

## Beware of the high-income trap



**RAISING THE BAR:** *There is a need to accelerate reform agendas in our labour market, education system and budgetary planning*



*Bangladeshi foreign workers at a construction site in Kuantan, Pahang. Excessive reliance on migrant labour has masked productivity growth of local workers which is even lower than workers from Bangladesh.*

BY 2020 or 2025, Malaysia will finally attain the much coveted title of high-income status, an occasion that will surely be accompanied by much fanfare when the per capita clock finally strikes US\$15,000 (RM63,037).

Then, it becomes apparent that we had somehow outgrown the travails of our past without much difficulty, like a common cold. Issues that used to affect us as a middle income nation will seem distant and irrelevant, in particular, worries of being stuck in a middle-income trap.

We have grown the economy larger for all Malaysians without much hurdle. Friendly ties have helped us move up the value chain by facilitating quicker imports of foreign capital, technological know-how and labour.

Whenever a crisis hits, a combination of outright fiscal and monetary stimuli, and the occasional use of capital controls, have enabled us to bounce back stronger and more resilient.

We take centre stage, greeted and congratulated by the rest of our high-income peers, while our critics and sceptics cringe away at the back. Attaining this high-income status is the final seal of validity to our tried and tested economic model, which we can continue to comfortably rely on.

However, herein lies the greatest fallacy of our irrational exuberance and obsession with attaining this high-income status. What is missing in the discussion among our policymakers is the risk of a high-income trap.

By postponing necessary reforms, high-income countries, just like their middle-income counterparts, are equally susceptible to this pitfall of prolonged periods of little or no economic growth after decades of momentous growth.

Sure, we can put on the high-income cape, but still retain our middle-income Achilles heel. The issue is not when, but how we achieve this high-income status. By not undertaking crucial reforms today, we are only setting ourselves up for a potentially devastating high-income trap in the not too distant future, reaching a tipping point that may take years, if not decades, to recover from, as experienced by many high-income nations still stuck in their high-income traps.

To be sure, Malaysia is particularly proactive in seeking external interventions when it comes to addressing its middle-income trap woes. Our look-here, look-there policy is not new. Interestingly enough, our attention towards any particular foreign model changes whenever it hits a brick wall.

We were enthralled by the Western approach, then the Japanese way, the Asian miracle and the oil-rich Gulf states. Of late, we increasingly rely on China, before coming full circle with Look East Policy 2.0.

As proficient as we are at emulating the successes of others while they last, we failed to take stock of their subsequent failures; since the global financial crisis, half of the developed world are still reviving their economies using only fiscal and monetary stimuli. The much needed economic reforms remained in the backburner.

Japan is the proverbial poster boy of this high-income trap. Wages have stagnated for over two decades, while the broader economy has flirted in and out of recession for the fourth time even as the Bank of Japan introduced negative deposit rates.

The experiences of Greece and the broader Eurozone are not unfamiliar to us. Their economies continue to hobble along in a low growth environment until today.

Although the United States has been a brighter spot, ending a decade-long experiment of zero interest rate, it is contingent on China making the necessary reforms while avoiding a hard economic landing without dragging the rest of the world along with it.

Sure, we can step up fiscal and monetary stimuli today and achieve any growth targets we want while coexisting with growing income inequality, brain drain, subpar education system, human trafficking, competition from emerging neighbours, dominance of government-linked companies in the local economy and deteriorating commodity prices.

Excessive reliance on stimuli also masks the miserable productivity growth of Malaysian workers, which has only grown by an average of 2.1 per cent per annum for the past 20 years. It is the lowest among Asean members. It is also lower compared with workers in Bangladesh.

In a post high-income Malaysia, however soon that may be, once we have exhausted our fiscal and monetary ammunition and potential foreign models to emulate, can we still prop up growth while sidestepping critical reforms?

This is our potential high-income trap, if we are not already experiencing it to a certain extent. We should be accelerating the reform agendas in our labour market, education system, budgetary planning and the broader political economy, rather than our quest for achieving the high-income status.

*The writer is an analyst (Economics) with the Institute of Strategic and International Studies (ISIS) Malaysia*