ECONOMIC INEQUALITY IN MALAYSIA: THE ENEMY WITHIN

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ABSTRACT: The worsening inequalities across and within many countries have been an important part of the discussions among the international community in general and welfare economists in particular. The frequency of the recent economic crises across the globe had demonstrated that certain social groups are the hardest hit and disabled from recovering satisfactorily, despite swift national efforts and regional support. This research paper is part of a larger project viewing the current inequalities prevalent in Malaysia from a normative perspective through the lenses of Islamic Economics. It is aimed at providing complementary policy prescriptions in managing the widening socio-economic inequalities between the different marginalized groups. Given the conceptual nature of this research work, the emphasis remains in the critical literature reviews and latest report findings, both national and international. The ultimate objective of this study is to better understand the reality of economic inequalities and their long-term adverse effects on society perceived as vulnerable. Thus the main concern of the present work is to be clearly aware of the dangers of socio-economic inequalities and the various alternatives existing under the Islamic Economic System in managing inevitable inequalities. Key findings of this research paper include the recent relevant evidences of increasing economic inequality globally and Malaysia, the need for the stakeholders in Malaysia to begin considering the implications of economic inequalities critically and the effective application of several readily available schemes and tools in Islamic economics.
Keywords: equity, inequality, inclusiveness, human capital development, rights

INTRODUCTION

The extent of inequality, and what to do about it, are among the most hotly debated issues in economics. Equality matters because it carries an intrinsic value for most of the world's faiths and ideologies, religious or secular. Every faith and ideology has normative views on how much inequality is tolerable, or desirable. Islam for instance, permits inequalities resulting from differences in natural endowments such as talent and other God given faculties. It is equity that Islam emphasizes upon, although extreme inequalities are among the major concerns of redistributive schemes laid out by the *Shariah*. Normative theories of social arrangements that have stood the test of time also seem to demand equality of something. Some forms of inequality generate costs to society whereas others entail benefits. Arguably, inequality is a type of market failure which is said to occur when there is an inefficient allocation of resources in a free market. On the one hand, inequality is necessary for providing incentives in a free market economy, for without a degree of inequality there would be economic stagnation and lack of enterprise. Inequality promotes reward based performance, i.e. productivity and encourages entrepreneurs to take risks and set up new business. The challenge lies in the ability to identify the turning point at which the costs of inequality start to exceed its benefits.
Debates on inequality seem to become more intense in periods of rapid structural transformation, both in advanced economies and in developing countries. While discussions are often framed in either-or terms as to whether the government should tackle inequality or boost growth first, there is also a tendency to focus on simple, aggregate indicators of inequality which hide as much as they reveal (Le Houérou, 2015).

The World Bank Report (2015) on 'Addressing Inequality in South Asia' takes a fresh look at inequality in one of the most dynamic regions in the world, by focussing on well-being, exploring both monetary (income, consumption and wealth) and non-monetary (basic services in health, education, and infrastructure, as well as subjective assessments) dimensions of inequality. Apparently, some countries that do not appear to be particularly unequal when focusing on consumption per person are host to both extravagant wealth at the top and appalling human development outcomes at the bottom. When standard monetary indicators are taken at face value, South Asia has modest levels of inequality, with Gini coefficients for consumption per capita ranging between 0.28 and 0.40, much lower than in China, Mexico, or South Africa. Comparisons are suspected to be tainted by the nature of the monetary indicators used, with advanced countries and many Latin American countries using the income per capita, while South Asian countries continuing to rely on consumption per capita data. Nevertheless, the nonmonetary indicators of well-being in some South Asian countries convey a more striking story. For example, the share of children under five who are stunted among the poorest quintile is 50 per cent in Bangladesh and 60 per cent in India. The latter and Pakistan also report the highest infant mortality rates across comparators.

The extent of inequality is another matter of concern, especially in countries where it depends primarily on policy choices. The use of nonmonetary indicators of inequality captures the dispersion in human capabilities (an idea proposed and strongly defended by Sen; 1980, 1992). A multi-dimensional approach to human functioning that takes into account disparities in asset holdings, net worth and vulnerability offers a bigger and better understanding of the state of distribution of well-being of a nation. Inequality continues to be interesting and a challenging concern for the economists world around, given its implications on tangible matters related to achieving sustainable growth and development. The objective of this paper is to explain the economic situations in Malaysia that entails inequality done via review of policies and analyses of current economic situations.

Global Perspective of Inequality

As the international community shapes its vision for a post-2015 global development agenda, worsening inequalities across and within many countries have been an important part of the discussions. There is a growing recognition among all that economic growth is not sufficient to sustainably reduce inequality if it is not inclusive. Across the globe, people living in poverty and vulnerable social groups have been hit particularly hard by the global financial and economic crisis. There is urgency in finding ways to effectively reduce inequality involving an inclusive approach. Growing inequalities can be curbed by integrating policies that are universal in principle, but with particular attention to the needs of disadvantaged and marginalized populations. In reality, inequality affects not only the poor, but can also be detrimental to growth, stability and well-being in general.
World leaders, in adopting the Millennium Declaration in 2000, pledged to create a more equitable world. Disparities in education, health and other dimensions of human development remain large despite, marked progress in reducing the gaps. Various social groups suffer disproportionately from income poverty and inadequate access to quality services. The failure to pursue a comprehensive, integrated approach to development perpetuates such a predicament in the long run.

According to Stiglitz (2012), inequality leads to a less stable, less efficient economic system that stifles economic growth and the participation of all members of society in the labour market. Inequalities also pose serious barriers to social development by slowing the pace of poverty reduction and increasing the vulnerability of particular groups within societies to economic crises and prolonging the time it takes to recover from such crises.

Globally, the distribution of income remains very uneven. In 2010, high-income countries that accounted for barely 16 per cent of the world population were estimated to generate 55 per cent of global income. Low-income countries created just above one per cent of global income even though they contained 72 per cent of global population. Poor people in more unequal countries can have lower living standards than poor people in countries with lower average incomes but less unequal distribution. Between 1990 and 2012, inequality in disposable income, increased in 65 out of 130 countries for which data trends were available.

Palma (2011) observed that, in absolute terms, the top 10 per cent of the population in middle-income countries has succeeded in catching up with the top 10 per cent in rich countries, while the bottom 40 per cent of the population of middle-income countries is still far below its counterpart in rich countries. The author proposed an alternative to the Gini coefficient for measuring income inequality: the ratio of the top 10 per cent of the population’s share of income to the bottom 40 per cent’s share.

In addition, the wage gap between top and bottom earners has also increased in the majority of developed countries and in many developing countries. Labour-saving technologies have also had a negative impact on the earnings of less-skilled workers in developed countries (Stockhammer, 2012). Well-designed minimum-wage policies can have very significant, positive effects in reducing wage inequality.

Income inequality measures do not capture all household wealth which may include ownership of capital, including physical assets (land, housing) and financial assets. While the two are highly correlated, the distribution of wealth is typically more unequal than the distribution of income. Household debt is a new form of liability that plagues the urban poor than the rural poor. Regional and national trends in economic inequality suggest that there is no clear relationship between inequality and development. According to the empirical literature, social transfers have had a larger redistributive impact than taxes. Wang and Caminada (2011) estimated that social transfers accounted for 85 per cent of the observed reduction in inequality. Both social transfers and taxes should have immediate, direct effects on income distribution, although the magnitude of their impact will depend on the degree of progressiveness of the tax system and on the degree to which the poor benefit from social transfers and social insurance.

Malaysia's Situation

Contemporary Malaysia sees persisting inequalities, especially of regional, gender and ethnic dimensions, and a lagging development of human capability, institutions fostering inclusiveness and effective governance. The World Bank's (2010) *Malaysian Monitor: Inclusive Growth* broadly outlined the theme, making three principal proposals: i) Increasing economy-wide income-earning opportunities; ii) Promoting investment in human capital and iii) Providing social protection for the poor and vulnerable. Inclusive growth entails lifting households out of poverty and facilitating upward, especially inter-generational mobility. It is defined as comprising equitable distribution of the benefits of economic growth and of social spending across distinct income groups and the poor irrespective of their group membership; robust generation of broadly accessible opportunity for economic participation and safeguards for the vulnerable; and inclusion of citizens in policy formulation and implementation, towards minimising social exclusion and increasing social cohesion.
Although Malaysia's growth from 1971 to 2012 meets the criteria of inclusiveness to a considerable degree, its average annual Human Development Index (HDI) growth has slowed down from 1.21 per cent in 1980-1990 to 0.64 per cent in 2000-2012. This means despite the inclusive economic growth often claimed to eventually include development and welfare effects in the form of participation of commercial activities and inclusiveness, the rate of growth of HDI in general is deteriorating.

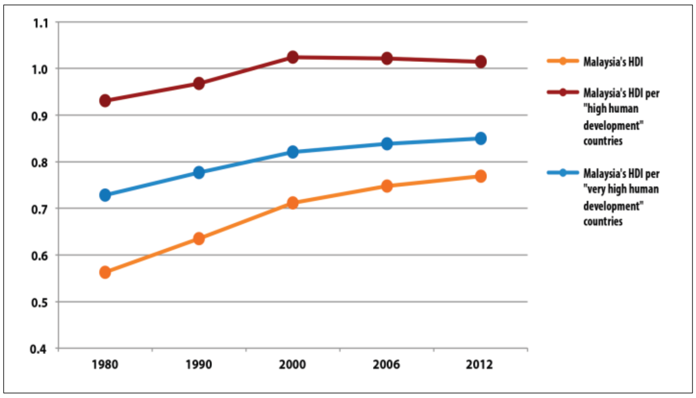

Figure 1: Malaysia's Human Development Index: score and relative position
Source: UNDP (http://hdrstats.undp.org/en/indicators).
Note: There are four categories of human development: very high, high, medium and low. The values are based on consistent indicators, methodology and time-series data, thus showing real changes in values and ranks over time reflecting the actual progress countries have made.

The Malaysian case study of inclusive growth shows that state sponsorship through human resource development, institutional and infrastructural amenities has brought tremendous social change and transformation to the nation. The educational process should be embedded with motivational content based on local knowledge so as to develop an individual's self-efficacy. A cross-sectional regression exercise shows that the better an individual education, activity status, location strata, occupation and age, the higher the purchasing power they would enjoy. Furthermore, men do better than women, all else equal, the married or widowed is better off than a single person or a divorcee, and a Bumiputera is relatively worse off than a Chinese or an Indian, all else equal. (MHDR, 2013: App. B6.3, pg. 305).

FINDINGS

Historically, Asia has experienced lower inequality than other developing regions. However, despite remarkable growth and impressive declines in extreme poverty, the region has seen widespread increases in income inequality at the national level, as well as in both urban and rural areas. Between 1990 and 2012, income inequality rose in 18 out of 31 countries accounting for over 80 per cent of the region's population. In countries where inequality has declined, two key factors have contributed to such declines: the expansion of education, and public transfers to the poor. The share of income owned by the top quintile of the population increased in the majority of countries (61 out of 111) although it did not increase globally from 1990 to the mid-2000s (Ortiz and Cummins, 2011).

In many developing countries, the distribution of land ownership has been particularly relevant in explaining inequality. Land concentration remains particularly high in Latin America, followed by Western Asia and Northern Africa (Vollrath, 2007; World Bank, 2005). In addition, the wage gap between top and bottom earners has also increased in the majority of developed countries and in many developing countries with data (Galbraith, 2012; ILO IILS, 2008; OECD, 2011). A significant part of the difference observed in disposable income disparities across countries can be explained by the redistributive impact of social transfers and taxes. In some cases, the negative effects of indirect taxes on the incomes of the poor, or nearly-poor, can be stronger than the positive effects of cash transfers (Lustig, 2012).

The Current Scenario for Malaysia

Although the doctrine of 'pro-poor growth' of the 1990s is increasingly seen as a flawed idea, the role of the state in managing distribution in the case of Malaysia has enjoyed unprecedented endorsement from economists and policy makers. However, the context of identifying the best indicators of national development, and ways to capture these indicators calls for looking beyond the standard approach of income and economic growth in explaining the development (Stiglitz et al., 2009).The Tenth Malaysia Plan Targets (2010) explicitly spelled out the equality related objectives of the New Economic Model (NEM) as follows:

Table 1: Distributive Targets of NEM

POLICY AIM	2009	2015
To reduce the incidence of poverty	3.8%	2.0%
To improve overall income inequality by reducing the Gini coefficient	0.441	0.420
To increase the mean income of the bottom 40 per cent households	RM1,440	RM2,300
To increase the percentage of bottom 40 per cent households with SPM qualification and above	30%	45%

The rapid increase in relative poverty of Malaysians from 17.4 per cent (2007) to 19.3 per cent (2009) and 20 per cent in 2012 contradicts the claims of successfully reduction of absolute poverty to 1.7 per cent in 2012, from 49.3 per cent in 1970. (MHDR, 2013). While the Gini was reduced by about seven per cent from its original 0.453 before the minimum wage intervention, the compulsory secondary education reduced the Gini by almost four per cent. The least effective method to reduce inequality is the cash handout known as the Bantuan Rakyat 1Malaysia (BRIM) which only reduced Gini by 2.3

per cent to 0.443 for RM1,200 cash offer per head, and by 0.96 per cent to 0.449 with the cash offer of RM500.

According to The Malaysia Human Development Report (MHDR) 2013, the case study of inclusive growth experienced in Malaysia shows that it is state sponsorship through human resource development, institutional and infrastructural amenities that had brought tremendous social change and transformation of the nation. The inaugural report commissioned by the United Nations Development Programme (UNDP) instead maintains that poverty is best measured against what households earn in general, rather than by a fixed minimum level. Available evidence of the national distribution of income indicates a steady decline in inequality; the Gini coefficient dropped by about 16 per cent from 0.51 in 1970 to 0.43 in 2012. Despite the improvement in income disparity, the income gap between the top 20 per cent and bottom 40 per cent of households when measured in absolute terms, has actually increased during the period from 1970 to 2012. For instance, the income gap between the rich and the poor jumped 13 times from RM659 in 1970 to RM10,312 in 2012. The absolute gap between the urban and rural also widened, from RM228 in 1970 to RM2,262 in 2012, an increase by about 11 times.

In terms of ethnicity, the highest gap in absolute terms was registered among Bumiputeras, where the income gap jumped by nearly 20 times compared to 11 times for the Chinese and the Indians during the period of 1970 to 2009. Importantly, the widening gap appears to have come from increased income disparities within the groups, be it on the basis of ethnic, strata or gender. Another interesting finding is that rural Sarawak has a lower educational attainment capability than rural Sabah. This signifies that the official income poverty rate of Sarawak, which is substantially lower than that of Sabah, may not be a true reflection of all the important aspects of its socioeconomic development. The human capability mapping by the Ministry of Human Development and Resource (MHDR, 2013) confirms this reality, as Sarawak continues with its largest urban-rural gap for Malaysia. The chart below clearly shows that as of 2010 the total enrolment in tertiary education, as a percentage of the 20-24 years old population was approximately 34 per cent with East Malaysia starkly lagging behind the Peninsular. Undoubtedly, the bottom 40 per cent of households which are of grave concern are concentrated within the region of Sabah and Sarawak.

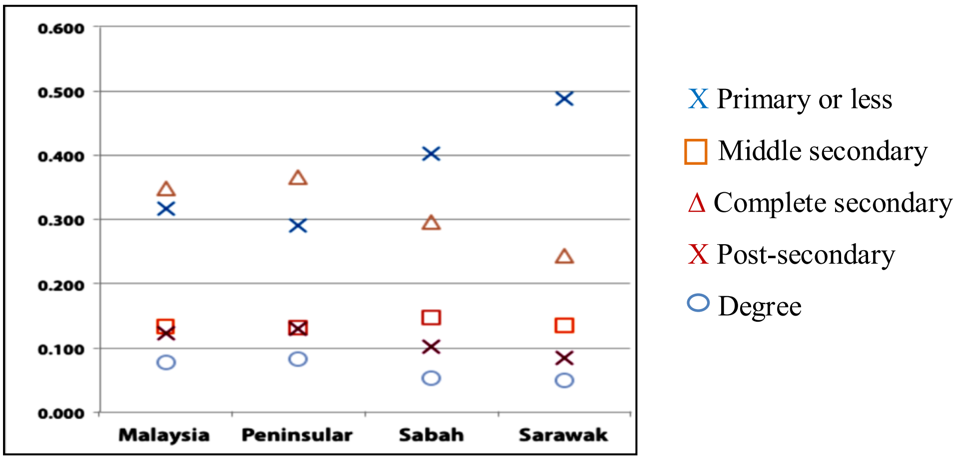

Figure 2: Educational Attainment of Adult Population

The growth in higher formal qualifications corresponds with an increasing proportion of workers in occupations demanding more skills, knowledge and expertise. But the degree of inclusiveness in attaining human capabilities is most appropriately evaluated not at the household level, but at the personal level. Sizeable disparities hold between Peninsular Malaysia and East Malaysia, with Sarawak registering the lowest educational profile. Urban and rural disaggregation accentuates the disparities, with rural Sarawak, with 64 per cent of adults having only primary schooling or less, lagging far behind the rest.

RECOMMENDATIONS

The decline in international inequality is due largely to the more rapid growth of a relatively small number of large countries. Therefore, international cooperation to create an international environment that enables poor countries to grow faster is important for reducing aggregate global inequality. Experiences show that while the national context is important for policy effectiveness in combating inequality, elements such as universalism in the provision of social services, reducing social exclusion and intergenerational disadvantage, renewed emphasis on universal social protection, investing in education and strengthening labour-market institutions, prudent fiscal and monetary policies, creating more and better-paying jobs and reducing asset inequalities are key.

Given these guidelines and the unique character of Malaysia which practices dual laws, Civil and Syariah, it may be worth experimenting on readily available Islamic economic mechanisms and institutions in place. Zakat, a pillar in Islam plays an important role in ensuring that income and wealth circulates from the well-offs to less so. When implemented and if necessary enforced accordingly, the institution of zakat is expected to at the least reduce extreme inequalities originating from inherited poverty which then transforms into a vicious cycle of lost opportunities among the vulnerable. The zakat fund ought to be used to create lasting influences on lifelong chances for the zakat recipients through expansion of educational and business opportunities. They are referred to asnafs by the Quran; *"The alms are only for the poor and the needy, and those who collect them, and those whose hearts are to be reconciled, and to free the captives and the debtors, and for the cause of Allah, and (for) the wayfarers; a duty imposed by Allah. Allah is knower, Wise."(9:60)*

The successful functioning of Lembaga Zakat Selangor in uplifting the lives of thousands of previous zakat recipients serves as a testimony that setting Zakat goals beyond helping the poor and needy to fend them has a number of by-products. The obvious success being the significant reduction in gross inequalities. Then there are the lagging external effects of improved healthcare towards prolonged life-expectancy and higher productivity and later on reducing inequalities further. At the other end, lies the relevance of property rights, equal opportunities to fulfilling basic needs and equitable returns based on efforts as the cornerstones of the economic justice in Islam. The disparities between urban and rural areas, known as spatial inequalities, in the case of Sabah and Sarawak might yield positive results with the introduction of land reforms as recommended by the Syariah. In the absence of an active market for land added by the heavy acquisition through inheritance are the common factors to land idleness and concentration.

Islam is a way of life, providing us with an array of choices to manage all aspects of our lives. It prescribes all the necessary aids for one to cope with life challenges. Therefore, it becomes the collective responsibility of Muslim scholars specializing in the areas of welfare economics to explore, create awareness and promote the Islamic Economic System as a viable alternative to understand and manage the various types of economic inequalities prevalent in Malaysia.

CONCLUSION

Despite the broad expectation that inequalities should decline systematically as societies develop, inequality trends have not followed a universal pattern. In fact, the empirical evidence suggests that much depends on country-specific conditions and national policymaking. The vulnerable are more likely to benefit where pro-poor national policies are in place, growth is equitable, and labour markets inclusive. Countries that have used redistributive fiscal policy measures, developed universal social protection programmes, or even wide-ranging social assistance, with emphasis on education and health spending, and those that have increased labour-market opportunities for those at the bottom, have weathered better than others.

At the risk of oversimplifying, some degree of monetary inequality is needed to create incentives for people to study and accumulate human capital, to work instead of taking leisure, to save for the future, and to invest in risky businesses. Returns to education are a clear example of a differentiation in labour earnings that spur the accumulation of human capital and economic growth, but at the same time results in inequality in outcomes. However, incentives may fail to change behaviour when economic mobility is lacking. In countries where inequality had declined, two key factors contributed to such declines: the expansion of education, and public transfers to the poor.

Based on the discussions with regards to Malaysia, one can conclude that despite the numerous on-going government efforts to increase economic equality by expanding inclusiveness through the promotion of equal opportunity, certainly more needs to be done for equity to play an active and leading role in national development plans. The adoption of the readily available Islamic Economics mechanism in Malaysia can facilitate the fine-tuning of the existing distributive justice initiatives aimed primarily at reducing economic inequality between ethnics, region or other demographic traits. Fostering greater inclusion in the quest to reduce inequality between the urban and rural demands attention to a focussed development of the latter in East Malaysia.

The conventional ways of dealing with economic inequalities which, if left unattended may cause social unrest, has proven to be ineffective in responding to the rising inequality among fellow Malaysians. Some have migrated to greener pastures, resulting in a considerable brain drain, whereas the remaining many are beginning to demand solutions to reverse the predicament. In my humble opinion, there is much at stake if we wish to capitalize from our sizable labour force. A majority of which that appear to fall into identified as disadvantaged social groups. They include youth, (whom having lost their protection as children), are seen as a generation at risk, older citizens (in the form of income insecurity and insufficient access to quality health care), persons with disabilities, the indigenous (face inequalities in land rights and environmental challenges) and migrants.

Therefore, it is timely to introduce and establish other economic institutions readily available in the Islamic economic system, besides existing institutions of *zakah* and *waqaf* which (to the author's mind) can be improved in terms of their respective functions and achievements. The formalizing al-*Hisbah* (the independent market regulator) is a good start to ensure that government policies aimed at reducing extreme inequalities in income and wealth within the society are implemented accordingly. The success of Islamic banking and finance and the rapidly growing interest in businesses related to halal hub are in fact evidences of non-Muslims Malaysians to accept and support efforts geared towards narrowing the socioeconomic inequalities at national level.

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