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# How Malaysian Politics Shaped Chinese Real Estate Deals and Economic Development

Guanie Lim and Keng Khoon Ng



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## China Local/Global

China has become a global power, but there is too little debate about *how* this has happened and what it means. Many argue that China exports its developmental model and imposes it on other countries. But Chinese players also extend their influence by working through local actors and institutions while adapting and assimilating local and traditional forms, norms, and practices.

With a generous multiyear grant from the Ford Foundation, Carnegie has launched an innovative body of research on Chinese engagement strategies in seven regions of the world—Africa, Central Asia, Latin America, the Middle East and North Africa, the Pacific, South Asia, and Southeast Asia. Through a mix of research and strategic convening, this project explores these complex dynamics, including the ways Chinese firms are adapting to local labor laws in Latin America, Chinese banks and funds are exploring traditional Islamic financial and credit products in Southeast Asia and the Middle East, and Chinese actors are helping local workers upgrade their skills in Central Asia. These adaptive Chinese strategies that accommodate and work within local realities are mostly ignored by Western policymakers in particular.

Ultimately, the project aims to significantly broaden understanding and debate about China's role in the world and to generate innovative policy ideas. These could enable local players to better channel Chinese energies to support their societies and economies; provide lessons for Western engagement around the world, especially in developing countries; help China's own policy community learn from the diversity of Chinese experience; and potentially reduce frictions.

Evan A. Feigenbaum

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## Summary

Iskandar Malaysia is the oldest and by far the most prominent economic corridor in Malaysia. Located in the southernmost state of Johor, the corridor came to host several real estate developments (such as Princess Cove and Forest City) involving multinational corporations (MNCs) from China almost immediately after the Belt and Road Initiative (BRI) was launched in 2013. On one level, the infrastructure-spending spree associated with the BRI helped boost Malaysia's economy as Chinese real estate MNCs invested in Iskandar Malaysia to grow their overseas portfolios. However, their involvement in the corridor disrupted the existing dynamics between Malaysia's central and local governments.

Although these Chinese projects offered an opening for Johor's state government to counter Putrajaya's dominance in the economic corridor, some swiftly became a magnet for divisive electoral campaigning and voter anger. Combined with several socioeconomic issues, the discontent generated by these Chinese real estate projects contributed to the unexpected defeat of the long-ruling United Malays National Organization (UMNO) in Malaysia's May 2018 general election. Chinese real estate MNCs have sought to adapt to these shifting dynamics, yet it is uncertain to what degree their adaptive strategies will bear fruit amid a looming real estate crisis back in China and other related issues.

Ultimately, Chinese real estate investment has been both a tool and an enabler of efforts undertaken by various Malaysian stakeholders, rather than the all-powerful China-imposed juggernaut that some commentators on Malaysia's development over the last two decades have tended to see. Despite the allure of lucrative real estate deals, it is equally important to recognize the potential pitfalls when local politics go awry. Events in Iskandar Malaysia demonstrate that it is politically unsustainable to push real estate projects that are too expensive for most local residents to afford.

## Introduction

The 1997 Asian financial crisis had far-reaching economic effects throughout the region. For one thing, it dramatically interrupted the heady growth Malaysia had enjoyed in the 1980s and the early to mid-1990s. In its aftermath, the government in Putrajaya sought to revive the country's economic fortunes by exploring alternative economic strategies in the 2000s. Notably, Malaysia's central government began to target Asian investors in particular, including capital providers and businesses from Singapore, Japan, and eventually China.

Because of its rapidly growing economy and relatively cordial ties with Malaysia, China became an especially attractive prospective investment partner during this period. By the mid-2000s, Malaysian policy planners had begun to foster regional economic corridors to better attract international capital, but these corridors cut across multiple Malaysian subnational states. The central government intended to support high-priority sectors, especially in less developed parts of the country, and to spread projects among multiple geographic areas to ensure greater national synergies across state-level jurisdictions. Although investment in manufacturing has been encouraged, these corridors also have targeted the services sector. In 2006, the first such corridor—Iskandar Malaysia—was launched in Johor, the southernmost state of peninsular Malaysia. By the early 2010s, four other regional corridors had been established.<sup>1</sup>

But because these corridors cut across states and given Malaysia's federal system of government, they soon became caught up in the tug-of-war of local politics, as Malaysia's central and local governments jockeyed to attract capital for their own preferred projects and priorities. Thus, what has appeared to many outsiders to be an aggressive Chinese push into Malaysian real estate came to reflect many of the *local* features of Malaysia's diverse, increasingly contested political system.

Iskandar Malaysia, the oldest and by far most prominent of these corridors, has become a test bed for adaptive Chinese investment strategies in Malaysia. Malaysian federal and local players have leveraged Chinese foreign direct investment (FDI) to meet the country's needs, but Chinese players and interests have adapted with limited success to Malaysian politics by seeking to diffuse political opposition to their high-end residential real estate ventures. Upon closer inspection, it is clear that Chinese investment (and by extension, other sources of foreign capital) is both a tool of and accomplice to the efforts various Malaysian stakeholders have made to meet their developmental, commercial, and sometimes political priorities, not the all-powerful China-imposed juggernaut of capital that some commentators on Malaysia's development over the last two decades have tended to see.<sup>2</sup>

In fact, state officials from Johor welcomed Chinese multinational corporations (MNCs) for their own purposes—namely, to counter the Malaysian *federal* government's encroachment into Iskandar Malaysia. This domestic political interplay, pitting a local government and its priorities against those

of Putrajaya, is most clearly observed in the case of Forest City, a luxury real estate project within the corridor developed by a Guangdong-based Chinese firm called Country Garden.

In addition to being engulfed in a tug-of-war between Putrajaya and Johor, Forest City was soon singled out by the national opposition bloc (Pakatan Harapan), captained by Mahathir Mohamad, who has served multiple stints as prime minister from 1981 to 2003 and again from May 2018 to March 2020. Combined with other hot-button topics, the project undermined voters' confidence in the long-ruling United Malays National Organization (UMNO) in the May 2018 general election and heralded the defeat of the party, which was then at the helm of both the federal government and the subnational governments of multiple states including Johor.<sup>3</sup>

Put bluntly, Chinese real estate MNCs' challenges in Malaysia have owed much both to their own lack of business acumen and the fluid political dynamics in the host economy. Of course, these Chinese projects also have been affected by wild card events, including China's capital controls in 2017 to curb the outflow of funds and stabilize the Chinese renminbi.

The paper begins by examining the gradual deceleration of the Chinese economy since the late 2000s. The slowing economy meant that domestic firms were running out of lucrative low-hanging fruit in China, which pushed some of them to look for more investment opportunities offshore. Although industrial overcapacity and an inability to more vigorously stimulate consumption affected different Chinese industries unevenly, the impacts of these forces were borne heavily by real estate MNCs. For these Chinese firms, the 2013 promulgation of the Belt and Road Initiative (BRI), a multitrillion-renminbi program by the Chinese government to invest in overseas infrastructure, offered a strategic avenue to pursue development abroad.

The next section turns to Iskandar Malaysia, how the corridor evolved, why it attracted Chinese investors, and how it developed both before and after the establishment of the BRI. Once this corridor was established, it became a major focus of competition for capital and physical resources between Malaysia's central government and Johor. Chinese MNCs internalized this dynamic and became part of the story of the corridor. This section discusses how and to what extent some Chinese real estate projects in Iskandar Malaysia, especially Forest City, became politicized by Mahathir and his allies. The final section outlines recommendations both for stakeholders in countries like Malaysia that are wrestling with Chinese investment and for Chinese corporations as they navigate complex local investment environments.

## How Real Estate Developments in China Pushed Local Firms Offshore

The 2007–2008 global financial crisis had widespread economic effects both in major economies like China and the United States and in emerging markets such as Malaysia. It shrank demand in Western markets (and, to a lesser extent, in Japan). Meanwhile, Chinese policymakers wasted no time in pump-priming the Chinese economy. The Chinese government implemented an aggressive stimulus package worth as much as 4 trillion renminbi (\$586 billion).<sup>4</sup> Much of this money went to infrastructure projects such as ports, real estate ventures, and high-speed railways. The financial crisis also put a damper on the export-reliant Malaysian economy, prompting a search for alternative engines of growth.<sup>5</sup>

China's 2008 fiscal stimulus package intensified the country's already heavy reliance on fixed capital formation, while pushing down the shares of both exports and household consumption in terms of gross domestic product (GDP).<sup>6</sup> In the short run, this investment glut staved off a recession. However, overcapacity, soaring government debt, and other challenges had materialized by the early to mid-2010s to complicate China's economic expansion. Chinese politicians, bureaucrats, and economists have since gradually come to accept that annual GDP growth will slow to between 7.0 and 7.5 percent per year from the double-digit levels achieved in the past.<sup>7</sup>

This slowdown was one of the major reasons for Chinese President Xi Jinping's 2013 move to promote the BRI, regarded by many as arguably China's most crucial tool of economic and strategic engagement with the rest of the world.<sup>8</sup> Although there are multiple interpretations of how the BRI should be defined and operationalized, analysts generally agree that the exporting of capital-intensive infrastructure constitutes a key component of the initiative.<sup>9</sup> For Chinese real estate MNCs, the BRI was a godsend. As early as 2010, there was already speculation that China's real estate bubble would soon burst.<sup>10</sup> Around this time, commentators began to note the emergence of several "ghost towns" in remote parts of China where many housing units remained unoccupied.<sup>11</sup> Such projects were usually pushed by local governments, in conjunction with real estate companies and their backers. When Beijing announced the BRI in 2013, some of these Chinese real estate MNCs took it as an opportunity to undertake projects outside of China or otherwise diversify into new businesses.

For example, the Wanda Group, at one point one of the country's largest real estate MNCs, was once renowned for its sprawling global business empire. In the years immediately before and after 2013, this firm poured money into overseas businesses, especially in the entertainment industry, in a bid to "enhance Chinese culture [and] the country's soft power."<sup>12</sup> Some of its most eye-catching deals included the 2012 acquisition of AMC Entertainment Holdings (the second-largest U.S. cinema chain at the time and eventually the nation's largest) and the 2013 purchase of a luxury property on

Nine Elms Lane on the southern bank of London's River Thames.<sup>13</sup> Some observers said that the AMC deal in particular helped to enhance the Wanda Group's standing with the Chinese Communist Party as it provided the firm with a strategic avenue to sway public opinion in the West.<sup>14</sup> Diversifying into other business lines, pushing capital overseas, and serving the aims of the Chinese Communist Party became useful strategies for Chinese real estate players in the years after the launch of the BRI.

Several real estate MNCs decided to explore opportunities in China's near abroad, particularly in Southeast Asia. In Malaysia, they found a host economy with a relatively pro-business environment. In addition to its 30-million-strong population, Malaysia offers an outlet to the wider Southeast Asian market.<sup>15</sup> The two countries also enjoy a cordial relationship as Malaysia was one of the first countries in Southeast Asia to establish diplomatic ties with China (in 1974).<sup>16</sup> Former Malaysian prime minister Najib Razak (2009–2018) courted Chinese MNCs to push high-profile development endeavors.<sup>17</sup> Some of the most prominent Chinese projects begun by Najib—and continued by successive prime ministers—include the East Coast Rail Link, the Malaysia-China Kuantan Industrial Park, and the China-Malaysia Digital Free Trade Zone.<sup>18</sup> As of 2021, Chinese firms are the third-largest source of FDI in Malaysia with aggregate FDI totaling 31.3 billion ringgits (\$7.5 billion). Chinese MNCs trail only their counterparts from the Netherlands (78 billion ringgits or \$18.6 billion) and Singapore (47.3 billion ringgits or \$11.3 billion).<sup>19</sup>

## The Origins of the Iskandar Malaysia Corridor

Starting in the early 1970s, Malaysia began industrializing aggressively by attracting FDI, taking advantage of its low labor costs and favorable position between East and West. The 1997 Asian financial crisis interrupted Malaysia's hitherto heady growth trajectory. While the economic contraction in the country was not as serious as those of other regional economies, its unorthodox response, promoting expansionary (not contractionary) policies, attracted a mixed response from the international community. Some observers were skeptical of certain Malaysian policies, particularly the imposition of capital controls, but more detailed analysis reveals that these measures helped to stabilize market confidence during the downturn.<sup>20</sup> Investor confidence only returned in the mid-2000s, by which time Malaysia had to face another cohort of late-developing economies in the region such as Cambodia and Vietnam. For Malaysian policymakers, it was no longer sufficient to rely on their prior strategy of competing on the basis of lower business costs, especially to attract labor-intensive manufacturing. This was when Malaysian policymakers began shifting to the promotion of regional economic corridors.<sup>21</sup>

While these corridors still promote manufacturing, the service sector began to receive more attention. Some analysts attribute this pivot toward services more to policymakers' view of manufacturing.<sup>22</sup> The electrical and electronics industry, which played a major role in Malaysia's economic progress from the 1970s up until that point, was "seen to . . . be 'unstable,' and insufficiently value-added, with the implication that marketing and promotion efforts should be directed elsewhere."<sup>23</sup> By the mid-2010s, construction, a key component of the services sector, had expanded more rapidly than many other major industries (see table 1).

TABLE 1  
**Production Index of Key Industries in Malaysia**

|      | Construction | Manufacturing | Mining | Electricity |
|------|--------------|---------------|--------|-------------|
| 2010 | 100.0        | 100.0         | 100.0  | 100.0       |
| 2011 | 110.8        | 105.7         | 94.8   | 102.0       |
| 2012 | 114.4        | 111.3         | 96.2   | 107.2       |
| 2013 | 121.2        | 116.0         | 97.0   | 113.1       |
| 2014 | 130.6        | 123.0         | 99.8   | 118.4       |
| 2015 | 136.7        | 128.9         | 104.8  | 121.2       |
| 2016 | 140.9        | 134.5         | 107.2  | 131.5       |

**SOURCE:** Authors' calculations based on data purchased from CEIC Data Manager.

**NOTE:** The 2010 figures in this table represent baseline values against which subsequent years are measured.

Against this backdrop, Chinese MNCs planning to develop their international portfolios began to turn their attention to Malaysia and to Iskandar Malaysia in particular. The corridor came to host several of these real estate MNCs almost immediately after 2013. Some of the highest-profile projects announced (and being developed) include Princess Cove and the aforementioned Forest City. However, the MNCs' entry into Iskandar Malaysia did not take place in a vacuum, nor was it a wholly one-sided affair in which supposedly unsuspecting locals were caught off-guard by a massive influx of Chinese money.

Rather, Chinese investment soon got caught up in elite competition between Malaysia's federal government and state officials in Johor. These national and state government officials have long been locked in a competition to establish the economic and political order in the Iskandar Malaysia corridor by inviting their preferred coalition partners to participate in projects and seeking to exclude rival factions. Viewed in this way, the Chinese real estate MNCs are not only accomplices of these federal and local Malaysian elites but also have their autonomy circumscribed by political affairs in the host economy.

To see why, it is useful to go back to Iskandar Malaysia's origins and subsequent evolution. The corridor was launched in 2006 as the Malaysian government attempted to reignite the economy after a sluggish stretch following the 1997 Asian financial crisis. Khazanah Nasional Berhad—Malaysia's sovereign wealth fund, which is known by the shorthand Khazanah—was the main planner for this economic corridor at the southern tip of peninsular Malaysia.<sup>24</sup> Drawing inspiration from the Shenzhen model of special economic zones and broader metropolitan development areas, as well as Shenzhen's geographic proximity to prosperous Hong Kong, Khazanah officials envisioned the corridor encompassing an area as wide as 2,217 square kilometers.<sup>25</sup> In a parallel to the ties between Shenzhen and Hong Kong, Iskandar Malaysia aimed to leverage its proximity to affluent Singapore by recreating the business climate of the prosperous city-state.<sup>26</sup>

Five flagship zones were created in the Iskandar Malaysia corridor: A (Johor Bahru City Centre), B (Iskandar Puteri, formerly known as Nusajaya), C (Western Gate Development), D (Eastern Gate Development), and E (Senai-Skudai). Flagship Zones A and B have attracted the most attention from foreign investors (especially real estate developers) because of their more urbanized setting and connectivity to Singapore. Flagship Zones C, D, and E, by contrast, have been primarily geared toward attracting industrial capital.<sup>27</sup> To attract global investors, the Malaysian federal government liberalized most economic activities, while offering generous fiscal incentives. It also loosened its decades-old New Economic Policy—a vehicle for redistributing income along ethnic lines—within Iskandar Malaysia.<sup>28</sup>

And yet the corridor has arguably not lived up to its hype. For one thing, the mere creation of Iskandar Malaysia disrupted the revenue streams of Johor's state government. Before it was established, the government of Johor had enjoyed a near-monopoly on land sales in the state through a state-owned enterprise (SOE) called the Johor Corporation.<sup>29</sup> But an uneasy dynamic emerged because of the creation of a joint venture company, Iskandar Investment Berhad (IIB), which was tasked with pushing the development of Flagship Zone B within the corridor.



IIB was formed by two federal agencies—Khazanah and the Employees’ Provident Fund—and the commercial arm of Johor’s state government, an entity known as Kumpulan Prasarana Rakyat Johor (KPRJ). However, KPRJ holds only a 20 percent equity stake in IIB, with its federal counterparts holding the lion’s share of the joint venture. Khazanah’s 60 percent share gives it a commanding say, even before one accounts for its status as the architect behind Iskandar Malaysia.<sup>30</sup> Additionally, one of Khazanah’s subsidiaries, UEM Sunrise Berhad, owns large tracts of land in Flagship Zone B. UEM Sunrise Berhad’s landholdings in the area came about after a series of corporate restructurings involving Khazanah in the years after the 1997 Asian financial crisis.<sup>31</sup>

Iskandar Malaysia also has a complex governance structure. Officially, the corridor is governed by the Iskandar Regional Development Authority, a federal statutory body jointly headed by Malaysia’s prime minister and the chief minister of Johor.<sup>32</sup> This means that governing responsibilities are shared by Putrajaya and Johor’s state government, an arrangement quite unlike those of Malaysia’s other economic corridors, where leadership rests almost exclusively with the prime minister. The incongruity of Iskandar Malaysia’s governance structure is especially reflected in how the Iskandar Regional Development Authority has responsibility for development planning, policy formulation, and investment facilitation but lacks the authority to manage land and deliver local services. The latter functions rest with the state government.<sup>33</sup>

The competition to gain revenue from land sales and project development, in addition to the unclear division of labor within the Iskandar Regional Development Authority, has created a schism between the central government and state officials. Despite some efforts to close ranks (such as by making KPRJ a junior partner in IIB), their differences remain challenging to surmount. More prosaically, both sides have seen fit to welcome investors to promote their favored projects, especially luxury real estate ventures. From 2006 to 2012, real estate investment amounted to 35.1 billion ringgits (\$11.7 billion), representing 33.1 percent of the total investment in Iskandar Malaysia. This amount is equivalent to the investment derived from manufacturing (33.1 percent). The rest of the corridor’s investment came from other industrial activities (27.1 percent) and the central government (6.9 percent).<sup>34</sup>

This real estate bonanza, however, has had side effects. It has skewed the housing supply in and around the economic corridor toward high-end units, despite clear political demands from voters to instead promote and favor low- and medium-cost homes.<sup>35</sup> This imbalance, in turn, has impacted the area’s ethnic Malay population the most because they are disproportionately represented in the low-income segment of the population in Johor (and the rest of the country).<sup>36</sup>

## Chinese Money in Iskandar Malaysia

The BRI provided a lifeline to Johor because Chinese real estate MNCs eager to grow their overseas portfolios became key targets of the state as it sought to attract investment for favored real estate projects. Many of these investment funds were subsequently diverted to Flagship Zone A, with land parcels being reclaimed, sold, or leased to Chinese firms to prop up the state government's coffers.<sup>37</sup>

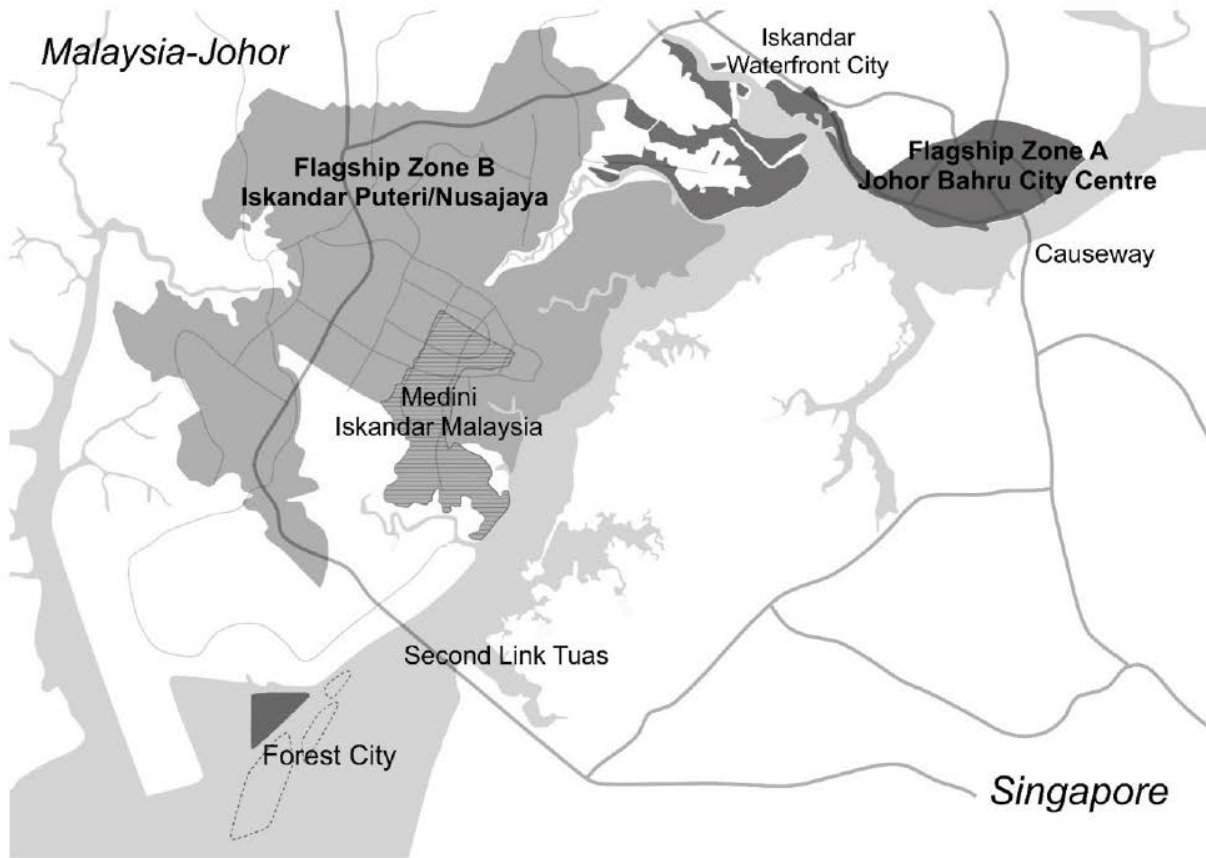
These projects attracted attention from several quarters, raising the corridor's profile. For example, to market their projects in Iskandar Malaysia, virtually all the Chinese MNCs organized subsidized tours to Malaysia for potential buyers, which primarily catered to consumers in China. When reporters questioned Zhang Yuliang, the chairman of the Greenland Group, a Shanghai-based SOE, on his company's foray into Iskandar Malaysia, he cited Malaysia's economic stability, Iskandar Malaysia's proximity to Singapore and other major urban areas, and the country's immigration policies as key factors.<sup>38</sup> In late 2015, former Guangdong governor Zhu Xiaodan (2011–2016) visited some Chinese-financed projects during a working visit to Johor.<sup>39</sup>

The influx of Chinese money into Flagship Zone A also gave those projects promoted by the federal government (largely in Flagship Zone B) a run for their money. Analysts raised concerns about whether the mushrooming of Chinese-financed projects would compete against Medini Iskandar Malaysia, a massive high-end development undertaken mainly by the federal government and its cohort of business groups since 2006.<sup>40</sup> More practically, this center-state competition in high-end real estate does little to ameliorate the increasingly lopsided housing supply in Johor, especially for those in and around Iskandar Malaysia. In addition to demonstrating that the housing supply in the region has been skewed toward higher-end units, researchers argue that the cost of private housing drastically exceeded the limits of housing affordability (median housing price) of 260,000 ringgits (\$65,000) merely a few years after Iskandar Malaysia's inception.<sup>41</sup>

### The Boom Phase

To date, six Chinese-invested projects—Country Garden Danga Bay, Greenland Jade Palace, Helios Cove, Princess Cove, Forest City, and Central Park—have been established.<sup>42</sup> The intermediary role played by KPRJ and Iskandar Waterfront Holdings (a holding company involved in construction, real estate development, and property management services, especially in Flagship Zone A) facilitated the involvement of Johor's state government in these projects either as a land seller or as a joint developer with the Chinese real estate MNCs.

FIGURE 1.  
**Real Estate Development in Iskandar Malaysia**



**SOURCE:** Prepared by the authors

Figure 1 provides a bird's-eye view of how Iskandar Malaysia has hosted two main sets of business groups. Since the nationally oriented Khazanah and parties aligned with it are an entrenched force in Flagship Zone B (the light-colored area), Flagship Zone A (most of the dark-colored area) aimed to house real estate projects driven by the Johor authorities and its allies, not least the Chinese MNCs.

Take Country Garden Danga Bay, for example. It was the first Chinese-financed real estate undertaking in Iskandar Malaysia and the first overseas venture of Guangdong-based Country Garden. This project was relatively well-received by the public, as about 5,000 units were sold during its official launch in August 2013, just months after Country Garden acquired 57 acres of land from Iskandar Waterfront Holdings.<sup>43</sup>

That optimism was shared by the sultan of Johor himself, a popular figurehead especially among ethnic Malays. The sultan proclaimed that Country Garden's expertise would encourage even *more* Chinese MNCs to invest in Iskandar Malaysia, while cementing better Malaysia-China ties.<sup>44</sup> These positive feelings, generated by the Country Garden Danga Bay investment, raised Iskandar Malaysia's profile among Chinese real estate MNCs intending to go out (or *zou chuqu* in Mandarin) under the broad banner of the BRI. In 2014, for example, two major deals were announced to much fanfare. First, the Greenland Group purchased nearly 14 acres of land in Danga Bay from Iskandar Waterfront Holdings for 600 million ringgits (\$183.5 million). Another firm, R&F Properties, based in Guangdong, then bought 116 acres of land (with a portion of reclaimed land) for 4.5 billion ringgits (\$1.4 billion) near the Johor-Singapore Causeway directly from the sultan.<sup>45</sup> The two projects were subsequently developed and branded as Greenland Jade Palace and Princess Cove, respectively.

Country Garden was buoyed by its initial foray into Iskandar Malaysia and those of other Chinese real estate MNCs. It soon launched an even bigger project, namely Forest City (see the dark-colored area on the left side of figure 1). Forest City is a China-Malaysia joint venture involving Country Garden (which holds a 60 percent stake) and Esplanade Danga 88 Sdn Bhd (which has a 40 percent stake).<sup>46</sup> The latter is in turn owned by three parties: the sultan of Johor (with a 64.4 percent stake), KPRJ (with a 20 percent stake), and Daing Malek Daing Rahman, an adviser to the sultan of Johor (15.6 percent).<sup>47</sup>

This project, valued at about \$100 billion, is the most capital-intensive project in Iskandar Malaysia to date.<sup>48</sup> Launched in 2013, the project is to be constructed on an area that spans 1,370 hectares. Forest City is also projected to house 700,000 people, so its advocates' big ambitions are clear: to become Southeast Asia's largest smart city, complete with environmentally sustainable infrastructure.<sup>49</sup> Taking advantage of the site's proximity to the Malaysia-Singapore Second Link, Country Garden has aggressively marketed Forest City as "a prime model of a future city" while offering prospective residents "an exclusive island living paradise."<sup>50</sup> Conceived as four reclaimed islands, this project, as will be shown later, has slowed considerably. As of late 2021, only one of the four islands has been completed. Moreover, only 10,953 homeowners have received their keys as of the end of July 2021.<sup>51</sup>

As much as an estimated 70–80 percent of Forest City is designated for high-end residential units, with the remaining 20–30 percent to be allocated as industrial lots.<sup>52</sup> However, Forest City's average price for a residential unit is around 1,200 ringgits (\$300) per square foot.<sup>53</sup> Such a steep price, nearly equivalent to those of high-end residential units in Kuala Lumpur, suggests that Country Garden is not actively targeting *domestic* buyers. This was because economic opportunities (and by extension, expected capital gains and rental returns) are traditionally higher in Kuala Lumpur com-

pared to those in the rest of the country. Among other things, consider that Kuala Lumpur has higher household incomes on average compared to the rest of Malaysia. In particular, Johor's median household income is only about 61 percent that the size of Kuala Lumpur's.<sup>54</sup>

When asked whether they were aware of Johor's small population size (less than 3.8 million in 2020) and how disproportionately large a population increase of 700,000 would be, sales executives reasoned that this was not an issue to be overly concerned about, at least in the early phases of development. They explained that the expansion is to be pushed through several phases, by which time Johor's population size would also be projected to increase.<sup>55</sup> However, a search on the Malaysian Department of Statistics website revealed that Johor's population growth rate actually hit a peak of 1.4 percent growth in 2018 and has since fallen from those levels. Its yet-to-be-finalized growth rate in 2021 was just 0.5 percent.<sup>56</sup> Given these apparent projections, it seems unlikely that local population growth will be a major driver of demand for the foreseeable future.

The company's primary target, therefore, appears to be *Chinese* customers, not least those on the lookout for a second home and/or retirement property outside of their own country.<sup>57</sup> Perhaps aware of the preference among high-net-worth Chinese investors for more renowned cities such as London and New York, Country Garden focused on China's growing middle class, especially those from second- and third-tier Chinese cities. The basic sales routine has involved organizing holidays paired with site visits to Forest City and the surrounding area. These middle-class Chinese customers were usually flown first to Singapore to spend at least one night before being brought to Johor. The firm's goal is to project the image of Iskandar Malaysia as the next Shenzhen, with neighboring Singapore portrayed as an analogue to Hong Kong during Shenzhen's initial boom years in the 1980s and 1990s. For sales purposes, associating Johor with Shenzhen is vital, given Shenzhen's impressive growth during China's reform and opening-up policy beginning in 1978.

Country Garden saw it as so critical to establish a psychological and legal link between Iskandar Malaysia and Singapore that it aggressively lobbied for a new customs, immigration, and quarantine complex dedicated just to Forest City.<sup>58</sup> In early 2016, the firm even took to advertising Forest City during National Basketball Association games, which are widely watched in China, highlighting selling points such as "duty-free island-based living next to Singapore."<sup>59</sup>

### The Bust Phase

But while attracting *Chinese* investors has been central to Johor's commercial strategy in Iskandar Malaysia, it is *Malaysian* politics, especially central-state dynamics, that really shapes outcomes. For one thing, the influx of Chinese money into Forest City and other projects like it provided an avenue for Johor's state government to recover lost ground in Iskandar Malaysia.

But then the real estate boom there caught the attention of Mahathir, the former prime minister then serving as the leader of Malaysia's Pakatan Harapan opposition bloc. Aiming to make a triumphant return to politics, the veteran politician, beginning in early 2017, singled out Forest City as a target of his anti-government political rhetoric. According to Mahathir, the project had evolved in ways detrimental to Malaysia's national interests because it had led to huge outflows of capital and employment opportunities from ethnic Malays to Chinese firms.<sup>60</sup> He alleged that Forest City's creation opened the gates to Chinese immigration to Malaysia, claiming that Chinese citizens would be given Malaysian identity cards, thus linking what had been a commercial real estate venture to one of the most explosive political topics in Malaysia. He wove an entire political tapestry around these arguments by further alleging that these putative identity cards would enable Chinese property buyers to vote in Malaysian general elections and reshape the country's political equilibrium—implying that this was the intent of the ethnic Malay elites who were promoting the real estate projects.<sup>61</sup>

By conflating homebuyers from China buying property in Forest City with domestic ethnic Chinese citizens of Malaysia, Mahathir sought to attack the project to curry favor with conservative ethnic Malays, eroding the principal vote bank of the ruling party, the UMNO. Many of those Malays, especially those from rural constituencies, remain wary of their ethnically Chinese fellow citizens. And as China itself has become more powerful in the international arena, such fears among conservative Malays have become more pronounced and thus harder to contain or downplay.<sup>62</sup>

Mahathir's broadside was quickly countered by the sultan of Johor, who stated publicly that Mahathir's comments had little basis, saying, "[Mahathir] has gone too far with his twisting of the issue . . . creating fear, using race, just to fulfil his political motives."<sup>63</sup> These public attacks and counterattacks stirred unease among some of the Chinese nationals involved in the project. They believed that Forest City had benefited Malaysia by generating significant employment and business opportunities for the local economy and that such opportunities would never have arisen without Forest City.<sup>64</sup>

One Chinese interviewee told the authors that Country Garden (owing to its Chinese ownership) also got caught up in Malaysia's sometimes explosive ethnic politics, with local Malays painting ethnic Chinese Malaysians and investors from China with the same unnuanced brushstrokes for populist gain. This interviewee lamented that the firm might have underestimated the fluidity of Malaysian politics when it invested in Iskandar Malaysia in the first place. The interviewee previously had had the impression that Malaysia was one of the more politically stable countries in Southeast Asia but now concluded the opposite.<sup>65</sup>

To be sure, some of the firm's local staffers agreed that Country Garden executives from China had very little understanding of commercial practices in Malaysia. One of their complaints was an excessively top-down reporting structure, which meant that on-the-ground information reflecting local considerations and concerns could not be relayed to the senior executives sent from China in a

timely manner. On some occasions, these Malaysian locals felt that senior executives—especially those from China—*intentionally* turned a deaf ear to their ideas. Another common grouse was the firm’s apparent preference that employees, regardless of nationality, work overtime (including on weekends and public holidays) without being directly compensated.<sup>66</sup>

But Forest City was also caught off guard by the Chinese government’s imposition of capital controls in March 2017, a development that indicates that the firm’s Chinese executives may not have understood Chinese politics any better than Malaysian politics. Implemented to curb the outflow of money and stabilize the Chinese renminbi, Beijing’s capital controls aimed to prevent Chinese firms from pursuing foreign investments in an overly exuberant fashion; real estate (alongside entertainment) was one of two industries that came under especially intense scrutiny.<sup>67</sup>

Compounding Country Garden’s misery was a parallel move by Beijing to ban Chinese citizens from converting renminbi into other currencies for overseas property purchases.<sup>68</sup> These moves almost immediately triggered a fall in overseas mergers and acquisitions, so Chinese MNCs that had overleveraged on their buying sprees soon had to downsize or even auction off hard-earned foreign assets. Like Country Garden, Wanda was affected by this sudden change in policy and had to shed significant overseas assets to reduce its debt load and keep its businesses afloat.<sup>69</sup>

To make matters worse, the UMNO and its allies were voted out of office in May 2018, with Mahathir returning to power in Putrajaya as the country’s prime minister. The people’s loss of confidence in the UMNO was so great that it lost control not just in Putrajaya but locally in Johor, its birthplace and stronghold. In Johor, the UMNO and its allies were dealt a mortal blow as Pakatan Harapan took thirty-six out of a total of fifty-six seats.<sup>70</sup> Mahathir’s public critique targeting Forest City certainly played a role in undermining both the national and local UMNO administrations, although other hot-button issues, ranging from perceived corruption to the haphazard introduction of the Goods and Services Tax, also played a role in the ruling party’s defeat.<sup>71</sup>

True to form, Mahathir did *not* adopt a more conciliatory approach to Country Garden upon becoming prime minister. In August 2018, about three months after the watershed general election, Yeung Kwok Keung (also known as Yang Guoqiang), the chair of Country Garden, paid Mahathir a visit at the prime minister’s office. In an apparent attempt to put aside differences, Yeung endorsed the new Pakatan Harapan administration, saying, “I am confident that Malaysia, under the leadership of [Prime Minister] . . . Mahathir Mohamad, will continue to welcome foreign businesses and investors. Therefore, I intend to invest more in Malaysia in the coming years . . . as per the country’s law and regulations.”<sup>72</sup>



However, about one week after their meeting, Mahathir announced in a news conference that Malaysia would not allow foreigners to buy residential units in Forest City, contradicting Yeung.<sup>73</sup> Further embarrassing Country Garden was Mahathir's brief, belated clarification that "they can buy the property, but we won't give them visa[s] to come and live here."<sup>74</sup> Then Zuraida Kamaruddin, who was serving in the cabinet as the minister of housing and local government, placed the project under further scrutiny. She reasoned that she needed to safeguard the interest of locals, especially those from Johor, by restricting property sales to foreigners. To ensure locals were not being sidelined from purchasing homes in Forest City, Zuraida announced that there would henceforth be a tighter screening process to limit the number of foreign home buyers.<sup>75</sup> These moves were basically populist measures that reflected real policy challenges in Malaysia today.

For one thing, the inadequate supply of affordable housing has been a major political issue since at least 2010, years before Country Garden set foot in Iskandar Malaysia.<sup>76</sup> So Forest City's massive introduction of exorbitantly priced residential units worsened the already scarce supply of low-cost housing in the state. Moreover, these new lots disproportionately hurt the prospects of ethnic Malays, who are overrepresented among the country's low-income earners.<sup>77</sup> Similar to the interests of the UMNO, any national administration in Malaysia (not just one led by Mahathir) would need to safeguard this particular group's socioeconomic wellbeing, while being careful not to be overly restrictive toward prospective investors.

The most immediate step Country Garden could have taken to resolve this issue would have been to lower the price of its residential units, thereby reducing the cost barrier of ownership. However, doing so would have indirectly reduced the appeal of the high-end lifestyle that is one of the development's main selling points to wealthy clientele. Another constraint is the sunk costs involved in land reclamation, one of the main reasons for the rather exorbitant price tags of Forest City's real estate.

Instead, what Country Garden has done to adapt to local realities can be observed in other aspects of its business operations. For example, the firm has contributed consistently to corporate social responsibility efforts, ranging from community care to environmental conservation. The most significant part has been channeled to donations and infrastructure upgrades for the surrounding villages affected by the Forest City development. The company also has adopted a number of schools within the vicinity, including SK Morni Pok, SK Pendas Laut, SK Tanjung Kupang, SK Tiram Duku, and SK Tanjung Adang.<sup>78</sup> In addition to infrastructure renovation funds, the company also provides scholarships to needy and deserving students of these schools.<sup>79</sup> Playing its part in environmental conservation, Country Garden has supported the Johor state government's conservation efforts, including a program that released 200 seahorses into the adjacent Sungai Pulai Forest Reserve, which

is an official site designated by the Ramsar Convention on Wetlands.<sup>80</sup> Moreover, it has devoted resources to conserve sea grasses located in the Tanjung Kupang Meadow through a collaborative program with University Putra Malaysia.<sup>81</sup>

While Beijing's capital controls and ban on converting renminbi into other currencies to purchase property abroad have surely hurt developers like Country Garden, these firms could have lessened the impact of these decisions if they had exhibited a deeper understanding of host country politics, especially before committing funds to these projects. Indeed, in a candid public address in late 2018, Country Garden revealed that it might have been overly optimistic in Forest City's early phases. Marking a break from its initial exuberance, the Chinese MNC acknowledged, for the first time, that if demand does falter, it will have to slow down the project's implementation. One senior official explained, "If the demand is there, we will build. If it's not there, we will slow down . . . So there's no worry of a ghost town, oversupply—if the demand is not there, we won't be building."<sup>82</sup>

To be fair, the Chinese MNC has also sought to more clearly align its commercial strategy to address the complaints of Malaysian stakeholders, particularly since the May 2018 election. However, these measures seem to be too little, too late. While its corporate social responsibility programs are welcome, the fundamental issue of inadequate affordable housing in Johor has not been properly addressed. In addition to undercutting Forest City's unique selling point of a high-end lifestyle, a substantial reduction in residential unit pricing would be challenging for the firm to implement because of the high fixed costs of land reclamation.

## Conclusion

The huge, albeit transient, investments that Chinese real estate MNCs have made in Iskandar Malaysia in recent years have been consequential. Nowhere has this trend been more obvious than with Forest City, even as it became a lightning rod for local criticism, especially among ambitious Malay politicians and a broad swath of low-income ethnic Malay voters. Amid broader societal cleavages in Malaysia, the firm became engulfed in popular discontent during the May 2018 general election, and its development projects contributed to the unexpected defeat of the UMNO at the polls. The project attracted notoriety when Mahathir publicly criticized it, using the issues of the income gap and high-priced real estate to campaign against the specter of an alleged alliance between Malaysia's ethnic Chinese citizens and their mainland Chinese counterparts to dominate ethnic Malays.

Still, the tale of Forest City turns heavily on the role of the state of Johor, which both welcomed Country Garden and other Chinese real estate MNCs and incorporated them into its investment promotion strategy. As a quid pro quo for their investment dollars, these Chinese MNCs were given

a high degree of freedom to pursue projects in the economic corridor. In other words, the BRI provided opportunities for Chinese real estate MNCs to increase their foreign revenue streams and offered an opening for Johor to counter the outsized footprint that Putrajaya initially had in the economic corridor. Although seldom discussed, this long-standing competition between Malaysia's central government and state officials in Johor played an important role in shaping the way Chinese FDI was attracted and injected into Iskandar Malaysia. Multiple political-commercial coalitions have been forged by both levels of government to push their respective projects. This is reflected by the layout of the corridor: Putrajaya-linked firms dominate Flagship Zone B, while the majority of Chinese MNCs cooperate with their Johor partners in Flagship Zone A.

Country Garden arguably overlooked or heavily discounted the importance of host country politics in conceptualizing Forest City. Nevertheless, the company appears to be making some attempts to adapt to the challenges it has faced, not least after the May 2018 general election. Some of the MNC's more noteworthy adjustments to local realities include corporate social responsibility outreach programs revolving around community service and environmental conservation. The company also admitted that it had been too optimistic in the construction of Forest City. Despite these efforts, the core issue of a dearth of affordable housing in Johor remains unresolved for now. It also appears unlikely that Country Garden will drastically reduce the price of its residential units to tap into this reservoir of demand. Doing so would dilute the high-end, luxurious image that Country Garden seeks to curate for this project. In addition, it would not be easy to push down home prices because land reclamation constitutes a significant material cost to the company.

More generally, a looming real estate crisis in China has meant liquidity challenges and a concomitant decrease in the overseas portfolios of many Chinese MNCs (including those with holdings in Iskandar Malaysia).<sup>83</sup> The introduction of Chinese capital controls in 2017 merely exposed the fragility of many of these MNCs' underlying business strategies. And in the case of Forest City, current sentiment is to, as a Chinese expression puts it, *bao jiaolou* (meaning to guarantee the completion of homes)—a rather modest, short-term goal. This state of affairs is a far cry from Country Garden's initial calls of *haiwai jiancheng* (plans to build complete cities outside China), the spirit of enthusiasm that prevailed during the BRI's early days.<sup>84</sup>

Worse for Country Garden's current business prospects is the broader political context in Malaysia. On the political front, the UMNO has rebounded, regaining control of Putrajaya and several state governments after Pakatan Harapan's sudden implosion in early March 2020. But the UMNO has not been able to make a concerted push to stimulate confidence in the Malaysian economy, especially because of the onset of the coronavirus pandemic in early 2020, which shuttered almost all workplaces and caused massive disruptions and losses. In 2020, Malaysia's GDP shrank by 5.6 percent, the country's worst economic performance since the fallout of the 1997 Asian financial crisis.<sup>85</sup> This recession hit Johor especially hard as it heavily depends on international trade and financial flows.

Although output recovered in 2021, the country's 3.1 percent GDP expansion was still well below the initial official projection of up to 7.5 percent growth.<sup>86</sup> In view of these political and economic challenges, coupled with Johor's longstanding housing affordability quagmire and the ongoing uncertainties about China's real estate outlook, it is likely that Country Garden will continue to face headwinds in Iskandar Malaysia.

Several lessons and recommendations follow. First, it is increasingly obvious that Chinese MNCs cannot avoid the need to navigate local politics in the places they invest, something that their Western and Japanese counterparts also struggle with when they invest abroad. Aspiring Chinese firms (in real estate and other sectors) would do well to engage well-trained, experienced third-party firms to analyze the political risk in prospective host economies. Alternatively, they can establish in-house units to provide risk analysis. At a bare minimum, they have to be more aware of local political sentiments. Indeed, some Chinese firms operating in Malaysia have shown greater willingness to understand and address the concerns of their domestic stakeholders.<sup>87</sup> A dispassionate ex ante assessment not just of commercial returns but also of political risk could reduce the likelihood of these Chinese firms getting sucked into potential turf wars between various local stakeholders.

By the same token, it is worthwhile to carefully screen the socioeconomic milieu and history of a host economy before investing. One Chinese interviewee, when asked to recap some of the key takeaways from the experience of working in Iskandar Malaysia, lamented that the firm could most likely have avoided some of the political complications it eventually faced in Malaysia if these issues had been more carefully taken onboard before initial investments were made.<sup>88</sup> Chinese firms are also handicapped by their speed-to-market approach, a unique selling point of Chinese real estate MNCs. In the case of Forest City, land reclamation started in late 2013 and early 2014, just under three years before its official launch in March 2016.<sup>89</sup> However, this approach did not insulate the project from local politics. If anything, it exposed the project to even more politicking.

Lastly, in trying to tap capital and know-how from Chinese investors, policymakers from Malaysia or other potential host countries need to rethink their existing approaches. Ultimately, when benefits and gains are not distributed equitably, a project, even one with a local sponsor or champion, can get caught up in local politics and countervailing pressures from opponents. This reality further underscores the need to ensure that FDI is productive and offers widely shared benefits, rather than unproductive or even predatory terms.

In Iskandar Malaysia thus far, Chinese FDI has run into precisely these pitfalls. Some of the challenges that have plagued Iskandar Malaysia can already be seen elsewhere—in the real estate bubble now forming in Cambodia, for instance, following years of aggressive Cambodian courting of Chinese FDI. Political pressure is building in Phnom Penh (the country’s capital) and in the coastal city of Sihanoukville.<sup>90</sup> Tempting as these lucrative Chinese investments are, especially for catalyzing economic growth, it is equally important to recognize the potential pitfalls when local politics invariably comes into play.

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