DEVELOPMENT OF POLICIES AND INCENTIVES FOR FOREIGN INVESTMENT IN MALAYSIA

JAPAN INTERNATIONAL COOPERATION AGENCY (JICA)
MALAYSIA OFFICE

1998

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PREFACE

Malaysia has achieved rapid economic development since independence in 1957 The country has transformed from being a primary commodity producer to a rapidly industrialising country Over the last decade, until the Asian economic crisis of 1997/1998, the Malaysian economy achieved annual growth of more than 8% The country's GDP has more than doubled from RM61 billion in 1987 to RM141 billion in 1997. Per capita, income has expanded from RM4,600 to RM12,100. Malaysia is today among the top 20 trading nations in the world. The International Institute of Management Development in 1998 ranked Malaysia fourth among non-OECD countries in terms of overall competitiveness.

The contribution of foreign investment to the remarkable economic development in Malaysia is considered very significant.

As a donor agency providing technical assistance under the Government of Japan, JICA Malaysia Office would like to share the Malaysian experience with other developing countries and donor communities by compiling the policies and incentives adopted by the Malaysian Government for foreign investment.

JICA Malaysia Office has commissioned this compilation work to Deloitte Touche Tohmatsu Malaysia/ Kassim Chan Management Consultants Sdn Bhd

I would also like to acknowledge co-operation of the Malaysian Government including the Malaysian Industrial Development Authority (MIDA) for assisting in preparing this report.

Ryuzo Nishimaki
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Preface (cont'd)

This report was prepared jointly by JICA Malaysia Office and Deloitte Touche Tohmatsu Malaysia/ Kassim Chan Management Consultants Sdn Bhd (DTT/ KCMC). The findings, interpretation and view expressed in this report are entirely those of the authors and should not be attributed to JICA Malaysia Office or Deloitte Touche Tohmatsu Malaysia/ Kassim Chan Management Consultants Sdn Bhd.

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DEVELOPMENT OF POLICIES AND INCENTIVES FOR FOREIGN INVESTMENT IN MALAYSIA

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1. EXECUTIVE SUMMARY

Malaysia has over a span of about 40 years transformed itself from being a primary products producer in the 1950s to become a rapidly developing country, on the path to achieving its objective of being a fully developed country by the year 2020

The main contributor to this remarkable transformation of the country has been the industrial sector The manufacturing sector, which was virtually non-existent 40 years ago, is today the 2nd largest component of the country's GDP, contributing to approximately 35% of GDP and about 80% of the country's export earnings.

The development of the Malaysian industrial sector in the past has been fuelled largely by foreign investments in the sector. Foreign Direct Investment (FDI) accounted for RM55.1 billion or 47% of the total investment in Malaysia between 1993 and 1997

Two factors which greatly contributed to investments, especially foreign investments in the industrial sector has been the government's introduction of timely **industrial development policies** at the appropriate times and the award of **incentives** (both fiscal and non-fiscal incentives)

Malaysia's Industrial Development Policy

In the early years, there was no distinct industrial development policy for the country The industrial development initiatives followed by the government then was part of 5-year development plans, called the **Malaysia Plans**, which was started from 1966 To date seven 5-year Malaysia Plans have been launched. Presently the seventh plan covering the period 1995 – 2000 is in the implementation stage.

Malaysia launched its first comprehensive industrial development policy called the **Industrial Master Plan** in 1985. The 1st Industrial Master Plan (IMP1) which covered the period 1986 – 1995 was aimed at laying the foundation for the co-ordinated and comprehensive development of the country's industrial sector. The plan identified 12 industrial sectors to be developed with each sector set a target to achieve by 1995. The plan is considered to have been successfully implemented with almost all sectors exceeding the targets set

The IMP1 was followed by the 2nd Industrial Master Plan (IMP2), covering the period 1996 till 2005. The IMP2 builds on the success and foundation laid by the IMP1 The IMP2 also introduces the **"manufacturing plus-plus"** and **"cluster based"** industrial development The manufacturing plus-plus Concept aims at backward (R&D, design, prototyping, etc.) and forward (distributing, marketing, logistics, etc) integration to Malaysia's already established manufacturing (largely assembly oriented) operations. The cluster based development involves the concurrent development of inter linked activities of manufacturers, suppliers, related service providers, etc to create broad based, resilient and internationally competitive industrial clusters. The IMP2 has identified 22 industrial clusters to be developed

The Industrial Master Plans (IMPs) guide the development of the industrial sector The IMPs are consistent and part of Malaysia's larger socio-economic plans, like the:-

- **Outline Perspective Plans (OPPs)** [The 1st OPP covered the period 1971-1990, while the 2nd OPP covers the period 1991-2000] The OPPs form the socio-economic development framework of Malaysia.

Executive Summary

- The **New Economic Plan (NEP)**, covers the period 1971 till 1990 and its replacement, the **National Development Plan** (NDP) covers the period from 1990 onwards The NEP and the NDP have 2 primarily focus i e eradicating poverty and restructuring Malaysian economic society based on the realities of Malaysia's multiracial composition.

All the above-mentioned plans are part of the government's **Vision 2020** launched in 1991 to make Malaysia a fully developed country by the year 2020

Incentives for Investment

The government's use of incentives was the other main contributor to the rapid industrial development of the country.

Fiscal Incentives (Tax Related)

The main fiscal incentives provided by the government for industry are **Pioneer Status** (tax holiday for a predetermined period), **Investment Tax Allowance** (a portion of the capital expenditure given as a tax credit) and **Reinvestment Allowances** (a tax credit on the capital expenditure incurred, to encourage reinvestment) The government has also in the past provided other tax related incentives to encourage exports, dispersal of industry from the main industrial areas, employment, etc

Non Fiscal Incentives

The Malaysian government views non-fiscal incentives as very important to complement fiscal incentives to attract investors in the industrial sector. Accordingly, the government undertook the development of numerous world class infrastructural facilities such as industrial zones, telecommunication facilities, power plants, road networks, ports, airports, etc. The government continues to invest substantially to continuously develop new industrial infrastructure and upgrade existing facilities

Effectiveness of Incentives

The government over the years constantly reviews and periodically changes the incentives awarded in line with the changing focus of the country's industrial development. The government's thinking from the mid-1990s has been to provide less fiscal incentives. This is because the government now views that **tax incentives are not the main reasons why investors come to Malaysia** The government is of the view that other non-fiscal incentives, like political stability, good industrial infrastructure, investor friendly policies, an educated and trainable workforce, etc , are regarded higher than tax incentives by investors.

Our own review substantiates the government's assumption on the relative importance of fiscal incentives The use of incentives in the past has been effective and instrumental in the industrial development of the country.

Executive Summary

Industrial Focus Over the Years

The government's industrial development focus since the government began developing the industrial sector in the 1960's is summarised below

1960's

In the 50s, Malaysia was primarily an agriculture and resource-based country, being the world's largest producer of natural rubber and tin These commodities were exported in their raw form without much production done in Malaysia At that time, Malaysia had no industries of substance Most of the country's requirement were imported.

Since the country's independence from Great Britain in 1957, the country decided to reduce it dependence on its primary commodities and on imports for its essential requirements

Accordingly, the government's early industrial policy focus was aimed at encouraging the setting up of industries to process the raw materials produced by Malaysia, instead of exporting them in their raw form The government also encouraged the development of **import substitution** industries to reduce the dependence on imports for basic needs and other consumer goods

1970s

In the 1970s the government's focus shifted from import substitution to **export orientation** This shift was made because Malaysia's population and domestic market was too small to support an industrial base Furthermore, the availability of raw materials, cheap labour and abundant land made the country ideal for foreign multinationals to set up production facilities in Malaysia, for export to the world market This phase of Malaysia's industrial development has been quite successful, with Malaysia today hosting world renowned multinationals like Matsushita, Sony, Motorola, Intel, Siemens, Phillips, etc Malaysia is also among the largest exporter of televisions, room air-conditioners, video players, ICs, rubber gloves, catheters, etc

1980s

The 1980s saw the transformation of Malaysia from an agricultural country to an industrialising country, when for the first time manufacturing overtook agriculture as the main sector of the economy The government also decided to establish **heavy industries** like steel mills, automotive plants, petrochemical plants, etc The government viewed the establishment of these industries with extensive linkages possibility as an important prerequisite for the next stage of development of the industrial sector It was in 1985 that the government launched the 1st IMP

1990s

In the early part of the 90s, the government's industrial development focus was to develop supporting industries like tool making, mould and die, plastic injection moulding, metal stamping industry, component manufacturing, etc The focus was to broaden the industrial base of the country from being merely an assembler of imported components to becoming a manufacturer and exporter of sophisticated and precision components, parts and finished products

Executive Summary

Late 1990s

From the middle 1990s onwards, to deal with the emergence of labour and skill shortages and competition from other Asian countries, the focus of the Malaysian industrial development policy moved into high technology, high value-added, capital and skill intensive manufacturing to deal with increasing global competitiveness.

Currently, to face the challenges of the next millenium, the government's industrial development focus for the future is on **multimedia** development to produce world class corporations As a first step the government has launched the Multimedia Super Corridor, a 15km x 50km (9 by 30 miles) greenfield development with state of the art technology to attract world class high technology companies to operate there. It is hoped that the operations of these companies will result in a "spillover" effect with Malaysians becoming ready for competition in the information-based society of the future

Institutional Framework

The main legislation relating to industrial development is the **Industrial Coordination Act 1975 (ICA)** and the **Promotion of Investment Act, 1986 (PIA)** Together these Acts serve to regulate and promote the manufacturing sector in the country

The main organisation responsible for the industrial development of the country is the **Malaysian Industrial Development Authority (MIDA)**, a special agency under the **Ministry of International Trade and Industry (MITI)**. MIDA is responsible for promoting Malaysia as a site for industrial investments and for coordinating the industrial development of the country MIDA is essentially a "one-stop" agency where investors in the Manufacturing Sector, especially foreign investors, can go for assistance for implementing manufacturing projects in Malaysia

MIDA is regarded very highly by industry sources and investors MIDA has been very effective in spearheading the industrial development of the country

2. ABBREVIATIONS

FDI	Foreign Direct Investment
MIDA	Malaysian Industrial Development Authority
USD	United States Dollar
USA	United States of America
GDP	Gross Domestic Product
MITI	Ministry of International Trade and Industry
NDP	National Development Policy
NEP	National Economic Policy
OPP	Outline Perspective Plan
BCIC	Bumiputra Commercial and Industrial Community
FIC	Foreign Investment Committee
MP	Malaysia Plan
SMI	Small and Medium Industry
TFP	Total Factor Productivity
IMP	Industrial Master Plan
R&D	Research and Development
VAPE	Value-Added Per Employee
N/A	Not Applicable
ITA	Investment Tax Allowance
FIDA	Federal Industrial Development Authority
IIA	Investment Incentives Act 1968
FTZ	Free Trade Zone
EPZ	Export Processing Zone
PCA	Principal Customs Area
LMW	Licensed Manufacturing Warehouse
ICA	Industrial Co-ordination Act 1975
PIA	Promotions of Investment Act 1986
HICOM	Heavy Industry Corporation of Malaysia
PROTON	Perusahaan Otomobil Nasional Berhad
COI	Centre of Investment
PS	Pioneer Status
RA	Reinvestment Allowance
IPP	Independent Power Producers
MSC	Multimedia Super Corridor
KLIA	Kuala Lumpur International Airport

Abbreviations

SME	Small and Medium Enterprises
CIPE	Capital Investment Per Employee
ISIS	Institute of Strategy and International Studies
FMM	Federation of Malaysian Manufacturers
MOU	Memorandum of Understanding
COMFADI	Confederation of Small and Medium Industries of Italy
APRODI	The Association of Pour La Promotion Et Le Development Industral
MIGA	The Malaysian, Italian, Gulf and African Chamber
EDCB	The Economic Development Corporation of the state of Bremen
SMIDC	The Small and Medium Industry Promotion Corporation
CIB	The Cambodian Investment Board
BFCE	Banque Francaise du Commerce Exteriur
DOE	Department of Environment
DOSH	Department of Occupational Safety and Health
MOF	Ministry of Finance
ACI	Action Committee of Industries
IRB	Inland Revenue Board
MIER	Malaysian Institute of Economic Research
f.o b	Freight on Board
c i f.	Carriage, Insurance and Freight

3. INTRODUCTION

3.1 OBJECTIVE AND SCOPE

The two main objectives of this report are

- To provide an understanding of the Malaysian experience in the development of policies and incentives for foreign investment.
- To share this valuable experience with other developing countries and donor communities

This report examines and tracks the Malaysian experience and is not an evaluation of the results of policies

This report focuses on manufacturing sector and incentives for Foreign Direct Investments (FDI)

The scope of the report is to gather information and data relating to:

1. The development of industrial policies and the use of incentives as a tool for the economic development of Malaysia.
2. Lessons from the experiences of the Malaysian Industrial Development Authority (MIDA)
   - To obtain feedback from MIDA on the agency's experience on the use of incentives to promote industrial development, focusing on the following
     - how MIDA attracts foreign investment
     - role as a one stop agency
     - role in changing incentives
   - To obtain feedback on MIDA's experience that could be disseminated among other less developed countries
3. To gather views and reactions of foreign companies which have set up their business in Malaysia, on how much incentives have influenced their decision to invest in Malaysia instead of other South-east Asian countries, covering also other non-fiscal incentives which might have influenced the decision.

This report relates mainly to tax-incentives and non-tax incentives related to the foreign ownership and approval procedures (e g. provision of one-stop agency services, etc), although there could be many other incentives.

"Foreign investment" in this report refers to "Foreign Direct Investment"

3.2 LIMITATIONS

Whilst every effort was made to verify the information obtained from our desk research and interviews, we are unable to provide any warranty as to the accuracy of the information so obtained.

Accordingly, readers of this report are reminded to obtain advice from the relevant competent authority before making any business decision and not to make decisions based solely on information contained in this report.

3.3 BACKGROUND INFORMATION ON MALAYSIA

Malaysia is centrally located in Southeast Asia, one of the fastest growing trade and economic region over the last decade The country comprises 13 states, 11 making up Peninsular Malaysia and 2 (Sabah and Sarawak) situated in the northern part of the island of Borneo, which is separated from the mainland by the South China Sea The country also has 2 federal territories: the city of Kuala Lumpur on Peninsular Malaysia and Labuan, a small island lying off the coast of Borneo Peninsular Malaysia shares a common frontier with Thailand to the north To the west, it faces the Indonesian Island of Sumatra across the narrow Straits of Malacca, and to the south, it is linked with Singapore by a causeway The states of Sarawak and Sabah share a 1,448 kilometre (900 mile) frontier with Indonesian Borneo

Malaysia is a multiracial country comprising mainly of Malays, Chinese, and Indians. More than 80% of the country's total population live in Peninsular Malaysia

Islam is the official religion while other religions are also freely practised.

Kuala Lumpur, the federal capital is the largest city in Malaysia It is centrally located in Peninsular Malaysia The other principal cities and towns in Peninsular Malaysia are Penang, a port and tourist centre, Ipoh, a former tin mining centre, Johor Bahru, a port and gateway to Singapore, Malacca, a historical centre, Kota Kinabalu, the capital of Sabah, and Kuching, the capital of Sarawak

The national language in Malaysia is Bahasa Malaysia (Malay), although English is widely used everywhere especially in business circles

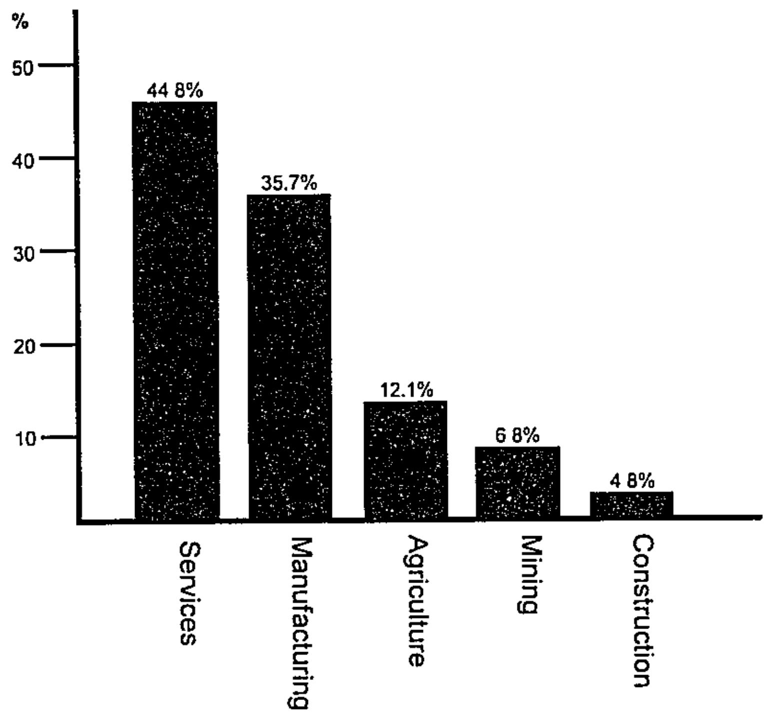
MALAYSIA IN 1997

Land Area	329,758 square kilometres
Population	21.7 million
GDP	RM141 billion
GDP growth	7 8%
Per capita income	RM12,100
Inflation rate	2.7%
Labour force	8 6 million
Unemployment	2 7%
Total exports	RM218 7 billion
Total imports	RM207.6 billion
Major exports	Manufactured goods, palm oil, crude petroleum and LNG, sawlogs and sawntimber, rubber
Major imports	Machinery, transport equipment, manufactured goods, chemicals, food
Major trading partners	USA, Japan, Singapore, Taiwan, Korea, Hong Kong, Germany
Exchange Rate (RM to USD 1)	2.5209 (Average Rate for 1996); 2 8132 (Average Rate for 1997), 3 8000 (Fixed Rate from 1 Sept 1998).

Source: ***Bank Negara Malaysia***

The country has undergone a structural transformation over the last 40 years since achieving independence from Britain in 1957. From a country principally dependent on primary commodities in the 1960's, with practically a non-existing manufacturing sector, today the manufacturing sector accounts for approximately 35% of the country's Gross Domestic Product (GDP) and about 80% of the country's exports.

Table 1: Malaysia: GDP By Economic Sector



Source: Bank Negara Malaysia

The country's rapid industrialisation has been attributed largely to the Foreign Direct Investment (FDI) into Malaysia.

The FDI in the manufacturing sector totalled RM55 1 billion or 47% of total investment in Malaysia between 1993 and 1997.

Please refer to Exhibits 1 and 9-15 for some economic data on industrial development in Malaysia.

4. INDUSTRIAL DEVELOPMENT POLICIES

4.1 INTRODUCTION

The Malaysian government generally does not differentiate between foreign and domestic investments Both types of investments are promoted and welcomed

Accordingly, there are no specific government policies aimed at foreign investments only

Similarly, in the award of incentives, both foreign and domestic investments are treated equally

The government's policy towards foreign investments is part of the government's overall "Industrial Development" policy Foreign investments are seen as one of the major means of achieving the objectives of the industrial policies of the government

Accordingly, foreign investments form an important and integral part of the government's industrial development policy In the past, foreign investments have practically been the most important contributing factor to Malaysia's phenomenal economic performance and development, especially since the 1970s

Foreign investments provided the initial capital and technology, which transformed Malaysia from a primarily agricultural products producer with almost no industrial technology during the 60s to a fast industrialising country

Foreign investment and technology are expected to continue to be a major factor in Malaysia achieving industrialised nation status by 2020 as envisaged by the government.

Accordingly, the Malaysian government actively promotes foreign investments into the country.

The Ministry of International Trade and Industry (MITI) is responsible for foreign investments The Malaysian Industrial Development Authority (MIDA) is the primary agency under MITI with responsibility for promotions of both foreign and domestic investments in Malaysia

The development of policies relating to foreign investments which are part of the Malaysian government's industrial development strategy is outlined below

4.2 POLICY DEVELOPMENT PHILOSOPHY

To understand the Malaysian government's policies towards foreign investments, it is important to understand the Malaysian government's development philosophy which is based on a firm commitment to **free business environment with active government support and direction.**

Essentially, the **government provides broad policy directions** for the whole economy. The government then **provides institutional and infrastructural support** so that the **private sector can operate freely to achieve its objectives**

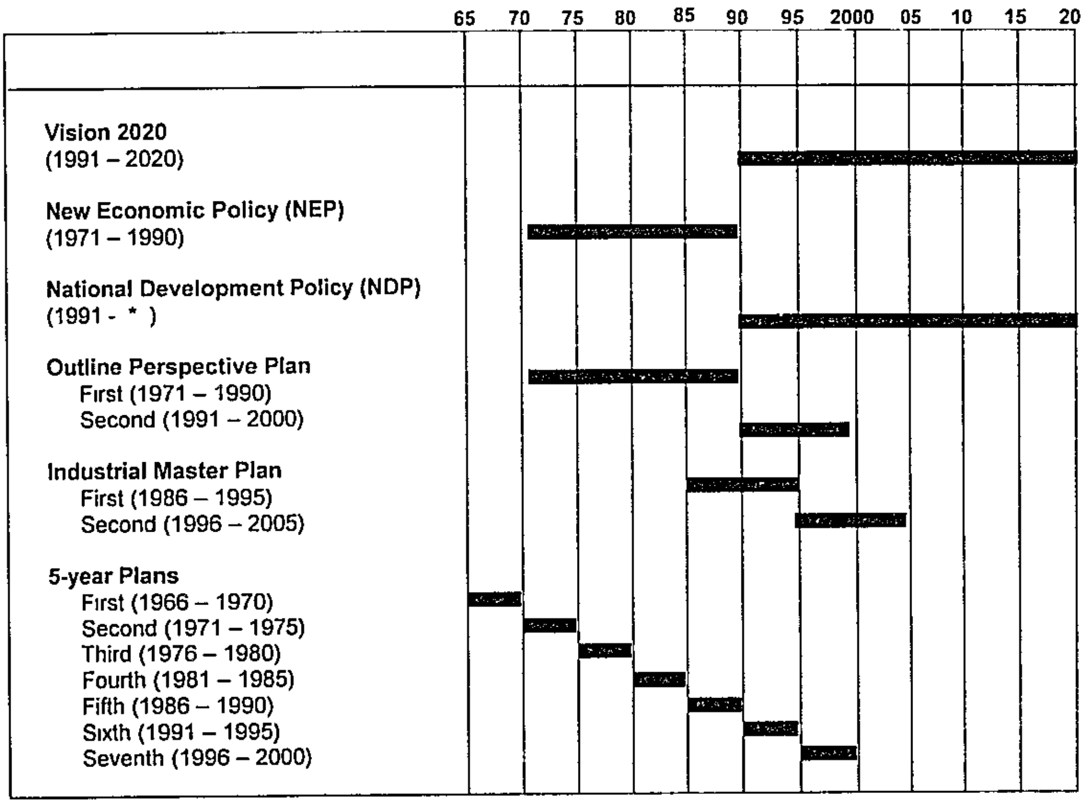
Based on the above-described Development Philosophy, various development policies have evolved in Malaysia

These policies form the framework for foreign investments into Malaysia.

4.3 POLICY FRAMEWORK

The time span and overlapping relationship between some of these policies and plans are shown in Chart 2

Table 2: Malaysian Development Policies and Plans



* The NDP was launched as an ongoing policy with no fixed time frame for completion It is an open-ended policy.

4.4 DEVELOPMENT POLICIES

The main thrust of some of the development plans and policies which are relevant to this report are outlined below.

4.4.1 VISION 2020 STATEMENT

The 'Vision 2020' statement launched in 1991 is the development vision of the country for 30 years until the year 2020

It outlines the overall vision of the government and what the government hopes to achieve for Malaysia The Vision 2020 statement has set the broad framework for the development of Malaysia until the year 2020

The overall objective of the government's 'Vision 2020' is to achieve.-

- **Total Development**

  To become a nation which is economically, politically, socially, spiritually, psychologically and culturally developed

- **Human Development**

  To improve the quality of life and standard of living to reach a level enjoyed by other developed countries

- **Economic Development**

  To achieve the following·

  - Average annual output growth at 7% with low inflation
  - An eight-fold increase in GDP
  - A four-fold increase of per capita income

Vision 2020 has identified 9 strategic challenges for Malaysia

1 The establishment of a united Malaysian nation made up of one Malaysian race

2 The creation of a psychologically liberated, secured and developed Malaysian society

3 The fostering and development of a matured democratic society.

4 The establishment of a moral and ethical society

5 The establishment of a matured, liberal and tolerant society

6 The establishment of a scientific and progressive society

7. The establishment of a caring society

8. The development of an economically just society, with fair and equitable distribution of wealth

9 The establishment of a prosperous society with a fully competitive, dynamic, robust and resilient society

The Vision 2020 statement is used as a rallying call to inspire and motivate the nation to achieve developed nation status

4.4.2 LONG TERM DEVELOPMENT PLANS

The government's long term development plans are contained in the Outline Perspective Plans (OPPs)

The OPPs outline the government's socio-economic development framework for Malaysia

There have been 2 OPPs launched to date

a) First Outline Perspective Plan (OPP 1)

The OPP 1 covers the period of 1971 till 1990 and embodies the **New Economic Policy (NEP)** introduced in 1970 The OPP1 and the NEP were introduced just after the race riots in Malaysia in 1969 and had the overriding objective of restructuring the Malaysian economy to achieve national unity

The OPP 1 adopted a high growth strategy with Gross Domestic Product (GDP) targeted to grow at 8% per annum Such a high growth was required to generate sufficient business and employment opportunities to allow for restructuring of the Malaysian economy without causing too much disruption to the existing economic structure

The projected high growth was to be achieved from the **utilisation of the country's large natural resources** by expanding agricultural production as well as raw materials based industrial development

The major stimulus for the growth was to come from the **expansion of public and private investments** (both domestic and foreign)

The other major stimulus to expand the economy was a **strong export growth** Exports earnings were targeted to grow at 7 1% per annum Export of manufactured products, resource based manufactured products and other industries with potential were targeted for development

Exports of manufactured goods were targeted to increase from 11% in 1970 to 38 1% of total exports in 1990.

The OPP 1 also sought to achieve greater integration among the various states and regions to reduce regional disparity

The performance of the OPP 1 is given below

OPPI Macro-Economic Targets & Achievements

Average Growth Rate, 1971-90	*Target OPP 1 (% p.a.)*	*Achieved OPP 1 (% p.a.)*
GDP	8.0	6 7
Private Investment	8 5	9 4
Public Investment	10 1	10 0
Exports	7 1	9 2

- *New Economic Policy (NEP)*

  The NEP which covered the period 1971-1990 was a direct result of the race riots in 1969 The NEP had 2 main objectives i e **eradication of poverty** and **restructuring society**

  (i) Eradication of Poverty

  In 1970, poverty in Peninsular Malaysia was 49 3% of all households The target was to reduce the poverty rate to 16 7% by 1990

  Bumiputras (Malaysians of indigenous origin) formed the bulk of the poverty group accounting for 74% of all poor households in Peninsular Malaysia. The incidence of poverty among the Bumiputra was also the highest at 65% compared with 26% for the Chinese and 39% for the Indians

  Accordingly, a major target of the NEP was the eradication of poverty, irrespective of race

  (ii) Restructuring of Society

  The second major objective of the NEP was the restructuring of society to eliminate the identification of race with economic functions and to allow for balanced economic participation among the various races

  Before the NEP, the Bumiputras were mainly concentrated in the agricultural and other low-income sectors, while the non-bumiputras were more represented in the business sectors and professional services, where productivity and income were higher

  Accordingly, the NEP sought to restructure the employment pattern, ownership of share capital and representation in the corporate and professional services sector by creation of a Bumiputra Commercial and Industrial Community (BCIC).

The target was for Bumiputras to own and manage at least 30% of the total commercial and industrial activities of the economy by 1990 from 2.3% in 1970.

However, this target was not achieved as the Bumiputra participation in the corporate sector in 1990,at the end of the NEP, was estimated at approximately 18% only

In order to achieve restructuring of business with Bumiputra participation, the government also set up the Foreign Investment Committee (FIC) in 1974 and introduced guidelines whereby foreign equity exceeding 30% in the companies in Malaysia needed to be approved by the FIC

Further the guidelines stipulated that Malaysian companies should have at least 30% Bumiputra equity

The OPP 1 and the NEP covered the Second Malaysia Plan (1971-1975), the Third Malaysia Plan (1976-1980), the Fourth Malaysia Plan (1981-1985) and the Fifth Malaysia Plan (1986-1990)

b) Second Outline Perspective Plan (OPP 2)

The OPP 2 took over the OPP 1 and covers the period 1991-2000 The OPP 2 embodies the "**National Development Policy**" **(NDP)** which replaced the NEP. The OPP 2 also covers the first 10 years of 'Vision 2020' and sets the groundwork for achievement of 'Vision 2020' and the development framework for the 1990s

The objective of the OPP 2 and the NDP is to attain **balanced development** of the country and establish a more **united and just society** in Malaysia

The detailed objectives of the OPP 2 and the NDP is provided below.

- Striking an **optimum balance** between the goals of economic growth and equity;
- Ensuring a **balanced development** of the major sectors of the economy so as to increase their mutual complimentary to optimise growth,
- Reducing and ultimately eliminating the social and economic inequalities and imbalances in the country to promote a **fair and more equitable sharing of the benefits** of economic growth by all Malaysians;
- Promoting and strengthening **national integration** by reducing the wide disparities in economic development **between states** and between the **urban and rural areas** in the country;
- Developing a **progressive society** in which all citizens enjoy greater material welfare, while simultaneously imbued with positive **social and spiritual values**, and an increased sense of **national pride and consciousness**;

- Promoting **human resource development** including creating a productive and disciplined labour force and developing the necessary skills to meet the challenges in industrial development through a culture of merit and excellence without jeopardising the restructuring objectives,

- Making **science and technology** an integral component of socio-economic planning and development, which entails building competence in strategic and knowledge-based technologies, and promoting a science and technology culture, in the process of building a modern industrial economy, and

- Ensuring that in pursuit of economic development, adequate attention will be given to the protection of the **environment** and ecology so as to maintain the long-term sustainability of the country's development

The two OPPs, the NEP and the NDP were mainly focused on socio-economic objectives of **eradication of poverty**, restructuring society to achieve **balanced distribution of the national wealth among the races** and attaining balanced development

4.4.3 5-YEAR DEVELOPMENT PLANS (MALAYSIA PLANS)

The 5-year development plans or 'Malaysia Plans' are medium-term plans. These plans translate the long range development plans and policies of the government contained in the Vision 2020, OPPs, etc. into **5 year operational plans** for the country

To date, 7 Malaysia plans have been introduced as follows -

1st Malaysia Plan 1966-1970
2nd Malaysia Plan 1971-1975
3rd Malaysia Plan 1976-1980
4th Malaysia Plan 1981-1985
5th Malaysia Plan 1986-1989
6th Malaysia Plan 1990-1995
7th Malaysia Plan 1996-2000

The 6th Malaysia Plan and 7th Malaysia Plan are relevant to this study as they cover the period 1990 till 2000. This period encompasses the launch of the Vision 2020, OPP 2 and 2nd Industrial Master Plan (IMP 2). These are 3 important development policies/plans guiding Malaysia's current and future industrialisation

6th Malaysia Plan (6th MP)

The 6th MP covered the period 1991-1995 and is the first phase of the implementation of the OPP 2 and NDP.

The main thrusts of the 6th MP were:

- Sustain the growth momentum achieved by Malaysia and manage growth to achieve a more **balanced development**

- Increase internal strength and resilience of the economy by improving **productivity** of each factor of production and greater **competitiveness**
- Maintain **price** and **exchange rate stability**
- Strengthening the **financial infrastructure**
- Improving the quality of the **human resources**

7th Malaysia Plan (7th MP)

The 7th MP (1996-2000) also covers OPP 2, NDP and the first half of the IMP 2 and aims to reorientate Industrial Policy towards large scale production for the export market, promote manufacturing of **capital and intermediate goods** and promote greater **inter and intra industry linkages**

The development thrusts of the 7th MP are

- Maintain high growth and stability of the economy
- Effect further structural transformation of the economy
- Maintain balanced development in the economy
- Develop a strong human resource base
- Emphasize social development amidst industrial development
- Strive for sustainable development

The Industrial Development Strategies under the 7th MP are aimed at

- Reorienting industrial policies to focus on **large scale production** for the world market
- Aggressively promote the manufacturing of **capital and intermediate goods**
- Promote the development of new growth industries e g. **wafer fabrication**, aerospace, **petrochemicals** and strategic industries like integrated steel mill etc
- More investments in downstream activities of resource based industries
- Emphasis on **Small and Medium Industries (SMIs)** to become world class suppliers

New Dimensions of the 7th Malaysia Plan

In response to new challenges to Malaysia's industrialisation programme, the 7th MP introduces new dimensions to the Malaysian industrialisation programme

- ♦ Shift from input-driven to productivity-driven growth by enhancing contribution of **Total Factor Productivity (TFP)**
- ♦ Enhance competitiveness by strengthening economic foundations, expanding global marketing and reinforcing competitive industry clusters
- ♦ Accelerate human resource development

- Strengthen Science & Technology, Research & Development and promote Information Technology

- Generate new growth sectors

  - Develop outward-oriented services sector
  - Industrialisation strategy to target for global market, large-scale operations and capital, skill and technology-intensive industries
  - Revamp of the agricultural sector

The 7th MP has attempted to address some new domestic and international challenges which emerged in the early 1990s To date 3 years of the 7th MP has lapsed The government is currently in the process of producing the **mid-term review of the 7 MP**

It appears that with the current financial and economic crisis inflicting Malaysia and the region, some of the 7th MP targets cannot be achieved Accordingly, the mid-term review of the 7th MP is expected to **revise downward** the target for the 7th MP and introduce new strategies to face the current situation

4.4.4 INDUSTRIAL MASTER PLANS (IMPS)

The achievement of the government's socio-economic objectives required a strong, high growth and vibrant economy for Malaysia. The industrial sector was identified as the main sector, which could drive the Malaysian economy with the high growth levels required to achieve the socio-economic objectives of Malaysia.

Accordingly, the government formulated a master plan for the development of the industrial sector

The Industrial Master Plan (IMP) is an indicative plan which provides the framework for the industrial development of Malaysia

The IMP does not contain detailed plans for investment projects (These are contained in the 5 year Malaysia Plans) The IMP outlines industrial development strategies to accelerate the growth of the manufacturing sector and to build the base for Malaysia to be an industrial country.

The Malaysian government has so far introduced 2 IMPs

1st Industrial Master Plan (IMP 1)

The 1st Industrial Master Plan (IMP 1) covers the period 1986-1995

The IMP 1 had 3 broad objectives -

1 Accelerate the growth of the **manufacturing** sector
2 Optimum and efficient utilisation of Malaysia's **natural resource** through value added manufacturing
3 Laying the foundation for the development of **indigenous technological capability**

The IMP 1 called for technology and manpower development, improved incentive systems, infrastructure development and modernisation and rationalisation of the industrial sector

The thrust of the IMP 1 was to -

- Create outward looking industrialisation based on **export led growth**
- Intensive development of **resource based industries** for export
- **Diversification** and upgrading of non resource based industries for export

Accordingly, the IMP 1 identified 12 industrial sectors to actively promote, with each sector having specific target to achieve by 1995

The **12 industrial sectors** were -

7 Resource Based Industries

- Rubber Products Industry
- Palm Oil Products Industry
- Food Processing Industry
- Wood-based Industry
- Chemical & Petrochemical Industry
- Non- ferrous Metal Products Industry
- Non-metallic Mineral Products Industry

5 Non Resource Based Industries

- Electrical & Electronics Industry
- Transport Equipment Industry
- Machinery and Engineering Industry
- Iron & Steel Industry
- Textiles & Apparel Industry

The actual performance of the IMP exceeded the target set as seen below -

Progress of the Manufacturing Sector During the First IMP

IMP (1986-1995)	*Forecast*	*Actual*
Gross Domestic Product (GDP) (% average annual growth)	6.4	7 8
Manufacturing Value Added (% average annual growth)	8 8	13.5
Share of Manufacturing Value Added to GDP (%) in 1995	23 9	33 1
Growth of Manufacturing Exports (% annual growth)	9 4	28 6
Growth of Manufacturing Employment (% annual growth)	6.8	8.9
Total Manufacturing Employment (Million) in 1995	1.5	2 0

The IMP 1 was considered a great success in that it laid the foundation for the planned development of the industrial sector in Malaysia

2nd Industrial Master Plan (IMP 2)

The IMP 2 covers the period 1996 till 2005 and builds on the foundation laid by the IMP 1

The IMP 2 outlines five strategic thrusts

1. **Global Orientation**

   Increase focus on the changing global market for the manufacturing sector to prepare to compete globally

2. **Enhancing Competitiveness**

   The competitiveness of the manufacturing sector to be enhanced through deepening and broadening of linkages within the industrial clusters to be developed

3. **Improving Requisite Economic Foundation**

   Improving requisite economic foundation to support the manufacturing sector e g supporting industries, R&D facilities etc

4. **Malaysian-owned Manufacturing Companies**

   Increased participation of Malaysian-owned companies in the broad range of manufacturing activities including promotion of Malaysian brand names

5. **Information-intensive and Knowledge-driven Processes**

   Adoption of information-intensive and knowledge-driven processes in manufacturing and in related activities such as in R&D, product design, marketing, distribution and procurement

The main operational focus of IMP 2 is aimed at achieving 2 main objectives as follows -

1 **"Manufacturing Plus Plus" Orientation**

   The IMP 2 is aimed at making Malaysian manufacturing operations more integrated and introduces the "**Manufacturing Plus Plus**" concept This concept emphasises going beyond mere manufacturing by integrating backward (upstream) and forward (downstream) thus increasing the manufacturing "value added".

   Backward Integration

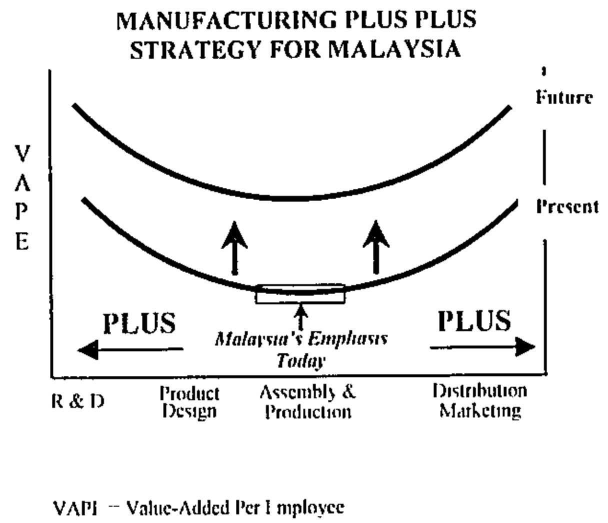
   Undertake R&D, design, prototyping, product development, etc

Forward Integration

Undertake distribution, logistic and marketing services

The Manufacturing Plus Plus concept in depicted diagrammatically below -

Table 3: Manufacturing Plus Plus



Source : IMP 2 Report

2 Cluster-Based Industrial Development

The IMP 2 also stresses cluster based industrial development emphasising the concurrent development of supporting clusters including the service sector for the achievement of a broad based, resilient and internationally competitive industrial sector

The development of industrial cluster requires the concurrent development of interlinked activities comprising of manufacturers, suppliers, critical supporting service providers, required infrastructure and related inter-dependent institutions

The IMP 2 has initially identified 22 industrial clusters to be developed (more clusters could be added later if deemed necessary)

The 22 clusters have been classified into 3 broad groups:-

Internationally Linked Cluster

Industrial Groups	*Potential Clusters*
• Electrical and Electronics	- Electrical and Electronics
• Chemical	- Petrochemicals - Pharmaceuticals
• Textiles and Apparel	- Textiles and Apparel

Policy Driven Cluster

Industrial Groups	*Potential Clusters*
• Transportation	- Automotive - Marine - Motorcycles - Aerospace
• Materials	- Polymers - Composites - Metals - Ceramics
• Machinery and Equipment	- Machinery and Equipment

Resource-Based Cluster

Industrial Groups	*Potential Clusters*
• Resource Based	- Wood-based products - Palm oil-based products (food) - Rubber-based products - Cocoa-based products
• Agro-based and food products	- Fish & fish products - Livestock & livestock products - Fruits and vegetable - Floriculture

To ensure the success of the "Manufacturing Plus Plus" concept and the cluster based industrial development concept, the IMP 2 emphasises the development of a strong and efficient economic foundation, comprising of -

- Human Resource Development
- R & D and Technology Development
- Availability of Fiscal and Non-Fiscal Incentives
- Development of Critical Support Services
- Development of Broad Based Supporting Industries Especially Small and Medium Industries

IMP 2 Targets	***IMP*** **(1986-1995)**	***IMP2*** **(1996-2005) Forecast**
• Gross Domestic Product (GDP) (% average annual growth)	7 8	8 0
• Manufacturing sector value-added (% average annual growth)	13 5	9.6
• Share of manufacturing sector value-added to GDP (%)	33 1 (Year 1995)	38 4 (Year 2005)
• Growth of manufacturing sector exports (% average annual growth)	28 6	16.0
• Total manufacturing sector employment (Million)	2 0 (Year 1995)	2.8 (Year 2005)
• Total Investment Required in the Manufacturing Sector	N/A	RM250 Billion (Year 2005)

The IMP 2 strategies have been framed to firmly establish Malaysia's growth to achieve industrialised nation status as outlined in the Vision 2020 statement

The IMP 2 guides the government's current strategies for the manufacturing sector till the year 2005

5. INCENTIVES FOR INVESTMENT

5.1 INTRODUCTION

Within the overall Policy Framework outlined in the previous chapter, various policies and incentives have been developed to promote **Foreign Direct Investments (FDI)** into Malaysia

Investment incentives are an instrument of industrial policy Malaysia like many countries uses incentives to attract and direct investments to be in line with the country's industrial policy e.g creating employment, dispersal of industries, etc

Malaysia offers many fiscal and non-fiscal incentives

Fiscal Incentives

Fiscal incentives are **tax** related Some examples of fiscal incentives offered by the Malaysian government are:

- **Pioneer Status**

  Companies granted Pioneer Status are either fully or partially exempted from paying corporate tax for periods ranging from 5 to 10 years This incentive is suited for investments that involve relatively small capital outlay and start making profits within a short time and remains profitable during the duration of the incentive period

- **Investment Tax Allowance (ITA)**

  Companies granted with the ITA incentive are given allowances up to 100% of the qualifying capital expenditure (mainly expenditure incurred on plant and machinery excluding land) incurred over a 5-year period. The tax credit can be utilised to offset against taxable income, indefinitely into the future until the tax credit is completely used up The ITA incentive is suitable for capital intensive projects which may not be profitable in the initial years

- **Reinvestment Allowance**

  This incentive is given to manufacturing companies that do not enjoy the Pioneer Status or ITA incentives, to encourage reinvestment. Manufacturing companies that are in operation for at least 12 months can apply for this incentive. Such companies that incur qualifying capital expenditure for expansion of production capacity, modernisation, etc are eligible for this allowance. 60 % of the qualifying capital expenditure is given as an allowance to offset against 70% of the taxable income.

Non-fiscal Incentives

Non-fiscal incentives are non-tax related incentives and cover a wide range of incentives Non-fiscal incentives include all non-fiscal benefits provided by the government to encourage investments. In the broad sense it also includes all **government policies which are pro-investors.**

Some examples of **non-fiscal incentives** offered by the Malaysian government include

- Stable political and economic climate
- Good infrastructural facilities
- Availability of educated and trainable workforce
- Government's "welcome" attitude and policies towards investments
- Reduced level of bureaucracy
- Relaxed equity policy for the manufacturing sector
- Ease of approval for expatriate employment passes for the manufacturing sector
- Rapid growth rate of the country (resulting in growth of local market)
- Established clear legal framework for conducting business
- Etc

5.2 EVOLUTION OF INCENTIVES FOR INVESTMENTS

The evolution of the use of incentives to attract investments in Malaysia is described below:

5.2.1 EARLY YEARS (BEFORE 1970)

The conscious use of incentives for the development of industries started in the late 1950s

a) Non-fiscal incentives

- 1958, one year after the independence of Malaysia from Great Britain, marked the beginning of conscious effort by the Malaysian government to promote investments in Malaysia with the introduction of the **Pioneer Industries (Relief from Tax) Ordinance, 1958**.

  This was the start of the government's use of incentives to promote investments

- Though 1958 marked the beginning, it was only in the 1960s that the government seriously commenced its policy of using incentives to promote investments. Initially, the incentives were for the promotion of investments mainly in **import substitution** industries

  During this period, industries catering for the domestic market like food and beverages, construction material, printing and publishing materials, chemicals and plastic material etc were promoted.

- During the initial years, the government's role was largely confined to the creation of a favourable investment climate by providing infrastructure in the form of **industrial estates and utilities**

- The most important development in the 1960s relating to industrial development and the promotion of investment was the creation in 1967 of the Federal Industrial Development Authority (**FIDA**), the predecessor to the present **MIDA**

b) Fiscal Incentives

The earliest attempt by the government to introduce fiscal incentives was the introduction of the **Pioneer Industries (Relief from Income Tax) Ordinance 1958**

- The introduction of this incentive is the start of the use of fiscal incentives by the Malaysian government to promote investments

- The 1958 Ordinance provided for.-

  - **Pioneer Status**

    This incentive provided for relief from income tax (the prevailing rate was 40%) for **2 years** with

    - Additional 1 year if capital investment between RM100,000 and RM250,000 was incurred
    - Additional 3 years if capital investment of more than RM250,000 had been incurred

- In 1965, the 1958 Ordinance was amended with the introduction of the **Pioneer Industry (Relief from Tax) Variation Act 1965**

  The Act increased the capital investment requirement to qualify for the incentive as follows

Capital Investment Requirement	**Tax Holiday from effective date of Income**
up to RM250,000	2 years
between RM250,000 and RM500,000	3 years
above RM500,000	5 years

- The incentive was introduced to encourage import substitution industries to produce goods, which were being imported then, at a time when Malaysia was primarily an agricultural country which imported most of its other requirements

Towards the late 1960s, the government found that the Act had shortcomings as it resulted in the growth of industries for the local market only. As the small domestic market became saturated, the government began to realise the need to encourage exports orientated industries

Accordingly, a review of the incentives was undertaken which resulted in the Act being replaced by the **Investment Incentives Act 1968 (IIA)**

Under the IIA, Pioneer Status was granted to an industry or product if:-

1. The industry or production was not currently being carried out in Malaysia, or if being carried out, was not on a commercial scale.
2. The industry/ product had good prospect for future development
3. The award of Pioneer Status was in the public interest

The major incentives provided by the Act included

- **Pioneer Status**
  - Tax relief for 2-5 years, depending on the amount of capital invested.
- **Investment Tax Credit**
  - **Tax credit of 25% to 40%** of the approved capital expenditure, depending on factors such as the location of the factory, whether the product was a promoted product and the local content level of the product
- **Labour Utilisation Relief incentive**
  - Incentive to encourage employment creation The incentive provided for various levels of tax exemption for companies which employs more than **50 employees**
- **Locational incentive**
  - **Tax incentive** up to **10 years** for locating in less developed areas of the country, depending on the capital investment and the number of employees
- **Export Incentive**
  - **Export allowance of 5%** of the value of the export
  - **Accelerated depreciation allowance of 20%** if at least 20% of the production was exported
  - Deduction of expenses incurred overseas for export promotion
- **Duty Exemption**
  - **Full or partial exemption of import duties on machinery and raw materials** for companies manufacturing for the export market

This Act introduced incentives to encourage employment creation and dispersal of industries.

Employment creation and **dispersing industries** all over the country was **two major objectives** of the government's industrial policy in the **late 1960s**

5.2.2 THE SEVENTIES (1971 – 1980)

The 1970s saw the introduction of many incentives, especially non-fiscal incentives.

In the 1970s, manufacturing, especially **export oriented manufacturing** was identified as a strategic sector Accordingly, the 1970s was the decade of the development of the manufacturing sector especially export orientated industries in Malaysia (When the decade started, there was not a single 100% export orientated manufacturing company in Malaysia)

a) Non-fiscal incentives

In 1970, the First Outline Perspective Plan (OPP1) was launched The OPP1 embodied the New Economic Policies (NEP) launched in 1969 The OPP1 and the NEP which placed paramount importance on **eradication of poverty and restructuring of society** identified the need for high growth to achieve the objectives of OPP1 and the NEP Since the domestic market was considered too small to sustain competitive industries, emphasis was placed on export orientated industries to provide high growth for Malaysia

In the 1970s, policies and incentives were introduced to especially promote export orientated industries Some of the developments are described below

- Introduction of the **Free Trade Zones (FTZs)** Act in 1971 FTZs are "Export Processing Zones" (EPZs) developed by State Governments to facilitate the operations of export oriented manufacturers The FTZs were developed for companies that exported 100 % of their production In certain exceptional cases companies exporting at least 80 % of their production were also allowed to locate in the FTZs The FTZs are deemed outside the Principal Customs Area (PCA) Goods imported into and exported from the FTZs are not liable for Malaysian customs duties However, goods exported from the FTZs to the PCA are liable for customs duties (if applicable). Accordingly, export orientated factories could bring to Malaysia all their required components and raw materials without customs duties and with minimal of custom formalities The FTZs are mainly located near seaports and airports The first FTZs was set up in Bayan Lepas, Penang

- The establishment of **Licensed Manufacturing Warehouse (LMW)** facilities in 1974. The LMW facilities were introduced to encourage the dispersal of export orientated industries into areas where the establishment of FTZs was not practical. Manufacturing companies exporting at least 80 % of their production could apply for LMW status The LMWs were accorded similar facilities and incentives as FTZs The LMW facility allowed factories to locate in areas other than FTZs and still enjoy the facility to import their required raw materials and components without import duties This incentive was useful to disperse industries in the country

- During the 70s, the conscious **push** for foreign direct investments in the manufacturing sector especially the **Electrical and Electronics Industry and other labour intensive industries** also commenced.

- To encourage foreign investments, the government allowed **100% foreign** equity ownership for companies exporting more than **80%** of their production.

  (Prior to this the government had in 1974 set up the **Foreign Investment Committee** (FIC) and issued guidelines which generally restricted foreign equity to 30 % and required that at least 30 % equity in Malaysian companies, including manufacturing companies be held by Bumiputras)

- The government also introduced regulations to facilitate the orderly and co-ordinated development of the industrial sector with the introduction of the **Industrial Coordination Act 1975 (ICA).** The ICA introduced the requirement for **Manufacturing Licenses** for companies involved in manufacturing with more than **RM250,000** shareholders' funds and/or employing more than **25 full time** employees.

b) Fiscal Incentives

- **No major fiscal incentives were introduced in the 1970s. This was because the** Investment Incentives Act (IIA) **was just introduced in 1968 and was deemed adequate for the 1970s.**

  The **IIA** was used to grant **Pioneer Status, Investment Tax Credit** etc to encourage investments in the industrial sector

  Tariff protection and duty exemption was also given to companies setting up operations in Malaysia.

The incentives introduced by the government were instrumental in attracting substantial investments into the manufacturing sector in the 1970s

During the 1970s the manufacturing sector's share of the Gross Domestic Product **(GDP)** grew from **13.1%** in 1971 to **19.7%** in 1980 i e. a **50.4%** increase

During the same period, the **manufacturing sector's share of exports** grew from **11.9%** to **21.7%** i e. an **82.4%** increase

5.2.3 THE EIGHTIES (1981 – 1990)

The 1980s saw the turning point in the transformation of Malaysia from an agricultural country to an industrialising country with **manufacturing overtaking agriculture as the main sector of the economy in 1987** Within **30 years**, the manufacturing industry which was virtually non-existent in 1957, became a major sector of the economy

1980 – 1985

During the first 5 years of the 1980s, Malaysia's industrial policy was still largely geared to investments in the resource based industries and exports i.e to improve exports of processed goods utilising Malaysia's natural resources e.g rubber, tin, palm oil, etc.

The global recession in the early 1980s and the declining price of primary products resulted in the recession in Malaysia in the mid-1980s In 1985 Malaysia recorded a real **GDP decline of 1 % i.e. –1% growth.**

The recession was partly due to the appreciation of Malaysia's **real weighted exchange rate** between 1980 and 1985 This resulted in Malaysian exports being less competitive.

Please refer to Exhibit 2 for graph depicting the change in the real effective exchange rate.

The government responded by introducing more aggressive strategies and programmes to develop the industrial sector The industrial sector was seen as a strategic sector to stimulate the economy to recover from the recession and provide the base for future high growth for the country

The government also realised the need to diversify the manufacturing base from being concentrated in a few sectors The need to widen the industrial sectors became apparent.

This led to a major review of the policies and incentives offered by the government to the industrial sector.

1986 – 1990

As a result of the review, the Government replaced the Investment Incentive Act 1968 with the **Promotion of Investments Act, 1986 (PIA).** To further promote foreign investments, which were seen as crucial to pull the country out of the recession, the government also began to liberalise the equity conditions imposed on foreign investors and liberalised control of the industrial sector imposed through the ICA

Also during the second half of the 1980s, the Malaysian government's industrial policy started to shift more towards **heavy industries** and supporting industries In 1986, the government launched the first **Industrial Master Plan (IMP 1)** which covered the period of **1986-1990** and laid the foundation for the industrial sector in Malaysia.

The government initiated the development of heavy industries and supporting industries e.g motor vehicles, steel plants, etc During this period, the government set up companies like the Heavy Industry Corporation of Malaysia (**HICOM**), Perusahaan Otomobil Nasional Bhd (**PROTON**) [the National Car Project], etc.

These moves were partly to "deepen" the industrial sector and partly an "import substitution" move to rely less on import for heavy and sophisticated machinery and equipment

The new fiscal and non-fiscal incentives and changes introduced in the 1980s are summarised below:-

a) Non-fiscal Incentives

In the 1980s, especially in the second part of the 80s, due to the recession, most of the non-fiscal incentives introduced by the government were aimed at attracting investments, especially foreign investments into the industrial sector The incentives liberalised the industrial climate to attract more foreign investments

- The major non-fiscal incentives introduced were the relaxation of the export requirements to hold 100% foreign equity and increase in the threshold for company's to be exempted from the ICA This exempted more companies from the ICA, which was seen by some investors as restrictive

  The various changes to the export requirement and ICA exemption thresholds are summarised in Exhibit 3.

- Companies with **US$2.0 million foreign** paid-up capital were automatically promised **5 Key Expatriate Posts** (could be held by foreigners permanently).

- MIDA was designated as the **"Centre of Investment" (COI)** in 1988 to be a 'One-Stop Agency' to promote and co-ordinate investments in the industrial sector

b) Fiscal Incentives

Major changes in fiscal incentives were introduced with the passing of the **Promotion of Investment Act 1986 (PIA)** The PIA, which replaced the Investment Incentives Act of 1968, streamlined the incentives offered and introduced new incentives aimed at encouraging the development of selected priority sectors

The major incentives offered under the PIA in the 1980s are

- **Pioneer Status (PS)**

  Refer to Section 5 1 for detail explanation of PS

- **Investment Tax Allowance (ITA)**

  Refer to Section 5 1 for detail explanation of ITA

- **Abatement Of adjusted income for exports of manufactured goods**

  An allowance equivalent to 25% of the total export sales value, which can be used to offset against the company's income for tax purposes

- **Abatement of adjusted income for location in a promoted industrial area**

  An incentive for manufacturing companies to locate in a promoted industrial estate An allowance equivalent to 5% of the adjusted income will be given.

- **Abatement of adjusted income for small scale companies**

  An incentive for small-scale manufacturing companies in Malaysia. An allowance equivalent to 5% of the adjusted income for every year shall be granted for a period of 5 years

- **Abatement of adjusted income for compliance with government policies on capital participation or employment in industry**

  Available for manufacturing companies that have complied with government policy on capital participation or employment

- **Abatement of adjusted income for the use of domestically produced materials which are incorporated in the manufacture of exports**

- **Abatement of adjusted income for purchases from small scale companies**

- **Export allowance**

  Available for companies exporting local agricultural produce and for trading companies exporting locally manufactured products An allowance of 3% of the gross income from the above activities shall be granted

- **Double deduction of expenses for promotion of exports**

- **Industrial adjustment allowance**

  An incentive granted to manufacturing companies that undergo approved restructuring activities, which will lead to further improvement or enhancement of operations. The amount of the allowance is determined by the Minister of Finance, but is not more than 100% of the expenditure incurred for that year This allowance can be offset against the adjusted income of the company for the same year. This allowance is given for expenditure incurred within 5 years from the date of approval

The PIA remains until today as the main government legislation governing incentives for promotions of investments.

Though there are many incentives offered under the PIA, the Pioneer Status (PS), Investment Tax Allowance (ITA), and the Reinvestment Allowance (RA) incentives are the most popular incentives with manufacturing companies/investors

Please refer to Section 5.1 for a description of these incentives.

All these incentives effectively provide exemptions from corporate tax for the investors

The government while maintaining the above 3 major incentives since their introduction in 1986, periodically changes the level of effective corporate tax exemption allowed by these incentives, depending on the prevailing investment environment

Please refer to Exhibit 4 for a chronologically listing of the changes to the level of corporate tax exemptions offered under the PS, ITA and RA since the introduction of the PIA in 1986.

c) Results of policies and incentives introduced in the 1980s

Malaysia's industrial policies and incentive especially in the 2nd half of the 80s to attract and direct investments were generally very successful

Further, during the second half of the 80s Malaysia's real effective exchange rate depreciated by more then 30% **(Refer to Exhibit 2)** This resulted in Malaysian exports being more competitive

There was also a steep 90% appreciation of the Japanese Yen against the US Dollar between August 1985 and April 1988. This resulted in sharp increases in the prices of Japanese products worldwide, including in Japan To remain competitive, Japanese manufacturers began relocating overseas especially into South East Asia, including Malaysia

The combination of all these factors resulted in the manufacturing sector in Malaysia which was non-existent in the 1950s to grow and account for **26.9% of the GDP** and **60.2% of exports in 1990**

Malaysia also emerged from being a country without even a single 100% export orientated company in the early 1970s to become in the 1990 the world's

- Largest exporter of **electronic semiconductors**
- Largest exporter of **rubber gloves, latex**, etc
- **Second largest exporter of** room air-conditioners

5.2.4 THE NINETIES (1990 – PRESENT)

1990 saw the end of the OPP 1 and the NEP

In 1990, the Outline Perspective Plan 2 (OPP 2) was launched to replace the OPP 1. The OPP 2 also embodied the New Development Plan (NDP) which replaced the New Economic Plan (NEP) Both the OPP 2 and the NDP placed emphasis on **national unity and balanced development among the different races in Malaysia**

The year 1990 also saw the launch of **Vision 2020** and setting of a timetable to achieve developed nation status by the year 2020. To achieve these objectives, the need to fine tune the economy, especially the industrial sector became more apparent

Further, the success of the earlier policies introduced by the government and developments in the international business environment brought new challenges to Malaysia in the 1990s Some of the challenges were

- Emergence of **labour shortage and skill shortages** to support the further development of the industrial sector

- Lack of indigenous technical capabilities among Malaysians became apparent.

- An over dependence on foreign direct investments to drive the economy and achieve the country's industrial objectives
- Lack of supporting industries to support the industrial sector
- Little industrial linkages between industries already well established in Malaysia
- Extended use of tax incentives with resulting implications on tax revenue to the government and implications on the long-run competitiveness of industries operating in Malaysia
- Emergence of new developing economies providing cheaper labour and more incentives and becoming more competitive, challenging Malaysia in certain industries
- Increased global competition in attracting foreign direct investments especially from new developing countries
- The emergence of new technologies and rapid changes of existing technologies

Malaysia responded to these challenges by formulating industrial policies to encourage industries to shift from labour intensive to high value-added, capital intensive, skill intensive and high technology industries

The government also became more selective in the promotion of investments While high technology and high value-added industries were promoted, labour-intensive industries were discouraged. The government introduced the **Capital Investment Per Employee (CIPE)** ratio, whereby new industries with CIPE of less then RM 55,000 were selectively discouraged However, this regulation was frozen in 1998 because of the economic crisis

The government also pushed for the industrial sector to shift from being "**input-driven**" (more input for more output) to be "**productivity-driven**" (less input but more output) to increase **'Total Factor Productivity' (TFP)**. This was to create a competitive edge against the new emerging economies and to deal with the labour shortage

The current industrial development of Malaysia is guided by the **IMP2** and the **7 MP**

From the second half of the 1990s Malaysia's current industrial policies are aimed at developing:

- **High technology industries**
- **High value-added industries**
- **Capital intensive industries**
- **Skill intensive industries**
- **Supporting industries**
- **Service-based industries**
- **Cross border (overseas) investments**

It is believed that the development of the above are crucial for Malaysia to be an industrialised country. Accordingly, the government's current industrial development policy and policy towards foreign investments are geared to achieve the above.

a) Non-fiscal Incentives

- The government realised that the availability of good infrastructural facilities was an important 'incentive' to attract investments and will provide Malaysia with an edge over other developing countries that do not have these facilities but provide better tax incentives

  Accordingly, the government embarked on a massive infrastructural development programme

  Some of the infrastructural projects are:

  - Construction of the Kuala Lumpur International Airport **(KLIA)**, a world class **airport** (supposed to be the **biggest in Asia** and **second biggest in the world)** and upgrading of other regional airports. KLIA has begun operations since July 1998

  - Construction of new ports and expansion of existing port facilities especially in Port Klang and Johor Bahru

  - Construction of **inland 'ports'** to facilitate export. Inland ports are inland depots managed by port authorities whereby exporters only need to send their goods to the inland port and the port authorities will arrange the transportation to the port and shipment overseas

  - Construction of **dual carriage highway** from the northern tip (Alor Setar) till the southern tip (Singapore) to facilitate the shipment of goods and dispersal of industries.

  - Licensing of human Independent Power Producers **(IPPs)** to supplement the generation of power for industry and domestic use.

  - Upgrading of telecommunication facilities

  - Construction of industrial parks all over the country to facilitate the setting up of industries in less developed areas

- To prepare Malaysia for the information age, the government embarked on the development of the **Multimedia Super Corridor (MSC)**, a 15 km by 50 km corridor near Kuala Lumpur with world class infrastructural and telecommunication facilities to attract the world class companies to set up operations in the corridor

- To immediately eliminate the shortage of labour, especially in the manufacturing sector, the government allowed the employment of **foreign workers**. However, subsequently, in response to social problems, which emerged from having large numbers of foreign workers, the government became more stringent in approving foreign workers and at times even froze the new employment of foreign workers

b) Fiscal Incentives

In response to the new issues and challenges that developed, the government undertook a major review of the tax incentives offered under the PIA in 1991

The purpose of the review was to -

- **Phase out** tax incentives which were less effective
- Encourage incentives more selectively and in a focused manner
- Fine tuning incentives to generate revenue besides encouraging investments
- Phase out non-performing incentives like locational incentives, abatements, export related incentives, etc
- Relate the granting of incentives to the achievement of -
    - **Higher local content**
    - **Higher value added**
    - **Higher level of technology**
    - **Extensive intra industry linkages**

As a result of the review, the Malaysian government concluded that fiscal incentives were not the main reason for investments into Malaysia.

Accordingly, in 1991, the government **withdrew** the granting of **full (100%)** tax exemption except for very few selective investments Changes were made to the incentives as follows:-

- Pioneer Status corporate tax exemption was reduced from **100% to 70%**

- Investment Tax Allowance was reduced from **100% to 70%** of statutory income

(The decision to reduce the quantum of the tax exemption/tax allowance (credit) was partly to increase government revenue).

The government in response to the changing industrial development focus of the country also introduced **special new incentives** through the PIA

- **Incentive for High Technology Companies**

  Incentive to promote the development of high technology industries in Malaysia

  The incentives include.

    - Pioneer Status with 100% corporate tax exemption for 5 years (The normal Pioneer Status for other companies only allowed for 70% tax exemption i e tax has to be paid on 30% of the profits).

    - Investment Tax Allowance of 60% of qualifying capital expenditure for 5 years The allowance can be offset against 100% of the income (The normal ITA for other companies only allowed for exemption against 70% of the income i e tax has to be paid on 30% of the profits)

- **Incentive for Research and Development (R&D)**

  To promote the establishment of R&D facilities, the government offered the following incentives:

  - Double deduction of R&D expenditure incurred subject to approval by the Minister of Finance.
  - Industrial Building Allowance with initial allowance of 10% and annual allowance of 2% for buildings use for approved R&D
  - Capital Allowance on capital expenditure incurred on plant and machinery used for R&D
  - Exemption from duty/tax for machinery/ equipment, materials, raw materials/ component parts and samples used for approved R&D that attract duty/tax.
  - ITA of 50% for 10 years to offset 70% of statutory income for approved in-house R&D.

  These incentives essentially involved allowances which could be offset against income to effectively reduce the corporate tax payable

- **Incentive for Multimedia Super Corridor (MSC) Companies**

  Special incentives are offered for companies located in the MSC and being heavy user of multimedia or provider of multimedia services

  Among the financial incentives include

  - PS with 100% tax exemption for 5 years, renewable to a further 5 years
  - 100% ITA on Qualifying Capital Expenditure incurred in the MSC
  - Duty-free importation of multimedia equipment
  - R&D grants for local Small and Medium-Size Enterprises (SMEs)

  Among the non-financial incentives offered to companies approved with MSC status include

  - Freedom of ownership i e. 100% foreign equity ownership possible
  - Unrestricted employment of foreign knowledge workers.
  - Freedom to source capital globally for MSC infrastructure and to borrow funds globally.
  - Intellectual property protection and a world-first comprehensive framework of cyberlaws

- World-class physical and IT infrastructure
- Globally competitive telecommunication tariffs and service guarantees
- No censorship of the Internet
- High-quality, planned urban developments
- Excellent educational facilities, including the region's first Multimedia University.
- Green environment protected by strict zoning

Generally in the 1990s, with substantial flow of investments into Malaysia, the Malaysian government became more selective and stringent in the awarding of tax incentives Some non-tax or non-fiscal incentives were also withdrawn, e g

- **Sales to FTZs and LMWs were no longer deemed as export from 1993 for the purpose of qualifying for higher foreign equity level** (This change in classification meant that new manufacturing companies had to **physically export** 80% of their production **out of the country** to be eligible for 100% foreign equity. Previously, sales to FTZ and LMW were deemed as exports even though the goods physically did not leave the country
- The approval of expatriate posts was more stringent
- The government introduced a minimum ratio for Capital Investment Per Employee (CIPE) to discourage labour intensive industries

Response to Current Economic Crisis

However, as the financial and economic crisis hit Asia including Malaysia, in 1997 the government again began to **liberalise** incentives especially non-fiscal incentives to attract foreign investment into the manufacturing sector. The manufacturing sector with its contribution to exports was identified as a crucial sector to deal with the economic crisis in Malaysia

Some of liberalisation policies introduced by the Malaysia government are

- The **temporary relaxation** of export conditions for manufacturing companies Companies imposed with **80%** export conditions for approval for 100% foreign equity were allowed to export only **50%** and still maintain their 100% equity. This exemption is valid till the year 2000.
- The government also announced the **automatic approval of technology transfer agreements** between 100% owned subsidiary companies and their foreign parent companies.

- In July 1998 the government announced that all applications for manufacturing activities approved from **31 July 1998 until 31 December 2000 will be granted 100% foreign equity** ownership without having to comply with any export condition. However, the following manufacturing activities are excluded from this relaxation.

  1. Paper packaging
  2. Plastic packaging (bottles, films, sheets and bags)
  3. Plastic injection moulded components
  4. Metal stamping, metal fabrication & Electroplating
  5. Wire harness
  6. Printing
  7. Steel service centre

- In September 1998, the government pegged the exchange rate of the Malaysian Ringgit to the US Dollar at RM3.80 per US Dollar. This was to stabilise the Malaysian currency, which had fluctuated from RM2 50 per US Dollar to RM4.80 per US Dollar within a matter of one year.

  This move had the effect of stabilising the Malaysian currency, assisting Malaysian manufacturers and exporters being able to better plan their activities

- In September 1998, the government introduced capital controls restricting the repatriation of capital from Malaysia However, these capital control measures were directed mainly at portfolio investments. Foreign Direct Investments in the manufacturing sector were exempted from the capital control

As it has been seen from the previous chapters, the Malaysian government uses incentives extensively to achieve the industrial development strategy of the government

5.3 EFFECTIVENESS OF INCENTIVES

It is widely accepted and admitted that incentives played an important role in attracting investments, especially foreign investments into Malaysia The fact that Malaysia has been transformed from being an agriculture-based economy to a rapidly industrialising country, is testimony to the past effectiveness of incentives However, there is very little published data on the past effectiveness of incentives, especially fiscal incentives

A review of available data has revealed the following on the effectiveness of **tax incentives** in the past·

- The earlier 'Pioneer Status' incentive was biased towards large projects as the amount of tax incentive was based on the amount of investment and size of the labour force The incentive did not encourage important projects which may be small and projects with long gestation period.

  To encourage such projects, the government introduced a new incentive called the Investment Tax Allowance (ITA) specifically for projects with **long gestation period** The government also introduced Pioneer Status and ITA specifically for Small and Medium Industries (SMIs)

- In the early years, the incentives were mainly aimed at promoting import substitution industries which could also enjoy tariff protection Accordingly, the tax incentives were overlapping and redundant to some extent

- **Locational incentives** have generally **not been effective** in encouraging industries to locate in less developed areas. A study* in 1971 found that the tax incentive ranked low among the factors which influenced location decisions

  Between 1980 and 1990 companies approved with locational incentives accounted for only 54 out of 6340 companies approved with incentives i e less than 1 percent**.

  Generally large and foreign investors tend to concentrate in more developed areas

- An analysis of projects approved from 1988-1996 (**See Exhibit 5**) indicated that except for 1992, investments approved **with tax incentives** have been consistently **higher than approvals without tax incentives** This indicates that tax incentives are still important and required by investors

- The analysis also indicated the gap between the two categories **narrowed** in recent years indicating more and more projects being approved without tax incentive Further, investments approved without tax incentives appear to be growing at a faster rate than projects with tax incentives

  Accordingly, it could be argued that tax incentives are becoming relatively a less important factor in attracting investments in the manufacturing industry

  This may be explained by the fact that manufacturing investment is increasingly been determined by several other factors e g political stability of the country, availability of suitable infrastructure, etc besides tax incentives

- This observation is backed by a study* of 292 manufacturing companies established between 1970-1976. The study apparently indicated that **tax incentives were not a major factor** in determining manufacturing investment Other factors such as availability of industrial estates, transportation facilities for finished goods, accessibility to main markets, and availability of trainable labour were deemed more important

  Further, a large number of the plant managers interviewed as part of the same study indicated that they only applied for tax exemption after they had decided the investment and the location of the investment

Note:

* = P.405 "The Investment Incentives and Trends of Manufacturing Investment in Malaysia" (Fong Chan Onn and Lim Kok Cheong) 1982

** = P.66 "Managing Industrial Transition in Malaysia" (ISIS) 1995

- More recent results of the Federation of Malaysian Manufacturers (FMM) / Anderson Consulting survey of Chief Executive Officers in Malaysia on "Trends, Directions and Outlook in Malaysia" for the reasons for locating in Malaysia is provided below.-

A 1987

Ranking	Reason for Locating in Malaysia
1.	Political stability
2	Availability of labour
3.	**Tax incentives**
4	Economic stability
5	Competitive cost advantage

B. 1989/90

Ranking	
1.	Political stability
2.	Economic stability
3.	Availability of labour
4.	Competitive cost advantage
5.	**Tax incentives**

C. 1991/92

Ranking	
1.	Political stability
2.	Economic stability
3	Competitive cost advantage
4.	Geographic location/access to market
5	Availability of raw materials

D. 1994/95

Ranking	
1	Political stability
2	Geographic location/access to market
3.	Economic stability
4	Competitive cost advantage
5	Availability of raw materials

As it can be seen, the importance of tax or fiscal incentives for locating in Malaysia has dropped from **3rd place** in 1987 to **5th place** in 1989/90

From 1991, tax incentive doesn't appear in the top five reasons for locating in Malaysia

Though the FMM / Andersen Consulting survey was discontinued after 1995, the following Trade organisations have indicated that their internal survey of members have shown that tax or fiscal incentives **is not among the top 5 reasons for investing in Malaysia**

1. The Federation of Malaysian Manufacturers representing more than 10,000 manufacturers in Malaysia

2 The Malaysian International Chamber of Commerce and Industry representing more than 2,000 international investors in Malaysia

3. The American Chamber of Commerce and Industry in Malaysia representing more than 800 members.

Similar sentiments have been expressed by MIDA senior officers who are convinced that fiscal incentives are only **"ICING ON THE CAKE"** and is **not a major reason** for investment in Malaysia

Also our interviews have indicated that investors locating in Malaysia regard fiscal incentives as **an important** factor to their project but **not the main reason** for investment in Malaysia

6. INSTITUTIONAL FRAMEWORK

6.1 RELEVANT LEGISLATION

The 2 main Legislation relating to Foreign Direct Investment in Malaysia are:

1 The Industrial Coordination Act 1975
2. The Promotion of Investments Act 1986

6.1.1 THE INDUSTRIAL COORDINATION ACT 1975 (ICA)

The ICA was introduced in 1975 to regulate the manufacturing sector by introducing the requirement for a Manufacturing Licence

Companies undertaking manufacturing operations in Malaysia (other then those exempted) are required to apply and obtain a Manufacturing Licence

In approving the Manufacturing Licence, the government usually imposes conditions on the manufacturing companies, thus controlling the activities of the manufacturing companies

The ICA was also used to implement Malaysia's equity policy especially relating to foreign equity and Bumiputra equity in the manufacturing sector For companies exporting less than 80% of the production, the government imposed limits on foreign equity and imposed the requirement for Bumiputra equity as a condition for approving the Manufacturing Licence.

- **Standard Manufacturing Licence Conditions**

  The conditions normally imposed on the Manufacturing Licence relates to

  - Limits on foreign equity
  - Minimum Bumiputra equity (if applicable)
  - Export requirement/obligations
  - Need for approval for Technical Agreements with foreign parties
  - Requirement to obtain prior approval for sale of the foreign shares in the manufacturing company
  - Need to obtain approval for expansion project, etc

  Please refer to Exhibit 6 for a sample of the conditions usually imposed on the Manufacturing Licence

- ***Equity Conditions***

  Malaysia has tied the level of foreign equity permitted in manufacturing companies to the level of export Generally, if a foreign company set up operations in Malaysia and intends to export at least 80% of its production overseas, then the foreign company will be allowed to have 100% foreign equity. However, if the company intend to supply to the local market then the company will be required to have local equity

  The actual level of export required to hold 100% foreign equity has been changed several times over the years

  Please see Exhibit 3 for details of the changes over the years.

Exemption from the ICA

When the ICA was introduced in 1975, small manufacturing companies i.e. those with shareholder funds **below RM250,000 or employing less than 25 full-time employees were exempted** from applying for the Manufacturing Licence

Over the years, the threshold for exemption was increased several times, thus exempting more manufacturing companies from applying for the Manufacturing Licence These moves were attempts to liberalise the investment climate in the manufacturing licence

The various changes to the threshold for exemption from the Manufacturing Licence is provided below

	Threshold for exemption from Manufacturing Licence	
Year	**Shareholder Fund**	**No. of Full-time Employee**
Introduction of Act	< 250,000	< 25
12 Dec 1985	< 1,000,000	< 50
24 Oct 1986	< 2,500,000	< 75

6.1.2 THE PROMOTION OF INVESTMENT ACT 1986 (PIA)

The PIA was introduced in 1986, replacing the Investment Incentive Act introduced in 1968.

The PIA remains till today as the main legislation relating to the award of fiscal incentives in Malaysia

The PIA provide for the following incentives:

1 Pioneer Status (PS)

2 Investment Tax Allowance (ITA)

3 Abatement of adjusted income for manufactured exports

4. Abatement of adjusted income for location in a promoted industrial area

5 Abatement of adjusted income for small scale companies

6 Abatement of adjusted income for compliance with government policies on capital participation or employment in industry

7. Abatement of adjusted income for the use of domestically produced materials which are incorporated in the manufacture of exports

8 Abatement of adjusted income for purchases from small scale companies

9 Export allowance

10 Double deduction of expenses for promotion of exports

11 Industrial adjustment allowance

The above incentives have been discussed in Section 5 of this report.

6.2 RELATED INSTITUTIONS

6.2.1 MINISTRY OF INTERNATIONAL TRADE AND INDUSTRY (MITI)

MITI is the main agency responsible for foreign investment in the manufacturing sector in Malaysia

Please refer to Exhibit 7 for the organisation chart of MITI

MITI is headed by a Minister who reports to the Cabinet (Council of Ministers) and the Prime Minister.

MITI is responsible for matters relating to foreign investment in the manufacturing sector in Malaysia

To promote and coordinate the industrial sector in Malaysia, the government set up a special agency under MITI, called the Federal Industrial Development Authority (FIDA) in 1968. FIDA was renamed the Malaysian Industrial Development Authority (MIDA) in 1979 (MIDA) and is today the primary agency responsible for the promotion and coordination of the industrial sector in Malaysia

6.2.2 MALAYSIA INDUSTRIAL DEVELOPMENT AUTHORITY (MIDA)

MIDA plays two main roles

1. **Promotional Role**

   MIDA **promotes** both domestic and foreign investments in the manufacturing sector in Malaysia

2. **Coordination Role (One-stop Agency)**

   MIDA also **coordinates** investment in the manufacturing industry in Malaysia

   Please refer to Exhibit 8 for organisation chart of MIDA

   Besides the above 2 main roles, MIDA also plays an important role in **formulating and reviewing tax incentives**

a) **Promotional Role**

MIDA is the main government agency responsible for promoting investments especially foreign investments in the manufacturing sector in Malaysia.

MIDA uses the following promotional tools to promote investments in Malaysia

1. **Promotions through Network of MIDA Offices**

MIDA presently has a network of 13 international offices and 13 domestic offices as follows:

International Offices

- Sydney, Australia
- Tokyo, Japan
- Osaka, Japan
- Seoul, South Korea
- Taipei, Taiwan
- Paris, France
- Cologne, Germany
- Milan, Italy
- Stockholm, Sweden
- London, United Kingdom
- Los Angeles, United States of America
- Chicago, United States of America
- New York, United States of America

(MIDA closed its Singapore and Hong Kong Offices early in 1998)

Domestic Offices

- Head Office in Kuala Lumpur
- Johor Bahru, Johor
- Alor Setar, Kedah
- Kota Bharu, Kelantan
- Malacca
- Seremban, Negeri Sembilan
- Kuantan, Pahang
- Ipoh, Perak
- Kangar, Perlis
- Georgetown, Penang
- Kota Kinabalu, Sabah
- Kuching, Sarawak
- Kuala Terengganu, Terengganu

The offices are staffed with officials whose main role is to promote investment in the manufacturing sector in Malaysia.

2. Organising Trade and Investment Missions

The government also organises many missions abroad every year. These missions are organised and coordinated by MIDA.

- The purpose of the missions is to promote Malaysia as a strategic investment partner and to update potential investors on policies, incentives and business opportunities in Malaysia

- The trade missions are usually led by the Minister of International Trade and Industry. Occasionally, the missions are led by the Prime Minister The members of the missions are private companies, federal and state government officers

- The missions are targeted at technologically advanced countries and major 'capital exporting' countries like Japan, the United States of America, etc

- Typically, during the trade missions potential investors in the respective countries are invited to seminars for dissemination of information on Malaysia followed by one-to-one meeting opportunities for potential investors with the Malaysian delegation

3. Specific Promotion Missions

- MIDA also organises specific promotion missions besides the general promotion missions MIDA identifies specific industries, technologies or R&D capabilities deemed necessary for the industrial development of the country. MIDA then organises specific promotion missions to attract investments in these specific areas

  For example in 1996, MIDA organised 6 specific promotion missions as follows:

Specific Industry	Trade Missions to
1. Telecommunications Equipment	Germany, Sweden and Finland
2 Wrapping and Packaging Paper	Sweden and Finland
3 Cutting Tools, Heat Treatment, Forging, Measuring and Scientific Equipment	Japan and Taiwan
4. Oleochemicals	Germany, France and Netherlands
5 Advanced Ceramics	United Kingdom and Germany
6 High Technology and Related industries	United States of America

- The specific missions are usually led by the Chairman/ Director General/ Director of the relevant industry divisions of MIDA and members of the missions consist of local experts and companies in the relevant industries

  As part of the trade mission, visits are organised to specific companies In 1996, visits to **72** manufacturing, R&D companies and training institutions were made

- MIDA has found the specific trade missions to be very effective for establishing direct contact with top management of leading companies

  Team members also found the factory visits very useful, especially the opportunity to learn about the latest and world-class technology

  MIDA also sends its officials to attend specific trade fairs and seminars internationally to expose the officers to the latest technologies available around the world.

4. Targeting of Individual Companies

- MIDA also targets selected high technology and R&D companies for possible relocation and investment in Malaysia
- The selection is usually done by MIDA offices overseas The offices then approach the selected companies to convince them to invest in Malaysia.
- Sometimes high powered 'round table' meetings are organised with top management of the companies On the Malaysian side, the round table meeting are usually led by the Senior MITI or MIDA officials

5. Collaboration with other agencies

MIDA also works with local and international trade associations and financial institutions This is to enhance industrial co-operation and foreign investments in Malaysia

MIDA has signed **17** Memorandum of Understandings (MOUs) as follows·

Industrial Associations

- Confederation of Small and Medium Industries of Italy (COMFADI), **Italy**.
- The Association of Pour La Promotion Et Le Development Industral (APRODI), **France**.
- The Malaysian, Italian, Gulf and African (MIGA) Chamber
- The Economic Development Corporation of the state of Bremen (EDCB), **Germany**
- The Small and Medium Industry Promotion Corporation (SMIDC), **South Korea**.
- The Cambodian Investment Board (CIB), The Kingdom of Cambodia

Financial Institutions

Foreign Banks

- Bank of Tokyo-Mitsubishi, Japan
- Sakura Bank, Japan
- Sanwa Bank, Japan
- Tokai Bank, Japan
- Bank of Nagoya Ltd , Japan
- Banque Francaise du Commerce Exteriur (BFCE), France
- Instituto Bancario San Paolo, Italy
- Nacional Financier, Mexico

Malaysian Banks

- Public Bank Berhad
- Standard Chartered Bank Berhad

6. Investment Promotion Publications

- MIDA promotes investment by publishing brochures and guidebooks on investment in Malaysia Some of the guidebooks are published in 7 languages

- English
- Japanese
- French
- Italian
- German
- Chinese
- Tamil

- MIDA has also prepared audio-visual presentations in 6 languages providing an overview of the economic and investment environment in Malaysia

- English
- Japanese
- French
- Italian
- German
- Chinese

- Advertisements and Advertorials (Advertisement Editorials)

  MIDA advertises in leading foreign business newspapers and international magazines like Times, Newsweek, Fortune etc. and in local business directories like the Federation of Malaysian Manufacturers (FMM) magazine.

- Close Relationship with the Press

  MIDA maintains close relationship with the press by

  - Sponsorship of journalists from leading magazines to visit Malaysia and write about the country, economic development, investments in Malaysia etc

  - Assisting foreign and local television crew to produce documentaries on Malaysian industrialisation

  MIDA also issues periodic press releases to local and foreign media, highlighting the industrial development in Malaysia.

7. **Participation in Exhibitions and Trade Fairs organised by other parties**

   MIDA participates in local and foreign exhibitions and trade fairs to promote investment opportunities in Malaysia

b) Co-ordination Of Investment Role

The coordination of investments into Malaysia is another major role of MIDA

MIDA implements its coordination role in 2 ways

1. **Acting as a "One-Stop Agency" for investments in the manufacturing sector.**

   - The one-stop agency was set up in September 1979 as a 'Central Unit' so that investors need to come only to MIDA

     These investors are able to obtain the necessary information on the various approvals required by the Federal Government

     The purpose is to cut down the time wasted in consulting numerous government agencies

   - In 1988, the **'Centre of Investment' (COI)** was set up to replace the 'Central Unit' Subsequently the COI was renamed as the **'Advisory Services Centre'** (ASC) as it is called today

The ASC comprises of representatives from

- Ministry of Finance (Treasury)
- Ministry of Human Resources
- Royal Customs and Excise Department
- Immigration Department
- Department of Environment (DOE)
- Department of Occupational Safety & Health (DOSH)
- Telekom Malaysia Berhad (National Telecom Company)
- Tenaga Nasional Berhad (National Electrical Power Company)

The representative from the Customs and Excise Department, Immigration Department, DOE and DOSH are **permanently stationed in MIDA** to provide advice to investors and to assist in evaluation of the project

The objectives of the ASC are to facilitate investors in obtaining the approvals required from the various departments and agencies of the Federal Government This removes bureaucratic delays and red tape to reduce the time taken to obtain approvals to set up manufacturing projects in Malaysia

2. **Evaluation of application for various approvals related to various government agencies and departments in Malaysia.**

- MIDA receives and evaluates various applications related to manufacturing industries on behalf of the Federal Government

- Copies of the applications are also sent to the relevant ASC members based in MIDA, if the application relates to their department These representatives give them inputs and assist in the evaluation of the project

- After evaluation by MIDA officials, the applications will be deliberated by **special committees** based in MIDA The members of these special committees are representatives from the relevant government agencies MIDA also provides the Secretariat for these special committees

- The special committees after deliberation, make recommendations to the relevant Ministry/ Department for the final approval of the relevant Ministry/ Department

- Usually, approvals of the relevant ministry/ department are a formality once the relevant special committee in MIDA has deliberated the matter and made recommendations on the application

  This is because, usually a representative from the relevant department will be a member of the special committee. The relevant representative will give their inputs/comments which if accepted by the committee, will be imposed as a condition on the approval

On average it takes about 2-3 months for the application to be processed and approved/rejected

The special committees set up in MIDA are described below

- **Action Committee of Industries (ACI)**

  The ACI deliberate applications related to the **Manufacturing License** required under the Industrial Coordination Act 1975 and **incentives** under the Promotion of Investments Act 1986

  The committee also approves Expatriate Posts for manufacturing companies

  The committee submits its recommendations for final approval as follows

  - **Manufacturing License** – Ministry of International Trade and Industry (MITI)
  - **Incentives** – MITI and Ministry of Finance (MOF)
  - **Expatriate Posts** – Immigration Department

  The composition of the ACI is given below

  Chairman

  Chairman of MIDA, **or**
  Director-General of MIDA

  ACI Members.

  1) Director-General of MIDA
  2) Both Deputy Director Generals of MIDA
  3) Representative from the Ministry of International Trade and Industry (MITI)
  4) Representative from the Ministry of Finance (MOF)
  5) Representative from the Inland Revenue Board (IRB)
  6) All MIDA Directors

  Co-opted Members

  Representatives from the

  1) Immigration Department
  2) Agricultural Department
  3) Ministry of Culture, Arts & Tourism
  4) Department of Environment (DOE)

- **Duty Exemption on Machinery and Equipment Committee**

The committee considers applications and makes recommendations for duty exemption **on machinery and equipment** under the Customs Act 1967, Sales Tax Act 1972 and the Excise Act 1976

The composition of this committee is made up of the following:

Chairman. Representative from the Ministry of Finance (MOF) [Tax Analysis Division]

Members. Representatives from

1) Ministry of Finance (MOF)
2) Ministry of International Trade and Industry (MITI)
3) Royal Custom and Excise Department
4) Department of Occupational Safety and Health (DOSH)
5) Directors of Industry Divisions in MIDA

- **Duty Exemption on Raw Materials/ Components Committee**

  This committee considers applications for duty exemption **on raw materials/ components** and makes recommendations to the MOF for final approval

  The composition of this committee is made up of the following

  Chairman Deputy Director-General II of MIDA

  Members·

  1) Directors of Industry Divisions in MIDA

- **Special Advisory Committee on Tariffs**

  Advises the government on any requests for tariff protection against imports and measures to protect local industries. This is to develop the local industry.

  The composition of this committee is made up of the following:

  Chairman Deputy Chief Secretary I of MITI

  Members: Representatives from

  1) Ministry of Finance (MOF)
  2) Ministry of International Trade and Industry (MITI)
  3) Royal Customs and Excise Department
  4) MIDA

- **Committee on Technical Agreements**

  Considers technology transfer agreements between Malaysian manufacturing companies licensed under the Industrial Coordination Act 1975 and foreign parties

  Generally, the Deputy Director-General I of MIDA approves most technology transfer agreements

  However, if a meeting is required, the composition of this committee is made up of the following

  Chairman Deputy Director-General I of MIDA

  Members

  1) Directors of Industry Divisions in MIDA

     Generally, MIDA officials and the Representatives from the relevant government agencies based in MIDA provide support to the investors by answering their queries and assisting in filing in the application and applying for the various incentives

c) Development Of Incentives

Tax incentives are continuously reviewed to fine tune the incentives to meet government objectives

Additional incentives are introduced when necessary and existing incentives are reviewed and dropped from time to time.

Further the list of products /activities eligible for incentives are also reviewed. The review of the incentives is usually initiated in one of the following ways:-

1 MIDA's recommendation

2 Proposal by external parties

3 Prompted by Budget announcement, announcements by ministers on some new amendments, etc

MIDA, being the main government agency responsible for industries is in the best position to fine tune incentives MIDA is organised into divisions based on specific industries, MIDA is able to monitor new developments in specific industries worldwide.

Accordingly, MIDA's offices are in the best position to recommend granting of incentives for new technologies or for dropping certain products from the promoted list of products currently eligible for incentives

This is most common method of how the incentives are formulated/reviewed

Even where an incentive for a particular product/ activity is initiated by budget announcement or by third parties like individual companies, trade associations etc , the matter will be referred to MIDA for further action.

The respective division in MIDA responsible for the particular industry will prepare a paper for the introduction of incentives to a particular product or for dropping some products from the incentives list

The paper will be sent to the "**Incentives Committee**" set up by the government The committee, also called the "**Action Committee No. 2**", is chaired by the Chairman of MIDA The other members include MIDA's Director General, Deputy Director General, Directors of Industrial Divisions, Senior Officers from the Ministry of Finance (Treasury), Inland Revenue Board, the Ministry of Science, Technology and Environment, and SMIDEC

The Incentives Committee meetings are held on an ad hoc basis usually if there are at least 3 cases pending for the Committee's decision.

The Incentives Committee also undertakes reviews of the products/ activities currently on the promoted list on whether it should be maintained or dropped from the Promoted List These reviews are usually done on an annual basis

The committee also considers the suggestions from the various chambers of commerce and industry support groups, received either during the annual dialogue that MITI has with these bodies or if these bodies

The Committee's recommendations are forwarded to MITI and Ministry of Finance (MOF) for their approval

Once approved by MITI and MOF, the new products/ activities will be gazetted The gazette notification will take the form of amendment to the List of promoted products/ activities published earlier

The process of gazetting may take 6 months or longer due to administration procedures involved

However, the implementation is made before being gazetted

d) Lessons from MIDA

Our interviews with various segments of industries and government have revealed the following assessments about MIDA which can be lessons for other developing countries·

1. Promotional Role

- Constant and active promotion of investment opportunities in the country is crucial to continuously attract domestic and foreign investments.

- There are lots of competition globally, especially from developing countries in attracting foreign direct investment

- Many developing countries have begun promoting investment opportunities in their countries. Accordingly if Malaysia does not actively promote the country, the investors may not come to the country

- Promotion of investment opportunities should be more focused as too many countries are doing general promotions

- Investors generally view MIDA as the '**Best Government Agency**' not only in Malaysia but also in the region

2. One-stop Agency Role

- The one-stop agency role of MIDA is very much appreciated and viewed as very effective by various Trade Associations and foreign/ domestic investors.

- Trade Associations have voiced that the one-stop agency role could be enhanced if MIDA is given **approving** powers also Presently MIDA only considers the application and makes recommendations, while the final approval comes from the relevant ministries

  It is believed that this proposed approach would cut more red tapes and speed up approvals This would make MIDA more effective in promoting and coordinating investments in the country

- Many countries send delegations to MIDA to learn about MIDA's one-stop agency role This is testimony to the effectiveness of MIDA in this role

- MIDA organises familiarisation programmes for investment promotion officials from less developed countries to share MIDA's experience in promoting and coordinating investments

3. Incentives Role

- Incentives are very important for foreign investors There is competition for Foreign Direct Investments among many developing countries

- However, tax or fiscal incentives is not the most important criteria for deciding to invest in Malaysia as most countries give similar forms of tax incentives

- Tax incentives should be focused to achieve specific objectives

- Non-fiscal incentives such as stable political climate, the availability of infrastructural facilities, an investor-friendly business environment etc are more important

- MIDA's views incentives as only **"icing on the cake"** i e something that the investors want after they are convinced that Malaysia is the best place for their investment evaluating other factors

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11 **MIDA Seminar Notes:**

- ASEAN Member Countries
- Functions of MIDA
- Incentives for Investment in the Manufacturing Sector
- Experiences in the Development of the Manufacturing Sector in Malaysia
- Special Incentives for Industries Locating in the Eastern Corridor of Peninsular Malaysia, Sabah and Sarawak
- Evolution of the Manufacturing Sector in Malaysia from 1960s & MIDA's Role
- Planning for Industrial Development & Evolution of Incentives Scheme
- Free Zones (FZ) & Licensed Manufacturing Warehouses (LMW)
- Technical Agreements, Tariff Protection, Duty Exemption on Raw Materials & Components, Duty Exemption on Machinery & Equipment & Case Study
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EXHIBIT 1

ECONOMIC PERFORMANCE INDICATORS, 1985 – 1998

EXHIBIT 1

ECONOMIC PERFORMANCE INDICATORS, 1985 – 1998

	1985	1986	1987	1988	1989	1990	1991
Population (million, persons)	13 0	13 3	13 7	14 0	14 3	14 6	18 3
Labour force (thousands, persons)	6,039	6,222	6,409	6,658	6,850	7,042	7,204
Employment (thousands, persons)	5,625	5,707	5,881	6,176	6,390	6,686	6,891
Unemployment (%)	6 9	8 8	8 2	7 2	6 7	5 1	4 3
Gross Domestic Product (RM million at current prices)	77,470	71,794	79,625	90,861	102,451	115,701	132,381
Gross Domestic Product (RM million at 1978 prices)	57,093	57,751	60,863	66,218	72,297	79,329	86,149
Growth rates (%)							
• Gross Domestic Product	-1 2	1 2	5 4	8 9	9 2	9 7	8 7
• Agriculture, forestry and fishing	2 0	4 2	7 0	5 4	6 0	0 2	0 2
• Manufacturing	-3 8	7 5	13 4	17 6	14 2	15 7	13 9
• Mining and quarrying	-1.9	6 9	0 6	6 1	8 5	5 1	2 4
• Construction	-8 4	-14 0	-11 8	2 7	11 6	19 1	14 3
• Services	1 7	-0 6	5 3	7 5	8 5	11 6	10 4
Gross National Product (RM million at current prices)	75,962	66,814	74,679	85,777	96,548	110,637	125,581
Gross National Product (RM million at 1978 prices)	52,8358	54,155	57,164	62,517	68,212	75,904	81,511
Growth rates (%)							
• Gross National Product	-1 3	2 5	5 6	9 4	9 1	11.3	7 4
• Public consumption	-0 9	1 3	1 5	4 9	7 6	5 3	12 4
• Private consumption	0.3	-10	2 1	16 1	12 6	13 1	9 5
• Public investment	-10 4	-2 4	-17 0	5	34 3	17 1	18 6
• Private investment	-8 6	-16 6	6 2	22	30 5	24 8	23 1
• Exports	0 4	11 8	14 4	11 8	18 0	17 1	14 1
• Imports	-9 8	-6 5	8 4	24 4	26 7	24 2	24 5
Balance of payments							
• Merchandise balance	8,883	8,378	14,703	14,524	11,871	7,093	1,449
• Services balance	-10,391	-8,790	-8,409	-10,180	-11,392	-9,723	-13,195
• Transfers	-14	96	348	395	219	147	102
• Current account (f o.b)	-1,522	-316	6,642	4,739	698	-2,483	-11,644
• *% of GNP*	-2 1	-0 5	8 9	5 5	0 7	-2 2	-9 3
External Trade (RM million)							
• Total exports (f o b)	38,017	35,319	45,225	55,260	67,825	79,646	94,497
• Total imports (c i f)	30,438	27,921	31,934	43,293	60,858	79,119	100,831
• Balance of trade	7,579	7,397	13,291	11,697	6,966	528	-6,335
Consumer Price Index (%)	0 4	0 8	2 5	2 5	2 8	3.1	4 4
External Debt (RM million)	42,249	50,489	50,331	46,973	42,138	41,488	43,798
• National Debt service ratio (%)	15 6	17 9	14 8	13 1	9 6	7 9	6 6
• *(% of exports)*	15 8	18 9	16 4	13 1	9 6	8 3	7
• *(% of GDP)*	54 8	70 5	63 2	54 4	44 3	39 7	38 5
Net Bank Negara Reserves (RM million)	12,457	16,539	19,432	18,328	21,660	27,025	30,452
Months of retained imports	5 0	7 2	7 4	5 1	4 3	4 1	3 6

*As at 15 December 1998

Exhibit 1
Economic Performance Indicators
Page 2

	1992	1993	1994	1995	1996	1997	1998
Population (million, persons)	19 2	19 6	20 1	20 7	21 2	21 7	22 2
Labour force (thousands, persons)	7,370	7,627	7,834	8,257	8,641	9,038	9,007
Employment (thousands, persons)	7,096	7,498	7,603	8,024	8,417	8,805	8,540
Unemployment (%)	3 7	3 0	2 9	2 8	2 6	2 6	5 2
Gross Domestic Product (RM million at current prices)	148,537	165,206	190,274	218,671	249,503	275,367	279,816
Gross Domestic Product (RM million at 1978 prices)	92,866	100,618	109,977	120,272	130,621	140,684	131,783
Growth rates (%)							
• Gross Domestic Product	7 6	8 3	9 3	9 4	8 6	7 7	-6 3
• Agriculture, forestry and fishing	0 2	4 5	-1 0	1 1	2 2	1 3	-4 9
• Manufacturing	10 5	12 9	14 9	14 2	12 3	12 5	-9 5
• Mining and quarrying	1 6	-0 4	2 5	8 9	4 5	1 0	-0 2
• Construction	11 7	11 2	14 1	17 3	14 2	9 5	-23 9
• Services	8 2	9 8	9 7	9 4	9 7	8 0	1 8
Gross National Product (RM million at current prices)	140,531	156,941	180,862	208,294	237,687	261,094	257,865
Gross National Product (RM million at 1978 prices)	87,667	95,291	104,006	113,704	123,166	132,811	123,776
Growth rates (%)							
• Gross National Product	7 6	8 7	9 1	9 3	8 3	7 8	-6 8
• Public consumption	4	10 7	9 9	7 3	1 4	5 3	1 1
• Private consumption	3	4 6	9 9	9 3	6 0	4 7	-9 3
• Public investment	28	8 4	-0 6	8 7	1 1	8 6	-11 4
• Private investment	0 5	19 1	27 9	25 3	13 4	8 4	-58 8
• Exports	6 2	17 2	22 5	17 6	7 2	10 8	1 5
• Imports	1 2	19 1	27 7	21 4	4 2	10 2	-16 0
Balance of payments							
• Merchandise balance	8,609	8,231	4,460	97	10,154	11,337	59,961
• Services balance	-14,568	-16,670	-17,005	-19,229	-19,414	-21,792	-21,502
• Transfers	337	503	-2,225	-2,515	-2,936	-3,698	-4,043
• Current account (f o b)	-11,644	-7,926	-14,770	-21,647	-12,196	-14,153	34,416
• *% of GNP*	-4 0	-5 1	-8 2	-10 4	-5 1	-5 4	13 3
External Trade (RM million)							
• Total exports (f o b)	103 657	121,238	153,921	184,987	197,026	221,408	287,156
• Total imports (c i f)	101 441	117,405	155,921	194,345	197,280	220,984	232,214
• Balance of trade	2,216	3,833	-2,000	-9,358	-254	424	54,942
Consumer Price Index (%)	4 7	3 5	3 7	3 4	3 5	3 2	5 3
External Debt (RM million)	42,794	51,861	59,147	68,810	73,182	125,672	150,337
• National Debt service ratio (%)	6 4	6 2	5 2	6 2	5 7	5 1	7 2
• *(% of exports)*	6 9	7 1	5 5	6 6	6 9	5 5	6 7
• *(% of GDP)*	37 7	41 9	38 7	38 9	39 2	62	57 3
Net Bank Negara Reserves (RM million)	47 196	76,435	68 173	63,770	70,015	59,123	93,854*
Months of retained imports	5 6	8 3	5 5	4 1	4 4	3 4	4 7

*As at 15 December 1998

Source National Economic Action Council (NEAC)

EXHIBIT 2

(a) REAL EFFECTIVE EXCHANGE RATE – MALAYSIA, 1980 – 1990 [Table]

(b) REAL EFFECTIVE EXCHANGE RATE – MALAYSIA, 1980 – 1990 [Graph]

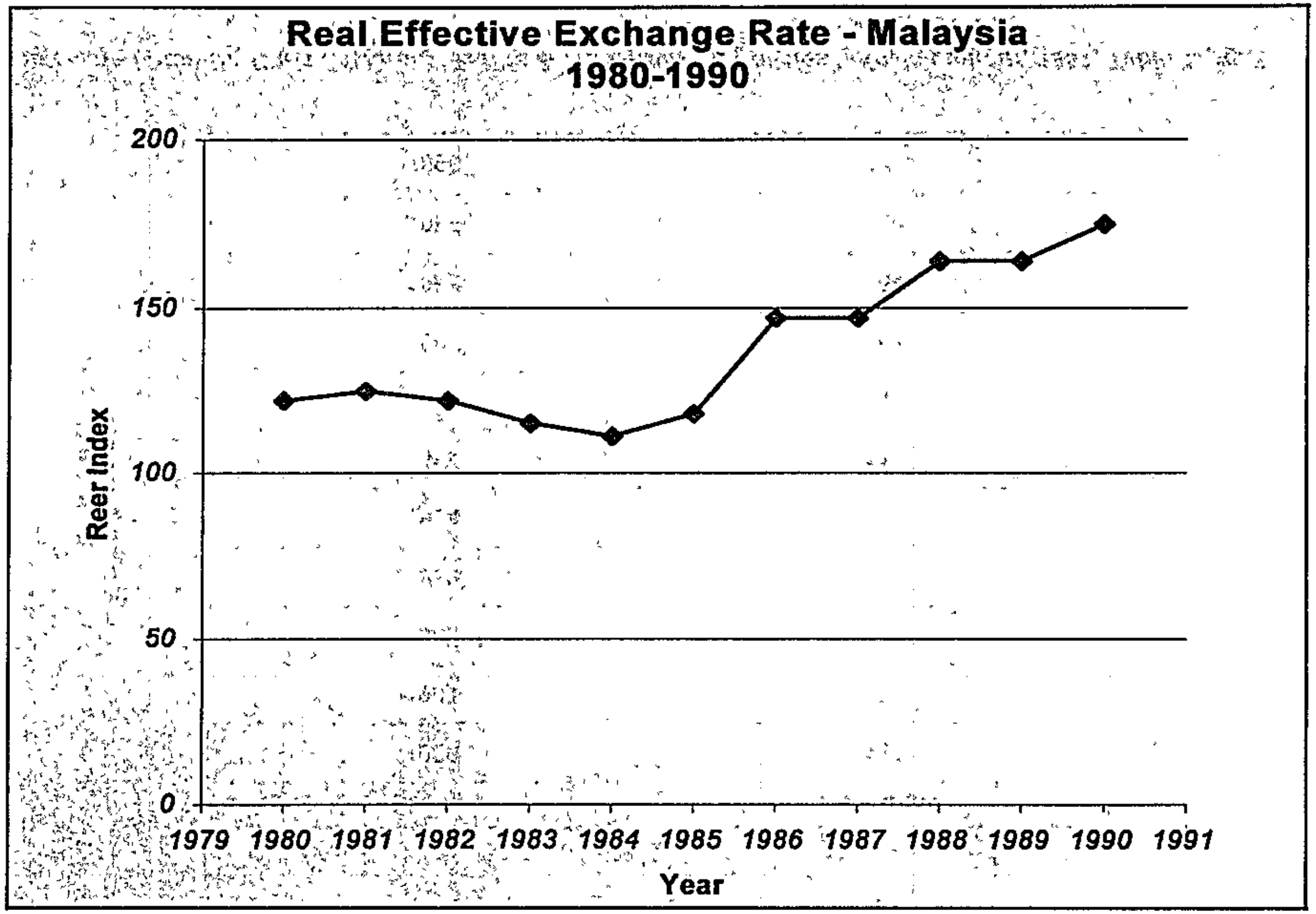
EXHIBIT 2(a)

REAL EFFECTIVE EXCHANGE RATE – MALAYSIA
1980 – 1990

Year	Reer Index
1980	122
1981	125
1982	122
1983	115
1984	111
1985	118
1986	147
1987	147
1988	164
1989	164
1990	175

Source: *Recalculated from Dr. Chris Edwards, "Tariffs & Trade-Related Policies", Kuala Lumpur, 1991, Table 4, pg. 8*

EXHIBIT 2(b)



Source: *Recalculated from Dr. Chris Edwards, "Tariffs & Trade Related Policies", Kuala Lumpur, 1991, Table 4, pg. 8.*

EXHIBIT 3

CHANGES TO THE FOREIGN EQUITY CONDITION IMPOSED ON THE MANUFACTURING LICENCE UNDER THE INDUSTRIAL COORDINATION ACT, 1975

CHANGES TO THE FOREIGN EQUITY CONDITION IMPOSED ON THE MANUFACTURING LICENCE UNDER THE INDUSTRIAL COORDINATION ACT, 1975

	Foreign Equity Condition
Up to 1984	Foreign equity ownership of **up to 70%** allowed for capital intensive, resource processing and export orientated industries
From 1986	a) Foreign equity ownership of **up to 80%** allowed for manufacturing companies **exporting 80% or more** of its products Foreign equity ownership of above 80% will be granted only on a case-to-case basis. b) Foreign equity ownership of **up to 50%** allowed for manufacturing companies that produced high tech or priority products **for local market** This condition was applicable only for new projects approved until 1994 (The foreign equity ownership was **increased to 100%** from January 1995)
1 October 1986	Foreign equity ownership of **up to 100%** allowed for manufacturing companies if a) **50%** or more of its products are exported, and at least **350 employees** are under its employ, and b) Products sold do not compete with those in the local market These conditions were initially applicable for new projects approved until 31 December 1990 (The above conditions were further extended until 31 December 1991)
From 1987	Foreign equity ownership of **up to 100%** allowed for manufacturing companies exporting **up to 80% or more** of its products [including sales to Free Trade Zones (FTZs) and Licenced Manufacturing Warehouses (LMWs)]
From January 1992	Foreign equity ownership of **up to 100%** allowed for manufacturing **exporting more than 50%** of its products, if a) Investment in fixed assets (excluding land) is 50% or more of total assets, or project has at least 50% value added, and b) Products sold do not compete with those in the local market (These conditions were abolished in January 1995)
From 1 July 1993	Sales to FTZs and LMWs no longer considered as export
From July 1998	Foreign equity ownership of up to 100% allowed for new manufacturing projects or expansion of existing manufacturing projects (excluding 7 specific industries)

Exhibit 3
Changes to Manufacturing Licence and Foreign Equity Ownership
Page 2

Manufacturing Licence (ML)

The level of exemption from the requirement for a **Manufacturing License** under the ICA was increased from RM250,000 and 25 full-time employees (in 1975) to **RM1 million** and **50 full-time employees (in 1986)**

The level of exemption was further increased to **RM2.5 million** and **75 full-time employees in 1987** This level is still applicable

This allowed more companies to be outside the scope of the ICA (**The ICA was seen as restrictive especially the requirement for local equity**, etc for manufacturing companies under the ICA supplying to the local market)

Source Malaysia Industrial Development Authority (MIDA), MALAYSIA Investment in the Manufacturing Sector (Policies, Incentives and Facilities) (Various years)

EXHIBIT 4

CHANGES TO THE TAX EXEMPTION CONDITIONS OF PIONEER STATUS, INVESTMENT TAX ALLOWANCE AND REINVESTMENT ALLOWANCE OVER THE YEARS

EXHIBIT 4

CHANGES TO THE TAX EXEMPTION CONDITIONS OF PIONEER STATUS, INVESTMENT TAX ALLOWANCE AND REINVESTMENT ALLOWANCE OVER THE YEARS

Pioneer Status (PS)	
Before 1 January 1986	PS of 100% for **5 years only**
After 1 January 1986	PS of 100% can be extended **another 5 years**.
After March 1988	Extension of PS for another 5 years, given at the end of 5 years, if the company has: a) Fixed Assets (excluding land) of at least RM25 million, or b) Employs at least 500 full-time employees, or c) Other requirements stated by authorities
After 1 November 1991	PS **reduced from 100% to 70%** and limited for **5 years only**.
From January 1995	PS of 85% for 5 years for projects located in the "Eastern Corridor"* of West Malaysia, Sabah and Sarawak
Investment Tax Allowance (ITA)	
January 1986	ITA up to 100% of qualifying capital expenditure for **5 years**
After 1 November 1991	ITA **reduced to 60%** of qualifying capital expenditure for 5 years
From January 1995	ITA up to 80% of qualifying capital expenditure to offset against 85% of statutory income for projects located in the "Eastern Corridor"* of West Malaysia, Sabah and Sarawak
Reinvestment Allowance (RA)	
1986	RA up to 25% of qualifying capital expenditure incurred for expansion purposes until 31 December 1988
1 January 1988 – 31 December 1990	RA **increased to 40%** of qualifying capital expenditure incurred for expansion purposes
From March 1991	RA of 40% extended until 31 December 1995
From 1 January 1995	RA **increased to 60%** of qualifying capital expenditure incurred for expansion purposes.

Source: Malaysia Industrial Development Authority (MIDA), MALAYSIA Investment in the Manufacturing Sector (Policies, Incentives and Facilities) (Various years)

* The "Eastern Corridor" of Peninsular Malaysia covers the states of Kelantan, Terengganu, Pahang and the district of Mersing in the state of Johore