**The Structural Causes of Poverty in Malaysia**

According to government statistics, poverty is virtually non-existent in Malaysia – the incidence of poverty was pegged at 0.6% of the population1 in 2014 by the BN government. But this was because the poverty line was fixed at ridiculously low levels then. It is still unrealistic now - RM920 per month for a family of 2 adults and 3 children, working out to a per capita income of USD 1.60 per day. A more realistic poverty line would be a household income of RM3000 per month, which would be about 50% of the current median household income. Around 25% of Malaysian households are below this income level.

There are many who are perplexed by the persistence of poverty in Malaysia. For the Malaysian economy has been growing healthily over the past 50 years from a GDP of RM 10.3 billion in 1970 to RM1.45 trillion in 20182. The economy has diversified from agricultural commodity production to manufacturing which in 2015 contributed 23% of the GDP and employed 17.9% of the work force compared to 8.8% and 11.7% for the agricultural sector3. Moreover, Malaysia is a significant petroleum/natural gas exporter – accounting for 13% of total exports in 20184. Per capita income in real terms (after taking into account inflation) has increased 10-fold5 between 1970 and 2018.

Moreover The Barisan Nasional government has committed a lot of resources for affirmative action to uplift the lot of the Bumiputra6 population since the institution of the New Economic Policy in the 1970s. Why then is there still poverty in Malaysia? And why does the Bumiputra community still make up some 80% of the bottom 40% of the population (the B40) when they are only constitute about 65% of the population? There are some who blame it on laziness – that the Bumiputra population has been spoilt by too much pampering such that they are unable to stand on their own feet and are always expecting handouts.

But the truth is somewhat more complicated, and has a lot to do with the way that Malaysia is articulated into the global economy. Let’s examine the main aspects -

1. **The depressed prices for agricultural commodities.**

There are around 172,000 padi farmers, 375,000 rubber smallholders, 275,000 oil palm smallholders and much smaller numbers of coconut, cocoa and pepper smallholders in Malaysia. Over 85% of them work on plots less than 5 acres. They are all affected by the prices of their commodity on the world market which is characterized by a marked imbalance in “market power”. A small number of buyers with deep pockets and accumulated stockpiles face off with millions of poor small farmers spread out over several countries. This inequality in market power has led to depressed commodity prices ever since the nations in Asia and Africa gained independence. It isn’t an unique Malaysian problem – it affects millions of farmers in other third world countries as well who have been and are still being “short-changed” by the international system of trade!

This problem of over-supply of the commodity has been recognised by third world countries and there have been efforts to correct it by limiting production. For example, Malaysia, Indonesia and Thailand formed the International Tripartite Rubber Council in 20017 and they have attempted to stabilize the price of rubber on the world market. But they have not been very successful for unlike a commodity like petroleum which requires high initial investments and therefore has a small number of big producers, agricultural commodities require much smaller investments, and there are millions of poor peasants throughout Asia and Africa who desperately need money. Any success in restricting supply will tend to push up the price of that commodity and that would encourage the planting of that crop in more countries. So efforts to restrict supply of agricultural commodities in the world market have not succeeded.8

One strategy used by developing countries is to go “downstream” and process the commodity before exporting it. Malaysia has done some of that – we are now the largest producer of surgical gloves in the world. We also manufacture tyres and a host of palm oil products such as cooking oil, soap and margarine and that adds to our GDP. However this strategy of expanding into downstream manufacturing does not do much for the commodity price or for the income of the smallholders.

1. **A low wage economy**

18% of the Malaysian work force is employed in factories. However the vast majority of factory workers are taking home less than RM 1500 per month.

This is because Malaysia’s industrialization strategy has been to offer low costs of production. Free Trade Zones were set up to attract multinationals looking for places to outsource some portions of their production chain. In addition to the tax-free status that these Free Trade Zones offered, Malaysia also provides electricity at cheap rates as well as low waged labour. The fact that the Malaysian government has taken a strong stand against trade union activism also enhanced Malaysia’s standing in the eyes of foreign investors. This strategy succeeded and Malaysia is now the world’s largest exporter of electronic components.

But the down-side of this industrialization strategy is that Malaysia is now locked in to global chains of production which use the threat of transferring production to another third world country as a potent weapon to keep cost of production (especially wages) down. This is what was argued at the Malaysian National Wage Council meeting in mid 2018 that was convened to discuss setting the new minimum wage level. The unions and PSM (Parti Sosialis Malaysia) argued for an increase to RM1500 per month from the then rate of RM1000. The employers federation argued that they needed to keep costs down otherwise they would lose competitiveness. They asked that increase be only to RM1050. Finally the government agreed to RM11009. The fear of not being able to attract new foreign direct investment or of losing existing foreign investors to Thailand or to Vietnam where the wages are lower has a significant impact on minimum wage rate set by the government.

The ASEAN Free Trade Agreement is another dampener to effort to raise the minimum wage. At present there are hardly any tariffs to the import of goods from other ASEAN countries10. This means that Malaysian manufacturers of consumer items – clothes, shoes, toiletries and such similar items have to contend with imports of the same products from Vietnam and Thailand. Too drastic a hike in the wage rate would make it difficult for our local factories to maintain market share. “You may get a higher minimum wage,” the employers federation warned, “but many workers will lose their jobs.”

1. **Fiscal constraints to expanding the safety net.**

An effective modality of sharing the wealth of the nation is by subsidizing essential services and instituting cash transfers to sectors in need. Malaysia has already gone some way down that road –

* Education is practically free from primary to secondary level. The fees charged are minimal – between RM100 to RM 200 per year. Most primary school children are supplied texbooks free. Parents only need to cover the cost of school clothes, transport and canteen meals. The Ministry of Education was allocated RM 60.2 billion in the 2019 budget, 19.1% of the total federal Budget11.
* The Ministry of Health (MOH), which has a budget of RM 29 billion11 (or 9.2% of the total) maintains 2860 Health Clinics distributed throughout the nation as well 141 hospitals2. In 2017, there were a total of 2.37 million admissions to government hospitals compared to 1.05 million admissions to private hospitals.
* The Ministry of Women, Family and Community, with its budget of RM 2.4 billion11 gives financial aid to some single mothers, old persons without family support and severely incapacitated individuals. The quantum however isn’t much – usually its less than RM400 per month, but still does provide significant relief for the families that receive this help.
* The Ministry of Agriculture (2019 Budget RM 4.4 billion11) has several programs targeting padi farmers. The padi production incentive scheme pays out an additional 75 cents per kilogram of padi that the farmer sells to the mill, thereby doubling his earnings. (RM 281 million has been allocated for this scheme for 2019) Fertilisers and pesticides are provided free to padi farmers. (Budget allocated in 2019 is RM 232 million11) Traditional fishermen (around 70,000 of them) were given a monthly stipend of RM300 under the previous government.
* The Ministry of Rural Development (2019 Budget RM 8.4 billion11) provides infrastructure to rural population – bridges, roads, community centres – and helps in repairing or even building houses for the rural poor.

There are suggestions that this safety net could be widened. Specific suggestion include

a/ ***Old age pension***. At present only the government servants (who constitute 15% of the working population) can look forward to old age pension. 6.5 million Malaysian workers are contributors to the Employment Provident Fund – they contribute 11% of their wages monthly while their employer contributes 13%. However since wages are low, a survey in 2016 found that only 22% of EPF contributors aged 54 years had RM196,800 or more in their savings, which translates to about RM820 monthly during retirement12. There are another 5 million working people who are neither on the pension scheme nor the EPF scheme.

The suggestion is that all Malaysians aged above 70 years who are not on government or SOCSO pension should be given RM300 monthly. This would require a budget of RM 3 billion per year currently, and would increase as the population ages.

b/ ***Increasing the Health Budget to 4%*** of the GDP. That would mean an extra RM 29 billion. The rationale for the increase is because the government hospitals and clinics are severely overcrowded and there is a long waiting time to see the specialists. This has forced quite a number of people to turn to the private sector, which is expensive.

c/ ***Subsidized tertiary education***. At present college students can take loans from a government run agency – the PTPTN. A 3 year degree course in a private university will saddle the graduate with a RM 70,000 loan. The proposal is to reduce the fees drastically by giving grants amounting to 90% of the academic fees. This would require approximately RM 13 billion per year.13

d/ Subsidized ***bus based public transport*** in all our towns and cities. This will reduce transport costs as well as Malaysia’s carbon footprint, and is a much cheaper alternative to building train transit systems.

e/ ***Monthly cash transfers*** of RM 300 to the poorest 20% of households – cost would be RM 4.5 billion14.

There are also suggestions to increase the budget of the Department of Welfare, increase the stipend given to single mothers, provide subsidized housing to the population, take over the maintenance of low-cost residential flats (many of which are in a deplorable state), and others.

The problem here is that all these good ideas, that will undoubtedly alleviate the financial pressures on the bottom half of our population, require additional funds. The total Federal Revenue for 2019 is estimated at RM 261.8 billion. But total budgetary allocation for 2019 is RM314.5 billion. That means RM52.7billion has to be borrowed - a Fiscal Deficit of 3.4% of GDP for 2019. (The Malaysian GDP in 2019 is projected to be RM 1.55 trillion). Given the fact Federal Government Debt is about RM750 billion, the government needs to sell securities worth about RM 75 billion in the course of 2019 to roll over the bonds and securities that are maturing this year. This is in addition to the RM 52.7 billion that has to be raised to meet this year’s budget shortfall.

I am quoting all these figures to drive the point that there are real limitations to a strategy of building a more comprehensive safety net on the back of a larger budgetary deficit. It will impact negatively on our credit ratings and drive up the costs of borrowing. Malaysia allocated RM 30.88 billion (or 10.94% of the total Federal Budget) for debt servicing in 201815 (To pay the interest on government bonds and securities.) This works out to an average interest rate of 4.1%. The interest we will have to pay on future debt will go up if our budget deficit goes up from its current 3.4%.

Fiscal prudence dictates that the government has to raise additional revenue if it decides to embark on augmented social spending. A consumption tax is politically out of the question at present. The PH government came in on the campaign promise that it would abolish the GST (Goods and Services Tax) and it has done so. It cannot now reinstitute this tax. And in any case, such a tax is regressive as poorer families spend a larger portion of their income as compared to better off families who save or invest a portion of their income.

The government also faces problems in raising corporate taxes as that might lead to companies shifting their headquarters to other countries. A competent accountant can transfer company earnings out of Malaysia into the accounts of the HQ located in a tax haven using a variety of techniques – routing purchase of intermediate products with hiked up prices through the HQ, routing exports through the HQ but at discounted prices, charging large royalties and fees for accounting and other consulting services – and all of these are quite legal given the liberalized financial environment . All these tricks will ensure that profits declared in Malaysia are at a minimal level.

Malaysia had a corporate tax rate of 40% before, but starting in 1988 we began to reduce it because other countries in the region were at lower rates and Malaysia was afraid that we would lose out on FDI (Foreign Direct Investment). As a result corporate tax in Malaysia is now at 24% and the Minister of Finance has said he would reduce this even further soon! The reason is that Singapore only has an 18% corporate tax rate, and Thailand 19%. It is a classical “race to the bottom” scenario that has unfolded over the past 30 years and it shows no sign of abating.

So, this then is the situation that Malaysia finds itself in. A significant portion of the wealth created in Malaysia is transferred out by unfair pricing mechanisms (perhaps 40% or so) through low commodity prices and low wages, and we have to do with the remainder left to us. But our hands are tied because Malaysia is deeply integrated into the global economy. The value of our exports was 74% of our GDP in 2017. (This doesn’t mean we exported 74% of what we produced because we imported significant amount of chips and other components for our manufacturing sector to process and re-export.) We are definitely in no position to tell off the global chains and “de-link” from the global economy! Greece couldn’t in 2015 despite Syriza being in power, and Britain, a much larger and richer country is facing enormous problems in trying to partially de-link from the EU!

The way forward I believe, is to gradually, and collectively renegotiate our terms of engagement with the global economy. For example, can tax havens be closed? Can we bring in legislation to restrict transfer-pricing? Can we get the richest 0.01% to pay their fair share of taxes? In this matter we would have the support of the majority of the populations in other countries including the advanced countries which are also struggling with huge sovereign debts and are being forced to reduce social spending.

Can we stop the ruinous race-to-the-bottom in corporate tax rates among ASEAN countries? This is do-able and perhaps it should be linked to the ASEAN Free Trade Agreement – for example if any ASEAN country reduced corporate tax any further, its exports to other ASEAN countries will be charged a tariff of 5% for every 1% lowering of corporate tax. In a similar manner, can we agree on jointly raising our minimum wage – 10% next year from whichever base we are on now? So that we can help the poorest in our population without suffering a comparative disadvantage in terms of FDI and market competitiveness.

Can these sort of initiatives be canvassed in the Group of 77 and further initiatives be developed?

These are the kinds of issues we need to discuss if we want to end persistent poverty in this country. However the current PH government doesn’t seem to have explored this line of reasoning.

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 Notes

1. Eleventh Malaysia Plan Document. Page 3-3.
2. Department of Statistics.
3. Appendix A2-3 and A5-2, Eleventh Malaysia Plan.
4. 4.
5. <https://www.ceicdata.com › Home › Countries › Malaysia>
6. Population increase = x 3.1; Cumulative inflation 1970 - 2018 = x 4.4

Therefore: 1450 divided by (10.3 x 3.1 x 4.4) = 10.36

1. Malays and the indigenous peoples of Sabah and Sarawak
2. On 12 December 2001, the three major natural rubber (NR) producers namely Thailand, Indonesia and Malaysia signed a Joint Ministerial Declaration (Bali Declaration 2001) pledging to work collectively to ensure fair and remunerative income for rubber smallholders of the three countries. The International Tripartite Rubber Council (ITRC) was then established with the main objectives to ensure sustainable NR production.

International Rubber Consortium website.

1. The Thai government tried to buy up and stockpile rubber in 2014 in an effort to prevent prices from sliding down further. At one point they had more than 300,000 tonnes of rubber in government stockpiles. /www.reuters.com/article/thailand-rubber/update-1-thailand-set-to-sell-98000-t-of-rubber-from-state-stockpiles-idUSL4N1F91VC
2. The government initially announced in September 2018 that the minimum wage would be raised next year to RM1,050 monthly throughout the country. After workers gathered outside Parliament to protest the government today raised it to RM1,100 starting January 2019.
3. Brunei, Indonesia, Malaysia, Philippines, Singapore, and Thailand have eliminated intra-ASEAN import duties on 99.65 percent of their tariff lines. Cambodia, Lao PDR, Myanmar, and Viet Nam have reduced their import duties to 0-5 percent on 98.86 percent of their tariff lines. [investasean.asean.org/index.../asean...trade.../asean-trade-in-goods-agreement.html](https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=5&ved=2ahUKEwie27H31NLiAhWMtY8KHaT5CiQQFjAEegQIABAB&url=http%3A%2F%2Finvestasean.asean.org%2Findex.php%2Fpage%2Fview%2Fasean-free-trade-area-agreements%2Fview%2F757%2Fnewsid%2F872%2Fasean-trade-in-goods-agreement.html&usg=AOvVaw2ip8FKZ8gEi7CX2aN9yJYf)
4. All figures quoted regarding the 2019 Budget are from http://www1.treasury.gov.my/efe\_2019.html
5. https://www.freemalaysiatoday.com/category/nation/2016/11/10/epf-savings-may-not-be-enough-for-retirement/
6. This is an estimate based on following assumptions

- 672,000 students enrolled in Public colleges and universities and 350,000 in Private Colleges and Universities

- Average annual fee of RM10,000 for Public Institutions and RM20,000 for the Private.

 14. RM 300 x 12 months x 1.25 million households = RM 4500 million

 15. Federal Expenditure Estimates 2018 – Pg 16