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ABOUT ISIS MALAYSIA

The Institute of Strategic and International Studies (ISIS) Malaysia was established on 8 April 1983, in realization of a decision made by the Malaysian Government to set up an autonomous, not-for-profit research organization, to act as the nation's think-tank. ISIS Malaysia was envisioned to contribute towards sound public policy formulation and discourse.

The research mandate of ISIS therefore spans a wide area. It includes economics, foreign policy, strategic studies, nation building, social policy, technology, innovation and the environment.

ISIS Malaysia today fosters dialogue and promotes the exchange of views and opinions at both national and international levels. It undertakes research in collaboration with national and international organizations, in important areas such as national development and international affairs.

ISIS Malaysia also engages actively in Track Two diplomacy, fostering high-level dialogues at national, bilateral and regional levels, through discussions with influential policymakers and thought leaders.

RESEARCH

Economics

Research in this area is generally aimed at promoting rapid and sustained economic growth and equitable development in the nation. We study specific (rather than generic) issues that concern the nation's competitiveness, productivity, growth and income. Areas of research include macroeconomic policy, trade and investment, banking and finance, industrial and infrastructure development and human capital and labour market development. The objective of all our research is to develop actionable policies and to spur institutional change.

Foreign Policy and Security Studies

The primary aim of this programme is to provide relevant policy analyses on matters pertaining to Malaysia's strategic interests as well as regional and international issues, with a focus on the Asia-Pacific Region. These include security studies, foreign policy, Southeast Asian politics and military affairs.

Social policy

Demographic and socio-cultural trends are changing Malaysian society and the social policy programme was established to respond to these developments. Research in this area is concerned with effective nation building, and fostering greater national unity. In particular, we look at issues involving the youth, women and underprivileged communities. In conducting its research, ISIS Malaysia networks with non-governmental organizations and civil society groups.

Technology, Innovation, Environment & Sustainability (TIES)

The TIES programme provides strategic foresight, collaborative research and policy advice to the public sector, businesses and policy audiences, on technology, innovation, environment and sustainable development. Its focus includes green growth as well as energy, water and food security. Towards this end, TIES has been active in organizing dialogues, forums, policy briefs and consultancies.

HIGHLIGHTS

ISIS Malaysia has, among others, researched and provided concrete policy recommendations for:

- Greater empowerment and revitalization of a national investment promotion agency;
- A strategic plan of action to capitalize on the rapid growth and development of a vibrant Southeast Asian emerging economy;
- A Master Plan to move the Malaysian economy towards knowledge-based sources of output growth;
- The conceptualization of a national vision statement;
- Effective management and right-sizing of the public sector; and
- Strengthening of ASEAN institutions and co-operation processes.

ISIS Malaysia has organized the highly regarded Asia-Pacific Roundtable, an annual conference of high-level security policymakers, implementers and thinkers, since 1986.

INTERNATIONAL NETWORKING

As a member of the Track Two community, ISIS Malaysia participates in the following networks:

- ASEAN-ISIS network of policy research institutes;
- Council for Security and Cooperation in Asia and the Pacific (CSCAP);
- Network of East Asian Think Tanks (NEAT); and
- Pacific Economic Cooperation Council (PECC).

It is also a partner institute of the World Economic Forum (WEF).

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The Current Global Economic Situation and Multilateralism

*Dr Danny Leipziger, Professor of International Business, George Washington University, delivered a talk entitled `The Current Global Economic Situation and Multilateralism,' at an ISIS International Affairs Forum on the 22nd of February 2012. ISIS Researcher **Nor Izzatina** reports.*

The 2008 global financial crisis altered the shape of the world economy and its repercussions persist until today. The Occupy movement and the recent Greece debt crisis are the result of inadequate solutions to the financial crisis. As countries try their best to address domestic concerns like unemployment and burgeoning government expenditure, the focus on the multilateral system is fading and the common goals promoted are under threat.

The global financial crisis saw the emergence of the `new economic norm'. Under the new norm, while advanced economies experienced lagging or anemic economic growth, as seen in recent years, several developing countries continued to post healthy growth levels, thus increasing their prominence globally. Brazil, Russia, India and China (collectively called BRIC by Goldman Sachs in 2001) are expected to grow rapidly and by 2050 will be the most dominant economies in the world. It is projected that by 2035, BRIC's accumulated Gross Domestic Production (GDP) will outstrip that of the G-7 nations. Complementing the rise of BRIC will be the N-11 (Next Eleven) group of Bangladesh, Egypt, Indonesia, Iran, Mexico, Nigeria, Pakistan, Philippines, Turkey, South Korea and Vietnam. In the last decade, and especially since the financial crisis, these economies have been on the right trajectory to achieve the scenario envisioned in 2001.

The rise of these new economic superpowers has been followed by several new policy realities and circumstances. Dr Leipziger cited findings from the Growth Commission that in 2008 examined the

Danny Leipziger

growth patterns and the trajectories of developing countries over the years. The Commission found that countries sampled attained growth by implementing 'textbook' prescribed policies like openness to trade and high investments and savings.

However one finding from the Growth Commission can be considered as an outlier, namely, the active role of government or to be more specific, the role of government that allows growth to take off and continue. The role includes: i) leadership and governance, ii) credible commitment to growth, iii) credible commitment to inclusion and equality, and iv) capable administration.

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Industrial policy is an important policy tool that helped developing countries transform into developed countries. Industrial policy concentrates government efforts on selected industries, enabling countries like South Korea and Japan to be competitive and industrialized, and therefore emerge as manufacturing powerhouses. Tacit industrial policy has also long been practiced by industrialized countries – for example, the US science and technology-driven policy in the 20th century.

Given their current economic situation, and the success of proactive industrial policy, advanced countries are considering focusing on industrial policy, particularly to minimize problems like unemployment and trade deficits. The United States has decided to pay more attention to its manufacturing sectors by offering corporations incentives to bring back their manufacturing capacity to the US. On the sectoral part, active industrial policy can be found in technology and green growth driven sectors.

For several countries, government's active role in promoting economic growth extends into a very participatory one, to the extent that state capitalism becomes institutionalized. Dr Liepziger added that state capitalism is an attractive policy tool due to government's ability to stake its vision for the future without barriers or opposition. For example, China has for years been using state capitalism in its development goals, such as using state-owned and related financial institutions to fund selected sectors like technology and manufacturing.

The renewed focus on a more participative government economic policy to prop up growth, especially in advanced countries, is not without trade-offs. The biggest trade-off is the dilution of the global common economic vision that has been driving the multilateralism framework after World War II. The current multilateral economic institutions are creations of the Bretton Woods Conference of 1944.

For nearly 70 years, organizations like the World Bank and the International Monetary Fund have been extending development and financial emergency assistance, while the GATT/WTO made the international trading regime more civil. The records for the three institutions might not be constantly impeccable but given the current as well as expected economic situation, their roles have to be constantly adaptive in order to maintain some civility in international economic relations.

The IMF has for a very long time been criticized for the conditions it attaches to the financial assistance it renders, while the WTO for the past ten years has been unable to complete the Doha Development Round. Development assistance given by the World Bank has at times also resulted in unintended consequences for the less-developed and developing countries. The 2008 Global Financial Crisis resulted in reforms within the Bretton Woods institutions.

For instance, the WTO's dispute settlement mechanism prevented the rise of trade protectionism policies during the crisis. The IMF has also softened its 'Washington Consensus' stand in some aspects, such as the capital control

… advanced countries are considering focusing on industrial policy, particularly to minimize problems like unemployment and trade deficits

... countries cannot pursue democracy, national self-determination and economic globalization simultaneously

regime, since the financial crisis. The World Bank and the FAO have also been on the ball in improving the food security situation for developing countries recently. The pace of reform however needs to be improved further.

The desire of governments to have better control over economic direction and policies brings into question the feasibility of multilateral goals. Dani Rodrik explains this as an impossible trilemma under the globalization paradox. Countries now have to choose to allocate their attention and resources between national economic policies, demands for democracy or multilateral responsibilities. In essence, countries cannot pursue democracy, national self-determination and economic globalization simultaneously. Rodrik's work concluded that when clashes take place between domestic-driven democratic issues and globalization, national issues should and will prevail.

Given this outlook, the question is, who should take up the mantle of multilateralism and uphold the principle for common benefit. According to Dr Leipziger, countries like Russia are not ready to take up the responsibility given their overly nationalistic ideologies. Countries like Brazil, India and China, while they have gained much influence under the G20 setting, and other multilateral bodies like the World Bank, are still adolescents in global economic power and are not ready, or are unwilling to take up the multilateral gauntlet from the United States and the European Union.

The new economic reality will see several new challenges that will require improvements in the current multilateral system. Countries, even the developing ones, will find out that economic growth will be harder to generate and efforts to generate it will face intensified global competition. While the economic development level of countries will converge, the convergence will be accompanied by growing internal inequalities. Therefore, a certain level of civility and safety nets operating in international settings will be required.

In conclusion, Dr Leipziger reiterated that attention needs to be paid to improving multilateral institutions. While the urgency to solve domestic imbalances is both easier to act upon and popular, policymakers around the world must not lose sight of the benefits of multilateral institutions, given that they have long assisted in the creation of prosperity in the past.

Participants at the forum

Climate Change and Green Economy: International Cooperation for Energy Transition

***HE Mr Masahiko Horie**, Japan's Ambassador for Global Environmental Affairs spoke on the topic of international cooperation for energy transition at an International Affairs Forum organised by ISIS Malaysia. The forum was held in Kuala Lumpur, Malaysia, on February 23, 2012. Ambassador Horie is involved in various environmental issues including climate change negotiations, and he has participated in COP17/CMP7 at Durban. ISIS analyst **Alizan Mahadi** reports.*

Recent decades have witnessed a rise in international activities to protect the Earth by 'retuning' development along lines that are less energy–intensive. One important policy action is to execute energy transition – from fossil fuel to renewables, from roads to railways and to other climate-friendly energy solutions. In the past five years, renewable energy such as solar has grown by 54 per cent in Japan, and is bound to increase further following the Fukushima incident. However, for developing countries, transition to a green economy means huge investments. Against this backdrop, some questions arise in establishing international cooperation to face these challenges: -

1. What is the current situation regarding international cooperation on climate change?
2. What are the promises from COP17 in Durban with regard to climate change and green economy?
3. What are the potential roles of Japan and the developed world in ensuring access to finance and technology in shifting to a greener economy?

The history of international agreements to address climate change has to be understood to paint a picture of where we currently stand. The United Nations Conference on Environment and Development held in Rio de Janeiro in 1992 produced the United Nations Framework Convention on Climate Change (UNFCCC) treaty.

Masahiko Horie

The objective of the treaty is to stabilize greenhouse gas (GHG) concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system. It however set no mandatory limits on GHG emissions and contains no enforcement mechanisms.

The treaty provides for updates (called 'protocols') that would set mandatory emission limits. The principal update to the UNFCCC is the Kyoto Protocol, an international agreement that sets legally binding targets for industrialized countries and the European community for reducing GHG emissions, to an average of five per cent against 1990 levels, over the five-year period 2008-2012.

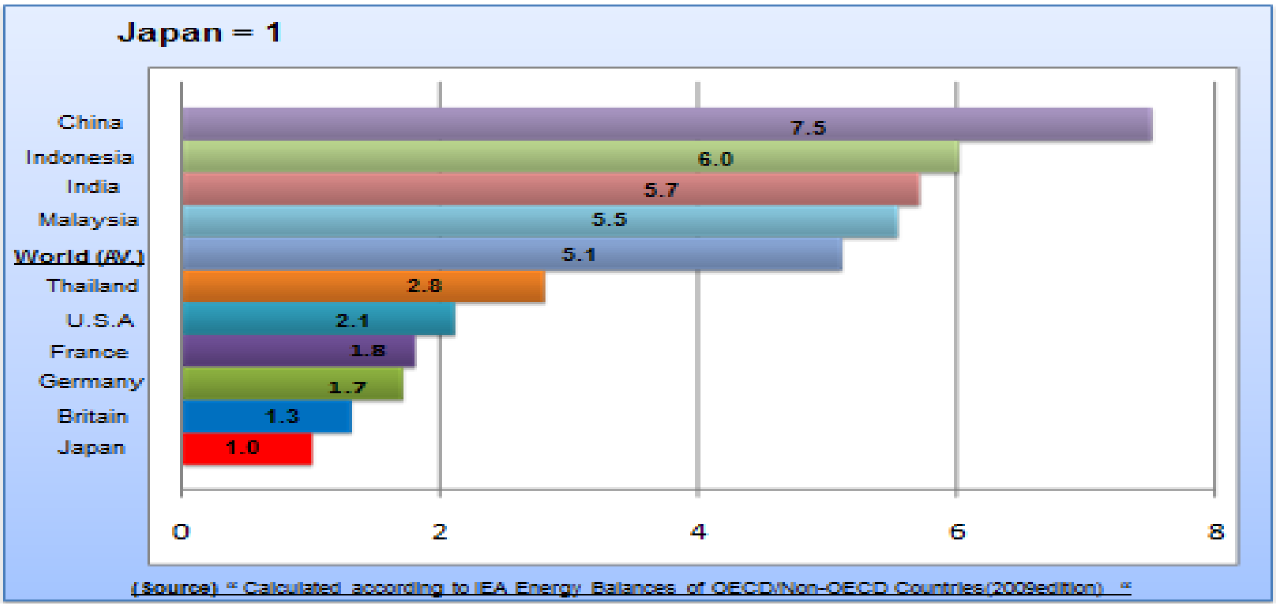

Table I: Primary Energy Supply per GDP Unit of each Country

The mandatory national limitations for emission reduction were based on a lengthy negotiation process. National limitations range from eight per cent reduction for the EU, seven per cent for the US and six per cent for Japan. The Kyoto Protocol included the biggest emitters in 1990 and covers 65 per cent of global GHG emissions. This provided an optimistic platform to combat climate change as it directly addresses the reduction of GHG emissions from the biggest emitters. Despite this, disagreements have plagued the Kyoto Protocol process.

Firstly, the US Congress did not ratify the treaty. The US signed the Protocol in 1998. However, the Protocol was not submitted to the Senate for advice and consent and was consequently rejected in 2001. The significance of the US failure to ratify the Kyoto Protocol was that only 41 per cent of global GHG emissions are accounted for under the Protocol as the United States alone accounted for 23 per cent of GHG emissions in 1990. Furthermore, this provoked widespread international criticism, and undermined inter-national cooperation efforts towards the 'common but differentiated responsibilities' principle.

China increased its share of global GHG emissions more than two-fold, from 11 per cent to 23 per cent between 1990 and 2009

Secondly, the global economic landscape has changed significantly since 1990. Economic development has spurred growth in developing countries, which has also resulted in a huge change in the share of global GHG emissions. The initial Kyoto Protocol (with the exclusion of the United States) covered only 26 per cent of global GHG emissions in 2009. Most notably, China increased its share of global GHG emissions more than two-fold, from 11 per cent to 23 per cent between 1990 and 2009. India has also become one of the biggest emitters with 5.5 per cent of emissions. An effective mechanism to reduce global GHG emissions must be inclusive of the biggest emitters.

From Japan's perspective, a point of contention is the methodology of the quantified limitation targets. Japan's efforts towards energy efficiency have been highly successful; achieving further reductions would be a major challenge as

Japan is nearing its limit for improvement. By comparing Japan's primary energy supply per GDP unit with other countries, it is argued that Japan is the most energy-efficient country in the world (see Table 1). This demonstrates that for every unit of GDP produced, Japan uses one unit of energy. In comparison, the world average is 5.1 energy units, meaning that Japan is five times more energy-efficient than the world average.

An Asian regional research network is being established by the National Institute of Environment of Japan as a knowledge-share platform

The parties to the UNFCCC meet annually in the Conference of Parties (COP) summits to address these challenges but the outcomes of COP15 and COP16 have come in for criticism. COP15 which took place in Copenhagen in 2009 aimed for a global climate agreement for the period commencing from 2012, when the first commitment period under the Kyoto Protocol expires. However, the difficult task of reaching a climate agreement was put off to reach instead a less specific `politically binding' agreement. The outcome was the signing of the Copenhagen Accord, an agreement between the US on the one hand, and a united position by the BASIC countries (Brazil, South Africa, India and China) on the other hand. The Copenhagen Accord has been criticised for being vague and non-binding. This also led to a breakdown in international cooperation such that a few powerful countries dictated the proceedings and the outcome of the conference.

Due to the perceived failure of COP15, COP16, which was held at Cancun in 2010, had low expectations. The conference aimed to officialise the Copenhagen Accord towards a binding international agreement. The major

Green growth under the desert sun: Solar energy from the Middle East & North Africa outcome of the COP16 is the Green Climate Fund, where it is proposed that US$ 100 billion be mobilized for climate change adaptation and mitigation. Whilst not absent of criticism, COP 16 laid the foundations for COP17 and a new international agreement.

While the previous COP meetings did not produce positive outcomes, Ambassador Horie believes that COP17, held in Durban in 2011, was a paradigm shift in international climate negotiations. The Durban Platform was agreed as part of a legally-binding treaty to address global warming. The terms of the future treaty are to be defined by 2015 and will come into effect in 2020. The agreement is being acclaimed as, for the first time, it is inclusive not only of both developed and developing countries, but of the United States as well. The developed countries will have legally-binding quantity targets of GHG emissions, whilst developing countries will participate on a voluntary basis. This is in line with the common but differentiated responsibilities principle and recognises that not all countries can be bound by the same legislation.

The key criticism of the COP17 was the uncertainty regarding the future of the Kyoto Protocol. Although the EU and a few other countries committed to the second period of the Kyoto Protocol (2013-2018 or 2013-2020), Canada withdrew, whilst Japan and Russia did not commit. Ambassador Horie argues that because the Kyoto Protocol no longer represents the majority of the world's biggest emitters, it would be unfair for Japan to commit to legally-binding targets, while the biggest emitters are relieved of any external pressure to reduce their GHG emissions. Despite Japan's non-committal, it is important to note that Japan did not withdraw and continues to actively engage in the improvement of the Kyoto Protocol mechanism.

Whilst the Durban Platform has provided a promising foundation for climate negotiations, addressing the challenges in implementing the agreement will require further international cooperation. Agreements and mechanisms will have to be established in many areas, such as the level of responsibility of each country; the legal form of the framework; inclusion of major emitters, in particular China and India; and obligations of developing countries.

Meeting the challenges of the climate change problem requires international cooperation that goes beyond climate negotiations.

Japan is actively engaged in activities worldwide in facing the climate change challenge. The African Green Growth Strategy, which aims for low carbon growth and climate resilient development, is currently being funded by the Japanese government. An Asian regional research network is being established by the National Institute of Environment of Japan as a knowledge-share platform that consists of the leading environment-related research institutes of Asia.

The intention is to create a network that is capable of forming proposals that can influence policy-making and enable informed decision-making in the region. As a leading energy-efficient country, Japan is also helping developing countries reduce their emissions by adopting Japanese technology and by exhorting them to learn from Japan's experience.

The challenges faced in international cooperation on climate negotiations demonstrate the wicked nature of the problem of climate change. Although many barriers were faced and many still persist, the evolution of international agreements have demonstrated progress, and highlighted reasons to be optimistic. The key is to follow through with this paradigm shift in international cooperation and maintain the momentum achieved at the Durban Platform.

The China Conundrum and Implications for Southeast Asia

*D**r Yukon Huang**, Senior Associate, Carnegie Endowment, Washington DC, spoke on **'The China Conundrum and Implications for Southeast Asia,'** on 10 February 2012. ISIS Director of Economics, Mr Steven Wong chaired the Lecture. ISIS Analyst **Zarina Zainuddin** has the report.*

For one of the most studied countries in the world, China, said Dr Huang, elicits some of the most diverse views, ranging from the view that the nation is on the threshold of being a superpower to the view that it is on the verge of collapse!

Huang, who has somewhat unorthodox views on economic issues examined China from three aspects :

- One is China's unbalanced growth, which for most people is either a source of strength or a source of weakness, with most leaning towards the latter view.
- Two, China's trade surplus, particularly *vis a vis* the West, mirrors the trade deficits of the US and Europe, creating trade tensions globally .
- Third is China's struggle with the new economic model, one which promotes innovation as a way towards becoming a high income country, much as in the case of Malaysia.

To address the three issues, one needs to understand China's growth history, specifically Deng Xiaoping's 1979 era, said Huang. Deng was the architect of China's deliberate unbalanced growth strategy. He embarked on establishing production for export, the industrial bases of which were concentrated in coastal cities. He put in place various tax and credit incentives but limited them to the export-oriented-coastal-located industries (see Figure 1, p. 9).

Yukon Huang

Deng focused on the export-oriented industry because of its competitiveness, particularly against Chinese state industries. The move to establish coastal cities was followed by heavy investment in infrastructure. Soon migrant labour from inland, 250 million strong, started to move towards coastal cities such as Shanghai, Beijing and Guangdong. What Deng created was an area of concentration, specialization and economies of scale unrivalled elsewhere, which in turn made China a highly competitive nation.

Eventually, the rapid economic growth in coastal cities spread inland and created what became known as 'second', 'third' and 'fourth' tier cities. The economic growth in inland cities is now not only at par with coastal counterparts, these cities are also developing twice as fast, growing at the rate of 10 per cent annually. Thus, an unequal

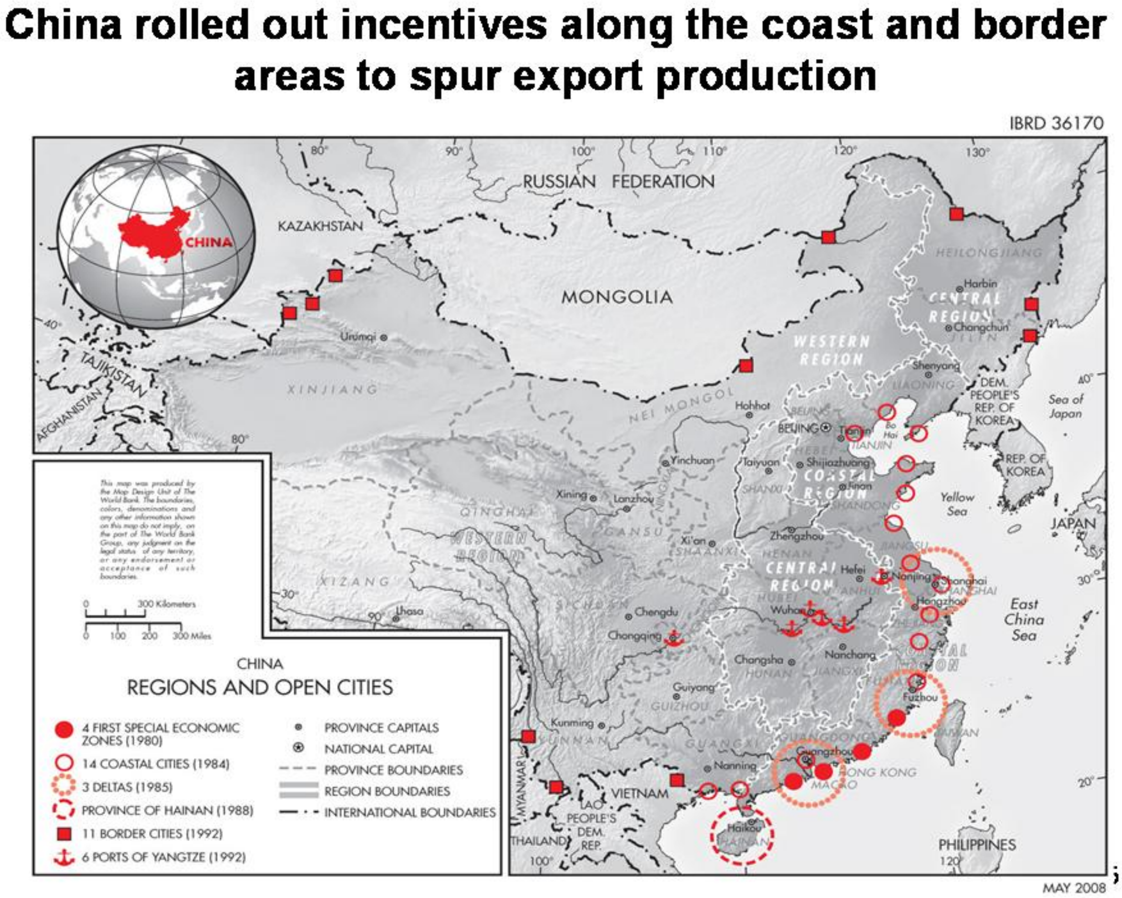

Figure 1

growth strategy, said Huang, if implemented properly, can be a good thing! (Figure 2, p. 10).

Currently there is a lot of concern about the imbalance between the rate of investments and the rate of consumption to GDP. As a share of GDP, China's consumption has fallen to 35 per cent, the lowest in the world, while investments have increased to about 48 per cent, the highest in the world. Many see this trend as a potential huge problem for China, but Huang said one should examine the underlying causes before making any conclusions.

One of the key questions to ask is whether consumption is being repressed. Figure 3 (p. 10) shows China's household/personal consumption has been growing at eight per cent annually. China has the fastest growing rate of personal consumption per person in the world — higher than India, South Korea and Brazil among others.

Why has consumption as a share of GDP fallen when personal/household consumption has been growing? The answer lies in China's development- the shift from an agriculture-based economy to an industrial-based one. Agriculture is more labour-intensive. Wages make up about 90 per cent of the cost of agriculture while the share of labour in production is only 50 per cent. As China shifted from agriculture to production, personal/ household consumption doubled, but the share of personal/household consumption to income (GDP) was reduced (Figure 4, p. 11).

The falling share of personal consumption to income could also be explained by the increase in the number of private enterprises and the corresponding reduction in the number of state enterprises. State enterprises tend to be more labour-intensive and worker remuneration is generally higher than in private enterprises. So as

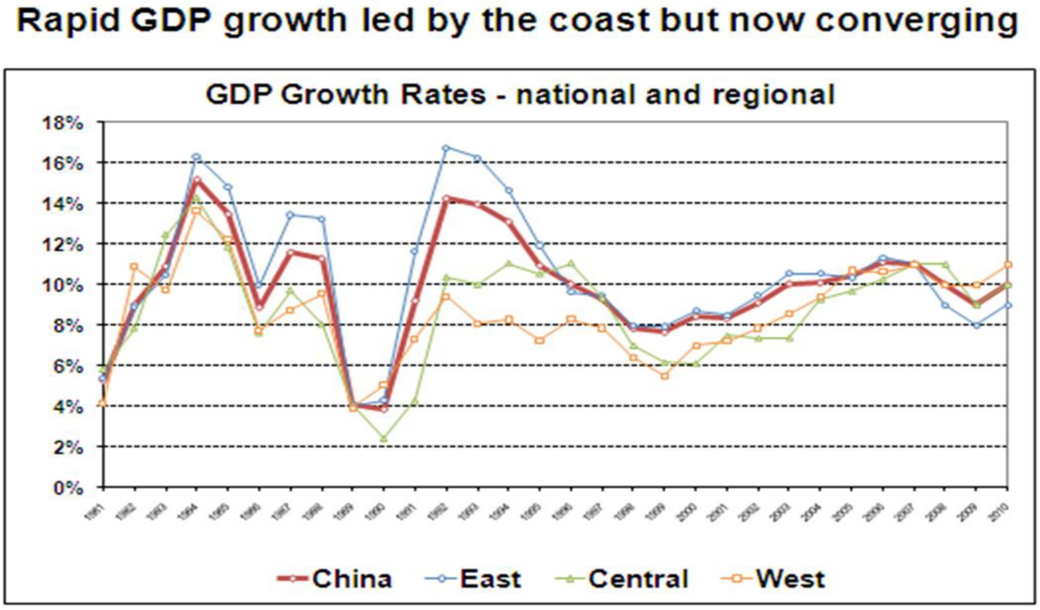

Figure 2

private enterprises become more dominant, the smaller number of workers and lower wages contribute to the lower share of personal/ household consumption to total income.

Another factor to look at is the savings rate. The household savings rate, particularly in urban areas, has been rising. Chinese household savings increased from 20 to 35 per cent. The increased savings rate is important because of the implications to trade, specifically China's trade surplus (in calculating national income, the excess of savings over investment equals trade surplus). Many scholars have attributed the increase in the savings rate to factors such as China's weak social security system, its demographic trends, interest rates, etc. Huang on the other hand focuses on one unnoticed factor – the saving habits of migrant workers. The 250 million strong migrant workers do not get access to many of the benefits other workers get, hence they save twice as much as their urban counterparts. He speculated that a change in migrant worker habits towards savings and consumption would affect China's trade

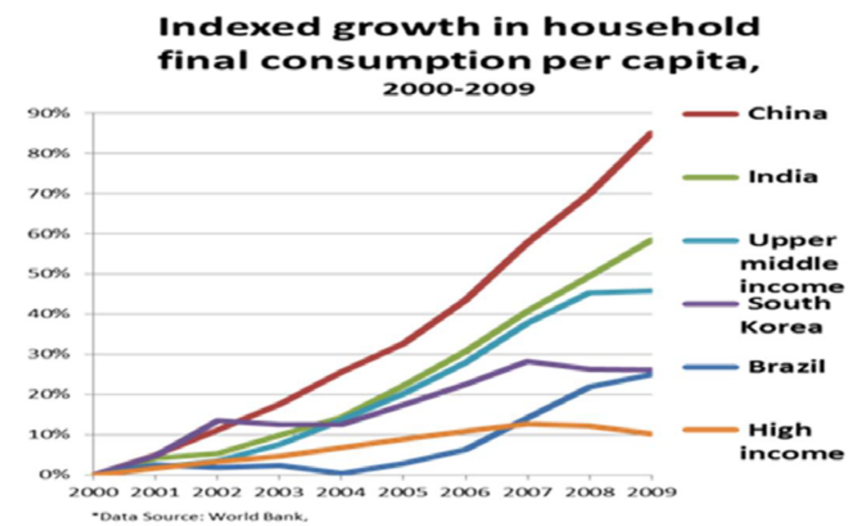

Figure 3

Sector Shifts and Impact on Labor's Share of GDP

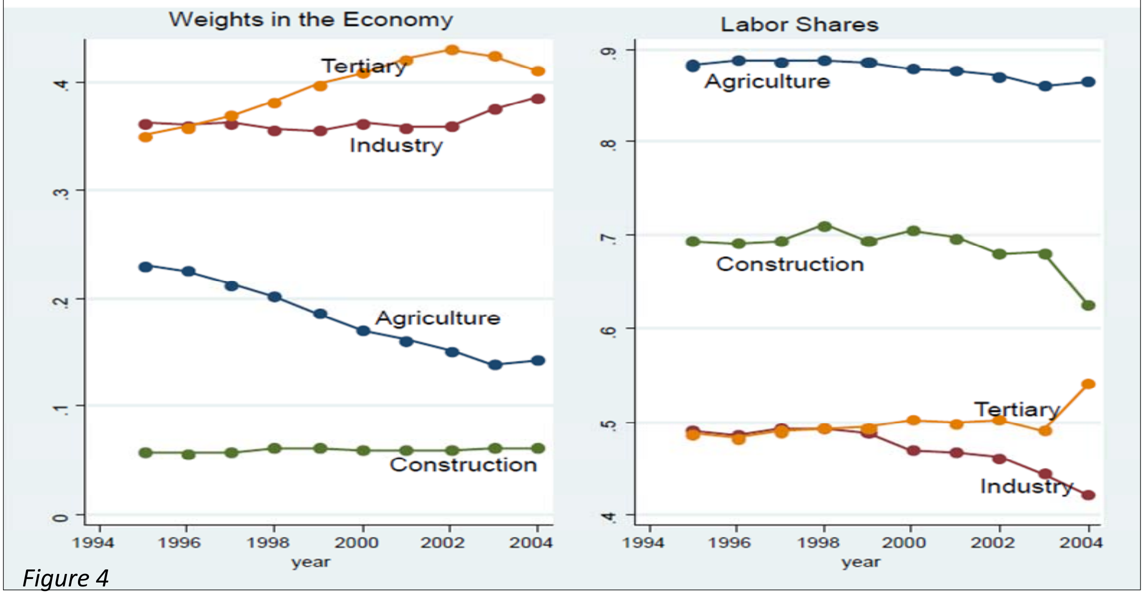

Figure 4

surplus, adding jestingly that if migrant workers were to save less and consume more, China's trade surplus problem would soon be a thing of the past!

The Implications of the China Conundrum for Malaysia and Southeast Asia

In discussing the situation in China and its implications for Malaysia, Huang looked at five aspects:

1. Does spatial concentration matter?
2. Are trade relationships becoming more differentiated?
3. Are regional investments and wage rates linked?
4. Can countries become more innovative than expected for their income level?
5. How to deal with inequality?

Unbalanced growth and the concentration of economic activities can create wealth. That is what the growth experiences of China tell us. Urbanization and internal migration are tools to facilitate economic concentration. In Table 1 (p. 12), Huang lists the criteria for measuring concentration of economic activities, which include the rate of urbanization and urban and job density. Malaysia despite being one of the most urbanized countries in Asia, scored the lowest in 'Deng Xiaoping's concentration index' as indicated by its low urban and job density scores. In the Klang Valley, jobs, people, universities and other economic activities are scattered too widely.

In a globalized world, spatially concentrated activities, specialization and economies of scale in production will determine success. Part of the reason the East Asian countries are trade powerhouses lies in their use of production-sharing networks and their intra-trade in parts and components (processing trade). Such activities allow even the smallest countries in East Asia to achieve economies of scale and specialization which in turn allow them to produce goods efficiently. East Asian nations lead the world in the trading of parts and components across borders.

However this could pose a problem for China as China's trade surplus is a result of the trade in parts and components and not because of its exports (the difference between exports and imports is also a measure of trade surpluses/ deficits).

Malaysia has the lowest density Indicators despite perception of being highly urbanized

	% Urban	% in cities > 1 million	Urban Density Pers/ha	Job density ʻjobs/ha
Malaysia	67	6	58 (KL)	24 (KL)
China	50	20	123 (Beijing)	96 (Beijing)
Thailand	32	10	139 (Bangkok)	74 (Bangkok)
Indonesia	48	12	173 (Jakarta)	67 (Jakarta)
S. Korea	81	51	230 (Seoul)	109 (Seoul)
Philippines	63	14	206 (Manila)	92 (Manila)

Table1

All of East Asia ship their parts and components to China to be assembled and shipped world-wide. So, trade surpluses of all of East Asia are showing up as China's trade surplus. Therefore, when Americans and Europeans complain about China's trade surplus and exchange rate, it is not really about China, it is really about the East Asia trade network system (Figure 5, p. 13).

Renminbi appreciation will not help address the trade imbalance between China and the West. The production-sharing system of the region renders the action of a single currency less effective. As East Asian economies become more integrated and intertwined, their currencies begin to move in tandem. So the issue of the Chinese trade surplus is more complex; it is less about China and more about the region's ability to compete and produce efficiently, and of currency alignments, all of which were brought about by the region's production-sharing network.

Investment Rate and Wages in East Asia

Since the Asian financial crisis of 1997, it has been noted that East Asian countries have not fully

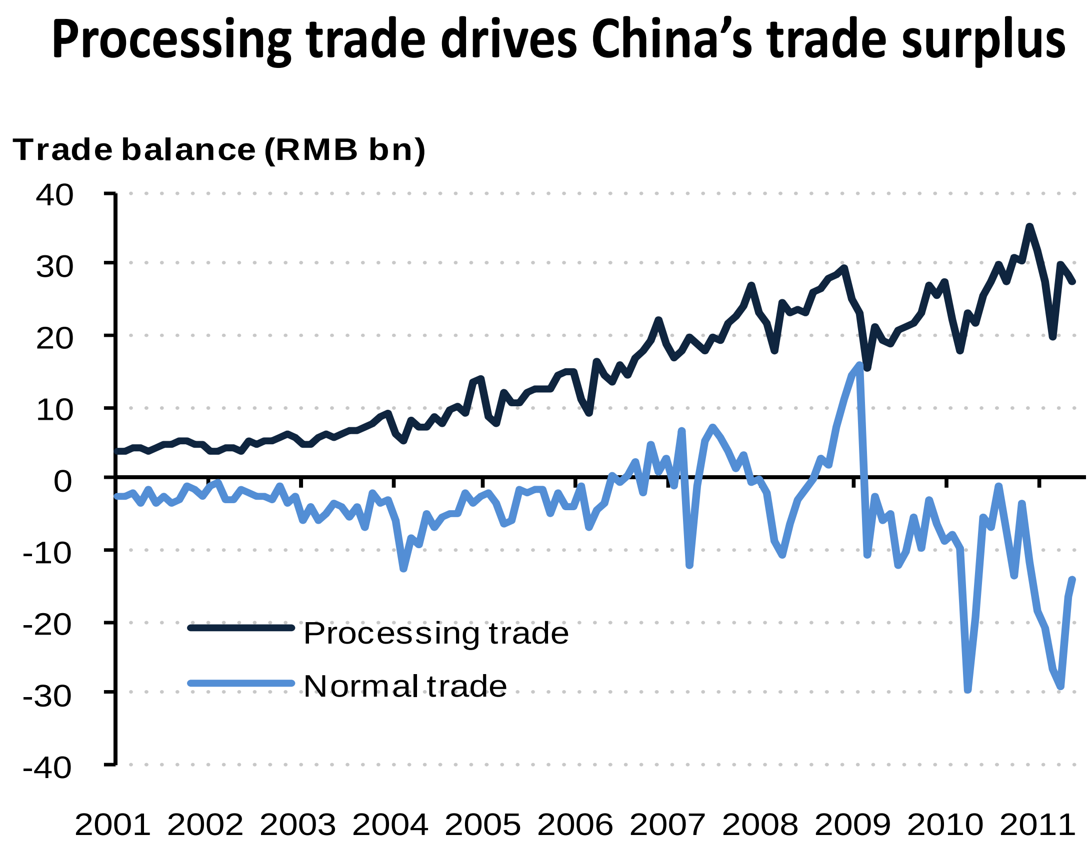

Figure 5

recovered from the collapse of FDI. For most East Asian countries, investment rates, as measured by the percentage of investments to GDP, are lower than pre-crisis levels. Huang contended that investment rates do not give the full picture.

Due to the increasingly integrated production-sharing network in the region, the more appropriate measure would be the capital stock of a country (see Figure 6, p. 14). The capital stock of a country looks at the country's investment minus depreciation relative to the size of the economy. Figure 6 shows that not only have East Asian countries (with the exception of the Philippines) been utilizing capital more efficiently, but that their capital stock ratios or value of production are now becoming more closely aligned to each other.

Furthermore, individual countries have to some degree lost the power to control investment since investors are now looking at opportunities at the regional level. Production 'is no longer a country issue, production is the question of the network controlled by many different elements and we can no longer look at production for trade as a country issue.'

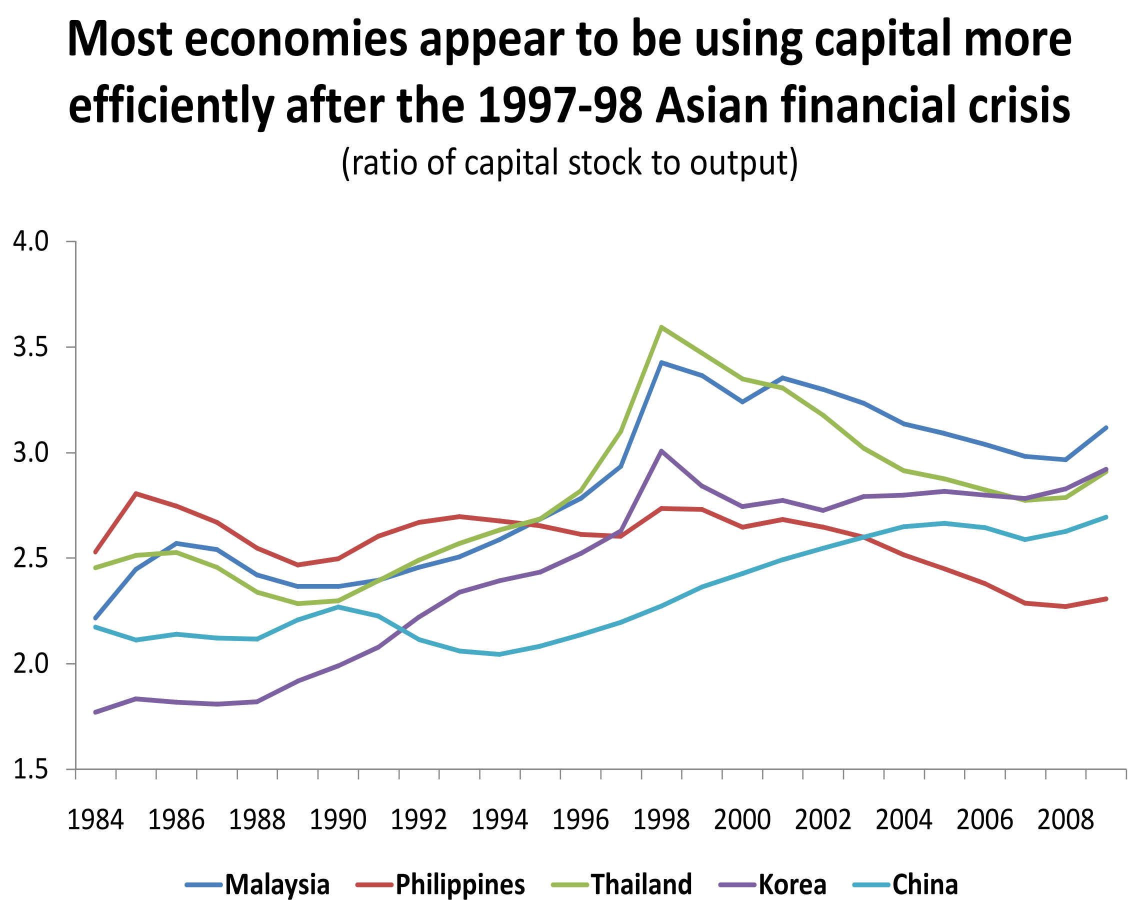

Figure 6

Likewise the wage rates for countries in the region, including Malaysia, are being influenced by the wage rate in China because of the production–sharing network. China's wage rate is growing at a rate of 10-12 per cent in real terms. When a country's labour productivity increases very dramatically, it represses the growth rate of another country because the production-sharing network shapes where people want to buy and make things and that puts pressure on costs and prices.

Huang shared an interesting finding on the subject of innovation. The general view is that innovation is a powerful variant that increases wealth. However, said Huang, it is the other way around – it is the wealth of society that determines how innovative a country is. In other words, as one becomes wealthier, one becomes more innovative! The implications are interesting as many countries are implementing policies to promote innovation in an effort to move up the income ladder (see Figures 7 & 8, p. 15).

While wealth determines innovation, China has shown that innovation can assist a country to grow, not by being innovative but by being able to adapt technology available globally faster than any other country can. Huang said the secret to growth is adaptation intensity, not innovation, and

East Asian economies are innovating no more than comparators with similar income levels

(ranking)

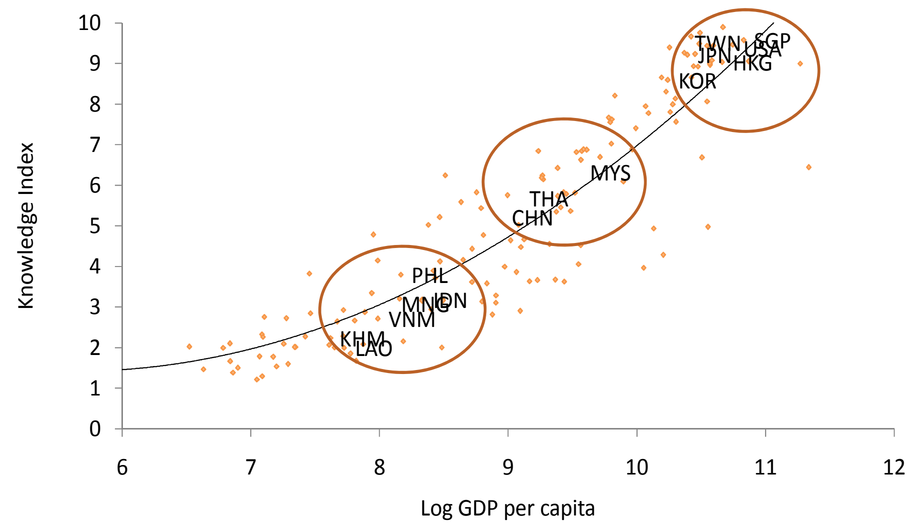

Figure 7

But China really stands out in terms of adoption of technology

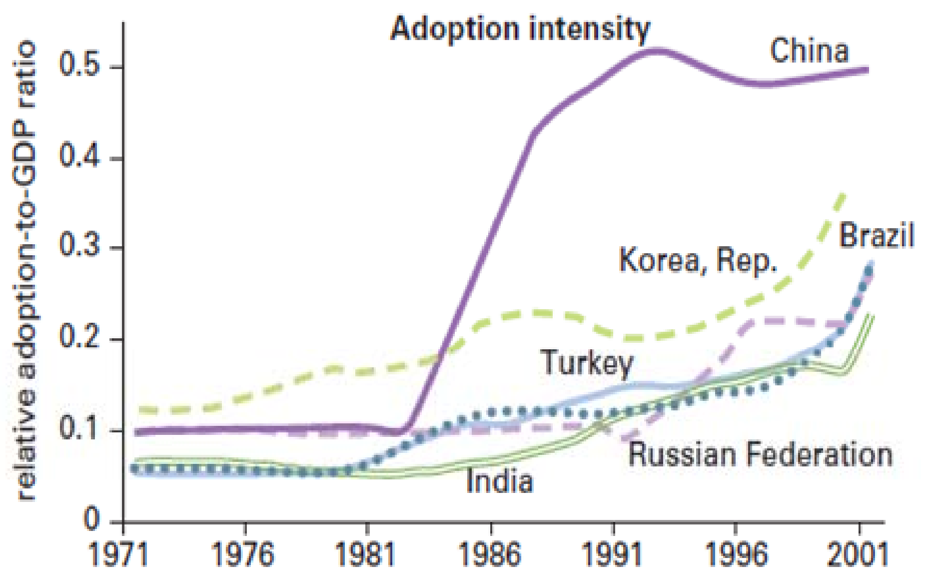

Figure 8

the big issue coming up is not trade war but a technology transfer war!

Lastly, Huang briefly compared the paths to development of China and Malaysia and the outcomes of both programmes. While China deliberately adopted an unbalanced growth strategy, Malaysia adopted a balanced growth strategy which aimed at equalizing opportunities so that wealth could be shared by all stratas of society. Both countries have done well in reducing poverty. Interestingly, both countries experienced the same level of income inequality (Gini coefficient measurement) despite adopting opposite strategies!

China's income inequality is a spatial issue – urban/rural and coastal/inland. In the past, inequality in Malaysia was the result of inter-ethnic inequality, and programmes implemented at correcting such inequality made sense. However in present day Malaysia, ethnic inequalities are less severe; it is spatial inequalities — urban/rural, west/east coast of Peninsular Malaysia, and Peninsular Malaysia/East Malaysia — that are more worrisome.

In the final part of his talk, Huang spoke on Malaysia's place in the East Asian production-sharing network. He felt that Malaysia is handicapped from efficiently feeding into the region's production-sharing network by its current 'groups, structure and organization society'. It is something that Malaysia has to address, given the increasing integration of the region's economies, and competition from its neighbours for a share of the pie. While Malaysia has fared fairly well in its economic development, it still faces some very difficult issues and therefore ingenuity, creative thinking, political will and favourable circumstances may well be required in taking the next step forward.

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