

Handle With Care: Malaysia's New FTAs and Transformation Toward Market-Based Policies

Firdaos Rosli

Senior Analyst, Economics, ISIS Malaysia

'Transform' is the buzzword *du jour* in Malaysia. Just to name a few, we often hear phrases such as the Government Transformation Plan, Economic Transformation Programme and '*salam transformasi*' or transformational greetings in Malay before the start of a speech. In April last year during the Invest Malaysia 2011 seminar, Najib Tun Razak, the Prime Minister of Malaysia, even said that some of his staff referred him as the leader of transformers, or the 'Optimus' Prime Minister.

The truth is: there is a much bigger 'transformation' process going on in Malaysia that people do not talk about. Malaysia's new free trade agreements (FTAs) are becoming new-age, or so-called high-quality 21st century agreement, FTAs that are indirectly transforming the country into a more liberal, market-friendly economy.

Malaysia's new FTAs are not old wine in new bottles. Malaysia's FTAs are anchored on a rules-based multilateral system with complementary agreements in both bilateral and plurilateral trade pacts. New and more comprehensive FTAs are embedded into existing ones over time in order to create a much larger trade and investment framework. This 'building-block approach' started from 'traditional' areas of duty elimination and removal of non-trade barriers and now transformed to new areas such as government procurement (GP), competition policy, intellectual property rights (IPR), labour and environment.

Today, Malaysia is playing a different ball game altogether. The country is now ready to negotiate high-quality issues such as regional integration, regulatory coherence, competitiveness, supply chain and small medium enterprises collaboration. In other words, Malaysia's new FTAs are also 'new' FTAs.

Malaysia's involvement in the Trans-Pacific Partnership (TPP), for example, explicitly implies that the country is all geared up towards liberalizing its domestic economy more aggressively than before. To begin with, the TPP, unlike any other, has no exclusion list. In addition, the TPP will adopt the negative list approach that requires all services sectors to be fully liberalized from the very beginning unless specific measures are set out in the reservations list.

Contrary to its previous stance, Malaysia is also ready to negotiate specific requests and offers under the GP chapter. The government acknowledges that protectionist industrial policies cannot last forever. Home-grown players must improve their capacity by participating in larger and more competitive markets. Now, this is new to Malaysia.

Be that as it may, Malaysia's commitments in FTAs are getting deeper as they progress. Malaysia's latest signing – Malaysia-Australia FTA (MAFTA) – marks the point of departure from its previous FTAs. MAFTA is Malaysia's most comprehensive agreement encompassing trade in goods, services, investment, economic cooperation, IPR, E-Commerce and Competition Policy.

Australia is Malaysia's first FTA partner which will eliminate all of its tariffs on goods starting from Day One. That is to say, duty elimination for all Malaysian exports is significantly deeper than that of the ASEAN Australia-New Zealand FTA. Under the services sector, the Australian market will remain open except for minor restrictions on its telecommunications industry.

Malaysia's big-scale FTAs are usually used as benchmarks to its subsequent trade deals and translated into domestic economic policies. Commitments made under AFTA, for example, were adopted as Malaysia's point of reference to its bilateral FTAs such as with Japan and Pakistan. As for the domestic economy, the government is slowly liberalizing its foreign equity participation in the services sector and *bumiputera* development policies, including the highly protected automotive industry in line with Malaysia's commitments made under AFTA and other FTAs.

As a result of continuous economic liberalization process, Malaysia's economic ranking is improving over the years. According to the Economic Freedom of the World 2012 Annual Report by the Institute for Democracy and Economic Affairs with Canada's Fraser Institute, Malaysia have improved its ranking from 78th to 71st amongst 144 countries. Malaysia also moved up two places from 14 to 12 in the World Bank's Doing Business 2012 report.

Despite being a late-comer in the FTA game, Malaysia has a good pool of trade negotiators. The country's preparedness in negotiating high-quality FTAs started after having to deal with tough negotiators under the Malaysia-US FTA. It was a great capacity building platform for its negotiators. Although the negotiation ended in a stalemate, Malaysia came out strongly as a credible player in the global FTA game thereafter and now willing to take on economic giants with a view to continue reforming its domestic economy.

But of course, economic liberalization will inevitably open its economy to a level playing field to foreign players. High-quality trade agreements must provide space for domestic SMEs to participate in the global supply chain via capacity building programmes with advanced economies. As such, Malaysia is expected to continue to push for provisions under high-quality FTAs that allow the domestic industry to adjust and adapt to the new trade and investment environment.

Malaysia's large corporations, regardless of their size, are still tiny compared to many globally connected foreign corporations. As a developing economy, Malaysia still requires a higher degree of flexibility to allow the domestic development agenda to be implemented in an inclusive and sustainable manner. In this respect, the government could use various provisions under the TPP to protect the domestic economy from being clobbered as a result of market opening.

The liberalization of the domestic economy can be a great deal for Malaysia to continue its race-based development agenda that surrounds the progress of *bumiputera's* involvement in the economic pie. Racial affirmative policies are still seen as relevant to some today as it is also the fundamental feature of the ruling coalition of the day. However, the effectiveness of current race-based policies is highly debatable since it was first introduced in the 1970s.

Suffice to say that Malaysia has transformed its FTA game with advanced countries for future trade gains. The upcoming Regional Comprehensive Economic Partnership (RCEP) negotiations and the TPP will inevitably be Malaysia's reference point towards negotiating high-quality FTAs in the future and will provide opportunities to continue transforming its domestic economy towards market-based policies.

The question is: how much of economic liberalization is enough before injuring the local players? It is yet to be seen how the government will comply with its future FTA commitments if the vote bank of the ruling coalition continues to fight for its rights to participate in the domestic economy, let alone participating in the global supply chain.
