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Doing Business In Malaysia

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Executive Summary

The importance of international trade to the Malaysian economy can hardly be exaggerated. Trade represents a lifeline for the Malaysian economy. Trade has brought much prosperity to the Malaysians. Export oriented industrialisation has converted the labour-surplus economy into a labour-deficit one. The incidence of poverty has fallen from 42.4 percent in 1976 to 17.1 percent in 1995. Trade has also contributed much to the structural transformation and modernisation of the economy. Had Malaysia been a closed economy, Malaysia would have shared the same fate as some other less developed countries that remain economically backward. Its external trade policy has paved the way for greater inflows of foreign direct investment, as foreign direct investors are not so much interested in serving the small domestic market as serving the vast external market. The large inflows of foreign direct investment have conferred positive effects on the domestic economy. These include technological improvements, broader production spectrum, and new market dimensions. The developments in the export sector have also contributed directly and indirectly to the development of the non-trade sector such as the construction sector. All this has meant significant improvements in the overall living standards for the Malaysians. Internationalisation has provided employment opportunities, thereby raising their standards through higher and more stable earnings.

Doing Business in Malaysia

Introduction

Peninsular Malaysia has an area of 131,582 square kilometers. It shares a border to the north with Thailand and, to the south, with the Republic of Singapore across the Johore Straits. The Federation of Malaysia is composed of two major landmasses: Peninsular Malaysia, the 11 states that, before 1963, made up the Federation of Malaya; and East Malaysia, which consists of Sabah and Sarawak, two former British colonies in Northern Borneo.

Malaysia is a South East Asian country with a culturally diverse population of 22 million people in 1999. The largest ethnic group is the Malay, which total 12.1 million people (55% of the population), then the Chinese, with 7.48 million people (34% of the population), followed by Indian with 2.2 million people (10% of the population) and other ethnic groups with 0.22 million people (1% of the population). In terms of religion, Malaysia demonstrates a unique blend of eastern religions – Islam, Confucianism, Buddhism, Taoism, Hinduism and Animism.

Economically, Malaysia has undergone quite a remarkable transformation from a traditional, agricultural-based economy to a modern industrial-based economy in a mere 30 years. The Malaysian government has undertaken a serious drive towards industrialization during this period. Malaysia's trade with the world has increased in the past ten years, growing from RM 128.7 billion in 1989 to RM 515.1 billion in

1998. The Malaysian Ringgit (RM) is the unit of currency used in Malaysia and 4RM is the approximate equivalent to 1US dollar.

Malaysian Economy

International Trade has always been the lifeblood of the Malaysian economy. Its importance to the economy has grown stronger over the years. The composition and direction of trade flows have changed significantly, reflecting the dramatic transformation of the primary-producing economy into a rapidly industrializing one. Interestingly, structural changes in the Malaysian economy during the last three decades or so have enhanced the economic openness of the country so much so that Malaysia continues to project itself as one of the most open economies in the world. In 1998, the Malaysian economy had an exports-GNP ratio of 84.3 percent. Exports represent a major determinant of the state of the economy. Malaysia's rapid economic growth at the annual average rate of about 7.0 percent since independence in 1957, has much to do with Malaysia's impressive export performance. Imports have also contributed much to the economic development of the country, by providing not only competitively priced consumer and capital goods, but also intermediate inputs for Malaysian manufactures that have rendered Malaysian-manufactured exports competitive in world markets.

Malaysia recorded total exports of RM286.8 billion and total imports of RM228.3 billion in 1998, compared to RM221.4 billion and RM221.0 billion respectively in 1997 (see Table 1). Exports grew 29.8 percent over that of 1998 while imports recorded a lower growth rate of 3.3 percent (see Table 2).

Table 1 - Total Trade and Balance (1991-1998) Value (RM Billion)

	1991	1992	1993	1994	1995	1996	1997	1998
Export	94.5	103.7	121.2	153.9	185.0	196.7	221.4	286.8
Import	100.8	101.4	117.4	155.9	194.3	197.3	221.0	228.3
Balance	-6.3	2.3	3.8	-2.0	-9.3	-0.6	0.4	58.4

Source: Department of Statistics, Malaysia 1999

Table 2 - Growth of Trade (1991-1998) Value (RM Billion)

	1991	1992	1993	1994	1995	1996	1997	1998
Export	18.7%	9.7%	16.9%	27.0%	20.2%	6.3%	12.6%	29.8%
Import	27.4%	0.6%	15.8%	32.8%	24.6%	1.5%	12.0%	3.3%

Source: Department of Statistics, Malaysia 1999.

Commodity Exports

Although Malaysia is a relatively small economy by any measure, it has had a fairly high profile in the international marketplace as the number one exporter of several primary commodities, including rubber, tin and palm oil, and more recently, as the leading exporter of several electrical and electronic goods, such as air-conditioners and semiconductors. The commodity composition of Malaysian exports has been changing, with primary products declining in importance relative to manufactures. The export base has also broadened as a result of efforts at diversification. At the time of independence in 1957, natural rubber and tin accounted for 60 per cent and 11 per cent of the countries export earnings respectively. Malaysia contributed about 33 per cent and 37 per cent of the total world output of natural rubber and tin, respectively, in 1957. A subsequent export diversification drive led to the emergence of palm oil and timber as the major export commodities, with Malaysia accounting for about twothirds of the global exports of tropical hardwoods in the 1990s. Export-oriented industrialization initiatives undertaken in the early 1970s have brought about significant changes in the composition of exports, with manufactures playing an increasingly important role. The share of natural rubber in total exports has fallen sharply from 55.1 percent in 1970 to 2.2 percent in 1998. Likewise, the relative importance of tin had declined from 14.0 percent to 0.7 percent during 1970-1998. Timber exports as a proportion of total exports increased from 2.1 percent in 1970 to 4.0 percent in 1980 before falling gradually to 3.3 percent in 1998. Palm oil exports, too, have exhibited a similar pattern, its share rising from 1.7 percent to 14.3 percent between 1970 and 1985 and declining to 5.2 percent in 1998. Petroleum emerged as a major export item in the late 1970s, with the intensification of oil exploration activities. All in all, the share of primary commodities as a percentage of total exports has fallen from 80.1 percent in 1970 to 23.8 percent in 1998.

Exports of Manufactured Goods

The contribution of manufactured goods to total exports has expanded significantly from 11.9 percent in 1970 to 69.8 percent in 1998. As in the case of primary exports, there has been a heavy commodity concentration in manufactured exports. As a matter of fact, electronics and electrical goods, textiles, clothing and footwear have constituted the bulk of Malaysia's manufactured exports. It is remarkable that the share of electronic and electrical items in total manufactured exports has increased to 58.6 percent in 1998 from 8.5 percent in 1970. The share of textiles, clothing and footwear in total manufactured exports rose from 5.2 percent in 1970 to 12.8 percent in 1990 before declining to 7.2 percent in 1998.

Within the electronic and electrical category, electronic components have figured most prominently, although their relative importance in total exports has declined somewhat since 1992. By contrast, exports of electrical appliances and machinery have grown steadily in importance, their combined share rising from 11.5 percent in 1990 to 38.4 percent in 1998. It is estimated that a typical electronics assembly plant in an Export Processing Zone (or Free Trade Zone) sources as much as 60 percent of its material inputs from overseas (Verbruggen, 1984). Over the years, however, the local content of Malaysian manufactured exports has increased significantly, thanks to growing linkages between foreign-owned export manufacturing activities and domestic industries through subcontracting transactions. In the 1990s, the profile of Malaysian manufactured exports underwent significant changes, with a widening range of products. Exports of rubber products, paper and paper products and petroleum products grew at a rate of not less than 25 percent per annum in the 1990s. Transport equipment registered the highest average annual growth of 40.3 percent in the 1990s (Government of Malaysia, 1996).

Table 3 indicates the growing importance of the manufacturing sector in the Malaysian economy**.** The average annual growth rate of the manufacturing sector from 1990 to 1995 was 13.3 percent. The growth of the manufacturing, services and construction sectors provided the major impetus to overall economic growth. In 1990, the share of Gross Domestic Product (GDP) of the manufacturing sector was 26.9 percent. This grew to 33.1 percent in 1995 and to 37.5 percent in the year 2000. The manufacturing sector thus had the largest share of GDP compared to the other sectors (see Table 4).

In line with the strong domestic demand and significant expansion of the leading sectors of the economy, the service sector is estimated to grow at 8.4 percent per annum, while its share of Gross Domestic Product (GDP) expanded to 43.9 percent in the year 2000. The service sector as a whole grew at an average rate of 9.3 percent per annum between 1990 and 1995, with its share of GDP reaching 43 percent. Table 4 shows GDP by industry between 1990-2000.

Table 3 Growth of Manufacturing Industries, 1990 and 1995 (RM million)

Industry	1990	1995	Average Annual Growth Rate (1990-95) %
Resource-Based	12,482	19,288	9.1
Food Manufacturing	1,106	1,680	8.7
Oils & Fats	1,610	1,773	1.9
Beverages Industries	436	489	2.3
Tobacco Manufacturing	501	447	-2.3
Wood & Wood Products	1,305	2,226	11.3
Chemical & Other Chemicals	3,491	5,671	10.2
Industrial Chemicals	2,282	3,485	8.8
Plastic Products	495	927	13.4
Petroleum Refineries	402	597	8.2
Rubber Re-milling & Latex	640	676	1.1
Rubber Products	1,161	2,516	16.7
Non-Metallic Mineral Products	1,664	2,945	12.1
Glass & Glass Products	222	311	7.0
Non-Metallic Products	1,442	2,634	12.8
Non-Ferrous Metal	166	268	10.1
Non-Resource-Based	8,858	20,537	18.3
Textiles & Clothings	1,458	2,557	11.9
Manufacturing of Textiles	857	1,751	15.4
Wearing Apparel	601	806	6.0
Iron & Steel Basic Industries	665	1,377	15.7
Fabricated Metal Products	615	2,863	36.0
Electrical & Electronic Products	5,052	12,068	19.0
Manufacture of Machinery	343	1,076	25.7
Electrical Machinery	4,709	10,992	18.5
Transport Equipment	1,068	1,672	9.4
Total	21,340	39,825	13.3

(Source: Seventh Malaysia Plan 1996, p.265)

Table 4 Gross Domestic Products by Industry of Origin, 1990-2000

	RM million (in 1978 prices)			Share of GDP (%)		
Sector	1990	1995	2000	1990	1995	2000
Agriculture	14,827	16.406	18,460	18.7	13.6	10.5
Mining	7,757	8,938	10,023	9.8	7.4	5.7
Manufacturing	21,340	39,825	66,251	26.9	33.1	37.5
Construction	2,832	5,277	8,560	3.6	4.4	4.8
Electricity	1,526	2,823	4,686	1.9	2.3	2.7
Transport	5,487	8,787	14,599	6.9	7.3	8.3
Hotel & Restaurant	8,806	14,568	22,378	11.1	12.1	12.7
Finance & Insurance	7,758	12,884	20,977	9.8	10.7	11.9
Government Services	8,447	11,683	14,354	10.6	9.7	8.1
Other Services	1,678	2,436	3,749	2.1	2.0	2.1
Imputed Bank Service Charges	4,076	8,414	13,242	5.1	7.0	7.5
Import Duties	2,947	5,101	5,840	3.7	4.3	3.2
GDP at Purchasers Value	79,329	120,316	176,635	100.0	100.0	100.0
PRIMARY SECTOR	22,267	24,665	27,337	28.1	20.5	15.5
SECONDARY SECTOR	23,832	43,894	71,802	30.0	36.5	40.6
TERTIARYSECTOR	33,230	51,757	77,496	41.9	43.0	43.9

(Source: Seventh Malaysia Plan 1996, p:52)

The performance of the financial sub-sector was enhanced by continuous modernization of the sector. The service sector must, therefore, be more competitive and prepared to enter international markets more extensively. The service sector will increasingly become a major source of growth in the economic transformation process. In an effort to accelerate the industrialization process, the Malaysian government has encouraged investors from many parts of the world to invest in Malaysia. Foreign investment has played, and will continue to play, an important role in the economic development of Malaysia. With regard to the source of Foreign Direct Investment (FDI), Japan, Taiwan, the United States, France and Singapore account for RM40.56 billion (65.8 %) of total FDI in Malaysia**.** Japan provides the highest contribution towards FDI in Malaysia with a total of RM11.91 billion (19.3%), followed by Taiwan with RM10.32 billion (16.8%) and the United States of America with RM9.91 billion (16.1%). Table 5 provides an indication of the importance of FDI in Malaysia.

Table 5 Foreign Direct Investment in Approved Projects by Country, 1991-95 (RM million)

Country	1991	1992	1993	1994	1995	6MP[1]	% of Total
Japan	3,705.90	2,684.30	1,661.20	1,765.20	2,096.30	11,913.00	19.30
Taiwan	3,607.20	1,500.00	894.20	2,874.30	1,442.20	10,317.80	16.80
USA	1,798.40	3,298.70	1,757.70	1,253.20	1,801.60	9,909.50	16.10
France	27.00	4,066.0	30.80	49.60	97.90	4,271.20	6.90
Singapore	1,114.30	442.40	521.90	1,063.50	1,008.70	4,150.80	6.70
Republic of Korea	1,818.70	99.40	111.10	8.80	604.40	3,042.40	4.90
Australia	410.50	2,125.60	52.10	175.60	139.50	2,903.30	4.70
United Kingdom	546.20	1,304.00	44.10	94.10	189.90	2,178.30	3.50
Indonesia	1,242.90	480.20	245.10	-	88.00	2,056.20	3.30
Hong Kong	600.60	78.60	93.80	873.90	175.20	1,822.10	3.00
Germany	193.30	72.80	64.90	655.40	149.50	1,136.00	1.80
Others	1,990.40	1,620.20	810.40	2,125.30	1,350.30	7,896.60	12.80
Total	17,055.30	17,772.10	6,287.20	11,339.10	9,143.50	61,597.20	100.00

(Source: Seventh Malaysia Plan, 1996 p.275)
Note:
[1] 6MP (Sixth Malaysian Plan) from the year 1991-1995

Export Barriers

Ariff (1991) stated that Malaysia's export drive has by no means been an easy task. It had to overcome protectionist forces in export markets and had to face competition from the Newly Industrialising Economies (NIEs) and other Developing Countries such as Indonesia. The exports of textiles, clothing and footwear, wood and wood products, foodstuffs, and oils and fats, in particular, have encountered tariff and non-tariff barriers and stiff competition.

Malaysian manufactured exports are hurt more than primary commodity exports by protectionism in developed countries. Among the primary commodities, palm oil has been singled out for special attention by the protectionist forces in these markets. In the European Community, for example, tariffs on palm oil escalated with the degree of processing, while palm oil imports in crude form were duty-free. In Japan, refined palm oil imports remained tariff-bound, although tariffs on crude palm oil were abolished in 1985. In the United States market, the Malaysian palm oil recently had to fight off a negative campaign launched by the United States soybean industry against tropical vegetable oils.

The developed country tariffs on textiles; wood products and electrical and electronic goods are of particular concern to Malaysia. The United States, for example, imposed tariffs of over 20 percent on footwear and woven textiles. In the US market, electronic components exported by the American multinational corporations do not face tariffs, but electrical goods such as television sets and radios are subject to tariffs. The European Community, too, imposed a 14 percent levy on such items. The non-tariff barriers such as quantitative restrictions in advanced country markets are of greater concern to Malaysia. The Japanese market remains impenetrable for Malaysian textiles, except in the case of basic wearing apparels such as jeans. Japan's quota restrictions have affected Malaysia's canned pineapple exports. Other export items subjected to quota controls include veneer sheets and plywood, garments, iron and steel products, and toys. Import restrictions would have forced the Malaysian manufacturing sector to source their inputs locally, which would have made Malaysian manufactures not competitive in the international arena.

The importance of international trade to the Malaysian economy can hardly be exaggerated. Trade represents a lifeline for the Malaysian economy. Trade has brought much prosperity to the Malaysians. Export oriented industrialisation has converted the labour-surplus economy into a labour-deficit one. The incidence of poverty has fallen from 42.4 percent in 1976 to 17.1 percent in 1995. Trade has also contributed much to the structural transformation and modernisation of the economy. For example, the manufacturing share of the GDP has risen steadily from 12.2 per cent in 1970 to about 28.8 per cent in 1995. Had Malaysian been a closed economy, Malaysia would have shared the same fate as some other less developed countries that remain economically backward. Its external trade policy has paved the way for greater inflows of foreign direct investment, as foreign direct investors are not so much interested in serving the small domestic market as serving the vast external market. The large inflows of foreign direct investment have conferred positive effects on the domestic economy. These include technological improvements, broader production spectrum, and new market dimension. The developments in the export sector have also contributed directly and indirectly to the development of the non-trade sector such as the construction sector. All this has meant significant improvements in the overall living standards for the Malaysians. Internationalisation has provided employment opportunities, thereby raising their standards through higher and more stable earnings.

According to Chee (1984) small and medium-sized industries (SMIs) in Malaysia face many barriers to internationalisation, which are similar to those of its large-scale counterparts. However, some of the problems are more endemic among small firms than in larger firms. Among the most important problems faced by small and medium-sized industries in Malaysia to engage in international trade are finance, inadequate land or building, shortage of skilled labour, lack of raw materials, competition, management, technology, and the lack of information.

A survey on SMIs in Malaysia shows that most of the firms complain of inadequate finance and lack of access to commercial bank credit to engage in international business. The most pressing problem appears to be a shortage of working capital. The main reasons given for the lack of working capital include problems in obtaining loans and other types of credit facilities from commercial banks and other financial institutions. A number of small and medium-sized firms complain that they do not have enough cash to buy raw materials in order to purchase or produce whatever is required by foreign firms.

Many small and medium-sized firms complain of inadequate land or buildings. These firms complain that they do not have sufficient land or buildings for expansion or in some cases even for their present scale of operation. The shortage of suitable land or buildings has forced some of the small and medium-sized firms to produce in a residual area or in backyard factories. Needless to say, this has affected production, and makes it difficult for the small and medium-sized firm to meet the huge demand of products that was ordered by the foreign firms. Few firms, particularly those in the east coast, complain about flood conditions. Production is often interrupted during the monsoon season when premises are often flooded. Firms in the rural areas generally complain about the low voltage of electric power, the poor water supply, and inadequate communications and transport facilities that hinder them engaging in international business.

Chee (1984) also discovered that there was a serious shortage of skilled labour in Malaysia, especially skilled metal tradesmen and maintenance tradesmen. In the foundry and textile industries, for example, there was a shortage of moulders, foundry technologists, and tool-and-die designers. Such a problem affects small and medium-sized industries severely because small firms are often unable to compete with their large counterparts for skilled labour. Most of the small and medium-sized firms are unable to engage in international business due to a lack of skilled labour to produce the products required by the foreign companies. The problem arises because government-sponsored training schemes are inadequate to meet the demand for skilled workers. Employers also complain that the trainees do not receive sufficient attention in the practical application of their training. Many establishments, especially the larger ones, have their own apprenticeship training courses.

Small and medium-sized firms also blame the large ones for taking away their skilled workers by offering them better wages and conditions of work. Small industries find it difficult to obtain and retain skilled labour because of their inability to pay high wages comparable to those offered by the large establishments. Most of the employees in small and medium-sized firms regard the experience gained as a form of training and means of developing skills that would give them access to highly-paid jobs and improved social security benefits in large establishments. This is one of the reasons, small and medium-sized firms do not engage in international trade. That is, due to a lack of skilled workers and being afraid that they cannot fulfill the levels of demand placed on them by foreign firms.

Shortage of raw materials appears to be another problem for many of the small and medium-sized firms. Raw materials are either unavailable or difficult to obtain. Apart from the shortage, many of the small and medium-sized firms complain that the prices of raw materials have increased, in some cases by a wide margin. High prices and shortages are, of course, related. Small and medium-sized firms which face this problem are mainly found in the bakery, iron foundry, coconut oil, saw mill and tin-can industries. For example, several factories in the coconut oil mill industry had to stop production and not engage in international trade because they could not get sufficient copra from Indonesia and the Philippines, the country's main suppliers. Local supply was inadequate because a large amount of copra was exported and smuggled to Thailand where it fetched a higher price. Some of the affected factories turned to processing a substitute for coconut oil from palm oil. The new oil, though better than coconut oil, had not gained popularity in the foreign market.

The oil crisis caused a shortage of carbon black used in the making of rubber compound. This affected the tyre retreading industry, which depended on the materials. Another industry, which was badly affected by the oil crisis, was plastic. The shortage of materials for the plastic industry caused many of the small firms to operate below capacity and produce just enough to meet the demand of the domestic market. As such, these firms ceased exporting the product to foreign countries. Chee

(1984) further stated that small and medium-sized firms appeared to be more severely affected by the shortage of raw materials than the larger firms. A number of the small firms had to bribe their suppliers to ensure an adequate supply. Those who were unable to do so lost out to their rivals, mainly to the favour of large firms. Small firms located in the outlying areas were even more severely affected by the shortage. In a seller's market, supplies are often sold on first come, first served basis. Since the rural firms are often located far from the main sources of supply, they are frequently at a disadvantage.

Marketing problems include a seasonal demand of product from foreign importers, customer-related problems, delivery and keen competition. A number of small firms have problems marketing their products because of issues such as poor design, poor product quality due to the use of poor quality raw materials, lack of after-sales service and precision due to inadequate equipment and shortage of skilled personnel. In the metalworking industry, for example, it is common to find a number of defects in the metal parts after welding. Cracks and other defects tend to appear at welding joints and these are not remedied even after the final inspection before sending it to overseas markets. One of the reasons for the poor quality of work is the lack of welding techniques in the small firms. Another type of defect known as material defect occurs because of the use of unsuitable raw materials or welding electrodes or the application of wrong heat-treatment on metal. The most common defect occurs during the machining process. Many of the defects can easily be rectified if the small firms have access to technical advice and assistance. Due to the inferior quality of the products, most of the foreign companies stop importing the product from Malaysian firms.

Chee (1984) also discovered that Malaysian batik producers needed to improve the quality of their products, especially in dyeing and printing. This is vital if Malaysian batik is to be marketed overseas. At present, Malaysia controls only 16 percent of the batik market in Japan while Indonesia has the major share. Malaysian batik can only increase its share if its quality is improved. A Japan Export Trade Organisation (JETRO) report on the marketability of Malaysian batik showed that the variety of batik cloth was limited, patterns were too local, printing was neither elaborate nor accurate and dyeing was uneven.

Small firms also have problems in obtaining technical information on technical processes, machinery and equipment. Technical processes are usually described in technical journals, which are not available to small firms, while machinery and equipment suppliers tend to visit the large rather than the small and medium-sized firms. Another technical problem facing small and medium-sized firms in Malaysia is the inability to produce original designs. Instead, they tend to copy foreign designs due to the fact that they do not have the expertise to design their own products. Chee (1984) stated that small and medium-sized firms in Malaysia lacked knowledge on foreign market opportunities. Small firms also complained of unfair competition from their large-scale rivals. Unfair competition may arise from certain government policies, which tended to favour large firms when awarding contracts from overseas firms than to the small and medium-sized firms.

Management problems arise mainly because many of the small firm's entrepreneurs have a relatively low level of formal education with limited training or professional qualifications. Thus they have a limited exposure to modern management principles and practices. Most of them were involved in small industries after having acquired some experience either in sales or production. Thus, they lack all-round managerial competence to engage and deal with international trade transactions. Unlike their large-scale counterparts, small firms are unable to rely on specialists to look after each of the functional areas. On the contrary, small-industry entrepreneurs generally have to handle every business aspect themselves and thus it is difficult for them to cope with the demands of the foreign business firms.

The technology used by small and medium-sized firms is often outdated. Some of the firms do not trust modern technology while others are unable to afford it. Thus the majority of them rely on traditional technology, which, in many cases, is inefficient. For example, the furniture industry suffers from a lack of designing skills. Most of the designs used are copied from abroad. Design is an important aspect of the industry but most of them, except the large firms, do not have a qualified designer. There is little incentive to produce new designs because there is no copyright for furniture designs. Thus the majority of the small and medium-sized firms will merely copy a particular design once it has become popular. The same problem plagues the plastic and batik-making industries. That is the reason most of the small and medium-sized firms tend to engage in domestic business rather than international business because they have neither the expertise nor the resources. Even if they do, production costs and prices are generally too high to be competitive overseas.

Chee (1984) also discovered that lack of information and knowledge about foreign markets and export procedures has been one of the stumbling blocks for small and medium-sized firms to engage in international business. Small and medium-sized firms want more information on how to discover or open a foreign market, how to establish personal contacts with potential buyers and foreign markets' competitive conditions.

Balance of Trade

Malaysia has almost always enjoyed a favourable balance in the current account of its balance of payments. More often than not, the surplus trade balance was large enough not only to finance the perennial deficit in the services account but also to post a sizeable current account surplus. It was only in the 1990s that Malaysia ran into trade deficits, which aggravated the balance of payments strains caused by the deficits in the service accounts. The large trade deficits incurred in these years were apparently due to the low prices of primary commodities on the export side, high price-inelastic import demand generated by rapid industrialisation in the country, and the appreciation of major currencies especially the Japanese Yen, the Deutsch mark, the Korean Won and New Taiwan Dollar. Imports of capital goods associated with foreign investment activities in the country have contributed much to the growing trade deficit. In other words, deficits have been financed largely by foreign capital inflows.

Imports have exceeded exports, despite export-oriented industrialization in these years, because FDI in manufacturing activities generated imports of capital goods immediately where export output would begin to flow after a time lag. The trade balance would reverse itself, with deficit giving way to surplus once the export-oriented investment projects came on-stream. The overall trade balance, not bilateral trade balance, is what really matters. Malaysia has incurred bilateral trade surpluses with some trading partners, despite overall deficits in some years. By the same token, bilateral deficits with some trading partners running parallel to overall surpluses are not uncommon. Thus, Malaysia has always enjoyed the bilateral trade surplus vis-à-vis the rest of ASEAN, especially Singapore. Malaysia has also been posting trade surpluses with the United States except during 1992-1994. It is also remarkable that Malaysia has been registering trade surpluses with the European Community since 1980. It is only with Japan that Malaysia has frequently incurred bilateral trade deficits, which were particularly large during the years 1990-1993 and 1994-1996. Evidently, trade with Japan has contributed most to the overall trade deficits of Malaysia in recent years.

Direction of Trade

Malaysia's trade matrix exhibits considerable concentration of trading partners, with the major export destinations acting as the main sources of imports as well. Singapore, Japan, the United States and the European Community have always been the most important export destinations, each accounting for over 12 percent of total exports. Their combined share of Malaysia's export has always exceeded 73 percent (see Table 6).

For historical and geographical reasons Singapore has been Malaysia's important trading partner. Currently, it is the number one export destination for Malaysia. Other ASEAN countries (Brunei, Indonesia, the Philippines and Thailand) have accounted for a negligible proportion of Malaysia's export trade, jointly absorbing about 5 percent of the total since 1991.

Table 6 - Malaysia: Direction of Export (% share)

Year	Singapore	ASEAN	Japan	US	UK	Germany	Holland	EC	ASEAN, Japan, US and EC	Northeast Asian NIEs
1970	21.5	24.7	18.2	13.0	6.6	3.1	2.2	19.2	75.1	n.a.
1980	20.3	24.2	14.5	16.1	6.0	4.3	8.4	23.2	78.0	n.a.
1990	19.1	22.4	22.8	16.4	2.8	3.6	6.0	17.0	78.6	n.a.
1991	20.7	25.8	24.4	12.9	2.6	2.6	5.9	14.1	77.2	9.7
1992	17.1	22.1	21.2	16.6	3.5	3.6	3.4	14.6	74.5	9.9
1993	18.2	24.2	19.6	16.6	3.2	2.4	3.5	14.3	74.7	10.9
1994	19.3	24.4	17.0	17.4	3.5	3.4	3.0	14.4	73.2	11.5
1995	19.8	25.5	16.1	18.7	3.8	3.6	3.6	15.4	75.7	10.3
1996	22.7	29.0	15.8	16.9	3.9	3.9	2.6	14.9	76.4	10.0
1997	23.3	29.3	15.9	16.9	4.4	3.6	2.4	14.8	76.9	10.5
1998	23.3	29.8	13.2	18.6	4.0	4.1	2.4	14.8	76.4	10.3

Source: Central Bank of Malaysia, Quarterly Economic Bulletin 1999

Although the European Community still remains a major export destination for Malaysian products, its relative importance has declined over the years, its share falling from 19 percent in the early 1970s to about 15 percent in the late 1990s. Among the EC countries, the United Kingdom, Germany and Holland are the most prominent destinations for Malaysian exports. However, United Kingdom's share had fallen from 6.6 percent in 1970 to 4.0 percent in 1998 (see Table 6).

Recent changes in the direction of Malaysia's export trade have centred largely around North East Asia's newly industrialised economies (NIEs), that is, South Korea, Taiwan and Hong Kong. These three economies have become increasingly important destinations for Malaysia exports in recent years. Their combined share of Malaysia's total exports has risen from 9.7 percent in 1991 to 10.3 percent in 1998. However, it appears that Malaysia's exports to these NIEs consists of mostly primary products, although the share of manufacturers is on the increase. By far the most important market for Malaysian manufactured exports is the United States. However, its share of Malaysian manufactured exports has fallen from 30 percent in 1980 to 25 percent in 1998 (see Table 7).

Table 7 - Malaysia: Manufactured Exports by Destination (% share)

	Country								
Year	Singapore	U.S.	Japan	Hong Kong	Germany	UK	France	European Community	West Asian Countries
1980	23.5	30.1	7.4	5.1	5.1	5.5	2.1	16.9	1.7
1990	27.5	25.0	8.1	4.8	5.6	5.4	1.8	17.6	2.4
1995	27.9	23.6	9.1	4.6	4.9	5.9	1.8	17.3	2.1
1998	26.9	25.2	7.6	5.0	5.4	5.0	1.7	16.7	2.0

Source: Central Bank of Malaysia, Annual Report 1999

It is also pertinent to note that manufactured goods constituted as much as 24 percent of Malaysian exports to the United States in 1995 which sharply contrasts with the 9 percent share of manufactured goods to Japan in that year (Ariff, 1991). The low proportion of manufactured goods in Malaysian exports to Japan is largely due to the fact that Japanese multinational corporations (MNCs) operating in Malaysia have been using Malaysia as an offshore base for producing goods aimed largely at third country markets in North America and Western Europe. This is in sharp contrast with US MNCs that export their manufactured goods back to the United States. Nonetheless, there are signs that the Japanese MNCs in Malaysia are beginning to direct some of their exports back to Japan, following the sharp appreciation of the Yen and the relaxation of import controls and tariffs in Japan. As mentioned, Malaysia's major export markets are also the major source of its imports. In fact, the country concentration has grown stronger in the case of imports, with Japan, ASEAN, the European Community and the United States jointly accounting for 75 percent of Malaysia's total imports in 1998 compared with their combined share of 65 percent in 1970.

Clearly, Japan is by far the most important source of Malaysian imports, accounting for about one-quarter of the total. Much of this may be explained by huge Japanese investments in Malaysia. The share of countries from North East Asia in Malaysia's imports has also grown, largely due to their increased investments in the Malaysian manufacturing sector in recent years. Among the ASEAN countries, Singapore has always been the single most important source of imports for Malaysia, with its share of total imports overwhelmingly exceeding the combined share of all other ASEAN countries. This is attributed partly to the strong traditional ties that have long existed between Malaysia and Singapore and partly due to the substantial Singapore investments in Malaysia.

The European Community (EC) is relatively less important as a source of imports than as an export destination for Malaysia. The European Community's share of Malaysia's imports has fallen from 23.2 percent in 1970 to 12.6 percent in 1998. This declining role of the European Community as an import source may have much to do with its declining share of foreign investments in the country.

Malaysia's bilateral trade with its major trading partners has been expanding at a much faster pace during 1991-1996 compared with the preceding period 1985 -1990. Malaysia's import growth rate has clearly exceeded that of exports during 1991-1996. Malaysia's trade with the European Community has gathered renewed momentum during the same period and that the other categories have exhibited some dynamism reflects Malaysia's efforts to diversify the direction of its trade flows.

Role of Government

The government has continued to provide one-off or "unpackaged" assistance to the Bumiputera[1] business community. Efforts to create the Bumiputera Commercial and Industrial Community (BCIC) were also strengthened through the implementation of the resolutions of the Third Bumiputera Economic Congress, held in 1992.

These included the introduction of the Bumiputera Joint-Venture Scheme by a consortium of commercial banks to finance the establishment of genuine joint ventures between Bumiputera and non-Bumiputera entrepreneurs. With the implementation of the BCIC, it is hoped that aspiring Bumiputera entrepreneurs would be given the opportunity to gain a foothold in strategic industrial business activities and involve themselves in domestic and international trade. In general, the BCIC programs enable Bumiputera entrepreneurs to participate in strategic small and medium-sized enterprises (SMEs) in the manufacturing, construction and modern services sectors. These programs managed to gain the support of Government-owned companies and, more importantly, that of privatized entities and privately owned manufacturing companies to act as anchor companies. To lay a strong foundation for the development of future Bumiputera entrepreneurs, the government is now actively encouraging Bumiputera entrepreneurs to expand their business to enter overseas markets.

The Second Malaysia Plan of 1971-1975 in particular, sets out two quantitative targets. First it was decreed that employment by sector should reflect the ethnic composition of the population: Bumiputera 54 percent, Chinese 35 percent, Indian 10 percent and others 1 per cent. Second, by 1990, it was intended that the

[1] Bumiputera in this context is the indigenous Malay race, which constitute 55% of Malaysia' population

Bumiputera group should own and manage at least 30 percent of the corporate sector, an increase from its 2.4 percent share in 1970.

The central assumption of the Second Malaysia Plan was that national unity would result via its provisions, which would lead, to greater equity and balance among Malaysia's social and ethnic groups. Since 1950 the government has implemented numerous plans, but an unequal distribution of economic wealth among the races in Malaysia still prevails.

The mean monthly gross household income by ethnic group in 1990 and 1995 shows that there is a great disparity of household income between races in Malaysia. The Bumiputera mean household income grew at an average rate of 9.3 percent per annum from RM940 per month in 1990 to RM1,600 in 1995, whereas the Chinese mean monthly household income increased by 10.0 percent per annum from RM1, 631 to RM2, 895 over the same period.

Furthermore, the ownership of share capital at par value for limited liability companies between the years 1990 and 1995 amongst races in Malaysia shows the value of ownership of share capital in Malay limited companies is very low compared to Chinese firms. For example, in 1990 the ownership of share capital by Malays was RM20.88 billion (21%) and in 1995 it was RM36.98 billion (22.4%), compared to non-Bumiputera in 1990 at 50.75 billion (51%) and in 1995 at RM78.03 billion (47.3%). This shows that the non-Bumiputera ownership of share capital exceeded the Bumiputera by RM29.87 billion in 1990 and by RM41.05 billion in 1995.

The objective to achieve 30% Bumiputera equity in the corporate sector, as forecasted in the Second Malaysia Plan (1971-1975), therefore, had not been achieved. The income imbalance between Malays and Chinese had widened because most Chinese in Malaysia engaged in both domestic and international trade, whereas Malays mostly work in the agricultural sector and in government agencies. Only a small proportion of Malays are engaged in commercial activities, whether domestic or international business.

Malay and Chinese Entrepreneurs

In 1997, 299 (69.2%) Chinese companies were engaged in manufacturing businesses compared to 72 (16.7%) Malay companies. There were 66 (51.6%) Chinese companies engaged in the service sector compared with only 36 (28.1%) Malay companies. Furthermore, 1,022 (71.3%) Chinese manufacturing companies were engaged in international business and trade activities compared to only 102 (7.1%) Malay manufacturing companies. There were 13 (41.9%) Chinese service companies engaged in international business compared with only 5 (16.1%) Malay service companies. From the above analysis, it is concluded that the majority of companies engaged in local and international business in Malaysia were Chinese-owned companies. Since the government plans were implemented, only a small number of Malay entrepreneurs had shown significant interest in engaging international business.

In a study by Aziz (1970) of 144 Malay and Chinese firms in the context of international trade, he found that the problems faced by Malay entrepreneurs in exporting their products were mainly due to a lack of knowledge about foreign markets. Malay firms often employed 100 percent of their staff from their own race, and often only catered for customers from their own race. Malay firms often did not want to expand their business outside of their own county and that is contrary to Chinese entrepreneurs who wanted to expand their business outside of Malaysia and had multiracial customers. The workers in Malay firms were less motivated to venture into international business because the owner did not pay annual increments based on performance but based on seniority of employment. Aziz (1970) also found that there was no significant degree of association between firms engaged in international business and the level of family dominance between Chinese and Malay entrepreneurs. It was interesting to note that a higher percentage of Malay than Chinese businessmen reported that they had recruited able personnel. The Aziz (1970) data also revealed that only 22 percent of all entrepreneurs had recruited professionals as members of their staff. It further revealed that Malay entrepreneurs had a slight edge over Chinese entrepreneurs in terms of utilization of such qualified personnel but only in relation to conducting domestic business.

The study also revealed that there was no significant degree of association between Malay and Chinese entrepreneurs in international business, whether or not they had specific plans for the next five years. This means that the empirical data did not appear to support the contention that forward planning was a necessary prerequisite for engaging in international business. The possible explanation for this conclusion could be that many Malay businessmen were making big plans because their expectations had been raised significantly by constant information and rhetoric that Malays should be alert to international business opportunities that now exist for them because of strong government incentives and programs to develop Malay entrepreneurs under the government's New Economic Policy. In the Aziz (1970) study, a lower percentage of Chinese reported that they had specific plans to engage in international business and kept their business plans very much to themselves.

In relation to business training courses, there was no statistically significant difference between attending business courses and the motivation to engage in international business. The Aziz (1970) study found that the Chinese firms engaging in international business performed significantly better than did the Malay firms. Most Malay firms in the study revealed a lack of experience as a problem when engaging in international business compared to the Chinese firms. The Aziz (1970) data also revealed some degree of association between successful and unsuccessful entrepreneurs and the size of their firms in terms of total employees in their first year of operation. For instance, more Malay firms tended to belong to the smallest category when compared to the Chinese firms. Due to their small size and youth, the majority of Malay firms tended to operate their business within the domestic market to reduce the risk of business failure, compared to the Chinese firms who were long established and had medium and large sized firms engaged in international business.

The Aziz (1970) study also revealed that Malay businessmen when engaging in international business faced serious financial problems compared to Chinese businessmen. This is because many Malays tended to start their business with very low capital and capital investment. Many Malay businesses, therefore, suffered from under capitalization. Lack of finance forced many Malay entrepreneurs to produce inferior quality goods and thus lower the quality of material supplied to overseas markets. Poor financial resources by Malay entrepreneurs also lead to their inability to recruit able employees whose wage demands were high. This ultimately lead to the employment of mediocre staff who made poor business decisions leading to poor domestic and international business sales thereby affecting the performance of the firms. The data in the Aziz (1970) study also revealed that there was a degree of association between Malay and Chinese entrepreneurs engaging in international business when their initial capital came from their own savings vis-à-vis borrowed money. For instance, more Malays relied on their own savings for initial capitalization; conversely, more Chinese businessmen relied on borrowed money for financial business start-ups. The Aziz (1970) study also found that entrepreneurs who used mostly their personal savings to finance their business initially found it more difficult to engage in international business. A significant number of Malays that used mostly their personal savings to start their domestic business implied that this constituted a disadvantage and handicap, which contributed to their lack of motivation to engage in international business.

Also in the Aziz (1970) study most of the Chinese entrepreneurs that were engaged in international business were much older and more experienced than the Malay firms. The Aziz (1970) study showed that the Malay entrepreneurs were not serious in their business, and were dependent upon government assistance to engage in international business, likewise the Chinese business counterparts were self-motivated when it came to engaging in international business.

There was also a statistically significant degree of association between Malay and Chinese entrepreneurs and their attitude towards forming joint ventures when engaging in international business. The Aziz (1970) study revealed that generally Malay businessmen had a significantly more favourable attitude towards joint ventures with foreigners than with local Chinese. The Chinese entrepreneurs attitudes towards foreign joint ventures were less secure and confident when working hand-in-hand with the often more sophisticated and aggressive foreigners. Malay entrepreneurs were found to be more inclined to take risks, all of which probably augurs well for their future development efforts when engaging in international business.

Marketing and Production

Malay small to medium-sized industries (SMIs) tend to neglect marketing functions whilst placing greater emphasis on production functions. The marketing practices of SMIs in Malaysia are found to differ significantly from those of large businesses. Malay SMIs generally lack marketing strategies altogether. Malay SMIs in manufacturing are characterised by their indifferences to market planning, limited market spread, dependence on a narrow product range, pricing for the short term, preference for direct selling and distribution by themselves and priority to personal promotion. The large number of competitors to the Malay's SMIs, striving to sell rather similar products to a large number of buyers, results in very small margins for smaller firms. Although product quality in terms of customer acceptability is a serious problem, great difficulties are also encountered in price determination and in anticipating competitive reaction. The reluctance of large distributors to handle the unknown brands produced by SMIs, and not displaying the goods of SMIs on the shelves of larger retail outlets is well known. The alternative of Malay SMIs selling direct themselves was also hampered by the lack of competence and the operating cost of a direct sales force. Media promotion was not widely practised by Malay SMIs due to limited, localised markets and inadequate resources. Economic factors were regarded as the most threatening external forces that affect the marketing function of Malay SMIs in Malaysia. However, competition from local competitors appeared to be most problematic. Financial support was recognised as important for marketing activities as financial resources were closely related to credit extension, billing and collection practices. Also, problems of updating production technology were important because failure to overcome these meant that product quality was not acceptable in the market. Political, legal and government administrative factors did not appear to cause any hindrances to Malay SMIs marketing activities, whilst external factors of religious, social and cultural associations were the least inhibiting.

The operations of Malay SMI manufacturers conformed to those of other developing countries, as they tended to be relatively labour intensive, had relatively low labour and capital productivity. Their management tended to concentrate on problems encountered in the day-to-day management of manufacturing processes to the neglect of planning, development and the improvement of operational systems. There was a general lack of technical, as well as management training, despite years of experience on the part of the SMIs. Malay SMIs were more disturbed by external problems rather than by internal technical or management problems. Rising costs, the impact of government regulations and uncertain customer demand were factors outside the firm that caused great concern. The most important internal production problem was the SMIs' ability to produce quality goods acceptable to customer standards. Other problems included comparative quality with respect to competitors' products and the technical ability to produce to specified standards consistently. Other technical problems included yield, rejects, keeping abreast with process technology and ageing plant and equipment. Other than poor sales forecasting, Malay SMIs were not that worried about problems of production management and administration. However, low direct labour productivity was an area where more could be done.

According to Fong (1989), small businesses in Malaysia in the early 1970s were largely managed by high school dropouts. Graduates were sought and employed by large corporations and government institutions. But in the early 1980s, while the dropouts continued to pursue the business line, graduates were finding that the larger institutions and corporations could no longer absorb them and thus they began to infiltrate small businesses as entrepreneurs.

According to Chew (1998) the Chinese and Indian communities have been actively involved in businesses for a long time, while the Malay population usually opted for government jobs such as civil servants, teachers, uniformed personnel and others. Therefore, when the Malay community later became entrepreneurs, they did not have the culture, the experience nor family contacts or guidance to make them successful. The majority failed miserably, forcing the government to take action to reduce the failure rate. Statistics indicate that about half did not make it through the first year while only 10% remained after five years.

Zainal (1992) stated that besides the limited business culture and low educational background, the majority of Malay businesses also lacked discipline, management knowledge, experience and dedication. Mohayidin and Hamid (1988) and Fong (1989) commented that while the reasons for Malay business failures in Malaysia could be universal, they were of varying degrees among different sectors. The ten common reasons for failure were lack of capital, mismanagement, bad timing, lack of market knowledge, obsolete technology, labour shortage, poor supply of raw materials, lack of qualified personnel and lack of financial discipline.

Conclusion

Malaysia offers strong business opportunities for many different products and services, some of which have been highlighted in this article. From a cultural perspective, and because of governmental protection of the Bumiputera (the indigenous Malay), Malaysia can be a challenging market in which to operate. While changes are occurring, the pace is extremely slow. Foreign business people should be prepared to conduct thorough preliminary research, visit the country on a regular basis, show genuine concern for Malaysian development goals and culture, be patient in business negotiations, and adapt carefully to the Malaysian environment.

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