

**Asian RCI Roundtable Conference :**  
**Session 4: How Can RCI Help**  
**Middle-Income and High-Income**  
**Aspirants?**

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# Background

- Sustained growth and poverty reduction have pushed more and more Asian economies into middle income level transition. This transition to middle income opens a new set of development challenges.
- Meanwhile, many economies that have managed to quickly reach middle-income status, face the risk of falling victim to a slowdown in productivity and growth.

# Productivity Challenges of Middle Income and High Income Aspirants

- Transition from low to middle income initially driven by factor accumulation and labor reallocation
- But many developing countries are unable to sustain growth in productivity:
  - Productivity gains from factor accumulation eventually reach their limit;
  - Inability to sustain gains in exports, FDI, and employment, once labor costs rise or preferential market access disappears; and
  - Inability to capture, over time, technological spillovers from FDI, due to lack of absorptive capacity, weak backward and forward linkages, supply-side constraints, inadequate policy support, or the predominance of low-skill assembly-type activities

# Addressing the Challenges and the Potential Role of RCI

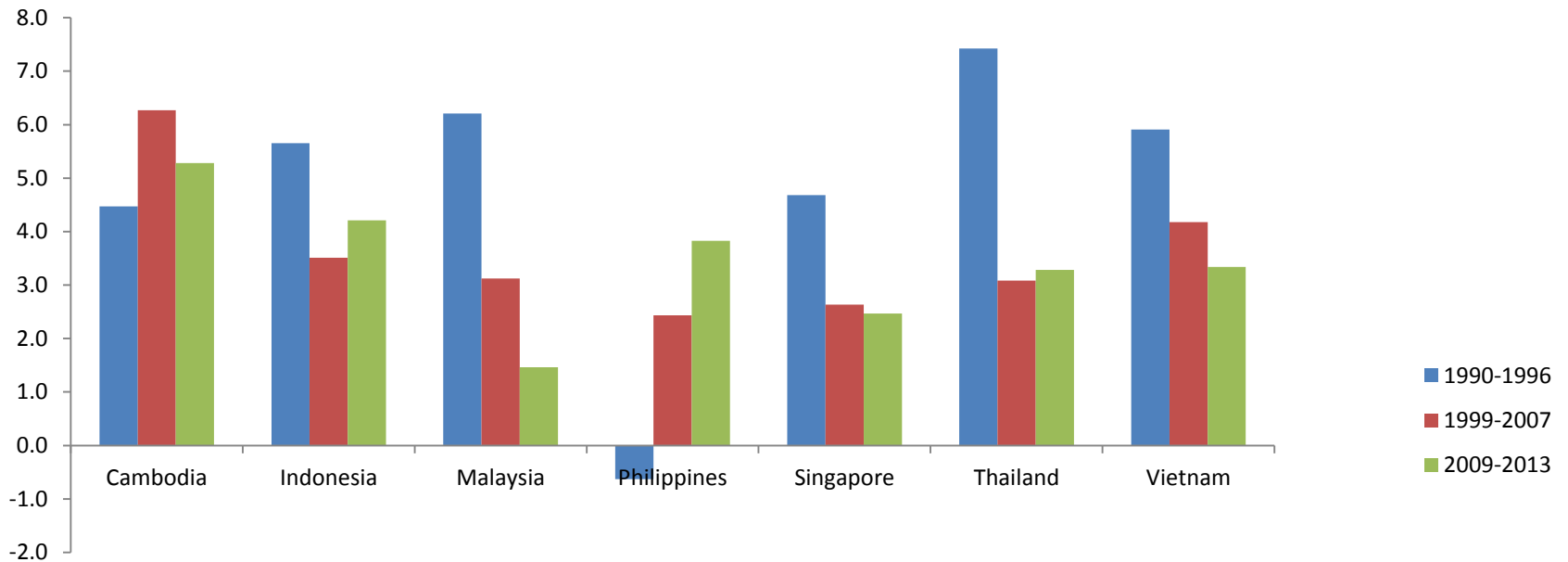
- To sustain productivity and economic growth, need to move away from productivity driven by factor accumulation, to productivity underpinned by sectoral diversification, innovation, and improvements in the quality of human and physical capital
- RCI can help change the pace of structural change, spur innovation, and potentially drive a shift from low- to higher-productivity sectors
- RCI can also help address other challenges that could affect long-term productivity and growth, including rising inequality, and shared vulnerabilities

# Research Questions

- How can RCI help middle-income and high-income aspirants?
  - What are the development challenges of middle-income and high-income aspirants?
  - How are the factors that affect middle-income aspirants different from high-income aspirants?
  - What role can RCI play in addressing the challenges in these countries by driving growth and productivity?
- Session will look at two case studies: Cambodia and Malaysia

# SE Asia Labor productivity growth

SE Asia: Labor productivity growth (%)



# Cambodia: Background and Main Challenges

- Growth has averaged about 7% per annum, faster than almost any other post-conflict society
- Per capita GNI reached \$950 in 2013, now on the threshold of becoming a middle-income country
- Key challenges:
  - Sandwiched between giants and in the center of ASEAN
  - Small domestic market with potential scale economies from integration
  - Economy narrowly based and externally dependent
  - Various supply-side constraints which limit competitiveness
  - Vulnerability to shocks due to high degree of openness

# Key Messages: Cambodia Case Study

- How can trade and FDI drive productivity growth?  
Focus on two high growth, internationally oriented sectors: garments and tourism
- How can RCI address supply-side constraints to competitiveness and productivity growth?  
Focus on infrastructure investment, trade facilitation, and skills development under the GMS program



# The Importance of Garments and Tourism in Cambodia

- Garments and tourism now generate about 70% of the country's exports of goods and services.
- In 2012, garment exports totaled \$4.2 billion, while tourism receipts were \$2 billion.
- Garments and tourism are the most important sources of non-agricultural employment, providing jobs for about one-seventh of the workforce.
- Garments employs about 400,000 workers and tourism about 620,000, out of a total workforce of approximately 7 million.

# Garments as a Driver of Productivity Growth in Cambodia

- Key challenge in garments: How to maintain dynamism as wages rise and competition from other low-wage economies intensifies
- Policy actions:
  - Improve efficiency of logistics and utilities provision, especially electricity costs
  - Improve regulatory regime for import-export, and port access
  - Broaden the industry's base, with greater emphasis on skills, both at the level of basic education and specialist knowhow

# Tourism as a Driver of Productivity Growth in Cambodia

- Key challenge in tourism: Industry is highly competitive and quite volatile; some criticism regarding its “enclave” nature
- Policy actions:
  - Preserve environmental amenities;
  - Maintain domestic peace and security;
  - Further developing tourism-support infrastructure— including hotels, transport, guide facilities.

# The Role of RCI in Addressing Supply-Side Constraints

- Key challenge: Several supply-side constraints render Cambodia much less competitive on ‘behind-the-border’ infrastructure and logistics services
- RCI can help address some of the constraints. Some noteworthy initiatives include:
  - The ASEAN Economic Community : Pillar 1 strategic actions. NSW
  - GMS: Physical infrastructure projects, primarily in the transport and energy sectors; Cross-Border Transport Agreement (CBTA); and Strategic Framework for Action on Trade Facilitation and Investment
  - Transport and trade facilitation reforms as part of accession to the WTO, or as a party to FTAs signed by the ASEAN

# Malaysia: Background and Key Challenges

- Development story often hailed as a model of FDI-driven, export-led industrialization
- More recently, references to Malaysia tend to highlight it as a classic case of the “middle income trap”
- Key Challenges:
  - Falling competitiveness in labor-intensive manufacturing activities and exports, due to factor price adjustments
  - Unable to move up the value chain to more sophisticated activities within manufacturing and services
  - Private investment never recovered after the Asian Financial Crisis
  - Development outcomes remain highly uneven across states

# Key Messages: Malaysia Case Study

- Most challenges require national actions, but RCI can still play a role
- How can trade and FDI drive productivity growth? Support upgrading within regional production networks
- How can RCI address inter-regional income inequalities? Through sub-regional initiatives such as the Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA), and the Indonesia-Malaysia-Thailand Growth Triangle (IMT-GT).

# Supporting Upgrading through Production Networks (1)

- Key challenge: Malaysia remains a key player in global production networks, but after several decades, still weak domestic linkages and a concentration on low-skilled assembly type activities have constrained growth in domestic value-added.
- The most commonly cited factor, among a number, is a skills mis-match
  - Greater investments in appropriate skills, and R&D
  - Better enabling business environment, including lesser government involvement in government-linked corporations (GLCs) to revive domestic investment, spur innovation, and strengthening internal competition

# Addressing inter-regional income inequalities through RCI

- Key challenge: Malaysia's affirmative action policies have been distortionary; they have also promoted a culture of dependence on state handouts, as well as rent-seeking behavior
- Engaging in RCI initiatives to address inter-regional inequality may produce better results
- There is some evidence to suggest that IMT-GT and BIMP-EAGA have affected development outcomes and narrowed development gaps in Malaysia- need rigorous impact studies.



# IMT-GT Results: Poverty and Per Capita GDP

Poverty incidence in Malaysia GT by state (% , 2004–2012)

Sub-region	2004	2007	2009	2012
Malaysia	5.7	3.6	3.8	1.7
Malaysia-GT	<b>4.2</b>	<b>2.4</b>	<b>2.3</b>	<b>1.0</b>
Melaka	1.8	1.8	0.5	0.1
Kedah	7.0	3.1	5.3	1.7
Kelantan	10.6	7.2	4.8	2.7
Negeri Sembilan	1.4	1.3	0.7	0.5
Penang	0.3	1.4	1.2	0.6
Perak	4.9	3.4	3.5	1.5
Perlis	6.3	7.0	6.0	1.9
Selangor	1.0	0.7	0.7	0.4

Notes: Poverty incidence is the proportion of the population whose income falls below the national poverty line. Poverty incidence of Malaysia GT is not based on country submission but estimated using the proportion of derived magnitude of poor population to the total population (2007-2012) and average of the states' estimates (2004).

Source: IMT-GT Statistical Figures and Trends

Real per capita gross domestic product of Malaysia-GT by state (at constant 2005 prices, \$, 2005–2012)

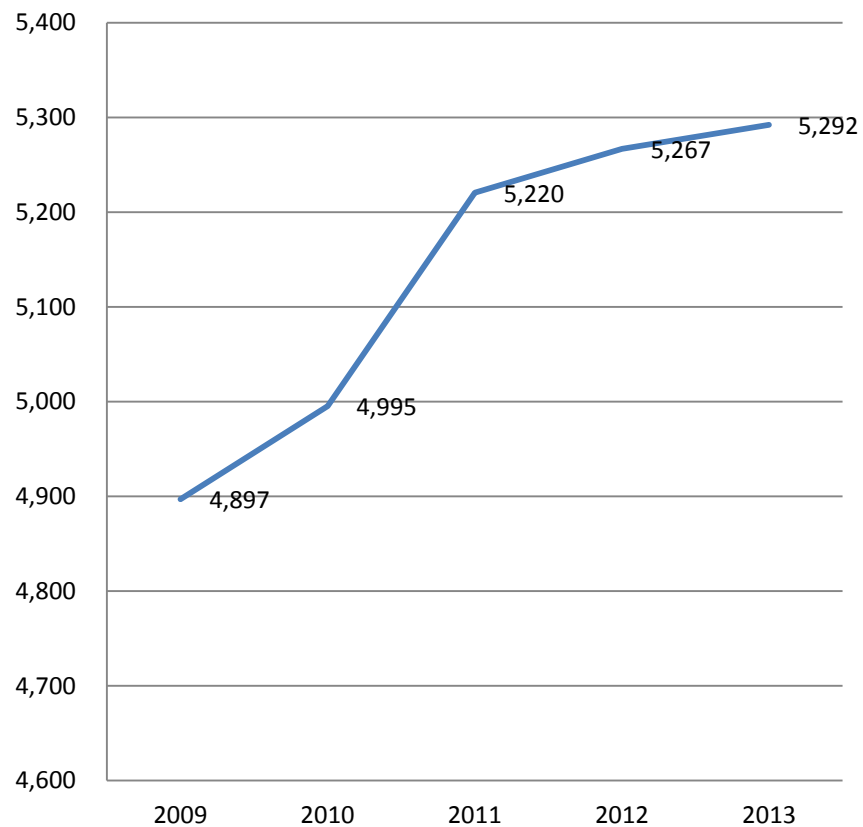
Sub-region	2005	2006	2007	2008	2009	2010	2011	2012
Malaysia	5,511	5,893	6,559	6,955	6,364	7,348	7,999	8,242
Malaysia-GT	<b>4,688</b>	<b>5,074</b>	<b>5,689</b>	<b>6,144</b>	<b>5,597</b>	<b>6,599</b>	<b>7,225</b>	<b>7,507</b>
Melaka	5,390	5,898	6,558	6,921	6,488	7,422	8,033	8,433
Kedah	2,586	2,841	3,265	3,346	3,108	3,504	3,955	4,107
Kelantan	1,604	1,746	1,994	2,167	2,067	2,341	2,578	2,644
Negeri Sembilan	5,484	6,076	6,708	7,095	6,655	7,592	8,239	8,428
Penang	7,085	7,972	8,918	9,543	7,964	9,488	10,211	10,460
Perak	3,253	3,535	3,916	4,250	3,938	4,512	5,030	5,287
Perlis	3,390	3,578	4,042	4,234	3,856	4,369	4,657	4,788
Selangor	6,163	6,496	7,272	7,959	7,292	8,788	9,605	10,012

Note: Values are computed from derived per capita GDP in RM and official US\$-RM exchange rates.

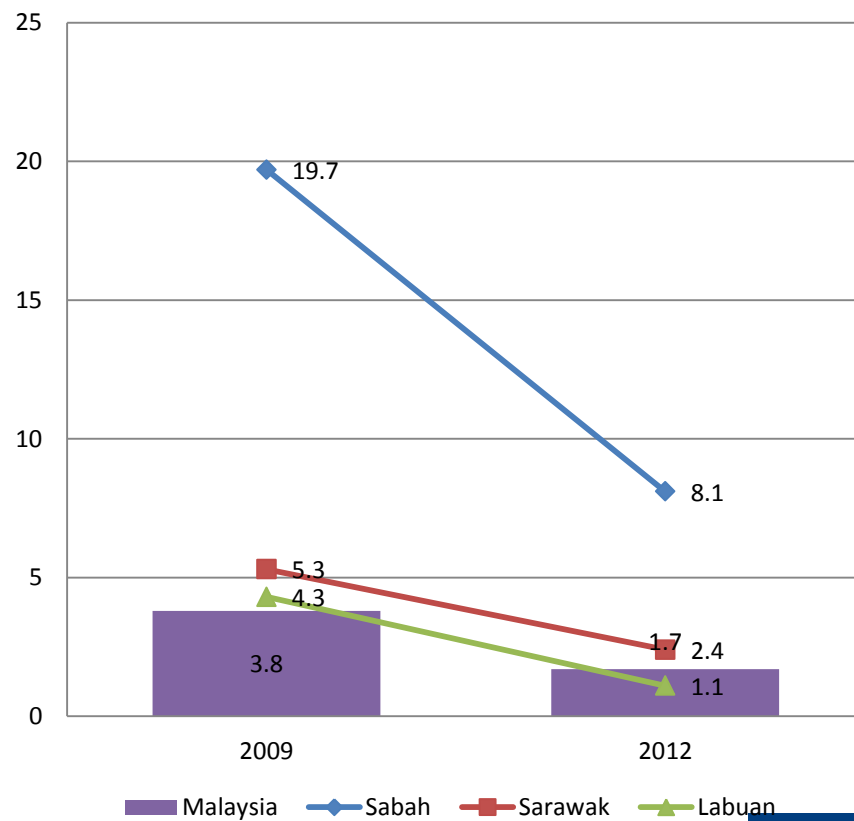
Source: IMT-GT Statistical Figures and Trends

# BIMP-EAGA Results: Poverty and Per Capita GDP

Real GDP per Capita in Malaysia-EAGA, 2009–2013



Poverty incidence in Malaysia-EAGA, 2009 and 2012



Source: Preliminary Statistics, BIMP-EAGA Database (forthcoming)