CHINA AND INDIA:
Challenges and Opportunities
for Poverty Eradication and
Moderating Inequality in Malaysia

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Abstract

Malaysia has employed the mechanism of growth with equity in order to eradicate poverty and ameliorate inequality. During the New Economic Policy period, the Government intervened extensively to ensure that all levels of society benefited from economic development and thereby maintaining social cohesion. However, the increasing pace of liberalization coupled with developments in the region such as the rise of China and India has eroded the Government's ability to ensure the equitable sharing of the economic pie.

The objective of this paper is to look at the challenges as well as opportunities posed by the rise of China and India with respect to poverty eradication and reducing income inequality. The challenges include competition for markets with the Malaysian SMIs and competition for foreign direct investment (FDI). This has serious implications on employment opportunities and efforts to eradicate poverty and narrowing income disparity. On the other hand, the rise of these two giants also gives opportunities to Malaysia in its effort to tackle poverty and inequality through the "prosper thy neighbour" effects, as there will be spill over from their growth and wealth accumulation. Furthermore, as China (particularly) becomes integrated into the multi-national regional production network, it will contribute to increase trade in the region through increase in intra-trade, thus expanding exports and growth.

Key words: poverty, inequality, growth

Biodata

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TABLES OF CONTENTS

Notes

References

LIST OF TABLES

China and India: Challenges and Opportunities for Poverty Eradication and Moderating Inequality in Malaysia

1.   Introduction

The New Economic Policy 1971-1990, which was introduced after Malaysia was traumatised by the worst racial riots in her history, was hailed as a successful model of redistributing income without sacrificing growth. It was launched with the objective of attaining national unity and fostering nation-building through poverty eradication and economic restructuring so as to eliminate the identification of race with economic functions. Since the implementation of this policy, Malaysia has achieved growth, structural transformation, and poverty alleviation and improved income distribution in an ethnically diverse society.   More specifically, studies on income distribution during this period (see, for example, Ishak and Ragayah 1990, Bhalla and Kharas 1992, World Bank 1993, Ragayah 1994, Zainal Aznam 1994) have shown that growth was also accompanied by improved income distribution.

The NEP was succeeded by the National Development Policy 1991-2000 (NDP), which retains the basic strategy of *growth with equity* of the NEP. This in turn is followed by the current National Vision Policy contained in the Third Outline Perspective Plan 2001-2010 (NVP). In essence, the NVP represents the consolidation of all past development efforts (NEP and NDP) to attain a united, progressive and prosperous Malaysian society. The quest of the nation is to become a developed nation in its own mould. In order to meet the challenges towards this end the same strategies expounded in the NEP and NDP of building a resilient, competitive nation and an equitable society to ensure national cohesion and social stability will also be emphasised in the NVP. While poverty reduction continued unabated during the NVP and NVP, except for the glitch as a consequent of the 1997-1998 financial crisis, income inequality has suffered a U-turn since the end of the NEP period.

The process of liberalization and globalization would be more likely to cause a financial crisis such as that experienced in 1997-1998 that resulted in financial volatility and economic insecurity. It is this onslaught of the globalization process that is changing the economies,

environments, cultures and societies that would affect the urban poor adversely. These people do not have the capital and access to information, or the ability to translate the information into economic, political and social gain (UNESCAP 2000). Hence, the economic situation tends to be unstable and hinders the poverty eradication effort by causing retrenchment, inability to find employment and thus less transfers to assist their families. Moreover, devaluation also raised the prices of imported goods and thus lowering the real income of their purchasers, particularly of the urban poor. And the crisis of 1997-1998 is not an exception as McGee and Scott (2000: 235) quoted what Brad Glosserman wrote on the comment of Stephen Roach, chief economist of Morgan Stanley Dean Witter, that "there is little talk that the crisis could ever recur. Yet that flies in the face of painful reality. From 1975 to 1997, the IMF identified 158 specific country crises, 54 banking crises and 32 instances where a country experienced a combined currency/banking crisis. Financial crises have become the rule not the exception".

As if this is not enough to contend with, Malaysia together with the rest of the world but with ASEAN countries in particular, is now forced to deal with the awakening of the two giants, China and India[i]. Tham and Kwek (2005) note that many economies view China's rise with trepidation and fear, including a developed country like Japan. The latter's apprehension is founded on the fact that industrial upgrading in China with the assistance of Japanese multinational corporations (MNCs) will keep moving continuously upstream until China has acquired a full industrial structure, at the expense of Japan. Increasing anxiety is also felt by ASEAN member countries, including Malaysia, that employ the path of foreign direct investment (FDI) and export promotion to further their development goals as Chinese exports flood the world. Amidst this unease, they also see that the growth of China may offer increasing opportunities trade and invest, especially with the accession of China into the World Trade Organization (WTO) in the year 2001. The growth and development of China and India will provide opportunities to Malaysia in its effort to tackle poverty and inequality through the "prosper thy neighbour" effects, as there will be spillover from their growth and wealth accumulation. Moreover, as China (particularly) becomes integrated into the multi-national regional production network, it will contribute to increase trade in the region through increase in intra-trade, thus expanding exports and growth.

The objective of this paper is to outline the Malaysian experience absolute poverty eradication and managing income distribution or relative poverty, as well as to look at the challenges posed by the rise of China and India as well as opportunities they provide with respect to poverty eradication and reducing income inequality. For this purpose, the next section will provide a description of the achievements in poverty eradication while Section 3 presents a mixed picture in the success of reducing income inequality. Section 4 will touch on the pattern of Malaysian trade with China and India while Section 5 describes some of the opportunities and challenges faced by Malaysia in achieving growth and in turn its poverty eradication and income inequality reduction efforts in the midst of the awakening giants. Section 6 concludes the paper.

2.   The Structure of Poverty

2.1   Definition of Poverty Line Income[ii]

Incidence of poverty in Malaysia is estimated on the basis of poverty line income (PLI). The Eighth Malaysia Plan (Malaysia 2001) stated that the PLI was estimated based on the minimum requirements of a household for three major components, namely food, clothing and footwear, and other non-food items such as rent, fuel and power; furniture and household equipment; medical care and health expenses; transport and communications; and recreation, education and cultural services. For the food component, the minimum expenditure was based on a daily requirement of 9,910 calories for a family of five persons while the minimum requirements for clothing and footwear were based on standards set by the Department of Social Welfare to welfare homes. The other non-food items are based on the level of expenditure of the lower income households, as reported in the Household Expenditure Survey, 1998/1999. The poverty line income is updated annually to reflect changes in the levels of prices by taking into account changes in the Consumer Price Indices.

Researchers on the Malaysian poverty situation had been concerned with the appropriateness of using the same poverty line, adjusted for inflation, for over two decades (Shireen 1998, Ragayah

2001) and the fact that the same poverty line is utilised for both urban and rural areas although separate poverty lines are employed for Peninsular, Sabah and Sarawak. While the approach of adjusting the PLI to inflation is adequate for absolute deprivation, its relevance as a measure of relative deprivation is questionable. Shireen has shown that poverty in Malaysia is officially seen as a situation of relative rather than absolute deprivation and argued that a PLI that is updated for inflation over a long period of time ceases to reflect relative deprivation since the Malaysian standard of living had not remained constant over the period (Shireen 1998:161). Secondly, a separate PLI for urban and rural areas is more accurate because the relationship between food energy intake and consumption expenditure varies by region, activity levels, relative prices and taste. This would result in an underestimate of the incidence of urban poverty since the income level required to sustain a household subsistence level in the rural areas would not be adequate for a similar household in the urban areas. Thirdly, the Malaysian PLI does not take into account the differences in household size. A measure that takes into account the differences in the composition of the household, especially in terms of age and sex, would be more accurate. Similarly, the PLI also neglects the regional differences in food consumption pattern and the changes in consumption patterns as income grows. Finally, it also does not allow for economies of scale in consumption. Hence, these flaws must be borne in mind in looking at the Malaysian poverty data.[iii]

Using the current method of calculation, the PLI for 1987 was RM350 per month for a household size of 5.14 in Peninsular Malaysia, RM429 for a household size of 5.24 in Sarawak and RM533 for a household size of 5.36 in Sabah (Malaysia, 1989). The poverty line was adjusted in 1993 to RM405 per month for a household size of 4.8 in Peninsular Malaysia, RM582 for a household size of 5.1 in Sabah and RM495 for a household size of 5.1 in Sarawak. The Seventh Malaysia Plan (Malaysia 1996) revised the poverty line for 1995 to be RM425 monthly for a household size of 4.6 in Peninsular Malaysia, RM601 per month for a household size of 4.9 in Sabah and RM516 per month for household size of 4.8 in Sarawak. In 1997, these were revised to RM460 per month for a household in Peninsular Malaysia, RM633 for a household in Sabah and RM543 for a household in Sarawak. In 1998, these PLIs were RM493, RM667 and RM572 respectively while in 1999 the PLIs were RM510, RM685 and RM584 respectively for Peninsular Malaysia,

Sabah and Sarawak for similar size households. The PLI in 2002 was RM529, RM690 and RM600 respectively for each of the three regions.

2.2   Incidence and Trends of Poverty

Since the implementation of the NEP, Malaysia has achieved outstanding progress in poverty eradication. In this effort, greater emphasis was given to eradicating poverty in the rural compared to the urban areas. This focus on the former is justified since the incidence of poverty has always been much higher in the rural than the urban areas. The progress in poverty eradication according to region and strata between 1970 and 2002 is shown in Table 1. For the whole of Malaysia, the total number of poor households decreased from one million households to 267,900 households over the period, resulting in the poverty incidence plunging from 52.4 % to 5.1%. Over the same period, urban poverty incidence shrank to 2.0 % while the rural poverty incidence fell to 11.4 %[iv]. Urban poor households numbered 111,800 in 1976 but dropped to 69,600 in 2002 while poor rural households, which totalled 864,100 in 1976, shrank to 198,300 over the same period. As can be seen, poverty in Malaysia is mainly a rural phenomenon but the Malaysian government had not neglected the problem of urban poverty since the urban poor was identified as one of the seven poverty reduction target groups (Malaysia 1976).

Table 1

Malaysia: Incidence of Poverty by Rural-Urban Strata, 1970-2002

Strata	1970		1976		1984		1990		1993		1995		1997		1999		2002	
	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %	Total Poor Households ('000)	Incidence of Poverty %
Penin. M'sia	791.8	49.3	764.4	39.4	483.3	18.4	448.9	15.0	325.3	10.5	260.6	7.4	196.5	5.2	264.1	6.5	195.9	4.3
Rural	705.9	58.7	669.6	47.8	402.0	24.7	371.4	19.3	268.2	14.9	192.1	12.9	152.9	9.4	190.5	11.0	143.5	10.3
Urban	85.9	21.3	94.9	17.9	81.3	8.2	77.5	7.3	57.1	4.4	68.5	3.3	43.6	2.0	73.6	3.2	52.4	1.7
Sabah	n.a.	n.a.	95.5	58.3	76.0	33.1	96.6	34.3	123.9	33.2	66.9	22.4	49.5	16.4	68.4	20.1	49.2	16.0
Rural	n.a.	n.a.	87.5	65.6	68.5	38.6	91.1	39.1	108.1	36.2	56.3	28.8	43.2	22.5	55.7	26.0	35.4	24.5
Urban	n.a.	n.a.	8.0	26.0	7.5	14.3	8.5	14.7	15.8	19.8	10.6	10.3	6.3	5.8	12.7	10.1	13.8	8.5
Sarawak	n.a.	n.a.	115.9	56.5	90.1	31.9	70.9	21.0	68.0	19.1	38.1	10.0	28.2	7.3	27.6	6.7	22.8	5.8
Rural	n.a.	n.a.	107.0	65.0	85.9	37.3	67.8	24.7	63.0	23.6	33.4	15.7	25.7	11.8	24.8	10.5	19.4	10.0
Urban	n.a.	n.a.	8.9	22.9	4.2	8.2	3.1	4.9	5.0	6.0	4.7	2.8	2.5	1.5	2.8	1.6	3.4	1.7
M'sia	1,000	52.4	975.8	42.4	649.4	20.7	619.4	17.1	517.2	13.4	365.6	8.7	274.2	6.1	360.1	7.5	267.9	5.1
Rural	n.a.	n.a.	864.1	50.9	556.4	27.3	530.3	21.8	439.3	18.6	281.8	14.9	221.8	10.9	271.0	12.4	198.3	11.4
Urban	n.a.	n.a.	111.8	18.7	93.0	8.5	89.1	7.5	77.9	5.3	83.8	3.6	52.4	2.1	89.1	3.4	69.6	2.0

Note: n.a. - not available

Source: Malaysia (1981, 1986, 1991a, 1991b, 1993, 1996) for 1970-1993; for 1995-2002, calculated from the data provided by Economic Planning Unit.

A critical dimension of poverty in Malaysia is from the ethnic point of view. Table 2 shows that poverty is concentrated among the Malays and other Bumiputeras. Although the incidence of poverty among all ethnic groups has been reduced, it is still relatively high among the Malays and other Bumiputera

Table 2

Incidence of Poverty by Ethnic Groups, 1970-2002

	1970	1976	1984	1987	1990	1997	2002
Malays	64.8	56.4	25.8	23.8	20.4	7.7	7.3
Other Bumiputera	na	na	na	na	36.8	17.3	na
Chinese	26.0	19.2	7.8	7.1	5.4	1.1	1.5
Indian	39.2	28.3	10.1	9.7	7.6	1.3	1.9
Others	44.8	44.6	22.0	24.3	22.8	13.0	na
Total	49.3	35.1	18.4	17.3	16.5	6.1	5.1

Note: na = not available
Source: Malaysia. Various Malaysia Plans.

3. Trends in Income Inequality

The impacts of the changes in Malaysian development policies as well as external influences on income distribution on the overall, rural and urban household incomes distribution are shown in Table 3. Income inequality rose between 1970 and 1976, and fell continuously till the end of the NEP period. However, the Gini ratio has shown a trend reversal in the 1990s. This U-turn in income inequality almost wiped out all the gains that were made under the NEP. The crisis managed to bring down the Gini ratio to 0.443 in 1999 but it rose again, except for the moderating impact of the 1997-1998 financial crisis, to 0.4607 in 2002 (Malaysia 2003).

Table 3: Distribution of Household Income by Strata: Malaysia 1970-2002

Percentage of Households	Income Share (Percentage)										
	1970	1976	1979	1984	1987	1990	1993	1995	1997	1999	2002
Overall											
Top 20%	55.7	57.7	55.8	53.2	51.2	50.4	n.a.	51.3	52.4	50.5	51.3
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	5202	6854	6268	7745
Middle 40%	32.9	31.2	32.4	34.0	35.0	35.3	n.a.	35.0	34.4	35.5	35.2
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1777	2250	2204	2660
Bottom 40%	11.5	11.1	11.9	12.8	13.8	14.3	n.a.	13.7	13.2	14.0	13.5
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	693	867	865	1019
Gini Ratio	0.513	0.529	0.505	0.483	0.458	0.446	0.459	0.464	0.470	0.443	0.461
Mean Household Income (RM)	264	514	763	1095	1074	1163	1563	2020	2606	2472	3011
Rural											
Top 20%	51.0	54.5	53.2	49.5	48.3	47.1	n.a.	47.4	48.2	47.9	49.6
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	3153	4130	4124	4057
Middle 40%	35.9	33.7	34.4	36.4	36.7	37.1	n.a.	37.1	36.6	36.5	35.7
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1235	1564	1577	1612
Bottom 40%	13.1	11.8	12.4	14.1	15.0	15.8	n.a.	15.5	15.2	15.6	14.7
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	515	649	670	699
Gini Ratio	0.469	0.500	0.482	0.444	0.427	0.409	n.a.	0.414	0.424	0.418	0.405
Mean Household Income (RM)	200	392	550	824	852	927	n.a.	1326	1704	1718	1729
Urban											
Top 20%	55.0	55.9	55.6	52.1	50.8	50.6	n.a.	49.8	50.2	48.7	46.7
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	6474	8470	7580	9085
Middle 40%	32.8	32.2	32.1	34.5	35.0	35.1	n.a.	35.7	35.6	36.5	37.2
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	2323	3000	2844	3265
Bottom 40%	12.2	11.9	12.3	13.4	14.2	14.3	n.a.	14.5	14.2	14.8	16.1
Mean Household Income (RM)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	842	1193	1155	1344
Gini Ratio	0.503	0.512	0.501	0.466	0.449	0.445	n.a.	0.431	0.427	0.416	0.439
Mean Household Income (RM)	407	830	975	1541	1467	1591	n.a.	2589	3357	3103	3652
Disparity Ratio:											
Urban:Rural	2.14	2.19	1.90	1.87	1.72	1.70	1.75	1.95	2.04	1.81	2.11
Chinese: Bumiputera	2.25	2.28	2.13	1.76	1.65	1.70	1.78	1.80	1.83	1.74	1.80
Indian: Bumiputera	1.75	1.56	1.51	1.28	1.25	1.29	1.29	1.33	1.42	1.36	1.28

Sources: Anand (1983); Malaysia (1981, 1986, 1989, 1991, 1993, 1996, 1999, 2001): mean household incomes of income classes for Malaysia, Urban and Rural were provided by EPU.

Note: n.a.: not available

The state of income distribution both in the rural and the urban areas also exhibit similar trends over the NEP period. It can be seen that the Gini ratio for rural households rose between 1970 and 1976 but fell thereafter before rising again after 1990. However, the trends in income distribution in the rural and the urban areas diverged during the 1990s. The trend in the rural areas replicates the overall trend, where there is also a U-turn in income inequalities. Nevertheless, inequality moderated slightly in the rural areas after that. In the urban areas, the Gini ratio first rose 1976 but fell continuously thereafter till 1999, at which point it rose again. This high inequality, one of the highest in East Asia is worrying since for any given rate of growth, high inequality would impede poverty reduction and human development, which implies exclusion for many in the society.

Ethnic inequality is the most sensitive issue in Malaysian income distribution and hence information on this subject is often unavailable to the public. This is why the patterns and changes in income distributions for the three main ethnic groups in Peninsular Malaysia shown in Table 4 are rather scanty in recent years. In 1970, the degree of inequality among the major ethnic group in Peninsular Malaysia was highest among the Malays, followed by the Indians and lowest among the Chinese. Between 1970 and 1976, the Gini coefficients indicate that the income distribution of all the three ethnic groups deteriorated, with the inequality among Chinese households exceeding that of the Malay and Indian households. The income shares of the first two ethnic groups show that while the top income groups increased their shares of the total income, the lower two groups suffered losses. Income inequality actually improved among the Indian households.

Table 4

Distribution of Household Income by Ethnic Groups, Malaysia*: 1970-2002

% of Households	Percentage of Income Share											
	Malay/Bumiputera				Chinese				Indian			
	1970	1976	1979	1984	1970	1976	1979	1984	1970	1976	1979	1984
Top 20%	52.5	53.9	52.6	51.9	52.6	56.1	52.8	51.1	54.2	52.6	50.8	48.4
Middle 40%	34.8	34.3	35.5	34.8	33.5	31.3	35.3	34.9	31.3	32.7	36.3	35.3
Bottom 40%	12.7	11.8	11.9	13.3	13.9	12.6	11.9	14.0	14.3	14.7	12.8	16.3
Mean Income[1] (RM per month)	172	345	513	852	399	787	1094	1502	310	538	776	1094
Median Income[1] (RM per month)	122	233	332	581	269	480	636	1024	196	360	522	770
Gini Ratio : Overall	0.466	0.494	0.470	0.469	0.455	0.505	0.473	0.452	0.463	0.458	0.452	0.417
Rural	0.419	0.471	n.a.	0.447	0.399	0.486	n.a.	0.412	0.363	0.388	n.a.	0.347
Urban	0.445	0.478	n.a.	0.462	0.474	0.507	n.a.	0.456	0.502	0.504	n.a.	0.441

% of Households	1987	1990	1997	2002	1987	1990	1997	2002	1987	1990	1997	2002
Top 20%	50.2	49.5	n.a.	n.a.	49.2	48.9	n.a.	n.a.	47.2	47.7	n.a.	n.a.
Middle 40%	35.7	35.7	n.a.	n.a.	35.7	36.0	n.a.	n.a.	35.9	35.8	n.a.	n.a.
Bottom 40%	14.1	14.8	n.a.	n.a.	15.1	14.2	n.a.	n.a.	16.9	16.5	n.a.	n.a.
Mean Income[1] (RM per month)	868	931	2052	2376	1430	1582	3743	4279	1089	1201	2887	3044
Median Income[1] (RM per month)	612	677	n.a.	n.a.	1021	1137	n.a.	n.a.	799	881	n.a.	n.a.
Gini Ratio: Overall	0.447	0.429	0.448	0.435	0.430	0.419	0.416	0.455	0.402	0.390	0.409	0.3989
Rural	0.426	0.410	0.408	1	0.399	0.392	0.420	2	0.350	0.341	0.362	n.a.
Urban	0.437	0.435	0.431	n.a.	0.440	0.428	0.402	n.a.	0.435	0.424	0.403	n.a.

Note: Figures from 1970-1987 refer to Peninsular Malaysia only.
Sources: Compiled from Ishak and Ragayah (1990); Kumpulan Penelitian Sosial UKM (1990): Ishak (2000) and Ismail (2004).

All three ethnic groups show declining trends after that till 1990. The Chinese trend reflects that the disparity continued to narrow till 1999 after which time it has jumped to be the most unequal among all the three groups. Inequality among the Indians remained the lowest it did increase slightly after 1990. Although inequality among the Bumiputera also narrowed, but the reduction proceeded extremely slowly, resulting in this group having the most unequal distribution in these years except for 2002.

Table 4 also illustrates that non-Bumiputera mean incomes continue to outstrip that of the Bumiputera mean income. However, while the growth rate of non-Bumiputera household incomes far exceeded that of the Bumiputera prior to 1970, this trend was reversed during the NEP period. The later disparity in relative growth rates meant that inter-ethnic group gap in incomes had narrowed. This amelioration in the disparity ratios can also be seen from Table 3. The income disparity ratios between Chinese and Bumiputera households fell from 2.29 in 1970 to 1.90 in 1980 and 1.74 in 1990. In contrast, the Indian-Bumiputera disparity ratio fell from 1.77 in 1970 to 1.29 in 1980 and remained at that level till 1990. This decline in inter-ethnic income disparity, together with the reduction in inequalities within all major ethnic groups, accounted for the overall improvement in the size distribution of income during the NEP period.

Unfortunately, the developments after this period, while still upholding "growth with equity", had resulted in the re-emergence of inequalities among the ethnic groups to almost the level prior to the NEP. This is because in the 1990s the speed in the rate of increase of household income among ethnic groups changed again. Table 5 reflects the average annual rate of increase of household income for the different ethnic groups between 1990 and 1997. In terms of the overall increase, the Indians had the fastest rate of increase, followed by the Chinese and the Bumiputeras. This table also reveals that it is the Indians in the top 20% income group followed by the Indians in the 40% middle income group followed by the Chinese in the top 20% income group that are having the biggest jumps in their household incomes. Among the urban dwellers, it was the Chinese in the 40% middle income group that were experiencing the fastest rise while in the rural areas, the Indians in the top 20% income group led the pack. Thus, it is not surprising that the disparity ratios between the Bumiputeras and the Indians and particularly the Chinese in Table 4 widened again in 1990s, to be moderated only by the financial crisis.

Table 5
Average Rate of Increase of Household Income By Ethnic Groups,
1990 – 1997 (Average Annual Growth Rate)

Ethnic Group	Highest (20 %)	Middle (40 %)	Bottom (40 %)	Overall Average
Malaysia	11.4	10.0	9.1	10.6
Bumiputera	11.1	10.1	8.9	10.3
Chinese	11.3	11.0	10.0	10.9
Indian	12.1	11.4	9.9	11.4
Others	-4.8	-10.3	3.0	9.9
Urban	10.2	9.6	9.0	9.8
Bumiputera	10.3	10.0	9.3	9.8
Chinese	9.4	11.8	9.9	10.3
Indian	10.1	10.0	10.0	10.0
Others	1.9	-14.7	-3.9	7.9
Rural	7.6	7.3	6.9	7.3
Bumiputera	7.9	7.9	7.6	7.7
Chinese	9.7	7.8	7.5	8.6
Indian	10.0	9.6	8.0	9.4
Others	-8.7	0.8	6.6	5.1

Source: Economic Planning Unit

4.   Trade with China and India

Table 6 shows the trends of rapid expansion in trade between China and the ASEAN-5 countries, which accounts for about 90 percent of the total ASEAN trade with China. It can be seen that the total exports of the ASEAN-5 countries to China jumped from 10.59 billion US dollars to 38.12 billion US dollars over the 5-year period. Over the same period, the total imports of these countries from China leapt to 41.36 billion US dollars from 12.6 billion US dollars. Singapore ranks top in both its exports and imports from China. This is followed by Malaysia whose exports rose by about three and half times but its imports climbed almost five fold quickly turning it from a net exporter to a net importer. Only Indonesia has consistently been a net exporter in the last five years.

12

Table 6

ASEAN-5 Trade with China

Unit: Billion US dollars

Exports						
	1999	2000	2001	2002	2003	2004
Indonesia	2.01	2.77	2.20	2.90	3.80	4.60
Malaysia	2.32	3.03	3.82	5.25	6.43	8.38
Philippines	0.57	0.66	0.79	1.35	2.14	2.65
Singapore	3.92	5.37	5.32	6.86	10.15	15.40
Thailand	1.77	2.79	2.85	3.54	5.69	7.09
Total ASEAN-5	**10.59**	**14.63**	**14.99**	**19.91**	**28.21**	**38.12**
Imports						
	1999	2000	2001	2002	2003	2004
Indonesia	1.24	2.03	1.84	2.43	2.96	4.10
Malaysia	2.14	3.24	3.80	6.18	6.73	10.34
Philippines	1.04	0.78	0.98	1.25	1.80	2.53
Singapore	5.70	7.10	7.19	8.87	11.08	16.21
Thailand	2.49	3.37	3.70	4.92	6.06	8.17
Total ASEAN-5	**12.60**	**16.53**	**17.52**	**23.64**	**28.62**	**41.36**

Source: Suthiphand, 2005, reproduced in Tham and Kwek (2005).

In terms of the products, ASEAN's pattern of trade with China has shifted out of primary resources into manufactured goods over the years. Tham and Kwek (2005) have shown that the increasing importance of electrical and electronic (E&E) products in both ASEAN's exports to and imports from China. For example, in 2000, E&E goods constituted 27.6% and 45.5% respectively, of total exports and imports to China and by 2003, these have risen to 31.9% and 46.3% respectively of total exports and imports to China. The authors argue that the rise in E&E trade with China reflects the integration of China into the international production networks as a result of increasing multinational production in China. In turn, the use of China as an export platform for these goods are facilitated by the relatively lower labor costs in the country as well as by the use of selective trade liberalization policies that has provided duty exemptions for selected categories of imports in export-promotion industries (Lemoine and Unal-Kesenci, 2002). Moreover, Weiss (2004) noted that falling trade costs (import tariffs, transport, and freight charges, time in transit, the cost of information and of managing international supply

chains) have facilitated rapid regional integration in trade and capital flows within the East-South East Asian region, resulting in increasing trade ties between ASEAN and China.

Tham and Kwek (2005) also shows that the trade intensity index of ASEAN's trade with China that compares the relative intensity of ASEAN's trade with China relative to its trade with the rest of the world has increased noticeably for each of the ASEAN country. As shown in Table 7, the trade intensity between the Philippines and China has increased more than five fold from 3.14 to 15.8 over the 10-year period. Similarly, Thailand's trade intensity also increased slightly more than five times while Singapore's trade intensity with China rose 3.5 times. Indonesia and Malaysia's respective trade intensity had the slowest increase, three fold, over the same period.

Table 7
ASEAN-5 Trade Intensity Index with China

	1993	1995	2000	2003
Indonesia	3.87	4.46	6.79	12.06
Malaysia	2.01	1.60	2.50	6.04
Philippines	3.14	4.26	3.84	15.77
Singapore	1.27	1.18	2.18	4.40
Thailand	1.45	2.23	4.67	7.40
Korea	2.29	2.49	3.67	6.43
Japan	0.78	0.97	1.51	2.81

Source: Tham and Kwek (2005)

Tham and Kwek (2005) also examine the impact of the increase in trade intensity with China on the growth of the ASEAN-5 economies and the results of the estimates are summarises in Table 8. They argue that based on these results, the only meaningful interpretation of the findings on multipliers hold true for Indonesia, the Philippines, and Thailand. In the short run, Indonesia benefits the most out of the more trading with China while in the long run, the Philippines has the greatest benefits from growing trade with China. Overall, their estimates based on the simple dynamic models and the Autoregressive Distributed Lag models; show that the Philippines would be the largest recipient of any future trading growth with China.

Table 8

Summary Benefits of Growing Trade of ASEAN-5 with China in the Short Run and Long Run

1998:Q1-2003:Q4			
Impact Multiplier		**Long-run Multiplier**	
(R5) Singapore	23.74958	(R5) Malaysia	0.121667
(R4)Malaysia	24.77848	(R4) Indonesia#	0.260996
(R3)Thailand#	27.05174	(R3) Thailand	0.575573
(R2)Philippines#	31.93949	(R2) Singapore#	0.918241
(R1) Indonesia#	31.97633	(R1) Philippines#	2.841518

Note: R is rank and # indicates countries that have statistical meaningful interpretation of the estimated models.
Source: Tham and Kwek (2005)

The rise of India is a more recent phenomenon. Hence, not as much information is available on the impact of the rise of India compared to the impact of the rise of China. Malaysia which accounted for 1.63 billion US dollars trade value and 2.3 trade share was India's 7th ranked trading partner in 1996. Although the trade value swell to 2.64 billion US dollars in 2003, the trade share fell to 2.1 and Malaysia was only India's 10th largest trading partner. **Table 9** shows the major export destinations while **Table 10** shows the major sources of imports for India. These two tables reflect that Malaysia is a more important source of import (ranked 11th in 2003) than as its export destination (ranked 19th in the same year), that is, Malaysia is a net exporter to India.

Table 9

Major Export Destinations for India

Country	1996			2003		
	Value (US bil)	Share (%)	Rank	Value (US bil)	Share (%)	Rank
Total Exports	33.47	100.0		57.46	100.0	
USA	6.56	19.6	1	10.99	19.1	1
UAE	1.48	4.4	6	4.13	7.2	2
Hong Kong	1.86	5.6	5	3.23	5.6	3
UK	2.05	6.1	2	2.68	4.7	4
China	0.61	1.8	14	2.47	4.3	5
Germany	1.89	5.7	4	2.26	3.9	6
Belgium	1.10	3.3	7	1.74	3.0	7
Singapore	0.98	2.9	8	1.69	2.9	8
Japan	2.01	6.0	3	1.68	2.9	9
Italy	0.93	2.8	9	1.54	2.7	10
Malaysia	0.53	1.6	17	0.78	1.4	19

Source: MATRADE 2004. Trends in Global Trade, mimeo.

Table 10

Major Sources of Imports for India

Country	1996			2003		
	Value (US bil)	Share (%)	Rank	Value (US bil)	Share (%)	Rank
Total Exports	39.11	100.0		71.18	100.0	
USA	3.62	9.2	1	4.81	6.8	1
Belgium	2.23	5.7	3	3.66	5.1	2
China	0.76	1.9	17	3.57	5.0	3
Switzerland	1.13	2.9	10	3.10	4.4	4
UK	2.13	5.5	5	2.97	4.2	5
Germany	2.83	7.2	2	2.72	3.8	6
ROK	0.88	2.3	14	2.34	3.3	7
Japan	2.19	5.6	4	2.32	3.3	8
Australia	1.32	3.4	9	2.01	2.8	9
South Africa	0.00	0.0		1.93	2.7	10
Malaysia	1.10	2.8	11	1.86	2.6	11

Source: MATRADE 2004. Trends in Global Trade, mimeo.

In 1999 Malaysia was India's 2nd ranked export destination of its E&E products worth US$68.21 million. By 2003, the value of export has dropped to US$44.02 million and Malaysia was only the 9th most important destination for India's E&E exports. As an import source of E&E products for India, in 1999 Malaysia accounted for US$192.73 million with 7% share and ranked 4th. However, although India's imports of E&E products from Malaysia expanded to US$419.78 million in 2003, Malaysia's share of India's imported E&E market had shrunk to 5.7% and its rank fell to 5.

5. Opportunities and Challenges

The rise of these two giants gives opportunities to Malaysia in its effort to tackle poverty and inequality through the "prosper thy neighbour" effects, as there will be spillover from their growth and wealth accumulation, not only in commodity trade but also trade in services. Furthermore, as China (particularly) becomes integrated into the multi-national regional production network, it will contribute to increase trade in the region through increase in intra-trade, thus expanding exports and growth. In fact, it was recently reported that Singapore Prime Minister Lee Hsien Loong that China's growth would "create a favourable environment for other Asian countries to grow…"[v]. Tham and Kwek (2005) have shown that the share of China in the total exports of ASEAN increased from 3.5% in 2000 to 6.4% in 2003. Similarly, China's share in the total imports of ASEAN increased from 5.2% in 2000 to 7.8% in 2003. They concluded that that contrary to the expectations of the doomsayers, the accession of China to the WTO has actually increased the trade between ASEAN and China.

ASEAN and the Peoples' Republic of China (ROC) have signed the Framework Agreement on Comprehensive Economic Cooperation (CEC) between in 2002 that came into effect on 1 July 2003. This includes an agreement on the establishment of an ASEAN-China Free Trade Area (or ACFTA as well as programs for strengthening and promoting economic cooperation in priority sectors[vi] as well as cooperation in other areas[vii].

In an FTA, the abolishment of trade barriers will allow for trade expansion either through trade creation or trade diversion. Tham and Kwek (2005) have shown that the average tariff rates and non-tariff barriers (NTBs) of the ASEAN-6 (Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand) on China's products are low as compared to the tariff rates and NTBs of China on ASEAN products. They conclude that while lowering the tariff barriers under the ACFTA will increase the market access for ASEAN firms in China's market and thus ASEAN firms should seize the opportunities accorded by this agreement to identify the potential customs duty savings arising from the margin of preference between the Most-Favored Nation (MFN) tariff rate and the lower preferential ASEAN-China tariff rate. On the other hand, they caution that capturing China's market, especially the domestic market as opposed to using China as an export platform, will still encounter other challenges in the form of non-tariff barriers, direct competition from domestic producers in China as well as competition from other ASEAN producers. The use of special certificates as NTBs for selected products can pose obstacles for ASEAN firms that are seeking to access China's market. The authors cited the example of the import of electrical goods in China, which requires a Certificate of Electrical Equipment (CCEE) that has to be issued by the China Commission for Conformity. Similarly, metals, chemicals and similar commodities may require a certificate of analysis while animals, plants, their products and items such as animal vaccines and serums also require sanitary health certificates.

The ACFTA provides ASEAN producers with a bigger market, but it will also require these producers to compete among fellow members of ASEAN for a slice of China's market as well as in their respective countries. While established entrepreneurs with large enterprises might be ready to face competition from other producers, small and medium producers (SMIs) might face problems and this has serious implication for employment opportunities and efforts to eradicate poverty as well as reducing income disparity. Since the trade structures of the ASEAN countries, especially among the older ASEAN-4 member countries (that is Indonesia, Malaysia, the Philippines and Thailand), are similar and fundamentally competitive rather than complementary, Malaysian producers have to look for market niches, such as the 'halal products' in the food industry.

Malaysia, like other developing countries in the region, has also been concerned with the fact that China (and may be India in the future) has been attracting heavy FDI inflows and this could be at the expense of their neighbours. Table 11 shows the trend of FDI into Malaysia is falling in recent years, and this could deprive Malaysia from capital, technology and expertise as well as employment opportunities. At the same time, while the government is expected to play a big role in eliminating poverty and narrowing inequality, the globalisation process requires the government to reduce its role and increase that of the private sector in economic development. In order to attract FDI and to improve competitiveness, the government has to scale back on labour rights and welfare, which are regarded as costs that erode a country's competitiveness. At the same time, the government is also pressured to reduce the progressive and corporate tax rates, provide various incentives, for example, tax holidays, exemptions, etc., provide infrastructure (both physical and human resource training). This means that there is less resource to be spent on redistribution, that is, on social expenditure including education, health and housing.

Table 11

Trend of Foreign Direct Investment (FDI) in Malaysia, 1991 – 2004
(RM Million)

Year	Net* FDI in Malaysia	Nominal Gross Domestic Product (GDP)	FDI as a % of GDP	Gross Fixed Capital Formation (GFCF) in current prices	FDI as a % of GFCF
1991	11118	135124	8.2	30599	23.1
1992	13088	150682	8.7	53497	24.5
1993	14799	172194	8.6	63356	23.4
1994	12017	195461	6.1	76357	15.7
1995	14586	222473	6.6	107825	13.5
1996	18356	253732	7.2	121384	15.1
1997	17790	281795	6.3	121494	14.6
1998	10648	283243	3.8	75982	14.0
1999	14801	300764	4.9	65841	22.5
2000	14393	342157	4.2	87729	16.4
2001	2105	334589	0.6	83345	2.5
2002	12173	362012	3.4	83764	14.5
2003	9398	395017	2.4	87089	10.8
2004#	17934	449609	4.0	91818	19.5

Note: * Net: Inflows after taking into account the outflows arising from liquidation of FDI in Malaysia and the loan
       repayments to related companies.
       # : Estimated.
Source: 1991 – 2001 Tham (2004)
       2003 – 2004 : Data for Net FDI from Bank Negara Annual Report 2004
       Data for , GDP and GFCF, Economic Report of Malaysia, 2005-2006.

However, Weiss (2004) argues that this concern is greatly overstated for a number of reasons. First, although in absolute terms FDI to China is huge, once this figure is compared with either population or some measure of economic activity in the country, the ratio is not an outlier in comparison with other countries. Second, the comparison is based on officially recorded FDI flows, which included 'round-tripping'—that is the export of domestically generated funds and its return to its country of origin as FDI—is more significant in China than elsewhere, where it has been estimated to be as high as 40% of FDI flows in recent years. Weiss also quotes an econometric study that shows that the level of FDI in the eight neighbouring economies is not negatively related to FDI in China and there is FDI creation. Hence, he concludes that it seems

preferable to view FDI flows as at least partially endogenous to regional activity, with FDI responding to the profit opportunities generated by regional growth and FDI flows to one economy interacting positively with FDI flows to another as multinational firm exploit regional production sharing in a segmentation of the supply chain.

6.   Concluding Remarks

The above discussion has shown that Malaysia was successful in moderating income inequalities during the NEP period. However, with the liberalisation of the economy and the intensification of the globalisation process, inequality has been widening since the early 1990s. While the Government is emphasising on the eradication of absolute poverty, it must also attend to the reduction of income disparity, which means the reduction of relative poverty. As Malaysia had experienced, unequal income distribution is not conducive for promoting social cohesion and providing an acceptable level of quality of life for all Malaysians. It is also not consistent with our national development strategy of growth with equity.

Although this paper tries to link the prospects of growth and expansion of the Chinese and Indian economies on poverty eradication and narrowing income inequality in Malaysia, it must be cautioned that relationships are tenuous. As there are many factors that determine the effectiveness of poverty eradication and the ability to reduce income and wealth inequality in a particular country, it is difficult to establish a direct causal relationship between the growth of these two giant economies on the internal situation in Malaysia. Nevertheless, growth of an economy is important for poverty alleviation, particularly emphasised by the experience of the 1997-1998 crisis when negative growth was accompanied by an increase in poverty incidence. It is also crucial for income redistribution in the Malaysian case given its philosophy of redistributing from the enlarged size of the economic pie and not through the redistribution of income or wealth of one group to another. The trends that are unfolding in both China and India seems to imply that there are opportunities for mutual benefits. Thus, if Malaysian firms can seize the opportunities and overcome the challenges, then these benefits could trickle down to

result in further poverty eradication. A strong growth also makes it easier for the government to manoeuvre the policies for reducing income disparity, particularly between the different ethnic groups in Malaysia. For all these opportunities to be realised, the Malaysian firms need to enhance their competitiveness vis-à-vis their neighbours and create their own niche as well.

Notes

' The discussion in this paper focuses more on the impact of the rise of China rather than India due to the constraint in information on the latter.

" For a definition of income, sources and comparability of the data used to estimate poverty incidence and income distribution in Malaysia, see Ragayah (2003).

''' The Malaysian Government has responded and has revised the methodology of calculating the PLIs to be used in the coming Ninth Malaysia Plan 2006-2010.

'' The figures for 2002 are from the Mid-term Review of the Eighth Malaysia Plan (Malaysia 2003), which provides figures for Malaysian citizens only.

' Reported by Qin Jize, "China's growth good for Asia" in *China Daily*, 26.10.2005.

'' These are agriculture, information and communication technology, human resource development, investment and Mekong Basin Development.

''' These include the promotion and facilitation of trade in goods, services and investment, technology transfer, capacity transfer, promotion of e-commerce, and other areas such as banking, finance, tourism, industrial cooperation, transport, telecommunications, intellectual property rights, SMEs, biotechnology, fishery, forestry, mining, energy and sub-regional development.

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