HOW MALAYSIAN MANUFACTURING EXPORTS REACT TO THE GLOBAL ECONOMIC CRISIS

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ABSTRACT

The global economic crisis which originated in the USA following the subprime mortgage problem, caused damage to the world economy. The crisis, indeed, affected the Malaysian economy. Malaysian exports of manufactured products were hit hard by the sharp drop in demand from developed economies, since most destinations countries of Malaysia manufacturing exports have been affected by the crisis. This paper examines the current global crisis impact on the Malaysian economy, mostly on manufacturing export performance. The paper also highlights the ability of Malaysia in response to the crisis by increasing the productivity of its human capital development and adopting an export diversification market for enhancing the economic integration of Intra-Asian and Intra-ASEAN exports. Recommendations are made which it is believed will enable Malaysia to respond effectively to the worldwide crisis.

Keywords: global economic crisis, manufacturing export, export diversification

INTRODUCTION

The current global economic crisis originated from USA has brought enormous ramifications for the world economy. The crisis that rooted from the US subprime mortgages spread the risk globally. Within a short time, the crisis affected the global financial system as well as the real economy through the Asia-Pacific Region (Mujeri, 2009). The effects of the global crisis have spread into developing Asia with significant speed and rapid force especially resulting from the highly globalized nature of the countries in the region and the contagious nature of the crisis. Overall, exports are falling because of lower international demand and reduced trade finance. In developing Asia, the most obvious areas of impact include currency and credit markets, exports, and social equity. The sensitivity has been heightened by the export led growth strategies that most of these countries follow thereby affecting export related production and investment as well as softening domestic demand. The GDP growth rates have fallen leading to increased financial and fiscal stress, unemployment, poverty, and deprivations in the countries across the region (ADB, 2009, Hassan et al., 2009).

In fact, the paper addresses issues relating to the global economic crisis impact on Malaysian economic condition. Firstly, the paper explains the general effect of global crisis to Malaysian economic condition, later, it narrow down to the specific industry sector. The continuous decline in export is the main channel the global economic crisis has mainly penetrated by Malaysian economy. The paper analyse further on the export manufacturing sectors that mostly demand by the developed countries which now mainly suffered by the crisis. Lastly, the paper provides two recommendations of human capital development and diversification of export trade which believe to respond effectively to the worldwide crisis.

THE EVOLUTION OF GLOBAL ECONOMIC CRISIS

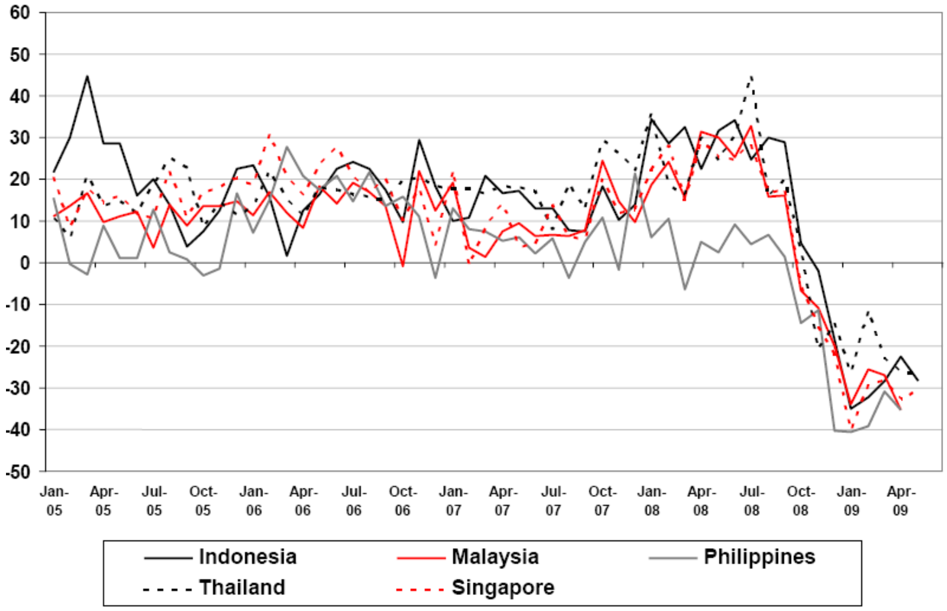
The crisis started by an asset bubble which caused by an array of financial derivatives. The big housing boom in the US from 2000 to 2006 led to a sharp rise in subprime lending (Cyn, 2009). The subprime mortgages were repackaged and sold to prospectors of the global investors. That particular form of financial innovation spread the risk globally. At the same time, the interest rates were very low practically driven by the US Federal Reserve which provided extra liquidity in the global financial market.

Furthermore, the global financial crisis that originated from the US subprime mortgages took a dramatic turn in September 2008 when Lehman Brothers filed for bankruptcy, Merrill Lynch was sold to the Bank of America, and the American International Group (AIG) which is probably the biggest insurance company in the world, almost would have gone bankrupt if not timely bail out by the US Federal Reserve. As a consequence, the broader impact of the subprime mortgages boom exploded into housing and banking crisis with a cascading effect on consumer and investment demand (Abidin and Rasiah, 2009), as well as merchant banks which absorbing the impact to spread to the commercial banks (Krugman, 2009).

The subprime crisis has now evolved worsened into global financial and economic crisis, the worst since the Great Depression in the 1930s (Kawai, 2009). This crisis is different from other financial crises over the last several decades, not only in its breadth and magnitude, but in its origin. The crisis is global, thus, affecting almost all countries in the world, not just a few, and its impact so devastating. The epicentre of this crisis is not a peripheral country but the United States, which is the largest and central economy in the world, and home to the most dominant global key currency –the dollar- and the world’s most sophisticated and developed financial system.

EFFECT OF GLOBAL CRISIS TO MALAYSIAN EXPORT

The global crisis did not originate in Asia, and indeed, the direct damage to the financial sector in Asia has been much less than in Europe and the U.S. The overall economies in Asia were decline (Kawai, 2009). Most countries in the region are now showing double-digit declines in exports as shown in Figure 1. The large declines were seen in Singapore, Indonesia, Thailand, Malaysia and Philippine from year 2008-2009. The effect of the global financial crisis on the global economy is far broader and more severe than earlier anticipated. Its depth and contagion across the global economy was unprecedented with several of the large industrial countries and a number of the regional economies having slipped into recession. While global efforts have been intensified to counter the effects of the slowdown, risks remain on the downside and recovery is likely to be slow and protracted. Under these circumstances, the Asian economies have been adversely affected. In many cases, the declines were greater than those seen during the bursting of the information technology bubble in 2000-2001. Nevertheless, Asian economies, especially Malaysia have been hit hard by the sharp drop in demand in the developed economies and elsewhere.



Source of Department Statistic Malaysia, 2005-2009

Figure 1: Export Growth in ASEAN Economy

The bitter experience of the Asian financial crisis had already provided the incentive for Bank Negara Malaysia (BNM) to regulate the financial sector better performance. World Bank (2008) stated that the country financial assets for foreign loans and non-performing loans (NPLs) had been one of the lowest registered among Asian economies for 2008. This statement led the Government to confidently say in early 2009 that Malaysia's economic fundamental were strong. Additionally, as stated by Deputy Finance Minister Datuk Kong Cho Ha told the Dewan Negara, Malaysia is only feeling the minimum impact of the global economic crisis and financial meltdown (Bernama, 2009). Furthermore, he claimed that reaffirming the country's economic fundamentals were sound and strong. Malaysia has not been directly exposed to the full impact of the global financial crisis. In his speech, he added that the country's national reserves were still strong at 37 per cent of the Gross National Product, a clear indication of the nation's surplus liquidity that can be financed to generate economic activities. The country's banking sector was also stable, with the non-performing loan rate at 2.4 per cent and the risk weighted capital ratio at 12.6 per cent, far above the eight per cent limit of the international standard.

On the contrary, the contraction in external demand gives negative responds, particularly in manufacturing. Manufacturing primarily is target markets for developed economies that currently gripped by the crisis. The impact showed in export performance of several regional countries as well. The ongoing global crisis had profound impact on the Asia and Pacific region. As a result, the region's aggregate growth is expected to fall to 3.3% in 2009 (ADB Statistic, 2009) from the remarkable growth of 9.8% in 2007. The latest data (table 1) shows Malaysia's gross export fell 18% from RM 185 billion in third –quarter 2008 to RM 151 billion in the fourth quarter. Malaysia experienced a contraction in exports and imports from the fourth quarter of 2008.

Table 1: Gross Exports, Imports, and Trade Balance

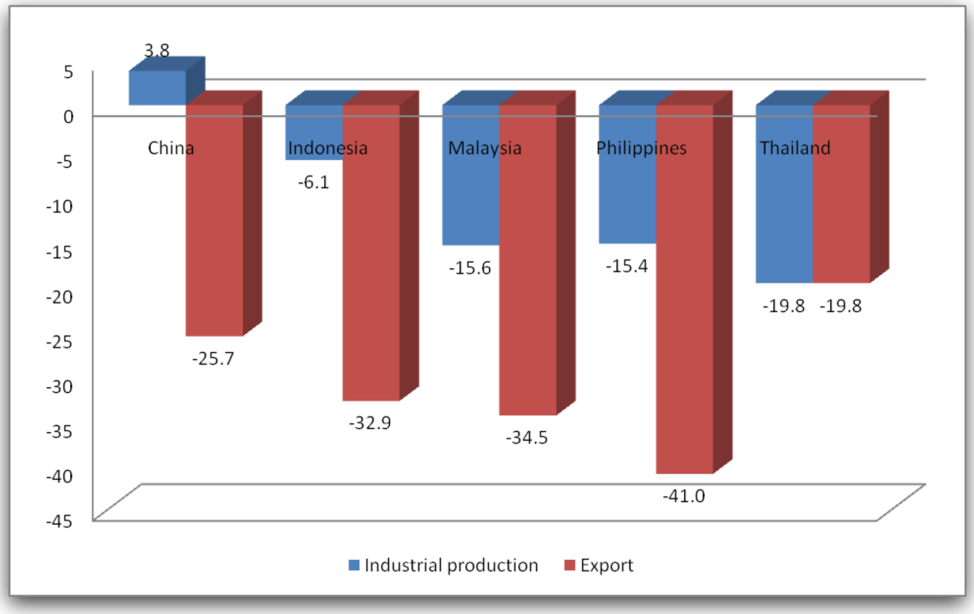
Value (RM Million)	2007				2008				2009	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Gross exports (f.o.b)	138,125	145,005	158,532	163,492	151,798	175,169	185,234	151,293	121,472	129,128
Gross imports (c.i.f)	117,065	122,383	130,273	135,093	124,972	134,525	143,474	118,639	88,802	102,611
Trade balance	21,059	22,622	28,259	28,399	26,826	40,644	41,759	32,654	32,670	26,517
% annual change										
Gross exports (f.o.b)	1.0	1.3	0.9	7.6	9.9	20.8	16.8	-7.5	-20.0	-26.3
Gross imports (c.i.f)	5.5	1.7	2.0	10.9	6.8	9.9	10.1	-12.2	-28.9	-23.7
Trade balance	-18.3	-1.0	-3.8	-5.9	27.4	79.7	47.8	15.0	21.8	-34.8

Source: Department of Statistic, Malaysia, 2007-2009

The trade balance improved marginally in the first quarter of 2009 but dropped again in the second quarter. The trend in falling exports is not encouraging, as it shows a continuous decline in aggregate demand from external effects, which is the main channel through which the global financial crisis has penetrated the Malaysian economy.

THE MANUFACTURING INDUSTRY IMPACT OF GLOBAL CRISIS

As consumers in developed economies abruptly cut back on spending in 2008 and the beginning of 2009, demand for Asia's exports have fallen sharply, as shown in Figure 2. In February 2009, exports from China fell nearly 26 per cent compared to the previous year, while in Indonesia exports contracted about 33 per cent. Similarly, the January 2009 export data for Malaysia and the Philippines were just as astounding and indicated a year-on- year drop of more than 34 per cent and 41 per cent, respectively.



Source: World Bank: East Asia and Pacific Update: Battling the Forces of Global Recession (2009)

Figure 2: Real GDP by Sectors, Asia, 2008-2009 (% Annual Change)

The current global crisis has impact Malaysia via the trade channel. For a country like Malaysia which dependent on trade, therefore, if the country's dominant trade partners were to decrease, its repercussions would be felt throughout the economy.

Table 3: Real GDP by Sector, Malaysia, 2008-2009 (% Annual Change)

	2008				2009	
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**
Sectors						
Agriculture	6.5	6.3	3.3	0.5	-4.3	0.3
Mining and Quarrying	3.6	-0.5	-0.3	-5.7	-5.2	-2.6
Manufacturing	7.0	5.6	1.8	-8.8	-17.6	-14.5
Construction	5.3	3.9	1.2	-1.6	0.6	2.8
Electricity, Gas and Water	4.7	4.1	2.5	-2.6	-8.2	-1.1
Service Sub-sectors						
Wholesale and Retail Trade	11.8	12.7	9.4	5.9	-1.7	0.4
Accomondation and Restaurant	10.0	7.3	4.7	7.4	2.1	2.9
Transport and Storage	9.9	8.1	5.9	1.0	-3.9	-6.4
Communication	7.5	7.9	7.4	6.3	4.9	5.8
Finance and Insurance	9.9	7.5	10.0	3.5	1.2	3.3
Real Estate and Business Services	4.8	3.8	-2.0	-0.6	-6.7	3.0
Government Services	7.0	7.9	10.5	18.2	2.8	0.5
Other Services	5.0	5.3	5.3	5.3	5.2	4.5

Source: Department of Statistics, Malaysia 2008-2009

The evident is striking when notes to the structure of Malaysian export. This structure clearly indicates the dominance of manufactured goods which accounts for about 82% of total export (Nambiar, 2009). Within the category of manufactured goods, electronics, electrical machinery, and appliances are about 53% of the export share. There is no doubt that the export of manufactured goods is particularly vulnerable to drops in external demand. Since the demand for electronics goods largely comes from developed countries has been hit by recession (particularly the US, Europe, and Japan), a decline in consumption in these economics is bound to have a negative impact on the exports of Malaysian manufactured goods.

Table 3 above shows the continuous decline in manufacturing which the steepest in export-oriented than others sectors. The decline in manufacturing is facing the full brunt because of the collapse demand from developed markets. Manufactured exports dropped by -8.8% in the fourth quarter of 2008, -17.6% in the first quarter of 2009 and -14.5% in the second quarter. Additionally, Table 4 supports the statement where export faced a contraction of -11.7% in the fourth quarter of 2008 and -19% and -22.3% in the first and second quarter of 2009 respectively. Disaggregating the data, semiconductor exports recovered slightly in the first quarter of 2009 but dropped sharply in the second quarter. Other electronics exports faced a severe contraction over both quarters of 2009.

Table 4: Gross exports by Major Destinations, 2008-2009 (% Annual Change)

Major Sectors	**2008**				**2009**	
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**
Semiconductors	-24.7	13.2	0.1	-17.5	3.6	-18.4
Electronic equipment & parts	-2.5	1.0	-5.5	-27.2	-30.8	-27.0
Consumer electrical products	16.2	36.0	50.5	14.7	-29.9	-13.9
Industrial & commercial electrical products	-9.3	19.8	18.1	-9.2	-22.4	-30.2
Electrical industrial machinery & equipment	0.0	3.8	-1.5	0.9	-19.5	-23.1
Household electrical appliances	9.2	-3.7	-2.7	-6.9	-29.2	-5.5
Total (Electronics and Electrical)	-9.4	9.2	2.6	-17.2	-19.0	-22.8
Transport equipment	0.3	40.3	13.0	3.8	22.2	-17.0
Food	36.8	55.4	57.2	22.0	0.5	-20.7
Beverages & Tobacco	12.5	6.6	23.3	-2.5	-5.5	18.2
Textiles, clothing & footwear	3.3	5.7	3.1	-1.5	-6.2	-15.3
Wood products	-9.5	-4.3	14.6	3.7	-24.9	-22.8
Rubber products	23.3	26.4	32.4	1.5	-8.3	-4.7
Paper & pulp products	16.2	17.2	19.5	-0.9	-10.9	-0.5
Petroleum products	96.7	56.3	67.8	-24.7	-40.8	-49.5
Chemicals & chemical products	6.8	27.3	23.0	-17.0	-29.8	-25.2
Non-metallic mineral products	14.2	42.0	55.1	22.8	14.3	6.1
Manufacturers of metal	26.9	8.4	18.5	-8.3	-30.2	-21.8
Optical & scientific equipment	7.2	22.1	-0.4	10.8	-13.0	-31.4
Toys & sporting goods	7.2	14.3	19.4	-2.0	-20.3	-17.9
Furniture & parts	0.6	-4.1	8.1	4.5	-13.5	-14.4
Other manufacturers	-15.3	-11.2	10.8	23.5	8.9	38.5
Total	1.0	14.4	11.4	-11.7	-19.0	-22.3

Source: Department of Statistics, Malaysia 2008-2009

The most worrying fall has been in manufacturing export, and within that in the exports of electronics, electrical machinery and appliances. The decrease of these products due to attributed to fewer exports of office machines and other machines and parts to the United States and Europe (Xinhua, 2009). Optical and scientific equipment, petroleum products, textile, clothing and footwear also experienced a sharp fall in exports in the first two quarters of 2009. The sharper decline in exports to key markets in the first two quarters of 2009 left the Malaysian economy in a precarious situation.

RECOMMENDATIONS

This paper provides two recommendations for Malaysia in order to eliminate the worldwide crisis. Recommendations explained are social impact of structural adjustment. Increasing the productivity of its human capital development and adoption a diversification on its export market for enhancing the economic integration of Intra-Asian and Intra-ASEAN exports These two recommendations are believe will enable Malaysia respond effectively to the worldwide crisis.

Human Capital Development

Economic development has critical and mutually reinforcing features involving human capital. Humans are the only material in the world that can create material value, while others focus on material development (including sustainable development) targets humans as the beneficiary of the processes they create. Additionally, researchers study about human resources on international scale can be seen as a key determinant to the success of globalizing strategies. Furthermore, organization attempting to succeed in a global business environment must invest in the acquisition and development of employees, and acquire effective managers throughout the world (Dowling and Welch, 2004; Drost et al., 2002; Schuler et al., 1993). The complex and ever changing global environment requires flexibility; however, the organization's ability to devise strategic responses may be constrained by a lack of suitably trained, internationally oriented personnel. This section thus examines the employment and income effects of the 2008-2009 global crises and also existing policy targets meet the objective to enabling Malaysia's human capital to compete in global markets and sustain material improvements in standards of living. A number of issues such as poverty levels, unemployment, and education and healthcare are discussed in the effect of human capital development.

Unemployment and wage levels are among the immediate variables to be affected in a worldwide crisis. With export falling and GDP contracting, the early problem faced by Malaysia includes retrenchment, which has resulted in lay-offs. The worst hit sector is manufacturing sector. Retrenchments are worst in the manufacturing sector as it continues declined throughout 2008 until first quarter of 2009. It resulted for more than 50% retrenchments are from manufacturing sector. As shown in Table 5 below.

The slowdown in manufacturing productivity will also restrict the country's capacity to achieve its vision 2020 goal of achieving developed status. The slowdown in GDP growth from the late-1990s is a consequence of Malaysia's failure to upgrade into high value-added activities.

Table 5: Retrenchments, Malaysia, 2008-2009

	2008					2009	
	Q1	Q2	Q3	Q4	Total	Q1	Q2
No. of workers	2,397	2,821	1,379	7,254	**13,851**	12,590	7,470
Agriculture, forestry & fishing	-	2	84	312	**398**	20	208
Mining	8	18	28	35	**89**	28	45
Manufacturing	1,415	2,080	2,618	4,901	**8,396**	9,778	5,307
Construction	42	44	32	81	**199**	100	336
Services of which:	932	677	1,235	1,925	**4,769**	2,664	1,274
Electricity, gas, and water supply	74	3	-	-	**77**	5	38
Wholesale and retail trade, hotels & restaurants	339	405	176	1,132	**2,052**	483	318
transport, storage & communications	347	68	254	104	**773**	210	235
Finance, insurance, real estate	138	87	192	591	**1,008**	620	388
Other services	34	114	613	98	**859**	1,346	595

Source: Ministry of Human Resources, 2009.

The main innovation deficiency facing manufacturing firms in Malaysia relate to the lack of technological upgrading. On the other hand, the resourcefulness in the human capital supports process technology changes to lower production costs, shorten delivery times, offer continuous improvements in product and service quality, and provide flexibility in the labour force to step production up and down, as appropriate. Therefore, Malaysia needs to move to another stage of development to produce higher value-added products that can only be achieved in an innovation-driven economy dominated by technology-intensive operations.

To ensure that a temporary shock is not converted into severe permanent declines in welfare of poorer household, social protection and human development should be implemented. There are many programs have been shown in evaluations to be worth investing by Government of Malaysia. The Malaysian Government should prioritize protection and expansion of those that most effectively buffer the impact of crises in the poorest household (Ravallion, 2008). Malaysian Government should take on the Keynesian strategy of expanding human capital development in the country to provide the basis for raising wages and, in that way, support the upgrading of the Malaysian economy into higher value-added activities. In Keynesian strategy, government has intervention in the economy for the purpose to achieve full employment and stable prices. In addition, the current crisis has highlighted the urgent need for Malaysia to restructure its economy to stimulus a shift towards a high income and high value-added economy and society (Abidin and Rasiah, 2009). As a consequence, Malaysia should strengthen its human capital to enable them to successfully achieve the type of economic restructuring it needs.

In recognition to the importance of human development, Malaysian Government introduced various measures in the stimulus packages cover areas such as employment opportunities, educational development, promotions of healthcare and social benefits, improvement of housing requirements, and upgrading roads and the transport infrastructure (Abidin and Rasiah, 2009). As a result, the impact on development human capital will contribute to a better quality of life, increase in domestic demand on products and services, and reduce dependence on the Government expenditures.

Another implementation Malaysian Government should do in order to improve the productivity of its human development by reducing precautionary savings. Malaysian Government should spend more on health, education, and social security to reduce household needs for precautionary savings. Survey shows that high household savings rate in Asia are partly due to precautionary demand for savings as a result of low levels of government spending on social safety nets, including unemployment insurance, health insurance and retirement pensions, and on education. They need strategies to transfer more corporate savings to households to encourage greater consumer spending. Furthermore, they also need the policies that promote small and medium-sized enterprise and service industries to better align domestic production with domestic demand. All above strategies are believe can achieve the goal of high income and high value-added economy and society.

Export Diversification

While the challenges are substantial, the crisis could also be an opportunity for Asia to fundamentally restructure its approach to develop and bring about a more sustainable global balance- a new development paradigm for Asia (Kawai, 2009). Asia has become the leader in world's manufacturing sector. This gives an opportunity for Asia especially Malaysia to become not only a major source of goods and services in production, but also a major source of demand. To rebalance growth, hence, developing Asian countries need to reinforce domestic and regional demand as well as revitalize their domestic economies. Further diversification of export markets and increasing intra-ASEAN and Intra-Asian trade are believed can widen the domestic demand base. Formerly, the composition of trade from intermediate input for the production of goods for final demand in traditional markets are sent to Europe and the United States hence, the needs to shifts towards meeting in increasing final demand within Asia itself are now encouraging.

Malaysia has a technology transfer unit in the Ministry of International Trade and Industry but its tasks are only limited to registering applications (Rasiah, 1999). Malaysia, purposely should pursue both strategies and remove incentives given to labour-intensive, low-technology and non high-tech industries of manufacturing industries to technological deepening. The industrial policy in at least the last 20 years has been centred on increasing export growth. The government has tackled employment generation and poverty eradication through export-led economic growth, creating five-year plans and industrial policy largely premised on this assumption. The approach, however, must be re-evaluated and alternative scenarios must be devised to prepare for what could be a prolonged period of soft demand for Malaysian exports. Accomplishing strategies will be very difficult because some of the assumptions that have traditionally driven policy-making must be re-examined and replaced. Accordingly, new strategies to drive economic growth must be designed and implemented.

In view of the current global crisis, Malaysia will have to readjust its growth strategies and shift away from its dominant emphasis on export-oriented growth, if the crisis is prolonged. Currently, support for the export-oriented policy comes from other elements in the policy landscape and involves a suitable industrial policy, export promotion institutions and strategies, and fiscal incentives. A reorientation can only be successfully accomplished if a suitable alternatives policies and strategies are selected and implemented. A reorienting strategy would function along three lines. One of the strategies is resources would be shifted from manufacturing industries that are concentrated on exports to developed countries to industries and services that serve the domestic market.

In developing countries which exports remains one of the few channels that in the longer run significantly contribute to higher income per capita growth rates of a country. As a consequence, export diversification is one way to alleviate constraints of unstable global demand. Another issue relates to the competitiveness of a country's exports since globalization by accelerating cross-border trade exposes countries' exports to global competition. To be successful in export diversification, countries' export needs to be globally competitive to take advantage of leveraging world markets. Lederman and Maloney (2007) provide robust empirical evidence of a positive effect on export diversification on per capita income growth. Export diversification could help to stabilize export earnings in the longer run (Ghosh and Ostry, 1994; Bleaney and Greenaway, 2001). Agosin (2007) supports that export diversification has a stronger effect on per capita income growth when a country's exports grow faster than alone. Furthermore, in a dynamic cross-country panel model, Lederman and Maloney (2007) also find some evidence in support diversification-led growth. Within country studies by Amin Gutierrrez de Pineres and Ferrantino (1997) as well as Herzer and Nowak-Lehmann D. (2006) examine the link between export diversification and economic growth in Chile, and their findings do suggest that Chile has benefited greatly from diversifying its export base. Maximising the growth potential for regional demand calls to encourage intraregional trade. A promising area is investment in infrastructure at both the national and regional level to improve cross-border connectivity to achieve "seamless Asia".

SUMMARY

Improving the productivity in human capital development and enhancing the economic integration of Intra Asian and Intra ASEAN are two recommendations believed will enable Malaysia to respond effectively to volatility in international markets. In addition, the domestic resources available can be mobilised to mitigate the adverse impact of a worldwide crisis.

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