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DEVELOPMENT PLANNING AND REGIONAL IMBALANCES IN MALAYSIA

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Abstract

The international trade and foreign capital are the main factors contributed to the Malaysian economic development since pre-independence. Basically, the economy is an export-oriented. The government development plans beside restructure and diversify production bases, conversely, the plan had reinforce and revitalise dependency on external sector for economic growth. The First Outline Perspective Plan, 1971-1990 (OPP1), which implanted New Economic Policy was regarded the main catalyst of rapid economic growth and development that the country's achieved now. The objectives and strategies of FP continued in the Second Outline Perspective Plan, 1991-2000 (OPP2). The development plans constituted dual approaches, i.e. (i) government intervention mainly eradicating poverty and restructuring society regardless of races; and (ii) rely on private sector for industrial development (emphasise on role of foreign direct investment). Land reformation (new development and rehabilitation) proceeded, i.e. by establishing industrial zone, and agricultural center (new development for agricultural land stopped in 1984), as a "growth pole" to stimulate urbanisation and economic growth. The plans succeeded transform the economy from agricultural to industrial bases, and poverty has been reduced relatively. On the other hand, due to policy makers and foreign investors preferences, strategic economic locations and transportation facilities, had develop economic disintegration and an acute economic disparities among regions of the country. The government recognised the issue and has (re)constructed a plan to promote development in less developed regions, but the move failed address the matters significantly. In this paper we will apply a static approach to analyse the impact of the Malaysian government planning on regional economic disparities.

[1] Paper was presented at the **9th International Planning History Conference**. 20-23 August 2000. Helsinki University of Technology, Finland. This is a crude draft, please do not quote.

INTRODUCTION

Since 1981, states in Malaysia have been aggregated into six regions (Malaysia 1981). Each region consists of a contiguous landmass, which is in a more or less uniform stage of development and may encompass an entire state or group of states. In general, these regions share similarities in resources and in term of economic activities, and have been dominated by single metropolitan area. Peninsular Malaysia consists of four regions while East Malaysia consists of two regions (Figure 1).

Regions in Peninsular Malaysia (West Malaysia);

1. *Northern region;* consists of four states – Perlis, Kedah, Pulau Pinang, Perak and Georgetown as the growth centre.

2. *Central region;* consists of four states - Selangor, Federal Territory of Kuala Lumpur, Negeri Sembilan, Melaka and Kuala Lumpur as the growth centre.

3. *Eastern region;* consists of three states - Kelantan, Terengganu, Pahang and Kuantan as the growth centre.

4. *Southern region;* consists of one state, Johor and Johor Baharu as the growth centre.

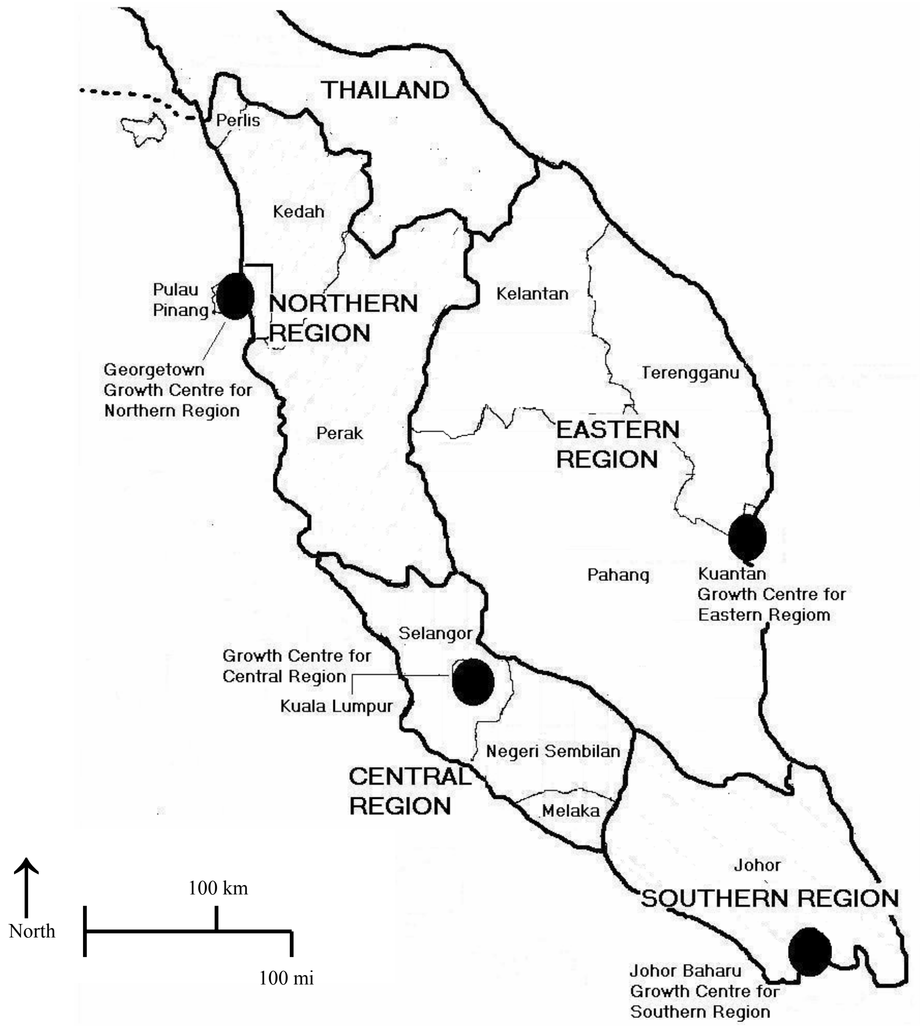
Regions in East Malaysia;

1. *Sabah region*, consists of Sabah (including Federal Territory of Labuan) state and Kota Kinabalu as the growth centre.

2. *Sarawak region*, consists of Sarawak state and Kuching as the growth centre.

Johor is defined as a single-state region because of its pace of development and pattern of resource flow which was influenced by the neighbouring Singapore island, while Sabah and Sarawak were defined as a single-state region because of their location, large physical size and unique socio-economics characteristics.

Figure 1
Location of Regions in Peninsular Malaysia



Source; Malaysia 1981, Fourth Malaysia Plan

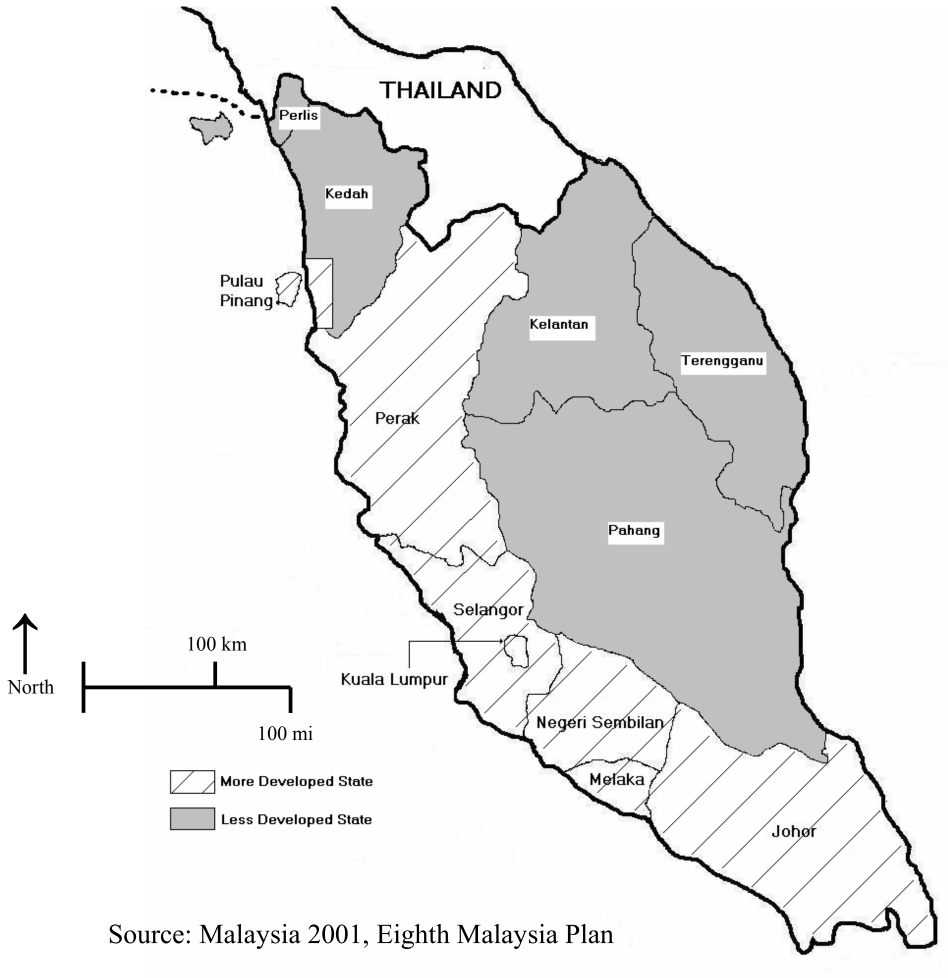
Since 1981 also, states in Malaysia have been divided into three categories based on their level of GDP per capita. There are two high-income states: Federal Territory of Kuala Lumpur and Selangor. There are eight middle-income states: Johor, Melaka, Negeri Sembilan, Pahang, Perak, Pulau Pinang, Sabah and Sarawak. Finally there are four low-income states: Kedah, Perlis, Kelantan and Terengganu. However, GDP per capita is not a good enough measure to compare development between states. This is because growth is a part of development and growth of GDP is not the only objective of development. Growth actually refers to a quantitative increase in GDP while development is conceptualised as qualitative changes in non-economic variables (Brinkman 1995). In other words, development is more concerned not only with changes in GDP but also its relation with development values (Baster 1972).

Therefore, starting in 2001, the composite development index has been used and states in Malaysia have been divided into two categories based on level of development (Malaysia 2001: 116). The composite development index comprises ten indicators; GDP per capita, unemployment rate, urbanisation rate, registration of car and motorcycle per 1,000 of population, poverty rate, population provided with piped water, population provided with electricity, infant mortality rate and number of doctors per 10,000 of population. Based on these indicators, states in Malaysia have been divided as follows (Figure 2):

1. *More developed states*; Johor, Melaka, Negeri Sembilan, Perak, Pulau Pinang, Selangor and Federal Territory of Kuala Lumpur.

2. *Less developed states*; Kedah, Kelantan, Pahang, Perlis, Sabah, Sarawak and Terengganu.

Figure 2
Location of States by Level of Development in Peninsular Malaysia



Source: Malaysia 2001, Eighth Malaysia Plan

DEVELOPMENT PLANS AND STRATEGIES

The development planning during pre-independence relied on private sector and lassie-fair approach. The government concentrated economic development sector mainly in agricultural and infrastructure, industrial and social development were less emphasized. After independence in 1957 and up to year 1970, the role of private sector in the development plans resumed. Also during the period, the government started introduce industrial development base on import-substitution (ISI) strategy under economic diversification programmes (Table 1). As mentioned by Mohd Yaakub and Kiong (1990), development policies and programmes have been oriented primarily towards accelerating the growth of the economy through investment in the leading sectors such as agriculture, mining and primary industries, without an explicit formulation of distribution targets to redress socio-economic imbalances which have characterised Malaysian society at the time of independence. The development programmes was concerned accelerating economic growth at the expense of growing regional and rural-urban inequalities (Mohd. Yaakub and Kiong 1990). The introduction of ISI as a momentum for industrialisation failed in accelerating economic growth, unemployment rose to 8 per cent in 1968 (total population about 10 million), while distribution of income widen as noted by Gini coefficient increased from 0.49 to 0.55.

As social-economic imbalances worsening[2], and indigenous people, Malays (Bumiputras) left out in the economic (business) sector, the government introduced a new development strategy. The New Economic Policy (NEP) formulated and the NEP incorporated in the twenty-year First Outlined Perspective Plan, 1971-1990 (OPP1). The NEP takes full recognition of the problems and needs in a multi-racial society and was designed to ensure that the governments is sufficiently equipped to influence the pattern of economic growth in directions which will bring about a more equitable sharing of the benefits of growth and development among all Malaysians so that no particular group will experience any loss or feel any sense of deprivation. The NEP formulated to allowed Malay join the economic activities and compete with non-Malay mainly Chinese.

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[2] Racial riot occurred May 13, 1969.

Table 1: Government Development Expenditure (actual) (RM million at current prices)

		Economics				Social				General[b]	TOTAL
Years	Five year Development Plan	Agriculture	Infrastructure	Industry	Total	Education	Health	Housing	Total		
1950-1955	Draft Development Plan, Malaya	156	395	-	550	33	15	-	48	82	681
1956-1960	First Malaya Plan	228	520	12	760	61	13	65	139	108	1,007
1961-1965	Second Malaya Plan	468	1,237	59	1,764	237	102	69	414	474	2,652
1966-1970	First Malaysia Plan	1,114	1,430	141	2,685	329	147	207	752	805	4,242
1971-1976	Second Malaysia Plan	2,129	3,353	1,618	7,100	676	174	235	1,348	1,373	9,821
1977-1980	Third Malaysia Plan	4,688	5,637	3,246	13,571	1,548	307	1,291	3,635	3,395	21,201
1981-1985	Fourth Malaysia Plan	8,742	26,824	20,212	55,778	4,688	737	3,935	9,981	8,306	80,333
1986-1990	Fifth Malaysia Plan	7,920	21,243	8,365	35,528	6,185	745	1,060	8,441	3,243	49,212
1991-1995	Sixth Malaysia Plan	6,344	13,169[a]	4,047	22,712	7,315	2,387	1,828	13,558	13,438	54,708
1996-2000	Seventh Malaysia Plan	5,460	16,878[a]	5,864	33,706	10,210	2,658	2,875	19,803	13,991	67,500

[a] included transportation, communication, power/electricity

[b] administration, security etc.

Source: Malaysia Development Plan, various issues

There are two pronged objectives of the NEP: (i) to eradicate poverty among all Malaysians, irrespective of race, through raising income levels and generating new employment opportunities, and (ii) to restructure Malaysian society in order to correct racial economic imbalances in terms of wealth, education and employment and economic (business) opportunity. The NEP introduced due to the existence of widespread poverty and income and wealth ownership disparities between the Bumiputras and non-Bumiputras[3]. The plan proposed that the inequalities be reduced drastically so that greater unity could be achieved. One of the ways to do this, apart from rural and urban development, would be to promote regional development rather than maximizing growth (Wah and Ee 1988). The rationale for emphasizing regional development was to achieve closer integration among the various regions of the country as well as to achieve a more equal distribution of incomes (Wah and Ee 1988). To supplement this strategy, four basis methods were relied upon by the planners; they include and the creation of new growth centres incorporated under new-land or resource-frontier development and industrial dispersion (create industrial zone), and *in-situ* development in rural areas.

Growth Centre

Under the OPP1 (1970-1990) the government emphasizes the growth center strategy to eliminate poverty, decrease disparity among regions and states and to promote economic growth. The growth center adopted or assumed as a catalyst to future economic development. The growth center created to enhance industrial development and agricultural expansion and to increase urbanisation. There are two type of growth-center base on location. First establishment of industrial zone (or free trade zone) as growth center and the center located near to major town. The strategy seeks to encourage new manufacturing industries to move to the less developed parts of the country especially in the east coast states from the congested Klang Valley and other major urban centres in the west coast. A number of instruments have been used to achieve this including tax holidays, investment allowances, provision of industrial estates and free trade zones (Alden and Awang 1985). Industrial decentralisation is seen as a means to accelerate

[3] According to Fatimah (1990), the NEP which seeks to create a viable Malay middle class and to ensure 30% Malay participation in equity and empoyment in all sectors of the economy by 1990. More importantly, the NEP serves the primary ideological tool for mobilizing the Malay masses towards solving two crucial problems: (1) rural poverty and more specifically reproduction of rural labour and (2) the exclusion of the Malay masses from the capitalist sector (Fatimah 1990).

development in the poorer states through the utilisation of the local resources and thus absorbing a large number of the unemployed, especially the Malays. This strategy is linked to the strategy of growth centres in that the development of these centres would spread the development to the hinterlands.

Second establishment of growth center to promote “agro-town or center” by development of new land. New land development accompanied with the establishment of new centre of growth (new town). This type of growth centre to promote rural urbanisation. The main mechanism under this program, that the government open up new land and selected settlers to manage the land. Also the government created agricultural processing center to attract other type of industries or similar to locate nearby. One of main feature of this the new town that the center located quite far from the major town nearby or area which high density of population.

The development of new land proposed in the states, which has high abandoned of land or resource unutilized and less have economic activities such as in Pahang, Terengganu and east of Johor (on it west coast mainly in Pasir Gudang and Tampoi, manufacturing is a main economic activities).

STATE AND FOREIGN CAPITAL

There are solely two agents in the economic development planning in Malaysia, i.e. the government (or the state) and foreign capital. We can be divided the role of the state and foreign capital according the areas. The state largely involve in agricultural sector and also in economic activity by establishing state enterprises. While the foreign capital mainly devoted in the manufacturing sector. There are foreign capital in agricultural and services (banking and financial), but we neglected in this paper.

State Enterprise.

One of the major objectives under the NEP to increase the Bumiputra wealth by 30% at the end of OPP1. Theoretically, the NEP justified state or government intervention in the economic in area of labour organization, capital restructuring (acquisition of private companies) and establish corporate enterprise (known as a public enterprise). The government has made an acquisition of major companies in the plantation and tin mining sector and financial sector: by pressure on companies to restructure their equity to comply with NEP requirements (thus forcing some to dispose their shares at below market value). By rapid establishment of new state enterprises preferably in joint venture with multinationals and especially in the fast developing industrial sector the state was able to expand its share in the economy to have virtual control over the organization of national production (Fatimah 1990). In the decade of the 1970s to 1980s the state was almost always the leading investors in the private sector. Generally, the public enterprises (PE) account about one-quarter of the economic activities in Malaysia, responsible for almost one-third of growth in investment and emerge as the major borrowers in external market (Ismail 1993).

In 1951 there were only 10 public agencies, increased to 701 in 1979 and by April 1989 there were 1,139 public enterprises. The government held equity and control of 60% of the tin mining sector, 77% of the combined capital of 21 Malaysian banks (60-70% of Malaysian banking services in 1986), and 60% of planted acreage and virtual monopoly of the petroleum sector. Particularly, there are 144 PE in agriculture sector; 131 in building and construction; 33 in extractive industries; 125 in financial institutions; 327 in manufacturing; 299 in services; 68 in transportation and 22 others. Out of the 1,139 firms, 291 (25.55 percent) have been identified as inactive (Ismail 1993). These include firms whose operations have been ceased, closed down or dormant, under liquidation, in pre-operation stage, under receivership, suspended or are just "shell" firms (Ismail 1993). Total paid-up capital of the total about RM21.4 billion and the government share (federal and state) about 71.1%. Total loans by the PE as at April 1989 about RM40.14 billion. The expansion of PE also attributed in increase of employment in the sector. Total employment in the public sector increased to more than 900,000, forming about 23% of total national workforce.

In the early 1950's foreigners controlled over two-thirds of the Malayan economy comprising mainly tin and rubber production and the export-import trade (Fatimah 1990). The Chinese share amounted to 14%. The Malay (or alternatively, Bumiputra) share was only 2.6. Europeans handled about 60-70% of the trade. The Malay equity was 4.3% in 1971 and in 1990 it was 20.3%. Non-indigenous local participation also increased from 34% in 1971 to 54.6% to in 1985. Foreign participation however, declined from 61.7% in 1971 to 25.1% in 1990 (Mohamed Aslam 2000). In some extent the state control and direct capital accumulation has stimulated interest in the question of state autonomy.

The establishment of the PE as mentioned earlier was to achieve the NEP goals. There is PEs in the agricultural sector, which was mainly helping the government eradicating poverty in the rural areas where majority are Malays. There are few large federal and state agricultural corporation such as FELDA, FELCRA and KEJORA (as will be mentioned in subsequent subject) involve in new land development. To achieve the objective of restructuring society, the government participated directly by establishing enterprises for Bumiputras through such statutory organizations as PERNAS and MARA. Additionally, the rural sector would be modernized, regional imbalances corrected, opportunities for education provided to more Bumiputras, and urbanization stepped up. The private sector, too, was expected to play a positive role and complement the government's efforts in achieving the objectives.

Agricultural

Since the incidence of poverty was very high and critical in rural areas, the policy towards eradicating poverty in the sector by creating new areas of development and modernise the sector. The goal of eradicating poverty basically base on increasing infrastructure development in the rural areas, establishing more land development schemes, and providing a wide range of free or subsidized social services. In the urban sector, programmes aimed at alleviating poverty took the form of greater public amenities, such as low-cost housing and utilities. In this part we only focus on agricultural.

Development in agriculture sector divided into two main focus (i) regional development- new land development forms a major means in the future growth of agriculture. The exploitation of natural resources and development of agro-based activities complement the land development in resource rich states, and (ii) the development of existing agricultural areas with a high incidence of poverty through an integrated *in-situ* development approach. The strategies aimed to reduce imbalance between sector of the economy, between rural and urban areas, and between races.

For the development of the sector the government has allocated a huge amount of fund as indicated in Table 2. In 2MP total allocation on the sector about RM7.4 billion and the allocation increased to RM80.33 billion in 5MP.

Table 2: Public Expenditure on Agriculture and Rural-Urban Development

Malaysia Plan (MP)	Total Development Allocation (RM billion)	Allocation on Agriculture and rural-urban development	
		RM billion	Percentage
1MP (1966-1970)	4.21	1.11	26.4
2MP (1971-1975)	7.42	1.79	24.1
3MP (1976-1980)	21.20	4.67	22.0
4MP (1981-1985)	49.03	7.99	16.3
5MP (1986-1990)	80.33	8.71	10.8
6MP (1991-1995)	104.00	9.02	8.7

Source: Malaysia Development Plan, various issues

The regional development strategy under the NEP seeks to bring about closer integration among the states of Malaysia. This will be achieved through redressing economic and structural imbalances among the regions in the country. It will draw and build upon the strengths of each region for agricultural and industrial development particularly in the less developed states, to ensure that regional development contributes towards the national goals for economic development. The underlying aim is equitable distribution not only of income but also of facilities for health, education, utilities, services, recreation, housing and most important of all, opportunities for social and economic advancement of the people in accordance with the goals of the NEP.

Regional Development Strategies

Since the First Malaya Plan (1956) and subsequently under the NEP (1971-1990) four important regional development strategies can be identified: (a) new land and resource development strategy, (b) *in-situ* rural development strategy, (c) rural urbanization and creation of new growth centres strategy, (d) industrial dispersal strategy. Sub-region (between ASIAN countries) cooperation was added as one more regional strategy under the National Development Policy (1991-2000) (Asan Ali 2002).

New Land Development

This strategy is geared towards the utilisation of available land in the less developed areas and at the same time increasing the rural population income, eradicating poverty and achieving greater equity in the distribution of income by mobilising large numbers of the rural poor population to the more productive land development schemes. The new land development schemes form the most important sectoral planning strategy under Malaysia's rural development programme. It aims to create employment opportunities in the rural sector, thereby stopping the rural-urban migration flow, to increase farm productivity, and to produce viable farming communities. These schemes concentrate on the cultivation of commercial crops such as rubber, oil-palm, and cocoa (Ly 1988).

Besides diversification and expansion of primary cash crops, this strategy will also overcome the unemployed and underemployed population problem from depressed agricultural areas, to improve the living standard in the rural areas, and finally to direct further growth in manufacturing and services towards the less developed areas, aiming to create employment opportunities in the rural sector. This strategy, which encourages rural-to-rural migration, will decrease the rural-to-urban migration that caused congestion in the well-developed area.

This new land development strategy was proposed by the World Bank in 1954 and has been implemented in the First Malaya Plan (1956-1960). In 1956, the Federal Land Development Authority (FELDA) was formed under the Land Development Ordinance, with the specific aim to develop the rural area. The main objectives of this scheme are to overcome the landless and unemployment problem as well as to increase rural income and to improve the living standard in rural areas[4].

FELDA is primarily engaged in opening new lands and developing its settlement

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[4] The development of these land schemes, which mainly consisted of organized oil palm and rubber smallholding, marked the beginning of the key role played by palm oil in the export diversification and poverty alleviation programs of Malaysia (Arif and Tengku 2001:1). FELDA also was the largest single producer and exporter of palm oil in Malaysia (Pletcher 1990:331).

housing area (so-called FELDA village) with basic infrastructure facilities[5]. Most of the FELDA schemes are located in the eastern (Pahang and Terengganu) and southern (Johor) part of Peninsular Malaysia where substantial land resources for new land development are available (Figure 3).

Besides FELDA, two more authorities at the federal level which have primarily engaged in increasing rural income are Federal Land Consolidation and Rehabilitation Authority (FELCRA) and the Rubber Industry Smallholders Development Authority (RISDA), established in 1972[6]. Both of these authorities focus on redeveloping and increasing the productivity of already existing agricultural areas.

At the state level, since 1971, the government has introduced a number of regional development authorities (RDA) in the resource frontier regions. It was started by Pahang Tenggara Development Authority (DARA) in 1972, Johor Tenggara Development Authority (KEJORA) and Terengganu Tengah Development Authority (KETENGAH) in 1973, Kelantan Selatan Development Authority (KESEDAR) in 1978 and followed by Kedah Development Authority (KEDA) in 1981 (Figure 4).

DARA, KETENGAH and KEJORA stress more the development of new land areas, while KESEDAR and KEDA aim to redevelop and increase the productivity of already existing agricultural areas. In future, the new land development scheme will reduce due to the constraint of land for industrial and residential development. Since OPP2 (1991-2000), rehabilitations of existing land has been emphasize rather than developed new land. On the other the government of state of Sarawak and Sabah (East Malaysia) continued develop new land.

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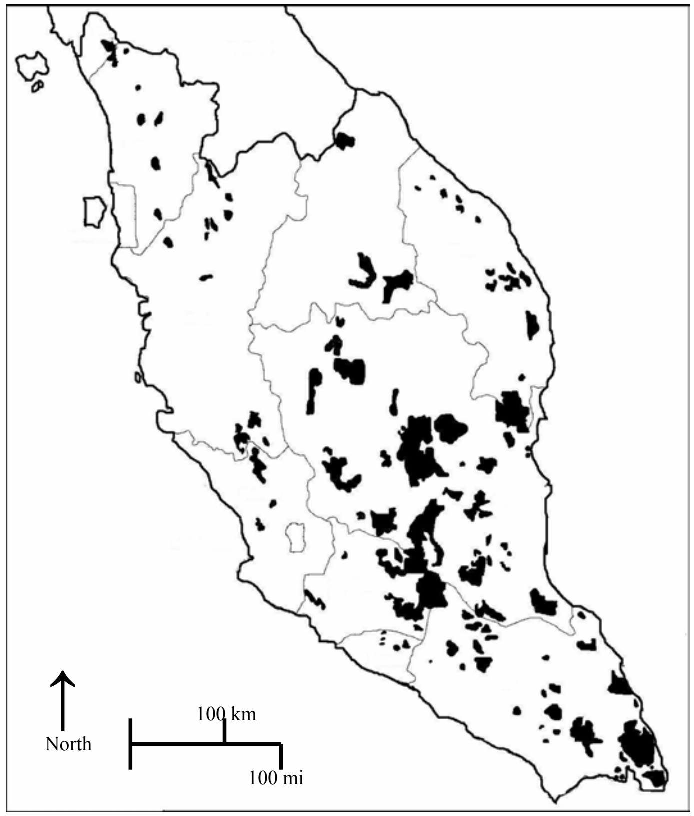
[5] The authority plans and carries out land development and settlement projects in new areas with the aim of producing at the end of the development period (normally six year) prosperous farming communities with economically viable farms (Tunku Shamsul and Thong 1988:10). Settlers who are accepted in this scheme will be provided with a house and ten hectares of land with palm oil or rubber trees and expected to own their house and land after 15 years after having paid their debts to FELDA.

[6] FELCRA focuses on the consolidation and rehabilitation of land in existing agricultural areas, involving the improvement of agricultural holdings through the adoption of modern agricultural practices and the provision of basic infrastructure facilities and support services. While RISDA aimed more toward increasing productivity and low income among rubber smallholders through the provision of subsidies, replanting of rubber trees, the improvement of processing facilities and marketing (Shamsuddin 1984:92).

Figure 3
Location of FELDA Scheme



Source: Tunku Shamsul and Lee Boon Thong 1988: 245

Until 2000, there were 275 FELDA land schemes with about 102,750 settlers. More than 48,800 settlers had already been given their individual land titles (FELDA 2001). Compared to other land schemes, FELDA was the most successful scheme. The FELDA schemes are very comprehensive, and have not only attained their objectives of creating employment, providing ownership of optimal-sized holdings and a capacity to earn higher incomes, but they have also developed technology and group organization through management inputs to raise efficiency and productivity up to the level of many private estates (Wah and Ee 1988). FELDA has resettled 79,900 families and developed more than 480,000 hectares of land for the cultivation of commercial crops such as rubber and oil palm. The cultivated acreage forms 41 percent of the total land development under the various schemes. Nowadays, FELDA concentrates on oil palm and is a major producer of oil palm in the country[7].

[7] Since 1991, rehabilitation of existing land has been emphasized rather than developing new land due to the constraint of land for industrial and residential development.

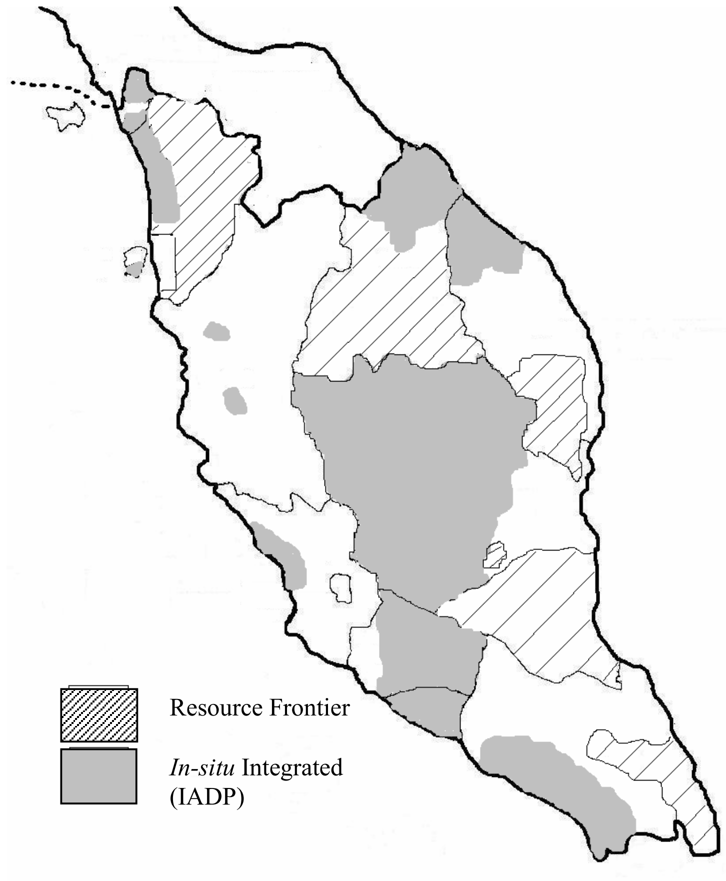
In-situ Development

Basically *in-situ* is a top-down approach and was introduced under the Third Malaysia Plan (1977-1980) In this approach the government will direct relevant machinery (agencies) to the undeveloped agriculture area or less fertile or less productive to become more productive in terms of yield. *In-situ* development aimed at increasing productivity in existing depressed rural areas is given equal emphasis. *In-situ* developments programmes are mainly in the form of specific project plans, referred to as Integrated Agricultural Development Projects (IADP).

This type of project planning involves the provision of necessary infrastructure, inputs and service support, institutional development, extension and training facilities – all of which are integrated into a package focusing on the development of specific potential areas. Besides focusing on the paddy plantation sector, *in-situ* development programmes also carried out drainage and irrigation schemes, replanting and rehabilitation programmes, fisheries, and livestock and forestry development programmes. The responsible authority was the Muda Agricultural Development Authority (MUDA) - covering the state of Kedah and Perlis, KEMUBU and North Kelantan – in the state of Kelantan and Besut in the state of Terengganu. In the late 1980s, a total of 15 IADPs were implemented, covering an area of 847,500 hectares and 480,100 farm families have benefited. The income has grown from 23.6 to 197 percent per household and productivity increases ranged from 23 to 103 percent (Wah and Ee 1988).

Most of the *in-situ* project concentrated in the paddy sector which located in north of Peninsular Malaysia, namely Kedah, Perlis and Kelatan. Also in north of state of Perak there is a large paddy area. These regions were the main produces of rice in Malaysia. Development of the sector supervises by the Muda Agricultural Development Authority (MUDA) (for Kedah and Perlis), Kemubu (for state of Kelantan) and Besut (for state of Terengganu). Also there are agencies related to the modenisation of paddy sector, Department of Agriculture, Malaysia Research Development Institute (MARDI-developed new seeds), Farmers Organisation (FAO) and LPN (National Paddy and Rice Authority-has been privatised, known as Bernas).

Figure 4
Location of Resource Frontier and Programmes



Sources: Masato Ikuta 1994: 36.
Malaysia 1990, Economic Planning Unit: 2-14

Other *in-situ* developments programmes carried out are drainage and irrigation schemes, replanting and rehabilitation programmes, fisheries, and livestock and forestry development programmes. There are also facilities such as training and extension programmes provided under the National Extension project and credit and subsidy schemes, offered by the Agricultural Bank (Bank Pertanian Malaysia). Agencies such as RISDA, MARDEC (Malaysian Rubber Development Corporation), FAMA (Federal Agricultural Marketing Authority) and LKIM (Malaysia Authority Fisheries Development)- extend processing and marketing services to ensure stable and fair prices for the farmers, In general, under OPP1 development of agricultural sector has been given strong emphasize to improve income distribution among rural-urban areas.

Rural Urbanization and the Creation of New Growth Centres Strategy

Under the NEP, the government emphasized the growth centre strategy to eliminate poverty, decrease disparity among regions and states and promote economic growth. The growth centre was adopted or assumed to be a catalyst to future economic development. The growth centre was created to enhance industrial development and agricultural expansion and to increase urbanisation. There are two types of growth-centre based on location. The first one is the establishment of an industrial zone (or free trade zone) as a growth centre with the centre located near to major towns. The strategy seeks to encourage new manufacturing industries to move to the less developed parts of the country, especially in the east coast states from the congested Klang Valley and other major urban centres the west coast. A number of instruments have been used to achieve this including tax holidays, investment allowances, provision of industrial estates and free trade zones (Alden and Awang 1985).

Industrial decentralisation is seen as a means to accelerate development in the poorer states through the utilisation of local resources and thus absorbing a large number of the unemployed, especially the Malays. This strategy is linked to the strategy of growth centres in which the development of these centres would spread the development to the hinterlands. Secondly, the establishment of growth centres to promote “agro-town or centre” by the development of new land. In the long-term, the new land development will be accompanied by the establishment of new centres of growth (new town) and will promote rural urbanisation. The main mechanism under this program is that the government will open up new land and select settlers to manage the land. The government will also create agricultural processing centres to attract similar types of industries or be located nearby. One of the main features of this new town is that the centre is located quite far from any major town nearby or any area with high density of population.

Industrial Development

Industrial development in Malaysia was vital under the First Malaya Plan covering 1956 to 1960[8]. Subsequently after independence in 1957, horizontal and vertical economic diversification remained an important objective of Malaysian economic

[8] This was drafted at a time when Peninsular Malaysia was on the threshold of political independence.

development. The Pioneer Industries Ordinance 1958 was introduced to increase private sector investment, whereby the role of the private sector in the development plans resumed[9].

In 1968, the government introduced the concept of a ‘development area’ in the Investment Incentive Act, 1968. Under this Act, industries that were located in these areas would get additional incentives[10]. The goal of this incentive was to promote industrial activities in the less developed states (or districts). It covered the entire state of Perlis, Terengganu, Malacca, Sabah, Sarawak and the relatively less developed districts in Kedah (excluding Kuala Muda district), Pahang (excluding Kuantan district) and southeast of Johor. Besides that, this incentive also focused on increasing industrial activities in the pioneer industrial estate in the median income state (industrial estates of Senawang in the state of Negeri Sembilan and Kamunting in the state of Perak). At the same time, the Free Trade Zone industrial areas were introduced to encourage export-oriented industrialization[11]. Along with the special incentive, in the beginning the pioneer FTZ areas in Malaysia that were also gazette as development areas were Bayan Lepas FTZ in Pulau Pinang (1971) and Sungei Way FTZ in Selangor (1972)[12] (Figure 5).

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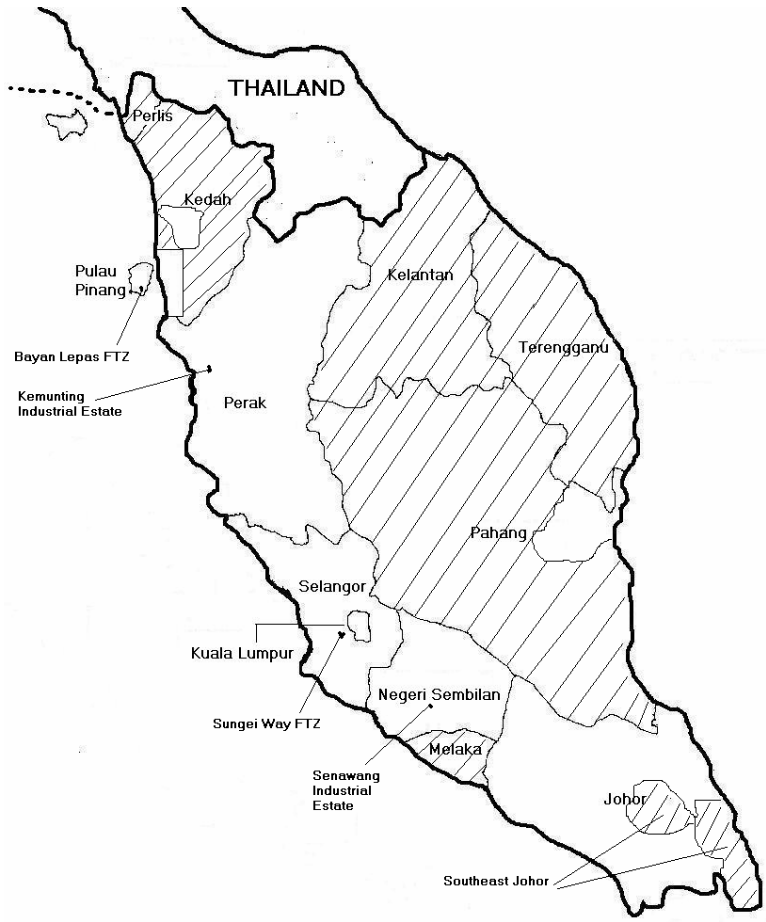
[9] Industrial dispersal strategy has been used in many countries as an instrument for the achievement of development goals (Bar-El 1985).

[10] The incentive provided for industries to locate in a development area was linked to some of the incentives provided under the Investment Incentives Act, 1968. For pioneer industries locating in a development area, an additional year of tax relief was granted irrespective of the size of the capital investment. Also, should an electronic firm which enjoyed the special incentive for the electronics industry be located in a development area, it became eligible for an additional year of tax relief. For a company that had been granted the investment tax credit (ITC), an additional credit of 5 percent of the approved capital expenditure would be granted if the company were to be located in a development area (Lee 1978:456-458).

[11] In early 1970s, the industrial stage in Malaysia shifted from import-substitution to export-oriented industrialization.

[12] The first FTZ programme in less developed countries was at Shannon Airport, Ireland in 1959. In Asian region, it started in India and Taiwan in 1965, late 1960s in South Korea and early 1970s in ASEAN countries (Amazawa 1986:97).

Figure 5
Development Areas under the Investment Incentive Act, 1968.



Source: Malaysia, Malaysian Industrial Development Authority

After the implementation of NEB – growth with equal distribution, the government introduced the Location Incentive Scheme (Act, 1972). More incentives were given to the local and foreign investors to locate their activity in the less developed states (or districts)[13]. Compared with the development area under the Investment Incentive Act, 1968, the Location Incentive Act only covered the entire state of Perlis, Terengganu, Malacca, Sabah, Sarawak and the relatively less developed districts in Kedah (excluding Kuala Muda district), Pahang (excluding Kuantan district) and

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[13] In additional to the 'development area' in the Investment Incentive Act, 1968, any industry located in the gazetted location incentive scheme became eligible for five years of tax relief compared with three years tax relief if the industry was located in the development area. Areas covered under Location Incentive Act overlapped with the location under development area in the Investment Incentive Act, 1968.

southeast of Johor.

The first Industrial Master Plan (IMP) (1986-1995) under the National Industrial Policy was launched in 1986 in order to further reinforce export-oriented industrialization. Further incentive was given under the Promotion of Investments Act 1986, which was introduced as a replacement of the Investment Incentive Act, 1968. Although industrial development focused more on the west-coast corridor, additional incentive[14] was given to the industries located in the East-Coast corridor of Peninsular Malaysia (covering Kelantan, Terengganu, Pahang and the district of Mersing in southeast of Johor).

Besides focusing on further diversification and deepening the resource and non resource-base industries, the IMP also emphasised the dispersal of industries' location and increasing technical and industrial skills workforce[15]. Under the National Industrial Policy, the government lessened the concentration on congested locations by limiting the existence of crowded areas within the high-tech industry and capital intensive industry, while the median and small cities with labour-intensive industry, based on natural resource and traditional (low) technology. In an attempt to diversify the economic base of the less-developed areas, focus has been given to efforts at broadening the manufacturing base of these states, particularly through the development of agro and wood-based industries, petrochemical industries, non-metallic mineral products and other resource-based industries. This is in line with the efforts to promote investment in the East-Coast and East-West investment corridors in Peninsular Malaysia[16] (Figure 6).

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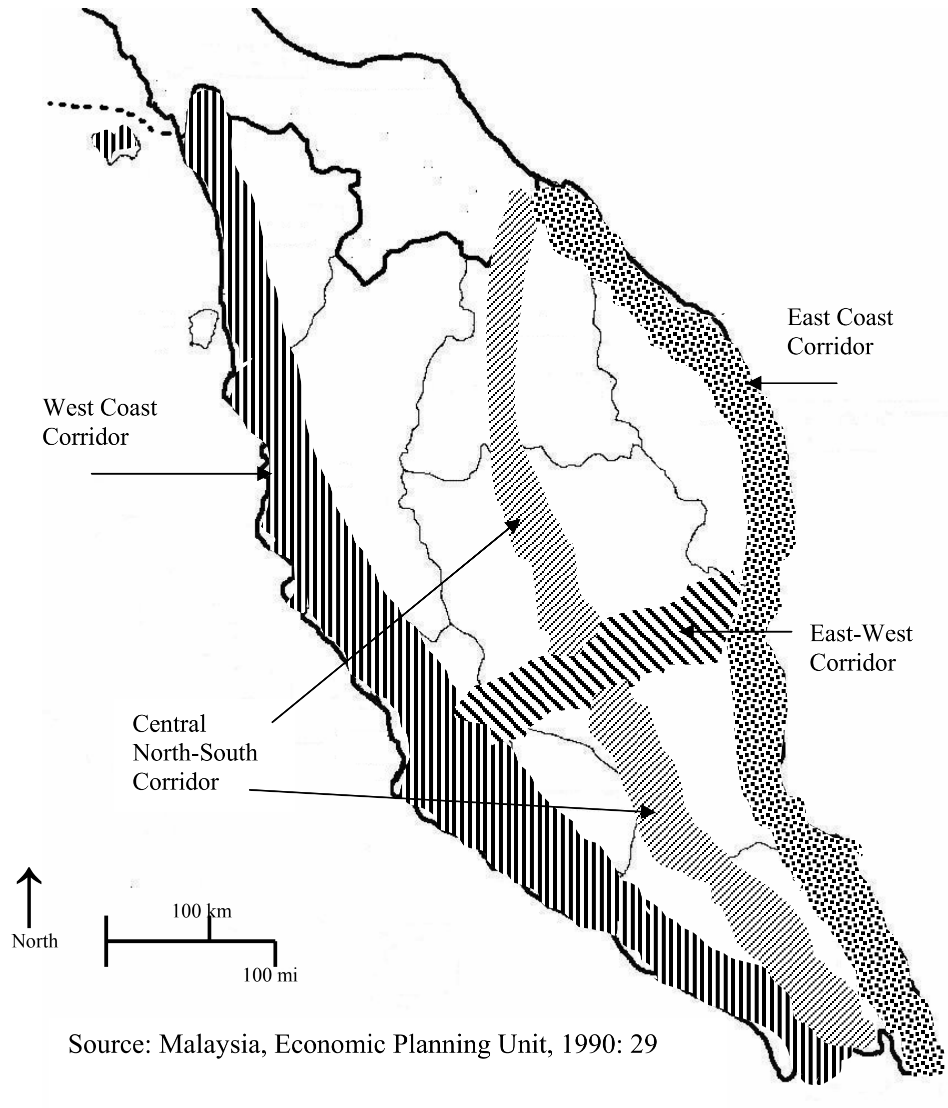
[14] Additional incentive related to location of industries under Promotion of Investments Act 1986 is shown in Appendix 1

[15] IMP1 ended on 1995 and continued by IMP2 (1996-2005). IMP2 emphasises on the full integration of manufacturing operation through the value-chain in order to enhance industrial linkages, increase productivity and competitiveness and promoting knowledge-intensive industries.

[16] Seventh Malaysia Plan 1996, pp.162-163

Figure 6
Industrial Development Corridors



Source: Malaysia, Economic Planning Unit, 1990: 29

Under the NDP (1991-2000), the government has implemented the concept of the Specialised Industrial Estate (SEI) based on location, such as High-Tech Industries in Kedah, Pulau Pinang and Johor; wood-based industries in Selangor, Pahang and Negeri Sembilan; ceramic based industries in Perak; technoplex (textile) industries in Pulau Pinang; electric and electronic industries in Malacca; and Petrochemical based industries in Terengganu. Until 1995, there were 14 SEI scattered in all the states in Peninsular Malaysia except Kelantan and Perlis. SEI will encourage the process of industrial dispersal by developing well-equipped industrial estates, which are provided with sufficient physical facilities and other amenities such as education, health and housing in selected locations in the less developed states, so as to make the rural locations more attractive to private investors and in line with developing new growth centres in the less developed states[17].

In pre-independence period manufacturing activity was limited to the processing of primary products, handicraft and a few essential goods produced on a small scale. The lack of industrial development was because of (i) the effective demand generated by foreign trade, which stimulate various economic activities, leaked abroad through the profits from mining, rubber planting, and trading paid to foreigners, (ii) the two important ports of Singapore and Penang which were free ports acted as a deterrent to the establishment of diversified industrial activity, (iii) the small size of the population and therefore the small size of the market, and (iv) the absence of government policies to encourage industrialisation (Rao,Bhanoji, 1980: 93). Thus, industrialisation during that period was inadequate to build concrete diversification of the country's economy and unsuccessful to reduce dependence on imported finished products mainly for consumption use.

The Malaysian government started to give attention to industrial development as part of economic planning since 1955. Industrial development was promoted on the basis to reduce dependence on a few primary products and the need to absorb an increasing labour force. The early stage of industrial development was ISI. Export-oriented industry (EOI) was in second phase introduced in 1968 and has been a major industrial policy under OPP1. The development of the ISI and EOI was to meet the 'balance-growth', to expand and diversify the economy's production base and not only concentrate on the primary sector, as well as to reduce violation of the instability of commodity prices, while EOI strategy to absorb unemployment and accelerate economy growth by growth of export of manufactures. Since the country lacked of capital, expertise and technology, foreign capital was sought to promote industrialisation. Reliance on foreign capital in industrial development is an essential condition for Malaysia. Although the embarkation of industrialisation was to promote modernization

[17] Malaysia, OPP2 1991, pp.28-29 and Sixth Malaysia Plan 1991, p.55.

and self-sufficient development, but this direction increased the degree of dependency at the ends.

Industrial Policy

The government established Pioneers Industries Ordinance (PIO) in 1958 to encourage development of ISI industrial sector. The PIO is the mark of formal industrial development in Malaysia. The strategy (ISI) involved protection (granted selectively) of domestic producers against foreign competition and explicitly attempted to foster the development of domestic industries at a faster rate (Naya 1990). Tariff and quotas were imposed to encourage the establishment of ISI industries. The government established the tariff board, i.e. the Tariff Advisory Committee (TAC) in 1959, to recommend tariff protection. By 1963, the TAC had instrumentally established a modest tariff protection (Peng 1977: 49). However, the institution was quite slow and cumbersome in advising the government on the matter. In 1963, the government set up the Tariff Advisory Board (TAB) and in 1969 it was reconstituted and renamed the Action Committee on Tariffs and Industrial Development (ACTID). The major task of the committee was to introduce and reconstruct tariff protection (including non tariff barriers), give consideration to pioneer status applications, export incentives and any matter concerning industrial development. The TAB and ACTID ceased to function after May 1969 and were formally abolished in August 1970. The TAC, TAB and ACTID had undoubtedly increased tariff protection level, however the level is still below international standards. In mid 1969, the Capital Investment Committee was established to take over TAB and ACTID responsibilities. Basically, the CIC was used to enhance business confidence and to increase employment. Its main tasks were (i) to identify industries with the potential for development and formulate policy guidelines and incentives to encourage them; and (ii) to streamline the government machinery so as to accelerate the pace of industrialization (Peng 1977:52).

The tariff was used vigorously and discriminately to attract industries under the auspice of CIC. Besides the CIC (was de-established in 1971), the Federal Industrial Development Authority (FIDA), now known as the Malaysia Industrial Development Authority (MIDA) has been developed, and some of the functions of TAB and ACTID have been taken over by MIDA. The government has also formed the Special Advisory Committee on Tariffs (SACT), and the Tariff Unit of the MIDA services it. The body is responsible for imposing or removing tariffs, besides recommending on investment and export incentives.

The CIC and SACT were initiated after the government announced the Investment Incentive Acts (IIA) in 1968. The act offered industrial and fiscal incentives such as exemptions from company tax and duty on imported inputs, investment tax credits and accelerated depreciation allowances on investment. The IIA does not directly promote ISI industries further, but encourages and promotes export-oriented industries (EOI). The government has recognized that the ISI lacks exports expansion, economic growth and employment opportunities. Therefore, for future prospects for industrial development the country has to depend upon the EOI (Athukorala 1996).

In addition to IIA, in 1971, the Free Trade Zone (FTZ) Act was enacted to enhance the expansion of the EOI industries base, also on top of that Licensed Manufacturing Warehouses (LMW) were established as a ‘tariff-free zone’. EOI has been reinforced further in 1986 with the introduction of Promotion Investment Act (PIA), the PIA also as a replacement of IIA 1968. Under the PIA, government allowed foreign ownership to 100% provided the ventures export at least 50% of their products; sell at least 50% to factories in the free trade zones and employ 350 full-time Malaysian workers. To enjoy a list of other concessions like being allowed to employ five expatriate staff, companies must have a paid-up capital of US$2 million and be established between October 1986 and December 1990 (Fatimah 1990).

Even though the EOI industries were strongly promoted in the early 1970s, the government still encouraged the development of the ISI type industries (also resource-based industries) but on a selective basis. The committees, CIC and SACT assist the government on tariff protection and incentives matter for both industrial strategies. In the early 1980s, the government reinstated the ISI strategy by promoting heavy industrial projects. The Heavy Industries Corporation of Malaysia (HICOM) was established in 1980 to lead heavy industrial development. The government has granted tariff protection to the heavy industries, and the effective rate of protection (ERP) has increased firmly for the automotive, steel, cements and paper industries. The establishment of industrial institutions such as tariff committees, MIDA and HICOM, has resulted in the reconstruction of tariff protection frequently to gear industrial development.

The tariff rates vary and diverge largely by products and industries. Generally, tariff rates in Malaysia are low compared to other developing countries. The average tariff rate of 21 per cent in 1960 increased to 24 per cent in 1969 before declining to 16 per cent in 1984 and fell to about 9 per cent in 1996 (Mohamed Aslam 2000). The unweighted average nominal rates of protection (NRP) in 1973 and 1978 were 36.7 per cent, respectively, and in 1987, the NRP value fell to 27.31 per cent. While the effective rate of protection (ERP) dropped from 64.9 per cent in 1970 to 45.1 percent in 1987 (Mohamed Aslam 1993).

Foreign Direct Investment

In the 1960s, foreign participation in the industrial development was small, even though the government had provided pretty incentives. On top of that, since the ISI industries type needed protection for growth, the government had restructured the tariff systems so as to lean to ISI development. Although FDI was encouraged by the tariff protection, however, the FDI inflow in this sector was considered small. FDI, actually, had contributed to the Malaysian economic development in the early part of development, i.e. pre-independence.

The growth of rubber plantation and tin mining sectors were due to the foreign capital mainly from British sources. Foreign capital has been regarded as the main agent and stimulator and has strengthened the foundation or base of the Malaysian economy. For diversification of the production bases, under the industrialisation programme, foreign capital reinvaded due to the lack of capital (saving) in the country itself. This paper argues that the foreign capital role is inherited in the Malaysian economic development. The economy in caught in dependency because of the inherent relationship between developed and developing nations.

Foreign capital inflow in Malaysia has increased tremendously since the 1970. In 1970 capital inflow, which was RM200 million, increased to RM21 billion in 1980 and in 1995 was recorded at RM24 billion. As a percentage to domestic private capital formation (DPCF), it has also shown some significant descriptions. On average the percentage of FDI to DPCF is 20 per cent per year. A look at the FDI by industry shows that the non-resource based industries, namely electrical and electronics; and chemicals and chemical products; and other machinery, accounted for a relatively high proportion of the investment. The capital has increased from RM50.9 million in 1980 to RM4825.4 million. Followed by chemicals and chemical products, and the textiles and textiles industries. These sectors mainly were labour intensive and located largely in the (EPZs) areas.

The expansion of industrial development in Malaysia was driven by FDI (input-driven growth) (Aoki and Takayasu 1995: 163). To a certain extent, the Malaysian economy has gained a greater degree of sophistication through the industrialisation process, which has been contributed by the FDI. The industrial structure is polarized between a modern sector based on foreign companies located in the FTZs (capital and technology intensive, high technical level large corporations oriented toward exports and non-resource based) and at the other pole the indigenous industries with very weak linkage between the two. In short, the Malaysian economy can be called a disintegrated co-habitation economy (Aoki and Takayasu 1995: 165). Whether by design or not, the Malaysian economy can be said to be an economy "with no average values" (Aoki and Takayasu 1995: 165)

REGIONAL ECONOMIC PERFORMANCE

In evaluating the development plans, it could be stated generally that reasonable progress was achieved in respect of the specific objectives of eradicating poverty and reducing economic imbalances. There was overall economic development in terms of growth and employment generation, despite the uncertainties of the international economic situation. On average GDP grew by 8 percent per-annum in 1998-1997, about 7.4 percent from 1971-1984. The agricultural on average grew by 5 percent per annum, due mainly to the phenomenal growth of palm-oil (which was registered a 25 percent per annum growth rate), and remained the predominant sector in the economy. Transport and manufacturing grew by more than 10 percent annually during the period. Economic growth during this period was largely the result of public investment and consumption, which also provided a counter-cyclical impact during periods of weak exports and private investment. In terms of employment, the number of new jobs created was 588,000 in 1970s increased to 4,816,900 in 1980. The unemployment rate was 5.7 percent.

However, the job opportunities dropped in 4MP due to economic recession in 1983-86. The fell in major commodities prices harmed the performance of economy. There was major retrenchment in the manufacturing, mainly owned by foreigner located in EPZ. The unemployment grew to 7.5 percent in 1986. Since recover from economic depression in 1987, the economy grew rapidly and the unemployment declined below 3 percent since 1994. The rate of employment growth was highest in the manufacturing sector, which registered a rate of 6.6 per cent annually.

As a result of the restructuring policies of the government, which included preferential treatment of the Bumiputras in education, financial assistance in the of easy credit facilities, training and advisory assistance, and son on, there was substantial improvement in the racial structure of employment as well as ownership of share capital. The percentage of employment of Bumiputras in all the main sectors increased considerably, and all the rates of growth exceeded the overall rates of growth of employment. In restructuring patterns of employments, Bumiputras were still under-represented in manufacturing and commerce and other high earning professional jobs. In terms of equity restructuring, Bumiputra ownership went up from 12.5 percent in 1980 to 22 percent in late 1980, due mainly to acquisitions by government trust agencies.Since affected by the economic recession, public sector spending has been trimmed. The government has decreased investment. The private sector has been encouraged to contribute to economic growth. The government has promoted privatization and "Malaysia Incorporated" announced in 1983 to reduce the burden of PEs. The government and private sectors expected to be no longer regarded as separate entities; they were to complement each other for the overall benefit of the nation. In keeping with these concepts, the government was to hand over selective public services and industries (e.g. television, telecommunication, public utilities) to the private sector.

The end of the 5MP marked the closing of two decades of development planning in Malaysia. During this period, regional development approach was geared towards disparities between states and regions in both social and economic terms. While there was some success in the distribution of social amenities and infrastructure, there was however, limited success in efforts towards narrowing states and regional disparities (Mohad Yaakub 1990). Discussion on achievement of development plans will be base on OPP1.

Economic Growth

Regional development was given increasing importance in order to bring about a more balanced distribution of economic activities and a closer integration among the States of Malaysia. Industrial decentralisation is seen as a means to accelerate development in the less developed states through the utilisation of local resources, emphasis on infrastructure and communications development, (particularly in the east coast of Peninsular Malaysia), to help strengthen the physical linkages between regions, besides absorbing a large number of the unemployed, especially the Malay ethnic group. The strengthening of such linkages, apart from fostering closer integration between regions, also paved the way for greater mobility of factors of production, such as machinery and equipment and skilled labour, essential for accelerating industrial development in these regions.

There has been good response to policies to increase manufacturing activities in the less developed states. Since 1970, the percentage contribution to GDP by the agriculture industry decreased rapidly in all states (and regions). Decrease in the GDP by agriculture sector has been taken over by an increase in manufacturing industry. The importance of agriculture as a main contributor to GDP in the less developed states has decreased by about 63.8 per cent (from 48.6 per cent in 1970 to 17.6 per cent in year 2000) (Table 3). Meanwhile, the percentage contribution by the manufacturing industry increased drastically by about 308 per cent (from only 6.3 per cent in 1970 to 25.7 per cent in year 2000). In terms of geographic region, GDP percentage by agriculture industry decreased more in the Northern and Eastern regions.

Table 3
Percentage of GDP by Industry of Origin and Region,
1970, 1980, 1990 and 2000

	year	Northern (N)	Eastern (E)	Central (C)	Southern (S)	*Less Developed Region (L)*	*More Developed Region (M)*	*Peninsular Malaysia*
Agriculture, forestry, fishing, etc.	1970	34.0	42.6	19.3	41.0	48.6	25.4	30.2
	1980	18.4	35.6	11.5	32.8	28.9	16.3	19.3
	1990	21.7	20.7	6.9	29.4	25.1	13.2	16.0
	2000	15.0	15.2	4.0	17.2	17.6	8.3	10.4
Percentage decrease		*-55.9*	*-64.3*	*-79.3*	*-58.0*	*-63.8*	*-67.3*	*-65.6*
Manufacturing	1970	9.3	6.3	19.1	14.0	6.3	15.3	13.4
	1980	18.0	10.5	28.5	23.8	7.0	27.1	22.2
	1990	28.7	10.9	37.9	28.0	13.4	34.6	29.6
	2000	36.5	21.2	44.0	40.8	25.7	41.6	38.0
Percentage increase		*292.5*	*236.5*	*130.4*	*191.4*	*307.9*	*171.9*	*183.6*

Source: Calculated from various Malaysia Plans

At the same time, economic structure in more developed states was not static, and also changed towards industrialisation. Although the percentage contribution by manufacturing industry increased less than in less developed states (about 172 per cent) in the same period, the decrease in percentage GDP by the agriculture industry was more (about 67 per cent) than that in the less developed states. As an example, in the Central region (comprising the four more developed states; Selangor, Kuala Lumpur, Melaka and Negeri Sembilan), the percentage GDP by agricultural industry decreased by about 79 per cent, the highest compared with other.

Although in all states the percentage GDP by agriculture has decreased and percentage GDP by manufacturing industry has increased, the gap between states in the GDP by manufacturing industry still occurred. However, this gap has decreased since the implementation of the NEP. The GDP by manufacturing industry ratio to the highest state (Selangor) decreased rapidly from a range of 13.7 (Kelantan) to 2.3 (N.Sembilan) in 1970, to 8.7 (Kelantan) to 1.2 (P.Pinang) in year 2000. If Kelantan is not included, the range in year 2000 is only between 3.1 (Pahang) to 1.2 (P.Pinang) (Table 4).

Table 4
Ratio of Manufacturing GDP Distribution by State[a]

		Johor	Kedah	Perlis	Kelantan	Melaka	N.Sembilan	Pahang	P.Pinang	Perak	Kuala Lumpur	Selangor	Trengganu
GDP Manufacturing	1970	2.8			13.7	7.3	2.3	4.7	2.8	4.0		1.0	11.7
	1980	4.0	19.3	15.1	35.4	8.4	4.7	6.8	1.9	5.7		1.0	17.6
	1990	2.9	6.3	4.6	17.2	2.7	2.8	6.4	1.4	4.6	2.2	1.0	5.8
	2000	1.6	2.7	2.6	8.7	1.8	1.9	3.1	1.2	2.6	2.2	1.0	2.4

[a] Ratio to the Selangor state

Source: Calculated from various Malaysian Plans

Over the period, from 1971-1990, economic growth was concentrated in the Central Region, comprising Melaka, Negeri Sembilan and Selangor (including the Federal Territory of Kuala Lumpur). The slowest growing regions seemed to be the Northern and Eastern Regions. The state with the lowest GDP per capita over the period was Kelantan. There are few main points we mentioned about the imbalances.

Firstly, concentration of foreign direct investment. Foreign investment prefer to locate their activities at the rich regions or where there is a good and sufficient incentive in terms of infrastructure development, location matter (near to major town and financial centre, port) and federal administration. FDI largely concentrated in the more developed states of Peninsular Malaysia. This also can be traced base on approval of investment by MIDA as stated in Table 5. There are three states preferred by the foreign investors, Johor, Selangor and Penang. Huge investment in Terengganu (Eastern region) since 1990 attributed to the petroleum and chemical projects, since Terengganu one of the major states producing petroleum, beside Sarawak. Therefore job opportunities are high in the regions.As a result a migration rural-urban inevitable. The rate of unemployment in the state receive high FDI reduce dramatically contrast to the states receive less FDI.

Table 5
Number of Projects Approved 1980-1990

	1980-1989	Per cent	1990-1999	per cent	Change 80-89=90-99	per cent change
Northern Region	1,310	25.69	2,176	28.69	866	34.8
Eastern Region	379	7.43	413	5.44	34	1.4
Central Region	2,329	45.68	3,129	41.25	800	32.2
Southern Region	1,081	21.20	1,867	24.61	786	31.6
More developed states	4,417	86.62	6,587	86.84	2,170	87.3
Less developed states	682	13.38	998	13.16	316	12.7

Source: Malaysia, Malaysian Industrial Development Authority office

Secondly, the growth centre base on agricultural activities less stimulates urbanization than industrial zone located in the west coast of Peninsular Malaysia. The agricultural centre as developed by FELDA and other state agencies such DARA, KEJORA and JENGKA concentrated in particular economic activity, producing oil-palm (and rubber). There is no incentive creating or spillover effect on other development of industries. Consequently, expansion of the created town centre actually retarded, less development in terms of expansion of residential area and shop houses or commercial outlets. This is contrast to industrial zone, which located at near major town. There are no homogenous firms in the zone and of course there is should be spill-over effect Tampoi near to Johor Bahru; Shah Alam and Petaling Jaya near to Kuala Lumpur; Bayan Baru, Seberang Jaya, Prai near to Georgetown. [The main states as mentioned above, Johor (major town/city: Johor Bahru), Selangor (major town/city: Petaling Jaya and Shah Alam, next to Kuala Lumpur metropolitan) and Penang (major town/city: Georgetown)]. Base on this fact, the urbanization rate will be much higher than other states which receive low FDI and have large plantation areas. Excluded Kuala Lumpur, the three main states as mentioned included Perak (main town Ipoh) has a higher urbanization rate as shown in Table 6. Thirdly, the historical factor; centre of economic development and urbanisation in Malaysia begins with the growth of the Straits Settlements of Penang (port) and Singapore (port) (near to Johor Bahru) and the mining towns of Ipoh (Perak) and Kuala Lumpur (Kuala Lumpur was in Selangor) during British colonial rule.

Table 6
Urbanisation Rate by State, 1970-2000

		Urbanisation rate						Ratio KL to the others					
		70	80	85	90	95	00	70	80	85	90	95	00
More developed states	Selangor	45.0	34.2	34.5	55.3	80.8	88.3	2.2	2.9	2.9	1.8	1.2	1.1
	Pulau Pinang	50.7	44.7	49.3	60.4	77.0	79.5	2.0	2.2	2.0	1.7	1.3	1.3
	Perak	27.5	32.2	32.3	33.6	56.2	59.5	3.6	3.1	3.1	3.0	1.8	1.7
	Johor	26.3	35.2	35.3	43.7	54.4	63.9	3.8	2.8	2.8	2.3	1.8	1.6
	Melaka	25.1	23.4	23.3	23.3	49.5	67.3	4.0	4.3	4.3	4.3	2.0	1.5
	Negeri Sembilan	21.5	32.6	32.6	42.1	47.3	55.0	4.7	3.1	3.1	2.4	2.1	1.8
	Kuala Lumpur	100	100	100	100	100	100	1.0	1.0	1.0	1.0	1.0	1.0
Less developed states	Terengganu	27.0	42.8	42.8	51.1	46.6	49.4	3.7	2.3	2.3	2.0	2.1	2.0
	Kedah	12.7	13.9	14.4	16.0	35.1	38.7	7.9	7.2	6.9	6.3	2.8	2.6
	Kelantan	15.1	27.7	27.7	32.1	33.5	33.5	6.6	3.6	3.6	3.1	3.0	3.0
	Pahang	19.0	26.2	26.2	24.6	35.0	42.1	5.3	3.8	3.8	4.1	2.9	2.4
	Perlis[a]	-	8.7	8.8	11.2	29.6	33.8	-	11.5	11.4	8.9	3.4	3.0

[a] Perlis, urbanisation rate 1970 = 0

Source: Calculated from various Malaysian Plans

Investment Incentive and Industrial Development

As mentioned before, the levels of regional income have strong linkages with the establishment of the manufacturing sector. Since independence and subsequently after the implementation of the NEP (1971), the government has made serious efforts to decentralise the manufacturing activities. This is because industrial imbalance has an important relation to the imbalance of household monthly income, poverty and unemployment. Under British colonialism, Peninsular Malaysia was the main supplier of tin and rubber to the world. Economic activities focused more on the primary sector. However, since independence (1957), the government has started to promote the secondary sector (manufacturing and construction) as a source of growth besides export commodities (tin, rubber and oil palm). In 1958, the Pioneer Industries Ordinance was introduced to increase private sector investment.

From 1970 onward, the Malaysian economy experienced a drastic structural transformation. The share of the agricultural sector in total GDP and employment declined rapidly. The percentage of agriculture sector contribution to employment decreased from 52.2 per cent in 1970 to only 15.2 per cent in 1997. At the same time, the GDP decreased from 23.3 per cent in 1970 to only 6.3 per cent in 1997. The manufacturing sector in Peninsular Malaysia experienced an average annual output growth rate of 23.3 percent between 1970 and 1979. However, the average annual output growth rate decreased to 12.2 percent for the period of 1980 to 1989 because of the worldwide economic recession. The average annual output growth rate increased again to 16.4 percent for the period of 1990 to 1999. This average was expected to be greater, however it was offset in the late 1990s by a financial crisis in the East and Southeast Asian countries (Malaysia, Economic Report 1998/99).

In order to promote industrial activities in the less developed states (or districts), the government introduced the concept of a ‘development area’ under the Investment Incentive Act, 1968. Industries that were located in these areas would be granted with additional incentives. The ‘development areas’ covered the entire state of Perlis, Terengganu, Malacca, Sabah, Sarawak and the relatively less developed districts of Kedah (excluding Kuala Muda district), Pahang (excluding Kuantan district) and southeast of Johor (Figure 7). It also included two industrial estates; Kemunting Industrial Estate (in the state of Perak) and Senawang Industrial Estate (in the state of Negeri Sembilan) and two Free Trade Zones (FTZ) industrial area; Bayan Lepas FTZ (in the state of Pulau Pinang) and Sungei Way FTZ (in the state of Selangor). These two industrial areas were the pioneer industrial areas and were isolated from the concentrated industrial areas in the state of Selangor and Pulau Pinang while; the FTZ’s were the pioneer FTZ in Malaysia.

After the implementation of NEP, the government introduced the ‘Location Incentive Scheme’ (under Investment Incentive Act, 1972). More incentives were given to the local and foreign investors to locate their activities in the less developed states (or districts)[18] mainly to redistribute the industrial activities from more concentrated areas in the more developed states. Compared with the development area under the Investment Incentive Act, 1968, the Location Incentive Act, 1972 only covered the entire state of Perlis, Terengganu, Malacca, Sabah, Sarawak and the relatively less developed districts of Kedah (excluding Kuala Muda district), Pahang (excluding Kuantan district) and southeast of Johor. It did not include Kemunting Industrial Estate, Senawang Industrial Estate, Bayan Lepas FTZ and Sungei Way FTZ because it referred only to the less developed states (or districts).

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[18] In addition to the ‘development area’ in the Investment Incentive Act, 1968, any industry located in the gazetted location incentive scheme became eligible for five years of tax relief compared with three years tax relief if the industry was located in the development area. Areas covered under Location Incentive Act were overlapped with the location under development area in the Investment Incentive Act, 1968.

Further incentive was given under the Promotion of Investments Act 1986, which was introduced as a replacement for the Investment Incentive Act, 1972. Although industrial development focused more on the west-coast corridor, additional incentives[19] were given to the industries located in the East-Coast corridor of Peninsular Malaysia. It covered Kelantan, Terengganu, Pahang and the district of Mersing in southeast of Johor. Compared with the 'Location Incentive Scheme' (under Investment Incentive Act, 1972), additional incentives under the Promotion of Investments Act 1986 did not cover the states of Malacca, Kedah and Perlis (located in the West-Coast of Peninsular Malaysia) because the additional incentives were only given to the industries located in the East-Coast corridor of Peninsular Malaysia mainly to give it more of a comparative advantage[20]. The manufacturing activities in these states were relatively less and the economic sector still depended on the agricultural sector, which recorded less monthly income, high poverty and unemployment as well as out-migration (Asan Ali 1998).

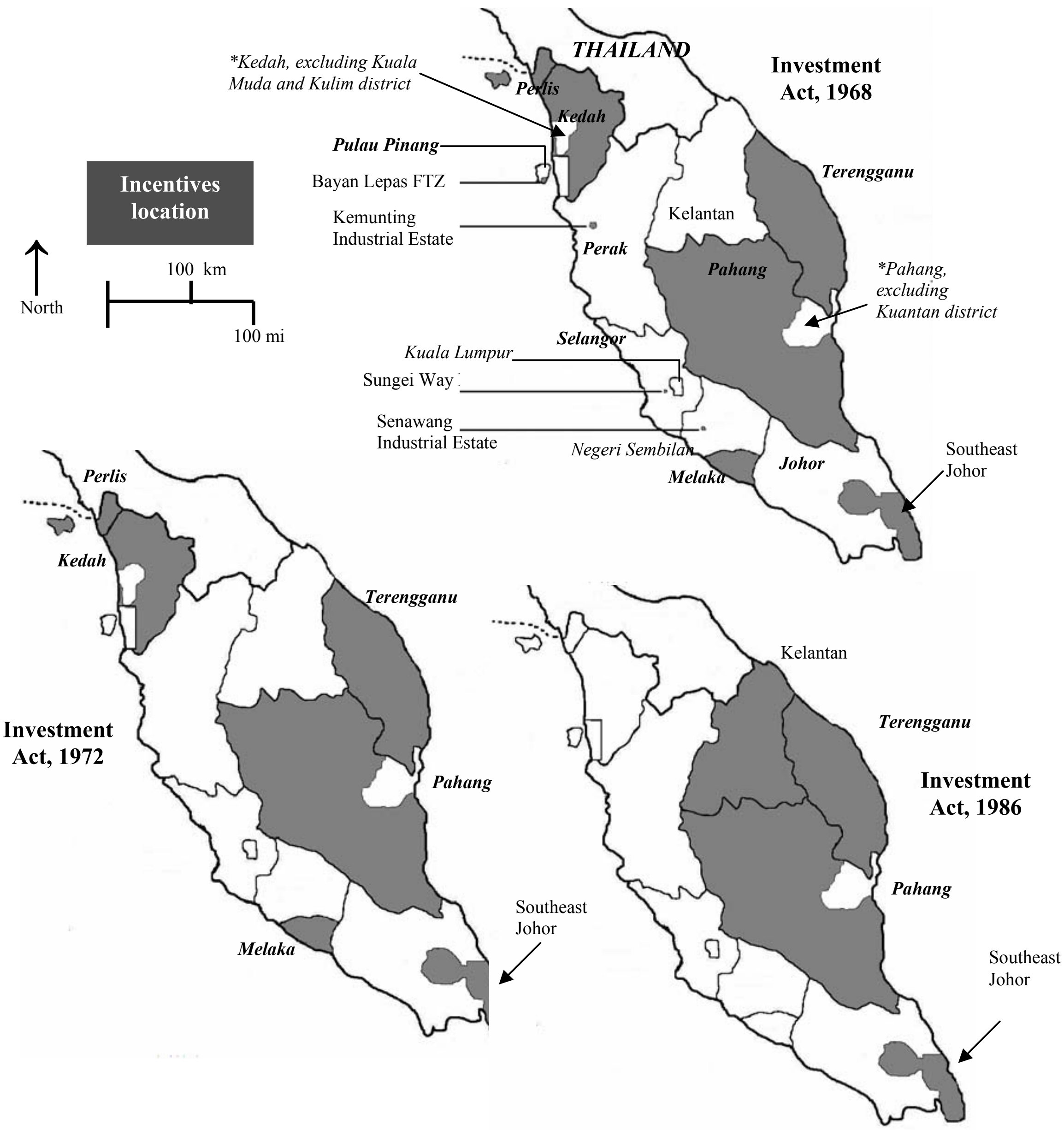
The Investment Incentive Act was replaced for two reasons, firstly to make investment in Malaysia more attractive and to have extra competitive advantage compared with other countries in the ASEAN region. This is because other countries also have their investment incentive and Malaysia has to compete to attract the FDI especially from multinational companies. Secondly, regarding the additional incentives given to the selective states or districts, the number of states that receive the incentive was decreased from six states under Investment Act 1972 to only three states under Investment Act 1986. Kedah, Perlis and Malacca that were given additional incentives under Investment Act 1972 no longer received additional incentives under Investment Act 1986. Manufacturing activities in these states increased rapidly, and focus had to be given only to the states located in the East-Coast corridor (Kelantan, Terengganu and Pahang) where the manufacturing activities were relatively less. Besides incentives under the Investment Incentive Act,

[19] Additional incentives related to location of industries under Promotion of Investments Act 1986 are shown in Appendix 1.

[20] It was hoped these additional incentives would decrease the cost of production. States in the East-Coast of Peninsular Malaysia recorded less comparative advantage in terms of concentration of population (consumer), labour force (high out-migration especially those who are experienced and educated), and social infrastructure.

since 1971, the State Economic Development Council (SEDC) also provided some incentives to promote investors especially FDI to set-up factories in those particular states. All these incentives provided under the Investment Incentive Act (Federal government) and under the State Economic Development Council (state government) can be summarised in Table 7.

Figure 7
Investment Incentives Location Under Act 1968, Act 1972 and 1986



Sources: Malaysia, Ministry of International Trade and Industry office

Table 7
Incentives Provided Under Investment Incentive Act and Under State Economic Development Council

	Incentive under Investment Incentive Act			Incentive under State Economic Development Council				
	Act, 1968, under Development Area	Act, 1972, under Location Incentive Scheme	Act, 1986, under East-Coast corridor	Reduction in land price instalment payments	Reduction in quit rent	Reduction in assessment rate	Discounts on purchase of industrial land	Discount in rentals of ready built factory
Perlis	*	*						
Kedah	*[1]	*[1]					*[a]	*[a]
P.Pinang								
Perak	*[2]					*[b]		
Northern								
Pahang	*[3]	*[3]	*	*[FELDA]	*[f]	*[f]		
Kelantan			*	*[d]				*[d]
Terengganu	*	*	*	*[e]		*[e]		
Eastern								
Selangor								
N.Sembilan	*[4]							
Melaka	*	*		*[c]	*[c]		*[c]	
K.Lumpur								
Central								
Johor*/ Southern	*[5]	*[5]	*[5]					

[1] excluding Kuala Muda and Kulim District; [2] industrial estates of Kamunting only; [3] excluding Kuantan district (other than Gobeng Industries Area and Bentong District; [4] industrial estates of Senawang only; [5] southeast (Mersing district) of Johor only.

[a] Bumiputera investors in the state of Kedah are provided discount of 5% on purchases of industrial land and ready built workshops/factories.

[b] The Perak State Economic Development Council (SEDC) has lowered the assessment rates for factory sites within Ipoh City from 16% to 10% and provides a 30% reduction in the land premium.

[c] Investors in Melaka are allowed to purchase industrial land through an extended payment scheme over a period of 5 to 10 years. Industrial land in industrial estates in Melaka enjoys concessionary quit rent and water rates. Melaka also gives a discount of 7% on all payments made within 6 months from the date of offer; a further 3% is given on completion of factories within 12 months from the same date.

[d] Kelantan's installment plan is 10% payable on signing of agreement, 10% one month later, 30% two months later 50% payable within three months of signing of agreement. Kelantan's rental rate for ready built factories allows discount based on number of workers and floor space.

[e] Terengganu SEDC operates a Special Incentives Scheme. Under this scheme, investors creating total employment for more than 200 staff obtain industrial land prices at RM0.50 per square meter to a maximum of 4 hectares and a 50% lowering in the annual assessment rate. Quit rent is also negotiable.

[f] Pahang SEDC operates a progressive payment scheme with the 20% down payment into two installments of 10% each with a grace period of 6 months. Investors are given a grace period of 6 and 9 months after the first and second down payment respectively and the balance is paid in 4 installments equally distributed over the next 9-month period. Quit rent for industrial land lowered by 50% to 15% per 100 meters for the first two hectares.

Sources; Malaysia, Ministry of International Trade and Industry office
Malaysia; Economic Planning Unit 1990: 4-9
Young Poh Chey 1988: 4

Besides the huge incentives in manufacturing industries especially in the less developed states, the government also took further steps to promote manufacturing industries by developing industrial estates. The strategy seeks to encourage new manufacturing industries to move to the less developed parts of the country especially in the east coast states from the congested areas in state of Selangor (Klang Valley) and other major urban centres in the west coast. Numbers of existing industrial estates increased rapidly in the states of Kedah, Perak, Terengganu, Selangor and Johor. In the less developed states, the number of existing industrial estates increased rapidly from none in 1970 to 105 in 2002, while in more developed states, it increased from 8 in 1970 to 188 in 2002 (Table 8).

Although the number of existing industrial estates in the less developed states increased, the size (hectare) of the industrial estates was rather small. This is because most of the industries located in the less developed states were Small Medium Industry (SMI) and labour intensive. About 41 percent of the industrial estates in less developed states were less than 25 hectares compared with 26 percent in more developed states. Only three percent of industrial estates in less developed states were more than 200 hectares, while 11 percent industrial estates in more developed states were more than 200 hectares (Table 9).

Table 8
Number of Existing Industrial Estates, 1970, 1990 and 2002

	1970	1990	2002	
			Number	Expansion 1990-2002
- Perlis*	0	2	7	5
- Kedah*	0	15	28	13
- Pulau Pinang	3	9	18	9
- Perak	1	19	34	15
Northern Region	4	45	87	42
- Pahang*	0	11	34	23
- Kelantan*	0	6	15	9
- Terengganu*	0	12	21	9
Eastern Region	0	29	70	41
- Selangor	2	25	37	12
- N.Sembilan	1	8	18	10
- Melaka	0	7	27	20
- K.Lumpur	0	4	19	15
Centre Region	3	44	101	57
Johor/ *Southern Region*	1	20	31	11
*Less Developed States**	0	46	105	59
More Developed States	8	92	188	96
West MALAYSIA	8	138	289	151

Sources: Malaysia, Malaysian Industrial Development Authority office
Lee Hock Lock 1978: 505

Besides that, all of the industrial estates in the less developed states were developed by the public sector (government), while in the more developed states; some of the industrial estates were developed by the private sector. For example, until 2002, from 28 industrial estates in Perak, ten of them were developed by private sector, while in Kelantan and Terengganu, all the industrial estates were developed by the public sector. Although the industrial area developed by the private sector was generally 30 per cent higher than the industrial area developed by the public sector (depending on location), the demand for the industrial area in the more developed states was relatively high and the private sector (property sector) took this opportunity to create marginal profit.

Table 9
Size Distribution of Industrial Estates Developed, 1990 (Hectare)

	<25	25-50	51-75	76-100	101-200	201-400	401-800	>800
- Perlis	2	0	0	0	0	0	0	0
- Kedah	9	1	1	1	2	1	0	0
- Pulau Pinang	3	0	3	0	2	0	1	0
- Perak	0	2	7	2	3	4	1	0
Northern	**14**	**3**	**11**	**3**	**7**	**5**	**2**	**0**
- Pahang	2	2	2	0	3	2	0	0
- Kelantan	1	1	1	1	2	0	0	0
- Terengganu	5	1	3	0	3	0	0	0
Eastern	**8**	**4**	**6**	**1**	**8**	**2**	**0**	**0**
- Selangor & K.Lumpur	14	13	3	2	4	1	2	0
- N.Sembilan	1	2	0	2	3	0	0	0
- Melaka	1	0	2	3	1	0	0	0
Centre	**16**	**15**	**5**	**7**	**8**	**1**	**2**	**0**
Johor/ **Southern**	**8**	**3**	**2**	**2**	**3**	**1**	**0**	**1**
Less Developed Region	19	5	7	2	10	3	0	0
More Developed Region	27	20	17	11	16	6	4	1
Peninsular Malaysia	46	25	24	13	26	9	4	1

Sources; Malaysia, Economic Planning Unit 1990: 3-20

Although the manufacturing sector in Peninsular Malaysia as a whole experienced rapid average annual output growth rate, its distribution was still more towards developed states (Table 6.4). In fact, although the federal and state governments have made serious efforts to increase manufacturing activities in less developed states by introducing several incentives, the distribution of manufacturing activities in Peninsula Malaysia did not change much by the end of the New Economic Policy (NEP) (1970-1990).

Under the redistribution policy of the manufacturing activities, it was hoped that the manufacturing activities would increase in the less developed states. Although in overall percentages terms, contribution of output by less developed states increased, it was by less than one percent. For example, the percentage of output contributed by the state of Perlis only increased 0.2 percent from 0.2 to 0.4 percent, and the state of Kedah only increased by 0.2 percent from 3.7 to 3.9 percent, Pahang only increased by 0.4 percent from 2.1 to 2.5 percent and Terengganu increased by 0.8 percent from 0.5 to 1.3 percent. It was the reverse for the state of Kelantan; the percentage of output contribution did not increase but decreased one percent from 1.6 to only 0.6 percent by the end of the NEP period. The percentage of labour contribution in the less developed states only increased by 0.3 percent in Perlis and 3.2 percent in Kedah. In the state of Terengganu, it remained unchanged, at 1.2 percent, while in the state of Kelantan it decreased by 0.3 percent from 2.4 to 2.1 percent.

Figures 8 and 9 show the percentage contribution of output and labour by region for the period of 1970 until 1999. This trend shows that decreasing output and labour contributed by the central region were not overtaken by the northern and eastern regions but by the southern region. It contradicted the government policy to increase output and labour contributed by the northern and eastern regions.

Figure 8
Percentage Contribution of Output

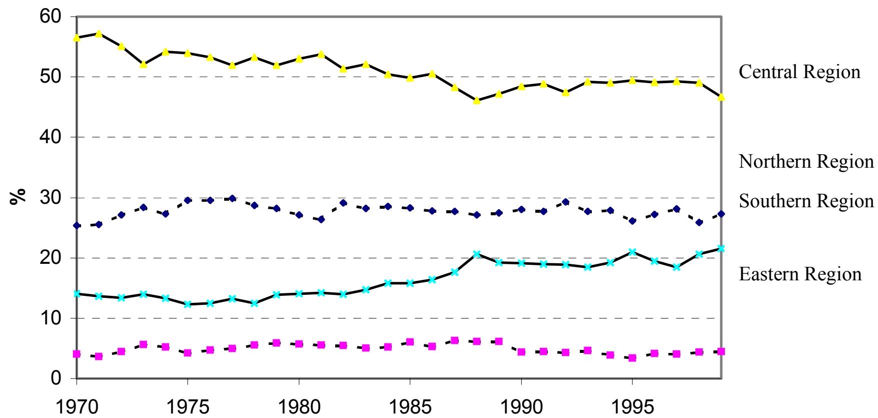
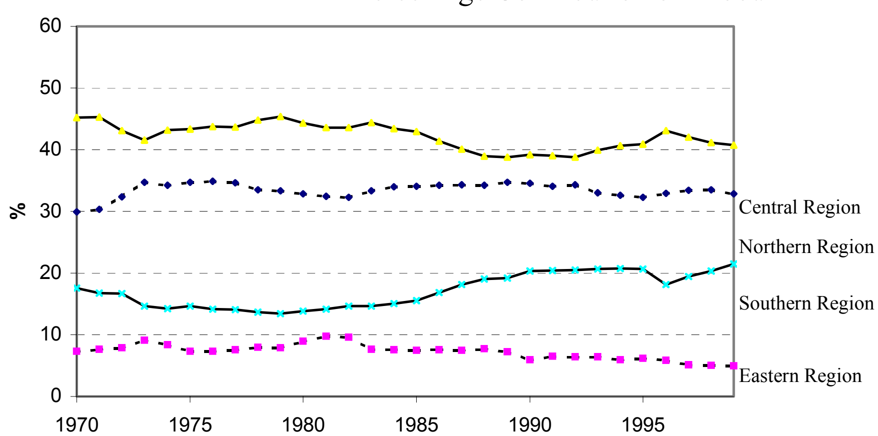


Figure 9
Percentage Contribution of Labour



Source: Malaysia, Industries Surveys, various issues

Although government redistribution policy has increased manufacturing output and labour in the northern region, a greater percentage increase came from the state of Pulau Pinang and not from the states of Kedah and Perlis (less developed states). In the eastern region (all states in Eastern region were categorised as less developed states), the output contribution was relatively small, at only 0.3 percent, while labour contribution did not increase but decreased about 1.4 percent. Government policy was also intended to decrease output and labour contributed by the central and southern regions. However, the policy only succeeded in the central region. In the southern region, output and labour contribution continued to increase.

States that recorded a huge decrease in their output and labour contribution to the Malaysian total were Selangor and Perak, while states that recorded a big increase in output and labour contribution to Malaysian total were Pulau Pinang (7.4%) and Johor (5.1). This situation showed that several incentives under the federal and state government were not successful in their goal to increase manufacturing activities in the less developed states. Pulau Pinang and Johor were not placed under any status of 'Development Area' or under 'Location Incentive Scheme' as well as 'East-Coast corridor' or any other incentives under SEDC but the manufacturing output and labour contribution was increasing and still relatively high. Although the district of Mersing (in southeast Johor) was placed under the status 'Development Area' and under 'Location Incentive Scheme' and currently under 'East-Coast corridor', Mersing industrial area only contributed less than two percent to total manufacturing output and labour[21].

An investment incentive plays an important role in increasing manufacturing activities in Malaysia. Investment incentives in Malaysia started with the Investment Incentive Act, 1968 which was replaced by the Investment Incentive Act, 1972. Further incentives

[21] Although district of Mersing (at southeast Johor) was placed under the status 'Development Area' and under 'Location Incentive Scheme' and currently under 'East-Coast corridor' Mersing industrial area only contributed less than two percent to total manufacturing output and labour. In 1996 (July), from 4,403.47 total hectares industrial land developed under Johor State Economic Development Corporation (SEDC), only 16.59 hectares (0.38%) located at Mersing Industrial Estates(Mersing I). While, 1998 (January), from 4,443.78 total hectares industrial land developed under SEDC only 1,500 hectares (0.33%) located at Mersing Industrial Estates (Mersing II).

were given under the promotion of Investments Incentive Act, 1986[22], which was introduced as a replacement of the Investment Incentive Act, 1972. Most apparent effect from the government industrial incentive is in terms of Investment Incentive Act, 1986. Before the 1986 Act, about 37 to 47 percent of approved projects were the result of investment incentives given by the government (Table 10). This amount increased rapidly after the 1986 Act, for instance, in 1990, the amount increased to about 58 percent. However, it decreased in 1997 due to the economic downturn. Most of the industries that received this incentive were the export-oriented industries located in the more developed states especially in Selangor, Pulau Pinang and Johor. Location incentives were less effective; projects approved under this incentive were small compared to other incentives - it only accounts for less than three percent of the approved manufacturing projects with incentives.

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[22] For example under Investment Incentive Act, 1986, a company granted Pioneer Status will enjoy partial exemption from the payment of income tax. It will only have to pay tax on 30% of its statutory income. The period of tax exemption is five years, however as an added incentive, companies located in the designated Eastern Corridor of Peninsular Malaysia, will only have to pay tax on 15% of their statutory income during the tax exemption period of five years. A company granted Investment Tax Allowance will be given an allowance of 60% in respect of qualifying capital expenditure incurred within five years from the date on which the first qualifying capital expenditure is incurred. The allowance can be utilised to offset against 70% of the statutory income in the year of assessment. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up. The balance i.e. 30% of the statutory income will be taxed at the prevailing company tax rate. As an added incentive, companies located in the designated Eastern Corridor of Peninsular Malaysia will be granted an allowance of 80 % in respect of the qualifying capital expenditure incurred. The allowance can be utilised to offset against 85% of the statutory income in the year of assessment (adopted from MIDA information guide for investors).

Table 10
Approval of Manufacturing Under Investment Incentive Act of 1972 and 1986

Investment Incentive Act	Investment Incentive Act, 1972			Investment Incentive Act, 1986		
	1976	1980	1985	1990	1997	2000
With incentive:	202 (47.5)[a]	184 (40.0)	229 (36.6)	524 (57.8)	213 (28.1)	205 (25.5)
- Pioneer status	105	104	78	440	154	153
- Investment Tax Allowance	76	73	143	84	59	52
- Location incentive[b]	7	2	8	-	-	-
Without incentive	223	276	396	382	546	600
Total	425	460	625	906	759	805

[a] Figures in parentheses show the percentage.
[b] Number of manufacturing approved with location incentive was not recorded separately because it was incorporated under Pioneer status and Investment Tax Allowance deduction (Act, 1986).

Source: Malaysia, Malaysian Industrial Development Authority office
Chamhuri and Surtahman 1999: 112

Poverty

Although, generally the urbanisation rate has increased in less developed states (due to increased new economic activities), high out-migration still occurred in the less developed states. This phenomenon occurred mainly because of the large disparity of wages between the less developed states and more developed states. For example, in 1984, the average monthly household income in Kuala Lumpur was 3.1 times higher than that in Kelantan (Table 11)[23]. Although in 1999, the ratio of mean monthly household income in Kuala Lumpur to other states has decreased, it still is at least 2.5 times higher than that in less developed states. This ratio, in the less developed states, ranged from 3.1 to 2.5 in 1999.

The combine effect of the poverty eradication policies added with the rapid growth of the economy led to a decline in the incidence of poverty in all states in Peninsular

[23] As in most others countries, the income measures typically used in Malaysia are biased toward easily measured monetary income (Kusnic and DaVanzo 1982:18).

Malaysia. Incidence of poverty in Malaysia obviously decreased from 49.3 per cent in 1970 to 29.2 per cent in 1980 and from 17.1 per cent in 1990 to only 7.5 per cent in 1999. In another words, incidences of poverty have decreased 85 per cent since the implementation of the NEP, which was attained through rapid socio-economic development with significant participation of the poor.

Table 11
Mean Monthly Household Income by State, 1984 and 1999

	State	1984	Ratio[a]	1999	Ratio[a]
Less developed states	Kelantan	500	3.1	1,314	3.1
	Kedah	552	2.8	1,612	2.5
	Terengganu	604	2.5	1,599	2.6
	Perlis	553	2.8	1,431	2.9
	Pahang	767	2.0	1,482	2.8
More developed states	Perak	706	2.2	1,743	2.4
	Melaka	831	1.8	2,260	1.8
	Negeri Sembilan	831	1.8	2,335	1.8
	Johor	851	1.8	2,646	1.6
	Pulau Pinang	946	1.6	3,128	1.3
	Selangor	1,271	1.2	3,702	1.1
	Kuala Lumpur	1,535	1.0	4,105	1.0

[a] ratio of mean monthly household Income Kuala Lumpur to other states

Sources: Hashim Shireen-Mardziah 1998: 73
Malaysia 2001, Eighth Malaysia Plan

Prior to the NEP, much of the focus of development policies and programmes was centred on growth. Under the NEP, the strategy of poverty eradication called for a pattern of development, which provided opportunity for the poor to participate effectively in the growth process and share in the benefits of development[24]. Major poverty eradication strategies were through land development and *in-situ* agriculture programmes apart from the absorption of the rapidly growing rural labour force into higher income jobs in the industrial and services sector.

The improvements made in respect to poverty eradication in Peninsular Malaysia are shown in Table 12. Despite the substantial progress made, poverty remained a problem in the less developed states, especially in Kedah, Perlis (in the Northern

[24] The burden of poverty in developing countries is often thought to fall most heavily on children who must begin work at an early age to help make ends meet. However research in Malaysia finds no evidence to support that picture. Malaysian children from poor families neither participate more in productive activities nor work longer hours when they do participate than children from more well-to-do families (De Tray 1983: 452).

region) and Terengganu and Kelantan (in the Eastern region)[25]. In these states, the poverty rate was still relatively high, ranging from 11.8 per cent to 22.9 per cent in 1999. In the more developed states, the poverty ranged only from 9.1 to 0.5 in 1999. In less developed states, besides the high incidence of poverty that existed in the beginning of the NEP, the agricultural sector remained important in these particular states. In most developing countries including Malaysia, poverty rate was high in the agricultural sector especially among the small holders (Williams 1991; Malaysia 2001). In Malaysia, the incidence of poverty in the agricultural sector only decreased from 68.3 per cent in 1970 to 46.1 per cent in 1980, while the decline in the non-agricultural sector was relatively faster, from 27.8 per cent in 1970 to 16.8 per cent in 1980 (Malaysia 1981, Fourth Malaysia Plan).

Table 12
Incidences of Poverty by State

	State	1970	1987	1990	1995	Per cent change 1970-1995
More developed states	Kuala Lumpur		5.2	3.8	0.5	-96.4[a]
	Johor	45.0	11.1	10.1	3.1	-93.1
	Selangor	29.2	8.9	7.8	2.2	-92.5
	P.Pinang	43.7	12.9	8.9	4.0	-90.8
	Melaka	44.9	11.7	12.4	5.3	-88.2
	N.Sembilan	44.8	21.5	9.5	4.9	-89.1
	Perak	48.6	19.9	19.3	9.1	-81.3
Less developed states	Pahang	43.2	12.3	10.3	6.8	-84.3
	Perlis		29.1	17.2	11.8	-80.0[b]
	Kedah	64.5[c]	31.3	30.0	12.2	-80.0[d]
	Terengganu	68.9	36.1	31.2	23.4	-66.0
	Kelantan	76.1	31.6	29.9	22.9	-69.9

[a] per cent change 1982-1995
[b] per cent change 1976-1995
[c] Kedah including Perlis for the 1970 data
[d] per cent change 1976-1995

Sources; Malaysia 1983, Mid-Term Review Fourth Malaysia Plan
Malaysia 1988, Mid-Term Review Fifth Malaysia Plan
Malaysia 1991, Second Outline Perspective Plan
Malaysia 1996, Seventh Malaysia Plan

[25] Poverty in Malaysia is primarily a rural phenomenon. Within each ethnic group, rural residents are more likely to be poor. Rural Malays and rural Indians are the two most poverty-prone subgroups; in both rural and urban subsets, Chinese are the least poverty-prone (Kusnic and DaVanzo 1982:25).

Although poverty rate was high in the agricultural sector especially among the small holders, it was relatively different in the state of Pahang. The opening of new land for resettlement represented one of the programmes that contributed to the reduction of poverty. About 30 per cent of the rural households in this state were involved in the FELDA schemes[26]. Income improvements among settlers in land development schemes were more substantial. The average monthly income of settlers on Federal Land Development Authority (FELDA) schemes ranged from RM490-RM810 in 1979 compared with incomes of only about RM80-RM120 from their previous occupations (Asan Ali et al. 1999).

The encouragement by the Government towards dispersal of industries in the less developed states in which majority of them was the Malay ethnic group enabled the poor rural and urban households to be gainfully employed in manufacturing activities, thereby raising their level of income. In 1980, only about 17.1 per cent of the total investment approved in manufacturing projects was planned to be located in the relatively less-developed states where the incidence of poverty was high. By 1997, the proportion increased to 44.7 per cent of total investment approved in manufacturing projects.

Mean monthly gross household income by the Malay ethnic group increased slightly from only RM172 in 1970 to RM1,984 in 1999 (Table 13). The percentage of annual growth rate of the mean monthly gross household income of the Malay ethnic group was highest compared to other ethnic groups in the period 1970 to 1999. The ratio of Malay (M) to Chinese (C) mean monthly gross household income increased from 0.4 in 1970 (M:C; 0.4:1.0) to 0.6 in 1999, while the ratio of Malay (M) to Indian (I) mean monthly gross household income increased from 0.6 to 0.8 in the same period. However, the Chinese mean income was still above the national average.

As mean monthly gross household income increased, the poverty rate for the Malay ethnic group decreased from 64.8 per cent in 1970 to 20.8 percent in 1990 (Table 14). Although it has decreased by about 32 per cent since 1970, it is still high compared to only 5.7 per cent for the Chinese ethnic group and 8 per cent for the

[26] Until 1994, a total of 114,170 settlers were settled on FELDA schemes. This is roughly equivalent to 600,000 people if we take an average household size as 5.21 (UNDP 1995: 47).

Indian ethnic group in the year 1990. The poverty rate for the Malay ethnic group was about 2.5 times higher than that of the Chinese ethnic group in 1970 and was increased to about 3.3 times higher in 1990.

Table 13
Mean Monthly Gross Household Income by Ethnic Group (RM)

	1970	1979	1990	1999	per cent Annual Growth rate 1970-1999
Malay	172	492	940	1,984	36.3
Chinese	394	938	1,631	3,456	26.8
Indian	304	756	1,209	2,702	27.2
Others			955	1,371	
MALAYSIA	264	693	1,167	2,472	28.8
Urban	428	975	1,617	3,103	21.6
Rural	200	550	951	1,718	26.2

Sources; Malaysia 1980, Fourth Malaysia Plan
Malaysia 1986, Fifth Malaysia Plan
Malaysia 1996, Seventh Malaysia Plan
Malaysia 2001, Eighth Malaysia Plan

Table 14
Poverty by Ethnic Group

	1970	1976	1984	1987	1990	Percentage Decrease 1970-1990
Malay	64.8	56.4	25.8	23.8	20.8	32.7
Chinese	26.0	19.2	7.8	7.1	5.7	4.1
Indians	39.2	28.5	10.1	9.7	8.0	18.8
Others	44.8	44.6	22.0	24.3	18.0	4.6
Average	49.3	35.1	18.4	17.3	15.0	18.9

Source: Chamhuri and Surtahman 1999: 374

The higher education level and experienced labour force are another two factors that make the investors more interested in the developed regions as compared to the less developed areas (Meerman 1979). Moreover, there is an inverse relationship between the education level and the poverty rate. This means that when the education level is getting higher, the poverty rate gets lower (Mohd. Yusuf 1990). Also, an educated and experienced worker will migrate to the developed regions and the inexperienced ones will remain in the less developed state (Pryor 1976).

While rural-urban migration usually helps to reduce the over-supply of labour in the rural areas, it also tends to affect the age distribution of the rural population, since most of the migrants are youngsters. Thus, the majority of the rural folk are mostly of old age, and those who are younger than 15 years of age. Official figures have shown that 64.1 percent of farmers in Peninsular Malaysia are over 45 years old. This factor, coupled with increasing production costs, has led many farmers to abandon their land; a problem that is becoming more serious of late. In addition, the old age problem has hampered new technology from being introduced in the rural areas, thus reducing output productivity of the farmers. In fact, there is a high correlation between rural poverty and lack of younger farmers in rural areas (Ishak and Asan Ali 2001).

The migration of youths has left the elderly to work on their land. The children of the small farmers are not interested in agricultural sector, thus resulting in lack of labour in this sector. The manufacturing sector, not only offers higher wages, but also prestige and better living. It is estimated that 30 percent of idle rubber land exists because of lack of labour (Othman 1998). Most of the household heads are old, and being supported by children that are working in other sectors. These farmers do not rely on agricultural income, resulting in low farm productivity and higher average costs (Abdul Malik 1998).

Low monthly income in the agriculture sector was the main rural-to-urban “push factor”[27]. Plantation workers, especially rubber tappers earned lower mean monthly income than other workers in other sectors. For instance, plantation workers only earned mean monthly income about RM258 (RM2.5 = US$1) per month, much lower compared with general labourers (RM315), production operators (RM480), watchmen (RM491), and lorry drivers (RM673) respectively in the electronic and electronic industries in 1989. The services sector, waiters and waitresses in the hotel industry earned mean monthly income about RM630 and office boys in the banking industries about RM492 (Ramachandran and Shanmugam 1995). For the smallholder

[27] Push and pool factors, was mainly discussed in by Todaro (1976), and Harris and Todaro (1970) in the migration theory.

farmer, large fluctuations in price of commodity products (especially rubber)[28], was the other rural-to-urban "push factor" to move to other permanent jobs especially in the manufacturing sector, where the salary was high and relatively consistent (pull factor). Although since 1986, efforts have been undertaken by the Labour Ministry to encourage the unemployed to work in the plantations areas, the results have not been very encouraging (Business Times 1990:47). To overcome this problem government encouraged migration of unskilled foreign workers from Indonesia to work in the agriculture sectors to fulfil the shortage of workers in that particular sector.

The economic growth in Peninsular Malaysia is generally based in more developed states. The government has diversified the economic activities in these regions by introducing manufacturing industries and it relatively reduces the important role of the agriculture sector. In addition, the urbanisation process also creates a large population in these areas. This situation in fact, will not only lead to the income differential between urban and rural areas, but also to the poverty problems in the urban area. This situation is related to education level/ basic experience, old age, a large family, lack of job opportunities and/or inappropriate jobs. In more developed states, manufacturing and services industries are well developed. In contrast, the importance of primary industries is declining in these states (Asan Ali 1998).

There is an inverse relationship between the education level and the poverty rate. This means that when the education level is getting higher, the poverty rate gets lower (Mohd Yusuf 1990). It is undeniable that an educated and experienced worker will migrate to the developed regions and the inexperienced ones will remain in the less developed state (Pryor 1976). This creates a lower technological industrial environment in the less developed state giving rise to such industries as food processing, drinks, furniture, paper products, rubber products and non-metal products. These industries are not only providing lower labour product ability but also lower wages (Anuwar 1983).

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[28] For instance, reduction in international demand, the sport-market price of Rubber Smoked Sheet (RSS) dropped from RM280 per kilogram in January 1974 to only RM0.97 in November 1974 (Stubbs 1983:86).

In fact, most of the professionals, technicians, administrators and managers work in the well-developed regions. This has a close relationship with experience and education level. The percentage of the population that has been to school (literacy rate) in these states is high compared to the less developed states. Most of the people in less developed states work in agriculture, farming, forestry and fishery industries. These states have a slow population growth, as a result of those who are educated and well experienced migrating to the developed regions and those who are inexperienced being left behind. Besides that, these regions also have to deal with a poverty problem. Perhaps only lower-end technological industries are involved in these regions. Of course, these industries are more suitable for the population as they only require inexperienced and less educated labour. Besides that, the number of towns in these states was relatively small compared to the number of towns in the more developed states. Thus, the development in these regions will be slow because it cannot cope with the business flow between the towns/regions (Asan Ali 1998).

One important implication of rural-to-urban migration is the rise in urban poverty. Studies have shown that an influx of migrants from the rural areas, especially the poor, will increase poverty in urban areas. On the contrary, the Malaysian experience is the reverse. According to the official figures, the poverty rate in Peninsular Malaysia for example, has fallen from 22.3 per cent in 1970 to 8.2 per cent in 1985, and further reduced to 4.4 per cent in 1993. In Malaysia, the poverty rate in urban areas decreased from 8.5 per cent in 1985 to 4.1 per cent in 1995 (Ishak and Asan Ali 2001).

The domestic migration for the period of 1971-1990 has helped to reduce the poverty in the rural areas, as well as improve the wealth distribution in the country. However, the migration process also created poverty in the cities. The problems of poverty of Malays in the cities are the extension of the poverty they endured in the rural areas. There is an inverse relationship between the education and poverty levels; the higher the education level of a population, the lower is their poverty level. Increase in the size of the urban labour force mainly expanded through rural migration. Most of the immigrants were who were Malay, unskilled and lacked qualifications for industrial employment and worked at the lowest level (of salary) (Ishak and Asan Ali 2001).

Squatter settlements in Malaysian cities especially in Kuala Lumpur have continued since 1958 in the wake of increased displacement of rural population into towns and cities. The increase of squatter areas appear to have absorbed the largest proportion of Malay migration. While Malays increased from 15 per cent to 25 per cent of the total population of Kuala Lumpur between 1957 to 1970, they accounted for an estimated 80 per cent increase in squatter numbers in that particular period. The urban Malay population rapidly increased since the implementation of the NEP in 1971. This increase in urban Malay has been encouraged by the government and the preferential treatment given to Malay squatters (Johnstone 1983).

Household poverty has tented to increase in urban areas since 1971. There are two areas of concentration of poor; in the less developed states (Kelantan, Kedah, Perlis, Terengganu) and the more developed states (Selangor, Penang, Kuala Lumpur). Ishak Shari (1992) discovered that Terengganu, Kelantan, Kuala Lumpur and Johor had a large number of urban poor households in 1989. In fact, one-third of the urban poor households in that year were from Terengganu and Kelantan.

If these findings are to be accepted, two points need to be emphasized. One, urban poverty in this country is mainly concentrated in states that provide less job opportunities. Thus, these states have a high unemployment rate compared to other states, and many people work in the low paying informal sector. Second, those states that are experiencing a high urbanization rate are also facing a serious urban poverty problem. In fact, a continuous rural-to-urban migration would occur and increase the number of poor in the urban areas. Although the poverty rate in urban areas is declining, there are still many that have low incomes but are not categorized as poor. These people could not afford to own houses and become squatters in the city (Ishak and Asan Ali 2001).

Regional Co-operation

Sub-regional cooperation was one of the regional policies of the Association of Southeast Asian Nations (ASEAN). Three growth triangles involved Malaysia, namely:

Indonesia-Malaysia-Thailand Growth Triangle (IMT-GT), 1994. Consists of the state of Perlis, Kedah, Pulau Pinang, and Perak in Peninsula Malaysia; Special Territory of Aceh, the Provinces of North Sumatra and West Sumatra in Indonesia; and the provinces of Satun, Narathiwat, Pattani, Yala, and Songkhla in Thailand.

Brunei Darulssalam-Indonesia-Malaysia-Philippine East ASEAN Growth Area (BIMP-EAGA), 1995. Consists of the State of Sarawak, Sabah and Federal Territory of Labuan in East Malaysia; Brunei Darussalam; and the provinces of East and West Kalimantan and North Sulawesi in Indonesia; and Mindanao and Palawan in the Philippines.

Indonesia-Malaysia-Singapore Growth Triangle (IMS-GT), 1996. Consists of the states of Johor, Melaka, Negeri Sembilan, and Pahang in Peninsula Malaysia; the Provinces of Riau and West Sumatra in Indonesia; and Singapore.

From sixteen states (including two Federal Territory) in Malaysia, fourteen were involved in one or other of the Growth Triangles. Two states not included in any Growth Triangle were Kelantan and Terengganu, both in the eastern region of Peninsular Malaysia. The main objective of the growth triangles is to improve the living standards and the quality of life of the population of the participating countries (or state at national level) by creating new job opportunities and increased incomes. Under sub-region cooperation, economic development of the participating countries is expected to accelerate by exploiting underlying economic complementarities and comparative advantages of the related sub-region. It is important in terms of trade globalisation and regional integration[29]. The government's effort with the cooperation of neighboring countries to gazette certain regions in economic development cooperation is expected to affect the regional growth pattern.

CONCLUSION

Rural-to-urban and rural-to-rural migration in this country, especially during 1971-1990, has contributed not only to economic development but also income distribution and decreasing poverty. Although the migration process helped to induce economic growth,

[29] Seventh Malaysian Plan 1996, pp.158-159.

and was in line with regional policy to redistribute population especially to the more developed states and at the same time reduce the poverty problem in the rural areas, it also had side effects in urban and rural population. In the urban areas, this included urban poverty, housing problems and a high influx of foreign workers, while in the rural areas, it included an increased dependency ratio, gender inequality, increased poverty and abandoned land (Ishak and Asan Ali 2001). In terms of raising the standard of living of the settlers, FELDA has clearly achieved its objective. However, FELDA is currently facing a critical continuity problem that is the transition phase from the first to the second generation. Among the main problems are poverty, income instability, and other second-generation high out-migration problems (Asan Ali et al. 1999)

Malaysia's economic development was of a dependent type and was regarded as one of the more open economy in the world. The economic growth is due entirely to external factors rather than from internal causes. This can be traced from year 1870 onwards where the British colonial rule designed the Malaysian (Malayan) economy into export-import economy. Rubber and tin were two commodities which made-up the export-import economy. It was considered as the fundamental or backbone of the production and export bases of the economy. These two commodities were produced wholly for exports and were the sterling area's top dollar earner before 1950 (White, Nicholas J. 1996: 179). Tin and rubber industries were mainly dominated by the foreign firms, substantially owned by British (White, Nicholas J. 1996: 179) and followed by Chinese capitalists. Both sector were the mark of the dependent development of the Malaysian economy. The openness of economy continued into the post-war era, whereby reliance on both commodities still dominates. . External trade (both exports and imports) account for a significant and rising portion of its Gross Domestic Product (GDP). In 1960, exports to GDP of 55 per cent increased to 69.4 per cent in 1980 and recorded 89 per cent in 1995. Import proportions to GDP in 1960 were 42 per cent and increased to 69 per cent and 91 per cent in 1980 and 1995 respectively. This reflects the importance of international trade to the Malaysian economic development.

After independence, the base and pattern of dependence of the Malaysian economy has been broadening. The structure of international trade has changed significantly since Independence, especially in the 1960s. The export base has been broadened and diversified, whereby palm oil, pepper and a few minerals such as bauxite and aluminum have been introduced in the export components besides the major commodities of rubber and tin. Prior to industrial development in the 1960s, agricultural products had been predominant. They contributed more than 75 per cent of exports before pre-Independence and decreased to 66.1 percent in 1960. The merchandise share to total exports value has declined since the 1970s. The contribution of this sector fell to 43.6 per cent in 1980 and to 12 per cent in 1999. Rubber initially was the principal export in pre-Independence days. However in the 1960s, oil palm and forestry products contributed significantly, and their shares to the agricultural sector have increased over the years.

Industrialisation in Malaysia depends on trade strategy and industrial policy, which is either by adopting ISI or EOI or both simultaneously. These policies had contributed to the growth of export of manufactured goods. The share of the manufacturing sector outputs to Gross Domestic Products (GDP) has increased from 8.5 per cent in 1960 to 13.1 percent in 1970, 20.5 per cent in 1980 and 35 per cent in 1997. The average share of exports in the total production of the manufacturing sector has increased from 36.5 to almost 50 per cent during the same period. The ISI strategy discouraged export growth and expansion of the manufacturing sector. The contribution of the manufacturing sector to the GDP in the 1960s was less than 10 per cent, the export of manufactures increased very marginally (Mohamed Aslam, 1998). The embarkation of EOI significantly accelerated production of manufactured goods. Exports of manufactures increased from 11 per cent in 1970 to 24 percent in 1980 and 85 percent in 1997.

Not only did manufactured exports increase their share to total exports, but the structure of manufactured exports had also undergone substantial changes. In the 1960s, petroleum products dominated exports, followed by food, beverages and tobacco and wood products. By the 1980s, electrical and electronic goods had become the major export, accounting for more than 61 per cent during 1990-1999 (during 1966-1970, 4.4 per cent), followed by textiles, transport equipment, and wood based products. The success of Malaysia’s export has certain features that is worrying :(i) a very high degree of concentration, in terms of reliance on a few manufactured products - especially electronic - to drive exports, (ii) TNCs continue to dominate Malaysian exports, providing over three-quarters of the total value of manufactured exports, and (iii) the local content of most manufactured exports remains low (Jomo K.S. et. al,1997: 107).

The import structure has also changed from one of a more broad-based imports to one emphasizing imports of intermediate goods and investment goods. In the 1960s, imports of consumption goods were more than 40 per cent on average, while imports of investment and intermediate goods were above 20 per cent. However in 1999, imports of consumption goods slipped to 13 per cent, whereas, imports of intermediate and investment goods were above 40 per cent. The substantial imports of intermediate and investment goods are linked to foreign direct investment, mainly in EOI industries, as mentioned earlier. Also the growth of the imports influenced by the reduction of tariffs of the goods, and the imports of the goods are for "habit formation' and not for "inventory behaviour" (Mohamed Aslam, 1997a).

The transformation of the economy into a more industrialized base is evident from the changing export structure and export mix over the period. The trends of exports and imports have followed the investment trends. This is particularly evident in the period after 1987, consequential to the increased inflow of FDIs into the country, which in turn can be attributed to the intensified efforts of the government to attract FDIs. It can also be discerned that trade is investment-driven, as can be seen from the relationship between total exports and imports as against approved capital investment. For example, in the exports of electric and electronic products, the export trend generally follows the level of approved investments (MITI, 1996: 96). This is particularly evident in the post-1987 period, following the steep rise in FDI inflows. Although electrical and electronic products, including electrical machinery, appliances and parts constituted the major export category in 1985, 1990 and 1994, it has a high import content (MITI, 1996: 96). For example, although the exports of thermionic valves and tubes reached a value of RM11.7 billion and RM33.1 billion in 1990 and 1995, respectively, imports under this same category reached RM10.3 billion and RM39.3 billion respectively (MITI, 1996: 98).

In regards to industrialization, even though the EOI regime had accelerated the growth of manufactures exports, however, the recipient income is not accrued to the country but to the foreign firms. Thus, outflow of the income in terms of dividend, profit and interest increased hugely in 1980s. The EOI strategy has contributed significantly to the GDP and to export growth, besides increasing employment generation, thus decreasing the level of unemployment. The outcome of the strategy has produced overwhelming results and has increased the well being of the people of Malaysia by reducing the poverty level. However, the development produced by the EOI strategy is not real development because the main actor of the development is foreign capital and not the local.

The inflow of FDI has resulted the foreign ownership in Malaysia increased and it was growing in import-substituting industries in the 1960s and in non-resource based export-oriented manufacturing since then, as well especially from the late 1980s onwards. The foreign share of gross fixed manufacturing assets has increased from 19 per cent in 1985 to 40 percent in 1991. Electric/electronic, beverages and tobacco, and some other manufactures (mainly scientific instruments and toys) continue to be strongly dominated by foreign capital, which accounts for more than 60 per cent of such investments. Textiles and garments have been more than 50 per cent foreign-owned, while foreign capital has also owned more than 40 per cent of fixed assets in rubber products, transport equipment and machinery (Rasiah 1995: 112). Japan's share of foreign-owned fixed manufacturing assets in 1993 was 33.6 per cent, followed by Singapore's 14.8 per cent, the USA's 10.0 per cent, Taiwan's 6.9 per cent, the United Kingdom's 6.3 per cent and Hong Kong's 5.0 per cent (Menon and Athukorala 1996). Foreign establishments increased from 7.6 per cent of all firms in 1985 to 16.2 percent in 1991, while industrial output from foreign firms increased from 34.6 per cent in 1985 to 47.1 percent in 1991 (Rasiah 1995: 115).

Most develop mentalists do not deny the contribution of foreign capital in economic (industrial) development, as suggested by the structuralisms and neo-classical theorists. But increased foreign capital participation in the economic development (industrialisation) will eventually create foreign control of an economy, and in certain circumstances will dilute the sovereignty of a particular nation-state. This was evident in Latin America. Industrialisation was supposed to be the way to beat dependency and become self sufficient, now it is increasingly seen that industrialisation has turned out to be a new vehicle of dependency through direct investment and control by foreign capital, especially the capital controlled by transnational corporations (Larrain 1989: 151).

The above matter contrast with what happen in agricultural sector in terms of foreign involvement. In the agricultural, the expansion of the sector largely attributed to the large state capital in the sector (federal: FELDA, FELCRA; states agencies: DARA, JENGKA, KETENGAH, KEJORA and SALCRA), essentially in expanding production of palm oil. The massive new land development, contribution of the palm oil to exports increase dramatically. In agricultural sector, most of capital and income of export from the sector accrued to the state. The state involvement in this area has speed up the exports of the commodity (palm oil) and accumulation of capital increased tremendously (Halim Salleh, 1990). The government since in late 1980s has put less emphasis on rubber and tin sectors. These two commodities are very price sensitivity. Moreover, private sectors no longer keen to invest in the sectors. The major producer of rubber is a smallholder generally. Currently there are about more than 200,000 smallholders in rubber industry. Contribution of the rubber to the exports is getting less significant. In primary commodities sector, palm oil and petroleum has become major foreign exchange earnings. However, most of the production exports to foreign market. More than 94 percent of total of production of palm oil exports to abroad. Within the primary commodities, pattern of dependency has shifted shifted from rubber and tin to palm oil and petroleum.

The land development and industrialisation basically has reinforced of the dependent development, which created by British. The government policy on economy development is basically export-oriented. The only changes in terms of ownership of wealth, restructuring of employment sectors, which depend substantially on the government intervention.

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APPENDIX 1

Location Incentives Under Promotion of Investments Act 1986[a]

a. Pioneer Status

A company granted Pioneer Status will enjoy partial exemption from the payment of income tax. It will only have to pay tax on 30% of its statutory income. The period of tax exemption is five years, commencing from the Production Day as determined by the Minister of International Trade and Industry.

As an added incentive companies located in the States of Sabah, Sarawak, the Federal Territory of Labuan* and the designated “Eastern Corridor”** of Peninsular Malaysia, will only have to pay tax on 15% of their statutory income during the tax exemption period of five years.

* Only applicable to the hotel and tourism industry in the Federal Territory of Labuan.

** The Eastern Corridor of Peninsular Malaysia covers Kelantan, Terengganu, Pahang and the district of Mersing in Johor.

b. Investment Tax Allowance (ITA)

As an alternative to Pioneer Status, a company may apply for Investment Tax Allowance. A company granted Investment Tax Allowance will be given an allowance of 60% in respect of qualifying capital expenditure (such as factory, plant, machinery or other equipment used for the approved project) incurred within five years from the date on which the first qualifying capital expenditure is incurred. The allowance can be utilised to offset against 70% of the statutory income in the year of assessment. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up. The balance i.e. 30% of the statutory income will be taxed at the prevailing company tax rate.

As an added incentive, companies located in the States of Sabah, Sarawak, the Federal Territory of Labuan* and the designated “Eastern Corridor”** of Peninsular Malaysia will be granted an allowance of 80 % in respect of the qualifying capital expenditure incurred. The allowance can be utilised to offset against 85% of the statutory income in the year of assessment.

c. Incentives For Reinvestment

Reinvestment Allowance (RA) is granted to manufacturing companies which have been in operation for at least 12 months and incur qualifying capital expenditure for the expansion of production capacity, modernisation and upgrading of production facilities, and diversification into related products and automation of production facilities.

The RA is in the form of an allowance of 60% of capital expenditure incurred by the companies. The allowance can be utilised to offset against 70% of the statutory income in the year of assessment. Any unabsorbed allowance will be allowed to be carried forward to the following years until it is fully utilised. RA will be given for a period of five (5) years beginning from the year the first reinvestment is made. The RA can only be claimed on completion of the qualifying project i.e. after the building is completed or when the plant/machinery is put to operational use. However, assets acquired for the reinvestment cannot be disposed within two (2) years of reinvestment.

Companies which undertake reinvestment projects in Sabah, Sarawak and the designated "Eastern Corridor" of Peninsular Malaysia will be allowed to utilise the allowance fully to offset against the statutory income for the year of assessment.

d. Infrastructure Allowance

Companies which are engaged in the manufacturing, agricultural, hotel or tourism or other industrial/commercial activities in the States of Sabah and Sarawak and the designated Eastern Corridor of Peninsular Malaysia and which incur qualifying capital expenditure on infrastructure such as reconstruction, extension or improvement of any permanent structure including bridges, jetties, ports and roads, are eligible for an infrastructure allowance of 100%. The allowance can be utilised to set off against 85% of the statutory income in the year of assessment. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised allowance can be carried forward to the subsequent years until it is fully utilised.

[a] *this appendix only list out the promotion that have a location incentive section*

Source: Ministry of International Trade and Industry, Malaysia