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IMPACT OF GLOBALIZATION TO MALAYSIAN FIRMS

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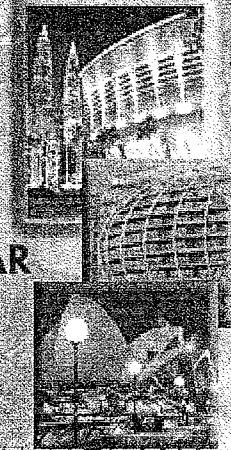
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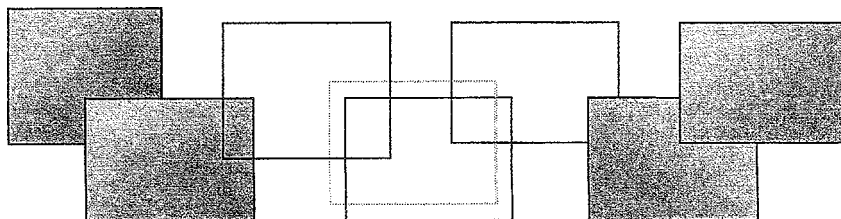
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IMPACT OF GLOBALIZATION TO MALAYSIAN FIRMS

BY

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ABSTRACT

Recent developments in the world economy show market integration to have strengthened international trade among nations. Market integration is an important element of globalization which is also predicted as an important phenomenon in business activities around the globe in the twenty first century. This paper discusses the impact of globalization to firms in the Malaysian economy. It highlights Malaysia's industrial development in the light of globalization. The process of industrialization and globalization have had a positive impact on Malaysian firms through the development of manufacturing capability, strengthened linkages and by way of attracting increasingly more multinational firms to relocate part of their operations in the country. However, challenges remain in maintaining the nation's competitiveness in the face of fierce competition from emerging markets not only in the region but also globally.

1.0 INTRODUCTION

Globalization is an important phenomena that has put countries and societies across the world to undergo huge transformation process. The fundamental understanding behind globalization is the integration of markets worldwide into a single global economy that advocates free market as exemplified by many nations opening their market i.e. China, former Soviet Union and the Eastern Europe block as explained by Rosiatimah (2002). She pointed out that the reason behind this trend is the growing global independence between nation and regions in terms of trade, investment, production, distribution, consumption and marketing. Another important element of globalization is trade liberalization involving providing a greater market access to foreign firms by lowering barriers to trade i.e. reduction of tariffs. Opening of markets certainly warrants industries and businesses to increase their competitiveness especially in this knowledge-based economy era. Recent developments in the world economy have proved that business environment is undergoing tremendous changes with the advancement of knowledge and technology. The World Bank (1998) had predicted that wealth creation in the twenty first century would depend on the ability of parties to access and expand stocks of knowledge and information in the process of production.

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2.0 GLOBALIZATION

There are various definitions given to explain the meaning of globalization. According to IMF, globalization is defined as the growing economic interdependence of countries worldwide through the increasing volume and variety of cross-border transactions in goods and services and international capital flows, and also through the rapid and widespread diffusion of technology. Thus, global economy would involve three pillars: international trade, outward investment and worldwide transfer of technology as pointed by Sieh (2000) in which these pillars are interconnected and reinforced by each other.

Anderson (2001) defines globalization as the declination of cost in business transactions internationally due to two factors, namely technological and government barriers. As markets integrate into one single global economy, the advancement of technological methods and deregulation of trade barriers by government is expected to reduce production cost. Rapid developments in computer information and communications technology have further shrunk the influence of time and geography on the capacity of individuals and enterprises to interact and transact around the world (Carbaugh, 2006). As cross borders barriers are reduced, transfers of technology would be widespread in the borderless economy and cheaper too as a result of easier accessing and processing knowledge, information and ideas from different parts of the globe.

According to Rodrik (2002), globalization refers to the emergence of a single global market that reduces trade barriers and advocate borderless business transactions. This process lead to an increase in the share of foreign good in a country's product. In other words, international trade becomes much more cheaper and freer and in many cases imported capital goods are likely to be significant cheaper than those manufactured at home.

3.0 INDUSTRIAL DEVELOPMENT AND GLOBALIZATION IN MALAYSIA

Industrialization and the process of globalization is quite synonymous in the Malaysian industrial context. Although initially the country's industrialization was inward focused i.e. to reduce dependency on primary commodities and importation of consumer goods, it steadily shifted its focus beyond her borders. From the onset, Malaysia's industrialization, which initially focussed on import substitution strategies and later export orientation, has significant traits of globalization. The country's industrialization process was characterized by the need to attract foreign firms and this would subsequently develop domestic firms to compete not only locally but also in the international market. Although the nation was successful in attracting foreign firms, development of local firms have yet to reach a critical mass to have a global presence. The dominant role of foreign firms in every phases of the country industrialization process had impacted the industrial development process. The immediate section discusses briefly Malaysia's industrial development and the eventual process of globalization that cometh with it.

Industrialization in Malaysia was formally pursued after the country had achieved her independence from Britain in 1957. Import-substitution industrialization (ISI) strategies for developing the manufacturing sector were immediately implemented after independence and were aggressively pursued until the late 1960s. A realization of the limitations of ISI strategies, and the relocation of the international semiconductor industry in the 1970s from developed countries to developing countries, saw a new industrialisation strategy. Export-oriented industrialization (EOI) strategies were adopted.

EOI was heavily dependent on foreign investors. Strategies were sought to encourage foreign firms which already had marketed their products locally, to set up production lines, and assembling and packaging plants, to supply finished goods. To encourage this industrial development, infrastructure was developed, manufacturers were indirectly subsidised and the domestic market was protected (Malaysia, 1966). The introduction of the Pioneer Industry Ordinance (PIO) of 1958 followed by Investment Incentives Act (1968 and 1986) marked the major involvements, policy-wise, of the state in developing the industrial sector. Despite market-led developments, government policies played a significant role in attracting foreign manufacturers.

The 1970s, 1980s and first-half of 1990s witnessed a massive influx of Multinational Corporations (MNCs) from the Japan, USA and the EU. Low wages, a trainable workforce and incentives, particularly Free Trade Zones (FTZs), were the main attractions for these multinationals. Japan was the largest source of investment in Malaysia. Japanese investment was mainly in the manufacturing sector, producing a wide range of products of varying levels of technology, such as electronic components and electrical appliances (including air-conditioners, radio-cassette players, stereos, television sets, etc.), textiles and basic metals. The influx of MNCs were also followed by the MNCs' suppliers from the home country, as especially in the case of Japanese based MNCs (Phongpaichit, 1990). Obviously this did not help in developing the manufacturing capability of the local firms i.e. one of the intended spillovers of FDI.

Despite the influx of foreign manufacturers as a result of EOI, which led to high growth and increased exports from the manufacturing sector, there were several structural weaknesses in the industry. Most MNCs, especially in the electrical and electronics (EE) industry, operated from FTZs and exported most of their products. This enclave factor and access to duty free importation of raw materials and intermediate inputs led to weak linkages with local firms. Furthermore, the existence of a distinct technological gap between foreign firms and local firms was also noted by O'Brien (1993) in his study. Foreign firms which utilised a higher level of technology had to source their inputs from elsewhere due to the low and unreliable product quality of local firms. Consequently, MNCs in EOI which operated a global strategy, sourced inputs from affiliates elsewhere, and in many cases were supplied by other sister subsidiaries located in a third country.

Another major criticism of EOI was that it created a narrow-based manufacturing sector. EOI was highly dependent on the electronics and electrical industry which formed the crux of the Malaysian manufacturing sector. EE, with its poor linkages, offset its high export earnings with its high import contents (O'Brien, 1993). These shortcomings were

the main factors influencing the government's decision to embark on the next stage of Malaysia's industrial strategy.

To reiterate, the high importation of intermediate goods, implying weak linkages as noted above, was undermining industrial development; while decline in the growth of the manufacturing industries, especially in the early 1980s, spurred policy makers to greater efforts to find another avenue for industrial growth. Thus it was hoped that heavy industry would anchor the new industrial growth and create the necessary backward and forward linkages. This was also in line with country's Look East policy which tried to emulate the heavy industries of Japan and South Korea. However, some argued that it was premature to develop heavy industries, due to the 'shallowness' of Malaysia's industrial development. The Malaysian manufacturing industry lacked the capability and supporting networks enjoyed by heavy industries in Japan and Korea. The structure of Malaysia's local industries differed from that of Japan and Korea. Japanese and Korean local firms are famous for the linkages that exist between them and large local firms.

In the Malaysian context, local firms were mostly small scale firms with limited capital, supplying only local markets. In the past the majority of SMEs concentrated on the production of food, beverages and tobacco, fabricated metal products, machinery and equipment, wood and wood products, textile and wearing apparel as well as leather (Malaysia, 1996)¹. Furthermore, SMEs produced a limited number of intermediate products for larger industries. In 2005, SMEs contributed to 29% of the total gross output, 31% of value added and 44% of employment of the manufacturing sector (Malaysia, 2006). This suggested that Malaysia's SMEs, especially small scale enterprises, were making progress in terms of contribution in the manufacturing sector. These figures show that SMEs do play a significant role especially in term of job opportunities. However there are plenty of room for improvement that could be done to enhance the contribution of local SMEs.

As for large local manufacturing firms, other than state-owned enterprises in the heavy industries, these were traditionally concentrated in the resource-based industries such as tin mining, agriculture and petroleum. Several other large local firms were suppliers to MNCs in the EE industries. However, these firms were too few in number in Malaysia to make a great impact to the domestic manufacturing sector.

4.0 GAINS OF GLOBALIZATION TO FIRMS

The process of industrialization, arguably led to the positive impact of globalization. For example, one study has found evidence of the development of local supporting industries such as tool and die machinery (Rasiah, 1993). This study argued that the development of supporting industries was attributable to two main factors; first, the rising cost of production in the MNCs' home countries and, second, the withdrawal of the Generalised

¹ SME are firms with a capital of less than RM 2.5 million which employ less than 200 workers.

System of Preferences (GSP)² status from NICs, especially Taiwan and South Korea, led firms in these countries to relocate their operations to Malaysia. Nevertheless, the number of large local firms in Malaysia was too small to have a large impact, when compared to the number of large local firms in NICs.

The presence of MNCs is significant in providing Malaysia's domestic firms access to advanced technologies through subcontracting, the creation of spin-off firms, OEM and training activities. R&D activities of MNC affiliates in Malaysia, as in other countries, are determined by the global strategy adopted by the parent firm. US-based MNCs, for example, have adopted a globalised strategy in their R&D activities - preferring to capitalise on the advantages and strengths of its worldwide affiliates and their locations. For example, INTEL has chosen Malaysia as the location for its design centre for microprocessors for hand held equipment (UNCTAD, 1995). It has globalised its R&D activities to such an extent that engineers from its Malaysian affiliate have been required to assist in the establishment of one of INTEL's highly-automated plants in the US. Motorola also has established an R&D centre in Malaysia and has designated it a corporate design centre for cordless telephones for Motorola worldwide (Hobday, 1996). It has been argued that with such rapid advances in manufacturing technology, MNCs operating in Malaysia can no longer be described as merely "screwdriver plants" (Ibid). Malaysia is attracting many high-tech MNCs. The presence of these firms and numerous others such as Motorola, Sony, Phillips and Mitsubishi present many valuable opportunities for technological development of local firms.

Being a more developed economy as far as the industrialising countries are concerned, Malaysian firms has started to benefit from globalisation by venturing abroad. With easier access to foreign markets plus government-to-government initiatives, increasing Malaysian owned firms are taking advantage of globalization. Three main industry where Malaysians are active are petroleum, automobile and the construction industry. Petronas, the national oil petroleum company, is involved in the Middle East and Africa, extending their know-how gained from years of joint-ventures with global oil giants. Petronas' involvement in producing liquefied petroleum gas sector in Iran and acquisition of Lotus by PROTON in order to gain access to the latest automobile technology are some examples. PROTON recently announced its decision to venture the vast market in China. Malaysian companies are also increasingly getting jobs such as construction of highways, IT projects and buildings.

5.0 CHALLENGES TO FIRMS

Globalisation enhances trade. Malaysia have benefited immensely from industrialization and globalisation. These are the factor that sets the country apart from most developing

² GSP is a preferential treatment by way of reduced or duty-free tariff rates granted by developed countries (preference-giving countries) to developing countries (preference-receiving or beneficiary countries). This preferential treatment is granted without any reciprocal obligation on the part of the developing countries. The aim of the tariff preferences is to provide a competitive edge and better market access to goods from developing countries.

economies. Despite these successes, a significant portion of the economy is adversely affected by it. The benefits that were discussed mainly confined either to large firms or government-linked companies (GLC), as far as most local firms are concerned, they face stiff competition not only globally but also in their own backyard.

This paper attempts to highlight certain issues and scenario of firms in context of globalisation. Among the issues that are surfacing Malaysian firms and industries are the ability to compete and to build linkages with foreign counterparts. Among other issue that should be in the mind of Malaysian corporate figures are how ready are their firm in facing greater challenge and competition both from local and foreign firms. The opening of trade barriers is expected to create greater challenges for Malaysian firms to compete against foreign giant firms who are well established in the global market in term of production efficiency and superior marketing strategies. However, on the positive aspect of reduction in trade barriers are opportunities for Malaysian firms to gain market share from especially from developing countries. For example PROTON has been trying to penetrate Middle East markets for sometime and indications have shown great potential that has led PROTON to announce their confidence to build assembly plants in Iran and Qatar. However, PROTON realise that their main obstacle is the ability to produce new technologies to enable them to reduce production cost from time to time as automobile giants from Europe and Japan, well known to have superior technologies.

A more important issue is the future of smaller firms that are relatively great in number but play minimal role in economic contribution to the nation. The future of these firms is much in the dark with the removal of trade barriers as they face stiff competition from not only local giants but also from the world best. This can be seen in the automobile industry as local vendors face the requirement of established manufacturers who demand high standards of quality. The main questions facing the local vendors are they able to meet stringent specification of manufacturers with competitive prices? Are they able to match their foreign counterparts in terms of quality, efficiency in delivery and attractive prices? To be able to match their foreign competitors, local vendors have to increase their technological capability in adopting new technologies to be able to increase production and cost efficiency.

Another important aspect is the ability to build linkages with both local and foreign large firms. Small firms should build significant linkages that create substantial value added to the value chain of goods and services. The country's policy makers are worried with trend of local vendors and supplier that provide very small value in the process of production such as simple and manual process that carry minimal value added. A study by Abd Halim & Mohamed Saladin (2002) in their study in Melaka found that linkages with foreign firms in the form of either joint-ventures or suppliers have enhanced technological capability of local firms. Their study showed that collaboration with foreign firms reflected the increase in the composition of technical workers. Abd Halim, Mohamed Saladin & Rosfadzimi (2004) revealed that there were evidence of local firms 'readiness in facing globalisation. However, readiness occurs among firms in the low value added industry in which export goods require low level of production and

consequently low level of production. In addition, firms that undertake R & D tend to be relatively smaller firms but with higher level of mechanization.

CONCLUSION

To enhance the competitiveness of the Malaysian firms in facing the globalisation era, the government thru various agencies such as Ministry of International Trade and Industries (MITI), Malaysian Industrial Development Authorities (MIDA) and Small and Medium Industries Development Corporation (SMIDEC) are advised to conduct a thorough study and revise the various incentives in the industrial sector to attract firms with high technological capabilities and willing to build linkages with local Malaysian firms. In addition joint ventures and other forms of collaborations that contribute to substantial value added from local firms should be encouraged with attractive schemes. In addition, the policy makers should play a bigger role in assisting small sized firms and also medium sized firms to create smart partnerships with big players with both established local firm and MNCs. Again the most important aspect of linkage that formed should benefit local firms in terms of both technology and value added.

In addition, there is an urgent need to intensify research in this area. With the foreign sector contributing more than half to the country's national income it is vital that local firms are able to compete competitively vis-à-vis foreign firms. Numerous in-depth studies are required if the phenomenon highlighted in this paper to be clearly understood and used to the advantage of local firms. In-depth studies will contribute in constructing more appropriate variables that can be proxies in studying, for example, the technological capability of the firms and the ability of firm to compete globally. These studies should also be wider in scope, covering small, medium and large firms nationwide and would become the source for data and evidence of the state of the local firms' performance vis-à-vis globalisation. Subsequently, these studies will provide recommendations to the Malaysian industrial authorities in designing refined and accurate trade and industrial policies to enhance local firms performance in face of globalisation.

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