CHAPTER 2

RESEARCH CONTEXT: LARGE FIRMS IN MALAYSIA

2.0 Overview of Chapter 2

This chapter presents the contextual background of the study, with special reference to the large firm sector in Malaysia. There are three topics discussed in this chapter. The first topic describes the definitions of large firms globally and specifically in Malaysia. The second topic examines the contributions of large firms in Malaysia. The third topic examines the public listed companies in Malaysia. The last topic describes the government intervention in large firms.

2.1 Various Definitions of Large firm

Large and small firms are faced with completely different challenges (Beaver, 2003) and thus, both have to adopt different business strategies to achieve high performance (Ballantine et al., 1993; Fiegenbaum & Karnani, 1991; Wagner & Hansen, 2005). For example, in generating innovation, large and small firms face different managerial and technical issues (Knight, 1989). Studies found that the manufacturing and innovation strategies employed by large and small firms also differ (Wagner & Hansen, 2005; Zahra and George, 2000). Accordingly, it is important to conduct separate studies on the effects of corporate entrepreneurship on firm performance according to firm size. This is because it is questionable whether the results of studies on small firms can be generalized to larger firms and vice versa, largely due to the fact that all core references with smalls firms as samples used the perceptual performance data (Andersen, 2010). Therefore, this study is focused on large firms.Generally, the large firm can be defined as an organization that grows beyond the medium-sized business. However, there is no standardized definition of a large firm as every agency, country or researcher has given varieties of definition based on various justifications.

Among the justifications used for each definition include the following to promote entrepreneurship, investment and growth, facilitate access to venture capital, cutting administrative burdens and increase legal certainty (European Commission, 2003). Furthermore, the classification of the firm size varies according to their capital assets, number of employees, sales turnover, skill, legal status and method of production (Abor & Quartey, 2010).

The European Commission (2009) defined the large firm in terms of the number of employees, sales turnover and total balance sheet. According to them, regardless of the industry type, the large firm has a common definition; an organization that has 500 and more employees and sales turnover of more than €50 million or a €43 million balance sheet total.

The United Nations Industrial Development Organization (UNIDO) defined firm size based on the number of employees by giving classifications for industrialized and developing countries (Elaian, 1996). Notably, for industrialized countries such as the United States and Europe, the large firm is an organization that has 500 and more workers while the developing countries defined it as an organization with 100 or more workers. The various definitions of firm size across industries and also across countries demonstrate that there is no uniformity in what constitutes firm size across the globe. Therefore, it is crucial to determine the definition of the large firm in the Malaysian context.

In Malaysia itself, different agencies have defined firm size (e.g. Micro, Small, Medium and Large) differently based on their own criteria, usually according to their annual sales turnover, number of full-time employees or shareholders' funds (Secretariat to National SME Development Council, 2005). Therefore, the National SME Development Council on 9th June 2005 approved the common definition of firm size across economic sectors for adoption by all Government Ministries and Agencies as well as financial institutions. Therefore, this definition was used in this study. According to the council, the large firm can be defined according to the type of industry within two categories. Firstly, those in the manufacturing, manufacturing-related services and agro-based industries, must have more than 150 employees or more than RM25 million in annual sales turnover.

Secondly, those firms in services, primary agriculture and information and Communication Technology (ICT) must have more than 50 employees or annual sales turnover of more than RM5 million. Details of the classification of economic activities across sectors in Malaysia are illustrated in the Appendix A. This classification of firm size definition is essential for the purpose of enabling more effective formulation of policies, development of programmes and provision of technical and financial assistance and also for better monitoring of their performance as well as their contributions to the economy (National SME Development Council, 2005). The summary of the definitions of large firms across the globe is listed in Table 2-1. It can be seen that, unlike Malaysia, the United Kingdom and other European countries share a common definition that is applicable for all industries.

Table 2-1: Definition of Large Firms

	Agencies	Definition
1.	SME Corporation Malaysian (2010)	Manufacturing, Manufacturing-Related Services and Agro-based industries:- • Sales turnover above RM25 Million or full time employees of more than 150. Services, Primary Agriculture and Information & Communication Technology (ICT):- • Sales turnover above RM5 million or full time employees of more than 50
2.	European Commission (2009)	500 and more employees and sales turnover of more than € 50 million (RM225, 365, 950) or a € 43 million (RM 193, 814,717) balance sheet total.
3.	Industry Canada	500 employees or more
4.	United Kingdom (sections 382 and 465 of the Companies Act 2006)	More than 250 employees and turnover of more than £25.9 million (RM141, 561, 396.90), a balance sheet total of more than £12.9 million (RM70, 507,413.90).
5	United States of America	More than 500 employees.

2.2 The Large Firms in Malaysia

It is shown in Table 2-2 that, in the period from 2003 - 2010, the number of large firms increased almost 3-fold to about 17,800 which accounts for only 2.7% of the total firm establishment. On the other hand, the SMEs accounted for 645,136 firms or 97.3% of the total firm establishment as at year 2010. This indicates that many of these establishments could have graduated from SMEs to large enterprises. Another reason for this may be because the criterion used in the SME definition i.e. sales turnover may show low figures due to inflationary effects (SME Annual Report, 2011/2012). However in this study, only the large firms listed in the main market, Bursa Malaysia will be taken as a sample.

Table 2-2: Number of Firms Establishment in Malaysia according to Size

	Census of Establishments and Enterprises 2005 (Reference Year 2003)			Economic Census 2011 (Reference Year 2010)		
	SMEs	Large	Total	SMEs	Large	Total
Number of establishments	548,267	4,537	552,804	645,136	17,803	662,939
Percentage share of the total establishment	99.2	0.8	100	97.3	2.7	100

Source: Census of Establishments and Enterprises 2005 and Economic Census 2011, Department of Statistics, Malaysia

Table 2-3 shows that more than half of the large companies are in the services sector which represents 61.21% (10,898) as at 2010. This is followed by the construction sector, 16.05% (2,857), agriculture, 10.16% (1,808), and mining and quarrying, 0.67% (119). The large firms also contributed to the nation in many ways which will be discussed in the next section.

Table 2-3: Large Firms by Sectors in 2010

Sector	Total Establishments of the Firms (including SMEs)	Large Firms	Percentage of Large firms over total (sector)	Percentage of Large Firms over total Large Firms
Services	591,883	10,898	1.84	61.21
Manufacturing	39,669	1,808	4.56	10.16
Agriculture	8,829	2,121	24.02	11.91
Construction	22,140	2,857	12.90	16.05
Mining and Quarrying	418	119	28.47	0.67
Total Establishments	662,939	17,803	2.69	100.00

Source: Census of Establishments and Enterprises 2005 and Economic Census 2011, Department of Statistics, Malaysia

2.3 Contribution to Malaysian Economic Growth

In other developed Asian countries like Japan, Korea, Taiwan and others, their economic growth was significantly generated by SME activities. The percentage contribution of SMEs to the Gross Domestic Product (GDP)/total value added represented more than 55%, ranging from 60% in China, 57% in Germany, 55.3% in Japan and 50% in Korea (Bank Negara Malaysia, 2003). In contrast, in Malaysia, large firms contributed more to the Malaysian GDP. For example, in 2011, large firms in Malaysia contributed 67.5% to the gross domestic product (Bernama, 2013). In other words, the Malaysian large firms contribute a sizable amount of revenue to the Malaysian economy.

2.4 Contribution to Total Export

Similarly, the large firms also contributed a substantial amount to the total export. For example in 2005, the contribution of these large firms to the country's total exports was 81%. The major export products include electrical and electronic, refined petroleum products, liquefied natural gas, chemicals and chemical products, and palm oils.

2.5 Contribution to Employment Opportunities

In terms of employment opportunities, large firms contributed approximately 43.5% of the Malaysian labour force in 2005. This percentage is considered vast, compared to its total establishment, which represents only 2.7% of the total business establishments in Malaysia.

2.6 Large Firms as a Financial Provider for SMEs

It is the norm for large firms to provide vendor development programmes and corporate venture capital (CVV) to support SMEs. The purpose of these programmes is to provide financial support to the small firms particularly for creating innovative products and services. For example, Telekom Malaysia (TM) has thousands of vendors supplying them and Tenaga Nasional Berhad (TNB) has 440 manufacturing and service companies attached to them. Another example is the Faber Group Berhad that has awarded contracts to more than 2500 vendors as at 2010. These vendors must comply with certain standards of innovation practice and thus support the increases of SME's level of innovativeness.

2.7 Established and Good Reputation

The large firms have also established their branding outside Malaysia, for example, PETRONAS, CIMB Bank, Maybank, Air Asia and many others. Thus they are easily able to expand their businesses abroad.

2.8 Public Listed Companies

The firms become public companies when they decided to offer and sell some part of the firm to the public through a registration statement filed with the Securities and Exchange (SEC) pursuant to the Securities Act of 1993. As a result, the firms will have greater access to capital markets in the future and the public can have a more objective picture of the value of the business (Hisrich et al., 2005).

In Malaysia, the Bursa Malaysia, previously known as the Kuala Lumpur Stock Exchange (KLSE), is an exchange holding company approved under Section 15 of the Capital Markets and Services Act 2007. It operates a fully-integrated exchange, offering the complete range of exchange-related services including trading, clearing, settlement and depository services. In a move to improve global accessibility to its derivatives, Bursa Malaysia Berhad entered into a strategic partnership with Chicago Exchange (CME) in September 2009.

Bursa Malaysia offers a choice of two dynamic markets to companies that aim to be listed companies. First, the main market provides an ideal platform for established companies to raise funds. Second, the ACE market is an alternative sponsor-driven market designed for companies with growth potential from all business sectors. However, in this study, only firms on the main market will be included as these firms are large and established. In order to be listed on the main market, the firms must comply with the criteria listed in Tables 2-4 and 2-5. The criteria stipulate that the firms must have uninterrupted profit after tax (PAT) of three to five full financial years, with an aggregate of at least RM20 million; and PAT of at least RM6 million for the most recent full financial year. This level of financial condition is important in order to alert the investors.

There are a few advantages and disadvantages of the firms of going public. Among the advantages are the ability to obtain equity capital, enhanced ability to borrow and to raise equity, liquidity and valuation, prestige and personal wealth. On the other hand, the public listed companies also have disadvantages such as increased risk of liability, expenses, regulation of corporate governance policies and procedures, disclosure of information, pressures to maintain growth patterns and, lastly, loss of control (Hisrich et al., 2005: 513).

Table 2-4: Listing Quantitative Criteria for the Main Market

Aspect	**Quantitative Criteria**
Mode of Listing	a. Profit Test • Uninterrupted profit after tax ("PAT") of three to five full financial years ("FY"), with an aggregate of at least RM20 million; and • PAT of at least RM6 million for the most recent full FY b. Market Capitalisation Test • A total market capitalisation of at least RM500 million upon listing; and • Incorporated and generated operating revenue for at least one full FY prior to submission c. Infrastructure Project Corporation Test • Must have the right to build and operate an infrastructure project in or outside Malaysia, with project costs of not less than RM500 million; and • The concession or licence for the infrastructure project has been awarded by a government or a state agency, in or outside Malaysia, with the remaining concession or licence period of at least 15 years

Aspect	Quantitative Criteria
Public Spread	• At least 25% of the Company's share capital; and • Minimum of 1,000 public shareholders holding not less than 100 shares each

Source: Bursa Malaysia's Website as at 17th June 2013

Table 2-5: Listing Qualitative Criteria for Main Market

Aspects	Qualitative Criteria
Core business	• An identifiable core business which has majority ownership and management control • Core business should not be holding of investments in other listed companies
Infrastructure Project Corporation test	• Continuity of substantially the same management for at least three full financial years prior to submission • For market capitalisation test, since the commencement of operations (if less than three full financial years)
Financial Position & Liquidity	• Sufficient level of working capital for at least 12 months; • Positive cash flow from the operating activities for listing via profit test and market capitalisation test; and • No accumulated losses based on its latest audited balance sheet as at the date of submission
Moratorium on Shares	• Promoters' entire shareholdings for six months from the date of admission • Subsequent sell down with conditions for companies listed under Infrastructure Project Corporation test
Transaction with Related Parties	• Must be based on terms and conditions which are not unfavourable to the company • All trade debts exceeding the normal credit period and all non-trade debts, owing by interested persons to the company or its subsidiary companies must be fully settled prior to listing

Source: Bursa Malaysia Website as at 17th June 2013

2.9 The Government Intervention in Large Firms

Our Government is committed to supporting the large firms by the implementation of Government-Linked Companies (GLCs) and innovation policies as discussed in further subsections.

2.9.1 Government-Linked Companies (GLCs)

The GLCs are firms with primary commercial objectives and the Malaysian Government has direct controlling stake. This controlling stake means the ability of the Government to appoint a Board of Director, senior management, and make a major decisions such as contract awards, strategy, structuring and financing, and acquisition, among others. GLCs are controlled by the Malaysian Government via the Federal Government-Linked Investment Companies (GLICs). GLICs are investment arms of the Government that allocate government funds to the GLCs (Putrajaya Committee on GLC High Performance, 2006).

It is apparent that, the GLCs are the backbone of the country's economy growth and critical to the development of Malaysia (Mariati & Kamarulzaman, 2005). The statistic shows that GLCs employ roughly 5% of the national workforce and account for approximately 36% and 54% respectively of the market capitalisation of Bursa Malaysia and the benchmark Kuala Lumpur Composite Index. They are also the major service providers to the country in key strategic utilities and services, including electricity, telecommunications, postal services, airlines, airports, public transport, water and sewerage, banking and financial services (Khazanah Nasional Berhad, 2014). The examples of GLCs that are also listed in the Main Market, Bursa Malaysia are, Petronas Dagangan, Affin Holdings Berhad, Axiata Group, BIMB Holdings, Boustead Holdings, Chemical Company of Malaysia, CIMB Group, Malayan Banking Berhad, Malaysia Airports Holdings, Malaysian Airline System Berhad, Sime Darby Berhad, Telekom Malaysia Berhad, Tenaga Nasioanl Berhad, TH Plantations, UEM Group Berhad, and UMW Holdings. These firms are also among the top ten companies, by size, in term of their revenue in 2010 (Azim et al., 2011).

The empirical study has found that government intervention in GLCs improves firm value, thus, provides evidence on the effectiveness of the ownership, and controls the structure of Malaysian GLCs in creating firm value (Lau & Tong, 2008). Thus, the government interventions in these particular firms are better governed (Ramirez & Tan, 2004; Ang & Ding, 2006). Consequently, the management of these companies is more conscious of the importance of maximizing shareholders' value over self-interests (Lau & Tong, 2008).

2.9.2 Support to Innovation

The role of the government in driving the innovation in Malaysia is essential. This can be seen by looking at the implementation and planning of various programmes to increase and encourage innovativeness of firms in Malaysia. Among the contribution of the government in innovation was the invention of the Smart Tag lane to decrease traffic at the toll booths by Teras Teknologi Sdn. Bhd. Another role played by the government was the introduction of the Entry Point Projects (EPP). There were 131 projects introduce under EPP. These projects are high impact, matched with specific ideas and actions, to spur the growth of the National Key Economic Areas (NKEAs). Billions of investments have been announced for manufacturing and infrastructure projects, for example, RM 50 billion for MRT project in Kuala Lumpur. All of these government efforts are to ensure the firms in Malaysia will innovate further (Azim et al., 2011). The government also has created policies to support the innovation among the firms in Malaysia as discussed in the next subsection.

2.9.2.1 Current Policies and Support for Innovation in Malaysia

The government has identified three priority areas that crucial in innovation activities; Science and Technology (S&T), Research and Development (R&D), and talent development. These areas were allocated the bulk of the Federal Government's funding expenditure for over the last four decades. The main institutions or ministries related to innovation were the Ministry of Science, Technology, and Innovation (MOSTI), Ministry of International Trade and Industry (MITI), Ministry of Higher Education (MOHE), Ministry of Finance, and the SME Corporation. Early Science and Technology Policies (S&T) (Azim et al., 2011).

First, the Science and Technology Policies, Research and Development, and talent development were implemented to provides the support and funding for innovation and research and development such as grant system, technology acquisition, tax incentives and training of private sector workforce to build the minimum required researchers and scientists in the country. The government has outlined seven (7) core priority areas that had the potential for big impact on the innovation ecosystem. The seven critical focus initiatives are as follows (Azim et al., 2011:68); i) strengthening research and technological capacity and capability, ii) promoting commercialisation of research outputs, iii) developing human resource capacity and capability, iv) promoting a culture for science, innovation and technoentrepreneurship, v) strengthening institutional framework and management for S&T, and monitoring of S&T policy implementation, vi) ensuring widespread diffusion and application of technology, leading to enhanced market-driven R&D to adapt and improve technologies, and, vii) building competence for specialization in key emerging technologies.

All these policies and incentives show government's effort to encourage innovativeness among the firms to ensure that our economy growth rapidly. Malaysia is ranked among the top 20-30 most innovative countries in the world based on various indexes-World Economic Forum (WEF), Economic Intelligence Unit (EIU) and INSEAD. Indicators from WEF position Malaysia as an efficiency-driven but not yet an innovation-led economy. However, our innovation ranking may decline in the future as other countries such as China and India are catching up rapidly according to EIU. Our nation growth is not yet led by innovation. Thus, in order to achieve Vision 2020, the country needs to aggressively grow the GDP by doing innovation as the way to move forward (Azim et al., 2011).

According to the Asian Wall Street Journal (2010), the top five most innovative companies in Malaysia are DiGi, Nestle, Maxis, Astro and Public Bank. The World's 50 Most Innovative companies 2008 has included only one company in Malaysia which is AirASia. All these firms are large in terms of their size and the key players in the Malaysian innovation ecosystem (Azim et al., 2011).

2.10 Summary of Chapter 2

This contextual chapter presented the definition of large firms, their contributions, briefing about public listed companies and the government intervention in large firms. In Malaysia, the large firm can be defined as a firm that has more than 150 employees or with more than RM25 million in annual sales turnover for manufacturing, manufacturing-related services and agro-based industries. Firms specialising in services, primary agriculture and information and Communication Technology (ICT) must have more than 50 employees or with annual sales turnover of more than RM5 million. Thus, this definition was used in this study. Despite representing only 2.7% of the total firms' establishment of large firms as at 2010, these large firms have significantly contributed to the Malaysian GDP, total exports, employment opportunities, and as a financial provider to small firms. The public listed companies constitute firms that offer and sell some part of the firm to the public in order to have greater access to capital markets in the future. The government interventions in large firms are obvious through the implementation of GLCs and innovation policies. The next chapter discusses the first part of the literature reviews on the background and definitions related to the variables under study.