

## CHAPTER ONE

### INTRODUCTION

#### 1.1 The early state of play

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The first attempt at industrialisation began way back in the year of independence. This attempt, although undertaken, lacked drive as Malaysia's primary commodities were performing well and industrialisation did not seem that urgent nor important at that time. As it was, in 1957, the manufacturing sector's share of GDP was a mere 6.5 %. Nevertheless, following the Industrial Working Paper of 1957, the Government formulated a strategy to develop the manufacturing sector.

The Pioneer Industry Ordinance 1958 was implemented to provide incentives for the growth of import-substitute industries. There was reasonable growth in the manufacturing sector and in the 1960s, its share of GDP increased to approximately 9 %. The main problems with these import-substitute industries were that they were limited to consumer goods and there was difficulty in going beyond the easy stage of import substitution in view of the high degree of protection accorded to these goods by foreign countries. Thus, when the import-substitution phase weaned off, the strategy was then diverted to the promotion of export-oriented industries.

Generally, the policies adopted were aimed at creating a conducive atmosphere for investment. Through out the 1960s and 1970s, the Government encouraged direct foreign investment. For

instance, the Free Trade Zone Act 1971 was launched and together with the Investment Incentive Act 1968 brought in many multinational corporations (MNCs) especially those from the electronics and textile industries. There was thus a strong link between industrial development and MNCs. In the 1970s, the manufacturing sector's share of GDP rose to 13 %. Amidst this improved performance, other problems surfaced. The development experienced was regionally concentrated and at the end of the day it was discovered that there was not much savings in foreign exchange either. This was because 70 % of the gross manufacturing sales composed of imported inputs. It was also believed that wages in these industries were depressed but most important of all, the desired technology transfer did not materialise. Malaysian workers were basically engaged in low skill activities. These prompted the Government to adopt a new policy thrust of direct intervention.

The new policy thrust provided a more liberalised economic atmosphere where physical incentives no longer played such an important role. To facilitate the move to a higher phase of technology, the Government moved more aggressively into the heavy industry sector. This marked the beginning of the second phase of import-substitution strategy. For this purpose Heavy Industries and Corporation of Malaysia Berhad (HICOM) was incorporated on November 27, 1980. It was assigned the task of planning, identifying, initiating, investing, implementing and managing projects in the field of heavy industries. The Government pursued a "Look East Policy" and the "Four Dragons",

especially Japan, were looked upon as exemplary in its pursuit of industrialisation. At the same time, an analysis of past policies was made and several weaknesses were identified. These were :

- \* Unlike the newly industrialised countries (NICs) like Taiwan and S. Korea, the manufacturing sector of Malaysia was concentrated on only a few industries, especially the export-oriented ones. This provided the country with only a small industrial base to work on.
- \* Weak inter-industry linkages were pronounced. Thus, there was not much spin-off effects. These weak linkages were the result of the high import content of the industries' inputs.
- \* Small and medium size Industries (SMIs) development had been neglected. A study of the development of NICs shows that these economies achieved rapid economic growth because their Governments encouraged the simultaneous growth of both big and small firms.
- \* Weak Science and Technology development was the norm. Insufficient emphasis had been given to Research and Development. For instance, in 1988, S. Korea spent 2 % of its GDP on R & D while Malaysia only invested 0.8 % of its GDP for the same purpose.

\* The dominance of MNCs had a negative effect on innovation and R & D and was the cause of market failure.

Thus, the Government realised the heavy responsibilities and the task it had to take to lead the economy towards industrialisation and development. Yet, not every heavy industry was to be promoted. The criteria would be that the project must be commercially, financially and technically viable. More important, it must spearhead the rest of the industrial sector through technical spin-offs and linkages effects. For these purposes, four industries were selected as priority industries. The automobile and component industry, which falls under the engineering industry, was one of the successful candidates.

## 1.2 Objective of the Study

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The main objective of this Research Paper is to make a study on the contribution of the National Car Project to the automobile and component industry. The progress of PROTON Berhad in its first decade of operation and the impact it has on the various aspects of the Malaysian economy will be discussed. Emphasis will be placed on its achievement in relation to the objectives underlying its establishment and the way the Government has supported it in its venture into an already established market. An attempt is also made to look into some of the less desirable effects that the National Car Project may have invoked. At the end, it is hoped that the reader will realise that what appears

to be a patriotic commitment to produce a Malaysian Car by the Government has so far turned out to be an economic sound decision although there is a cost involved.

### 1.3 Methodology

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This Research Paper is expected to entail considerable field work as its scope is relatively wide. Existing literature will be gathered from the brochures and publications of companies involved and articles from newspapers and magazines. References will also be made to the Input-Output Tables 1983 and 1987 so that a comparison of their values can throw some light on the impact of the National Car Project on the Malaysian economy. Interviews will be sought with the management of PROTON Berhad, especially the Vendors Development Department and the Accounts Department. This serves the purpose of gathering information on the Company's policy and progress in the various aspects of production, employment, attempts at localisation and participation in the Government small and medium size industries vendors development programme.

An analysis will also be made on PROTON Berhad's vendors to gain insight into their equity structure and operations. A questionnaire will be prepared for this purpose and the information obtained from this exercise will provide some basis for assessing the extent by which the Government has succeeded in encouraging Bumiputera participation in the automotive industry and the importance of PROTON Berhad as the engine of

growth for the industry.

Reference will also be made to the various publications and reports by the private institutions and Government bodies to keep track of developments in their respective domain. Of particular interest will be reports by Malaysian Motor Trade Association (MMTA), Malaysia Automotive Components Parts Manufacturers (MACPMA), Ministry of International Trade and Industry (MITI), and Malaysia Industrial Development Authority (MIDA), the Transport Ministry and the like.

#### 1.4 Organisation of study

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Chapter One of the Research Paper serves to recollect the early economic policies taken by the Government in its pursuit of industrialisation and an assessment of their success with respect to Government goals. Although the early attempts at industrialising the economy did not yield the desired results, lessons have been learnt from them. These, coupled with the Government openness to the experiences of the so called "Newly Industrialised Countries" (NICs), have made possible the adoption of more efficient policies. The Government long term commitment and intervention has been important in the industrialisation process of the NICs and the realisation of this has encouraged the Malaysian Government to take a giantic step at developing the country's own automobile industry. The objectives, methodology and organisation of the study are also spelt out in this Chapter.

An analysis of the motor-vehicle sector (as described according to the International Standard of Industry Category and the Malaysian Standard of Industry Category) before the launch of the National Car Project is presented in Chapter Two. This will provide the framework for understanding the significance of this sector at base values 1983. References will again be made to the findings of this analysis in the later Chapter when a similar exercise is performed on the Input-Output Tables 1987 (the latest available).

Chapter Three charts the mileage achieved by PROTON Berhad in its production and market penetration effort in its first decade of operation. Some of the major contributing factors to its success are also being discussed in this section.

The macro-economics effects of the Project are given in Chapter Four. The values given in the Input-Output Tables 1987 are used to measure the extent by which the motor-vehicle sector had changed over the five year period (1983 - 1987). The beginning of this period happens to be the pre-PROTON era while the end of it, 1987, marks the third year of PROTON's operation. Although the implied assumption is that all changes in this period are due to the National Car Project, it is hoped that the comparison of the values in this period can give some indication of the impact of PROTON Berhad on the economy. A relatively detailed discussion will be made on the linkages effects of the National Car Project as this is a major reason for its launch. Nevertheless, other effects will also be given due consideration.

The final Chapter attempts to look at the costs of the National Car Project from the economist's stand point. An attempt is made to identify some possible opportunity costs that may be incurred from the Project and the market distortion that comes with a regulated industry.