Export-led Industrialisation, Employment and Equity: The Malaysian Case

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ABSTRACT

Malaysia is undoubtedly a development success story. Over the past decade or so rapid economic growth through export-led industrialisation has been accompanied by rising living standards and improvement in the distribution of income, ameliorating the twin problems of poverty and racial imbalances. The key lesson to come from the Malaysian experience is that in a small open economy, the task of achieving the apparently conflicting objectives of growth and equity is facilitated by a long-term commitment to outward-oriented trade and industrial policies.

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1. Introduction

A distinguishing characteristic of the economic performance of Newly Industrialising Countries (NICs) in East Asia is the highly equitable distribution of gains from economic growth. The rapid and sustained growth in these economies since the late 1960s has been accompanied by a reduction in poverty and improvement in living standards of their people across the board. Income distribution continued to remain relatively more equal than in other countries at a comparable stage of development. The mainstream (neoclassical) economists interpret this achievement as a *natural* outcome of export-led industrialisation, which can be replicated in other developing countries provided the policy fundamentals are right. With the comparative advantage of developing countries in international production being in relatively labour intensive production, so the argument goes, the expansion of manufactured exports translates into higher employment. Given the fact that labour is the most widely distributed factor of production in the economy, employment expansion and the subsequent increase in real wages reduce poverty and income inequality (Krueger 1995, Balassa and Williamson 1987, Fei *et al*. 1979).

The economists of structuralist persuasion (the revisionists) are, however, less sanguine about the replicability of the NIC experience in other developing countries (Amsden and Van Der Hoeven 1996, Helleiner 1994, Taylor 1991). According to these economists, the 'growth with equity' outcome was largely brought about by favourable initial conditions of these countries and the highly accommodative world market situation at the formative stage of their economic transformation. The NICs had a head start over the other developing countries in terms of higher educational standards, relative equality in income distribution, and broad-based wealth ownership.

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These initial conditions were instrumental in setting up a virtuous circle of high growth and low inequality. At the same time, the rapidly expanding markets in developed countries in the 1960s and early 1970s provided a fertile milieu for rapid expansion of labour intensive manufactured exports without requiring any real wage restraint. If the NIC firms were forced to face market forces in a depressed world market context (like in the period since the mid-1970s), so the revisionist argue, they would have been under persistent pressure to cut cost (rather than to raise prices) leading to stagnation in real wage growth and a massive shift of income from labour to capital (Amsden and Van Der Hoeven 1996).

This paper seeks to shed some light on this debate by examining the case of Malaysia, a country which has achieved phenomenal growth through export-led industrialisation since the mid-1980s. In terms of the initial conditions and structural characteristics, Malaysia had more in common with the many other developing countries in the region than it did with the East Asian NICs. Thus, the lessons from the Malaysian experience would be relevant to the debate on trade and industrial policy reforms in developing countries.

The paper is organised as follows: Section 2 surveys Malaysian economic policy since independence, in order to place the ensuing discussion in context and to delineate the key policy shifts so as to guide the analysis of globalisation and its developmental implications. Overall growth trends are surveyed in the context of the ongoing process of globalisation of the economy in Section 3. The implications of export-oriented growth for domestic employment and income inequality are examined in Section 4. The paper ends in Section 5 with some concluding remarks.

2. Policy Context

At independence (Merdeka) in 1957, economic conditions of Malaysia (then the Federation of Malaya[1]) appeared generally favourable. The colonial inheritance included well-developed infrastructure, an efficient administrative mechanism and a thriving primary export sector with immense potential for expansion. In terms of per capita income, literacy and health care, Malaysia was ahead of most of its neighbours. Even though the rate of population increase was already very rapid, the highly favourable ratio of land and other natural resources to total population offered potential to raise income per head.

The mobilisation of this developmental potential for building the new independent Malaysian economy had, however, to be done under conflicting challenges posed by a plural society inherited from its colonial past. At the time the native Malays, who accounted for 52 percent of the population, dominated politics, but were relatively poor, and involved mostly in low-productive agricultural activities.[2] The ethnic Chinese (37 percent of the population) enjoyed greater economic power and dominated most of the modern-sector activities, but did not match the ethnic solidarity or political power of the Malays. Economic policy making in post-independence Malaysia, therefore, turned out to be a *continuing struggle to achieve development objectives while preserving communal harmony and political stability*.

The government policy during the first decade of independence is perhaps best described as a "holding" program, designed to suppress growing inter-communal rivalries. The policy thrust was to continue with the colonial open-door policies relating to trade and industry, while attempting to redress ethnic and regional economic imbalances through rural development schemes and the provision of social

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[1] The Federation of Malaya, comprising 11 states in the Malay Peninsula secured independence from Britain on 31 August 1957. Sabah, Sarawak and Singapore joined Malaya to form Malaysia on 16 September 1963. Singapore left the federation in August 1965.

[2] In 1957-58, 34.9 percent of households had incomes of less than RM120 per month (the official cut-off point for measuring poverty). More than half of these households were Malay, and more than two-thirds were rural (Snodgrass 1980).

and physical infrastructure. Like in many other developing countries, import-substitution industrialisation was on the policy agenda in Malaysia during this period. However, unlike in other countries, attempts were not made to achieve "forced" industrialisation through direct import restrictions and the establishment of state-owned industrial enterprises.[3] Whilst foreign investment was welcomed with open arms during this period, its impact on the economy was bound to be limited for two reasons. First, in the absence of binding import restrictions, tariff-jumping was not a major motive to establish import-substituting plants in Malaysia. Second, the process of internationalisation of production through the international division of labour within vertically integrated global industries had not yet begun.

By the late 1960s, there was a growing recognition that the easy stage of import substitution industrialisation was coming to an end and that future prospects for industrial development depended upon the expansion of export-oriented industries. It was decided accordingly to give more emphasis to those industrial and investment incentives which would encourage the growth of export-oriented activities (Lim 1992). This led to the enactment of the Industrial Incentives Act in 1968. The incentives offered to export-oriented ventures by the Act included exemptions from company tax and duty on imported inputs, relief from payroll tax, investment tax credits and accelerated depreciation allowances on investment.

Economic expansion during 1957-69, though respectable, failed to make a substantial contribution towards solving the "special" problems of the Malays. On the other hand, with urban unemployment rising and education and language again looming as issues, non-Malays began to question the extent to which their interests were being safeguarded in the new Malaysia. The growing disenchantment among all

[3] Snodgrass (1980, 206) ascribes this policy neutrality to the influence of advice from a major World Bank mission to Malaysia in 1954. There are at least two other factors which might have been more influential in determining the direction of Malaysian policy, however. First, throughout this period, Malaysia generally enjoyed a sound balance of payments position (due mainly to booming primary exports), and hence felt no compulsion to resort to stringent import restrictions. Second, the ethnic tensions that existed between the Malay political leadership and the Chinese business sector may also have held back any concerted effort to promote local industry through trade protection and other means of direct government involvement.

segments of the population ultimately erupted in the bloody communal riots of May 1969. This event resulted in a clear shift from planning and policy making based purely on economic considerations and towards an affirmative action policy based on ethnicity. This policy shift was formalised in the New Economic Policy (NEP), a sweeping affirmative action program, which formed the basis for the Second Malaysia Plan (1971-75).

The overriding objective of the NEP was to maintain national unity through the pursuance of two objectives: eradication of poverty through employment generation and restructuring of society with a view to eliminating the identification of race with economic function. For the first objective, the overall development strategy was reformulated with emphasis on export-oriented industrialisation and an ambitious rural and urban development programme. The Free Trade Zone (FTZ) Act was enacted in 1971 to entice export-oriented foreign direct investment (EO-FDI). The rich assortment of incentives offered by the Act to FTZ ventures included duty-free imports of raw material and capital equipment, streamlined customs formalities, subsidised infrastructure facilities and company income tax incentives (Warr 1987). For the second objective, long-term targets were established for Bumiputra ownership of share capital in limited companies, and the proportion of Malays employed in manufacturing and installed in managerial positions. The NEP aimed to increase the Malay share in corporate assets from 2 percent in 1970 to 30 percent in 1990, and to have employment patterns in the urban sector reflect the racial composition of the country. Malay participation in business was promoted in two ways: (i) through the expansion (both by setting up new ventures and the purchase of foreign-owned businesses) of the public sector where Malays held most of the key positions, and (ii) by providing Malays with privileged access to share ownership and business opportunities in the private sector. The Industrial Coordination Act (ICA) was passed in 1975 to strengthen measures to implement NEP norms on Bumiputra participation at the enterprise level. Under the ICA, the conduct of medium- and large-scale enterprises was subject to licensing with the aim of improving the relative position of the Malays in the modern sector of the economy.

As part of the NEP, Malaysia moved into the promotion of heavy industries over the term of its Fourth Five-Year Plan (1981-85). The Heavy Industries Corporation of Malaysia (HICOM), a public-sector holding company, was formed in 1980 to go into partnership with foreign companies in setting up industries in areas such as petrochemicals; iron and steel; cement; paper and paper products; machinery and equipment; general engineering; transport equipment; and building material. These industries were expected to "strengthen the foundation of the manufacturing sector ... [by providing] strong forward and backward linkages for the development of other industries" (Government of Malaysia 1984, 271). Even though the new selective industrialisation push was often rationalised as an attempt to emulate the examples of Japan and Korea (hence the "look East policy, a term coined by Mahathir in 1981), in practice the selection of new projects were based largely on traditional import-substitution criteria. These projects were supported with subsidised credit, government procurement provisions and heavy tariff protection, without subjecting them to any market-based performance norms.[4]

The blow-out in public expenditure owing largely to the heavy industrialisation move began to reflect in widening budget and current account deficits, and an increase in external debt from about 1981. The macroeconomic imbalance was compounded by a significant fall in the prices of tin and palm oil and depressed demand for fledgling manufactured exports (in particular electronics) as a result of the world economic recession in the mid-1980s (Corden 1993, 35). The required cuts in government expenditure had invariable contractionary effects on the domestic economy. At the same time, the uncertainty in the policy environment was reflected in stagnation in private investment (both local and foreign) in the economy. These factors brought the economic advances of the 1970s to a halt and created an environment in which race relations became increasingly tense. This volatile climate paved the way for a series of policy reforms, which placed greater emphasis on the role of the private sector and strengthening the conditions for export-oriented growth.

[4] By 1987, there were 867 corporate public enterprises in Malaysia, more than a third of which were in manufacturing. The symbol of the selective industrial policy was the Proton (Malaysian car) project which was set up by HICOM in collaboration with the Mitsubishi Corporation in Japan.

The government declared the NEP to be 'in abeyance'. The Promotion of Investment Act of 1986 introduced fresh, more generous incentives for private investors, and some of the ethnic requirements of the NEP were relaxed. Regulations on foreign equity participation in Malaysia were also relaxed and up to 100 percent foreign equity ownership of export-oriented companies was allowed. Work permit requirements for foreign employees of companies with foreign paid-up capital of US$2 million or more were eased. The NEP was subsequently replaced (in 1990) with the National Development Policy (NDP). The NDP eased the remaining strictures of the NEP with a view to putting the *creation of wealth ahead of redistributing it*. The policy thrust of the NDP was to redress racial imbalance in a more overt fashion through various initiatives geared to entrepreneurship, managerial expertise and skills development within the Malay community.

The reforms since the mid-1980s have also involved a gradual process of privatisation and restructuring of sate-owned enterprises. By the early 1990s state-ownership in manufacturing was limited only to some politically sensitive ventures in automobile manufacturing, petrochemical, iron and steel and cement industries. Tariff protection to domestic manufacturing, which had always been relatively low relative to other developing countries,[5] was further reduced over time. The effective rate of manufacturing protection declined from 31 percent in 1979-80 to 17 percent by the late 1980s (Salleh and Meyanathan 1973, 12).

The market-oriented policy reforms were accompanied by a strong focus on restoring and maintaining macroeconomic stability (including the maintenance of a realistic real exchange rate), and meeting the infrastructure needs of a rapidly expanding economy. The Fifth (1986-90) and Sixth (1991-95) Malaysia Plans saw a significant reduction in overall government expenditure and a shift in government

[5] In a recent comprehensive study of the patterns and chronology of trade policy reforms during the postwar era, Sachs and Warner (1995, Table 1) identify Malaysia as one of the eight developing countries whose trade regimes remained *open* throughout the period. The other seven countries are Barbados, Cyprus, Hong Kong, Mauritius, Singapore, Thailand and theYemen Arab Republic.

spending away from public sector enterprises and towards infrastructure projects designed to enhance private sector development.

In the area of labour market reforms, there was a new emphasis (like that of the East Asian NICs) on job creation rather than protecting workers' rights through labour legislation. Towards this end, attempts were made to achieve labour market flexibility through industrial relations legislation which provided for compulsory arbitration of disputes and prohibition on the right to strike in "essential services". Furthermore, unions were banned in the most important export-oriented industry - electronics - until 1988, after which only 'in-house' unions were allowed at the plant, rather than the industry, level.[6] This labour market policy, despite many criticisms, has certainly facilitated the outward-oriented growth process with foreign capital participation.[7]

3. Growth and Structural Change

The data on overall economic growth and export orientation of the Malaysian economy are summarised in Table 1. Annual growth from 1965-1986 averaged 5.5 percent, a respectable figure by developing country standards. The performance record was, however, rather uneven, reflecting the impact of primary commodity cycles and changes in government expenditure. Growth of real GNP averaged about 6.5 percent per annum during the 1970s, but then slowed down in the first half of the 1980s falling to negative one percent in 1985. With better domestic macroeconomic policies and market-based reforms, the Malaysian economy has picked up again since 1987. Real GDP growth accelerated to over 8 percent a year on average over the nine years up to 1995. Interestingly, this outstanding economic performance was achieved in the context of a depressed world economic environment.

Table 1 about here

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[6] In any case, unionism has not historically been a powerful force in the Malaysian labour market. Even by 1985, less than a quarter of the workers in manufacturing had been unionised (Mazumdar 1993, 171).

[7] For a lucid discussion of Malaysia's political changes as they relate to the industrialisation process, see Crouch (1994).

The data point to a close association between growth acceleration and the degree of export orientation of the economy. The export-GDP ratio increased at a modest rate during the 1970s, slowed down in the first half of the 1980s and then increased sharply from about 1987. The export-GDP ratio in 1995 (96 percent) was twice as high as in 1970.

In the 1970s and early 1980s, Malaysian economic growth was predominantly accounted for by the expansion of service industries emanating from public sector activities and growth in primary production (Table 2). In the primary sector, growth performance in the 1970s was led by a rapid expansion of the palm oil sector, and a modest expansion of rubber production. In the deregulated environment since the late 1980s, not only has there been a significant increase in growth, but much of it is has come from the expansion of manufacturing through private sector initiatives. In 1989, for the first time the manufacturing share in GDP overtook that of agriculture. Between 1987 and 1995, the manufacturing sector grew by an average annual rate of 14.5 percent, with the share of manufacturing in GDP increasing from about 20 percent to over 33 percent. Between these two years, over 50 percent of the growth in GDP came directly from the manufacturing sector. In addition, much of output and expansion in the tertiary (service) sectors in recent years has been closely related to the expansion of the manufacturing sector (Ariff 1991).

Table 2 about here

Table 3 about here

The expansion of manufacturing production has predominantly been export-led. The export structure of Malaysia, as it evolved during the colonial era, was characterised by heavy reliance on a limited range of primary commodities. In the early 1970s, the share of manufactures[8] in total merchandise exports was about 10 percent (Table 3). Since then, manufactured exports have emerged as the most dynamic element

[8] Manufactures are defined to include commodities belonging to section 3 of the International Standard Industry Classification (ISIC).

in the export structure. Exports of manufactures grew (in current US dollar terms) at an annual compound rate of 35 percent during 1980-95. In 1994, with a manufacturing share of about 78 percent, Malaysia was the developing world's sixth largest exporter of manufactures, after the Four Dragons of East Asia and China. As a result of this rapid export expansion, the share of exports in gross manufacturing output was over 60 percent in the early 1990s, compared to less than 10 percent in the early 1970s. In the 1970s, resource-based manufacturing such as food, beverages, tobacco, wood products and basic metals loomed large in the structure of manufactured exports. The transformation of the export structure in line with emerging patterns of the international division of labour gathered momentum in the late 1980. To begin with Malaysia found market niches in simple assembly operations in electronics and electrical goods, and diffused-technology consumer goods production (Table 3). However, in recent years the export composition has begun to diversify into mature technology final products such as radios, TVs, cameras and computers.

Foreign direct investment (FDI) has been the engine of manufactured export expansion. FDI flows to Malaysia have grown remarkably over the past two decades.[9] There has been a boom in the amount of FDI coming into the country, particularly since the mid-1980s; between 1987 and 1991, foreign capital inflows have increased by almost ten-fold. Since the mid-1980s, FDI flows to Malaysia have been increasing at a faster rate than that to the other ASEAN countries. Since 1991, the volume of FDI flowing to Malaysia has remained higher than to any of the other ASEAN countries. By the late-1980s, FDI inflows had shifted from production for the domestic market to using Malaysia as a base for manufacturing for the global market. The share of projects with an export orientation of 50 percent or more increased from 24 percent of total approved projects in 1984-85 to about 82 percent by 1988-89. The proportion of projects with an export orientation of 80 percent or above increased from one-fifth of the total in 1984 to about three-quarters in 1989. There are no direct estimates of the share of foreign firms in exports. However, a simple comparison of data on export and output shares of foreign firms show that they provided over three-quarters of total

[9] The Malaysian experience with attracting FDI has been discussed in detail elsewhere (Athukorala and Menon 1995).

manufactured exports by the mid-1990s (Lall 1995). There is a close association between the degree of foreign presence in product sectors and their relative contribution to total manufactured exports (Athukorala and Menon 1996). The electronic industry (which is almost completely foreign owned) alone contributed to over 63 percent of total exports in 1994. Malaysia's efforts in attracting FDI in the electronics industry were so successful that since the early 1980s it had been the largest developing-country exporter (and one of the world's major exporters) of electronic components, particularly integrated circuits.

There is little evidence that either the government leadership in industrial policy in general or the heavy industrialisation push in the early 1980s in particular have affected the export-led industrialisation process. The structure of industry that has evolved over the past two decade is much in line with what one would have expected given the nature of Malaysia's comparative advantage and changing factor endowment. Most of the industries set up under HICOM were "born losers" which were artificially spawned with subsidies (Chee 1994, 249). By the late 1980s HICOM had invested over RM42 billion in various projects which generated less than 5000 jobs directly (RM400,000 per job), and exports from these industries were almost negligible (Chee, 1994, Table 10.5). Undoubtedly some employment, some technical and managerial skills and scale economies have been generated, but these have been achieved at considerable expense. Apart from the direct economic cost, the inefficient heavy industry projects (which were mostly in investment and intermediate goods industries) burdened downstream industries, which were forced to pay higher prices for the protected products (Lim 1992).

4. Employment and Equity

Unemployment received public attention for the first time as an important issue in Malaysia only in the early 1960s. A sample survey conducted by the Department of Statistics in 1963 reported the unemployment rate in Peninsular Malaysia at 6 percent. By the time the NEP was promulgated in 1970, this had increased to 8 percent, but the Second Malaysia Plan could not offer anything more promising than containment at that level (Snodgrass 1980, p. 59). After a drop to around 5 percent in the early 1980s, the unemployment rate continued to increase reaching a peak of 8.3 percent in 1986.[10]

From then on, the unemployment rate began to decline. By 1995 the economy reached virtual full-employment with unemployment at only 2.8 percent (Table 4). It is interesting to note that this impressive employment record has been achieved in a context of increasing labour force participation of the population. This latter increase is a reflection of both the rapid rate of urbanisation and the increased labour force participation of women.

Table 4 about here

Table 5 about here

Most of the new employment has come from the rapid expansion of the manufacturing sector (Table 5). The share of manufacturing in total labour deployment in the economy increased from 14 percent in the mid-1970s to over 25 percent by the mid-1990s. The *direct* contribution of manufacturing to total employment increment between 1987 and 1994 was as high as 60 percent. In addition, as noted much of output (and hence employment) expansion in the tertiary (service) sectors in recent years has been closely related to the expansion of the manufacturing sector. The data reported in Athukorala and Menon (1996) point to the important role played by export-oriented foreign investment to manufacturing employment. The percentage of workers employed in foreign firms increased from about 30 percent in 1983
to 42 percent in 1992. The increase in the employment share was much faster than the increase in the share of output of these firms (from 41 to 48 percent), suggesting that

[10] The unemployment rates reported in this paragraph are surprisingly high by developing country standards, given the relatively rapid rate of growth of the Malaysian economy compared with that of many other developing countries. In his study of the Malaysian labour market, Mazumdar (1981) ascribes this apparent peculiarity to two special features of the Malaysian economy (which was predominantly a reflection of an extreme case of youth unemployment): prevalence of joint households (a household that supports dependent (non-earning) relatives) which generally encouraged youth unemployment and the relatively small size of the informal sector. This factor may also partly account for the long pre-employment waiting period and high-level of open unemployment among school leavers.

with the rapid expansion of export-oriented manufacturing, the structure of manufacturing production has become more labour-intensive over the years. This pattern was particularly noticeable in non-metallic minerals, basic metal products, fabricated metal products and miscellaneous manufacturing. In the case of electronics, the employment and output shares have remained virtually unchanged at comparable levels as this industry has been highly labour-intensive right from the start.

Real wages in the manufacturing sector declined in the early 1970s. The index of real wages (1990 = 100) in manufacturing was 61 during 1970-74 compared to 68 during 1965-69 (Table 6). At the time, critics of the export-led industrialisation strategy claimed that the working class was subject to high “disciplines” (through restrictions on labour unions) and low wages for the benefit of multinationals and local capitalists (Lee 1984, Jomo and Osman-Rani 1984, Osman-Rani 1983).[11] This pessimistic view was, however, repudiated by subsequent developments.

Table 6 about here

The decline in real wages in the early 1970s was partly a reflection of the shift in the structure of production away from capital-intensive import substitution activities and towards labour-intensive export production. At the same time, real wages were kept low by the availability of a vast pool of surplus labour in economy, particularly in the rural sector. With the gradual absorption of surplus labour in export-oriented industries, real wages started to rise from the late 1970s. The real wage index increased from an average level of 74 in 1975-79 to 105 in 1985. Following a mild decline during the years of macroeconomic adjustment in the mid 1980s,[12] the index increased continuously reaching a historical high level of 110 in

[11] Reflecting the impact of restrictive labour legislation (see Section 2), trade union activity in Malaysia has been low-key; for instance, only 12 percent of the manufacturing labour force was unionised by the late 1980s. The annual average number of strikes in the manufacturing sector in the 1970s was 5 and this declined to 3 in the 1980s (Source: Ministry of Labour, *Labour Indicators* (annual, various issues).

[12] During these years of macroeconomic adjustment, the downward flexibility of real wages enabled adjustment to be quicker and less painful. The relatively rapid adjustment helped with the resumption of economic growth, which in turn made subsequent real wage growth possible.

1992. Judging from the significant decline in the unemployment rate, real wages would have continued to increase during the ensuing years. Interestingly, the recent increases in real wages have occurred in a context where the profitability of manufacturing production (as measured by the price-cost margin) remained virtually unchanged. Thus, it appears that with the rapid depletion of surplus labour reserves in the economy, the workers have become the major beneficiaries of productivity growth in manufacturing. Higher productivity, rather than lower wages, seems to have borne the burden of creating competitiveness. In the absence of minimum wage legislation, employment levels have risen first followed by market- and productivity-driven increases in wage levels.

Growth in real wages in the 1990s would have presumably been much sharper had it not been for the influx of migrant workers. As the domestic labour market approached full employment, forcing rapid increases in real wages, there was a massive inflow of migrant workers from neighbouring labour surplus countries, Indonesia in particular. Official estimates put the number of migrant workers in Malaysia at half a million in 1994. However, there is circumstantial evidence that the number could be as high as 2 million (about 16 percent of the work force). By the early-1990s, more than half of the workforce in the construction industry and the plantation sector consisted of foreign workers, by which time they had also begun to enter the manufacturing sector (Pillai 1995).

The impact of various government programmes during the first three decades of the post-independence period on reducing poverty and income inequalities were, limited, to say the least. The ethnic and rural-urban distribution of poverty and income inequality had hardly changed over the period. By the late 1980s, 88 percent of poor households were rural, and almost 60 percent of rural households were poor (Anand 1983).

Since the mid-1980s, Malaysia's record of reducing poverty and income inequalities has been a success (Table 7). The incidence of poverty among all households has fallen from 18.4 percent in 1984 to 9.6 percent in 1995; this figure is projected to fall to 6.0 percent by the year 2000. A significant decline is observable for both urban and rural households. The Gini coefficient fell from 0.54 in 1970 to 0.45 in 1984 and remained virtually unchanged around that level during the ensuing years. This suggests that the benefits of rapid growth since the late 1980s were distributed reasonably widely. There has also been an improvement in the relative position of Malay households in terms of mean household income (Table 8). The data for 1995 indicate a slight worsening of the relative position of Malay households. The disaggregated data suggest that this worsening has been due mainly to differential growth rates of incomes in the top 20 percent and the bottom 40 percent of households. Within the middle 40 percent of households, however, the relative position of Malays has remained virtually unchanged (Government of Malaysia 1996, p. 89).

Table 7 about here

Table 8 about here

The most important factor underlying the reduction in poverty and increase in overall living standards has been the growing opportunities for non-agricultural work, particularly in the rapidly expanding export-oriented manufacturing industries. The demand for unskilled labour created by the process of export-led industrialisation has been so great that it is now a scarce factor with a rising price (ie. real wage rate). Since unskilled labour is the most widely distributed factor of production, the increase in its real wage has brought about an overall reduction in poverty in the country. In addition, the increase in the number of two-income households has contributed to the increase in total household income. This is underpinned by the increasing importance of women in the work force. Again, much of this increase is due to the demand for low-skilled labour generated by the rapid expansion of labour intensive export-oriented manufacturing activities (Rasiah 1995). The labour force participation rate for women increased from 37.2 percent in 1970 to 46.7 percent in 1990, while the share of women in employment increased from 31 percent to 35 percent over the same period (Government of Malaysia 1991). In sum, the Malaysian experience with employment generation and poverty reduction since the late 1980s compares closely with that of Korea and Taiwan in the late 1970s and 1980s (Fei *et al*. 1979; Hong 1990).

5. Concluding Remarks

Malaysia is undoubtedly a development success story. While economic performance has been impressive by developing-country standards throughout the post-independence period, the achievements have been truly remarkably since the late 1980s when there was a decisive shift towards greater outward-orientation of economic policy. Economic growth during this period has been accompanied by rising living standards, and an improvement in the distribution of income, ameliorating the twin problems of poverty and racial imbalances.

Malaysia's economic success can be attributed to the ability it has shown in positioning itself within the new world economic order characterised by increased internationalisation of production. As a small-open economy, Malaysia's economic policy stance has not been to isolate itself from these global trends, but rather to respond to developments on the international front as they unfolded. While there were some policy excesses triggered by conflicting objectives in a plural society, the policy makers have been successful in rectifying policy errors swiftly.

The Malaysian experience of growth with equity is consistent with the mainstream (neoclassical) policy stance relating to export-led industrialisation. The key lesson to come from the Malaysian experience is that in a small open economy, the task of achieving the apparently conflicting objectives of growth and equity is facilitated by a long-term commitment to an open and liberal trade and investment policy regime. Unlike many other developing countries, Malaysia never resorted to stringent quantitative trade restrictions. Domestic price signals were therefore never insulated from world market conditions, and resource costs arising from rent-seeking activities have always been minimal by developing country standards. Despite the affirmative action policies under the NEP, the private sector was never marginalised and the policy emphasis on export orientation was never compromised. With this policy regime, coupled with a stable political climate, the Malaysian economy has been well placed to take full advantage of the new opportunities arising from integration with the global economy. There is little doubt that the affirmative action program under the NEP was instrumental in establishing the legitimacy of government policy and achieving political stability and social harmony. It was an effective explicit mechanism in demonstrating that all would share in future growth. At the same time, the resource cost of these direct redistributional policies was not a major drag on growth because of the key role played by FDI flows and rapid export expansion in augmenting the domestic resource base.

Table 1: Malaysia: Growth and Export Orientation, 1970-1995

	GDP		Per-capita GDP		Export-orientation
	value* (millions of ringgit)	growth (%)	value* (ringgit)	growth (%)	X/GDP (%)
1965-69	30149	7.08	29023	3.97	46.09
1970-74	35986	9.12	3257	6.04	42.30
1975-79	51703	7.22	4734	4.17	50.44
1980	64883	7.44	4736	5.48	57.54
1981	69387	6.94	4918	3.83	52.34
1982	73509	5.94	5066	3.02	50.89
1983	78104	6.25	5245	3.54	51.18
1984	84116	7.70	5509	5.02	54.27
1985	83305	-0.96	5313	-3.55	54.85
1986	84179	1.05	5225	-1.65	56.31
1987	88717	5.39	5367	2.71	63.85
1988	96647	8.94	5705	6.30	67.61
1989	105547	9.21	6083	6.63	73.26
1990	115828	9.74	6522	7.21	76.28
1991	125861	8.66	6923	6.15	80.84
1992	135667	7.79	7290	5.30	77.65
1993	146987	8.34	7636	4.74	81.45
1994	159848	8.75	7972	4.41	89.82
1995	175225	9.62	8506	6.70	95.50

Notes: * At constant (1990) prices.

Source: IMF, *International Financial Statistics Yearbook - 1995* and Malaysia Ministry of Finance, *Economic Report 1995* (for estimates for 1995).

Table 2: Sectoral Growth Performance: Contribution to GDP and Real Growth Rates (in brackets), 1970-1995*

	1970	1975	1980	1985	1990	1995
Agriculture	28.5	26.9	22.9	20.8	18.7	13.9
	....	(9.5)	(5.1)	(3.1)	(4.6)	(2.5)
Industry	32.3	32.6	35.8	36.7	42.2	47.2
	....	(6.7)	(10.7)	(5.7)	(9.8)	(11.2)
Manufacturing	15.8	17.3	19.6	19.5	26.9	33.1
	....	(6.7)	(11.4)	(5.3)	(13.7)	(13.3)
Services	33.5	40.5	41.3	42.6	39.1	38.9
	...	(12.2)	(13.9)	(5.8)	(5.1)	(8.6)
Total	100	100	100	100	100	100
	.....	(10.6)	(8.5)	(5.2)	(6.8)	(8.7)

Notes: * Output shares and growth rates are based on constant (1978) prices. Growth rates are annual averages between the reported years.

Source: Ministry of Finance Malaysia, *Economic Report* (various issues)

Table 3: Manufactured Exports: Composition and Share in Total Exports (%)

	1970	1975	1980	1985	1988	1990	1993
Food, beverages and tobacco	24.9	15.6	8.5	6.8	5.3	3.4	2.9
Textile, clothing and footwear	7.0	11.4	13.2	11.3	9.1	6.5	6.2
Wood products	19.8	10.7	7.7	3.2	3.5	2.2	4.6
Rubber products	3.7	2.3	1.4	1.0	3.5	2.3	2.8
Paper products	1.2	0.5	0.6	0.6	1.0	0.7	0.6
Petroleum products	35.5	5.5	3.1	9.1	2.9	2.1	1.9
Chemicals	7.7	4.6	3.1	5.3	5.3	2.4	3.2
Non-metallic minerals	4.5	1.2	1.0	1.3	1.7	1.3	1.2
Metal products	7.6	3.2	4.1	3.1	4.4	2.6	3.5
Electronics and electrical products	11.5	42.2	49.3	56.8	58.1	44.1	62.6
Electronic components	---	---	37.5	38.8	33.4	19.5	21.2
Electrical appliances	---	---	4.5	4.0	4.7	4.1	5.7
Other elecrical machinery	---	---	7.3	14.0	20.0	20.5	35.7
Transport equipment	7.2	3.5	3.6	5.0	1.9	3.2	4.1
Optical and scientific equipment	0.8	1.8	2.2	2.0	1.9	1.8	2.3
Toys and sporting goods	0.4	0.7	0.9	1.5	1.6	1.6	1.8
Other manufactures	3.9	2.3	4.6	2.1	2.7	3.6	4.3
Total manufactures#	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Value (million US$)	148.1	799.9	2811.3	4603.1	9960.5	22194.6	34201.7
As % of total exports	8.8	20.7	21.7	30.1	47.2	75.4	72.6

Note: # Excuding petroleum products, and processed palm oil and other oil products.

Source: Bank Negara Malaysia, *Quarterly Bulletin*, Kuala Lumpur, various issues.

Table 4: Summary Statistics on Employment and Unemployment, 1980 and 1985-1996

	Labour force ('000)	Labour force participation rate			Unemploy-ment rate
		total	male	female	
1980	5122	65.3	87.6	43.1	5.6
1985	6039	65.8	87.4	44.3	6.9
1986	6222	65.8	87.5	44.2	8.3
1987	6409	65.9	86.9	44.9	8.2
1988	6622	66.1	85.8	46.5	8.1
1989	6850	66.3	85.8	46.9	6.3
1990	7042	66.5	85.7	47.3	5.1
1991	7204	66.6	85.7	47.5	4.3
1992	7370	66.7	85.7	47.6	3.7
1993	7627	66.8	87.0	46.1	3.0
1994	7846	66.9	87.1	46.5	2.9
1995	8060	67.0	87.2	46.8	2.8
1996*	8278	66.8	86.6	46.9	2.8

* prediction

Source: Ministry of Finance, *Economic Report* (various issues)

Table 5: Employment by Sector, 1976, 1980, 1985, 1990 and 1995 (% shares)

Sector	1976	1980	1985	1990	1995
Agriculture, forestry and fishing	43.6	40.6	31.3	29.9	18.9
Industry	20.9	22.7	23.6	24.6	34.9
Manufacturing	14.2	15.8	15.2	17.6	25.5
Services	35.5	36.7	45.1	45.5	46.2
Total	100	100	100	100	100
(‘000)	4376	4817	5622	6682	8060

Source: Ministry of Finance, *Economic Report* (various issues).

Table 6: Employment, Profitability and Real Wages in the Malaysian Manufacturing Sector.

	Employment (1990=100)	Price-cost margin (%)	Real value added per worker (1990=100)	Real Wages (1990=100)
1965-69	12.1	17.3	57.1	67.6
1970-74	24.9	21.5	64.0	61.6
1975-79	53.4	20.3	67.5	74.2
1980	--	--	--	--
1981	58.2	17.3	73.6	82.5
1982	61.7	16.6	71.8	86.4
1983	54.8	17.9	82.6	93.0
1984	59.2	19.0	89.9	97.6
1985	56.3	18.6	94.1	105.2
1986	56.8	20.1	102.8	104.1
1987	61.4	18.6	98.6	102.4
1988	71.0	18.1	99.5	98.7
1989	82.7	18.9	104.5	99.4
1990	100	18.6	100	100
1991	115.8	18.9	106.7	104.4
1992	122.5	18.8	107.3	108.3
1993	139.9	--	--	109.7
1994	152.6	--	--	112.9

-- Not available

Sources: Compiled from Malaysian Department of Statistics, *Annual Survey of Manufacturing* and *Monthly Bulletin of Manufacturing Statistics* (for 1993 and 1994).

Table 7: Incidence of Poverty and Hardcore Poverty by Region, and Gini Coefficients, 1970-1995 and Forecast for 2000

	1970	1984	1990	1993	1995	2000**
Incidence of Poverty						
Urban	0.255	0.082	0.075	0.053	0.041	0.022
Rural	0.586	0.247	0.218	0.186	0.161	0.110
Total	0.493	0.184	0.171	0.135	0.096	0.060
Incidence of Hardcore Poverty*						
Urban	0.158	0.024	0.014	0.011	0.009	0.010
Rural	0.446	0.087	0.052	0.043	0.037	0.001
Total	n.a.	0.063	0.040	0.030	0.022	0.005
Gini Coefficient	0.537	0.479	0.446	0.459	0.464	---

Notes:
* The cut off income level for the determination of hardcore poverty is set at half of that used in defining poverty (which varies from year to year; refer to source documents listed below).
** Forecast
--- Not available
Sources: Anand (1983); Government of Malaysia (1989, 1991, 1993 and 1996).

Table 8: Mean Monthly Household Gross Incomes by Ethnic Group*, 1957-1995

	1957/58	1967/68	1970	1984	1990	1995
All Groups**	199	217	264	1095	1167	2007
Malay	144	130	172	852	940	1600
	(100)	(100)	(100)	(100)	(100)	(100)
Chinese	272	321	394	1502	1631	2895
	(189)	(247)	(229)	(176)	(170)	(181)
Indian	217	253	304	1094	1209	2153
	(151)	(195)	(175)	(128)	(128)	(135)

Note:
* Figures in parentheses indicate group incomes relative to Malay incomes. All other figures are in Ringgit.
** Includes minorities and non-citizens.

Sources:
For years up to and including 1970: Anand (1983); 1984 and 1987: Government of Malaysia (1989); 1990 and 1995: Government of Malaysia (1996).

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