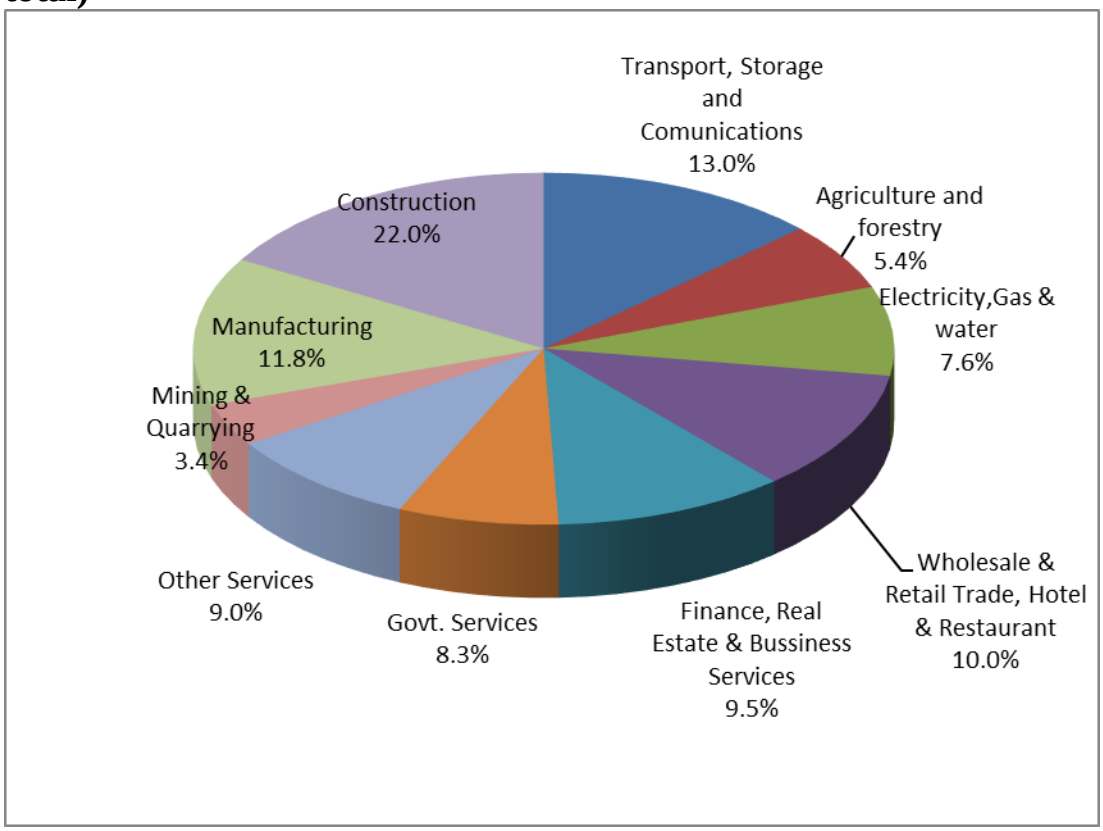


Table 5.C.3: Major Roads Projects, 1995-2005

MAJOR ROAD PROJECTS IMPLEMENTED

1995-2005

Project	*Length (km)*	*Completion (Year)*
COMPLETED PROJECTS		
i. Government-Funded Projects		
Access Road to Kulim Hi-Tech Industrial Park	9	1996
Kota Tinggi Bypass	10	1997
Eastern Access to KLIA	17	1998
Berungis-Kota Belud Highway	38	1998
Middle Ring Road II (Phase I)	35	1998
Access Road to Belaga, Sarawak	126	1999
Kuala Perlis-Changloon Highway	36	2000
Access Road to Port of Tanjung Pelepas, Johore	8	2000
Sungai Dinding Bridge	10	2000
Upgrading of B15	10	2000
South Klang Valley Expressway Section 1A	11	2000
Access Road to Toxic Water Plant in Bukit Nenas, Negeri Sembilan	17	2000
ii. Privatised Projects		
Butterworth-Kulim Highway	17	1996
Seremban-Port Dickson Highway	22	1997
North-South Expressway Central Link	48	1997
Shah Alam Expressway	35	1998
Second Link to Singapore	45	1998
Kuala Lumpur-Karak Highway	60	1998

MAJOR ROAD PROJECTS IMPLEMENTED

1995-2005

Project	*Length (km)*	*Completion (Year)*
Cheras-Kajang Highway	12	1998
Damansara-Puchong Highway	40	1998
Upgrading Sungai Besi Road	16	1999
UNDER CONSTRUCTION		
i. Government-Funded Projects		
Upgrading Beaufort-Sindumin Road	65	2001
Beaufort-Mempakul Road	64	2001
Lipat Kajang (Melaka) Interchange to North-South Expressway	2	2001
Sungai Rejang Bridge	7	2001
Brinchang-Lojing Road	22	2001
East-Coast Highway	169	2003
ii. Privatised Projects		
New North Klang Straits Bypass	18	2001
Western Kuala Lumpur Traffic Dispersal Scheme	26	2001
New Pantai Highway	20	2003
Kajang-Seremban Highway	48	2004
Butterworth Outer Ring Road	19	2004
Ipoh-Lumut Highway	70	2004
Kajang Traffic Dispersal Highway	37	2004

Source: Ninth Malaysia Plan, 2006.

Table 5.C.4: Recent and Upcoming PPP Projects in Malaysia, 2011-2015

Road Sector	• Seven highway projects amounting to an estimated RM19 billion, including: – West Coast Expressway – Guthrie-Damansara Expressway – Sungai Juru Expressway – Paroi-Senawang-KLIA Expressway – Ampang-Cheras-Pandan Elevated Highway
Rail and Transport	• Integrated Transport Terminal in Gombak, Selangor • Mass Rapid Transit (MRT) project in Greater Kuala Lumpur (RM40 billion) • Kuala Lumpur – Singapore High-Speed Rail covering 400 km (RM18.6 billion – currently in feasibility stage) • East Coast Rail route (RM29 billion – currently in feasibility stage)
Power	• Two-coal electricity generation plants (RM7 billion) • 300-megawatt Combined-Cycle Gas Power Plant in Kimanis, Sabah (RM1.5 billion) • Construction of the liquefied natural gas regassification by Petronas in Melaka (RM3 billion)

Education	• Perdana University, a joint venture between Academic Medical Centre Sdn Bhd and John Hopkins • Medicine International as well as Royal College of Surgeons Ireland (RM2 billion) • Five Universiti Teknologi MARA (UITM) branch campuses • International Islamic University Malaysia Teaching Hospital in Kuantan (RM413 million)
Port	• Privatisation of Penang Port Sdn Bhd
Others	• Development of Malaysian Rubber Board's 3,300 acre land in Sungai Buloh, Selangor (RM10 billion) • Redevelopment of the Angkasapuri Complex Kuala Lumpur as Media City • Kuala Lumpur Strategic Development by 1MDB; Sungai Besi Airport area • International Financial District in Kuala Lumpur (RM26 billion) • Two aluminium smelters in Sarawak Corridor of Renewable Energy (SCORE)

Sources: Chan (2012).