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AT THE LAUNCH OF  
“MALAYSIA: POLICIES & ISSUES IN ECONOMIC DEVELOPMENT”  
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Ladies and Gentlemen

I am delighted to be here this morning to join all of you in celebrating the launch of the publication of this wonderful collection of essays entitled “Malaysia: Policies & Issues in Economic Development”.

2. As an Eminent Fellow of ISIS, I do so with a sense of pride. This book was conceptualized as a publication to coincide with a significant milestone in ISIS’s history – the 25<sup>th</sup> anniversary of its establishment. This book also pays tribute to all those who founded ISIS, gave it direction over the years, and steered it to its current stage of development. In particular, I would like to pay tribute to the late Tan Sri Nordin Sophe, Tan Sri Jawhar Hassan and Datuk Dr Mahani Zainal Abidin. The celebration of this anniversary is also an opportune time for us to evaluate the country’s development record, draw lessons and assess future challenges.

3. Malaysia is, by any measure, a success story. We have emerged to become one of Southeast Asia’s most developed and prosperous countries. The UNDP regards Malaysia as a country with a high development index, being on track to achieve or exceed the Millennium Development Goals by 2015. The economic leap we have made is remarkable vis-a-vis countries we were on par with half a century ago. At

independence in 1957, Malaya was comparable with Sri Lanka, the Philippines, Ghana, Morocco and Senegal in terms of per capita income.<sup>1</sup> Fifty years on, the country's per capita income had increased sixfold, to reach a level that is double that of Sri Lanka, three times that of the Philippines and Morocco and six times that of Ghana and Senegal. Moreover, progress was not limited to income growth. Poverty has been reduced drastically. There have been significant improvements in life expectancy, infant mortality, literacy and other indicators of human development.

4. The question as to why some countries grow rapidly while others grow slowly or not at all constitutes one of the most important in all of economics. It is a question that has kept economists busy for decades, and, I expect, will continue to do so for some time yet. When I was in graduate school, I learned something about the growth performance of the East Asian countries during the post-Second World War period, first that of Japan then those of the newly-industrialising tiger economies, namely South Korea, Taiwan, Hong Kong and Singapore. These countries had grown at an average of 6% per annum in per capita terms over a sustained period. To put things in perspective, compare this with the growth record of the leading economies during the Industrial Revolution in the late eighteenth and nineteenth century (around 1-1.5% per annum) or the growth record of the advanced capitalist economies during the first three decades of the post-Second World War period (around 3% per annum). To put it simply, these East Asian countries underwent the fastest economic transformation in human history up to then, to be surpassed only by developments in China and India, and Brazil, in recent years. The spectacular economic performance of these countries naturally generated a lot of interest in the so-called East Asian model of development, and in particular on the extent to which this model could be replicated in other countries.

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<sup>1</sup> 1990 Geary Khamis \$.

5. In certain important respects, I would argue Malaysia makes a more suitable model for other developing countries than the original East Asian tiger economies of Japan, South Korea, Taiwan, Hong Kong and Singapore. This is because Malaysia shares common features with many countries in Asia, Africa and, to a lesser extent, Latin America that makes it an ideal case study.

6. First, Malaysia is a resource-rich country, in contrast to the East Asian tiger economies that are resource-poor. It is a well-known fact among development economists that many resource-rich developing countries have found natural resources to be a curse rather than a blessing. They have experienced little more than short-lived resource booms, their economies expanding rapidly while resources last, but contracting once these have been exhausted. Some have succumbed to the dreaded Dutch disease, with its attendant ills of accelerating inflation, declining export of manufactures and rising unemployment. Many have squandered their resource riches on wasteful expenditures. Malaysia remains one of the few that have managed to transform its rich natural resource base into sustainable development. Resource rents were productively invested in primary and manufactured exports, in improving infrastructure and in strengthening the human capital base. Within a span of 50 years, the economy underwent significant structural transformation, from one that was heavily dependent on primary commodities to one that is more broad-based. Gaining a better understanding of how this was achieved is not only of academic interest to scholars but should be of relevance to policy-makers in other countries.

7. Second, Malaysia shares with many countries in the developing world in having a multi-ethnic, multi-religious population. This is in contrast to the East Asian societies that are largely homogenous. Governing a country that is multi-ethnic and multi-religious is very different from governing one that is homogeneous. In Malaysia, particularly in the early years, ethnic groups differ sharply in occupational pattern, income level,

geographic location, language and appearance. This makes promoting national unity of utmost importance for continued political stability and economic progress. The New Economic Policy (NEP), formulated after the 1969 riots, was an ambitious socio-economic restructuring program that had as its two major objectives, “the eradication of poverty among all Malaysians, irrespective of race,” and “the restructuring of Malaysian society so that the...identification of race with economic function and geographical location is reduced and eventually eliminated”. These objectives were to be undertaken “in the context of rapid structural change and expansion of the economy so as to ensure that no particular group experiences any loss or feels any sense of deprivation in the process”.

8. In societies where political dominance by one ethnic group is combined with economic weakness, state intervention in the economy is likely to be widespread and pervasive. In such a situation, the state has an important role to play in ensuring an equitable distribution of income between people, between groups of people and between regions. When it has worked well, the result has been a developmental state that has promoted industrial transformation and stimulated economic development. When it has not worked well, state intervention has verged on the predatory, extracting resources and providing nothing much of value in return.

9. Today the results of the NEP are hotly debated. On the one hand, the NEP is credited with restoring social and political stability to the country by bringing about growth with equity. The argument can be made that the Malaysian experience is a classic illustration that development, particularly in multi-ethnic societies, consists of more than just unleashing market forces. It demands economic growth that is broadly shared among all citizens, as well as the necessary institutional environment to help bring it about.

10. On the other hand, some have argued that these results have been achieved at a high cost. That it has resulted in greater income inequality within the Malay community; that it has led to gross inefficiency in the public sector; that it has encouraged a dependency mentality among sections of the population; and, that it has increased the scope for patronage and rent-seeking.

11. The debate continues.

12. That Malaysia was able to prosper is due in large part to political resolve, economic pragmatism and effective implementation of policies. A well-conceived policy shift from import substitution in the 1960s to export-oriented industrialization in the 1970s and 1980s ensured continuous rapid growth. In response to the economic slowdown in the mid-1980s, the government moved away from state-led industrialization and promoted private investment across a broad range of sectors, thereby significantly improving productivity and attracting large inflows of foreign capital. As a result of these and other macroeconomic adjustments, the economy grew rapidly until it was cut short by the Asian financial crisis in 1997. Despite initial scepticism, criticism and opposition at home and abroad, it is now generally acknowledged by many economists that the government's policy measures, including controls over short-term capital flows, helped the country weather the Asian financial crisis and put it on the road to recovery.

13. Some old challenges remain; and new ones have appeared on the horizon. Malaysian policy-makers are acutely aware of the changes that need to be made if the country is to continue to prosper. This begins with the acknowledgement that policies that have worked in the past are unlikely to work in the future. Malaysia today finds itself squeezed, in the so-called middle-income trap, between the low-cost economies of China and Vietnam and the high-technology economies of Japan and South Korea. Malaysia's comparative advantage in the export of manufactured labour-intensive

products has been fast eroding. To keep internationally competitive, the country needs to take a big step up the technological ladder by moving into high-technology and knowledge-intensive industries. It is well understood that Malaysia's past growth was driven mainly by large increases in the use of inputs of labour and capital. Future growth will have to come from productivity gains and technological breakthroughs. This in turn requires the country to vastly improve its human capital base by investing heavily in training and education, and promoting research and development.

Ladies and Gentlemen

14. Allow me to take a moment to pay tribute to a person who is no longer with us today. Dato Dr Zainal Aznam was a distinguished scholar and one of the two advisors of this book. He is also the author of the final chapter of this book entitled "Looking Forward". I first met Dr Zainal when we were both students at Oxford University, he a doctoral candidate and I an undergraduate. To a young student like myself, he was nothing short of inspirational. We remained good friends since then. Later, when I embarked on my doctoral studies, I drew on the work of Dr Zainal and other excellent scholars like him.

15. It was Dr Zainal who early on impressed upon me the importance of institutions in the development process. As someone who received much of his academic training in economics, it should not come as a surprise that I believe incentives to be hugely influential in shaping human behaviour. Create the right incentives and people will respond accordingly. It is only when China and India reformed their incentive structure were they able to achieve high growth rates. However, for growth to be sustainable, these incentives must be embodied in institutions. The ability to provide the appropriate institutional environment for markets to flourish and operate efficiently is essential to sustainable development. Countries that have failed in this respect have experienced stagnating or falling incomes and persistent poverty. This institutional environment

should include the protection of property rights, the rule of law underpinned by a strong legal system, an independent judiciary and the protection of the environment. There must also be incentives for governments to provide good governance. This can be achieved through mechanisms such as the separation of powers, readily available avenues for the public to monitor public behaviour and rules that inhibit corruption. They all contribute toward the effective and efficient functioning of a modern economy.

16. Today, I would like to add my voice to the many tributes to Dato Dr Zainal. I will always cherish his friendship, his independence of mind and his unrelenting search for solutions to combat economic backwardness and achieve social justice. With his passing, our nation has lost a great intellectual resource, and someone who embodied the spirit of dedicated public service.

17. In the closing chapter of the book, Dato Dr Zainal described Malaysia's development path as "marked by learning, by doing, an absence of a fixation on ideology, a good measure of pragmatism, and a continuing obsession with growth and distribution". We could do worse than to take these words to heart.

18. In closing, I would like to congratulate the authors, editors, advisors and all those involved in the production of this much-needed study. It will be an excellent intellectual resource for scholars and policy makers in our continuing journey in economic development.

19. It now gives me great pleasure to launch "*Malaysia: Policies & Issues in Economic Development*".