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Linkage between Malaysia's FTA Policy and ASEAN Diplomacy

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Introduction

In 1992, Malaysia agreed to launch the ASEAN Free Trade Area (AFTA) as one of the Association of Southeast Asian Nations (ASEAN) economic cooperation projects. Since then, Malaysia has positively committed to AFTA and its tariff reduction schedule. In 2000, however, Malaysia requested a delay in its AFTA tariff reduction schedule on automotive products in order to protect its automotive industry. With some exceptions including this Malaysia's deferment, AFTA was realized as a 0–5 per cent tariff regime among ASEAN 6 members (Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand) in January 2003. Singapore and Thailand began to pursue bilateral free trade agreements (FTAs) with non-ASEAN countries from 1999. Malaysia criticized the two members and argued that these bilateral FTAs could harm AFTA. In addition to the movement towards more bilateral FTAs, ASEAN itself has started to discuss the possibility of FTAs with non-ASEAN countries such as an ASEAN-China FTA and an ASEAN-Japan FTA since 2000. Malaysia prioritizes ASEAN-based FTAs over bilateral FTAs in order to maintain ASEAN's solidarity. In particular, Malaysia links ASEAN-based FTAs with its own proposal called the East Asia Economic Group (EAEG) initiated in 1990.

In 1990, at a dinner in honor of visiting Chinese Premier Li Peng, the Prime Minister, Mahathir Mohamad, proposed the EAEG, which excluded four members of Asia-Pacific Economic Cooperation (APEC): the United States, Canada, Australia and New Zealand (Lim 2001: 54).¹ The idea behind the EAEG proposal was to give East Asian countries a powerful and coherent voice in trade negotiations in the General Agreement on Tariffs

and Trade (GATT). The EAEG aimed to build a forum, not a trading bloc, for discussing common trading problems, particularly those related to discriminatory trade practices of the West (Mahathir 1994: 97; Mahathir 1995: 35–36).

This chapter argues that there are two key aspects of Malaysia's policy towards FTAs. The first is the economic impacts on domestic industries. The Malaysia's deferment on AFTA in 2000 was related to this aspect. Malaysia has domestic economic concerns that hinder pursuing FTAs. AFTA is Malaysia's first FTA and Malaysia could defer its tariff reduction schedule in AFTA because AFTA is a flexible FTA that enables members to change their commitments. The second is a diplomatic aspect of FTAs that is closely related to its ASEAN diplomacy. AFTA is an important ASEAN economic cooperation scheme for Malaysia. In addition, Malaysia considers pursuing ASEAN-based FTAs as a crucial part of ASEAN diplomacy. Furthermore, Malaysia insisted that ASEAN should construct a close relationship with ASEAN+3 members (ASEAN, China, Japan and South Korea) in its EAEG proposal. AFTA became Malaysia's model for ASEAN-based FTAs since it gave members a wide range of discretion on implementation. This chapter aims to analyze how both Malaysia's need to balance trade liberalization through FTAs with concerns for domestic industry and its preference for ASEAN diplomacy affects its approach to FTAs.

Incentives for FTAs: Domestic Perspectives

This section deals with Malaysia's domestic perspective on pursuing FTAs. By and large, Malaysia responds negatively towards FTAs as its official documents illustrate below. This response is derived from Malaysia's concerns about effects of FTAs on the domestic economy, which explains why Malaysia asked for the delay of its tariff reduction schedule in AFTA. These concerns will be analyzed from industrial and trade structures of Malaysia's economy.

Negative Responses towards FTAs

In order to understand Malaysia's position on FTAs, it is important to investigate how Malaysia perceives FTAs. This perception is illustrated in the Malaysia International Trade and Industry (MITI) Report. In 1993, the report stated:

Regionalism should not be an alternative to multilateralism, nor can it detract from globalism. However, regionalism can, in fact, complement and reinforce multilateralism. Regional trading arrangements can strengthen and enhance the natural trading patterns existing within the region, as well as make for new forms of economic cooperation. Also, these trading arrangements can evolve into larger regional markets and thus can attract more foreign direct investments into that particular region.

(MITI 1993: 64)

In 1992, ASEAN agreed to launch AFTA and Malaysia was one of its original members. Therefore, the above statement in 1993 reflected Malaysia's commitments to AFTA. Malaysia acknowledged that regional FTAs (such as AFTA) could attract foreign direct investment (FDI) and those FTAs were good for multilateral trade liberalization. Nonetheless, it also emphasized that regionalism was ultimately subordinate to multilateralism. This position has been consistent throughout the 1990s (MITI 1997: 112; MITI 1999: 92). Malaysia has considered it necessary to strengthen rules of the GATT and World Trade Organization (WTO) to regulate FTAs. In fact, Malaysia condemned the North American Free Trade Agreement (NAFTA) for some discriminatory provisions, arguing that they would cause trade diversion effects (MITI 1993: 64; 1994: 97).

The MITI Report 2001 stated:²

The mandate to clarify and improve disciplines and procedures under the existing WTO rules on free trade arrangements is important and timely, especially in view of the proliferation of bilateral Free Trade Area (FTA) Agreements and the inability of the WTO to ascertain the compatibility of these arrangements with WTO multilateral rules. There is a need to strengthen the rules to ensure that the objective of regional integration envisaged in the rules is not replaced by bilateral market sharing arrangements.

(MITI 2001: 48)

Malaysia has insisted on clarification of rules for FTAs in the GATT/WTO from 1993 to 2001. The interesting change over this decade is that Malaysia began to emphasize negative aspects of FTAs. This change in position is derived from the proliferation of bilateral FTAs especially in the Asia Pacific region since 2000. Malaysia is anxious about negative effects such as trade diversion from the proliferation of bilateral FTAs.

In sum, Malaysia has acknowledged the benefits of FTAs, but insisted FTAs should be subject to the GATT/WTO rules. Given Malaysia's reaction towards NAFTA, it can be also assumed that Malaysia has concerns about trade diversion effects from FTAs, particularly bilateral ones in recent years.

Costs for Removing Industrial Protection: Trade and Industrial Structures

In terms of trade, the Malaysia's industrial structure consists of domestic-oriented industries and export-oriented industries. Domestic-oriented industries include transport equipment, non-metallic mineral products, food manufacturing, and iron and steel basic products. Export-oriented industries are rubber, textiles, wood products and electric and electronics (E&E) (MITI 2001: 158).

TABLE 10-1
EXPORTS BY COMMODITY, 2001

	Value (Billion RM)	Share (%)
Manufactured Goods	276.2	82.6
Electrical and electronics products	189.4	56.6
Chemicals and chemical products	14.4	4.3
Machinery, appliances and parts	10.9	3.3
Wood products	9.8	2.9
Textiles and apparel	8.9	2.7
Optical and scientific equipment	7.8	2.3
Manufacturers of metal	6.4	1.9
Rubber products	4.5	1.3
Others	24.1	7.3
Mining	32.5	9.8
LNG	12.7	3.8
Crude petroleum	11.4	3.4
Others	8.4	2.6
Agricultural Goods	21.3	6.4
Palm oil	11.7	3.5
Others	9.6	2.9
Others	4.5	1.3
Total	334.4	100.0

Source: MITI (2001).

Malaysia depends on trade since it has a small economy. The trade structure in Malaysia has been constituted by export-oriented industries since the early 1980s when there was its rapid industrialization in the manufacturing sector. This sector has accounted for most of Malaysia's exports. In particular, the E&E industry accounts for most of its exports. Palm oil, crude petroleum and liquefied natural gas (LNG) are among its exports (TABLE10-1). However, primary industries such as the mining and agricultural sectors have decreased their share of total exports since the 1980s. The E&E sector also accounted for 51.9 per cent of Malaysia's total imports of manufactured goods (MITI 2001: 162). Most imports are intermediate goods in the E&E sector, which supply component parts of products for export (TABLE10-2).

TABLE 10-2
IMPORTS BY COMMODITY, 2001

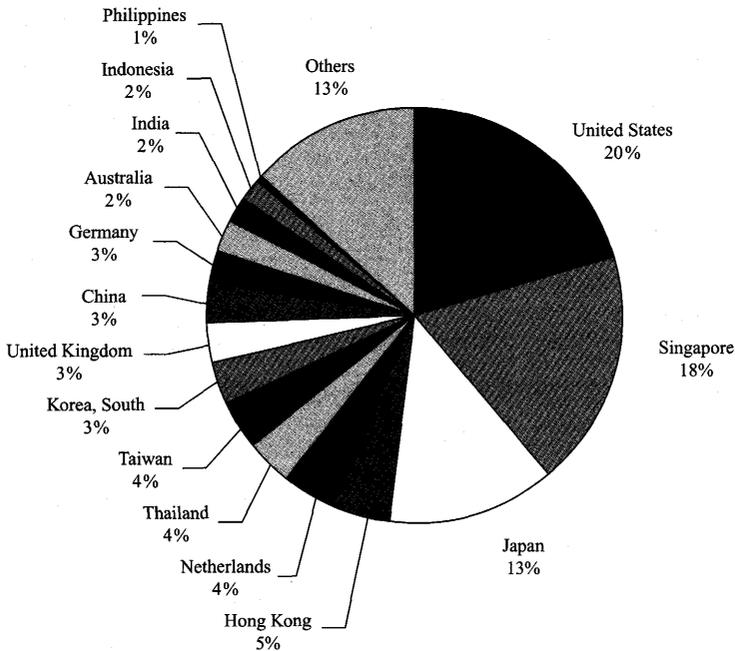
	Value (Million RM)	Share (%)
Intermediate Goods	201,766.7	71.9
Capital Goods	43,691.7	15.6
Consumption Goods	17,524.2	6.2
Others	17,708.5	6.3
Total	280,691.1	100.0

Source: MITI (2001).

As for trade by country, Malaysia's major partners have been the United States, Singapore and Japan since the 1980s (FIGURE 10-1, 2). Exports to those countries are mainly E&E products. Malaysia enjoys exporting E&E products with almost zero import duties to the United States on a most favored nation basis.³ As for exports of primary products, the main destinations are India and China for palm oil; Thailand, South Korea and India for crude petroleum and Japan for LNG (Department of Statistics, Malaysia 2001). Malaysia has condemned India for high import duties and China⁴ for its quota system on palm oil from Malaysia (MITI 2001: 99–100). The average tariff rate for imports in Malaysia is 9.1 per cent, relatively low compared with other developing countries. But Malaysia still maintains high tariffs on automotive products (25.4 per cent on average) and raised tariff rates of iron and steel products from 0 to 50 per cent to

protect domestic industries in 2002 (JETRO 2002: 217). Moreover, some products in the E&E and other industries have 30 per cent as the highest tariff rate (METI 2002: 170).

FIGURE 10-1
EXPORTS BY COUNTRY, 2000

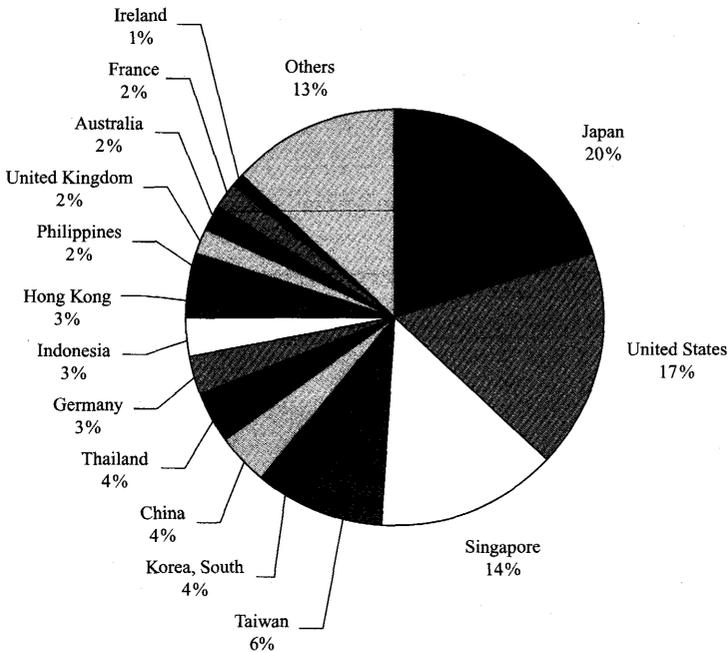


Source: Department of Statistics, Malaysia (2001).

These industrial and trade structures were established when the government implemented the following two industrial policies.⁵ The first is the export-promotion policy, which allows foreign multinational corporations (MNCs) to take part in some export-oriented industries. In order to promote export-oriented industries, the government enacted the Investment Incentives Act in 1968 and introduced the Licensed Manufacturing Warehouse (LMW) system in 1967.⁶ In addition, Free Trade Zones (FTZs) were established under the 1971 Free Trade Zone Act to increase export-oriented industries (Rasiah 1993:

118–46). With either FTZ or LMW treatment, companies can enjoy duty-free status for all imports as well as other tax incentives. With the 1985 economic slowdown in Malaysia, the government enacted the Promotion of Investment Act in 1986 and deregulated foreign investment policies to promote foreign participation in export-oriented industries.⁷ Furthermore, the 1985 Plaza Accord of the Group of Five that led appreciation of the yen, resulted in vast amounts of investment flows from Japan into Malaysia.

FIGURE 10-2
IMPORTS BY COUNTRY, 2000



Source: Department of Statistics, Malaysia (2001).

The second policy is the heavy industrialization program that was created in the early 1980s based on the realization that establishment of FTZs only led to promoting foreign-dominated industries. Under this program, the government established some government-owned industries.⁸ The

automotive industry is one example of an industry that has been highly protected by the government. As part of this program, the government launched the two National Car Projects, Perusahaan Otomobil Nasional Berhad (Proton) in 1983 and Perusahaan Otomobil Kedua Sdn. Bhd. (Perodua) in 1990. During the initial five years, Proton and Perodua enjoyed import duty-free status for completely knocked down (CKD) kits, a package of auto parts from which one car can be completely built up. Even after the initial stage, they have enjoyed a 13 per cent tariff rate for importing CKD whereas other foreign automotive assemblers have been subject to 42 per cent (FOURIN 2000: 54). Furthermore, these two national assemblers have been overprotected by high tariffs 140–300 per cent for completely built-up units (CBU) (Horii 1989: 125). Simultaneously, the government has fostered local supplier industries called “venders” to supply auto parts and components to these two national assemblers.⁹ In 2000, under the Agreement on Trade-Related Aspects of Intellectual Property Rights, the government asked for a second extension of the timeframe to phase out the local content requirement in the automotive sector from 2000 to the end of December 2003 (MITI 2001: 51).¹⁰ The local content is maintained at 45 to 60 per cent for passenger and commercial vehicles and 60 per cent for motorcycles (USTR 2002: 283). This is due to the need to protect local venders in this industry from global competition (Koo 2001: 4–8).

In sum, Malaysia has maintained a dual economy consisting of domestic-oriented industries and the export-oriented industries. In this structure, MNCs in export-oriented industries do not have to complain about high import tariffs since they are duty-free, thanks to the FTZ and LMW policies. Malaysia has incentives to consider FTAs with developing countries, where trade barriers such as tariffs are still high. For instance, Malaysia has some incentives to reduce tariffs on its palm oil products in India. However, Malaysia has its own problem of high tariffs in several industries such as the automotive industry and the iron and steel industries. Therefore, it is not easy for Malaysia to pursue FTAs without reforms of its own protective industrial policies.

Different Responses towards Regional and Bilateral FTAs

Malaysia is unique in that it links its policy towards FTAs with its ASEAN diplomacy. This section deals with Malaysia's linkage of FTAs with ASEAN diplomacy by analyzing Malaysia's participation in AFTA and its response to bilateral FTAs and ASEAN-based FTAs.

AFTA as a Flexible FTA

Despite domestic constraints described in the previous section, Malaysia agreed to AFTA in 1992. The Prime Minister, Ministry of Foreign Affairs and MITI have mainly conducted Malaysia's policy for ASEAN. Since AFTA is one of ASEAN economic cooperation projects, it is primarily dealt with by the Minister of MITI and the ASEAN Economic Cooperation Division in MITI. After MITI prepares policy recommendations for ASEAN including tariff concessions in AFTA, they are distributed to the Cabinet. The role of the Prime Minister, Mahathir Mohamad, cannot be underestimated in the analysis of the country's trade policies.

Upon assuming the office of Prime Minister in July 1981, Mahathir articulated Malaysia's foreign policy priorities as follows: (1) ASEAN, (2) Islamic countries, (3) the non-aligned community, and (4) the Commonwealth (Nair 1997: 80). ASEAN cooperation has been given the highest priority in Malaysia. When Mahathir proposed the EAEG in December 1990, ASEAN was supposed to be the core group. The EAEG was proposed because "it is aimed at giving its members more leverage against the United States-Canada free trade agreement and the EC [European Community]" (Low 1991: 376-77; Liow 2001: 149-50). Mahathir himself explained that the EAEG was needed in order to balance the power of other regional trading blocs in North America and Europe.¹¹ The EAEG was controversial not only among ASEAN members, but also between Malaysia and Japan (Yamakage 1997: 192-96). In addition to negative responses from Japan, Indonesia also strongly opposed the EAEG proposal. This was partly because of the fact that President Soeharto and Prime Minister Mahathir were competing for the leadership of ASEAN (Kurus 1995: 410). Despite the controversy, Malaysia made progress towards achieving its goal of establishing the EAEG. Malaysia succeeded in setting up a working group after the twenty-fourth ASEAN Ministerial Meeting (AMM: Foreign Ministers Meeting) in July 1991 to discuss various aspects such as EAEG membership, approach and modality.¹² However, Indonesia proposed to change the name of the EAEG to the East Asia Economic Caucus (EAEC) (Yamakage 1997: 141-42). At the twenty-third ASEAN Economic Ministers Meeting (AEM) in 1991 at Kuala Lumpur, ASEAN members agreed to Indonesia's proposal. Although Malaysia had to accept this change, its idea of regional economic cooperation in East Asia gained recognition among ASEAN members. These achievements were possible partly because Malaysia was the chair of the twenty-fourth AMM and the twenty-third AEM.

To counter Mahathir's proposal for the EAEG, Thai Prime Minister Anand Panyarachun first proposed AFTA in June 1991 (see Chapter 9). Both the AFTA proposal by Thailand and the EAEG proposal were based on the need to build a pressure group against the US-Canada FTA (future NAFTA) and the EC (Mutoh 1997: 32-45; Low 1991: 376-77). Malaysia supported AFTA as long as it aimed at building a pressure group against trading blocs in other regions. At the twenty-fourth AEM, Mahathir "welcomed the proposal by the Prime Minister of Thailand for an AFTA" (AEM 1991). When AFTA was formally signed at the 1992 ASEAN Summit, Mahathir also stated that the "movement towards a free trade arrangement (that is AFTA) is not as big as a change as a single European Market, but for us, it is significant."¹³

However, it can be argued that Malaysia as the chair of the AEM and the AMM in 1991 agreed with the AFTA proposal in return for taking up the EAEG matter despite negative reactions from other ASEAN members. In fact, Malaysia maintained its cautious attitude towards AFTA in terms of how to realize this FTA. This attitude was envisaged in statements of Rafidah Aziz, Minister of MITI, during the preparation for the AEM. In addition to the EAEG, there were four proposals for economic cooperation submitted by ASEAN members before the AEM. These were the AFTA by Thailand, the Common Effective Preferential Tariff (CEPT) scheme by Indonesia, the ASEAN Treaty on Economic Cooperation by the Philippines and the Growth Triangle concept by Singapore. Rafidah stated that:¹⁴

The proposals are related to the proposed EAEG.

... The proposed EAEG would not become a trading bloc and it would benefit ASEAN countries by strengthening regional economic cooperation.

Admitting that the proposed ASEAN Treaty of Economic Cooperation and AFTA would take some time to materialize, Indonesia's proposal on ACEPT [ASEAN CEPT] could probably be used as an interim measure to enhance intra-Asean trade.

In addition, Rafidah, as the twenty-third AEM chairman, confirmed that:¹⁵

The FTA will have its own identity based on the Asean situation and will not follow the example of other such schemes in the world.

"Other such schemes" referred to the US-Canada FTA and the EC. Malaysia did not oppose AFTA in principle, but it insisted on constructing AFTA very

carefully to avoid it becoming a trading bloc. At this stage, Malaysia regarded AFTA as an umbrella agreement.¹⁶

Despite its cautious attitude at the beginning, Malaysia, following Singapore, started to reduce its intra-ASEAN tariffs in 1993, followed by Thailand and Indonesia in 1995 and the Philippines in 1996 (Yamakage 1997: 199).¹⁷ There are two reasons why Malaysia promptly implemented AFTA. First, Malaysia had confidence in economic growth after it had experienced a high-growth period during the first half of the 1990s. Second, the government estimated that the risk that AFTA might negatively affect the economy was minimal because intra-ASEAN trade accounted for a small percentage of Malaysia's total trade, while the bulk of it depended on Japan, the United States and the EC. Therefore, AFTA did not go beyond having a "demonstration effect" (Ravenhill 2002: 176) against other regional groupings.

The 1997–98 Asian economic and financial crisis affected economies in ASEAN members, especially, Thailand, Malaysia and Indonesia. The FDI inflows into ASEAN dropped rapidly due to the crisis. ASEAN members strongly felt that AFTA should be strengthened to revive FDI inflows into the region. At the thirty-first AEM in September 1999, ASEAN members, for the first time, agreed on specific dates for eliminating intra-regional tariffs: 2015 for ASEAN 6 and by 2018 for others called CLMV (Cambodia, Laos, Myanmar and Vietnam) (AEM 1999).¹⁸ Furthermore, at the third ASEAN Informal Summit in November 1999, ASEAN members agreed to shorten the time schedule for tariff elimination to 2010 for ASEAN 6 and 2015 for CLMV (ASEAN Summit 1999). These agreements were based on a shared understanding among members that it was necessary to induce more investments from outside ASEAN to boost their economies.

However, it was not easy to adjust their overall trade policies to bring them in line with these agreements. Thailand, the Philippines and Malaysia increased tariffs for several products affected by the crisis (Kawada 1999: 41–44), and Malaysia had proposed to defer the deadline of tariff reduction under AFTA for CBU and CKD passenger cars, motorcycles and commercial vehicles from 2003 to 2005 at the thirty-first AEM in September 1999. This proposal was accepted, in spite of other members' resentment, at the fourth ASEAN Informal Summit in November 2000. Conditionally, ASEAN members at this summit agreed on the *Protocol Regarding the Implementation of the CEPT Scheme Temporary Exclusion List*, requesting that Malaysia should enter negotiations for compensation with those who believed they would be negatively affected by this deferment. In accordance

with this Protocol, Malaysia was engaged in four bilateral consultations with Thailand and two with Indonesia. As for the results of these consultations, MITI Report 2001 states:

With Thailand, both countries agreed to settle the issue amicably. As part of the settlement, both countries agreed to undertake measures that will strengthen further and expand relations between the two countries. Among others, Malaysia and Thailand have agreed to sign a Bilateral Payment Arrangement (BPA) which involves the use of local currencies for trade transactions.

Similarly, Malaysia and Indonesia had reached an amicable settlement, whereby both countries agreed to consider establishing cooperation programmes in the areas of mutual interest, particularly in the automotive and iron and steel industries.

(MITI 2001:60–61)

These consultations did not, however, achieve any concrete measures for compensation. The Malaysian government insisted that it fulfilled the necessary procedure indicated by the Protocol and therefore it had not undermined AFTA.¹⁹ Malaysia also understood that its commitments could be changed because of the Asian crisis.²⁰ This indicates Malaysia's understanding that AFTA is a flexible umbrella framework that enables members to change their commitments when necessary.

Nonetheless, deferment on certain products, CKD and CBU, is due to its unchanged domestic concerns for its automotive industry. Ford Motor Corporation, Malaysian Automotive Association (MAA) and Japanese Automobile Manufacturing Association expressed concerns about this deferment and urged the Malaysian government to review its plan to delay opening up its automotive industry by two years.²¹ On the contrary, Proton asked the government for a further extension of the rescheduled tariff reduction until 2008.²² Mahathir "has called on the national automotive industry to increase its production of locally-made components to bring down the price of national cars in order to remain competitive globally ... especially once AFTA compelled Malaysia to dismantle tariff barriers within five years."²³ During his official visit to Thailand in July 2002, he also confirmed that Malaysia was strongly committed to fulfilling its part of the commitment under AFTA.²⁴ This indicates the government has little intention to further defer tariff reduction schedule on automotive products. Rafidah said in February 2002 "[t]he government has not yet decided whether to bring down the tariffs on CKD and CBU cars imported from ASEAN members on a staggered basis."²⁵ However, in November 2002, Mahathir

finally announced, "we cannot impose high duties but there will be other taxes on both locally-produced and imported cars. It means there will be no more protection and all cars will be subjected to the same tax. ... Proton might have difficulty competing with cars assembled in some Asean countries with a much local content compared to Proton."²⁶ This revealed Malaysia's intention to reform its automotive industrial policy in accordance with its tariff reduction in AFTA.²⁷

To summarize, Malaysia agreed on AFTA because it considered AFTA a tool to exert pressure on other regional trading blocs. In 2000, Malaysia changed its commitments to AFTA due to its need to protect the automotive industry. This problem was rooted in the 1980s even before AFTA was agreed to in 1992. The government expected this industry to mature without tariff protection by the time AFTA was to be implemented in 2003. The Asian crisis, therefore, was not the determining factor but a catalyst for Malaysia to realize that it was still difficult to remove policies protecting its automotive industry. Malaysia then changed its commitment to AFTA to defer tariff reduction schedule on certain automotive products. However, it is important to note that, after this deferment, AFTA could make Malaysia start reviewing protective measures for its automotive industry at least within the ASEAN region. On the other hand, the reason why the Malaysian government still insisted that AFTA was its high priority is because it believed that commitments to AFTA could be changed for domestic reasons. Other ASEAN members, in particular Thailand, condemned the Malaysia's perception that AFTA is a flexible FTA.

Criticism against Bilateral FTAs: Backdoor Entry into AFTA

As mentioned above, AFTA will not be realized as a complete free trade area until all tariffs are eliminated by 2010 and 2015. Therefore, it is still necessary for ASEAN members to make strong commitments to the AFTA process. But at this stage, Singapore and Thailand had started to pursue bilateral FTAs with non-ASEAN countries, and Malaysia criticized these actions because it believed they would impede ASEAN cooperation. This position, together with its deferment on reduction of CBU and CKD tariffs, is based on unique Malaysia's interpretation of AFTA. MITI has been a leading agency in analyzing the effects of these bilateral FTAs. The National Economic Action Council (NEAC),²⁸ chaired by the Prime Minister, has also participated in discussions on this matter in order to make policy recommendations to the Cabinet.²⁹

Just after Singapore signed an FTA with New Zealand, Malaysian Foreign Minister Syed Hamid Albar warned against this bilateral FTA at the fourth ASEAN Informal Summit in November 2000, stating that, "when we do something outside the ASEAN context which could weaken the organization, we must think twice."³⁰ In February 2001, Mahathir also insisted that:³¹

This is a worrisome thing because you know, generally in the AFTA, we accept that anything that has a 40 per cent local content, that must be regarded as national.

That means they can enter into the markets of other countries. It would be very easy for these other countries to bring in partly completed products and complete them in Singapore and regard that as Singapore products, which would have free access into the other countries.

We have to watch this very carefully because this can be a back-door entry into AFTA.

After Thailand also began to pursue bilateral FTAs, Malaysia instructed ASEAN members not to allow outsiders to enter ASEAN markets through the backdoor into AFTA. In April 2001, Mahathir said in his speech at a dinner held in honor of Thai Prime Minister Thaksin Shinawatra:³²

Afta actually provides us with the opportunity to enlarge our industrial and commercial capacities and we must not let the opportunities be wasted and lost to us.

Malaysia on its part would not renege on its commitment to liberalize and open its markets as required under Afta.

Yes it is true that we have sought to defer temporarily the inclusion of completely built up and completely knocked down automotive parts in the Afta scheme but the deferment is merely to allow our domestic national car industry, adversely affected by the 1997 regional financial and economic crisis, to undertake necessary restructuring exercise to remain competitive in the post-Afta Asean.

Malaysia's interpretation of AFTA is that changing the agreed upon tariff reduction schedule within AFTA is allowed for domestic reasons, but bilateral FTAs with non-ASEAN countries could impede the effectiveness of AFTA.

Faced with the Malaysia's concerns on this matter, the Singaporean government responded to this backdoor entry argument as follows:³³

Asean had in place a mechanism that would pre-empt a "backdoor entry" into Afta by any of Singapore's FTA partners.

Asean had a system to ensure compliance to a "rules of origin" condition, whereby at least 40 per cent of the product's content must originate from within Asean for it to enjoy Afta's preferential tariffs.

... such agreements could not be used as an alternative means of entry to the Asean free trade zone.

There is only one door into Afta and that is the front door, referring to the criteria used to determine the national origin of a product.

Also, Singapore and Thailand discussed this matter at the foreign ministers' and prime ministers' levels in July and August 2001. They confirmed that bilateral FTAs would not open the backdoor for non-ASEAN countries to benefit from AFTA's preferential tariffs and instead urged that ASEAN should not delay the implementation of AFTA.³⁴ As the Singaporean government pointed out, AFTA has already built the rules of origin into its mechanism against the backdoor entry in the same way as any other FTAs.

Since mid 2001, Malaysia ceased to argue the backdoor entry problem. Instead, it began to emphasize that bilateral FTAs should not violate AFTA rules and that benefits of those FTAs should be given to other ASEAN members. In July 2001, Minister of MITI Rafidah Aziz said that:³⁵

When it comes to bilateral agreements, we have no right to question, but in the case of free trade agreements (FTAs) where you bargain on tariff concessions ... then it is going against Afta rules and that cannot be done. We must get Asean consensus.

... whatever benefits Asean countries provide to their partner in an FTA agreement should also be offered to the grouping.

Even in 2002, Malaysia repeated this statement.³⁶ However, tariff concessions in bilateral FTAs do not violate any provision in AFTA. Besides, it is unlikely that Singapore and Thailand would accept this Malaysia's claim because tariff concessions are a very crucial provision of FTAs. Since there is no provision in AFTA that expressly forbids bilateral FTAs, this statement reinforces that Malaysia's interpretation of AFTA is not necessarily shared by other ASEAN members. Therefore, it can be said that Malaysia's criticism against ASEAN members' bilateral FTAs were logically baseless at the beginning and even much more so in 2002. Even if Malaysia considered having bilateral FTAs, it would be impossible to have FTAs without any

tariff concessions. However, this event at least implies that Malaysia will not pursue bilateral FTAs without ASEAN consensus.

Nonetheless, Malaysia's concern is understandable if one takes into consideration that the argument about backdoor entry revealed the following problems for the AFTA mechanism. Firstly, Malaysia worried about the backdoor entry because AFTA's rules of origin, namely the 40 per cent ASEAN content, were rather "liberal" (Pelkmans 1997: 221). For instance, the Australia New Zealand Closer Economic Relations Trade Agreement (CER) and Mercado Común del Sur (MERCOSUR) require a 50 per cent value added standard with some other requirements (Palmer 1997: 341–55). Besides, the 40 per cent ASEAN content is a "net" cumulative regional content (Pelkmans 1997: 221). Due to such liberal rules of origin, Malaysia worries that outsiders can easily trade cheap products with CEPT tariffs under AFTA. However, it should be pointed out that the 40 per cent ASEAN content was agreed when AFTA was launched in 1992. Moreover, AFTA is not a custom union; therefore, ASEAN members can unilaterally impose their own import tariffs on products from non-ASEAN countries. Malaysia itself maintains FTZ and LMW policies with which all import tariffs are duty free.

Secondly, the backdoor entry argument was also derived from Malaysia's recognition that AFTA lacked an accurate system for certification of origin, by which it was measured if products were eligible for CEPT rates. ASEAN members only agreed that "a product shall be deemed to be originating from ASEAN Member States, if at least 40 per cent of its content originates from any Member State" (ASEAN Secretariat 1993: 32). According to the operational certification procedures for the rules of origin of the CEPT scheme, "the Certificate of Origin shall be issued by the exporting Member State" (ASEAN Secretariat 1993: 57–68). In 1997, ASEAN signed the ASEAN Agreement on Customs in order to simplify and harmonize customs valuation and improve efficiency and transparency on customs procedures (ASEAN Secretariat 1998: 105–12). But, there is not so much progress so far to ensure the accurate implementation of certification of the rules of origin under AFTA.³⁷ Malaysia's concern about this matter is confirmed with Rafidah's statement at the thirty-fourth AEM in September 2002.³⁸

ASEAN needs to standardize the definition of the Common Effective Preferential Tariff (CEPT) to fully implement the ASEAN Free Trade Area (AFTA).

... It was identified that the difference in definition of tariff under the CEPT was one of factors that can hinder or delay the implementation of AFTA.

Other obstacles include bureaucracy such as Customs process and

procedures of the respective countries that at certain time do not allow exporters to access through the Cept to penetrate into ASEAN markets.

This statement is true not only of Malaysia's exports into ASEAN markets, but also of its imports from other ASEAN countries. Malaysia cannot be sure if imported products from other ASEAN members are truly eligible to apply for CEPT rates.

To summarize, Malaysia's warning statements were regarded as political pressure on Singapore and Thailand to concentrate on implementation of AFTA and further to deter other ASEAN members from entering bilateral FTAs. Malaysia did not support this movement because it feared that bilateral FTAs could disturb ASEAN cooperation and unity. From Malaysia's point of view, members that choose to enter bilateral FTAs must make sure that they do not adversely affect ASEAN unity. This indicates that Malaysia does not intend to pursue bilateral FTAs without consensus among ASEAN members. Despite Malaysia still having some concerns about these bilateral FTAs, its warnings became more ambiguous in 2002. Malaysia has gradually learned that the backdoor entry argument could not be sustained because there were rules of origin in AFTA. Nonetheless, the argument illustrates that AFTA rules remain liberal on certification of origin. From this perspective, Malaysia has had to worry about other ASEAN members' bilateral FTAs because those FTAs might substantially weaken the AFTA rules.

ASEAN-based FTAs: After AFTA and Linkage with the EAEG

Even though Malaysia criticized Singapore and Thailand for pursuing bilateral FTAs, it does not mean Malaysia generally opposed FTAs. In 1999 ASEAN started to consider its FTAs with non-ASEAN partners. Mahathir stated in May 2002 "Malaysia believed that ASEAN should enter into FTAs as a grouping and not on their [ASEAN members'] own."³⁹ This shows that Malaysia considered the best to have ASEAN-based FTAs rather than bilateral FTAs with non-ASEAN countries. In particular, Malaysia wishes for closer cooperation in the ASEAN+3 framework, which is in line with its EAEG proposal. Also, AFTA can be a good model for Malaysia to establish ASEAN-based FTAs that would give flexibility on implementation.

For Malaysia, the EAEG has been an important regional policy proposal since 1990. Malaysia is a small economy and depends on foreign trade to a great extent. It is a constant necessity for Malaysia as a developing country

to defend its economic interests in world trade negotiations. ASEAN has been successful in fostering closer cooperation within Southeast Asia, but has limited influence in order to play a more effective role in the world economy (Lim 2001: 62). Consolidating East Asian countries is especially crucial to counter other regional groupings in Europe and the Americas. In order to revive the EAEG proposal, Malaysia volunteered to set up an ASEAN+3 secretariat in Kuala Lumpur at the fifth ASEAN+3 Summit in November 2001 (ASEAN and ASEAN+3 Summits 2001).⁴⁰ However, at the thirty-fifth AMM and ASEAN+3 Foreign Ministers Meetings in July 2002, other ASEAN members rejected this proposal because they were afraid that Malaysia intended to control ASEAN+3 cooperation.⁴¹ In the end of 2000, Mahathir admitted that the EAEG grew out of the ASEAN+3 dialogue, mentioning, "it [ASEAN+3] will become more of an East Asian grouping."⁴² Rafidah also said at the thirty-fourth AEM plus three dialogue partners in 2002, "this [ASEAN+3] is considered to be an endorsement on Malaysia's proponent of the East Asia Economic Caucus (EAEC) concept."⁴³ This can explain Malaysia's enthusiasm for an ASEAN+3 secretariat.

In 1999, ASEAN launched a high level task force to pursue the possibility of an FTA with CER. This was the first attempt for ASEAN as a group to establish an FTA with non-ASEAN countries. In September 2000, Malaysia proposed that the task force should look at facilitating trade between the two groupings as a short-term measure. Rafidah suggested that, "removing trade barriers would require time as it involves further negotiations on the mechanism for the free trade area."⁴⁴ Although Malaysia agreed to set up a task force, it did not intend to support establishing this FTA. In February 2001, Rafidah maintained this position and mentioned that an East Asian community did not extend to Australia or New Zealand.⁴⁵ There was also a tension between Australia and Malaysia in terms of their proposals [APEC and EAEG] in 1989 and 1990 (Milne and Mauzy 1999: 140–41; Liow, 2001: 150). Malaysia responded negatively to the ASEAN-CER FTA as well as APEC because it did not fit to its EAEG proposal in terms of membership. The linkage between Malaysia's opposition to an ASEAN-CER FTA and composition of an East Asian community is highlighted by Malaysia's willingness to consider an ASEAN-China FTA despite its potential economic damage on domestic industries in Malaysia.

At an informal ASEAN Summit in November 2000, Chinese Premier Zhu suggested setting up the ASEAN-China Expert Group to look into economic cooperation between ASEAN and China. According to the Report submitted by this Expert Group in October 2001, it was pointed that:

Hence, an ASEAN-China free trade area would represent an important move forward in terms of economic integration in East Asia. It would serve as a foundation for the more ambitious vision of an East Asia Free Trade Area, encompassing ASEAN, China, Japan and Korea.

The removal of trade barriers between ASEAN and China will lower costs, increase intra-regional trade and increase economic efficiency. The FTA will lead to greater specialization in production based on comparative advantage.

On the other hand, there will be challenges arising from the establishment of a FTA between ASEAN and China. There would be intensified competition in each region's domestic market given the similarity in industrial structures.

(ASEAN-China Expert Group 2001: 30-31)

This report attaches *ANNEX 1: ASEAN Member Countries National Report* to give each member's perspective for economic relationship with China. The Malaysia's report made recommendations as follows:

Given the current relatively small percentage of trade between Malaysia and China, short and medium-term measures should target at improving the export opportunities for Malaysian companies to China. While tariff reductions have been scheduled under the bilateral negotiations between Malaysia and China, based on the survey response, the facilitation of trade between the two countries will be greatly enhanced by using international standards as well as by simplifying customs procedures in China.

While the formation of an ASEAN-China Free Trade Area (FTA) is also deemed as very important, this is a long-term measure and the actual modalities for an FTA are beyond the current scope of this study.

(ASEAN-China Expert Group 2001: 64)

At the ASEAN-China Summit in November 2001, ASEAN members and China "endorsed the proposal for a Framework on Economic Cooperation and to establish an ASEAN-China Free Trade Area within ten years with special and differential treatment and flexibility to the newer ASEAN members" (ASEAN and ASEAN+1 Summits 2001). Just after this Summit, while Malaysia agreed to have an ASEAN-China FTA in principle, Mahathir pointed out that:⁴⁶

China is a big producer of goods which are in direct competition with goods produced in the region, and we must make sure the influx will not cause our industries to shut down.

To a great extent, this Malaysia's anxiety is shared by other ASEAN members. Malaysia particularly recognizes that the FTA will take some time to be realized due to its potential economic damages. At the ASEAN-China Summit in November 2002, ASEAN and China "signed the Framework Agreement on ASEAN-China Economic Cooperation which will serve as the fulcrum for establishing the free-trade area by 2010 for the older ASEAN members and 2015 for the newer members with flexibility on sensitive commodities" (ASEAN, ASEAN+3 and ASEAN-China Summits 2002). Based on this Framework, both parties agreed to implement an *Early Harvest Programme* in which tariff rates of mainly agricultural products will be reduced by 2006, earlier than other products. However, Malaysia and the Philippines extended the date to complete the appropriate product lists for this Programme until March 2003 whereas other ASEAN members have already submitted theirs (ASEAN-China Summit 2002). Malaysia agreed in principle with the ASEAN-China FTA because it would contribute to closer cooperation in ASEAN+3. This attitude contrasts with the opposition to establishing an ASEAN-CER FTA. On the other hand, Malaysia made reservations on implementation of the ASEAN-China FTA because it fully recognized the economic impact of the FTA on domestic industries.⁴⁷ Based on Malaysia's deferral of submitting its list of products, it can be argued that Malaysia is attempting to incorporate an AFTA-like flexible mechanism into implementation of the ASEAN-China FTA.

Two months after ASEAN and China agreed to establish an FTA within ten years, Japanese Prime Minister Koizumi visited ASEAN members and proposed an initiative for the Japan-ASEAN Comprehensive Economic Partnership in January 2002. This proposal mentioned an idea for an East Asian community consisting of ASEAN members, China, Japan, South Korea, Australia and New Zealand. Koizumi emphasized that the Japan-ASEAN Comprehensive Partnership was an important platform for building up such a community and took a Japan-Singapore FTA as an example of this partnership (Koizumi 2002). Mahathir supported this proposal and suggested that this proposal could be realized within the framework of ASEAN+3.⁴⁸ Mahathir supported the Koizumi's initiative because its core idea was consistent with his own EAEG proposal, but he still opposed CER membership. At the AEM-METI (Ministry of Economy, Trade and Industry, Japan) meeting in September 2002, ASEAN and Japan finally agreed that:

The Ministers welcomed the joint study report of the ASEAN-Japan Closer Economic Partnership (CEP) Expert Group and were encouraged by the positive findings of the study, including the possibility of an FTA.

... The implementation of measures for the realization of the partnership, including elements of a possible FTA, should be completed as soon as possible within ten years while according due consideration to the economic levels and sensitive sectors of each country. For this purpose, the Ministers agreed to recommend to the Leaders the establishment of a committee, consisting of senior officials of ASEAN and Japan, by the year 2003.

(AEM-METI 2002)

The ASEAN-Japan CEP is regarded as in line with the Koizumi's initiative. After this agreement, Japan showed its intention to start discussing the possibility of bilateral FTAs with each of the ASEAN countries as well as a Japan-ASEAN FTA.⁴⁹ In November 2002, ASEAN and Japan endorsed "the approach that, while considering a framework for the realization of a Comprehensive Economic Partnership between Japan and ASEAN as a whole, any ASEAN member country and Japan could initiate works to build up a bilateral economic partnership" (ASEAN-Japan Summit 2002). In December, Mahathir, for the first time, showed a positive response towards a bilateral FTA between Malaysia and Japan.⁵⁰ This positive response was made possible after the ASEAN-Japan agreement in November 2002. Malaysia's proposal for its bilateral FTA with Japan does not contradict its policy for ASEAN-based FTAs. Rather, it reveals that Malaysia regards ASEAN-based FTAs as the most important. Cooperation with Japan is an essential element for materializing the EAEG for Malaysia. Malaysia and Japan are complementary in terms of their industrial structures. In addition, Japan has been the most important trading partner for Malaysia since the 1980s and the largest importer of LNG from Malaysia.⁵¹ Therefore, although feasibility of implementing this bilateral FTA needs to be investigated closely, it is unlikely that Malaysia has concerns for its domestic industries, which were expressed in the case of an ASEAN-China FTA.

In December 1998 President Kim Dae-jung of the Republic of Korea proposed the formation of an East Asia Vision Group. ASEAN, Japan and China welcomed this proposal and the Group was established in October 1999 at the Summit of ASEAN+3.⁵² The Group submitted the report to the ASEAN+3 Summit in 2001. The report stated that:

The Vision Group recommends the formation of an East Asia Free Trade Area (EAFTA) and liberalization of trade well ahead of the Bogor Goal set by APEC. In order to facilitate the formation of a region-wide FTA, East Asia needs to consolidate all existing bilateral and sub-regional FTAs within

the region. We recommend the establishment of a ministerial committee to oversee the development of an EAFTA.

(East Asia Vision Group 2001: 20–21)

After receiving this recommendation, the ASEAN+3 Summit in 2001 released the following statement.

We considered the Report of the East Asia Vision Group and once again warmly thanked President Kim for launching the initiative in 1999. The report contains key proposals and concrete measures to broaden East Asia cooperation. Some are bold yet feasible such as establishing an East Asia Free Trade Area and liberalizing trade well ahead of APEC's goals.

(ASEAN and ASEAN+3 Summits 2001)

ASEAN+3 members reacted positively to the recommendation to establish an EAFTA. Although Malaysia agreed with moving towards an EAFTA, Mahathir pointed out that "East Asia is not ready to be transformed into a free trade zone due to economic disparity among countries in the region."⁵³ Malaysia recognizes that it would take a long time to establish this FTA because it has similar concerns about impacts on domestic industries as on the ASEAN-China FTA. However, the ASEAN+3 framework seems to fit into the EAEG concept in terms of membership.⁵⁴ In addition, it should be noted that Mahathir linked the ASEAN+3 framework that excludes CER countries with his support for the Koizumi's initiative that aimed to include the concept of FTA in an East Asian community.⁵⁵

As has been noted, Malaysia considered it best to have ASEAN-based FTAs rather than bilateral FTAs that receive no ASEAN consensus. Moreover, Malaysia expects ASEAN-based FTAs to contribute to realizing its EAEG proposal. Malaysia did not support an ASEAN-CER FTA even as a framework agreement because it did not admit CER countries as East Asian. As for an ASEAN-China FTA, Malaysia officially agreed because China is a part of East Asia. This also applies to an ASEAN-Japan FTA. Obviously, Malaysia is happy with membership of an ASEAN+3 FTA. Malaysia supported an ASEAN-China and an ASEAN-JAPAN FTA because these FTAs could contribute to formation of an ASEAN+3 FTA in the future.

However, Malaysia has fully recognized impacts of implementation of FTAs on domestic industries. When Mahathir is cautious about implementation of an ASEAN-China FTA, he fears that imports from China would have negative effects on domestic industries in Malaysia. He also

finds it difficult to implement an ASEAN+3 FTA that includes China. To put it differently, AFTA is a good FTA because its flexibility allows Malaysia to protect domestic industries. Therefore, it can be concluded that Malaysia hopes that those potentially problematic ASEAN-based FTAs will adapt an AFTA-like flexible mechanism for their tariff reduction.

Conclusion

There are two important aspects that should be considered when trying to understand Malaysia's position on FTAs: economic impacts on domestic industries and the linkage with its ASEAN diplomacy. The former leads Malaysia to waver in its support for FTAs. When Malaysia agreed to AFTA, it expected its domestic automotive industry to become competitive enough to survive on its own by the time that AFTA was scheduled to be fully realized as a 0–5 per cent tariff regime in 2003. The Asian financial and economic crisis led to Malaysia's realization that it was still difficult to remove measures protecting its automotive industry. As a result, Malaysia asked for deferment of its tariff reduction schedule of some automotive products in 1999, and the request was approved by other ASEAN members in 2000. Although the Malaysian government has finally attempted to change its automotive policy in accordance with its commitments to AFTA since 2000, this deferment illustrates that Malaysia views AFTA as a flexible FTA that enables members to change their commitments on tariff reduction.

The second aspect of Malaysia's FTA policy is the linkage with its ASEAN diplomacy. Malaysia has fully recognized that it should be engaged in some groupings in order to promote its economic interests in multilateral trade liberalization. This was one of the motives behind Malaysia's proposing the EAEG in 1990 and agreeing to establish AFTA in 1992. The EAEG remains an important regional policy for Malaysia even after 1992. Malaysia admits that the EAEG is about to be realized through cooperation in the ASEAN+3 framework. This suggests that Malaysia supports FTAs with ASEAN+3 members even in the long run. Bilateral FTAs emerged as another policy option for ASEAN members for trade liberalization apart from AFTA and the WTO. Malaysia criticized Singapore and Thailand that they pursued bilateral FTAs with non-ASEAN countries because it feared that the move towards bilateral FTAs might disturb ASEAN unity or its cooperation. According to Malaysia, ASEAN members should receive ASEAN consensus when they pursue bilateral FTAs with non-ASEAN members. In this sense, Malaysia could justify its own proposal of a bilateral

FTA with Japan since this was initiated after the ASEAN-Japan FTA agreement in November 2002. Finally, the Malaysia's fear towards other ASEAN members' bilateral FTAs is partly derived from the character of AFTA's rules that remains liberal on certificate of origin. However, AFTA is also a comfortable mechanism for Malaysia because it gives some room to change its commitments. This point is related to the first aspect of FTAs. Malaysia is very careful about implementation of an ASEAN-China FTA due to potential damage to domestic industries by imports from China. One of the reasons why Malaysia supports ASEAN-based FTAs is because it is likely for those FTAs to adopt an AFTA-like flexible mechanism. Mahathir insists that the EAEG is a loose economic grouping, but establishing an ASEAN+3 FTA with such a flexible mechanism can be categorized as a loose cooperation scheme in East Asia.

Malaysia's policy towards FTAs has the following theoretical implications. First, the linkage between its FTA policy and ASEAN diplomacy is based on a diplomatic group formation or coalition building approach. This point has been shared with other ASEAN members since AFTA was launched as a pressure body against the EC and NAFTA. Second, ASEAN members aim to build a sub regime or a trading network based on ASEAN. In particular, Malaysia hopes for ASEAN to play a central role in building a network of FTAs. Third, Malaysia's strong commitments to the East Asian regional cooperation is based on its regional concept under the EAEG. Fourth, Malaysia understands FTAs as policies that should be negotiated and enacted within the context of ASEAN. AFTA is more flexible than other regional FTAs in terms of implementation. Malaysia is satisfied with AFTA-like FTAs whereas Singapore and Thailand started to take their stances that AFTA and bilateral FTAs can coexist. This means that ASEAN members do not necessarily interpret the latter two points in the same way. These perceptual differences have emerged as AFTA moved to the implementation stage. These differences could be divisive when it comes to ASEAN's strategy towards establishing FTAs with Japan and China.

Notes

- 1 In 1990, the rest of APEC members were Brunei, Indonesia, Japan, Malaysia, the Philippines, Singapore, South Korea and Thailand. Although China entered APEC in 1991, it was assumed to be a member of the EAEG because Mahathir proposed the EAEG to the then Chinese Premier.

- 2 The MITI Report 2000 also mentioned a similar statement (MITI 2000: 66).
- 3 See 2003 Tariff Database on the website of the United States International Trade Commission. (<http://dataweb.usitc.gov/scripts/tariff2003.asp>). Last accessed on February 26, 2003.
- 4 China became the fourth largest trading partner for Malaysia in 2001 (MITI 2001: 13).
- 5 In Malaysia, most domestic policies have been conducted in line with the so-called *Bumiputra* policy. This policy was officially introduced as the New Economic Policy (NEP) to give economic and social privileges to the *Bumiputra* (which are mainly the Malays) over the Chinese and Indians (Gomez and Jomo 1997: 24–66). In the context of industrial policies, the NEP helps the Malays, who are economically underdeveloped, to participate in the industrialization process by attempting to increase the *Bumiputra* employment and its capital accumulation. Both of the two industrial policies (the export-promotion policy and the heavy industrialization program) could contribute to the *Bumiputra* employment in the manufacturing sector, but particularly the heavy industrialization program played a role in increasing the *Bumiputra* capital in the manufacturing sector.
- 6 On the condition of at least 80 per cent for exports in total production, companies can receive LMW treatment.
- 7 This was in line with Industrial Master Plan (1986–95) to promote outward-oriented industrialization. The 1975 Industrial Co-ordination Act regulated the requirement in establishing companies that the *Bumiputra* capital must share at least 30 per cent of the total equity in accordance with the NEP principle. But, since 1985, foreign investors in Malaysia's manufacturing sector had been able to hold 100 per cent equity on the condition of at least 80 per cent exports of their production (Kitamura 1990: 114–20). In 1998, the government further liberalized this foreign equity policy. Currently, foreign investors can hold 100 per cent equity irrespective of their level of exports as long as project applications are received by December 31, 2003. (<http://www.mida.gov.my/invest.html>). Last accessed on February 27, 2003.
- 8 The heavy industrialization program was carried out by a public sector agency, namely the Heavy Industries Corporation of Malaysia. In Malaysia, "heavy industrialization" meant setting up a hot briquetted iron and steel billet plant, an additional cement plant, the national car project and small engine plants (Jomo and Edwards 1993: 28–29).
- 9 This policy was also to ensure employment of the *Bumiputra* and the participation of their capital.
- 10 Thailand and Indonesia have already phased out this requirement in 2000.
- 11 Mahathir said that Asian countries on the Pacific Rim should explore ways of strengthening regional cooperation. He further explained that "initially at least we should learn to consult each other and speak with one voice when negotiating with the European and American blocs" (*New Straits Times*, January 12, 1991).
- 12 *New Straits Times*. October 2, 1991.
- 13 *The Straits Times*. February 1, 1992.
- 14 *New Straits Times*. October 2, 1991.
- 15 *New Straits Times*. October 9, 1991.
- 16 Foreign Ministry Secretary-General, Ahmad Kamil Jaafar, said that the agreements of the 1992 ASEAN Summit signaled "the beginning of a process to develop AFTA" (*Business Times* (Malaysia), January 17, 1992).

- 17 For details on AFTA implementation schedules, see (ASEAN Secretariat 1993, 1995a, 1995b, 1996, 1998).
- 18 Before 1999, it was only agreed on the 0–5 per cent tariff reduction schedule in AFTA.
- 19 Indonesia did also defer its tariff reduction schedule for sugar products without any Protocol. In this case, there was only an informal meeting between Indonesia and Thailand although Thailand strongly complained about this Indonesian deferment (Interview with an official of ASEAN Secretariat. September 4, 2002; Interview with an official of Ministry of Trade and Industry, Indonesia. September 2, 2002).
- 20 Interview with an official of ASEAN Economic Cooperation Division, MITI, Malaysia. August 22, 2002. In June 2001, Mahathir also said, “AFTA was established before the Asian economic and financial crisis, and at that time we had not realized what FTAs were like” (Nihon Keizai Shimbunsha 2001: 32, translated by author).
- 21 *Business Times* (Malaysia). February 22, 2002; *The Star*. June 6, 2002; Interview with the President of MAA. August 26, 2002.
- 22 Interview with Dr Mohammed Ariff. August 20, 2002; Interview with the President of MAA. August 26, 2002.
- 23 *The Star*. June 15, 2000.
- 24 *The Star* and *New Straits Times*. July 7, 2002.
- 25 *Business Times* (Malaysia). February 27, 2002; Interview with an official of ASEAN Secretariat. September 4, 2002.
- 26 *New Straits Times*. November 8, 2002.
- 27 As mentioned earlier, this industrial policy is closely related to the *Bumiputra* policy. Thus, reforms of the *Bumiputra* policy could lead to restructuring of this industry. Mahathir himself recognizes that the *Bumiputra* policy should be amended or reformed (*The Star*. July 20–21, 2002).
- 28 NEAC was established as a consultative body to the Cabinet in January 1998. The membership of the NEAC consists of Economic Ministers and representatives from various fields in the private sector and selected organizations. (<http://www.neac.gov.my/start.cfm>). Last accessed on February 27, 2003.
- 29 Interview with an official of the Economic Planning Unit (functioning as the NEAC Secretariat) in Prime Minister’s Office. August 23, 2002.
- 30 *The Star*. November 23, 2000.
- 31 *Bangkok Post*. February 27, 2001; Rafidah also repeated the warning (*The Straits Times*. February 21, 2001).
- 32 *New Straits Times*. April 25, 2001.
- 33 *The Straits Times*. May 3; June 14, 2001. Singapore’s Prime Minister Goh Chok Tong even asserted “those who can run faster should run faster and should not be restrained by those who do not want to run at all” (*Bangkok Post*. February 27, 2001).
- 34 *Bangkok Post*. July 18, 2001; *The Strait Times*. August 24, 2001.
- 35 *The Nation*. July 6, 2001.
- 36 In January 2002, Rafidah stated again “Singapore was free to enhance bilateral trade relations with any nation as long as it did not violate the provisions of the ASEAN Free Trade Agreement” (*New Straits Times*. January 8, 2002). In May 2002, Mahathir stated “[w]e are waiting and watching to see how the Singaporean FTAs with Japan, New Zealand and the US will be used by these countries to enter the ASEAN market by taking advantage of AFTA” (*The Star*. May 22, 2002).

Furthermore, Rafidah said at the AEM Retreat in July 2002 that "a Free Trade Agreement made by individual ASEAN country with non-member countries would not affect the group as long as it does not involve any tariff issues or violate the grouping's current agreements" (*New Straits Times*. July 7, 2002).

- 37 Interview with an official of ASEAN Economic Cooperation Division, MITI, Malaysia. August 22, 2002.
- 38 *New Straits Times*. September 16, 2002. This point is also confirmed by an interview with an official of ASEAN Economic Cooperation Division, MITI, Malaysia. August 22, 2002.
- 39 *The Star*. May 22, 2002.
- 40 Interview with an official of ASEAN Economic Cooperation Division, MITI, Malaysia. February 21, 2002.
- 41 The Philippines Foreign Ministry Undersecretary Lauro Baja said the ASEAN Standing Committee had considered three options. The first was along the lines of Malaysia's proposal to establish a secretariat to be hosted by an ASEAN member country. The second option was to expand the ASEAN secretariat in Jakarta, and the third was to establish an ASEAN+3 bureau within the ASEAN secretariat. Thai and Philippine officials were said to suggest the committee to look into other options besides Malaysia's proposal. Suchitra Hiranpreuk, the director-general of ASEAN Department in the Thai Foreign Ministry said "[w]e prefer to strengthen the ASEAN secretariat in Jakarta but we are open to discussion" (*New Straits Times*. July 28, 2002).
- 42 *The Star*. November 25, 2000.
- 43 *New Straits Times*. September 16, 2002.
- 44 *The Star*. September 5, 2000.
- 45 *The Straits Times*. February 21, 2001. Mahathir has his view that Australia has little in common with Asia other than being geographically close. He blocked Australia's bid to participate in Asia-Europe Meeting summits (Milne and Mauzy 1999: 131).
- 46 "Asian nations agree free-trade zone." *BBC News Online: World: Asia-Pacific*, November 6, 2001, quoted from Ravenhill (2002: 182, footnote 15).
- 47 China is one of the main destinations for palm oil from Malaysia and China's trade barrier on palm oil is not tariffs but the import quota system (MITI 2001:99-100). Thus, it is not easy for Malaysia to reduce this non-tariff barrier in China by pursuing an FTA.
- 48 *Nihon Keizai Shimbun*. May 14, 2002.
- 49 *Nihon Keizai Shimbun*. November 6, 2002.
- 50 *Nihon Keizai Shimbun*. December 12, 2002. See also a press interview with a Japanese government official. (<http://www.meti.go.jp/speeches/>). Last accessed on February 27, 2003.
- 51 Malaysia imports passenger motor vehicles with high tariffs from Japan, but this accounts only for 5.2 per cent of total imports from Japan (MITI 2001: 26).
- 52 The East Asia Vision Group was composed of intellectuals who participated as individuals, not as representatives of their countries (East Asia Vision Group 2001: Appendix I).
- 53 *New Straits Times*. March 21, 2002.
- 54 At the AEM plus 3 dialogue partners meeting in September 2002, Rafidah said that, "as a follow-up to the vision group [the East Asia Vision Group], South

Korea had set up a task force to study the recommendations put forward by the vision group to realize the potential of EAEC." She further stated that "[i]n the long term, the integration process would also evolve in the establishment of the East Asian free trade area" (*New Straits Times*, September 16, 2002).

- 55 In May 2002, he repeated that the proposed EAEG would continue to be a very loose grouping for a very long time, "confining itself to discussion of regional affairs and common problems" (*The Star*, May 22, 2002). He also stated that the EAEG could work on a concept like the European Economic Community (EEC), explaining that "the most significant achievement of the EEC is not so much economic as the half century of peace that it brought to Europe" (*New Straits Times*, May 22, 2002). This indicates that Mahathir began to envisage the EAEG as an ideal idea for contributing to security cooperation in East Asia.

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