Malaysia’s 3rd Pivot: Operationalizing Malaysia Madani Agenda in RMK13

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Economic Prosperity: #1, #2, #3, #4, #6, #8, #9 <Seven economic SDGs>

Social Justice: #5, #10, #16 <Three social SDGs>

Environmental Protection: #7, #11, #12, #13, #14, #15 <Six ecological SDGs>

Total mobilization for effectiveness: #17

The SDG Framework is based on Three Insights

1. Economic prosperity makes it easier to finance investment programs to promote social development and to protect the environment i.e. education and health programs for the poor, and energy transition programs to move from fossil fuel to renewable energy.
2. The sustainability of economic progress, in turn, requires social harmony and environmental health, i.e. no collapse in law and order, and in the ecological system.
3. Proper management of the complex interactions among economic growth, social balance, and environmental health is easiest when communities work together and when countries work together, i.e. SDG #17 is the glue holding the dynamic system together.

The Three Pivots in YB Rafizi Ramli's Speech

- 1st Pivot – The First Malaya Plan 1955-1960 pivoted from colonial focus on revenue extraction and continuation of its rule to raising economic growth through investments in
  - basic infrastructure, and
  - agricultural development → FELDA founded in 1956.
- 2nd Pivot – The Second Malaysia Plan 1971-1975 sought to make economic growth sustainable by increasing economic equality to ensure social harmony → The NEP framework.
- RMK13 → 3rd Pivot. Why?
  - the growth engine has slowed down → 5 governments in 5 years
  - the new global situation has made economic growth also dependent on climate policy and international relations.

Growth slowdown since 2001 (annual, %)

actual growth		(The 3rd Outline Perspective Plan 2001-2010) Mahathir's expectation in 2001
1970-97	1988-97	2001-2010
7.7	9.3	7.5

Actual annual growth rate under successive Malaysia Plan

8th MP	9th MP	10th MP				
2001-2005	2006-2010	2011-2015	2016	2017	2018	2019
4.5	4.2	5.3	4.5	5.7	4.7	4.5

Many Good Suggestions on Raising the GDP Growth Rate

- Free the market to improve national competitiveness, e.g. make domestic monopolies face import competition by reducing import restrictions & joining free trade areas like CPTPP
- Increase the National Talent Pool to achieve the critical mass necessary for knowledge-led growth, e.g.
  - ➢ Strengthen education institutions at all levels by benchmarking international standards e.g. PISA
  - ➢ Stop the brain drain & attract foreign talent → Talent Corp
- Induce firms to modernize their technologies, and break into new high-value industries of the future (e.g. EVs, digital medical devices) → New Industrial Master Plan 2030 in 2023

Post-2000 Growth Slowdown is due to the Collapse in Private Investment

Composition of Investment by Ownership (% of GDP, current prices)

Updated 2020-11-20

	1990	1995	2000	2005	2010	2015	2019
Total	33.9	45.7	25.6	20.0	22.4	25.9	23.0
Govt	12.0	13.0	12.7	11.2	10.1	9.0	6.3
Private	21.9	32.7	12.8	8.9	12.3	16.8	16.7

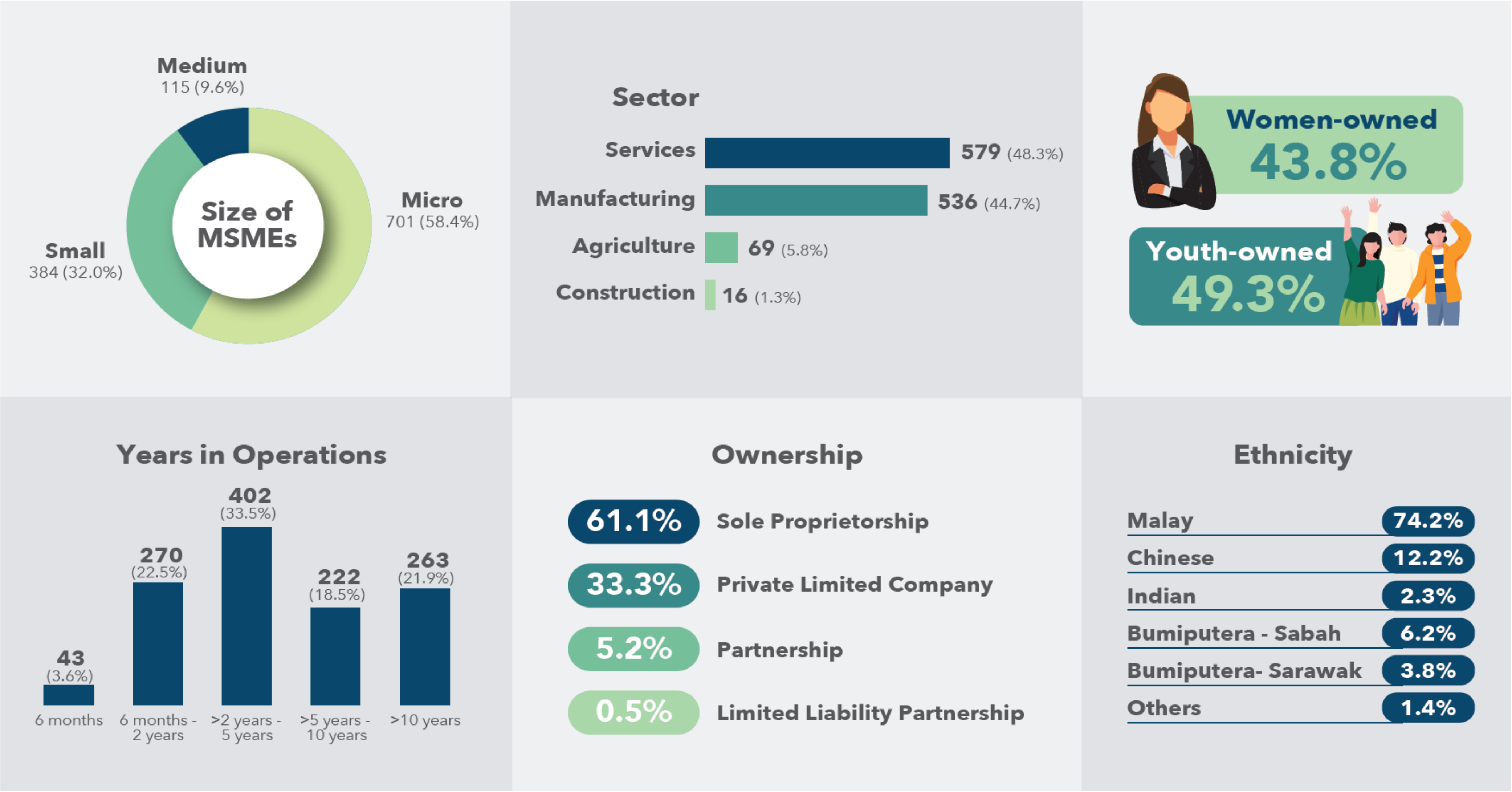
Any policy that can increase the trend GDP growth rate will cause the investment rate to rise. **I will devote rest of talk on how to revive investments that increase economic equality.**

Why the big post-1998 Collapse in Investment?

- Cannot be NEP because NEP has been in existence since 1970. High growth rate of 7.7% despite massive capital flight, brain drain & mis-governance in 1971-1997.
- Two sustained negative shocks in 2001-2019
  1. External blow of diversion of FDI to China after successful US-China bilateral discussions in November 1999 on Chinese membership in World Trade Organization (WTO) → negative FDI shock.
  2. An internal blow (self-inflicted) to economic vitality of Malaysia's SME sector → post-1998 negative policy shock to SME investment.

A total of 1,200 MSMEs responded to the survey whereby 83.1% (997) were beneficiaries and 16.9% (203) were non-beneficiaries of development programmes by SME Corp. Malaysia.

Chart 1: Profile of Respondents



84.2% of SMEs in 2021 were owned by Bumi-puteras

The Size Distribution of European Firms is PYRAMIDAL

(% of total number of firms in each size category)

Source: Johansson (1997)

Table 25 The size distribution of firms (%)

	All sectors		
Country	Small	Medium	Large
Germany	92.3 (5)	6.5 (8)	1.2 (6)
France	91.2 (7)	7.3 (6)	1.6 (5)
UK	89.7 (12)	8.7 (2)	1.6 (4)
Sweden	90.2 (10)	8.0 (3)	1.8 (1)
Italy	96.3 (1)	3.2 (12)	0.5 (12)
Spain	93.7 (2)	5.5 (11)	0.8 (11)
Belgium	90.7 (9)	7.6 (4)	1.7 (3)
Portugal	92.3 (6)	6.8 (7)	0.9 (10)
Denmark	93.4 (3)	5.7 (10)	1.0 (9)
Luxembourg	90.1 (11)	8.8 (1)	1.1 (7)
Finland	91.0 (8)	7.3 (5)	1.7 (2)
Norway	92.5 (4)	6.4 (9)	1.1 (8)
Average	91.8	6.9	1.3

Note: Rank in parenthesis.

Size Distribution of Malaysian Firms is not pyramidal, and increasingly less pyramidal as middle is continually squeezed

(% of total number of firms in each size category in that year)

Size of firms	2016	2019	2022
Micro	73.3%	76.2%	76.7%
Small	22.8%	19.6%	19.2%
Medium	1.8%	1.6%	1.6%
Large	2.1%	2.7%	2.6%
Number of Firms	1,109,840	1,214,420	1,204,929

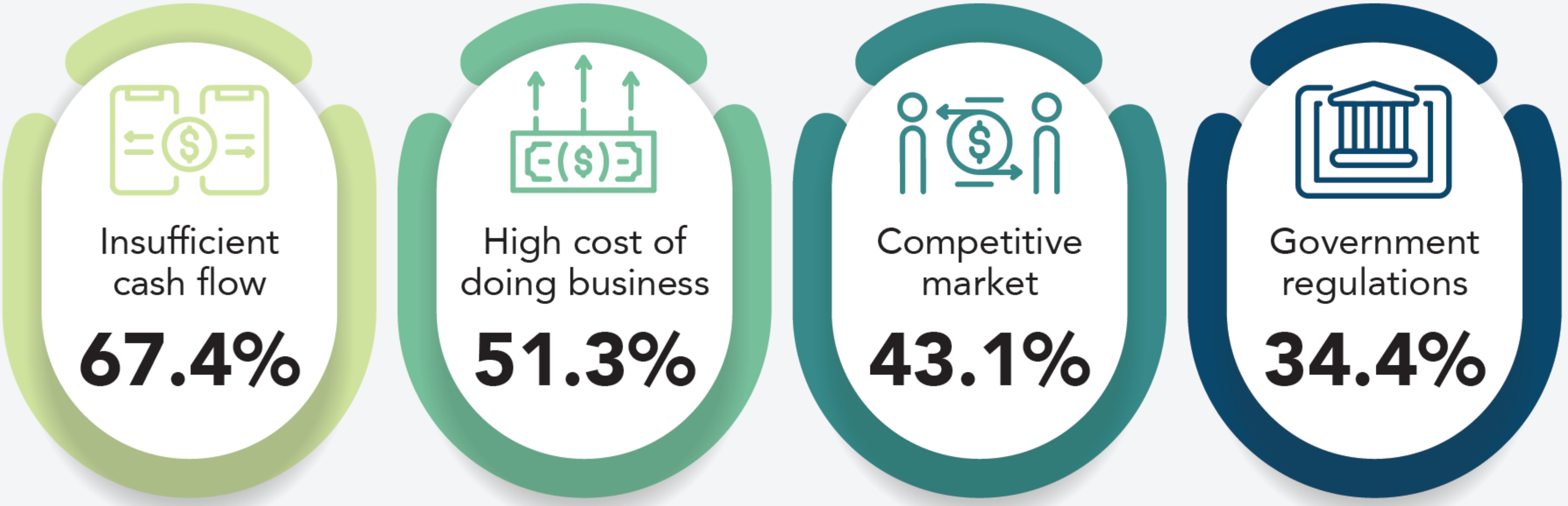
The Size Distribution of SMEs Changed became less pyramidal over 2016-2022

- The proportions of micro firms and large firms increased in this period, while the proportions of small firms and medium firms fell. Whatever that is preventing micro firms from becoming small firms, and small firms from becoming medium firms, must also be preventing medium firms from becoming large firms.
- **How did the proportion of large firms get bigger over time?** Firms established by FDI are invariably large firms. When domestic conglomerates enter into new businesses, they do not set up workshops, they set up factories with modern technology and at economies of scale

2021 SME Survey: What are your biggest problems?

Insufficient Cash Flow and High Cost of Doing Business

Insufficient cash flow was the top concern among MSMEs, mainly due to the higher price of raw materials & packaging, rental & utility charges and lower demand for goods & services. Key issues faced by MSMEs were as follows:



Cash Flow Problems of SMEs and their Debilitating Results

- When several buyers are not able to pay their bills on time, the SME does not have the working capital to buy inputs and keep workers to maintain production at full capacity → make less profits.
- If the SME had been able to get a working capital loan from a bank at the same the interest rate that the bank charges GLCs, the decline in production, employment, and profit would have been avoided.
- As SMEs have such serious trouble in getting working capital loans, they definitely have no access to longer term loans to fund investments for technological upgrading and capacity expansion to achieve economies in scale to become globally competitive and move up the value chain.

Artificial worsening of “capital shortage” for the SME sector since 1998

- To facilitate repair of the damaged balance sheets of financial institutions from the 1997 Asian Financial Crisis, 10 domestic anchor banks were created by 2002 through merging the 22 domestic commercial banks, 33 finance companies, and 2 merchant banks.
- By 2023, the number of domestic anchor banks had gone down to 8, with four of them being state-owned banks (SOBs) holding 63% of total portfolio. Independent finance companies had a negligible role.

Forced merging of financial institutions in response to 1997 Asian Financial Crisis

	1990	2002
Domestic Commercial Bank	22	10
Foreign Commercial Banks	16	13
Finance Companies	45	12
Merchant Banks	12	10
TOTAL	95	45

In 2007, BNM reported zero finance companies because they have all been "rationalized" into commercial banking groups. By 2011, the number of domestic commercial banks had been reduced to 8 from 10 in 2002.

In response to "capital shortage' at the SMEs, the Government established SME Bank in 2005

- In 2021, SME bank loans is 0.49% of the sum of corporate bonds outstanding and total business loans of the banking sector (commercial banks, Islamic banks and investment banks) -- Support from SME Bank is piddling pittance
- 2022 US News ranking of "ease of access to capital for entrepreneurship": USA = 100, UK = 60.6, China = 52.8, Thailand = 16.8, Indonesia = 16.5, Vietnam = 16.1, India = 15.9, Malaysia = 12.9
- The serious shortage of working capital is why many people have taken up the risky profession of "Ah Long lenders".

How have Malaysian SMES reacted to their frequent cash flow problems which caused decline in production, employment, and profit?

They attempted to lower their production costs by lobbying for more and more cheaper unskilled workers from abroad when they should be asking for solutions to the shortage in working capital and investment capital.

Big banks behave differently from small-medium banks and finance companies (SMBs & SMFCs)

- **Large banks do not like to lend to SMEs** because the cost of making a $1 billion loan is much lower than the cost of making 100 $10 million loans.
- SMBs and SMFCs would also prefer to lend to large firms but they cannot provide the full range of financial services demanded by large firms as cheaply as the large banks. And, when there are many large banks and many SMBs, **SMBs and SMFCs are forced to make lending to SMEs their specialty because they are locked out of lending to large firms.**

Malaysia should start issuing licenses to small-medium banks (SMBs) and finance companies (SMFCs)

- Give operating license to qualified Ah Long financiers to open SMBs and SMFCs. **License 10 new SMBs and 10 new SMFCs, with attention to geographical concentration of manufacturing SMEs.**
- To also help fund government programs and create SMBs, the government should divide one or two of the SOBs into five smaller banks each and sell them.
- Proper regulation of SMBs-SMFCs → no accidental strangling of SMBs with uniform regulation of banks regardless of size. Unlike SMBs, big banks pose systemic threats (too big to fail) and hence should be regulated more stringently than SMBs.

There is now a New International Environment that increases SME demand for investment-financing

1. **Climate Change: The Dictate of Net Zero Emissions** EU-North America-Northeast Asia will impose tariffs on goods from countries with weak climate action policies → necessity for green transformation for survival of SMEs
2. **Cold War 2.0** USA-Europe-Japan (UEJ) are importing more from ASEAN and less from China. Who should supply the additional ASEAN exports to USA-Europe?
   - FDI expand i.e. foreign firms investing in Malaysia to to start exporting to USA-Europe AND/OR
   - SMEs expand to export more to USA-Europe, and to supply more inputs to FDI (displace more imported inputs)

RMK13 can eliminate the SME vicious cycle of low profitability, low productivity, low wages, and labor shortage

- SMEs lack adequate access to working capital which makes them operate below production capacity frequently, profit not maximized
- SMEs lack access to fixed-asset-investment capital which prevents them from (a) expanding capacity to achieve economies of scale and (b) upgrading technology → bad news for global competitiveness, product innovation, and net zero emissions.
- A modernized SME sector will have substituted capital for foreign workers, and will also be able to pay higher wages to domestic low-skill labor → achieving EPU's progressive wage agenda.
- In short, solve the SME capital shortage problem → Malaysia will also move up the value chain with a more equal distribution of income.

Thank you
Please give me comments
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