What makes Malaysia sail?

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1. INTRODUCTION

Malaysia is a small country but has some big achievements to its credit in the field of economic development. Starting as a low income country in 1957, it has long climbed up the ladder into the upper middle grouping in the World Development Reports. Its per capita income at constant prices rose from US$ 306 in 1965 to US$ 5490 in 2007 and its economy with GDP worth 357.9 billion US dollars occupied the 29th position in the world with per capita income rank at 57 the same year.

Geographic location, an abundance of natural resources, especially in agriculture, forestry and mineral, a small population with low density, a work friendly climate, and a plural social order have been the initial advantages the country enjoyed. However, there was a lack of capital, and a shortage of both skilled and unskilled manpower. The size of domestic market was too small to warrant industrialization. Expediency demanded that the country evolve a policy design that could cash on its strengths and convert its deficiencies into advantages keeping at the same time her options flexible. This paper takes a brief look at the contours of its economic transformation and the major policy light houses that guided her sail along merrily for over half a century.

II. POLICY FRAMEWORK

Direction planning has been a major factor in shaping the economic destiny of Malaysia. It has been instrumental in achieving social goals like the redistribution of wealth, and the provision of vital public utilities. The transformation process adopted an open economy model, choosing trade as its engine of growth. The country provided infrastructural facilities, tax concessions, and unrestricted remittance options to attract foreign capital It rapidly expanded education and training facilities for human resource development; Malaysia has already past the UNDP threshold for high human development and was ranked 63 with her index at 0.811 in 2005 as per HDR for the year 2008. In addition, the country brought in a large number of foreign workers and professionals to fill the critical gaps, even as their presence in large numbers caused some socio-cultural problems.

The country ensured an efficient coordination of major sectors and kept economy operating almost friction-free. The hurdles and crises that came along occasionally were managed well. The leadership *had* a long run view for development from the very start which eventually culminated in what is known as *Vision* 2020. It aimed at achieving a per capita income of US $ 10,000 by that year. With an average growth rate of 7%, it was well on course until late nineties, when it suffered a setback during the Asian financial crisis and had to devalue its currency by about a third making the task difficult.

III. THE TRANSFORMATION

Malaysia started its economic journey with dependence on rubber, tin and oil palm. These three commodities along with other raw materials had already set her economic tempo prior to independence. During the seventies the country decided on shifting from the primary sector to manufacturing under a protection regimen. Foreign assistance from Japan and the West eased and hastened the process of transformation. Exports of manufactured goods were soon fuelling her growth. The structure of the economy underwent rapid transformation. The share of the primary sector declined progressively from 42.7% in 1970 to a mere 16.7% in 2006. The industrial and services sectors both expanded but the share of the services grew much faster.

Table 1: Sector contribution to GDP (%)

Sectors	1970	1980	1990	2000	2006
Agriculture 1	29.0	22.9	18.7	8.6	7.9
Mining 2	13.7	10.1	9.7	7.5	8.8
Primary 1+2	**42.7**	**33.0**	**28.4**	**16.1**	**16.7**
Manufacturing 3	13.9	19.6	27.0	32.3	31.1
Construction 4	3.8	4.6	3.5	3.3	3.1
Secondary 3+4	**17.7**	**24.2**	**30.5**	**35.6**	**34.2**
Services: 5	36.2	40.0	42.3	53.6	51.8
Others* 6	3.4	2.8	-1.2	-5.3	-2.7
Tertiary 5+6	**39.6**	**42.8**	**41.1**	**48.3**	**49.1**

Source the Table has been constructed using information in the Statistical annexure in the Bank Negara Annual Reports for the relevant years.

However, the declining share of agriculture in the GDP should not be misunderstood as neglecting its importance in the economy. Rising food prices, dependence on imports even for chicken feed, increasing demand for palm oil and natural rubber abroad have led to a renewed interest in the sector and a special fund for the development of agriculture has been established at the federal level. The country is now in the third phase of the National Agricultural Policy for directing towards the agro-year 2010. Diversification is encouraged and taking place in the expanding industrial sector. This was made possible by the simultaneous and rapid expansion of the services sector. Malaysia spent colossal amounts on developing infrastructural facilities to good effect.

IV CRSIS MANAGEMENT

The Asian crisis announced its arrival in Malaysia with an abrupt fall in the Kuala Lumpur Composite Index (KLCI) on July 29, 1997 accompanied with a depreciation of the Ringgit. Both trends were gaining pace unabated by the following week; one could clearly see the economy rolling down the hill. During the 63 weeks from July 1997 to September 1998, the stock market fell by over 68% and the domestic currency lost no less than 37% in terms of US dollar. The nexus between the two markets was: sell stocks at KLSE and with Ringgits so released buy dollars in the forex market to take out. This hastened the melt down in both the markets. The consequence: short term foreign capital worth 33 billion US dollars left the country in a short span of time and her economy suffered a negative rate of growth (-7.5%) in 1998.

Most of the literature on the subject does not deny the stated market nexus but there has been much difference of opinion on two vital issues: (i) what was essentially responsible for the crisis – internal economic weaknesses or external forces - and (ii) the imposition of credit controls with dollar peg for the currency or going to the IMF like others in the region was the better remedial choice. Most economists at the national circuit were critical of the government for blaming solely the outsiders for the crisis and choosing capital controls as the cure. I found it difficult to go with them.

A crisis by definition is an unforeseeable short-term shock. This is why no one could or did fire a warning shot then as in the current global melt down now. Its occurring or intensity could not be determined by distant happenings; for, it is perceptions that abruptly overtake rationality in a crisis situation. Malaysian economy *had* weaknesses; which economy does not. Nevertheless, her economic fundamentals around the crisis were by no means fragile. Even in 1997 the economy grew at 7.8%, inflation stayed low (2.7%), trade-GDP ratio was 1.86 and exports exceeded imports by 12%. The debt service ratio to export earnings too did not cross 6.7% during the period. Indeed, there is a well researched conclusion in the literature that currency speculators played a leading role in the 1997-1998 crises. Even the IMF admitted in 2001 that Malaysia was essentially the victim of contagion.

Individual countries are so different from one another in their structures, political affiliations, resources and social ethos that comparing their results for policies looks quite hazardous. Still, Malaysia opting for controls perhaps made a better choice. The country maintained its self-esteem and came out of the crisis less scathed and faster than those like Thailand and South Korea who went for the IMF bailout programs. Table 2 juxtaposes some key variables for the three economies for the years 1996-2000 in support of the observation. It was not, for example, until July 31, 2003 that Thailand could fully clear the IMF loan of US $ 14.5 billion which the country got as part of a reform package. On the occasion her Prime Minister vowed on the television that the country would never enter into the bail-out support of the US based financial institution again. It would be a mistaken view that Malaysia gained nothing by taking a different route to meet the crisis. If nothing else it certainly saw fewer bankruptcies and, therefore, unemployment remained within normal limits. Indeed, the country eventually won praise from the IMF itself for her reforms including capital controls.

Table 2: Key comparative variables for Malaysia, South Korea and Thailand

Countries	Years				
	1996	1997	1998	1999	2000
Real GDP growth %					
Malaysia	8.6	7.3	- 7.4	6.1	8.3
South Korea	5.5	5.0	- 6.7	10.7	9.3
Thailand	7.1	-1.4	-10.5	4.4	4.6
Unemployment %					
Malysia	2.5	2.6	3.2	3.4	3.1
South Korea	2.0	2.6	6.8	6.3	4.1
Thailand	0.9	4.4	4.2	3.6	3.3
Current BP as % of GDP					
Malaysia	-4.8	-5.2	13.2	15.9	9.4
South Korea	-4.4	-1.7	12.7	6	2.7
Thailand	-7.9	-2.0	12.8	10.2	7.6

Source: Calculations based on data from World Development Reports

Malaysia being a wide open economy with US as its major trade partner cannot remain, like other countries in the world, unaffected by the current global melt down though its growth rate is still not in the red. The country is in a relatively better position to face the impact. It has a steady domestic demand, labour market is stable and there currently is a huge external reserve of around US $110 billion which is sufficient to finance nine months imports. Furthermore, there is a declining trend of non-performing loans in the financial sector; adequate liquidity exists in the system. Also, the development of Islamic banking and insurance lends a measure of stability to the financial sector. The country is in a strong position to face the current economic challenges. Its precautionary measures are putting money straight into the hands of those who have high propensity to spend; the country is supporting its unemployed by enrolling them into public funded training schemes for improvement of skills in addition to shortening waiting period to move into new jobs.

V. SOCIAL EQUILIZATION

The social equalization programme of Malaysia, now known as the new economic policy (NEP) has been one of a kind in the world: in a social contract, the haves have voluntarily agreed to grant economic concessions to the have-nots to increase their share in the national cake. This is intended to reduce poverty and improve income distribution. Though impact is slow for a variety of reasons but of late things are brightening up. The population below the poverty line is now reported as no more than 13% albeit the rise in urban poverty due to migration from rural to urban centres is disquieting. The Gini coefficient for the country is on the decline and stood at 49.2 in 1997, the latest survey year. The narrowing of the gap is accounted for by the fall in the share of top 20% in the GNP combined with an improvement in the share of 40% in the middle and lower income groups.

VI. CONCLUDING REMARKS

Malaysia has done remarkably well in economic development. Natural endowments, sound policies, socio-cultural ethos and political stability have all combined, as the foregoing discussion shows, to hasten her pace on road to economic prosperity. The country has taken in its stride the challenges it faced on various fronts and shows resilience to meet those ahead. No two countries are alike; each grows in its own way. Malaysia is a unique case but what others can learn from her is national unity, accommodation, patience, consultation, management styles and a measure of self confidence that have been among the factors making her sail smooth and fast through turbulent global environment.