Unemployment may worsen despite recovery.

By

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Developments in 2001 have been dominated by a marked deterioration in external conditions which were fortunately cushioned somewhat by the government's counter-cyclical fiscal policy. Placing severe recessionary pressure on the economy was the syncronised global economic slowdown, the first in decades. As in any typical major global economic slowdown, the effects of these adverse deflationary pressures were seen in a severely depressed employment market, especially in the export-dependent manufacturing sector.

Over the past one and the half decades, the rapid development of the manufacturing sector as the key driving force of the economy has created major job opportunities to a rising labour force. In fact, a milestone was reached in 1993 when manufacturing surpassed the agriculture sector as the biggest employer (excluding the services sector). Since then, the gap has widen progressively with manufacturing now accounting for 27.4 per cent of total employment compared with the 14.8 per cent in the agriculture sector. Apart from its declining importance, the fall in the percentage share of labour employed by the agriculture sector also reflects the difficulties this sector faces in retaining workers in view of the persistent rural-urban migration and the relatively lower wages in this sector.

Given its significance, a severe slump in manufacturing production would inevitably result in severe job loss, as indicated by the retrenchment data supplied by the Ministry of Human Resources (MHR). The number of workers retrenched in 2001 was up a worrisome 51 per cent from the previous year to total 38,116. Out of this total, the manufacturing sector accounted for a significant 75 per cent. Within this sector, the electronics and electrical products industry accounted for almost half of the total number of workers retrenched. Penang, being the electronic hub of Malaysia, was the worst hit, accounting for 23 per cent of total retrenchment..

The latest Bank Negara Annual Report revealed that the growth in employment has slowed substantially to 2.6 per cent in 2001 from 4.6 per cent in 2000. With the labour force rising at a faster pace of 3.2 per cent, the unemployment rate for 2001 has risen sharply to 3.7 per cent from 3.1 per cent in 2000. This rate of unemployment, which is the highest in ten years, has even surpassed the 3.4 per cent recorded in 1999 following the Asian Crisis.

In line with the retrenchment data released by the MHR, employment in the manufacturing sector took the biggest hit, shedding 29,900 jobs compared with a substantial 156,100 new jobs created in the previous year. Apart from the fact that firms are scaling down on production, which fell by 5.1 per cent last year, the retrenchments are also due to the ongoing process of high labour-intensive manufacturing processes relocating from Malaysia to other lower labour cost economies such as China and, to a lesser extent, Thailand. The problem is further compounded by the repatriation of retrenched Malaysian electronic workers from Singapore, another major casualty of the global hi-tech bust.

The significant contraction in employment in the manufacturing sector was, however, more than compensated by the encouraging increase in new employment in the services sector, especially in domestic oriented businesses. Despite a sharp fall in employment in the banking services sector due to the on-going consolidation and merger, a total of 217,300 jobs were created in the services sector, especially in areas such as social services, private services, non-profit services of households and domestic services of households. A similar positive trend was also seen in the construction sector with 55,500 new jobs created, owing primarily to a modest recovery in residential housing construction activity and the increase in public sector spending on infrastructure projects.
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The vital precondition to a recovery in the employment market is a pick-up in economic activity. Since Malaysia is very trade dependent, no account of the outlook for the employment market will be complete without mentioning the growth prospects of the US economy, our largest trading partner. And for now, the worst appears to be over for the US, with the advance estimate of GDP for the final quarter of last year posting a modest growth. In line with the positive developments in the US economy, there are some hopeful signs, according to the latest set of headline figures, that the worst may also be over for the Malaysian economy. The pace of economic deceleration, according to the latest Bank Negara quarterly report, has slowed markedly with real output falling by 0.5 per cent in the fourth quarter compared with a contraction of 1.2 per cent in the previous quarter. In the face of a still weak external demand, domestic demand, underpinned by the government's pump priming activities, has played a big part in the improvement seen in the fourth quarter.

However, despite signs of the economy bottoming out, the situation on the employment front, unsurprisingly, is still bleak. Firms continue to retrench as part of the rationalisation process to lower costs. Sony recently announced that it is offering voluntary separation to some 3,500 employees in Penang. Perwaja Steel has also announced that it is closing its manufacturing plant for a month and offering voluntary retirement to more than 1,600 workers. UOB Malaysia also plans to cut its workforce by one-fifth of its 2,580 employees. And the retrenchment data in the early part of this year also tells a similar story. Compared with the same period last year, the number of workers retrenched during the first two months of this year continued to surge upwards markedly by over one hundred per cent to total 6,123 persons with the manufacturing sector still being hit the hardest.

Going forward, though there is still much uncertainty especially in view of the fact that Japan, the second largest economy in the world, is still stuck in reverse gear, the balance of evidence suggests that the local economy will recover, albeit at a gradual pace. Reinforcing the belief of a modest recovery is the positive growth trend seen in the leading index. The index, which leads the business cycle by three to six months has been recording positive growth for five consecutive months since July 2001. Across the border, the forward looking Purchasing Managers' Index (PMI), which is the key indicator of Singapore's future manufacturing activity improved further, inching up by 0.3 point from the previous month's reading to reach 49.6 points in February. With the index almost reaching the 50-point threshold, there is renewed optimism that Singapore's economy has reached a point of inflection. This is an important piece of news, given that the export cycles in Malaysia and Singapore are highly syncronised.

Against the background of an improving economic climate, what does this mean for the labour market this year? Does a recovery in general economic activity also mean, as some economic observers believe, an immediate recovery in the employment market? The answer to these questions really depends on the strength of the recovery. Historically, unemployment has lagged the rest of the economy as jobless rates normally continue to increase for a while even after an economic recovery takes hold.

From the period 1970 to 2000, the Malaysian economy has suffered three major economic setbacks. Except for the period 1975-76, the norm in past recoveries was that the growth performance would typically come in below its long-term trend, estimated to be about 7 per cent. This happened during the 1985-86 recession and the 1998-99 Asian Financial Crisis. During these periods, the unemployment rate only improved a year after economic recovery has taken hold.

The only time in which the improvement in the unemployment rate happened the year the economy improved was way back in the 1975-76 period. Unlike the other two slowdowns, economic growth during 1976 exceeded its long-term trend with a strong upward bounce of 11.6 per cent from 0.8 per cent in 1975. This, consequently, has brought the unemployment rate down noticeably to 6.1 per cent from 6.9 per cent respectively. What this analysis provides is a vital clue that for idled workers and machines to fully rejoin the workforce, the prerequisite is that the growth recovery should exceed its potential long-term trend.

Applying this simple rule of thumb, the unemployment rate may worsen this year. This is because the pace of recovery is expected to be shallow at best. The forecast made by economic observers current ranges between 3 to 5 per cent, with Bank Negara's recent forecasts conservatively coming in at the lower end of the range. With growth likely to fall well below its long-term trend, the recovery this year is therefore unlikely to be fast enough to halt a further rise in joblessness. The outlook on employment could, of course, change if the economic recovery turns out to be much stronger than expected. But for now, against the expectation of a modest recovery, the emphasis on building profit and improving productivity suggest that employers will still be misery in their hiring. Compounded by the job mismatch prevailing in the labour market, the unemployment rate this year could, therefore, surpass the 4.0 per cent full employment benchmark.