FDI's – Are We Keeping Pace?

Gregore Pio Lopez

Foreign direct investment (FDI) has played a critical role in Malaysia's development strategy. The government continues to rely heavily on FDI as a means to finance development. However, FDI stocks for Malaysia have been stagnating since the financial crisis and is worrying especially when compared to our competitors.

Malaysia's reliance on foreign direct investment (FDI) is well noted. Historically, it was FDIs, under British imperialism that laid the backbone of the Malaysian economy – plantation (rubber and palm oil), mining (tin, petroleum) and after independence, the manufacturing sector (electrical and electronics). FDI has played an important role financing long-term economic growth in Malaysia. However, since the financial crisis of 1997/98, the changes in Malaysia's FDI stock have been a cause for concern especially when compared to its competitors.

UNCTAD reports that global FDI stock has risen from US$551 billion to US$12 trillion since 1980 with most of the FDI concentrated in developed countries. In 2006, 70 per cent of FDI stocks were located in developed countries while developing countries accounted for only 26 per cent. The lion's share of the FDI stock in developing countries was in the East Asian economies. Together, they accounted for 38 per cent of FDI to developing countries

FDI stock in China increased from US$1.1 billion in 1980 to US$293 billion in 2006, with significant jump recorded since the 1990s. If the FDI stock in Hong Kong SAR, the gateway to China, is included, the performance all the more startling. FDI stock in HKSAR alone increased from US$21 billion in 1980 to US$769 billion in 2006. This is truly remarkable, as HKSAR does not offer any incentives for FDI compared to other developing economies. India, another awakening giant, too has been recording tremendous growth in FDI stock. In 1980, FDI stock in India was only US$452 million. This grew to US$51 billion in 2006.

In ASEAN, the star performers are Singapore and Viet Nam. FDI stock in Singapore rose from US$5 billion in 1980 to a staggering US$210 billion in 2006. As for Viet

Nam, FDI stock increased from US$1 billion in 1980 to US$33 billion in 2006. This is remarkable considering the fact that Viet Nam was at war until 1975 and faced economic embargo from the US until 1994.

Malaysia started like Singapore with an FDI stock of US$5 billion in 1980. In 2006, its FDI stock stood at only US$53 billion, which pales in comparison with Singapore's US$210 billion. Furthermore, for the years 2000 to 2005, FDI stock fell lower than the US$53 billion recorded in 2000. This is distressing as Malaysia has all the pre-requisites as a favoured FDI destination and provides generous incentives to foreign investors.

There are several reasons why Malaysia is failing to attract and retain FDI in comparison to the frontrunners especially Singapore and HKSAR. The main problem has much to do with institutions. In the World Bank Doing Business 2007 Report, which measured "the ease of doing business," Singapore was at the top while HKSAR ranked fifth. Malaysia was only ranked 25. It takes 11 days to start a business in Singapore and HKSAR and 30 days in Malaysia, while addressing licensing issues takes 281 days compared to 129 in Singapore and 160 in HKSAR. The WEF Global Competitiveness Report and the IMD World Competitiveness Yearbook provide similar findings on institutional challenges in Malaysia.

Malaysia cannot emulate China, India, or Vietnam but should emulate Singapore and HKSAR given similar socio-economic conditions. Lessons from Singapore and HKSAR call for a return to meritocracy in the Malaysian civil service and an arms length relationship between politicians and civil servants.

The writer is Senior Research Officer at the Malaysian Institute of Economic Research.