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# **Frozen Identities. Inter-Ethnic Relations and Economic Development in Penang, Malaysia**

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## **Abstract**

Identity formation is probably one of the most discussed aspects of strategic positioning within anthropology, sociology and political science. In general notions of identity have been based on either an absolutist or primordial understanding of belonging or a constructionalist view in which social and political positioning in terms of identity formation are governed by a given societal context. This paper bases its understanding of identity formation on the latter approach. This means that depending of context individuals have several different although related identities to choose between when manoeuvring in a complex and dynamic social environment. Identity formation, achieved or ascribed, and its various forms of externalisation are thus negotiated and not absolute. The dynamic behind this notion of identity formation is individual agency strategically manipulating social, economic and political positioning in a given societal setup. To illustrate the complexities and in this case negative ramifications of social engineering the article focuses on inter-ethnic relations and industrial development in Penang, Malaysia.

**Keywords:** *identity formation, inter-ethnic relations, industrialisation, nation building, Penang, Malaysia*

## Introduction

The ethnic composition between the three main ethnic groups in Malaysia, the Malays, the Chinese and the Indians, can in 2006 be delineated as follows<sup>1</sup>:

	Malaysia	Penang State
<b>Malays</b>	56 %	40 %
<b>Chinese</b>	31 %	43 %
<b>Indian</b>	7 %	10 %
<b>Others</b> (including Orang Asli)	6 %	7 %

Since the introduction of the New Economic Policy (NEP) in 1971 this inter-ethnic setup has since 1971 been locked in a negative triangulation. A driving force behind this can be defined as a positive discrimination of the Malays in comparison to the other two ethnic groups. This has resulted in a hardening of ethnic borders thus making social mobility across ethnic boundaries rather difficult. Processes of identity formation are therefore closely following ethnic borders. Due to this state of affairs the most wealthy and best educated ethnic group, the Chinese, are not getting the most attractive jobs within neither the top echelons of the state bureaucracy nor in academia thus leaving Malaysia altogether for better job opportunities abroad. The same goes for young Chinese graduates who aspire to pursue a university degree. In both cases Malays are getting the most attractive jobs and most of the government grant for taking up studies at the universities. Because of their ethnically determined positioning at the bottom of the society the majority of Indians are facing tremendous problems moving up the social system,

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<sup>1</sup> <http://en.wikipedia.org/wiki/Penang>

as they have neither the wealth nor education to do that. In other words all three ethnic groups are locked in their respective ethnically defined cages.

The main consequences of this negative ethnic triangulation are that the most important jobs within the state bureaucracy are not necessarily manned by the best educated, and the students at the universities are not necessarily the best qualified due to the politically designed preferential treatment of the Malay. Perhaps the most serious consequence of this is that it has denied Malaysia the freedom of manoeuvre as a nation. This is so much more problematic as Malaysia is facing a serious economic problem now that the current global economy is contracting due to the financial and economic crisis. For Penang in particular this has meant that the main economic players, the multinational companies (MNCs), in the high-tech sectors of the industrial setup have threatened to move to other countries, for example, Vietnam, that can offer lower production cost than Penang. This means that if Penang is to uphold its position as a regional high-tech hub then it has to move up the value chain by making the 250 plus MNCs in the high-tech business move their R&D departments to Penang. The possibility for doing so is there due to a highly developed industrial infrastructure and an investor friendly government, but the problem is, however, that a complex state bureaucracy is taking a heavy toll on an effective handling of business matters. The same goes for the production of university graduates for the R&D heavy high-tech and bio-tech industries. Put together these two main factors seem make the MNCs reconsider their position in Penang. As indicated above one of the main reasons behind these serious problems are the politically designed preferential treatments of Malays thus choosing ethnic belonging over the best qualified individuals regardless of ethnic background. Even though the political establishment has maintained several times that the preferential treatment of the Malays is to be phased out and all citizens of Malaysia regardless of ethnic belonging is to be perceived as Malaysian per se the preferential system is still very much in place. The political cost of dismantle it

seems to be too high for the Malays. Basically the reluctance of initiating such a change jeopardizes the overall strategy of moving Penang up the value chain. The frozen ethnic boundaries and thus locked mode of identity formation constitute a kind of lid on the economic development in this the fourth largest contributor to the national Malaysian GDP.

In the following the article focuses on the ethnic Chinese SMEs within the high-tech sector. They are to constitute a counter study towards the general perception of the Chinese as an ethnic group that perceives the latter as a coherent, intra-ethnically oriented as well as more or less homogeneous group.<sup>2</sup> The article takes a global economic perspective of the Chinese thus introducing a more complex view stressing that the Chinese entrepreneurs are more inter-ethnic rather than intra-ethnic oriented economic players.<sup>3</sup> This way of perceiving the Chinese Malays demonstrates that the general perception is based on a politically motivated social engineering that is to reinforce an ideationally designed multicultural image of Malaysia which basically is to legitimise a perpetuation of the current preferential treatment of the Malay majority.

### **On the Economic set-up in Penang**

When discussing the economic development of Penang one has to distinguish between prior and post 1971. In pre-1971 Penang was mainly an agricultural economy complemented by government initiated import substitution schemes. This was to ensure that the local economy could stay independent and produce enough for local consumption. As there were no manufacturing companies and that the British owned companies in mainly the trading and plantation sector did not restore

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<sup>2</sup> Gomez (2002), Gomez and Benton (2004), Boulton (2005), Yeung (1999).

<sup>3</sup> Jacobsen (2006), Yen Ching-Hwang (2002), Tan Chee-Beng (2004), .

their operations to the pre-war level after WWII, unemployment was rather high during that period.

After 1971 things changed quite rapidly. The southern part of the island became highly industrialised and has over the years attracted more than 250 MNC high-tech electronic plants such as Dell, Intel, AMD, Altera, Motorola, Agilent, Hitachi, Osram, Plexus, Bosch, Fairchild and Seagate, most of which are mainly located within the Bayan Lepas Free Industrial Zone, which was set up in 1972. Based on the MNCs, Penang has thus concentrated mainly on information and communication technology (ICT), semiconductors, computer and computer peripherals, data storage devices, telecommunications equipment (software) and consumer electronics. To service the MNCs more than 1200 local support industries have sprung up within and outside Bayan Lepas. They are mainly specialised within automation, plastics, precision engineering and metal work, chemical products and packaging of various kinds.

A consequence of these developments has been that today Penang state has the fourth-largest economy in Malaysia, after Perak, Selangor and Johor. Manufacturing is the most important component of the Penang economy, contributing about 43% to the State's GDP.<sup>4</sup> Furthermore, in January 2005 Penang was formally accorded Multimedia Super Corridor Cyber City status, the first outside of Cyberjaya on the Malaysian peninsula, with the aim of furthering the development of high-tech industrial parks that are to conduct cutting-edge ICT research. The latest area of research in Penang to be taken up is the establishment of a biotech park thus leveraging on its industrial infrastructure that has made it Malaysia's foremost electronic hub. It is the expectation that this will poised Penang to take off in the highly promising frontier of biotechnology. This new initiative is in line with the 9<sup>th</sup> Malaysia Plan, which has identified this sector as

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<sup>4</sup> Penang Sustainability 2008.



one of the main areas that is to help drive the country forward towards a developed knowledge economy status as required by the Cyber City status.

In recent years, however, the state is experiencing a gradual decline of foreign direct investments (FDI) due to factors such as cheaper labour costs in Vietnam, China and India, and arguably, lagging human capital in the form of a well educated and up-to-date labour force. Furthermore, the entrepôt trade has declined due in part to the loss of Penang's free-port status in 1969, but also due to the active development of Port Klang near the federal capital Kuala Lumpur. However, the container terminal in Butterworth, on the mainland side of Penang State, is in for a major upgrade as detailed in the Northern Corridor Economic Region developmental plan that were initiated in 2007. The main objective is to service the northern Malaysian region but still cater for the rest of Malaysia in competition with Port Klang.<sup>5</sup> Other important sectors of Penang's economy that is to be upgraded according to this plan includes health tourism, which is mainly clustered in the northern part of Penang Island as well as in Georgetown, together with finance, shipping and a variety of service sectors catering for the industrial development.

### **Penang State Government's Economic Policies and the Chinese SME Community**

In order to counter the above mentioned industrial decline the previous Penang State Government (PSG) under chief minister Tan Sri Dr. Koh Tsu Koon initiated an aggressive economic policy. Owing to limited land size and the highly industrialised nature of Penang's economy, agriculture is given little emphasis in its developmental plans. This comes as no surprise, as agriculture was only contributing about 1.3% to the state GDP in 2000 and there is no prospect of it to

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<sup>5</sup> Lim Wei Seong 2007, <http://en.wikipedia.org/wiki/Penang>.

increase substantially in the years to come. The PSG is thus concentrating on servicing the industrial setup.

Even though Penang got the Multimedia Super Corridor (MSC) status in 2005 the Penang high-tech industry still faces stiff competition from the original MSC on the Malaysia mainland thus threatening its position as Malaysia's 'Silicon Valley'. The up until March 2008 Chinese dominated Gerakan Party that has led the state government since 1969, was well aware of this and took several steps to address this threat. According to Peggy Toe, selling Penang was an important element in the government's industry competitive strategies and in line with the economic prescriptions promoted by both Vision 2020 and MSC for setting-up a new Malaysia. Accordingly, Penang stepped up its plans to become a symbol of this new emerging era (Toe 2003: 554).

In 1992, Penang Development Corporation (PDC)<sup>6</sup> was asked to develop a road map for operationalising the main ideas behind Vision 2020. In drawing on this vision PDC developed the theme 'Penang: Into the 21<sup>st</sup> Century' to outline its goals. It first aimed at diversify Penang's economy by creating a local manufacturing capability that was high-tech based and competitive driven thereby responding to the demands from the various MNCs, and second, to develop a sophisticated service sector buttressed by the 'state-of-the-art' technology and skills, and finally, to modernise and upgrade the dormant productive capabilities in the agricultural sectors.

Besides these initiatives the Penang State Government, strongly supported by the private sector, initiated several projects that laid the groundwork for achieving the

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<sup>6</sup> PDC was inaugurated in November 1969. It still is the main state development agency to help develop, plan, implement and promote socio-economic projects on behalf of the state government. It thus functions as the investment arm of the state government (<http://www.pdc.gov.my/>).

strategies as defined by PDC. For example, two Free Industrial Zones and five industrial parks covering 1,850 ha of land on both Penang Island and Port Wellersley on mainland Penang were developed. Tax incentive schemes were introduced to entice foreign capital. A highly diversified electronics industry and supporting industries in engineering, metal, plastics and packaging for the electronic/electric industry were courted together with industries in the textiles and apparel sectors.

Initially MNCs were attracted to Penang due to its highly qualified labour resource, an efficient transport and communication infrastructure and the existence of an efficient banking and insurance sector combined with well developed freight and forwarding services. Automation was encouraged right from the start in order to keep labour costs down. The Penang State Government was quite supportive of foreign ventures and proved an important facilitator of business. The Penang State was so successful in reinventing itself as a progressive developmental state that manufacturing increased from 13% of GDP in 1971 to more than 50% of the GDP in 2000, employing more than 40% of the total labour force. In June 2000 there were 693 factories in Penang with a paid-up capital exceeding RM 7.3 billion. Of these 37.8% of investments came from overseas investors, the largest being Taiwan followed by Japan, the US and Singapore (ibid 2003: 554).<sup>7</sup> Furthermore, besides providing both tax and non-tax incentive packages for both local SME industries as well as for MNCs the Penang State Government introduced two new economic facilitators to help further develop the industrial setup in Penang, namely investPenang and the Socio-Economic and Environmental Research Institute (SERI).<sup>8</sup>

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<sup>7</sup> Although tourism is the second pillar of growth in Penang this sector will not be discussed in this report due to main topic, which focuses on Chinese SME entrepreneurs. For further readings on the tourism sector, see Peggy Teo 2003.

<sup>8</sup> These economic facilitators will be discussed later on in this section.

Now, before discussing how the various types of economic facilitators and government initiatives have impacted on the Chinese SME business community that constitutes a major part of the industrial setup in Penang and is the main focus of attention in this article, a definition of what is meant by SME is described. Generally, it can be defined into two broad categories<sup>9</sup>:

1. Manufacturing, Manufacturing-Related Services and Agro-based industries:

Small and medium enterprises in the manufacturing, manufacturing related services and agro-based industries are enterprises with full-time employees not exceeding 150 or with annual sales turnover not exceeding RM25 million.

2. Services, Primary Agriculture and Information and Communication Technology

(ICT): Small and medium enterprises in the services, primary agriculture and Information & Communication Technology (ICT) sectors are enterprises with full-time employees not exceeding 50 or with annual sales turnover not exceeding RM5 million.

Based on these framework definitions a characteristic of the Chinese SME community in Penang can be summarised as follows: about 85% of the local industry in Penang can be classified as SMEs, the majority of which are owned by Chinese. During an interview with representatives from the Chinese Chamber of Commerce in the provincial capital Georgetown it was emphasised that the typical Chinese SME is currently undergoing a change. They are not only family run enterprises but are evolving into more complex and diversified entities, the specific characteristics of which depends on the size and constitution of the individual company. The micro or 'Mom and Pap' Chinese SMEs are typically very small

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<sup>9</sup> The following is based on definitions provided by 'Small and Medium Industries Development Corporation' (<http://www.smidec.gov.my/index.jsp>). For further information of the SME community in Penang, please see Penang Economic Monthly. Vol. 9, Issue 4. April 2007.

family owned and run companies that produce a rather narrow range of products. This is especially the case if they are suppliers to major local or foreign companies. The small and medium SMEs constitute a more diversified lot. The most efficient of them has hired professional, not necessarily Chinese, managers to run the business in an 'arm's length' mode, but maintain the control over the business strategies themselves. Interestingly, the development of such strategies is based on generally acknowledged Chinese modes of networking. For example, *guanxi* ways of networking constitute an important strategy thus matching the general stereotype of Chinese business practices.<sup>10</sup>

It is thus possible to divide the Penang Chinese SME community into three main categories: 1. a 'classical' one consisting of 100% family owned and run SMEs (mainly micro SMEs), 2. 100% family owned SMEs that are professionally managed according to 'arm's length' principles, but make use of 'classical' Chinese business strategies and network practices (mainly small and some medium SMEs), and 3. those SMEs that are about 50% or less owned by Chinese entrepreneurs, are professionally, that is, not family managed, and combine 'classical' Chinese strategies and network practices with modern market seeking techniques thus pushing them towards the upper level of the SME category and perhaps into the category of public listed companies (PLC) thus leaving the SME category all together.

There are two main reasons behind this differentiation of the Penang SME community. First and foremost, there is an ever entrenching global market economy that forces structural as well as organisational changes on the companies towards establishing a division of labour between ownership and management and to venture outside the immediate domestic market in order to expand their reach. The second reason for this differentiation is what can be defined as a negative

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<sup>10</sup> Cribb (2000), Jacobsen (2007), Tong and Yong (1998).

tendency towards re-investment in one's own company due to what other observers have defined as a localised mindset that focuses more on profit optimisation than technological and managerial upgrading. This goes especially for the 100% family owned and run companies. This kind of companies is open towards new production avenues that turn them into becoming, for example, suppliers to MNCs but this does not move them up the value chain due to the before mentioned mindset. What, however, all categories of Chinese SMEs share is a kind of openness towards change per se that drives them forward although in different directions. This is, according to representatives from the Chinese Chamber of Commerce, an inherent aspect within the nature of the Chinese business practice, namely openness towards change.

Interestingly, the differences between the three groups of Chinese SMEs are also reflected in their respective network practices. For example, the smaller the SME the more ethnically based their network practices become. As a company moves up the value chain its network practices begin to cross ethnic boundaries and branch out into a non-ethnic related business environment. This has a direct bearing on the degree of linkages to the global business community. Such linkages demand cross-cultural relationships, as market forces do not distinguish between race and culture, but rather on whether a company is capable of thriving in a competitive environment. In this particular context there is thus a real difference between the global and the local. The above described differences within the Chinese SME business community constitute what I later on will refer to as a variety of fault lines within this community, thus showing that the latter is not a homogeneous community but rather a dynamic one in which firms develop, die or don't do anything but survive and are quite satisfied by doing just that!

**Dynamics with the SME community: From SME to PLC and (almost) back again: on the impact of the *bumiputra* policy**

As discussed above the Chinese SME community in Penang is not a homogeneous or static group, - a fact that will be elaborated upon later on in greater detail. Not even the top companies of the SME group constitute a static upper layer of the SME category. Here medium sized companies move beyond the upper limits of the SME category and into the order of public listed companies. The demarcating lines between these two categories are thus not absolute! The latter type of companies constitutes a kind of role model for those SMEs that aspire to move up the value chain. There are some factors, however, that work against the full developmental potential of the PLCs, - factors that have their roots back to the New Economic Policies (NEP) and the embedded *bumiputra* policy, both initiated in 1971.

In an attempt to explain the relationship between NEP's economic policies and the underlying inter-ethnic dimension Khoo Boo Teik writes that without dismissing some of NEP's underlying, more generalised principles about an equitable inter-ethnic distribution of wealth via affirmative action programmes, he suggests that Malaysia's NEP was never exclusively restricted to ethnicity and ethnic relations. NEP encompassed state policies that affected ethnic identities, inter-ethnic power sharing and an ethnically targeted distribution of developmental benefits, but was not confined to these issues (Khoo 2004: 4).

Khoo concludes that NEP could heighten as well as diminish ethnic differences to the extent that issues of ethnic identity and problems of cultural grievances in Malaysia had always had an economic essence to them. The substantive attainment of NEP's socioeconomic goals diminished the likelihood of intense ethnic economic rivalry, while the Mahathir regime's economic solutions to cultural problems in the 1990s encouraged a deeper sense of national purpose and identity (Khoo 2004: 18).

However, the ethnic issue still lingers on. Zooming in on the political realm one finds several examples of a discourse on more or less tense inter-ethnic relations just beneath the surface. For example, during 2006 several complains from the Malaysian community in Penang have been voiced of being marginalised in terms of political influence due to the fact that the Chinese dominated political party Gerakan from the ruling coalition Barisan Nasional has held the position of Chief Minister since 1969 and up until March 2008. This critique of not being a multi-cultural party and thus not contributing towards forwarding Penang's and ultimately Malaysia's, racial harmony has been denied by the party's vice-president, Datuk' Teng Hock Nam. He said that such statements are not fair just by looking at the racial makeup of its members. Even though about 80 % of Gerakan members are Chinese, the party has always adopted a non-racial approach to Malaysian politics.<sup>11</sup>

Despite indicated otherwise by various observers, racial tensions do exist and contemporary Malaysia has still not moved beyond the confines of the *bumiputra* policy. As a consequence conflicting inter-ethnic relations are occasionally surfacing, if not constantly simmering just beneath an otherwise tranquil multiracial surface. One only needs to read the articles in the Straits Times in late November 2007 on Malay Chinese, who immigrated to other countries due to better 'life' conditions there than in Malaysia, as well as the articles on Malay Indian demonstrations in November and early December 2007. That the inter-ethnic question was still not solved in July 2009 could be seen in an article in The Straits Times, where the former Prime Minister Mahathir Mohamad maintained that non-Malays are the real masters in Malaysia. Mahathir were cited for saying that the bumiputra share of the corporate pie is only 20% while Chinese Malaysians hold

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<sup>11</sup> The Star. Nov. 13, 2007.



50% despite them making up a mere 26% of the population.<sup>12</sup> On the basis of these simmering sub-societal tensions I will in the following maintain that the *bumiputra* policy, besides demonstrating that it is still in existence, also hampers the Chinese SMEs efforts to move up the value chain, thus damaging the development of the Malaysian economy per se.

As stated by representatives from several PLCs during fieldwork in Penang in 2007 and 2008, due to a federal governmental requirement of 30% Malay equity ownership of non-bumiputra owned PLCs, most Chinese company owners have chosen to transform their companies into holding companies in stead of creating one big local or transnational company. The logic behind this dates back to a 1975 federal governmental legislation on investment practices, which states that Chinese entrepreneurs had to apply for permission to invest more than 2,5 million Ringgit (RM) in any type of business. This benchmark is currently (2008-2009) being debated and a new benchmark of about 10 million RM is proposed. If a Chinese entrepreneur got the permission to invest from the authorities, then 30% of this new enterprise is to be handed over to Malays as either shares or 30% Malay equity ownership of the business in question. In case a company intended to invest more that 2.5 million RM, then they will be scrutinised if the targeted 30% bumiputra equity is not met.<sup>13</sup>

The political rationale behind this business ownership policy was and still is to in enforce Malay participation of Chinese owned companies so as to raise the percentage of Malay entrepreneurship in the Malaysian corporate world. The downside of this policy has so far been twofold. First, it has created tensions between Chinese and Malay entrepreneurs in terms of business ownership due to a general notion of that the Malay private investment rate is relatively low and that

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<sup>12</sup> The Straits Times Wednesday, July 22, 2009. See also The Straits Times 21 April 2008.

<sup>13</sup> For a critical discussion of this remnant from the NEP, see [www.atimes.com](http://www.atimes.com) 11 April 2008 and again on 23 January 2009.

suitable Malay partners are difficult to come by. Second, Chinese entrepreneurs have, when contemplating listing their companies on the stock exchange, formed holding companies instead, which consist of numerous specialised subsidiaries that functions as each other's supplier. In this way their companies are bypassing federal governmental regulations on investment practices and thereby maintaining full control over their companies.

Several major Chinese owned SMEs and PLCs do, however, have Malays on their board of directors. This they have chosen to have due to investment plans thus tapping into the political advantages that such a partnership might entail. To have or not have Malays on the board of directors thus depends on a given business strategy! The main rationale behind such strategies is thus based on how to control company assets and to implement investment plans.

### **SMEs/PLCs and the Impact of the Governmental Economic Facilitators (PDC, investPenang and SERI)**

The Chinese SME community does not exist in a vacuum but relates to and depends on a variety of external institutions for their technological and managerial development and ultimately their economic survival. In this section I focus on investPenang as a representative of a governmental initiated economic facilitator. Other governmental facilitators such as Penang Development Corporation (PDC) and SERI will only slightly be touched upon, as data collection in relation to these two institutions is still in progress. When discussing these facilitators with the Chinese SME community the latter feels being left out of the Penang State Government's economic policies, as it is putting a rather heavy emphasis on the high-tech sectors in which a majority of the Chinese SMEs are not engaged in or do not have the capacity to do so. There is a feeling that the government is especially catering for the major SMEs and PLCs, as they are in a better position to

attract FDI so that the government can fund and thus further its own economic development scheme(s). Those SMEs that are not within the high-tech sector thus loose out and have to more or less fend for themselves. This has over time the potential of creating negative economic fault-lines within the SME community, as only a minor part of the SMEs and PLCs are capable of upgrading and subsequently expand into this specialised field.

From the perspective of the Penang State Government this scenario is not the case. The state has initiated a SME bank so as to support and further the economic development of all sections of the SME community. It has furthermore introduced various governmental institutions such as PDC, investPenang and SERI so as to help the SMEs to grow and prosper.<sup>14</sup> Focusing on, for example, investPenang, its main centre of attention is to sustain, rejuvenate and promote the business environment in Penang through encouraging to continued investments in especially the high-tech sector. investPenang envisions itself as the main driver of a three-pronged strategy that is based on combining technological development, industrial infrastructure and private business so as to attain a sustainable economic growth and development for Penang and Malaysia in general.

In relation to the SME community in general, investPenang recognises that SMEs are very important for the economic development of Penang, as they constitute about 90% of the industrial setup. The SMEs, however, are not, according to investPenang, that easy to work with due a particular mindset that dominates many of the SMEs. First of all, several of them are content by maintaining the size they have achieved by now. They generally have a negative attitude towards reinvesting their surplus capital in their businesses thus pushing them up the value chain. Instead, they concentrate on profit maximisation that results in a seemingly

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<sup>14</sup> With regard to SERI this is a research institution that is mainly used by the Penang State Government and as such is of no direct help to the SME community. It does, however, provide the government with input of the developments within this part of the industrial setup (<http://www.seri.com.my/index.php>).

contradictory planning, namely exhibiting rather high saving rates of about 30% to 40%, and at the same time wanting to show off their wealth and therefore not necessarily reinvest the profit they have generated in new technology and/or management practices. This has resulted in what has been called a localised mindset that works against those developmental initiatives that investPenang are suggesting for this particular section of the industrial setup. As a consequence a rather negative attitude towards the SME community has developed, as investPenang does not see it as its responsibility to nurture the SMEs toward higher growth and greater market integration. According to investPenang their mission in this connection is only to prepare the ground for the development of pertinent SMEs. Basically, the latter must help themselves to develop further!<sup>15</sup>

Interestingly, there is a contradiction in what investPenang is saying it is doing and what they are supposed to be doing. According to investPenang's statutes, it is to groom the SME and PLC environment in order to prepare them for pushing themselves and Penang up the value chain, especially in the high-tech and related sectors. This means that these companies will face increasing global competition, as the market opens up the higher up one move along the value chain. On the basis of this, investPenang seems to be reluctant in helping SMEs to prepare for this increasing competition or to go abroad in order to become more competitive internationally. Instead, the strategy seems to be on upgrading the SMEs so that they can support pertinent PLCs in their respective internationalisation strategies. In this sense investPenang follows the theories of Michael Porter, especially that section in his 'Determinants of National Advantages' that caters for related and supporting national industries in order to prepare for global competition.<sup>16</sup>

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<sup>15</sup> Personal communication March 2008.

<sup>16</sup> Porter 1990: 33-129.

The present author is sceptical towards such an approach, as making a distinction between local and/or global in terms of being a company is problematic. Arguably, being competitive globally and having a solid position in ones domestic market is not a contradiction but a complementary state of being thus reinforcing a company's capabilities to compete in both areas. As it is now it seems as if investPenang is tying the SMEs to a specific locality in the hope of developing it domestically thus sheltering it from global competition. If this is the case, then it is not a productive approach, as it reduces the individual company's competitive edge thus jeopardizing its long term survival. Instead, investPenang must help or at least prepare local SMEs to go global, as otherwise they will not be able to withstand global competition. The latter is currently penetrating even the most remote sections of the domestic market. It seems that this is a weak spot in investPenang's business strategy with regards to the SME community and the latter's position in an increasing globalising industrial development.

### **SMEs/PLCs and the Non-Governmental Economic Facilitators**

When analysing the impact of the governmental economic facilitators on the Penang SME community one is only researching the first tier of economic facilitators that are focusing on the SME section of the industrial setup. One also has to focus on the so-called non-governmental economic facilitators, as they constitute a second tier of institutions that are engaging the SME business environment. I have chosen to focus on Penang Skill Development Centre (PSDC), the Penang Chinese Chamber of Commerce and a newly established chamber called the South-West Penang Chamber of Commerce. By looking at both these tiers of economic facilitators one gets a holistic understanding of the forces that define the field within which the SMEs are working.

#### *Penang Skill Development Centre (PSDC)*

PSDC was established in 1989 and is Malaysia's first industry-led training centre located within the free industrial zone Bayan Lepas in the southern part of island Penang. While initiated and sponsored by the Penang State Government and aided by academia PSDC itself operates as a non-profit organisation that currently has a membership of about 146 companies employing more than 100,000 workers. Described by a regional magazine as 'unique in Malaysia', the PSDC was singled out not because it trains shop floor workers as technicians and engineers, but also because competing companies are requesting specific courses and services of PSDC thus keeping the latter on the cutting edge of Penang industrial development.<sup>17</sup>

This, according to the centre's CEO, offers the most cost-effective training for the industry while bridging the gap between skills taught in tertiary institutions and those required by companies. 'As a vehicle that seeks to better understand the needs of transnational companies by combining and using joint resources, PSDC is a model which has worked very well', says the CEO, as he acknowledges the role played by the eight pioneer electrical and electronics firms, which set up factories in Penang three decades ago: Intel, AMD, Osram, Hitachi, Clarion, Agilent technologies, Robert Bosch and Fairchild Semiconductor. Together with other major companies they have enabled the PSDC to develop models, which enhance the quality of the work force, upgrading its services towards major companies and to initiate a development that transforms local SMEs into global suppliers.

Mindful that Penang's future as a preferred industrial location hinges on the Penang State Government's ability to provide a workforce that can keep pace with

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<sup>17</sup> For more details on PSDC see <http://www.psd.com.my/page.cfm?name=Profile-History>

technological change. The CEO for PSDC stressed that advanced manufacturing technology, automation and research and development have to be adopted not only by the MNCs but also by the local support industries. PSDC was thus conceptualised on the basis that if Penang was to continue keeping established and attracting new MNCs, its human capital must constantly be updated so as to keep a pace with the latest changes in technology and management.

Finally, PSDC concentrates in particular on the SME's, as they constitute the backbone of the economy as also stated by investPenang, the public initiated economic facilitator. Furthermore, PSDC is also catering for the MNC community so as to further develop and create a conducive business environment for them in Penang. As a matter of fact, PSDC aims at establishing connections between the SMEs and the MNCs in order to create a productive synergy between them. The relationship between the two, however, has changed over the last couple of years. Previously the MNCs employed pertinent SMEs as suppliers when entering the Penang market. Now this relationship has changed towards a more competitive one. Today the relationship between the two can be characterised as one based on co-opetition, which indicates that each SME and pertinent MNC relate to each other on a competitive but also collaborative basis. This is the reality that also the Chambers of Commerce has to take into account. Now, let us first take a look at the small South-West Penang Chamber of Commerce<sup>18</sup> and after that the biggest of them all, namely the Penang Chinese Chamber of Commerce.

#### *South-West Penang Chamber of Commerce*

This Chamber focuses mainly on micro and small SMEs within trade, service and manufacturing. Regional wise it concentrates its efforts on the south-western

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<sup>18</sup> This chamber of commerce was previously called Bayan Baru Chamber of Commerce.

district of Penang, that is, around the industrial zone Bayan Lepas. It is a multicultural Chamber that does not distinguish between the ethnic backgrounds of its members. This does not mean, however, that it does not communicate and work together with the three ethnic distinct Chambers, that is, the Chinese, Malay and Indian Chambers of Commerce.

South-West Penang Chamber of Commerce's main role is to help SMEs to develop. This they do partly through their contacts in the governmental sponsored SME Bank, and partly by forcing the SMEs to comply with the official rules and regulations, which are imperative if they want to obtain loans from the SME Bank. As such, this is a mode of formalising an otherwise more or less informal sector of the economy. Their aim is to make these SMEs more efficiently managed and thus more competitive in a dynamic market. In case they do not adjust to these changing conditions then eventually they will be out-competed by more consolidated and developed companies, both local and transnational.

Here the representatives from the Chamber pointed towards the biggest problem currently facing the SMEs community, a problem that investPenang also pointed towards, namely the mindset that governs the majority of the SMEs. Most of them are family owned and managed, which in many cases result in that there is a greater incentive for showing off personal success rather than reinvesting profits in new technology, know-how and management systems.

This problem, however, depends, according to the Chamber, on the size of the individual SME. The further down in size one goes, for example, a micro ('mom-and-pop') SME consisting of one family only with an annual turnover of less than 250,000 Ringgit, the more conservative in terms of management and technological innovation they become. These kinds of SMEs can generally be found at the



bottom of the SME business hierarchy so to speak, whereas PLCs such as Pentamaster<sup>19</sup> and LKT<sup>20</sup> with their 550 and 166 employees respectively and an annual turnover of more than 115 and 83 million Ringgit respectively, represent companies which originally have their roots in the SME community but have move beyond this category of companies.<sup>21</sup>

This divide points towards a growing fault-line within the SME community. Furthermore, this potentially negative development has also a bearing on network practices among the SMEs, as that too contributes to further a budding division within the Penang SME community. The smaller the SME the more ethnically dominated their network practices become. As the SMEs move up the value chain their network practices begin to cross ethnic borders and branch out into a non-ethnic related business environment. It is exactly here that various degrees of linkages to the global business community can be observed. The problem for the smaller SMEs is, as mentioned above, that the global market is beginning to manifest itself even in the tiniest market place. This is something that South-West Penang Chamber of Commerce is very much aware of, which is also why they constantly urge the smaller companies to mould their mode of doing business along the lines of more professionally run and managed companies. In case they do not do that they will face problems getting loans in the government controlled SME bank. Promoting this alternative business strategy towards the more traditionally oriented SME community is also, however, where the Chamber is confronted with the greatest resistance towards changes in business practices.

As also noted by investPenang many SMEs are not interested in upgrading their management system or the work force due to traditional modes of ownership and profit maximisation. What is basically at stake here is a change of company

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<sup>19</sup> Pentamaster web page: <http://www.pentamaster.com.my/subsidiaries.htm>

<sup>20</sup> LKT web page: <http://www.lkt.com.my/index5.html>

<sup>21</sup> Penang Automation Cluster Directory 2007.

structure, from a family run company towards an arms-length governed company, where an otherwise very close relationship between management and investors and thus ownership and control of the company is broken up and professionalised. This is seen, according to the South-West Penang Chamber, by the Chinese owned companies as a threat towards the very existence of their family run businesses, which for a long time constituted and to a certain extent still constitute the backbone of the industrial setup in Penang. For these entrepreneurs their history and thus legitimacy is at stake here.

When discussing the ethnic representativeness in the multi-ethnic Penang SME community the Chamber representatives emphasised that they were a truly multi-cultural Chamber compared to the other Chambers of Commerce in Penang. However, the Chinese companies were in a majority in the South-West Penang Chamber, but the contingent of Indian and Malaysian companies is sufficient to define it as multicultural. The Chamber was of the opinion that setting up this kind of Chambers was the only way forward if Malaysia was to develop into one coherent nation. In this way the Chamber is critical towards the positive discrimination towards the Malays. However, they also recognised that the three other Chambers, the Chinese, the Malay and the Indian one, had for decades been divided along ethnic lines and this was something that was very difficult to change, - both in terms of tradition but also due to the continuing impact of the *bumiputra* policy on business.

The South-West Penang Chamber of Commerce does have some working relations with the other Chambers of Commerce as well as with Penang Skills Development Centre (PSDC), as especially the latter represents a way of upgrading the various SMEs, that is, those of them that are prepared to do so.

### *The Penang Chinese Chamber of Commerce*

According to representatives from this Chamber it does not have that many relations to the other three Chambers, the Malaysian, the Indian and the multi-ethnic South-West Penang Chambers of commerce. The Chinese Chamber called itself a 'one point Chamber' meaning that all what its members had to do when experiencing problems was to contact the Chamber, whereas the latter would take care of the problems whatever they might be.

The Chinese Chamber has about 75% of all SMEs in Penang as members; the Malaysian Chamber has about 20% and the Indian Chamber about 2%, a division that to some extent reflects the ethnic division of Penang's business community. The Chinese Chamber is fully privately sponsored and is run on the basis of member fees, whereas the Malaysian Chamber is linked to the Penang State Government and is, according to informants, partly sponsored by the latter. Informants from the Chinese Chamber of Commerce said that they did not know the multi-ethnic South-West Penang Chamber of Commerce.<sup>22</sup> They maintained that the current three ethnic distinct Chambers were enough to cater for the SME community in Penang.

The Chinese Chamber was servicing various kinds of industries ranging from trade over manufacturing to high-tech companies. The main membership criteria are that they have to have at least 51% Chinese ownership of the individual company. They serviced all sizes of SMEs, from micro over small to medium. They maintained that they still had good contact with those SMEs that had become PLCs. This was, however, contested by the PLC Pentamaster that maintained it did not have much to do with the Chinese Chamber mainly because the two were working in different

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<sup>22</sup> Nonetheless, I was attending a meeting at the Chinese Chamber of Commerce in 2007, where the South-West Penang Chamber of Commerce presented its platform and asked for ways to collaborate.

sectors of the economy. Interestingly, Pentamaster was used by the Chinese Chamber as a role model for how SMEs could grow if they invested in new technology and adopted more advanced management systems instead of holding on to traditional Chinese modes of doing business, which, as mentioned above, was mainly based on high saving rates and profit maximisation.

According to the Chinese Chamber the Penang Chinese SME community that can be divided into three main parts: a 'classical' one consisting of 100% family owned and run SMEs (mainly micro SMEs), 100% owned family SMEs that is professionally managed but make use of 'classical' Chinese business strategies and network practices (mainly small and some medium SMEs), and finally those SMEs that are about 50% owned, professional managed and combine 'classical' Chinese business strategies and network practices and modern market seeking techniques thus pushing them toward the limit within the SME category and further on towards PLC status.

There are two main reasons behind the above noted differentiation of the Penang SME community. First and foremost there is an entrenching global capitalism that forces such a change on those companies who ventures outside the immediate local market. The second force of change is an inward looking drive behind a 100% family owned and managed company. There are thus various kinds of pressure towards change that drives the different SMEs into the different slots mentioned above. These changing developments amongst the Chinese SMEs were interpreted by representatives from the Chinese Chamber as an inherent aspect of Chinese entrepreneurship, namely openness towards change. That might be so but also societal factors such as local and national political and social aspects have a huge impact on how the Chinese entrepreneurs operate in the market place.<sup>23</sup>

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<sup>23</sup> For details, see Wee, Jacobsen and Tiong Chong Wong (2006).

Currently there seems to be developing a fault-line within the Penang industrial set-up, a fault-line that manifest itself in increasing non-cooperation and linkages between SMEs and PLCs, and between them and the government initiated and non-government initiated economic facilitators. This development is driven by an ever entrenching global economy that penetrates both national and local economies indirectly. Before going into detail with this, a final aspect needs to be included, namely one that briefly discusses the impact of Vision 2020 and the development of the Multimedia Super Corridor (MSC), a subject that is important to take into account due to the fact that Penang has been declared the second stage in the MSC!

### **The SME/PLC community and Vision 2020, MSC and NCER**

According to a top state executive councillor Vision 2020 and the MSC was and still is a kind of wish thinking. As such the Penang State Government accepts it. However, the vision is gradually losing its attractiveness, as a split between ideology and reality begins to emerge. As previously mentioned there are many tensions in Malaysia in terms of ethnic and religious cleavages that hinder a realisation of the vision. When relating Vision 2020 and MSC to the industrial sector, and in particular to the SME community, the latter is becoming more sceptical towards it, and is beginning to term it (political) 'hot air', meaning that both the vision and the MSC is more rhetoric than action, implementation and development. The main problem for the industrial sector, and especially for the biggest SMEs, PLCs and MNCs, is human resources. This is a problem that, according to the state executive councillor, is not taken probably care of by the political establishment in terms of fund, education and training facilities. The quality of the current level of labour power is not high enough compared to international standards. This has a negative impact on industrial performance, as the different industries, representing both local as well as transnational companies in the

Penang industrial setup, are loosing their competitive edge in the global competition.

When asked whether 2020 and MSC fit into the state economic planning schedule the state executive councillor said that there was no deliberate attempts of incorporating the two. Penang is dominated by low end manufacturing high-tech industries and cannot as such move up the value chain just by incorporating the two. There are simply not enough skilled labours to do that. In order to move up the value chain in a more concrete manner, pertinent and realistic R&D initiatives are needed, not visions! As already mentioned there is a great lack within the area of human resources. This is currently being sought solved by simultaneously importing technicians from abroad and by upgrading PSDC, which plays a key role in this connection. Unfortunately, Universiti Sains Malaysia in Penang is currently not capable of contributing effectively towards solving this problem due to a lack of qualified staff and funding. Finally, further but perhaps more indirectly aggravating this situation is the increasing competition from China and India as well as competition from other ASEAN countries such as Thailand, The Philippines, Indonesia and not the least Vietnam, as they attract both low level manufacturing and high-tech MNCs. This is why more R&D and a continuing upgrading of human resources are urgently needed in Penang if it is to maintain and further develop its position as a high-tech hub.

Some of the things that the Penang State Government can do to leverage this situation is to re-orientate the current dominant position of the low end manufacturing sector towards more focus on R&D, upgrading PDC, invest Penang and PSDC's role as industrial facilitators as well as adding further financial means to the tertiary institutions in order to make them work more closely with the industrial sectors. Furthermore, the Penang State Government should through SERI take a more serious approach towards the SME community by upgrading

and integrating it into an overall industrial master plan so as to create a more holistic industrial policy for Penang per se. Finally, the state government should, as an economic facilitator *par excellence*, focus even more on upgrading the physical infrastructure and stage more aggressive international investment promotion tours so as to make more foreign companies and investors aware of the possibilities in Penang thus encouraging them to establish themselves in the pertinent industrial sectors. All these initiatives, however, will not bear fruit if the current bumiputra policy is not gradually dismantled or abolished all together. Equal opportunities for all the three main ethnic groups in Penang and in Malaysia in general are a *sine qua non* if the industrial setup is to move up the value chain as mentioned earlier on in this article. Interestingly, this seems to be recognised by the federal government according to newspaper articles in the New Straits Times on 3 August 2009. Here Prime Minister Najib Razak is quoted as saying that the bumiputra equity shareholding since the inception of the NEP in 1971 seems to be stuck at 18% or 19% here in 2009. He continues: 'It is madness if we continue with these policies (bumiputra policies (MJ)) even after they had failed for up to 19 years' (NST Aug. 3, 2009). The important question is, however, whether such a policy change is also implemented.

Now, let us change the perspective, how do, for example, the Chinese Chamber of Commerce, Pentamaster, LKT and the SME community in general relate to Vision 2020, the MSC and NCER? The Chinese Chamber of Commerce does not see major benefits coming out of the Northern Corridor Economic Region (NCER) initiatives, as the latter focuses mostly on agricultural developments, logistics and on so-called medically related recreational tourism. In relation to the question of sub-contracting the Chamber is of the opinion that most of it would probably go to Malay companies, as they had the best governmental contacts! What, according to the Chamber, their members could expect of the NCER would mostly be small contracts that unfortunately might not have a great impact on the SME community

as a whole. In relation to Vision 2020 and SMC this was also of little interests for the Chinese Chamber, as its members would not be able to draw any benefits out of it due to different industrial specialisation. Furthermore, the localised and thus parochial focus that permeates many SMEs does not fit into these two dynamic developmental schemes thereby nurturing a budding fault-line between them and the SME environment.

In relation to Vision 2020 and the MSC a representative from Pentamaster said that it was a good vision but poorly implemented. This has something to do with the ability of bureaucrats who are to implement these schemes. As for now they do not have the right educational background to implement the vision and the more concrete initiatives in a professional and correct way. The level of professionalism has to be raised considerably if Vision 2020 and MSC should become a reality and not only a national political rhetorically construction. Like several other informants, the representative from Pentamaster did not have high thoughts about the general abilities of the bureaucracy when discussing actual implementation and functionality.

In relation to 2020 and MSC, LKT is not a mainstream company in this connection, meaning that as a company that mainly works within automation and in the plastic industry it is only indirectly related to these visions, as the latter mainly concentrate on high-tech companies. Generally speaking, LKT has problems with these political ideological initiatives, as they encroach on LKT in terms of labour power! According to LKT Vision 2020 and MSC had hit it hard in terms of employment, as they snatch away the best graduates thus increasing the transaction cost for LKT, as it has to recruit qualified labours from abroad. Those labours lured away from, say, LKT ends up in the call-centres that are sat up in Cybercity on mainland Malaysia.



I think it is important to point towards a lack of sensitivity on behalf of the federal developmental state, when introducing new directions for how Malaysia should develop. Vision 2020 and especially MSC is a case in point. Vision 2020 is in a sense harmless as it does not have direct impact on the industrial setup in Penang nor does it have a major impact on the political realm, as the latter is far more pragmatic oriented. MSC, on the other hand, have had a direct impact on state economic policies, as it highlights certain sectors within the industrial set up thus neglecting other ones. This means that the latter ones, and here we are talking about SMEs and PLCs that are not engaged in the high-tech sector, find it more difficult to attract support from the various governmental initiated economic facilitators, as they are, so to speak, out of focus.

If we focus in particular on the Chinese SME community then the impact of SMC will really make a difference, as it will favour those SMEs that work in the high-tech sector. Those SMEs that do not work in this field but concentrate on service and trade instead will definitely be left out of the loop in this connection. This means that they will not have access to financial means and developmental schemes in terms of upgrading their technological base as well as their management systems. The perhaps most important problem facing both the Chinese SME community as well as a further development of PLCs are, however, not the advancement of technological development but the quality and educational level of the labour force. Actually, this is the Achilles' heel behind the attempt by Penang's industrial establishment to move up the national as well as international value chain. For example, a representative from SERI suggested more focus on bio-technology as a way forward for Penang, but a senior state adviser shot it down by saying that before one initiate such initiatives one have to have the right kind of labour power. Currently Penang cannot offer this kind of employees to pertinent companies. As previously mentioned, PSDC did its best to upgrade the current labour force and management practices but it has so far not been enough. Universiti Sains Malaysia

and the tertiary sector in general are likewise not capable of supplying the industry with qualified employees. As for now, the best students leave these institutions for the better universities and companies abroad, thereby reinforcing a downward negative spiral in term of producing a higher qualified workforce.

## **Conclusion**

The main conclusions of this article are thus two-fold: first, the various fault-lines within the SME community and the relationships between it, the PLCs and the MNCs have to be addressed so as to create more synergy between the three of them. This is essential for initiating a more holistic industrial development in Penang. Second, the question of qualified labour power is a crucial one, as this is a *sine qua non* for Penang's industrial establishment to change its current state as a low level manufacturing site and move towards a more R&D dominated industrial complex. Finally, it is not enough to focus on the PLCs and the MNCs and their respective needs. The SME sector is of crucial importance here, as it first of all constitutes about 80% of the industrial setup, and second, it constitutes an important service sector and a pool of more or less specialised suppliers for the PLCs and MNCs. Upgrading the SMEs in terms of technological know-how as well as management skills is highly important if the whole industrial setup is to be lifted further up the value chain.

Furthermore, this article has also tried to show that the Chinese owned SMEs in the high-tech sector do not constitute a homogeneous entity thus indicating that it is not notions of Chineseness that binds this group together. On the contrary, the diversification among these firms points towards other forces which introduces different economic fault-lines between the various sections within the SME community. The major fault-lines were identified as consisting of, first, those which divided the SME community into those that catered for the global market and those

that were mainly directed towards the domestic market, and second, those SMEs that were working within the high-tech sector and those working in the trade and service sectors. A more subtle fault-line that is indirectly conditioned by the previous two ones was a change in which the Chinese owned SMEs were managed in terms of technological and managerial practices. This depended on where on a developmental continuum a SME could be identified. The smaller the more traditionally oriented the SMEs were managed, and the higher up the value chain a SME could be identified a more arms-length structure of management practices began to emerge. Arguably, the forces that lay behind these developing fault-lines shows that intra-ethnic relation are not the driving forces behind the diversification of the Chinese SME business community, but rather an encroaching global market economy that pushes through changes within the individual firm thus producing the above mentioned fault-lines in the process.

These developments thus highlight a situation in which external forces in relation to a given market create inter- and intra-ethnic diversification and not vice versa. For example, what make the Chinese in Penang Chinese is not based on those definitions that some academic and economic conventions on Chinese entrepreneurship in Malaysia, or for that matter in Southeast Asia in general, are based on, namely intra-ethnic relation.<sup>24</sup> Instead we are talking about political engineered notions of ethnicity so as to maintain a given macro-political inter-ethnic triangulation which maintains the Malays as the dominant ethnic group. We thus have a situation in which, on the one hand, engagement in the global market economy produces inter-ethnic co-opetition, and on the other hand a nationally political engineered notion of inter-ethnic relation co-exists. Inter- and intra-ethnic relations are thus pushed from a back-stage to a front-stage scenario and vice versa depending on where one wants to put ones perspective as an

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<sup>24</sup> Bolt (2000), Gesteland (2005), Redding (1993), Weidenbaum and Hughes (1996).

observer. As stated in the very beginning of this article notion of identity and thus ethnic belonging are not something given but created and constructed.

Interestingly, the bumiputra system has never posed a constraint to Chinese entrepreneurs. It however has significant impact on the limits to growth of Chinese enterprises. The entrepreneurial spirit of the Chinese and other ethnic groups has been and will continue to be thriving. This is evident from the increasing number of Chinese owned petty traders and hawkers, small over medium to big business units currently operating in Penang. Indeed, the pro-bumiputra policies have deprived the other ethnic youths of job opportunities in the government sector as well as entry into the public tertiary institutions even though they are qualified. However, these "drop-outs" have an enterprising drive that is motivated exactly because of the bumiputra policy thus making them fend for themselves by either studying or seeking jobs overseas or by venturing into private business. These kinds of challenges were interpreted by representatives from the Chinese Chamber of Commerce as an inherent aspect of Chinese entrepreneurship, namely openness towards change. As has been discussed in this article it is not possible to make a distinction between the past and the future of Chinese entrepreneurship. In Penang the two will always be conflated in the present.

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