1. Introduction

Malaysia is one of the few countries in the Asia Pacific region that has not implemented a national competition policy. This is surprising given the importance of the private sector as an engine of growth in the country. The Malaysian government began implementing a privatization program in the early 1990s. This was sometimes accompanied by market liberalization in selected markets. Despite such initiatives, most economic sectors remain heavily regulated. Competition policy has not been taken seriously as an alternative to regulation even though there were some early efforts to introduce competition policy elements in sectoral regulations such as in the telecommunications sector.

One of the main reasons why Malaysia has been rather cautious about implementing a national competition policy is the extensive use of industrial policy in the country. Much of the past and present successes of the Malaysia economy have been credited to a series of industrial policies in Malaysia since the 1960s. There is a fear amongst some policy makers in the country that competition policy is in conflict with some of the important existing industrial policies.

A few interesting questions to consider include:

- What are some of the industrial policies that are perceived to be incompatible with a competition policy?
- In what way would such industrial policies conflict with a competition policy?
- If such conflicts are real, how should a competition policy be implemented to mitigate such problems?

We explore these issues in the rest of this short paper. Section 2 briefly discusses the state of competition policy in Malaysia. Section 3 examines the types of industrial policies that have been implemented in Malaysia and their impact on
competition. Section 4 discusses the possibility of reconciling industrial policy with competition policy in Malaysia.

2. Competition Policy in Malaysia

Malaysia does not have a national competition policy. What exists is competition policy at the sectoral level. Only two sectors have made some legal provisions in this area, namely in the energy and communications sectors. The institutional framework and structure in the communications sector is more advanced – the regulatory commission has actually issued guidelines related to competition policy related issues and have even made a public determination on dominant firms. However, significant enforcement problems remain. Initiatives to implement a national competition policy in Malaysia have been made since 1991. However, to date, the implementation of such a policy remains elusive, due to bureaucratic and possibly, political resistance. Much of this resistance comes from the perceived conflict between competition policy and the existing industrial policies in Malaysia.

3. Industrial Policies in Malaysia

There are major four types of industrial policy in Malaysia, each characterized by the different objectives:

(i) Wealth redistribution industrial policy – that is aimed at ensuring a fair distribution of wealth amongst the different races in the country.
(ii) Export promotion industrial policy – that is aimed at promoting the development of manufacturing industries serving foreign markets.
(iii) Import substitution industrial policy – that is aimed at promoting the development of manufacturing industries serving domestic markets.
(iv) Response to globalization industrial policy – that is aimed at coping with new competition from large foreign firms in the domestic (primarily services) markets.

3.1 Wealth Redistribution Industrial Policy

Malaysia experienced racial riots in 1969. In response to this event, the Malaysian government implemented the *New Economic Policy* (NEP) in 1970 with the objective of eradicating poverty and rectifying the unequal distributing of wealth among the
different races. Even though NEP originally covered a twenty year period, it has since been renewed under successive policies. Today, affirmative action-type policies continue to affect current economic policies such as ownership control (e.g. under Industrial Coordination Act 1975) and government-related contracts.\textsuperscript{1} The purpose of the Act was to ensure that firms complied with NEP guidelines on ownership and employment. In implementing this type of industrial policy, the government accord preferences to businesses (e.g. in government procurement) based on criteria other than market competition. As such, it is perceived to be in conflict with competition policy. One may argue that such practices affect only business dealings involving the government; that private sector ventures would not be affected. However, this argument may not be valid because firms may gain competitive advantages initially via government-related dealings.

3.2 Export Promotion Industrial Policy

Malaysia has implemented export promotion industrial policies extensively for more than 40 years. This has assumed the form of the granting of tax incentives and holidays, the establishment of export processing zones and industrial areas. One could argue that competition policy is chiefly about competition in domestic markets. If this view is correct, export promoting industrial policy would be consistent with competition policy and policy makers should not worry about any possible conflicts between these two types of policies.

3.3 Import Substitution Industrial Policy

Malaysia has implemented at least two waves of import substitution policies. The first wave in the 1960s targeted at encouraging the development of light industries such as paint, food and clothing. In the second wave, which began in the early 1980s, the focus was on the development of heavy industries such as the steel and car industries. The two big projects related to this are - Proton (car) and Perwaja (steel). This type of industrial policy is being implemented via targeted government investments accompanied by tariff protection (e.g. import duties), import restrictions and sometimes government procurement favouring locally produced products. The second wave of import substitution, which is still on-going, does lessen competition in

\textsuperscript{1} Under ICA 1975, manufacturing firms with RM2.5 million or more shareholder funds or with 75 or more employees are required to apply for operating license from the Ministry of International Trade and Industry.
the affected sectors. For example, imported cars incur import duties and excise duties while Proton gets a large rebate on excise duties. Given the substantial public investments in projects under the present import substitution policy, it is unlikely that the Malaysian government will abandon the policy overnight. Recent developments (such as changes in ownership structure and the search for joint-ventures with foreign partners) indicate a gradual withdrawal from the policy. The implication of this development for competition policy is that any competition policy that will be introduced should allow for such restructuring processes. Otherwise, the competition policy itself might not be implemented at all. This indicates the importance of time-bound exemptions in Malaysia’s future competition policy.

3.4 Response to Globalization Industrial Policy

The opening of domestic markets to foreign entry and competition, particularly the services sector, has been a major area of concern for policy makers in recent years. Some of these developments are related to Malaysia’s commitment under the WTO e.g. the financial sector. One salient response to these developments has been the government’s encouragement of industry consolidation. In 2000, Bank Negara Malaysia, the central bank, announced a consolidation plan for the financial sector that would reduce the number of financial institutions from 56 to just 10 ‘anchor banks’.\footnote{In an earlier announcement, in July 1999, the central bank proposed a consolidation that would leave only six anchor banks.} The decision affected 23 commercial banks, 16 merchant banks and 17 finance companies. The main objective was to enhance the competitiveness of locally owned financial institutions in anticipation of increased competition from foreign-owned financial institutions; under its WTO commitments, Malaysia had agreed to liberalize the sector by 2003. Such policies have significant impact on competition. It is imperative that Malaysia implements a competition policy that will monitor this industry that has become very concentrated. Furthermore it is not the function of a central bank to monitor and ensure competition in the banking sector.

4. The Way Forward: How Should Malaysia Implement a Competition Policy?

Several challenges lie ahead in implementing a national competition law in Malaysia. First, the government will have to reverse the devolution of competition regulation to sectoral regulators, who are likely to resist any such efforts at centralization. It will
also need to convince existing national-level regulators – such as the Securities Commission, which regulates mergers and acquisitions of companies listed on the Kuala Lumpur Stock Exchange – of the need for a new agency to regulate competition-related issues.

Second, competition policy may come into conflict with existing industrial and socioeconomic policies, such as selective import substitution, bank consolidation and wealth redistribution policies. Accommodating all these policies, with their varying objectives, exemptions and authorizations, is likely to be an important element in Malaysia’s proposed competition policy and law. In this regard, the government will need to be mindful that too many exemptions may weaken competition regulation and make it vulnerable to regulatory capture. When unavoidable, exemptions should be time-bound and gradually removed over time.

Third, given the extent of resistance to the implementation of a national competition policy, some compromise in the content of the policy may need to be made. One example is merger controls – and in particular whether pre-notification of proposed mergers would be necessary. India has chosen to do away with pre-merger notifications, and Malaysia might follow its example. Another way of making competition policy more palatable might be to orient it more towards conduct than market structure, an experience that was observed in Europe earlier.

Fourth, a sequenced approach to the implementation of competition policy, as in India, would probably be appropriate for Malaysia. Almost all the competition-related problems discussed in this chapter were not perceived as such by the government or the public. This indicates that competition policy advocacy will remain an important area of activity for years to come.