14

Achieving the AEC 2015: Challenges for the Malaysian Private Sector

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In January 2007, heads of ASEAN governments declared their strong commitment to accelerating the establishment of the ASEAN Economic Community (AEC) to 2015 as envisioned in the ASEAN Vision 2020. The ASEAN Economic Community Blueprint which comprises four thrusts was adopted. Out of the four thrusts in the AEC Blueprint, more progress has been made in the first, third, and fourth thrusts which aim at fostering (1) a single market and production base, (3) a region of equitable economic development, and (4) a region fully integrated into the global economy, compared with the second thrust (2) on making ASEAN a highly competitive economic region. Ministers have been tasked to implement the AEC Blueprint and report to the Council of the ASEAN Economic Community on the progress of its implementation.

Since then significant progress has been made on the free flow of goods under the first thrust via the removal of tariffs through the

ASEAN Free Trade Area (AFTA). Except for Sensitive and Highly Sensitive Unprocessed Agricultural Products, ASEAN Six, which includes Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore, and Thailand, have eliminated the import duties on 99.65 per cent of traded tariff lines since 1 January 2010, while Cambodia, the Lao PDR, Myanmar, and Vietnam (CLMV) have 98.86 per cent of their traded tariff lines reduced to 0–5 per cent.

While AFTA has fostered intra-ASEAN trade since 1992 when it was first established, recent numbers since 2007 show little improvement in trade. This could be due to the unavoidable contraction in trade as a result of the global financial and economic crisis, especially since a significant portion of ASEAN's trade comes from supplying to the advanced economies that were affected by the global crisis. Intra-ASEAN trade rose by 13.6 per cent to US$458 billion and comprised 26.8 per cent of total ASEAN trade in 2008. However, in 2009 the momentum slowed as intra-ASEAN trade fell back to US$376 billion (US$403 billion in 2007), comprising 25.8 per cent of total trade, which was similar to the level in 2007 (25 per cent).

Apart from promoting the free flow of goods, ASEAN member nations are also committed to promoting free flow of services through the ASEAN Framework Agreement on Services (AFAS), which deals with the liberalization of services through successive rounds of negotiations with the aim of submitting increasingly higher levels of commitments for priority areas, as well as mutual recognition agreements on professional services. Priority areas for liberalization include air transport, e-ASEAN, health care, and tourism by 2010, and professions for mutual recognition agreement include architecture, accountancy, surveying, medicine, and dentistry.

As for the free flow of investment, ASEAN investment cooperation is being implemented through the ASEAN Comprehensive Investment Agreement (ACIA) whereby investment liberalization will be implemented with a view towards achieving a free and open investment environment in the region. Investment liberalization will be progressive and have clear timelines. With limited exceptions, national treatment and most-favoured nation treatment will be extended to ASEAN investors during the pre- and post-establishment stages of any investment.

Investment flows into ASEAN had been trending upwards before the global economic crisis and they peaked at US$74 billion in 2007. However, with the onslaught of the global crisis, ASEAN was not spared and foreign direct investment (FDI) into ASEAN fell by 36 per cent in 2008, and 21 per cent in 2009. The fall in FDI inflows into ASEAN was not as severe as that experienced by developed nations, which fell between 30 per cent and 44 per cent. Growth in intra-ASEAN investment flows was buoyant, increasing by 8.1 per cent to US$10.5 billion in 2008, but this level was not sustained as it collapsed by 57.7 per cent to US$4.4 billion in 2009.

While ASEAN governments remain committed and have abided by the declaration in the blueprint, it is important that the private sector also responds strongly to the AEC. Of late, investment and trade figures have not been very encouraging due to the global economic slowdown, but it is essential that intraregional economic activities be expanded. Indeed the success of the AEC will be determined by the participation from the private sectors which are the main beneficiaries of the AEC.

The objective of this report is to determine the responses of the Malaysian private sector to the initiatives by the Malaysian Government to promote the AEC, by gauging their level of awareness, the level of cross-border activities, as well as other positive or negative responses to government initiatives on the AEC. A survey was carried out in August 2010 for this purpose and the result is expected to represent the views of the private sector on the challenges they face in realizing the AEC.

Malaysian Intra-ASEAN Trade and Investment under the ASEAN Economic Community

The ASEAN Economic Community (AEC) serves as platform for growth and prosperity in the Southeast Asian region. Even before the introduction of the AEC in 2007, Malaysia has been engaging with its neighbours as a trade partner and an investor.

Malaysian exports to ASEAN amounted to US$41.9 billion in 2006 and that number grew to US$42.9 billion in 2009. However, the share of Malaysian exports to ASEAN remained consistent over the two periods at 26 per cent in comparison to Malaysia's total export to the world. The biggest export market in ASEAN for Malaysia is Singapore, with 59.1 per cent of Malaysian exports to ASEAN going to Singapore in 2006. While the proportion of Malaysian exports to Singapore remained high at 57.3 per cent in 2009, a minor increase in Malaysia's exports to Indonesia, Thailand, and Vietnam was seen. Malaysian exports to the Lao PDR was the lowest for the period observed. Table 14.1 shows Malaysian exports and imports to other ASEAN members.

In value terms, Malaysia's total imports from ASEAN nations have increased from 24.5 per cent in 2006 to 32.7 per cent in 2009. Among ASEAN countries, Singapore commands the lion's share of imports to Malaysia. In the observed period, the share of Malaysian imports from Singapore had increased at the expense of both Thailand and Indonesia. In recent years, Malaysia's trade with ASEAN has been producing surpluses (exports in excess of imports) with the exception of 2009. It is interesting to know whether this will be a trend or just an anomaly, given the rise of other ASEAN members as manufacturing powerhouses.

Malaysia has established itself as an attractive investment destination worldwide while, at the same time, investing in other countries. The amount of investment outflows from Malaysia to the world has nearly tripled from US$39 billion in 2006 to US$113.2 billion in 2009. However, the share of Malaysian investment outflows to ASEAN in comparison to its investment worldwide fluctuated over the observed period. The

TABLE 14.1
Malaysian Exports to and Imports from ASEAN
(US$ millions)

US$ million (per cent)	2006		2009	
	Export	Import	Export	Import
Brunei	346 (0.8)	76 (0.2)	421 (1.0)	72 (0.2)
Cambodia	108 (0.3)	20 (0.06)	152 (0.4)	13 (0.03)
Indonesia	4,074 (9.7)	4,952 (15.5)	5,140 (12.0)	5,213 (11.9)
Lao PDR	6 (0.01)	49 (0.2)	9 (0.02)	0 (0)
Myanmar	165 (0.4)	125 (0.4)	221 (0.5)	132 (0.3)
Philippines	2,173 (5.2)	2,901 (9.1)	2,270 (5.3)	1,140 (2.6)
Singapore	24,744 (59.1)	15,329 (47.9)	24,572 (57.3)	26,943 (61.7)
Thailand	8,502 (20.3)	7,167 (22.4)	8,099 (18.9)	8,225 (18.8)
Vietnam	1,758 (4.2)	1,415 (4.4)	1,990 (4.6)	1,952 (4.5)
Total ASEAN[1]	41,876 (26.0)	32,034 (24.5)	42,874 (26.1)	43,690 (32.7)

Note: Total ASEAN parentheses refer to Malaysian exports and imports share to ASEAN in comparison to its total exports to the world. The parentheses for each country refer to share of Malaysian exports and imports to each country in comparison to its total trade in ASEAN.
Source: IMF's Direction of Trade Statistics.

peak was in 2007, when 17 per cent of Malaysian investment abroad went to ASEAN members.

Malaysian investment in ASEAN has been growing at a steady pace and went to all ASEAN countries. In 2006 Malaysia invested US$1.8 billion in ASEAN, with Singapore taking the biggest share. By 2009 Singapore was still attracting most of Malaysia's investment, with total Malaysian investment in ASEAN having grown by 70 per cent compared with 2006. Prior to 2006 there was no investment made in the Lao PDR by Malaysians, but between 2006 and 2009, Malaysian firms made cumulative investments worth US$12 million in the country. Table 14.2 shows investment outflows from Malaysia to ASEAN and inflows from ASEAN members to Malaysia. The investment flows consist of both equity investment (foreign direct investment) and portfolio investment.

For the period 2006–9, outflows of investments from Malaysia to other ASEAN members were more than double the inflows of investments from other ASEAN members to Malaysia. Much of Malaysian investment abroad was concentrated in Singapore and Indonesia. Malaysian investments in Singapore could, to a large extent, be portfolio investments as Singapore's more advanced and liquid capital market serves as an outlet for Malaysian investors with a shorter term profit horizon. However, with countries such as Cambodia, the Lao PDR, Myanmar, and Vietnam, which have less-developed capital markets, there is high probability that the investments made in these countries are in productive business operations. Malaysian investment abroad also highly gravitated to its closest neighbours (with the exception of Brunei): Indonesia, Singapore, and Thailand. Investment in Vietnam, on the other hand, is mainly due to its rapid growth to establish itself as a middle-income economy.

It is expected that Malaysian firms will continue to pay attention to ASEAN as their investment destination. Malaysia's financial services sectors have been expanding in ASEAN. A notable case of a Malaysian firm investing in ASEAN is the CIMB Group that undertook the merger of PT Bank Niaga Tbk with PT Bank Lippo Tbk in 2008 to create the sixth-largest bank in Indonesia. Currently there are six Malaysian financial institutions that have investments in ASEAN (Ambank Group, CIMB Group, Maybank Group, Hong Leong Bank, Public Bank, and RHB Bank). However, the performance of other sectors, especially those with a high proportion of small and medium enterprises (SMEs), remains to be seen, particularly after the full implementation of the AEC.

TABLE 14.2
Malaysian Investment Relationship with ASEAN
(US$ millions)

	2006		2009		2006–2009	
	To ASEAN	**To Malaysia**	**To ASEAN**	**To Malaysia**	**To ASEAN**	**To Malaysia**
Brunei	7	4	10	5	46	19
Cambodia	2	2	45	2	149	11
Indonesia	274	23	613	102	4,650	264
Lao PDR	0	0	0	1	11	2
Myanmar	13	0	87	1	205	2
Philippines	34	2	29	15	110	36
Singapore	1,261	822	1,663	1,024	9,209	5,823
Thailand	122	47	368	369	815	844
Vietnam	68	109	228	177	992	619
Total ASEAN	1,781	1,011	3,043	1,696	16,187	7,620

Source: Bank Negara Malaysia.

Status/Progress of Scorecard by Malaysia in the ASEAN Economic Community

The ASEAN Economic Community Scorecard is an official mechanism developed to track progress towards the ASEAN Economic Community (AEC) by 2015. The first scorecard was published in March 2010 and contained the progress that had taken place from January 2008 to December 2009. The second scorecard's measures are being implemented between January 2010 and December 2011.

Under the first scorecard (Scorecard I), 110 measures had been identified for implementation by ASEAN and its members. From the 110 measures, 68 were under Thrust I, 34 under Thrust II, 3 under Thrust III, and 5 under Thrust IV.

- Thrust I deals with measures to liberalize and facilitate the free flow of goods, services, investment, skilled labour, and capital.
- Thrust II focuses on laying the foundation for competition policy, consumer protection, intellectual property rights, and ratifying transport agreements.
- Thrust III focuses on studies and development of SMEs and the initiative for ASEAN Integration Work Plan 2.
- Thrust IV deals with the coming into force of the free trade agreements between ASEAN and other partners.

Scorecard I for the period 2008–09 shows that on average 73.6 per cent of targeted measures were implemented by every ASEAN member. Perfect implementation (100 per cent) can be found in the Thrust III and Thrust IV initiatives, while the lowest implementation rate experienced was under Thrust II (competitive economic region), that recorded on average a 50 per cent implementation rate. For Thrust III and IV, their implementation achievement of 100 per cent was due to their low number of targets (three and five measures implemented). Thrust I recorded a 82 per cent implementation rate on average. Overall implementation rate for Thrust I to Thrust IV was 73.6 per cent of measures targeted at the end of December 2009.

Malaysia has managed to implement 86 out of the 110 measures targeted, bringing its rate to 78.2 per cent, above the ASEAN average. The Malaysian Government considers the implementation of the measures as important as it reduces or eliminates the barriers for investment and trade and aligns national regulations to regional commitments through effective regulatory and structural reform. At the same time, implementation of the measures signifies the importance of ASEAN's efforts in improving the economic well-being of its members.

In the area of trade of goods (or free flow of goods), Malaysia ratified the ASEAN Trade in Goods Agreement (ATIGA) on 17 June 2009. Along with this, the tariff liberalization process has been taking place since 1 January 2010 which has resulted in the following:

- 12,169 tariff lines (98.69 per cent) have zero import duties
- 56 tariff lines (0.45 per cent) of selected tropical fruits and tobacco were reduced to 5 per cent
- 10 tariff lines (0.08 per cent) on rice were reduced from 40 per cent to 20 per cent
- 96 tariff lines (0.78 per cent) on alcoholic beverages and weapons are excluded from tariff reduction and elimination

Included under the effort to increase the flow of goods in ASEAN is the implementation of the National Single Window (NSW) to facilitate the creation of an ASEAN Single Window (ASW), where ASEAN member countries will operate and integrate to expedite cargo release and clearance. On Malaysia's part, the implementation of its NSW took place on 1 January 2009 and is supported by five core services, which have been in full operation since 19 November 2009 and consist of (1) e-Declare, (2) e-Permit, (3) e-Payment, (4) e-Preferential Certificate of Origin (e-PCO), and (5) e-Manifest. The services offered under the Malaysian NSW incorporate the usage of information and communication technology to facilitate trade and improve the efficiency of the government delivery system that benefits the trading community. As an example, the approval of a preferential certificate of origin can now be done within a working day.

Another area under trade in goods that requires action under the AEC Scorecard is standards and conformance. Here Malaysia adopted Annex 3 of the World Trade Organization's (WTO) Technical Barriers to Trade (TBT) Agreements as the basis for standards development, based on international practices, beginning 31 December 2008. The adoption of WTO's TBT Agreement signifies the fourth thrust in the AEC, which is promoting the full integration of the region into the global economy. Conformance in cosmetic products took place in ASEAN where individual members adopted the ASEAN Cosmetic Directive (ACD) into their national legislation. Malaysia has incorporated the ACD into its

Guidelines for Control of Cosmetic Products starting 1 December 2007, while the harmonization of cosmetic regulation procedures has been in place since 1 January 2008. With this, companies are now required only to notify/declare their compliance to the ACD instead of registering with the National Pharmaceutical Control Bureau.

The free flow of services under the AEC is made possible under the ASEAN Framework Agreement on Services (AFAS), which adopted the framework under WTO's General Agreement on Trade in Services (GATS) by offering a positive list of services sectors that have been liberalized. Currently, under the seventh round, Malaysia has made changes in its services sectors not only to comply with the AEC timeframe, but also to increase its competitiveness. Between 1 January 2008 and 31 December 2009, the following steps have been made by the Malaysian Government:

- Schedule 10 new services subsectors under the Seventh Package;
- Schedule "none" for Modes 1 and 2 market access and national treatment, with exceptions to bona fide regulatory reasons subject to agreement by member states;
- Schedule at least 49 per cent of foreign equity on logistics services and other sectors;
- Schedule a maximum of three types of non-equity market access limitation for twelve sub-sectors of other sectors.

On investment, Malaysia has kept to the given timetable and ratified the ASEAN Comprehensive Investment Agreement (ACIA) on 16 August 2009. Despite the existence of the ASEAN Investment Agreement (AIA), the ACIA is a more comprehensive agreement that covers four pillars of investment such as liberalization, protection, facilitation, and promotion. An implementation of the ACIA under the AEC includes the selection of a reservation list (negative-list approach on reserved sectors) which was decided by Malaysia in October 2009.

In an effort to build ASEAN into a competitive economic region, the Malaysian Government has made major strides in improving its transportation infrastructure. The first is the ASEAN Framework Agreement on the Facilitation of Goods in Transit, parts of which have been ratified by Malaysia. Much headway has been made in the ASEAN Multilateral Agreement on the Full Liberalization of Air Freight Services (ratified on 15 December 2009) and the ASEAN Multilateral Agreement on Air Services (ratified on 15 December 2009).

There are only eight measures to be implemented under Thrust III and IV (equitable economic development and integration with the global economy) and Malaysia has managed to fulfil its implementation target.

Under the second AEC scorecard (Scorecard II), 146 measures have been targeted for implementation between 2010 and 2011. Out of the 146, 105 measures were scheduled to be implemented in 2010, while the remaining forty-one were scheduled for implementation in 2011. As of 30 June 2010, Malaysia has complied with 32 out of 142 measures targeted for the period 2010–11. The breakdown of the 32 is as follows; 16 measures under Thrust I, 12 under Thrust II, and 4 under Thrust IV. It is expected that the Scorecard II will require more attention and efforts from regulators as measures to be implemented are deeper and more comprehensive compared with those of Scorecard I.

Malaysian Private Sector

In order to identify responses and challenges faced by the private sector (business community), a survey was conducted to obtain primary data resources. The survey took place from August to September 2010.

Questionnaire

The aim of the questionnaire was to gauge private sector responses to the AEC. As the AEC is in its early implementation stage, the questionnaire was designed to measure businesses' awareness and their responses to measures that have been implemented and challenges faced. Since the majority of the measures that have been implemented come from Thrust I, the questionnaire was designed to cater to Thrust I initiatives. Thrust I initiatives are also the main concerns of businesses as they affect their businesses directly.

The questionnaire consists of two parts. The first is on the awareness of the private sector of the AEC and its components and transmission channels. The second part deals with the implementation (domestically or by ASEAN counterparts), private sector responses, and expectations of the measures taken under Thrust I. Questions were asked on mechanisms such as the ASEAN Free Trade Area (AFTA) and the Common Effective Preferential Tariffs (CEPT), the ASEAN Framework Agreement on Services (AFAS), the ASEAN Investment Agreement (AIA), the

ASEAN Comprehensive Investment Agreement (ACIA), and the Mutual Recognition Agreements (MRAs).

Data and Survey Samples

The survey questionnaire was sent to sixty-six companies, out of which only sixteen responded. The breakdown of the sixty-six companies is as follows:

- Six questionnaires were sent to six professional associations (for nurses, dental and medical practitioners, accountants, surveyors, and lawyers);
- Five questionnaires were distributed to each of the following sectors: agriculture, plastics manufacturers, rubber products, pharmaceuticals, textile and apparels, car manufacturers and assemblers, business services, travel services, chemical production, logistics providers, private education institutions, and legal services.

However, a number of companies requested that their respective trade associations answer the questionnaires because they felt that these associations know more about the AEC than they themselves. Several questionnaires were then distributed through trade associations for private hospitals, airfreight forwarders, plastic manufacturers, textile and apparels, automotive, and travel services.

Admittedly, the response rate to the questionnaire of 20 per cent is poor. From the sixteen responses, seven respondents spent 40 to 50 minutes for a face-to-face interview while eight respondents replied through e-mail or fax. A phone interview was conducted with one respondent.

The response rates are equal between services-based and manufacturing sectors (eight respondents each). Half of the total number of respondents were from professional or industrial associations, mostly from the services sector. Meanwhile, the bulk of respondents from the manufacturing sector comprised manufacturing firms (see Table 14.3).

Although the response rate is low, responses from professional or industrial associations can be treated as a collective sector response and more weight should be accorded to their opinions. The poor response rate can be attributed to the limited time available to conduct a comprehensive survey fully and the reluctance of businesses to answer individually. More information on the respondents and their cross-border activities are tabulated in Appendix 14.1.

TABLE 14.3
Breakdown on the Nature of Respondents

Sector	Association or firms	Number of respondents
Manufacturing	Associations	2
	Firms	6
Services	Associations	6
	Firms	2

Findings

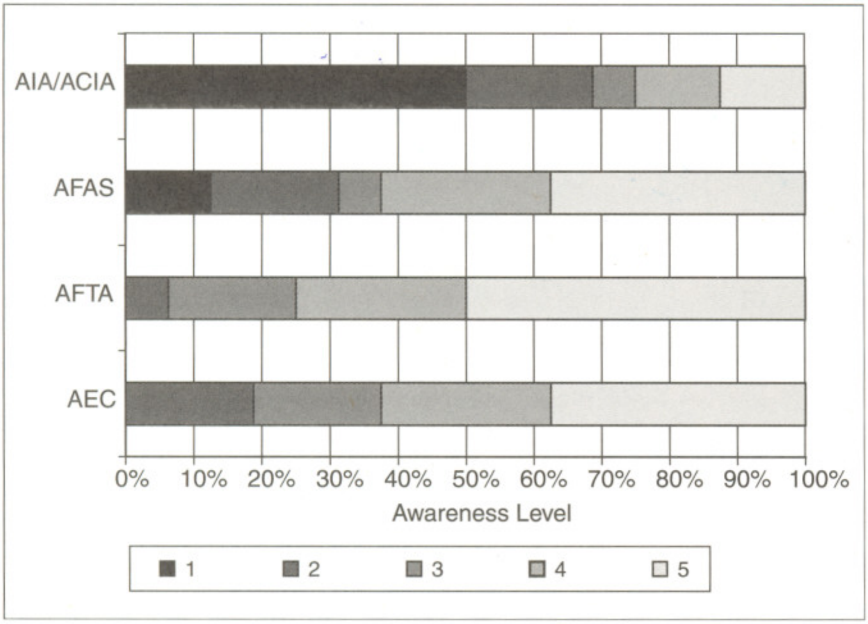
General Awareness of AEC

Responses from the surveyed companies indicate that 37.5 per cent (six respondents) of the respondents were fully aware and knowledgeable about the AEC and its contents, while 18.8 per cent (three respondents) had limited knowledge on the AEC. Awareness about other AEC initiatives such as the AFTA and AFAS was also low. Surveyed companies have poor awareness on investment-related and global integration initiatives (namely the ASEAN Investment Agreement and ASEAN Comprehensive Investment Agreement).

Understandably, manufacturers (eight respondents) were more aware of the AEC and AFTA, while service providers were more aware of the AFAS, as the appropriate agreements are relevant to their businesses. While most respondents indicate in the later part of the survey that they were eager to invest or increase their operation in other ASEAN countries, the awareness level on the AIA or ACIA was the lowest compared with other AEC initiatives. In addition, there were cases where respondents interviewed have never heard of terms such as ASEAN Investment Agreement or ASEAN Comprehensive Investment Agreement.

The awareness level of firms to AEC initiatives also correlates to their business operations and orientation. In general, manufacturing associations that were more knowledgeable and aware of the AEC were the ones that reported that most of their members' revenues came from ASEAN countries. In contrast, services-based respondents have smaller revenues generated from ASEAN countries, with the exception of private hospitals and tertiary education institutes. The services sectors are

FIGURE 14.1
Awareness of the AEC and its Initiatives
(1 = not aware, 5 = fully aware)



domestically oriented in their business outlook, and this might explain their lack of awareness and understanding of the AEC.

Despite the considerable lack of awareness of the AEC, all respondents were not prevented from:

1. exporting or importing goods
2. providing cross-border services
3. hiring foreign professionals from ASEAN
4. serving ASEAN customers in Malaysia
5. taking part in a regional production network across ASEAN

This finding questions the fundamental idea behind the AEC, which is to drive economic integration. Even without the AEC, transborder economic activities in ASEAN are bound to happen as firms look beyond their borders to expand, or, at least, source materials from other ASEAN countries. On the other hand, the lack of awareness also signifies ignorance on the part of some respondents with respect to AEC goals and how these will affect the respondents.

The media (newspaper and television) and government/ASEAN websites were identified by respondents as the main sources of information on the AEC and its initiatives. While the media might not be able to give a comprehensive picture of the AEC, websites have filled this gap and enabled firms to search for targeted information. Thirteen respondents indicated that government/ASEAN websites were an important source of information on the AEC. At the same time, four respondents reported dialogues/meetings held by ministries and government agencies as useful for getting in-depth information on the AEC. Two respondents indicated that the information provided by the channels above was not useful and cited the briefings given by the government/ministries as, at times, too theoretical.

Associations that responded to the questionnaire also stated that they have put in effort to inform and educate their respective members on the issues their industries will face under the AEC or other policy changes such as the Trans-Pacific Partnerships. Information gathering cost is a factor to be considered, especially for small firms, therefore the task of gathering information falls on associations, which have also acted as a bridge communicating their members' interests to the government and vice versa. Trade facilitation efforts have also been supported by associations, for example, the Malaysian Textile Manufacturers Association has been authorized by the Ministry of International Trade and Industry to issue and endorse certificates of origin for its exporters. Given the complexities and overlapping policy efforts by the Malaysian Government to enhance transborder economic activities under bilateral and multilateral engagements, we can expect the role played by associations to increase.

Responses on Trade of Goods

AFTA is the main initiative under the AEC that reduces or eliminates tariffs on intra-ASEAN trade for goods. The Common Effective Preferential Tariff (CEPT) was the mechanism for reducing or eliminating tariffs in AFTA, but after 17 May 2010, CEPT was replaced by the ASEAN Trade in Goods Agreement (ATIGA).

From the total number of respondents, only eight are manufacturers; each acts as an exporter and/or importer of goods. They are in plastics, textiles and apparels, construction materials, medical equipment industries, chemicals and automotive sectors. The manufacturers reported that exports to ASEAN have consistently contributed to their yearly share of revenues/profits.

Of the eight respondents (associations and firms), seven managed to utilize the CEPT scheme fully in trading their goods in ASEAN. The percentage of exports traded by respondents using the CEPT scheme ranged from 11 per cent to 75 per cent.

Respondents that engage in intraregional trade in ASEAN, particularly in textile and apparel, are of the view that CEPT has been beneficial to their operations. However, a respondent representing a company engaged in the production of construction materials reported that the company's share of ASEAN trade has been stagnant and it has not been using or able to benefit from the CEPT scheme. Of the eight respondents, six said the elimination of tariffs under AFTA has had the biggest impact on their business activities, while a firm reported that the simple, harmonized, and standardized trade facilitation practice by custom offices in ASEAN and the uniformity on rules of origin (ROO) have been significant in improving its business operations. With regard to the regional supply chain, three respondents indicated that AFTA has influenced their decisions to locate their production networks in ASEAN. Another respondent indicated that despite ASEAN's role in creating a free trade regime in the region, the main consideration for having a production network in the region was due to low labour costs.

Despite the overall positive comments on the AFTA, seven respondents also pointed out several accompanying problems when utilizing the lower tariffs. The problems cited seem to be mainly in trade facilitation. This is a major obstacle that needs to be resolved as it can discourage more exporters from taking advantage of opportunities offered by the AFTA. The respondents have experienced difficulties in clearing their goods at other ASEAN country borders, particularly at customs, in terms of delays or the requirement of exporters to complete irregular forms. Two respondents explained that the product classifications of their goods have been suffering from unsynchronized product classifications originating from differences between the ASEAN Harmonized Tariff Nomenclature (8 digits) and the international tariff codes (HS 9), therefore causing the application of inconsistent tariffs. Two respondents have also reported that their goods at some point had been subjected to some sort of non-tariff barriers by officials from other ASEAN countries such as Indonesia and Vietnam. Inefficiency in the delivery system as a result of the lack of coordination between countries was encountered by a respondent who experienced physical arrival of products at the destination prior to the receipt of the e-PCO (Preferential Certificate of Origin). A respondent that utilized CEPT to establish its production network also experienced barriers in terms of delay in the application process involving its vendors.

Only one respondent surveyed admitted they have yet to utilize AFTA initiatives fully in their business operation. The main reasons given was the lack of understanding of the AFTA initiatives, while the most-favoured nation tariff rates differentials are miniscule for their traded products.

Responses on Trade in Services

To find the effects of the AEC on trade in services done by the Malaysian private sector, a specific section of the questionnaire was designed to gauge the responses of services providers in Malaysia to the trade in services components in the AEC.

In total, there were eight responses from various services sectors, including accountancy, the medical profession, private education, and surveyors. The main trade in services activities undertaken by respondents are (1) catering to the needs of foreign clients or consumers in Malaysia (six respondents) and (2) hiring and using foreign professionals to support their core business activities (two respondents).

Although they were mostly aware of the existence of AFAS, six out of eight respondents reported that the implementation of AFAS has not improved their business operations, while the rest indicated an improvement in their services trade to ASEAN since the introduction of AFAS. On the question as to whether AFAS has benefited their business activities, three respondents concluded they have yet to benefit from AFAS. The rest managed to benefit in terms of increased demand from ASEAN clients, collaboration with other ASEAN counterparts, and enjoying a bigger talent pool for recruitment. Benefits could also be traced to the ease of hiring employees and bringing consumers from ASEAN to their facilities in Malaysia.

The inability of the majority of respondents to benefit from AFAS can be taken as a sign that they are still unable to position themselves well with the greater liberalization that will take place under AFAS. However, seven of the eight respondents said they were confident they would be able to compete with services providers from other ASEAN countries. In fact five respondents had reportedly taken steps to strengthen and improve their business operations to face stiffer competition from greater liberalization. Two firms from medical services had yet to take any steps to improve their business operations in view of the changes from AFAS. The main steps taken by firms to strengthen their business operation were by increasing their business size through merger and acquisition, capacity building, and the improvement of services offered (three responses), and applying pressure on the local chapter of professional associations to be more engaging and proactive in designing guidelines and higher standards in ASEAN (three responses).

Given the domestic orientation of services, the negative responses by services-based respondents on the liberalization process were expected. Reasons such as government regulations (three respondents), lack of scale/capital/funds (two respondents), lack of knowledge of targeted market (two respondents), and lack of business/clients networks (one respondent), were cited as obstacles hindering service firms from starting operations in ASEAN. While some barriers to expand might be due to the business nature of the respondents (that is, private clinics), regulatory burdens posed huge barriers for services firms to expand either domestically or abroad.

A few respondents considered government domestic policies or regulations as obstacles for them to expand their services abroad or even locally. A respondent in private tertiary education pointed out that the restrictions placed on the size of student intakes by the Malaysian Ministry of Health is preventing them from offering their services despite enquiries from interested individuals residing in ASEAN. The main reason behind this restriction is to prevent the overproduction of medical and health related professionals in Malaysia who are currently having difficulties fulfilling their required residencies at government hospitals due to limited spaces.

Medical and dental practitioners operate under restrictive rules and guidelines. For example, dental premises must be owned by a licensed dental practitioner who must have referrals from two other dental practitioners. Dental practitioners also have to comply to fee structures and operating hours set by the regulating body. The dental practice in Malaysia also prohibits employment of foreign dentists on private dental premises. Malaysia also exercises stringent guidelines on advertisements and this ruling has only been relaxed recently. Related government authorities are believed to be inhibiting the supply of foreign medical specialists needed for the growing medical services sector in Malaysia. Some of the reasons are linked to professional requirements to meet international standards. Regulations with regard to dental and private medical practices have over the years kept high standards in Malaysia compared with many other ASEAN countries, but some of these rules and regulations have also hampered growth in the local establishments and even in offering sufficient capacity to serve domestic consumers.

The effort to expand services trade through Mode 1, for example, is difficult with the lack of Internet connectivity in newer ASEAN member countries, making any outsourcing efforts harder (with the exception of Singapore). Under Mode 2, a respondent reportedly found that efforts to market their services in other ASEAN members were met with multiple layers of bureaucracy that led to instances where some Malaysian doctors were deemed to be breaking provincial law just by promoting and marketing Malaysian private hospitals services abroad.

The implementation of greater liberalization can be expected under trade in services in the AEC Scorecard II. The establishment of the ASEAN Core Competencies on Nursing Services and the eighth round of AFAS will be expected to include more services sectors. No doubt a huge transformation process is bound to take place in Malaysia's services sectors, and firms will have to reorientate their business strategies to meet the incoming challenges. From the responses gathered, the process would be made easier if domestic policies are accommodating for service providers in Malaysia to expand their services.

Response on Investment

Of the sixteen respondents, eight admitted that they have investments in ASEAN in the form of a regional production network or an extension of domestic services offered in other ASEAN countries. Vietnam is the main destination for investment from Malaysia (four responses), followed by Indonesia and Cambodia (three responses each) and the Lao PDR (one response). Out of the eight respondents, four indicated that less than 10 per cent of their total investments are in ASEAN (ex-Malaysia), two respondents reported that between 11 and 25 per cent of their total investment are in ASEAN, and a respondent indicated that between 26 to 50 per cent of their investment are in ASEAN. There was no response from the eighth respondent.

Only three respondents gave positive responses when asked about their awareness of the main investment initiatives under the AEC. When told that the objective of the AIA/ACIA is to enable the creation of a level playing field in the region, nine respondents expressed doubts that it would benefit them, with a respondent citing an example that Malaysian companies are now susceptible to takeovers from other firms in ASEAN.

At the sectoral level, only four respondents gave a positive answer that the AIA/ACIA is beneficial for the growth of their respective sectors. Three respondents remained neutral on that issue while four viewed it as being capable of having negative effects on their sector. One of them did not respond to this question.

The surveyed respondents might not be fully aware of the AIA/ACIA, but they showed strong interest in increasing their investment in ASEAN. Nine respondents indicated that they were willing to look closer at AIA/ACIA and utilize it in their future investment in ASEAN. Apart from the lack of awareness in the AEC investment initiatives, challenges such as limited local knowledge (two respondents) and the lack of scale/funds/capital to expand (two respondents) are cited as hampering respondents from investing in ASEAN.

Face-to-face interview sessions conducted gave more information on the challenges of investing in ASEAN. A respondent reported that their factory in Vietnam was facing persistent labour strikes, made worse after the incidences of strikes in China early this year. Another respondent also made a remark that the high inflation rate in Vietnam was detrimental to its operations there. The respondents from manufacturing industries who were interested in investing abroad looked for places which were cost effective, had low wages, and required low skills. On the other hand, respondents from the services sector who invested abroad made their decisions based on market potential, such as market size and the growing middle income class in countries such as Cambodia, Indonesia, and Vietnam.

Responses on Freer Labour Movement

The AEC Blueprint also covers the aspiration of freer professional and skilled labour movement across ASEAN. The main instruments are the sectoral schedule of Mode 4 under AFAS and the Mutual Recognition Agreements (MRAs) on a few selected professionals.

There were more respondents who viewed AFAS as not helpful in recruiting the skilled workforce needed in Malaysia. Rather, six respondents (five from the services sectors) felt that AFAS has encouraged highly skilled and experienced Malaysian workers to work abroad, citing Singapore as the main magnet in the region. The positive responses (five) on AFAS came from respondents who had experience in hiring professionals from ASEAN in sectors such as tertiary education and private hospitals.

Since the MRAs are limited to six professions, only three respondents in recent years were able to hire using standards outlined in the MRAs. The same respondents also reported that the procedures in hiring and getting a work permit for ASEAN foreign professionals under the MRAs is easier and timely, with the exception of dental practitioners. Of late, respondents have experienced smoother procedures even for professionals not covered by MRAs, such as lecturers.

Most respondents (eight) felt that increasing the number of professions covered by MRAs is a positive development that they look forward to. A firm suggested that MRAs be made on IT and design services. Two respondents were neutral on this issue while one respondent felt that expanding MRAs could erode the premiums received by domestic service providers.

While respondents seemed eager for the scope of MRAs to be enlarged, the majority of them (ten respondents) felt that professional associations' roles are important in order to maintain the standards of professionalism in the region and to ensure a level playing field. Respondents who had experience in hiring foreign professionals pointed out problems related to the domestic immigration office's inefficiency and reluctance to issue work permits.

Professionals, even those covered by the MRAs, reported that requirements, such as citizenship and language, are making it impossible for Malaysian services providers to work in other ASEAN countries. Other domestic regulations, such as the Dental Act 1971, prevent the hiring of foreign dental practitioners unless it is by the government. The same situation is also faced by medical professionals (doctors). A few respondents (three) were reluctant to hire professionals from abroad because the services provided may be of a different quality compared with that of domestic professionals.

Policy Recommendations

Awareness about the AEC

Awareness of the positive benefits of the AEC has to be raised. Lack of awareness and negative perception of the AEC can be a major hurdle in the successful implementation of the AEC. Industry associations play a very important role in raising the level of awareness and promoting ASEAN as a trade and investment area. Private sector participants generally had little knowledge about regional services and investment liberalization agreements among ASEAN member countries even though most of them were aware of AFTA.

Based on the scorecards, much has been done by the Malaysian Government. Knowledge of this has to be transmitted to the private sector. Industry associations are important channels for relaying the progress of the implementation of the AEC and also for obtaining private sector feedback as to whether the scorecard meets their expectations. Some industry players fear liberalization because it may disadvantage them. Thus, the implementation of the initiatives under the AEC in ASEAN must be explained clearly to dispel this misgiving. Dialogues and discussions between industry associations and government agencies will foster more effective implementation.

Currently, there are many rules and regulations that govern business practices within the services sector. Some of these may be restrictive and prevent the private sector from expanding their services into other ASEAN nations. Hence, the private sector, through their respective industry associations, also needs to engage with the Malaysian Government to provide a more conducive environment for the services sector which is on par with that of ASEAN neighbours. Meanwhile a balance must be found to promote the AEC as a way for firms in Malaysia to unleash their competitiveness while at the same time prepare them to compete with other ASEAN players that can do better as a result of subsidies or less regulation.

While the study has been targeted at the private sector, the survey also found that the public sector's level of awareness was also relatively weak, especially when it came to facilitating cross-border trades. Malaysian firms that attempt to take advantage of the agreements still encounter many obstacles. Even though regional governments may have already made agreements on tariff reduction, liberalization of priority service sectors, investments through mechanisms such as CEPT, AFAS, and AIA, the private sector encounters situations where some of the terms of the agreements have not been implemented at all levels. In some cases, customs or municipalities may insist on their own rules or terms that override the regional agreements. In more extreme circumstances, local service providers fearing liberalization may also act in concert with local municipalities to drive away ASEAN investors. Because of this, local municipalities, states, customs, and other related government bodies should be briefed by central government authorities to give priority to cooperation with ASEAN nations on trade and investments.

Promote the Potential of ASEAN as a Platform of Production Network

Individually, many of the ASEAN nations have relatively small domestic markets and low per capita income to attract significant FDIs inflows, but collectively these nations can be a viable production network if costs of transportation can be reduced and goods and services can flow across borders seamlessly.

To encourage more trade and cross-border investments, there should be more clarity, industry standardization, and transparency in the activities of each sector, subsector, or profession. An outreach programme where more detailed cooperative mechanisms by sector and subsectors for both manufacturing and services is required if ASEAN is to become a platform for a regional production network.

Expedite Trade Facilitation

To encourage more trade within ASEAN, the expeditious implementation of trade facilitation should be given a priority. Malaysian exporters encounter obstacles in trade facilitation and this may negate the advantages of reduced tariffs as agreed in CEPT. Focus should be given to smoother customs and logistics integration that will enable a smooth and speedy passage for the export and import of goods. Harmonized and standardized trade and customs processes and procedures with the establishment of an ASEAN e-Customs will reduce transaction costs, enhance export competitiveness, and facilitate the integration of ASEAN into a single market and single production base.

Adopt Wider Investment Liberalization

Of the AEC components, investment has shown significant progress over a four-year period in terms of intra-ASEAN investment flows despite the lack of awareness on regional investment agreements under the AEC. More recently in 2009, however, intra-ASEAN investments collapsed by 57.7 per cent to US$4.4 billion in the aftermath of the global financial crisis. To arrest this decline in intra-ASEAN investments, more efforts can be made to increase the level of awareness on the official agreements (AIA and ACIA) in the business community.

In addition, partnerships that involve ASEAN with non-ASEAN investors should also be encouraged in order to increase levels of innovation among ASEAN member nations. It may, therefore, be more effective for ASEAN countries to opt for general investment liberalization that can make ASEAN countries a very attractive investment location and this will likely see a significant boost in investments, particularly in higher value added and technologically advanced companies.

Assistance for SMEs

SMEs face more difficulties than larger companies in expanding abroad. The larger manufacturing firms and service providers are more positive about the AEC since they have already invested or have intentions to invest in ASEAN countries. On the other hand, the main focus of SMEs is the domestic market and they are generally less in favour of liberalization and expanding abroad as these firms fear erosion of market share by new players. The SMEs lack financial and technical capacity and they need financial support, knowledge of networks, and knowledge of the market to encourage them to venture into ASEAN countries. Government agencies can increase their assistance in providing them with the useful links and information needed.

Facilitate the Movement of Skilled Workers

The free movement of skilled workers is still a challenging issue and there is a need to increase the number of MRAs. Currently language proficiency and professional standards vary widely across ASEAN countries. Even basic tertiary education qualifications differ across ASEAN countries and it may be necessary for ASEAN countries to recognize mutually a certain standard as the entry qualification for tertiary education.

Respondents from the services sector were more negative towards the AEC as they face more obstacles in exporting their services than those from the manufacturing sector. A more specialized and focused effort, possibly based on services subsectors or specialized activities, can be established to assist these services providers to build capacity and minimize the export obstacles. This measure will facilitate the harmonization of domestic regulations which involve many ministries or agencies and cross-industry technical requirements.

APPENDIX 14.1
Profile of Respondents and Their Cross-Border Activities

Sectors	Respondents	A	B	C	D	E	F
Manufacturing	Textile and Apparels 1	•				•	•
	Textile and Apparels 2	•				•	
	Plastics	•		•	•	•	•
	Constructions Materials		•	•		•	•
	Medical equipment			•	•	•	•
	Automotive 1	•					
	Automotive 2	•					
	Chemicals	•			•		•
Services	Medical 1			•	•		
	Medical 2				•		
	Medical 3			•	•	•	
	Medical 4				•		
	Education 1			•	•		
	Education 2			•	•		
	Accountancy		•		•		•
	Surveyors		•		•	•	

Notes:
A – export or/and import goods to/from ASEAN
B – provide cross-border services in ASEAN
C – hire professionals from ASEAN
D – serve ASEAN customers in Malaysia (Mode 2 of services trade)
E – invest in ASEAN
F – form part of a regional production network

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