Boosting productivity is key for Malaysia to attain high-income-country status

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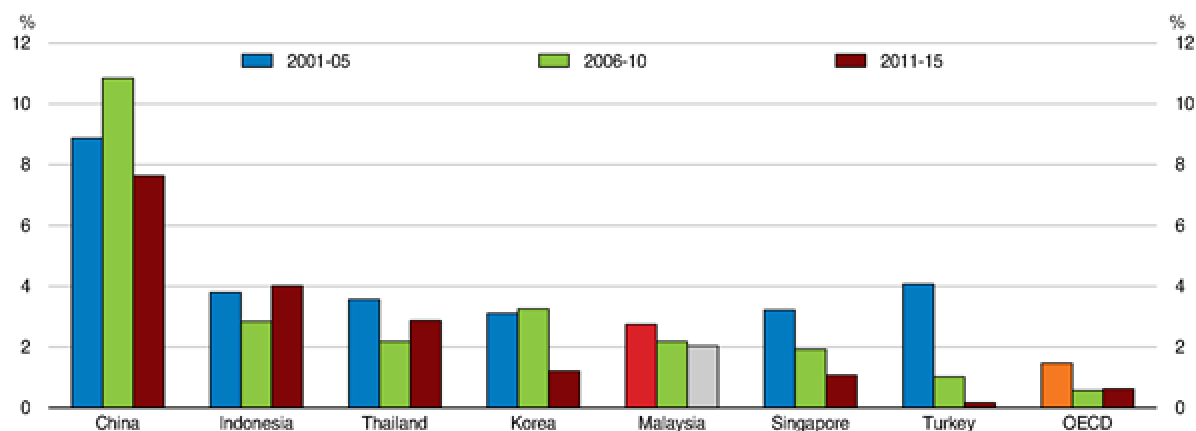
Productivity growth is essential for living standards to durably improve. Malaysia has reached a development stage where growth needs to be driven more by productivity gains than the sheer accumulation of capital and labour inputs. The 11th Malaysia Plan (2016-20) sets an ambitious labour productivity growth target of 3.7% per year, well above than the 2% average growth recorded from 2011 to 2015 (Figure 1). The first OECD Economic Assessment of Malaysia calls for coordinated structural reforms to achieve the productivity improvements needed for Malaysia to attain high-income-country status.

Figure 1. Labour productivity growth has declined

Average of growth of real value added per employee per year



Note: The underlying employment data for Malaysia might underestimate the number of legal and undocumented foreign migrant workers.

Source: OECD calculations based on data provided by national statistical office and OECD (2016), Productivity Statistics (database), http://dx.doi.org/10.1787/data-00685-en.

To boost productivity, three priority areas for further reform stand out.

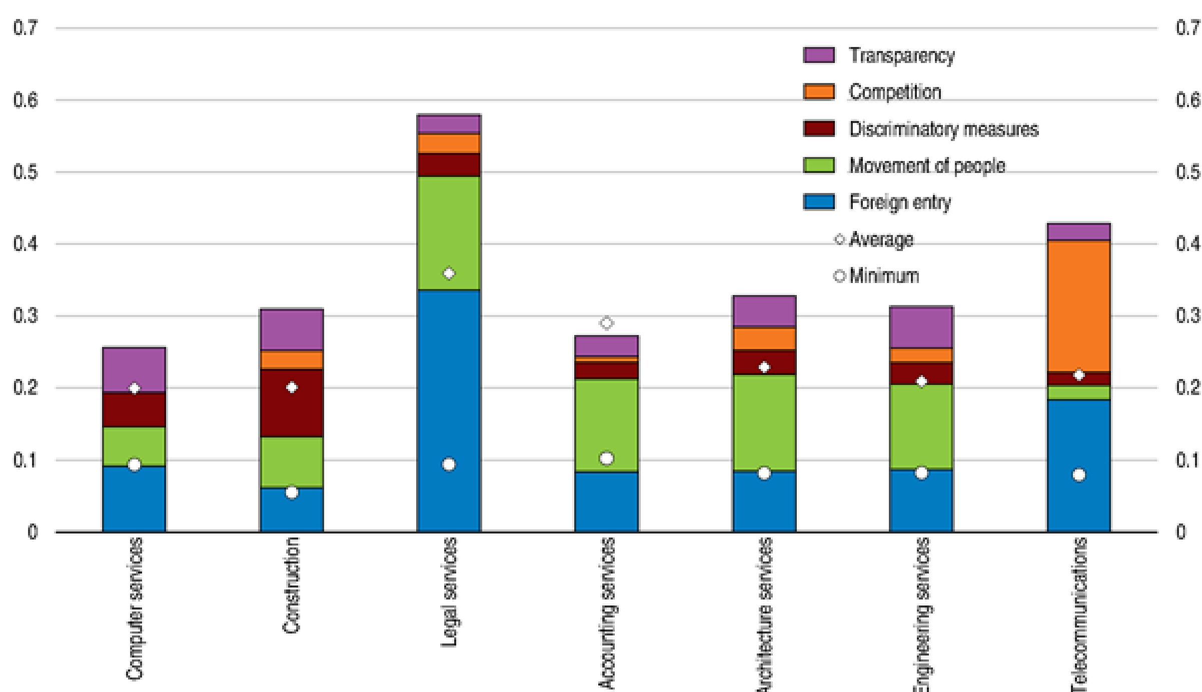
First, enhancing the quality of education is critical to increase the availability of skilled workers and improve Malaysia's attractiveness for investment in higher value-added activities. Improvement in teachers' evaluation, training and upskilling is necessary to raise basic education outcomes. Enrolment in tertiary level education has expanded, but graduates often lack the skills required by industry. To narrow the skills mismatch in the labour market, more focus should be put on vocational education and training.

The second priority is improving the regulatory framework. Malaysia's efforts to create a more business-friendly environment through regulatory reform resulted in the country ranking 18th in the World Bank's Ease of Doing Business 2016. But observation of OECD best practice suggests Malaysia could do even better. Implementation of competition policy could be strengthened further by enhancing the independence and funding

of the regulator. Productivity could be boosted by facilitating the entry of innovative firms and the exit of unproductive ones. With this in mind, a key recommendation is the reform of rigid bankruptcy laws in line with OECD standards.

Thirdly, further investment liberalisation will also boost growth in the services sector and enhance competitiveness. Indeed, a set of indicators measuring restrictions to services sector trade (the OECD's Services Trade Restrictiveness Index – STRI) was computed for the first time for Malaysia, revealing that the country has more restrictive regulations than the average of OECD member countries and major emerging economies (Figure 2).

Figure 2. The STRI for selected sectors



Note: The STRI indices take values between zero and one, one being the most restrictive. They are calculated on the basis of the STRI regulatory database which contains information on regulation for the 34 OECD Members, Brazil, China, Colombia, India, Indonesia, Latvia, Malaysia, Russia and South Africa. The STRI database records measures on a Most Favoured Nations basis. Preferential trade agreements are not taken into account.

Source: OECD (2016), Services Trade Restrictiveness Index.

Reference

OECD (2016), *OECD Economic Surveys: Malaysia 2016: Economic Assessment*, OECD Publishing, Paris.