



**FAIRNESS,
COMPETITION &
DEVELOPMENT:
FOUNDATIONS FOR A
SOCIAL MARKET ECONOMY
IN MALAYSIA**

Supported by:



FOREWORD

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The global economic crisis, the world financial crisis and the recent Euro-zone crisis have raised questions about the fundamentals of the western economic system and the need for structural and systemic reforms. The call for economic reforms is also an important issue in Malaysia and the subject of political debate.

The Malaysian Government has adopted a comprehensive and ambitious reform programme in order to transform the domestic economy and to consolidate the well-being of the country. Germany, with its model of a Social Market Economy and thanks to recent structural reforms, has so far defied the crisis well and its economy is in a relatively good shape.

In this report, a group of Malaysian and international experts have studied the German model of the Social Market Economy and compared it with the situation in Malaysia. Although it is not possible to transfer the German example fully, due to its historical and cultural specifics, there are still some principles and solutions, which can enhance the reform debate in other countries. With this study we would like to provide some ideas and recommendations for Malaysian decision makers and experts and contribute constructively to the economic discussion in Malaysia.

On behalf of the Konrad-Adenauer-Stiftung, I would like to thank the authors of the booklet for their excellent work and scientific engagement.

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As part of Malaysia's next stage of economic development, the Government has identified the urgent need to escape the "Middle-Income Trap" and achieve the "High Income" status of a modern, developed, industrial nation.

To this end a number of plans including a "New Economic Model," the Economic Transformation Programme (ETP) and the Government Transformation Programme (GTP) have been developed but there is still much debate about the way the economy and society should evolve.

Some important questions that must be considered include: What makes a developed country?; Is it just a matter of achieving 'high income' or does it require something more?; What will it take for Malaysia to achieve sustainable development?; and Can Malaysia do it?

To address these questions, this timely report presents of a set ideas and recommendations arising from an on-going research programme to study the so-called Social Market Economy model, popularised in Germany, which many people believe delivers a socially-just form of economic development.

The authors provide a realistic assessment of the state of the Malaysian economy as it is today and how we have arrived here. They then look at some key issues affecting Malaysians including: economic and enterprise development; the role of labour, jobs and fair wages and; social policies, social protection, social welfare and education. With comparisons to the German Social Market Economy and other economic models, the authors make some useful and interesting suggestions on possible reforms within a Social Market Economy framework tailored to the Malaysian context.

I am very pleased that UniRazak has been able to contribute to this research team and its various reports, seminars and study groups. We were pleased to host the launch of the Social Market Economy research programme and we are again happy to be part of its on-going success. We hope the report and its conclusions will make a useful contribution to the economic debate in Malaysia and we look forward to new insights from further research in the future.

Executive Summary

"Malaysia is at a crossroad. ... If we do not correct our course we will be unable to continue improvements in education health and quality of life. However if we redouble our efforts to attract investment, drive productivity improvements and innovate we can compete successfully in the global economy and achieve high-income status."

Dato' Sri Najib Tun Razak
Foreword to the ETP

Malaysia at a crossroads

The history of socio-economic development in Malaysia is one of relative underperformance. Although Malaysia's economic growth and social indicators have out-performed regional peers such as Thailand, the Philippines and Indonesia, other countries such as South Korea, Singapore, Taiwan, and Hong Kong have out-performed Malaysia by many times since the 1980s.

The Malaysian Government has in recent years recognised this problem which has come to be called Malaysia's "Middle-Income Trap."

The administration of Prime Minister Dato' Sri Najib Tun Razak has produced a clear and honest assessment of Malaysia's current position and has provided proposals in a series of policy programmes including the New Economic Model (NEM), the Economic Transformation Programme (ETP), the Government Transformation Programme (GTP) and the 10th Malaysia Plan (10MP).

While there is widespread consensus that Malaysia is at a crossroads, there is less consensus about which road to follow to achieve world-class education, health and quality of life that reflects that of a high-income economy.

Our primary concern in this study is to discuss the main issues in the Malaysian economy and to consider some alternative reforms required to achieve a new just model of sustainable socio-economic development.

Our emphasis is on social and economic performance taken together, guided mainly but not exclusively by the Social Market Economy (SME) model of Germany and drawing on the economic policy frameworks of other countries in Asia and around the world.

Transforming Malaysia

The task of the next Malaysian Government - national transformation - is of a different order of magnitude from that facing any other government since Merdeka. Transformation requires a sea-change in Malaysia's social, institutional and economic systems and a revolution in the mind-sets of all stakeholders among the Malaysian people - the *Rakyat*.

For any government interested in national transformation, it is not sufficient to rely on the *Rakyat*'s material dissatisfaction with their current economic situation. Transformation must represent an explicit decision to change the existing state of affairs into something morally and economically better - the creation of a new, socially-just model of sustainable socio-economic development.

A successful socio-economic transformation strategy must ensure that the design and preparation of policy includes plans for the reform or removal of social, economic and institutional obstacles that hinder its effective implementation.

Among the many obstacles facing Malaysia, both domestically and internationally, one major obstacle stands out - the negative perception, real or otherwise, that whatever policies are proposed and whatever resources are devoted to pursuing them, the social and economic position of the vast majority of Malaysians will not change.

Unless a satisfying and creative transformation strategy can be developed national transformation will be virtually impossible.

Social Market Economy approach

This report will present an overview of the "big picture" and draw attention to the key issues which include:

- The Malaysian Economy and its performance in the current very challenging global economic environment
- The Malaysian Corporate Sector and whether and how it can respond to the challenges ahead
- The Malaysian Labour Market and the inclusion of employees in the growth process
- The Social Dimension and whether and how Malaysian economic growth will ensure inclusion and delivery of social as well as economic needs
- The Education System and how it can be transformed to provide a framework for

creative thinking, skills and quality in both academic and vocational studies

internalise a new approach to socially just economic development.

- The Institutional Dimension and whether Malaysia's social, economic and political institutions are fit for creating a developed economy

We also examine how these issues are inter-related when we talk about creating a new socially-just model of sustainable socio-economic development

Socially just development

A new model of socially-just development for Malaysia has important issues to consider which include:

- Building strong economic foundations based on monetary stability and fiscal responsibility to promote an ordered-liberal market which promotes growth and inclusion together;
- Changing the role of the state. The Government should spend prudently, regulate justly and nurture accountable and productive ties with business so as to create a conducive environment for investments that can generate growth;
- Respecting private property rights to create the confidence that no expropriation of firms or private assets will occur once their investments lead to productive enterprises;
- Creating a transparent and accountable tripartite link between the Government, banks and industries to shape corporate development;
- Promoting a social compact within firms, facilitated by the Government, involving employers and employees. Such ties nurture the development of firms and provide just wages;
- Employing resourcefully GLCs so that their overwhelming presence in key economic sectors should not be seen as an impediment to economic growth;
- Investing in education to foster a well-trained labour-force that can contribute to productive R&D that leads to the creation of new technologies;
- Reforming institutions through devolution of power to ensure checks and balances within the political system;
- Finally, fostering an ethical foundation, based on common values that recognise, promote and

The Economic Backdrop

- **Malaysia has grown strongly since independence but not as well as others**
- **Over-dependence on the Government and Export sector underpins growth**
- **The high income target is challenging and overlooks other development needs**
- **Reducing inequality in income and wealth should also be targeted**
- **Real economic transformation requires a change in policy institutions**

Malaysia's Economic Development

Malaysia is a plural society of around 28 million people. It is rich in resources and has a relatively good, modern infrastructure. Over the past five decades, the Malaysian economy has undergone significant structural change, transforming itself from a "rubber and tin" economy to one that is well-diversified and industrialized. Malaysia is now acknowledged as an upper-middle income country with a good Human Development Index (HDI) ranking.

Table 1:
HDI for Malaysia and selected regions

| Year | Malaysia | High HDI | East Asia & Pacific | World |
|------|----------|----------|---------------------|-------|
| 2011 | 0.761 | 0.741 | 0.671 | 0.682 |
| 2010 | 0.758 | 0.739 | 0.666 | 0.679 |
| 2005 | 0.738 | 0.716 | 0.622 | 0.660 |
| 2000 | 0.705 | 0.687 | 0.581 | 0.634 |
| 1995 | 0.674 | 0.662 | 0.544 | 0.613 |
| 1990 | 0.631 | 0.648 | 0.498 | 0.594 |
| 1985 | 0.600 | 0.630 | 0.463 | 0.576 |
| 1980 | 0.559 | 0.614 | 0.428 | 0.558 |

Source: World Bank, 2012

However, this transformation has been heavily reliant on the contribution of the Government and the External sectors. From a trade perspective, flows to and from the American, East Asian and EU markets dominated, while Malaysia was heavily dependent on Foreign Direct Investments (FDI) from these three regions to drive its industrialization process. In the current situation, the question that arises is whether Malaysia can continue to rely on government spending, foreign investments and exports that are heavily import dependent. The answer is: No!

Even though the HDI ranking is good ((rising three notches from 2010 to number 61 in 2011),

Malaysia is still not ranked in the "Very High" HDI group and other social and governance rankings are poor. There are growing concerns about environmental degradation; education and health services are in urgent need of revamp and social protection policies for the vulnerable are grossly inadequate in a society that has high inequality of income, wealth and opportunities. Malaysia is also in evident need of a viable import-substitution industrial policy that nurtures domestic entrepreneurship and ensures a fair wage for employees. These problems suggest that Malaysia has traded economic development against socio-political development.

These major socio-economic and governance problems indicate an urgent need for Malaysia to adopt an economically productive and sustainable model of development that fosters an equitable, sustainable and socially-just pattern of growth.

The Middle-Income Trap

The Malaysian economy has grown strongly but not as fast as other East Asian countries. The rate of growth has fallen behind in recent years and as a result Malaysia has fallen into a "Middle-Income Trap."

Table 2:
GNI per capita (Current US\$, Atlas Method)

| Country | 1980 | 1990 | 2000 | 2010 | 2011 |
|---------------------|--------|--------|--------|--------|--------|
| High income | 9,906 | 18,510 | 25,324 | 38,765 | 39,783 |
| World | 2,552 | 4,089 | 5,278 | 9,074 | 9,488 |
| East Asia & Pacific | 1,285 | 2,762 | 3,728 | 7,099 | 7,857 |
| Middle income | 735 | 890 | 1,252 | 3,732 | 4,121 |
| Japan | 10,670 | 27,580 | 35,040 | 42,050 | 45,180 |
| Singapore | 4,710 | 11,450 | 24,500 | 39,410 | 42,930 |
| Hong Kong | - | - | 26,570 | 32,780 | 35,160 |
| S. Korea | 1,810 | 6,000 | 9,910 | 19,720 | 20,870 |
| Malaysia | 1,820 | 2,370 | 3,420 | 7,760 | 8,420 |
| China | 220 | 330 | 930 | 4,270 | 4,930 |
| Thailand | 710 | 1,480 | 1,930 | 4,150 | 4,420 |
| Indonesia | 490 | 600 | 560 | 2,500 | 2,940 |
| Philippines | 700 | 730 | 1,050 | 2,060 | 2,210 |
| Vietnam | - | 130 | 390 | 1,160 | 1,260 |

Source: World Bank, 2012

For example, in 1970 Malaysia's per capita Gross National Income (GNI) measured by the World Bank's Atlas Method stood at US\$400, above that of South Korea which was at US\$270. By 1980 these two countries had equal GNI per capita, but while Korea grew quickly to high-income levels Malaysia struggled to reach that target bracket. By 2011

Korea had a GNI per capita of US\$20,870 compared to Malaysia's of US\$8,420, which is also way below the high-income threshold and lower than the world average of US\$9,488.

**Table 3:
Malaysia - Average Growth, 1970-2011**

| | 70's | 80's | 90's | 00's | 2011 |
|--------------------------------------|------|------|------|------|------|
| GDP Ave Annual Growth for the Decade | 7.73 | 5.88 | 7.25 | 5.0 | 5.1 |

Source: World Bank, 2012; GDP growth (average decade %)

The Malaysian economy is now clearly slowing down and, unlike in the 1990s, there are no longer huge inflows of FDI. With the worsening global scenario and increased competition, the Government's main concern, and rightly so, is the need to move to knowledge-based economic growth.

There are, however, major structural problems if Malaysia is to create a thriving knowledge-based economy. Productivity issues and competitiveness are in decline and while there is an urgent need for new sources of growth, the human capital necessary to drive these sectors is in very short supply. Domestic investments in these new sectors are poor and R&D by the private sector to upgrade technology and enhance productivity has not been encouraging.

The Government's New Economic Model (NEM) has acknowledged these problems, primarily within the 12 National Key Economic Areas (NKEA) and the 131 Entry Point Projects (EPPs). Although these problems suggest that we cannot continue with "business as usual," in fact only about 15% of the EPPs do not require specific government funding or policy-support, suggesting that significant government involvement will continue well into the foreseeable future.

The High-Income Target: The Future We Want?

To counter this problem the Malaysian Government has announced the Economic Transformation Programme (ETP), that involves increasing GNI per capita from US\$6,700 (RM23,700) in 2009 to US\$15,000 (RM48,000) by 2020.

According to estimates in the ETP, this requires 6% real GDP growth per annum between 2009 and 2020. This is a challenging and perhaps unachievable target. The ETP's own estimates show that GDP growth has been only 4.3% per annum in the period 2001-09. Recent Bank Negara Malaysia forecasts estimate that real GDP growth may be around 4-5% per annum until 2015, so that for

more than half of the ETP planning period economic growth may be under target.

There is also the question of whether the high-income target is of any value in measuring actual incomes for the population in general. GNI measures total economic activity, the Gross Domestic Product (GDP) plus net income earned from abroad. Household income by contrast is the sum of salaries and wages, commissions, retirement benefits and dividends for all household members and is a better way to gauge actual income for the typical Malaysian.

Data from the Household Income and Basic Amenities Survey Report 2009 by the Department of Statistics Malaysia reports average income per household member of was around RM11,208 in 2009, very much below the GNI per capita income level of RM23,700 in the same year. Since there is no direct correlation between GNI per capita and average household income, the GNI target may be of limited use in raising overall income levels.

The other challenge to the High-Income Target is that it is a nominal income target. Since GNI per capita rises due to increases in prices, the target measure does not account for the erosion of purchasing power when incomes do not rise in line with inflation.

The ETP points to some other "Characteristics of a 'High Income' Economy" which are identified as:

- A high proportion of services in domestic output
- Domestic Consumption as an increasingly important driver of economic activity
- A "more balanced economy" which is less dependent on resource-intensive industries such as Oil & Gas
- Greater urbanization, especially in the Greater KL and Klang Valley areas

What is missing is any rationale to explain why these characteristics are desirable when considering the features of a "high-income economy"?

**Table 4:
Malaysia sectors (value added % GDP)**

| | 1980 | 1990 | 2000 | 2010 |
|-------------|------|------|------|------|
| Agriculture | 22.6 | 15.2 | 8.6 | 10.6 |
| Industry | 41.0 | 42.2 | 48.3 | 44.4 |
| Services | 36.3 | 42.6 | 43.1 | 45.0 |

Source: World Bank, 2012

The discussion lacks balance in consideration of other characteristics of a high income economy which are not desirable. These would include:

- Higher inequality – not just of income but also of social and economic opportunity, mobility and aspiration
- Higher dependency rates for the inevitable number of people who will not be in the workforce. Those who have retired, for example, will become relatively poor if their pension or retirement fund income fails to keep pace with rising average incomes
- Urbanisation causes obvious problems including crowded cities with pressure on housing, traffic flows, public transport, civic infrastructure including waste management, urban education infrastructure and so on
- Negative environmental characteristics of a “high income” economy including higher waste, demand on resources such as water and waste treatment, higher CO2 emissions and greater greenhouse gas emissions
- Resource Scarcity across all areas has consequences either in terms of limited access to resources or rising local resource prices

The experience of development in high-income economies is that income growth itself does not provide all of the solutions to these problems and that a new conception of resource creation and access has to be considered in the absence of a market response.

Income Inequality

Malaysia has one of the highest ratios of inequality in East Asia. Despite strong economic growth over the past four decades, the proportion of income held by various income groups has remained largely unchanged. The Gini Coefficient, a more general indicator of inequality, has also not significantly improved despite general economic growth.

Household income is also very unequally distributed. In 2009 the mean household income for the top 20 per cent of urban households was around RM11,312 while the top 20 per cent of rural households had a mean income of around RM6,028.

About 44.2 per cent of households in Malaysia still earned less than RM2,500 in 2009, down from 56.2 per cent in 2004. *Bumiputeras* have the highest rate of inequality of income between the three races in terms of inequality of income share.

Inequality also persists across different categories of resources including wealth, financial assets, real estate, investment assets and savings. Around 90% of Malaysians have no savings and 14% have no wealth. The bottom 80% of individuals holds only

5% of total financial assets with the top 20% holding nearly 95% of private assets.

Table 5:
Malaysia inequality indicators

| Income Share | 1984 | 1987 | 1997 | 2007 | 2009 |
|--------------|------|------|------|------|------|
| Bottom 20% | 4.6 | 4.9 | 4.4 | 4.7 | 4.5 |
| 2nd 20% | 8.4 | 8.7 | 8.1 | 8.7 | 8.7 |
| 3rd 20% | 13.0 | 13.3 | 12.9 | 13.7 | 13.7 |
| 4th 20% | 20.1 | 20.5 | 20.3 | 21.5 | 21.6 |
| Top 20% | 53.9 | 52.7 | 54.3 | 51.4 | 51.5 |
| | | | | | |
| Bottom 10% | 1.8 | 2.0 | 1.7 | 1.9 | 1.8 |
| Top 10% | 38.5 | 36.9 | 38.4 | 34.8 | 34.7 |
| | | | | | |
| GINI index | 48.6 | 47.0 | 49.2 | 46.0 | 46.2 |

Source: World Bank, 2012

Inter-ethnic inequality appears to have improved, but intra-ethnic inequality among *Bumiputeras* has remained almost the same. Spatial inequality still persists with *Bumiputeras* on the East Coast of the peninsula and in East Malaysia still living in poverty. This is an irony since affirmative action-based policies have targeted *Bumiputeras* for many decades.

The Inflation Element

Malaysia usually reports relatively low inflation based on the Consumer Price Index (CPI) but within this measure around 30% of consumer prices are controlled or subsidised. The CPI therefore understates the actual price level.

Table 6:
Malaysia inflation indicators (annual %)

| | 1980 | 1990 | 2000 | 2010 | 2011 |
|-----|------|------|------|------|------|
| CPI | 6.7 | 2.6 | 1.5 | 1.7 | 3.2 |
| WPI | - | 0.9 | 3.1 | 5.6 | 9.0 |
| GDP | 6.9 | 3.8 | 8.9 | 5.1 | 5.9 |
| GNI | 6.9 | 3.9 | 8.8 | 5.2 | 5.9 |

Source: World Bank 2012; CPI – Consumer Price Index; WPI – Wholesale Price Index; GDP – Gross Domestic Product Deflator; GNI – Gross National Income Deflator (local currency)

Using wider measures of inflation such as wholesale prices or the national income deflators, we can see that Malaysia has a significant inflation problem which should be seen as a major cause of concern.

High inflation erodes incomes and purchasing power for everyone who cannot increase their incomes in-line with rising prices. It is particularly damaging for

those on low incomes or on fixed incomes, such as retirement pensions. Inflation also erodes the returns on investments and can affect the competitiveness of Malaysian goods in the international market.

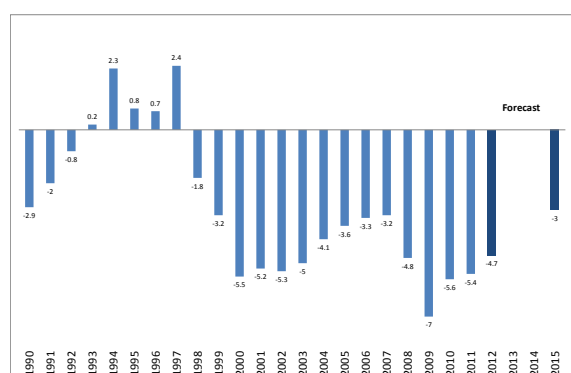
An independent central bank and an independent budgetary oversight body would provide credibility in monetary and fiscal policy

An additional pressing concern in Malaysia is the cost of subsidies used to keep consumer prices down. By 2012 these are projected to reach RM42.4 billion (US\$13.9 billion) greater than the Government deficit of RM42.2 billion. They are also the second largest component, accounting for 20.9%, of Government spending. The Government's Subsidy Rationalisation Programme has been repeatedly delayed and estimates produced as part of this programme suggest that inflation could rise between 2-3% during a five year period. This would suggest that a new form of monetary policy, perhaps in the form of a fully independent central bank, would be necessary for the control of prices as subsidies are removed.

Budget Deficit, National Debt and Savings-Investment Gap

Malaysia has had fourteen consecutive years of deficits since 1998 and achieved a surplus in only five of the ten years between 1990 and 1999. The Government targets a deficit of 3% by 2015 so that that there is expected to be at least eighteen years of deficit spending.

Figure 1:
Malaysian Government Deficit (% GDP)



Source: World Bank, 2012

National Debt is nearing 55% of GDP and is projected by some to reach 100% of GDP by 2019. Since there is heavy dependence on oil revenues there is a real danger that government finances will become unsustainable. In addition, inefficiencies

and overpriced government spending have been highlighted by the Auditor General Reports and although there has been high spending on sectors such as education, for example, much of it is focusing on overpriced construction projects.

There is already widespread recognition that the Government cannot continue to provide stimulus in the economy. Recent reports by the international ratings agencies have expressed concern about the absence of a credible framework to manage the fiscal position and its exposure to international shocks. The main concerns are ever increasing government spending, especially on operational costs and a narrow revenue base. There is also a need for the government to be smaller and for the private sector to play a bigger role in the economy and society.

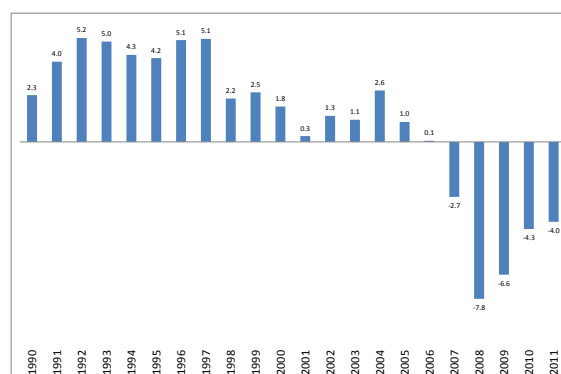
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This would suggest a new form of fiscal policy management such as an independent fiscal agency as is common in developed economies. Agencies such as the Office for Budgetary Responsibility in the United Kingdom help to forecast and monitor government spending and provide independent oversight of fiscal management.

Domestic and Foreign Investment

While investment in the boom years leading up to the 1998 economic crisis was as much as 40% of GDP, much of it from the private sector, today private investment is only around 14% of GDP. The savings rate is still very high, but it is not being transformed into investment. In 2009, savings were equal to 38% of GDP but Gross Capital Formation was only 22% of GDP.

Figure 2:
FDI Net Flows (current US\$ billions)



Source: World Bank, 2012

One reason for this is that of “investor confidence,” while money outflows, to alternative investment options around the world, is an increasing trend. During the 1990-99 period there was a cumulative net inflow of Foreign Direct Investments (FDI) of around US\$39.9 billion. Since then things have reversed, from 2000-09 there was a cumulative net outflow of US\$9.1 billion and between 2007-11 there has been a net outflow of US\$25.5 billion. These trends must be reversed and new ways to increase private investment, especially from domestic sources, must be found.

The Global Economy and International Trade

Malaysia is a small, open, trading country and total trade flows are over 150% of GDP. Nonetheless exports are overly dependent on the Electronic and Electrical sector, Palm Oil and, more recently, Petroleum. Since exports are overly dependent on imports – 90% of imports are intermediate and capital goods – and Malaysia lacks quality import-substitution industries, in the long term these problems pose a threat to the stability of a trade-based growth programme.

Table 7:
Malaysian trade indicators (% GDP)

| | 1980 | 1990 | 2000 | 2010 |
|---------|------|-------|-------|-------|
| Exports | 56.7 | 74.5 | 119.8 | 97.3 |
| Imports | 54.3 | 72.4 | 100.6 | 79.5 |
| Trade | 95.4 | 133.4 | 192.1 | 152.9 |

Source: World Bank, 2012; Exports of goods and services (% of GDP); Imports of goods and services (% of GDP); Merchandise trade (% of GDP)

Another growing concern is that all Malaysia’s major trading partners are facing a slowdown. EU and USA are already in or near a second recession while the Chinese economy faces a high risk of slowing down going forward.

This means that demand for imports in those countries will fall. And now that Malaysia has lost its export competitiveness and its place as a major FDI destination relative to other neighbouring countries, its exports will be adversely affected. Alternative sources of domestic growth are urgently needed.

Agriculture and Food Security

With the exception of Palm Oil, the agricultural sector has been relatively neglected from 1980s till the mid-2000s to the point where Malaysia has become a net food importer in key commodities such as rice and meat. Malaysian agriculture has been plagued by low productivity and poor income generation. As a result, this sector has the main concentration of poor households, in padi small-

holdings, coconut small-holders and small-scale fisheries.

Malaysia’s over-reliance on foreign workers, especially in palm oil plantations, has put pressure on agricultural wages and held back productivity and innovation, factors contributing to new social tensions. Malaysia must shift to higher productivity agriculture, not least to reduce its dependence on imported basic foodstuffs and strengthen its domestic food security situation.

Ethical Economic Development

Malaysia’s economic development record has not been accompanied by good governance and social progress.

Corruption, patronage, wastage and leakages have been a constant feature of the Malaysian economy. Malaysia’s ranking on the Transparency International (TI) Corruption Perception Index has continuously worsened over the last decade.

There is a widespread consensus that the political, legal and ethical framework must be strengthened. On the social side, education, welfare and the health systems require massive reform. There is a need to create a new relationship between the Individual, the Government and Society. This in turn requires a new model of development.

Why are we here?

- **Malaysia has had an eclectic policy process for more than thirty years.**
 - **Most approaches have not been applied in their full form**
 - **Despite positive measures, reforms have not fostered entrepreneurship**
 - **The most recent privatizations do not appear to have a clear economic rationale**
 - **Socio-economic transformation requires a new mind-set and institutional reform**
-

To understand Malaysia's socio-economic development it is useful to review three major policy approaches: Affirmative Action, the Developmental State and neo-Liberalism. The simultaneous implementation of all three policies has been a key feature of all administrations since that of Tun Mahathir Mohamad (1981-2003). This unusual and eclectic policy process has shaped Malaysia's socio-economic development significantly over the past four decades.

Affirmative Action is based on the New Economic Policy (NEP), introduced in 1970 to reduce poverty and redistribute wealth more equitably, through government intervention, via public enterprises that would acquire corporate equity on behalf of the *Bumiputeras*. Under Tun Mahathir, Affirmative Action was used to selectively target recipients of government concessions to nurture Malay-owned big business. Affirmative Action has had a major bearing on the shape of business formation and development in Malaysia.

The Developmental State Model is often referred to as the "Look East" approach due to its origins in Japan. A defining characteristic of industrialized Asia's Developmental State Model, involving considerable government intervention in the economy, is public-private cooperation. The government is a key player in steering resources to companies in order to attain its economic and social goals. In this model, a pact between the government, business and labour, through respect for trade unions, fosters stability in policy planning and implementation.

... the tenets of the Developmental State and neo-Liberalism were not applied in their full form. In practice the government has been highly selective when planning and implementing policies.

Of equal importance is the development of an autonomous and highly competent bureaucracy to

manage this relationship as well as investment in education to ensure an adequate supply of well-trained labour.

The neo-Liberal Model is a vastly different development approach, promoted actively by Margaret Thatcher in the United Kingdom and Ronald Reagan in the United States during the 1980s. Both espoused policies that limited government intervention and promoted liberalization and privatization of the economy with the private sector as the primary engine of growth. During the implementation of this model in the United Kingdom, there was extensive deregulation of the economy and curbs on trade union activity and power.

In Malaysia, deregulation, privatization and other "supply-side" policies were announced by Mahathir in the early 1980s as a mechanism to resolve the massive public debt problems. This policy initiative was presented as "new directions," but within the framework of the NEP.

There was greater reliance on "individuals" rather than trust agencies which led to the creation of an elite "new rich". However, the NEP also helped create a bigger *Bumiputera* middle-class, primarily through its focus on providing good early education to poor members of this community. Malaysia has undoubtedly undergone tremendous social and economic change involving the Malays since 1970s, primarily due to the NEP.

Today, however, these approaches are widely considered to be discredited, in the case of neo-Liberalism, following the global economic crisis, or outdated in the case of ethnically-based Affirmative Action.

Outcomes post-Mahathir

The consequences of mixing extremely contradictory policies can be judged by some key features of corporate Malaysia. No firm in the top-20 in 1957 or in 1970 managed to retain its position by 2010. There were no *Bumiputera*-owned firms among the top-20 firms and of the top-10 firms, six were Government-Linked Companies (GLCs), in spite of active privatization – many firms were re-nationalized after the 1998 crisis. Three were Chinese-held and one under Indian control.

Family firms emerged as an important component making up 40% of listed companies. Malaysia's top 10 corporate families own a quarter of the total market capitalization but none has a major brand product. Only a handful of Small and Medium-sized Enterprises (SMEs) have produced brand products of local and international repute.

In sectoral terms, no Malay-owned firm appears in the top-20 in the industrial sector. Most Malay-dominated firms are involved in finance, construction, property development and telecommunications. None of the top-50 has yet made it into new sectors such as technology, biotechnology, agro-industries, medical services or pharmaceuticals, in spite of active government effort to nurture firms in these industries. Banking is one key sector where Chinese influence has diminished and GLCs and *Bumiputera* individuals have increased ownership.

One reason for these outcomes was that the tenets of the Developmental State and neo-Liberalism were not applied in their full form. The Government has been highly selective when planning and implementing policies. During privatizations, there was no transparency in the exercise or support for independent regulatory institutions as the state retreated. The labour market was not liberalised. Instead trade unions were suppressed, ostensibly to ensure investor-friendly market conditions. Social compacts between labour and business were not encouraged. The same rationale is said to drive the large scale reliance on low-cost imported labour, the result of which has been to depress local wages. There was piecemeal support for social safety nets for the poor as privatization of core services, such as health and education, expanded and often reduced rather than expanded opportunities for their involvement.

The Abdullah Reforms

Tun Abdullah Ahmad Badawi, as Prime Minister between 2003 and 2009, continued a developmentalist agenda, although he intervened in different economic sectors. His administration emphasized the commercialisation of agriculture, to increase income in rural areas where poverty remains a serious issue. He actively nurtured SMEs which constitute approximately 99.2% of business establishments in Malaysia. The promotion of SMEs was still influenced by the government's attempts to cultivate *Bumiputera* businesses through Affirmative Action-type initiatives.

Despite ... positive measures, Tun Abdullah's reforms were not able to foster entrepreneurial SMEs.

Tun Abdullah's major institutional reform involved an attempt to use the GLCs more efficiently to generate growth. Reform of the GLCs was imperative as they had emerged as major publicly-listed firms. In 2005, 57 companies quoted on Bursa Malaysia were GLCs, with a market capitalisation of RM260 billion, constituting 36% of

the stock exchange's total capitalisation. New GLCs such as the Malaysian Biotech Corporation (MBC), the Halal Industry Development Corporation (HDC) and the Multimedia Development Corporation (MDeC) were created to select aid and encourage new industries. The promotion of high technology industries, in bio-sciences and pharmaceuticals, was to be implemented through these GLCs.

The Government promoted links between local and multinational corporations (MNCs) through its vendor system such as the Vendor Development Programme (VDP), Industrial Linkage Programme (ILP) and Global Supplier Programme (GSP). The VDP and ILP involved firms such as Proton, Dell and Intel, while the GSP linked SMEs to Carrefour, Tesco and Nestle.

Though still highly interventionist and heavily directed by the Government, these SME-Big Business ties were created to allow SMEs to learn from their engagement with MNCs and in the long-term reduce Malaysia's dependence on FDI. These links would enhance the productivity of SMEs and help them gain greater access to local and international markets. This vendor system was supposed to encourage competition that would spur innovation and upgrading and lead to the rise of independent entrepreneurial SMEs. These programmes were, however, predominantly captured by Malay firms, raising concerns about the issue of bypassing entrepreneurial non-*Bumiputera* firms. With liberalisation following economic crises, more non-*Bumiputeras* have benefited from these vendor programmes.

Despite these positive measures, Tun Abdullah reforms were not able to foster entrepreneurial SMEs because of selective patronage due to Affirmative Action. Although SMEs' share of GDP is about 32%, the contribution of *Bumiputera* SMEs in 2009 was only about 11.5%. Abdullah's attempt to promote *Bumiputera* SMEs proved as unsuccessful as Tun Mahathir's goal of creating internationally-recognized Malay conglomerates.

New Models by Najib?

The reform process has continued during the administration of Prime Minister Dato' Sri Najib Tun Razak (2009-present) primarily through the New Economic Model (NEM), the Economic Transformation Programme (ETP), the Government Transformation Programme (GTP) and the 10th Malaysia Plan (10MP).

The GTP outlines key social and economic problems. It highlights widely held views that education is in a rut, corruption and crime are on the rise, rural poverty is still a serious issue and the Malaysian economy has come to be "stuck in middle."

The GTP is an honest document outlining key social and economic problems.

The NEM promised a “new model” and raised expectations in many quarters. Nonetheless the key concern with the NEM, as well as the 10MP, is that they are both ignoring history. The 10MP, for example, is persisting with private sector-led growth leading to this question: why is privatization being promoted when neo-Liberalism has been so roundly discredited? There is also the issue of who these institutions are going to be privatized to? The most recent privatizations look more like “selling the family silver,” a crude transfer of public assets to highly concentrated, well-connected business conglomerates.

Khazanah, the most prominent Government-Linked Investment Company (GLIC), incorporated in 1993 to emulate the success of Singapore’s Temasek Holdings, has investments in over 50 major companies. Khazanah has been instructed by the Government to privatize its corporate interests. This has led to the privatization of key firms such as Pos Malaysia and Proton to well-connected companies such as DRB-Hicom, leading to concerns of wealth concentration, a factor that also undermines investor confidence and raises questions about the continued practice of rent-seeking and patronage.

The most recent privatizations look more like “Selling the Family Silver” ...

There is also the question of what will happen to the funds raised from the privatization process. It appears that divestment of real Malaysian assets will be followed by investment in international financial assets. Investments overseas provide more opportunities within a diversified portfolio, they are likely to be less expensive and they offer greater scope for higher returns both in terms of capital gains and dividend flows. Following the example of the United Kingdom in the 1980s, the rationale is that maximization of financial returns will take precedence over where or how those returns are made. This strategy has not proved sustainable.

By investing overseas Malaysia is in danger of capitalising its own competitors at the expense of domestic producers. In addition, international financial portfolios held by the Malaysian Sovereign Wealth Fund will be subject to the vagaries of international financial markets and returns can and will be exposed to the risk of adverse exchange rate changes that can wipe-out capital gains overnight.

Germany, by contrast, has retained a high level of investment in real domestic industrial assets, supported by a proactive role of the Government at the Federal and State level. As a consequence, Germany is considered as the “engine of growth” for the European economy and in turn a pivotal player in the stability of the global economic system. This accolade is well-deserved and is a model Malaysia would do well to follow.

Following the Global Financial Crisis, debates emerged worldwide, including in the United States, about the role of the Government in determining the pattern of socio-economic development. In Malaysia, GLCs dominate key sectors of economy. However, there has been insufficient debate on how the Government can be transformed to function more effectively in the economy, especially to promote growth, after the 2008 crisis. It appears that the conventional wisdom, especially in UMNO circles, is not to raise the issue of the role of the government in the economy for fear this will scare off domestic investment and FDI.

Germany ... has retained a high level of investment in real domestic industrial assets, supported by a proactive role of the Government at the Federal and State level ... a model Malaysia would do well to follow.

Instead the NEM and 10MP talk of “market friendly affirmative action” which is unlikely to inspire investor confidence. Meanwhile, huge investments to promote *Bumiputera* capital have proved very unproductive.

Enterprise Development: Lessons from Past Policies

Policies to cultivate local entrepreneurship have long been tempered with the need to promote *Bumiputera* enterprise, a crucial goal of Affirmative Action. This has hampered investments to enhance productivity and upgrade the quality of products. In manufacturing, non-*Bumiputeras* are reluctant to spend on R&D and acquire new technology for fear that ethnic-based policies would work against them as they develop their ventures. This inadequate investment in R&D is one reason for the presence of only a handful of large entrepreneurial firms with a long corporate history and for the demise of firms owned by some of Malaysia’s leading businesspeople.

Importantly too, race-based policies within the NEP, such as the *Bumiputera* Commercial and Industrial Community (BCIC), have undermined enterprise development involving Malay businesses, primarily due to the politics of patronage. The abuse of

Affirmative Action impeded Malay presence in the industrial sector and the rise of a dynamic domestic entrepreneurial community. Tun Mahathir's employment of the Developmental State Model and his subscription to privatization were used to justify the parcelling out of concessions to elites, ostensibly as part of Affirmative Action to pull *Bumiputeras* out of poverty. To ensure effective implementation of his unorthodox mix of policies, Tun Mahathir significantly re-moulded important institutions, including his own party, UMNO. Such systematic measures of "institutional degradation" profoundly hampered checks and balances in government, informing the pattern of selective patronage. Inevitably, the way the Government "picked winners" was flawed, fraught with corruption and conflicts-of-interest.

Real socio-economic transformation requires a change in mindset and institutional reform involving effective checks and balances

The BCIC has not fostered a large pool of independent *Bumiputera* businesses. The poor entrepreneurial capacity of domestic firms is evidently not due only to a poor public delivery system and weak institutional capacity among bureaucratic institutions. The Government's institutional framework is sound. However, trust in the Government's willingness to protect property rights is missing, inhibiting risk-taking and thus curbing entrepreneurial ventures.

The Government is now reforming its implementation of Affirmative Action, but this is not sufficient. Real socio-economic transformation requires a change in mindset and institutional reform involving effective checks and balances.

That no leading domestic firm is involved in new technologies, chemicals, pharmaceuticals or computers is a point of much concern in Malaysia. Old capital in manufacturing has fallen behind because public policies have bypassed them or appear to have undermined their activities. This factor contributed to businesspeople investing abroad, seen most cogently in the case of Robert Kuok, one of Malaysia's leading entrepreneurs. The diminishing presence of old entrepreneurial firms is a serious problem as the Government has failed to nurture a new breed of industrial capitalists.

Among family firms, there is also cause for concern as the founding generation is passing on and few from the new generation has emerged of any major standing, with the possible exception of those in the YTL, Genting, Hong Leong and Sapura groups. This is of vital concern as large business groups of the colonial period as well as inherited wealth have not been able to sustain themselves. Major business

groups established by Loke Yew, Tan Kah Kee, Lau Pak Khuan and H.S. Lee no longer have any presence in the economy. The corporate presence of the highly entrepreneurial Loh Boon Siew's Oriental Holdings group has been diminishing since his demise in 1995. The key issue is the extent to which these firms have been investing in R&D, a core factor if Malaysia is to escape the "Middle-Income Trap."

The diminishing presence of old entrepreneurial firms is a serious problem as the Government has failed to nurture a new breed of industrial capitalists

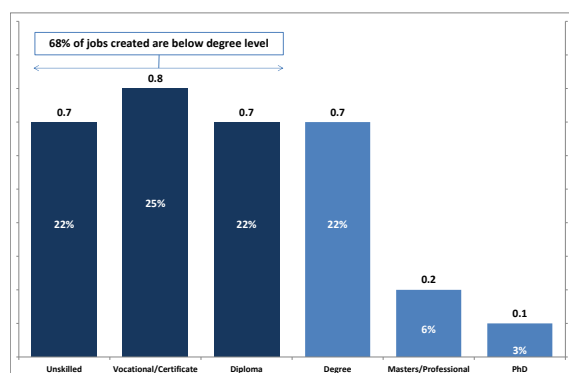
Domestic enterprises have to invest in R&D if they hope to emerge as key global suppliers. Malaysia's R&D spending as a share of GDP is 0.95%, higher than 0.4% in the late 1990s, though still very much behind other East Asian countries such as Japan (3.4%), Singapore (2.39%), South Korea (3.23%) and even China (1.5%). To encourage progressive R&D, there has to be little fear among domestic investors of expropriation due to Affirmative Action.

Labour, jobs, fair wages

- **Malaysia is in danger of creating a large number of low-paid, low-skilled jobs**
- **Low-value jobs create social and economic vulnerability**
- **Although there is low unemployment this has not fostered high productivity**
- **Inclusion of employees helps improve labour market outcomes**
- **Labour market reforms: Social compact between employers and employees**

The ETP aims to create 3.3 million new jobs by 2020 with the main growth sectors seen as Oil & Gas; Palm Oil; Wholesale & Retail; Tourism and Business Services. This is an ambitious target but on closer investigation what emerges is the alarming fact that the largest percentage of new jobs is in Low-Middle Income groups.

Figure 3:
Job Creation in the ETP – skills level



Source: ETP, 2010

Meanwhile, skill levels, especially the level of vocational skills, are low in the key areas targeted for employment creation. The largest number of jobs, accounting for 68% of the total, will be below degree-level jobs and 46% will be low-skilled or unskilled job types.

One can also legitimately ask if Malaysia can create even these low-skilled jobs and how training and human capital development, such as it is, will be provided. The bigger question is the long-term socio-economic implications of creating "low-value-added" jobs on such a large scale.

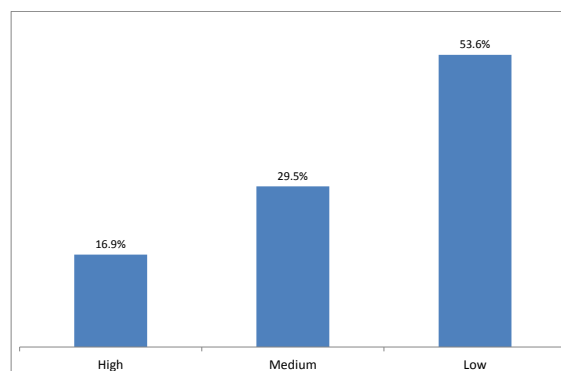
The Nobel Laureate Michael Spence notes that the US economy has created 27 million new jobs since 1990. This sounds impressive, but around 40% of these jobs are in "low-value-added" areas in the Government and Healthcare sectors. When one includes jobs in Leisure, Retail and Consumer

Services, the number of low-value-added jobs rises to around 70% of all the new employment created.

Malaysia is in danger of falling into a similar trap as the United States of creating a large number of low-value jobs

These types of jobs do not generate high incomes that provide real opportunities for financial independence and social and economic mobility. They are also vulnerable to economic cycles and are under continuous pressure from globalization which pushes down their incomes and threatens the stability of their employment. This creates vulnerability for people in these jobs, as well as for their families. People with employment in these sectors suffer from a "low-middle income trap," which is much more serious than a national-level "middle-income trap."

Figure 4:
Job Creation in the ETP – incomes level



Source: Derived from data in ETP, 2010

Malaysia is in danger of falling into a similar trap as the United States of creating a large number of low-value jobs. This has obvious risks to the viability and sustainability of the ETP's job creation targets. More importantly, it risks wider social consequences due to the creation of a "low-middle income" workforce exposed to on-going uncertainties and unstable income flows, lifestyles and access to social and economic opportunities.

Of major concern is that even this job creation ability is in doubt. Malaysia has lost its cost advantage to countries such as Cambodia, Indonesia and Vietnam. Malaysian companies can import labour cheaper than employing Malaysian workers.

High-Income versus Inclusion

Inclusion within the ETP is defined as a concept that "enables all communities to fully benefit from the wealth of the country." This is explained in terms of

employment-rich growth that creates new higher-wage jobs, investment in education and training to allow greater participation and improvements for the lowest income household groups. This endeavour will help lift the bottom 40%, from a mean income of RM1,440 in 2009 to RM2,300 by 2015.

There is a need to ensure the inclusion of Labour – employees – in reforms, primarily in terms of offering workers a fair wage.

However, the ETP focuses only on two key stakeholders: the Government and Private Business or public-businesses such as the GLCs. Little attention is paid to the role of Labour except within the concept of human resources.

This is an input-output approach in which employees are considered as a human resource input and the jobs created are viewed as an output of the process. Incomes from employment are also an "output," but the ETP avoids any discussion as to whether the higher incomes that are targeted reflect a "fair-share" of the surplus created from the expected new economic activity.

There is, therefore, a need to ensure that Labour is included in a new model of development if it is to be seen as inclusive, and just, primarily in terms of offering workers a fair wage. There are lessons from other models of development where Labour is seen to play a role, along with Business and Government, in generating equitable economic growth. One example is the Developmental State Model in Japan, while the other is Germany's Social Market Economy, the latter a highly inclusive model that has received too little attention in Malaysia.

Germany's Social Market Economy

The Social Market Economy model has a sophisticated understanding of the importance of stakeholder inclusion in the creation of a sustainable and resilient economy. This model acknowledges the need for the inclusion of employees in the process of creating productive market outcomes.

Central to this model are the notions of:

- Solidarity – inclusion of all stakeholders in the process of developing the market economy, in good and bad times, and in reviewing the outcomes of development. This ensures economic, social and individual involvement, both in the creation of wealth and in its benefits

- Subsidiarity – the delegation of responsibilities to the organisational level that is most effective in delivering the desired outcomes

The Social Market Economy model has demonstrated important benefits from including employees within the management of businesses, specifically to enhance economic value-added and to create an ordered approach to liberal economic markets, so-called Ordo-liberalism.

In the Social Market Economy the inclusion of the views of employees is managed in three main ways:

1. Co-determination – the inclusion of worker representatives on the "Supervisory Boards" (equivalent to the Board of Directors) of large companies, those with more than 2,000 employees
2. Works Councils – Independent of Management; for all companies larger than 5 employees but takes different forms and different sizes, similar to Joint Consultative Committee
3. Legislative Requirement – Basic Law, Co-determination Act, Works Constitution Act and derivative legislation (including EU Directives increasingly)

The principles of co-determination are presented succinctly in a handbook of the German Federal Ministry of Labour and Social Affairs which states:

"Virtually all operational and entrepreneurial decisions taken by an organisation also affect its employees. This is why employees have been granted the right to share in such decision-making, known as co-determination. The idea stems from a basic conviction that democratic principles should not be confined to the State but need to be rooted in all areas of society."

Supervisory Boards are used in large corporations to allow both employers and employees to take part in decision-making processes. For companies whose activities have an impact on thousands of people externally, representatives of the Government also have a seat in the Supervisor Boards.

For small and medium sized firms, Works Councils at the plant level play a role in the decision making processes in the company.

The long-term success of the German economy and its resilience, even in times of crises, has been largely attributed to co-determination, based on a clear recognition of the positive role that Employers' Organisations and Labour Unions can play in delivering mutually beneficial solutions for effective economic management.

Social harmony in employment

The rapid development of Germany – and Japan – as industrial powerhouses cogently indicates the value and viability of a social partnership between employers (Business) and employees (Labour). This social partnership, as the case of Germany and Japan indicates, will benefit all stakeholders and will support socio-economic development.

Social partnership, as Germany and Japan show, will benefit all stakeholders and will support socio-economic development

The reality in Malaysia is rather different. Malaysia inherited from British colonial rule a Business-Labour relations model that often positions employers and employees as adversaries rather than as social partners. Labour legislation, in form, favours industrial harmony, but in practice it often favours employers, disempowering employees and Labour Unions.

In Malaysia, a lack of inclusion of employees in the business process manifests itself in widely observed and long running problems in the labour market which include *inter alia*:

- High staff turnover
- Low employee motivation
- Low levels of employee loyalty to the companies that employ them
- Poor working conditions, pay and remuneration
- Under-performance of the labour-force as a whole

The absence of a role for employees within an inclusive market reform programme undermines the overall success of the transformation process and the productive development of Malaysian enterprises. Malaysia should therefore abandon this adversarial model of Business-Labour Relations and move towards one based on social partnership. To achieve this, however, there is a need for a change in mind-set among Malaysians of the nature of the relationship between Employers' Organisations and Labour Unions as well as between individual employers and employees. This change in mind-set must lead to a new model of partnership where employers and their representatives work together with employees and their unions.

Legislating and Socializing Co-determination

The route to successful co-determination, as in Germany, is through legislation. Such legislation will oblige employees and employers and their organised representatives to confer in a spirit of

pro-active negotiation and compromise. This type of legislation will enable employees and Labour Unions to be partners in the management of firms, sharing decision-making processes and so sharing in the risks and benefits that result.

When implemented properly employers treat their employees as part of a "family," and gain their loyalty and cooperation freely as a result. This expression of solidarity recognises the human needs of the workforce as well as the profit-motive of the employers. In this way businesses are not only economic entities but also living social organisms and a form of miniature society.

In Malaysia, there is a need for a new Social Partnership Model to promote solidarity in employment relations and enhance sustainable socio-economic development.

This expression of solidarity recognises the human needs of the workforce as well as the profit-motive of the employers

There will, undoubtedly, be resistance from some quarters to the idea of co-determination but the Government must have the political will to legislate processes that encourage Business and Labour to cooperate for the greater good. The Government must be an independent intermediary in this process and not, which often appears to be the case, allied to businesses.

Employees and Labour Unions on their part must also be ready and willing to take on parts of the responsibility of management as well as promote the firm's interests, its survival and growth.

The Minimum Wage

One area where the inclusion of employers and employees has proved successful is in the decision to introduce a minimum wage, which has received wide-spread support. Nonetheless this process could have been more successful if tripartite cooperation had been internalised. Employers' Organisations have complained that the common minimum wage fails to take into account wages and conditions within specific industries and so is inadequate in some instances and too high in others.

A system of employer-employee dialogue, as in the case of Germany, would be more effective in determining the minimum wage and would allow greater flexibility at the industry and sector level to allow the minimum wage to be set and adjusted according to economic conditions.

Social Policy, Social Protection and Social Welfare

- ***Social Policy and Social Protection require a fresh approach***
 - ***Reform of EPF into a full National Pension Fund is a necessary first step***
 - ***Well-structured Unemployment Insurance will protect incomes during downturns***
 - ***Social Welfare Assistance must cover a wider group of vulnerable people***
 - ***State Health Insurance can complement existing healthcare programmes***
-

Recent Government plans are silent on the role of Social Policy as a form of Social Protection in terms of promoting social harmony in employment, guaranteeing social security and providing a universal net for social welfare.

As a general proposition, Social Policy must provide universal coverage for everyone, especially marginal and vulnerable groups. Social Policy serves to reduce people's exposure to risks and enhance their capacity to protect themselves against hazards or loss of income. These propositions are based on the principle of Social Solidarity which recognises that although we remain individuals with rights and freedoms, we are part of a community and have responsibilities to others. This is the route to creating real and effective social inclusion.

Social Protection is defined as the set of policies and programmes designed to reduce poverty and vulnerability across society, as well as within specific targeted groups. This is best achieved by promoting efficient labour markets that provide meaningful and sustainable sources of income.

Social Policy and Social Protection serve to reduce exposure to risks and enhance capacity for self-protection against loss of income

Social Protection includes employment conditions and labour relation policies. It covers programmes for social insurance and social assistance as well as welfare policies for people not in the labour market. Social policies are not limited to social protection but encompass social harmony in employment relations, social security and social welfare components.

A National Pension Scheme

In Malaysia there is no universal coverage for all categories of people within the existing social protection system. This system is good at targeting certain categories of people but by doing so excludes others who are often equally in need of support. The Employees' Provident Fund (EPF), for example, Malaysia's mainstay social security and social welfare system, despite its size, is partial in that it serves as a one-off retirement fund and does not provide the universal coverage seen in more effective social protection systems.

To correct these limitations, the EPF should be transformed into a full-fledged National Pension Fund to ensure that fund participants maintain a sufficient pensionable monthly income for the rest of their lives. To enable this implies that the EPF is to be used solely for pension and nothing else. A National Pension Fund of this form also encourages social solidarity and individual inclusion since individual contributions accumulate into a common pool that can be re-distributed to benefit everyone in times of need.

Unemployment Insurance Scheme

Officially recorded levels of unemployment in Malaysia are very low, at around 3% of the working population. In reality many Malaysians are forced into low-paid, low value-added forms of employment because of an absence of income support options if they choose not to participate in the labour market or to take time in choosing better paid positions.

Long-term unemployment allowances lead to dependency, Unemployment Insurance should provide assistance for a limited time only

This means that unemployment is often disguised as under-employment which manifests itself in widely observed and long running issues in the labour market which include high staff turnover, low employee motivation, low level of employee loyalty to companies, poor working conditions and under-performance of the labour-force. Taken together these are symptoms of a market in which employees are not actively engaged in the determination of pay and conditions due to the imperative to find work at any wage.

Since high productivity is central to Malaysia's socio-economic development, the absence of an active role for employees is a significant risk to an inclusive labour market. An effective Unemployment Insurance Scheme which involves contributions by both employers and employees into a common pool

which is then distributed equitably during times of need would help to overcome this.

Long-term unemployment allowances lead to dependency, so a well-designed Unemployment Insurance Scheme should provide assistance for a limited time only, conditional on an active willingness to find a job, accept job placement or participate in re-training programmes. This supports social solidarity and individual inclusion but is primarily a rights-based process aimed at returning the unemployed to self-supporting employment and to release them from dependency on unemployment allowances. Any scheme must make hard decisions to deny unemployment cover for those who avoid or refuse participation.

Social Welfare Assistance

The Malaysian Social Welfare system is not an all-inclusive concept, though such an approach has proved more effective in combating social exclusion and long-term poverty. Currently, the Government only identifies the hard core poor as a pressing problem that has to be addressed. The poor middle class are excluded from systemic support. In a volatile market or crisis situation many individuals can fall into social welfare category but are not eligible for support from current schemes.

Effective Social Welfare Assistance for the active population without previous employment or the long-term unemployed helps them find routes out of poverty and into active and productive lifestyles.

The existing Azam scheme, for example, designed for the poor, should be upgraded to incorporate a self-supporting aim and extended to all categories of people. The overall mission should be to integrate these categories into the working population, especially those who are physically and mentally able to work and hence become self-supporting.

The inactive population includes the aged, the retired without a pension, senior citizens, the disabled who cannot work or those needing continuous healthcare. Existing welfare programmes for senior citizens without pensions, the poor and those without family support should be extended and made universal.

State Health Insurance Scheme

Malaysia has a well-developed universal health service, but free medical care is only partially available. Most government servants and the poor have access to free medical services from government hospitals. However, the majority of Malaysians still seek treatment at government hospitals that provide highly-subsidised general wards. Private medical insurance schemes are

beyond the reach of the poor and even the middle class who all have a right to the best medical care.

An effective Health Insurance Scheme to address these issues would involve contributions made by both employers and employees into a common pool which is then distributed equitably during times of need.

Malaysia has a well-developed universal health service, but free medical care is only partially available

Such an insurance scheme will enable the best treatment for the poor whose membership to the insurance scheme should be paid by social welfare out of taxation. It should cover major medical or surgical interventions and medications and would avoid the need for employees to have to use EPF savings for unplanned medical expenses.

The Government can create order in the market and ensure trust in the social system through a rights-based approach with appropriate legislation.

Social Care Policies

In Malaysia there is no universal system for social care for all categories of people in need, especially those at the end of their lives or in need of constant care and attention. Although people live longer lives now, they are often frail and require medical attention more often. They also suffer from isolation and are in need of opportunities, just as everyone else, to socialise and meet people to share and enjoy good times which enhance their quality of life.

Within the existing social protection system long-term care is all too often placed in the hands of family members, who are mostly untrained to provide such care and more often than not struggle financially when they cannot work due to the need to look after a loved one. Charities and community groups cannot take on this role without support from the state.

To correct these limitations, the social contributions system, perhaps through the EPF should be transformed to ensure that fund participants maintain a sufficient resources to cover long-term care needs as they live longer lives. There should also be reform for disability care allowances for families and carers to make sure sufficient financial resources and professional support are in place to make sure everyone can enjoy a good quality of life whatever their personal circumstances.

Education

- **The Malaysian education system is widely viewed as in need of urgent reform**
- **Institutional change and curriculum revision should be the first priorities**
- **Mass higher education should be balanced with vocational dual-system alternatives**
- **A focus on quality, choice and pace of learning for pupils and parental involvement**
- **Proficiency in Bahasa Malaysia and English**

As a general proposition, a world-class educational system is characterized by top-quality teaching and research that nurtures the human capital required for sustainable socio-economic development. This system creates a workforce that is employable, skilled, creative, inventive, productive, adaptable and flexible.

In countries where economies were industrialized at a rapid pace, such as those in East Asia – Japan, South Korea, Taiwan and Singapore – there was a strong focus on ensuring that a highly competent education system was created to produce well-trained human capital.

Table 8:
PISA International Education Rankings

| Reading | Mathematics | Sciences |
|--------------------------|------------------------------|-----------------------------|
| 1. China* | 1. China* | 1. China* |
| 2. S. Korea | 2. Singapore | 2. Finland |
| 3. Finland | 3. Hong Kong | 3. Hong Kong |
| 4. Hong Kong | 4. S. Korea | 4. Singapore |
| 5. Singapore | 5. Taiwan | 5. Japan |
| 18. UK [†] | 20. Austria [†] | 20. Ireland [†] |
| 19. Germany [†] | 21. Slovak Rep. [†] | 21. Czech Rep. [†] |
| 42. Russia [‡] | 41. Croatia [‡] | 40. Greece [‡] |
| 43. Chile [‡] | 42. Israel [‡] | 41. Malta [‡] |
| 53. Thailand | 52. Thailand | 51. Thailand |
| 55. Malaysia | 57. Malaysia | 52. Malaysia |
| 62. Indonesia | 68. Indonesia | 66. Indonesia |

Source: Malaysia Education Blueprint 2013-25, September 2012;
*Shanghai – China; [†]OECD Average; [‡]International Average

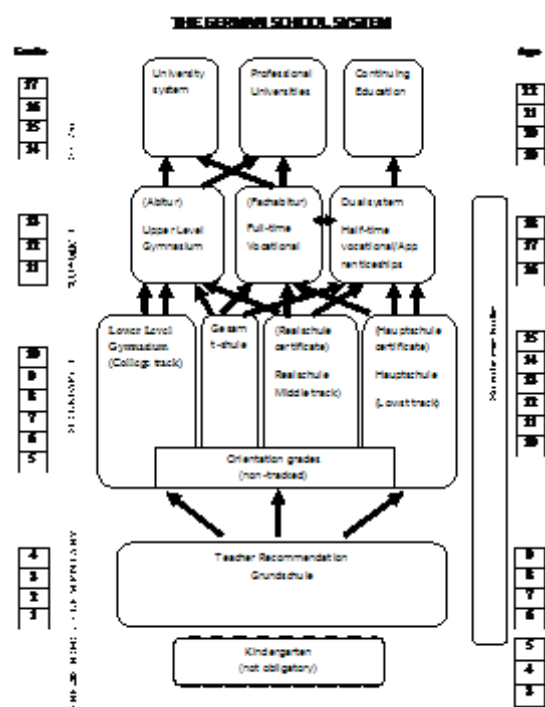
In Malaysia, however, the educational system, from primary to tertiary level, is widely perceived to be in need of urgent reform. The Government itself has acknowledged this need in the Malaysia Education Blueprint 2013-25 launched in September 2012. Critics argue that the key features of the education

system include excessive emphasis on examinations and rote learning, poor development of an enquiring mind, lack of soft skills development, little emphasis on need for second-language acquisition, an under-developed and out-dated curriculum and an assessment and reward system that is compromised by a reluctance to fail under-performing students and institutions.

As a comparison with one well-conceived model of education, take the case of Germany to draw some lessons. Figure 5 shows the structure of the German education system.

Kindergartens, for children aged between 3 and 5 years, literally is a child's garden, or play time. The child does not start to learn to read and write but instead learns to socialize with others. The child is allowed to explore the world to help develop creativity, inventiveness and imagination. Imposing a highly structured curriculum on a child at this stage will have negative consequences in terms of cultivating an enquiring mind.

Figure 5:
German School System



In elementary school, ages 6-9 (i.e. Grade 1-4), students follow a common curriculum of learning to read and write as well as basic math, a foreign language and general knowledge. At the end of elementary school, the teacher in consultation with the parents decide which track/stream (i.e. lower/vocational, middle and upper/academic) the child will follow, based on ability. This system also allows the child to learn at a pace he or she is

comfortable with. At the lower secondary level, students follow a common curriculum of classical language, modern language, mathematics, natural science (physics, chemistry, biology), history, music, art, religious studies/ethics and geography. Those in the lowest track (Hauptschule) have additional vocational courses to prepare them for a dual system at the upper secondary level.

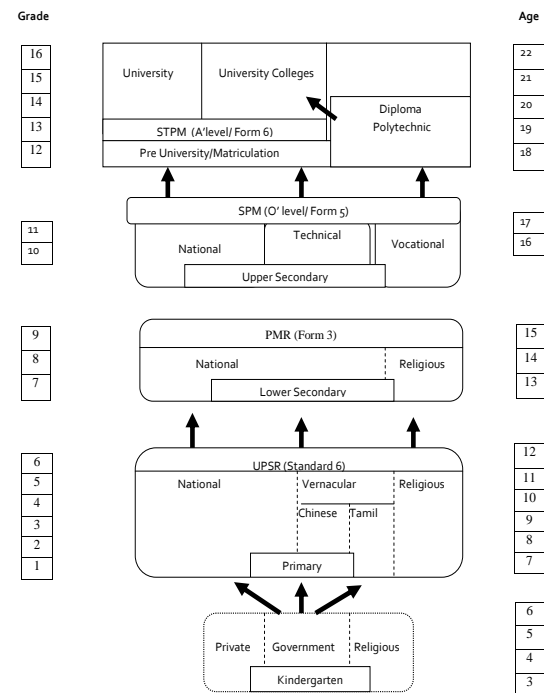
The Dual System is unique in that students spend twice a week in the vocational school while the remaining three days are devoted to an apprenticeship with a company. A key feature of the Dual System is the involvement of the Chamber of Industry and Commerce in structuring the curriculum, together with the trade unions and schools.

There is much flexibility during the transition period, when the student moves to the Upper Secondary level. Here the student can switch between streams or tracks. In this system, a slow learner can bloom and will be well suited to enter into a faster track while a fast learner has the option to switch to different tracks based on his or her interest and choice.

At the tertiary level (Grade 13: 18 years and above), students from the fastest track go to university but they could opt for a professional/technical university which has dual academic and vocational credentials. While those in the middle track normally prefer the professional/technical universities, they may instead opt for the academic universities. Those who finished their dual-system apprenticeship in the lower track can upgrade their specific skills by continuing formal training at a *Fachschule* (upper level career training school).

A quick comparison of the German model and the Malaysian school system provides insights into some crucial differences (see Figure 6). In Malaysia, a fragmented school system, inherited from the British during colonial rule, means that there are diverse pathways to obtaining a basic educational foundation. The school structure does not cater to the individual development of the student, based on the pace at which he or she can cope with the curriculum. Streaming is considered somewhat too late, that is when a child is 16 years old. A student is channelled to either a predominantly science-based or humanities-based stream, with the latter considered for those considered as "weak" students. Those who are channelled to the humanities stream are often stigmatized, while those in the science-stream have little or no exposure to important subjects such as history or literature, hindering their capacity to think creatively.

**Figure 6:
The Malaysian School System**



Reform Areas

If Malaysia is to produce the right type of human capital to deal with the problem of the "Middle Income Trap," the following issues and recommendations should be considered.

Institutional Reform

As for institutional reform, the primary concern is the quality of Malaysia's school teachers and university academics. In highly industrialized countries, particularly in East Asia, there is a stress on ensuring that the quality of staff in schools and universities is extremely high. The same emphasis on the presence of only the highest quality teachers and academics in the education system was not stressed in Malaysia.

A scheme of service should be introduced to attract and retain sound teachers while a similar scheme is required for academics to ensure that the tutelage that undergraduates and post-graduates receive is of the highest quality. This scheme of service for academics and teachers should be structured differently from that created for other civil servants.

Streaming and Curriculum Reform

Curriculum reforms require thoughtful consideration. The Malaysian education structure does not cater for the individual

pace and development of the student. Instead, everybody is thrown into the same basket from the primary level. Streaming in Malaysia is implemented too late and should start at lower secondary level. An earlier streaming mechanism will allow students who have a different pace of learning to absorb the curriculum according to their level of development. This is imperative as students now move up every year even when they fall behind in their understanding of core subjects. These students then fail to obtain a strong foundation in core subjects like Maths, Science and languages such as Bahasa Malaysia and English.

A sound method of assessment should be introduced to gauge the capacity of students to deal with the subjects they study, instead of allowing them to proceed to a higher level each year. Students may fare very well in the humanities, for example, but find it difficult to cope with Maths and Science.

Based on a sound assessment, students will be able to spend more time on subjects they are weak in before being allowed to move on to the next level. While this system may be more expensive to implement at the school level, it should be encouraged if students are to obtain a sound foundation in core subjects.

Students should be exposed to Maths, Science, languages and the Humanities from primary school level and for as long as possible, preferably up to pre-University age. They can then move into academic or vocational training. This would entail a major revamp of the curriculum, one that possibly emulates the International Baccalaureate system, a process that helps promote creative thinking.

Vocational Dual-system Options

In Malaysia, there is a stigma associated with vocational training which pushes students into the academic stream or forces them to drop-out without any effective skills to place them in productive employment.

Consequently, the universities are not getting the right type of students. Entering university has become a "birth right." There is a growing mismatch in the abilities of students and the academic programmes offered by universities. With non-academically-inclined students in universities, this has hampered their proper training, contributing to a shortage of skilled labour. A reluctance to fail students has resulted in falling

standards, reflected in the poor quality of graduates from public universities.

There is a growing mismatch in the abilities of students and the academic programmes offered by universities

The Government's preponderant focus on mass tertiary education at universities, as opposed to an equal emphasis on vocational training, must be reviewed. The stress on ensuring university training is available to many is ostensibly because having a high number of university graduates is imperative if a country is to be seen as highly industrialized. This has created a system in which education has become a commodity rather than an effective mechanism to create a world-class workforce. Meanwhile, the poor emphasis on vocational training has stymied attempts to provide for a well-trained technical work force that a highly industrialized country would need.

There is a need to reform the method of streaming, involving the creation of **dual-system**. Slow learners who are better equipped for the vocational stream should be trained accordingly to enable them to secure vital skills required by industry. In this system, no one is considered weak or is left behind. Every individual has a place in the education system. There is a need for greater partnership between industry (chambers of commerce and trade associations) and public schools when devising an appropriate curriculum for the vocational stream. This will ensure that the curriculum is in accordance to needs of different types of industries. To de-stigmatize the vocational professions, the educational and industrial systems should confer students with professional status through proper certification that will enable them to secure higher wages. In this scenario, greater autonomy has to be given to schools to allow them to create networks with industry. This approach will ensure that the vocational education that students obtain conforms with the rapid changes occurring in the relevant industries.

Quality University Personnel and University Entry

To increase student enrolment in tertiary institutions, the Government has been establishing a number of public universities. This has resulted in a lack of high quality lecturers in many universities because of the great demand for academics. This in turn has contributed to the selection of under- or poorly-qualified candidates as lecturers and doctoral degree students as universities try to expand the academic cohort.

There is a lack of good quality lecturers in many universities because of the great demand for academics

Meanwhile, the Government's focus on university rankings, with almost obsessive stress on research publications, has apparently compromised teaching. A good university must also provide high quality teaching. A balance of quality research publications and quality teaching must be achieved to build the reputation of a university which will inevitably lead to its high ranking as a tertiary institution.

Entering university has become a "birth right." Matriculation has become a bypass route to tertiary education, thus compromising entry standards set for university education, especially in public universities. The commodification of education with the proliferation of private education enterprise has resulted in intense competition for students leading to the lowering of entry requirements in all universities.

There is a need for entry-level screening into university. Entrance exams into university should involve an examination of a student's capacity to comprehend the literature he or she will have to read. This means, in most cases, the student should have a good command of the English language.

More stringent screening of applicants for entry into universities can be done through entrance examinations as well as interviews. Within the university system, higher marking thresholds are necessary with a strict policy of failing students who are ill-equipped or not up to the mark to acquire the necessary expertise.

The Government should allow universities the autonomy to train undergraduates properly. The emphasis should be on the quality of the graduates, not the number of graduates Malaysia produces. Universities should be aiming at smaller intakes if the goal is to provide high quality education. Those who are not academically inclined should be encouraged to obtain vocational tertiary education and technical university education.

English vs Bahasa Malaysia

There is also the persistent and unresolved issue about the use of English language and the problems of striking a balance involving the use of Bahasa Malaysia in the education system as a whole. Since Bahasa Malaysia is the national language, every Malaysian should have proficient command of it. Bahasa Malaysia should constitute a core component of the curriculum. However, English is

used in most areas of study and acquiring proficiency in this subject must be stressed.

Serious efforts to teach subjects such as history and geography at the secondary level in English will enable students to acquire greater proficiency for wider access to knowledge and prepare them for the global market place. Crucially too, there is a serious lack of high quality Bahasa Malaysia academic material in many academic subjects. And, the economy has become highly reliant on an English-speaking workforce. This has led to a situation where Malaysians who are educated abroad find employment relatively easily while local graduates from public universities are often unemployable primarily due to their poor command of this important language.

A New Model of Socially Just Development

- **Malaysia needs a new model of socially just development**
 - **Strong economic foundations, monetary and fiscal stability are essential**
 - **The role of the state must balance the inclusion of employers and employees**
 - **Social protection for all in good times and bad will promote solidarity**
 - **Combining common values, justice and fairness will ensure long-term success**
-

Strong Economic Foundations

The Social Market Economy is a competitive system but one which is also orderly and managed, a so-called Ordo-liberal market system. Its main principles are, among others, subsidiarity and solidarity. The former implies that individual effort must be the basis of the system, but where necessary, the state and society can assist in achieving a socially just outcome. The latter means that all components of the system, employers, employees, individuals and the state, work together to achieve common agreed goals.

The Social Market Economy is one where monetary stability and fiscal responsibility are important features, especially of government policy. In addition, the protection of private property, clear and enforceable liability rules, contractual and commercial freedom, access to open markets and a long-term, reliable and principled economic policy are fundamental.

Monetary and Fiscal Stability

Price stability and solid public finances are essential for successful socio-economic development. In Malaysia these issues are combined because the price controls and subsidies used to make basic items affordable are now putting stress on public finances and account for around 77% of the Government's deficit.

Price stability and solid public finances are essential for successful socio-economic development

An independent monetary policy focusing on maintaining price stability and controlling the cost of living and an independent budgetary oversight board to monitor and guide public finances would provide a credible framework for economic

management which would add confidence in the financial markets and international ratings agencies both at home and abroad.

Respect for Property Rights

Protection of property rights, involving ownership and control of firms, is fundamental and has hindered firms from entrenching operations in the economy. One reason for poor cumulative learning among firms in Malaysia, apart from limited professionalization, is insecure property rights.

Inadequate Government support of entrepreneurial industry constrains the rise of domestic enterprises. Malaysian firms with R&D capacity face potentially greater losses from public policies though they are aware that such investment is crucial to further the process of innovation. Investments in R&D are imperative to create brand products or obtain "first-mover" advantage. However, progressive R&D can only emerge if there is little fear of expropriation.

The Role of the State

The role of the State is clearly fundamental to the socio-economic transformation of Malaysia because of the significant presence of GLCs in all key sectors of economy. This emphasises the need to consider the creation of a tripartite link between the Government, finance and industry.

In Germany, such a system successfully nurtured entrepreneurial domestic firms that had symbiotic ties with public institutions. The 19th Century political economist Friedrich List stressed systematic but temporary protection for infant industries.

Japan had a similar pattern of government-business alliance in late 19th Century. The Government built factories in key industries to promote industrialization to catch up with the West. These factories were then sold to favoured firms such as Mitsui and Mitsubishi. A similar system of patronage was again promoted after World War II to rebuild the economy rapidly.

Malaysia needs to consider creating a new tripartite link between the Government, finance and industry

It is important to note the role of financial sector in industrializing Asia. Industrial and financial institutions were linked, a process that was imperative in driving industrialization. In Japan firms and banks created interlocking ownership ties to implement long-term business strategies. In South Korea public agencies, in charge of economic and industrial policy implementation, and

government-controlled banks provided “policy loans” at favourable rates to create industrial *chaebols*, or large industrial business groups.

The Financial Sector and Industrial Linkages

East Asia’s pattern of industrial growth has not been replicated well in Malaysia even though a large proportion of loans came from Government-owned banks. The Government still has role to play in nurturing new industries which can lead to the emergence of a vast industrial base of firms that have the capacity to compete internationally.

Since banks are now predominantly under control of the Government, this sector can expedite industrialization. The channelling of loans must be based on merit and done in transparent manner.

Malaysia’s stock exchange, *Bursa Malaysia*, has not proven beneficial in promoting the rise of domestic industry. This suggests a need for reform and greater liberalisation of the stock exchange to use it to secure funds for productive forms of enterprise development that can benefit from effective investment strategies.

Creation of Social Compacts to Support and Sustain Innovation

Germany’s Social Market Economy model provides a compelling example of the compact between employers and employees (co-determination) which has driven industrialization and innovation.

Within the co-determination principle business owners and employees have a mutually beneficial advantage by collaborating in decision-making to nurture the entrepreneurial capacity of the firm. If owners offer employees equity stakes in the firm this helps consolidate the co-determination principle.

Successful models such as the Social Market Economy indicate the importance of institutions for employee inclusion

In Scandinavia the social democratic structure helped create a business-labour nexus that encouraged equity and the development of dynamic enterprises.

Successful models such as the Social Market Economy indicate the importance of institutions for employee inclusion such as trade unions, for large firms, and works councils, for SMEs. Such institutions help maintain worker loyalty, promote

inclusion in decision-making and create a sense of co-ownership in firms.

The Developmental State model in Japan supports a compact between the Government, Business and Labour and enabled its quick emergence as the second largest economy in the world while also reducing poverty. Aspects of this social compact involving business and labour are also evident in South Korea where trade unions retain a prominent place in the economy.

They can also be seen in Taiwan where the focus is on the development of SMEs. SMEs across the globe have shown a capacity to be more responsive to market demands. They can be more flexible and better equipped to adopt innovations.

Taiwanese SMEs offer perhaps the best example of high capability to compete globally. Japan ranks alongside Italy as having highest proportion of SMEs among OECD countries. As in many countries, Japanese SMEs employ a majority of the country’s workers. The competitive strength of Italian SMEs in global markets is due in large part to industrial districts that have operated in labour-intensive industries producing consumer products.

Social Protection

The German Social Market Economy also had a second pillar, a social security system based on insurance for pensions, unemployment protection, and healthcare and social welfare assistance system based partly on taxation.

If we are really thinking of how to improve the lives of people, of a more just society and state, we must think of social protection

These systems of social protection are rooted in social solidarity as a means of income protection and reflect the view that although we are individuals first, we are also part of a community but it also helped firms to retain their skilled employees in the economic and financial downturns.

If we are really thinking of how to improve the lives of people, of a more just society and state, we must think of social protection. A developed country is one that takes care of everyone resident in its territory.

Role of family firms

A key feature of large firms and SMEs alike in Europe and Asia is the role of family firms. In Europe 75-90% firms are family enterprises. One in eight firms on London Stock Exchange are family

firms. By the mid-1990s nearly a third of the top-500 US firms were family-owned.

Family firms key in Germany and Taiwan play an important role in nurturing innovation and brand products. This is also seen also in Italy where many family-owned companies are SMEs

The majority of leading listed firms in Malaysia are family-owned and a similar situation prevails among SMEs. A key issue is the extent to which the management of firms has been professionalized, specifically to facilitate investing in R&D. In Germany and Taiwan professionalization of management is a key factor in its industrialization process.

Promoting R&D

To develop new industries, particularly SMEs, policy strategies must focus on supporting R&D and innovation. A three-pronged strategy of investing in manufacturing, management and distribution is needed to acquire competitive advantage. This is particularly evident in firms in Germany and Japan which are both highly innovative countries.

A three-pronged strategy of investing in manufacturing, management and distribution is needed to acquire competitive advantage

An assessment of Malaysian firms suggests that their organizational structure, investment strategies and productive capabilities are conditioned by the context in which they operate. This highlights the need to tackle the issue of property rights effectively.

High Quality Education

Another key issue is investment in education for well-trained labour that contributes to productive R&D and leads to the creation of new technologies. There is an urgent need to review the curriculum across the whole education system, including in the vocational and tertiary sectors.

Malaysia should learn from the German vocational education system ... where public teaching institutions and private firms work together to provide technical training

Education needs institutional and curriculum reforms to promote professionalization, a dual system of work and study, initiatives to raise the quality bar and programmes to promote scholarship

that helps inculcate critical and creative thinking skills.

The Government should consider learning from the German vocational education system on how to implement this dual system, where public teaching institutions and private firms work together to provide technical training. The curriculum for this dual system combines academic and technical education that also provides a route to tertiary education in technical universities and higher technical institutes. This dual system should be constantly reviewed in tandem with changes in the economy. This approach to education takes into consideration students' aptitudes, inclinations, talents, capacities and abilities at their pace and absorption capacity. This will avoid pushing one and all into the academic track when they are not apt for it.

With the Malaysian economy entrenched in the middle income trap, it is imperative that universities actively promote high quality scholarship that also helps foster R&D

Given the contribution of the university to industrial and social development, there has to be a system in place that recognizes and rewards sound scholarship. In developed economies, including in industrialized East Asia, these governments have recognised that if any contribution is to be made by academics to society, entailing the creation of new technologies or input to policy planning, this can only be done if sound research is first undertaken. Cultivating well-schooled graduates, creating new technologies and contributing to policy planning can occur concurrently with high quality research and publications.

With the Malaysian economy entrenched in the middle income trap, it is imperative that universities actively promote high quality scholarship that also helps foster R&D. The evolution of universities in industrialized East Asia indicates that there need not be a compromise on contribution to society if academics focus on research and publish well. Considerable attention to ensuring that their academics research and publish well, while tertiary institutions are led by those who provide sound academic leadership.

Nurture GLCs Productively

Economic growth in post-World War II Europe was driven in large part by the European equivalent of GLCs, particularly in France, Italy, Norway, Finland and Austria.

Leading European firms in the industrial sector have been under Government control and ownership at various stages in their development. In France internationally-recognized firms linked with the Government include those in a range of industrial sector such as Renault in automobiles, Alcatel in telecommunications, Usinor in steel and Thomson in electronics.

In Asia GLC equivalents in South Korea, such as POSCO, have similarly driven industrialization. Taiwan's early industrialization endeavours during the 1950s were led by government-owned enterprises. In spite of active privatization, by 1990 six of Taiwan's top ten companies in terms of assets were GLCs. The leading enterprises in Singapore and China are also GLCs.

Instituting political reforms

Institutional reform is essential to create confidence in the foundations for investment, growth and socio-economic development. For business to flourish and thereby create jobs, income and economic growth the legal and political framework must be stable, predictable and rational. That is it must be easily understandable and must provide a level playing field for everyone who takes part.

The rule of law must be beyond question and there must be no room for arbitrary decisions which favour one group over another or which vary from one person to the next.

A key challenge in Malaysia remains to convince private investors that Government policies do not undermine their corporate goals. Investors have to be assured that policies such as affirmative action or consolidation exercises including in the financial sector will not be used to expropriate wealth.

The rule of law must be beyond question and there must be no room for arbitrary decisions

In Malaysia the NEM, GTP and 10MP mention the need to curb corruption, patronage and rent-seeking. However, none of these Government documents mention institutional reform to devolve power to key institutions to ensure checks and balances.

A common values-based approach

Finally, there is a need for an ethical foundation that guides and gives meaning to socio-economic development. Social capital is increasingly recognised as an important ingredient in a successful development agenda.

Traditions, culture, religion and common sense can be the bases for a universal value system applicable in plural societies, which recognises individual rights and responsibility, social cohesion, self-discipline, fair competition, justice, honesty, moderation, public spirit, respect for the human dignity of others especially in times of need and firm moral standards which uphold the rule of law and intolerance for corruption, abuse of power and discrimination that undermines merit.

All these must be promoted and internalised to ensure that a new model of socially just development can thrive and succeed in the long term

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