

# Foreign Workers in Malaysia

## Assessment of its Economic Effects & Review of the Policy and System

Chiba, Japan

2<sup>nd</sup> - 6 September , 2013



Ministry of Human Resources, Malaysia

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# Human Capital Development Planning framework

## DELIVERY SYSTEM

- Education
- Training

### Education:

- Early childhood
- Preschool
- Basic education

### Tertiary:

- University
- Colleges
- Polytechnics
- TEVT

Flow

Stock

Labour Force



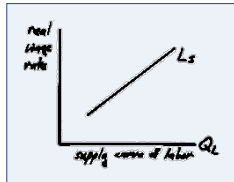
## LABOUR MARKET OPERATION



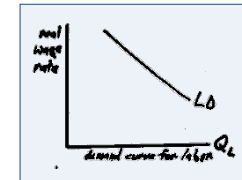
Issues

- 1 Unemployment
- 2 Competitiveness
- 3 Wage Flexibility
- 4 Critical Skills
- 5 Manpower requirements
- 6 Labour Mobility

Labour Supply



Labour Demand



Elasticity of employment and output by economic sector



Economic Growth by Sector

Factor Intensity



Production Technology

Population growth

+

Immigration

Cohort component method to estimate population

- Prices of Labour + Capital
- Industrial Incentives
- Labour Legislation
- Fiscal & Monetary Policy
- Exchange Rate

Capital

+

Labour

Elasticity of substitution between labour and capital

# Data Instrument

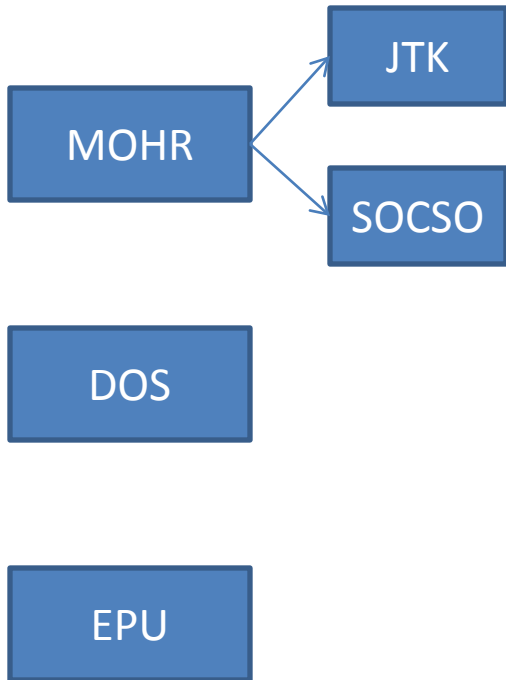
- Measure current distribution of various skills sets (technical, cognitive, and non-cognitive) in the labor force and compare to the demands by employers across economic sectors
  - New household survey instrument or customized modules in the LFS
  - New firm-level survey instrument or customized modules in the NER

# Overall Scope

## Data Sources

## Quality Assurance Framework

## Labour Market Information (LMI) Indicators and Statistics

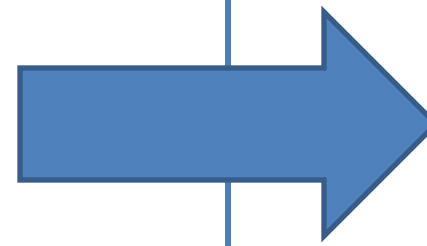
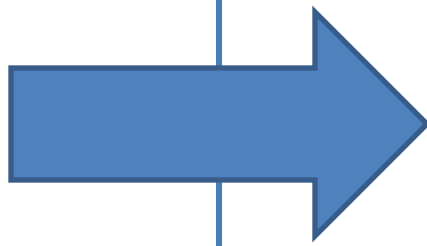
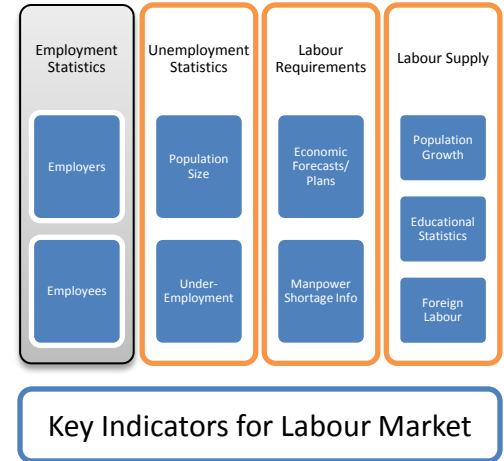


### Filtering

- Relevance
- Accuracy
- Timeliness
- Accessibility
- Interpretability
- Coherence

### IT & Coding

- Database Integration & Standardization
- Integration Process Flow



# Detailed Flow

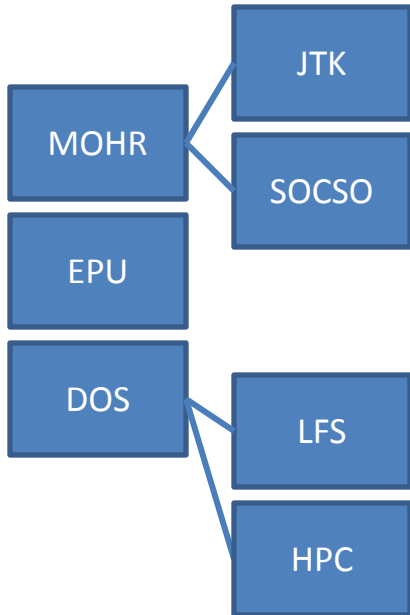
## Data Quality Assurance Framework

- Relevance
- Accuracy

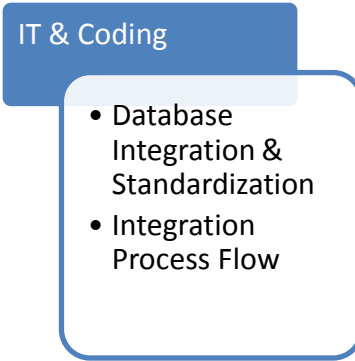
- Timeliness
- Accessibility

- Interpretability
- Coherence

### Data Source



### Process

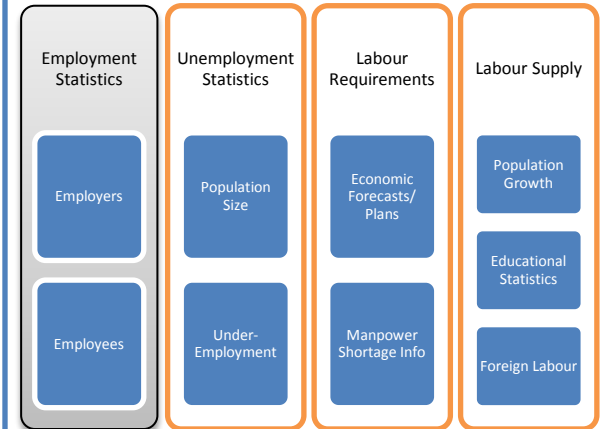


### Storage

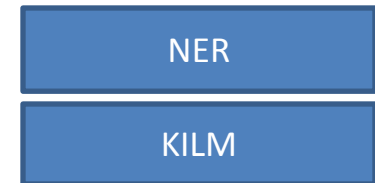


### Result

#### Indicators/ Statistics



#### Feed Into

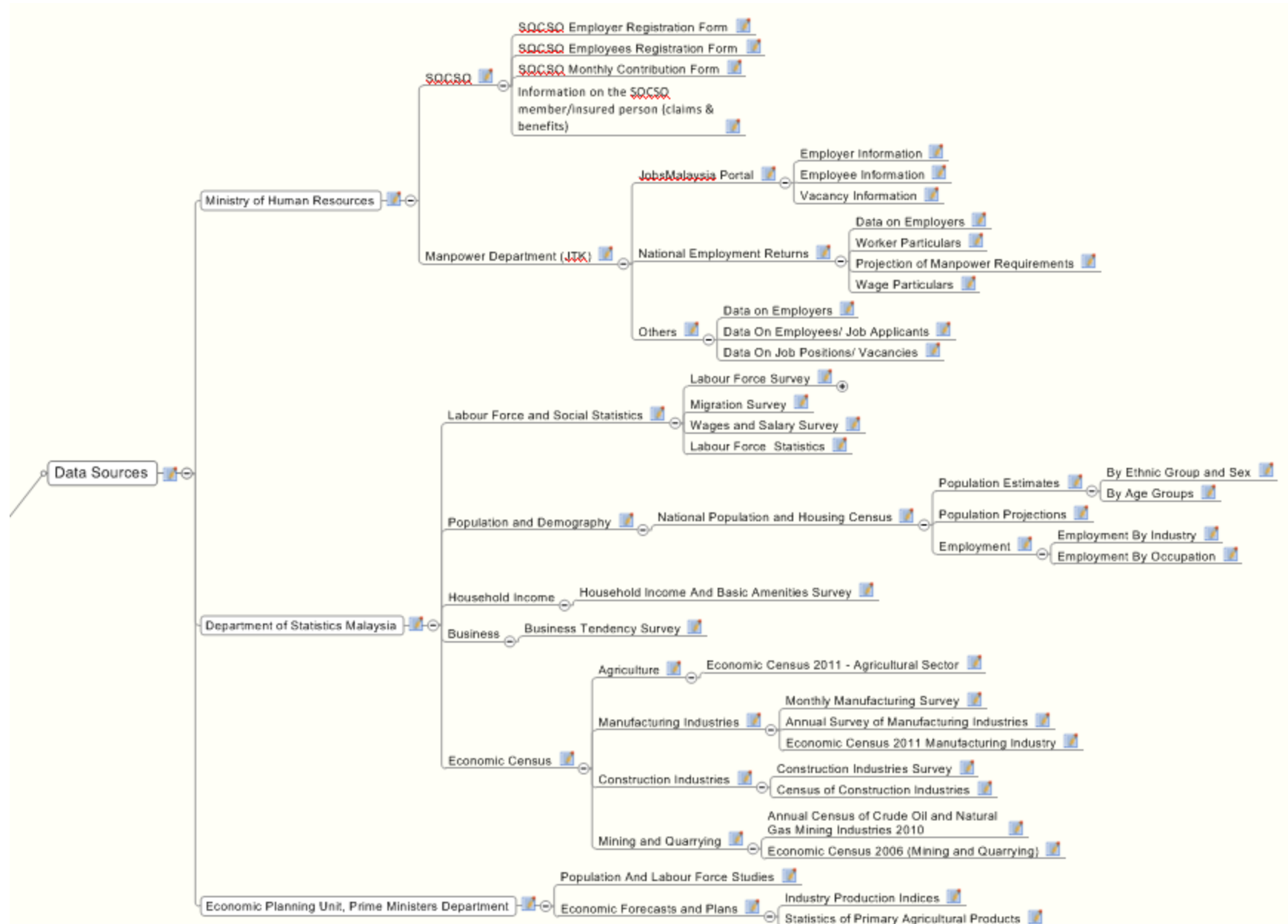


Data Acquisition

Codification

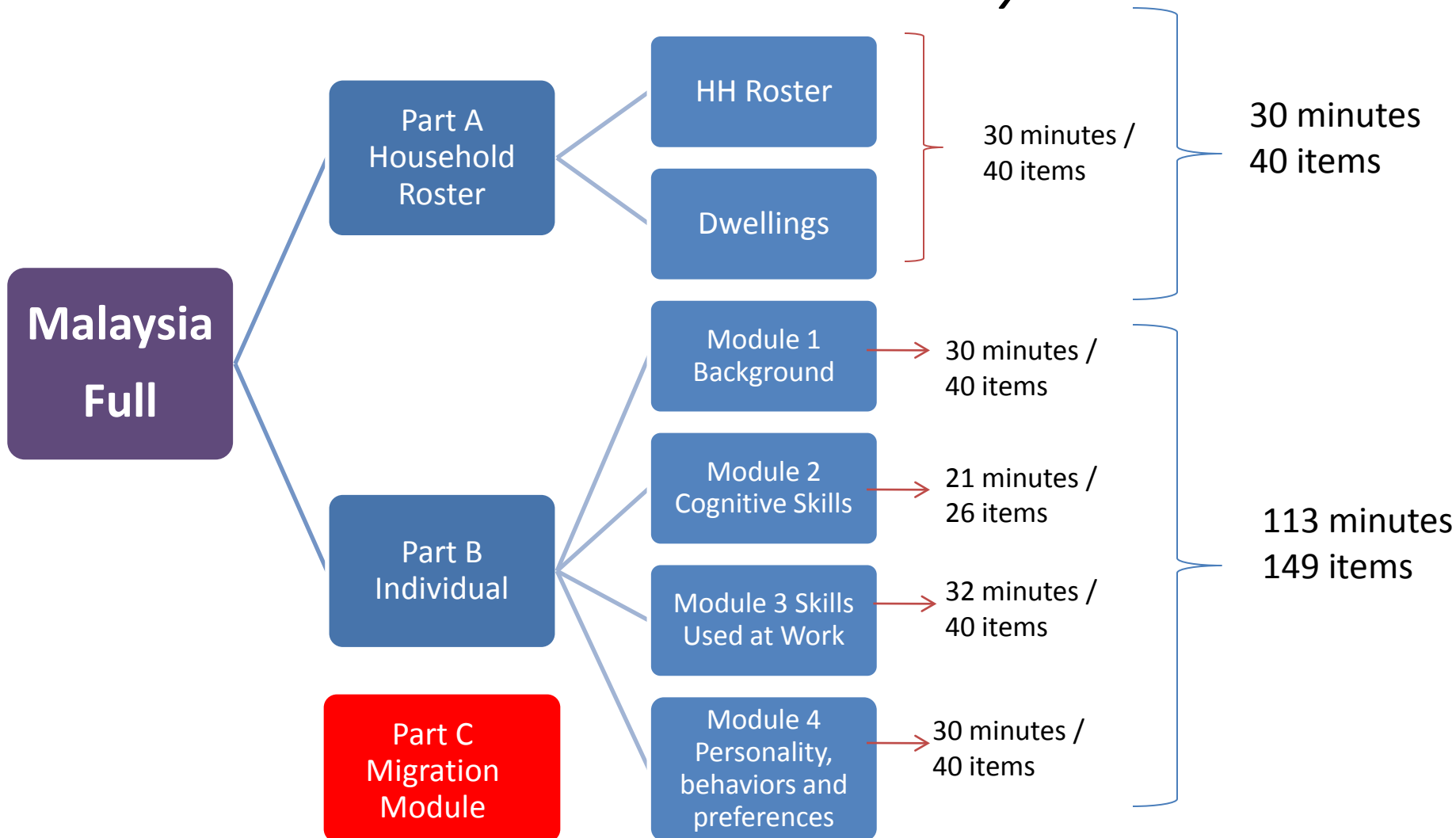
Presentation

# Data Sources (Section 7)



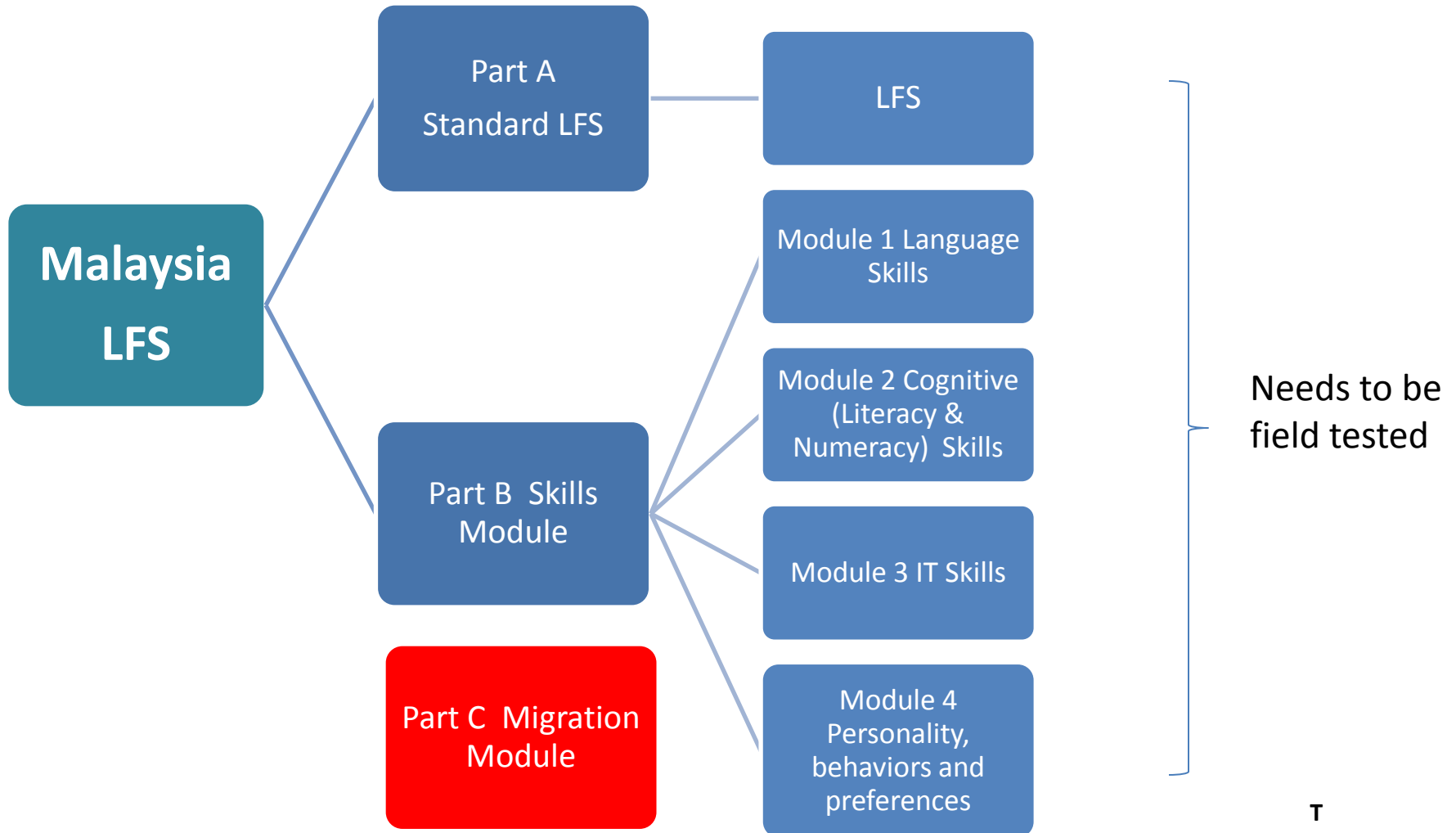
# Individual Survey

## *Stand-Alone Survey*



# Individual Survey

## *Labor Force Survey*

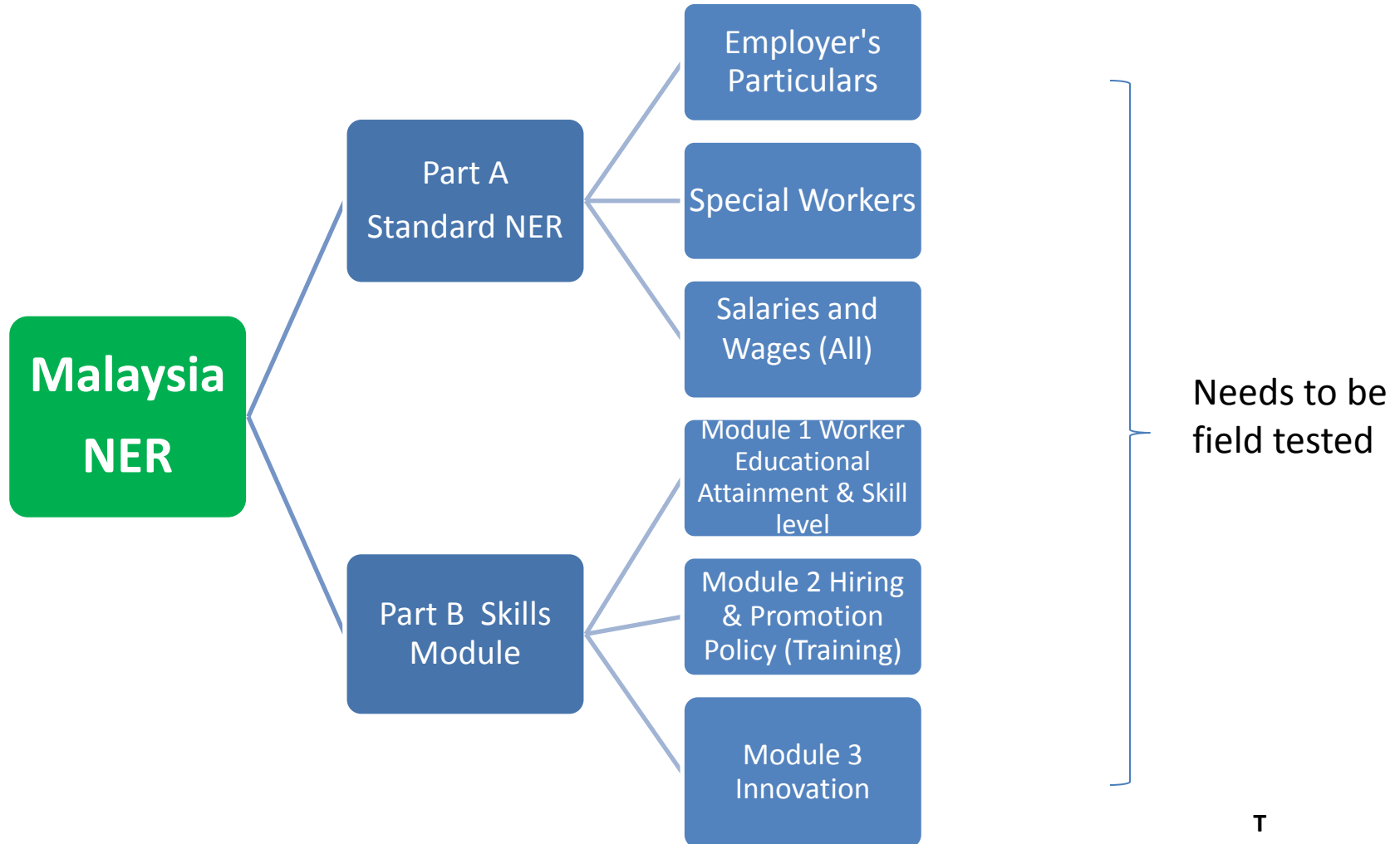


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# Employer Survey

## *National Employment Return Survey*



T

# Data Information

- Monitor the progress of the NER data collection
- Define how to move the household survey forward: With DOS or independently
- Finalize methodological approach for measuring mismatch
- Explore other data sources and method of assessing mismatch (e.g. tracer study)

# Malaysia Already Has a Strategy

## Principles

- Improving the quality of education from pre-school through university
- Having better educated and trained teachers with stronger incentives
- Providing more autonomy and accountability for schools
- Up-skilling the current workforce
- Mainstreaming TVET while upgrading quality of qualifications
- Ensuring opportunities for drop-outs at basic and secondary levels



# **FOREIGN WORKERS IN MALAYSIA**

## **MAIN DETERMINANTS**

# Education levels in Malaysia improved drastically over the last 20 years

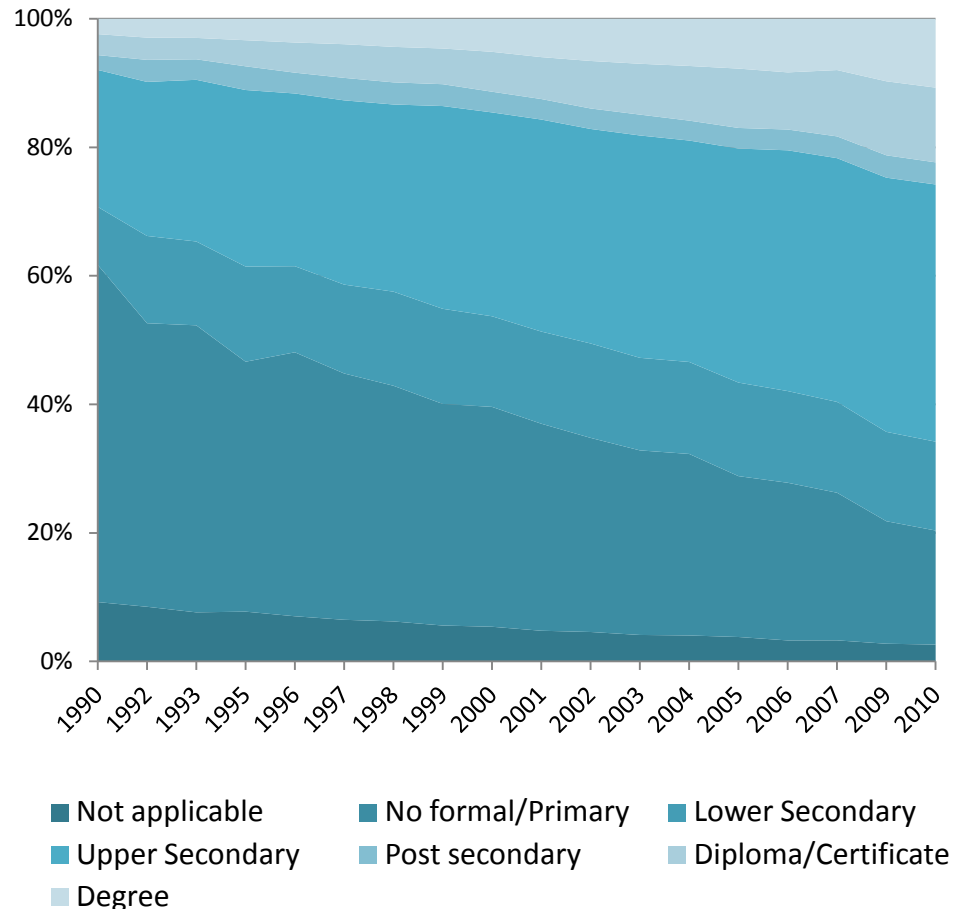
One of the most remarkable features of the Malaysian experience has been the advances achieved in education levels of the labor force over a very short period.

The share of Malaysians with (at most) primary school education declined from 61% in 1990 to 26% in 2010

The share of secondary educated (at most) increased from 34% to 56%.

The share of college educated increased from 5% to 18% in the same period.

### Education distribution of Malaysian workers



Note: The analysis is focuses on the working age population (15 to 64 years of age)

## Education levels of younger workers improved even faster

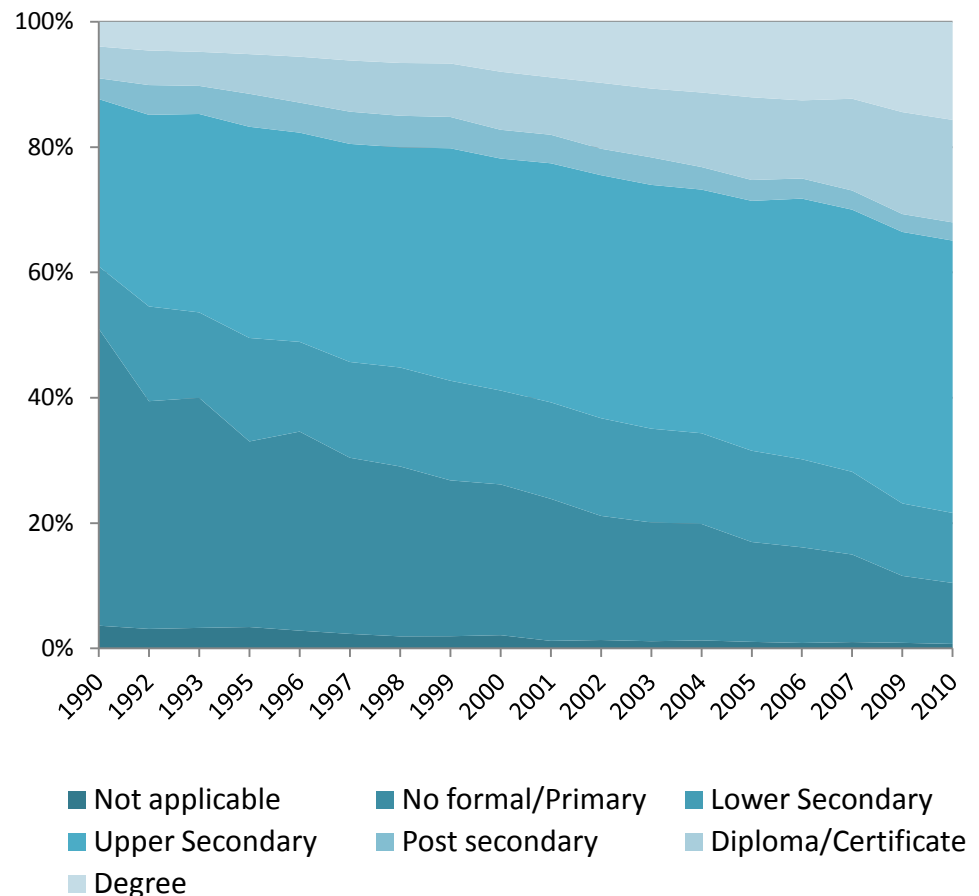
The increase in the education levels of the new entrants to the labor market - 25-35 age group - has been even more remarkable.

In 1990, over 50% of young workers had primary education (at most), 40% had secondary education and less than 10% had tertiary education.

In 2010, around 10% had primary, over 60% had secondary and close to 30% had tertiary education.

**The remarkable expansion of formal education and human capital levels led to changes in job preferences of many Malaysians.**

**Education distribution of Malaysian workers (25-35)**



# **FOREIGN WORKERS IN MALAYSIA**

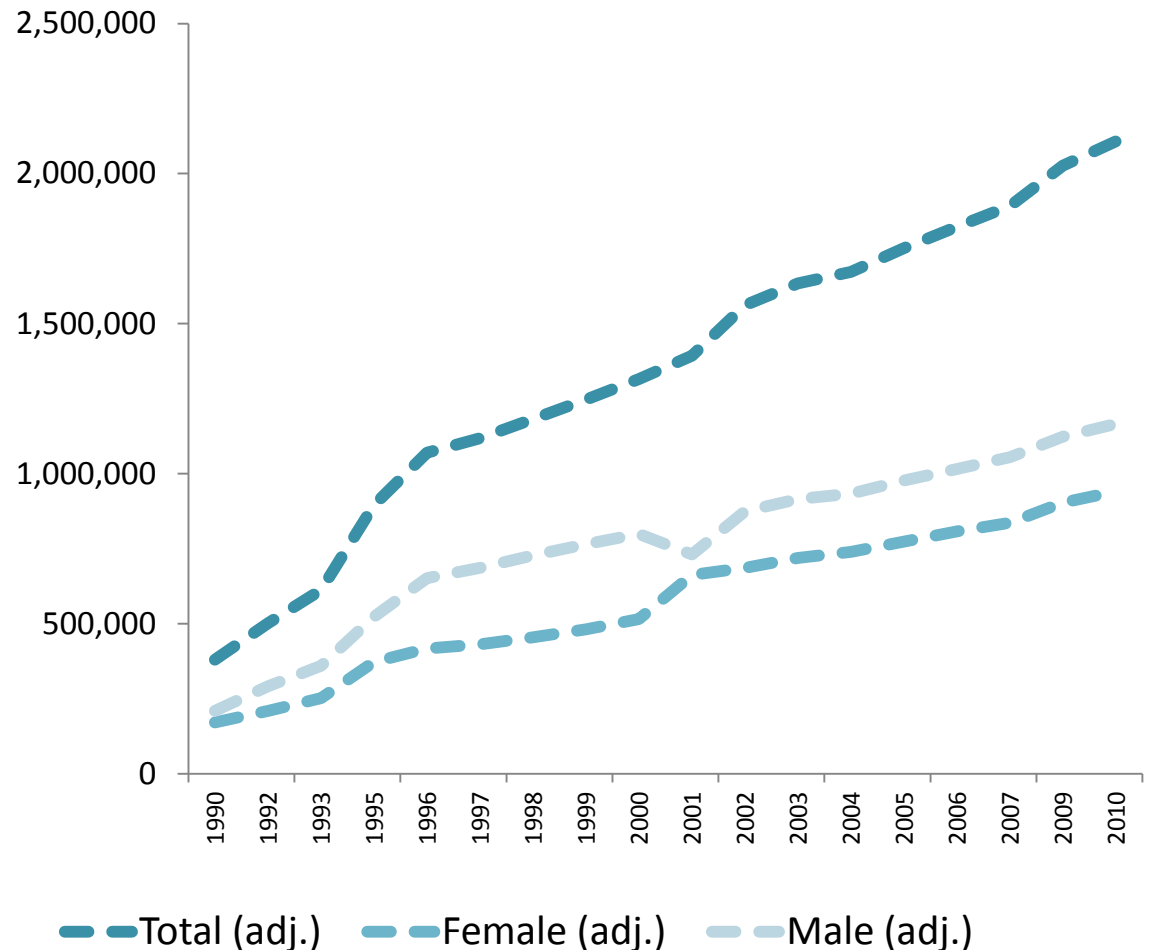
## **PROFILE**

## Labor Force data account for about *2+ million* foreign workers in Malaysia

Inflows of foreign workers have steadily increased since the early 1990s, when the government introduced formal guidelines on foreign workforce management.

Due to large number of unregistered undocumented workers, it is difficult to get a more precise estimate.

### Foreign Workers in Malaysia, 1990-2010



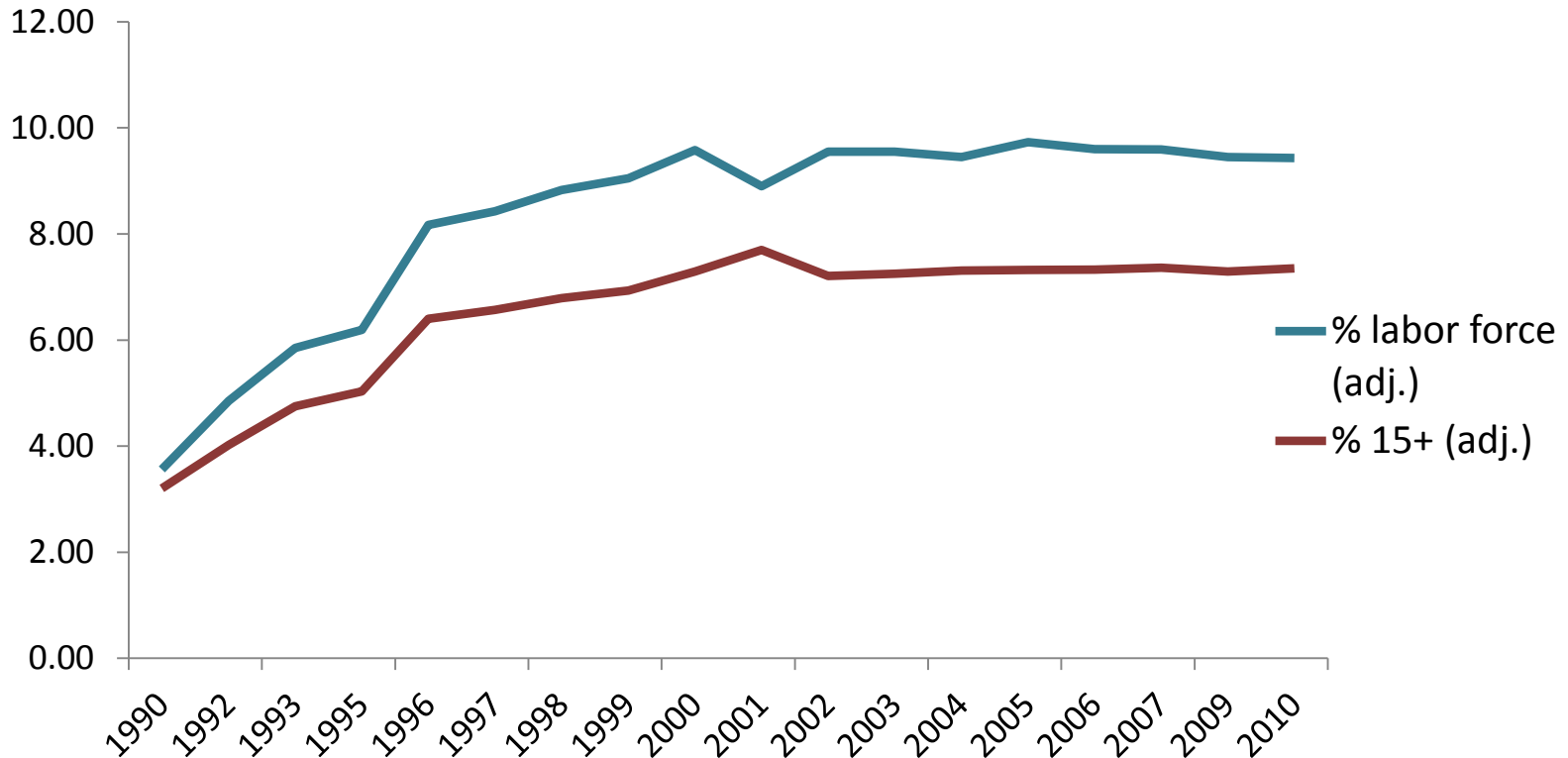


## Foreign workers compose around 10% of the labor force

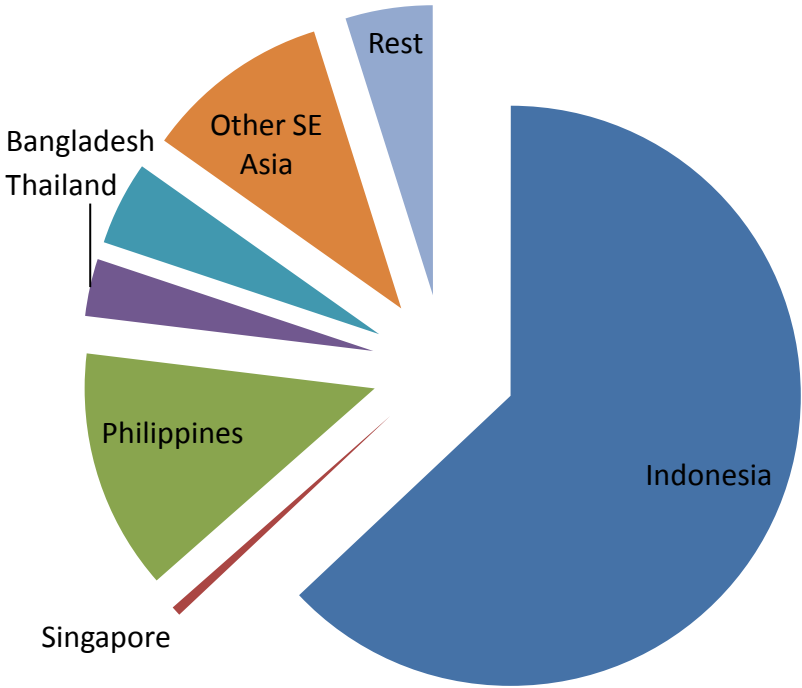
Estates/group housing are excluded from labor force survey.

Other estimates show the total at 18% (NER,2009) and 20% (MOF, 2009).

### Foreign Workers as share of the Labor Force

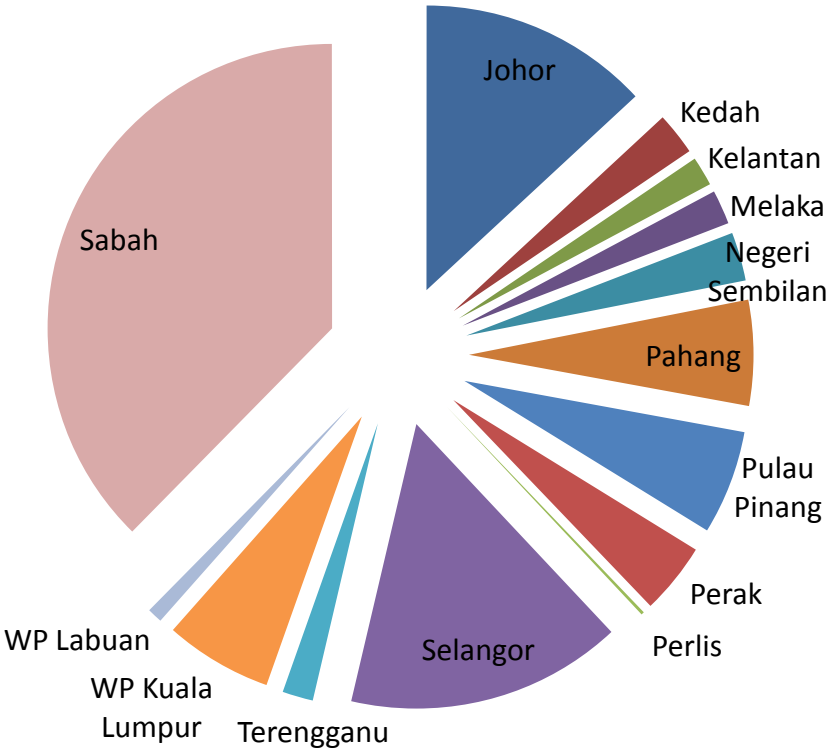


# Indonesia is the main sending country and Sabah the main recipient state



Almost two-thirds of the foreign workers come from Indonesia. The next largest group are from the Philippines (13%).

Nearly two-thirds of foreign workers in Malaysia are in three states – Sabah, Selangor and Johor.

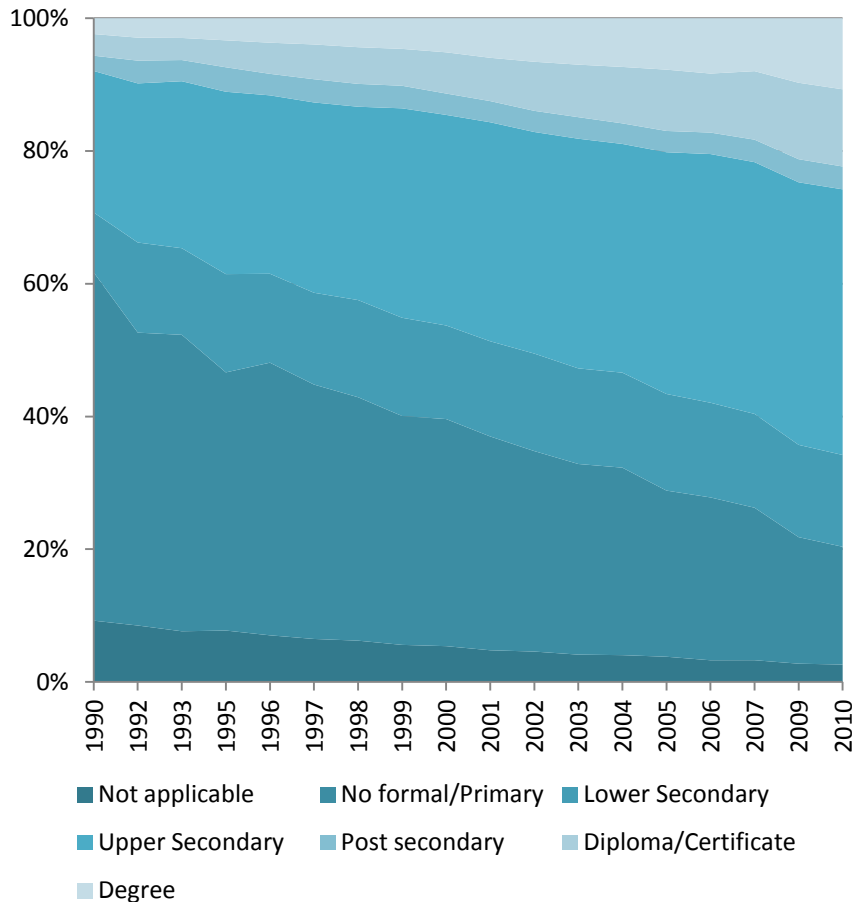




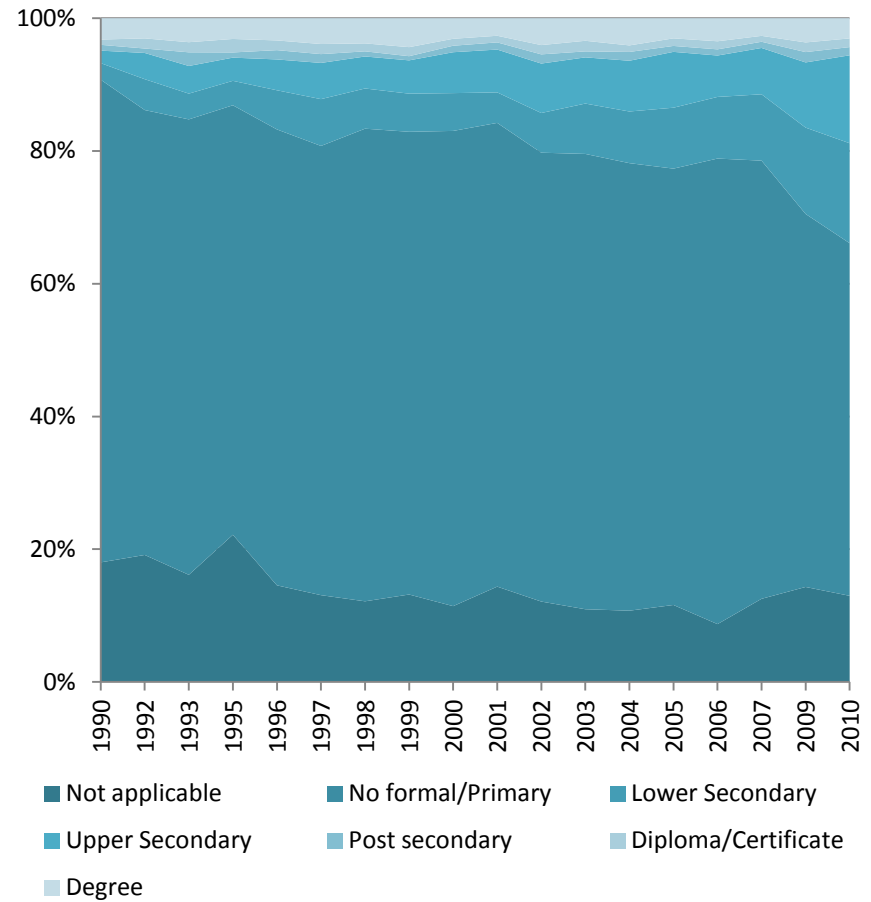
# Foreign workers are significantly less educated than Malaysians...

20 Their educational distributions that have been more stable over time. This pattern is simply due to demand factors in the Malaysian labor market.

**Education distribution of Malaysian workers**

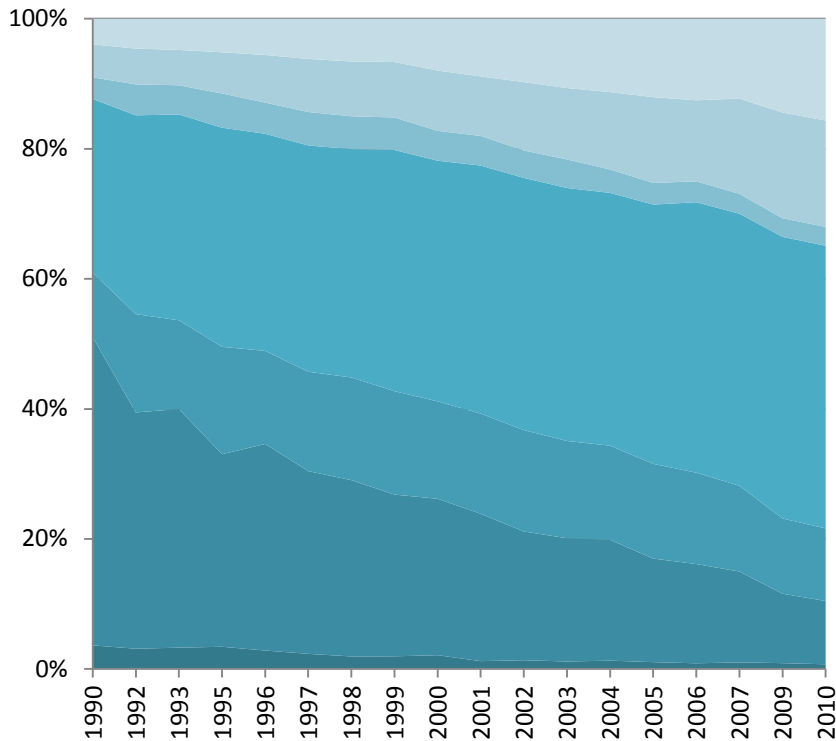


**Education distribution of foreign workers**

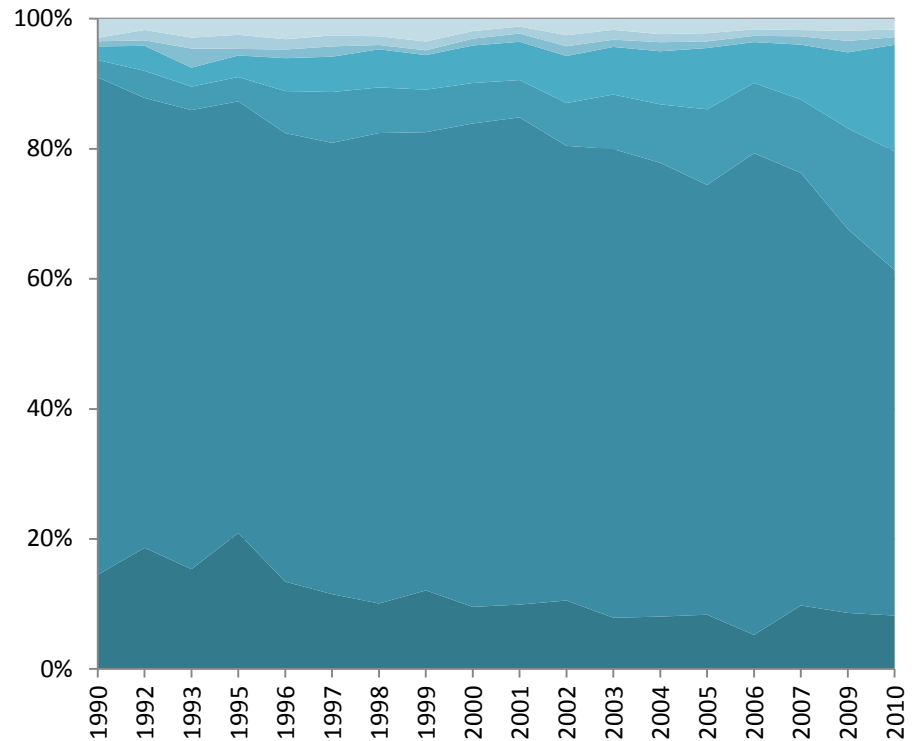


...this is reinforced when we look at workers in the 25-35 age group

**Education distribution of Malaysian workers (25-35)**



**Education distribution of foreign workers (25-35)**



- Not applicable
- No formal/Primary
- Lower Secondary
- Upper Secondary
- Post secondary
- Diploma/Certificate
- Degree

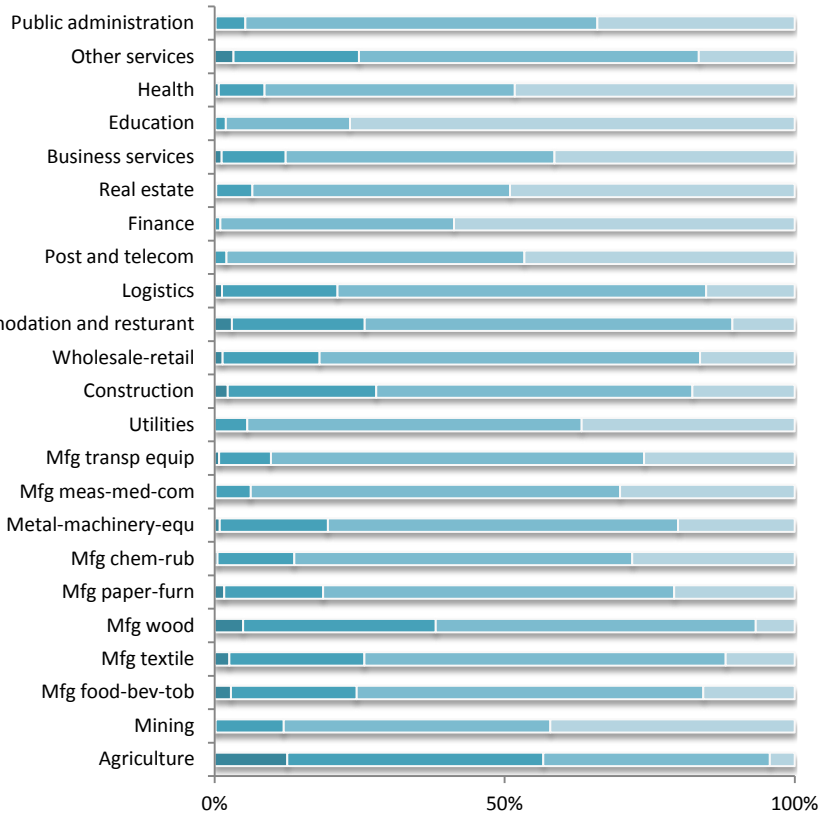
- Not applicable
- No formal/Primary
- Lower Secondary
- Upper Secondary
- Post secondary
- Diploma/Certificate
- Degree

# Labor intensive economic sectors rely on foreign rather than Malaysian labor

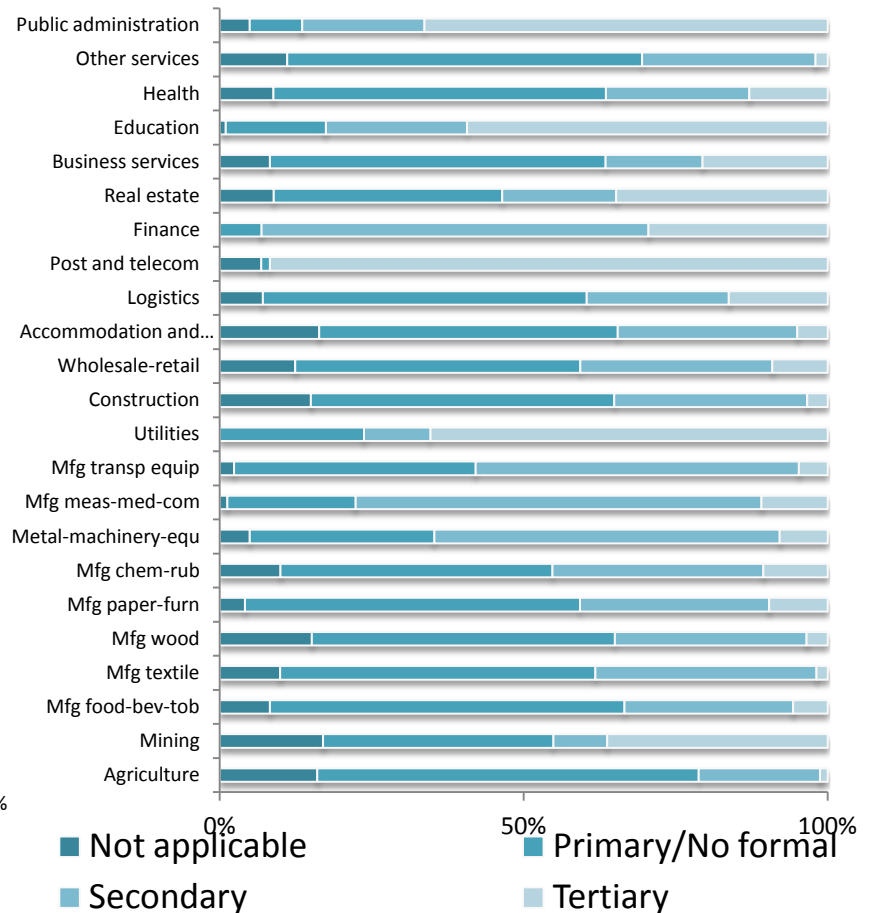
22 Even when employed in capital intensive sectors, foreign workers hold low skill occupations.

## Education Levels by Economic Sectors, 2010

### Malaysian workers



### Foreign workers



Not applicable

Secondary

Primary/No formal

Tertiary

## Pull vs. Push Factors

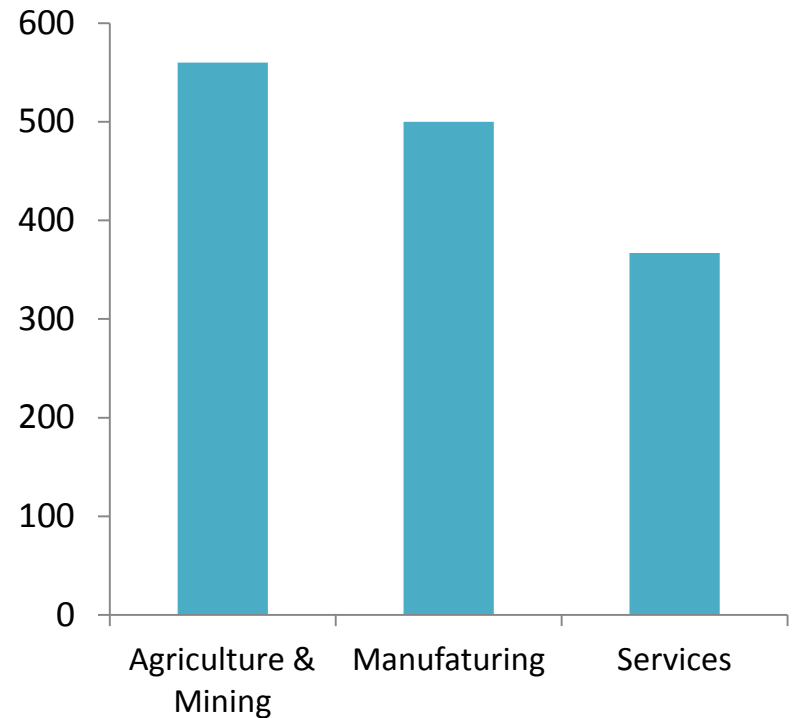
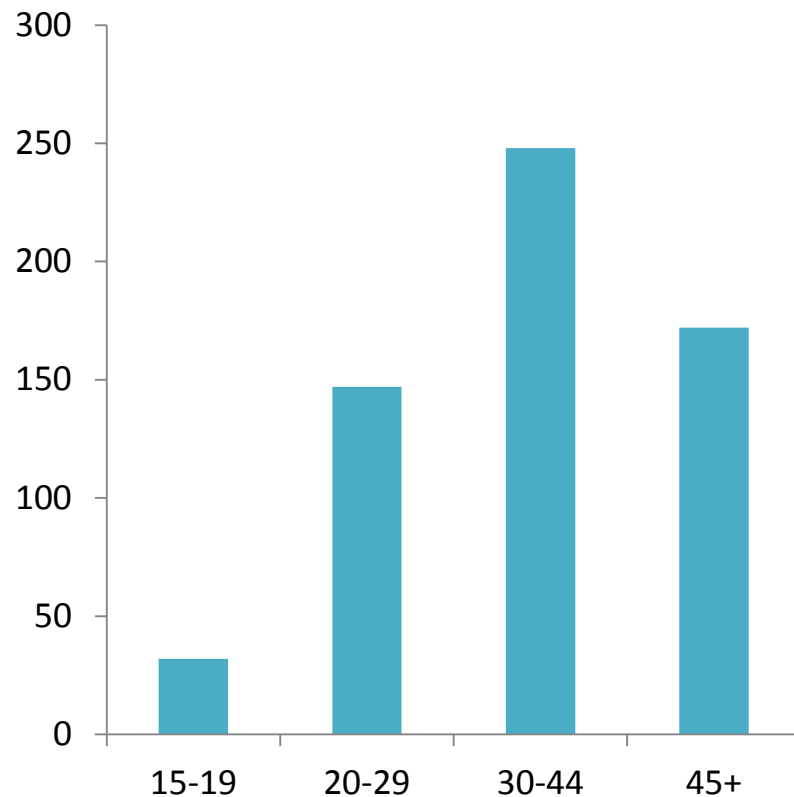
Pull factors in the destination countries and push factors in the origin countries jointly determine the inflows of foreign workers.

These two effects need to be separated to identify the effect of foreign labor on economic outcomes in destination countries.

Using demographic data from the main origin countries and historical migration patterns by sector and state, our econometric methodology is able to identify the **causal effect of foreign labor** on the labor market outcomes in Malaysia.

## Effects are heterogeneous across age groups and sectors

Small effect on young workers, while much larger positive effect on other age groups.

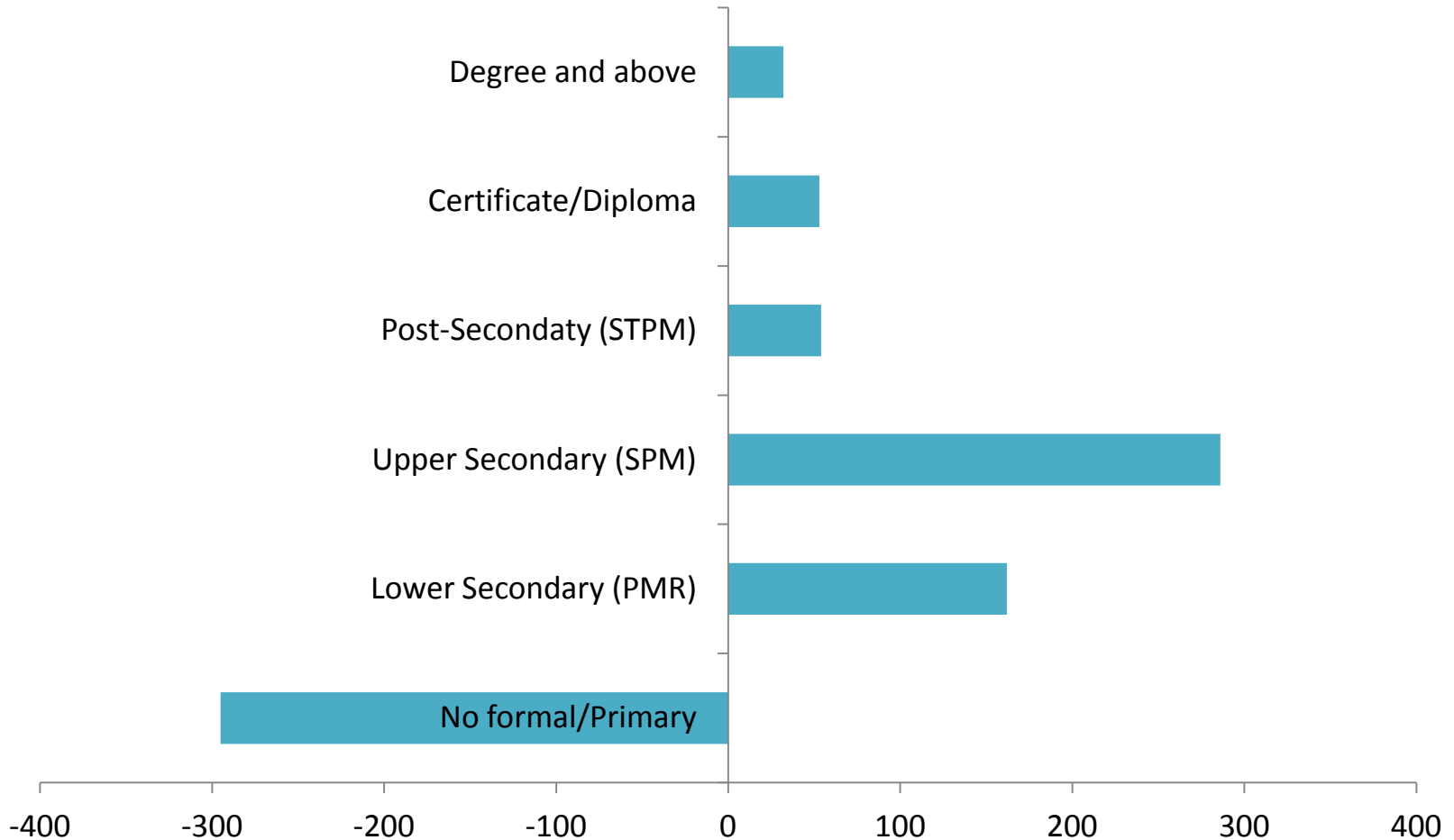


The employment of foreign workers leads to increased employment of Malaysians in every major sector.



## Effects Also Differ Across Education Categories

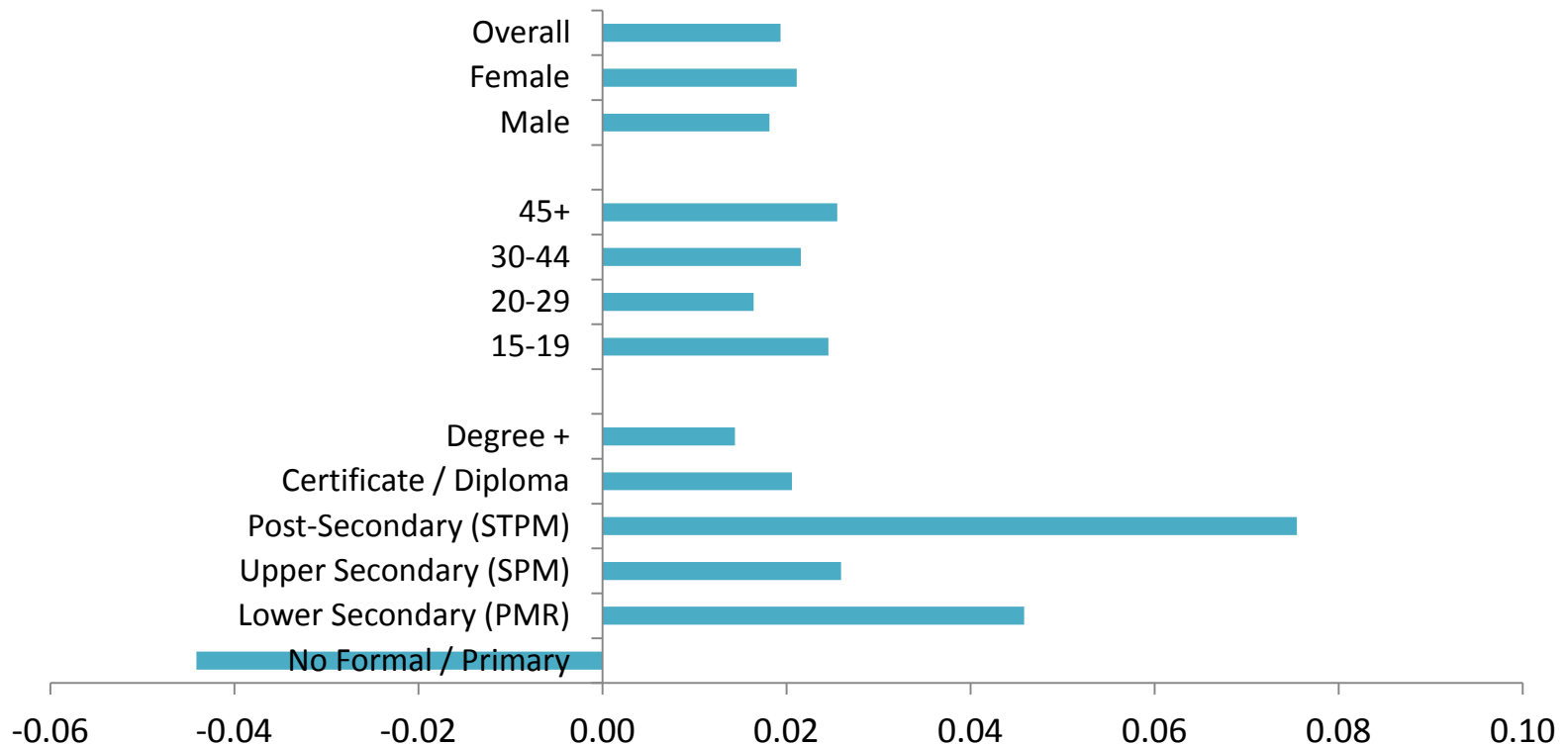
Low educated/unskilled workers are hurt, while the impact on tertiary educated are much smaller. The main beneficiaries are Medium Skilled/Educated Workers.



## Impact on Wages of Malaysian Workers

Changes in employment due to increases in employment of foreign workers (for a given region and sector) do not lead to significant changes in the wages of Malaysian workers, mainly due to tightness of labor markets

Personal characteristics (age, gender, education) play a role on how much Malaysians can benefit in terms of higher wages.



## When additional Foreign Workers enter Malaysian labor market...

- ❑ The main effect is re-allocation from other sectors and regions. Entry of foreign workers into a sector leads to further expansion by employment of additional Malaysian workers.
- ❑ There is no contraction in national employment levels of Malaysian workers.
- ❑ Malaysian workers' wages increase by a small amount.
- ❑ Existing Foreign workers' wages decline considerably.

# **POTENTIAL IMPACT OF POLICY CHANGES**

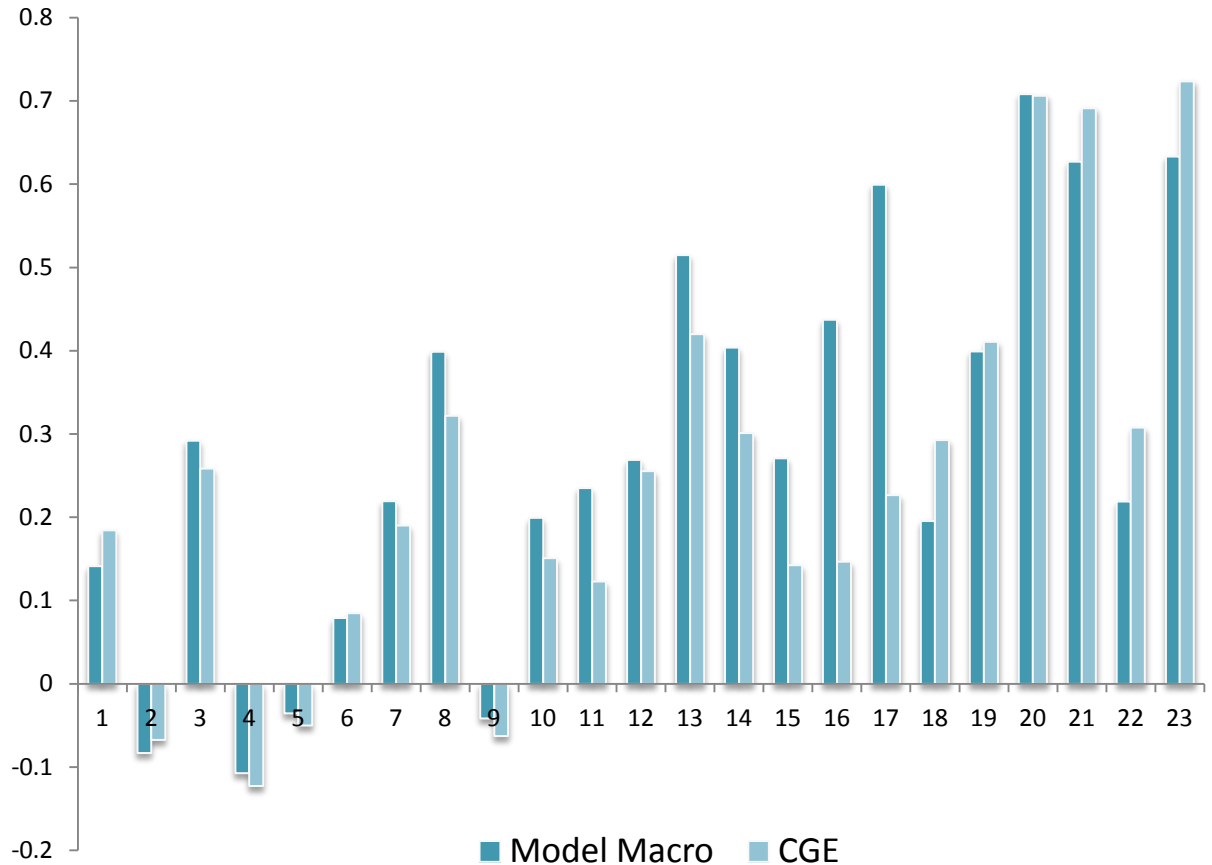
## Goals of the Computable General Equilibrium (CGE) model

- Detailed model of production with 23 sectors and 21 separate skill categories to capture a wide range of policy options.
- Simulate different levy scenarios – as well as from whom they are collected.
- Identify the effect on macroeconomic variables – growth, investment
- Identify the effect on wages and unemployment of Malaysian workers in different sectors and different skill levels.
- Identify the effect of minimum wage policies on these variables.

# The Model Has 23 sectors

## Sectoral Growth Rates 2005-2010

- 1 AGRICULTURE**
- 2 MINIG**
- MANUFACTURING**
- 3 Mfg food-beverage-tobacco
- 4 Mfg textile
- 5 Mfg wood
- 6 Mfg paper-furniture
- 7 Mfg chemical-rub
- 8 Metal-machinery-equip
- 9 Mfg measurement-med-com
- 10 Mfg transport equip
- 11 UTILITIES**
- 12 CONSTRUCTION**
- SERVICES**
- 13 Wholesale-retail
- 14 Accommodation and restaurants
- 15 Logistics
- 16 Post and telecom
- 17 Finance
- 18 Real estate
- 19 Business services
- 20 Education
- 21 Health
- 22 Other services
- 23 Public administration



# The Model Has 21 Educational Categories Tracked Over Time

## Skill Levels

**Lower Skill** - Secondary or less

- 1 No schooling
- 2 UPSR/UPSA equivalent
- 3 PMR or equivalent
- 4 SPM or equivalent
- 5 STPM or equivalent

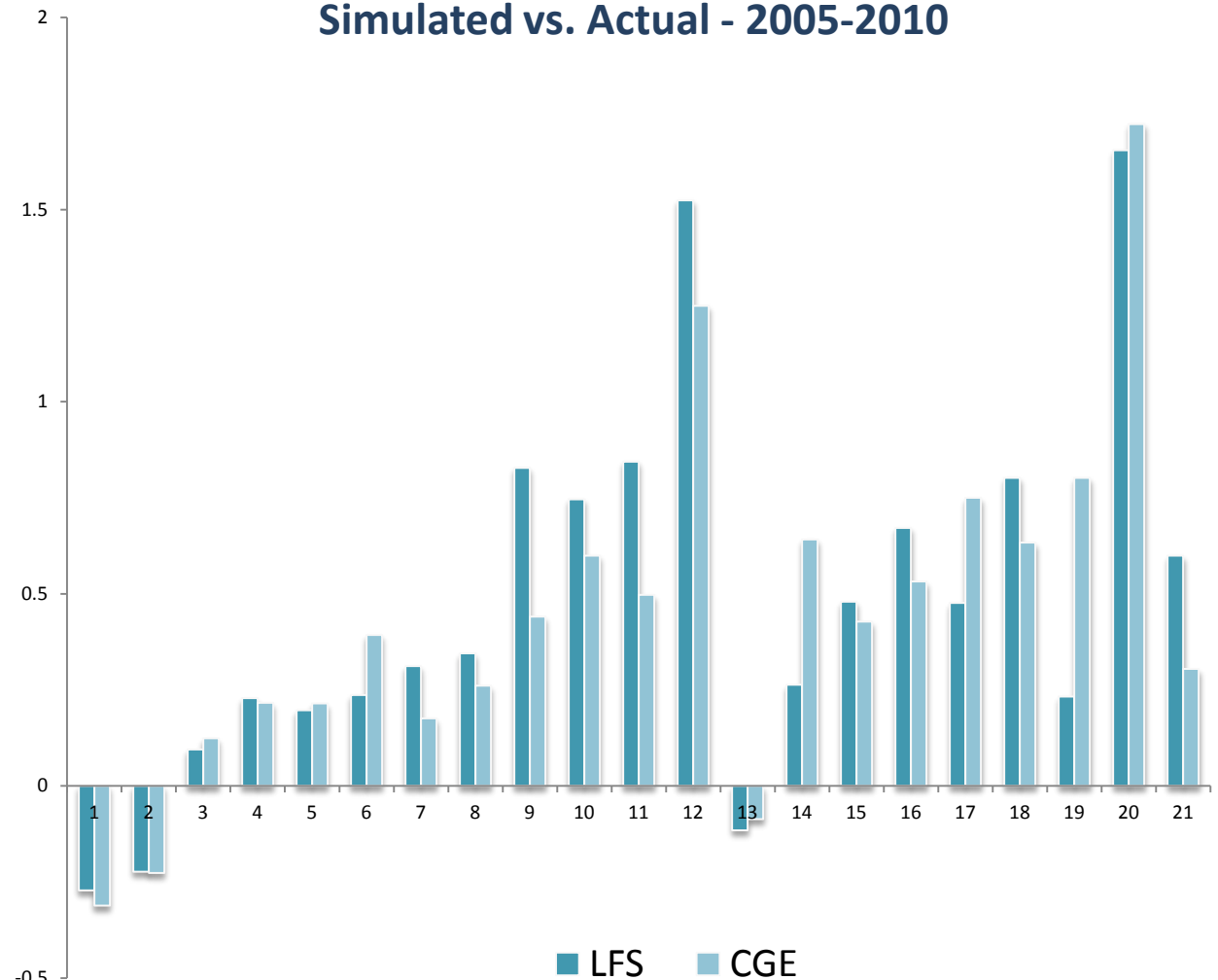
**Medium Skill** -Certificate/Diploma

- 6 Arts & Humanities
- 7 Social science, business, law
- 8 Science, math, IT
- 9 Engineering
- 10 Agriculture
- 11 Health
- 12 Services

- 13 Education
- Higher Skill** -University Degree
- 14 Arts & Humanities
- 15 Social science, business, law
- 16 Science, math, IT
- 17 Engineering
- 18 Agriculture
- 19 Health
- 20 Services
- 21 Education

## Evolution of Labor Supply by Skill Level

### Simulated vs. Actual - 2005-2010



## Minimum Wage Implementation and Levy Collection

- **Minimum Wage Deferral for Foreign Workers – March 2013:**

The Malaysian government has approved the **delayed implementation** by small and medium-sized enterprises (SMEs) of **new minimum wage standard** for their **foreign workers**. The National Wages Consultative Council, which is responsible for the implementation of the standard, said in a statement that the employers in SMEs are permitted to defer the implementation until Dec. 31.

- **Levy to be Paid by Foreign Workers– January 2013:**

“The minimum wage, which came into force this year has raised the salary for all workers on an average of between 30 per cent and 50 per cent, or from RM600- RM700 per month to RM900 monthly.”

“The Government’s move to **impose a levy on foreign workers** will not be a burden to them as the levy paid is between RM34.16 and RM154.16 per month as compared to a salary increase of between RM300 to RM500 per month”

Second Finance Minister Datuk Seri Ahmad Husni Hanadzlah



**FOREIGN WORKFORCE MANAGEMENT  
POLICIES AND COMPARABLE SYSTEMS**

## Designing Immigration Policies

Building an immigration system is a complex task with repercussions on a multiplicity of spheres.

Learning from other countries is important, but a one-size-fits-all approaches do not exist.

**Key factors** to take into account are:

1. **Age structure and dynamics** of the population
2. **Labor Market** conditions (unemployment, labor force participation, wage growth, etc...)
3. **Education levels** of natives and migrants (supply, demand and skill gaps)
4. **Geographic and cultural** factors

## Flexibility of Policy Regime

**Institutional bodies in charge of immigration need the flexibility to respond to sudden changes in the economic environment.**

Basic levies, fees and taxes can be used to influence total number of foreign workers.

Differential levies can be used to channel foreign workers to targeted sectors which face shortages and have national priorities.

**South Korea** has a very flexible approach with sector specific quotas revised regularly.

The **Singaporean** system is regularly adjusted based on market conditions by using the foreign workers levy system that differs by sector, skill and firm size.

**Malaysia:** annual **levy** system and **quotas** at the sectoral and sub-sectoral level. This system does not fully respond to underlying market conditions and their rapid evolution.

## Consultations with stakeholders

Policy decisions should be taken in consultations with key stakeholders, in particular the private firms in sectors that critically depend on foreign labor. Such consultations should take place on a regular basis and be clearly structured.

In **Singapore**, extension of the maximum employment period for foreign low skilled workers (from 6 to 10 years) to maximize productivity gains.

In **Australia** every a list of occupations in need is compiled in consultation with representatives of unions and industries.

In **Canada**, reports of consultations with unions, employers and experts are made public.

**Malaysian** stakeholders revealed that consultations are ad-hoc and do not effectively inform the government of market conditions on a regular basis.

## Preventing Undocumented Workers

A country should remove the economic incentives (created by high levies/visa fees, high minimum wages ) for undocumented migration by:

- (1) having repercussions for employers hiring undocumented workers
- (2) imposing reasonable costs and fees for employing documented foreign workers so that incentives for undocumented migration stays low
- (3) having in place a clear legislation regulating the activities of *migration agencies*

In **Malaysia**, several measures to prevent illegal migration (Anti-Trafficking in Person Act, stricter conditions for private agencies to be licensed by MOHA, implementation of a new regularization (6P) program).

Only countries with natural barriers (e.g. **Australia**) can properly manage to limit undocumented migration.

In countries with large porous borders (**United States** and **European Union**) unskilled workers have relatively easy access through irregular channels.

# **KEY POLICY MESSAGES**

## Underlying Economic Environment is Key

Malaysia's rapid economic growth accompanied with labor market shortages for unskilled workers continue to attract foreign workers from neighboring countries.

The differences in growth differentials and overall educational gaps between the labor forces of Malaysia and its more populous neighbors, such as Indonesia and the Philippines, are the key pull and push factors that fuel the current migration patterns.

Appropriate policies need to be designed with these economic fundamentals in mind.

## Policy Adjustment Should be Gradual

An abrupt disruption of foreign unskilled labor supply could cause unpredictable effects in the economy.

Since unemployment levels are low and vast majority of the Malaysian workers do not compete with foreign workers, benefits to domestic workers from a decline in the inflow of foreign labor are limited.

Thus, the government is highly encouraged to review its foreign workers program and design nuanced policies to accommodate the economy's particular needs by sector and human capital categories.



## Certain firms & sectors depend on Foreign Workers

Large number of firms in labor intensive sectors would not exist without the cost advantages provided by low-skilled low-cost foreign labor.

Given the types of activities and markets that some of these companies operate in (low value added), they will continue to rely heavily on low skill (low cost) foreign labor in the foreseeable future.

Without foreign labor, these sectors would simply disappear and lead to unemployment of significant number of mid-skilled local workers in the short to medium term.

## Impact of Foreign Workers is ....

Positive on average for both Malaysian workers and Firms.

The main negative impact is on low skilled workers and small firms.

The main positive effect is on medium skilled workers and larger firms, especially in manufacturing.

The effect is smaller on female, younger or highly educated workers.

## Discussion of Policy Tools: Levies Vs. Quotas

### QUOTAS

Almost every government in the world uses quantitative restrictions to control the number of migrants and foreign workers entering their jurisdictions.

Economics literature and policy discussions are full of examples showing why price mechanisms – taxes, tariffs, levies – can be more efficient and effective than quantity restrictions.

## Levies Vs. Quotas

### LEVIES

Levies provide flexibility to government agencies to respond to sudden changes in the economic environment.

Levies allow governments to raise revenues as a taxation mechanism. This revenue would otherwise accrue to the recruiting agencies and employers. They can be used training, enforcement and other objectives related to foreign worker policies.

Levies can act as wage stabilization mechanisms and provide balanced wage growth paths.

## Who might oppose the Levies?

Recruitment agencies capture a portion of the “quota rent” (difference between wage in Malaysia and back at home).

They are likely to oppose a regime based on levies! But their role is critical in design and implementation of efficient system that also minimizes undocumented flows.

They should also be better supervised and rules enforced.

## Also focus on Higher End of Skill Spectrum

There are also skills gaps on the higher end of the labor market spectrum.

It takes a long period for the education and training systems to produce new core skills. It is possible that the country will have to rely on foreign talent to fill these occupational gaps to avoid having bottlenecks.

Government should consider more flexible entry regimes and promising long-term opportunities in order to attract and retain skilled foreign workers, including university students.

## Data Collection is Critical

Another clear lessons to emerge is to invest in the collection of reliable, high quality, regular and detailed data on all workers—local and foreign— and firms to track the labor market conditions, properly understand the effects of foreign labor and evaluate future policy changes.

The data collection program has to be a joint effort of all relevant agencies that are responsible for labor markets, education, taxation and domestic security.

A close-up photograph of a person's hand holding a rectangular sign. The hand is positioned on the left side of the frame, with the thumb and index finger gripping the edges of the sign. The sign is a light beige or off-white color and features the words "Thank You" written in a white, elegant cursive font. The background is a plain, light-colored surface, possibly a table or a wall, which is softly lit, creating a warm and appreciative atmosphere.

*Thank You*