

# Empirical Evaluation on Income Gap Reduction in Malaysia

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Household income gap have been identified as one of the major contributions of slow and weak economic growth. It becomes at the forefront of academic subjects and issues that arose from the unequal income distribution. For the past decades, governments, policymakers, economist have tried to solve this problem that persistently occur throughout the years but unable to effectively eliminate income disparity. There are numerous empirical research on income disparity by researcher across the world. However, the income disparity has many dimensions to gauge its composition. One of the most prominent indicator of measuring income disparity is through using Gini index that measures disparity of the total population followed by the disparity between ethnic groups, urban-rural disparity, gender, head of household, total household, and income share by household groups. However, this current study will shed light on new perspective on income disparity, which is the household income gap between groups of households of bottom 40% (B40), middle 40% (M40), and top 20% (T20) of household income distribution. These groups are cut-off points of the household income levels for the 7.3 million households in Malaysia. The state of household is under the category of socioeconomic nexus. The household income gap has widened and creating an increasing trend of disparity over the past two decades. This gap will lead to several consequences on socioeconomic development, such as depressive symptoms, severe poverty, social conflict, underinvestment, political instability, undermines progress in health, unable to resists economic shocks especially for the low-income group, and household become pessimistic about their expectation of future income. Hence, the purpose of this study is to conduct an empirical analysis to investigate the short run and long run relationship between household income gap, physical capital, human capital, and technological progress in Malaysia over the period from 1999 to 2019. Based on the theory of Solow's growth model, this study uses a panel cointegration estimation of the FMOLS and Granger causality analysis. The variables in the estimated model are analyzed to determine their influences on reducing the income gap between groups of households. The findings show that there is a short run and long run relationship between household income gap, physical capital, human capital, and technological progress. Meanwhile the causality effects show that there is a bidirectional relationship between human capital and household income gap across 13 states and 3 federal territories in Malaysia. Therefore, the recommendation for policymakers is to emphasis on the implementation of strengthening human capital investment by initiating multiple programs and strategic thrusts aiming at higher learning institutions in Malaysia.

**Keywords:** *B40/M40/T20, FMOLS, Granger Causality, Household Income, Panel Cointegration*