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Economic implications of ASEAN integration for Malaysia's labour market

Rajah Rasiah

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Preface

By 2015, the ASEAN Economic Community (AEC), envisioned as a single common market and production base, will become a reality. This will lead to the freer flow of goods, services, investment capital and skilled labour in the region. Tariff and non-tariff barriers will be reduced, which will have implications for intraregional trade and investment. New opportunities for growth and prosperity are likely to emerge, but the challenge is to ensure that growth is inclusive and prosperity is shared.

Ultimately, the success of ASEAN regional integration will depend on how it affects the labour market and therefore how it improves the quality of life of women and men in the region. To prepare for the impact and find the opportunities to seize, the International Labour Organization initiated with the Asian Development Bank a joint study to examine the impact of the AEC on labour. Findings from the series of studies that were initiated are collected in the 2014 publication *ASEAN Community 2015: Managing integration for better jobs and shared prosperity*. That report highlights the challenges and opportunities that will accompany the AEC, including managing labour migration, boosting productivity and wages and improving job quality. The report offers policy recommendations for creating better jobs and ensuring that the benefits of the AEC are equitably shared among different countries and sectors.

The background papers to the joint publication are available as part of the ILO Asia–Pacific Working Paper Series, which is intended to enhance the body of knowledge, stimulate discussion and encourage knowledge sharing and further research for the promotion of decent work in Asia and the Pacific. This paper by Rajah Rasiah examines the impact of ASEAN economic integration on Malaysia's labour market by looking at the nature of structural change that the country has experienced.

The ILO is devoted to advancing opportunities for women and men to obtain decent and productive work. It aims to promote rights at work, encourage decent employment opportunities, enhance social protection and strengthen dialogue in handling work-related issues. As countries in the Asia and the Pacific region continue to recover from the global economic crisis, the ILO's Decent Work Agenda and the Global Jobs Pact provide critical policy frameworks to strengthen the foundations for a more inclusive and sustainable future.

Yoshiteru Uramoto
Assistant Director General and
Regional Director for Asia and the Pacific

Contents

Tables

Figures

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Abstract

This paper examines the implications of the formation of the Association of Southeast Asian Nations (ASEAN) Economic Community (AEC) in 2015 on Malaysia's labour market. The discussion centres on the nature of the structural change that Malaysia has experienced, especially since the 1980s, and how that has impacted on its labour market. Integration into ASEAN markets has obviously helped Malaysia enjoy the synergies of regional coordination. Although Malaysia's economic growth has been steady, the onset of deindustrialization before a shift to higher value-added activities has impacted somewhat negatively on per capita income growth rates since 2000. Although it is typically part of structural change for manufacturing's share of gross domestic product to rise and fall, evidence reveals that Malaysia is facing premature deindustrialization, with a slowdown in labour productivity. In particular, trade performance since 2000 has impacted somewhat negatively on the labour market. Not only has the trade performance of manufacturing been falling, manufacturing labour productivity has slowed, with key sectors, such as electric–electronics, textiles and transport equipment, showing either negative or low productivity growth since 2000. Foreign low-wage labour has largely helped Malaysia maintain its trade competitiveness in low value-added activities. Despite the introduction of minimum wages in 2012, real wages have grown little in the manufacturing sector, which is the largest employer of low-skilled foreign workers. Weak trade unions have not helped. Although unemployment and inflation have remained low, the preoccupation with low-end activities has restricted per capita income growth.

The paper argues that the Malaysian Government must focus on rejuvenating productivity by emphasizing the infusion of innovation-based activities. The achievement of the high road to industrialization will require the introduction of strong labour market institutions to ensure that real wages grow with minimal inequality. A low level of inequality will help expand domestic consumption, which will reduce the country's dependence on export markets. The paper also argues that the AEC should be used to attract professional and technical labour from ASEAN Member States in areas the Government has targeted for catching up technologically.

About the author

Rajah Rasiah is Professor of Economics and Technology Management at the University of Malaya in Kuala Lumpur.

Acronyms

AEC	ASEAN Economic Community
AFTA	ASEAN Free Trade Area
ASEAN	Association of Southeast Asian Nations
CEPT	Common Effective Preferential Tariff
FDI	foreign direct investment
GDP	gross domestic product
MYR	Malaysia ringgit
R&D	research and development

1. Introduction

Malaysia was a founding member of the Association of Southeast Asian Nations (ASEAN) in 1967. From a focus originally on political stability following fears of a potential domino effect from the spread of communism, ASEAN gradually shifted to become a major regional economic platform. Malaysia became part of the ASEAN Free Trade Area (AFTA) in 1992, which targeted the rationalization of tariffs under the Common Effective Preferential Tariff (CEPT) mechanism. The latest development within this regional platform, the ASEAN Economic Community (AEC), will unfold in 2015. Although the prime focus of the AEC has been on the liberalization of trade and investment, it includes efforts to harmonize a range of institutions to enhance growth and engender the conditions for the evolution of a more egalitarian regional community.

The development of a common labour market *à la* the European Economic Community rather than the United States of America will require streamlining of bureaucratic procedures on professional qualifications and skills certificates, yet it will likely intensify the movement of labour across the region. The implications of this process will be manifold. Malaysia will enjoy the benefit of drawing its labour from a far wider labour market and targeting production directly to a far wider goods and services market. As much as the potential to access professional and skilled labour will expand, it will also come under greater competition from firms in the neighbouring countries. Similarly, professional labour from Malaysia will also find it easier to relocate to Singapore or even in the other countries if the desired opportunities appear in those countries.

The integration is expected to drive growth and structural change in each of the countries, with consequences for distribution. Apart from a focus on infrastructure to strengthen connectivity between the countries, greater security, provision of utilities and coordination of trade and investment, governments will have to strengthen their institutions and regulations governing technical change and intellectual property rights, employment, unionization, wages, skills and professional qualifications. These changes will have to be juxtaposed against Malaysia's national goal of becoming an industrialized country by 2020.

From dependence on the primary sectors of mining (tin) and agriculture (mainly rubber) during its colonial era, Malaysia has enjoyed rapid growth and structural change since 1971, when foreign direct investment began to be a major vehicle propelling manufacturing expansion. However, without strategies to stimulate rapid technological upgrading from low to high value-added activities, the contribution of manufacturing to gross domestic product (GDP) began to decline as of 2000. Instead of pursuing human capital-deepening strategies and putting in place strong research and development support, manufacturing began to lose its competitiveness in the 1990s. The Government's regulatory framework did not help much, especially as large inflows of low wage foreign labour sustained the competitiveness of low value-added industries. Hence, the dynamics of increasing returns associated with industrialization, including stimulating structural change from low to high value-added activities and the consequent differentiation and division of labour, was not fully realized. The lack of technological upgrading has impacted on the type of industrialization that has taken place. Slow growth in value added has denied the country a "high road" to industrialization, with wages growing slowly since the late 1990s.[1]

[1] The high road to industrialization is associated with structural transformation from low to high value added activities alongside enskilling and improvements in wages and working conditions of workers (see Piore and Sabel, 1984).

This view is complicated further by a related argument from political economists concerned with the impact of differentiation and division of labour on the quality of jobs created; in particular, Piore and Sabel (1984), Pyke and Sengenberger (1992) and Zeitlin (1992) focused on the high road to industrialization. In examining the Malaysian experience, this paper draws on that argument to evaluate the proposition that economies gripped by negative deindustrialization are incapable of supporting significant improvements in wages.

For a long time, Malaysia was heralded as a model of a rapidly industrializing country that other countries should imitate (World Bank, 1993). The aggressive promotion of export processing zones since 1972 assisted manufacturing in becoming Malaysia's leading sector contributor to GDP in 1984 and since 1988 (Government of Malaysia, 1991a). Foreign direct investment (FDI) helped make Malaysia a major exporter of light manufactured goods. Electric–electronics, vegetable oils and fats, textiles and clothing are among the main manufactured exports generated by the Malaysian economy since the 1990s. Import-substitution policies targeted at heavy industries from 1981 drove the expansion of steel, transport equipment and cement manufacturing through protection, subsidies and government capitalization (Government of Malaysia, 1986). Transport equipment, in particular, has continued to enjoy strong government support. Nonetheless, the rapid growth recorded from 1988 to 1996 could not be sustained, thus derailing the Government's ambition to shift to industrialized country status by 2020.

Massive inflows of FDI into the manufacturing sector led to serious tightening of the labour market by the mid-1990s (Ariff, 1991; Rasiah, 1995). The focus of the industrial policy shifted towards deepening as the Government attempted to take advantage of low unemployment levels (which reached 2.7 per cent in 1995) to stimulate structural change into high value-added activities. Following the Government's introduction of The Way Forward initiative in 1991, which revolved around the 2020 goal of an industrialized economy, a series of instruments were launched to promote the industrial deepening (Government of Malaysia, 1991b). The Action Plan for Industrial Technology Development of 1990 contributed to the groundwork for the opening of the Human Resources Development Fund, the Malaysian Technology Development Corporation, the Malaysian Industry–Government Group for High Technology, the cluster-based Second Industrial Master Plan, the Multimedia Super Corridor (now the MSC Malaysia) and the Multimedia Development Corporation in the 1990s to support technological deepening (Rasiah, 1999). The Malaysian Institute of Microelectronic Systems was corporatized in the 1990s. Unfortunately, a combination of ethnic-based implementation and appraisal mechanisms reduced the effectiveness of these instruments to stimulate structural change from low to high value-added activities. Hence, firms resorted to importing foreign unskilled labour to sustain their operations, which further aggravated the situation by reducing the pressure to upgrade (Rasiah, 1999; Best and Rasiah, 2003; Henderson and Phillips, 2007). Imports of unskilled foreign labour and the failure to stimulate the upgrading of the country's technological capability weakened the capacity of the manufacturing sector to support improvements in labour productivity and wages.

With that backdrop, this chapter contributes to the debate on deindustrialization by showing that its premature occurrence has restricted both improvements in labour productivity and wages in Malaysia's manufacturing sector.

The remainder of the paper is organized as follows: The next section discusses the theoretical arguments on labour markets, with a special focus on the high road to industrialization. Section three discusses the

structural change that Malaysia has experienced. The fourth section presents analyses on the impact of existing structural change on labour productivity and wages. Section 5 discusses the implications for structural change and labour markets following the formation of the ASEAN Economic Community. The final section wraps the argument with the conclusions and policy implications.

2. Malaysia's integration into ASEAN

As a pioneering member in ASEAN, Malaysia became an integral part of its economic cooperation initiatives. The first major such endeavour was launched under the ASEAN Industrial Projects in 1976 to establish large-scale regional industrial projects to meet the needs of the region and ensure more efficient use of the region's resources. Following the Industrial Projects, the ASEAN Aceh Fertilizer and ASEAN Bintulu Fertilizer plants were established as part of the ASEAN integration projects. Using broad categories, this section looks at the history of the harmonization and integration processes in the region.

2.1 Trade liberalization

Malaysia was a member of the ASEAN Industrial Complementation Scheme that formed in 1981. That scheme led to the introduction of the Brand-to-Brand Complementation Scheme in 1988. Targeting the automotive sector, both schemes were designed to promote industrial complementarity among companies operating in ASEAN. Both schemes encourage automotive brand holders to exploit economies of scale of production through rationalization and specialization of production units by allowing the exchange of approved automotive parts and components for specific automotive brand models. Under these schemes, automotive parts and component producers are granted a 50 per cent margin of preferences on the prevailing most favoured nation rate by firms in participating importing countries and were also accorded local content accreditation.

Malaysia was also a beneficiary of the ASEAN Industrial Joint Venture Scheme, which was introduced in 1983 and revised in 1987. That scheme aimed to encourage greater investment into and within the region, and to increase industrial production through resource pooling and market sharing activities. Products originating from the scheme were granted a 90 per cent margin of preferences on the prevailing most favoured nation rate and local content accreditation was given, where applicable, to firms in the participating importing countries.

Malaysia became an important member of AFTA when it was launched in 1992. Its key mechanism, the CEPT Scheme, targeted tariff liberalization across ASEAN. Malaysia is among the countries that have followed the liberalization process as scheduled.

In 1995, the ASEAN Member States agreed to phase out the Brand-to-Brand Complementation and the Industrial Joint Venture schemes and put in place a new industrial cooperative scheme, taking into account the gradual tariff liberalization that had been taking place since 1992 through the CEPT Scheme under AFTA. The ASEAN Industrial Cooperation Scheme was signed in April 1997 and became operational on 1 November that year. The Scheme aimed to promote joint manufacturing activities of companies operating in ASEAN. Products under the scheme were granted a 0–5 per cent preferential

tariff rate, which was in sync with the CEPT rate, and local content accreditation, where applicable. As a member of the Industrial Cooperation Scheme, Malaysia has participated actively to promote cooperation through its private sector.

2.2 Finance and banking

ASEAN began to promote cooperation in finance with the first ASEAN Finance Ministers Meeting (in March 1997 in Phuket, Thailand). Financial cooperation was deemed necessary to support the regional initiatives and schemes expounded by the ASEAN leaders, which included, *inter alia*, AFTA, the Industrial Cooperation Scheme and the ASEAN Investment Area.

Malaysia was one of the signatories to the Ministerial Understanding on Finance Cooperation and the ASEAN Agreement on Customs. The former lays down the foundation for strengthening cooperation in finance. In particular, the ministerial understanding provides a framework for enhancing cooperation in several areas of finance, which include banking, financial and capital markets development, customs matters, insurance matters, taxation and public finance matters, monetary policy cooperation and human resource development in the area of finance.

The Customs Agreement was signed to strengthen ASEAN cooperation to speed up the implementation of AFTA with respect to greater intraregional trade and investment flow. This agreement was also targeted at supporting joint efforts to check smuggling, coordinate better customs control activities, promote mutual technical assistance, modernize customs systems and upgrade customs skills.

Malaysia became a member of the ASEAN Senior Finance Officials Meeting, which was started to assist the ASEAN finance ministers in streamlining financial flows in the region. This body has strongly encouraged insurance regulators, capital markets and tax and central bank authorities to establish a forum for initiating activities and strengthening cooperation in the financial sector.

2.3 Investment coordination

Since the Fifth ASEAN Summit (in Bangkok) in 1995, ASEAN Member States have worked towards investment coordination in the region, which contributed to the establishment of the ASEAN Investment Area. The ASEAN Investment Area seeks to help the region attract greater and sustainable levels of FDI flows through collective measures that enhance the attractiveness, competitiveness and complementarity of the region. As a consequence, several investment bodies have been organized at the ASEAN level. The ASEAN Heads of Investment Agencies, assisted by the Senior Officials Meeting on Trade and Investment, began to discuss, initiate and implement regional investment cooperation matters. A number of milestones have since been achieved in the coordination of FDI.

2.4 Coordination of primary sectors

Various measures have been implemented to promote the production and trade in agriculture and forestry products and minerals, given that these sectors are still significant to many ASEAN economies. ASEAN Cooperation in Food, Agriculture and Forestry provides a framework for sector cooperation in those areas. A Memorandum of Understanding on ASEAN Cooperation and Joint Approaches on Agriculture and Forest Products Promotion Scheme was designed to improve the competitiveness of the region's agriculture and forest products.

The Programme of Action for ASEAN Cooperation in Minerals was approved by the Fifth ASEAN Summit to promote trade and investment in industrial minerals. Member States have pursued initiatives to exchange information on policy, regulations and legislation to attract investment. To further strengthen ASEAN cooperation in the sector, member countries agreed to establish an ASEAN Industrial Minerals Information System and a Directory of Research and Development and Training Centres available in the region.

2.5 Transportation and communications

Following the AEC initiative, ASEAN Member States have embarked on increasing connectivity within the region. Plans are underway to connect the countries with better highways and railway lines and to expand broadband coverage. Malaysia has achieved excellent expansion in these aspects, but its logistics coordination and ownership remain considerably below that of Singapore. ASEAN member countries are implementing the ASEAN Plan of Action in Transport and Communications through the Integrated Implementation Programme, involving 45 projects and activities in the following cooperation areas: multimodal transport, interconnectivity in telecommunications, harmonization of road transport laws, rules and regulations, airspace management, maritime safety and pollution, human resources and air services liberalization. The Singapore–Kunming (China) Rail Link Project and the development of the ASEAN Framework Agreement on the Facilitation of Goods in Transit are expected to raise land connectivity between the countries to a higher level.

2.6 Services

ASEAN member countries have agreed to enhance cooperation by liberalizing trade in services. The ASEAN Framework Agreement on Services was signed in 1995 in Bangkok during the Fifth Summit when it was agreed that a process of negotiations would commence on 1 January 1996 and end on 31 December 1998 (ASEAN, 2014). The negotiations produced commitments on increased market access and national treatment from member countries in the seven priority service sectors of air transport, business services, construction, financial services, maritime transport, telecommunications and tourism. A Coordinating Committee on Services was established with seven working groups. Member countries have exchanged information on their General Agreement on Trade in Services commitments and service regimes. Malaysia's private sector has taken advantage of these developments to expand the range of service activities across borders, such as banking in Cambodia and Indonesia, and IT services in the Lao People's Democratic Republic.

2.7 Intellectual property rights

Following enactment of the World Trade Organization's Trade in Intellectual Property Rights in 1995, intellectual property rights became a major instrument of technological governance. For ASEAN member countries, including Malaysia, to catch up economically depends heavily on both inflows of technology from abroad as well as domestic development. Malaysia recognizes its shortcomings in this area as the prime cause of its entrenched positioning among middle-income countries. It is important that Malaysia upgrade its technological competitiveness to sustain its high economic growth. There is an urgent need for ASEAN to strengthen its intellectual property legislation, administration and enforcement.

Greater cooperation among ASEAN member countries regarding intellectual property will increase the potential for the region to innovate as well as achieve egalitarian development (Rasiah, 2013). ASEAN Member States signed the ASEAN Framework Agreement on Intellectual Property Cooperation during the Fifth ASEAN Summit in 1995 (ASEAN, 2014). Among the activities included in the Programme of Action 1996–98 were measures to enhance and strengthen intellectual property enforcement, protection, administration, legislation and inculcation of public awareness. The ASEAN secretariat has increased its efforts to synchronize and stimulate strengthening of the IPR framework among member countries but especially the transition economies (ASEAN, 2014).

2.8 Private sector programmes

Malaysia's strong promotion of the private sector follows the coordination efforts within ASEAN, which has attracted a number of economic cooperation programmes. Considered the engine of growth, the private sector is strongly urged to participate actively in the economic cooperation process. Various channels have been established for regular consultations between senior economic officials and representatives of Chambers of Commerce and Industry. A consultation with high-ranking private sector representatives and the ASEAN economic minsters takes place annually. To ensure the effective functioning of the ASEAN Chambers of Commerce and Industry, a permanent secretariat is to be established. The ASEAN Secretary-General agreed to the secretariat's housing within the ASEAN Secretariat in Jakarta. The establishment of the secretariat will help foster even greater communications and links between the policy-making bodies and the private sector.

Although FDI inflows and trade have slowed since 1992, at least in comparison with activity during the 1970s (Asirvatham, 2014), there is evidence to suggest that the ASEAN integration processes have been instrumental in reducing the impact of China's integration into the global economy, especially since the 1980s, when FDI inflows into and exports from China grew the fastest in the world (UNCTAD, 2012). Although a number of the channels for cooperation and integration proposed under the AEC have taken root in ASEAN, both bilaterally and multilaterally, the AEC promises to generate a more official and broader framework of integration for capital and labour mobility and coordination in the region.

3. Theoretical considerations

While the integration into global markets has been the major driver of rapid growth in a number of ASEAN countries, workers in many of them have not enjoyed significant improvement in their material conditions (Limqueco, Mcfarlane and Odnoff, 1989; Rasiah, 2012). The share of income enjoyed by firm owners and labour has varied between countries so much that the low-income groups in the rich countries of the United States and the United Kingdom cannot afford some of their basic needs, such as proper heating, compared with the lowest quintile of income groups in the Scandinavian countries of Denmark, Finland, Norway and Sweden (Lim and Lim, 2010). Nonetheless, people who are poor in the industrialized countries are still exposed to far more opportunities than people who are poor in the poor economies of Bangladesh, Bhutan, Cambodia, the Lao People's Democratic Republic, Myanmar, Timor-Leste, Uzbekistan and Tajikistan.

More advanced electoral politics have reduced the potential for expansion of the "lumpen bourgeoisie"[2] in the industrialized economies of the United States and the United Kingdom. Several neo-colonial States, however, have been characterized by a dominant lumpen bourgeoisie that have done little to check the persistence of poverty and stagnation in real wages with substantial sections of the masses living in squalor (see also Freire, 1970). In addition, repressive political regimes have undermined the emergence of responsible unions to address the plight of workers in many countries. In fact, the political leadership in some countries has deliberately formulated policies to exclude trade unions from shaping development policies targeted at suppressing labour to stimulate foreign direct investment (see Jomo and Todd, 1993).

Unfortunately, the dominant neoclassical arguments have focused on growth as one that will automatically push wages up as surplus labour evaporates in free market conditions so that it will bring about equitable distribution of value added. The neoclassical argument of the free labour market is predicated on the assumptions that markets will always clear and that economic agents will enjoy symmetric relationships with the same urge to seek information and capacity to process and act and are rational and, hence, will not make the same mistakes twice (Lucas, 1978). Friedman (1968) called for the market to be freed from interventions so it could carry out its role in coordinating the supply and demand that establishes equilibrium in the labour market at the natural rate of unemployment; interventions to create more jobs, he said, will only accelerate inflation. Even though the "kinked" Phillips curve was Keynes' invention,[3] it was appropriated by some neoclassical economists who became concerned with stagflation[4] in the early 1970s (Rasiah, Yap and Santha, 2014).

Bhagwati (1975) reasoned that relaxing the Heckscher-Ohlin assumption of perfect capital immobility but keeping the immobility of labour perfect would then generate the following consequences: Rising inflows of FDI into the least developed countries would lower interest rates ([r], in Figure 1) as the supply of capital in relation to demand rises while wages [w] rise as the demand for workers rises in relation to the demand. Per capita incomes [Y] would eventually equalize across countries. Free exchange rates would

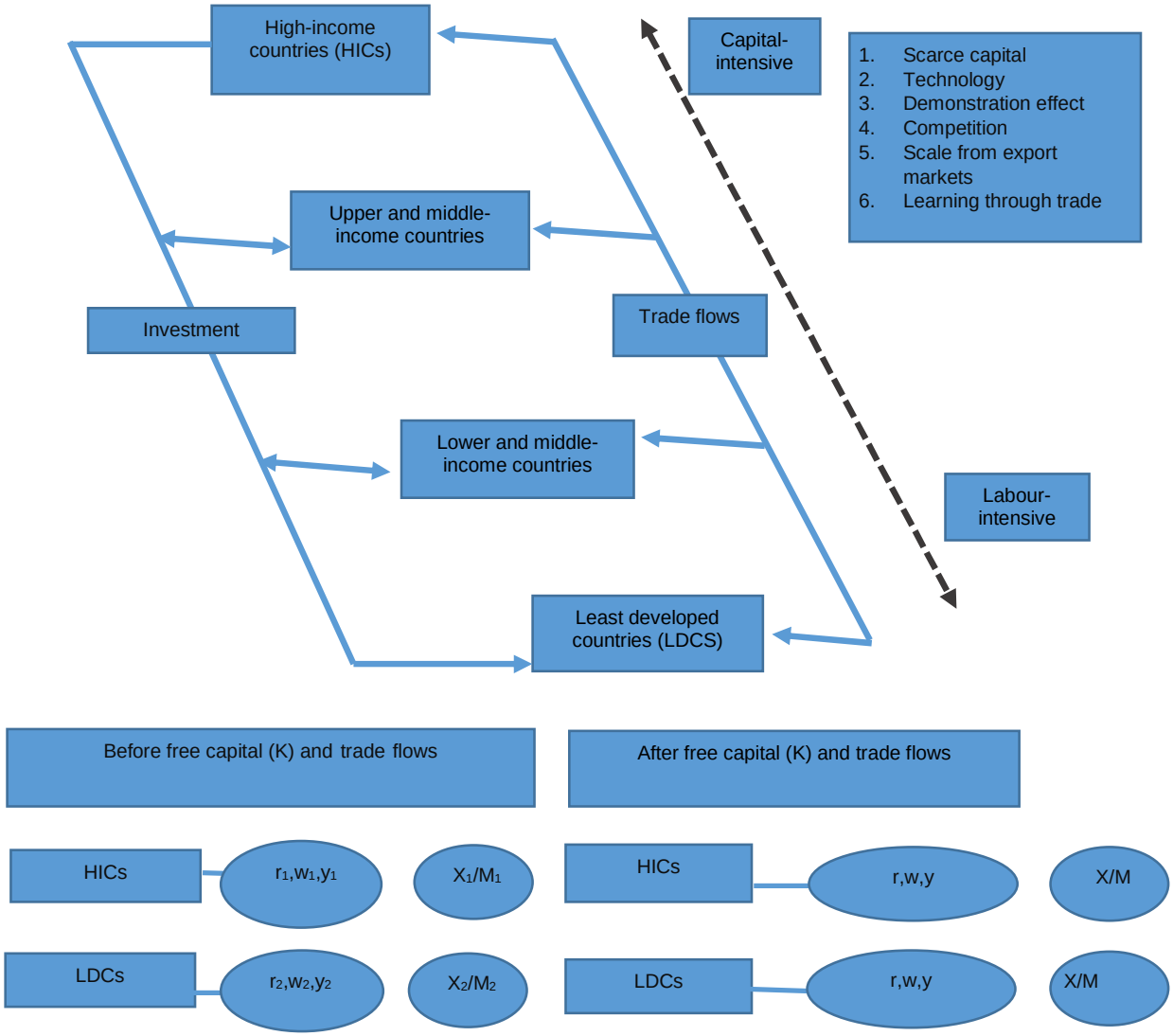
[2] Fanon (1963) used the term "lumpen bourgeoisie" to refer to the pseudo-bourgeoisie who lived the luxurious lives of the bourgeoisie but drew their material wealth as parasites on society.

[3] The kinked part of the Phillips curve starts from the point when inflation starts to accelerate, with small falls in unemployment, which is also known as the non-accelerating inflation rate of unemployment. Although the logic of Friedman's (1968) Phillips curve comes from this understanding, he instead referred to this point in the x-axis as the natural rate of unemployment.

[4] "Stagflation" refers to a situation in which economies experience stagnation and high inflation simultaneously, which is atypical of the inverse relationship between the two posited by the Phillips curve.

keep the balance of payments close to zero in the long run as deficits (when imports [M] exceed exports [X]) and surpluses (when exports [X] exceed imports [M]) would clear with demand adjustments domestically and abroad (see also Fleming, 1962; Mundle, 1963). Hence, inflows of capital from abroad in the absence of impediments to capital inflows and trade would reduce unemployment and at the same time raise wages. In fact, Krueger (1981) and Belassa (1982) presented the successful economic development of the Republic of Korea and Taiwan (China) as having been achieved through liberalization. This same logic has prevailed in several accounts of liberalization in ASEAN that positioned Singapore as a high-income country, with Indonesia, Malaysia, the Philippines and Thailand as the next-tier countries and the transition economies at the bottom.

Figure 1: Neoclassical thetis of economic convergence



Source: Author.

However, not only do perfect market conditions not exist, they discourage innovation (Schumpeter, 1961), leaving the arguments of Heckscher and Ohlin (1991) – that under conditions of perfect capital and labour mobility within borders and their immobility across borders, specialization on the basis of factor endowments will generate the best economic outcomes – confined to a classroom academic exercise. Keynes (1936) accepted the problems of information asymmetry and market imperfections and called for government intervention to generate full employment. But Keynesian arguments do not broach effectively the specific strategies essential to stimulate improvements for labour. Instead, any effort to examine the implications of growth for labour would require a full understanding of institutions – both in the participation of labour in the process as well as the instruments in place to ensure that there is effective distribution of value created between the owners and workers of the means of production. The successful industrialization experience that was achieved alongside significant improvements in the material conditions of labour in the Republic of Korea and Taiwan (China) were driven on the back of strong state intervention – a point that the World Bank (1993) finally conceded.

Complementing this argument is the related argument taken up by political economists concerned with the impact of differentiation and division of labour on the quality of jobs created. Piore and Sabel (1984), Pyke and Sengenberger (1992), Zeitlin (1992) and Wilkinson and You (1995) focused on the high road to industrialization. Kochan and Osterman (1994) discussed the importance of mutual gains enterprises in which hierarchies are minimized, with workers participating extensively in decision-making. In such enterprises, labour, management and government work together for mutual gains. Whereas the buzzword these days is on "inclusive development", flexible specialization exponents have long discussed the active participation of all in the knowledge flows and interaction between skilled workers through a systemic structure that addresses collective action problems in a blend of competition and cooperation that ultimately forms the basis of the high road to industrialization.

Unlike traditional notions of trade unionism, such as the British archetype that is gripped by heavy antagonistic relations between labour and capital (but was also important in championing workers' interests until Margaret Thatcher began dismantling the powers of trade unions in 1979), the evolution of electoral politics has driven a number of governments, including Denmark, Finland, Germany, Norway and Sweden, to assume a major responsibility for protecting the welfare of workers (Edwards and Elger, 1999). A similar framework, but with a unique form of co-optation, is the National Trade Union Congress that works with the ruling People's Action Party to protect mutual interests in Singapore (Wong, 1998). Kuruvilla (1995 and 1996) provided evidence from India, Malaysia, the Philippines and Singapore to argue that import-substitution industrialization was associated with industrial relations and human resource strategies that were plural and stable, whereas countries that moved from low to higher value-added through an export-oriented industrialization strategy experienced a shift from low-cost to workforce flexibility and skills development. Countries that failed to upgrade, such as the Philippines, have continued to experience casualization of labour and slow skills development (Ofreneo, 2008).

The environment confronting labour has varied among countries. Unlike the past when capital–labour relations were so antagonistic that militancy and collective bargaining deadlocks often culminated in strikes, layoffs and the persistence of low wages, changes in the labour process necessitated by rapid advances in technology and modern capitalist relations has transformed labour in a number of processes as a "value creator". The Taylorist production organization separated conception and execution from the labour process so that management performed the former and workers the latter (Braverman, 1974). These processes gave rise to the creation of specialized high-wage skilled workers with mass production

that the American automobile maker, Ford advanced (Best, 2001). Where large reserves of surplus labour or the industrial reserve army still exists, such as with low value-added clothing and cement manufacturing activities in such countries as Bangladesh, India and Myanmar, Taylorist practices still dominate. Although both Taylorist and Fordist labour processes still exist, modern industrial capitalism – as in the assembly of automotive and electronics products – has evolved to recognize that workers have the ability to create knowledge and thus add value to the labour process. This has led to the evolution of flexible production systems. This is the notion of relative surplus value that Marx (1957) and Luxembourg (2003) glorified as the supreme anchor driving accumulation in industrial capitalism (see also Brenner, 1977).

In market economies, such as Indonesia, Malaysia, the Philippines and Thailand, trade unions have largely acted as an independent representative of workers in their relations with the State. On one hand, States have tried to garner support from unions by enacting welfare instruments that govern employment relations and industrial relations. On the other hand, governments have offered generous incentives to woo investment that has included the imposition of restrictions on trade unions, the banning of strikes and the enactment of minimum wage legislation in certain industries. In some countries, trade unions are integral components of States – such as China, the Lao People's Democratic Republic and Viet Nam.

Fortunately, Malaysia's stance on trade unions may be changing, following the introduction of the minimum wage in 2012 and the pressure imposed by some industrialized countries to formalize efforts to form a national union in the electronics industry. Also, following the recognition that the manufacturing sector has stagnated without reaching a high value-added stage since 2000, government efforts to stimulate industrial deepening may offer an opportunity for the resumed pursuit of the high road to industrialization.

4. Structural change: Industrialization and deindustrialization

Despite Malaysia's considerable structural change, the country remains trapped in the group of upper-middle-income countries. Additionally, the contribution of manufacturing to GDP has been contracting since 2000. The primary pillars of Malaysia's manufacturing growth – the light export-oriented electric–electronics and textile–garment industries – faced a slowdown from 2000 to 2010. As well, the import-substituting automobile industry that was promoted through heavy protection as of 1981 has begun contracting. Real per capita income grew by an average of 5.9 per cent per annum between 1987 and 1996 – before the Asian financial crisis struck in 1997, but then it only grew an average of 2.8 per cent per annum between 2000 and 2012.[5]

Manufacturing enjoyed double-digit annual average growth since 1971 to overtake agriculture to become the leading propeller of Malaysia's GDP among the primary and secondary sectors in 1988 (Rasiah, 1995). The swiftest growth in manufacturing was achieved from 1971 to 1994. Then, average annual manufacturing growth fell, from 11.7 per cent in 1990–94 to 5.9 per cent in 1995–99 and further to 4.8 per cent in 2000–04 and 2.6 per cent in 2005–10 (Table 1).

[5] Computed from World Bank, 2013.

In contrast, the services sector recorded the largest expansion of its share of GDP, from 31.6 per cent in 1990 to 48.5 per cent in 2010 (Table 2). Because the intersector dynamics of structural change has not evolved sufficiently and with manufacturing value-added growth slowing since 2000 (before a structural shift to high value-added activities), the expansion in services (such as trade, transport and communication, finance and public administration) is unlikely to produce the complementary impact of driving GDP growth. Apart from investment forays into infrastructure, telecommunications and banking services development abroad, services has yet to become a major foreign exchange earner.

Table 1. Sector GDP growth, Malaysia, 1990–2010

Sectors	1990–94	1995–99	2000–04	2005–10
Agriculture	0.4	0.7	3.3	2.7
Mining	2.7	3.0	3.2	-1.7
Manufacturing	11.7	5.9	4.5	2.6
Electricity, gas & water	14.9	4.8	5.4	4.3
Construction	13.0	-1.7	1.6	4.9
Trade	12.8	3.8	4.2	8.4
Transport & communication	11.4	5.7	5.6	6.2
Finance [a]	16.0	9.6	5.9	8.2
Public administration	5.7	4.5	5.8	6.6
			4.1	2.3
Others [b]	10.6	4.9		
GDP	9.4	3.8	4.6	4.4

Note: a = refers to finance, insurance, real estate and business services; b = refers to community, social and personal services, producers of private non-profit services and domestic services of households, including owner-occupied dwellings.
Source: ADB, 2011.

Similarly, the contribution of manufacturing, which had risen from 24.2 per cent in 1990 to 30.9 per cent in 2000, fell to 24.6 per cent in 2010 (Table 2). The evidence shows a declining trend in the relative contribution of manufacturing to Malaysia's GDP growth since 2000. In addition, a shift is apparent in the share of agriculture, which fell in significance from the 1970s until 2005 (Osman, Pazim and Rasiah, 2011), when it began to rise again, going from 8.4 per cent in 2005 to 10.4 per cent in 2010.

Table 2. Structure of GDP, Malaysia, 1970–2010 (%)

Sectors	1970	1975	1980	1985	1990	1995	2000	2005	2010
Agriculture	29.0	27.7	22.9	20.8	15.2	12.9	8.6	8.4	10.4
Mining	13.7	4.6	10.1	10.5	11.8	6.2	10.6	14.4	10.9
Manufacturing	13.9	16.4	19.6	19.7	24.2	26.4	30.9	29.6	24.6
Construction	3.5	3.8	4.6	4.8	3.5	4.5	3.4	2.7	3.3
Utilities	0.3	2.5	2.7	0.7	2.8	3.1	2.5	2.4	2.3
Services	39.6	45.0	40.1	43.5	42.5	46.9	44.0	42.5	48.5
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Government of Malaysia, 1971, 1986, 1991, 2001, 2011.

From its 60 per cent contribution in 1957 (Osman, Pazim and Rasiah, 2011), agriculture remained the main employment generator in Malaysia until around 1990, when services took over as the lead job creator (Table 3). Manufacturing surpassed agriculture around 1995 to become the next leading employment creator in Malaysia. The infusion of foreign unskilled labour into manufacturing helped raise the share of employment in manufacturing, which rose significantly to 28.7 per cent in 2005 before falling slightly to 28.3 per cent in 2010.

Table 3. Sector employment structure, Malaysia, 1970–2010 (%)

Sector	1970	1975	1980	1985	1990	1995	2000	2005	2010
Agriculture	53.5	49.3	39.7	35.7	26.0	19.0	16.0	12.9	11.6
Mining & quarrying	2.6	2.2	1.7	1.1	0.6	0.5	0.5	0.4	0.3
Manufacturing	8.7	10.1	15.7	15.1	19.9	25.7	27.1	28.7	28.3
Construction	2.7	2.9	5.6	6.9	6.3	8.9	9.2	7.0	6.4
Services*	20.5	22.5	23.6	26.2	34.5	35.1	37.2	51.0	53.3
Total employment ('000s)	**3 340**	**3 928**	**4 817**	**5 625**	**6 686**	**8 024**	**8 547**	**10 895**	**11 956**

Note: * = includes gas, water and electricity.
Source: Calculated from Government of Malaysia, 1971, 1986, 1991, 1996, 2001, 2006, 2011; Osman, Pazim and Rasiah, 2011.

Rapid intersector structural change also took place with exports. Agriculture accounted for 57 per cent of Malaysian exports in 1970, but its share in total exports fell dramatically, reaching its trough of 3.7 per cent in 2000 before rising again to 10.8 per cent in 2010 (Table 4). Manufactured exports enjoyed the biggest expansion, rising from 11.1 per cent of total exports in 1970 to the peak of 90.1 per cent in 2000 before falling to 76.2 per cent in 2010. The relative slowdown in manufacturing has allowed the agriculture and mining sectors together to increase their share in total exports, from 9.8 per cent in 2000 to 22.3 per cent in 2010.

Table 4. Sector export structure, Malaysia, 1970–2010 (%)

Sector	1970	1975	1980	1985	1990	1995	2000	2005	2010
Agriculture	57.0	49.8	39.9	30.2	19.1	9.3	3.7	7.1	10.8
Mining	21.4	18.6	30.0	29.6	15.9	5.0	6.1	9.3	11.5
Manufacturing	11.1	20.9	21.8	32.7	58.8	84.2	90.1	81.6	76.2
Others*	10.5	10.6	8.3	7.4	6.2	1.4	0.1	2.0	1.6
Total (MYR billion)	**5.6**	**10.2**	**30.7**	**42.5**	**88.7**	**204.0**	**427.0**	**552.1**	**638.5**

Note: * = Includes unclassified agricultural, mining and manufactured goods and services. MYR = Malaysian ringgit.
Source: Calculated from Government of Malaysia, 1971, 1986, 1996, 2011.

Although manufacturing became the largest real sector since 1988, its share in GDP began to fall after 2000. Table 5 shows average annual growth in value added experienced by the manufacturing industries in Malaysia. Foreign capital became the prime driver of manufactured exports as large waves of foreign capital relocated textile, garment and electric–electronics assembly and processing plants to Malaysia in the 1970s; subsequently, from the second half of the 1980s and following massive inflows from Japan, the newly industrialized Asian economies helped to expand export manufacturing further.

Table 5. Manufacturing value added growth, Malaysia, 1979–2010 (%)

Sector	1979–1985	1985–1990	1990–95	1995–2000	2000–05	2005–10
Food	5.5	6.6	12.2	10.7	3.0	11.0
Beverages	0.3	2.4	-3.0	5.5	20.0	
Tobacco			15.2	-13.7	4.4	16.7
Textiles & garments	4.7	12.8	17.1	6.8	-11.5	-1.3
Footwear (except rubber)	NA	NA	10.2	7.3	-2.7	14.3
Wood	-4.5	13.1	16.4	3.8	-0.3	1.0
Furniture & fixtures	NA	NA	35.8	19.3	2.6	-1.7
Printing, publishing & allied industries	NA	NA	17.9	5.1	4.5	2.1
Paper	NA	NA	20.3	15.0	-3.3	7.0
Leather	NA	NA	29.4	-2.4	2.9	4.4
Rubber	4.2	25.0	13.6	7.6	-1.6	4.6
Chemical	2.8	7.9	12.5	12.0	12.3	-27.3
Petroleum & coal	NA	NA	25.3	37.4	11.1	11.2
Non-metallic mineral	3.6	7.4	16.7	4.4	1.3	8.4
Basic metal	9.8	5.0	8.7	10.2	4.4	13.6
Fabricated metal			23.9	9.9	1.7	7.6
Machinery	9.0	6.6	26.0	25.3	-16.5	2.7
Electrical machinery	8.0	16.4	26.8	12.1	0.5	1.3
Transport equipment	9.0	15.0	17.6	6.5	4.6	10.6

Source: Computed from Government of Malaysia, 1986, 1991, 1996, 2001, 2006, 2011.

Foreign direct investment had an important role in the transformation of manufacturing from import-substitution to export-oriented industrialization. Foreign capital dominated the origin of manufacturing in Malaysia as British firms in particular relocated from the 1950s to supply final consumption goods (Jomo, 1986; Rasiah, 1995). The Pioneer Industries Ordinance of 1958 stimulated further inflows of import-substitution manufacturing foreign capital into light consumer goods manufacturing. Although there is no available data on ownership in the earlier years, most industries enjoyed more than half of foreign equity in 1968 (Table 6). From 61 per cent ownership of manufacturing equity in 1968, the foreign share fell in trend terms to 31 per cent in 2010. Nevertheless, foreign ownership has remained dominant in the light industries of electric–electronics and textiles. Instead of spearheading structural transformation from low to high value-added activities, the lack of human capital and institutional support for upgrading has left the foreign-dominated industry of electric–electronics to rely on imported low-wage foreign labour.

Although manufacturing expansion began in the 1970s, government efforts to stimulate industrial widening and deepening only began with the introduction of the Industrial Master Plan in 1986 (Government of Malaysia, 1986), which was followed by the Second Industrial Master Plan in 1996. The first Master Plan targeted incentives to attract foreign capital and to stimulate training and the second plan continued it with the addition of incentives and grants for clustering and R&D activities (Government of Malaysia, 1996). However, serious shortages in human capital and the failure of the meso organizations created as of 1991 to stimulate knowledge-based activities (such as designing and R&D) restricted the capacity of the second Master Plan to stimulate industrial deepening (Rasiah, 1999).

Table 6. Foreign equity ownership, manufacturing, Malaysia, 1968–2010 (%)

	1968*	1975*	1980	1985	1990	1993	1998	2000	2005	2010
Food & beverage	74	55	32	25	30	33	27	18	17	20
Tobacco	93	79	76	67	62	58	69	38	53	45
Textiles	52	63	54	48	61	64	76	73	67	63
Wearing apparel & fur								27	22	15
Leather	17	48	48	54	59	57	61	34	28	27
Wood	15	8	13	9	19	36	27	18	19	18
Paper	NA	16	10	20	14	13	10	9	12	24
Printing & publishing								6	6	15
Petroleum & coal	78	79	78	37	44	50	34	35	19	17
Chemical	53	63	53	16	24	25	46	40	36	19
Rubber & plastics	14	42	46	42	55	51	50	28	36	24
Non-metallic mineral	57	52	19	32	33	39	34	22	22	48
Basic metals	49	42	35	32	17	33	30	13	12	21
Fabricated metals	66	59	26	23	30	56	36	38	29	23
Machinery & equipment	74	51	42	35	53	65	66	58	50	43
Office, accounting & computing machines								84	83	
Radio, telephone & communication equipment	70	84	80	73	89	91	83	71	52	67
Medical equipment, watches & clocks								78	82	
Electrical machinery & apparatus								48	52	39
Motor vehicles, trailers & semi-trailers								8	9	16
Other transport equipment	NA	51	32	15	25	35	29	11	11	11
Others	60	69	57	53	69	81	56	25	20	10
Manufacturing	61	52	39	33	42	50	47	38	32	31

Note: * = refers to peninsular Malaysia figures; the merged cells show that ownership classifications by industry in those years were broader; NA = not available.
Source: Computed from Government of Malaysia, 1971–2011a.

The failure of the meso organizations to stimulate the production of human capital and knowledge stocks to spur upgrading led to a slowdown in manufacturing growth as of 2000. The Government introduced the Third Industrial Master Plan in 2006 in an attempt to continue the focus on clustering, with the addition of support for services. But the third Master Plan neither enjoyed the positive elements of clustering contained in the second Master Plan nor addressed the latter's weakness of not comprehending complementing activities effectively (Rasiah, 2011). Manufacturing value added only grew by 2.6 per cent annually on average from 2005 to 2010. The fastest-growing industries in that period were beverages and footwear, and the resource-based industries of petroleum, coal and basic metals (Table 5). The textile and garment industries experienced a contraction from 2000 to 2010, recording an annual average change rate of -11.5 per cent in 2000–05 and -1.3 per cent in 2005–10. The electric–electronics industry, which is Malaysia's largest manufacturing industry, recorded an annual average growth rate of 0.5 per cent in 2000–05 and 1.3 per cent in 2005–10. Although the contraction of the textiles industry appears as an unavoidable result of the termination of the Multi-Fiber Agreement and rising competition from China, India, Viet Nam and the least developed countries,[6] the contraction and slowdown in other manufacturing industries is a consequence of slow upgrading.

The discussion on premature deindustrialization is not complete without analysis of the trade balance by the major manufacturing industries. The trade balance index denotes the relative significance of exports against imports; estimations are shown in Table 7. The trade balance index varies between -1 and 1, with negative balances denoting that imports exceed exports. As displayed, wood and petroleum and coal

[6] Particularly from Cambodia (Rasiah, 2009a).

products enjoyed the highest trade balances from 1990 to 2012. Between 2000 and 2012, the trade balance improved for wood, chemicals, rubber, plastics, non-metal mineral products and other manufacturing. However, the trade balance fell for food, beverage, textiles, garments, basic metals, machinery, professional and scientific equipment, and transport equipment.

The transport equipment industry has performed dismally, despite enjoying strong protection since the promulgation of the Heavy Industries Corporation of Malaysia in 1980 and the subsequent launching of Proton cars (Alavi, 1996). The Government further approved domestic automobile manufacturers Perodua, Naza Motors, Modenas and Inakom. However, the trade balance account of the transport equipment industry has shown little improvement (Table 7). The export value of automotive products from Malaysia rose (in US dollar value), from $121 million in 1990 to only $369 million in 2000 and $1.15 billion in 2008. The commensurate export figures for Indonesia rose from $22 million in 1990 to $369 million in 2000 and $2,783 million in 2008 while those of Thailand rose from $108 million in 1990 to $2,417 million in 2000 and $16,227 million in 2008 (WTO, 2009, Table 11.60). Clearly, exports from Thailand and Indonesia grew significantly faster than exports from Malaysia between 1990 and 2008.

Table 7. Manufacturing trade balance, Malaysia, 1979–2012

Sector	1979	1985	1990	1995	2000	2005	2008	2012
Food & beverage	-0.171	-0.327	0.594	0.641	0.520	0.594	0.159	0.166
Textiles & garments	-0.058	0.106	0.082	0.122	0.271	0.082	0.302	0.170
Wood	0.913	0.874	0.660	0.491	0.417	0.660	0.854	0.855
Chemicals	-0.710	-0.721	-0.635	-0.428	-0.176	-0.635	0.174	0.001
Petroleum & coal	NA	NA	0.512	0.382	0.379	0.512	0.052	0.051
Rubber & plastics	0.470	0.113	0.218	0.177	0.106	0.218	0.734	0.733
Non-metallic mineral	-0.335	-0.518	-0.464	-0.420	-0.156	-0.464	0.155	0.160
Basic metal	0.570	0.252	-0.492	-0.517	-0.393	-0.492	-0.393	-0.317
Machinery (incl. electrical)	-0.069	-0.071	-0.093	-0.019	0.104	-0.093	0.087	0.007
Transport equipment	-0.652	-0.624	-0.598	-0.502	-0.518	-0.598	-0.407	-0.587
Professional & scientific equipment	-0.477	-0.451	-0.385	-0.279	-0.150	-0.385	-0.322	-0.327
Others	NA	NA	0.357	0.024	0.223	0.357	0.288	0.291

Note: Formula used: export – import / export + import.
Source: Calculated from Government of Malaysia, 1971–2011b; ADB, 2008.

These results suggest that domestic capabilities seem to have developed more in resource-based industries enjoying natural endowments in the country. However, given that these industries are dependent on finite non-renewable resources, the Government will have to gradually reduce overdependence on those industries. A sustained long-term strategy of industrial deepening cannot be built in those industries.

Machinery (mainly electric–electronics products) dominated manufactured exports from Malaysia between 1990 and 2012 (Table 8). Petroleum and coal products enjoyed the next-largest share of exports. The contribution of textiles and garments shows a falling trend since 1990. Whereas the relative contraction in exports in the 1990s was a consequence of massive expansion in electric and electronics exports, the fall after 2000 was caused by the termination of the Multifibre Agreement and increased exports from China and least developed countries, such as Cambodia (Rasiah, 2009a).[7]

[7] A number of Malaysian firms have even relocated manufacturing in Cambodia to access developed markets (Rasiah, 2009a).

Table 8. Composition of manufacturing export, Malaysia, 1979–2012

Sector	1979	1985	1990	1995	2000	2005	2008	2012
Food & beverage	0.123	0.127	0.101	0.088	0.044	0.059	0.038	0.055
Textiles & garments	0.072	0.100	0.049	0.036	0.027	0.019	0.021	0.019
Wood	0.043	0.028	0.122	0.070	0.041	0.035	0.021	0.016
Chemicals	0.034	0.033	0.014	0.021	0.030	0.041	0.088	0.091
Petroleum & coal	NA	NA	0.193	0.073	0.098	0.141	0.067	0.101
Rubber & plastics	0.016	0.009	0.064	0.054	0.039	0.053	0.027	0.037
Non-metallic mineral	0.010	0.011	0.022	0.016	0.014	0.016	0.011	0.011
Basic metal	0.307	0.140	0.033	0.029	0.025	0.031	0.017	0.058
Machinery (including electrical)	0.321	0.497	0.341	0.533	0.624	0.541	0.597	0.552
Transport equipment	0.033	0.043	0.025	0.029	0.008	0.010	0.020	0.019
Professional & scientific	NA	NA	0.014	0.016	0.020	0.023	0.018	0.042
Others	NA	NA	0.023	0.035	0.030	0.031	0.075	0.069

Note: Formula used: Export of the industry divided by total manufactured exports; NA – not available.
Source: Calculated from Government of Malaysia, 1971–2011b; ADB, 2008.

There is evidence that the expansion of local suppliers benefited from dynamic changes in multinational companies, especially American companies.[8] In contrast, the number of electronics firms in Malaysia engaged in designing and R&D activities only constituted 1 per cent of the total in 2007 (Rasiah, 2010, p. 310). As the firms failed to evolve their technological capabilities to designing and R&D activities in the face of rapid expansion in China and Viet Nam, the supplier base began to contract as of the late 1990s (Grunsven, 2006; Rasiah, 2010). The lack of engineers and scientists, in particular, has been a glaring problem that has slowed productivity growth in the industry. For example, in 2007, Malaysia had only 729 researchers per million people when there were 7,059 researchers in Singapore and 6,028 researchers in the Republic of Korea (UNESCO, 2010).

The declining trend in manufacturing labour productivity growth, with the key export-oriented industries and inward-oriented industry of transport equipment recording either sharply declining or negative growth rates from 2000 to 2008, is a consequence of falling competitiveness arising from slow upgrading. Beverages and tobacco enjoyed the highest productivity growth from 2005 to 2008. Although the share of electronics exports from Singapore and Thailand in global exports rose from 7.6 per cent and 1.9 per cent, respectively, in 2000 to 2 per cent and 8.1 per cent, respectively in 2006, the commensurate shares from Malaysia fell, from 5.4 per cent in 2000 to 4.7 per cent in 2006 (Rasiah, 2009b).

Massive inflows of foreign capital into the manufacturing sector helped reduce the pressure on the Government to create jobs (Ariff, 1991; Rasiah, 1995 and 1999). The focus of industrial policy shifted towards industrial deepening as the Government attempted to take advantage of low unemployment levels, which reached 2.7 per cent in 1995. The Action Plan for Industrial Technology Development of 1991 contributed to the groundwork for the opening of the Human Resources Development Fund, the Malaysian Technology Development Corporation, the Malaysian Industry Government Group for High Technology, the cluster-based Second Industrial Master Plan, the Multimedia Super Corridor (now the MSC Malaysia) and the Multimedia Development Corporation in the 1990s to support technological deepening (Malaysia, 1991a; Rasiah, 1999). The Malaysian Institute of Microelectronic Systems was corporatized in the 1990s. A combination of poor coordination efforts and the lack of performance

[8] American multinational companies initiated such efforts for their own expansion (Rasiah, 1988 and 1994; Narayanan and Lai, 2000).

standards attributed to ethnic-based policies reduced the effectiveness of these instruments to stimulate value addition in the manufacturing sector. Hence, firms approached the Government to import foreign labour to sustain their operations, which aggravated the situation further by reducing the pressure to upgrade. The Government's focus on unskilled labour over the 1980s and the 1990s also undermined firm-level initiatives to upgrade. These developments led a number of authors to warn that the Malaysian industrialization project may have stalled (Rasiah, 1999; Best and Rasiah, 2003; Henderson and Phillips, 2007).[9]

Taken together, the evidence is overwhelming that manufacturing started to fall in significance as of the mid-1990s, with the contraction the most serious since 2000. Additionally, manufacturing industries have experienced a slowdown or a fall in trade performance and productivity since 2000. The chronic contraction trends suggest that manufacturing growth in Malaysia has, as of 2000, plateaued and is facing deindustrialization.

5. Impact on the labour market

This section presents evidence that the premature slowdown has restricted both labour productivity and wage growth in manufacturing in Malaysia. Weaknesses in tripartite relations and a general focus on capital, including FDI, has limited the extent of improvements in the material conditions of labour. Due to the paucity of comparable data, the period of 1988 through 2010 is used in this section, with the period defined on the basis of growth in mean wages in the manufacturing sector. Owing to data constraints, data from manufacturing only is used in some references, while in others data from the whole economy is presented. This section focuses on employment, labour force participation rates, labour productivity, real wages, gender segregation and discrimination, foreign labour, unemployment and inflation in Malaysia.

5.1 Employment

Average annual employment enjoyed positive growth in all industries from 1988 to 1997 (Table 9). Tobacco, textiles, footwear, petroleum and coal products then experienced negative growth from 2001 to 2005. The number of industries experiencing negative employment growth increased further from 2005 to 2010, including tobacco, textiles, footwear, wood products, furniture and fixtures, rubber, chemicals and electrical machinery.

[9] Rasiah (2011) offered conclusive evidence to show that the manufacturing sector has been experiencing negative deindustrialization since 2000.

Table 9. Annual average growth of employment, 1988–2010 (%)

Sectors	1988–1990	1990–97	2001–05	2005–10
Food & beverages	2.38	4.19	6.06	6.05
Tobacco products	24.32	13.37	-8.26	-18.01
Textiles	8.30	2.63	-0.70	-4.96
Footwear (except rubber footwear), other wearing apparel & made-up textile goods	18.14	0.41	-0.18	-1.93
Wood products	18.78	8.11	3.38	-3.09
Furniture & fixtures	12.55	17.69	6.97	-4.66
Printing, publishing & allied industries	5.86	8.50	10.72	2.53
Paper & paper products	15.61	9.05	5.50	7.82
Leather & leather products	69.03	2.83	3.41	0.41
Rubber products	12.26	3.20	7.47	-0.08
Chemicals & chemical products	11.62	7.46	8.85	-9.50
Products of petroleum & coal	0.00	16.29	-2.84	9.96
Non-metallic mineral products	17.26	10.07	3.11	3.31
Basic metal industries	18.84	11.04	5.33	7.87
Fabricated metal products	18.54	13.57	8.73	5.48
Machinery except electrical machinery	30.24	16.67	2.88	5.47
Electrical machinery & electronics	28.61	11.36	3.79	-1.50
Transport equipment	31.00	13.74	5.88	7.48

Source: Computed from Industrial Surveys, various issues, Government of Malaysia, 1971–2011a.

5.2 Labour force participation rates

Overall, labour force participation rates in Malaysia are fairly high among males but low among females (Table 10). Although the participation rate of males fell, from 85.3 per cent in 1982 to 79.7 per cent in 2011, that of females rose only slightly, from 44.5 per cent in 1982 to 47.9 per cent in 2011. Consequently, the unemployment rate among males rose slightly, from 2.7 per cent in 1982 to 2.9 per cent in 2011, while that of females fell, from 4.6 per cent in 1982 to 3.3 per cent in 2011. Because of the much higher participation rates, the Malaysian labour force is dominated by males.

Table 10. Labour force participation rates and unemployment, by sex, Malaysia, 1982–2011

	Male				Female			
	LF	Employed	PR	U	LF	Employed	PR	U
1982	3 562.3	3 465.3	85.3	2.7	1 869.1	1 783.7	44.5	4.6
1983	3 693.1	3 570.4	85.6	3.3	1 978.8	1 886.5	45.7	4.7
1984	3 832.2	3 662.6	85.4	4.4	2 030.3	1 904.1	45.2	6.2
1985	3 896.7	3 700.5	85.6	5.0	2 093.5	1 952.8	45.9	6.7
1986	4 037.7	3 753.5	85.8	7.0	2 184.3	2 006.6	46.4	8.1
1987	4 151.3	3 868.0	85.6	6.8	2 305.5	2 115.9	47.5	8.2
1988	4 268.7	3 984.0	85.9	6.7	2 368.4	2 173.2	47.7	8.2
1989	4 389.1	4 155.3	85.6	5.3	2 390.3	2 235.5	46.7	6.5
1990	4 489.8	4 310.7	85.3	4.0	2 510.3	2 374.3	47.8	5.4
1992	4 716.5	4 554.2	84.9	3.4	2 602.5	2 493.6	46.9	4.2
1993	5 043.3	4 853.8	86	3.8	2 656.9	2 529.6	46.5	4.8
1995	5 203.1	5 056.6	84.3	2.8	2 690.0	2 588.4	44.7	3.8
1996	5 653.9	5 514.2	84.9	2.5	2 962.1	2 885.0	46.8	2.6
1997	5 787.3	5 657.7	84.3	2.2	2 996.7	2 911.5	46.0	2.8
1998	5 904.2	5 718.9	83.1	3.1	2 979.4	2 880.7	44.4	3.3
1999	6 063.5	5 851.20	82.8	3.5	3 088.0	2 986.5	44.6	3.3
2000	6 156.2	5 973.50	83	3.0	3 399.9	3 295.7	47.2	3.1
2001	6 268.3	6 055.90	82.3	3.4	3 431.1	3 301.1	46.8	3.8
2002	6 352.3	6 141.80	81.5	3.3	3 533.9	3 400.8	46.7	3.8
2003	6 559.4	6 323.60	82.1	3.6	3 680.1	3 546.1	47.7	3.6
2004	6 615.1	6 390.40	80.9	3.4	3 731.1	3 589.1	47.2	3.8
2005	6 700.9	6 470.50	80	3.4	3 712.5	3 574.8	45.9	3.7
2006	6 843.5	6 618.60	79.9	3.3	3 785.40	3 656.8	45.8	3.4
2007	6 963.5	6 747.10	79.5	3.1	3 926.00	3 791.0	46.4	3.4
2008	7 074.6	6 851.10	79	3.2	3 953.50	3 808.5	45.7	3.7
2009	7 218.1	6 955.70	78.9	3.6	4 097.20	3 941.6	46.4	3.8
2010	7 955.5	7 707.80	79.3	3.1	4 348.40	4 191.7	46.8	3.6
2011	8 129.5	7 889.80	79.7	2.9	4 546.30	4 394.7	47.9	3.3

Note: LF = labour force; PR = participation rate; U = unemployment.
Source: Labour Force Surveys, Government of Malaysia,1984–2012.

5.3 Labour productivity

Manufacturing experienced significant labour productivity growth from 1990 to 1997 (Table 11). However, except for petroleum and coal, chemicals and basic metals, the remaining manufacturing industries experienced such negative labour productivity growth that overall manufacturing labour productivity actually declined from 2000 to 2005. Apart from some inward-oriented and resource-based industries, labour productivity of several export-oriented industries then recorded negative or low annual

average growth from 2005 to 2010. The inward-oriented industry of chemicals also experienced a sharp decline in labour productivity in this period.

Petroleum, coal and basic metals were the only manufacturing industries to record positive labour productivity growth in both periods of 2000–05 and 2005–10 (Table 10). Although labour productivity of most industries grew positively in the ensuing period, from 2005 to 2010, the improvement was very small, so that overall manufacturing labour productivity only grew by 1.8 per cent on average per annum. Labour productivity of the electric–electronics industry grew at an annual average of 11.8 per cent during 1990–97 but dropped to an average of -0.9 per cent from 2000 to 2005 and rose to only a 0.04 per cent average from 2005 to 2010. The strong technological synergies offered by multinational corporations in the late 1980s and early 1990s appear to have been undermined by a lack of effective technological rooting policies for local firms to upgrade to the technology frontier (Rasiah, 2012).

Table 11. Annual average growth of labour productivity, 1988–2010 (%)

Sector	1988–1990	1990–97	2001–05	2005–10
Food & beverages	6.63	2.74	-3.91	4.66
Tobacco products	-25.57	1.56	-0.14	42.31
Textiles	4.64	13.87	-10.57	6.79
Footwear (except rubber footwear), other wearing apparel & made-up textile goods	3.87	5.63	-4.81	0.63
Wood products	2.62	4.75	-0.38	4.25
Furniture & fixtures	9.72	10.57	-6.00	3.12
Printing, publishing & allied industries	17.62	7.07	-4.59	-4.55
Paper & paper products	8.69	4.46	-11.56	-0.76
Leather & leather products	-12.04	13.26	-1.70	3.95
Rubber products	10.19	9.09	-3.97	4.68
Chemicals & chemical products	-6.95	5.43	5.48	-19.69
Products of petroleum & coal	33.37	5.93	28.15	1.08
Non-metallic mineral products	-0.32	3.28	-7.58	4.97
Basic metal industries	7.48	3.53	4.34	5.43
Fabricated metal products	6.20	6.27	-4.87	2.00
Machinery except electrical machinery	6.47	8.60	-3.05	-2.62
Electrical machinery & electronics	4.97	11.79	-0.91	0.04
Transport equipment	11.26	4.57	-12.41	3.24
Total manufacturing	**6.53**	**5.87**	**-1.46**	**1.75**

Source: Computed from various issues of Industrial Surveys, Government of Malaysia, 1971–2011a.

When the Multi-Fibre Agreement was in place from 1974 to 2004, the textile and garment industry expanded in Malaysia. The total export value of the industry in 1998, for example, amounted to 9.6 billion ringgit (MYR), which was 4.7 per cent of total exports and the third-largest foreign exchange earner after the electronics and palm oil industries. In the previous years, the amount of export value in the textile and garment industry more than doubled. But in 2012, the industry had the same value as it did in 1998, and in 2012 it registered a 12.4 per cent loss (Crinis, 2013). As already noted, the end of the Multi-Fibre Agreement triggered that decline. But additionally, most small and medium-sized garment factories have not introduced higher levels of technology and instead have relied on a combination of labour intensification and foreign and home-based workers to meet the increased competition and the demands of "just-in-time" production. Home-based production has expanded in urban areas because working-class Malaysian women are unable to work the long hours in the factories and thus have opted for home-based work in the manufacturing industries (Crinis, 2013). The dual workforce of unskilled factory workers and home-based workers has kept wages low.

5.4 Real wages

Real wage growth in Malaysia's manufacturing sector has never reached double digit figures owing to a combination of both a preponderance of specialization in low value-added activities and the Government's anti-union labour policies (Jomo and Todd, 1993; Rasiah, 1995). Real wages grew most in the 1990s, despite the inflow of foreign labour imports into the manufacturing sector, because of the saturation in the labour market. However, real wages grew little after 2000, when investments and labour productivity in manufacturing began to fall.

While the regulatory environment confronting workers in Malaysia has remained hostile since 2010, low increments in labour productivity growth have undermined the capacity of labour to enjoy higher wages in the manufacturing sector. Despite strong claims by the Malaysian Trade Union Congress leaders that official inflation figures produced by the Government are manipulated,[10] most industries still recorded negative or low growth in real wages between 1988 and 2010 (Table 12), which reflects the low wage and low skills in manufacturing overall. Real wages in the sector only grew annually by an average 0.6 per cent from 2001to 2005 and then by an average of 1.3 per cent from 2005 to 2010. Except for tobacco, which enjoyed substantial growth in domestic demand (despite campaigns about its deleterious effects on health), all the manufacturing industries have experienced either low or negative growth since 2001.

Wages also have remained on the low side because of the massive inflow of foreign unskilled labour into manufacturing since 1990. Figure 1 and Tables 11 and 12 show tremendous official inflows of foreign workers over time and their source countries, based on immigration records. Truer estimates of the total number of foreign workers would include both documented and undocumented workers, which are harder to obtain. In 2012, the 6P biometric registration and amnesty programme registered 2.3 million foreign workers, or about 16 per cent of the total employed population in Malaysia. That figure may be closer to 4 million – even the Government cited such a number in May 2012, which amounts to staggering quarter of total employment. It is safe to say that the share is large and immensely impacts on the orientation and capacity of the Malaysian economy. The educational profile of foreign and Malaysian workers makes clear the overwhelming disparity in qualifications. In 2010, 60 per cent of foreign workers had a primary school level of education or less, compared with 16 per cent of Malaysian workers (Lee, 2014).

The Government eventually introduced the minimum wage requirement, setting the monthly rate at MYR900 ($291) for Peninsular Malaysia and MYR800 ($259) for Sabah and Sarawak in January 2013. The minimum wage is a basic wage and excludes overtime, allowances and other benefits. In response to an outcry from small and medium-sized enterprises, the Government, without trade union or NGO consultation, allowed such enterprises (through an amendment to the legislation) to defer payment until December 2013 (Lee, 2014). Larger companies had to pay the minimum wage increase but the Government allowed them to deduct money from migrants' wages to recover expenses that they had incurred to employ them (such as paying the government levy). Although the Government stopped the practice of allowing employers to deduct the levy in 2009 (after the Nike and Hytex incident), the Malaysian Cabinet decided to let employers resume the practice (Crinis, 2013). In such a situation, workers were actually better off before the minimum wage legislation. Hence, the Minimum Wage Act offers little support for wage improvements in the manufacturing sector.

It is clear that real manufacturing wages grew little over the years owing to little technological upgrading; but the persistence of low value-added and wage manufacturing activities further undermined any rise (Tables 11 and 12). The strategy to import massive numbers of foreign unskilled labour has accentuated the problem because it removed the pressure for firms to raise wages. The national policies to transform the country to industrialized status since 1991 also has been ineffective because not only has the country been unable to mobilize human capital domestically and from abroad, but the meso organizations created to stimulate research and development (R&D) and other forms of knowledge networks have translated little into firms participating in knowledge-intensive activities. Only a handful of firms have benefited from hiring the limited human capital available to participate in R&D and designing activities. Malaysia has remained confined to the low industrialization route and, hence, not able to support significant increments in real wages.

Table 12. Annual average growth in real wages, 1988–2010

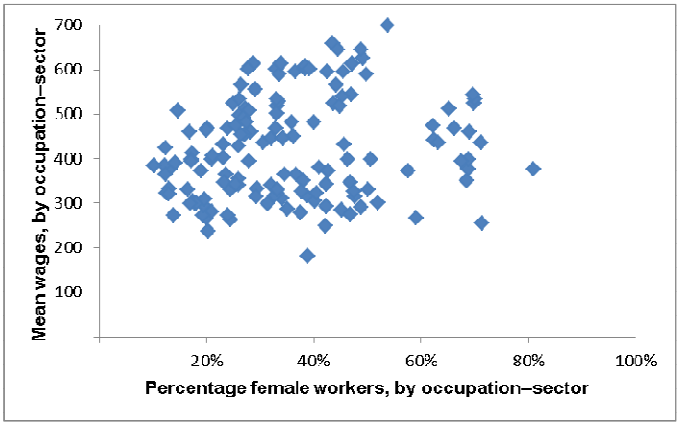
Sector	1988–1990	1990–97	2001–05	2005–10
Food & beverages	2.45	-0.23	0.01	1.66
Tobacco products	-14.92	-13.66	6.93	18.20
Textiles	5.77	3.06	-2.01	0.07
Footwear (excluding rubber footwear), other wearing apparel & made-up textiles	7.56	1.96	-1.61	-1.33
Wood products	1.29	-1.36	1.30	1.91
Furniture & fixtures	5.76	3.34	1.07	0.50
Printing, publishing & allied industries	3.12	0.01	-1.28	-4.22
Paper & paper products	2.74	3.51	-1.54	-0.01
Leather & leather products	-4.99	6.66	0.42	1.01
Rubber products	3.14	3.64	0.48	3.14
Chemicals & chemical products	1.23	2.19	2.96	-5.71
Products of petroleum & coal	-2.69	-0.80	0.70	-0.88
Non-metallic mineral products	-1.21	0.76	0.76	2.46
Basic metal industries	-1.54	1.58	0.74	5.43
Fabricated metal products	-1.78	1.69	0.25	1.18
Machinery except electrical machinery	-1.20	2.78	-0.02	-0.83
Electrical machinery & electronics	1.24	4.29	1.41	1.82
Transport equipment	-2.87	3.74	-0.92	0.42
Total manufacturing	**-1.17**	**0.92**	**0.55**	**1.31**

Source: Computed from various issues of industrial survey, Government of Malaysia, 1971–2011a.

5.5 Gender segregation and discrimination

This paper is using a broad data set to examine gender segregation and discrimination in Malaysia's labour force. A scatter diagram of the percentage of females in 144 occupation–sectors against mean wages is presented in Figure 2. There does not appear to be any distinct pattern in the proportion of females in an occupation–sector and the mean wages represented. The largest female representation is among clerical support staff in mining, where they constituted 81.1 per cent of workers in the occupation-sector, with mean wages of $376 in 2009. The highest mean wage for females by occupation-sector was among professionals in agriculture, where they earned a mean monthly wage of $699 while constituting 53.9 per cent of the workers in this group.

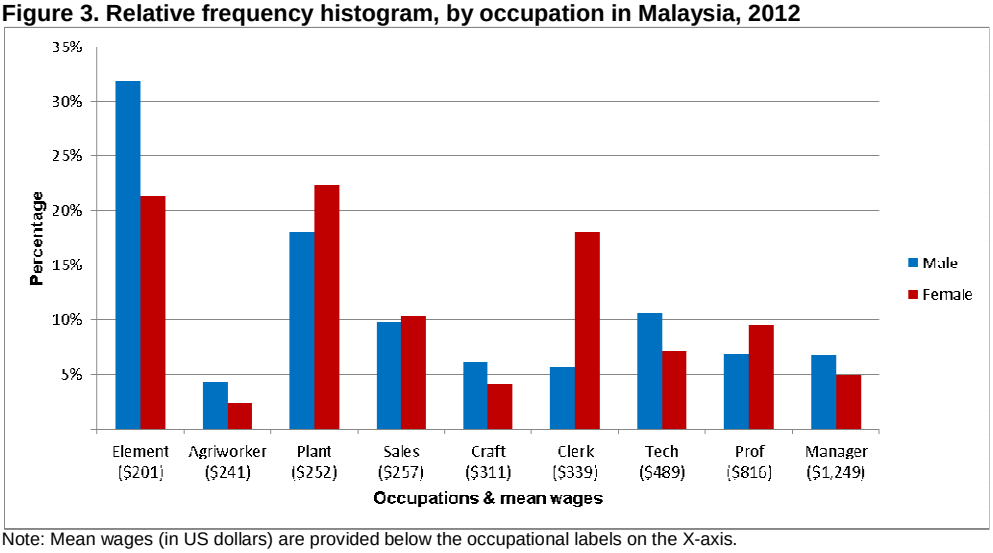
Figure 2. Scatter diagram of the proportion of female workers compared with mean wages, by occupation–sector, Malaysia, 2012



Source: Sanjivee and Rasiah, 2014.

Figure 3 presents a relative frequency distribution of male and female workers across occupational groups, which are arranged on the x-axis in ascending order of mean wages. The largest occupational group, which constitutes 28.1 per cent of the sample, consists of elementary workers who are also the lowest mean wage earners. Male workers make up 71.2 per cent of the total workers of this group. The second largest occupational group consists of plant and assembly workers, where females contribute 40.7 per cent of the workers. The occupational group where female workers are dominant is the clerical workers, where they females make up 64.0 per cent of the workforce. Females also show strong participation among professionals, although greater proportions of males employed are employed as managers and technicians.

Figure 3. Relative frequency histogram, by occupation in Malaysia, 2012



Note: Mean wages (in US dollars) are provided below the occupational labels on the X-axis.
Source: Sanjivee and Rasiah, 2014.

Reflecting the Blinder-Oaxaca decomposition of the sample, the mean male wage in Table 14 is 5.702 log points while the mean female wage is 5.682 log points. This translates into a mean wage of $299.38 for males and $293.53 for females. This indicates that the mean wage of males exceeds the mean female

wage by 0.02 log points which approximates 2 per cent. However, the explained portion of the decomposition returns is a negative -0.087, implying that if females were paid equal wage for the same worker characteristic as males, they would earn a mean wage higher than males. As a result, the unexplained portion of the male–female sex-based wage difference is 0.106 log points. If workers' endowments are taken into consideration, males are on the average rewarded 11.2 per cent more than females for similar endowments. This finding suggests that sex-based wage discrimination is present in the labour market.

Table 13. Skewedness of occupational distributions

Sex	Skewedness	Standard error of Skewedness	Confidence internal (95%)	
			Lower limit	Upper limit
Male	0.548	0.003	0.543	0.554
Female	0.202	0.004	0.194	0.209

Source: Sanjivee and Rasiah, 2014.

Table 14. Aggregate Blinder-Oaxaca decomposition

Dependent variable: in (Y)	Coef.	Std error	z-statistics	P>lzl
Males	5.702	0.001	4 593.920	0.000
Females	5.682	0.001	6 538.510	0.000
Difference	0.020	0.002	13.010	0.000
Explained characteristics	-0.087	0.001	-72.290	0.000
Unexplained characteristics	0.106	0.001	100.940	0.000
Number of observations	1 316 692			

Note: Coef. = coefficient; Std error = standard error.
Source: Sanjivee and Rasiah, 2014.

A study of two electronic firms showed that, unlike in the textile and garment industry, factory women with access to long-term employment had the opportunity to increase their technology skills in the 1990s when production became more automated, incorporating flexible techniques evident in the components subsector with the introduction of "just-in-time" and "quality-control circle" methods (Maznah, 1999). During the 1990s, Malaysia was moving towards the Government's vision of high-tech industries. But the electronics industry, especially the semiconductor and electronic consumer goods section, is a globalized industry extremely well known for its sporadic retrenchment of workers. The employment pattern is unstable, and the industry is highly subject to the predicament of overproduction. In the Asian economic crisis that began in 1997, large numbers of electronics workers were laid off. After 1998, the numbers of Malaysian workers stopped applying for jobs in electronics factories because the wages were too low. Yet, instead of training workers and limiting the numbers of foreign workers, the Government allowed manufacturers to resume foreign worker recruitment (Lee, 2014). As a result, the industry has remained low tech and labour-intensive due to the dependence on low-skilled, poorly paid foreign workers on short-term contracts from poor countries in the region.

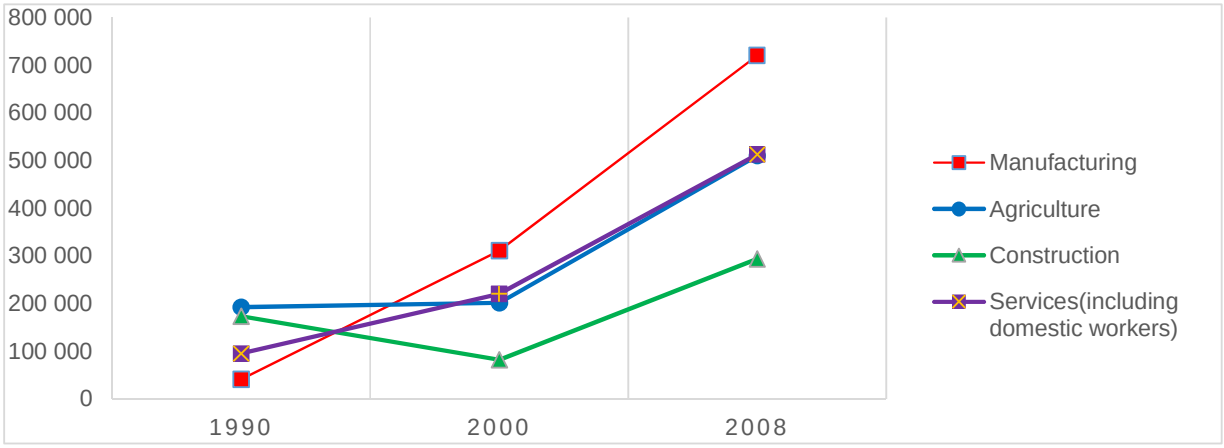
5.6 Foreign labour

In the manufacturing industries, foreign workers are employed on one- to three-year contracts (but can be extended to five years) and provided accommodation and, in some cases, transport. The employment contract specifies the name of the employer and the conditions, such as the wage rate and terms of work, including hours of work and overtime. In Malaysia, the lowest-paid category of workers on the Government's Doing Business in Malaysia website are production workers (Crinis, 2013). Yet, foreign workers' wages are often much lower than what is stated there. Before the minimum wage introduction, foreign workers were paid between MYR18 and MYR26 per day. For the first three months of employment, workers were paid only MYR18 per day and then the rate went up to the ceiling rate of MYR26 per day. Migrant workers do not bargain for higher wages because they fear losing their jobs. Instead, they increase their wages by working as much overtime as allocated. During the global economic crisis, the numbers of foreign workers declined by 300,000 because expiring work permits were not renewed, and the Government restricted further intake of migrant workers. By the end of 2009, manufacturers had to increase wages to entice Malaysian workers. During that period of labour shortage, the wages of manufacturing workers rose, from MYR450 ($130) a month in 2008 to MYR650 ($185). In response to pressure from manufacturers, however, the Government once again allowed electronics and textile firms to resume recruitment of male and female foreign workers (Crinis, 2012).

Since 1995, more than 90 per cent of foreign workers have engaged in low-skilled jobs, compared with less than 50 per cent of Malaysian workers. Between 1985 and 2008, the number of foreign workers in low-skill production jobs increased 81 times (from 5,500 to 447,400). Over the same period, the number of foreigners increased fourfold at the management and professional levels, 19 times among technical and supervisory staff and 21 times for clerical and general workers. In 2010, 96 per cent of foreign workers in manufacturing were classified as unskilled, compared with 73 per cent in 1985 (Crinis, 2012).

Not only did the numbers of foreign workers by sectors shoot up sharply between 1990 and 2008 (Figure 4), manufacturing has become the largest employer of foreign workers, followed by agriculture and services.

Figure 4. Foreign workers in Malaysia, by sector (number of workers)



Source: Athukorala and Devadason, 2012.

As Table 15 shows, more than half of foreign workers in 2007 came from Indonesia, followed by Bangladesh, Nepal and India. Whereas the largest group of Indonesians are in domestic work, the largest group of Nepali and Bangladeshi workers are in manufacturing.

Table 15. Foreign workers in Malaysia, 2007

Country	Domestic	Construction	Manufacturing	Services	Plantations	Agriculture	Total
Indonesia	294 764	211 016	206 780	41 012	290 454	103 974	1 148 000
Nepal	31	4 493	172 311	1 904	2 584	8 080	189 403
India	126	7 382	28 446	60 049	22 451	23 575	142 029
Myanmar	61	14 857	29 906	6	1 484	7 911	54 225
Viet Nam	31	5 251	104 948	2 951	79	645	113 905
Bangladesh	21	40 497	128 664	21 843	14 207	12 006	217 238
Philippines	10 443	1 640	2 858	1 103	4 562	2 577	23 173
Thailand	426	1 122	793	15 532	53	530	18 456
Pakistan	2	4 947	3 140	1 708	971	6 045	16 813
Cambodia	7 458	173	2 582	240	207	95	10 755
China	18	2 284	959	3 137	221	14	6 633
Sri Lanka	883	106	1 580	731	91	295	3 686
Lao PDR	1	13	16		1	1	32
Uzbekistan		6	1	4			11
Total	**314 265**	**293 787**	**682 984**	**150 220**	**337 365**	**165 748**	**1 944 358**

Source: Immigration Department, cited by Khamis Ar Majid, Labour Minister, 2008, see Lee, 2014.

Within the manufacturing sector, the foreign workforce is dominated by Indonesians, Nepalese and Bangladeshis (Table 16). The order of rank among the top-three source countries remained the same in 2007 and 2010. Workers from Myanmar took third place ahead of Viet Nam in 2010.

Table 16. Foreign workers in manufacturing industries, Malaysia, 2007 and 2010

2007		2010	
Source country	**Malaysia**	**Source country**	**Manufacturing**
Indonesia	206 780	Indonesia	198 643
Nepal	172 311	Bangladesh	170 332
Bangladesh	128 664	Nepal	135 764
Viet Nam	104 948	Myanmar	92 135
Myanmar	29 906	Viet Nam	68 433
India	28 446	India	13 866
Philippines	2 858	Pakistan	2 217
Thailand	793	Philippines	1 915
Pakistan	3 140	Cambodia	2 353
Cambodia	2 582	China	935
China	959	Thailand	893
Sri Lanka	1 580	Sri Lanka	1 382
Lao PDR	16	Lao PDR	16
Uzbekistan	1	Uzbekistan	0
		Others	2
Total	**682 984**		**688 886**

Source: Malaysian Bar Council; Malaysian Textiles Manufacturing Association; reproduced from Lee, 2014.

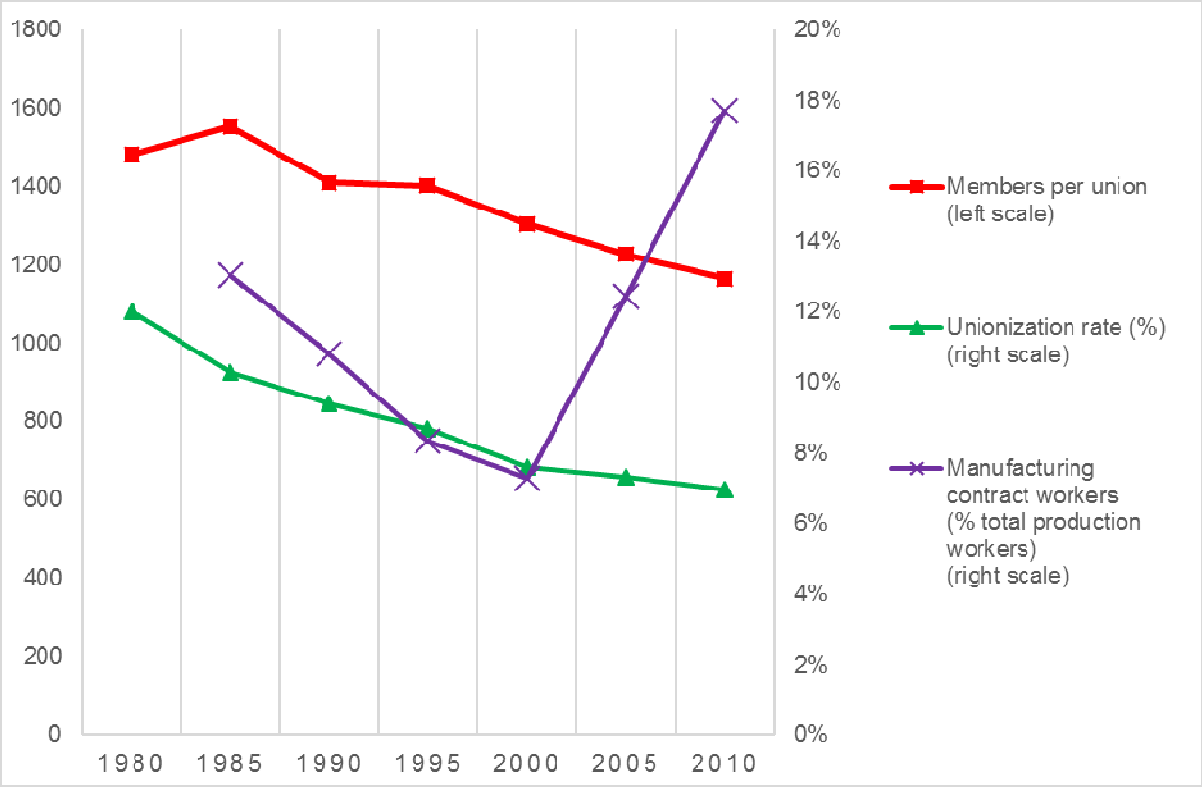
The Malaysian Trade Union Congress tried to persuade the Government to stop the flow of foreign labour on the grounds that it depresses the wage structure and weakens incentives to attract Malaysian workers, but to no avail (Crinis, 2008). During the 2000s, the numbers of foreign workers continued to increase in the manufacturing sector. By 2012, the number of foreign workers exceeded national workers in all manufacturing industries except electronics factories. In the garment factories, foreign workers now make up about 80 per cent of the production workforce, leaving the industry heavily dependent on foreign workers (Crinis, 2012*)*.

Foreign workers are subjected to a range of abuse, from wage deductions to injuries and premature repatriation; many injustices are overlooked because there are few labour inspectors (around 300) for a workforce of almost 14 million (Crinis, 2013; Lee, 2014). The burgeoning presence of foreign workers is inextricable from the chronic decline in union density in Malaysia and an increasing utilization of labour contracting in the 2000s, as shown in figure 5. These trajectories weaken the capacity for stable employment and worker representation, which otherwise would contribute positively to upgrading skills. Standing (1992) found, from a broad survey of Malaysian manufacturing establishments, that unionized firms are more likely to engage in training and technological change.

Most migrant workers are not organized in the electronics, textile and garment industries due to government restrictions and initial union inaction towards short-term contract workers. Initially, the Government limited the rights of workers to join unions in the export industries in the 1970s because of the risk of increasing labour costs and undermining international competitiveness. The union movement in Malaysia was unable to reach the large numbers of workers in the electronics industry because the Government and employers preferred the Japanese model of in-house unions. Although the Malaysian Trade Union Congress continued to lobby the Government to lift the ban on unions in the electronics industries, US employers threatened to relocate if the bans were lifted. After more than 30 years, workers were allowed to form regional unions in 2010 (Crinis, 2013).

Additionally, the Malaysian Trade Union Congress (MTUC) initially argued that migrants were a source of labour that undermined unionized workers' job security and their terms of employment (Crinis, 2013). It was not until 2008 that the MTUC reported to the International Labour Organization on the denial of freedom of association for migrant workers and began working towards making migrant workers aware of their rights under the national labour laws. Then the MTUC started to lobby on behalf of contract workers as well as foreign workers and called for the Government to assess labour market needs before issuing more work permits for overseas workers. Nonetheless, employers continue to hire foreign workers because they are flexible, willing to work long hours and to be repatriated when their contract ends. In more recent times, the MTUC has supported worker associations, such as the General Federation of Nepalese Trade Unions, which includes foreign workers.

Figure 5. Unions and contract labour



Sources: Lee, 2014; calculated from MTUC: *Labour and human resource statistics, Labour and manpower Report* and *Yearbook of statistics, annual survey of manufacturing establishments.* Available at: www.mtuc.org.my [accessed 27 Oct. 2014].

The MTUC also called on the Government to at least set a minimum wage for the lowest paid workers (both nationals and foreign workers) that met the cost of living, which had increased over the 2000s due to increases in food, rents, petrol prices and water privatization (Crinis, 2013). But according to MTUC officials, the Government listened to employers, who argued that a minimum wage would reduce competition and that FDI would move to another "low-cost" location if a minimum wage was introduced (Crinis, 2013). Even though minimum wages of MYR900 for Peninsular Malaysia and MYR800 for Sarawak and Sabah came into effect on 1 January 2013, they were confined to national workers.

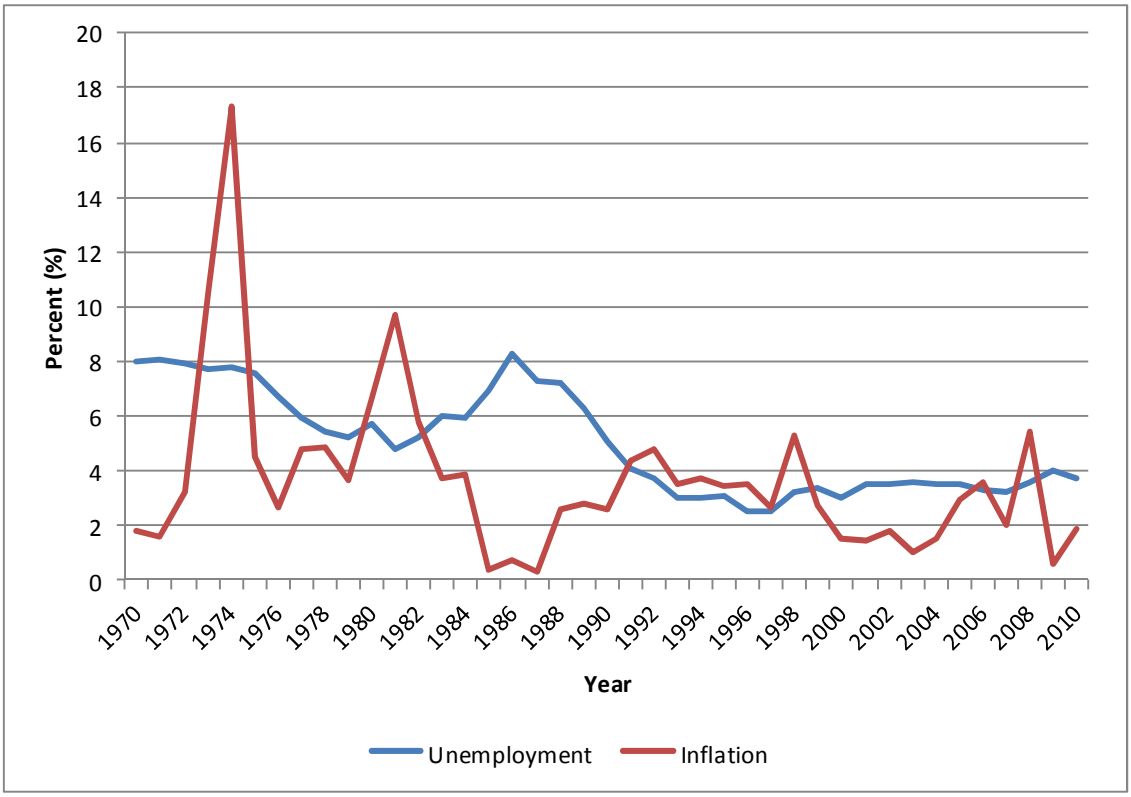
Not only have some employers preferred non-unionized unskilled foreign workers because of the attraction of low wages, they have also been able to bind foreign workers contractually over longer periods to reduce job hopping. The Human Resource Development Act of 1992, which was targeted at forcing firms to train national workers, became ineffective because those most likely not to train shifted to hiring foreign workers.

5.7 Unemployment and inflation

Apart from the inflationary years of 1973–75 and the deflationary years of 1985–87, 1997–98 and 2008–09, unemployment and inflation in Malaysia have remained fairly low (Figure 6). Although foreign labour has acted as a cushion during times of crisis, it has also reduced the pressure for firms to shift towards

higher value-added and capital-intensive activities. Also, the withdrawal of fuel subsidies and the impending introduction of the goods and services tax that was announced in the 2014 budget have already driven up prices of several essential items (Bank Negara Malaysia, 2013). Because the removal of subsidies and the impending goods and services tax are viewed largely as targeted at trimming public debt, it is likely that inflationary pressures may remain for a while.

Figure 6. Unemployment and inflation rates, Malaysia, 1970–2010



Source: Extracted from Rasiah, Yap and Santha, 2014.

Another structural characteristic of Malaysia's labour markets relate to the persistence of what Lee (2014) referred to as "exertion-intensive employment". Productivity can be generated through higher skill and efficiency per time unit (relative surplus value appropriation) or increased by raising labour time (absolute surplus value appropriation). Malaysia's conventional approach to measuring productivity in per worker terms omits important information on the efficacy of work, captured in output per worker hour. Available cross-country data on hours worked (per week) indicate patterns in levels and changes over time between high-income, middle-income and low-income countries (Lee, 2014). Although hours worked against GDP have fallen since 2000 in the Republic of Korea and Taiwan (China), in Malaysia it rose to the same level as the poorer economies of Indonesia and the Philippines.

The availability of a large reservoir of foreign labour, especially low-skilled workers, has exacerbated the preoccupation of the Malaysian Government with the low road to industrialization. In 2009, for instance, foreign workers reported an overall average of 55 hours of work per week, compared with 46 hours for Malaysian workers in 2009 (Lee, 2014). The disparity is greater among the less-skilled workers. Among

workers without formal education, 20 per cent of foreign workers worked more than 70 hours per week, compared with 54 hours for Malaysians.

6. Conclusions and implications

The evidence shows that the cooling of the manufacturing sector prematurely has led to the persistence of low value-added activities in Malaysia, with profound implications for the labour market. Integration into ASEAN has helped Malaysia enjoy the synergies of regional coordination, though its effects have, at most, only shielded it from serious decline as China has become an important recipient of FDI and participant in the export markets. Although Malaysia's economic growth since 2012 has been steady, the onset of deindustrialization before a shift to higher value-added activities has negatively affected value-added growth since 2000. And even though it is typically part of structural change for manufacturing's share in GDP to rise and fall, the evidence reveals that Malaysia is facing premature deindustrialization, with a slowdown trend in labour productivity and trade performance as of 2000. Not only has the trade performance of manufacturing been falling, manufacturing labour productivity has slowed, with the key sectors of electric–electronics, textiles and transport equipment showing either negative or low productivity growth since 2000. Foreign low-wage labour has largely helped Malaysia maintain trade competitiveness in low value-added activities. Despite the introduction of a minimum wage system for national workers in 2012, real wages have grown little in the manufacturing sector, which is the largest employer of low-skilled foreign workers, as a consequence. Weak trade unions have not helped. Although unemployment and inflation have remained low, the preoccupation with low-end activities has restricted per capita income growth. The formation of the AEC offers both opportunities as well as threats to Malaysia's labour market.

The increasing focus on the service sector, especially in knowledge-based high value-added activities, is good; but the Government should not abandon manufacturing. Given four decades of export-oriented manufacturing growth, it should implement a strategic industrial policy to stimulate value addition in the key industries of electronics, downstream palm oil and machinery and equipment and revisit agriculture to modernize the sector. The role of government should ensure that rents are provided for public goods, such as R&D, and the right incentive and penalty framework should be introduced to stimulate a structural shift in GDP activities, from low to high value-added activities.

Although the Malaysian Government intervened in the economy – offering strong incentives and indirect subsidies to export-oriented industries, such as electric–electronics, textiles and garments, and protection and direct subsidies to the import-substitution industries, such as steel and automobiles – the lack of human capital development and other meso organizations has restricted technological upgrading in the sector. Also, state interventions in Malaysia has been eclectic, with a largely pro-capital set of tax and tariff incentives and R&D grants, with little focus on performance standards (Rasiah, 1999 and 2011). By the late 1990s, it became clear that government strategies to stimulate upgrading in the country had run out of steam while labour productivity growth in most manufacturing industries either contracted or slowed down. Driven by ethno-patronage politics, the incentive system in Malaysia has lacked a mechanism to attract the performers as well as the appraisal system to transform the rents productively. In addition, especially lacking in human capital supply and support from meso organizations associated with knowledge synergies, the foreign-dominated electric–electronics and textile industries have increased

their reliance on low-wage foreign labour, which has aggravated the capacity of manufacturing to shift towards high value-added activities.

Hence, the low road of industrialization experienced by Malaysia grew worse when labour productivity and trade competitiveness in a number of industries began to fall, with real wages either slowing down substantially or contracting as of 2000. Although the successful industrializers, such as the United States, Germany, Japan, the Republic of Korea and Taiwan (China) experienced a sustained rise in real wages even after deindustrialization set in, Malaysia's premature deindustrialization process has undermined its manufacturing sector's capacity to support a similar experience. Large imports of unskilled labour from abroad have only further aggravated the situation.

Malaysia was a pioneering member of ASEAN and at the forefront shaping the critical events of the grouping. But now the AEC is unlikely to dramatically change the landscape of economic growth in the country. Nevertheless, this paper focused on two worthy questions in addressing further integration through the AEC in 2015: How can structural change from low to high value-added activities in manufacturing be promoted? And how can Malaysia pursue the high road to industrialization? The answers obviously suggest that the Government must focus on national instruments to revive and support upgrading in the manufacturing sector and to use the ASEAN framework, which includes economic cooperation in several fields, including on intellectual property rights, to appropriate group synergies.

One major warning for the Government is to avoid being dragged into the quicksand of unrestrained liberalism. As Chang (2003) and Reinert (2007) have argued, if Malaysia were to follow the neoclassical approach to economic integration with the government focus only on infrastructure development, it is very likely that Malaysia will continue to lose export competitiveness, which will further undermine its efforts to transform into a high-income country by 2020. Also, its ability to sustain competitiveness in low-wage activities will depend on the availability of low-skilled low-wage labour from the poorer members of ASEAN. With greater stability and infrastructure development in these countries, foreign capital may prefer to relocate to those countries than to Malaysia, and hence, it is likely that free market augmenting policies may further undermine Malaysia's ability to sustain growth in a number of economic activities.

ASEAN markets became integrated in terms of trade through the AFTA process, which began in 1992. But the opportunities that the AEC can provide will include further integration and, with that, a freer flow of people and labour across the region. Greater specialization can be expected. Malaysia has managed to attract foreign labour to sustain its exports of electronics, palm oil, rubber products, garments and textiles; but the prime reasons for the choice of Malaysia are better infrastructure and security compared with human resource endowments. With the Penang Skills Development Centre, Malaysia now has a model training centre that is industry driven. It is important that the Government strengthen its institutional capability to produce quality human capital and training to stem any possible competition that may come from (especially) Indonesia, the Philippines, Thailand and Viet Nam. Universities in Malaysia must be reinvigorated to contribute more to support innovative activities. The successful expansion of human capital will then act as a magnet to attract human capital from Indonesia, the Philippines, Thailand and Viet Nam in particular and also from the transition economies of ASEAN to strengthen Malaysia's attempt to stimulate a structural transformation from low to high value-added activities. This is essential for Malaysia to realize its goal to become an industrialized country by 2020.

Although foreign low-skilled labour can be a temporary substitute, the Malaysian Government must focus on rejuvenating productivity by emphasizing the infusion of innovation-based activities, with a concentration on manufacturing. Government policy has pushed this since the launching of the Economic Transformation Programme. However, government planning and policy implementation will require a pursuance of strong structural transformation methodologies. The use of input–output tables and dynamic computable general equilibrium models is critical to target a shift from low to high value-added activities. That will then require the provision and monitoring and appraisal of value-adding activities, such as R&D. Institutional change to stimulate this transformation would require the reinvigoration of the critical meso organizations, such as universities, and specialized R&D organizations, such as the Malaysian Institute of Microelectronic Systems, which must produce quality innovative personnel and the knowledge essential to drive productivity growth.

The achievement of the high road to industrialization will require the introduction of strong labour market institutions to ensure that real wages grow with low inequality. Trade unions should be accorded greater rights and representation, and they should be made participants in the Government's initiatives to absorb inclusive development. In doing so, efforts must be taken to keep inequality levels low. Low inequality will also help expand domestic consumption so as to reduce the country's dependence on export markets, which can be dangerous during times of global financial crises (Lim and Lim, 2010). The 2008–09 global financial crisis is a case in point. The minimum wage system introduced in 2013 is a step in the right direction, but the Government must ensure that there is enforcement. Efforts also must be taken to ensure that national and foreign labour is treated the same. Clearly, the exertion-based labour process targeted at foreign workers must disappear because it not only sends a wrong message to ASEAN Member States on cooperation, it also prevents structural transformation from low to high value-added activities. The AEC should be targeted to attract professional and technical labour from Member States in areas where Malaysia wants to catch up technologically, such as in the electric–electronics, palm oil and biotechnology industries.

Although the efforts to revise fiscal policy instruments to introduce the goods and services tax and remove subsidies are good because they will help stem economic leakage and the misallocation of resources to non-targeted groups, the Government must ensure that the lower-income classes enjoy subsidized access to essential goods and services.

The Malaysian experience serves as a good example of promotional strategies that were initially important in attracting FDI but were eventually found to be lacking in instruments to ensure industrial deepening of nascent economies that are necessary to engender the conditions to stimulate early manufacturing growth. Such approaches will not be sufficient to sustain long-term rapid growth and structural change towards high value-added activities and, with that, the pursuit of the high road to industrialization.

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Economic implications of ASEAN integration for Malaysia's labour market

This paper examines the implications of the formation of the Association of Southeast Asian Nations (ASEAN) Economic Community (AEC) in 2015 on Malaysia's labour market. The discussion centres on the nature of the structural change that Malaysia has experienced, especially since the 1980s, and how that has impacted on its labour market. Integration into ASEAN markets has obviously helped Malaysia enjoy the synergies of regional coordination. Although Malaysia's economic growth has been steady, the onset of deindustrialization before a shift to higher value-added activities has impacted somewhat negatively on per capita income growth rates since 2000. Although it is typically part of structural change for manufacturing's share of gross domestic product to rise and fall, evidence reveals that Malaysia is facing premature deindustrialization, with a slowdown in labour productivity. In particular, trade performance since 2000 has impacted somewhat negatively on the labour market. Not only has the trade performance of manufacturing been falling, manufacturing labour productivity has slowed, with key sectors, such as electric–electronics, textiles and transport equipment, showing either negative or low productivity growth since 2000. Foreign low-wage labour has largely helped Malaysia maintain its trade competitiveness in low value-added activities. Despite the introduction of minimum wages in 2012, real wages have grown little in the manufacturing sector, which is the largest employer of low-skilled foreign workers. Weak trade unions have not helped. Although unemployment and inflation have remained low, the preoccupation with low-end activities has restricted per capita income growth.

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