WHERE IS THE MALAYSIAN ECONOMY HEADED?

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1. INTRODUCTION

- This paper seeks to examine the structural change experience of Malaysia with a view towards explaining the direction the economy has taken.
- In addition to discussing the shift from primary sectors to industrialization, it distinguishes four clear policy-trade regimes used to promote industrialization in the country.
- It evaluates the impact of these policy regimes on employment, value added, trade and productivity.
- It eventually compares the impact of these developments against the growth gradients enjoyed by selected East and Southeast Asian economies.

2. KEY FEATURES

- Primary resources enjoyed stimulative support that began during British colonialism – to raise productivity; and was targeted for restructuring with the launching of land tenure programmes (e.g. Felda, Risda and Felcra) and government supported takeovers of foreign owned estates.
- Ethnic-coloured NEP restructuring targeted to be achieved through manufacturing as engine of growth.
- Initial FDI-led industrialization in the late 1950s until the ICA of 1975 was confined after that essentially to EO industries (exports exceeding 80% of output with imports largely constituting production materials and machinery and equipment).
- Dualistic industrial sector evolved between IS1 and EO1
- Unconnected development of IS1 and IS2
- From the 1980s the focus of government drive shifted extensively towards manufacturing growth with brief revival of emphasi on agriculture after the financial crisis of 1997-98.
- Electric FDI and labour policies provided little support for upgrading.
- Institutional development from1990 promised deepening. However, the misapplication of promotional strategies, and without the discipline of the market in IS2 industries and ethnic coloured forays into institutional coordination restricted the development of user-producer relations between institutions and firms.

3. INDUSTRIAL POLICY REGIMES

Table 1: Industrial Strategies and Trade Orientation, Malaysia, 1958-2005

Phases	Trade Orientation	Period of Dominance	Policy Instruments
Phase 1 Phase 2 Phase 3 Phase 4	IS1 EO1-IS1 IS2-IS1 EO2-IS2	1958-1968 1968-1980 1980-1985 1985-2007	Pioneer Industries Ordinance,1958 Investment Incentives Act, 1968 Free Trade Zone Act 1971 Heavy Industries Corporation of Malaysia (HICOM) 1980 Industrial Master Plan 1986 Promotion of Investment Act, 1986 Action Plan for Industrial Technology Development (APITD) 1990 IMP2,1996; IMP3 2006

Source: Compiled by author

Figure 1: Sequencing of Trade Regimes, Malaysia, 1958-2007

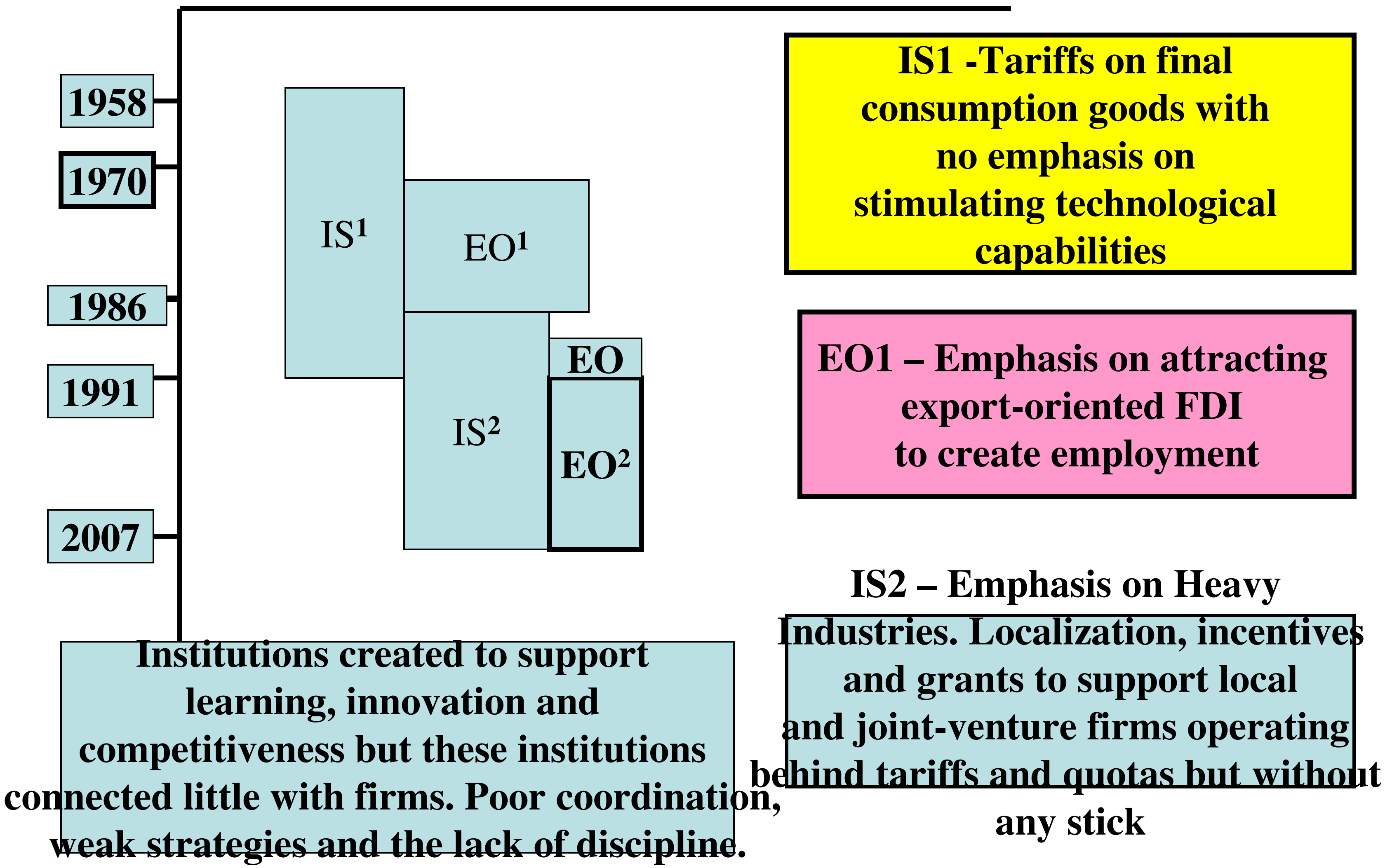


Table 2: Net FDI Inflows as a Share of Gross Fixed Capital Formation, 1988-2005 (%)

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
China	2.6	2.9	3.5	3.9	7.3	12.2	17.3	15.4	14.9	14.9	13.6	11.3	10.3	10.5	10.4	8.6	8.1	9.2
HK	33.1	11.5	16.3	4.4	13.8	21.5	19.8	14.4	21.4	19.5	29.4	58.6	138.9	55.7	26.4	40.6	96.4	97.0
Korea	1.6	1.0	0.8	0.9	0.5	0.4	0.5	0.7	1.0	1.4	4.8	7.3	5.4	2.7	1.9	2.1	3.9	3.1
Macao	0.1	-0.1	0.1	1.1	-1.3	-0.2	0.2	0.1	0.4	0.2	-1.6	0.9	-0.1	25.1	51.9	36.7	29.8	67.2
Mongolia	..	..	..	..	..	5.1	4.2	3.0	4.8	9.2	5.8	9.6	18.0	13.4	23.9	30.3	17.9	33.4
Taiwan	3.7	4.8	3.7	3.2	1.8	1.6	2.3	2.4	3.0	3.4	0.4	4.2	6.4	7.3	2.7	0.8	2.8	2.3
Banglades h	0.1	0.0	0.1	0.0	0.1	0.3	0.2	0.0	0.2	6.7	6.2	3.1	5.5	3.4	3.0	2.9	3.4	4.9
Bhutan	..	..	1.7	0.7	..	..	..	0.0	1.0	-0.5	..	4.8	0.0	0.1	0.1	0.3	0.3	0.2
India	0.2	0.4	0.3	0.1	0.4	0.9	1.4	2.4	2.9	4.0	2.9	2.2	3.5	5.2	4.9	3.4	3.1	3.5
Maldives	1.9	5.8	7.1	9.0	8.7	9.1	11.7	5.8	6.8	6.8	7.1	6.2	7.9	6.7	7.6	7.2	5.4	4.8
Nepal	0.1	0.1	1.0	0.4	..	..	..	..	1.9	2.2	1.2	0.5	-0.1	2.0	-0.6	1.3	0.0	0.4
Pakistan	2.2	2.8	4.1	3.7	4.0	4.4	8.6	4.9	4.3	7.4	5.7	6.4	2.7	3.6	7.2	4.2	7.5	13.0
Sri Lanka	2.7	1.2	2.5	3.3	5.4	7.5	5.3	2.0	4.0	11.8	3.8	4.7	3.8	5.0	5.7	5.7	4.7	5.2
Cambodia	..	..	..	..	17.0	19.9	23.1	31.5	66.1	36.4	62.6	41.4	22.1	22.7	17.3	9.0	11.4	31.5
Indonesia	2.5	2.5	3.4	4.1	4.7	4.8	4.3	7.6	9.2	7.7	-1.0	-6.6	-13.9	-9.4	0.4	-1.3	3.4	8.5
Lao	2.5	3.8	6.1	7.3	7.8	36.6	60.8	19.3	23.6	18.2	14.4	15.7	9.4	6.5	7.2	4.5	3.7	5.8
Malaysia	8.3	14.8	18.0	22.6	23.7	22.1	15.3	15.0	17.0	14.6	14.0	22.5	16.4	2.5	14.5	10.8	19.1	15.2
Philippines	14.8	6.4	5.4	6.1	7.0	9.6	10.5	8.9	7.8	6.2	12.7	8.6	13.9	1.5	11.4	3.7	4.8	7.5
Singapore	47.0	29.8	46.8	33.6	12.5	23.1	36.1	41.1	27.7	37.3	23.8	59.7	59.8	61.0	32.6	46.5	58.0	78.9
Thailand	5.9	7.3	7.5	5.0	4.9	3.7	2.4	3.0	3.1	7.6	29.9	23.9	12.4	14.6	3.3	5.7	3.4	7.2
Timor	..	..	..	..	..	..	..	..	..	..	..	0.0	0.0	54.9	1.0	4.5	2.3	..
Vietnam	0.3	0.6	21.2	35.9	28.9	32.2	49.2	33.8	27.8	36.1	23.1	20.1	15.0	13.7	11.0	11.0	10.5	11.3

4 INDUSTRIAL TRADE STRUCTURE

- Growth of manufacturing trade in exports, imports and GDP.
- Changing composition of manufactured exports
- Changing manufacturing trade balance
- Palm has arguably achieved the most dynamic deepening efforts as policy drove up the value chain production from crude palm oil (CPO) production to processed palm oil (PPO) (Jaya Gopal, 2002) and subsequently participation in new product development (Rasiah, 2006).
- The lack of a deliberate application of strategies to stimulate learning and innovation has stunted similar catch ups in electric-electronics, automotives, machinery and metals, chemicals, biotechnology, and textiles and garments. Hence, from the mid-1990s Malaysia;'s economy has again began to depend increasingly on natural resource exports – especially petroleum.

Figure 2: Trade Trends Against GDP, Malaysia, 1965-2005

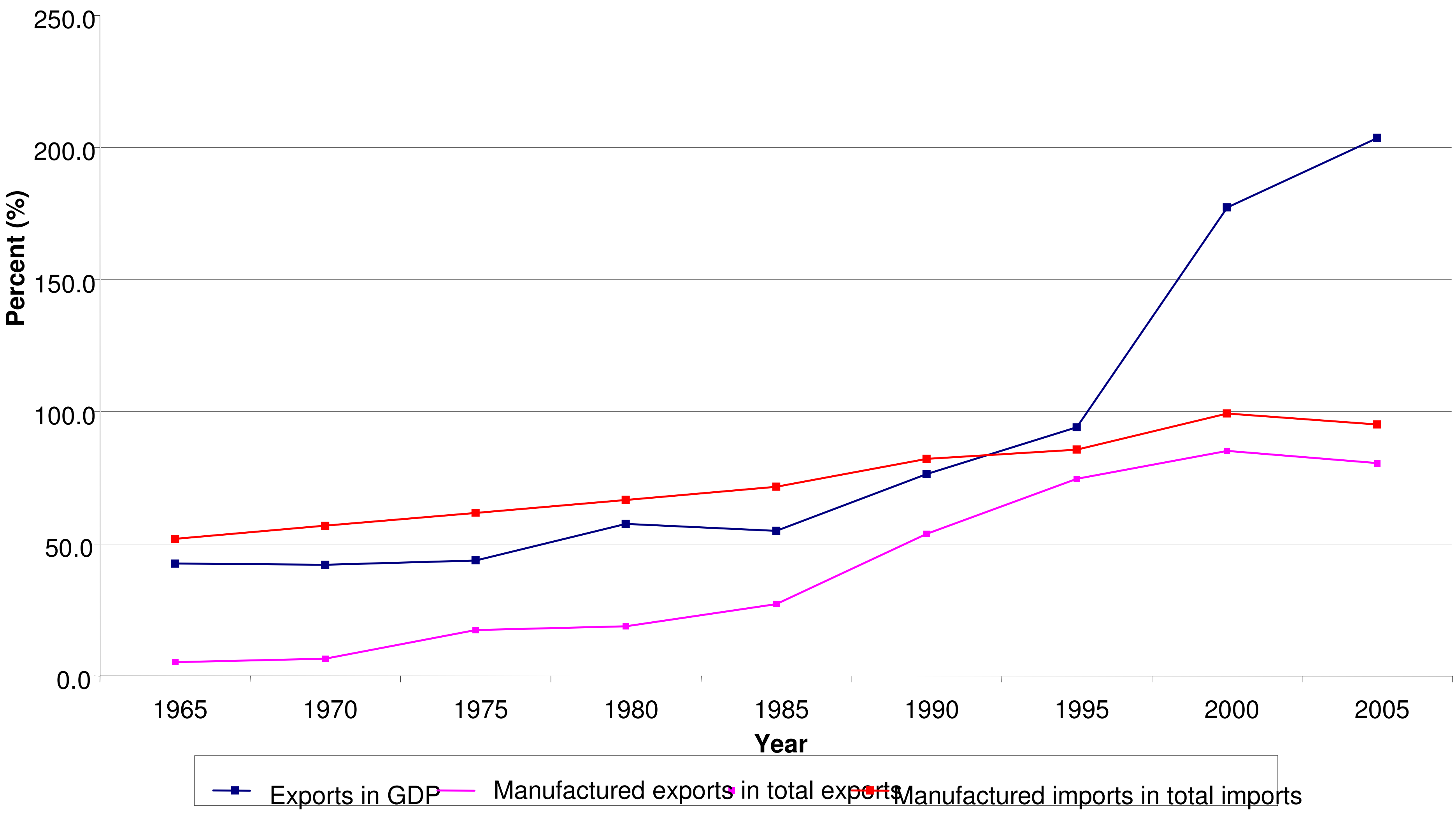


Table 3: Manufacturing Export Structure, Malaysia, 1968-2005 (%)

	xi/∑xi							
	68	73	79	85	90	97	2000	2005
Food	17.5	19.6	12.3	12.7	8.1	2.3	1.4	2.0
Beverage and Tobacco	0.9	2.9	2.5	0.2	0.2	0.5	0.4	0.4
Textile and garment	1.4	6.1	7.2	10.0	10.5	4.8	3.3	2.4
Wood	3.4	9.7	4.3	2.8	3.1	4.1	2.1	2.1
Chemical	3.0	5.2	3.4	3.3	3.1	5.1	4.7	6.9
Rubber	0.9	1.7	1.6	0.9	1.2	2.5	1.5	1.6
Non-metal mineral	0.8	1.1	1	1.1	1.8	1.1	0.8	0.7
Metals	66.3	45.2	32.2	15.0	5.6	4.6	2.7	4.0
Machinery	2.5	3.8	3.7	5.1	8.6	4.2	NA	NA
Electrical machinery	0.7	2.1	28.4	44.6	53.4	71.0	72.5	65.8
Transport equipment	2.6	2.7	3.3	4.3	4.5	3.1	0.9	1.6

Source: Computed from Malaysia, *External Trade Statistics*, 1969; 1974 1980; 1986; 1991; 1998

Table 4: Manufacturing Trade Ratios, Malaysia, 1968-2005

	(xi-mi)/(xi+mi)							
	1968	1973	1979	1985	1990	1997	2000	2005
Food	-0.562	-0.358	-0.274	-0.308	-0.163	-0.454	-0.126	-0.025
Beverage and Tobacco	-0.752	-0.106	0.15	-0.8	-0.509	0.061		
Textile and garment	-0.897	-0.482	-0.058	0.106	0.159	0.233	0.349	0.353
Wood	0.778	0.935	0.913	0.874	0.932	0.848	0.112	0.118
Chemical	-0.736	-0.628	-0.71	-0.721	-0.672	-0.040		
Rubber	-0.149	0.23	0.47	0.113	0.342	0.754	0.641	0.589
Non-metal mineral	-0.665	-0.507	-0.335	-0.518	-0.038	-0.213		
Iron and steel	-0.91	-0.78	-0.759	-0.826	-0.738	-0.709	-0.186	0.441
Metals	0.707	0.627	0.57	0.252	-0.307	-0.147		
Machinery	-0.824	-0.778	-0.706	-0.746	-0.573	0.023	-0.581	-0.278
Electrical machinery	-0.877	-0.723	-0.031	-0.037	0.100	-0.026	0.173	0.155
Transport equipment	-0.808	-0.813	-0.652	-0.624	-0.595	-0.561	-0.363	-0.226

Source: Computed from Malaysia, *External Trade Statistics*, 1969; 1974 1980; 1986; 1991; 1998; Malaysia, *Industrial Surveys*, 1969; 1974 1980; 1986; 1991; 1998

5 EMPLOYMENT, VALUE ADDED, EMPLOYMENT ELASTICITY AND PRODUCTIVITY

- Manufacturing employment growth
- Manufacturing value added growth
- Employment elasticity and labour productivity of inward-oriented and export-oriented manufacturing sectors
- Technological depth of automotive and electronics firms in Malaysia compared to firms in Taiwan and Korea.

Table 5: Average Annual Manufacturing Employment Growth, Malaysia 1971-2005 (%)

	1971-79	1979-85	1985-90	1990-97	2000-05
Food, beverage and tobacco	10.5	1.6	1.6	4.3	4.7
Textile and wearing apparel	12.6	5.2	12.4	1.6	-0.1
Wood and furniture	8.5	2.0	10.7	9.6	1.2
Paper, printing and publishing	9.4	2.9	7.8	7.6	2.5
Chemicals, petroleum, coal and plastics	-8.5	9.4	5.3	6.3	6.5
Non-metal minerals	6.5	6.4	2.5	6.0	1.9
Basic metals	-10.7	9.5	7.3	9.2	7.9
Metal products	8.1	1.5	10.5	11.1	
Machinery and equipment	8.6	-0.6	14.7	14.4	0.1
Electrical machinery	44.7	2.0	21.6	14.6	5.4
Transport equipment	13.9	4.3	5.8	9.2	4.7
Other manufactures	-6.0	12.4	17.3	8.2	5.4
Manufacturing	13.2	2.2	12.1	9.5	5.1

Table 6: Average Annual Growth in Manufacturing Value Added, Malaysia, 1971-2005 (%)

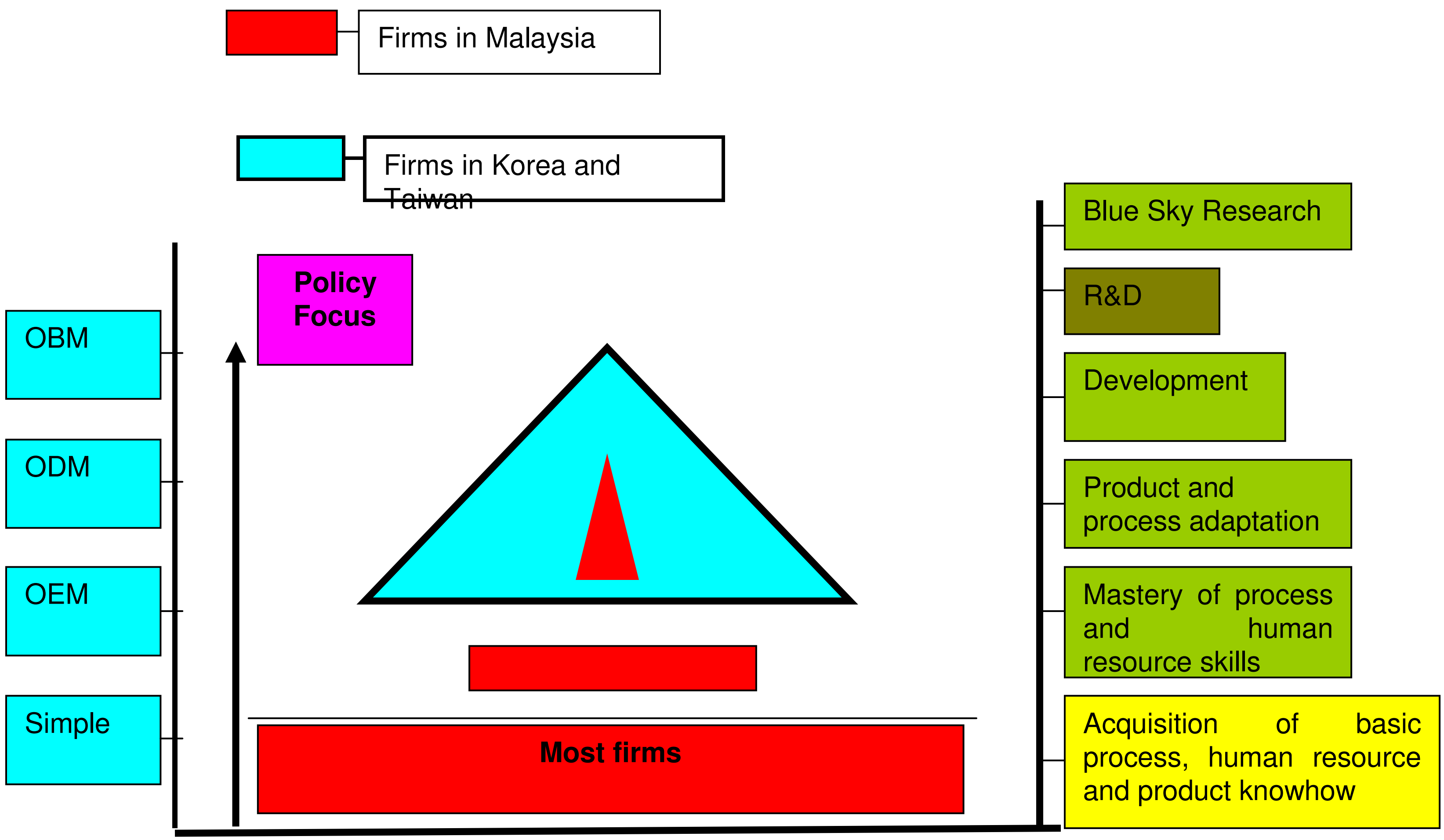
	1971-79	1979-85	1985-90	1990-97	2000-05
Food, beverages and tobacco	27.5	5.8	3.9	7.3	3.6
Textile and apparel	24.6	9.6	20.7	8.6	-4.8
Wood and furniture	23.0	1.0	15.6	15.4	0.3
Paper, printing and publishing				13.4	
Chemicals	6.5	23.2	6.1	11.7	2.9
Petroleum, coal and plastics	-29.0	59.2	8.5	17.0	3.1
Rubber	34.0	-3.1	15.8	10.4	9.7
Non-metal minerals	15.3	15.3	7.9	12.2	2.2
Basic metals	-5.0	17.1	12.8	11.5	2.6
Metal products	21.1	3.9	16.2	18.2	7.1
Machinery and equipment	25.9	0.6	28.2	23.2	2.4
Electrical machinery	46.4	11.4	21.1	21.3	2.1
Transport equipment	25.9	11.6	18.2	16.7	7.5
Other manufactures	2.7	16.0	23.2	7.5	8.4
Manufacturing	26.1	7.9	12.9	15.6	4.1

Table 7: Average Annual Manufacturing Employment, Value added and Labour Productivity Growth, Malaysia, 1971-2005

	1971-79	1979-85	1985-90	1990-97	2000-005
Employment growth					
Export-oriented	**13.9**	**1.9**	**23.4**	**1.2**	**3.4**
Inward-oriented	**11.1**	**3.2**	**6.8**	**9.0**	**4.9**
Value added growth					
Export-oriented	**28.1**	**5.9**	**14.8**	**20.5**	**2.0**
Inward-oriented	**21.9**	**19.0**	**15.6**	**14.8**	**5.7**
Employment elasticity					
Export-oriented	**0.5**	**0.3**	**1.6**	**0.1**	**1.7**
Inward-oriented	**0.5**	**0.2**	**0.4**	**0.6**	**0.9**
Labour productivity					
Export-oriented	**12.5**	**3.9**	**-7.0**	**19.1**	**-1.3**
Inward-oriented	**9.7**	**15.3**	**8.3**	**5.4**	**0.8**

Note: Employment elasticity computed using the formula $\Delta E/\Delta V$ where E and V refer to employment and value added respectively. Labour productivity
computed using value added and employment. Value added used in constant 1990 prices.
Source: Computed from Malaysia, Industrial Surveys, 1971, 1979, 1985, 1990 and 1997

Figure 3: Technological Location of Auto Parts and Electronics Firms in Korea, Malaysia and Taiwan, 2001



Source: Drawn from Rasiah (2004a; 2007b)

Figure 4: GDP Per Capita, Selected Economies, 1960-2005 (US$ in real prices)

	1960	1965	1970	1975	1980	1985	1990	1995	2000	2005
China	105	100	122	146	186	290	392	658	949	1445
India	177	188	209	215	224	261	318	374	454	586
Korea	1110	1296	1912	2489	3221	4386	6615	9159	10884	13210
Malaysia	784	937	1103	1378	1848	2081	2547	3510	3927	4434
Singapore	2221	2696	4470	6342	8934	10737	14478	19111	22768	25443
Thailand	329	397	530	615	804	960	1452	2057	1998	2440
Vietnam	Na	Na	Na	Na	Na	202	227	305	397	539

Table 8: Average Annual Growth in GDP Per Capita, 1960-2005 (%)

	60-65	65-70	70-75	75-80	80-85	85-90	90-95	95-00	00-05	60-05	85-05
China	-1.0	4.1	3.5	5.1	9.2	6.2	10.9	7.6	8.8	6.0	8.4
India	1.3	2.1	0.6	0.8	3.1	4.0	3.3	4.0	5.2	2.7	4.1
Korea	3.1	8.1	5.4	5.3	6.4	8.6	6.7	3.5	3.9	5.7	5.7
Malaysia	3.6	3.3	4.5	6.1	2.4	4.1	6.6	2.3	2.5	3.9	3.9
Singapore	4.0	10.6	7.2	7.1	3.7	6.2	5.7	3.6	2.2	5.6	4.4
Thailand	3.8	5.9	3.0	5.5	3.6	8.6	7.2	-0.6	4.1	4.6	4.8
Vietnam	NA	Na	Na	Na	Na	2.4	6.1	5.4	6.3	NA	5.0

6 CONCLUSIONS

- The contribution of manufacturing to employment, exports and value added in the Malaysian economy expanded in trend terms between 1958-2005.
- However, eclectic and uncoordinated policies coloured by ethnic considerations has restricted the capacity of a widening manufacturing sector to record industrial deepening.
- A serious slowdown in labour productivity growth in the key export-oriented manufacturing sectors in 2000-2005 underlines the threat Malaysia faces against newly emerging industrializers such as China and Vietnam.
- Whereas agriculture has undergone falling importance in GDP and employment levels productivity levels have continued to rise in the successful latecomer industrializers such as Korea and Taiwan. Malaysian agriculture has failed achieve significant levels of productivity increments.
- Unless efforts are taken to drive institutional change to stimulate upgrading in industry the Per Capita GDP gap with Korea, Taiwan and Singapore is expected to widen further and China and Vietnam are expected to overtake Malaysia’s in the next two decades.