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Income Inequality in Malaysia: The Dichotomy of Government Perception and Malaysians' Lived Experiences

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INCOME INEQUALITY IN MALAYSIA: THE DICHOTOMY OF GOVERNMENT PERCEPTION AND MALAYSIANS' LIVED EXPERIENCES

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According to the Malaysian government, income equality in Malaysia has been consistently improving for the past 15 years. However, several indicators suggest that the perception among the general Malaysian population is that income equality is not improving or even may be worsening. This article investigates the reasons why this disconnect between government and public perception exists as well as provides policy suggestions for ensuring equitable human development among Malaysians as the country makes strides toward high-income status.

Introduction

Reducing income inequality is essential to Malaysia's development. Income inequality can influence long-run economic growth, social inequality, political stability, and the overall welfare of the population. Historically, income inequality has substantially influenced Malaysia's social and economic development. For instance, it was income inequality among ethnicities that created social inequality and fueled the 1969 racial riots. The racial riots marked a turning point in Malaysia's development, as they immediately resulted in policy reform that has shaped Malaysia's economy today (Khalid).

Over the past several years, the Malaysian government has consistently reported that the country is making improvements in decreasing income inequality. However, many researchers are questioning the scope of the government's official inequality statistic. Research suggests that the government's method of measuring income inequality is overly narrow and in turn is restricting its view on the issue. Essentially, the government's measurement of income distribution indicates that income inequality in Malaysia is decreasing; however, the lived experiences of Malaysians say otherwise. A majority of households are not experiencing the developmental improvements that the national averages suggest.

The goal of my research is to address two main questions. First, why does this dichotomy of government and public perception exist? There is growth in incomes for the poor; however, food and housing inflation are outpacing that growth in income. Food and housing consume nearly all the expenditures of the poor, and, as a result, their real disposable income is decreasing, which indicates that saving and accumulating assets are becoming more challenging for the poor. While income equality is improving, evidence suggests that wealth equality is not. This increasing wealth inequality is having a greater impact on the public's perception than the decreasing income inequality, which the government's measure of income inequality fails to capture. The second question I address is, what can be done? If wealth inequality is the true issue, then the government's poverty assistance programs need to take this into consideration. Based on the 2019 budget, it is evident that the government is acknowledging recent research and public concern. In particular, the government is taking steps to increase the real disposable income of the poor. As Malaysia makes strides toward becoming a high-income country, mitigating the wealth inequality issue will play an essential role in ensuring equitable human development.

The Impact of Inequality

It is necessary for governments to understand the extent of income inequality within their countries because it can lead to inequality in human development. According to the Khazanah Research Institute (KRI) *The State of Households 2018* report, it is evident that not all households in Malaysia are experiencing the same developments in education, health, and access to basic amenities that the national averages suggest. Malaysia as a whole experienced slight improvement from 2014 to 2016 in various quality-of-life–related metrics, such as the percentage of rural households with access to pipe water, located 5 km or less from a secondary school, and located 5 km or less from a public health center. However, when broken down by state, the data show that several states experienced declines for each of these metrics. For instance, Labuan had 100% of rural households located 5 km or less from a secondary school in 2014 but only around 90% in 2016 (Khazanah Research Institute). A host of patterns such as these suggest the need for assessing a more expansive set of metrics to better evaluate the nature, trends, and causes of human development inequalities in Malaysia.

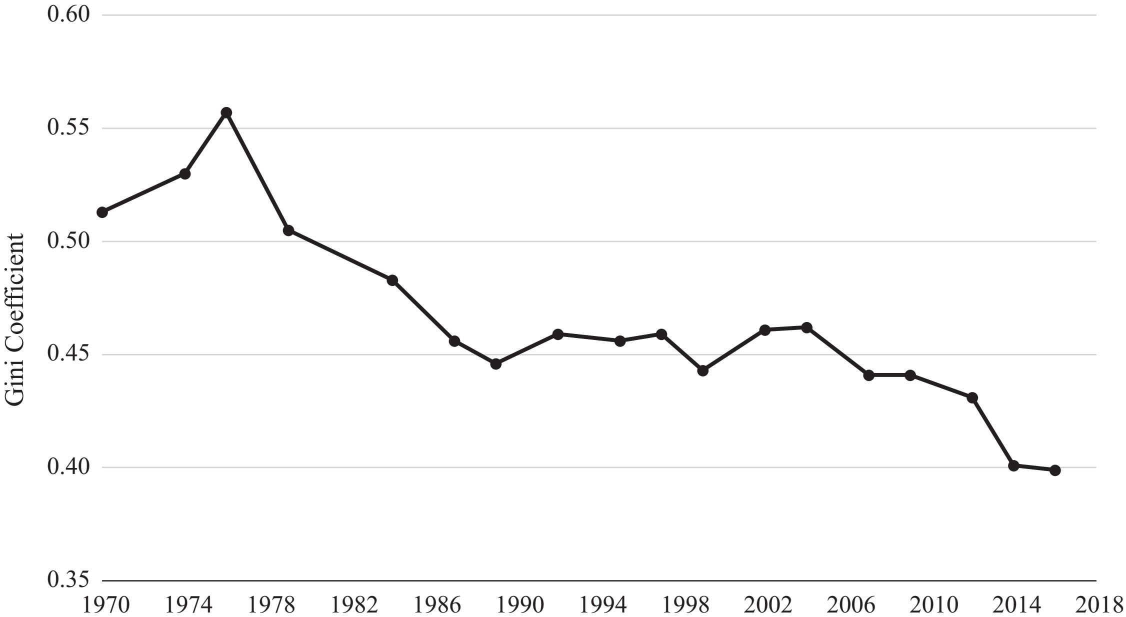
The Public's Perception

Several disparate types of indicators suggest that the general perception among Malaysians is that income inequality is not decreasing. First, income inequality is currently a hot topic in the press. For example, in 2018, one of Malaysia's leading newspapers*, The Star,* held a roundtable with experts on Malaysia's Employees Provident Fund (EPF), in which the topic of income inequality was brought up several times. When questioned about income inequality, the head of the EPF Economics and Capital Markets Department, Nurhisham Hussein, stated that he believes there is a disconnect between the numbers reported by the government and what Malaysians are actually experiencing ("EPF Advocates…"). Similarly, the journalist Lin See-Yan reported it is "widely perceived" that incomes among the poor have not risen, the rich are getting richer, and inequality is higher than ever. See-Yan also argued that "inequality is worse than is presented by the government and has been so for several decades." These articles suggest that public perception is that income inequality is actually increasing.

The tone of the press coverage is consistent with a second indicator of public perception, public polling. For instance, in 2013 the Pew Research Center surveyed Malaysians on how they felt inequality had changed in the preceding years. The resulting study showed that 32% of people thought inequality had increased, 38% thought it had stayed the same, and only 22% said that it had decreased, despite the decreasing official inequality statistic shown in Figure 1. If income equality truly had improved as much as the government reported, it is puzzling that 70% of the population believed that income inequality had not decreased.

Moving to a third type of indicator, national averages for various economic metrics are improving in Malaysia, but not all households are having the same experience. For instance, on a national scale, both median and mean household incomes have been increasing. Real median household income increased by 6.7% per year on average since 2009 and real mean income increased by 5.7%. In 2016, the nominal median income was RM5,228 ($1,281) per month. However, only 12 of the 144 districts in Malaysia had median incomes above the national median income. For the most part, highly urbanized and

Figure 1
Official Inequality Statistic, 1970–2018



Source: Department of Statistics, Malaysia.

populated districts had greater incomes, thus contributing to the greater overall median. Greater Kuala Lumpur was the district with the highest median income, at RM9,073, which was 4.3 times greater than that of the district with the lowest median income, Pitas, Sabah, at RM2,105 (Khazanah Research Institute). One possible explanation as to why some districts are far richer than others is urbanization. In 2016, urban Malaysian households earned 1.7 times more than rural households. Thus, although the national median income is high and growing, income trends for households clearly differ far more widely than national averages suggest.

The Government's Perception

To understand the Malaysian government's perception of income inequality, one must discern its current measure. The government's official income inequality statistic is a Gini coefficient calculated from the Household Income Survey (HIS) (Department of Statistics, Malaysia). The Gini coefficient is the most conventional measure of income inequality; it measures the degree to which an economy diverges from equality on a scale from 0 to 1. A Gini of 0 would imply that every person in a country has the same amount of income and there is total equality (i.e., 0 inequality). Conversely, a Gini of 1 would imply that a single person has 100% of the country's income. Essentially, a decreasing Gini coefficient indicates increasing income equality in a country. The HIS measures gross household income and is issued twice every 5 years. The government has reported a steady decrease in the Gini over the past 10 years, hitting 0.399 in 2016, well down from levels peaking above 0.55 during the 1970s (Figure 1). In short, the government's official measure suggests income inequality has been consistently decreasing for four decades.

Several factors suggest the government's calculation of the Gini is too narrow and is restricting its view on income inequality. For instance, the HIS does not account for various income sources or multiple income earners in the same household. According to World Bank studies, income data collected at the household level fail to measure inequality within the household, and therefore can produce estimates of inequality that are understated by more than 25% (Kanbur et al.). There are several possible explanations for this underestimate. For one, economic conditions may put extra pressure on household members to work when they otherwise would not. Additionally, household members may feel pressure to take on more work to sustain their income levels. Household income data do not capture these economic strains and thus do not capture the changes people believe they must make in order to sustain their lifestyles.

Evidence shows that household income data in Malaysia may be underestimated for additional reasons. According to the KRI October 2018 report, Malaysia's HIS may be suffering from under-sampling and under-reporting of households in the upper end of the income distribution. Survey income accounted for only 86% of final household consumption. The KRI attributes this to the fact that high-income households in Malaysia are rare, so when surveyors taking randomized samples encounter a high-income household, that household's income may not accurately represent the whole range of the very top income group. Also, it is challenging to contact higher-income households, and, even if contact is made, these households may be understating income (Khazanah Research Institute).

A study by Khalid and Lee discusses further limitations of the HIS. According to the study, changes in income inequality among individuals are not necessarily correlated with changes in household income inequality, signaling that the HIS does not fully capture fluctuations in the distribution of wages earned by individuals across a country. Although difficult to measure, changes in the wage distribution are important to evaluate because those changes could reflect the pressure members of low-income households feel to take on additional jobs. If growth in wages for lower-income jobs is lagging behind that of high-income jobs, or behind price inflation, employees in low-income jobs may feel pressure to take on more work to keep up with the economy. The purpose of the HIS Gini coefficient is to track Malaysia's progress in income inequality, but if this statistic is failing to capture the reality of wide swaths of the Malaysian population, the government must consider other forms of measurement.

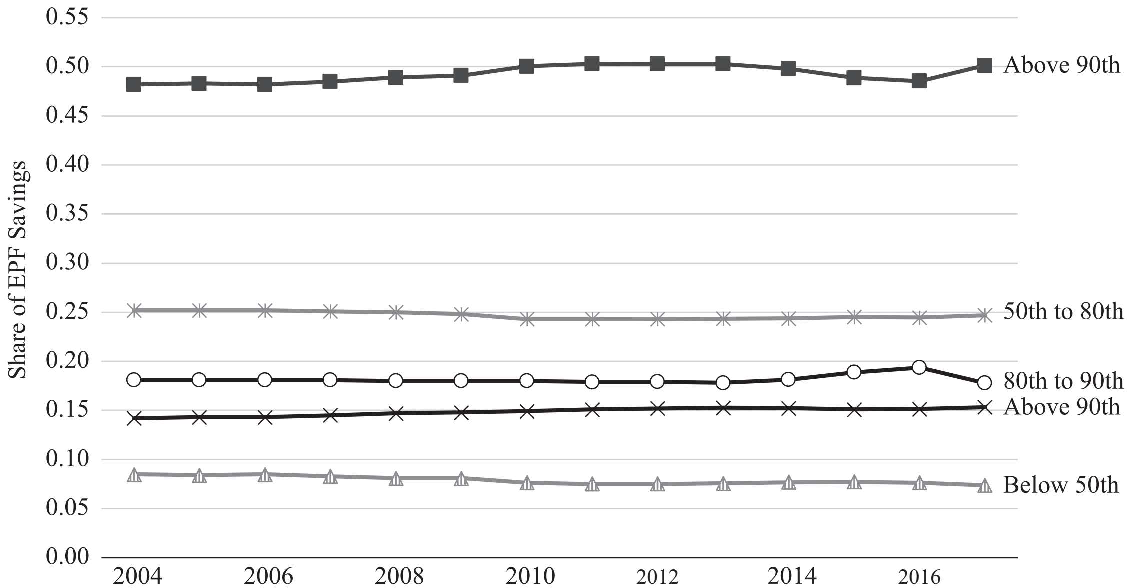
Wealth Inequality

Income is the *flow* of money received on a continuous basis, whereas wealth is the *stock* of assets accumulated at a point in time. Wealth equality is particularly important because assets, like housing, cars, and savings accounts, are more tangible than income; therefore, wealth has a strong influence over society's perception of inequality.

The HIS is limited in its ability to measure wealth inequality. Overall wealth might differ in important ways from the year-to-year income flows that the HIS uses. For example, respondents of the HIS do not report real estate property, investment incomes, savings accounts, or other types of accumulated stocks of wealth (Kahlid and Lee). Fortunately, other evidence is available to help illuminate how wealth distribution has evolved over time. The EPF is a government-owned pension plan that provides retirement benefits to its members through management of their savings. Savings in excess of the Basic Savings necessary for retirement planning can be invested in products offered by fund management institutions ("Overview of the EPF"). The share of total EPF savings by both the top 10% and top 1% of account holders steadily increased from 2004 to 2017, and shares held by individuals in the middle and bottom percentiles have been unchanging or declining (Figure 2), suggesting that wealth concentration based on private sector wages is increasing at the top, which is inconsistent with the declining inequality trend suggested by the HIS Gini. The rich accumulating a greater share of EPF wealth than the poor also is consistent with evidence, discussed in more detail later, that the poor have low fractions of income left over after consumption for basic needs, further supporting the hypothesis that the poor are saving less.

To evaluate changes in the wealth

Figure 2
EPF Savings by Percentile



Source: For 2004–2011, Khalid and Lee; author calculations based on data from Employees Provident Fund Board. Annual Reports 2011–2017.

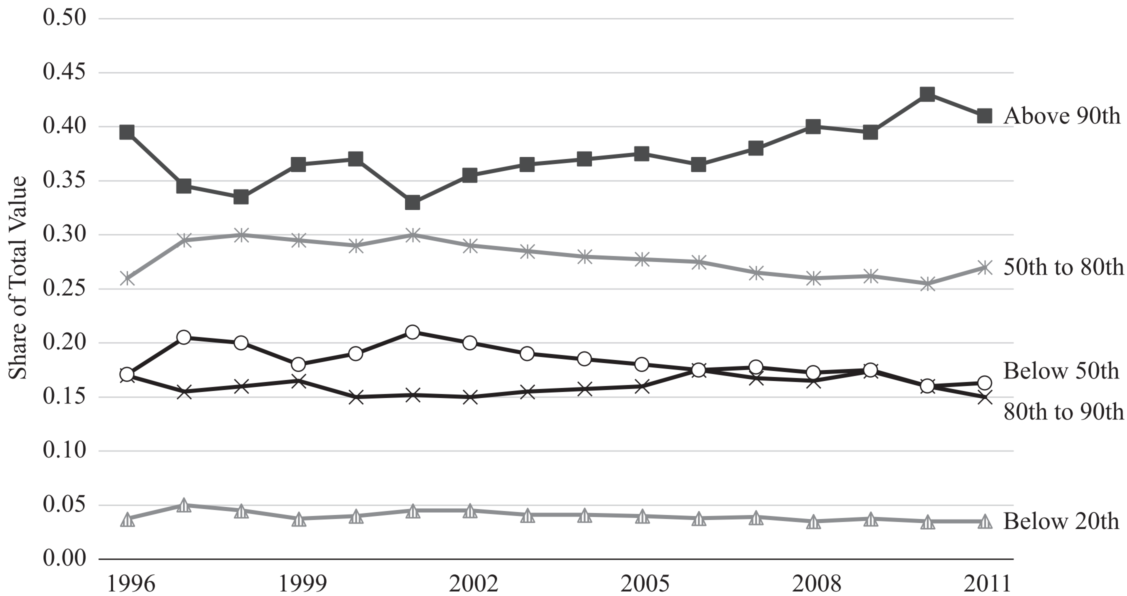
Table 1
Car Purchases: Percentage Share of Total by Price Range

Price Range (RM)	2001 (%)	2006 (%)	2011 (%)
≤40,000	24.4	30.1	30.0
40,001–60,000	43.5	36.2	34.0
60,001–80,000	19.4	15.5	16.3
80,001–100,000	1.5	8.5	5.9
100,001–200,000	9.1	8.0	11.4
200,001–500,000	1.9	1.5	2.2
≥500,001	0.1	0.1	0.2
Total cars sold	278,300	379,300	417,500

Source: Khalid and Lee.

distribution, researchers analyzed the asset classes of transportation and housing. Khalid and Lee, for instance, analyzed new car purchases and residential property sales. From 2001 to 2011, the share of vehicles sold that cost less than RM40,000 increased by 23%, and the share above RM500,000 doubled, resulting in a decrease overall in the share of mid-priced vehicles sold (Table 1). Similarly, the share of property purchases by Malaysians with incomes above the 90th percentile consistently increased from 2000 to 2010, whereas that of the middle percentile bracket decreased, and that of the bottom 20th percentile bracket

Figure 3
Property Purchases by Percentile



Source: Khalid and Lee.

saw no change (Figure 3). This analysis of car and property purchases suggests that wealth inequality increased in Malaysia from 2000 to 2011, which contradicts the income inequality conclusions drawn from the HIS.

The Khalid and Lee study was conducted on data only up to 2011; their analysis can be updated, however, using recent data from the same sources. In 2017, 37.6% of residential properties sold went to households with incomes above the 90th percentile, 17.7% to the 80th to 90th bracket, 28.1% to the 50th to 80th bracket, and 16.6% to the below 50th bracket, of which 3.3% was to the below 20th bracket (National Property Information Centre). Essentially, from 2011 to 2017, the concentration at the top decreased, the concentration in the middle increased, and the concentration at the bottom slightly decreased. These changes reveal that from 2011 to 2017, wealth inequality did not significantly improve, which contradicts the substantially improving Gini coefficient. Thus, analysis of at least these two asset classes over time suggests that the government's measure of income inequality misses key elements of the experiences of most Malaysians, particularly in terms of quality-of-life issues related more to wealth than to annual income.

Relative versus Absolute Changes in Income

A distinction useful in discussing inequality in Malaysia is the difference between relative and absolute changes in income. An absolute change in income is simply the magnitude of the change, and a relative change refers to the percentage change with respect to what income originally was. Changes in Gini coefficients reflect relative changes. In Malaysia, the relative income gaps between the rich and the poor are decreasing, thus explaining why its Gini coefficient is decreasing. However, real absolute differences among the lower-, middle-, and upper-income groups have consistently increased (Khazanah Research Institute). It is important to consider the absolute changes in income gaps, because their relation to changes in expenditure helps better understand how different households are accumulating wealth.

Not only is the absolute gap between the rich and the poor increasing but also evidence shows that those groups with similar growth in income may not be experiencing the same advances in quality of life. This discrepancy is primarily due to the increasing cost of living. According to the World Bank, food inflation has been consistently high in Malaysia, and this consumption category accounts for roughly 40% of low-income households' total expenditure. The HIS also measures expenditures for a variety of different consumption items, such as food, recreation, communication, transport, health, education, housing, and others. In 2016, households with monthly income below RM2,000 spent 94.8% of their incomes on these consumption items, up from 91.9% in 2014. By comparison, households of middle- and upper-income levels also experienced consumption expenditure increases, with households of middle-income levels going from 65.1% in 2014 to 67% in 2016 and households of upper-income levels going from 41.9% in 2014 to 45% in 2016. The nearly complete use of income for consumption by the poorest households highlights their vulnerability to emergencies and economic shocks. For households with incomes below RM2,000, the remaining monthly income after consumption in 2016 was only RM76, a nearly 40% decrease from RM124 in 2014 (Khazanah Research Institute). This decrease was due to the fact that inflation was highest for what the poor spend the bulk of their income on: food. While the rich also experienced the effects of high food inflation, it was relatively less dominant in their budgets, so they still had sufficient funds left over. Therefore, although incomes for the poor are increasing, their expenditures are increasing more rapidly, making it extremely difficult to save and accumulate wealth. Also, housing prices have elevated, and there has been a structural undersupply of housing at the lower end of the market (World Bank Group). According to the research of the KRI and the World Bank Group, a further increase in wealth inequality would be expected, which is consistent with the analysis above of asset classes over time.

What Can Be Done?

There is debate among economists whether income inequality is a policy variable or not. In other words, if income inequality is not a policy variable, income distribution cannot be influenced by policy changes. My take is that income inequality is a policy variable if the root cause of the inequality is known. This is illustrated by Malaysia's past success with reducing income inequality with the New Economic Policy (NEP) from 1971 to 1991. At the time the NEP was implemented, it was clear that a major source of income inequality was inequality among ethnicities. The NEP focused on reducing inequality among ethnicities, and overall income inequality decreased as a direct result. From 1970 to 1991, Malaysia's Gini coefficient of income decreased by 7%. Due to the success of the NEP, inequality among ethnicities is no longer as pressing an economic issue; rather, wealth inequality is now the issue at heart. Therefore, the government's socio-economic policies should focus on helping poor Malaysians develop an economic base.

Upon release of the Malaysian government 2019 budget, it appears that socio-economic efforts are headed in the right direction. The 14th Perak State Legislative Assembly passed the RM1.061 billion budget on December 5, 2018. The budget recognized the findings in the KRI *The State of Households 2018* report by focusing on the affordability of the two largest expenditure components of the poor other than food, housing and transportation.

Housing

In order to improve wealth equality, enhancing affordable housing policies to focus on helping the poor is essential. The historical development of housing policies provides insight into Malaysia's current affordable housing efforts. Malaysia's housing policy has evolved through four major stages: housing the poor (1971–1985), market reform (1986–1997), slums clearance (1998–2011), and state affordable housing (2012–present). During the housing the poor phase, the government imposed a rule on private housing companies, in which at least 30% of housing projects had to be for low-cost housing. However, the main providers of low-cost housing were state governments and government-owned companies, and the main providers of medium- and high-cost housing were private companies. During the market reform phase, the 30% quota became more effective, and private companies started using a cross-subsidy system in which revenues collected from the sales of high-cost homes were used to reduce the price of low-cost homes, which led to private companies having a greater role in housing provision and to state- and government-owned companies having less of a role. The changes that became the slums clearance phase were the result of the 1997 Asian financial crisis. During that time, the federal government once again became the main provider of affordable housing with the introduction of Program Perumahan Rakyat, aimed at relocating squatters by providing them with more affordable options for renting and owning homes (Iga).

Finally, the biggest change in affordable housing policy was during the transition to the present stage, state affordable housing, because the target group for housing provision changed. Previously, housing policies had focused on providing affordable housing options to the poor, but during the earlier administration of Prime Minister Najib Razak, federal and state governments shifted focus to direct housing provisions to the middle-income group. In 2011, the Perumahan Rakyat 1 Malaysia (PR1MA) scheme was introduced and provided middle-income homes at least 20% cheaper than the prevailing market rates. According to the World Bank Group (2017), rising housing inflation is affecting the bottom 20% of households significantly more than any other income group. Therefore, making middle-income households the target group of housing policies seems like a step in the wrong direction. Because Malaysia is no longer under Najib's rule, the hope among Malaysians prior to the release of the 2019 budget was that Prime Minister Mahathir Mohamad would again make the poor the target group of housing provision, as he did during his first term (Iga). The government's 2019 budget states that PR1MA will continue to be funded, with roughly RM1.5 billion allocated to support the completion and construction of affordable homes; however, it also introduces several new affordable housing initiatives that shift the focus back onto the lower-income group.

One of the key issues in Malaysia's present real estate environment is the growth in high-end housing and concurrent lack of growth in low-end housing. According to property experts, Malaysia is facing a potential crisis of a "homeless generation" where many poor Malaysians are unable to afford homes (Iga). Prior to the release of the 2019 budget, the National House Buyers Association of Malaysia (HBA) and the Real Estate and Housing Developers' Association Malaysia (REHDA), both non-profits, made suggestions on how the government could mitigate the threat of a homeless generation.

For example, many wealthy Malaysians are using real estate properties as an investment mechanism, speculating on housing prices by buying homes with the intention of selling them months later at a higher price. To combat this, the HBA proposed taxing property speculators. They suggested a higher stamp duty on purchases of third homes and a 30% real property gains tax on homes sold within the first 10 years of taking possession. In the 2019 budget, there was no stamp duty introduced on purchases of third homes, but the stamp duty on properties valued above RM1,000,000 was increased from 3% to 4%. In accordance with the HBA suggestion, the government increased the real property gains tax on homes disposed of within 5 years of purchase from 0% to 5% for individuals and from 5% to 10% for both companies and non-citizens/permanent residents. These two budget changes both suggest the new government is taking steps to disincentivize property speculation.

The HBA also proposed that the government should introduce more price control mechanisms for affordable homes and incentivize developers to build affordable housing. Unlike the previously used price control mechanisms, the HBA suggested placing a ceiling on the profit margin housing companies could earn rather than a ceiling on the price of the property itself (Lim). To incentivize developers, the government has stated in the 2019 budget that construction and building materials will be exempt from the sales and services tax. The budget introduces no added price control mechanisms, but in a negotiation between the government and REHDA, the latter agreed to a 10% reduction in prices of homes in new projects that are otherwise not subject to existing price controls.

Looking to expand on the HBA's proposal to incentivize developers, REHDA made suggestions on how the government can assist developers in making homes more affordable. For one, REHDA called on banks to make loans more attainable for the poor and loan terms more flexible. They proposed the direct transfer of buyers' EPF savings excess of Basic Savings to developers to cover the down payment. Also, REHDA suggested that the government increase the supply of affordable homes by using government land for these developments. The 2019 budget did include the REHDA suggestion of adjusting loan terms but did not address utilizing EPF savings or government land.

First-time homebuyers and the lower-income group are the intended beneficiaries of the government's 2019 budget. To help lower-income, first-time home buyers, Bank Negara Malaysia set up a RM1 billion fund. The fund will help first-time home buyers earning less than RM2,300 per month purchase homes priced up to RM150,000 by making the requirements to obtain a loan less rigid and reducing the monthly payments they will pay as borrowers. The government predicts that these measures will provide between 7% and 11% cost savings to home buyers. Overall, it is evident that the new Malaysian government took the suggestions of both the HBA and REHDA into serious consideration when developing the 2019 budget.

Transportation

In addition to adjusting affordable housing policies, the 2019 budget proposed efforts to reduce transportation costs to help increase disposable income. Research indicates that inefficient and unreliable transportation often stands in the way of low-income individuals building a better life. A Harvard study on upward mobility found that a low-income family has a worse chance of escaping poverty if the average commute time in their county is high (Chetty and Hendren). A lack of public transportation may require more personal vehicle reliance, thereby leading to lower disposable incomes. If having a car is less important because of the transportation infrastructure, then the relevance of the wealth gap related to that asset class may fall.

The government's strategy for improving transportation infrastructure is improving public transportation so that it is a suitable substitute for private car ownership. To do so, RM250 million is being allocated to introduce affordable unlimited public transportation and bus passes. The government also is working to improve the efficiency, quality, and coverage of its public transportation services. While this scheme is predicted by the government to immediately increase the real disposable monthly income of households, it will benefit only those living in Kuala Lumpur, where all the targeted transportation services are located. Therefore, this campaign directly omits low-income households living in rural areas. According to the KRI, urban households in Malaysia were 70% richer than their rural counterparts on average. Thus, it would be in Malaysia's best interest to include rural areas in its efforts to improve transportation services. Overall, it is encouraging that the Malaysian government is focusing its poverty assistance polices on asset classes, rather than flows such as income.

Conclusion

Malaysia is continuing to make strides toward becoming a high-income country, and it is essential for the government to comprehend how all Malaysians are experiencing the country's development. Evidence suggests that the improving national economic indicators about which the government boasts are somewhat misleading and not representative of the entire Malaysian population. The government's use of an overly narrow inequality benchmark has resulted in a gap in perception between the government and the public; the government believes inequality is improving, yet the general public believes inequality is not improving or even may be worsening. The dichotomy between government and public perception is fueled by the worsening *wealth* inequality in Malaysia. The detrimental combination of increasing absolute gaps in income and increasing expenditures that disproportionately affect the poor has made it consistently more difficult for poor Malaysians to accumulate wealth.

As the gap between government and public perception on income inequality has become more apparent, researchers have started to dig deeper into evaluating the true inequality in Malaysia. The government took that research into consideration for the Annual Budget 2019, and introduced several initiatives focused on housing and transportation with the intention of increasing the disposable income of the poor. The new initiatives are overall a step in the right direction; nevertheless, some holes remain. For instance, the government is continuing to fund PR1MA, which targets middle-income households. As rising housing inflation is disproportionately affecting the poor, it is clear that the target of housing policies should be low-income households, not middle-income households. Moreover, the government's efforts to improve public transportation are focused on Kuala Lumpur, the richest district in Malaysia. Because rural households are significantly poorer than urban households in Malaysia, focusing initiatives on increasing disposable income in exclusively urban areas will only increase the rural-urban gap further. While the Annual Budget 2019 is imperfect, it is certainly positive that the government is recognizing the importance of wealth to the well-being of Malaysians.

For the Malaysian government to fully comprehend the lived experiences of Malaysians, they must stop relying on one single inequality metric. It is clear that the Gini coefficient of household income is too narrow and does not capture the wealth gaps among Malaysians. I recommend that the government start tracking changes in the distribution of asset classes, such as property purchases, car purchases, and retirement savings. A country-wide collection of data on these metrics would give the government a more thorough understanding of inequality. Overall, if the Malaysian government were to expand their inequality metrics, they would have a more comprehensive approach to policy design and the tools necessary to accurately present Malaysia's progress as a country.

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