

CHAPTER 6

CHALLENGES, OUTLOOK AND CONCLUSION

6.1 Problems and Challenges Facing the Malaysian Natural Rubber Industry

When the idea to adopt an international agreement to stabilize the price of natural rubber was first mooted in the 1970s, Malaysia was one of the countries that have supported it unreservedly. The enthusiasm of Malaysia in supporting the idea was not difficult to understand given the fact that way back in the 1970s, rubber alone still accounted for more than 20 per cent of Malaysia's total export earnings. The keen interest of Malaysia on the subject of price stabilization could also be seen from its unilateral effort to intervene the rubber market in the late 1960s and the early 1970s. Those were the days when it was widely believed that price stability would guarantee the continued development of the commodity sector. However, it is evident from Malaysia's experience under the two INRA that price stability alone is insufficient to guarantee continued development in the rubber industry. This does not mean that price stability has no role at all in encouraging the growth of the commodity sector. The persistent expansion of Thailand's and Indonesia's rubber industry under the two INRA is a testimony that price stability does have positive impact. It has less impact on the development of Malaysia's rubber industry because Malaysia's industry is facing problems of its own.

Among the major factors that have deterred rubber producers in Malaysia to continue to stay in the rubber industry is the emergence of other cash crops that are now competing with rubber for resources such as land, labour and capital. One such crop is oil palm. Oil palm was first planted on commercial scale in the 1950s when the decision by the government to diversify the economy had prompted the plantation sector to seek an alternative cash crop. Over the years, the oil palm industry has grown by leaps and bounds to become the most important cash crop in this country. The emergence of the oil palm industry has not only drawn away many plantation companies but the smallholders as well. There are several factors that have attracted rubber producers, particularly plantation companies into the oil palm industry. First and foremost is the shorter gestation period of oil palm trees which require between three to four years to mature compared to the five to six years gestation period of rubber. The shorter gestation period means that plantation companies could begin to receive returns from their investment in the oil palm industry earlier. The second factor is the ease of recruiting workers to work in oil palm estates. Unlike workers in the rubber estates who need fine skill to tap the trees, workers in oil palm estates require much less skill. In fact, it has been said that workers in the oil palm industry need more brute strength rather than skill. Due to the lesser demand for skill, it is easier for the plantation companies to recruit workers including foreign workers who may not even have any previous experience of plantation work at all. However, the most important factor that has attracted plantation companies to venture into oil palm industry is the higher returns from this industry. In his book on the natural rubber industry, Barlow (1978) noted that oil palm is outstandingly superior to rubber in terms of returns. Barlow noted that the returns to factors such as land, capital,

management and entrepreneurship is RM 2,333 per hectare for oil palm compared to RM 983 per hectare for rubber. In the light of the general superiority of oil palm compared to rubber, it is not difficult to understand the trend among plantation companies and also some smallholders to convert their rubber estates into oil palm.

Apart from that, the natural rubber industry is also encountering the problem of severe shortage of labour. In the past few years, Malaysia has been enjoying buoyant economic growth of over eight percent. One side effect that accompanied such remarkable progress is the problem of labour shortage. Today, getting sufficient labour to work in the respective economic sectors and solving socio-economic problems that arose with the influx of foreign labour into this country have become a big concern for the government. The problem of labour shortage in the rubber industry is even more pronounced since not many people including foreign labour, are willing to work in the plantation sector. One direct impact of the problem of labour shortage in the rubber industry is the decline in yield. From 1976 until late 1980s, the yield in the rubber industry ranged between the lowest level of 1,100 kg/ha to the highest level of 1,267 kg/ha. However, since 1989, the yield of the industry has been suffering steady decline. From 1,267 kg/ha in 1988, it has dropped to only 950.6 kg/ha in 1993 before the price rally that began in 1994 halted further decline (Table 6.1). The decline in rubber yield could not have been due to the poor productivity of the trees as many of the rubber areas have been replanted with high yield clones. The decline in yield could however only be explained by the drop in tapping frequency and abandoned smallholdings as a result of lack of sufficient labour. The problem of

Table 6.1
Malaysia: Average Rubber Yield, 1980-1994
(kg/ha)

Year	Estate	Smallholding	Average
1980	1,427.7	964.2	1,108.4
1981	1,431.5	951.9	1,096.8
1982	1,425.5	956.0	1,093.0
1983	1,423.0	1,054.4	1,161.0
1984	1,387.2	1,052.6	1,147.4
1985	1,418.9	992.7	1,108.3
1986	1,497.0	1,071.5	1,181.6
1987	1,506.0	1,116.3	1,216.1
1988	1,490.3	1,191.8	1,267.4
1989	1,376.5	988.1	1,084.5
1990	1,334.7	921.4	1,020.9
1991	1,340.8	929.7	1,023.4
1992	1,335.0	902.2	996.2
1993	1,252.8	868.6	950.6
1994	1,214.6	957.1	1,010.0

Source: Malaysian Rubber Research and Development Board

insufficient work force is further compounded by the problem of aging workers in the rubber industry which exist not only in the estates but also the smallholder sector.

In the attempt to solve the problem of labour shortage, the Rubber Research Institute of Malaysia (RRIM) has invented a number of labour-saving technologies to overcome this problem. The REACTORRIM described in Chapter 2 is one such technology which has shown promising results. However, this new technology is yet to be adopted on a very large scale by the plantation sector and its effectiveness in solving the problem of labour shortage is yet to be seen.

In addition to the problems cited above is the shortage of new land for rubber planting and the rapid conversion of old rubber estates and smallholdings into housing estates, roads and other infrastructural amenities. It was stated in the Sixth Malaysia Plan that the hectareage under rubber is expected to decline further in future. This problem is further compounded by the conversion of old rubber estates for other development projects. In this connection, it should be noted that the many rubber estates that were once in outskirts areas are now in the vicinity of cities and town following the increase in population and urbanization. Due to the proximity of these estates to urban areas, many of these estates have been converted into housing estates and townships. The present site of Damansara, Subang Jaya, Shah Alam and the fast emerging Putra Jaya are among the old rubber estates that have been converted into townships. In the light of the increase in population and rapid urbanization, it appears inevitable that more and more rubber areas will fall prey to future development projects.

6.2 Outlook

To a very large extent, the prospect of natural rubber depends on the demand for this commodity. In this respect, the future of natural rubber is bright. In particular, it has been estimated that future demand for natural rubber will continue to grow. Although the consumption of natural rubber in the west has almost reached saturation point, the emergence of Asian countries as major consumers in this part of the world in recent years has provided natural rubber and rubber products new markets. Judging from the sizable population of many of these Asian countries and their booming economies, the demand for natural rubber in future is certainly encouraging.

However, while the future demand for natural rubber in general is bright, the future of Malaysia's rubber industry remains uncertain. As we have seen above, the main weakness of Malaysia's rubber industry is its diminishing comparative advantage. Coupled with this disadvantage is the severe problem of labour shortage which is faced by the other economic sectors as well. In the light of these adverse factors facing the industry, one sees little chance that Malaysia's natural rubber industry will see further expansion in future. Already we have seen the inability of Malaysia's rubber industry to revive its production capacity as that in 1988 despite the price rally in the rubber market that has persisted for more than two years. In 1988, when prices of rubber soared to 309.99 sen/kg, the country's rubber output responded by increasing to 1.66 million tonnes in that year. Since then it has been argued that Malaysia is capable of producing the same amount of rubber so long as the price is right. However, when rubber prices climbed to an even higher level in 1994 and 1995, Malaysia's production of rubber only managed to lift to 1.1 million tonnes. It is

therefore evident that even with such remunerative prices, it is difficult for the rubber industry to produce as much rubber as in the past.

However, this does not mean that the future of rubber is bleak. As we have seen in Chapter 2, the natural rubber industry of Malaysia is undergoing changes of its own. From one that emphasized on the export of raw rubber, it has transformed into an integrated industry that now comprises a well established upstream sector and a fast developing downstream sector. Although there are still weaknesses in the rubber product manufacturing sector e.g. its over dependence on the latex-based sector, the future of this sector is still bright as the demand for rubber products is expected to increase. In addition, there is still room for expansion in the tyre sector which is the largest user of natural rubber.

In so far as the raw rubber sector is concerned, it appears likely that it will decline further. However, it would be wrong to assume that the entire industry will disappear from the Malaysian scene. The increase in demand for natural rubber following the expansion in the rubber product manufacturing sector is expected to keep the decline in the production of raw rubber in check. Apart from that, the improvement in Malaysia's breeding programmes which have been producing high yielding clones and also progress in labour-saving technologies are also expected to solve the woes faced by the rubber industry to a certain extent.

Apart from the above, there has also been call for the industry to go off-shore to take advantage of the abundance of land and labour resources in neighbouring

countries such as Indonesia, Vietnam and Kampuchea. The idea of going off-shore is to exploit the comparative advantage of these countries to produce cheap raw materials for the home processing facilities in Malaysia. However, to what extent would such investment be successful is yet to be seen. Some of the countries such as Vietnam and Kampuchea that showed interest in rubber planting are formal communist states that are new to the idea of free economy and the plantation business. Their lack of experience in these respects may prove to be barriers to Malaysian planters' ambition to go off-shore.

Another area where there is bright future for the rubber industry is the rubberwood sector. Rubberwood is an invaluable product which had been ignored in the past. However, the widely acceptance for rubberwood furniture has made rubberwood a much valued raw material today. It has been reported that in future, rubber trees will be planted for both their latex and wood, thereby enhancing the economic value of the trees. The importance of rubberwood is likely to ensure that the most important cash crop in Malaysia's history will continue to play an active role in the economy.

6.3 Conclusion

Since the expiry of the second INRA in December 1993, negotiation for the agreement has been going on for more than two years. Until today, the fate of INRA remains uncertain although there were reports that response from member countries has been encouraging thus far. It would be a pity if it is not extended since the

agreement has proven to be a workable agreement that has brought stability to rubber prices.

As pointed out above, INRA was not meant to be a price support agreement. Although one of its objectives is to ensure stable income to the producers, there is no guarantee that the buffer stock operation of INRO would support prices at levels considered remunerative by the producers. The concept adopted by INRO for its buffer stock operation is one of market trend which entails the adjustment of reference price and price range of its BSO according to market conditions. The mandatory revision of the reference price and price range is the mechanism that will ensure that the levels at which prices are defended by INRO will not stay at unrealistic levels which could not be sustained for long in a free economy. Under the first agreement, revision of the reference price is done every eighteen months. When the second agreement was concluded, the revision period was shortened to fifteen months. There were reports that if the third agreement is ratified, the revision period will be shortened further to twelve months only. A shorter revision period for the reference price would ensure that the price range of INRO's BSO could be adjusted faster according to changes in market conditions.

There are limits that INRO's BSO can influence the prices of rubber. As we have noted earlier, the idea of INRO's BSO is to improve the balance between the supply and demand forces in the market in reducing price fluctuation. If the fundamentals in the market are too strong, then there is little that INRO can do. A case in point is the inability of INRO to halt the rapid price rally in the rubber market

that began in 1994 and persisted until today. In 1994, rubber prices reversed the declining trend that has lasted a few years and surged upward. The change in price movement is the result of shortage of rubber particularly TSR 20. In the second half of the year 1994, INRO intervened the market actively in the attempt to slow down the price rally. Due to the very volatile situation in the market, the disposal of INRO's buffer stocks amounted to more than 220,000 tonnes, was done in a swift manner. The entire stock of rubber was sold in just three months i.e. from August to October 1994. However, even the sales of such massive amount of rubber did not stop rubber prices from going up higher. The inability of INRO to halt the price rally attest to the fact that it is the fundamentals in the market that dictate price movement. However, this should not be viewed as a weakness of INRO as INRA is not an agreement designed to change market forces. In fact, it should be viewed as the underlying factor that has made the agreement a workable one. Experience from the other agreements are testimony that market intervention instruments that defy market forces could not sustain for long.

With regard to the effects of INRA on the development of Malaysia's natural rubber industry, we have seen that its effect under the first agreement appears to be far greater than that under the second agreement. This does not mean that price stability is no longer an important element in encouraging the growth of the natural rubber industry. The experience of Thailand and Indonesia show that the existence of a price stabilization agreement does give the producers, particularly the smallholders, a greater sense of security which is vital to keep these producers to remain in the industry. In the case of Malaysia, its rubber industry has been suffering deterioration

simply because of the internal problems facing the industry. The rapid diminishing comparative advantage of rubber in the face of the expansion of the oil palm sector and the manufacturing industry has rendered the rubber industry unattractive. Given the fact that rubber (raw rubber) now contributes barely two percent to the total export earnings of the country, it is no wonder that there is much less interest in rubber today. However, it is heartened to note that the rubber product manufacturing sector and the rubberwood industry are still expanding. In addition, progress in labour-saving technologies is expected to alleviate the labour problem encountered by Malaysia's rubber industry and to ensure that the most important cash crop in Malaysia's history will continue to contribute to the country's economic growth.