

## **CHAPTER 6**

### **SUMMARY, POLICY RECOMMENDATIONS AND CONCLUSIONS**

#### **6.1 Introduction**

In this chapter, we will attempt to summarise the findings on the investigation relating to JDI in the Malaysian manufacturing sector according to the chapters explored. Some policy recommendations and the prospects of JDI within Malaysian economy would follow this.

#### **6.2 Summary of Findings**

As highlighted in Chapter 3, Japan led the inflow of direct investment to Malaysia. Eventhough new groups of capital investing nations from Asia such as Taiwan and South Korea emerged in the late eighties. In fact, Taiwan has been singled out as one of the countries with the highest investment growth rate in the Malaysian manufacturing sector ahead of Japan. However, Japan was able to maintain it's investment to sustain top position in terms of investment volume by country of origin.

The JDI in Malaysian manufacturing sector was motivated primarily by the political stability, in addition to the cheap labour in Malaysia in the late eighties. Japanese firms also had used Malaysia as an off shore production base to penetrate European and US markets. These were coupled with the continuous investment promotion measures by the Malaysian government.

In terms of geographical distribution, more than 90 percent of the Japanese firms were located in Peninsular Malaysia while the remaining were found scattered in large towns of East Malaysia. In Peninsular Malaysia itself, JDI are primarily concentrated within the FTZs. This prevailing distributional pattern of JDI was attributed to the attitude fostered by the Malaysian government during its initial stage of industrialisation where emphasis was placed on locating foreign firms in industrial estates and FTZs along the west

coast of Peninsular Malaysia. However, lately all these areas are fully occupied and this resulted the JDI to spread to surrounding alternatives.

In terms of sectoral distribution, more than 50 percent of JDI in Malaysian is concentrated in the manufacturing sector, followed by a small amount in selected trade, commerce and service sector. The JDI's presence in extractive sectors such as agricultural, oil exploration and mining has traditionally been small. The high concentration of JDI in Malaysian manufacturing sector could be due to the booming market for manufactured goods compared to primary commodities.

There was a tendency for the Japanese investors in Malaysia to operate as joint ventures in line with the Malaysian government's policy, which discourages the establishment of wholly foreign owned firms. This might be in order to promote greater local participation, particularly from the Bumiputra community. Hence, joint ventures between Japanese investors and other foreign investors from single or multiple countries together with local investors seemed to be an eminent feature among the Japanese manufacturing firms in Malaysia.

Meanwhile, in Chapter 4, the contributions of the JDI in Malaysian manufacturing sector were highlighted. Most of the Japanese firms were involved in export-oriented industries. This was in line with the government's industrial strategy to promote export-oriented industries. The JDI were dominant in the manufacturing of textiles and electrical/electronics products, which are basically export-oriented. A large proportion of these Japanese firms' export's were destined to a third country, with little going back to Japan for home consumption. Exports of manufactured goods formed the lion's share of Malaysian total export. So the high dominance in export-oriented industries has enabled Malaysia to improve its export. It benefited Malaysia since the export of manufactured goods contributes substantially to the nation's export earnings.

Another notable contribution of JDI was the creation of employment. The Japanese companies initially established here were generally labour intensive types. For example, electrical/electronics products coupled with the assembling of machinery were examples of labour intensive types of industries, which have indicated a high level of JDI. In addition, the Japanese intention of taking advantage of the local supply of cheap labour has increased job opportunities and concurrently reducing the unemployment rate to less than 3 percent in 1997.

Within the manufacturing sector itself, the influx of JDI in Malaysian manufacturing sector has led to increasing demand for local intermediate products. The production of these intermediate goods by Malaysian small and medium scale industries has also benefited Malaysia. But this linkage between the Japanese firms and ancillary firms is not fully exploited. This is because the Japanese firms still have strong linkages with their foreign suppliers and parent plant for the intermediate goods.

Another contribution of JDI in Malaysian manufacturing sector is in the training aspect. Almost all-Japanese firms in Malaysia involve themselves with training the local workforce in technical front. Local Malaysian workforce has benefited in this aspect. But a further investigation shows that the training of the local staff and internal dissemination of skills and technology are still not sufficient to ensure eventual effective transfer of technology. The local firms still depend on foreign partners for technical guidance and expertise.

Chapter 5 explored the issues pertaining to the transfer of Japanese technology to the Malaysian manufacturing sector. The chapter started with the Malaysian governments policies on technology transfers. To encourage the entrance of foreign technology, the Malaysian government had implemented several investment promotion incentive plans to attract greater flow of direct investment. In addition many free trade zones and industrial estates were set up to facilitate greater transfer of technology.

Japanese investors showed a high tendency of transmitting their technology via a packaged mechanism which involved simultaneous transfer of capital, management and technical know-how. This is because the Japanese claimed that their technical and managerial resources are needed to produce high quality products effectively. The type of technology transferred is normally associated with the technical and engineering ability among the local workforce.

This chapter also examined the various channels through which the Japanese technology is transferred to Malaysia. The common channels are technology transfer agreements, purchase/loan of machinery and other capital equipment from parent company and patent technology.

In evaluating the effectiveness of the technology transfer, it is found out to be still less than the desired level. This is basically due to the process of transfer itself, which might lead to technology isolation. Japanese investors also identified that local workforce do not have sufficient knowledge to facilitate handling any technical problems which may arise in their course of work. This has led Malaysian to become machine operators rather than innovator. Lack of R&D activities within the local companies also hampered the continuous transfer of technology.

### **6.3 Prospects**

The most important facing the manufacturing sector are those of raising local content, maintaining high rates of growth of exports through diversification and product upgrading and developing the skill and institutional base to support these objectives. The depreciation of the Malaysian Ringgit might prompt another wave of Japanese direct investment to Malaysia. The ability of Malaysia to attract and absorb these investments will be critical to the structural upgrading of Malaysia's manufacturing sector.

However, Japanese investment in general, and in the manufacturing sector in particular, will not reach the high levels of the late 1980s for few

reasons. Hence, Malaysia's heavy dependence on Japanese MNCs to drive manufacturing production and exports may not serve the country well in the future. Among the reasons, labour and land cost in Malaysia are rising, making it less attractive for Japanese investors. For many Japanese firms, among the primary reasons for investing and operating in Malaysia were cheap labour and production costs. But now with the rising cost of production, there seems to be less reason to invest here.

In addition to this, there is a technology absorption problem in Malaysia, largely due to the shortage of skilled labour. This is a problem, which is of great concern to a number of Japanese investors. Many of Japanese investors had occasionally expressed their frustration at the low level of technical education of Malaysian workforce. Unless the government invests more into education and training, the skills shortage in Malaysia is likely to continue and this would hamper the continuous flow of JDI in Malaysian manufacturing sector.

Malaysia also had to be wary about the potential of China and Vietnam as alternative investment sites. These areas are becoming more attractive to foreign investors. Not only labour and land are cheap and in abundance in these areas, but the sheer size of the domestic market holds enormous opportunities and potential profits for Japanese investors. A lot of new Japanese direct investments might be directed to new areas as the cost of production in Malaysia is continuously rising.

This is coupled with the problems within Japanese economy itself, where the escalating bad debts problems in Japan had caused some major problem in their financial system and this might affect the amount of JDI in ASEAN countries, especially Malaysia. Unless Japan are able to solve their own problem back home, they might not be able to maintain such a high level of investment. Japan supposed to be the biggest investor in the ASEAN countries, so if they start to experience problem, then it might lead to some fall in JDI in the Malaysian manufacturing sector.

The major reason for Japanese to invest in Malaysia was Malaysia had been political stability in addition to cheap cost of production. This is evident as JDI continued to increase even though cost of production in Malaysia was higher than its neighbours (except Singapore). The reason that is always stated was political stability. But given the current political turmoil in Malaysia, it might seem that there's some element of uncertainty in Malaysian politics and this might affect Japanese direct investment to Malaysia.

Finally, Malaysia's Generalized System of Preferences (GSP) privileges were another major factor, which influenced Japanese companies to initially invest in Malaysia, as a way of gaining access to North American and European Committee (EC) markets. With this privilege disappearing, many companies are thinking twice about setting up new or additional production operations in Malaysia and opt for China or Vietnam instead.

#### **6.4 Policy Recommendations**

In light of the unstable future of the JDI in the Malaysian manufacturing sector, Malaysia should look to new ways to encourage and actively promote foreign direct investment. The first policy recommendation would call for government to instill greater enterprising attitude among local entrepreneurs and to shed the negative sentiments of merely receiving earnings annually without partaking in the operation. This is crucial if the objective to reduce foreign dependence is to be achieved. It is known that many local entrepreneurs or partners would rather leave the company's operation to the Japanese counterparts because of their insufficient supporting management expertise and technological know-how to operate efficiently and effectively.

Thus, by encouraging greater participation from local entrepreneurs, the Malaysian manufacturing sector will not be at the mercy of the foreigners should they decide to withdraw their investment commitment. In order to achieve this, the government should include more employment benefits in terms of tax reduction to companies, which employ a substantial number of indigenous personnel at all levels of production and management. By



implementing this, the government can increase local content in terms of labour input in foreign firms apart from merely emphasising local content in terms of raw materials alone. Foreign firms, including Japanese firms should be required to fulfill a specific percentage recruitment of local workers, particularly in the management hierarchy to create a more balanced workforce.

The second policy strategy calls for government intervention to restructure the Japanese industrial dominance in certain industries. From the summary of findings, we found out that the JDI held strong control over two major groups of industry which we are labour intensive and export oriented. As such, the involvement of local business persons in these industries is relatively small since since their insufficient technical ability, especially in export oriented industries which has to compete with other producers at international standards, has proven to be an impairment when contesting with the Japanese. The technical ingenuity of the Japanese is sufficient to keep them ahead and maintain an edge over local entrepreneurs.

Local investors were more interested in the manufacturing of resource based industries such as rubber products. Local involvement in textile and electrical and electronic industries are confined to production of light consumer products. To overcome this, the government should get involved in terms of R&D to local businessmen who wish to undertake investment in these industries. Research grant or aid should be given to firms that show initiative in undertaking R&D activities. The research work should be directed towards enhancing their manufacturing capability to produce more value-added goods for the market.

The government also can elicit new Japanese investors to take an interest in other resource-based industries that at present has a comparatively lower Japanese investment concentration. Apart from redistributing Japanese investment concentration, the government can also take advantage of the Japanese knowledge to develop more downstream processing industries, particularly resource-based related such as timber,

rubber and coal products. This will not only lead to the progressive enlargement of the Malaysian downstream industries, but will also expand the absorption of locally produced raw materials, thus increasing the local content in manufacturing sector. Generally, the government should be sensitive and receptive towards the needs of the investors and must be prepared to bend existing regulations should it be expeditious and beneficial.

Chapter 5 showed that the Japanese show a high tendency of transmitting their technology via a package mechanism which involved simultaneous transfer of capital, management and technical know how. The Japanese alleged that local investors are not capable of providing these supporting resources. As such, many manufacturing firms are forced to receive the wholesale package of technology with the least consideration for the local factor endowment criterion.

In consideration with this, the third policy strategy would be to recommend MIDA/MITI to ensure that the technology and know how entering the Malaysian environment is utilised in a manner most advantageous to Malaysia, bearing in mind the present and future needs of the nation. This is basically to supplement the existing function of MIDA as a screening board for all types of technology entering the country. A more intensive product R&D centre also could be established to localise research and development activities. This centre will be responsible for monitoring quality improvement, product design and packaging. With the formation of such a centre, the government can assist in upgrading the competitiveness of Malaysian products in the international market.

In addition to this, the government can also extend further assistance by providing sufficient subsidies for all related R&D activities pertaining to industrial and product development. More research grants should be extended freely to institutions of higher learning to undertake useful researches into various fields to facilitate industrialisation programmes. The government should also recognise efforts initiated by the private sectors by



offering contribution in terms of rewards for any new innovation of product lines or cost saving methods of production.

It was also noted that the adaptability of technical know how to comply with the local factor endowments can be minimal. This is because almost all R&D activities in Japanese firms were mainly carried out by the parent company. This is especially in the manufacturing of intermediate goods and assembling of machinery and transport equipment. In these types of industries, the Japanese have decided on a set of guidelines or techniques and methods of production that must be conformed to by the local workforce.

In addition, it should be noted also that the Malaysian workers have developed a strong technological dependence on the Japanese in terms of technical know-how. If this state is tolerated and allowed to perpetuate, the Malaysian manufacturing sector may face a quandary when the Japanese decide to withdraw their investment in Malaysia. In view of this, it is recommended that, Malaysia needs to embody a coherent policy related to technology transfer because of the urgent need to expedite technology transfers to accelerate its technological progress. The strategy should seek the utmost relevant and practicable imported technology for specific uses, and further assimilation of this imported technology should be independent of the MNCs.

This means that government investment authority such as MIDA, should be more aware of the technology needs of each industry. It should allow entry of relevant or suitable type of technology, particularly those which can incorporate the country's factor endowment. To reduce the prevailing technological dependence, the strategy drawn should be able to complement the third policy strategy to encourage the adoption of local R&D as well as development of new technology based on Malaysia's own existing comparative advantage, that is, in the agro-based industries.

The fifth policy strategy calls for the establishment of more training schools particularly in the rural areas, so that a greater spectrum of labour

can gain relevant technical knowledge. This would create a ready pool of local technical workers to provide a more solid supporting base for future technology diffusion. The provision of relevant vocational training is essential to augment occupational mobility so that workers could work in different sectors once they moved out of rural areas. At present, most of those moving into cities and towns from the rural areas and plantations do not have any notion of factory working conditions, and some of the basics of machine operation.

By setting up more technical training schools in rural areas, the government can prepare a younger generation which is more technically literate, since technical advancement is crucial to support development. Besides, this will ensure a continuous flow of trained and qualified technical personnel to undertake future R&D activities. The supply of more educated workforce will supplement the existing one not only within the manufacturing sector but within the entire economy as well.

A change in the education system towards one that emphasises practical training will eventually generate a more receptive manpower. If this stage can be achieved, there will definitely exist a ready pool of technically literate workforce. This in turn will serve as a lubricant to the process of technology transfer in particular and to the entire process of industrialisation in general.

Management education is another important field which requires urgent attention. No efforts, regardless of how well planned, how well meaning and how extensive will not be effective if one fails to recognise, realise and acknowledge the central role of managers in the economic activities. However, some of the presently employed managers have not undergone any sort of formal classroom education. Their expertise is more an accumulated experience over the years. Hence, these managers should be provided with some training so that the knowledge gained together with their indispensable experience can help them compete and keep abreast with the rising standards of competition.

## **6.5 Conclusion**

Japanese direct investment had played some major role in Malaysia's industrialisation (starting from pre Independence period). The transformation from an agricultural based economy to a manufacturing led growth nation is much due to the government's emphasis of promoting and welcoming greater inflow of direct investment. The Japanese investors were amongst the first to invest in Malaysia. Their direct investments in the manufacturing sector has enabled Malaysia to export manufactured goods and also had created job opportunities for Malaysians in urban and rural areas.

However we have to admit that given the number of years the Japanese direct investment has been in Malaysia, the effectiveness of the transfer of technology is still far from the desired level. This definitely contradicts claims from certain quarters that the local economy has benefited tremendously from the diffusion of Japanese technology. The local economy had received considerable amount of knowledge from Japanese transfer of technology but the extent and spread of the knowledge is still meager.

One of the important issues pertaining the Japanese transfer of technology is the inability of Malaysian workforce to absorb the technology transferred. So the government should increase R&D activities to better equip local technicians and engineers to adopt and innovate the transferred technology to our needs as Malaysia moves into Vision 2020.