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Industrialization Strategy and Industrial Relations Policy in Malaysia

Sarosh Kuruvilla

The notion that the logic of industrialism (Kerr et al. 1960) would lead to a convergence of industrial relations systems has been swept aside by history. Nonetheless, in addition to political regimes and market pressures, industrialization is still regarded as a central variable in explaining industrial relations policies or transformations in industrial relations systems. The argument that stages or levels of industrialization are correlated with certain patterns of industrial relations and trade union influence has received particular attention. For instance, Frenkel (ed., 1993) suggests that, in the most general terms, it appears that a country's level of industrialization is related to the influence trade unions have in shaping workplace industrialization. In Frenkel's nine-country study, the least industrialized countries—Malaysia, Thailand, and China—show less trade union influence in workplace industrial relations than the more developed countries, such as Singapore. Frenkel contends, however, that it is simplistic to assume that industrial relations systems in countries at similar levels of industrialization ought to be similar, given the variation in patterns of industrialization across the four "Asian tigers," which are at similar levels of industrialization.

M. Bjorkman, L. Lauridsen, and H. Marcussen (1988) hypothesize that different patterns of industrialization are associated with different kinds of capital-labor relations. Their theoretical work suggests little or no relationship between capital-labor relations and two levels of import-substitution industrialization (simple and advanced). They argue that simple export-oriented industrialization, based on labor-intensive production, is associ-

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ated with a highly repressive labor system, while more advanced forms of export-oriented industrialization, based on capital-intensive production systems and that rely on highly skilled labor, are likely to result in more inclusive and less repressive industrial relations systems. In their scheme, different forms of industrialization reflect the nature of different forms of capital accumulation, which translate into different kinds of capital-labor relations, an argument Sharma (1985) also advanced.[1] Empirical tests of their propositions have yet to be conducted, however. Deyo (1989) also finds policies of labor suppression by East Asian states consequent to export-oriented industrialization.[2]

Somewhat related to this argument is the suggestion of the new international division of labor (NIDL) theorists that industrialization has been thrust upon peripheral societies by core economic powers and that this industrialization, through the transmission belt of global multinationals and condoning local governments, has led to union repression and marginalization in peripheral societies. Frenkel (ed., 1993) does not find this hypothesis to be supported in his study, although he suggests that further research is necessary in this regard.

What is missing from this literature is a closely reasoned argument about how industrialization strategies affect the actions of management, labor, and government in the labor relations sphere. More specifically, what factors lead governments to decide on a specific industrialization strategy? What implications does the choice of such a strategy have for the industrial relations (IR) system and, specifically, the institutional arrangements governing labor relations? The institutional arrangements in particular are central to the way in which the industrial relations policies of the state and the industrial relations practices of the actors develop and change. A focus on rules and laws is not enough. Previous literature has, by and large, ignored these arrangements. Instead, they have concentrated on broader typologies of IR systems, such as "collaborative-repressive."

In this chapter, a different view is taken of the relationship between industrialization strategies and industrial relations policy and practice. I argue that it is not the logic of industrialism or the levels of industrialization per se but the choice of an industrialization strategy and the shifts between such strategies that influence changes in industrial relations policies. Different industrialization strategies exist, such as import-substitution, export-oriented, basic industries, and small-scale strategies, each with its attendant implications for industrial relations policies. The argument developed here is that it is the shift from one strategy to another that is important in understanding transformations in industrial relations systems (i.e., these shifts provide a window through which to assess the dynamics of change in industrial relations systems).

It is not my intent to suggest that the changes in industrial relations policies are solely determined by shifts in the industrialization strategy.

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Other factors, such as changes in political regimes, are often critical reasons industrial relations systems change, as demonstrated by Collier and Collier (1991) for Latin America and suggested by various others (e.g., Frenkel, ed., 1993; Bjorkman, Lauridsen, and Marcussen 1988). It is important to note, however, that the relative importance of various factors differs from country to country. In the countries of East Asia and Southeast Asia, whose industrialization experiences are relatively recent and largely successful and whose political regimes, with the exception of Thailand, have been relatively stable, the variables related to industrialization may have stronger explanatory power than those related to politics.

Nor do I argue that the type of industrialization strategy that a country pursues is deterministic (i.e., a change from strategy X will lead to industrial relations systems type Y). Rather, I argue that the shift from one strategy to another provides a rare "moment in the transition" of economies that enables researchers to view the dynamics of industrial relations transformation. The particular pressures and the direction of change in an IR system are necessarily specific to each country, but in the context of the NICs of Southeast Asia, the shifts in industrialization strategies could provide a general framework for the analysis of IR system change. Implicit in this argument is the notion that certain industrialization strategies tend to be associated with, and to sustain, certain industrial relations policies and practices.

In this chapter, Malaysia is used as an example to examine this "moment in transition" in an industrial relations system. In Malaysia, industrialization strategies were largely a function of the ethnic tensions and the economic results of policies introduced to manage these tensions. I argue that the shift from an import-substitution policy to an export-oriented policy resulted in an increasingly inflexible and government-dominated industrial relations system. In assessing the dynamics of change in the industrial relations system, three factors appear important. These include the demands of the industrialization strategy itself (EOI, based on low-cost, labor-intensive manufacturing), the state's dependence on foreign investment to sustain this strategy, and the state's need to increase the economic efficiency of state-run plants, all of which constituted pressures for change in industrial relations.

Although the focus is on Malaysia, the argument is equally applicable to the Philippines, Indonesia, and Thailand (Kuruvilla 1992), as well as to other Third World countries that are under pressure to restructure their economies (Katz, Kuruvilla, and Turner forthcoming; Singh 1992). The next section briefly describes the Malaysian economy, including previous and current state industrialization strategies. I then discuss industrial relations strategies. This is followed by an analysis of the outcomes of Malaysia's industrial relations policy. The final section provides some concluding observations and notes several implications for further research.

Malaysia's Economy Today

Malaysia is one of the fastest growing economies in the world and in many ways a Third World success story. Twenty years of sustained growth and diversification have reduced the economy's reliance on primary products, such as tin and rubber. Malaysia is still the world's largest exporter of tin and rubber, however, the largest exporter of palm oil, and a significant producer of oil, natural gas, and timber. More recently, it has become one of the largest manufacturers of semiconductors and a sizable manufacturer of electronics, electrical products, and textiles. Exports account for about 61 percent of gross national product (GNP), which makes the economy very dependent on the external economic climate.

Although growth was slowed during 1982 and 1985–86 as a result of falling prices in commodities, Malaysia has sustained high economic growth since then through its booming export trade in manufacturing, which is driven primarily by foreign investment. Industry has supplanted agriculture as the major contributor to gross domestic product, accounting for 42 percent of GDP, and low-cost, labor-intensive manufacturing accounts for about 48 percent of export earnings. In the last few years, Malaysia's GDP has grown at an average annual rate of 8.7 percent, making it among the highest in the world, and manufacturing has grown at about 15 percent annually. National and per capita incomes are increasing at a rate of 7 percent annually, and the per capita income—about U.S.$2,000—is higher than the per capita incomes of most Third World countries.

Foreign investment in Malaysia continues to increase, attracted by the favorable investment policies, the cheap, docile, and skilled labor, and the well-developed infrastructure (Malaysia has 30,000 kilometers of paved roads, reliable and efficient telecommunications, cheap and abundant electricity, and efficient transportation systems). Foreign investment is still dominated by low-cost, labor-intensive industries, although a small shift to more higher-technology production is apparent and the country has begun attracting more larger companies. Japan is the largest investor, closely followed by Taiwan, which alone accounts for 25 percent of the total foreign direct investment and the largest number of projects. Industrial relations in Malaysia have recently been characterized as becoming highly repressive and trade unions as weak, excluded by the government in decision making at national levels, and having very little influence at the workplace level (Arudsothy and Littler 1993). Table 3.1 provides basic economic statistics.

Industrialization Strategy in Malaysia

Malaysia's industrialization strategy has been determined largely by tensions between the three dominant ethnic groups: the Malays, who form

Table 3.1. Summary of the Ma

Population (in millions)	
Per capita income (in U.S.$)	
Civilian employment	
Agriculture	
Industry	
Services	
Sectoral share of GDP	
Manufacturing	
Agriculture	
Services	
Unemployment rate	
Unionization rate	
Exports as percentage of GDP	
Share of labor-intensive sector invol manufactured goods for export	
1980	
1988	
Contribution of EPZs to total expo	
1988	
Contribution of MNCs to total exp	
1971	
1980	
1986	

Sources: Lim and Pang Eng Fong 199

54 percent of the population
37 and 16 percent respecti
draws heavily on A. Bowie's
Before its independence
dependent on exports of prin
tion accounted for 85 percen
Agriculture, mining, banki
foreign interests (mostly Br
largely by ethnic Chinese ar
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businesses and less than 1.5
4 percent of the nation's i
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Import-Substitution Indu

Market-Led ISI. Economi
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(which accounted for 30 percent of planned expenditures), while industrialization was left to the private sector. The state restricted itself to the creation of a favorable climate to attract foreign investment in import-substitution industries. Among the state initiatives during this period was the enactment of the Pioneer Industries Relief from Income Tax Ordinance of 1958 and the creation of the Malaysian Industrial Development Finance Corporation, which was responsible for providing investment capital and for the development of industrial estates. After the 1968 withdrawal of Singapore from the Federation of Malaya, the Investment Incentives Act was introduced, aimed at stimulating industrial growth by attracting foreign investment with a plethora of tax concessions, enhancing the Pioneer status conditions, and creating free trade zones. (For a detailed description of specific policies, see Spinanger 1986.)

The decision to leave industrial investment to the private sector was largely a political compromise reached between the parties making up the ruling alliance (Bowie 1991). The United Malay National Organization (UMNO) realized that Chinese and Indian acceptance of the UMNO's political role was to some extent dependent on the state's not interfering in private commerce and industry (which they dominated) beyond its regulatory role. The UMNO therefore accepted (temporarily) the Chinese and Indian dominance of business and commerce, in exchange for their acceptance of UMNO political domination and UMNO efforts to increase Malay participation in the rural sector and in transportation, mining, construction, and timber industries. World Bank recommendations favoring industrialization under private sector auspices also influenced this policy (Spinanger 1986; Bowie 1991).

The strategy had mixed results. On the one hand, by 1969, Malaysia's economy had grown by more than 5 percent per year, manufacturing growth rates were high, at 10.2 percent annually, and private investment had increased by 7.3 percent annually. The fastest growing industries were textiles, electrical machinery, and motor vehicle assembly. On the other hand, the participation of the ethnic Malays in this economic growth was limited. Ownership among Malays still remained static, at 1.5 to 2 percent, while the share among the Chinese and Indians grew somewhat.[4] Malay participation in manufacturing employment had increased only marginally and was much lower in skilled and managerial jobs.

It became clear that the market-led approach succeeded in strengthening the economic position of the Chinese and Indians, relative to the Malays, and anger over this outcome was responsible for the communal violence after the 1969 parliamentary elections (Bowie 1991; Lim and Pang Eng Fong 1991). The relative economic stagnation of the Malays resulted in Malaysian politics becoming increasingly polarized on ethnic lines during this period (Bowie 1991).

New Economic Policy (NEP) and State-Led ISI. The NEP, promulgated in

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and the policies did not re
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The economic implicatio

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banks. Foreign debt as a percentage of GNP increased from 8.45 percent in 1975 to almost 11 percent by 1976–77.

Transition to Export-Oriented Industrialization

The resource crunch drove the government to articulate a mixed policy. On the one hand, the government launched a massive campaign to encourage private and foreign investment during the 1977–80 period. Policies emphasized investment incentives, the development of infrastructural facilities, and numerous tax, labor, and other incentives. (Spinanger 1986 and Lim and Pang Eng Fong 1991 discuss these in greater detail.) Electronics and textile industries were specifically targeted. Foreign companies manufacturing for export were exempted from the ICA policies on Malay share ownership, and labor laws that might have discouraged foreign investment were relaxed or went unenforced. Unions were excluded from key industries and the export sector. This new phase saw the beginnings of massive foreign investment in the electronics sector by U.S. and Japanese companies.

On the other hand, the state increased its involvement in the development of heavy import-substituting industries. The continued failure of state-led NEP and ICA policies to achieve economic power for Malays commensurate with their distribution in the population (Malays owned only 12.4 percent of corporate wealth in 1978, and the target of 30 percent ownership by 1990 appeared out of reach) led to further pressures from Malay nationalists to increase ownership by Malays (Bowie 1991).

In response, in 1980, Dr. Mahathir Mohammed, the then–industries minister, announced a heavy industries policy (HIP) geared to achieving the twin objectives of accelerating industrial growth and improving the economic position of Malays. Through the Heavy Industries Corporation (HIC), the state now had a leading role in establishing large-scale, capital-intensive, import-substituting industries to provide industrial goods and consumer durables for the domestic market and a foundation to support a range of private sector and consumer goods industries. The HIC invested

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Outcomes of Export-Orie

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in a series of large-scale joint ventures, including PROTON (Malaysian Small Car Project), iron and steel works at Trengganu, and plants for cement, motorcycles, aluminum, and gas, of which were Japanese private sector firms with about 30 percent investment from the government.[5]

The outpouring of government revenues to sustain the NEP and ICA policies, combined with the recessions of 1982 and 1985 and the draining of revenues by the heavy industries program, drove Malaysia's external debt to unprecedented levels (Lim and Pang Eng Fong 1991). By 1986, debt as a percentage of GNP had tripled, bringing it to 30 percent, over 1976 levels. Foreign borrowing became the primary source of foreign capital inflow in the first half of the 1980s. The poor performance of the HIC contributed further to the revenue crunch. Thus, by 1987, the HIC had reported losses exceeding U.S.$100 million, total state liabilities exceeded U.S.$2.24 billion, and 37 percent of the public debt was the result of government-backed foreign loans.

Given this second "resource" crunch, and under pressure from the World Bank and other lending agencies, Malaysia announced a series of austerity measures. In addition to cutbacks in public spending, these included the privatization of various state-owned public sector industries. Further, Malay managers in the state-owned heavy industries program were replaced by more "professional" Japanese and private sector managers.

To meet its interest payments on foreign debts, the state also encouraged export-oriented industries, simplifying bureaucratic controls, increasing investment allowances and incentives, and reducing corporate and development taxes. Clearly, the economic situation of the 1980s showed that the state could not reconcile its heavy industries program and its NEP and ICA programs with rapid industrial growth. The state came to be dependent on foreign investment for the growth of its manufacturing sector and exports. As a result, development priorities once again shifted to EOI from a policy of heavy industrialization for an increasingly protected domestic market. Since 1989, favorable external factors, dramatic increases in foreign investment, and growth in exports of manufactured goods have stimulated economic growth.

Outcomes of Export-Oriented Strategy

The description above suggests that during 1977 and then during 1988 it was the shortage of revenues brought about by the government's involvement in NEP, ICA, and the HIP, and the consequent increases in international debt, that brought about the shift to EOI policies. The shift from an import-substitution strategy to a more export-oriented strategy transformed the Malaysian economy in several ways.

First, foreign direct investment in Malaysia has grown dramatically since 1987. In 1989, total direct foreign investment in Malaysia exceeded