

GROWTH WITH EQUITY: THE MALAYSIAN CASE

Renuka Mahadevan*

While Malaysia is one of the few economies which has successfully enjoyed economic growth with equity from 1970 to 1990, recent studies suggest that income inequality rose in the 1990s. This paper re-examines these arguments in the light of Malaysia's economic development and the policies undertaken for the 1990s and beyond. In relation to Malaysia's progress to a second-tier newly industrializing economy, its success with growth and equity enables important lessons to be drawn for increasingly open developing economies facing the challenges of globalization and deregulation.

I. INTRODUCTION

Growth with equity has always been a central concern of policymakers. While countries in Latin America and Africa have major problems with poverty and income inequality, evidence shows that the rapid economic growth in East Asia accompanied improvements in income distribution, thereby accentuating the favourable effect of economic growth in alleviating poverty (World Bank, 1993).

The literature on the relationship between income inequality and economic growth stands divided on both theoretical and empirical grounds. Inequality is generally perceived as a necessary precondition for eventual improvement of everyone's income; this argument is formalized in the celebrated Kuznets (1955) inverted U-curve hypothesis. The implicit assumption in testing the Kuznets curve is that causality runs from growth to inequality. This assumption has been challenged on the grounds that inequality also affects growth. These views have been questioned further by the notion that there is no trade-off between growth and equity.

* School of Economics, University of Queensland, Queensland, Australia.

Studies by Ram (1988), Anand and Kanbur (1993) and Jha (1996) provide mixed evidence on the existence of a trade-off between economic growth and inequality. Research by Birdsall, Ross and Sabot (1995), Perotti (1996) and Glyfason and Zoega (2001) claims to show that equality is good for growth. On the other hand, empirical evidence provided by Barro (1999 and 2000) suggests that there is a certain threshold of income growth beyond which an economy can be expected to benefit from inequality, and this was found to be true for rich countries.¹ Thus, the current wave of research on income inequality has failed to confirm or reject the Kuznets hypothesis definitively. These days, the literature is littered with calls for careful reassessment of the relationship between economic growth and inequality in order to evaluate the specific channels through which the variables may affect one another.

In the light of the above discussion, Malaysia has been chosen as a case study to discuss growth and equity, as the country has successfully avoided the trade-off between growth and equity in an ethnically diverse society from 1970 to 1990. Interestingly, recent studies have suggested that there was an increase in income equality in the 1990s. However, in making their arguments none of these studies have sufficiently considered the policy or economic environment after 1990. Thus, the objectives of this paper are threefold. First, a closer look at Malaysia's growth-equity relationship for the 1990s is warranted given the end of Malaysia's National Development Policy from 1991 to 2000. Second, the paper examines where this relationship may be headed under the National Vision Policy 2001-2010. Third, transferable lessons from Malaysia's success are drawn for the benefit of other developing economies.

The paper is organized as follows. The next section briefly reviews Malaysia's macroeconomic performance and the third section examines trends of poverty incidence in both Peninsular Malaysia and East Malaysia.² The fourth section discusses overall income inequality patterns while the fifth section deals with interracial and interregional income inequality. The sixth section relates the observed income inequality trends to the two economic policies implemented over the periods 1970-1990 and 1991-2000, and comments on the implications of the current economic policy for the period 2001-2010. The seventh section analyses where Malaysian inequality may be heading, and the eighth section concludes by drawing

¹ Influenced by Keynes's General Theory of Employment, Interest and Money, it is believed that individual saving rates rise with the level of income. If this is so, then a redistribution of resources from the rich to the poor tends to lower the aggregate rate of saving in an economy. Through this channel, a rise in inequality tends to raise investment. In this case, more inequality would enhance economic growth, at least in a transitional sense.

² Malaysia is made up of East Malaysia comprising the states of Sabah and Sarawak, and West Malaysia (often known as Peninsular Malaysia) comprising 11 other states.

lessons for other countries from Malaysia's success in dealing with growth and equity.

II. THE MALAYSIAN ECONOMY

Malaysia is one of the fast-growing economies in the Asian and Pacific region that has done well despite the setback of the 1997/1998 financial crisis. Table 1 shows that inflation and unemployment rates have been low and Malaysia's average annual GDP growth rate was 7 per cent over the last three and a half decades. While much of this growth was driven by growth in the manufacturing sector, the World Bank (1993) noted that the rapid manufacturing growth helped to absorb women and Malays into the modern labour market and helped to alleviate poverty and inequality. The increase in real GDP per capita has been strong, growing from M\$1,932 in 1970 to M\$15,380 in 2003 (currently US\$ 1 = approximately 3.67 Malaysian ringgits).

Table 1. Selected macroeconomic indicators in the economy

	(percentage)					
	1971-1975	1976-1980	1981-1985	1986-1990	1991-1995	1996-2003
Real GDP growth	7.1	8.6	5.1	6.7	8.7	5.7
Inflation rate	2.9	2.4	3.1	1.4	3.5	2.3
Unemployment rate	6.6	6.2	5.9	7.5	3.9	3.3

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

Overall, Malaysia's growth performance has been enviable. This was not a coincidence as growth, poverty alleviation and redistribution in Malaysia from 1970 to 1990 were achieved under circumstances of interventionist policies and market coordination (Rasiah and Shari, 2001). The country's New Economic Policy, which was implemented between 1971 and 1990, had "redistribution through growth" as one of the main instruments for achieving its overriding objective of promoting national unity. The success of the Plan made it possible to achieve political stability in a multi-ethnic society, which later became a very important factor in attracting foreign direct investment (FDI) for fuelling further growth. The Plan was then succeeded by the National Development Policy 1991-2000, which retained the Plan's basic strategy of growth with equity. Today, Malaysia is spearheaded by the National Vision Policy 2001-2010, which emphasizes a more balanced and equitable participation among *Bumiputras*³ and non-*Bumiputras*.

³ This Sanskrit word literally means "sons of the soil" and generally refers to the indigenous people of Malaysia.

The interventionist State strategy of Malaysia was to help raise the living standards of Malays, also known as *Bumiputras* among the Malaysians. The proportion of Malays in the population, which was about 55 per cent in the 1960s, rose to 65.5 per cent, while that of the Chinese and Indian ethnic groups made up 25.6 per cent and 7.5 per cent respectively of the total population in 2003. By ethnicity, the incidence of poverty in Peninsular Malaysia was also highest for the *Bumiputras*, at 65 per cent in 1970. While the incidence of poverty was successfully brought down to 20.8 per cent by 1990, that of the Chinese decreased from 26 per cent to 5.7 per cent, and that of the Indians declined from 39.0 per cent to 18 per cent over the same period. The rural-urban divide is also reflective of the income disparity between non-*Bumiputras* and *Bumiputras*, as the latter group forms the majority of those who live in rural areas.

III. POVERTY

Table 2 shows the difference in poverty levels in East Malaysia and Peninsular Malaysia. As expected, Peninsular Malaysia's poverty rates in the rural areas are lower when less developed East Malaysia is included. In 1979, the rural population in East Malaysia made up 62.3 per cent of the total population, and 80 per cent of the poor lived in rural areas. In 2003, the rural population proportion declined to 37.5 per cent.

Table 2. Incidence of poverty

(percentage)

Year	Peninsular Malaysia				East Malaysia			
	Aggregate	Rural	Urban	No. of poor households (thousands)	Aggregate	Rural	Urban	No. of poor households (thousands)
1970	49.3	58.7	21.3	791.8	52.4	n.a.	n.a.	1 000
1976	39.4	47.8	17.9	764.4	42.4	50.9	18.7	975.8
1984	18.4	24.7	8.2	483.3	20.7	27.3	8.5	649.4
1990	15.0	19.3	7.3	448.9	17.1	21.8	7.5	619.4
1993	10.5	14.9	4.4	325.3	13.4	18.6	5.3	517.2
1995	9.1	14.1	4.1	329.5	8.7	14.9	3.6	417.2
1997	n.a.	n.a.	n.a.	n.a.	6.1	10.9	2.1	332.4
1999	n.a.	n.a.	n.a.	n.a.	7.5	12.4	3.4	409.3
2000	n.a.	n.a.	n.a.	n.a.	5.5	10.3	2.2	253.4
2002	n.a.	n.a.	n.a.	n.a.	5.1	11.4	2.0	267.9

Source: Malaysia (1981, 1986, 1991a, 1991b, 1996, 2001a and 2003).

Note: n.a. means not available.

Table 2 also shows that the aggregate poverty incidence has declined uninterrupted in the period 1970-1997. In fact, the reduction in the incidence of poverty to 15 per cent in Peninsular Malaysia by the end of 1990 exceeded the target of 17 per cent set when the New Economic Policy was initiated.⁴ The targets for the urban and rural groups in Peninsular Malaysia were also achieved. The number of poor households has consistently decreased over the period 1970-1997, with the largest decline occurring in the period 1976-1984, showing the first signs of success of the Plan's initiatives.

There has however been a slight increase in the proportion of households below the poverty line for Malaysia, from 6.8 per cent to 8.1 per cent over the period 1997-1999. The risk of becoming poor after the financial crisis is expected to be higher for households in urban areas, as the rural poor largely are not employed in the crisis-affected sectors of the economy. The thrust of the Seventh Malaysian Plan 1996-2000, to reduce poverty in Malaysia to 5.5 per cent by 2000, was met but that of the Eighth Malaysian Plan 2001-2005, to reduce the aggregate incidence of poverty to 0.5 per cent by 2005, would seem a little ambitious.

Although the incidence of poverty has decreased over time, rural poverty remains very much higher than its urban equivalent. Unlike the urban areas where occupational employment is wide-ranging in various sectors and hence income earned can vary substantially, the rural sector is mainly agricultural in nature. In general, urban poverty decreased more rapidly than rural poverty, and this contributed more to a fall in overall poverty. As poverty is mainly a rural problem, the development of the agricultural sector was given high priority in order to alleviate poverty. Table 3 shows the expenditure allocated to agricultural and rural development with a variety of programmes undertaken by the Government to raise rural income, as set out in the Malaysian Plans over time. In *in situ*, or area development, the idea was to overcome problems of low productivity and poverty by providing basic physical and economic infrastructure as well as social amenities.

It is hoped that the schemes set out in the Eighth Malaysian Plan for rural development would bear more fruit in the future. To increase the participation of the rural population in income-generating activities, the scope for credit facilities for rural industries is to be expanded to include tourism and agriculture, as well as the services sector. The National Vision Policy states that for *in situ* development, rehabilitation and consolidation of land is still given priority, and the replanting of old commercial crops with new higher-yielding clones and the use of better planting

⁴ The New Economic Policy was explicit in its concern for Peninsular Malaysia, as Sabah and Sarawak's ethnic problems were quite different and less pressing than that of Peninsular Malaysia.

Table 3. Expenditure allocation for agricultural and rural development, 1966-2005

Programmes	MP1 (1966-1970) (M\$) (%)	MP2 (1971-1975) (M\$) (%)	MP3 (1976-1980) (M\$) (%)	MP4 (1981-1985) (M\$) (%)	MP5 (1986-1990) (M\$) (%)	MP6 (1991-1995) (M\$) (%)	MP7 (1996-2000) (M\$) (%)	MP8 (2001-2005) (M\$) (%)							
1. Assisting traditional farmers/ in situ development:	557.4	420.0	5.7	1 155.0	5.5	3 033.6	5.3	2 688.2	7.6	3 864.2	7.1	2 941.9	3.0	2 265.1	2.1
Integrated agricultural development programmes	-	-	-	198.2	0.9	892.0	1.9	1 021.8	2.9	n.a.	-	n.a.	-	n.a.	-
Drainage and irrigation	342.6	8.1	217.8	3.0	554.8	2.6	860.3	1.9	200.3	0.6	n.a.	-	n.a.	-	n.a.
Replanting	188.5	4.4	177.7	2.4	241.8	1.2	386.5	0.8	581.2	1.6	844.6	1.5	n.a.	-	n.a.
Rehabilitation	17.6	0.4	24.5	0.3	54.7	0.3	64.5	0.2	812.7	2.3	n.a.	-	n.a.	-	n.a.
Rural flood control and coastal erosion	-	-	-	-	-	-	-	-	72.2	0.2	n.a.	-	n.a.	-	n.a.
Other programmes	8.7	0.2	-	-	105.5	0.5	189.4	0.5	-	-	n.a.	-	n.a.	-	n.a.
2. Land and regional development:	363.6	8.6	988.2	13.3	2 744.6	13.0	3 979.4	8.6	2 774.6	7.9	2 114.5	3.9	1 282.9	1.3	844.3
New land development	273.8	6.5	729.4	9.8	1 925.5	9.1	2 513.1	5.4	2 117.5	6.0	1 184.0	2.2	475.9	0.5	274.2
Regional development and other land schemes	89.8	2.1	258.8	3.5	819.1	3.9	1 466.3	3.2	657.1	1.9	930.5	1.7	807.0	0.8	570.1
3. Forestry	14.9	0.4	8.9	0.1	25.6	0.1	63.0	0.1	120.8	0.3	18.4	0.1	143.8	0.1	225.2
4. Livestock	18.5	0.4	57.0	0.8	127.2	0.6	241.0	0.5	130.9	0.4	191.4	0.4	176.3	0.2	127.5
5. Fisheries	9.0	0.2	32.8	0.4	105.8	0.5	434.6	0.9	264.4	0.8	370.0	0.7	465.3	0.5	414.3
6. Support services: Input subsidy	31.2	0.7	-	-	101.8	0.5	500.0	1.1	396.8	1.1	1 282.5	2.4	354.3	0.4	719.0
Agricultural credit and marketing	29.6	0.7	139.0	1.9	269.7	1.3	761.3	1.7	586.1	1.7	n.a.	-	n.a.	-	n.a.
Research and extension	32.7	0.8	64.8	0.9	90.3	0.4	172.9	0.4	28.9	0.1	n.a.	-	n.a.	-	n.a.
7. Other programmes under the Ministry of Agriculture	57.2	1.4	83.5	1.1	1.0	0.0	-	-	329.3	0.9	236.2	0.4	n.a.	-	n.a.
Total agriculture and rural development expenditure	1 114.1	26.3	1 793.5	24.2	4 666.2	22.0	8 608.6	18.6	7 325.0	20.8	8 215.2	15.0	8 139.3	8.2	7 900.0
Total planned development expenditure	4 242.0	100	7 415.1	100	21 201.9	100	46 320	100	35 300	100	54 705	100	99 037	100	110 000

Sources: Malaysia (1971, 1976, 1981, 1986, 1991a, 1996 and 2001a).

Note: MP = Malaysian Plan; n.a. = not available.

techniques are being undertaken. As set out in the Third Outline Perspective Plan for 2001-2010, the main strategy for poverty eradication was providing employment opportunities in higher-paying jobs. Since the poor are engaged largely in agriculture, they are encouraged to be involved in modern farming and non-farming or off-farm activities. In better targeting benefits for the poor, a more concerted effort needs to be made towards reducing poverty across Malaysia's states.

IV. OVERALL INCOME INEQUALITY

Although the relevant data for studying income inequality are those concerning wealth, as is the case in many other countries, data on wealth are non-existent in Malaysia; hence, income is used as a proxy. Furthermore, inequality data and Gini coefficients for Malaysia are based on income and not expenditure data. Table 4 shows that income inequality increased for all categories until 1970, and table 5 shows a decline in the trend of Gini coefficients from 1970 to 1990.

Table 4. Gini coefficients, 1957/58-1970

	1957/58 (Adjusted)	1967/68 (Ford Survey)	1970	1970 ^a
Area				
Peninsular Malaysia	0.412	0.444	0.502	0.5129
Rural	0.374	0.399	0.463	0.4689
Urban	0.429	0.447	0.494	0.5073
Race				
Malays	0.342	0.400	0.466	0.4664
Chinese	0.374	0.391	0.455	0.4656
Indians	0.347	0.403	0.463	0.4722

Source: Snodgrass (1980).

^a Data are from Anand (1983).

It can be seen in table 5 that, although the New Economic Policy was first implemented in 1971, its impact was not felt in Peninsular Malaysia during the early years. Income inequality persisted until the mid-1970s, but undoubtedly there has been a decline since then to 1990. For Malaysia too, there was a fall in the Gini ratio from 1970 to 1990. In general, the Gini coefficients in Peninsular Malaysia can be expected to be higher than that of East Malaysia, as the less developed states of Sabah and Sarawak have a higher proportion of rural households than urban, and income dispersion in rural areas is more even than in urban areas.

Table 5. Gini coefficients, 1970-2002

Year	Peninsular Malaysia	East Malaysia	
1970	0.513	0.501	
1976	0.529		
1979	0.508	0.493	
1984	0.480		
1987	0.456		
1990	0.445	0.446 ^a	0.442 ^c
1993		0.459 ^b	
1995		0.464 ^a	0.456 ^c
1997		0.470 ^b	
1999		0.443 ^c	
2002		0.461 ^c	

Source: Anand (1983), Malaysia (1981, 1986 and 1991a).

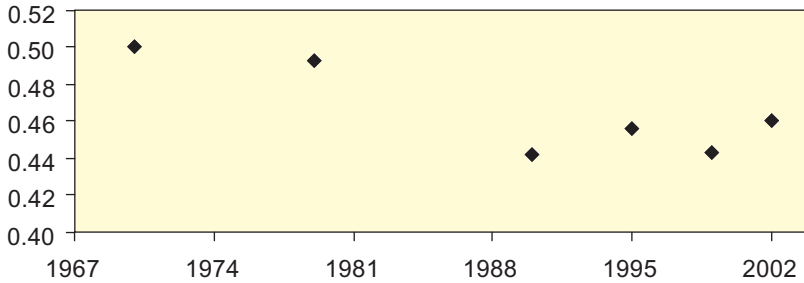
^a Malaysia (1996).

^b Malaysia (1999).

^c Malaysia (2001a, 2001b and 2003).

Interestingly, the reported Gini coefficients since 1990, shown in table 5, are quite different depending on which official publication is used, but the reported trend could be generalized as indicating an increase from 1990 to 1995 and possibly to 1997 and 1998 as a result of the previously mentioned financial crisis, but income inequality not only decreased in 1999 but it also almost reached the same level as that in 1990. Thus, the concern raised by many studies, such as those by Shari (2000), Yusof (2001) and Rasiah and Shari (2001), on the seemingly U-turn direction of the Gini ratio since the 1990s, is not borne out by the evidence shown in figure 1. One reason for the previous studies' claim stems from their use of different publications (as noted in table 5) to report the Gini ratios. While there was some volatility and structural adjustment⁵ taking place in the economy during the decade of the 1990s, income inequality was still on a downward trend until 1999, as seen in figure 1. However, there has been an increase in the Gini coefficient from 0.443 in 1999 to 0.461 in 2002. While this is a worry, it is too early to tell if this trend will continue or is merely a reflection of the recovery from the financial crisis.

⁵ This refers to coping with significant flows of FDI, the increased importance of the electronics and the information and communication technology industries, the establishment of the Multimedia Super Corridor Programme and the greater role of private entrepreneurship.

Figure 1. Gini ratios for Malaysia, 1970-2002

Source: Anand (1983), Malaysia (1981, 1986 and 1991a).

Although the information on income inequality relating to the existing data points does not allow us to establish a direct statistical empirical link between growth and income inequality, it is clear that there has been little trade-off between growth and income inequality since the mid-1970s.⁶

It is however unfortunate that no data are available on the income inequality trend in Peninsular Malaysia after 1990. It is not exactly clear why the Malaysian authorities have since then shifted their focus to East Malaysia. One reason could be that the New Economic Policy, launched in 1971, set targets only for Peninsular Malaysia that were to be attained by 1990. Thus, further reporting on Peninsular Malaysia was deemed unnecessary. Another likely reason could be that the shift was to address the neglect of East Malaysia and exploit the growing potential by consciously developing and modernizing the states of Sabah and Sarawak. Even if these reasons are valid, they are unsatisfactory, as more could be gained by reporting for both Peninsular Malaysia and East Malaysia.

It is further suspected that there may be political reasons for not publishing the Gini coefficients for Peninsular Malaysia, or not reporting the possibly widened Gini ratios by ethnic group after 1990. One such motive may have been to highlight the success of the New Economic Policy to gain the confidence of the *Bumiputras* and to enable the smooth handover of power within the political party in October 2003. On the other hand, an important economic reason could be the deliberate move of the Government to gradually steer the economy away from strong redistributive policies. The move from the New Economic Policy to the National

⁶ To date, the Kuznet's hypothesis for Malaysia has been tested using cross-sectional data by Anand (1983) and Hashim (1997), and time series data by Perumal (1989). While there are mixed conclusions, none of these studies had more than 10 degrees of freedom to validate their findings statistically.

Development Policy and then to the National Vision Policy has already been criticized as being less aggressive in terms of redistributive plans. This shift in policy direction reflects the Government's decision to allow market forces to play a greater role so that economic growth is not hampered by unnecessary intervention.

V. INTERRACIAL AND INTERREGIONAL INCOME INEQUALITY

Here, a closer look is taken at ethnic inequality as well as rural-urban inequality. Interethnic economic imbalances improved with a fall in the income disparity ratios (which is the ratio of the mean income of one group to the other) between *Bumiputras* and non-*Bumiputras* over the period 1970-1987, as seen in the table below.

Table 6. Income disparity ratios

<i>Peninsular Malaysia</i>	<i>Bumiputras- Chinese</i>	<i>Bumiputras- Indians</i>	<i>Rural-Urban</i>
1970	1 : 2.29	1 : 1.76	1 : 2.14
1976	1 : 2.28	1 : 1.57	1 : 2.12
1979	1 : 1.91	1 : 1.54	1 : 1.90
1984	1 : 1.76	1 : 1.28	1 : 1.87
1987	1 : 1.65	1 : 1.25	1 : 1.72
1990	1 : 1.70	1 : 1.29	1 : 1.73
<i>East Malaysia</i>			
1990	1 : 1.74	1 : 1.28	1 : 1.71
1995	1 : 1.80	1 : 1.33	1 : 1.99
1997	1 : 1.83	1 : 1.42	1 : 1.97
1999	1 : 1.74	1 : 1.36	1 : 1.81
2002	1 : 1.80	1 : 1.28	1 : 2.11

Source: Data were obtained from Shari (2000), Malaysia (1996 and 2003) and Department of Statistics (2002).

Table 6 also shows that the mean income is highest for the Chinese followed by the Indians. The increase in interethnic income disparity trends from 1990 to 1995 is not surprising as the inclusion of the states of Sabah and Sarawak can be expected to lower the mean income of *Bumiputras* far more than that of the other races. However, it is unclear if the fall in the ratio from 1995 to 1999 shows any real improvement in ethnic imbalances, as Malaysia was then in the midst of the 1997/1998 financial crisis. Since the decade of the 1990s, Malaysia has been undergoing a period of adjustment and this transition in the form of structural

changes in the economy, where there is a greater shift towards services and higher value added manufacturing activities, may have caused income imbalances that favoured some ethnic groups more than others. Thus, although all income groups shared in the ample opportunities springing from the rapid annual increase in GDP from 1990 to 1999, they did not do this equally, as Chinese and Indian household incomes rose more than those of *Bumiputras*. In general, there is no clear trend in income disparity ratios since 1990. With the rural-urban income disparity, table 6 shows a fall until 1990 and an increase from 1995 to 1999, after which no discerning trend emerges.

Table 7 shows that income inequality declined within the three ethnic groups in line with one of the aims of the New Economic Policy. The declines within each ethnic group however varied and the non-*Bumiputras* experienced greater reduction in income inequality than the *Bumiputras*. With rural households, income inequality declined faster than urban inequality. As no data on Peninsular Malaysia were available beyond 1990, further analysis is not possible.

Table 7. Interracial and interregional Gini ratios for Peninsular Malaysia

	<i>Bumiputras</i>	<i>Chinese</i>	<i>Indians</i>	<i>Rural</i>	<i>Urban</i>
1970	0.466	0.466	0.473	0.469	0.503
1976	0.506	0.541	0.509	0.500	0.512
1979	0.488	0.470	0.460	0.482	0.501
1984	0.469	0.452	0.417	0.444	0.466
1987	0.447	0.428	0.402	0.427	0.499
1990	0.428	0.400	0.394	0.409	0.445

Source: Shari (2000).

While reducing income disparity between races is one of way of reducing overall income inequality, another (possibly easier and politically more acceptable) way is to address the urban-rural divide because of the disproportionate presence of Malays in rural areas. Although regional development was mentioned as early as the mid-1970s in the Third Malaysian Plan 1976-1980, efforts to implement the plans have been rather slow and little success has been achieved, as the main focus was on the country's more developed states. The table below highlights the urban-rural differences.

Table 8. Some data on Malaysian states

State	Population (thousand) in 2000	Urbanization rate in 2000 (percentage)	Poverty incidence	
			1995	2002
More developed				
Johor	2 721.9	63.9	3.1	1.8
Melaka	634.1	67.3	5.3	2.7
Negeri Sembilan	858.9	55.0	4.9	2.2
Perak	2 109.7	59.5	9.1	7.9
Pulau Pinang	1 307.6	79.5	4.0	1.4
Selangor	4 175.0	88.3	2.2	1.1
Less developed				
Kedah	1 652.0	38.7	12.2	10.7
Kelantan	1 314.9	33.5	22.9	12.4
Pahang	1 290.0	42.1	6.8	3.8
Perlis	204.5	33.8	11.8	10.1
Sabah	2 656.4	49.1	22.4	16.0
Sarawak	2 071.8	47.9	10.0	5.8
Terengganu	899.0	49.4	23.4	10.7
East Malaysia	23 266.0	61.8	8.7	5.1

Source: Malaysia (2001a and 2003).

The table shows that, except for Pahang, all other less developed Malaysian states have a relatively high incidence of poverty. The situation is not to be taken lightly in view of the fact that 44 per cent of the population lives in these less developed states and they are predominantly Malays. Among the less developed states, the relatively higher urbanization rates of Sabah, Sarawak and Terengganu reflect some potential to provide employment in expanding urban areas and to help reduce poverty. This may be one of the reasons for the Government to turn its attention to setting targets for East Malaysia rather than limiting its focus to Peninsular Malaysia as in the past. Currently, agriculture and mining are the economic mainstays for the less developed states but the Government has plans for infrastructural development and for broadening the manufacturing base in these states. This can be expected to generate positive spillover effects, but there is the danger that the gains will accrue to the possibly more enterprising upper-income groups, such as Chinese businessmen, when these relatively backward states are developed. Overall, it is noteworthy that all states have experienced a decline in the incidence of poverty from 1995 to 2002.

VI. EFFECT OF REDISTRIBUTIVE POLICIES ON INCOME INEQUALITY

The Success of the National Economic Policy in the period 1971-1990

The National Economic Policy has been hailed as a successful model for redistributive policies. There is consensus among studies such as those by Lucas and Verry (1996), Hashim (1997) and Rasiah and Shari (2001) as to why and how income inequality was reduced in this period. Key distributional policies and their effects on income distribution and other aspects of the economy during this period are reviewed by drawing from these studies.

The urgency of the Malaysian inequality problem was the result of the country's worst racial riots, experienced on 13 May 1969. They resulted in a fundamental shift in public policies, with the announcement of the New Economic Policy in order to achieve racial economic balance. This paved the way for an interventionist State strategy to create a Malay commercial and industrial community.

Alongside the implementation of the New Economic Policy in 1971, there was a move away from import-substitution to export-orientation in Malaysia's economic restructuring efforts. With the establishment of free trade zones in 1972 and the creation of a liberalized foreign investment environment in the form of the Promotion of Investment Act passed in 1986, Malaysia was poised for increased growth. The Government took the initiative to lead the economy and State expansion took the form of numerous public enterprises in manufacturing, commerce and banking. Public sector employment growth was strongest in the 1970-1981 period (World Bank, 1993). The privatization policy launched in 1983 also allowed *Bumiputras* to extend their participation in business. Under the Industrial Co-ordination Act, foreign investors were influenced to comply with New Economic Policy employment and ownership targets for *Bumiputras* through the granting of specific fiscal incentives.

The 1980s saw a strengthening of existing bodies and the establishment of new public enterprises and trust agencies, which provided a range of financial, educational and training services to *Bumiputras*. Institutions such as the Majlis Amanah Rakyat, Bank Bumiputra Malaysia Berhad and Perbadanan Nasional were given wider roles and access to capital to raise the position of *Bumiputras*. While statutory bodies such as the National Corporation and National Equity Corporation were used to implement and promote *Bumiputra* ownership in leading sectors, the Urban Development Authority on a national level dealt with urban sectors ranging from property development to retailing and other services.

There was also direct intervention with the use of employment quotas for getting *Bumiputras* into non-agricultural jobs whereby written proficiency in *Bahasa Melayu*⁷ was imposed in order to provide an advantage for the *Bumiputras*. Targets set for the ethnic composition of employment in each major sector were also successfully met by 1990. In tertiary education, the importance of restructuring has been explicit in the form of a quota which, in the early days of the New Economic Policy, reserved 75 per cent of places for *Bumiputras*, though the quota was later lowered to 55 per cent. This saw the proportion of *Bumiputra* students at public universities increase from 12 per cent in 1970 to about 70 per cent in 1995. Obviously, the opportunities that this afforded, initially in public service and more recently in industry, have aided those *Bumiputras* fortunate enough to attend university.

The National Development Policy in the period 1991-2000

The National Development Policy which superseded the New Economic Policy in 1991 and was carried through until 2000, has been seen as less aggressive in terms of income distribution. Unlike the Plan, no time frame was set for achieving distributive targets in the associated five-year development plans of the National Development Policy. While there was still emphasis on the strategy of growth with equity, the National Development Policy relied on the private sector to be responsive and proactive in attaining these objectives. This is in line with the Government's move to ride on the waves of globalization and liberalization. While this meant that there would be increased economic opportunities for non-*Bumiputras*, one cannot rule out the positive outcome of the development of more genuine and capable *Bumiputra* businessmen and entrepreneurs, given the environment in Malaysia.

Nevertheless, the privatization efforts of the Government remained an important means of enhancing *Bumiputra* participation in the corporate sector. The Third Outline Perspective Plan 2001-2010 reports that, as of April 2000, the Government privatized a total of 180 companies, of which 109 were managed and controlled by *Bumiputras*. Also, while the New Economic Policy concentrated and succeeded in increasing *Bumiputra* participation in the non-agricultural sectors, under the National Development Policy, the emphasis was on raising the quality of *Bumiputra* participation in the corporate sector. Table 9 shows the employment by ethnic group in various sectors of the economy.

⁷ *Bahasa Melayu*, which is the mother tongue of the *Bumiputras*, was adopted as the medium of instruction in Malaysia from the 1970s.

**Table 9. Employment by sector and ethnic group
(percentage of total employed)**

Year	Group ^a	Agriculture, forestry and fishing	Mining and quarrying	Manu- facturing	Utilities	Con- struction	Transport and commu- nication	Wholesale and retail	Finance, insurance, real estate	Government and other services
1970	Bumi	68.0	25.0 ^b	29.0	48.0	22.0	43.0	24.0	n.a.	n.a.
	Chinese	21.0	66.0	65.0	18.0	72.0	40.0	65.0	n.a.	n.a.
	Indians	10.0	8.0	5.0	33.0	6.0	17.0	11.0	n.a.	n.a.
1980	Bumi	73.1	34.0	40.9	67.1	39.1	50.6	35.2	36.9	59.4
	Chinese	16.4	54.7	50.4	9.7	53.4	30.2	58.3	55.3	29.2
	Indians	9.7	10.6	8.0	22.6	6.4	13.9	7.4	7.4	10.1
1985	Bumi	75.0	51.9	45.1	70.7	42.2	51.5	36.1	42.5	65.7
	Chinese	16.1	33.1	43.3	13.9	51.1	34.4	56.0	46.9	24.7
	Indians	8.3	12.8	11.0	15.1	5.9	13.4	7.1	9.7	8.9
	Others	0.7	2.2	0.6	0.3	0.8	0.6	0.8	0.9	0.7
1990	Bumi	76.4	48.8	50.3	69.8	43.0	54.1	38.2	41.1	66.4
	Chinese	16.1	38.9	36.9	12.9	49.9	32.4	54.1	47.4	24.9
	Indians	6.7	10.8	12.2	16.6	6.2	12.8	6.9	10.3	8.1
	Others	0.8	1.5	0.6	0.7	0.9	0.7	0.8	1.2	0.6
1995	Bumi	76.1	57.5	49.8	72.1	37.4	53.2	36.5	45.1	64.4
	Chinese	11.7	22.0	30.3	10.4	41.1	29.4	50.0	42.3	21.2
	Indians	6.0	10.6	11.3	11.1	4.7	11.7	6.1	9.3	6.8
	Others	0.8	1.5	0.5	0.2	0.9	0.4	0.9	1.0	1.0
2000	Bumi	75.8	63.2	53.9	69.9	45.2	57.3	42.4	43.4	66.4
	Chinese	16.9	22.9	33.1	12.7	47.8	28.2	50.2	45.2	25.6
	Indians	6.7	11.2	12.5	17.2	6.1	14.1	6.4	10.6	7.7
	Others	0.6	2.7	0.5	0.2	0.9	0.4	1.0	0.8	0.3
2003	Bumi	74.9	63.3	54.5	72.3	43.9	56.2	40.5	45.8	69.5
	Chinese	13.5	22.8	32.6	11.9	45.7	28.7	51.3	41.7	22.2
	Indians	7.4	11.0	12.4	11.8	5.4	12.1	7.1	10.0	7.3
	Others	4.2	2.9	0.5	4.0	5.0	3.0	1.1	2.5	1.0

Source: Malaysia (1976, 1991a, 1991b, 2001a and 2003).

^a Bumi refers to *Bumiputras*.

^b This figure is only for the mining industry and is unlike that for all other years.

It can be seen that, in the agricultural sector, the proportion of *Bumiputras* employed did not decline in view of the fact that it was 68 per cent in 1970, 76.4 per cent in 1990 and 75 per cent in 2003; in manufacturing, the increase in *Bumiputra* participation was quite insignificant. While there was some increase in *Bumiputra* participation in the transport, finance, insurance and real estate sectors, as well as in the wholesale and retail sectors from 1990 to 2000, Chinese domination in most sectors has declined, except in the wholesale and retail sector. The proportion of Indians involved in most of the sectors has also declined over time.

**Table 10. Employment by occupation and ethnic group
(percentage of total employed)**

Year	Group ^a	Professional and technical	Teachers and nurses	Administrative and managerial	Clerical workers	Sales workers	Service workers	Agriculture workers	Production workers
1970	Bumi	47.2	n.a.	22.4	33.4	23.9	42.9	67.8	31.3
	Chinese	37.7	n.a.	65.7	51.0	64.7	62.5	20.8	59.9
	Indians	12.7	n.a.	7.5	14.3	11.0	13.4	9.6	8.6
1980	Bumi	53.7	64.5	28.7	52.4	32.1	54.0	69.5	43.7
	Chinese	32.6	28.7	62.5	36.6	60.1	33.7	18.1	44.6
	Indians	11.9	6.3	6.1	10.4	7.6	11.5	11.4	11.3
1985	Bumi	58.8	64.2	34.8	54.1	33.2	61.6	75.9	47.3
	Chinese	30.9	28.9	57.5	37.8	59.2	27.8	15.2	41.8
	Indians	8.7	6.4	5.1	7.6	6.8	10.1	8.2	10.5
	Others	1.6	0.5	2.6	0.5	0.8	0.5	0.7	0.4
1990	Bumi	60.3	68.1	33.3	54.9	36.0	61.5	76.4	48.5
	Chinese	30.8	25.1	58.7	36.9	56.5	27.0	15.8	40.4
	Indians	7.7	6.3	5.3	7.8	6.5	10.6	7.0	10.7
	Others	1.2	0.5	2.7	0.4	1.0	0.9	0.8	0.4
1995	Bumi	61.7	71.1	34.2	55.6	39.2	66.5	76.0	49.7
	Chinese	30.1	22.2	57.6	36.5	53.2	25.4	16.0	38.8
	Indians	7.3	6.2	5.4	7.6	6.3	10.8	7.2	11.1
	Others	0.9	0.5	2.8	0.3	1.2	0.3	0.8	0.4
2000	Bumi	63.2	73.1	34.7	56.2	40.2	64.3	75.3	50.6
	Chinese	29.3	20.3	57.0	34.3	52.4	24.1	17.0	37.5
	Indians	6.8	6.1	5.5	9.3	6.4	10.8	7.0	11.5
	Others	0.7	0.5	2.8	0.2	1.0	0.8	0.7	0.4

Source: Malaysia (1991a, 1991b and 2001a).

Note: Data for 2003 were published using different employment categories. It was not possible to reconcile them with the above categories, hence, they were omitted.

^a Bumi refers to *Bumiputras*.

Large imbalances in the racial pattern of occupational employment in the 1970s was first noted by Anand (1983). For 1970, Anand found that *Bumiputras* constituted 85 per cent of all farmers but only 28 per cent of all sales workers, and in the administrative and managerial, clerical and related, and production worker categories, the *Bumiputras* accounted for little more than 30 per cent of the workforce. In contrast, the Chinese constituted less than 13 per cent of farmers but some 60 per cent of sales workers, 57 per cent of production workers and 46 per cent of the administrative and managerial, clerical and related personnel. Table 10 shows that there has been an increase in *Bumiputra* participation in all occupational categories over that time except in the number of agricultural workers. The most notable increase of about 10 per cent from 1985 to 2000 comes from teachers and nurses, as there has been more government control in these jobs given the large number of government-owned schools and hospitals in Malaysia.

There have also been increases in the *Bumiputra* occupational share in the categories of sales workers, i.e., a 7 per cent and a 5 per cent increase in the professional and technical workers categories respectively. However, the smallest proportion of *Bumiputras*, at 34.7 per cent in 2000, was seen in the administrative and managerial positions, which remain dominated by the Chinese. The low make-up of *Bumiputras* in this category is the least successful aspect of restructuring of the society in the decade of the 1990s (Malaysia, 2001a).

Another unsuccessful policy has been the capital and assets accumulation policy of encouraging and regulating the private sector to ensure that *Bumiputras* held at least 30 per cent of the share capital of limited companies. Initiated under the New Economic Policy in 1971, this policy was continued under the National Development Policy. While there was a marked increase in the share from 2.4 per cent in 1970 to the highest level of 20.6 per cent in 1995, the target of 30 per cent has yet to be achieved, as shown in table 11. In fact, there has been a decline in the *Bumiputra share* since 1995.

Table 11. Corporate equity ownership

(percentage)

Year	<i>Bumiputras</i>	<i>Non-Bumiputras</i>	<i>Foreign</i>
1970	2.4	32.3	63.4
1975	9.2	37.5	53.3
1980	12.5	34.3	43.0
1985	19.1	35.9	26.0
1990	20.3	46.2	25.1
1995	20.6	43.3	27.7
1999	19.1	40.3	32.7
2000	18.9	41.3	31.3
2002	18.7	43.2	28.9

Source: Malaysia (1991a, 2001a and 2003).

Note: The figures do not add to 100 as the information on nominee companies is not included.

The highest proportion of *Bumiputra* equity ownership was found to be between 25 per cent and 29 per cent in the agricultural, construction and transportation sectors; that in the manufacturing sector remained low at 10.5 per cent in 2002. The share of foreign equity on the other hand increased in the 1990s, reflecting the significant inflow of FDI. In line with the efforts to revitalize the economy after the 1997/1998 financial crisis, there was a relaxation of regulations

on foreign equity ownership. As a result, foreign equity ownership in the manufacturing sector was highest at 56.3 per cent in 1999.

Studies such as Shari (2000), Yusof (2001), and Rasiah and Shari (2001), which have voiced concern over the rising trend of income inequality, point to the possible cause of this as being a government policy reversal towards liberalization, deregulation and privatization since the late 1980s. However, in the era of globalization, Malaysia has little choice but to allow the more responsive and less bureaucratic private sector to take up the challenges of operating in a more market-friendly and competitive global environment. This is a timely move on the part of the Government, as income inequality is a less politically sensitive issue than it once was due to the remarkable increase in living standards experienced in the economy.

There have been claims by Ragayah, Ismail and Shari (2000) and Shari (2001) that increases in capital intensity and manufacturing employment, resulting in a wide dispersion of wages and salaries, explain the resurgence of income inequality in Malaysia. While it is true that wage differentials in Malaysia have grown as the demand for skilled labour outpaces the demand for unskilled workers (Rasiah and Osman-Rani, 1995; World Employment Report, 1998) and have been further exacerbated by the entry of unskilled migrants, the assertion that this situation has caused income inequality is not supported by any analysis partly due to the lack of data, as noted by the studies. Importantly, their point is still an unconvincing concern in the long run. Wage stretching simply reflects low elasticity of skilled workers in the short run. This is a temporary phenomenon that takes place in the interval before an accommodating supply-side response is guaranteed. The long-run supply elasticity of skilled workers would be much greater and will eventually reverse the initial wage stretching.

The increases in capital intensity and manufacturing employment are inevitable for an economy such as Malaysia's, which has been attracting FDI since the 1980s. For the development/modernization hypothesis, it is believed that, even if FDI initially stimulates growth in only some leading or favoured sectors, the growth in these sectors could in the long run facilitate more even income distribution via positive spillover effects. While Athukorala and Menon (1997) show how FDI-related export-led industrialization has generated employment opportunities and reduced income inequality, Mahadevan (2002) notes that FDI in manufacturing is currently at a low level on the technology ladder. This means that the concern about wage levels being stretched if demand for skilled workers outpaces the supply may be overstated. Furthermore, FDI inflows into Malaysia have slowed down from an annual increase of 78 per cent in the period 1988-1991, to 20 per

cent in the period 1990-1995, and to 7 per cent in the period 1995-2000.⁸ This, together with the financial crisis of 1997/1998, has blurred the effect of FDI on income distribution.

Even if FDI increased income inequality, for Malaysia today, FDI is a necessary evil to gain access to better technology and remain competitive in the global market. However, if FDI is aimed at higher value added manufacturing activities, then wage levels can be stretched if the human resources development policy does not sufficiently ensure that there are enough high-skilled workers, and this would widen the earnings differential. In order to reduce the earnings differential, the Government has to increase its budget allocation for education and training at the macro level while firms should provide both pre-entry and in-service training for their workers. Thus, if policies related to human resources development can be devised appropriately and implemented effectively, the purported increase in income inequality due to FDI can be checked.

In this regard, the efforts of the Government of Malaysia so far are in the right direction. The government development allocation for education and training has been consistently rising from M\$5,812 for the period 1986-1990 to M\$22,660 for the period 2001-2005. In terms of higher education, while enrolment for diplomas and degrees has increased about 2.5 times from 1995 to 2003, the proportion of those in the work force with a tertiary education increased from 7.2 per cent in 1987 to 17.1 per cent in 2003. Malaysia (2001b) projects that the latter figure would rise to 35 per cent in 2010 and this would be met by an average annual growth rate of about 6 per cent over the period 2001-2010 in the categories of administrative and managerial workers and professional and technical workers.

However, one view of FDI and international openness is that it benefits most of the domestic residents who are already well-off in the sense that rich groups are better able than others to take advantage of the opportunities offered by trade expansion. While trade liberalization has distributional consequences, that is, there are "winners" and "losers" in the short run, it is also true to say that not all losers may come disproportionately from the disadvantaged group. To the extent that trade openness raises national income, it strengthens the fiscal ability of a society to provide safety nets or consider options to help the *Bumiputras* directly.

⁸ These figures were calculated using data from *World Investment Reports* published by UNCTAD.

The National Vision Policy in the period 2001-2010

The National Vision Policy is similar to the National Development Policy without being less or more aggressive in its redistribution stance. While the strategy of reduced State involvement was adopted under the National Development Policy, with the National Vision Policy, the Government has indicated areas in which it will address possible economic imbalances arising from its market-oriented approach. For instance, the Third Outline Perspective Plan for 2001-2010 has plans to:

- (a) Be target-specific in their poverty eradication programmes in remote areas and among *Bumiputra* minorities in Sabah and Sarawak;
- (b) Promote a conducive environment for *Bumiputras* to face the challenges of globalization by facilitating and assisting in the promotion of their products overseas and enabling *Bumiputra* entrepreneurs to venture into niche international markets;
- (c) Promote effective participation of *Bumiputras* and other disadvantaged groups in a knowledge-based economy with a *Bumiputra* information and communications technologies agenda to obtain recognition as reliable and capable market players;
- (d) Retrain (unemployed) social science *Bumiputra* graduates with market-related knowledge and skills to benefit from employment opportunities in other sectors of the economy.

In addition, the National Vision Policy would continue achieving *Bumiputra* equity ownership of at least 30 per cent by 2010 without resorting to microrestructuring of existing ventures. Here, the Government is open about its limited intervention in this particular goal, probably realizing that this may never happen in view of the fact that it has been unsuccessful since 1970. There is also continued emphasis on enhancing regional balance through the rapid development of the less developed states. Here, a gradual approach to developing the less developed states should be encouraged, as too rapid an increase in the urbanization rate without appropriate evenness in income dispersion (by means of sustained employment generation) would lead to greater overall income inequality.

Lastly, the National Vision Policy intends to have *Bumiputra* participation in leading sectors reflect the ethnic composition of the population. This has an advantage in that the racial employment targets would be implemented in relation to flows rather than stocks, as the racial allocation of new labour force entrants would be in proportion to the population ratios of the racial groups. In terms of *Bumiputra* employment in major sectors, table 9 shows that the agricultural and

utilities sectors could do with a decrease in *Bumiputra* participation. While some improvement has taken place in *Bumiputra* participation in manufacturing and non-government services, the racial make-up of 66 per cent *Bumiputras* (in line with the ethnic composition of the population) has yet to be achieved in these sectors.

However, employment restructuring by sector alone will help only to narrow income differences between the races but not to eliminate them. The occupational structure of employment within each sector too has to be balanced racially so that the income differences between the races will be reduced more effectively. Table 10 shows that *Bumiputra* participation improved in all occupational categories but there is a dire lack of *Bumiputras* in the administrative and managerial category. Production, sales and clerical workers also need an increase in *Bumiputra* participation of about 10 per cent in order to achieve the 66 per cent target in relation to the population's ethnic composition.

VII. WHAT NOW FOR MALAYSIAN INCOME INEQUALITY?

Although Malaysia's redistributive policies in the past have been successful, Rasiah and Shari (2001) note that the Government could have better managed its ethnic-based redistributive policies as "access to carrots was hardly countered by the stick of discipline" and if some of "the promotion of crony interests that sapped the economy of rents" could have been avoided. However, this is bound to happen in any society with a government strongly involved in addressing ethnic imbalances. It must however be true, in the case of Malaysia, given its record of economic success, that these effects may have been insignificant. Furthermore, the increased role of the market forces underlying the National Development Policy and the National Vision Policy can be expected to keep a check on such effects in the future.

The market-oriented approach of the National Vision Policy is further welcome, as redistributive action of any kind, if undertaken at the considerable cost of growth, is unlikely to be sustained and effective. The widening of relative inequalities, if accompanied by rapid economic growth in the expansion of productive capacity and its effective utilization, need not necessarily have long-lasting adverse effects. As long as economic growth keeps income inequality at a "tolerable" level, it should not cause concern. However, just what this level becomes the 64 million dollar question. Perhaps a different type of question can throw some light on this issue.

Given Malaysia's development and achievements so far, how important is ethnic economic imbalance today? It can be argued that a more unequal society currently is likely to confer more benefits than harm in the long run (Nelson, 1993). This brings forth another question as to whether there should be a limit to the provision of continued support and opportunities to the disadvantaged ethnic group.⁹ Snodgrass (1980) notes that the responsiveness of the ethnic groups in Malaysia to economic opportunities is (or has been) different and the capacities of different groups to respond may vary systematically given differences in achievement motivation. At the risk of over-simplification, Snodgrass provides evidence of the cultural hypothesis which fundamentally says that, "*something* in Malay culture – or could it be a 'culture of poverty' generated by Malay poverty itself? – makes the Malays immobile, irresponsive to economic opportunity and therefore poor, while *something* in Chinese culture – or in a 'culture of immigrants' – makes the Chinese mobile, more adept at seizing economic opportunities, thrifty, and therefore relatively prosperous". Snodgrass explains that such characteristics are inherent, or at least difficult to change, and this is a powerful deterrent to direct efforts to ameliorate economic inequality. Thus, in the past, while the New Economic Policy has been successful in raising the living standards of *Bumiputras*, what needs to be avoided is for *Bumiputras* born in the second generation during the New Economic Policy period, to consider it their right to be favoured without having to work hard for it. This is summed up in Somun (2003) who quotes the former Prime Minister of Malaysia, Mahathir Mohamad's words on this matter: "... Malays lean on the crutches of Malay privileges in order to protect themselves. Malays consider these crutches as symbols of their superior status in the country. The sad thing is that they are not even using the crutches properly".

In conclusion, what does the future hold for the Malaysian income inequality trend? While the trend was seen as leveling off until 1999, there was an increase in 2002. Figure 1 does not exclude the possibility that the 1990s and the early 2000s saw fluctuations (not necessarily large) in income inequality. Although it is important to determine whether this is a temporary interruption in an otherwise continuous downward trend, this has to await further statistical evidence in view of the fact that the Malaysian economy is still undergoing major structural changes.

⁹ While it is acknowledged that this is a highly sensitive and debatable matter, it provides another avenue of looking at the issue.

VIII. TRANSFERABLE LESSONS?

While the experience of the unequalizing consequences of faster growth was not borne out in the Malaysian growth process, it appears that there is no single general trend in the evolution of the distribution of incomes that applies to all countries over the past two centuries. Declining inequality has not been the rule in modern industrial societies, any more than rising inequality is found in all industrializing economies.

To the question of whether the twin objectives of growth and equity can be pursued simultaneously, there is clearly no direct or simple answer. In the field of economics and other social disciplines, growth and equity often are seen as a zero-sum game but this need not be the case as growth is necessary to gain equity (thereby supporting the trickle-down effect) and so is equity necessary for growth (thus the need for redistributive policies). The relevant question is then: how can an appropriate balance of growth and equity be achieved to maximize the benefits of both objectives to improve overall income and welfare? As Fields (1980) concludes, "Growth itself does not determine a country's inequality course, rather, the decisive factor is the type of economic growth". This in some sense is a warning against a rapid pace of industrialization, which may promise growth in the short run but the pace may not be right if the economy is ill-equipped to support the growth path in the long run. This would cause a large divergence in the incomes of people and hence an increase in income inequality. Not only is the growth-equity relationship complex but it is also fragile, as it could become a vicious cycle whereby inequity can prevent growth and poor growth can in turn lead to unrest and lower the chances of improving equity.

More often than not, a revolution or uprising of some sort motivates Governments to intervene and prescribe redistributive policies to stabilize the economy. However, Governments today need only look around to see that they should not wait before acting. Malaysia was blessed in that the May 1969 riots, which forced the Government to reassess its economic objectives with redistribution as a key thrust, did not turn out to be one of those social revolutions which overturned the class structure. Snodgrass (1980) highlights the operation of ethnic policies on behalf of a politically dominant but economically weak community as the motivation behind the riots in Malaysia. While Malaysia's initial rural development policies were not as successful as had been hoped,¹⁰ they nevertheless provide lessons to agricultural-based developing countries to draw up better plans for reallocating resources.

¹⁰ For a detailed analysis, see Snodgrass (1980).

In Malaysia, rapid and sustained economic growth, educational advancements, affirmative action programmes, tolerance or acceptance of the Government's redistributive policies, and luck, have all helped contribute to a sunny story about Malaysian equity. While there is no one-size-fits-all approach to improving income inequality, an appropriate institutional prerequisite and a commitment on the part of politicians are however essential for successful policy formulation and implementation. Salleh and Meyanathan (1993) explain how political will and institutional strength enabled the Government of Malaysia to engineer fundamental changes in development strategy, with redistribution as one of the objectives. A coalition of ethnic-based political parties, in which the Malay grouping is the dominant partner, has retained power since 1955. The long stay of a single political party in power can be advantageous in implementing policies that have long-term objectives. In Malaysia, political stability is unique as it reflects a social contract between the ethnic groups, allowing Malays to dominate the governance of the country while Chinese business interests remain intact.

In evaluating government actions towards maintaining the balance between growth and equity, the right emphasis is not on a simple, State versus market approach, but on the closeness of fit between strategy, circumstances and institutional capability on one hand, and development goals on the other. It takes time as well as the right group of people to build and cultivate the synergy between these various aspects to ensure that equity co-exists with growth, be it in a developing country or in a more open economy. For an economy intending to deregulate and become more open, the process towards such a move should be gradual so as to give the economy and its people enough time to cope with the demands and consequences of openness. Importantly, the Government needs to ensure that equity issues are not sidelined; redistributive policies go hand in hand with new opportunities arising from globalization.

Lastly, at the risk of being obvious, it is important to acknowledge that the size of the economy has a significant role to play in terms of the ease of implementing redistributive policies. Malaysia's geographical size turned out to be manageable; it enabled the effective and swift implementation of the Government's economic policies to successfully enjoy growth with equity.

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