

RSOG Seminar : Inclusive Growth – Past & Present And Key Challenges for Malaysia

With

Dr. Muhammad Abdul Khalid

When : 29 October 2013
Where : Razak School of Government
Speakers : Dr. Muhammad Abdul Khalid

About The Seminar

While Malaysia's economic achievements are a matter of record, much remains to be fully understood about the policies in the area of human development. Importantly, the challenge lies in ensuring that the benefit of growth is equally shared by its citizens, especially given the peculiarity of the country's political economy, which attaches an ethnic dimension to development policy.

This seminar will explore the inclusiveness of Malaysia's development agenda, and will critically review Malaysia's policy responses and ensuing development experience over the four decades since the implementation of the New Economic Policy. It will identify the current key issues and challenges in order to arrive at policy recommendations to achieve inclusive growth and human development in Malaysia as the country pursues developed status by the year 2020.

Summary

Tan Sri Dr. Kamal Mat Salih opened the session by providing a background of the seminar and introducing the speaker, Dr. Muhammad Abdul Khalid. He explained that the data that was to be presented was drawn from the first Human Development Indicators Report for Malaysia, prepared for the United Nations Development Program, a project on which they were both engaged as independent consultants.

Dr. Muhammed began his presentation by stressing that the main focus of the study for UNDP was to determine whether people benefited from the nation's growth and whether that growth had been inclusive. The key idea in inclusive growth is the relationship between economic growth, income distribution and poverty. For inclusive growth to prevail there must be strong economic growth, strong income distribution and low poverty. This is a challenge for many countries.

Many believe that the economic growth from 1970 to 2012 had only benefited the rich or higher income groups especially among the Bumiputera. The numbers from the in-depth study revealed that this is not accurate. The policies thus far have worked the way that it was planned to work. The study revealed that the bottom 40% in terms of income, i.e. the poor Malay, Chinese and Indian communities have experienced the highest income growth compared to the rich and the middle class across all races.

In order to achieve inclusive growth a system needs to demonstrate growing income, reduction poverty and reduction in inequality. Policies have to be analysed in relation to these three areas. The speaker pointed out that Malaysia has successfully managed to almost eradicate poverty, having among the lowest poverty rates (at 1.7%) compared to neighboring countries.

Unemployment also saw a reduction from 7.4% in 1970 to 2.9% in 2012. At the same time the economy experienced robust growth.

Inequality has also reduced during this period. Inequality can be identified in two ways, vertical inequality and horizontal inequality. Horizontal Inequality is defined as inequality among culturally defined (or constructed) groups, in contrast to vertical inequality, which is inequality among households or individuals. The country has seen a reduction in horizontal inequality. The inequality between ethnic groups has seen a reduction. In 1970 for every RM1 a Bumiputera earns, a Chinese will earn RM2 but now it has reduced to RM 1.40. The Inequality between urban and rural income levels has also dropped from RM2.2 to RM1.8 earned in urban areas for every RM1 earned in rural areas.

The study also revealed that the notion that past policies have increased the inequality among the Bumiputera is also inaccurate. There has in fact been a 10 % reduction in inequality among the Bumiputera during the period in question. There are, however, increased levels of inequality among the Indians and the Chinese, especially in the former.

Past performance does indicate a relatively healthy economy, however, there are several key issues that need to be addressed.

- Although the poverty is only 1.7 % but when it is broken into groups there is an alarming fact that poverty among the people in Sabah and Sarawak is very high. For

example the Bajau and Dusun ethnic groups in Sabah have poverty rates of 30% and 26% respectively.

- The absolute income gap between the rich and poor has also widened. In 1970, it was RM 700 per month, now it is RM 9000 per month.
- Inequality in absolute amount during this period has been stagnant. This can be read as positive as most other countries have seen an increase in absolute inequality. However inequality in Malaysia is among the highest in the world and given its growth rates, the fact that inequality index has been stagnant is not a good indication.
- Income also remains very low. If a couple earns a combined income of RM10,000 per month they will fall into the top 20%. The bottom 40% of couples earn a combined average of RM1800.
- Breaking down the contributions of wages, investment, savings and transfers identifies income. The income distributions seem very skewed. The bottom 40% sees 97 % of their income from wages, 1 % from wealth effects and 2 % from transfers.
- Asset distribution is also quite skewed. The top 1% owns more in assets than the bottom 40% combined. This means that one person in the top 1% will have more than 40 people in the bottom 40% combined.
- The top 40 richest Malaysians own an equivalent of 22% of the economy. In the US on the other hand, the top 40 richest individuals only control 4% of the economy.
- Looking at house ownership only 40% of Indians, Chinese and Malays own property. It is much harder to own property in Malaysia now than in the year 2000. According to the World Bank, price of a house should not be more than three times

the annual income. Based on this estimate, house ownership is very difficult in Malaysia. Some areas in Malaysia have been identified as severely unaffordable.

- Wages in Malaysia is very low making it difficult to retain good talent and contributes to the brain drain.
- The wage gaps between CEOs and average workers is very high. In 1990, the wage gap was RM272,000 and in 2010 it rose to RM1.7 million per month.
- Women's participation is very low in the workforce despite their high participation in universities (57% of student population). Women only make up 11% of middle management.
- Women also earn less than men in every occupation, even if equal in every other respect.
- Youth unemployment has also seen an increase. The Indian population has seen the highest at 26% followed by 15% Bumiputera and 10% Chinese.
- In labor market, there is discrimination in the both the private and public sectors. While qualification matters, race has proven to matter most in private sector. In the public sector, there is a racial imbalance whereby 90% of the workforce is Bumiputera.
- The area of social mobility has seen mixed results. The study looks at if people are poor due to circumstances they are born into. Based on the study, FELDA settlers saw a higher mobility than Indian Plantation workers.

The outlook in Malaysia is a bit cloudy because policies in Malaysia mainly focus on vertical inequality. Focusing only on the bottom 40% is not sufficient. Horizontal inequality such as gender and ethnic groups must be considered.

The current tax structure is expected to increase inequality in Malaysia. An individual with an earning capacity of RM8000 a month will pay the same tax rate as a millionaire. The current real capital gains tax and estate tax needs to be restructured to make it more inclusive, as it can impend future growth.

The moderator concluded the presentation by reiterating that Malaysia's growth has demonstrated inclusiveness but there are still pressing challenges that need to be addressed proactively.

Questions and Answers

Q1: What is your opinion on the low unemployment rate in Malaysia and its connection to the working poor? (Daniel)

A: It is true that despite the fact people have jobs there is still a percentage that is poor because of low wages.

Q2. What is your opinion on foreign income tax?

A: As long as it is termed as income it should be taxed. Any source of earning should be taxed. This will be a fairer system for all and it will not have a negative impact on growth.

Q3: Why, in your opinion, do some firms tend to recruit people from one particular ethnicity?

A: Ethic based companies and firms tend to recruit people a particular race only and the reason may not be racism but the conclusion is not yet clear. In the private sector, the Chinese seem to be preferred. In the public sector, non-Malay applications have been low. The implementation of an equal opportunity act will help overcome this problem but there is some political influences preventing this from happening.

Q4. How do you balance between the differences between the equality of opportunity and equality of outcome?

A: Equality of opportunity is our focus but it is also flawed. Equality of outcome is needed to balance things, therefore a combination between the two.

Q5: What proportion of the lower income group's income is from transfers and how does this affect the poor?

A: Transfers make up only 2% of income for the bottom 40%. While it does not address the problem of low income, removing these transfers is likely to increase the poverty index.

Q6: What is the reluctance for capital gain tax being implemented?

A: This is a very important institutional issue. There is worry that investment will move to Singapore.

About The Speaker

Dr. Muhammad Abdul Khalid is the the Head of Economics at the Securities Commission Malaysia. He was also National Consultant to the UNDP Human Development Report 2013. He obtained his PhD from the Institute d'études Politiques de Paris (SciencesPo), with a research focus on wealth inequality in Malaysia; and has contributed extensively to research in the areas of economic inequality and socio-economic development in Malaysia.

About The Moderator

Tan Sri Datuk Prof. Dr. Kamal Mat Salih was Dean and Deputy Vice Chancellor (Academic) at University Sains Malaysia (USM). He has extensive experience as consultant and advisor to various government bodies, in his capacity as Executive Director of the Malaysian Institute of Economic Research (MIER) and Rapporteur-General of the National Economic Consultative Council, among others. He founded and remains the Chairman of Yayasan Mahkota (formerly Yayasan Wangsa Maju)

Contact

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