

**A New Model to Make the Great Leap Forward
By Quah Boon Huat**

Using a new economic model to propel Malaysia out of its middle-income trap is a wise move. But let's not forget the importance of cultivating the right mind-set and value system.

"You can't change the wind; you can however adjust your sails". So goes a saying.

The same can be said for economic development policies and strategies: economic winds of change necessitate a rethinking of policies and strategies.

Malaysia's export-led growth model has been, up to a certain degree, a success. A brief flirt with an import-substituting growth model after independence had led nowhere, partly because of the small domestic market. Development via an export-led growth model was thus the only way forward then.

However, the export-led growth strategy, according to some, is no longer an optimal development strategy for developing countries. Continued emphasis on export-led growth will, among other things, increase the reliance of developing countries on the developed world and dampen domestic market growth.

Many export-dependent developing countries started tweaking their growth strategies especially after external demand for their exports dried up on account of the current global financial and economic crisis. Though Malaysia's growth strategy had started emphasizing domestic demand since about a decade back, it still remains largely dependent on external demand for its economic growth.

We are still middle-income

Malaysia seems stuck in a middle-income, or high middle-income trap, depending on definition. Tan Sri Nor Mohamed Yakcop, Minister in the Prime Minister's Department, himself admits that Malaysia appears "caught in a high-middle-income country trap", as well losing some of its high growth momentum. If Malaysia has already started losing its high growth momentum, it can only mean that we are going to sink deeper in the middle-income trap.

It's easy to see that we have already been stuck for quite a while if we compare Malaysia's economic performance with, for example, that of South Korea. Even though both countries started industrializing at around the same time, South Korea has pulled far ahead of Malaysia, both in terms of income and industrial capability.

In 1950, Malaysia's real per capita gross domestic product (base year 1990) was USD1,696, nearly double that of South Korea's USD 876. By 1973, Malaysia (USD3,167) was already losing ground to South Korea (USD2,840). And by 1996, South Korea (USD12,874) was already far ahead of Malaysia (USD7,764), and had joined the OECD club. South Korea's formidable industrial base now produces high-quality goods with well-recognized brand names that can take on the best in the

global market.

There are many reasons why Malaysia has not been able to make the high-income transition. For one, it has not specialized more in selected areas where it can achieve economies of scale; neither has it achieved technological leadership.

It is becoming increasingly difficult to make the transition because of the tightening squeeze between low wage competitors (like China) and cutting edge innovators. If we just sit back and remain complacent, our dream of making the high-income transition will just remain a dream.

New economic model

In the vernacular, an economic model is the framework used to create economic, social, and/or other forms of value in an economy. The framework includes, among others, policies and strategies, measures and incentives, infrastructure, institutions, organizational structures, trading practices and operational processes.

The recent series of announcements that the government will introduce a new economic model to take Malaysia from middle-income to high-income has generated a lot of media buzz. The announcements indicated that the new model would emphasize domestic consumption, and creativity and innovation to drive productivity. There were also pronouncements about the need to move Malaysia towards a knowledge- and innovation-based economy.

Though Tan Sri Nor Mohamed Yakcop has said that the 10th Malaysia Plan (2011-2015) would be based on the new economic model, it appears that the government has already started the ball rolling. For example, the Prime Minister's announcement on 30 June 2009 of a comprehensive deregulation of the Foreign Investment Committee Guidelines is actually one instance in the evolution of Malaysia's economic model. It is realistic to say that Malaysia's "new" economic model will have no "final form" because of the constant need to evolve, considering the rapidly changing global economic environment.

And looking at the challenges Malaysia currently faces, we can more or less expect the kind of changes that will be made. For example, against a backdrop of low external demand, what can we expect the government to say, except that Malaysia needs to emphasize more on domestic consumption? This particular pronouncement about Malaysia needing to emphasize more on domestic consumption is however not new. In Budget Speech 2001, for example, the then Minister of Finance said that the Malaysian Government would continue to "increase domestic demand, in particular private consumption to generate growth..." and "implement a low-tax regime to encourage domestic consumption..."

The buzzwords - creativity, innovation, productivity, knowledge economy, etc. – are also nothing new. For example, according to the Eighth Malaysia Plan (2001-2005), concerted efforts would be undertaken during the Plan period to facilitate the development of a knowledge-based economy and key strategies would include enhancing productivity growth. It also mentioned that it recognized the need to urgently build a critical mass of creative and innovative manpower.

We can therefore envisage that Malaysia's new economic model, as far as modelling goes, will not be revolutionary.

For sure, we will need to specialize in areas where we can achieve economies of scale and technological leadership. We will also need to tackle a lot of complex challenges, for example, raising the skills and innovativeness of the labour force, creating sophisticated financial systems, and reducing corruption.

The external sector will however remain important because Malaysia does not have a large enough domestic market. Manufacturing will remain a vital sector, and there will be a redoubling of efforts to move it up the value chain.

Efforts aimed at making the services sector the next engine of growth will continue, as will efforts to pump up domestic consumption. We can also expect an increased sense of urgency to further develop and promote Malaysia's resource-based industries – petrochemicals, pharmaceuticals, wood-based, rubber-based, palm oil-based, and food processing.

It may seem, at first, wise to want to create many more industries under the new economic model. However, it may be far wiser to focus and specialize more in the areas that we have competitive and comparative advantages, where we can achieve economies of scale and technological leadership.

Importance of mindset and value-system

Whichever way Malaysia's economic model evolves, our success at making the quantum leap from middle-income to high-income may ultimately depend on the Malaysian mind-set and value system. In the Foreword to the Eighth Malaysia Plan document, the then Prime Minister of Malaysia noted that “we will have to cultivate the right mind-set and value system in order to develop a culture of high productivity and excellence and ensure that our success is sustainable.”

Former Prime Minister Tun Abdullah Badawi once complained that Malaysia has a “first-world infrastructure” but a “third-world mentality”. Needless to say, no one expects much of a nation whose citizens have a third-world mentality. So, even if Malaysia has a well thought out viable economic model, it won't get us very far further up the economic development ladder, if we continue to have a third-world mentality. And that's expected because we remain our own worst enemy.

Of course, the right kind of mindset and value system can be cultivated. Japan has made it. Would anyone believe that a 1901 survey of Japanese factory workers found them lazy, unskilled, unspecialized, and footloose?

The Prime Minister has said that we need a transformational change, which is critical for Malaysia in its pursuit of a developed nation status. Let's not forget that we also need a transformational change in our mindset and value system. And this is probably more critical.

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