Foreign Ownership in Malaysia - A Look at Issues

Tan Pek Voon
Research Programme, INSPEN
Valuation and Property Services Department

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Abstract

The development of policy on foreign acquisition of Malaysian properties seems to be inconsistent. On one hand, it aims to protect Malaysian interests by restricting foreign ownership in landed properties, and on the other hand the foreign acquisitions of Malaysian properties are welcomed during the economic downturn to stimulate the economy. How significant is foreign ownership to the property market and the Malaysian economy? This paper discusses the contribution of foreign ownership to the property market and the Malaysian economy. It also discusses the potential harm of policy inconsistency to FDI and the economy.

Keywords: foreign direct investment, foreign acquisition, foreign investment committee, foreign acquisition guidelines and foreign ownership

Introduction

Foreign Direct Investment (FDI)[1] has been an important element in the Malaysian economy and is partly responsible for transforming the agriculture based economy to one of manufacturing. In the 1970s FDI played a significant role in the growth of the industrial sector. Its contribution to the economy can be seen in terms of job creation and employment opportunities, skill and manpower training, development of supporting industries, transfer of technologies and providing access to export markets as well as research and development facilities (Sulong, 1990). As such FDI is always welcomed in Malaysia. In 1970 about 60 per cent of the share capital of limited companies were owned by foreigners (Hoffman and Tan, 1980). This has raised concern about the dominant control of the Malaysian economy by foreign enterprises. As a result, the Foreign Investment Committee (FIC) was established in 1974 with the objective of ensuring a balanced ownership and control between foreign and local investors.

Recognising the significant role of FDI to the economy, prior to 1984, foreign ownership of real property was not regulated on the belief that it lent support to FDI. However, out of concern for the high volume of foreign purchases of land and houses in Johor Bahru, (which pushed up the house prices beyond the affordability level of most people), a legislative measure was taken to control such activity. This was reflected in 1984 with the amendment to the National

Land Code (NLC). The main objective of the legislation was to protect Malaysian interest by restricting foreign ownership on registered land or alienated land in West Malaysia. However, the recession of the mid-1980s necessitated the policy to be relaxed, as foreign acquisition was needed to stimulate the Malaysian economy. In 1987, sections in the NLC relating to foreign acquisition were repealed. Since then, there has been a series of tightening and relaxation of the foreign acquisition policy, frequently influenced by the state of the economy.

In the wake of the regional economic crisis and the slowdown in the property industry, the government has relaxed the policy on foreign acquisition of residential properties and lifted the levy imposed on such acquisition (Business Times, 1997). The development of policy on foreign acquisition of Malaysian properties seems to be inconsistent. On one hand, it aims to protect Malaysian interest by restricting foreign ownership in landed properties; whilst on the other hand, the foreign acquisitions of Malaysian properties are encouraged to help stimulate the economy. The questions at issue are first, whether FDI contribution to the growth of the property industry is in proportion to their economic influence derived from their majority command over the country's production capital and second, if it has, whether this should override the original objectives of FIC of ensuring a balanced ownership and control between foreign and local interests.

This paper attempts to provide a discourse on policy issues pertaining to foreign acquisition of residential properties in Malaysia. This paper is divided into four parts. The first part discusses the contribution of FDI to the economy. The second part discusses the role of FIC as a watchdog to the Malaysian interests. The third part traces the developments of foreign acquisition policy and the final part discusses the policy implications.

FDI and the Economy

Malaysia has a long history of foreign involvement in its economy, dating from the pre-independence period. The period of British colonialism was characterised by the dominance of foreign investors, the majority of whom were British. Foreign investments were mainly in the primary sector, trade, transport and utilities (Hoffman and Tan, 1980). After independence, foreign investment in Malaysia continued to be welcomed. This was partly due to the understanding contained in the Independence Agreement between Malaysia and the United Kingdom which stated that "*foreign capital must continue to play an important part in the economic and social development of Malaya*" (Hua, 1983, cited in Edwards, 1994, p 688).

Following independence, in the 1960s, foreign investors were welcomed to develop import substitution industries. Industries that grew rapidly were food and beverages, tobacco, printing and publishing, construction material, chemicals and plastic industries (Sulong, 1990). However, the domestic market was rather limited and reached saturation rather quickly. In the 1970s, the government changed its emphasis to export-oriented and labour intensive industries. In addition to tax concessions which were given to pioneer industries since the late 1950s, the new Investment Incentives Act of 1968, and the Free Trade Zone Act of 1971 were introduced to promote rapid development of Export Processing Zones (EPZs) which were almost dominated by FDI. Consequently, this sector expanded rapidly (Edwards, 1994).

However, by the mid-1980s the Malaysian economy was in recession. The appreciation in the exchange rate and the drop in competitiveness resulted in a fall in the net inflow of foreign investment (Edwards,1994). In 1985, FDI contributed only 0.64 per cent of Gross Domestic Product (GDP). Various measures were introduced to help boost foreign investment. This included, first, the devaluation of the exchange rate of more than 30 per cent in the second half of the 1980s. This dramatically increased the competitiveness and profitability of Malaysian exports (Edwards, 1994). Second, was the relaxation of the restrictions on foreign equity holdings. In July 1985, new guidelines on foreign equity were announced, under which highly export-oriented companies could be wholly foreign-owned (Edwards, 1994). In September 1986, as the recession continued, further concessions were introduced to foreign investors. Companies could be wholly foreign-owned if they export more than half of their products or even if they sell their products in the domestic market as long as they met certain employment conditions (Jesudason, 1989, cited in Edwards, 1994 p 691). As shown in Table 1, the various incentives given to attract FDI proved to be fruitful with the growth in FDI picking up. The share of foreign investment to total investment increased threefold and fourfold in 1986 and 1987 respectively compared to 1985. In 1987 the net inflow totalled

Table 1: Trend of Foreign Direct Investment

Year	Foreign Direct Investment (RM million)	Total Propesed Capital Investment (RM million)	Percentage Contribution of FDI (a/b*100)	Number of Project by Foreign Direct Investment	Total Number of Project	Percentage Contribution of FDI (d/e*100)
	a	b	c	d	e	f
1982	951.70	6,020.10	15.80	65	481	13.50
1983	363.70	2,987.30	12.20	69	498	13.80
1984	390.20	3,801.10	10.30	85	749	11.30
1985	368.75	5,686.90	6.50	78	625	12.50
1986	1,492.40	5,163.20	28.90	99	447	22.10
1987	1,930.70	3,933.90	49.10	131	333	39.30
1988	4,878.00	9,093.90	53.60	301	732	41.10
1989	8,652.70	12,215.40	70.80	439	792	53.40
1990	17,629.10	28,168.10	62.60	533	906	58.80
1991	17,055.30	30,818.40	55.30	561	973	57.60
1992	17,772.10	27,775.10	63.90	425	874	48.60
1993	6,287.20	13,752.70	45.70	328	686	47.80
1994	11,339.10	22,951.30	49.40	433	870	49.80
1995	9,143.60	20,869.10	43.80	403	898	44.90
1996	20,411.80	34,257.60	59.60	374	782	47.80
1997	11,246.95	25,763.40	43.60	255	754	33.80

Source: Malaysian Industrial Development Authority (1998)

RM1.9 billion and rose to an annual average of over RM6 billion in 1988 and 1989. This turnaround in foreign investment was dramatic; FDI had thus played a vital role in revitalising the economy.

In order to accelerate the growth of the manufacturing sector, the Industrial Master Plan (IMP) was formulated in 1985. Its objective was to provide a blueprint for the development of the manufacturing sector over a 10-year period, i.e. from 1986-1995. To develop the manufacturing sector, an outward-oriented industrialisation strategy supported by technology and manpower development, improved inventive systems and the modernisation and industrialisation of the industrial sector was recommended (Sulong, 1990). FDI played a significant role in the IMP. A one-stop centre on investments was established under the Malaysian Industrial Development Authority (MIDA) in October 1988 in an attempt to cut down on red tape (Zainal, 1990, cited in Edwards, 1994 p 692). As a result, the number of approved projects owned by foreigners reached its peak in 1990 where a total of 533 projects were approved, constituting 58.8 per cent of the total number of projects which included local projects. The value of investments, on the other hand, peaked in 1990 with a total of RM17.629 billion injected into the country, contributing 62.5 per cent of total approved investments.

However, FDI showed a downward trend after having reached its peak during 1990-1992 where an average of RM17 billion worth of investments was brought into this country. Subsequently in 1997, as shown in Table 1, the share of foreign investment dropped to 43.6 per cent when compared to its peak period in 1990 when it contributed 62.6 per cent of the total value of investments. Although the FDI contribution has reduced significantly, the contribution of the manufacturing sector to the economy is still strong. Indirectly this development trend also indicated that domestic or local investment is strengthening its contribution to the overall investments in the country and is moving towards achieving a balanced participation in the economic growth. Nevertheless, the government has maintained that foreign investment is still important and will continue to be encouraged to spur the growth of the manufacturing sector (New Straits Times, 1997). Under the Seventh Malaysia Plan 1996-2000, the government has set a target of RM 110 billion in investments in the manufacturing sector, of which domestic investments are targeted to account for 60 per cent of total investments, while foreign investments, 40 per cent. In addition, growth for the manufacturing sector is targeted at an average annual rate of 10.7 per cent, while the sector's share of GDP is forecasted to increase from 33.1 per cent in 1995 to 37.5 per cent in the year 2000.

The contribution of FDI to the manufacturing sector and to the economy is indeed great. It contributes significantly to the development of high technology industries and provides access to international markets with their brand names. It has large resources to compete in the international market through technological advancement and marketing capabilities. In this way Malaysia has gained access to the international market for its made-in-Malaysia goods. Malaysia needs FDI to make its leap towards industrialisation.

The Role of FIC

It was only in the 1970s with the introduction of the New Economic Policy (NEP), that some form of control on FDI was introduced. In the late 1960s and early 1970s the

Malaysian economy was dominated by foreign enterprises. In 1970, about 60 per cent of the share capital of limited companies were owned by foreigners (Hoffman and Tan,1980). In agriculture and fisheries, the foreign ownership was as high as 75 per cent with about 72 per cent in mining and quarrying. For commerce and manufacturing, foreign ownership amounted to about 63 per cent and 59 per cent of the total share respectively. There was a marked imbalance in ownership between Malaysians and foreigners. This dominance of foreign ownership and control of the economy is a direct by-product of Malaysia's historical past (FIC Guidelines, 1974).

In order to ensure a better distribution of wealth, it is therefore necessary to regulate such acquisitions, mergers and take-overs. In line with the objectives of NEP (1981-1990), i.e. of eradicating poverty and restructuring the economy, in 1974 the FIC was established to ensure balanced Malaysian participation in ownership and control. Due to the Bumiputera's lagging economic position and their special rights, most attention were focused on the advancement of the Bumiputera. In terms of capital ownership in the corporate sector, the ultimate aim was to achieve a distribution of ownership of 40 per cent by the Bumiputera, 30 per cent by the non-Bumiputera and 30 per cent foreigners by the year 1990 (FIC Guidelines, 1974).

After 1990, as the achievements were falling short of the objectives of NEP, the objectives were still maintained in the National Development Plan (NDP) 1991-2000 (Malaysia, 1991, cited in Jomo,1994 p 58). The government maintains that at least 30 per cent should be reserved for Bumiputera participation in the management levels in all the commercial and industrial activities, irrespective of categories and scales of operation (FIC Guidelines, 1974). Thus, the FIC is responsible for influencing the structure of the foreign interest in any acquisition of assets or any interests, mergers and take-overs of companies and businesses by foreign investors.

In order to encourage local investment, specifically to promote Bumiputera interest and to ensure that they will be able to compete with the foreign investors, the Industrial Coordination Act was passed in 1975. This legislation requires all manufacturing projects with shareholders' fund of RM250,000 and above or engaging 25 or more full-time workers to apply for manufacturing licences. As a step to boost local participation, projects on a joint-venture basis were encouraged. The level of foreign equity in a project was spelled out (Sulong,1990). The licensing was backed up by the work of two high-level Committees, namely the Capital Issues Committee (CIC) and the FIC. The CIC is responsible for supervising the capital market and influencing the price at which shares were offered to the Bumiputera whilst the FIC's role is to monitor foreign investments and to ensure companies restructure their capital (Edwards, 1994).

Although there is a marked imbalance in ownership between Malaysians and foreigners, foreign investment with a balanced structure of ownership and control are very much encouraged. Private investments, including foreign investment will be welcomed as long as it is consistent with the NEP (FIC Guidelines 1974).

Foreign Acquisition of Malaysian Properties - Policy Development

As mentioned earlier, prior to 1984, foreign ownership of real property was not regulated on the belief that it lends support to FDI. This is a reasonable assumption, as foreign investment would certainly require premises for their operations. Foreign investment involved in manufacturing would require industrial sites, while those involved in services would require office space. In addition, accommodation was required to house their personnel. A study on investment packages by MIDA revealed that a foreign investment of RM5.4 million entails the placement of five expatriates (Star,1993). In view of the government's industrialisation policy and the role of FDI, acquisitions of industrial property by foreign interests were not restricted.

With the exception of industrial property, foreign ownership of other landed properties or interest in land or properties is only permitted with the approval granted by the State Authority. The housing sector in particular received special protection due to the government's home ideology. In the past, an influx of foreign purchasers of residential properties in certain towns like Johor Bahru had pushed up property prices. Without proper control this will result in houses becoming unaffordable to most locals and retard the government's house owning objectives. Hence, the first legislation that governed and controlled foreign ownership of registered or alienated land was introduced in 1985. The main objective was to restrict foreign ownership of registered land or alienated land in West Malaysia. Another objective was to curb purchases of land and houses in Johor Bahru by foreigners. This statutory restraint on foreign ownership was intended to curb property speculation to a certain extent and to lower prices (Kok, 1997).

In January 1987, the restriction on foreign ownership provisions was lifted in the wake of the worldwide recession, which had affected the economy, and the property market of Malaysia. This repeal which allowed foreigners to invest in property, was aimed at stimulating the economy. As a result the economy began to pick up in 1988/1989.

However, with the re-emergence of speculative activity in the property sector, the restriction on foreign acquisition of property was reintroduced in 1993 together with additional provisions to restrict foreign ownership of landed property. This provision provides that:

'A non-citizen or a foreign company shall not be entitled to bid at the sale where the land is subject to the category of 'agriculture' or 'building' or to any condition requiring its use for any agricultural or building purpose without the approval of the State Authority.' (Section 433B(4) National Land Code (Amendment) Act 1992)

This provision, however, does not apply to land under the 'industry' category or to any condition requiring its use for industrial purposes. The first set of guidelines for the acquisition of residential properties by foreign interests was issued by the FIC in December 1992. It received a lot of objections from housing developers on the grounds that it might deter foreign buyers and dampen the property market, especially the demand for residential property. It was contended that with the imposition of the restrictions, about 21 up-market property development projects worth RM3.5 billion were at the risk of being abandoned (Business Times,1993). In addition, it was argued that the enforcement would indirectly affect the development of low-cost houses due to the inability of developers to cross subsidise[2] such developments from profit reaped from high cost housing units (Business Times,1993). The construction of low-cost housing would, therefore, fall short of targets. It further contended that changing investment rules would cause fear and uncertainties and could drive foreign investors away from Malaysia. It would, therefore, be unwise to impede foreign investments in any form, as it would lead to the country losing its competitive edge to their neighbouring countries.

Despite all the arguments, the Government further restricted foreign acquisition of properties and in August 1995 foreigners were only allowed to purchase houses exceeding RM250,000 per unit. This measure came about as a result of increasing prices of real estate due to the significant acquisition of properties by foreigners. In addition, all properties acquired by foreign interests were not permitted to be disposed within three years from the date of FIC's approval.

To further contain foreign acquisition, the 1995 Malaysian Budget introduced an additional measure where a levy of RM100,000 would be imposed on foreigners purchasing houses more than RM250,000 per unit. Furthermore, the disposal of any property by non-citizen individuals will be subjected to a 30 per cent flat rate of Real Property Gains Tax irrespective of the holding period. The objective of this measure was to curtail excessive speculation in the property market.

The regional economic crisis which affected Malaysia in July 1997 coupled with the March 28 Central Bank guidelines which curbed banks' lending to the property sector prompted the government to reconsider restrictions imposed on foreigners. Finally, the levy of RM100,000 imposed on foreign purchasers was lifted on 27 August 1997 when the government realised that supply of up-market properties priced more than RM250,000 was ample (FIC Guidelines, 1 November 1995).

Due to the continuing weakening of Malaysia's economy, the restrictions imposed on foreigners were further relaxed. The 1998 Malaysian Budget (pp 35-36) announced additional measures to stimulate property growth in view of the excessive supply of high-priced properties. The conditions imposed on foreign acquisition of residential properties were further relaxed as follows:

i. the 30 per cent quota on sale of condominiums at prices of more than RM250,000 per unit to foreign interests be increased to 50 per cent for projects which have commenced construction on 17 October 1997;

ii. each foreign interest be allowed to acquire 2 units of condominiums and any further acquisition will be subjected to the condition of having to incorporate a company;

iii. a permanent resident will be allowed to acquire dwellings priced at below RM250,000 but above RM60,000 on condition that the spouse is a Malaysian citizen or has applied for the status of Malaysian Citizen.

In addition, the Real Property Gains Tax on non-residents is reduced to a rate of 5 per cent if the disposal takes place after the fifth year.

Although the relaxation of foreign acquisition policy was regarded as positive move by property developers, they were not certain whether foreigners would come back to our shores as many of them had turned their eyes to countries with depressed economies after the levy was imposed (The Sun, 1997). Moreover, it would take between six months to a year for potential investors to make an impact. At the moment, potential buyers would rather adopt a wait-and-see attitude to analyse whether the market still has the fundamentals to support property purchases.

To further stimulate property growth, FIC announced another relaxation in April 1998 (FIC Guidelines effective from 22nd April 1998) based on the proposal made by the National Economic Action Council (NEAC). The relaxation stipulates that:

i. foreign interests will be allowed to purchase all type of residential units, shop-houses, commercial and office space as long as the purchase price is above RM250,000 per unit. This relaxation is only applicable to projects that are newly completed or projects where construction is at least 50 per cent in progress.

ii. the financing must be obtained from overseas financial institutions outside Malaysia.

iii. all acquisitions under this guideline must obtain FIC's approval to ensure that the purchase price is more than RM250,000 and that it will be financed through a financial institution outside Malaysia. Approval will be granted automatically when the purchaser fulfills these conditions.

From the development of the FIC guidelines above, it is evident that its role has slowly shifted from its original role of ensuring balanced participation of local and foreign investment to stimulating the economy via foreign acquisitions. The question to ask is, what are the policy directions?

Policy Implications

Discussions on policy implications would entail the examination of foreign share in the property market and the impact of foreign acquisition policy on foreign direct investment. As residential property transactions represent the biggest share of the property market, capturing nearly two-thirds of the total property transactions (Valuation and Property Services Department, 1989-1997) and it has been the objective of the government to provide affordable houses to all Malaysians (Seventh Malaysia Plan 1996-2000), the discussion here is therefore focused on the foreign acquisition of residential property. To examine foreign share in the property market, analysis is based on FIC approval given to foreigners for the acquisition of residential properties dated from 1994. In order to determine the impact of foreign acquisition policy on foreign direct investment, the trend of FDI after policy changes is examined.

Table 2 below shows the foreign share in the residential property market by volume and by value in the period between 1994-1997. The value of residential property transactions by the foreigners in 1994 and 1995 made up 11 per cent and 13 per cent of the total value of residential property transactions respectively while the volume of transactions was close to 4 per cent. However, after the imposition of the levy on residential property in 1995, the foreign share by value in the residential property market in 1996 reduced to 7.8 per cent, which was a reduction of about 40 per cent while its share by volume has reduced to 1 per cent. In 1997 share of foreign acquisitions by value further reduced to 7.1 per cent and in terms of value it constituted less than 1 per cent. This reduction in foreign share suggests that policy changes, such as imposition of levy, have an influence on volume and value of the foreign acquisition. However, this has to be put in context. The residential property sector dominates the property market, where the residential property transactions accounted for more than two thirds of the property transactions and made up more than 40 per cent of the total value of property transactions (Valuation and Property Services Department, 1989-1997). In this context, the overall impact of the foreign share in the property market is not significant enough to contribute to asset inflation. However, this analysis is on a national basis, the analysis on a regional basis perhaps present a different picture. While the overall impact of foreign acquisition is not significant to the property market, most of the foreign purchases are located in major towns like, Johor Bahru and Georgetown, where the competition arising from their presence has pushed up property prices in these places.

The impact of policy changes has to be examined against wider perspectives, i.e. its impact on the foreign investments. To what extent would the restrictions deter foreign investors? Table 3 shows that between 1994-1996 Malaysian properties were most favoured by the Singaporeans. While in terms of FDI, the top three countries that have invested actively in Malaysia are United States, Japan and Taiwan which constituted 20.3 per cent, 18.5 per cent and 11.9 per cent respectively (See Table 4). However, their share in the foreign acquisition of Malaysian properties only constituted an average of 0.9 per cent, 2.3 per cent and 3.2 per cent respectively.

Table 2: Foreign Share in the Residential Property Market by Volume and Value

Year	Total Property Transactions	Total Residential Property Transactions	Total Residential Property Acquisitions by Foreigners	Foreign Share in Residential Property Market by Volume	Total Value of Property Transactions	Total Value of Residential Property	Total Value of Residential Property Acquisitions by Foreigners	Foreign Share in Residential Property Market by Volume
	(Units)	(Units)	(Units)	(RM'000)	(RM'000)	(RM'000)	(RM'000)	%
1994	217,546	140,350	5,503	3.9	29,730,730	12,648,360	1,385,543	11.0
1995	251,891	156,913	5,687	3.6	39,857,440	15,813,670	2,113,612	13.4
1996	270,548	170,016	1,770	1.0	48,993,440	18,753,020	1,468,024	7.8
1997	280,384	175,682	753	0.4	53,128,404	21,610,485	1,542,420	7.1

Source: 1. Valuation and Property Services Department, Property Market Report, various years 1994-1997
2. Foreign Investment Committee, Economic Planning Unit, Prime Minister's Department (1998)

Table 3: Countries of Origin for Foreign Acquisitions 1994 - 1997

Country	1994		1995		1996		1997	
	Unit	%	Unit	%	Unit	%	Unit	%
Singapore	4,527	82.7	4,484	82.1	1,240	81.5	350	73.0
Hong Kong	184	3.3	158	2.9	28	1.9	7	1.5
United Kingdom	107	1.9	127	2.3	38	2.5	16	3.3
Japan	111	2.0	85	1.5	35	2.3	17	3.5
Taiwan	133	2.4	161	2.9	54	3.5	19	4.0
Indonesia	70	1.3	102	1.9	26	1.7	11	2.3
USA	27	0.5	32	0.6	12	0.8	9	1.9
Others	344	6.3	313	5.8	88	5.8	50	10.5
Total	5,503	100.0	5,462	100.0	1,521	100.0	479	100.0

Source: Foreign Investment Committee, Economic Planning Unit, Prime Minister's Department (1998).

Table 4: Countries of Origin for FDI 1994 - 1997

Country	1994		1995		1996		1997	
	RM Million	%	RM Million	%	RM Million	%	RM Million	%
United Kingdom	94.11	0.83	189.86	2.07	380.66	1.86	206.67	1.82
Hong Kong	873.87	7.70	175.15	1.91	13.85	0.06	23.19	0.20
Japan	1,765.24	15.56	2,096.32	22.90	4,607.27	22.57	2,096.80	18.55
Singapore	1,.63.50	9.37	1,008.65	11.03	4,765.48	23.34	1,279.39	11.31
USA	1,253.22	11.05	1,801.63	19.70	2,893.21	14.17	2,296.50	20.31
Taiwan	2,874.26	25.34	1,442.21	15.77	775.70	3.80	1,345.06	11.89
Others	3,414.80	30.15	2,430.20	26.62	6,975.83	34.20	3,999.39	35.61
Total	11,339.0	100.0	9,144.0	100.0	20,412.0	100.0	11,247.0	100.0

Source: Malaysian Industrial Development Authority (1998)

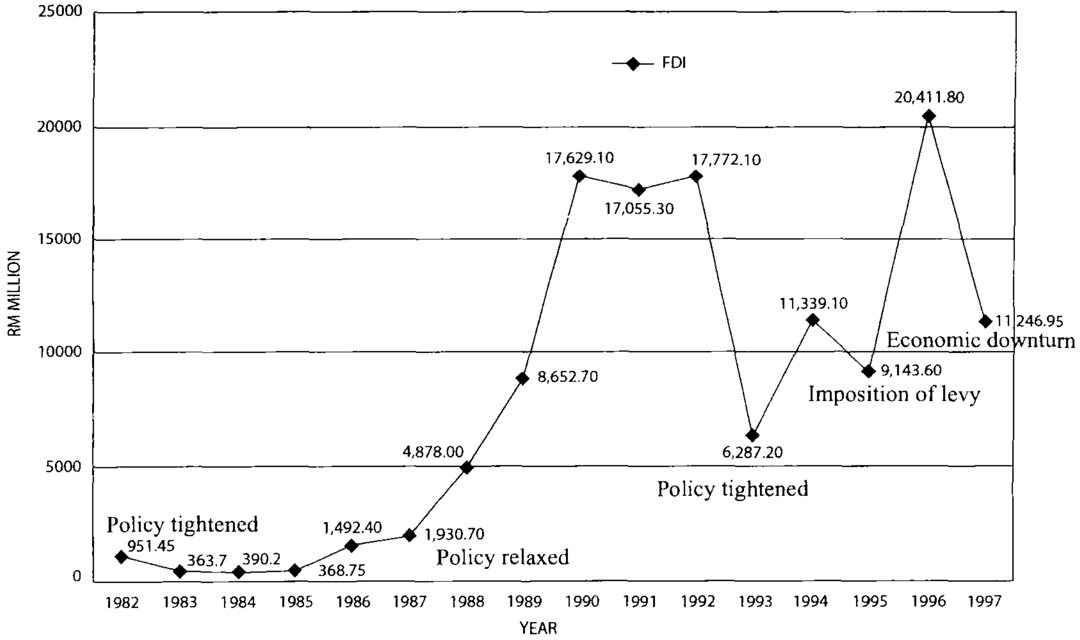
In this context, Singapore is not the leading foreign investor in terms of FDI as it only contributed an average of 11.0 per cent to total FDI. This suggests that foreign purchases of real properties are not directly linked to foreign investments. Hence, foreign acquisitions of Malaysian properties are not necessarily a product of FDI. Possibly, the foreign purchasers are attracted to this country by other factors. Observations made suggest that among some of the possible factors could be close proximity to the country of origin, especially the Singaporeans, where land is scarce in their country; and also due to high property prices in their home land like Singapore and Hong Kong.

While it has been established that the overall contribution of foreign acquisition to the property market is not significant and that the majority of the foreigners who bought property in Malaysia are individual purchasers, the impact has to be measured against the total value of new FDI. As shown in Figure 1 below, any tightening of foreign acquisition policy appears to influence FDI.

However, the effects were only temporary in nature and FDI picked up in the subsequent years. In 1987 when the foreign acquisition policy was relaxed due to the recession, the impact on foreign investment can be seen in terms of total value of new investment in the country where it increased to RM4,878 million in 1988 from RM1,930 million in 1987, an increase of 60 per cent. It continued to increase in 1990 to RM17,629 million and stabilised at this level until 1992. In 1993 when the foreign acquisition policy was tightened, the total value of new investments dropped to RM6,287.20. Similarly in 1995 when the levy was imposed, the value of total investments dropped. However, the situation improved in 1996. Despite the fact that the regulation of foreign acquisition was imposed only on selected properties and did not include industrial property, and that the foreign purchasers were individuals, it still affected the FDI. This is understandable as any policy changes always translate as risk and uncertainty to the foreign investors. Possibly, it may have created a fear that other types of property may be regulated. The foreign acquisition policy swings have occurred so frequently that to some extent it may deter potential investors from investing in the country.

With the regional economic crisis, the present policies are certainly encouraging foreign acquisition. As mentioned earlier, it has increased the quota of foreign interest to purchase condominiums costing RM250,000 from 30 per cent to 50 per cent. However, such a move may tempt the housing developers to maximise their profits by concentrating on condominiums or up-market property. There is also a danger in that the properties may be bought for speculative purposes as the Real Property Gains Tax is now reduced to 5 per cent after 5 years of holding. The Malaysian

Figure 1: Impact of Foreign Acquisition Policy



Source: Malaysian Industrial Development Authority (1998) currency has devalued by almost 50 per cent. To the foreigners the properties have become even cheaper. While this may create an influx of foreigners in the property market now, this may also lead to possible capital flights to the countries of origin in another five years time.

Conclusion

Malaysia aspires to become an industrialised country by the year 2020 and FDI is expected to play a significant role in achieving this aspiration. FDI will, therefore, remain a feature of Malaysia's development path as the country raises itself to a higher level of industrial development. As such the confidence of FDI in this country must not be undermined. Of utmost importance is the provision of a healthy and conducive climate for foreign investors. It has been established that foreign share in the residential property market is small. In this sense the contribution to the property industry is not significant but the impact would be more in their mind, the satisfaction from the knowledge that property ownership would be possible in Malaysia and the confidence it instils in foreign investors in Malaysia. Although foreign ownership of real property is not a direct by-product of FDI, any changes in the foreign acquisition policy appeared to affect the level of FDI. Frequent policy changes can create uneasiness among foreign investors. Therefore, consistency and clarity in the policy are essential. The policy directions and the underlying intentions must be spelled out clearly in order to facilitate the understanding of the foreign investors. Such understanding is vital in instilling the confidence of the foreign investors towards this country.

While foreign funds are important for the economy, and measures are being taken to attract these funds, the government should not overlook possible consequences, first the over-dependence of the economy on foreign funds. Many writers raise the concern of the potential danger of over–dependence on foreign funds. Jomo (1994), for example, argued that the trans-nationals are unreliable and if Malaysia were to rank among the newly industrialising economies, it would be better to rely on local participation. Hoffman and Tan (1980) raised the issue of potential danger of capital flight as all profits of foreign investments are transferred to the home country. In addition, foreign funds are sensitive to policy changes. As established earlier policy changes send shocks to FDI and affects the economy.

Second, consideration should also be given to the possible consequences on the residential property market. One possibility would be that property development companies would try to cash on the policy relaxation on up-market properties by concentrating on high cost developments and thereby neglecting the lower cost developments. Capital flight may occur if the purpose of property acquisition is for speculative reasons, especially now that the rate for Real Property Gains Tax is reduced to a low level after five years of holding. While measures are made to welcome funds, there must also be some measures to reduce capital flight and encourage reinvestment in the country.

Endnote

1. FDI is defined as an investment where a foreign person or corporation not resident in Malaysia has an equity or voting share in the investment and therefore some element of managerial control over the investment (Edwards, 1994).

2. The constructions of low cost houses are usually cross-subsidised by the higher cost houses (World Bank,1989).

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