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Abstract
The purpose of this paper is to examine and evaluate the extent to which the New Economic Policy (NEP) has been effective as an instrument for national integration in Malaysia. Based on a comparison of the situation before and after the implementation of the NEP, it is argued that although national development has been moving towards the achievement of the NEP objectives, ethnic tensions and conflict remain serious. While economic factors are important in preventing ethnic conflict, they are not sufficient to promote ethnic integration.

Economic Development and Ethnic Integration: The Malaysian Experience

H. Osman-Rani

The purpose of this paper is to examine and evaluate the extent to which the New Economic Policy (NEP) has been effective as an instrument for national integration in Malaysia. Based on a comparison of the situation before and after the implementation of the NEP, it is argued that although national development has been moving towards the achievement of the NEP objectives, ethnic tensions and conflict remain serious. While economic factors are important in preventing ethnic conflict, they are not sufficient to promote ethnic integration.

Introduction

A major challenge that Malaysia has been facing emerged from the creation of a multi-ethnic society[1] with different cultures, languages, religious beliefs, and socio-economic strata. This diverse mix of the population has fairly short historical roots.[2] Suffice it to say that the development of a dual economy (namely, an export-oriented commercial sector and a subsistence agricultural sector) and the emergence of a communal ideology under a century of British rule segmented Malaysian society along ethnic, occupational, and geographical lines.

While colonialism set the stage for ethnic friction during the post-independence era, at the centre stage was the so-called historic bargain struck by the Alliance, a coalition of multi-ethnic ruling élites. This was enshrined in the 1957 Merdeka Constitution as Article 153. The Constitution provided for Malay "special rights"[3] to improve their economic position in exchange for "political rights" to the non-

Malays by offering them citizenship status on the basis of *jus soli*.

Although the importance of national integration and unity was recognized immediately after independence, it was taken much for granted by the political masters of the time perhaps because it was thought that the spirit of independence itself might be sufficient to bind together the various ethnic groups by way of the "historic bargain", which tended to symbolize mutual trust, tolerance, and compromise;[4] or perhaps it was considered not critical and well within control as long as Malay political dominance could be maintained through the existing arrangements. Indeed, the prevailing attitude of the political leaders then was one of promise for the future and confidence in the institutional arrangements that had been put in place. There was a widespread belief that ethnic integration depended ultimately on economic development, in that rising prosperity accompanied by social modernization would eventually resolve communal antagonism, a belief shared by both Malays and non-Malays. Indeed, if there existed a notion of equity in the Alliance development strategy, it involved the equitable distribution of growth between the major ethnic groups rather than the redistribution of income and wealth between social classes. It was this very assumption of equity that provided the Alliance with a politically warranted rate of economic growth (Rudner 1975). It also reflected the Alliance's own interethnic commitment at the level of economic policies and strategies.

Moderate growth was achieved from independence until the outbreak of racial riots on 13 May 1969. Average annual growth rates of GDP and GDP per capita between 1958 and 1969 were 6.1 per cent and 3.3 per cent respectively. It was after the May 13 riots that the issue of national integration and national unity became more seriously exposed and explicitly translated into the New Economic Policy (NEP). Basically, the NEP was, and continues to be, an extension of past economic policy, where Malay "special rights" remain the cornerstone of the NEP, except that this time it became more openly and more forcefully expressed with direct state intervention. Whether such an approach may be considered more effective in forging national unity is a subject of major concern.

The purpose of this paper is to examine and evaluate: (1) the economic policies and trends that culminated with the May 13 incident and consequently the launching of the NEP in 1971; (2) the performance of the NEP and its effectiveness as an instrument of national integration; and (3) possible policy options.

1957–70: Malay "Special Rights" and Free Enterprise

On the eve of independence, Malaysia was already characterized by an economic scene in which the Chinese played an active role in commerce and industry, albeit largely confined to small and medium enterprises, while the bulk of big businesses were foreign-owned. Malay bureaucrats and aristocrats were rather indifferent to economics but concentrated on administration and politics. However, this does not mean that the majority of Malays were not aware and not concerned with their economic backwardness.[5] Economic inequalities were already present long before independence (Soltow 1982, 1983). Nevertheless, ethnic conflict was well contained for some years after independence.

There are several possible reasons for this. Firstly, the "historic bargain" was still fresh in the minds of the people, especially of the respective ethnic leaders. The bond of friendship and trust at the top Alliance leadership was particularly strong. Secondly, the tension, if any, was bound to be submerged as long as one community was too strong and the other too weak (Muzaffar 1984). Thus, the numerical weakness of the Malay community in economics and that of the non-Malays in politics was partly responsible for the superficial sort of social equilibrium that prevailed. This equilibrium, however, turned out to be very unstable.

Thirdly, the so-called special rights of the Malays, which were supposed to provide the impetus for Malay participation in commerce and industry, had never been effective under the free enterprise system, a system which had been in existence during colonial times (Pillay 1974). The implementation of it was also constrained in the beginning by the economic and administrative weaknesses of the Malays (Lim 1985). For example, Malay land reservations were not only insignificant but also enclaved the Malays in economically backward locations with their traditional economic activities. Scholarships too had not been given sufficient weight to enable poor Malays to enjoy higher education. The benefits of modern education still went largely to the non-Malays. The increase in recruitment of Malay civil servants served only to prevent Malays with potential from being directly involved in business and industry. Licences and permits to the Malays did not mean much since in practice trade and industry continued to be largely in the hands of foreigners and the non-Malays. In fact, the "special rights" had no value to most Malays in rural areas as they were (and still are) in poverty. For all these reasons, there was no need for the non-Malays, especially the capitalists, to be envious of the "special rights", let alone to be threatened by them.

Fourthly, there was always the hope that a faster rate of economic development would be able to satisfy two criteria simultaneously: (1) the equilibrium between Malay aspirations for progress towards parity with other communities and non-Malay desires to protect and improve their living standards; and (2) a continued Malay and non-Malay adherence to the inter-communal arrangement which would then serve to strengthen the political control of the existing government.

All along, the economic philosophy of the Alliance (later known as the National Front) government hinged on private enterprise as a logical concommitant of political democracy. Related to this was the Alliance conviction that economic expansion based on an open economy (although some would perhaps prefer to call it a dependent economy) required a continuation of the nation's traditionally liberal trade policy. Lacking capital, technology, know-how, and market connections, it logically follows that the economy had to rely on the import of foreign capital and direct foreign investment. In short, the scope of the government's economic policy was circumscribed by "neo-classical" notions about free enterprise, liberal trade, and foreign capital. This growth model was supposed to work on the assumption that problems of poverty and inequality could automatically be resolved through a "trickling down" process. The influence of the World Bank (International Bank for Reconstruction and Development, IBRD) on Malaysian planning was crucial to this mode of thinking. This led to the government taking a passive role in the management of the economy; that is, the government was to provide adequate infrastructure and incentives for economic development while private enterprises would be the active participants in the economy.[6]

However, in recognition of the seriousness of Malay poverty in rural areas, rural development then was seen as an important means and a sole means for the Malays to catch up economically with the non-Malays. Massive public investment was therefore shifted to rural areas. The Rural and Industrial Development Authority (RIDA) which started operating in 1950 to look after rural development was revitalized. The main thrust of RIDA was directed at development schemes for roads, bridges, social amenities, and giving loans and training to Malays for various developmental projects. However, the role of RIDA became too big and eventually suffered due to financial constraints and poor management. Malay demand for an adequate stake in the economy was obviously not met by the kind of rural programmes designed by RIDA. The Federal Land Development Authority (FELDA) schemes which were launched in 1956 played a more significant role in improving the lot of rural Malays through the clearing of jungle, creation of prosperous farming communities, and opening up of employment opportunities. The schemes were not cheap to operate. Hence, the number of participants to total Malay farming population fell far behind expectation, something in the ratio of 1:10 (Jomo and Ishak Shari 1986). The benefits of rural development did not go exclusively to the Malays: the Chinese capitalists also gained from the construction and business activities that went with rural development.

Meanwhile, with the promulgation of the Pioneer Industries Ordinance 1958, industrialization based on an import-substitution strategy became one of the pillars of the economy. In terms of growth, the manufacturing sector performed relatively well under the policy which allowed for free enterprise private initiatives. True to its conviction, the government played an indirect role in facilitating the growth of foreign and local investments through the provision of incentives and subsidies (for example, tax holidays, tariff protection, and industrial estates) and the training of labour. The main beneficiaries of these policies were mainly foreign and, to a lesser extent, Malaysian Chinese capitalists. Malay participation in commerce and industry, construction and mining was merely token: there were only a small number of Malay-owned or -controlled companies, while others had only a token number of Malays on their boards of directors. In 1970 *bumiputera* (Malay and other indigenes) effectively owned only 1.6 per cent and trust agencies 0.8 per cent of the share of capital in limited companies, whilst foreigners held 63.3 per cent and non-*bumiputera* Malaysians 34.3 per cent.

These trends did not go unnoticed. In the mid-1960s, there was already a strong protest by the First Bumiputra Economic Congress (Konggeres Ekonomi Bumiputra [KEB] 1965). The Congress expressed the need for greater participation of *bumiputera* in the modern sector and greater ownership of companies. Subsequently, RIDA had to be reorganized and expanded into MARA (Majlis Amanah Rakyat, Council of Trust for the Indigenous People) with more financial support. The number of scholarships offered to Malays increased. The intake of MARA Institute of Technology (ITM) expanded. Bank Bumiputra was established in 1965 with an authorized capital of M$20 million to provide credit and assistance to *bumiputera* traders and businessmen. The MARA Unit Trust was set up in 1967 to mobilize Malay savings. The Associated Malay Chamber of

TABLE 1
Peninsular Malaysia: Income Distribution by Income Group, 1957/58 to 1984

Income Group	Ethnicity	Strata	1957/58	1970	1976	1984
Top 20 per cent	Malay	Rural	40.0	49.0	51.8	50.0
		Urban	44.3	51.3	53.7	52.1
		Total	42.5	52.5	53.9	51.9
	Chinese	Rural	42.8	47.4	54.4	47.8
		Urban	48.3	55.0	56.1	51.1
		Total	45.8	52.6	56.1	51.0
	Indian	Rural	38.1	44.6	46.1	42.4
		Urban	51.9	59.4	56.1	49.9
		Total	43.7	54.2	52.6	48.4
	All		48.6	56.1	57.7	53.2
Bottom 40 per cent	Malay	Rural	20.8	15.1	12.6	14.1
		Urban	18.9	14.0	13.4	13.9
		Total	19.5	12.7	11.8	13.3
	Chinese	Rural	19.8	16.5	13.6	16.2
		Urban	16.5	13.5	12.5	13.7
		Total	18.0	13.9	12.6	14.2
	Indian	Rural	22.8	18.6	17.7	19.3
		Urban	14.9	11.5	12.3	14.4
		Total	19.7	14.3	14.7	16.3
	All		15.9	11.2	11.1	12.8

SOURCE: *Household Income Survey*, respective years.

Commerce was formed in 1967 to act as a Secretariat for Malay capitalists. Before such measures could show any tangible results, there had been a severe decline in commodity prices, particularly rubber, an increase in unemployment, and a drop in incomes. Spending was sluggish and the rate of capital formation slowed down (Datar 1983). The Second Bumiputra Congress (Konggeres Ekonomi

TABLE 2
Peninsular Malaysia: Gini and Mean/Median Ratios

Ethnicity	Strata	1957/58	1970	1976	1984
Gini ratios					
Malay	Rural	0.357	0.419	0.471	0.447
	Urban	0.357	0.445	0.478	0.462
	Total	0.342	0.466	0.494	0.469
Chinese	Rural	0.337	0.399	0.486	0.412
	Urban	0.404	0.474	0.507	0.456
	Total	0.374	0.455	0.505	0.452
Indian	Rural	0.283	0.363	0.388	0.347
	Urban	0.441	0.502	0.504	0.441
	Total	0.347	0.463	0.458	0.417
All		0.412	0.502	0.532	0.480
Mean/median ratios					
Malay		1.241	1.451	1.481	1.466
Chinese		1.345	1.483	1.640	1.467
Indian		1.207	1.590	1.494	1.421
All		1.378	1.599	1.642	1.515

SOURCE: As for Table 1.

Bumiputra Kedua [KEB Ke-2] 1968) followed, at which the weaknesses of *bumiputera* performance was raised again:

> But in spite of the above-mentioned measures undertaken by the Government, the Bumiputera because of their lack of capital and know-how, are unable to avail themselves fully of the facilities so provided. (KEB Ke-2 1968, p. 107)

As a result, the pressure to increase state intervention to help the Malays heightened.[7]

The reactions of foreign and Chinese capitalists towards increasing Malay participation in business through state intervention was rather mild (Lim 1985). This was perhaps partly due to the ineffectiveness

TABLE 3
Malaysia: Household Incomes by Ethnicity
(In 1970 prices, M$/household/month)

Ethnicity	Mean/Median	1957/58	1970	1976	1984
Malay	Mean	139	177	345	852
	Median	112	122	233	581
Chinese	Mean	300	399	787	1,502
	Median	223	269	480	1,024
Indian	Mean	237	310	538	1,094
	Median	188	195	360	770
Total	Mean	215	267	514	1,095
	Median	156	167	313	723
Mean ratio					
Chinese:Malay		2.158	2.541	2.281	1.763
Indian:Malay		1.705	1.751	1.559	1.284

SOURCE: As for Table 1.

of the government to generate Malay capital and to improve rural development even with Malay "special rights";[8] and partly because of the greater gains made by the non-Malays during the past, which were not initially recognized because of the widespread practice of having token Malay representatives on the boards of directors of companies which came to be known as "Ali Baba" companies. Nevertheless, with erratic world commodity prices and the limitations of an import-substitution industrial strategy, the GDP growth rate declined from 6.3 per cent per annum in 1960–65 to 5.5 per cent in 1966–70, unemployment increased from 6 per cent in 1962 to 8 per cent in 1970, and income distribution worsened.

As shown in Table 1, in 1957/58 the bottom 40 per cent of the population held 15.9 per cent of the total income while the top 20 per cent of the population held almost half of the total income; by 1970 the share of the bottom 40 per cent declined to 11.2 per cent while about

56.1 per cent of the income went to the top 20 per cent of the population. Measures of Gini and mean/median income ratios (Table 2) also confirm the trends. The Gini ratio increased from 0.412 to 0.502, and the mean/median income ratio increased from 1.378 to 1.599 during the same period.

The widening of income inequality during 1957–70 was also observed within ethnic groups. The income shares of the bottom 40 per cent of Malay, Chinese, and Indian populations declined from 19.5, 18.0, and 19.7 per cent respectively in 1957/58 to 12.7, 13.9, and 14.3 per cent in 1970 (Table 1). On the other hand, the income shares of the top 20 per cent increased from 42.5, 45.8, and 43.7 per cent to 52.5, 52.6, and 54.2 per cent respectively within the same period. The same phenomenon may be seen if we were to examine changes in the Gini ratio as well as the mean/median income ratio (Table 2) where, regardless of ethnicity, the indicators show a widening trend in the 1957–70 period. Table 3 indicates the mean and median incomes by ethnicity. It shows that the income gap between the Malays and non-Malays widened during the same period.

From Table 2 we can also see that there was greater inequality within all the three ethnic groups between 1957/58 and 1970, as indicated by higher Gini ratios in the latter year. A similar pattern is seen in the ratio trends within each ethnic group in both rural and urban sectors. All the ratios show an increasing trend. Based on a recalculation which takes into account changes in the poverty line, which was M$151.2 per household per month in 1957 and M$166.1 in 1970, Ikemoto (1985) found that the incidence of poverty was virtually unchanged at around 50 per cent during the 1960s.[9] He also observed that since the poor became poorer during this period, the incidence of poverty may be thought to be more serious in 1970, meaning that the extent of poverty might be worse than the figures of poverty incidence indicate.

The relative decline in the economic position of the Malays, on the one hand, and the dissatisfaction of the majority of Chinese towards

TABLE 4
Incidence of Poverty, Employment Shares, and Capital Ownership
(In percentages)

		Pre-NEP (Actual)		NEP Targets (Estimated)		NEP Results (Actual)	
		1957/58	1970	1980	1990	1980	1985*
Incidence of poverty							
Rural		59.6	58.7	43.1	23.0	37.7	24.7
Urban		29.7	21.3	15.8	9.1	12.6	8.2
Total		51.2	49.3	33.8	16.7	29.2	18.4
Malay		70.5	64.8	Decline	39.3		
Chinese		27.4	26.0	Decline	16.5		
Indian		35.7	39.2	Decline	20.5		
Employment shares in economic sectors							
Primary	Malay		60.2	67.6	61.4	73.1	73.2
	Chinese		24.9	21.4	28.3	16.4	16.3
	Indian		14.9	11.0	10.3	10.5	10.5
Secondary	Malay		25.7	30.8	51.9	42.5	44.3
	Chinese		58.1	59.5	38.1	47.9	46.1
	Indian		16.2	9.7	10.0	9.6	9.6
Tertiary	Malay		31.0	37.9	48.4	48.4	50.3
	Chinese		46.0	48.3	39.0	42.0	40.3
	Indian		23.0	13.8	12.6	9.6	9.4
Ownership of share capital in limited companies							
Bumiputera			2.4	16.0	30.0	12.5	17.8
Individuals			1.6	3.4	7.4	5.8	10.1
Trust agencies			0.8	12.6	22.6	6.7	7.7
Other Malaysians			34.3	40.4	40.0	44.6	56.7
Foreign residents			63.3	43.6	30.0	42.9	25.5

NOTES:
*1984 figures are given for "incidence of poverty".
"Primary sector" refers to agriculture; "secondary sector" covers mining, manufacturing, construction, utilities, and transport; "tertiary sector" covers wholesale and retail, banking, public administration, education, health and defence.

SOURCE: Malaysia 1976, 1981, and 1986.

"treatment by a perceived Malay government with respect to a question of land alienation, citizenship, white terror and the issue of Chinese education" (Hing 1984) on the other, were fully exploited by politicians and the resentment of these communities became evident in the 1969 general election results. The decline in support for the Alliance (including UMNO) in the general elections indicated a loosening of the Malay political grip and increased the fear of the Malays regarding the ability of UMNO and the Alliance to protect them.[10] The gains made by Chinese-based political parties at the same time induced an over-confidence among the Chinese electorate in their search for legitimate forms of control of the country and the economy; and this was expressed through their provocative post-electoral celebrations (Ongkili 1985). This interaction between fear and provocation eventually sparked off the May 13 riots.[11] As a solution to this ethnic conflict, the NEP was proposed by the Malaysian Government in 1970.

After 1970: The NEP and State Intervention

The NEP was formally presented in the Second Malaysia Plan (1971–75) with the aim of redirecting Malaysia's development policy from "growth" to "redistribution with growth", which became the stated goal of the World Bank model for development in Malaysia in the 1970s. The NEP had two immediate objectives, through which it ultimately aimed to achieve national unity. The first objective was "eradicating poverty by raising income levels and increasing employment opportunities for all Malaysians irrespective of race", and the second objective was "accelerating the process of restructuring Malaysian society to correct economic imbalance, so as to reduce and eventually eliminate the identification of race with economic function" (Malaysia 1973, p. 1). The NEP thus assumes that the primary sources of conflict are essentially inter-ethnic disparities rather than inter-class disparities. This is also reflected in the Report of the

Committee on the NEP which outlined that the problem had been studied "in terms of the imbalance between the two groups, Malays and non-Malays" in the areas of income, employment, and ownership of wealth (Report of the Economic Committee 1970). The NEP also stipulates that inter-ethnic conflict will be reduced in the context of a rapidly expanding economy. Under the NEP, although rural life would be modernized, the emphasis would be shifted to the development of a Malay commercial and industrial community in all categories and at all levels in the operation of urban economic activities, so that Malays and other *bumiputera* would become "full partners" in all aspects of the economic life of the nation (Malaysia 1973, p. 1).

The Third Malaysia Plan (1976–80)[12] provides the quantified targets of the NEP (see Table 4) which may be summarized as follows:

1. The incidence of poverty would be reduced from 49.3 per cent in 1970 to 16.7 per cent in 1990. While no figures were assigned to ethnic groups, the incidence in both rural and urban areas should decline respectively from 58.7 and 21.3 per cent in 1970 to 23.0 and 9.1 per cent in 1990.
2. In terms of employment restructuring, the NEP envisaged that the employment structure in every economic sector and occupational levels would in the long run reflect the population structure in the country. But between 1970 and 1990, the proportion of Malays was expected to be reduced in the primary sector from 67.6 to 61.4 per cent, while in the secondary sector it would be increased from 30.8 to 51.9 per cent, and in the tertiary sector from 37.9 to 48.4 per cent. Correspondingly, the Chinese share would decline from 59.5 to 38.1 per cent in the secondary sector, but increase from 21.4 to 28.3 per cent in the primary sector. The Indians would remain more or less the same at around 10 to 12 per cent in all sectors.
3. The ownership pattern of share capital in limited companies

TABLE 5
Allocation for Poverty Eradication and Restructuring of Society
(As a percentage of total FGDA*)

Malaysia Plans	Agriculture & Rural Development	Commerce & Industry	Social & Infrastructure	Total %	Total M$ million
2nd MP (1971–75)					
Poverty	23.8	—	2.5	26.3	2,350
Restructuring	—	4.0	1.6	5.6	508
Overlapping	—	—	0.04	0.04	3
Total	23.8	4.0	4.1	31.9	2,862
Total FGDA					8,950
3rd MP (1976–80)					
Poverty	14.3	0.6	5.6	20.5	6,373
Restructuring	0.3	6.2	1.1	7.6	2,376
Overlapping	0.3	0.2	0.02	0.5	149
Total	14.9	7.0	6.7	28.6	8,894
Total FGDA					31,147
4th MP (1981–85)					
Poverty	15.9	0.7	7.1	23.7	9,319
Restructuring	0.6	8.8	1.8	11.2	4,398
Overlapping	0.6	—	0.2	0.8	300
Total	17.1	9.5	9.1	35.7	14,017
Total FGDA					39,330
5th MP (1986–90)					
Poverty	15.6	—	6.8	22.4	15,446
Restructuring	—	5.7	1.6	7.3	5,076
Overlapping	—	—	—	—	—
Total FGDA					69,000

*Total Federal government development allocation (FGDA) in million M$.

SOURCE: The respective Malaysia Plans.

would change from the ratio of 2.4:34.3:63.3 (*bumiputera*:non-*bumiputera*:foreign) in 1970 to 30:40:30 by 1990.

The transformation, as it was envisaged, would be attained through growth by way of rapid sectoral change and increase in productivity. The manufacturing sector would eventually be the leading sector, growing at an average of 12.2 per cent per year so that by 1990 it would be the biggest sector (26.6 per cent of GDP), thus displacing agriculture, which would undergo a reduction in importance from 32.1 per cent in 1970 to 19.7 per cent in 1990. Productivity was to grow at around 4.6 per cent annually. With this, unemployment would be cut down from 7.4 per cent in 1970 to a full-employment level of 3.6 per cent in 1990. Economic growth would rely heavily on exports, especially agricultural products (where 41.8 per cent of growth was assumed to come from exports), followed by manufactured products (37.3 per cent based on exports). Thus there was an industrial policy shift from import substitution in the 1960s to export expansion in the 1970s. Within manufacturing, growth would be highly dependent on resource-based and heavy industries, where foreign capital would continue to be important albeit at a declining rate. In short, the economy would still rely on the capitalist system but the state would intervene only in terms of enhancing Malay participation in the modern capitalist sector.

The first objective of the NEP (poverty eradication) required that eventually no household should be living below the poverty line however defined; the second objective (restructuring of society) required that there should be equal distribution of income and occupations between ethnic groups. It should be noted that the first objective was concerned merely with the eradication of "absolute" poverty. Even if absolute poverty were to be reduced or eradicated, it does not necessarily follow that relative poverty would also be corrected. To reduce relative poverty means to achieve "equal distribution of income and wealth" irrespective of race, location, occupation, and so forth. The second objective does not imply "equal distribution" in this sense but rather in a limited sense. It means that the distribution of income among ethnic groups would be the same within each group however unequal the distribution might be (Ikemoto 1985). In other words, reducing the economic gap between ethnic groups in such a way that "no particular group would experience any loss or feel any sense of deprivation" — which is to be interpreted in a relative sense as this sense of deprivation, quite arguably, was already present in Malaysia long before independence and it has never been and can never be eliminated entirely in a configuration of a zero-sum society — is more crucial than reducing the gap within any one group, or even aiming for an overall income distribution.[13]

To achieve the NEP objectives, various forms of state intervention were undertaken in the economic life of the nation. As much as about one-third of total Federal government development allocations were directed into programmes for poverty eradication and the restructuring of society (Table 5). The emphasis of these allocations appears to have been placed on eradicating poverty rather than restructuring although from the Second Malaysia Plan (1971–75) to the Fifth Malaysia Plan (1986–90), the allocations for poverty eradication dropped from 26.3 per cent of the total to 22.4 per cent, while that for restructuring increased from 5.6 to 7.3 per cent (which was highest during the Fourth Malaysia Plan period, at 11.2 per cent). The allocations for poverty eradication were concentrated on agricultural and rural development, while the allocations for restructuring were focused on commerce and industry.

The state thus acts as a protector and a trustee of the *rakyat* (that is, the Malay community), the rationale being akin to that in the "infant industry argument" (Mehmet 1986); and with the "special rights", Malays and other *bumiputera* would be granted subsidies, favourable treatment in licensing and franchising, quotas in jobs and university places, as well as loans and grants to enter industry and trade and the purchase of equity shares.

However, the most significant form of state intervention in the implementation of the NEP was the direct participation of the state itself in commercial and industrial undertakings. This was done through wholly owned enterprises and joint ventures with the private sector. It was thought necessary for the state to set up individual companies and undertake projects in order to make them commercially viable; to open up new growth centres by expanding activities in places where private firms might be more reluctant to participate; and to help create a *bumiputera* commercial and industrial community. The role of the state in this regard includes the construction of business premises, direct investment in productive commercial and industrial enterprises to be controlled and managed by *bumiputera*, the promotion of in-service training programmes, and other activities covering financial and technical assistance. Perhaps the most striking is the acquisition of share ownership in profitable companies and eventually transferring them to *bumiputera* individuals. This emphasis was most vigorously pursued in the modern sectors of the economy marked by large foreign ownership.

An unavoidable outcome of the above policies and strategies has been a proliferation of state-owned enterprises (SOEs), especially "state-owned companies" established under the Companies Act, 1965.[14] Today there are about 900 SOEs in Malaysia. Many of them are not subject to detailed parliamentary scrutiny because of their semi-autonomous status.[15] They also have powers to establish subsidiaries. In this way they are better able to vary ownership structures in accordance with the requirements of the NEP (Puthucheary 1984).

The expansion of SOEs in Malaysia has been continuously accompanied by an increase in the allocation of development expenditure to state enterprises.[16] In order to finance their expenditures, the SOEs have relied heavily on loans in both the domestic and international markets, which in most cases require Federal government guarantee.[17]

So extensive has been the development of SOEs since 1970 that this form of state intervention has been given various interpretations. For some it represents a movement away from *laissez-faire* economic policies towards socialism (Milne and Mauzy 1978; Gale 1981) and a form of developmental state intervention (McEachern and Burns 1986). Seaward (1986*a*), however, has described it as "positive discrimination" in favour of *bumiputera*. At the other extreme, it has been regarded as an expansion of state capitalism or the bureaucratic bourgeoisie (Hing 1984; Jomo 1977) whereas Mehmet (1986) has termed it "development by trusteeship" while Muzaffar (1984) has branded it as "communal capitalism", and Hua (1983) has crucified it as an expression of the "Malay state bourgeoisie". Whatever it is, there are two basic features of state intervention in Malaysia under the NEP regime. Firstly, although the state owns or controls enterprises, it acts (at least theoretically) on behalf of the *bumiputera* rather than for its own sake. Secondly, it is "temporary" in nature, being guided by specific objectives to be accomplished within a specific time period. State intervention implies that redistribution decisions and implementation are determined by the state rather than simply by market forces, which in any case are not neutral.

Among the SOEs, the task of restructuring in terms of equity distribution falls heavily on PERNAS (National Corporation) and the PNB (National Equity Corporation). While PERNAS concentrates on building up a host of companies for trading on its own account, the PNB is a holding company for investment in areas such as industry and commerce, mining, properties, and plantations, most of which will eventually be transferred to *bumiputera* individuals through its unit trust scheme called Amanah Saham Nasional (ASN). It is worth noting, however, that the transfer rate from the state to individuals has in fact been faster than originally anticipated.[18]

Having discussed what the NEP is and how it has been implemented, let us next consider the performance of the NEP. This performance can be analysed from Table 4. In terms of poverty reduction, there are indications that absolute poverty has declined significantly from 49.3

per cent in 1970 to 18.4 per cent in 1984. The Fifth Malaysia Plan gives absolute figures for the total number of poor households: 791,800 in 1970 and 483,300 in 1984 — that is, a decline of 39 per cent over a fourteen-year period.[19] This decline can be seen for both rural households (from 705,900 or 58.7 per cent in 1970 to 402,000 or 24.7 per cent in 1984) as well as urban households (from 85,900 or 21.3 per cent to 81,300 or 8.2 per cent within the same period). Nevertheless, by 1984 the high incidence of poverty still remained amongst rural padi farmers (57.7 per cent), coconut smallholders (46.9 per cent), rubber smallholders (43.4 per cent), and other small agricultural farmers (34.2 per cent). In general, it is not far-fetched to conclude that the target of 16.7 per cent poverty incidence overall, 23 per cent for the rural and 9.1 per cent for the urban, would have been within reach if not for the prolonged recesssion.

The incidence of poverty for all ethnic groups declined from 1970 to 1980. However, for the Malays the incidence in 1980 was still above the national average (39.3 per cent as against 29.2 per cent) while the Chinese and Indians achieved 16.5 and 20.5 per cent respectively. Nevertheless, if these figures are accepted, then the NEP can be considered to have been successful in eradicating poverty.

Referring to Table 3 we can see that the mean household income in peninsular Malaysia increased fourfold from M$267 per month in 1970 to M$1,095 in 1984. Malay households experienced the highest growth (381 per cent), followed by Chinese (276 per cent) and Indian (253 per cent). There has clearly been a trend towards closing the income gap between the Malays and non-Malays. Whereas in 1970, the mean income of Chinese households was 2.3 times and that of Indian households was 1.8 times that of the Malays, by 1984 the gap was reduced to 1.8 and 1.3 times respectively.[20]

Employment shares too have been moving closer towards the NEP targets of 1990 with respect to *bumiputera* participation in the secondary and tertiary sectors. While in the secondary sector, the percentage of *bumiputera* employment increased from 30.8 per cent in

1970 to 44.3 per cent in 1985 (still below the 51.9 per cent target set for 1990), in the tertiary sector the quota has exceeded the 48.4 per cent target: the actual figure in 1985 was 50.3 per cent.[21] In the agricultural sector, the proportion of *bumiputera* surprisingly increased further to 73.2 per cent from 67.6 per cent. Of course, all these are crude estimations. At a more disaggregated level, the *bumiputera* are still under-represented in certain occupational categories or professions such as professional and technical (excluding teachers and nurses) and administrative and managerial.[22] But the point still remains that the *bumiputera* situation *vis-à-vis* the non-*bumiputera* has been improving during the NEP period.

The equity ownership structure has also undergone changes. From an equity share of 2.4 per cent of Malaysian limited companies in 1970, the *bumiputera* built up a stake close to 18 per cent by 1985. Official figures show that the share for non-*bumiputera* (56.7 per cent) has exceeded the 40 per cent target. The increase in the overall Malaysian share has largely been at the expense of foreigners whose share dropped from 63.3 per cent in 1970 to 25.5 per cent in 1985.[23]

Whether the targets set for 1990 have been reached or can be reached within the time frame of 1971–90 is an issue by itself.[24] What is important at this juncture is the direction of change resulting from the implementation of the NEP, which so far has been shown to be positive. In its original limited sense, then, the net results of the NEP can be summed up as being positive.

The implementation of the NEP, however, has not been without costs and problems. Any form of development has its side effects. The effects of the NEP include the creation of a new *bumiputera* "upper-middle" class, most of whom are new capitalists;[25] the expansion of the public sector and the heavy financial burden of running the government;[26] rising expectations and an increasing "dependency syndrome" or "subsidy mentality";[27] and not least of all, the resentment of the non-*bumiputera*, for whom the achievement of the NEP objectives has often been interpreted as discrimination against them.

Since this last effect is more directly related to the issue of national integration we will touch on it in the next section.

The above problems became more apparent and more serious when the economy failed to grow at the desired rate in recent years. Over-reliance on the world economy finally caused Malaysia's economic growth to decline, in terms of GDP, from 7.8 per cent per annum during 1971–80 to 4.3 per cent during 1981–85. In fact the growth rate was –1 per cent in 1985 and only 0.5 per cent in 1986. Indeed, the manufacturing sector, which was to be the main contributor to economic growth, failed miserably. Unemployment, which had been projected to decline, instead moved up to 8.2 per cent in 1985 and is still increasing. This economic tragedy has forced the NEP to be held "in abeyance" since mid-1986 (*Asian Wall Street Journal*, 2 June 1986).

Economic Development and National Integration

The purpose of this section is to discuss how far past economic policies and measures have contributed to national integration in Malaysia. If the assumption of the government is right (that is, inter-ethnic relations in Malaysia can be improved through economic restructuring so that there will be greater integration of the *bumiputera* population into mainstream economic activities), then logically a movement towards achieving the immediate twin objectives of the NEP would enhance the integration process.

Looking at ethnic relations in the streets, offices, firms, factories, shopping complexes, schools, and university campuses, it could quite possibly be argued that Malaysia could do with a higher degree of national integration of its population. Studies too point to the fact that there has been a tendency towards inter-ethnic tension and hostility in Malaysia (see, for example, Mohammad Haji-Yusof 1984; Yew et al. 1984). Although this is the final outcome of all factors taken together, it does appear that economic policies and performance in Malaysia at best bear no correlation with national integration and at worst have been used to promote greater ethnic polarization and aggravated inter-ethnic tension.

From various analyses made in the past, it is difficult to distinguish whether criticisms levelled against the government, particularly those regarding the NEP, pertain to the policies *per se*, or the way the policies were implemented, or the results (intended or otherwise) of its implementation. Similarly, it is difficult to ascertain whether criticisms levelled against the NEP have been genuinely intended to correct weaknesses inherent in the policy or whether such criticisms have sought to make the NEP a scapegoat in order to press for parity in other fields beyond the economic. If the implementation of the NEP is considered discriminatory, it is none the less difficult to assess whether this has been because the bureaucrats and administrators were over-zealous in implementing the NEP given the limited time frame of twenty years, or whether such a criticism represents an outright attack on any form of state intervention in the management of the national economy. After all, any form of state intervention, depending on the perspective adopted, may well be considered discriminatory.

In analysing the impact on national integration in Malaysia, it is always difficult to separate the inter-ethnic element from the inter-class element as both tend to overlap. Inter-class and inter-ethnic forces tend to be more complementary than offsetting, and yet inter-ethnic forces tend to be more obvious. This may be because it is easier to distinguish groups by ethnicity than by economic class.

Implementing government economic policies, of the kind found in Malaysia, too vigorously may also be problematic in that it can be construed by some quarters as a manifestation of "economic envy" or, worse still, as an "economic threat"; and this by itself has little value for the promotion of national integration. Obviously, it is difficult to say for certain to what extent past economic policies, measures, and performances have influenced national integration, be it negatively or positively, not only because of the multi-factor elements involved in the calculation, but also because of the fact that the whole issue is complicated by an aura of suspicion and distrust, a spirit of chauvinism and ethnocentrism, hypocrisy and selfishness, competition and patronage, and differing perceptions about the issue of national integration (see also Oo 1981).

Based on the results of past economic policies, there has certainly been an increase in the overall standard of living of Malaysians irrespective of ethnicity. Absolute poverty has declined; inter-ethnic inequality has been less pronounced. Since 1970 income distribution has not actually been worse off, at least as shown by the data. Although inequality within each ethnic group may have somewhat worsened, the problem now facing Malaysia is not inter-class conflict — at least not yet. Economically speaking, Malaysians were on average better off in the 1970s than in the 1960s or 1950s. Income inequality has been with Malaysians for a long time, but why does national integration seem to have worsened in recent years?

It does seem that economic success (in the NEP sense, at least) is not an effective answer to national integration. This does not mean, however, that economic factors are irrelevant. There are two possible interpretations for this. One, while success in the area of economics can easily be offset by negative factors in other areas, failure in economics is easily manipulated and politicized to the extent that it eventually jeopardizes the integration process. The other interpretation does not regard economic factors as being irrelevant to national integration, but rather that it is the culture of competition nurtured under the shade of free enterprise that is inherently devastating to individuals and society. It is this spirit of competition that causes anxiety, selfishness, self-doubt, and poor communication. As emphasized by Kohn (1986), competition poisons relationships among individuals, making life much more unpleasant than it need be and often resulting in outright aggression.

Next, we look at the policies themselves. There are two major criticisms against the NEP. One is the neglect of intra-ethnic inequality; the other is the clear-cut *bumiputera* and non-*bumiputera* dichotomy which presumably has created a sense of deprivation among the non-*bumiputera*. While the former is often linked to the tendency towards inter-class conflicts (which is of course potentially dangerous, but does not seem to adequately explain the present ethnic polarization), the latter has created a tendency towards intra-class conflicts, where non-*bumiputera* groups that constituted the middle and upper classes long since independence feel threatened by the emergence of the new *bumiputera* group in these classes. This can be seen in the memorandum of the Chinese business community to the government,[28] the protest against the Industrial Coordination Act 1975, and the setting up of Multi-Purpose Holdings (MPH) and the National Cooperative Society (KSM) by the Chinese community to rival state enterprises which tend to favour disadvantaged *bumiputera*. If the deterioration in ethnic relations is significantly due to the conflict between classes, then it must be between an "established class" and an "emerging class", not between different economic classes. Hence, the concept of "full partnership" as advocated by the government is still far from being realized.

Finally, with respect to the way the NEP is being implemented, there are two levels of criticisms by two opposing groups. The first level is by established capitalists who believe that government intervention in favour of one ethnic group is discriminatory against them, and this has escalated inter-ethnic tensions. The long-term solution therefore is to get rid of the interventionist approach and go back to the fundamentals of the free enterprise system. But the capitalist system as experienced in the 1960s is discriminatory and unjust too as it neglected the welfare of the poor and helpless, and thus perpetuated economic inequalities in all aspects: by region, economic activity, and ethnicity.

The next level of criticism at the failure of the NEP to improve ethnic relations in Malaysia comes from the anti-capitalist group. This group argues that the capitalist system which emphasizes the importance of the accumulation of wealth and profits as a symbol of success neglects the sense of insecurity among the poor masses and the human justice which transcends ethnic boundaries. Hence the low-wage policy, imports of foreign technology, monopoly power, capital-labour tensions, rivalries, among others, that go with capitalism are breeding grounds for human injustice, greed, corruption, exploitation of communal sentiments, and inter-ethnic antagonism. Evidently, what is being blamed here is not state intervention but the way the state intervenes.

From the above discussion, any future change in economic policy aimed at national integration should take the following into consideration: that economics is just one of many factors having an influence on integration; that economic factors tend to be more important in preventing ethnic conflicts than in promoting integration (given the present climate of ethnic politics); that any economic policy change must be part and parcel of the total change in the nation; and that human values, ethics, sincerity, trust, and the collective commitment to restructure institutions and society are critical ingredients in economic policy prescriptions.

NOTES

1 The present population of Malaysia is estimated to be around 16 million, of which 83 per cent are in peninsular Malaysia, 8 per cent in Sabah, and 9 per cent in Sarawak. In peninsular Malaysia, the Malays represent 56 per cent of the population, the Chinese 33 per cent, the Indians 10 per cent, and others 1 per cent. In Sabah *bumiputera* (Malays, Kadazans, Bajaus, Muruts, and so forth) account for 84 per cent of the population while the remainder is almost all Chinese. In Sarawak Malays and other *bumiputera* (such as Ibans, Bidayuh, Melanau, and Orang Ulu) account for 69 per cent, Chinese 29 per cent, and others 2 per cent of the population.

2 For the historical background, see for example Freedman (1960), Khoo (1981), Comber (1983), and Hirschman (1986).

3 Malay "special rights" give preference to Malays in terms of Federal scholarships, employment in the public sector, Malay reserve land, and licences and permits.

4 The transfer of power was generally regarded as a solvent of past ills and as the key to future development (Rudner 1975).

5 As far back as 1948, for example, the Malays had already complained about the Chinese being allowed to gain economic control of rural areas by taking over sectors such as rural transportation and rice milling (Lim 1985).

6 Hence, under the First Five-Year Plan (1956–60), public development expenditure allocated for infrastructure accounted for 50 per cent of total expenditure, 23 per cent for agriculture and rural development, and only 1.4 per cent for the development of industry and commerce. This policy and pattern with regard to development expenditures continued through the Second Five-Year Plan (1961–65) and the First Malaysia Plan (1966–70) periods, where the expenditure on infrastructure was large but with no apparent neglect of rural development (Lim and Canak 1981). The relative emphasis given to the rural sector as opposed to commerce and industry was a positive response on the part of the government to the poor rural Malay electorate which showed its dissatisfaction at being neglected as indicated by the outcome of the 1959 general elections. In the elections, the ruling Alliance Party then lost significantly in rural constituencies. It was in response to this that the Ministry of Rural Development was immediately established and Tun Abdul Razak, the then Deputy Prime Minister, took full control in the running of the Ministry (Gullick and Gale 1986). Nevertheless, expenditure on rural development was largely for rubber plantations and planting programmes, rather than for the development of knowledge and skills in the management of co-operatives and business, training to be independent, to be self-disciplined, and to inculcate a work ethic, which are more crucial for modernization.

7 In fact, the First Congress proposed greater state intervention drawing on the Meiji experience in Japan, where the state participated directly in business to accumulate capital on behalf of weaker economic groups and then gradually transferred resources to them.

8 It was estimated that only 10 per cent of the Malays received any of the "special rights" although 47 per cent of the Chinese perceived that all Malays had equal access to such rights. Only 13 per cent of the Chinese

thought that 60 per cent or more of the Malays would benefit (Hing 1984).

9 Perhaps because of this, Snodgrass (1980) argues that "What doomed the pre-1970 system was not that it was a failure of its redistributive efforts but that social change overtook it, forcing new priorities and thus a new development strategy on the government" (p. 286).

10 The Democratic Action Party (DAP), in particular, which was unwilling to acknowledge the legitimacy of these "special rights" and the Malay historical and cultural background, was viewed with distrust by the Malays in general who also questioned whether the party would be committed to help the poor, irrespective of ethnicity.

11 There are controversies regarding the actual cause(s) of the riots. Various factors have been mentioned, such as poverty, politics, motivational differences, beliefs and attitudes, educational background, and the economic system (von Vorys 1975; Datar 1983).

12 It was only on the launching of the Third Malaysia Plan that the government had sufficient data for more specific planning (Mohd. Nor 1981).

13 Although the NEP has been heavily criticized for bringing about intra-ethnic inequality (see, for example, Shamsul 1983; Ishak and Jomo 1984; Mehmet 1986), it has rightly or wrongly never been the intention of the NEP to address the issue of inequality within ethnic groups. However, the NEP concept was initially accepted by various ethnic representatives, including the DAP and Gerakan (in opposition then).

14 The development of state enterprises dates back to the colonial days, particularly after the formation of the Federation of Malaya in 1948. There were then public services classified as "undertakings of a commercial character" (Ahmad Nordin 1984). By 1957 there were already twenty-three state enterprises in existence, most of which were established for conventional reasons such as the provision of utilities, transportation and communication, the cultural, and financial (Raja Mohammed Affandi 1981).

15 With the rapid expansion in the number of SOEs engaged in commercial and socio-economic activities, many of these enterprises were later grouped under Off-Budget Agencies (OBAs); and under the Fifth Malaysia Plan, they were reclassified as Non-Financial Public Enterprises (NFPEs). The list of the NFPEs is constantly under review and a Central Information Collection Unit (CICU) was formed in 1985 to monitor and analyse

the operations of these enterprises.

16 In the First Malaysia Plan (1966–70), the total expenditure allocated for state enterprises amounted to about M$1.4 billion or 32 per cent of the total development expenditure. This figure increased to M$3.9 billion or 40 per cent in the Second Malaysia Plan (1971–75). By the Fourth Malaysia Plan (1981–85) period, the actual expediture turned out to be M$27.7 billion or 56 per cent of total development expenditure (Osman-Rani and Ismail Salleh 1986).

17 The amount of loans payable to the Federal government by SOEs totalled about M$15 billion in 1982 or 37 per cent of Federal government outstanding loans. The corresponding figure in 1970 was M$1.2 billion or 24 per cent of Federal loans.

18 By the end of 1985, M$632 million worth of shares had been transferred from PNB to ASN at or below market prices, and ASN had accumulated an additional investment of M$2.36 billion from 2.05 million *bumiputera* unit holders. To ensure that the units remain in the hands of *bumiputera* after 1990, *bumiputera* individuals would hold one-quarter and the state three-quarters of *bumiputera* shares. Official figures in 1985 show that *bumiputera* individuals already held 57 per cent of the *bumiputera* allocation.

19 These estimates seem to have taken into account, in the measurement of wealth, not only cash income but also land ownership, scholarships, services, and subsidies. Before that, analyses of the distribution of wealth rested on a narrow cash income basis which therefore threw up large disparities between the incidence of poverty among the ethnic groups (Seaward 1986*b*). Nevertheless, some may still question the data on the basis of the non-disclosure of the official poverty line.

20 If we were to take into account the argument made by the MCA and Gerakan that there have been higher participation rates in employment for Chinese households compared with Malay households (63 per cent as against 41 per cent), and the larger household size for the Chinese (5.5 per cent) than the Malays (4.9 per cent), then the gap between the Malays and non-Malays would effectively be smaller.

21 A substantial portion of this increase was due to an increase in public sector employment.

22 In 1984 *bumiputera* accounted for 5.6 per cent of architects, 8.9 per cent of engineers, 16.7 per cent of doctors, and 16.0 per cent of lawyers

(Malaysia 1986).

23 These figures have been challenged by Gerakan, which argued that the percentage of *bumiputera* has been underestimated and non-*bumiputera* overestimated. According to Gerakan (1984), share ownership of *bumiputera* has exceeded the 30 per cent target in plantation agriculture, mining, banking, and finance. It was only in manufacturing and construction that the shares were lower than 30 per cent. Of course, these figures include those still in the hands of the state.

24 It will at least partly determine whether the NEP should be continued after 1990. In any case, the continuance of the NEP may also hinge on whether the objectives set for 1990 are regarded as an end in itself or part of the entire process of restructuring, in which case it would have to be linked with actual population shares. This issue is still unclear.

25 The creation of a group of small *bumiputera* capitalists while the majority of the *bumiputera* remain in poverty along with other non-*bumiputera* has been subject to criticisms (for example, Lim 1985; Zawawi Ibrahim 1985; Jomo and Ishak 1986; Mehmet 1986; Ikmal Said 1980). Figures on income distribution within each ethnic group (Tables 1 and 2), however, do not show any significant change in the 1970s. Nevertheless, what is perhaps more crucial here is that intra-ethnic income inequality did not improve under the NEP but was greater than in 1957.

26 The expansion of the role of the state and the SOEs has generated a high level of development expenditure, loans, public sector deficits, and financial constraints. It has also brought about conflicts between groups of vested interests, for example, between the SOEs and Multi-Purpose Holdings (which represents the Chinese interests) or MAIKA (which represents Indian interests).

27 An oft-repeated criticism of the NEP has been that of over-dependency of *bumiputera* on the state — that *bumiputera* can make progress only where there is state intervention. Over-protection on the part of the state encourages *bumiputera* economic activities to subsist on continuing support from the state (Mohd. Nor 1981; Tham 1983; Milne 1986). Such a "dependency syndrome" in fact is also experienced by non-*bumiputera* and foreigners in their industrial and commercial activities by way of the need for higher protection and subsidies under the pretext of industrial development.

28 The Selangor Chinese Chamber of Commerce (SCCC) memorandum

submitted to the Associated Chinese Chamber of Commerce and Industry of Malaysia (ACCCIM), for example, noted that "The SCCC's view with regard to the attainment of 30 per cent ownership target for Malays is that it should be achieved in the context of expanding macroeconomy without having to interfere with the existing non-Malay individual companies" (SCCC undated). A memorandum from ACCCIM to the Malaysian Government stated that "in the case of (established) companies, regulations that make the existence of a prescribed percentage of *bumiputera* equity participation a condition for granting approval for expansion or diversification can only have the effect of stopping new investment. The whole approach should be abandoned." (ACCCIM 1980)

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