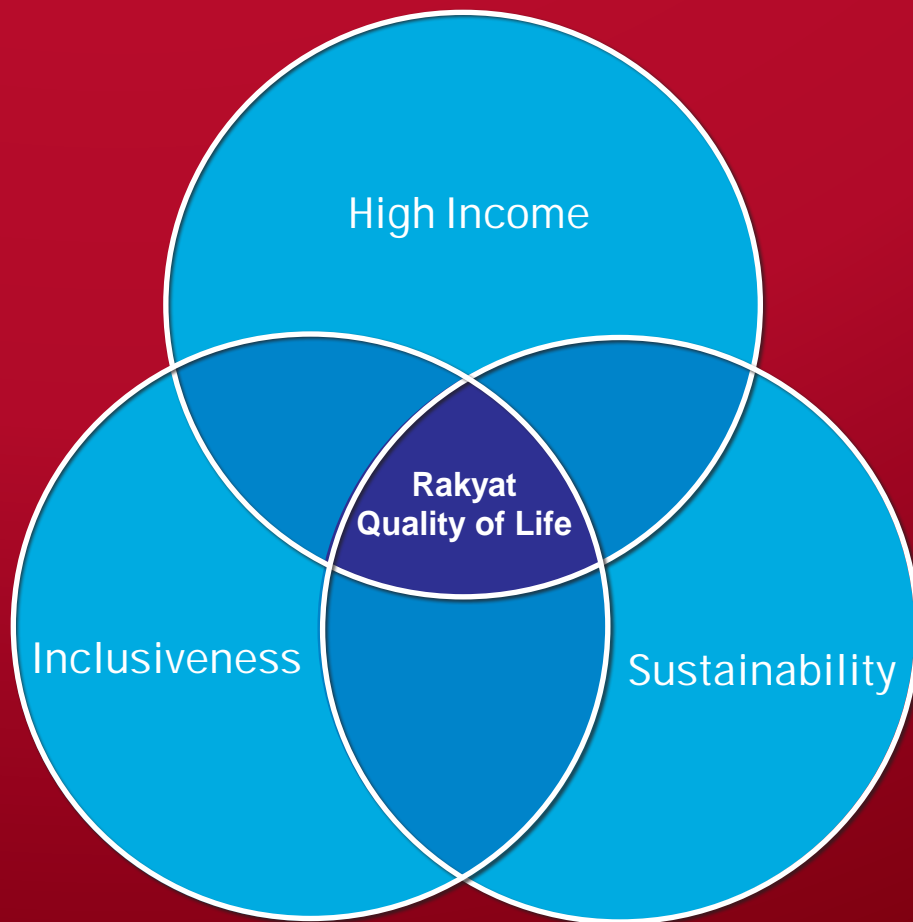




# NEW ECONOMIC MODEL FOR MALAYSIA CONCLUDING PART



**NATIONAL ECONOMIC ADVISORY COUNCIL**



**NEAC**

**NATIONAL ECONOMIC ADVISORY COUNCIL**

# **NEW ECONOMIC MODEL FOR MALAYSIA**

## **Concluding Part: Strategic Policy Measures**

**3 December 2010**



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# PREFACE

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This report is the second of two documents prepared by the National Economic Advisory Council (NEAC) on the New Economic Model (NEM). Building upon the overall policy framework set forth in the first document, this report presents greater details on the policy measures embedded in the eight Strategic Reform Initiatives (SRIs) of the NEM for the Government's consideration. These policy measures were developed following a series of meetings of the NEAC and consultations with stakeholders in the business sector, government, labour unions, academia and others.

The list of policy measures is not exhaustive. It represents the essential foundational policy measures that the NEAC believes will propel Malaysia towards the goal of becoming a high income, sustainable and inclusive economy by 2020.

The NEAC, as an independent advisory body, has put forward this set of recommendations, but upon their endorsement it will be the task of Government to immediately begin the meaningful implementation of these policy measures. Accordingly, the NEAC strongly advocates that the relevant government agencies and units, working closely with the private sector and other stakeholders, must assume the ownership and a leadership role in designing the implementation framework and timeline to ensure that the detailed policy measures are consistently and steadfastly adopted. In this context, it is highly likely that additional measures or modifications to the measures proposed in this report may be needed and should be undertaken in line with the policy objectives and guiding principles of the NEM.

More importantly, the urgent adoption of these policy measures is recommended as they constitute the foundation for the success of the projects under the National Key Economic Areas (NKEAs) launched by the Government at the end of October 2010. While simultaneously tackling the short-term macroeconomic imbalances stemming from the global economic crisis, Malaysia must stay the course in the bold implementation of the NEM cross cutting SRI policy measures of the Economic Transformation Programme.

This report is structured as follows:

**Chapter 1: Components of the Economic Transformation Programme (ETP)** begins by setting forth the changing international context within which Malaysia must urgently prioritise its economic transformation. Recognising that the problems Malaysia faces are multi-dimensional in nature, the Government has developed a blueprint for action with multi-pronged initiatives. The ETP is a key initiative in this blueprint involvings two integral components represented by the SRIs and the NKEAs. The SRIs seek to remove structural barriers to growth and address chronic weaknesses in the economy. Only when these shortcomings are addressed will Malaysia be able to ride on the NKEAS to achieve the ultimate objectives of high income, inclusiveness and sustainability.

**Chapter 2: Transformation through Reinvigorating the Private Sector** addresses the policy measures embedded in SRI1, SRI3, SRI7, and SRI8, to re-energise the private sector, create a competitive domestic economy, and enhance the sources of sustainable growth. Given the high level of current private sector skepticism, reflected in low private domestic investment, a massive policy package involving deregulation, liberalisation and effective enforcement of the competition law, in line with international standards, is required.

**Chapter 3: Enhancing Innovation** as reflected in SRI6 looks at how innovation can be rekindled with renewed vigor. Recognising that entrepreneurship and innovation are not going to emerge spontaneously, the NEAC discusses the role of the Government in implementing relevant policies and working with all stakeholders to generate a better environment and ecosystem for innovation.

**Chapter 4: Public Sector Transformation** is set forth in SRI4 and proposes an entirely new approach to revitalise, reshape, discard, and re-invent government structures and administrative procedures to meet the requirements of a high income nation. The Government's strategic direction should be to enhance its interaction with businesses and citizens by creating a Seamless Government. Improving the quality of the civil service requires a drastic revamp of its structure and size. Sound public finance is essential for safeguarding macroeconomic stability and enhancing the future prospects of the rakyat.

**Chapter 5: Intensifying Human Capital Development** underlies SRI2 which addresses the common complaint about the lack of talent and skilled labour as well as a dysfunctional labour market. Better educational and skill training programmes are prerequisites, as are appropriate labour laws and modern human resources management practices and systems. This chapter also highlights the importance of an enhanced worker safety net centred on unemployment insurance. The NEAC advocates a productivity-linked wage-setting system but, given the failures in the current wage-setting mechanisms, accepts the need for the introduction of a minimum wage policy in the interest of inclusiveness.

**Chapter 6: Narrowing Disparities** sets forth policy measures within SRI5 and looks at the key issues surrounding affirmative action and programmes focussed on the bottom 40% of households and the BCIC. The proposed programmes are centred on capacity building, and must be coordinated by a single agency employing a common database of beneficiaries. The NEAC also believes that targeted special programmes for certain groups outside of the bottom 40%, particularly SMEs within the BCIC, should continue but must be made market friendly, transparent, needs- and merit-based.

**Chapter 7: Implementation Considerations** looks at the implementation strategy for the policy measures. There is increasing awareness that there should be more centralised coordination and clear, accountable decision-making at all levels of policy implementation. As suggested in the 10MP, PEMANDU will be the central agency mandated to coordinate the further design and formulation of policy measures, monitor their implementation, and assess effectiveness for the purpose of suggesting any necessary remedial measures. The NEAC recommends supplementing the work of PEMANDU with an Independent Evaluation Board (IEB), whose main task would be to undertake every two years an in-depth strategic review of the impact and relevance of the policy measures underlying the SRIs.

**Chapter 8: From Vision to Results** concludes by highlighting the need for universal commitment to change. The blueprint for Malaysia's economic transformation is now complete and is encapsulated by initiatives set forth in 1Malaysia, the ETP, the GTP, the 10MP, and further reflected in the 2011 Budget recently unveiled. With an urgent purpose the nation's focus, energy, and efforts must quickly turn to the implementation challenges.

# Contents

1	COMPONENTS OF THE ECONOMIC TRANSFORMATION PROGRAMME (ETP) .....	3
1.1	THE CHANGING CONTEXT OF INTERNATIONAL COMPETITION.....	3
1.2	NATIONAL TRANSFORMATION AND THE ETP .....	4
2	TRANSFORMATION THROUGH REINVIGORATING THE PRIVATE SECTOR .....	11
2.1	INTEGRATION INTO THE GLOBAL SUPPLY CHAIN .....	11
2.2	REINVIGORATING THE PRIVATE SECTOR TO SUPPORT AN INTEGRATED MALAYSIA SUPPLY CHAIN REQUIRES BROAD-BASED STRUCTURAL REFORMS .....	13
2.3	A NEW SOCIO-ECONOMIC FRAMEWORK FOR INVESTMENT .....	14
2.4	REFORMS TO ELIMINATE RENT-SEEKING BEHAVIOUR.....	15
2.4.1	<i>Policy Measure: Revise the Public Sector Governance Framework</i> .....	16
2.4.2	<i>Policy Measure: Implement a Compliance Monitoring System</i> .....	17
2.5	RATIONALISING GOVERNMENT'S PARTICIPATION IN BUSINESS .....	18
2.5.1	<i>Policy Measure: Set Up a Central Oversight Authority</i> .....	20
2.5.2	<i>Policy Measure: Divest Non-Strategic Companies and Re-engineer the Roles of the Remaining GLCs</i> .....	21
2.5.3	<i>Policy Measure: Channel Proceeds from Divestment into a Sovereign Wealth Fund</i> .....	23
2.5.4	<i>Policy Measure: Re-engineer GLCs to Support the Private Sector</i> .....	23
2.6	ADOPTING INTERNATIONAL STANDARDS AND BEST PRACTICES.....	24
2.6.1	<i>Policy Measure: Follow International Standards – Governance and Management</i> .....	26
2.6.2	<i>Policy Measure: Follow International Standards - Sustainability</i> .....	26
2.6.3	<i>Policy Measure: Adopt Quality Standards for Goods and Services</i> ...	26
2.6.4	<i>Policy Measure: Convert Existing Malaysian Standards into International Standards</i> .....	27
2.6.5	<i>Policy Measure: Administer Compliance with Standards</i> .....	27
2.7	PROMOTING COMPETITION THROUGH LIBERALISATION AND DEREGULATION .....	27
2.7.1	<i>Policy Measure: Liberalisation of Entry, Ownership and Operations</i> .....	27
2.7.2	<i>Policy Measure: Reform the Regulatory Framework</i> .....	30

2.7.3	<i>Policy Measure: Swift and Resolute Implementation of the Competition Law</i> .....	32
2.8	INTRODUCING INNOVATION IN FINANCING .....	33
2.8.1	<i>Policy Measure: Supporting SMEs &amp; Innovation and Efficiency in Allocation of Capital</i> .....	33
2.9	ENHANCING CONNECTIVITY OF BUSINESSES AND BUILDING SMEs.....	36
2.9.1	<i>Policy Measure: Accelerate the Rollout of Broadband</i> .....	36
2.10	PRESERVING THE ENVIRONMENT.....	37
2.10.1	<i>Policy Measure: Internalise Externalities</i> .....	38
2.10.2	<i>Policy Measure: Promote Green Growth and Energy Efficiency</i> .....	38
2.10.3	<i>Policy Measure: Favour Sustainable Agriculture</i> .....	38
2.10.4	<i>Policy Measure: Strive for Energy Resource Sustainability</i> .....	39
2.11	ENHANCING SOURCES OF GROWTH - CASE STUDIES ON REMOVING BARRIERS IN SELECTED SECTORS .....	39
3	ENHANCING INNOVATION .....	43
3.1	A BETTER TOMORROW THROUGH INNOVATION.....	43
3.2	THE SETTING FOR INNOVATION .....	44
3.3	ISSUES IN INNOVATION AND TECHNOLOGICAL CHANGE .....	44
3.4	THE BARRIERS .....	44
3.5	OVERCOMING THE BARRIERS .....	45
3.5.1	<i>Policy Measure: Develop Government and GLC Procurement Policies That Support Local Innovative Products and Services</i> .....	46
3.5.2	<i>Policy Measure: Foster Better and Closer R&amp;D Links between Institutions of Higher Learning (IHLs) and the Private Sector</i> .....	47
3.5.3	<i>Policy Measure: Turn Existing HiCoEs (Centres of Excellence Accredited by the Ministry Of Higher Education) into Full Fledged Networks of Excellence</i> .....	47
3.5.4	<i>Policy Measure: Extract Greater Value from the Development and Management of Intellectual Property (IP)</i> .....	48
3.5.5	<i>Policy Measure: Consolidate and Merge National Enterprises to Create Scale</i> .....	48
3.6	ADDITIONAL POLICY MEASURES AND CONSIDERATIONS.....	49
4	PUBLIC SECTOR TRANSFORMATION .....	53
4.1	A LEAN AND CUSTOMER-FOCUSSED GOVERNMENT .....	53
4.2	BUREAUCRATIC REFORMS.....	55
4.2.1	<i>Policy Measure: Strengthen the Government's Facilitative Role</i> .....	55

4.2.2	<i>Policy Measure: Create a Citizen-Centered Public Service.....</i>	55
4.2.3	<i>Policy Measure: Expand Private Delivery of Public Services.....</i>	56
4.2.4	<i>Policy Measure: Enhance Public Agencies to Drive Growth .....</i>	56
4.2.5	<i>Policy Measure: Pursue Administrative Reforms in the Judiciary .....</i>	56
4.3	IMPROVING THE QUALITY OF HUMAN RESOURCES IN THE CIVIL SERVICE .....	57
4.3.1	<i>Policy Measure: Reform the PSC to Define Strategic Human Resource Policy and Management Processes in the Public Sector .....</i>	57
4.4	STRENGTHENING NATIONAL POLICY FORMULATION IN ECONOMIC GOVERNANCE.....	59
4.4.1	<i>Policy Measure: Revive the NDPC as the Premier Body for Policy Development, Coordination and Consultation .....</i>	59
4.5	FISCAL DISCIPLINE AND REFORMS.....	60
4.5.1	<i>Policy Measure: Adopting Accrual Accounting for Prudent Fiscal Management .....</i>	60
4.5.2	<i>Policy Measure: Implement Efficient Broad-based Tax for Revenue and Fiscal Stability .....</i>	60
4.5.3	<i>Policy Measure: Strengthen Expenditure Control .....</i>	61
4.5.4	<i>Policy Measure: Improve Fiscal Policy Institutions and Processes .....</i>	62
5	INTENSIFYING HUMAN CAPITAL DEVELOPMENT.....	65
5.1	A SKILLED WORKFORCE IN A VIBRANT LABOUR MARKET.....	65
5.2	WORKPLACE TRANSFORMATION .....	66
5.2.1	<i>Policy Measure: Modernise Labour Legislation .....</i>	66
5.2.2	<i>Policy Measure: Strengthen Strategic Human Resources Programmes.....</i>	67
5.2.3	<i>Policy Measure: Establish a National Wage Consultative Council (NWCC) .....</i>	68
5.2.4	<i>Policy Measure: Formalise a Productivity-Linked Wage System (PLWS) .....</i>	69
5.2.5	<i>Policy Measure: Consider a Minimum Wage Policy .....</i>	69
5.2.6	<i>Policy Measure: Enhance the Labour Safety Net by Introducing Unemployment Insurance .....</i>	70
5.3	INTENSIFYING HUMAN RESOURCE DEVELOPMENT AND WORKFORCE TRANSFORMATION .....	71
5.3.1	<i>Policy Measure: Undertake a Labour Market Forecast and Survey Programme .....</i>	72



5.3.2	<i>Policy Measure: Focus on Up-skilling and Upgrading the Workforce</i>	73
5.3.3	<i>Policy Measure: Leveraging Women's Talent to Raise Productivity</i>	74
6	NARROWING DISPARITIES	79
6.1	STRIVING FOR INCLUSIVENESS THROUGH MARKET FRIENDLY AND TRANSPARENT AFFIRMATIVE ACTIONS	79
6.2	AFFIRMATIVE ACTION AND THE FEDERAL CONSTITUTION	79
6.3	MARKET FRIENDLY AFFIRMATIVE ACTION	80
6.4	ADDRESSING THE BOTTOM 40% OF HOUSEHOLDS	81
6.5	REDUCING INCOME DISPARITY AND REGIONAL DIFFERENCES	82
6.5.1	<i>Policy Measure: Establish an Overarching Policy on Social Assistance Programmes</i>	83
6.5.2	<i>Policy Measure: Adopt a Single Comprehensive Database Based Initially on e-Kasih</i>	83
6.5.3	<i>Policy Measure: Address the Transportation and Housing Needs</i>	83
6.5.4	<i>Policy Measure: Break the Poverty Cycle through Education</i>	84
6.6	TARGETED PROGRAMMES FOR BCIC	85
6.6.1	<i>Policy Measure: Establish Specific Programmes for Bumiputera SMEs</i>	85
6.6.2	<i>Policy Measure: Focus on Capacity Building Programmes</i>	85
6.7	THE RELATIONSHIP BETWEEN HIGH INCOME AND INEQUALITY IN THE OWNERSHIP OF ASSETS	86
6.8	STRENGTHEN INSTITUTIONS FOR INCLUSIVE GROWTH	86
7	IMPLEMENTATION CONSIDERATIONS	89
7.1	GAME CHANGE NEEDED IN IMPLEMENTATION MACHINERY	89
7.2	TWO COMPONENTS: CENTRAL AGENCY AND INDEPENDENT EVALUATION BOARD	90
7.3	PEMANDU'S ROLE AS THE IMPLEMENTATION CENTRAL AGENCY	91
7.3.1	Managing Strategic Direction	93
7.3.2	Monitoring and Reporting	93
7.3.3	Policy Formulation and Design	93
7.3.4	Relationship with Independent Evaluation Board	94
7.4	THE FUNCTIONS OF THE INDEPENDENT EVALUATION BOARD (IEB)	94
8	FROM VISION TO RESULTS	99

# List of Appendices

---

Appendix A – Policies for the E & E Sector.....	103
Appendix B – Policies for the Palm Oil Sector .....	107

# List of Figures

---

Figure 1.1 – National Transformation .....	5
Figure 1.2 – SRIs and NKEAs.....	6
Figure 2.1 – Growth Can Be Consistent with Distribution.....	14
Figure 2.2 – Socio-Political Reforms to Remove Rent-Seeking Behaviour .....	15
Figure 2.3 – Government-Owned Companies.....	18
Figure 2.4 – Breakdown in the GLC Supply Chain.....	19
Figure 2.5 – Policy Strategy for Rationalising GLCs.....	20
Figure 2.6 – Standards and the Integrated Supply Chain.....	25
Figure 3.1 – The Innovation Eco-system.....	43
Figure 7.1 – The Implementation Framework.....	91
Figure 7.2 – Operationalising PEMANDU's Functions .....	93

# List of Tables

---

Table 2.1 – Summary of Policy Measures for Private Sector Transformation .....	13
Table 2.2 – Internationally Accepted Principles of Public Sector Governance .....	16
Table 2.3 – Alternative Methods for Strategic Control.....	21
Table 2.4 – Summary of Divestment Strategies for Non-Strategic GLCs.....	22
Table 2.5 – Suggested Liberalisation Policy Framework for Malaysia.....	28
Table 3.1 – Summary of Policy Measures for Enhancing Innovation .....	46
Table 4.1 – Summary of Policy Measures for Transforming Government .....	54
Table 5.1 – Summary of Policy Measures for Developing a Functional Labour Market.....	65
Table 5.2 – Comprehensive Modernisation and Consolidation of Labour Legislation.....	67
Table 6.1 – Summary of Policy Measures for Narrowing Disparities .....	82
Table 7.1 – Requirements of Implementation Process .....	94

# Glossary of acronyms

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<b>7MP</b>	Seventh Malaysia Plan
<b>8MP</b>	Eighth Malaysia Plan
<b>9MP</b>	Ninth Malaysia Plan
<b>10MP</b>	Tenth Malaysia Plan
<b>11MP</b>	Eleventh Malaysia Plan
<b>ASEAN</b>	Association of South East Asian Nations
<b>BCIC</b>	Bumiputera Commercial and Industrial Community
<b>BDS</b>	Business Development Services
<b>BLESS</b>	Business Licensing Electronic Support System
<b>BNM</b>	Bank Negara Malaysia
<b>CCR</b>	Commercial Credit Registries
<b>CEE</b>	Centre of Engineering Excellence
<b>CGC</b>	Credit Guarantee Corporation
<b>CPI</b>	Consumer Price Index
<b>CRS</b>	Credit Reporting System
<b>CSR</b>	Corporate Social Responsibility
<b>E&amp;E</b>	Electrical and Electronics
<b>EIAG</b>	UK Government's Environmental Innovation Advisory Group
<b>EKUINAS</b>	Ekuiti Nasional Bhd
<b>EPF</b>	Employees Provident Fund
<b>EPP</b>	Entry Point Projects
<b>EPU</b>	Economic Planning Unit
<b>ETP</b>	Economic Transformation Programme
<b>EU</b>	European Union
<b>FCP</b>	Forward Commitment Procurement
<b>FDI</b>	Foreign Direct Investment

<b>FSAP</b>	Financial Sector Assessment Programme
<b>FSMP2</b>	Bank Negara Malaysia's Financial Sector Master Plan 2
<b>FTA</b>	Free Trade Agreement
<b>GDP</b>	Gross Domestic Product
<b>GFC</b>	Global Financial Crisis (2007-2010)
<b>GLC</b>	Government-Linked Company
<b>GLIC</b>	Government-Linked Investment Company
<b>CMP2</b>	Securities Commission's Capital Market Master Plan 2
<b>GOA</b>	GLC Oversight Authority
<b>GST</b>	Goods and Services Tax
<b>GTP</b>	Government Transformation Programme
<b>HiCoE</b>	Centres of Excellence Accredited by the Ministry Of Higher Education
<b>HR</b>	Human Resources
<b>HRDF</b>	Human Resource Development Fund
<b>HSBB</b>	High Speed Broadband
<b>ICR</b>	Insolvency Creditor Rights
<b>ICT</b>	Information and Communication Technology
<b>IDFR</b>	Institute of Diplomacy and Foreign Relations
<b>IEB</b>	Independent Evaluation Board
<b>IHL</b>	Institutions of Higher Learning
<b>IIT</b>	Indian Institute of Technology
<b>ILKAP</b>	Judicial and Legal Training Institute
<b>ILO</b>	International Labour Organisation
<b>IMD</b>	International Institute for Management Development
<b>IMF</b>	International Monetary Fund
<b>IOM</b>	International Organisation for Migration
<b>INTAN</b>	National Institute of Public Administration
<b>IP</b>	Intellectual Property
<b>IPO</b>	Initial Public Offering

<b>ISIS</b>	Institute of Strategic and International Studies, Malaysia
<b>JAL</b>	Japan Airlines
<b>JKR</b>	Malaysian Public Works Department
<b>JPK</b>	Department of Skills Development
<b>KPI</b>	Key Performance Indicator
<b>KPO</b>	Knowledge Process Outsourcing
<b>KPWKM</b>	Ministry of Women, Family & Community Development
<b>LED</b>	Light Emitting Diode
<b>LTAT</b>	Armed Forces Fund Board
<b>MAMPU</b>	Malaysia Administrative Modernisation and Management Planning Unit
<b>MARA</b>	Council of Trust for the Bumiputera
<b>MIDA</b>	Malaysian Industrial Development Authority
<b>MIER</b>	Malaysian Institute of Economic Research
<b>MITI</b>	Ministry of International Trade and Industry
<b>MNC</b>	Multi-National Corporation
<b>MOHE</b>	Ministry of Higher Education
<b>MOHR</b>	Ministry of Human Resources
<b>MOSTI</b>	Ministry of Science, Technology & Innovation
<b>MPC</b>	Malaysia Productivity Corporation
<b>MPOB</b>	Malaysian Palm Oil Board
<b>MQA</b>	Malaysian Qualification Agency
<b>NCIA</b>	Northern Corridor Implementation Authority
<b>NDPC</b>	National Development Planning Committee
<b>NEAC</b>	National Economic Advisory Council
<b>NEM</b>	New Economic Model
<b>NGO</b>	Non-Governmental Organisations
<b>NIC</b>	National Innovation Council
<b>NKEA</b>	National Key Economic Areas
<b>NKRA</b>	National Key Result Areas

<b>NWCC</b>	National Wage Consultative Council
<b>OECD</b>	Organisation of Economic Cooperation and Development
<b>OEM</b>	Original Equipment Manufacturing
<b>PATA</b>	Pacific Asia Travel Association
<b>PCG</b>	Putrajaya Committee on GLC High Performance
<b>PEMANDU</b>	Performance Management and Delivery Unit
<b>PEMUDAH</b>	Special Task Force to Facilitate Business
<b>PLWS</b>	Productivity-Linked Wage System
<b>PMR</b>	Penilaian Menengah Rendah
<b>PNB</b>	Permodalan Nasional Berhad
<b>PSC</b>	Public Service Commission
<b>PSMB</b>	Pembangunan Sumber Manusia Berhad (HRDC)
<b>R&amp;D</b>	Research and Development
<b>RIA</b>	Regulatory Impact Analysis
<b>ROSC</b>	Report on the Observance of Standards and Codes
<b>SME</b>	Small and Medium Enterprise
<b>SMR</b>	Standard Malaysian Rubber
<b>SOCISO</b>	Social Security Organisation
<b>SOE</b>	State-Owned Enterprise
<b>SPM</b>	Sijil Pelajaran Malaysia
<b>SRI</b>	Strategic Reform Initiative
<b>SWF</b>	Sovereign Wealth Fund
<b>TC</b>	Talent Corporation
<b>TFP</b>	Total Factor Productivity
<b>THCDS</b>	Total Human Capital Development System
<b>TM</b>	Telekom Malaysia Berhad
<b>TNB</b>	Tenaga Nasional Berhad
<b>UI</b>	Unemployment Insurance
<b>UN</b>	United Nations

<b>US</b>	United States Of America
<b>USM</b>	Universiti Sains Malaysia
<b>USP</b>	Universal Service Provision Fund
<b>VC</b>	Venture Capital
<b>WGI</b>	World Bank's Governance Indicators
<b>WTO</b>	World Trade Organisation

CHAPTER

1

# COMPONENTS OF THE ECONOMIC TRANSFORMATION PROGRAMME (ETP)





# 1 COMPONENTS OF THE ECONOMIC TRANSFORMATION PROGRAMME (ETP)

The National Economic Advisory Council (NEAC) is honoured to submit this report 'New Economic Model for Malaysia – Concluding Part: Strategic Policy Measures' for consideration by the Government of Malaysia. A wide range of views and recommendations were made by Council Members, with input from various working groups comprising representatives from the private and public sector. This report reflects the broad consensus of the Council on key issues.

The sequential announcements and release of the NEM, the Tenth Malaysia Plan (10MP), the projects of the National Key Economic Areas (NKEAs) and the 2011 Budget, all between March and October 2010, have been generally well received by the public. The 10MP, a rolling plan covering the period 2011-2015, and the 2011 Budget, have incorporated most of the NEAC's policy recommendations designed to achieve the NEM goals of high income, inclusiveness and sustainability. We expect these policy directions to continue for the subsequent five years of the Eleventh Malaysia Plan (11MP). Moreover, it has been made clear that the success of the NKEAs hinges critically on the adoption of the SRIs of the NEM. Since the announcement of the NEM, domestic and foreign perception of Malaysia has improved in recognition of the Prime Minister's commitment to achieve Vision 2020.

## 1.1 THE CHANGING CONTEXT OF INTERNATIONAL COMPETITION

The required economic transformation is premised on a simple strategic reality. While Malaysia is richly endowed in natural resources, its economy is too small to compete directly with larger ones. Nevertheless, we must recognise that Malaysia's continued and future prosperity is inextricably linked to the global economy. Hence, Malaysia must exploit her comparative advantages within the global production network in order to raise income and enhance the quality of life. Many of the barriers to Malaysia's effective global integration are legacy structural issues and outdated policies clearly identified in the NEM.

The NEAC recognises that progress towards an advanced nation depends in part on social stability, inclusiveness, and greater equality, but this has to be achieved through an open system that encourages growth and innovation. It is only through growth that new resources will become available for continued social engineering to address inclusivity and environmental sustainability..

High subsidies, enabled by Malaysia's resource endowments, have shielded us from the full impact of several external shocks. But this has come at the cost of faster-than-prudent natural resource depletion and larger, persistent fiscal deficits. Malaysia could become a net importer of energy as early as 2015.

Furthermore, the rapidly changing external environment has become much more challenging. Since March 2010, the risk of a double-dip recession in industrial economies' has risen. The emerging-market countries are likely to compete more vigorously and directly with Malaysia in trade and inward investments. Hence, Malaysia's progress toward advanced income status will occur in a less favourable global economic environment than previously envisaged.

Domestically, the NEM has been met with demands for continued protection from those who fear change. But the reality is that the problems faced by Malaysia are not sectoral or factional, but national and global in nature. Irrespective of ethnic issues, both capital and human talent have been flowing outwards, fiscal debt is rising, wages are stagnating, graduate unemployment is increasing and growth prospects will remain weak unless the fundamental issues that impede progress are addressed.

In order to advance to a high income, inclusive and sustainable economy by 2020, Malaysia needs to confront two fundamental but inter-related issues.

- Malaysia cannot be an advanced country without social cohesion and stability.
- Malaysia cannot compete globally if the education system produces graduates and workers that are technically ill-equipped for a competitive global market.

Social cohesion and stability means that the benefits of growth and prosperity must be shared by all. At the same time, the education system must produce graduates who are equipped for modern day dynamic challenges and work demands.

If the 'New Normal' is flexible, innovative and creative economies that are highly competitive, then for Malaysia to advance into that category, the country must produce a labour force and enterprises that are nimble, innovative and constantly adjusting to the fast changing environment. This condition must be accompanied by a lean government bureaucracy that is flexible, facilitative, and enables the economic transformation advocated by the NEM. Its structures, processes, rules and activities must generate continuous learning and new thinking to meet the challenges of managing uncertainty.

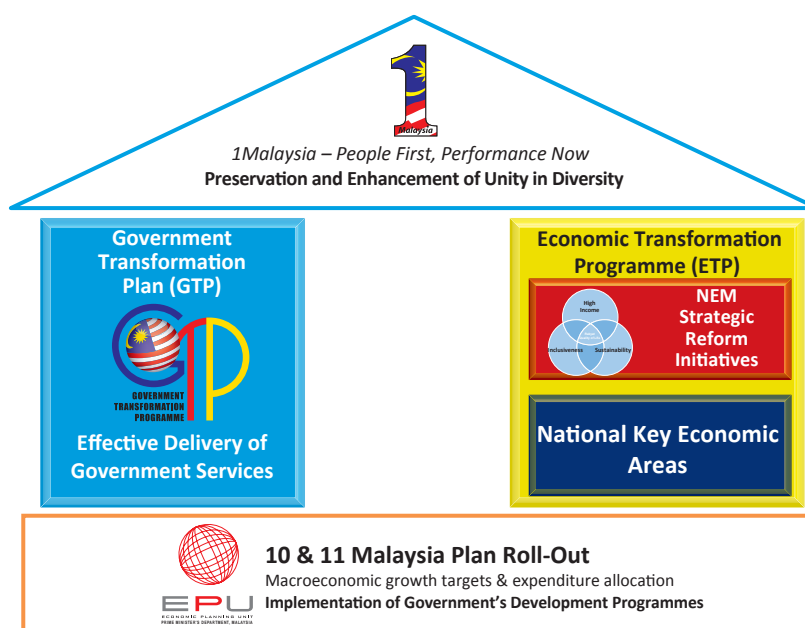
Incremental solutions to address considerable legacy problems and intense international competition will not succeed. Malaysia must aim for a "game change" package that will stimulate growth, whilst at the same time address the long-term structural issues that will take time to resolve. Foreign investment and confidence among domestic players depends greatly on increased competitiveness within the country. The path forward, however unpleasant to some, must be free of rent-seeking activities which are draining the Malaysian economy and greatly hindering the move towards an inclusive, high income and sustainable society.

## **1.2 NATIONAL TRANSFORMATION AND THE ETP**

Acknowledging that the problems Malaysia faces are multi-dimensional in nature, the approach chosen by the Prime Minister involves both government and economic transformation programmes over the span of two five-year development blueprints (**Figure 1.1**).

- Achievement of Vision 2020 must embody the principles of 1Malaysia – People First, Performance Now to unite all Malaysians.
- The Government Transformation Programme (GTP) will deliver the outcomes defined under the National Key Result Areas (NKRAs). The Performance Management and Delivery Unit (PEMANDU) has been managing the implementation of the reforms.

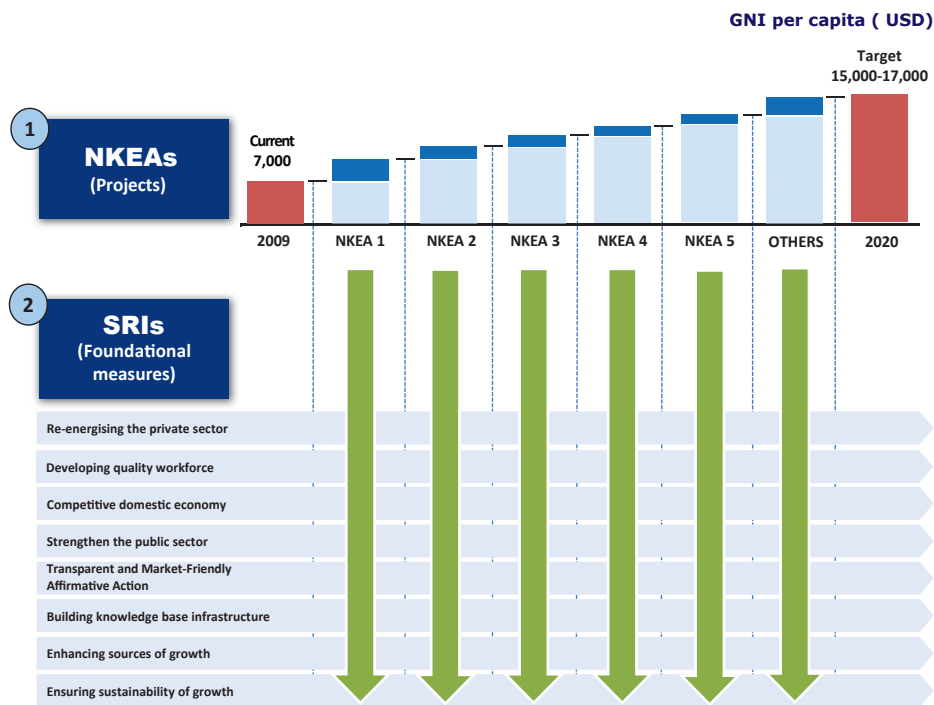
Figure 1.1 – National Transformation



- The Economic Transformation Programme (ETP) will transform Malaysia into a high income, inclusive and sustainable economy. The ETP has two parts: the Strategic Reform Initiatives (SRIs) of the NEM and the National Key Economic Areas (NKEAs) (Figure 1.2). The policies measures underlying the SRIs and as set forth in this report, are the foundational measures critical to the success of the NKEAs. PEMANDU is also tasked with managing the ETP and after working on the implementation aspects of the NKEAS through extensive labs, the Entry Point Projects (EPP) identified were launched at the end of October 2010.
- The platform for delivering the policy actions is set forth in the Ten Big Ideas of the 10MP which will be supplemented by further actions in the course of 11MP through 2020.

In March 2010, the NEAC presented a frank and realistic assessment of Malaysia's current economic situation and its future prospects. Eight SRIs were identified to propel transformation and growth in the Malaysian economy. Their successful implementation depends critically on political will and the determination of all Malaysians to work together and progress to an advanced nation status.

Figure 1.2 – SRIs and NKEAs



These SRIs are:

1. Re-energising the private sector
2. Developing a quality workforce and reducing dependency on foreign labour
3. Creating a competitive domestic economy
4. Strengthening of the public sector
5. Transparent and market friendly affirmative action
6. Building the knowledge base infrastructure
7. Enhancing the sources of growth
8. Ensuring sustainability of growth

The NEAC takes note that the work and research undertaken in the development of the 10MP and the NKEA Entry Point Projects (EPPs) have implicitly assumed that many of the foundational policy measures underlying the SRIs would be adopted in a timely manner. The NEAC wishes to emphasise that these cross-cutting policy measures would need to be implemented consistently and holistically to ensure that the results envisioned in the 10MP and the EPPs, and ultimately the goals of the NEM, are achievable.

Determining the right mix and sequencing of the policy measures is critical for Malaysia to break out of the middle-income trap. This NEM Report identifies several high-priority policies and the key cross-cutting issues to be tackled head-on and urgently. These priorities are set forth in the various chapters throughout the Report, which also highlights the key barriers to economic growth and national transformation. It provides recommendations on focussed and integrated policy actions.



CHAPTER

2

**TRANSFORMATION  
THROUGH  
REINVIGORATING THE  
PRIVATE SECTOR**





## 2 TRANSFORMATION THROUGH REINVIGORATING THE PRIVATE SECTOR

### 2.1 INTEGRATION INTO THE GLOBAL SUPPLY CHAIN

In a highly competitive and inter-connected world of trade and investments, national and global production of goods and services is part of supply chains that constantly evolve with the needs of domestic or export customers. A necessary step is for Malaysia to integrate the country's supply chains to create scale. Many of the production and service entities in Malaysia are segregated, do not adequately interact and cooperate with each other, and consequently, do not function effectively or efficiently. To further compound the problem, inefficiencies in the associated government processes are responsible for the inability of these entities to function properly and compete globally.

Given its small size, Malaysia has to be more nimble, focussed, flexible and efficient in order to compete. Malaysia needs to re-tool itself to find a niche and join the global supply chain in order to benefit fully from sales of its products and services through innovation-based comparative advantages. National and global production and trade are increasingly defined by supply chains. Supply chains are defined as the system of organisations, people, processes, technology, activities, information and resources involved in moving a product from supplier to customer or end user.

Today, MNCs have expanded the supply chain to include the production chain in East Asia and the distribution channels in the advanced markets. The Malaysian electrical and electronics (E&E) industry is a major part of this supply chain, with products designed in California, chips made in Taiwan, drives in Korea, LED screens in Japan and other parts manufactured and assembled in Malaysia for ultimate export to the US and EU. Once a company or a nation successfully plugs into the global supply chain, it would have the advantage of scale and branding that would be difficult for competitors to dislodge.

Globalisation has allowed companies to expand their operational scope and target markets beyond that of a traditional company looking to sell to its neighbourhood, city or country. Being part of the global supply chain gives exposure to higher level of standards and changes both the labour force and the consumer mindset and demand. This in turn feeds back into a virtuous circle – firms in the supply chain respond by upgrading their quality control, efficiency and standards to meet the end users' needs.

In the last 50 years, developing countries like Malaysia have advanced into middle-income and high income status by essentially joining the global supply chain. Globalisation is about cooperation and supply chain competition and the value of the network is larger than the sum of its parts. Wealth and income creation come from enhancing the value of the supply chain.

Malaysia's success must be geared towards generating income from being part of the global supply chain. Every corporation, multi-national or domestic, SME, non-governmental organisation (NGO), government or individual worker and government body should be integrated into a more wholesome national supply chain, which would then feed into the global one. Within the manufacturing space, the MNCs based in Malaysia can serve as a backbone to supply the world with Malaysian products. Malaysian SMEs would either supply the local MNCs or feed directly into foreign supply chains. The integration of Malaysian enterprises into a national supply chain

will support an even higher objective of building additional home-grown MNCs that will serve to enhance Malaysia's global brand.

The Government is central to this effort to help enterprises integrate into the global supply chain. This is by no means an easy feat. To begin with, national involvement needs to be orchestrated into creating an integrated national supply chain. The Prime Minister's 1Malaysia concept can be operationalised so that all segments of the Malaysian economy, be it private, government, or NGO, understand that we have a stake in Malaysia's success and that we must cooperate to improve the efficiency and connectivity of the economy.

Integrating the country's supply chains that are sub-scale is one of the key components to achieve NEM's objectives. The reason the Bumiputera Commercial and Industrial Community (BCIC) has not taken root is that the current delivery supply chain is not integrated with the rest of the local as well as globally connected and competitive supply chains. Joining and developing an integrated national supply chain is thus a prerequisite for a vibrant BCIC. Successful bumiputera firms need to be highlighted as champions, whose partnerships with the business community at large, including the GLCs, will raise the performance of the entire BCIC. This cannot be done in isolation and integration of the existing fragmented supply chain is essential, with every community having a role to play. The real danger to Malaysia is that if growth does not become top priority, our supply chains will be marginalised or worse, by-passed. Left unchecked, we will soon be taken over by regional competitors, especially if capital and talent outflows continue.

Malaysia's major obstacle is the absence of fairer competition to raise competitiveness within the nation. The existing restrictions on equity holdings and operations as well as slow liberalisation and deregulation policies make it difficult for domestic and global entrepreneurs to invest in Malaysia, undermining the efforts of local players to improve themselves through competition. The lack of investment has also resulted in poorly inter-linked and inefficient transport and distribution systems, which hinder economic progress and connectivity. Another key legacy and inherent obstacle in integrating the domestic economic network is the adversarial attitude between the Government/ GLC entities and the private sector. The lack of trust between the different ethnic groups in Malaysia is also a barrier to domestic economic network integration.

Striving for an integrated national supply chain could serve as a blueprint for facilitating the country's ability to compete. The Government must establish clear guidelines for national policy to support competitiveness. Benchmarking against international standards and best practices – instead of solely rankings – should be given a greater focus. An efficient feedback loop needs to be put in place urgently to ensure policies are relevant and user driven and achievements appropriately measured against desired outcomes. Applying the strategy to “Simplify, Focus and Integrate” will see the whole government network geared towards meeting the needs of all stakeholders, and at the same time provide an environment to support business in improving value chains and finding new market niches as well as improving sustainable practices.

The 10MP has recognised the overall national supply chain concept and with it, the need to integrate in order to achieve economic efficiencies. Although current operating structures cannot be changed overnight, reforms must begin now (**Table 2.1**). The Government has a critical role as a facilitator and an enabler in creating an efficient and integrated national supply chain, ensuring service delivery at all levels of the government is simplified, focussed and integrated.

**Table 2.1 – Summary of Policy Measures for Reinvigorating the Private Sector**

<b>Eliminating Rent-Seeking Behaviour</b>
<ul style="list-style-type: none"> <li>• Set a rationalised and robust framework for public sector governance to enable greater flexibility in response to the changing environment</li> <li>• Urgently address the NKRA initiative against corruption within the GTP</li> </ul>
<b>Rationalising Government's Participation in Business</b>
<ul style="list-style-type: none"> <li>• Divest non-strategic companies and re-engineer the roles of the remaining GLCs</li> <li>• Channel proceeds from divestment into a sovereign wealth fund</li> <li>• Re-engineer GLCs to support the private sector</li> </ul>
<b>Adopting International Standards and Best Practices</b>
<ul style="list-style-type: none"> <li>• Use international best practices to facilitate connection to the global supply chain</li> <li>• Convert existing Malaysian Standards into international standards</li> </ul>
<b>Promoting Competition through Liberalisation and Deregulation</b>
<ul style="list-style-type: none"> <li>• Continue the liberalisation programme, especially on the 12 identified NKEA sectors, to remove restrictions on ownership and operations, with a medium-term target of generating a negative list</li> <li>• Establish a deregulation unit and streamline regulations</li> <li>• Ensure independence and integrity of the Competition Commission</li> </ul>
<b>Introducing Innovation in Financing</b>
<ul style="list-style-type: none"> <li>• Increase access to funding (including a Transformation Fund) for start-ups and SMEs by shifting away from collateral based lending</li> </ul>
<b>Enhancing Business Connectivity</b>
<ul style="list-style-type: none"> <li>• Accelerate the rollout of broadband to facilitate business transactions and activities</li> </ul>
<b>Preserving the Environment</b>
<ul style="list-style-type: none"> <li>• Adopt a 'Polluter Pays' principle backed by legislation and target Green growth by capitalising on the potential to advance sustainable agriculture</li> <li>• Rationalise subsidies and remove price controls on energy to encourage in the long run the adoption of renewable and green technology</li> </ul>

## **2.2 REINVIGORATING THE PRIVATE SECTOR TO SUPPORT AN INTEGRATED MALAYSIA SUPPLY CHAIN REQUIRES BROAD-BASED STRUCTURAL REFORMS**

The NEM SRIs are aimed at building dynamism in the private sector as the driver of economic growth. The underlying policy measures (especially SRI1, SRI3, SRI7 and SRI8) are meant to reenergise the private sector, create a competitive domestic economy, enhance the sources of growth and ensure sustainability of development. These measures must be supported by reforms in the public sector and a vibrant labour market that support innovation while striving for inclusiveness from pro-poor affirmative programmes.

Reinvigorating the private sector rests upon restoring confidence in Malaysia as a choice destination for investments by both domestic and foreign investors. This calls for actions to address the existence of a sub-par investment climate, characterised by policy inconsistency/uncertainty, over-regulation and market failures. Systemic barriers affecting all sectors in the economy must be dismantled to create an optimal investment climate that will attract investors.

The 10MP and NKEAs have identified projects that will enhance Malaysian sources of growth. However, these projects will not take off successfully if structural barriers which impede implementation are still in place. Broad-based reforms must be implemented holistically across a range of areas to address foundational issues. But these may be insufficient unless there is social stability to be harnessed by growth which supports a sharing of economic wealth among the major communities. In this respect, promoting a vibrant BCIC to become an integral part of the Malaysian economy is essential.

### 2.3 A NEW SOCIO-ECONOMIC FRAMEWORK FOR INVESTMENT

Malaysia's balanced approach in economic management to meet objectives of economic and social stability has worked in the past and is still relevant in today's environment. In fact, the globalised markets and rapid communication technologies make balancing growth with stability even more important. The private sector needs stability and certainty in policy actions to build confidence for making corporate decisions on long-term investment and growth strategies.

To promote a longer-term stable and favourable investment climate, the NEAC recommends that priority be accorded to policies that are positive on growth as well as positive on distribution (**Figure 2.1**). For instance, provision of special education facilities for the bottom 40% of households (e.g. boarding schools for rural students) is good for capacity building and has a positive impact on both growth and distribution. In comparison, direct financial support is positive on distribution but may achieve little in terms of growth.

**Figure 2.1 – Growth Can Be Consistent with Distribution**

Effect of Policy Measure	Negative on Growth	Positive on Growth
Positive on Distribution	<ul style="list-style-type: none"> <li>• Low priority - policies having temporary adverse impact on Growth</li> <li>• Avoid - all other situations</li> </ul>	High Priority
Negative on Distribution	Avoid	<ul style="list-style-type: none"> <li>• Medium Priority - policies having temporary adverse impact on distribution</li> <li>• Avoid - all other situations</li> </ul>

Prioritise "win-win" policies that accelerate growth and promote equitable distribution

## 2.4 REFORMS TO ELIMINATE RENT-SEEKING BEHAVIOUR

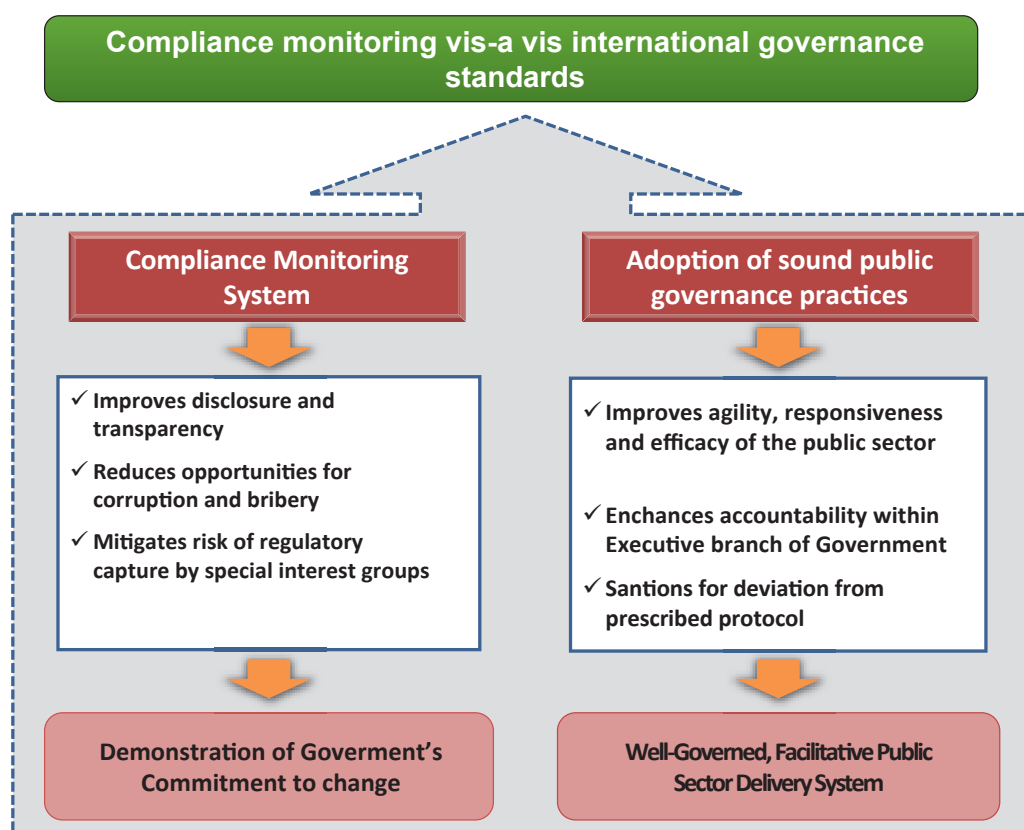
In its efforts to contain rent-seeking, Government has taken some significant steps towards inhibiting such practices. Promoting increased transparency in Government contracts, strengthening the independence of key institutions and establishment of the Malaysian Institute of Integrity are steps in the right direction. Despite these efforts, the Government continues to be perceived by the public as ineffective in its fight against these practices which are considered to be pervasive and entrenched.

Perception of a government ineffective in battling rent-seeking and corruption damages a country's attractiveness as an investment destination, and translates into high costs of doing business. The higher cost of doing business, combined with the erosion of confidence of citizens in the integrity of public institutions, has contributed to a slide in our competitiveness.

The GTP contains several initiatives to tackle corruption (see GTP: The Roadmap, Pages: 137-138). The NEAC recognises the importance of these GTP initiatives and fully supports the commitment in the NKRA to have zero corruption as this endeavour will have a positive impact on improving the competitiveness of and confidence in our nation.

The Government should also ensure that the principles of sound public sector governance are adopted by all agencies and that sanctions are levied against bad practices. The Malaysia civil service has always had a high reputation in supporting the executive arm within the legislative framework. Nevertheless, the nation's public delivery system can be further improved especially so to remain in line with the demands required to become a high-income economy. The findings of the Auditor General must be given greater emphasis by the civil service. This will enhance the civil service's reputation in line with the principle of good governance.

**Figure 2.2 – Socio-Political Reforms to Remove Rent-Seeking Behaviour**



Reinvigorating private investor confidence in the Malaysian economy requires an overhaul of public sector governance practices (**Figure 2.2**). Opportunities for rent-seeking and corruption must be minimised to lend business processes certainty and transparency. To achieve this, the NEAC recommends that the Government adopt a three-pronged approach comprising:

- (i) Revising the framework for public sector governance, covering an overhaul of the principles, processes and procedures as well as the prerequisites for successful implementation of governance precepts;
- (ii) Adopting the framework of initiatives as proposed under the NKRA on ‘fighting corruption’, and;
- (iii) Implementing a compliance monitoring system and defining measurement indicators to assess the effectiveness of public sector governance.

#### **2.4.1 Policy Measure: Revise the Public Sector Governance Framework**

The Malaysian public sector governance framework should be based on internationally accepted principles of public sector governance (**Table 2.2**).

The revised governance system should be principles-based rather than rules-based. This enables greater flexibility to respond to the changing needs of the Government in response to a constantly changing environment. A principles-based system requires civil servants to acquire an understanding of policy issues which influence policy decisions.

**Table 2.2 – Internationally Accepted Principles of Public Sector Governance<sup>1</sup>**

<b>NO.</b>	<b>Principle</b>	<b>The public sector must...</b>
1	<b>Accountability, with internal &amp; external compliance</b>	<ul style="list-style-type: none"> <li>• Be answerable for decisions and put in place mechanisms to ensure every agency adheres to well-defined internal controls and accountability</li> <li>• Ensure all applicable practices and procedures are within the set standards</li> <li>• Meet accountability expectations posed by external scrutiny</li> </ul>
2	<b>Transparency, information sharing &amp; openness</b>	<ul style="list-style-type: none"> <li>• Have clear roles and responsibilities across agencies and at all levels, and clear procedures for making decisions and exercising power</li> <li>• Institutionalise appropriate information management to ensure information gets to the right people in a timely manner to enable decision making</li> </ul>
3	<b>Integrity</b>	<ul style="list-style-type: none"> <li>• Ensure that actions at every level are in the interest of the agency, taken impartially and with integrity, and observe the fundamental principle of not misusing information that is confidential or acquired through a position of trust</li> </ul>
4	<b>Stewardship</b>	<ul style="list-style-type: none"> <li>• Exercise all abilities and talents to enhance the value accorded to the public and the private sector, and where relevant, to build value in public sector assets</li> </ul>
5	<b>Efficiency</b>	<ul style="list-style-type: none"> <li>• Continuously improve the quality of public service on the basis of evidence-based strategies to further the aims of each agency</li> </ul>
6	<b>Leadership</b>	<ul style="list-style-type: none"> <li>• Inculcate a culture of good governance from the top – a necessary ingredient for commitment across all levels in each agency</li> </ul>
7	<b>Risk management</b>	<ul style="list-style-type: none"> <li>• Operate within an understanding of the risks in order to achieve objectives</li> </ul>
8	<b>Evaluation &amp; sanctions</b>	<ul style="list-style-type: none"> <li>• Subject governance structure and public sector employees and leadership to regular evaluation and reviews to ensure compliance</li> <li>• Ensure appropriate sanctions are imposed and made public to ensure practices are consistent and effective</li> </ul>

<sup>1</sup>Adapted from ‘Building Better Governance: The Australian Public Service Commission’ (2007) and ‘A Guide to Good Governance: Principles of Good Practice’ by the Auditor General of British Columbia.



Strong leadership is required to lead implementation of the reformed governance framework and leaders must demonstrate exemplary governance behaviour. Appropriate governance committee structures should be designed and strengthened with internal control mechanisms.

All agencies should be required to establish risk management units which are accountable for setting up sound risk management frameworks. These frameworks will determine the risk assessment system, monitor risks and manage risks for the public sector agency. Within this framework, there must be a system for reporting emerging risks to management and, in response to such risks, modalities for corrective actions or damage controls. All aspects of risk issues must be mainstreamed into the business planning processes.

Where government services are outsourced, it is vital to recognise that the ultimate responsibility remains with the public sector. These arrangements should be formalised in memoranda of understanding and record-keeping standards should be adopted to ensure that all agencies maintain comprehensive documentation that will withstand scrutiny.

Malaysia needs to build a reputation of integrity, openness and accountability in its public sector. Domestic and foreign investors must trust that decisions are made consistently, in an open manner, and that decisions will not be changed or reversed without clear explanation and accountabilities. Public sector agencies should be governed by standardised protocols and checklists for dealing with external stakeholders. Regular client surveys should be conducted to measure satisfaction levels (**See also Chapter 4**).

#### **2.4.2 Policy Measure: Implement a Compliance Monitoring System**

Internal and external compliance monitoring systems are necessary to ensure that public sector governance reforms remain on track. Internal monitoring of compliance is essential to detect early signs of emerging poor performance. Areas to be assessed include organisational direction (relevance of strategic planning to deliver overall government policies), leadership, organisational capability (all measures taken to build capacity and skills to deliver mandates), relationships and integrity, and organisational culture. To facilitate monitoring, key indicators must be set up for each of these areas.

Sanctions are an essential aspect of any compliance mechanism. Imposing sanctions upon transgressors will improve private sector confidence by signalling the Government's commitment to improving governance. Sanctions should not be limited to individual staff, but also to whole units or agencies where necessary. As governance emanates from leadership, agency shortcomings should be borne by both the director of the agency and the Minister who exercises the oversight. A fair but strict sanction regime, which should include public reprimand to agencies as well as published data on sanctions, will serve to build a culture of strict adherence to governance, while giving comfort to the private sector that public sector governance practices make rent-seeking unviable.

External assessment of compliance undertaken by multilateral agencies like the World Bank will also lend credibility to public sector reform initiatives. It is necessary to adopt a set of indicators to measure the efficacy and efficiency and other benchmarks of the public sector governance framework. The indicators also provide information on the workings of the framework, thus enabling improvements to be instituted. Publication of the ranking of performance indicators intensifies peer pressure to enhance integrity and performance. Using an internationally recognised benchmark allows for country comparison and impacts the competitiveness ranking,



further putting pressures for continuous improvement. Indicators measured by the World Bank include judicial and bureaucratic efficiency, level of corruption as well as political freedom and stability.

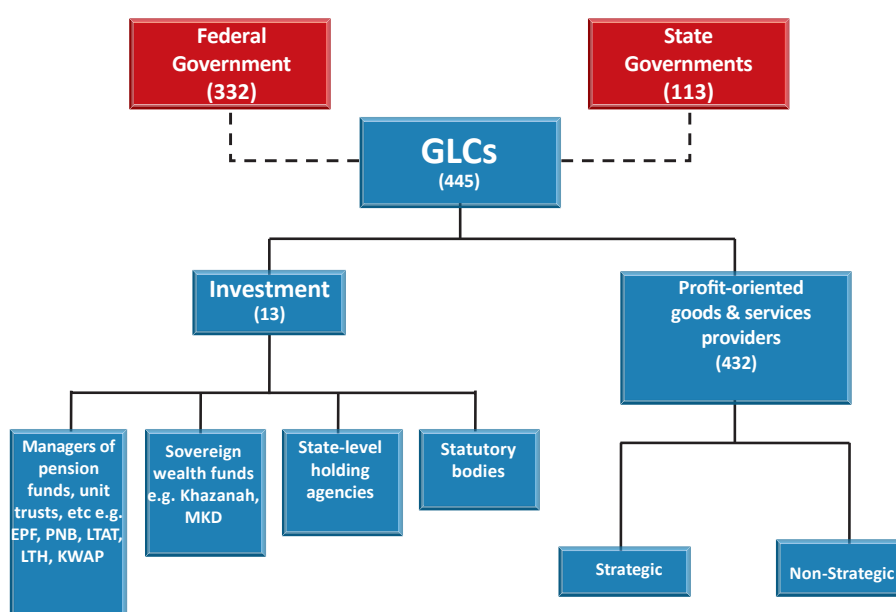
To eradicate the incentives that make rent-seeking viable, adoption of a revised public sector governance framework alone will not be enough. A monitoring mechanism to ensure comprehensive take-up of good public sector governance practices must be put in place. Implementation should be led by an independent team, reporting to a steering committee chaired by the Chief Secretary to the Government.

Successful implementation of this governance framework, in tandem with other market-optimisation efforts such as regulatory reform, promotion of competitive markets, GLC transformation and expansion of broadband access, will impact significantly upon private sector confidence. These measures, when executed as part of an integrated programme, will send a strong signal to investors of the Government's commitment to change and progress. The private sector will then once again become a powerful force to exert new dynamism in the economy.

## 2.5 RATIONALISING GOVERNMENT'S PARTICIPATION IN BUSINESS

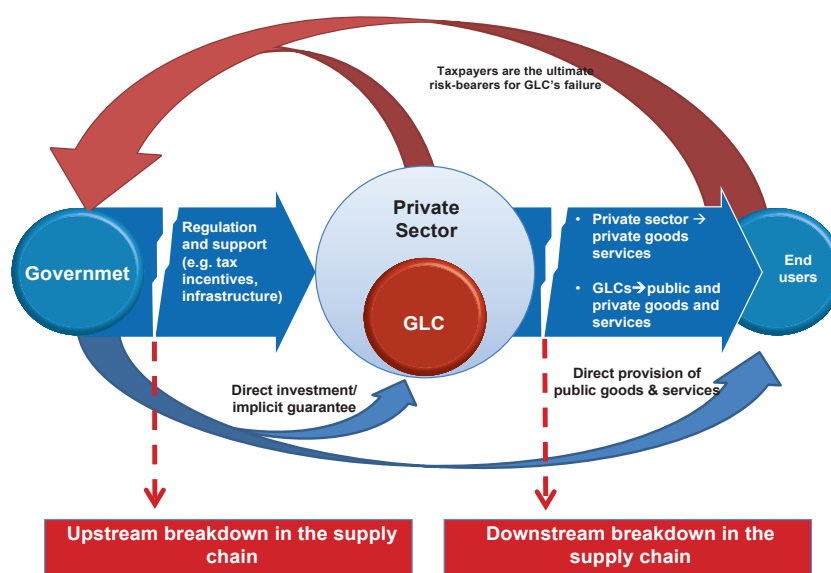
For the purposes of this Report, the NEAC coverage of GLCs is equivalent to the more internationally recognised term of SOE or State-Owned Enterprise, which refer to a company which trades marketable goods and services, is controlled by the Federal or State Governments and is directly funded by the Government or exposes the Government to contingent liabilities via capital, debt or income guarantees. The term 'Government-Linked Investment Company' (GLIC) refers to any agency that either receives funding or guarantees from the Government or is directly designated to invest in GLCs on the Government's behalf. An NEAC data search resulted in a list of 445 companies. As not all respondents submitted their list of holdings, it is plausible that the actual number of GLCs is significantly higher. In 1987, there were more than 1000 entities (**Figure 2.3**).

**Figure 2.3 – Government-Owned Companies**



GLCs are a dominant presence in the Malaysian economy. GLCs have played a key role in nation building as well as expanding the economy. However, in many GLCs a history of underperformance, poor governance practices and a host of other structural breakdowns in the GLC supply chain have put them in the spotlight for the wrong reasons (**Figure 2.4**).

**Figure 2.4 – Breakdown in the GLC Supply Chain**



It is important that there is complete information on the population of GLCs. Accurate and timely information will ensure the success of reform policy design and implementation. Unfortunately, there is no single body currently responsible for monitoring and collecting performance data on all GLCs.

Historically, GLCs have been tasked with providing public goods and services, maintaining government control in strategic sectors and engineering socioeconomic change through wealth re-distribution. However, investors feel that GLCs have ventured beyond their mandates and are now competing directly with private businesses, hence crowding out private investments.

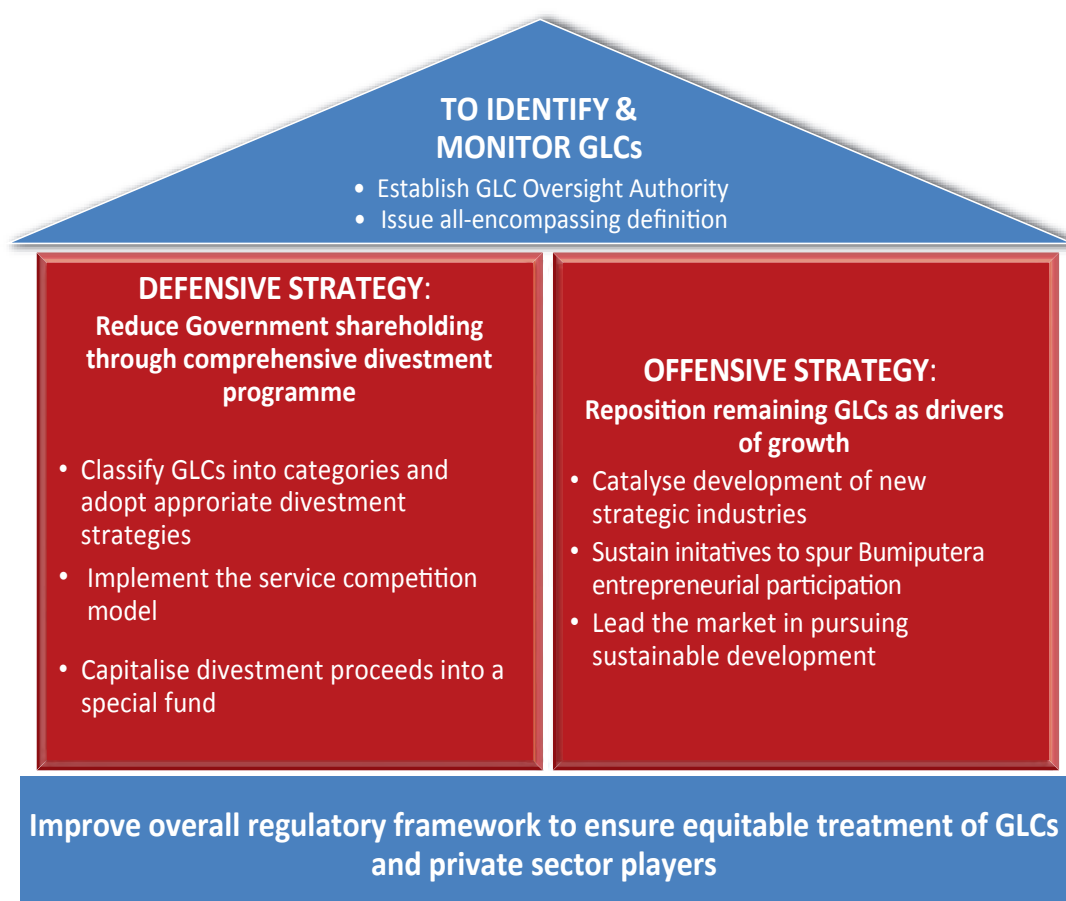
Because GLCs are frequently required to execute socioeconomic policy under the guise of corporate social responsibility, they are in return perceived to be enjoying preferential treatment in areas such as licensing and contract awards. The absence of proper objective cost-benefit analyses for contract awarding breed inefficiency and has anti-competitive repercussions within the private sector while disadvantaging minority shareholders.

Although the Government has engaged in a privatisation exercise in the late 1980s, most of the companies were only partially divested and remain government-linked. To date, daily trades on the Bursa are dominated by GLICs like the Employees Provident Fund (EPF) and Permodalan Nasional Berhad (PNB), with little scope for private investor participation in blue-chip listings due to heavy Government equity holding in Malaysia's biggest companies. This dampens private investor interest in Bursa-listed companies and hence constrains the scope for capital market development.

Policy recommendations are categorised into 4 main components (**Figure 2.5**):

- i. An oversight mechanism for GLCs
- ii. A model for the Government to divest non-strategic companies and re-engineer the roles of the remaining GLCs by adopting the service competition model and improving their governance.
- iii. Creation of a Fund from divestment proceeds to finance a GLC catalytic role to grow new private sector activities.
- iv. A re-engineered role for GLCs in the economy—one which supports and does not compete with the private sector.

**Figure 2.5 – Policy Strategy for Rationalising GLCs**



### **2.5.1 Policy Measure: Set Up a Central Oversight Authority**

While the boards of GLCs will continue to be ultimately accountable for their business, a GLC Oversight Authority (GOA) should be established to collect financial data on all GLCs, monitor their performance and hold GLCs accountable for their mandates and budgetary expenses incurred. Ideally, the GOA should report to the Prime Minister's Department and observe principles of transparency to build private sector confidence. It is conceivable that the existing Putrajaya Committee on GLC High Performance (PCG) should be formally institutionalised into the GOA.

The GOA should observe principles of transparency, including publishing an annual report, which would provide an analysis of the performance of all GLCs, their contributions to the economy, fulfilment of the GLC mandate and other necessary information.<sup>2</sup> The report should include summaries of the following information<sup>3</sup>:

- Objectives (financial and social) and the extent of their fulfilment;
- Key financial indicators and total Government portfolio value as at year end;
- Any trade-offs between commercial and public policy objectives and an estimate of their impacts on GLC resources and performance;
- Any material risk factors and steps taken to mitigate them;
- Financial assistance from the Government, including direct funds and guarantees, and;
- Transactions with related parties/entities.

### **2.5.2 Policy Measure: Divest Non-Strategic Companies and Re-engineer the Roles of the Remaining GLCs**

The Government should not hold large blocks of equity in non-strategic companies unless they are part of a liquid trading portfolio. The Government should privatise all non-strategic GLCs and concentrate on being the economy's regulator and facilitator. GOA should actively monitor this process and recommend divestment.

A strategic entity performs public sector functions which are critical for the country's economy and civil society. This often includes companies in the utilities, finance, transportation and telecommunications sectors. Any other entity is non-strategic.

Ownership is not a pre-requisite for control over strategic companies. The Government should consider capping its ownership of strategic companies to 30% of issued shares and adopt less invasive strategic control methods such as golden shares, industry policies and foreign ownership restrictions (Table 2.3).

**Table 2.3 – Alternative Methods for Strategic Control**

Method	Countries	Description
<b>Golden share</b>	Great Britain & Poland	<ul style="list-style-type: none"> <li>• The holder can influence major decisions of a strategic company; the Government retains control while ordinary shares are freed up for private investors.</li> <li>• To reduce scope for political interference, the discretionary powers of a golden share must be clearly defined and time-limited by a sunset clause.</li> </ul>
<b>Industry policy</b>	Japan	<ul style="list-style-type: none"> <li>• The Japanese Government holds only 0.05% of equity in Japan Airlines (JAL) but maintains strategic control via an aviation policy which requires all airlines to service regional airports as a form of CSR.</li> </ul>
<b>Foreign ownership restrictions</b>	Australia & Russia	<ul style="list-style-type: none"> <li>• The Australian Government does not use post-privatisation ownership controls but imposes foreign ownership limits on strategic entities (e.g. 49% in Qantas).</li> <li>• Russian strategic industries law requires foreign investors seeking a majority stake in any strategic company to obtain Government approval, while State-controlled foreign investors would require permission to hold stakes above 25%.</li> </ul>

<sup>2</sup> Adapted from the *OECD Guidelines on Corporate Governance of State-owned Enterprises*

<sup>3</sup> Aggregate reports for small GLCs and individual reports for larger GLCs

The NEAC recommends the following approach to the formulation of the divestment programme:

- i. Identify the objectives of the divestment programme.
- ii. Consider mitigating factors e.g. method of divestment and absorptive capacity of the capital market.
- iii. Determine principles of divestment.
- iv. Identify non-strategic GLCs and classify them based on their characteristics (e.g. performing/loss-making).
- v. Identify appropriate divestment strategy for each category of non-strategic GLCs.

Below is a summary of the divestment strategy recommended for each category of non-strategic GLCs (**Table 2.4**).

**Table 2.4 – Summary of Divestment Strategies for Non-Strategic GLCs**

Category	High-performing unlisted companies	Unlisted low performers with turnaround potential	Unlisted low performers without turnaround potential
<b>Strategy</b>	<ul style="list-style-type: none"> <li>Companies with a good track record that meet Bursa Malaysia listing criteria should be divested via the capital market.</li> <li>Aggregate Government shareholding capped at 10% of issued shares.</li> </ul>	<ul style="list-style-type: none"> <li>Appoint professional managers and provide incentives like employee/management buyout opportunities to revive the companies in order to graduate into the 'high performance' category.</li> </ul>	<ul style="list-style-type: none"> <li>Using objective criteria to determine strike price offer to the private sector for sale, failing which;</li> <li>Liquidate entities and establish an asset-management company to dispose of assets in a transparent and market-based manner.</li> </ul>
<b>Rationale</b>	<ul style="list-style-type: none"> <li>IPOs allow greater scope for private investors to own blue-chip equity; this contributes to capital market development.</li> <li>Listing would enable taxpayers to obtain direct equity stake in companies forged out of tax revenue.</li> </ul>	<ul style="list-style-type: none"> <li>Meritocratic appointments of professional managers allows experts to run GLCs.</li> <li>Decision-making independence minimises political interference that could jeopardise company performance.</li> </ul>	<ul style="list-style-type: none"> <li>The private sector may generate synergies by integrating these failing GLCs into their corporate structure.</li> <li>Liquidation will avoid further drain on fiscal resources.</li> </ul>

A portion of GLCs to be divested could be part of a special programme to support bumiputera entrepreneur consortiums through a transparent open tender process. GOA must ensure that this opportunity is accorded to a broad range of new entrepreneurs based on merit and capacity as an approach to halt worsening intra-bumiputera income disparities. Performance incentives such as opportunities for management buyout of successfully restructured GLCs also contribute to the achievement of the macro-level bumiputera equity ownership target.

In order to maintain momentum and market confidence, there should not be backtracking once the divestment programme is announced. The programme must be implemented in a transparent manner with clear procedures and the following set of principles:

- Divestment must follow internationally-benchmarked procedures and adopt proper governance principles;<sup>4</sup>

<sup>4</sup> Suggested standards include the OECD Guidelines on the Governance of State-owned Enterprises

- Divest non-strategic GLCs where the private sector has greater scope for value-creation;
- Divestments must be market-based using transparent procurement procedures and merit-based selection protocols with adequate safeguards against abuses;
- Other GLCs are disqualified from purchasing;
- Divestment cannot be reversed;
- Transactions should be conducted via the capital market to enable greater public participation and foster market development;
- Divestment proceeds must be settled in liquid funds and must be placed in a reserve account and not treated as general revenue;

The governance of remaining strategic GLCs should be improved according to best practices outlined in the GLC Transformation Manual issued by PCG<sup>5</sup>. Governance reform efforts should be expanded beyond the existing G20 companies to cover all GLCs, including State-owned entities, under the purview of GOA.

GLCs which manage physical infrastructure and are also service providers e.g. Telekom Malaysia (TM) and Tenaga Nasional Berhad (TNB) should adopt the service competition model. GLCs will only retain ownership of physical infrastructure and charge rent to businesses that tap into the network. The frontline content and service provision market will be fully liberalised, enabling network ownership and regulatory functions to be severed from operating rights.

### ***2.5.3 Policy Measure: Channel Proceeds from Divestment into a Sovereign Wealth Fund***

Divestment proceeds should not be treated as operating revenue (flow) but recognised as conversion of capital (stock). Proceeds should be placed into a sovereign wealth fund (SWF) that invests in various asset classes (e.g. securities, foreign exchanges and derivatives). This SWF will adopt a governance framework similar to BNM's foreign exchange reserves and be administered in accordance with the Santiago Principles which require, among others, disclosure of the SWF's investment policy, financial statements and risk management approach. Profits from the SWF could be used to catalyse new private sector initiatives, where risk issues may deter private sector activities.

### ***2.5.4 Policy Measure: Re-engineer GLCs to Support the Private Sector***

As GLCs reduce their involvement in businesses, they can play a more focussed and catalytic role in driving the private sector towards innovative new high value industries. GLCs should be accorded with responsibility to support innovation. It, however, must exit once these initiatives can be taken over by the private sector.

The PCG has proposed a six-pronged approach on the re-modelled roles of GLCs that remain after the divestment programme is completed. The NEAC supports this proposal as it will complement private sector development by attracting foreign investments and reducing entry barriers into new strategic industries. However, GLCs must have a clear exit strategy and must not linger in industries once the private sector no longer requires support.

<sup>5</sup> [http://www.pcg.gov.my/trans\\_manual.asp](http://www.pcg.gov.my/trans_manual.asp)

In rationalising the roles of GLCs, there must be a clear policy to ensure that GLCs as operators cannot be regulators. One key policy for transforming the private sector is to confirm that GLCs which provide services will not have regulatory functions in their industry. In this regard, the Government must work towards a mode where all regulatory functions are undertaken by independent regulators. There must be clear separation between regulators and operators, a key requirement to comply with the principles of good governance.

The Government should amend the existing legal and regulatory framework to level the playing field between GLCs and private businesses and alleviate private investor uncertainty.

As a matter of priority, it is essential that GLCs are covered under the provisions of the Competition Act 2010 to ensure that their trade practices are not anti-competitive. Any public policy obligation that has to be undertaken by GLCs (e.g. universal access requirements) must be mandated by laws and legislation. Information on these obligations, the resulting costs and impacts upon GLC performance and resources should be disclosed to the public in the GOA annual report.

The Government should refrain from providing automatic guarantees for GLC liabilities. Barriers, both formal and informal, in government procurement processes which accord GLCs preferential access should be removed. To ensure operational independence, political and ministerial interference in the day-to-day management of GLCs should be met with stiff sanctions. Officers and directors in GLCs also should be prohibited from being involved in formulating or enforcing regulations that directly affect their companies unless the non-GLC private sector is also duly represented.

To ensure that opportunity is accorded to disadvantaged groups, existing vendor development programmes should be expanded by partnering with SMEs, particularly those controlled by the bumiputera, and providing them management and technical expertise to grow the companies. GLCs could form a firm to provide one-stop business development services (BDS) to SMEs and exit once a viable market has been established with private sector BDS suppliers. Based on the success of a similar programme in Germany, GLCs also should develop an apprenticeship and internship system for bumiputera and low-earning households to build a bigger pool of entrepreneurs and technical experts in various fields in both the services and the real sector.

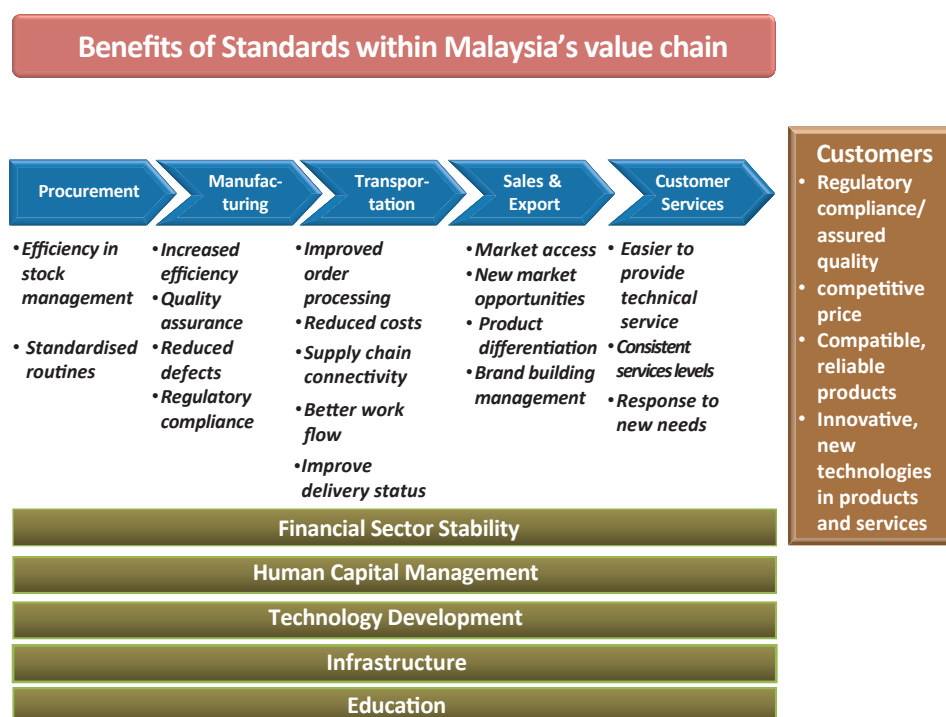
## **2.6 ADOPTING INTERNATIONAL STANDARDS AND BEST PRACTICES**

Malaysia currently has no systematic approach to ensure that businesses adopt international standards and best practices. This limits the ability of local producers and service providers to penetrate overseas markets, particularly jurisdictions with strict non-tariff import barriers such as the European Union.

Through a standard-setting body, the Government should mandate compliance with existing international product and service standards, and incentivise compliance with best practices. Malaysia's compliance should be assessed by credible external assessors, where possible, such as the World Bank and IMF. Furthermore, the Government should support efforts to establish Malaysia as a standard-setter in niche areas such as Islamic finance and halal products. Compliance with standards also could be used to substitute tariffs for the purpose of import control, which would be consistent with the move towards market liberalisation.



Figure 2.6 – Standards and the Integrated Supply Chain



Malaysia will always remain an open economy. Changes in the global economy dictate that Malaysia's export orientation must adjust to global demand, penetrate new regional markets and change strategies to earn more in traditional markets. To prosper in an integrated global market, Malaysia must comply with international standards (**Figure 2.6**). Sustainable growth tenets impose further demands on compliance. Concerns on food safety, labour rights, best practices in environmental protection and climate change management will also add to new international protocols that could impose barriers to Malaysian exports to global markets.

Foreign investors demand goods and services that meet international standards. They prefer to invest in countries that observe international best practices in governance, treatment of labour and the application of the rule of law. The Malaysian private sector also demands ease of doing business that is internationally benchmarked. It also seeks lower cost of capital through access to finance that is less collateral based, but tied to the quality of the business enterprise and the projected cash flows.

Investors ask for the best infrastructure in communications to access the new media to reach global markets. They demand efficiency in government service delivery and clean government. They favour market-based pricing structures of inputs and financial products, and rules that enable hedging against volatility. They expect incentives which are direct, transparent and not market distorting. They also desire living conditions in Malaysia which will meet the family demands of good education and lifestyles for their children. Benchmarking against international standards in sustaining the environment and the quality of life will make Malaysia a choice place to live.

The measures proposed cover two fronts: 1) complying with a set of international standards to facilitate connection to the global supply chain; 2) Malaysia as the originator of global standards on products such as halal foods and sustainable palm oil.



### **2.6.1 Policy Measure: Follow International Standards – Governance and Management**

- i. Malaysia should adopt all relevant international standards and, for each standard, target an improvement in ranking over a specified period to reach the top 10 places of choice for doing business.
- ii. In the finance sector, Malaysia has made a commitment to undertake the Financial Sector Assessment Programme (FSAP). It is recommended that Malaysia undertakes assessment of compliance in all the 12 standards under the FSAP. This covers the range of standards on the fiscal, monetary, corporate governance, accounting, payment systems, access to credit, creditor rights and insolvency and capital market standards. Two particularly important standards are for fiscal transparency and insolvency creditor rights (ICR). In addition, Malaysia should also adopt the credit reporting principles which together with the ICR will provide the basis for the legal and institutional framework to enable a move away from collateral-based lending practices.
- iii. Malaysia should make it a priority to adopt the Code of Good Practices on Fiscal Transparency to identify gaps in sound fiscal management and take corrective actions covering clarity of roles and responsibilities, open budget process, public availability of information and assurances of integrity.
- iv. Adopt the Guidelines on Corporate Governance of State-Owned Enterprises as discussed above.

### **2.6.2 Policy Measure: Follow International Standards - Sustainability**

Whilst there are various dimensions on sustainability, application of standards affecting the economic, environmental and social dimensions are crucial to build an economic environment necessary for the country to achieve sustainable growth. To sustain growth we need to preserve our natural resources and safeguard the interest of future generations that must be facilitated by applying appropriate pricing, regulatory and strategic policies to prudently and efficiently manage non-renewable resources. Hence Malaysia needs to outline all measures and targets consistent with the UN conventions to protect the environment and address climate change issues such as emission reductions, incentivising the deployment of low-carbon energy technologies to reduce carbon emission by 40% and enforce clean air and water standards.

### **2.6.3 Policy Measure: Adopt Quality Standards for Goods and Services**

Availability of goods and services in Malaysia which are of the same quality and standards in advanced countries will make Malaysia a choice for investments as foreign investors will be assured of quality they are familiar with. It will also lower production and delivery costs as standardisation facilitates economies of scale. Relevant ministries must require enterprises to apply international standards regardless of whether the goods and services are for export or domestic consumption.

- i. Adopt international standards on labour legislation and management. This is necessary to equalise labour-related cost of business in Malaysia and other production centres, and to be able to attract skilled labour from abroad.
- ii. The quality of labour is a function of education and on-the-job skills development. More rigorous application of the Malaysian Qualification Agency (MQA) standards on education facilities and course curriculum in Malaysian learning institutions is required.

- iii. In broadband, Malaysia should be focussing on the basic protocols, interfaces and interoperability standards between devices. As we increasingly see the convergence of communications, computing and content in devices, we need standards to enable this.
- iv. Malaysia needs to adopt standards which impact the level of service in the hospitality industry, particularly in the tourism sector e.g. the Pacific Asia Travel Association (PATA) Code for environmentally responsible tourism, environmental impact assessments, green hotel standards, food and beverage standards, public restroom standards, or home-stay standards.
- v. In the agro-based food production area, the emergence of food security concerns as well as environmental standards necessitate that Malaysia adopts international standards of agro-food production and processing. Partner with EU, US and Japan to develop mutually acceptable audits of food production facilities and processes and develop a list of qualified producers, based on internationally benchmarked standards.

#### **2.6.4 Policy Measure: Convert Existing Malaysian Standards into International Standards**

Being a standard setter is nothing new for Malaysia. The country introduced a national Standard Malaysian Rubber (SMR) scheme in 1965, which has since been adopted by all natural rubber-producing countries. Malaysia could regain its stature in the commodities sector by developing standards for the production of sustainable palm oil. The reserves from the palm oil levy could be used for the research towards this end.

Currently Malaysia is helping to set a global standard for halal certification and should leverage these efforts by converting existing Malaysian standards to be the preferred benchmark for adoption by the global community. Furthermore, Malaysia leads in the development of standards in the delivery of Islamic financial products. Malaysian expertise should become known for speedy, accurate and accountable documentation for the different Islamic products that meet international standards of transactional documentation, so that Malaysia could become the centre for outsourcing of documentation for Islamic financial product transactions from any territory.

#### **2.6.5 Policy Measure: Administer Compliance with Standards**

The blueprint to guide Malaysia in implementation of standards and its compliance was approved by Cabinet in 2004. The main authority tasked with oversight responsibility is Ministry of Science, Technology & Innovation (MOSTI). Given the cross-cutting nature of standards compliance, and the opportunities for Malaysia to become a standard setter in halal products and palm oil, a review of the standard setting and monitoring authority is required.

### **2.7 PROMOTING COMPETITION THROUGH LIBERALISATION AND DEREGULATION**

A reduction of Government involvement in business could stimulate innovation in the private sector if it is accompanied by new strategies to remove barriers to doing business and by creating a more favourable investment climate.

#### **2.7.1 Policy Measure: Liberalisation of Entry, Ownership and Operations**

Malaysia has subscribed to the principle of gradual and progressive liberalisation with the objective of attracting foreign investment while maintaining a balance with protection for domestic players. Liberalisation is not an end unto itself. It can, however, be a powerful tool for attracting investment, both foreign and domestic, in new areas of growth and emerging high

value activities. Recently, foreign investment has experienced an accelerated decline, particularly in sectors with no limitations on ownership. This suggests a need for a better understanding of the barriers to greater investment.

The recommendations on liberalisation policy have been grouped into three areas:

- i. Establish an overall liberalisation policy framework for the Malaysian economy.
- ii. Apply cross-cutting implementation processes on liberalisation measures.
- iii. Target immediate liberalisation in selected sectors, commencing with the 12 NKEA sectors, for the near-term.

There is currently no liberalisation policy framework or coordination mechanism to guide government agency efforts in their respective sectors. Nor is there a system to monitor and evaluate the impact and consequences of previously undertaken liberalisation measures. Information on past liberalisation initiatives is scattered throughout the various agencies. MITI faces significant resistance from these agencies in its attempts to compile liberalisation data and information. Accordingly, the Government should:

- Develop a liberalisation policy framework at the national level, particularly for the manufacturing and non-financial services sectors, to guide all liberalisation initiatives, including objectives, roadmaps, stakeholder management, and implementation issues.
- Set up a mechanism, potentially a multi-agency task force, to monitor and evaluate liberalisation impact, including the development of a central database for liberalisation information

A framework and roadmap for liberalisation is recommended below (**Table 2.5**).

**Table 2.5 – Suggested Liberalisation Policy Framework for Malaysia**

Measures to Directly Benefit Consumers for Inclusiveness	Ensuring Impact & Shaping Market Reactions	Ensuring Consistency	International Dimension
<p>1. <u>Immediate term</u></p> <ul style="list-style-type: none"> <li>Identify at-the-border quantitative measures to be removed or relaxed.</li> <li>Identify within the border measures to be removed or streamlined (e.g. licensing &amp; administrative procedures).</li> <li>Develop safety and environment standards in areas where their absence risks forming a barrier to trade and investment (e.g. automotive parts and components).</li> </ul>	<p>1. <u>Engaging the public</u></p> <ul style="list-style-type: none"> <li>Develop a public information strategy – how to manage press releases and announcements to project clarity, credibility and transparency in the objectives of liberalisation.</li> <li>Develop a direct channel for public and private sector enquiries to project openness and transparency.</li> </ul>	<p>1. <u>Bumiputera policy</u></p> <ul style="list-style-type: none"> <li>To ensure predictability to both investors and the bumiputera community, develop a set of criteria for which exemptions can be granted from the 30% equity and employment requirement.</li> <li>To eliminate the case-by-case approach of exemptions to the bumiputera policy, which does not offer consistency either within or across sectors.</li> </ul>	<p>1. <u>FTAs</u></p> <ul style="list-style-type: none"> <li>To assess if all trading partners should be treated equally in level of market openings. Should there be room to offer preferential treatment to selected partners, for example, ASEAN?</li> <li>To assess the suggestion that foreign companies in Malaysia should also benefit from preferences and concessions gained under FTAs.</li> </ul>

Measures to Directly Benefit Consumers for Inclusiveness	Ensuring Impact & Shaping Market Reactions	Ensuring Consistency	International Dimension
<p>2. <u>Medium to long term</u></p> <ul style="list-style-type: none"> <li>Identify new growth areas to be nurtured by greater foreign entry.</li> <li>Identify steps on prerequisites to be developed (e.g. regulatory framework, supporting supply chains and human capital requirements).</li> <li>Trade-offs to liberalisation to be assessed at the national level and cross-sectorally, not within a particular sector alone.</li> </ul>	<p>2. <u>Predictability &amp; certainty</u></p> <ul style="list-style-type: none"> <li>Where measures cannot be removed immediately to account for adjustment changes and meeting prerequisites, to specify the time horizon for phased-in market opening (should be no more than a maximum of three years).</li> <li>Demonstrate commitment in not backtracking on liberalisation to foreign investors and traders, by assessing to independently bind phased-in measures at the WTO.</li> </ul>	<p>2. <u>Parallel sectors</u></p> <ul style="list-style-type: none"> <li>Liberalisation measures assessed in a particular sector should take into account progress and milestones to be met in development of other closely related sectors (e.g. automotives and public transport system).</li> </ul>	<p>2. <u>Competing with others</u></p> <ul style="list-style-type: none"> <li>Liberalisation and facilitative measures taken need to be assessed in terms of staying competitive against other countries, particularly those around the region, such as, Singapore and Thailand.</li> <li>It is not about being better than before but better than what other competing countries are doing.</li> </ul>

**Note: This template highlights a non-exhaustive checklist of steps to be taken by the relevant ministries/agencies to ensure rigour in analysis to facilitate well-informed decisions. This process will involve qualitative and/or quantitative studies on the rationale behind the measures taken for a sector identified for liberalisation, including any impact analysis and risk management of unexpected adverse consequences, where relevant.**

The following steps for implementing cross-cutting liberalisation are needed:

- Ensure impact and shape market reactions by announcing the measures. Announcements should focus on the advantages of the measures and be clear on their objectives, direction, and range of actions.
- Issue guidelines on implementation of the liberalisation measures within 2 months of the announced changes.
- Undertake an evaluation of the liberalisation results after 6 months and define follow-up measures to be taken if objectives are not met.

In the near term, some quick liberalisation measures include:

- Allow a limited number of foreign legal firms to operate in Malaysia. This will create private sector confidence, raise standards and help retain talent.
- Phased-in liberalisation must be limited to a maximum of three years instead of 5-10 years.

- Develop a negative list approach to undertaking liberalisation. A thorough study of how best to implement the negative list approach should be undertaken.
- Undertake unilateral liberalisation bound under WTO, or regional or bilateral FTAs to give assurance of no roll-backs.
- Review recent liberalisation to see if actions are needed to liberalise operations, e.g. application of national treatment limits.
- Expand benefits from bilateral and regional FTAs to foreign-owned companies. Establish Malaysia as hub for various industries, e.g. Islamic goods and services.

### **2.7.2 Policy Measure: Reform the Regulatory Framework**

The existing regulatory framework is outdated and does not facilitate modern business. Malaysia has many onerous (and sometimes overlapping) regulatory and licensing requirements at various levels of Government, which increases compliance costs and deters private sector innovation and investment.

One of the characteristics of an advanced economy is that the Government undertakes to ensure that regulation for the pursuit of its social agenda does not impede private sector competitiveness and innovation. For this, the Government needs to lay out a comprehensive regulatory reform agenda aimed at building a seamless national economy and unleashing productivity. This should be pursued through a continuous programme that ensures policy consistency and maintains regulatory certainty and clarity. Regulatory environments which encourage competition have a positive impact on productivity. Regulations that are product- or institution-specific become highly distortive and prevent competition and innovation. Such regulations also quickly become irrelevant, creating bottlenecks in regulatory oversight.

A clear reflection of the decline in quality of the country's regulatory framework is Malaysia's recent 67th percentile ranking in the World Bank's Governance Indicators (WGI), which measures regulatory quality by the soundness of policies and regulations that promote private sector development. All benchmark countries rank higher than Malaysia on this count, with Hong Kong and Singapore leading at the 99th percentile. The Malaysian regulatory framework must be aligned with changes in global regulatory tools, processes and approaches, including new best practices and standards. Otherwise labour and capital will move out of stiflingly regulated jurisdictions to economies with more modern and market-friendly regimes.

Malaysia must urgently reform its regulatory framework to make it proportionate and up-to-date with global developments and to reduce business costs and complexity, while enhancing the country's productivity and international competitiveness. At the same time, a culture of continuous regulatory improvements needs to be embedded more strongly in government practices. Ministers and their departments must be made more accountable for the quality of regulation under their portfolios. The following measures are needed:

- **Adopt Principles of Good Regulation.** There are a number of principles to guide the Government in developing sound laws and regulations while assuring that social objectives are also effectively achieved in a manner that minimises the economic opportunity costs. These principles include transparency, due process in administration of laws and regulations, proportionality, predictability, non-discrimination, objective- and performance-based criteria, market-based mechanisms, and accountability.

Best practice for an effective regulatory process requires all new regulations to go through a mandatory Regulatory Impact Analysis (RIA), which assesses the impact and expected outcome of new rules and regulations before they are promulgated. The RIA findings must be distributed together with the draft regulation when it is tabled for discussion and enactment. The RIA should be a public document open to scrutiny by politicians, watchdog groups, industry associations, and members of the public. Once a regulation comes into force, it must be accompanied by clear guidelines within 2 months.

As part of the process of introducing new regulations, public consultation should be made mandatory. The form this consultation may take, however, will vary depending on the weight of the regulation in question. To ensure regulations remain effective and relevant over time, a periodic review mechanism should be instituted. This includes incorporating sunset clauses or automatic five-year review mechanisms in all new and existing regulations. A comprehensive database of all primary and subordinate regulations should be captured through a registry of regulations, maintained by a central body. Such a registry would enable businesses to easily identify all applicable requirements and would provide the means to track and reduce overlap or contradictions in regulation. Ideally, the registry should raise alerts several months in advance about laws and subordinate regulations that are coming into force, or due to be reviewed, modified, or repealed.

- **Remove Unnecessary Regulatory Burden.** The accumulated regulatory burden in Malaysia, measured in terms of rules and procedures, weighs heavily on businesses. The Malaysia Administrative Modernisation and Management Planning Unit (MAMPU) has identified a total of 896 agencies at the federal and state levels that administer over 3,000 regulatory procedures. The time needed for getting regulatory approvals in nearly 50% of procedures is about 14 days each.

To address this, an effective approach, often referred to as the ‘Dutch approach’, is to commit to a planned reduction of regulatory burden over a period of time, e.g. a reduction of 50% of outstanding regulations over four years. To ensure success, a synchronised approach to the measurement of regulatory burden must first be developed before establishing the organisational structure needed to oversee the reduction process. The ‘Mexican approach’ to streamlining and simplifying licensing could also be incorporated as part of this process. This requires compiling a complete inventory of existing business formalities — rules and forms, licenses, permits and other authorisations required to start and operate a business. At the same time, the Government should also more effectively utilise ICT to streamline business reporting requirements and reduce compliance costs. Common standardised business processes to improve access to information, messages and services on government websites could be developed.

As an immediate step in removing unnecessary regulatory burden, the Government should prioritise the review of selected laws and regulations. High-priority ones include the labour laws; the Industrial Co-ordination Act; Promotion of Investments Act; Uniform Building By-laws; Street, Drainage and Building Act; National Land Code; Personal Data Protection Act; as well as laws governing intellectual property rights and winding up proceedings.

In addition, sector-specific laws, particularly those affecting the manufacturing and oil and gas industries also need to be reviewed. For the manufacturing sector, restrictions on equity conditions which apply to manufacturing companies established before 2003 should



be removed to synchronise with companies established after 2003, which are no longer subject to equity conditions in their manufacturing licences. For the oil and gas sector, the bidding process for the award of contracts needs to be re-structured to encourage greater participation by SMEs.

- **Ensure an Effective and Efficient Enforcement Mechanism.** Ineffective enforcement has resulted in a lack of compliance with regulations and must be corrected to match the proposed reduction in regulatory burden. To address this, each regulatory body must undertake and make public the findings of an annual independent audit on the adherence to their client charter. Regulators should also undergo continuous training to learn new approaches and to upgrade/update their skills and enforcement effectiveness. An independent research and advocacy body could also provide further counter-checks through feedback from an autonomous assessment of the efficacy of the regulatory framework.
- **Strengthen Institutional Support.** The most important factor in ensuring a successful transition towards a more effective and coherent regulatory framework is the role of a central implementing agency charged with managing the critical changes to the existing regulatory approaches.

As envisaged in the 10MP, the NEAC supports the assignment to the Malaysia Productivity Corporation (MPC) the task of designing the regulatory burden reduction plan and of continuously following up on the effective implementation of the regulatory reform initiatives. To carry out this task earnestly, MPC must realign its priorities and be given the human and financial resources to carry out this mission.

### **2.7.3 Policy Measure: Swift and Resolute Implementation of the Competition Law**

The recently-passed Malaysian *Competition Act 2010* is acknowledged to be on par with comparable laws in other jurisdictions. However, the Competition Commission is currently answerable to the Minister of Domestic Trade, Cooperatives and Consumerism, which could compromise its independence as the Ministry is mandated to promote certain sectors while the Commission is expected to be impartial. Effective implementation of the Act could be scuttled if the Competition Commission is seen to be biased, which tarnishes credibility in the eyes of prospective investors.

The primary challenge in implementing the Competition Act lies in striking the right balance between achieving the country's social objectives and allowing healthy competition to flourish in the domestic market. This requires addressing subsidy and social protection policies as well as GLC operations, as they have an impact on competition.

The Government will signal its strong commitment to competition by appointing a credible and independent Chair to the Competition Commission, ideally a senior private sector representative with extensive operating experience in competitive and liberal overseas markets. In accordance with the Competition Act, the Government may give general directions related to the functions and powers of the Commission, but should not interfere in any decisions made by the Commission.

The composition of Commission members should represent not only the interests of the Government, but those of the private sector and consumers. Members will be given specialist training in competition and economic issues to build investor confidence in the efficacy of implementation of this Act.

The Commission should engage in competition advocacy to develop a competition culture among the business community, consumers and other regulators. In order for Malaysia to develop a competitive culture, businesses need to fully understand the aims of the competition law and how it can effectively promote genuine and healthy competition.

The Commission should work with other regulators to review and streamline existing policies, regulations and practices to ensure consistency with the objectives of the Competition Act. Cross-sectoral and cross-border applications of the Competition Act must be addressed. For example, selective import substitution policies and wealth redistribution policies which conflict with the competition policy should be reassessed with a view to removing or addressing market distortions. Entry-exit conditions, in particular the licensing conditions imposed by sector regulators, will also need to be streamlined to ensure that they do not prohibit entry of new market players. Gaps or overlaps in regulatory jurisdiction between the Competition Commission and other sector regulators will need to be reconciled. It must be clear which regulator will take the lead in unavoidable cases of regulatory jurisdiction overlap so that businesses do not have to deal with multiple regulators.

The Commission should limit granted exemptions in order not to compromise the effectiveness of the Competition Act. Any individual or block exemptions granted to industries or firms should be openly decided and regularly scrutinised with the expectation that they will eventually be terminated.

## **2.8 INTRODUCING INNOVATION IN FINANCING**

It is expected that the NEM-oriented financial sector reforms to be undertaken during the next decade will be covered by both the Securities Commission's Capital Market Master Plan 2 (CMP2) and the Bank Negara Malaysia's Financial Sector Master Plan 2 (FSMP2). The NKEA labs have also identified specific measures focussing on finance as a growth sector. As such, this report will focus only on selected growth-enabling finance issues, in particular on access to capital, which is both cross-cutting and critical to growth potential and private sector efficiency.

### ***2.8.1 Policy Measure: Supporting SMEs & Innovation and Efficiency in Allocation of Capital***

The Malaysian financial sector infrastructure is relatively well developed. However, significant legislative framework gaps, lack of credit information system transparency, complex fund structures, and a crowded SME and venture capital financing agency environment all converge to create bottlenecks in the funding supply chain. These shortcomings can be overcome to remove distortions in private sector allocation of capital and to improve the efficiency of financial institutions. Access to finance should be more transparent and be based on merit.

Recommended measures are:

- Within the legal, regulatory and institutional framework build expertise, confidence and best practices which will help financial institutions to develop the capacity to promote non-collateral-based lending.
- Develop mechanisms to support SME financing by banks, non-banks and the capital market.
- Enhance access to risk capital, including venture capital.



Collateral-based lending continues to be the backbone of lending practices in Malaysian financial institutions. A legal and regulatory framework is needed to give banks effective recourse in dealing with borrowers, a responsive platform for borrowers to proactively deal with financial difficulties, and facilitate bank involvement in restructuring of loans going bad.

Several pieces of legislation need to be amended to enable access to credit based on merit, monitor transaction risk, promote an environment favouring restructuring rather than premature close-out, and expedite foreclosure and other exit processes while allowing rehabilitation of companies and sole proprietorships. A support system for banks is needed to promote non-collateralised lending. This can be done by building SME capacity for loan applications based on cash projections. Good practices among credit information system providers must be fostered. Standardisation, user friendly reporting formats for SMEs, consistent with credit monitoring requirements, must be developed.

Financial institutions also lack capacity to make credit decisions through project evaluation and transactions risk monitoring, especially for projects with high technical content and social returns, such as “green technology” investments and venture capital-funded ICT projects. A centralised Commercial Credit Registry (CCR) to collect and share information on customers must be created to allow transparent borrower credit ratings based on comprehensive, accurate and timely data. The CCR should be benchmarked to international standards developed by the World Bank. We must also build capacity among financial institutions to assess and monitor high tech and other technology-intensive projects.

A key national policy objective should be to adopt international standards in all legal, regulatory and institutional practices across the finance sector. Assessments under the Financial Sector Assessment Programme (FSAP) would serve to gauge compliance with the relevant standards and identify gaps so that corrective measures can be taken. This will foster commercial confidence and predictability.

The majority of enterprises in many Asian countries, including Malaysia, are SMEs. Their productivity and earnings, as well as the wages they pay, matter crucially for general living standards. Steps to spur their adoption of productivity-enhancing technologies and diversification into modern production processes are critical to providing well-paid employment and enhancing the dynamism of the private sector in Malaysia. SMEs constituted 99.2% of total establishments in Malaysia in 2008, provided employment for about 60% of the total workforce, and accounted for approximately one third of GDP.

The key issue surrounding Malaysian SMEs is that they are unable to access the financing required to achieve greater scale and profitability. As such, they are not ready for integration into the global supply chain. SMEs are operating in an “un-fostering” system with low reproducible investment and economic returns. As part of the funding options, the NEAC’s proposal for a Transformation Fund could be implemented which should be much larger in scope and funding than the Facilitation Fund established in the 10MP.

- **Establish an “SME Angel Financing or Venture Capital Exchange”.** An entrepreneurs’ “Bulletin Board” for SMEs requiring venture capital or angel financing, should be set up by the SME Corp in collaboration with Bursa Malaysia, and with the consent of the SMEs. This will provide a streamlined and integrated ‘marketplace’ where potential investors can make enquiries as to which SMEs are worthy of investment.

A holistic framework is needed to support SMEs to manage loan repayment. This may take the form of technical assistance programmes which ensure that loans will not become non-performing, while building SME technical and business capacity.

- **Establish an institutional framework to undertake the rating of SMEs.** This will require rules for data collection and sharing so as to allow sound analysis for SME ratings for securitisation of SME loans and receivables. The currently dispersed facilities (credit scoring at SME Corp, Credit Reporting System at CGC) need to be rationalised and transformed into a dedicated SME Credit Reporting System that meets international standards. Loan application processing time needs to be reduced and the tracking of SME rankings must be strengthened to ensure good behaviour and facilitate prompt action to arrest emerging loan defaults.

The banking sector supervisory framework must be reviewed and changes implemented that will enable leveraging the unique ability of non-banks to play a greater role in improving access to finance for SMEs (**Box 2.1**).

- **Enhance Access to Capital for SME Development.** Despite significant government support for venture capital (VC), the industry remains nascent in its growth and public complaints about access to risk capital have not been addressed effectively. Access to finance for risk capital, including for venture capital, needs to be further analysed and expanded. A rationalisation of policies and funding access to improve the effectiveness of VC funding is needed. There do not appear to be funding constraints in the VC sector, but there are issues of effectiveness in the utilisation of the funds. The issues involve poor administration arising from too many agencies and councils with duplicate functions as well as weak governance and accountability practices.

Central to the issue is the need to create demand for VC finance, rather than relying on supply-driven finance, thereby avoiding the limited sources chasing the same deals and proposals. GLCs should be directed to explore the viability of setting up corporate VC units. Investments therein should be encouraged through tax incentives. Outreach initiatives to introduce potential Malaysian entrepreneurs to foreign VCs should be subsidised with offers to co-invest directly in these entrepreneurs. Public VC remuneration policies should be benchmarked to international standards to align incentives of personnel and attract talent.

Initial funding for professional non-profit angel networks should be created and provided, while corresponding angel investments should be incentivised via a matching funds programme. Angel networks are a superior channel for early stage risk capital as it pools capital, expertise and networks of informal investors. Most crucially, angel investors typically fund and support companies that are not yet mature enough to successfully obtain VC funding.

### **Box 2.1 – Measures to improve access to financing by SMEs**

Specific measures to create opportunities for greater access by SMEs to non-bank financing sources will focus on:

- (a) Development of “preferred” well-run credit companies to enhance their role as niche lenders to SMEs. This will include regulatory oversight to ensure confidence among banks and bond investors to channel credit to these companies for on-lending to SMEs.
- (b) Review of the current capital market framework and the role of Danajamin with a view to promoting greater use of the capital market (bonds and commercial papers) to raise funding.
- (c) Develop the CRS market with SME ratings as the basis for enabling securitisation of SME loans extended by credit companies.
- (d) Include credit companies in disbursements of special government funds created to support SME lending (currently disbursements is through banks only)
- (e) Review the Moneylenders Act to facilitate the growth of term loan financing by credit companies. Provisions in the Act requiring credit companies to use prescribed standardised security documentation restrict their ability to grant normal business loans. Requests for variations to the standardised documentation involve a lengthy process of negotiation with the relevant authority. Another constraint is that each branch of the credit companies is required to apply for an individual moneylender license before it can carry out term loan business. And different jurisdictions/local authorities processing such licenses do not apply consistent policies and procedures in the processing, vetting and issuing of licenses.
- (f) Build partnerships with larger companies to expand current banking products which attach SME lending risks to the larger firms which source products from SMEs.

## **2.9 ENHANCING CONNECTIVITY OF BUSINESSES AND BUILDING SMEs**

In the last decade, ICT has advanced to the stage where increasingly more business is done through the Internet than through conventional channels such as newsprint, television and post. The free flow and availability of information lowers the barriers to economic activity and stimulates growth and productivity in even the rural and under-developed areas. Broadband is no longer a luxury, but a vital utility.

The NEAC is convinced that expediting the implementation of Broadband is a national priority, not only to put Malaysia back on track to robust growth, but also as an important tool for the eight SRIs including the creation of new growth and income for the SMEs and the rural areas.

### **2.9.1 Policy Measure: Accelerate the Rollout of Broadband**

Broadband is key in the provision of innovative services nationally, globally and a critical platform for SMEs. A World Bank study suggested that if a country were to increase its broadband penetration by 10%, it could support more than a 1% increase in GDP growth. Broadband is more supportive of growth than older technologies such as Fixed Line, due to the higher speed and bandwidth that facilitates video-conferencing, content creation, and value propositions.

The recommended broadband expansion policies can leverage Malaysia's advanced infrastructure by:

- Attracting large data and processing centres (such as Google, Yahoo, etc.) to one of the five focus areas with good High Speed Broadband (HSBB), e.g. in Iskandar in order to generate content and spin-off services.
- Using the Universal Service Provision Fund (USP) to speed up the implementation of HSBB in Zone 1 as a matter of priority to generate revenue and growth by the incumbent telecommunication companies (Telcos).
- Focussing on content development. The NKEA Lab has suggested using eGovernment, eLearning and eHealth, as drivers for content provision, software, and process skills that could be adopted or replicated for other emerging markets. The NEAC suggests that there should be a concerted public-private initiative to focus on content development in the media and cultural areas that could assist the SME and tourism sectors.

There are several ways to incentivise the Telcos to accelerate rollout, reduce wastage, curtail red-tape procedures, and improve transparency and governance:

- Reduce the USP Fund contribution rate from 6% of revenues to 3% -4% to increase profitability and capacity to invest in wider rollout.
- Ensure projects are 'high-impact', by emphasising rollout to community congregation points such as schools, hospitals/clinics ("middle-mile" strategy). Such congregation points increase the 'bang-for-the-buck' and can reduce last-mile rollout costs. Ensure "future-proof" technology is utilised in such a middle-mile rollout (typically fibre-based technologies).
- Allow a 'claw-back' process against pre-agreed investments in USP areas.

Several legal and regulatory barriers cause delays and loss of opportunity in HSBB roll-out:

- National Land Code – impose inflexible restrictions on Right of Way.
- Law of Tort – overly rigid requirements on reimbursement if utility needs to be migrated due to road re-routing and claim of damage during work process done by Malaysian Public Works Department (JKR).
- State Laws – insufficient appreciation by Local Authorities who need to see broadband as a form of utility and reduce the hurdles to speed up the roll-outs.
- Street, Drainage and Building Act – may need to be revised to accommodate the rollout of network infrastructure.

In certain states, Telco companies cannot build their own towers because the state government's company has exclusive rights, causing delays and losses. In addition, Telcos have to apply for approvals from multiple agencies, resulting in a very time-consuming process.

## 2.10 PRESERVING THE ENVIRONMENT

Common problems faced by developing and developed nations alike are the lack of sustainability practices to assure that resources are consumed in the most economic manner. There is a growing global focus on sustainability resulting from climate change, environmental impact, and

the growing acceptance that our natural resources are limited. NEAC believes that within its proposed policy framework, the following actions are needed:

- i. Internalising externalities
- ii. Promoting energy efficiency and green growth
- iii. Favouring sustainable agriculture
- iv. Striving for energy resource sustainability

#### ***2.10.1 Policy Measure: Internalise Externalities***

A cornerstone of sustainability is ensuring that private sector investments and economic activities fully reflect the direct and indirect costs of their operations. Business activities which fully reflect the direct and indirect economic, social, and environmental cost of production are inherently more efficient and sustainable. This requires both the right mix of incentives and sanctions, the adoption of 'polluter-pay' principles, and more transparency on the real costs and benefits of various types of economic production. In this regard, the NEAC supports fully the removal of subsidies and a realignment of the pricing of energy to global levels as a matter of priority to facilitate the movement to a green economy.

In the Malaysian context, clear policy directions on rationalising subsidies and removing price controls will provide investors with greater certainty about future energy costs as a factor of investment decisions. In addition, market pricing of energy products may also in the long run encourage the adoption of renewable and green technology.

#### ***2.10.2 Policy Measure: Promote Green Growth and Energy Efficiency***

The issue of green growth is naturally a key element in any vision of sustainability in the context of resource constraints and threats from climate change. Emphasis must be placed on efficient energy usage and reducing wastage of resources to sustain a high quality of life. Fundamental rather than incremental changes are needed. Sustainable growth requires a mix of complementary and reinforcing strategies and policy innovations, partnerships, and qualitative and quantitative shifts in investment.

As the energy sector is the backbone of an economy striving for high productivity and high income, it is imperative that the new National Energy Policy prepared by EPU to address Malaysia's energy issues be implemented swiftly. These include sufficient supply of safe and economical energy, the use of efficient energy, and environmental protection in the process of consuming and producing energy.

Currently in Malaysia, there are no laws governing the efficient use of energy as in nations like Japan and India. Energy efficiency standards must be adopted which, together with the greater use of alternative renewable green energy sources, would represent big steps towards preserving the environment.

#### ***2.10.3 Policy Measure: Favour Sustainable Agriculture***

Global awareness of the effects of farming on the environment have led to a shift in the way developed countries purchase their agriculture products, moving from non-sustainable to sustainable organic farming methods. Sustainable agriculture not only covers the ecological side but it also covers social sustainability such as fair wages and working conditions, avoidance of child labour, and good working practices. Malaysia needs to respond to this growing demand for agri-food products which are produced in sustainable ways as verified by NGOs like the Rainforest Alliance and Fairtrade. There is a growing global demand for certified, sustainably-

produced commodities such as cocoa, coffee, tea, sugar, rice, and herbal medicine. Malaysia should set the standards on sustainable agri-food production and distribution, such as developing halal and organic food standards, including leading the Roundtable on Sustainable Palm Oil products. These are innovative high income opportunities that are ideal for the development of SMEs in rural areas, especially in Sabah and Sarawak.

#### **2.10.4 Policy Measure: Strive for Energy Resource Sustainability**

Malaysia is highly dependent on the diminishing supply of petroleum and natural gas, introducing a vulnerability to price volatility. The introduction of new and renewable resources (solar, biomass fuel cell, hydrogen technology, etc.) is critical for Malaysia. However, expanding into the use of such technology will be slow because of the high costs involved. Given the substantial hydroelectric resources in Sarawak, the NEAC recommends establishing a transparent priority-based ranking system for research and development and use of green energy technology so that the private sector can plan and invest in these areas, including downstream projects related to non-fossil based energies.

### **2.11 ENHANCING SOURCES OF GROWTH - CASE STUDIES ON REMOVING BARRIERS IN SELECTED SECTORS**

Whilst the NKEAs are addressing actions to stimulate growth sectors in detail, this report has also examined possible policies to remove barriers in the E&E and palm oil sectors to catalyse growth. Consideration of these policies are presented in Appendices A and B.



**CHAPTER**

**3**

# **ENHANCING INNOVATION**





### 3 ENHANCING INNOVATION

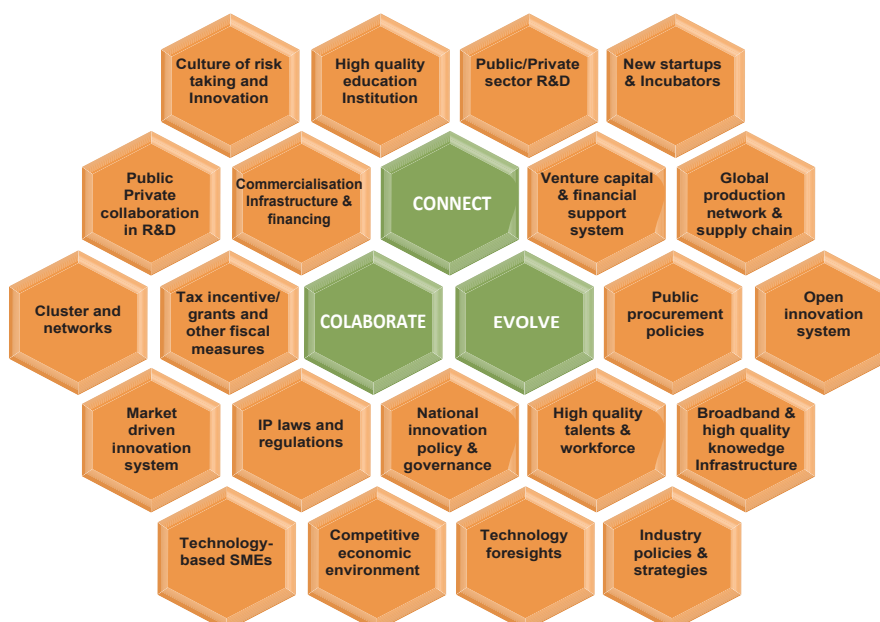
#### 3.1 A BETTER TOMORROW THROUGH INNOVATION

The economic growth required for Malaysia's transition to a high income nation will require the development and application of new technology, supplemented by purposeful efforts to conceive and acquire innovative products and processes, while designing and adopting more effective management methods. Moving up the value chain demands this process of change, innovation and productivity growth. SRI6 of the NEM highlights the importance of the recognition by public and private decision makers of the need for investment in innovation as a driver of growth and competitiveness.

Malaysia can no longer rely on MNCs alone to drive innovation and facilitate its integration into the regional and global network of production processes and markets. As discussed above, that integration depends on strengthening Malaysia's ecosystem for entrepreneurship and enhancing its environment for innovation.

Entrepreneurship and innovation will not emerge spontaneously, although they are more likely to materialise in an unfettered competitive market. While innovation can generate significant reward, it also comes with inherent risk. Failures should not be punished to the point that entrepreneurship is stifled. Similarly, a wide range of funding mechanisms should be made available. The Government, in collaboration with all stakeholders, has a major role to play in generating this sustaining environment and ecosystem (**Figure 3.1**). A strong government commitment to implement change and a willingness to take bold actions, including undertaking tough structural reforms, are key pre-conditions for industrial upgrading and innovation.

**Figure 3.1 – The Innovation Eco-system**



### 3.2 THE SETTING FOR INNOVATION

Since attaining middle-income status in the 1990s, Malaysia's economic structure has changed little with a strong focus on exports from the electronic sector, which employs primarily low-to medium-technology systems resulting in a low demand for innovation. While the policies embedded in several initiatives (e.g. Industrial Master Plans, 8MP and 9MP) are evidence of the recognition of the need for industrial change and transformation, progress has been limited in contrast to the substantial financial resources expended.

Moreover, these wide ranging initiatives have mainly been directed to enhance the supply side of the national innovation system, i.e. through fiscal support, financial incentives, institutional development, and infrastructure development that has created technology parks, incubators and several specialised technology centres. These efforts have not resulted in the desired impact in building national innovation capability. A re-think of the innovation efforts and a better approach is needed.

### 3.3 ISSUES IN INNOVATION AND TECHNOLOGICAL CHANGE

One of the key enablers for movement up the value chain is R&D expenditure, both public and private. R&D expenditure leads to knowledge creation and innovation. But the overall level of R&D in Malaysia is still low compared to several reference countries in the region. Accordingly, Malaysia's patent registrations are also low compared to those same countries.

While R&D expenditure is commonly used as a measure of a country's international competitiveness, a series of conditions must prevail at various stages for that expenditure to yield the desired results. At the project level, even with adequate financial and institutional support, the research must be sufficiently meaningful to yield further research capacity, push the frontier of knowledge, and generate commercialisation potential. At the intermediate level, the right combination and critical mass of entrepreneurial drive, capital, and incentives must be present to advance the development of the products and processes along the commercialisation path. Ultimately, the innovative product or process should generate high value added activity and contribute measurably to raising efficiency, Total Factor Productivity (TFP) and growth.

Another very important prerequisite is the availability of an educated and trained workforce, supplemented by a seamless capability to tap into the global pool of knowledge and talent. As has been discussed previously, Malaysia has experienced a steady decline in the output of science and engineering students as a percentage of total graduation of first degree and post-graduate scholars. Policies to address these shortcomings are included in the GTP and 10MP.

### 3.4 THE BARRIERS

- **Preference for Imported Technology.** There is a preference in Malaysia for imported technologies over those developed domestically, both by individual firms and entire sectors. MNCs located in Free Trade Zones do not invest significantly in research and innovation, preferring to undertake small incremental technical production-related operational changes to improve efficiency and productivity. There is limited technology diffusion and transfers through intra-industry trade and FDI flows.

- **Low Innovation Capacity among SMEs.** While there are examples of MNCs working with SMEs to help them innovate, most Malaysian SMEs still have low innovation capability as a result of the MNC eco-system which has focussed on a strong sub-contracting network for Original Equipment Manufacturing (OEM) suppliers. Thus they do not have the size and scale to expand their operations and compete in the regional and global space. This in turn inhibits their capacity to introduce and manage innovative activities.
- **Government and GLC Procurement Practices.** These weaknesses are compounded by government and GLC procurement practices that do not lend support to SMEs or budding-entrepreneur-researchers with innovative products/processes to offer.
- **Absence of an Innovation Culture and Community.** In Malaysia, insufficient attention is paid to recognizing and celebrating innovation and the efforts of individuals or firms that come up with innovative products and processes in an orchestrated commemorative manner. A culture of innovation involves a society that creates incentives, monetary as well as social rewards that value creativity and diversity of ideas. The culture is created through recognition that innovation is also a process with a supply chain that requires collaboration between many parties. In Malaysia, the relationship among industry, academia, and researchers is weak to non-existent. There is insufficient knowledge flow and collaboration on innovation projects. There is low demand for R&D personnel in industry and low mobility between industry, the public sector and academia. There is also an outflow of R&D talent to neighbouring countries due to unattractive compensation packages, poor job prospects, and insufficient opportunity to build a professional reputation.

### 3.5 OVERCOMING THE BARRIERS

The knowledge-based economy of the future differs from the capital-based economy of the past. Knowledge will become the core element of competitiveness and the driving force for long-term growth. The rules of the game in the knowledge-based economy are speed, flexibility and innovation. The Government's role is to foster innovation through sound governance arrangements developed with greater involvement of stakeholders in defining policy orientation and priorities. As described above, the private sector must be allowed to take the lead. Policies related to industry structure, upgrading and expansion, as well as product or process development and specialisation, need to be market-driven. The market will dictate the pace of technological innovation on the basis of sustainable demand trends, whether in traditional or new areas of growth. The market will decide whether to utilise domestically-sourced or internationally-acquired innovative products or processes. This is of course dependent on the adequacy of the physical and ICT infrastructure that facilitates the location and development of knowledge and innovation investment platforms, and on an adequate skilled workforce.

The Government must interact with the industry to develop a shared understanding of global demand trends and opportunities, the associated technological needs, the funding requirements, and the market risks. The Government does not always know best.

Many of the innovation- and knowledge-related policy measures contemplated under SRI6 in the NEM have since been included in the 10MP (Chapter 3, pages 80-88) and will be further elaborated in the NKEAs. This report, therefore, will focus on only a few selected policy measures (**Table 3.1**).

**Table 3.1 – Summary of Policy Measures for Enhancing Innovation**

<b>Policies to Drive Innovation</b>
<ul style="list-style-type: none"> <li>• Develop government and GLC procurement policies that support local innovative products and services</li> <li>• Establish institutes of higher learning as centres of excellence for R&amp;D collaboration with the private sector</li> <li>• Consolidate and merge of national enterprises to create scale</li> <li>• Encourage open innovation ecosystem – Foster knowledge sharing between firms, public, research institutions and universities</li> <li>• Align innovation support policies to extract greater value from intellectual property (IP)</li> </ul>

### ***3.5.1 Policy Measure: Develop Government and GLC Procurement Policies That Support Local Innovative Products and Services***

The 10MP recognises the need to develop a best practice-based public-private procurement policy to support innovation in sectors where Malaysia has a competitive advantage. Accordingly, the NEAC recommends the removal of any bias in government and GLC procurement practices against domestically developed and registered ideas. Domestic entrepreneurs with innovative products and services find it difficult to commercialise their ideas. They lack a track record to support the effectiveness of their inventions and poor access to financing for testing and marketing their products. International experience has shown that enterprising entrepreneurs can more quickly gain traction in interest and sales if the Government provides an initial outlet for their products. A specific policy to grant incentives to GLCs and the private sector to purchase locally patented innovative products and services would also further allow innovators to establish marketing credentials and materially improve their ideas from the feedback of domestic purchasers.

Another related mechanism that should be implemented is Forward Commitment Procurement (FCP) which has been shown to be quite effective in stimulating innovation (**Box 3.1**). Forward procurement allows innovative entrepreneurs to better understand the needs of the customers. It also gives assurance to inventors that there is an initial demand for their products which helps to secure the working capital for further product or service development.

#### **Box 3.1 – Forward Procurement**

Developed by the UK Government’s Environmental Innovation Advisory Group (EIAG), FCP was initially used to deliver cost-effective innovative environmental products and services to the public sector and to help to create the market conditions in which such goods and services can thrive.

The mechanism of FCP involves providing the market with advance information of future needs in outcome terms and early engagement with potential suppliers. The government typically signs an agreement to purchase a product or service that currently does not exist, at a specified future date, providing it can be delivered to agreed performance levels and costs.

### **3.5.2 Policy Measure: Foster Better and Closer R&D Links between Institutions of Higher Learning (IHLs) and the Private Sector**

Productive links between IHLs and the private sector would facilitate knowledge flows and catalyse the development of a network for the creation, circulation and diffusion of knowledge. Actions would include:

- Reviewing and changing IHL policies on collaboration with the private sector and supporting national and international collaboration. The 10MP (Chapter 3, page 80-81) includes some initiatives, but this area should be addressed in a holistic and systematic manner with the aim of institutionalising the links to avoid ad hoc and limited efforts. KPIs defined for IHLs should include collaboration efforts in addition to the traditional ones focussed on the number of R&D publications. At the same time, expectation on researchers to do independent work should be reduced in favour of collaboration with others.
- Formalising the use of the National Professors' Council as an official networking hub to enhance collaboration between higher learning institutions, as well as a vehicle for dissemination of private sector collaboration experience.
- Seeking, through improved collaboration, a dynamic balance between public and private financial resources devoted to R&D outlays. The Government should introduce criteria for award of funding that encourages collaboration between IHLs and industry.
- Establishing programmes that encourage mobility of R&D personnel between IHLs and public and private research institutions.
- Updating personnel policies to allow IHL researchers to not only collaborate with industry but also to participate, with agreed safeguards, in business ventures related to commercialising their R&D collaboration.
- Allowing private technology entrepreneurs access to IHL or public R&D centres through reduction or even elimination of bureaucratic obstacles.

### **3.5.3 Policy Measure: Turn Existing HiCoEs (Centres of Excellence Accredited by the Ministry Of Higher Education) into Full Fledged Networks of Excellence**

The Government should ensure that basic and mission-oriented research is supported in areas in which critical mass and excellence can be achieved. It should also use competitive funding more effectively to strengthen public research on well-defined priorities including the realignment to the priorities of the NEM. For this purpose, the Government should:

- Appoint an independent assessment body to implement a periodic (e.g. every two years) rating of HiCoEs and other research centres.
- Use the assessment from the ranking exercise to better understand how R&D resources are utilised, and to better manage the limited funding. Evolving priorities can then be taken into consideration in varying future funding allocation by areas of research and by research centres.

- Obtain from the assessment a clear understanding about areas of research and innovation where Malaysia has a competitive advantage. Since not many countries are capable of excelling in every area, such an understanding will guide the research community and government in funding considerations.
- Ascertain each research centre's relative strengths on the basis of standardised ranking criteria. The Government would then be in a better position to facilitate the specific needs of each HiCoEs and other COEs based on their ranking, including allocation of funding in strategic or priority areas of research.
- Use the results of the exercise for better management of human capital within the research community. The assessment will identify gaps in expertise and facilitate promotion and succession considerations.
- Promote the use of the assessment process as a mechanism for internal control and governance compliance within the research centre, in so far as its activities are financed from public funds. It would engender self-regulation of research activity.

#### ***3.5.4 Policy Measure: Extract Greater Value from the Development and Management of Intellectual Property (IP)***

The Government and the private sector must change the mindset from a focus on “protection of IP” to a focus on “collaborative exploitation of IP”. Fostering such an environment would require:

- Reviewing the operations of MyIPO against international benchmarks and providing the support for MyIPO necessary to meet and even exceed applicable international standards for assessment and protection of IP.
- Funding and expanding MyIPO to create “IP Malaysia” with the support of InnovationMalaysia set up under 10MP. The major functions of “IP Malaysia” will include:
  - Facilitating the assessment and certification of quality IP (“smart IP”) with the aim of reducing the number of trivial or nuisance IPs. Discontinue the practice of lenient pre-patent assessments.
  - Encouraging the bundling of IPs to enhance technical or market value.
  - Confiscating unused publicly-funded IP for broader benefit, after 5 years of non-use.
  - Acting as the clearing house for orphan IPs – e.g. through auctions.
- Establishing a professional society/association with self-regulatory functions to improve the standard of IP before it is brought for patent registration.
- Reducing the emphasis on establishing university KPIs based solely on the number of IP patents. The focus should be on the quality of the IP rather than the quantity.

#### ***3.5.5 Policy Measure: Consolidate and Merge National Enterprises to Create Scale***

Consolidation and merger of national enterprises and SMEs will give them the scale to participate and compete in the global market and create national champions and brand names (as was undertaken in Malaysia's financial sector with excellent results). In this connection, GLCs should



embark on specialised knowledge-intensive ventures, including diversifying into new markets. A number of GLCs have their own R&D centres which have generally been marginalised, particularly those operating within a protected market environment. GLCs involved in downstream plantation industries should invest in large scale R&D to support creation of new products in collaboration with international partners. KPIs for GLCs should not discourage risk-taking and pioneering new innovative growth strategies. Accordingly, GLCs should not focus solely on generating short-term profits. The time horizon of KPIs for GLCs should be lengthened so that GLCs will also focus on market development through new products and processes.

### 3.6 ADDITIONAL POLICY MEASURES AND CONSIDERATIONS

Additional innovation-related policy measures considered in the NEM and included in the 10MP are briefly discussed below.

- The NEM calls for a clear and transparent process for setting innovation promotion priorities in the innovation eco-system. The Government must continue to evaluate the impact of policies, programmes, incentives and funding in achieving the desired outcomes of economic change with innovation. The country should have a better balance between the current bias for a technology-driven approach towards one that favours a less risky market-driven approach for innovation.

The reform of the institutional structure supporting innovation and R&D has been announced in the 10MP (page 85), with the National Innovation Council (NIC) chaired by the PM and supported by the InnovationMalaysia unit in his office. The NIC reflects the commitment of the Government to promoting innovation. The NIC should emphasise an appropriate economic governance model that would integrate the demand and supply sides of sectoral transformation focussing on an outcome-based approach.

- Under the auspices of the NIC there should be better clarification and distinction of functional responsibilities between the agency responsible for defining the priorities and policy design, and the public agencies responsible for policy and programme implementation. It is important that the management of grants and funding programmes for innovation be undertaken by operational agencies.
- While the NIC will address funding support for innovation, special attention must be focussed on rationalising funding and support programmes that are currently spread over multiple agencies. The Government has recognised the need for an integrated approach to support innovation in knowledge-based enterprise. Duplication of programmes should be avoided in order to promote critical mass and lean procedures in public sector support for innovation. Past experience has shown that opacity in policy design and overlapping responsibilities among the government agencies (MOSTI, MITI, and related specialised agencies in science and technology) leads to programme capture by vested interests, inefficiency and weak outcomes. The NIC should strive to maximise the benefits from the internationalisation of R&D. In recent years R&D has become internationalised and the importance of involvement in the global production network has increased, as discussed above. Leading businesses around the world are shifting high-end processes to low cost destinations, a trend referred to as knowledge process outsourcing (KPO). KPO includes such areas as R&D, data management, business research, animation and design, and web content development. In KPO, the emphasis is on value-added processes which are highly complex and require the talent of professionals with specialised educational backgrounds.



The Government should develop a strategy to attract KPO opportunities to Malaysia. In addition to an emerging business opportunity, success in building KPO will serve to reduce the outflow of talent to other countries and contribute to a more effective diffusion of global knowledge to Malaysian enterprises.

- SMEs must undergo rapid transformation to spearhead the development of a knowledge-based economy. A culture of risk acceptance must be promoted to support commercialisation of ideas and creation of technology-based enterprises. Thus the NEAC welcomes the bold measures in the 10MP (page 82) to simplify the insolvency law that stifles risk taking and creates an undue stigma of failure.

**CHAPTER**

**4**

# **PUBLIC SECTOR TRANSFORMATION**



## 4 PUBLIC SECTOR TRANSFORMATION

### 4.1 A LEAN AND CUSTOMER-FOCUSSED GOVERNMENT

The cornerstone of the NEM is a private sector energised to rejuvenate investments, create high value jobs, and position Malaysia in global markets to propel sustained high income growth. However, it will be difficult for private firms to break out of their current shackles without a high-performance public sector to foster a supporting environment. The public sector must undertake a bold transformation and step up to its crucial role in the Malaysian economic structure. The Government's firm commitment to this formidable challenge is reflected in the GTP and 10MP policy strategies designed to strengthen public institutions, processes, and systems. These reforms entail the development of the capacities and capabilities of a lean and customer-focussed government.

The current reforms begin from a strong record of policy design and implementation that has resulted in Malaysia's considerable prosperity. Nevertheless, the policy measures embedded in the GTP and 10MP indicate recognition that the successful public sector structure and strategies of the past will not raise the economy to the next level. While there have been pockets of excellence in emerging efforts to make the public sector more efficient, connected, and responsive to the needs of citizens, the lack of a comprehensive strategy and mixed results have created a profoundly negative perception of the quality of public services on the part of the rakyat.

An entirely new approach is needed to revitalise, reshape, and re-invent government structures and administrative procedures to fit the requirements of a high income nation (**Table 4.1**). Reforms are needed to require the government bureaucracy to embrace a new paradigm on the role of government. The effectiveness and relevance of central agencies and other government entities must be critically assessed with a focus on streamlining. The panoply of government institutions resulting in overlapping functions, duplication of activities, and policy execution silos must be rationalised. The relationship between functions of federal, state, and local government must be reviewed and re-designed to be more responsive and to focus on outcomes. Institutional change agents such as PEMANDU and Special Task Force to Facilitate Business (PEMUDAH) must drive this process for reforms to take hold and to overcome resistance from vested interests.

Public sector reforms must support improvements in the functioning of the judiciary system. Rakyat and investor confidence is directly related to their perception of the expediency and transparency of the administration of justice and its adherence to internationally accepted precedence. The Government must promote best practice governance standards and mechanisms which espouse zero tolerance for corruption in both the public and private sectors.

The re-invention and transformation of public sector institutions must accommodate the new realities of global investment, finance, technology and human talent flows. The public sector must be better attuned to a new world view and be prepared to respond in new ways to promote Malaysian competitiveness. Public institutions and policies must respond to new challenges in building dynamic domestic businesses and exploiting regional and international opportunities. The vision is to create a "Seamless Government" that supports the Malaysian global supply chain. Coupled with this vision is an increasing expectation of high quality services and greater citizen involvement in services design. The creation of a seamless government is critical as citizens

struggle to identify, access and use government services. Citizens should be key partners in driving change in the public sector. Disclosure and access to public sector data will empower citizens to participate in policy design, review, and implementation.

**Table 4.1 – Summary of Policy Measures for Transforming Government**

<b>Bureaucratic Reforms</b>
<ul style="list-style-type: none"> <li>• Strengthen the Government's facilitative role <ul style="list-style-type: none"> <li>➢ Rationalise responsibilities and authorities between and among central agencies and ministries</li> <li>➢ Expand coverage of electronic licensing capability to all relevant ministries and agencies i.e. Business Licensing Electronic Support System (BLESS)</li> </ul> </li> <li>• Create a citizen-centred public service</li> <li>• Expand private delivery of public services by allowing access, on a competitive basis, to public funding (i.e. healthcare, higher education, technology support institutions, etc)</li> <li>• Enhance public agencies to drive growth</li> <li>• Extend judiciary administrative reforms to all levels and nationwide</li> </ul>
<b>Improving the Quality of Human Resources in the Civil Service</b>
<ul style="list-style-type: none"> <li>• Reform the Public Service Commission (PSC) to define strategic human resource policy and management processes in the public sector</li> </ul>
<b>Strengthening National Policy Formulation in Economic Governance</b>
<ul style="list-style-type: none"> <li>• Revive the National Development Planning Committee (NDPC) as the premier body for policy development, coordination and consultation</li> </ul>
<b>Fiscal Discipline and Reforms</b>
<ul style="list-style-type: none"> <li>• Implement accrual accounting to facilitate asset-liability management</li> <li>• Implement efficient broad-based tax for revenue and fiscal stability</li> <li>• Strengthen expenditure control <ul style="list-style-type: none"> <li>➢ Introduce value management in expenditure planning to get value for money</li> <li>➢ Extend transparent procurement policy and procedures for better price discovery</li> <li>➢ Introduce Funded Pension Schemes</li> </ul> </li> <li>• Improve Fiscal Policy Institutions and Processes <ul style="list-style-type: none"> <li>➢ Institute use of non-oil balance for fiscal policy formulation</li> <li>➢ Undertake an assessment of compliance with fiscal international practice under the programme of Report on the Observance of Standards and Codes (ROSC) for greater transparency and effectiveness of fiscal conduct</li> </ul> </li> </ul>

The proposed reform requires a form of “Entrepreneurial Government” to keep pace with the radical real time changes in the global, regional, and domestic environment. Public sector institutions play a key role in creating the capability for dynamic change and innovation. Its structures, processes, rules and activities must generate continuous learning and new thinking to meet the challenges of managing uncertainty. Policies and services should be designed and delivered from the citizen's perspective. Greater citizen choice is an important component in the establishment of the entrepreneurial government envisaged by the NEM.

Sound public financial management is critical to the sustainability of benefits envisaged under the NEM. The recently-launched 10MP anticipates that the deficit reduction efforts defined therein will reduce the federal government deficit to 2.8% of GDP by 2015. It is expected that the planned measures will continue in the 11MP and reach a balanced position before 2020. The SRI policy measures must build on those efforts. Enhanced fiscal prudence will contribute to the macroeconomic stability required for sustained economic growth. It will continue to address public debt to protect the prospects of future generations. It will also allow for effective response to unexpected crises like the recent GFC. The forward trajectory towards high income status will thus be better safeguarded.

## **4.2 BUREAUCRATIC REFORMS**

The Government-led economic model of the past was characterised by an interventionist approach. The establishment of strategic industries, centralisation of decision-making and wide ranging affirmative action policies resulted in pervasive government involvement in the economy. While generating benefits to the economy, this also created market inefficiencies and misalignments and led to policy inflexibility, increased the costs of doing business, and opportunities for corruption.

### ***4.2.1 Policy Measure: Strengthen the Government's Facilitative Role***

The Government's role should be less interventionist and more facilitative. A reduced government role will involve downsizing and re-focussing. Actions involved in the implementation of those measures would include:

- i. Review programme, project, and activity overlaps and duplications between and among central agencies and ministries.
- ii. Introduce best practices to reduce duplicative and redundant regulatory burden on businesses and corporate citizens.
- iii. Leverage ICT for hassle-free business licensing, efficiency gains, and reduction of the incidence for corruption. This will facilitate the creation of a seamless government through improved e-government platforms that enable on-line application and processing plus real-time tracking of decision making through a single access point.

### ***4.2.2 Policy Measure: Create a Citizen-Centered Public Service***

As Malaysia strives to attain advanced nation status, there will be greater citizen expectation for involvement in the design, implementation, and evaluation of policies and legislation. A new engagement model will allow citizens, business and community groups, including resident foreign nationals, to become active participants and contributors to policy formulation, execution, and review.

The creation of a seamless and connected government is facilitated by electronic government platforms. The use of a single electronic access point, real-time tracking, and effective call centre support would render the Government more transparent, reduce the costs of doing business, and reduce rent-seeking and corrupt practices. E-government platforms should drive

the seamless government agenda and promote the sharing of ideas between the government and citizens.

Specific policy actions that would facilitate such outcomes include:

- i. Establishing citizens' consultative councils within ministries and local government entities to enable citizen participation in policy design, implementation, and review.
- ii. Building information-sharing protocols to ensure citizens have access to information to enable effective participation in policy formulation.

#### ***4.2.3 Policy Measure: Expand Private Delivery of Public Services***

As society modernises and evolves, the Government's role, responsibilities, and structure should evolve with it. The legislative and regulatory framework must in parallel be continually reviewed for appropriateness and relevance. This regular appraisal will evaluate whether the Government is effectively carrying out its role on an on-going basis. An evolving government paradigm will be needed. Society will have increased expectations for greater choice. Public sector services may be increasingly provided by the private sector at potentially higher quality levels and at market prices. Public institutions may be required to compete with private sector providers for previously "captive" customers. The Government must be positioned to facilitate such choices.

#### ***4.2.4 Policy Measure: Enhance Public Agencies to Drive Growth***

Development of new sources will leverage Malaysia's traditional strengths in such industries as palm oil, education, tourism, halal food, Islamic banking, etc. Attracting investments into these areas requires a more focussed, inter-agency approach.

Specific measures to support investors include:

- i. Creating new institutional champions i.e. within MITI, MOHE, etc to spearhead one-stop cross-agency teams/committees to promote investments in new growth industries. Strengthening development and corridor authorities for clusters and sectors as coordinating mechanisms at local and regional levels.
- ii. Ensuring that the re-structured MIDA builds up capability to offer point-to-point support for investors in the new growth industries in manufacturing and services sectors. This will require hand-holding from the pre-inception stage to the final full business operations stage.
- iii. Energising the re-structured MPC to spearhead increasing competitiveness and productivity in the private sector.

#### ***4.2.5 Policy Measure: Pursue Administrative Reforms in the Judiciary***

The absence of effective judicial administrative modernisation will inhibit sustainable economic development. As the economy grows and additional laws are enacted, business disputes will increase. Legal disputes will become more complex as the economic sophistication increases. The capacity of the Malaysian judiciary to efficiently and effectively administer justice is critical to the country's enabling environment and to increasing investor confidence.

The judicial administration record has been poor, characterised by judicial hearing and resolution delays, high cost, and antiquated court management systems. While there has been commendable effort to address the issue, there has been a distinct lack of urgency in the existing modernisation efforts. Judiciary administrative reforms should be expedited at all levels.

Recommended policy actions to spur judicial administrative reform include:

- i. Creating a one-stop legal matters intelligence gathering resource centre, linked online to the world's best libraries and databases to become a premier repository of information and data. Stakeholders can access real time legal information, archives, scholarly contributions, comments, and critiques to assist in crafting weighted responses or make informed decisions. For a market driven economy, the ready availability of timely and relevant information is imperative to facilitate working more efficiently, transparently and confidently.
- ii. Establishing new specialised courts and tribunals e.g. courts to hear environmental, fiscal, and maritime issues, would send a signal to the world that Malaysia is addressing sophisticated cutting-edge world issues and concerns.
- iii. Increasing the performance and monitoring capabilities of the administrative processes in the judiciary to strengthen efficiency that in the modern business world is an indispensable part of the enabling environment of a vibrant economy. The quick and fair resolution of disputes is as important as adjudicating justice. The introduction of key performance indicators (KPIs) will impose greater discipline in courtroom procedures and curb routine adjournments which have hindered efficiency. There is a need for closer monitoring of the back-log of cases, improving management of back-office activities, and accelerating the disposal of cases through case better management.
- iv. Expanding the use of technology applications in court hearings and support activities e.g. Queue Management System (QMS) and Case Recording Transcription (CRT) which should be rolled-out nationwide.
- v. Upgrading administrative human resources management is vital in any organization. Continuing education and academic exposure should be made available to promote a culture of professional advancement among professional and other staff.

### **4.3 IMPROVING THE QUALITY OF HUMAN RESOURCES IN THE CIVIL SERVICE**

Improved quality of civil service human resources at the federal, state, local levels is essential for bureaucratic reforms to bear fruit. The civil service plays a critical role in setting policies, delivering services, and creating laws and regulations that affect citizens. The effectiveness of government institutions is determined primarily by the capacity, motivation, and integrity of the civil service and the quality of its leadership.

In an era of rapidly evolving global and domestic challenges, governments must continually re-define their role and recalibrate their public service capabilities. Governments grapple with the development of responsive and connected models that emphasise greater openness and partnership with civil society and the private sector. A key challenge is to incorporate or reinvigorate traditional civil service values such as impartiality, integrity, and dedication while promoting management innovations and efficiency improvements.

#### **4.3.1 Policy Measure: Reform the Public Service Commission (PSC) to Define Strategic Human Resource Policy and Management Processes in the Public Sector**

The PSC is tasked under the Federal Constitution with the responsibility for the appointment, confirmation, promotion and discipline of public sector employees. However, past policy decisions have diluted its responsibility for strategic human resource management and have restricted



its functions to administration of appointments and promotion confirmation. As a result, it has failed to perform the essential task of building a high-performing civil service that is efficient, effective and instilled with a professional ethos. The civil service currently lacks a sufficiently broad-based understanding and appreciation of the business world, economic trends, and international best practices in an increasingly globalised marketplace.

The PSC must be completely re-defined to play a dominant role in shaping strategic HR policies in response to the needs of a dynamic economy. It needs to create a policy environment that produces leaders and specialists prepared to drive innovation, provide forthright advice, and change attitudes in organisations to meet the needs of a private sector-led economy and its increasingly sophisticated citizens. For this purpose, the members of the PSC should be top-notch visionary professionals drawn from the public and private sectors, including top HR specialists that can reflect the demands of the NEM on the civil service.

The PSC will need to play a proactive role to attract the best and the brightest, promoting core values of commitment, integrity, and professionalism, and developing a merit-oriented civil service. The new PSC must instill a greater performance ethos and sustain motivation and integrity among public sector employees. It needs to promote higher employment mobility between the private and public sectors at all job levels, particularly mid- and upper-management, by enabling appointment flexibility and career development, irrespective of entry point. This would entail disentangling recruitment rigidities and reviewing remuneration packages, as well as shifting away from lifetime employment. The goal should be to attract and retain competence while maintaining high performance and motivation over a sustained period. The complex external and internal challenges facing the public sector call for a sense of urgency to forge a symbiotic relationship between the private and public sectors.

The newly defined and empowered PSC should address public sector HR issues by defining, among others, policies and programmes to accomplish the following:

- i. Revamp civil service HR policies to allow open recruitment and private-public sector mobility at mid-career level and above. Such a re-structuring will widen the leadership and talent pool in the civil service.
- ii. Reinforcing state and local government human resource capabilities using the federal level template.
- iii. Increasing flexibility in the public personnel system through a review of the public service pension system, which favours a funded portable pension scheme, contract employment, and separation mechanisms.
- iv. Widening the leadership pool in the public service through an open system of recruitment for top talent from the private and public sector.
- v. Undertake independent review and assessment of human capital management practice in the public sector to ensure effective implementation of various programmes.
- vi. The public sector needs to devote resources to encourage the development of specialised research (i.e. ISIS, MIER, etc) and training (INTAN, ILKAP, IDFR, etc) institutes in collaboration with one or more world leading institutions in public policy and economic management.

The NEAC supports the establishment of a School of Government. It is essential that this institution operates on a solid academic and intellectual basis to develop first-class executive and economic management training programmes

#### **4.4 STRENGTHENING NATIONAL POLICY FORMULATION IN ECONOMIC GOVERNANCE**

There are currently a number of committees that deliberate on major policy directions and monitor implementation of government projects. This includes the Economic Council, the National Planning Council, the National Action Council and a host of Cabinet Committees. The functions of, and interactions between, these units have over time become unwieldy and raised concerns about their cohesiveness and efficiency in vetting Cabinet-bound policy proposals.

##### ***4.4.1 Policy Measure: Revive the NDPC as the Premier Body for Policy Development, Coordination and Consultation***

There is an urgent need to re-visit the functions and efficacy of this review framework to ensure that adequate checks and balance exist and to generate a genuine integration of planning and implementation activities at the highest level of government. For this purpose, it is recommended that the National Development Planning Committee (NDPC) be reinvigorated to streamline and coordinate review of policy originating from ministries and agencies at the federal, state, and local levels. This is in line with the whole-of-government approach.

The NDPC is comprised of Secretary-Generals and Director-Generals of the respective ministries and agencies. It thus has the leadership capacity to decide on streamlining and coordination of policies before being presented to the Cabinet for final decision making. The original intention was to ensure that major policy papers from ministries/agencies be presented to NDPC for deliberation and review before submission to Cabinet. However, the NDPC has since come to be primarily deployed as a mechanism for the national development planning process. It has lost its function as an effective inter-agency policy coordination and consultation forum. The role of senior civil servants as policy advisors has been diminished and the incentive structure for considering difficult or tough measures has disappeared. There are insufficient debates on the pros and cons of policies. There is limited analysis of alternative policy scenarios or options and their underlying risks factors. As a result, there is greater incidence of unnecessary policy recalls contributing to the erosion of confidence in Government management.

For it to become effective, the 'new NDPC' needs to be reinvigorated to focus on both policy formulation and implementation, not exclusively on the development planning process. To ensure better coherence in the formation and implementation phase of high impact national policies, the existing range of committees needs to be reviewed and rationalised. The new role and functions of the NDPC will include:

- Reviewing policy recommendations from various ministries and agencies to ensure alignment with the overall national strategy, consideration of global impacts and repercussions, rigorous analysis, and thorough consultation across Government agencies. During implementation, ensuring coordination of policies among different levels of government i.e. federal-state-local.

- More intensive scrutiny of key tough or bold cross-cutting and multi-sectoral policy initiatives to address the broad economic objectives of the Government. This will ensure that policy decisions are well-grounded and based on pertinent facts, while recognising potential trade-offs and political implications.
- Monitoring implementation of policies and Government decisions and providing relevant information to the rakyat as appropriate.
- Designing adjustments and required additional interventions and measures to ensure that policy implementation is sustained and will stay the course towards achieving the desired outcomes.

## **4.5 FISCAL DISCIPLINE AND REFORMS**

Increasing tax system efficiency together with greater resolve in the control of expenditures will bring better balance to public finances over the coming years. Comprehensive revenue and expenditure management measures that will over time increase revenue collection while restraining expenditures, are needed. Fiscal reforms should focus on the establishment of an efficient, simple and transparent tax system. Expenditure containment should focus primarily on operating outlays. In addition, adoption of accrual accounting will facilitate asset-liability management, and hence, comprehensive and prudent fiscal management.

### ***4.5.1 Policy Measure: Adopting Accrual Accounting for Prudent Fiscal Management***

Sole reliance on cash accounting gives rise to significant risks stemming from inattention to asset-liability management. Additionally, contingent liabilities have risen over time. Although there is a low probability of their full realisation, these potential outlays must be better managed and accounted.

Analysis of fiscal aggregates needs to be based on a variety of presentations to better represent all aspects of the operations of the Government. Cash accounting provides only the cash flow state of government finances. Additional information that could be provided by accrual accounting would provide a more rigorous understanding of the sustainability of public finances. Accrual accounting would enable the generation of additional financial statements, including a balance sheet showing Government's assets and liabilities. Whereas the operating statement shows the financial results of Government's activities over a period, the net outturn may be a misleading indicator as excess expenditures could have been financed by asset sales the depletion of which may have implications for longer term fiscal sustainability. Additional details stemming from accrual accounting provides a more complete picture of Government financial transactions. International good practice calls for expanding Government financial information to include accrual accounting statements.

### ***4.5.2 Policy Measure: Implement Efficient Broad-based Tax for Revenue and Fiscal Stability***

An optimum tax system is one which engenders equity and fairness, efficiency and neutrality, simplicity, certainty, flexibility, and fiscal adequacy. Evidence suggests that Malaysia's tax system is far from this ideal. Only 12.4% of registered companies in 2010 paid taxes, reflecting in part excessive tax exemptions or credits. Similarly only 14.5% of Malaysian employees paid taxes

because most worker earnings fall below the tax threshold. The yield from those paying taxes remains low as wage levels have not changed over the last five years. Other non-oil revenue sources are losing ground, reflecting the narrow base and generous relief and exemptions.

Most notably, oil-related taxes made up 37% of total revenue in 2008. This revenue source is unsustainable as oil reserves begin to deplete, exposing public finances to increasing risk. Moreover, dependence on revenue from oil exposes Malaysia's expenditures to commodity price swings, made complicated in recent years by a rigid consumer energy price subsidy system. This has contributed to perverse budgetary practices, where expenditures are based not on need but on available revenue from oil. It also implies that windfalls from oil price spikes are not set aside as a buffer to meet future contingencies.

Recommended specific tax reform measures include:

- i. Implementing the Goods and Services Tax (GST) which has been under consideration for too long.
- ii. Rolling back some corporate tax incentives for selected industries and consider lowering tax rates in line with neighbouring countries.
- iii. Revamping personal income taxes to make them less regressive, consider lowering tax rates, and consolidate personal income tax credits into fewer categories.
- iv. Improving tax administration and compliance.
- v. Setting aside all petroleum related revenues as designated revenue into a special account/fund. Draw down from this account will be at a strictly rule-based, sustainable rate. Furthermore, starting from the 11MP, the funds from this account should not be used to finance current expenditure. This mechanism will impose fiscal discipline.

#### **4.5.3 Policy Measure: Strengthen Expenditure Control**

Malaysia's government expenditure at around 26% of GDP is not overly high by international standards, ranked 15th lowest among 54 countries sampled by International Institute for Management Development (IMD). However, outlays are larger than regional peers (Korea - 23.6%, Taiwan - 20.7%, Indonesia - 18.3%, and Thailand - 17.7%). Our expenditure efficiency is also deteriorating. During the 7MP period, to generate RM1 of GDP the Government spent 15.4 sen in operating expenditure and 6.4 sen in development expenditure. But during the 8MP period, to generate the same RM1 of GDP, Government spending had increased to 18.4 sen and 7.9 sen, respectively. Operating outlays increased further to 20.5 sen with development expenses falling back to 6.4 sen, in the first four years of the 9MP. This is a cause for concern, reflecting growing rigidities in current outlays.

While current expenditure is not readily amenable to cutbacks in the short term, there should be ample opportunity for curtailment and reallocation over the medium term. Structurally current outlays in 2009 can be disaggregated into emoluments (27.2%), supplies and services (16.8%), debt service charges (9.1%), pension (6.5%), subsidies (13.0%), grants and transfers and others (27.4%). The single largest component of current expenditure is emoluments. The Malaysian public sector is overstaffed. Another significant observation is that the public sector is bottom heavy as almost 70% of the public employees are in the support group category which is the group with the lowest skills in the public sector. This percentage rises to almost 79% when considering only the central government workforce.

Recommended specific expenditure reform measures include:

- i. Introducing value management in expenditure planning to ensure value for money. EPU has already issued voluntary guidelines that require all projects costing RM50 million and above to follow value management rules. These need to be strengthened and made mandatory.
- ii. Establishing transparent procurement policy and procedures to promote better price discovery and help in containing outlays. There is a need to review the current practices. More of the tender exercises should be based on the open tender process. A more widespread adoption of e-bidding in line with the latest electronic and internet environment would also contribute to better transparency and a more effective procurement system.
- iii. Right-sizing the public sector to reduce the wage bill.
- iv. Reforming the civil service pension system, to reduce the Government's contingent liabilities. Specifically, all new civil service recruits should be required to join a funded pension scheme. The pension scheme should also be able to address issues related to flexible entry and exit mechanisms proposed under the public sector reforms.
- v. Rationalising subsidies and transfer payments. This is already underway but should be accelerated.

#### ***4.5.4 Policy Measure: Improve Fiscal Policy Institutions and Processes***

Fiscal policy is an important component of the country's macro-economic management. As an oil producing country, the design of fiscal policy and position in Malaysia poses a higher challenge. Fiscal discipline and prudence require strong justification acceptable to all stakeholders. Every major decision of the Government will inevitably have fiscal implications. This can only be done effectively if relevant fiscal institutions play their role effectively. For this reason the NEAC proposes a review of fiscal policy institutions be undertaken with the objective of strengthening their role and functions.

The use of the overall balance to describe Malaysia's fiscal policy stance is not adequate. It sends misleading signals to policy makers due to the size and volatility of oil revenue. Malaysia's overall deficit could be low, creating the impression of fiscal consolidation when in fact there is considerable risk of fiscal impulse and the need for drastic expenditure cutbacks when oil prices drop. The NEAC proposes that the Government uses the concept of the non-oil balance, together with other non-oil aggregates, to complement the current commonly used aggregates in fiscal policy formulation.

Another important task is to undertake a Report on the Observance of Standards and Codes (ROSC) on fiscal transparency. This is a stock take on the state of fiscal transparency and effectiveness of fiscal policy formulation based on standardised international best practice. Longer term tasks would include introducing medium-to long-term budgetary frameworks and improving the dissemination of information on public finances.

CHAPTER

5

# INTENSIFYING HUMAN CAPITAL DEVELOPMENT



## 5 INTENSIFYING HUMAN CAPITAL DEVELOPMENT

### 5.1 A SKILLED WORKFORCE IN A VIBRANT LABOUR MARKET

The quality of the Malaysian workforce is regressing. New entrants into the labour force do not meet the skill needs of industry. Investors complain that potential workers lack analytical and problem solving capabilities. Deficiencies in language proficiency and social networking aptitude hinder progress in the adoption of cutting edge technology and modern teamwork processes needed for high-value added activities. Without a skilled workforce of adequate scale we risk spiraling towards mediocrity as a nation. Overcoming these shortcomings is a medium-term challenge for which actions under the GTP and 10MP are already underway as discussed in Section 5.3 below.

The pivotal need is a radical revamp of the current education system, ranging from the primary to the tertiary levels, and requiring improvements at each level. This constant refrain is well recognised yet the attempted fixes have failed to yield the desired results. In this instance the Government has shown that it does not know best. We need a comprehensive reform programme as opposed to a patchwork of disjointed actions. The education system must move beyond the “nation building stage” to providing the tools and skills to compete in the global marketplace. Close partnership among all stakeholders, i.e. Government, industry, academia, parents, and NGOs, drawing from past and international experience will be the key to achieving the desired outcome.

**Table 5.1 – Summary of Policy Measures for Intensifying Human Capital Development**

<b>Workplace Transformation</b>
<ul style="list-style-type: none"> <li>• Set up an expert group to modernise and align labour legislation and regulation consistent with international best practice, with the dual objectives of reduced costs to business of labour management and increased effectiveness of worker protection</li> <li>• Strengthen strategic human resources management</li> <li>• Enhance the workers safety net through the introduction of unemployment insurance</li> <li>• Establish A National Wage Consultative Council (NWCC)</li> <li>• Facilitate a Productivity-Linked Wage System (PLWS)</li> <li>• Consider a minimum wage policy</li> </ul>
<b>Workforce Transformation</b>
<ul style="list-style-type: none"> <li>• Undertake a labour market forecast and survey programme</li> <li>• Up-skill and upgrade the workforce               <ul style="list-style-type: none"> <li>➢ Set overall strategy for upgrading the workforce</li> <li>➢ Standardise certification of semi-skilled workers</li> </ul> </li> <li>• Leverage women’s talents to raise productivity</li> </ul>

While the NEM attaches supreme importance to intensifying human capital development and thereby upgrading the workforce, it also attaches equal weight to the creation of an inspiring workplace. Malaysia’s workplace environment needs a profound transformation to invigorate



the behaviour of both employers and employees to embrace new technology and innovative processes. There is much truth in the saying “We are a product of our environment”. An array of cross-cutting policy measures must be put in place to galvanise and energise all stakeholders in order for the right workplace environment to blossom. Many broad policy measures to strengthen Malaysia’s labour market have been proposed in the NEM under SRI2. Elements of the 10MP and GTP are addressing issues around education, talent and low skilled foreign labour. This report will focus on a few key measures that are essential to drive the sustained transformation of both the workforce and the workplace (**Table 5.1**).

## **5.2 WORKPLACE TRANSFORMATION**

In the workplace, employers are driven to acquire and sustain increased market share in order to survive. This is juxtaposed against the risk of failure from obsolescence, lost of reputation and insolvency. This dynamic involves a variety of factors including a balance of short- versus long-term strategies, sustained position in the supply chain, and corporate social responsibility (CSR). The latter is increasingly understood to include obligations to employees, compliance with environmental and safety standards, and contribution to the community.

By the same token, workers are driven by the rewards of well-paying and fulfilling jobs against the risks of unemployment, including for non-performance or inappropriate behaviour. Considering the perspectives of both the employers and the workers, reward and compensation structures must be designed to recognise good performance and achievement of high quality standards. Entitlement mindsets and rigid security-of-tenure demands, which both engender complacency and limit wages, must be avoided. In Malaysia, the wage-setting mechanism is defective as evidenced by stagnant and low wages of most categories of workers.

For the workplace to function effectively, a series of critical elements must be present. Among the most important are appropriate labour laws and modern human resources management practices and systems. Others involve the commitment of both employees and employers to add value to the final products or services. Still others revolve around effective and transparent communication between employees and employers, and between them and the Government, industry groups, unions, and civil society. Employer commitment is reflected by management consideration of employees’ interests when running the business. Employee commitment is demonstrated by the value assigned to their employment as well as their belief in, and internalisation of the objectives of the firm.

### **5.2.1 Policy Measure: Modernise Labour Legislation**

Recent amendments to labour legislation, including those proposed in the 10MP, have been piecemeal. The NEM has proposed a strategic, comprehensive revision of labour legislation with the purpose of reducing the costs to business of managing workforce-related issues while ensuring effective worker protection (**Table 5.2**). In particular, the improved legislative framework must address the following elements:

- Full flexibility in the hiring and separation of workers – the changes must remove the impediments that have deterred investment, fostered workplace complacency, and prevented the creation of an enhanced worker safety net.
- A more rapid, consistent, and efficient conflict resolution process.
- A more effective mediation and arbitration process whereby referral to the Industrial/Labour Court is a last resort and not the preferred avenue for resolution.

**Table 5.2 – Comprehensive Modernisation and Consolidation of Labour Legislation**

Current Situation	Recommended Approach
Multiple laws; some dating back to the 1940's and 1950's are outdated, overlapping and contradictory. These are unsuited to the modern economy, impeding progress, and obstructing our global competitiveness.	Consolidate and streamline existing labour-related laws into a structure appropriate to evolving labour market structures and practices in an increasingly knowledge-based and service-oriented environment.
Undue rigidity in the provisions for dismissal of employees contributing to higher costs of doing business.	Greater flexibility in dismissal procedures adaptable to, and consistent with, a rapidly evolving workplace setting. Provide fair treatment for workers, but do not protect obsolete jobs.
Worker safety net based mainly on unfunded severance compensation.	Employer and employee funded unemployment insurance including provisions for retraining, job search-placement and relocation.
Unwieldy and prolonged process for resolving labour disputes. Unclear mediation and arbitration framework.	Formalise a time-bound, transparent and binding mediation and arbitration process
Undue easy access to Industrial Court for resolving disputes. Industrial Court insufficiently cognizant of evolving labour market setting.	Access to Industrial Court should be a last resort, thus contributing to faster and more certain resolution of disputes. Stakeholders must keep abreast of rapidly changing business employment patterns.
Uncertain and dated coverage and protection for workers, particularly those in changing labour market structures/patterns, e.g. part-time, work-at-home, women workers, workplace harassment, etc. Some amendments/regulations being introduced on piece-meal basis.	A more holistic approach to the introduction of labour law changes relating to changing work environment and new generation of the workforce. Better compliance with international good practices or standards.

The Government should urgently commission a group of legal and operational experts tasked with modernising, consolidating, amending and/or rescinding Malaysian labour laws and adopting global best practices. The work of the experts should be facilitated by Ministry of Human Resources (MOHR). This Commission of Experts should be in place by end-2010 and submit their recommendations to target implementation by end-2011.

### **5.2.2 Policy Measure: Strengthen Strategic Human Resources Programmes**

International experience and that of MNCs operating in Malaysia has shown that there is a strong correlation between the quality of human resources (HR) management, stability in labour relations, and overall corporate performance. The use of progressive and modern HR practices is a key success factor for firms in attracting and retaining a high quality and productive workforce. Incentives should be given to firms that adopt specific HR practices consistent with international standards. The specific nature of the incentives (e.g. tax credits or expenditure write-offs) and the particular types of qualifying HR practices will need to be defined by the Government, the industry, unions and civil society.

In Malaysia, some 60% of the total private sector workforce is in SMEs, the smaller of which would face immense challenges in adopting the needed HR practices to enhance quality and productivity. To overcome this, the NEAC recommends establishing National Human Resources Centres to provide strategic HR support to all such SMEs.

These centres will provide both strategic and operational HR support to SMEs. Small businesses should be given incentives to subscribe to the services of the centres. The centres will play the role of effective HR departments with a strong focus on strategic and change management processes. They should adopt a holistic approach based on the Total Human Capital Development System (THCDS) which would among other things cover:

- Recruitment and Assimilation
- Performance Appraisal and Development
- Training & Education
- Compensation (including Productivity Linked Wage System)
- Skills Structure & Succession Planning
- Supporting Policies (including workplace flexibility & work environment)

The centres could be established and managed initially on a collaborative basis with the following organisations:

- MNCs / GLCs / SME Associations/Unions/Other worker groups
- MPC / PSMB / MOHR

A strong HR leadership team will have to be created to lead and manage the establishment of centres from inception to the full rollout of the service offerings. Staffing and talent to run the centres can come from the above organisations on a secondment basis, as well as from existing HR service providers. The proposed Talent Corporation under 10MP could provide the management oversight of the centres.

To incentivise the SMEs to subscribe to the services of the centres, tax incentives for 3-5 years could be considered. Likewise, there should be disincentives for SMEs for not subscribing or adopting such HR practices in the form of a labour levy.

A rating system to designate “Responsible Employer” status could be established by the industry as an incentive for employers for adopting the Total Human Capital Development System. A supplementary tax incentive could be granted through a modest drawback on HRDF and SOCSO contributions.

### ***5.2.3 Policy Measure: Establish a National Wage Consultative Council (NWCC)***

A major shortcoming in assessing the performance of the labour market is the availability of appropriate data on all aspects of the labour market. Critical and timely information on trends in wage development and productivity measures are either not available or inadequately analysed. Sparse and anecdotal information appears to indicate wage stagnation in recent years in almost all segments of the economy, with the possible exception of the financial sector and other high skill professions. Productivity growth overall is trending downwards and in the services sector may have even turned negative. The gains from productivity increases also appear to have accrued predominantly to the holders of capital and with labour receiving a negligible share.

A National Wage Consultative Council (NWCC) should be constituted. Employer groups, unions, non-union labour groups, Government, academia, and interested NGOs would all be represented on the council. The NWCC would have the authority and capacity to call on international and regional agencies, bilateral government agencies, and other groups to assist in specific projects on wage development and wage-setting mechanisms. It would be charged with collecting comprehensive data on wages, compensation packages and labour productivity in coordination with the Department of Statistics. It will analyse that data and collaborate with MPC in assessing productivity aspects of the labour market. This analysis will support the provision of guidance to employers and employees when deliberating wage agreements. The NWCC will, through periodic publications, disseminate this information and analysis. The NEAC is pleased to note that the formation of the NWCC was recently announced in the 2011 Budget.

Employers and employees would be required to refer to the information provided by NWCC when deliberating on wage and compensation agreements. Links to the consumer price index should not be the only indicator for assessing the adequacy of wage agreements.

#### **5.2.4 Policy Measure: Formalise a Productivity-Linked Wage System (PLWS)**

The NEM advocates that wages should be determined by market forces. Minimum wage mechanisms could be considered where there are clear market failures in segments of the market or where the wage-setting system is dysfunctional. Current explanations for wage stagnation have centred on the close link to the consumer price index (CPI) (precedence set by a 1982 court case), rather than on productivity or performance of the companies.

Global practices are moving towards linking wages to productivity and company/employee performance. Malaysia needs to do the same thing to participate in the global supply chain and retain and attract a highly productive workforce. It is also clear that increases in wages cannot outpace labour productivity gains. In tandem with an effective NWCC, the Government should facilitate and incentivise the adoption of a Productivity-Linked Wage System (PLWS). This system should be championed by the MPC working with employers and workers organisations to define the operational details.

There will be many challenges given the disparate interests of the stakeholders. A major obstacle will undoubtedly be the quality, reliability, and granularity of the data on wages and productivity. The work of the NWCC will contribute substantially to overcoming this obstacle. The revamped mediation, arbitration and judiciary process for wage conflict resolution must assign due importance to the PLWS when handling disputes.

#### **5.2.5 Policy Measure: Consider a Minimum Wage Policy**

As described above, the NEAC advocates a PLWS. However, it is also aware that dysfunction in the current wage-setting mechanisms is depressing wages to an unacceptably low level. In the spirit of the NEM objective of inclusiveness, the introduction of a minimum wage policy should be considered.

A study by MOHR indicates almost 34% of workers in Malaysia earn less than RM700 a month. This is relative to a poverty line household income set currently at RM720 per month. Latest data available from the 8MP reported that salary and wages increased by an average of 6.8% per year for the period of 1995-2000, while labour productivity increased at an average rate of 10.4% per year for the same period. A World Bank study found that the wage trend in Malaysia has recorded only an annual 2.6% growth during the past 10 years.

However, the design of a minimum wage policy must be fair, should not distort labour markets, and must not jeopardise employment creation, particularly for younger workers, women and those with special needs e.g. the disabled community. The minimum wage level should be set through a rational and objective process, devoid of political considerations. The NWCC should study the minimum wage issues and the experience of countries in similar situations in order to identify and propose options, e.g. the choice between a single national minimum wage, or multiple levels based on agreed criteria.

#### ***5.2.6 Policy Measure: Enhance the Labour Safety Net by Introducing Unemployment Insurance***

The NEM recommends bold reforms to the outdated labour laws. However, the NEAC also recognises that such labour reforms must be accompanied by enhanced safety net mechanisms. Malaysia's social protection system is still evolving, as in many Asian countries. Gaps and inefficiencies remain in safety net mechanisms, particularly for protection of workers. Economic transformation under the NEM is expected to result in some degree of frictional unemployment, for which an enhanced labour safety net is needed to help ease transition for workers.

A functioning and effective labour safety net forms an important part of the NEM and contributes to the objectives of high income and inclusivity. The main objective of a safety net is to help cushion the adjustment costs to beneficiaries without impeding the requisite reforms, i.e. it allows for the necessary tough measures to be taken up-front rather than be phased-in, which can dilute impact. Pressure on the labour market safety net can be reduced by an effective and efficient labour market that allows workers to quickly find new jobs matching their skills, which minimises costs to firms and negative impact on workers.

Safety net management must address issues surrounding access, extent and duration of benefits, and the obligations of recipients. Funding issues also have to be considered. During the establishment of the enhanced safety net, there may be a need for transitional arrangements.

The current safety net system focusses on retrenchment benefits for workers laid off due to economic circumstances. Multiple problems have been encountered with this system. Businesses have closed without meeting retrenchment obligations. Or in the case of insolvency, retrenchment benefit claims (other than outstanding wages) are not positioned advantageously for access to the proceeds from liquidation of the failed firm's assets.

An appropriate labour safety net would include an unemployment insurance scheme supported by up-skilling and retraining programmes, and upgraded employment services. Unemployment Insurance (UI) would alleviate reliance on retrenchment benefits to cover income loss from a job loss. UI would enable the risks from job market anomalies to be pooled and provide for payouts when needed, similar to any insurance model. It would need to be simple to minimise administrative costs. Benefit payouts should be of limited duration to preserve the financial integrity of the fund. Payouts should represent partial income replacement to force beneficiaries to actively seek a replacement job. This would minimise the risk of employability from prolonged unemployment. Laid-off workers must also participate in up-skilling or retraining for continued access to UI benefits. Dedicated training facilities must be set up for this purpose.

Finally, the labour safety net should provide relocation allowances, encompassing moving and transport costs, housing search assistance, and family essential needs, e.g. schooling.

Retrenched workers must be prepared for relocation to suitable job locations for continued access to UI benefits.

Best practice calls for UI funding through levies on employers and workers. This would add to the costs of doing business, but is understood worldwide as a normal cost of business. For employers it can be considered part of their CSR obligations.

Mechanisms for effective job search and placement services must be enhanced and tailored for retrenched workers. This will require a consolidation of existing public job search assistance agencies into a single nationwide network leveraging internet technology. Coverage could be expanded to include private sector job search networks. Pilot programmes could be established for job search networks for high skill workers and professionals. A side benefit of internet-based search networks is the collection of data to measure evolving demand. This data can be used to plan education, vocational, training/retraining efforts. Its systems can also be extended to access global talent networks to fill gaps.

### **5.3 INTENSIFYING HUMAN RESOURCE DEVELOPMENT AND WORKFORCE TRANSFORMATION**

Intensifying human resource development will result in the needed transformation of both the quality and structure of the workforce. The need for delivering a quality workforce is widely recognised in many of the ongoing Government initiatives. The GTP and 10MP contain proposals aimed at effectively transforming education over time to meet the future manpower needs of a high income economy. The GTP addresses improvement of student outcomes (see GTP, Chapter 8, Pages 149-166) through measures such as increasing pre-school enrolment, developing top teachers, and using high performing schools to lift the general effectiveness of all schools. The 10MP (Chapter 5, pages 196-228) contains measures to raise student competence through adoption of a modern curriculum that emphasises creativity and innovation. Teacher motivation and qualification will be taken to a higher level through an 'Open System' of training. Greater attention will be accorded to public-private partnerships in developing pre-schools and 'Trust Schools'. Through specific projects, the NKEA initiative on education will boost private investment and partnership in education services as a new area with growth potential. Initial progress has been made under the GTP with addressing the shortcomings in human capital development as represented by a successful identification of high performing schools, concrete actions to set up additional pre-school facilities and greater autonomy granted to public institutions of higher learning to improve the quality of graduates.

In addition, the 10MP (Chapter 5, pages 236-241) spells out several policy measures to attract and retain talent, which will be spearheaded by the new Talent Corporation (TC). Key components of the TC mandate should be to centralise the current disparate mechanisms for attracting and retaining high-skill talent, and to address talent demand information issues. The TC work programme needs to be swiftly formulated and the barriers to attracting and retaining talent quickly removed. In particular, the onerous immigration requirements for professionals need to be removed and there needs to be greater flexibility in the residency and work permit requirements for accompanying family members. The TC should also work with stakeholders towards liberalising professional services to create an environment that will ensure adequate, competitive compensation levels.

To better manage unskilled foreign labour, the Government is adopting a series of measures (10MP Chapter 5, page 231; and Recommendations from the Lab on Foreign Labour) to wean



industries off low-cost workers. Compliance with International Labour Organisation (ILO)/ International Organization for Migration (IOM) best practices on treatment of migrant labour is critical to dispel Malaysia's reputation for violations of conventions against human trafficking. There should be a better understanding of the needs of foreign labourers by industry and more importantly, greater emphasis on, and transparency in managing the supply of foreign workers. The number of foreign labour contracting agencies must be rationalised. Agencies and employers which violate workers' rights must be promptly and strictly penalised. In the case of undocumented migrant labour, enforcement should focus as much on the employers as on the workers themselves. While recognising sectoral differences, measures to manage foreign labour should include a simplified active levy system and a gradual tightening of the limits on the number of unskilled foreign workers allowed.

For Malaysia to graduate to high-value added industrial activities, "technical middle management" capacity needs significant upgrading. Higher technical middle management capacity will help significantly in the innovation improvement measures discussed in Chapter 3. University graduates destined for technical middle management must be proficient in all nine "technical readiness levels" from product design, to testing and marketing. The training programmes will need to be sector-specific. Considerable input from industry and training provided not by academics but by industrial specialists and practitioners is essential. Technical training provided specifically for the Electrical and Electronic industry by the industry-funded Penang Skills Development Centre can be replicated in the other State Centres throughout Malaysia.

The NEAC supports the Government's 10MP policies aimed at raising the labour force participation rate as an offset to reduce foreign labour dependence. In relation to this, legislative reforms should reduce obstacles for female participation in the labour force while establishing the requisite safeguards. Conducive policies should be developed in coordination with employees to address, among others, child-care requirements.

In general, the NEAC agrees that many of the Government's ongoing education reform initiatives are a step in the right direction and should be implemented consistently. However, in addition to the GTP's focus on high performing schools, the broad policy thrust should also address poor performing schools, especially those in poor or rural areas. Extra resources and effort must be devoted to ensuring that the benefits of education services (together with medical and social services) reach the poorer segments and more remote locations. School facilities in rural areas should be brought up to par with those in urban areas. Generous incentives can be provided for gifted teachers to relocate to rural areas or poor urban neighbourhoods.

This report focusses on the following specific human resources development and labour policy actions. The first is to deepen the Government's understanding of the factors influencing current and future skills demand. The NEAC reiterates the need for feedback as the basis for policy adjustments, ensuring that policy implementation is impactful and effective, leading to a quality workforce structured to suit industry needs. The information and feedback will inform the design of the remaining recommended policies focussed on up skilling and upgrading the workforce to meet the demand.

### ***5.3.1 Policy Measure: Undertake a Labour Market Forecast and Survey Programme***

Today there is no single comprehensive and nationally accepted source of information in Malaysia about the labour market structure, its prospects and its potential. This information gap must be corrected.

A comprehensive study of the labour market in each sector of the economy and the segments within each sector should be undertaken. This will form the basis for a thorough forecast of workforce demands for each industry sub-sector, covering the categories of workers and the variety of skills and experience required. The forecast will serve the present needs and future needs as the country moves up the value chain. The proposed study will consider global and regional labour market developments to capture broader market dynamics in which Malaysia will be competing.

This labour market forecast initiative should be championed by MOHR. To ensure sustainability, a Centre of Excellence in Labour Market Studies should be established within a leading research centre or university. The output of this centre should feed into the education system and worker training schemes to generate a quality workforce with the right skill sets.

In this connection, the Department of Statistics will also have a crucial role to play. Other than full participation in the labour market survey, there would be a need to review the overall policy on sharing key economic data and other social statistics with the general public, in particular researchers. There have been too many instances where access to essential data has been denied, including legitimate requests from multinational institutions like the World Bank. The Department of Statistics should adopt best practices in the sharing of data and statistics, including the application of charges as a means for cost recovery.

### **5.3.2 Policy Measure: Focus on Up-skilling and Upgrading the Workforce**

The NEAC makes a clear distinction between the training needed for semi-skilled workers and that needed by higher level professionals. Malaysia currently has a workforce of which 80% have only SPM entry level qualification and some 60% are employed in SMEs. Moreover, every year 100,000 SPM holders enter the job market without any skills, which poses a particular challenge for targeting distinctive policies for youth employment programmes through skills training and thus foster their inclusion in the high-income economic development process. The priority for training and up-skilling the workforce therefore needs to focus on SPM school leavers and the unskilled and semi-skilled segments most likely to be displaced by economic transformation.

A series of policy initiatives are needed to prepare the workforce to join the move up to high income status:

- Establish an overall strategy for up-skilling and upgrading the workforce
- Coordinate government agencies, industry and education entities to meet the objectives of the agreed overall strategy (MOHR)
- Consolidate all government-funded and HRDF training programmes under one roof
- Integrate private sector training programmes with those of the public sector
- Establish logistical links between industry needs and the outputs of training/vocational/tertiary entities
- Clarify, streamline, merge and/or better coordinate the Malaysian Qualification Agency (MQA) under MOHE and Jabatan Pembangunan Kemahiran (JPK)
- Extend MQA qualification standards to all industry sectors
- Align and/or integrate certifications developed by MNC and individual corporations with MQA



- Align MQA standards with regional and international practices
- Define and document all skills – technical, trade, vocations, etc. which should be conducted in coordination with industry and consistent with international practices
- Standardise formal certification of the different types of technical, specialised and trade skills industry-wide
- Certify and license skills to reflect qualification and experience and lift wages
- Formalise accreditation requirements, and encourage firms and households to contract services from only certified persons, e.g. provide agreed standardised warranties on services performed by certified workers, or link the use of certified skilled workers to insurance and safety requirements
- Develop a mechanism for industry-wide adoption of wage scales based on certified skills plus experience
- Reverse the trend for conversion of vocational, technical and community colleges to universities
- Involve industry in curriculum development and to ensure that teaching evolves to reflect new technology and processes. Employers should have a greater say in the vocational and skill-training education curriculum. It is essential that a cluster approach be adopted to take advantage of scale economies as well as proximity to industry; e.g. Human Capital Development Initiative of USM-NCIA-Deloitte
- Establish programmes to recognise and support businesses that roll out internship programmes, apprenticeships, on the job training and job placement services
- Establish closer connections between academic staff and industry and deploy industry experts as resource persons in educational institutions – academic staff must have industrial experience or be required to take sabbaticals in industry
- Consolidate and better coordinate training funds available through various government agencies. Government funding should be better integrated with contributions from industry, through cost-sharing and partnership schemes
- Revise the role of HRDF to be more supportive

### ***5.3.3 Policy Measure: Leveraging Women's Talent to Raise Productivity***

Achieving high income will require better attention to and leveraging of women's talents to raise productivity. It also requires the corresponding changes in business models, human resource management, marketing strategies etc. Women's particular talents and attributes in managing change can be harnessed to achieve these goals. Inclusiveness is about changing attitudes to harness talent from all sources. Economic sustainability necessarily involves care for the environment and effective management of finances. Relative to men, women in their daily lives tend to better demonstrate sound environmental protection and financial management practices by stretching each ringgit to meet the essential needs of the family.

The labour market participation rate for Malaysian women is lower than in other countries, despite a higher level of education. Within the public sector, the position of women has shown marked improvements where their presence in top management has grown to 30.5% in 2010 compared to 7% in 1990; while in Parliament female Dewan Rakyat representatives have doubled to 10% over the same period. Further purposeful improvements could be made; for instance in the education sector, where 71% of teachers are women, but only 44.8% of headmasters

are female. Moreover, the situation in the private sector is also not as encouraging, where with the exception of some high profile positions, women still occupy a small proportion of corporate decision-making roles and growth in their numbers has been slow. Only 6.1% of Malaysian corporate directors and seven of the CEOs of Bursa's 100 biggest companies are women (2008).

Unleashing the talent of women would contribute immensely to the outcome of the NEM. The participation rate of women in the economy must be raised through supporting policies. The 10MP has introduced measures to mainstream women's issues and has set targets to be met by 2015 (10MP Page: 178-181). The NEAC supports the government's plans to empower women to enhance their economic contribution to the nation. Whilst there is a need for the public sector to be more pro-active, the private sector too needs stronger directional initiatives in promoting participation of women through the following measures:

- Implement workplace policies as described above to allow for greater flexibility in working hours and the provision of child-care support
- Introduce policies requiring all Ministries and agencies to ensure that gender issues are part and parcel of their policy design. All programs must incorporate the gender element
- In both the public and private sectors encourage the introduction of Gender Impact Assessment (GIA). Implementation of the broad-base requirement of mainstreaming gender into public policy design and implementation can be facilitated when regular GIAs are conducted in all Ministries and agencies. It will provide the structure and tools to assess compliance with the gender mainstreaming directive in policy programmes
- Efforts should focus on encouraging private sector firms to place more women executives in decision making positions. Women's special capacity for recognizing talent and building a culture to sustain teamwork, contributes significantly to higher productivity. The driving principle is that higher representation for women in decision-making positions should be a business decision based on merit and performance and not merely a diversity exercise.



CHAPTER

6

# NARROWING DISPARITIES



## 6 NARROWING DISPARITIES

### 6.1 STRIVING FOR INCLUSIVENESS THROUGH MARKET FRIENDLY AND TRANSPARENT AFFIRMATIVE ACTIONS

The NEM recognises that limited opportunity to benefit fully from economic progress breeds resentment between and within segments of the population, whether urban or rural, in all regions, and particularly in Sabah and Sarawak. For this reason, the NEM emphasises pro-poor, inclusive growth which addresses income disparities and social inequality while lifting the disadvantaged population out of poverty. We must consciously recognise the strength of Malaysia's unique multi-racial social order. Our ethnic diversity will always be with us. We should preserve and leverage it to achieve high income for all.

Reducing inequality of opportunity is one of the defining features of the NEM (SR15). It is imperative to address the persistent inequality within and between ethnic groups, between regions, and between urban and rural areas. The NEAC acknowledges that the key challenge is to attain a balance between the special position of Malays and the natives of Sabah and Sarawak, and the legitimate interests of other communities, consistent with the Federal Constitution.

### 6.2 AFFIRMATIVE ACTION AND THE FEDERAL CONSTITUTION

Equality before the law is safeguarded in Article 8 of the Constitution. The special position of the Malays and the natives of Sabah and Sarawak, and the legitimate interests of other communities are set forth in Article 153 of the Constitution. The responsibility of the Yang di-Pertuan Agong over this matter is also set forth in Article 153. But above all this legal posturing, the tussle between the special position and legitimate interests must not lead to a breakdown in civil society which will be detrimental to all. As discussed above, the key challenge of inclusive growth is the design of a balanced set of measures that will address inequalities.

Article 153 of the Constitution has been the source, or foundation, of affirmative action. But some form of affirmative action has been in place since the mid-1940s even before Merdeka.

Recognising its safeguards and conditions, the NEAC's affirmative action policy is consistent with, and subject to Article 153. More specifically, the NEM does not advocate the removal of the special position of the Malays and the natives of Sabah and Sarawak and the legitimate interests of the other communities. However, the NEM does strongly seek to modify the manner in which the interests of all Malaysians are promoted through pro-poor, inclusive growth by means of market friendly and transparent affirmative action.

Article 153 of the Constitution clearly entrusts to the Yang di-Pertuan Agong the task of safeguarding the legitimate interests of the other communities. Provisions of Article 153 as applied to the other communities specifically shield them from the deprivation of public office, scholarship, educational or training privilege, special facility or of any right, privilege, permit or licence (including the renewal of permit or licence) to which they have been entitled. Article 153(9) also states that Parliament shall not restrict business or trade solely to Malays or natives. There are other parts of the Constitution, including Articles 89(2) on Malay reserve land, 89(4) on non-Malay land, 12(1) on discrimination in educational institutions which should also be considered together with Article 153. The affirmative action of the NEM has not violated any of these parts of Article 153.

### 6.3 MARKET FRIENDLY AFFIRMATIVE ACTION

Affirmative action has progressed successfully with an exemplary reduction in absolute poverty and notable advances in reducing economic functions by race. But this progress has also entailed fundamental negatives. The implementation of affirmative action has propagated and embedded a distributive and entitlement culture and rentier behaviour. An insufficient number of qualified bumiputera firms with the requisite capital resources have encouraged the establishment of spurious fronts. Excessive use of ethnic quotas has descended into acceptance of less qualified recipients and bred inefficiency. Preferential pricing and quotas have led to rent-seeking market distortions or perversion of the objectives. Recipients of share capital sell off their allotments and reap unearned windfall benefits. Deserving entrepreneurs have been marginalised and have little access to finance. Rent-seekers do not really create wealth, or add to economic growth. Rent-seekers are engaged in unproductive activities and can add sizeably to the cost of doing business. They are closely associated with the growth of bribery and corruption in the economy.

In light of the persistent inequalities, the relatively economically disadvantaged should be given the opportunity to overcome their disadvantaged position through the continuation of the affirmative action policy. But affirmative action must be revised and reformed by drawing lessons from, and by removing the negatives and flaws from past practices. The new approach will be a “market friendly affirmative action” that will ensure, wherever possible, that its implementation will not undermine the functioning of the market. Distortions in the market can lead to a misallocation of resources and reduce efficiency. It can be assumed that a market that is perfectly competitive is free from distortions but the existence of perfect competition is rare. Nevertheless, market-friendly affirmative action must minimise market distortions to allow the market to function as close as possible to perfect competition.

Market friendly affirmative action should ensure that it does not violate, or negate, the workings of the market. Nor should it cause, contribute or perpetuate distortions in the economy. Growth can be maximised if resources are used efficiently and prices are allowed to signal where and how resources should be utilised to maximise profits. Entry into, and exit from markets should not be constrained. Land, labour, capital and entrepreneurship should be allowed to flow in and out of the economy with minimum restrictions.

However, markets can at times malfunction with or without any form of affirmative action. Monopolies and collusions can hinder efficient market function. Excessive risk taking can lead to crises. Markets can fail when manipulated by interest groups that covertly seek to maximise their own interest. In such cases government intervention is necessary to regulate and correct the failures. However, government intervention can also exacerbate market failure. Excessive protection for reasons other than affirmative action can contribute to market distortions.

The market friendly affirmative action in the NEM advocates the use of transparent procedures and criteria to promote capacity building and the elimination of approaches that contribute to rent-seeking behaviour. The NEM also seeks to encourage reward based on performance and to foster greater competition by removing excessive protection and promoting sectoral liberalisation. Raising competitiveness and productivity is critically dependent on reward based on merit and effort, and not on other unwarranted criteria.

#### 6.4 ADDRESSING THE BOTTOM 40% OF HOUSEHOLDS

The NEM's inclusiveness objective is focussed on reducing disparity and uplifting the bottom 40% of households. Programmes to assist the bottom 40% shall be ethnically blind without any market distorting elements such as quotas or preferences or entitlements to access to financial resources, jobs, contracts and licences. The programmes will be implemented based on the needs and merit of the applicants and will be focussed on capacity and capability building.

The reference to the bottom 40% of households in 2009 has been given further prominence in 10MP whose key features are as follows:

- **Income threshold.** Households in the bottom 40% have an income of less than RM2,300 per month with a mean income of RM1,440. Income has risen over time. Whereas in 1990 60.6% of households had income below RM999, by 2009 this had fallen to 7.4% of households. 73% of the bottom 40% are bumiputera households.
- **Numerical size.** In 2009 there were 2.4 million households in the bottom 40% with an average size of 3.8 persons per household. This implies there are approximately 9 million persons in this low income household category. Of this, 7.6% are classified as poor and 1.8% as hard-core poor.
- **Geographical location.** 51.4 % of the bottom 40% resided in urban areas; 48.6% in rural areas. 65% were in Johor, Kedah, Perak, Sabah, Sarawak and Selangor. Among these, Kedah has the highest proportion; 57.6% of households in Kedah had incomes below RM2,300 per month.
- **Education status.** 52.3% of the bottom 40% had no school certificate while 25.4% had up to SPM and 17.9% secured the PMR.

Access to better education, health and housing facilities will be critical in raising the income and living standards of the bottom 40%, as more than half of that group is without formal education. Heavy emphasis must be put on providing educational and training opportunities for them to enhance their capabilities. By focusing pro-poor growth policies on the bottom 40% of households, the NEM will benefit overwhelmingly the bumiputera community, given that they form almost 73% of the bottom 40% of households.

Focusing on the bottom 40% of households, the NEAC advocates the key measures below (**Table 6.1**). The NEAC also believes that targeted special programmes for certain groups outside of the bottom 40%, particularly those SMEs within the BCIC, should continue. Preferences under such special programmes must be market friendly, transparent, needs- and merit-based.



**Table 6.1 – Summary of Policy Measures for Narrowing Disparities**

Reduce Income Disparity and Regional Differences
<ul style="list-style-type: none"> <li>• Establish an overarching policy on social assistance programmes. The Ministry of Women, Family and Community Development should be the coordinating agency for developing and monitoring this policy</li> <li>• All involved ministries and agencies adopt a single comprehensive database based initially on e-Kasih</li> <li>• Establish additional social assistance programmes on transportation and housing, which constitute the bulk of low-income household expenditure <ul style="list-style-type: none"> <li>➢ Increase the mobility of the bottom 40% for better employment opportunities by subsidising public transportation with savings from rationalisation of other government subsidies</li> <li>➢ Set up state-level Housing Boards to plan, develop and manage housing schemes for the bottom 40%</li> <li>➢ Shift the present focus of such schemes from ownership to leasing with an option to purchase at the end of a stipulated lease period</li> <li>➢ Offer loans through EPF for the housing needs of the middle 40%, that are repayable through deductions from employees' monthly contribution, which is neutral to cash flow</li> </ul> </li> <li>• Enable the bottom 40% to break the cycle of poverty through education <ul style="list-style-type: none"> <li>➢ Offer incentives to teachers for better performance and willingness to teach in rural/remote areas</li> <li>➢ Provide safety nets for parents to keep their children in school</li> </ul> </li> </ul>
Target Programmes for the BCIC
<ul style="list-style-type: none"> <li>• Continue specific programmes for bumiputera SMEs only</li> <li>• Focus on capacity building programmes</li> </ul>

## 6.5 REDUCING INCOME DISPARITY AND REGIONAL DIFFERENCES

The NEAC takes note of the many policy initiatives which have been set out in the 10MP to address the needs of the bottom 40% and which are consistent with the NEM (see Chapter 4, pages 140-164). They include improving the quality of life of rural households and enhancing the economic participation of the urban poor. During the 10MP plan period, the well being of the urban bottom 40% households will be addressed through capacity building programmes to improve their income and overall quality of life.

Programmes to increase the incomes of the rural households will focus on upgrading their skills, linking them to employers in nearby clusters and cities through better connectivity as well as providing support for self employment, micro-business and small scale industries. Programmes that cannot reach the hard core poor in remote areas would need to fall back on enhanced social welfare. In line with the NKEA for Agriculture, efforts will be undertaken to transform agro-based rural activities anchored upon market needs, economies of scale and value chain integration. Capitalising on the strength of the rural areas in natural resources would involve enhancing productivity and sustainability through the adoption of modern agricultural technology and adopting a demand-driven approach, for example, in the expansion of contract farming.

The needs of the children in low income households will be given prominence. An enhanced social safety net will mitigate impact on vulnerable groups. There will be a special focus on the bumiputera community in Sabah and Sarawak and the Orang Asli on the peninsula. Special assistance will be provided for residents of new villages and estate workers.

#### ***6.5.1 Policy Measure: Establish an Overarching Policy on Social Assistance Programmes***

There is a plethora of social assistance programmes dispersed across different ministries and agencies generating unnecessary overlap and leading to under coverage for certain groups in need. The NEAC recommends the Ministry of Women, Family & Community Development (“KPWKM”) be designated as the lead coordinating body for all other ministries and agencies in developing a holistic social programme. Within the budgetary envelope, KPWKM should be tasked with drawing up the overarching social assistance direction, policies, and high-level programmes, which would then be translated into specific programmes and projects by the respective implementing ministries and agencies.

#### ***6.5.2 Policy Measure: Adopt a Single Comprehensive Database Based Initially on e-Kasih***

Currently there is no effective method to determine the total amount of benefits each recipient receives. This results in an inability to evaluate the effectiveness of the wide array of social assistance programmes. It is therefore recommended that all ministries and agencies carrying out social assistance programmes adopt a single comprehensive database, based initially on the existing e-Kasih programme.

Under KPWKM’s lead, all ministries and agencies will ensure that all Malaysians within the poverty line are registered in the single database and that comprehensive data on each household is accurately recorded and periodically updated. Apart from household income, the data should include the age, gender, physical and health condition, level of education or skills, and current employment of each member, as well as standard of accommodation and location, including proximity to public amenities. Such a comprehensive database will allow for better structuring and design of programmes as well as more accurate monitoring and evaluation. The progress and weaknesses in the programmes should then be reported back to the KPWKM to enable strategic and coordinated corrective actions.

In line with the principle of transparent and market-friendly affirmative action, the implementation of social assistance policies and programmes must be transparent to ensure equal opportunities for all Malaysians. Every officer involved in such social assistance programmes must practice the 1Malaysia concept to ensure that programmes are properly implemented regardless of ethnicity.

#### ***6.5.3 Policy Measure: Address the Transportation and Housing Needs***

One of the main concerns for the bottom 40% is the provision of affordable housing. The current national housing policy obliges housing developers to allocate 30% of the units in housing projects of a specific size to low-cost houses. This poses a challenge when the development involves prime land and medium- to high-cost housing. The NEAC proposes that state level Housing Development Boards be established to work with developers and other stakeholders on strategic policies to address the housing needs of the bottom 40% of households.

To address the issue of those within the bottom 40% who are at risk of default or are unable to afford the already low monthly installments on the purchase of low-cost housing units, the Government could consider providing them a more affordable option by offering a lease on the low cost unit with an option to purchase at the end of the lease period. This option would need further study in consideration of the growing low-income household debt burden and the possible large financial impact on government expenditure. For households in the middle 40%, the NEAC recommends that the EPF be empowered to offer loans to purchase medium-cost houses which are repayable through deductions from monthly EPF contributions.

Another significant portion of household expenditure goes to transportation costs. The NEAC recommends that savings from rationalisation of government subsidies be channelled towards easing the transportation cost burden on households in the bottom 40% who are the major users of public transport. The approach would need to be further analysed, but a simple and cost-effective method would be a general subsidy for public transportation on the premise that the overwhelming proportion of urban users of public transport would be from the bottom 40%. An efficient and affordable urban public transportation system would also encourage more city residents to choose not to drive their own vehicles, thereby reducing traffic congestion and pollution within cities.

With identified NKEAs and proposed development by clusters, better job opportunities will be more readily available in and around these clusters (e.g. Klang Valley, state capitals and major towns). Rural households in the bottom 40% need to be given better access to higher paying job opportunities in these cluster developments. A subsidised and efficient public transportation system will enable rural residents to travel to these locations for employment. For the rural poor that do not rely on public transportation, cash grants via e-Kasih can include partial coverage of fuel costs for personal vehicles.

#### **6.5.4 Policy Measure: Break the Poverty Cycle through Education**

Apart from providing affordable transportation to access better job opportunities, education and skills training will be crucial in ensuring that people are qualified for the jobs. The number of vocational, technical and community training institutions will be increased under the 10MP. Similarly, special consideration for placements in matriculation centres and public universities should be given to students in the bottom 40% of households.

An important factor in ensuring better employment opportunities for the bottom 40% is education. As many Malaysians as possible must complete their basic education through to SPM. The 10MP addresses the issue of school attendance costs and providing for better school facilities throughout the nation which the NEAC fully supports. However, it should be recognized that it may not be economically possible to provide high quality schools in remote inland areas in the Peninsula and especially in Sabah and Sarawak. In such circumstances, the NEAC supports the 10MP initiative to build more hostels to house children from such remote areas and thus present them the opportunity to obtain quality primary and secondary level education.

Households in remote areas that find it financially challenging to send their children to residential schools would need to be provided with adequate financial and social support to ensure that the children remained enrolled in such schools. Such households can be identified and monitored via e-Kasih.

## 6.6 TARGETED PROGRAMMES FOR BCIC

While the market friendly affirmative action of the NEM will focus on the bottom 40% of households, the NEAC believes that targeted special programmes for certain groups outside of the bottom 40% (i.e. those in the middle 40% households) should continue. It was never the intention in the NEM that the existing special programmes benefiting these targeted groups would be immediately terminated.

The 10MP has provisions for enhancing bumiputera economic participation (see 10MP Chapter 4, pages 165-173), which are consistent with the recommendations of the NEM. The 10MP policy initiatives aim at strengthening and nurturing entrepreneurship and creating competitive bumiputera businesses through enhancing capacity and capability. The policy also envisages increasing wealth ownership beyond corporate equity to include other assets and businesses through the pooling of funds and institutional investments; and to promote greater bumiputera participation in high paying jobs.

### 6.6.1 Policy Measure: Establish Specific Programmes for Bumiputera SMEs

The NEAC advocates that the new approach for these special programmes should be market friendly and transparent and support should be granted on the basis of needs and merit. Based on such core principles, these programmes would allow beneficiaries to graduate to become self sufficient and compete in a liberalised environment, without prolonged dependence on such special programmes. Successful bumiputera firms need to be highlighted as champions, whose partnerships with the business community at large, including the GLCs, will raise the performance of the entire BCIC.

The strategy to create more competitive bumiputera SMEs should be made clear from the onset. For this purpose, the NEAC recommends that Government and GLC procurement reservation for BCIC should continue but be targeted for bumiputera SMEs only. It must be recognised that bumiputera SMEs would need to become increasingly competitive as such reservations would be reduced gradually as government procurement expenditure decreases in line with the government's fiscal stance. The eligibility criteria, processes, procedures, and monitoring mechanisms should be strictly transparent, market friendly and based on needs and merit.

### 6.6.2 Policy Measure: Focus on Capacity Building Programmes

Capability and capacity building programmes for sustainability should continue to be provided to bumiputera as well as non-bumiputera SMEs, on the same market friendly principles. Taking into consideration the change in the global economic landscape and the need for bumiputera SMEs to become more competitive, the objective of these programmes should be to focus on building talent, identifying new technologies and enhancing collaboration between bumiputera and non-bumiputera firms as well as with GLCs and MNCs. The effectiveness of bumiputera support institutions (like MARA, PUNB, PNB and others) should be improved through rationalisation and streamlining to reduce duplication and achieve greater accountability. The NEAC strongly recommends that improved efficiency and effectiveness of such support institutions will enable them to progressively expand their remit. These support institutions should identify the possible opportunities for bumiputera SMEs to play a significant role in the development of the 12 NKEAs. The building of the capacity and capability of these SMEs should be geared towards fulfilling their potential within these 12 NKEAs.

## **6.7 THE RELATIONSHIP BETWEEN HIGH INCOME AND INEQUALITY IN THE OWNERSHIP OF ASSETS**

Inequality in the ownership of assets is a key feature of any economy whether it is high income or otherwise. In circumstances where inequality in ownership of assets is compounded by an imbalance based on ethnicity, disharmony can arise. If not adequately addressed, such disparities could be exploited by unscrupulous factions to foment a perception of injustice where none in fact exist.

In many countries, the ownership of financial and other assets such as land and share capital is generally very concentrated, i.e. a small proportion of the population owns a disproportionately large share of assets. However, this ownership structure does not usually drive a nation into discontent, disharmony and, worst of all, open conflict. While encouraging efforts to prevent such disparities from becoming too wide, the spirit of 1Malaysia focusses rather on broad-based efforts to raise collective capabilities and move together towards high income.

On average, far more people depend on wages and salaries for their income than those lucky few living off income from accumulated assets. The NEM SRIs focus on economic opportunities through employment in productive economic sectors that would contribute to raising household income and would tend to narrow the gap between rich and poor. The NEM affirmative action is consistent with this focus.

The contribution to the growth of income from bumiputera ownership of share capital after more than 35 years has not been that significant and sizeable. In the future, with or without a 30% or higher target of bumiputera ownership of share capital, an overwhelming proportion of bumiputera household income growth will come from wages and salaries. Thus, both bumiputera and other communities would be better off if Malaysia is unencumbered by the never ending debates over wealth distribution. After all, before wealth is to be distributed it must first be sustainably generated.

## **6.8 STRENGTHEN INSTITUTIONS FOR INCLUSIVE GROWTH**

The NEAC notes that the 10MP retains the 30% bumiputera corporate equity ownership as a target at the macro level. Achieving this ownership target is to be delegated in part to special purpose vehicles like Ekuiti Nasional Bhd (EKUINAS), PNB, Armed Forces Fund Board (LTAT), Tabung Haji, PUNB and Yayasan Amanah Hartanah Bumiputera. This approach also advocates expanding the discussions on increasing wealth ownership beyond corporate equity to include other assets, particularly real assets and properties (including intellectual property), as well as pooled financial resources and institutional investments. The Government has rightly given prominence to increasing bumiputera representation in high income jobs, professions and higher risks/rewards enterprises (10MP, page 145-148), which moving forward will be a critical element in raising their share of wealth.

The NEAC welcomes the establishment of a high level council announced by the Prime Minister in the context of the 10MP (PM's speech in Dewan Rakyat paragraph 55, page 29) to coordinate and monitor the efficient and effective implementation of the bumiputera development agenda.

CHAPTER

7

# IMPLEMENTATION CONSIDERATIONS



## 7 IMPLEMENTATION CONSIDERATIONS

### 7.1 GAME CHANGE NEEDED IN IMPLEMENTATION MACHINERY

The achievement of the NEM's objectives is dependent upon the sustained, effective and wholesome implementation of foundational policy measures underlying all eight Strategic Reform Initiatives. As discussed in NEM Part 1, confidence in the economy is generated through an open, transparent feedback mechanism that ensures that the policies and projects undertaken for the NEM are delivered against global best standards and practices and in line with the objectives of high income, inclusivity and sustainability. Delivering this huge task requires a game change in implementation machinery compared to the current system.

Successful and continuous realisation of the foundational policy measures is only possible with the presence of dedicated implementation agencies that are supported by an authoritative feedback mechanism to assess and evaluate the effectiveness of the measures. This feedback mechanism also enables adjustments in policy intensity, determination of additional measures, or management of an unexpected situation. Dissemination of information from a transparent monitoring and reporting mechanism is just as critical as having capable implementation units. The rakyat must be kept informed on the progress in attaining the NEM objectives and NKEA goals to sustain their continuous buy-in for bold reform measures. The Government can be steadfast in staying the course when adopting difficult policies by being openly visible in managing resistance from vested-interest and transitory disruptions in the economy.

The NEAC assigns a very high priority to the simple implementation framework described in the preceding paragraph to secure the NEM objectives.

A vast majority of the NEM policy measures underlying the SRIs will ultimately be designed and implemented by government agencies, mostly at the federal level. However, in some instances state and local government units may also be involved. While the Government needs to pursue, with determination, the bold actions to support the ETP, it cannot undertake this transformation on its own. The Government must engage and seek to benefit from the suggestions and diverse opinions of the private sector and the rakyat, including:

- Industry
- Business associations and chambers
- Entrepreneurs
- Professionals
- Unions and Workers' associations
- Academia and think tanks
- Civil society and NGOs
- Political entities

The Government should also draw on the knowledge and insights of international and regional agencies, bilateral entities and international business groups.



## 7.2 TWO COMPONENTS: CENTRAL AGENCY AND INDEPENDENT EVALUATION BOARD

To sustain the momentum and monitor the impact of the NEM policy measures, two separate institutions must form part of the implementation framework.

One is a central agency with a mandate for coordinating the formulation and design of policy measures, particularly if the measures are cross-cutting traversing several implementing agencies. This central body will:

- i. monitor that policy is sequenced and delivered as required
- ii. report back on its impact and effectiveness
- iii. ensure that the different projects and programmes comply or are consistent with global best practices and standards and with each other
- iv. obtain feedback to contribute to policy adjustments and additional measures where needed

The work of this central agency will be reflected in the issuance and dissemination of periodic reports (quarterly and annually) on progress in achieving the objectives of the GTP, NKEAs, 10MP and the NEM. It is expected that this central agency will seek feedback and interact with the same array and set of stakeholders described in the preceding paragraph.

The second key institution is an independent assessment and evaluation board, whose main task would be to undertake an in-depth review every two years of the impact and relevance of the policy measures underlying the SRIs towards achieving the objectives of the NEM.

This evaluation board will have a very specific terms of reference and will comprise experienced and well-known professionals, including former members and advisors of the NEAC. It will only be constituted over the period (say three months) for undertaking the evaluation and drafting a report. The information and data requirements for the evaluation will be defined in the terms of reference of this independent board and be collected and collated by the central agency for delivery to the board when the assessment commences.

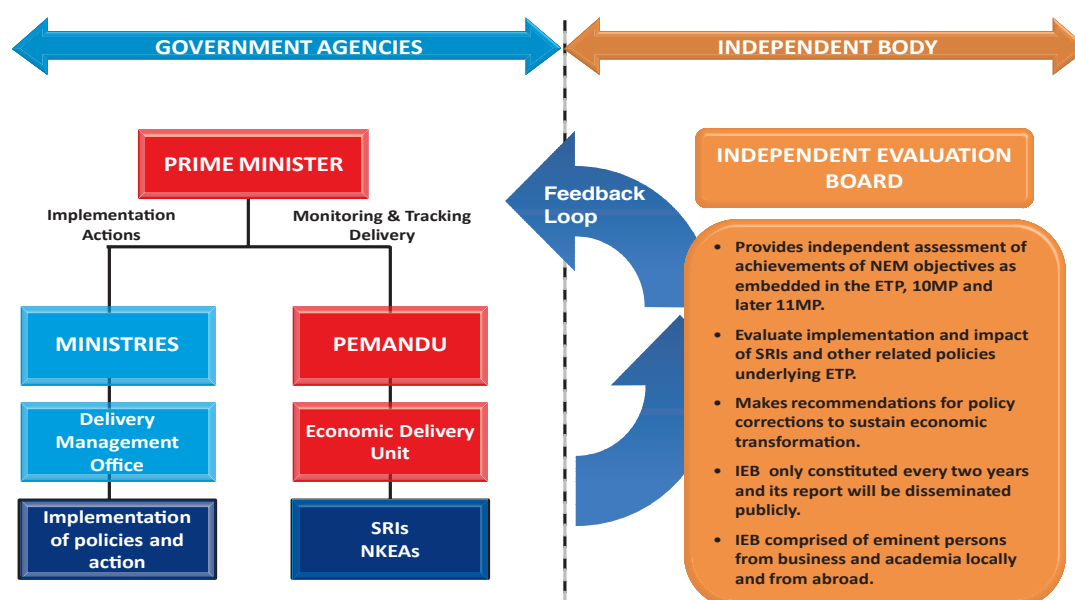
The NEAC is pleased to note that in the 10MP as part of policy initiatives for “Transforming Government to Transform Malaysia” there are specific provisions aimed at strengthening the mechanisms for designing, monitoring, reporting and making adjustments to policies underlying the GTP, ETP (NKEA/NEM), and 10MP (Chapter 1, page 31; Chapter 7, pages 342-343). A proper delineation of the functions of these entities, supplemented by the periodic assessment of an IEB as described above will suffice to ensure confidence that the transformation policies would be consistently implemented to achieve the NEM objectives.

In this regard, the NEAC proposes the following recommendations to make the policy monitoring and evaluation process more effective (**Figure 7.1**):

- As already contemplated in 10MP, PEMANDU will be the central agency with a mandate for coordinating the formulation and design of policy measures, monitoring their implementation, and assessing impact and effectiveness for the purpose of suggesting remedial measures if any are needed.

- The Government should make provisions for setting up an independent assessment and evaluation board, the IEB, whose main task would be to undertake an in-depth strategic review every two years of the impact and relevance of the policy measures underlying the SRIs.

Figure 7.1 – The Implementation Framework



### 7.3 PEMANDU'S ROLE AS THE IMPLEMENTATION CENTRAL AGENCY

As the central agency, PEMANDU will be faced with several implementation challenges which include:

- **Complexity** – Implementing policy change is often not a logical, linear process, but one in which activities are fragmented and multi-dimensional, both in scope and in sequence. Impacts and changes resulting from the activities can be unpredictable and can vary over the life of the implementation effort.
- **Organisational Scope** – Responsibility and authority for the various components of the implementation programme are distributed across multiple entities within the various segments of the economy. There can be no single organisation responsible for all the elements of the implementation. As such, the success of the programme depends as much on collaboration and buy-in as on traditional command and control management.
- **Global Standards and Best Practices** – there must be an institutional unit within PEMANDU that is dedicated to check that projects, programmes and policies are consistent with global best practices. This can be done from the benchmarking against the G20 Financial Stability Board Core standards, and a continual review of how these could be implemented domestically. Recognising that not all standards can be implemented due to domestic consideration, the Unit must at the same time draw attention to the policy makers of where the gaps are and why there should be a timeline to adopt global standards by 2020. This will help the work of the IEB discussed later in this Chapter.
- **Impact** – The impact of the transformation programme will be felt by the various stakeholders in different ways. There will be 'winners' and 'losers'. Even if ultimately everyone will

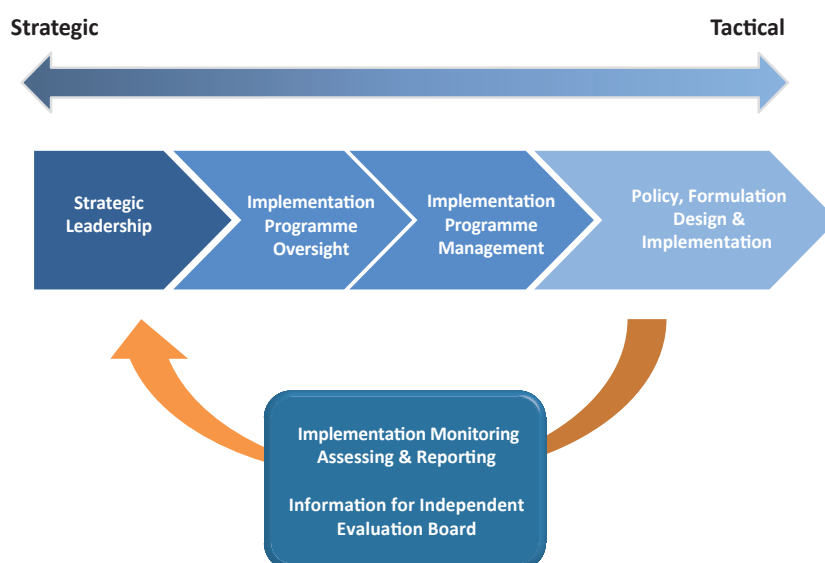
benefit from the changes, in the short term there will be segments of the economy that will 'lose' and thus will work to resist the changes. Those who perceive that they will lose are often invested in the status quo and may mobilise powerful political forces to resist any change.

The following key principles would serve to mitigate the challenges described above:

- **Mission Integration** – In order for implementation to be successful there must be “unity of purpose”. All stakeholders involved in the process must perceive and adopt the goals of the underlying policies as their own. Every organisation and individual will have a specific role to play in its implementation. Those roles must be fulfilled objectively and effectively. The functions of PEMANDU must be based on a mission-centric collaboration and an information-sharing model to overcome the considerable challenges. A significant element will involve a continuous communications programme aimed at breaking down resistance to the changes and mobilising sources of support from among the various segments of the economy.
- **Results and Impact Focus** – Large government programmes often include benefits-realisation models that are intended to measure the progress and report on the status of the implementation activities. However, these models have historically focussed on the ‘outputs’ of the projects or programmes rather than the ‘outcomes’ and the impact of those outcomes. Consistent with the 10MP emphasis on outcome-based approaches for planning, resource allocation, monitoring, and evaluation, PEMANDU must be focussed on achieving the desired outcomes.
- **Transparency and Accountability** – The ETP seeks to improve the lives of all Malaysians. It has been announced as a broad-based and inclusive transformation programme that will require commitment and sacrifice from some segments of the rakyat. As such, it will be critical to implement policies in a completely transparent manner. Responsibility, authority, and accountability must be assigned and publicly announced. The agencies and individuals responsible for implementation are directly accountable to the Government’s executive leadership, but they are ultimately accountable to the Malaysian people. As such, an independent, transparent public reporting process must be put in place.
- **Monitoring and review** – Once authority, responsibility, and accountability for the implementation programme are assigned and announced, rigorous, regular, systematic processes must be put in place to monitor both the progress of the activities and their outcomes and impacts. The results must be continually reviewed against the expected goals to ensure alignment. The monitoring and review functions should be performed internally and by an independent entity to ensure accuracy and objectivity.

As discussed above, there are several facets to the functions of PEMANDU (**Figure 7.2**) which are:

- i. Managing overall strategic direction
- ii. Monitoring, assessing and reporting on policy implementation
- iii. Interacting with implementation agencies on policy formulation and design
- iv. Interacting and collecting information for the IEB

**Figure 7.2 – Operationalising PEMANDU's Functions**

### **7.3.1 Managing Strategic Direction**

PEMANDU must ensure that the national leadership remains active and committed to the transformation programme, which is the anchor for successful implementation. The leadership must be committed to following through on the implementation of individual policy measures. Sustained attention and energy are required of the Prime Minister, who should be seen as the ultimate architect and biggest proponent of the transformation. During the detailed programme design and implementation launch stages, a great deal of work on consensus-building and on overcoming resistance needs to be done. PEMANDU must muster the leadership at each stage, especially when there is a need during the implementation period for policy adjustments which national leadership will need to consider, endorse, and provide ongoing support.

### **7.3.2 Monitoring and Reporting**

PEMANDU must put in place an overarching coordination framework for all of the policy initiatives to monitor implementation progress, resolve any implementation obstacles, track results, and recommend adjustments as needed. There must be high-performance management function capabilities that help to keep the implementation of each of the programme component on track and within budget. PEMANDU must respond to cross-project issues and intra-programme dependencies and communicate with implementation agencies across project teams. In coordination and monitoring activities across related institutions and stakeholders, a major function is the responsibility for collecting and recording in the appropriate systems, the primary data and other relevant information on programme progress or barriers that will be used for programme progress reporting and internal assessment purposes.

### **7.3.3 Policy Formulation and Design**

PEMANDU must have an efficient mechanism for interacting with implementation agencies for the formulation and design of each policy initiative, especially if policies cut across implementing agencies to identify overlaps and integration requirements. As such, PEMANDU must have executive authority to allocate implementation responsibility among implementing agencies, and to allocate human, financial, and material resources to implementation initiatives. As new policy decisions are made by the national leadership, PEMANDU together with implementing

agencies will translate them into programme components and assign them for implementation. Consideration will need to be given to the regulatory, organisational, financial resource and time frame requirements. **Table 7.1** summarises this process.

**Table 7.1 – Requirements of Implementation Process**

Category	Process
<b>Regulatory</b>	Changes to laws, regulations, decrees, orders, etc. are promptly enacted by the appropriate authorities in the prescribed manner and within the prescribed timeframes.
<b>Organisational</b>	The specific organisational and activity framework are defined for each of the policy measures (implementation roadmap), which may require further detailing by the implementing agencies. Any required new institutions are established, or changes to existing institutional structures made, and responsibilities and accountabilities defined.
<b>Financial Resources</b>	The impact on revenue and expenditure flows are assessed, and budgets are allocated for the resulting organisations and programmes.
<b>Programmatic</b>	Ensuring that specific programmes or projects defined under the policy initiative are undertaken within the prescribed schedules and allocated resources.

#### **7.3.4 Relationship with Independent Evaluation Board**

PEMANDU will coordinate and interact with the IEB. PEMANDU's tasks will include the collection of information needed by the independent strategic review and impact assessment process.

### **7.4 THE FUNCTIONS OF THE INDEPENDENT EVALUATION BOARD (IEB)**

The Government machinery, through PEMANDU, will be the primary driver for the implementation programme and will conduct its own monitoring and assessment of programme progress, particularly focussing on the delivery and impact of policy measures.

In parallel, the IEB will undertake an independent, strategic level review of the impact, success and relevance of the SRI policies underlying the transformation programme. The review will assess the pace of policy implementation, and if the NEM objectives are being achieved. Some specific research and analysis may be required to support the review, and these will be determined by the independent assessors. The review will also include recommendations for policy adjustments or additional policies in the face of unforeseen developments based on that analysis. In essence, this independent, strategic level review is the robust feedback mechanism described in the NEM report of March 2010.

In order to ensure sustained objectivity and independence, the IEB should be accountable to the widest possible set of stakeholders - the Malaysian people. In its purest form, the IEB will be the people's eyes and ears on the transformation programme to ensure that it stays in line with the strategic intent. As such, it must operate in a completely transparent manner and publish its findings and recommendations through independent channels. Principal aspects of the IEB are described in **Box 7.1**.

### **Box 7.1 – Terms of Reference for Independent Evaluation Board (IEB)**

#### **Description, Purpose and Scope**

1. Provide independent, nonpartisan information, analysis and advice to the Prime Minister and the Government of Malaysia on strategic actions to achieve the NEM goals of high income, inclusiveness and sustainability.
2. Review and evaluate the transformation policies, initiatives and actions by the Government of Malaysia given the prevailing and prospective economic landscape every two years; and in the process, recommend new or redesigned policies if necessary – publishing views, findings and recommendations in an ETP Results and Impact Report.
3. Consults and engages stakeholders as necessary.

#### **Establishment of the IEB**

1. Established by and reporting to the Prime Minister for a period through 2020 with provisions for future extensions.
2. The mandate of the IEB should delineate clearly its authority, roles and responsibilities.
3. As an autonomous body the IEB should be apportioned a dedicated budget.
4. The IEB shall commence its first evaluation no later than September 2011. The chairperson and remaining IEB members should be appointed by early 2011 to develop a work programme, including arrangements for the second evaluation in 2013.
5. The IEB work programme will be developed in coordination with EPU, which will also provide support to the IEB as required.

#### **Qualifications for IEB Members**

1. No more than six members who should:
  - Be prominent and reputable economists with experience in academia, think tanks or international organisations; or
  - Have in-depth Malaysian government experience, ideally a former senior bureaucrat, or
  - Have experience in Malaysian top-level business leadership.
2. Familiarity with the NEM as embedded in the ETP, NKEA, 10MP, 11MP and associated GTP.
3. Have a good understanding of the Malaysian socio-political and economic landscape.
4. Initial Board members will be appointed by the Prime Minister with staggered terms. Subsequent members will be recommended by IEB for appointment. IEB members will not serve for more than three evaluation cycles.
5. The IEB will include ex-officio members of one senior staff each from EPU and PEMANDU.

**Key Deliverables**

1. Publish, every two years, the ETP Results and Impact Report. The report will address the economic situation in relation to the goals of the NEM, assess progress since the last evaluation, review current and proposed policy initiatives relative to the SRIs, recommended policy changes or additional policies, discuss risks and outline the scope to guide the next evaluation.

**Key Information to be provided by PEMANDU to the IEB**

1. Information on NEM-related SRI policy initiatives and other associated measures designed and implemented by PEMANDU and implementing agencies.
2. Information shall be made ready by the deadline as determined in the IEB work programme.
3. As a minimum, information on each policy initiative shall comprise:
  - a. An overview of the rationale for the policy measure and the risks of inaction.
  - b. Comprehensive description of policy measure and any adjustments made.
  - c. Enablers and barriers to policy measure.
  - d. Intended impact and outcomes of policy measures and alignment with NEM goals.
  - e. Stakeholder assessment – feedback and nature of any resistance encountered.
4. Any other information that may be requested by the IEB.

**CHAPTER**

**8**

# **FROM VISION TO RESULTS**





## 8 FROM VISION TO RESULTS

The actions and policy measures recommended and described in this report represent a key design component of Malaysia's Economic Transformation Programme. The NEM, defined by the broad policy directions in the NEAC's first report and the SRI policy measures outlined herein, provides a focussed policy framework that, together with the recently-completed NKEA, form the substance of Economic Transformation Programme. The ETP, the on-going GTP, and the corresponding programmes and projects defined in the 10MP complete the full blueprint for the national economic transformation programme that, under the 1Malaysia banner, will propel Malaysia to high income status by 2020.

Timely and effective implementation of the SRI policy measures outlined in this document will ensure the achievement of the objectives under each of the strategic aims: reinvigorating the private sector, enhancing innovation, public sector transformation, intensifying human capital development, and narrowing disparities in the Malaysian economy. However, the best designs and plans, based on even the noblest intentions, are meaningless unless the prescribed actions are undertaken and the results realised. While the NKEAs focus on sectors and industries that will drive economic growth, its initiatives will face the same constraints and obstacles as those attempted in the past unless the foundational NEM SRIs are implemented simultaneously. Similarly, the SRIs themselves are interdependent and must be implemented in a holistic and comprehensive manner.

With the completion of the transformation blueprint, the nation's focus, energy, and efforts must quickly turn to the implementation challenge. Time is of the essence. Since independence, Malaysia has succeeded in building a globally-recognised national brand as an investment destination and business hub. Protecting and sustaining that brand will be much easier than re-building it if the erosion continues and we are overtaken by competitors.

Given the depth and the extent of the transformation, the nation's total commitment is going to be needed at the leadership, organisational, and individual levels. The Prime Minister has already demonstrated his commitment with the acceptance and announcement of the NEM and the dedication of substantial resources to the development of the SRIs and the NKEAs. The Government's on-going commitment can be further demonstrated by the preparation and announcement of an initial 'Big Push', a critical mass of the policy measures defined in this report to be immediately put in place. First and foremost among those policies should be the social safety nets and other protective measures designed to cushion the most vulnerable from the impact of the changes.

Once the programme is announced, the onus falls to the Government's implementing agencies, the nation's businesses and enterprises, and each individual to play their respective roles. PEMANDU has been assigned the pivotal role as the overall coordination, management, and oversight agency for the national transformation programme. It will work in hand in hand with the numerous government agencies responsible for the implementation of the specific policy measures. For PEMANDU and the other agencies, the task is clear. They simply need to tackle their work in a focussed, organised, and effective manner. It is after all, their purpose. While by its very nature, private enterprise is driven by the profit motive and inherent self-interest, the desired transformation calls for an element of attention to the greater common good and the interests of the broader community. Businesses within some segments must be prepared for limited sacrifice. On the individual level, each citizen of our great nation, irrespective of

race, ethnicity, religion, or gender, will need to look past what sets Malaysians apart, focus rather on our common interests, and work together towards the success of the transformation and our collective prosperity.

**APPENDIX**

**A**

# **POLICIES FOR THE E&E SECTOR**



## APPENDIX A: POLICIES FOR THE E&E SECTOR

The E&E sector is a key driver of the Malaysian economy, contributing RM288 billion in exports in 2007, which accounted for 61% of manufacturing exports and 47% of gross exports of the country. It is the single largest contributor to the manufacturing sector (over 33% of output) and employs more than 500,000 workers or 5% of the total workforce in the country. Most of the approved investments in the manufacturing sector for the past ten years have gone to the E&E sector.

A distinguishing characteristic of the E&E sector is the fact that it is totally private sector driven, is global in nature, and is highly technologically grounded. While the focus of government initiatives thus far has been on individual companies and their requirements, there is a strong need to look at these companies as part of a technology platform ecosystem and understand how these economic activities can be expanded, integrated and linked to the local economy.

The industry is dominated by foreign MNCs. The role of local companies has been largely confined to vendors, suppliers or outsourcing partners. Despite this sector being in Malaysia for more than 35 years, there is no internationally acclaimed Malaysian company in this field. In recent years, as the cost of skilled labour has increased or tax incentives expired, the MNCs have explored alternative competing locations. Although they continue to grow and deepen their roots in Malaysia, there is a real possibility that if the operating environment is not conducive, many of the higher value added activities could be re-located elsewhere.

Conversely, the development of the right environment (i.e. technology and product clusters) will promote the quantitative and qualitative growth of these companies, and deepen their integration into the local economy. A key drawback of the E&E sector is that it has limited integration with the domestic economy and weak backward linkages between MNCs and local companies. The E&E sector is also geographically dispersed spread over four clusters, namely Penang/Kulim corridor, Klang Valley, Johor region and the fabrication plant in Kuching.

There is no single government agency that champions the E&E sector with a deep understanding of how to leverage the presence of an important knowledge-based industry within Malaysia and to build on it as an ecosystem of innovation and new income growth. The lack of talent has been continuously highlighted as a key limiting factor to the growth of the E&E sector and needs to be addressed urgently if Malaysia is to remain relevant in tomorrow's E&E global supply chain. Without appropriately qualified and trained personnel in engineering and related fields, companies are unable to transform from high volume manufacturing to low volume high mix high value products.

### Recommendation

Establish a single window agency or a championing agency to manage all matters related to the E&E sector. This agency should be empowered and held accountable for all incentives, grants and policy implementation in the E&E sector. MIDA has been identified as this potential agency.

This will be complemented by the new Centre of Engineering Excellence (CEE) intended to provide a fertile ground for the sharing of expertise between the private sector and academia in order to develop the appropriate human capital urgently needed in the E&E sector. A partnership between USM and Indian Institute of Technology (IIT) has been established as the vehicle for this initiative.

Have a government procurement policy to encourage product-technology integrators to use Malaysia as a “test-bed” for new products and services and to stimulate the design and production of goods and services that increase Malaysian value-add and exports. In this context, an emphasis on energy-saving devices, green technologies and sustainable manufacturing practices will in turn open new market segments and opportunities in the region.

Foster the establishment of an “Asset-Light” type institution to enhance the Asset Light approach development of the E&E sector. These initiatives help reduce barriers to moving into higher value-add activities. Establishing an “Asset Light” type institution involves E&E production facilities to be built and leased to firms, allowing them to dedicate their limited resources to working capital. The initiative will need to be private sector-led with government encouragement via various incentives.

**APPENDIX**

**B**

# **POLICIES FOR THE PALM OIL SECTOR**



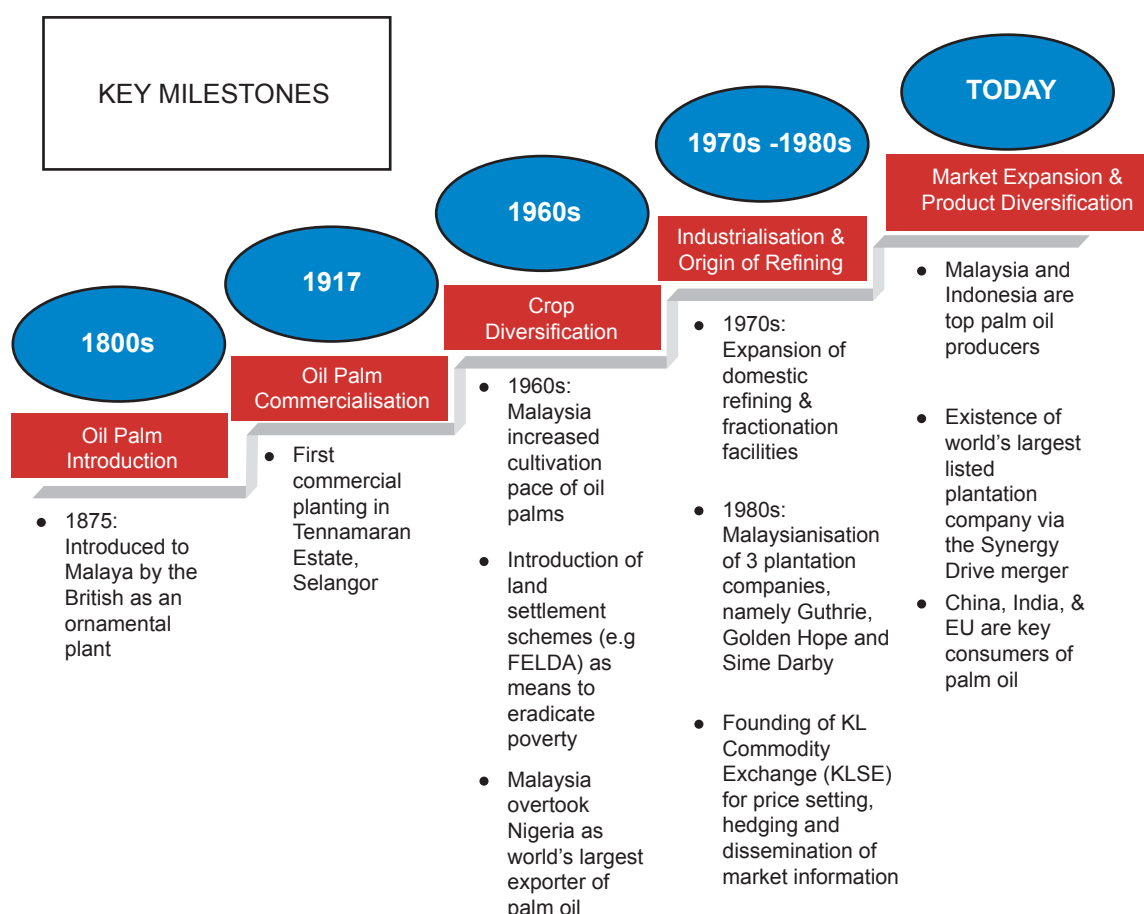


## APPENDIX B: POLICIES FOR THE PALM OIL SECTOR

The palm oil industry's landscape has drastically changed since its beginnings early in the 19th and 20th century (**Figure B1**). The current applications of palm oil have diversified from lubricants, soaps and cooking oils, to medicines, oleochemical products, biofuels and specialty fat products. These new applications have themselves spawned many burgeoning and related industries in the downstream segment.

From its initial 2% coverage of Malaysia's total agricultural produce, the industry now contributes 3.3% to Malaysia's total GDP. The industry also provides various socio-economic benefits including direct employment to over 600,000 workers and serves as a major tool in overcoming poverty in rural areas.

**Figure B1: History of the Malaysian Palm Oil Industry**



Malaysia enjoys a competitive edge over many other countries operating in the palm oil industry. The commercialisation of the palm oil industry in the 1960s allowed Malaysia to gain a 'first-mover' advantage, in terms of expertise and technological advancements, over other nations who started planting later. Currently, the palm oil industry stands at an inflection point. While Malaysia is one of the largest palm oil producers in the world, we are in danger of losing this competitive advantage to other producers in Asia, Africa and South America. Palm oil plantings in Malaysia have slowed as arable land in Malaysia become exhausted. Planted area with oil

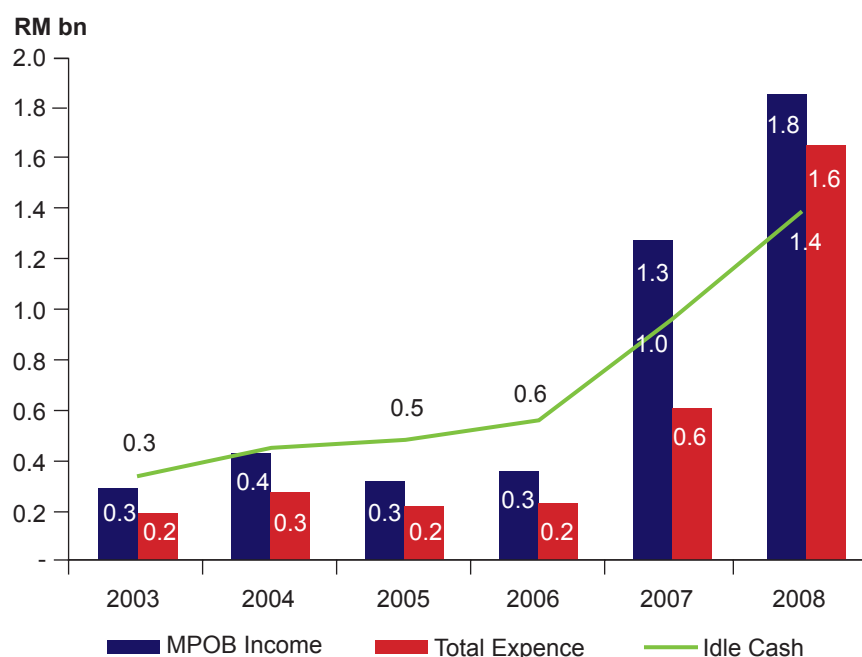
palm grew an annual average of some 3% in the last five years. There are labour shortages and production costs are rising relative to other producing nations.

For Malaysia to regain its competitive advantage in the palm oil industry it must:

- Improve R&D as a driver of not only technology and innovation but also skilled human capital in the upstream and downstream market segments
- Increase the contribution of smallholders, who make up almost 40% of Malaysia's planted area
- Move downstream into higher value added products

Malaysian planters pay a cess in aggregate close to RM14 per tonne to R&D agency Malaysian Palm Oil Board (MPOB) to fund their research programmes and the palm oil stabilisation fund. Much of this fund remains unused and could be better utilised elsewhere to benefit the industry (**Figure B2**). More focus on addressing the R&D needs of the industry is needed, especially in areas of mechanisation and productivity improvements.

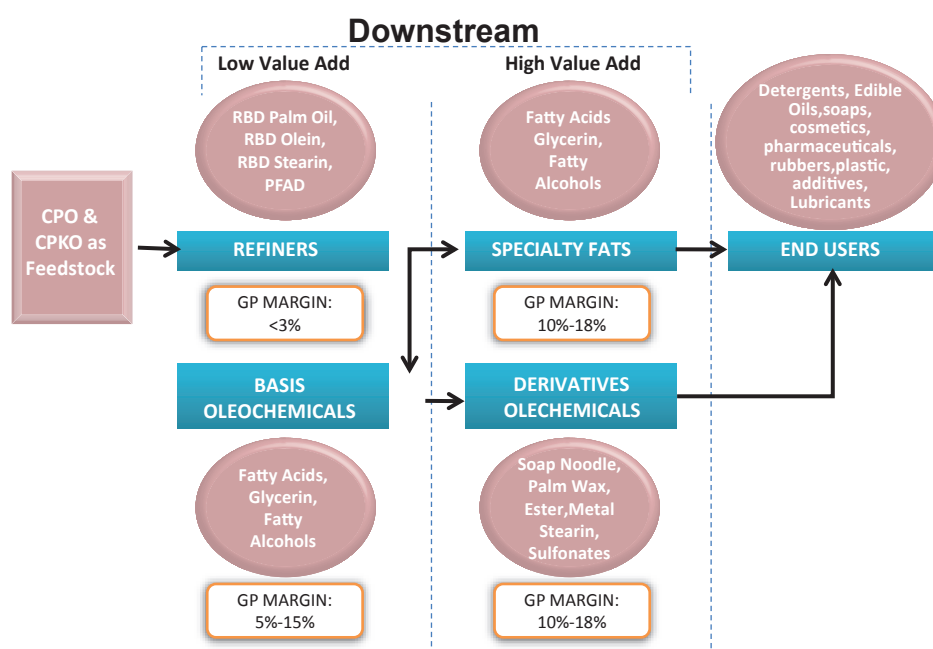
**Figure B2: Idle Cash in MPOB**



Source: MPOB Annual Reports

Downstream companies find it difficult to transit to higher value products such as derivative oleochemicals or branded/tailored palm products (**Figure B3**). Challenges include the elevated capital requirements and intense competition from established foreign players.

Figure B3: Downstream Industry Mostly Producing Low Value Add Products



Source : Frost &amp; Sullivan, May 2010

Smallholders' productivity is well below commercial levels stemming from a lack of management expertise, technological know-how, and financial constraints. Many of the smallholder R&D issues have been recognised in the 10MP. The NEAC recommends expansion of the solutions already proposed (**Figure B4**). R&D on mechanisation and biotech seed research (e.g. genome) can go a long way to improving productivity in the short and long-term.

Figure B4: Policy Measures in 10MP and additional NEM measures

10MP	NEM
<ul style="list-style-type: none"> <li><b>R&amp;D</b> <ul style="list-style-type: none"> <li>- Intensify collaborative R&amp;D with established agriculture research institutes</li> <li>- Promoting greater private sector participation</li> <li>- Drive productivity &amp; innovation, nurture and attract top talent and develop clusters with agglomeration economies</li> </ul> </li> <li><b>Downstream</b> <ul style="list-style-type: none"> <li>- Promote Malaysia as a global hub for palm oil</li> <li>- Develop Palm Oil Industrial Clusters</li> </ul> </li> <li><b>Smallholders</b> <ul style="list-style-type: none"> <li>- Set up agriculture consortiums and cooperatives to reap the benefits of scale</li> <li>- Centralise procurement of agricultural inputs</li> </ul> </li> <li><b>ICT</b> <ul style="list-style-type: none"> <li>- Utilise modern farm technology and ICT</li> </ul> </li> <li><b>Support services</b> <ul style="list-style-type: none"> <li>- Provide adequate and specific infrastructure, facilities and logistics to support value added activities</li> <li>- Enter into long-term contract agreements to export palm oil</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li><b>R&amp;D</b> <ul style="list-style-type: none"> <li>- Increase productivity through mechanisation and biotech seed research</li> <li>- Have collaborative programmes with consumer countries to identify next generation commercial needs</li> </ul> </li> <li><b>Downstream</b> <ul style="list-style-type: none"> <li>- Promoting Malaysia as a global hub for all edible oils</li> <li>- Collaborate with universities to not only produce R&amp;D but skilled labour force needed by industry</li> </ul> </li> <li><b>Smallholders</b> <ul style="list-style-type: none"> <li>- Incentivise private smallholders to improve palm oil yields</li> <li>- Utilise MPOB surplus funds to help industry transformation and R&amp;D</li> </ul> </li> </ul>

Source: 10MP

Partnerships with foreign companies can lead to direct investments in Malaysian innovation centres, processing refineries, and product development labs, which in turn will attract both foreign and local skilled talent. The idle funds under Malaysian Palm Oil Board (MPOB) should be channelled to private R&D institutes to work on specific value-adding projects. Furthermore, Malaysia should promote itself as a global hub for edible oils. Attracting foreign consumer companies such as Unilever or Nestle to establish their operations in Malaysia is the first step. The downstream industry needs to actively seek close partnerships with consumer brands for product development or R&D. The Government needs to step in to provide the right incentives and initiatives for local players to invest in refineries, innovation, and R&D centres.

# ACKNOWLEDGEMENTS



## ACKNOWLEDGEMENTS

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## **SPECIAL THANKS TO**

Chief Justice of Malaysia  
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Tan Sri Ramli Ngah Talib, Former Speaker of the Dewan Rakyat  
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# **LIST OF KEY ENGAGEMENTS**



## LIST OF KEY ENGAGEMENTS

DATES	PROGRAMME	ORGANISER
1 April 2010	Seminar on the NEM: An Appraisal	Persatuan Ekonomi Malaysia
5 April 2010	ASLI Forum	Asian Strategy & Leadership Institute (ASLI)
5 April 2010	Program Kerusi Panas (Azlan Idris) secara langsung 6.30-7.00pm. Tajuk perbincangan mengenai Model Ekonomi Baru (MEB)	BERNAMA RADIO24
5 April 2010	Forum membincangkan Isu 'Model Ekonomi Baru & Gagasan 1 Malaysia'	Dewan Bahasa dan Pustaka (DBP)
9 April 2010	NIEW GENDER SERIES: Woman & The New Economic Model	NAM Institute For The Empowerment of Women (NIEW)
9 April 2010	Taklimat Model Ekonomi Baru	Tabung Amanah Muhibbah (TAMU)
13 April 2010	Developing Creativity And Innovation, Rethinking Human Capital Development	Wawasan Open University
13 April 2010	SEDAR Forum	SEDAR Institute
15 April 2010	Dialogue of NEM/Briefing	Department of Special Affairs, Ministry of Information, Communication and Culture
19 April 2010	NKEA Workshop on E & E Penang, NEM Dialogue Penang. Opening Remarks and Overview of the New Economic Model (NEM) by Dato' Seri Panglima Andrew Sheng	
20 April 2010	MICPA 51st Anniversary Commemorative Lecture at Sime Darby Convention Centre	Sime Darby Convention Centre
20 April 2010	Driving Force Seminar	National Civics Bureau
20 April 2010	Deputy Ministers/BNBBC	National Front (BN) Members of Parliament
20 April 2010	International Advisory Board	CPDS University of Malaya
21 April 2010	Meeting Between Federal Government and State Governments	Cabinet Division, Prime Minister's Department



DATES	PROGRAMME	ORGANISER
27 April 2010	Forums on New Economic Model and Roles of Ministry of Science, Technology and Innovation (MOSTI)	MOSTI
29 April 2010	Seminar Kebangsaan 'Pengajian Tinggi dan Model Baru Ekonomi' Memacu Model Baru Ekonomi Melalui Pengajian Tinggi	AKEPT, Kementerian Pengajian Tinggi Malaysia
30 April 2010	Student's Seminar	Polytechnic Shah Alam
2 May 2010	Bengkel PERKASA: Membentang Kertas Kerja Mengenai Dasar-dasar Afirmatif Membantu Bumiputra di dalam Model Ekonomi Baru –Speaker	Pertubuhan Pribumi Perkasa Malaysia PERKASA
5 May 2010	Forum Model Ekonomi Baru (MEB) - Langkah Berinformasi Dasar, Strategi & Pelan Tindakan: Dimana Letaknya Ekonomi Melayu	Dewan Perniagaan Melayu Malaysia Negeri Terengganu
5-6 May 2010	Sarawak Civil Services Conference	Sarawak State Government
6 May 2010	Working Group C Session : Strengthening the Public Sector at Department of Local Government, Ministry of Housing And Local Government	National Economic Advisory Council
10 May 2010	NEAC Working Group Inaugural Meeting – Topic Discussion : Workforce	National Economic Advisory Council
10 May 2010	Mesyuarat Jawatankuasa Tindakan Penyelarasan Inovasi Negara (JTPIN) : Peranan JTPIN Dalam Merealisasikan Model Ekonomi Baru	MOSTI
11 May 2010	NEAC Working Group Inaugural Meeting - Topic Discussion : Knowledge Base	National Economic Advisory Council
11 May 2010	Malaysian American Electronics Association	Malaysian American Electronics Association
12 May 2010	NEM Dialogue/Briefing	EMPOWER & SUARAM (NGO)
13 May 2010	NEM Dialogue/Briefing to Seniors Officials	Ministry of Rural and Regional Development
13 May 2010	Working Group C Session : Strengthening the Public Sector at Malaysian Administrative Modernisation and Management Planning Unit (MAMPU)	National Economic Advisory Council

DATES	PROGRAMME	ORGANISER
14 May 2010	Konvensyen Usahawan Melayu : Agenda Ekonomi Melayu Dalam Model Ekonomi Baru	Dewan Perniagaan Melayu Malaysia
14 May 2010	FORUM of Management Team	UiTM
17 May 2010	Meeting of Federal Head Departments	Cabinet Division, Prime Minister's Department
18 May 2010	NEM Dialogue/Briefing	Penang State Government
18 May 2010	Working Group C Session : Strengthening the Public Sector at Secretariat of the Special Taskforce to Facilitate Business (PEMUDAH)	National Economic Advisory Council
20 May 2010	Seminar on Innovation and Creativity in Tourism	Ministry of Tourism
21 May 2010	NAPSEC (MATRADE Advisory Council Meeting)	MATRADE
21 May 2010	Working Group C Session : Strengthening the Public Sector at Public Service Department (PSD)	National Economic Advisory Council
21 May 2010	Working Group C Session : Strengthening the Public Sector at Iskandar Regional Development Authority (IRDA)	National Economic Advisory Council
24 May 2010	Sub-working group Meeting- Topic Discussion : Upgrading the Skills of the Labour Force and Enhancing Vocational and Technical Training	National Economic Advisory Council
24 & 25 May 2010	NEM Dialogue/Briefing	Pahang State Government
25 May 2010	Microsoft Conference with Steve Ballmer and Tony Fernandes	Microsoft
26 May 2010	Interview on NEM	RTM Radio News
26 May 2010	Sub-working group Meeting- Topic Discussion : Reducing the Dependence on Foreign Labour	National Economic Advisory Council
26 & 27 May 2010	NEM Dialogue/Briefing	Kelantan State Government

DATES	PROGRAMME	ORGANISER
27 May 2010	Sub-working group Meeting- Topic Discussion : Developing a Quality Workforce and Reducing Dependency on Foreign Labour	National Economic Advisory Council
27 May 2010	Working Group C Session : Strengthening the Public Sector at Legal Division, SHELL Malaysia	National Economic Advisory Council
29 May 2010	Bumiputera Economic Congress	The Parti Pesaka Bumiputera Bersatu
1 June 2010	NEM Dialogue/Briefing	Malacca State Government
2 June 2010	Plenary Forum	Academy Science Malaysia
2 June 2010	Sub-working group Meeting- Topic Discussion :  Improving Functioning of Labour Market and Managing Talent Workforce	National Economic Advisory Council
3 June 2010	Round Table Discussion PTD	Alumni of Administrative and Diplomatic Officer (PTD)
3 June 2010	Sub-working group Meeting- Topic Discussion : Promoting Stronger Enabling Institutions to Support Innovation to Move Up the Value Chain	National Economic Advisory Council
4 June 2010	Forum Positioning Perak in the NEM	Institut Darul Ridzuan Perak
7 June 2010	Meeting of Secretaries General of Ministries and Head of Services	Cabinet Division, Prime Minister's Department
14 June 2010	NEAC Workshop on Affirmative Action under the New Economic Model	National Economic Advisory Council (NEAC)
15 June 2010	Working Group C Session : Strengthening the Public Sector at Tan Sri Ramli Ngah Talib, Former Speaker of Dewan Rakyat	National Economic Advisory Council
16 June 2010	Forum NEM and 10 <sup>th</sup> MP	National University of Malaysia (UKM)
19 June 2010	NEM Briefing for Parti Bersatu Sabah	Parti Bersatu Sabah
21 & 22 June 2010	NEM Dialogue/Briefing	Negeri Sembilan State Government
23 June 2010	NEM Briefing for Management Team	RISDA

DATES	PROGRAMME	ORGANISER
23 June 2010	9th Conference on Status and Outlook of the Malaysian Steel Industry  Malaysian Economy and the New Economic Model	Malaysian Iron & Steel Industry Federation (MISIF)
23 June 2010	Diners' Club Guest Speaker for Malaysian Armed Forces Defence College  New Economic Model: The Way Ahead	Maktab Pertahanan Angkatan Tentera (MPAT)
1 July 2010	Working Group C Session : Strengthening the Public Sector at Chief Secretary to the Government	National Economic Advisory Council
2 July 2010	NEM Dialogue/Briefing	Ministry of Foreign Affair
3 July 2010	Univ. of Hawaii MBA Students	University of Hawai
5 & 6 July 2010	NEAC Workshop on Labour Market and Innovation	National Economic Advisory Council
6 July 2010	NEM Dialogue/Briefing	Co-operative College of Malaysia-Sarawak Branch
7 July 2010	NEM Dialogue/Briefing	Ministry of Information, Communication and Culture
7 July 2010	National Tax Conference	
9 July 2010	Working Group C Session : Strengthening the Public Sector at Malaysian Productivity Corporation (MPC)	National Economic Advisory Council
9 July 2010	Working Group C Session : Strengthening the Public Sector at Strategic Financial Management Division, Ministry of Finance (MOF)	National Economic Advisory Council
12 July 2010	Working Group C Session : Strengthening the Public Sector at Implementation and Coordination Unit (ICU)	National Economic Advisory Council
13 July 2010	Seminar 'Model Baru Ekonomi: Tinjauan dari Perspektif Islam Model Ekonomi Baru:	Institut Kefahaman Islam Malaysia (IKIM)
13 July 2010	Working Group C Session : Strengthening the Public Sector at Economic Planning Unit (EPU)	National Economic Advisory Council
14 July 2010	NEM Dialogue/Briefing	Ministry of Domestic Trade, Co-operatives and Consumerism

DATES	PROGRAMME	ORGANISER
14 July 2010	Meeting with Prof Frances Stewart, Director of the Centre for Research on Inequality, Human Security and Ethnicity (CRISE) at the University of Oxford	National Economic Advisory Council
16 July 2010	GLCs(G20) Meeting	Khazanah Nasional Bhd. Malaysia
16 July 2010	Working Group C Session : Strengthening the Public Sector at Petaling Jaya City Council (MBPJ)	
19 July 2010	NEM Dialogue/Briefing	Kedah State Government
20 July 2010	NEM Dialogue/Briefing	Perlis State Government
21 July 2010	NEM Dialogue/Briefing	Public Works Department, Ministry of Works
21 July 2010	Majlis Forum Ekonomi Baru Malaysia : Terpinggirkah Melayu Dalam Model Ekonomi Baru	Persatuan Guru2 Melayu Perak dan Persatuan Jaringan Perpaduan Melayu (PERGUM)
22 July 2010	NEM Dialogue/Briefing	Sabah State Government
26 July 2010	NEM Dialogue/Briefing with Students	Selangor International Islamic University College
26 July 2010	Working Group C Session : Strengthening the Public Sector at Cabinet Division, Prime Minister's Department	National Economic Advisory Council
27 July 2010	Working Group C Session : Strengthening the Public Sector at Unit Inovasi Khas (UNIK)	National Economic Advisory Council
27 July 2010	The New Economy What is in for the Rakyat	Malaysian Debt Ventures
27 July 2010	Meeting of Senior Offices of Department of Rural and Town Planning	Department of Rural and Town Planning
28 July 2010	NEM Dialogue/Briefing	The Malaysian Timber Industry Board (MTIB) Ministry of Plantation and Commodities
29 July 2010	NEM Dialogue/Briefing	Terengganu State Government
2 August 2010	ASLI National Symposium	Asian Strategic & Leadership Institute
3 August 2010	MEF Conference	Malaysian Employers Federation
11 August 2010	Working Group C Session : Strengthening the Public Sector at Kuala Lumpur City Hall	National Economic Advisory Council

DATES	PROGRAMME	ORGANISER
11 August 2010	Working Group C Session : Strengthening the Public Sector at Auditor-General's Office	National Economic Advisory Council
17 August 2010	Working Group C Session : Strengthening the Public Sector at Ministry of International Trade and Industry (MITI)	National Economic Advisory Council
14 August 2010	Chinese Economic Congress "Role of the Chinese Community in achieving the NEM and 10th Malaysia Plan Targets"	Malaysian Chinese Association Congress (MCA)
29 September 2010	NEM Dialogue/Briefing	Federation of Malaysian Manufacturing (FMM)
30 September, 2010	NEM Dialogue/Briefing	Selangor State Government

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