

The U.S. - Malaysia Free Trade Agreement

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The Basis of Free Trade

Theoretically, international trade arises from the concept of competitive advantage. It is a means to facilitate specialization, to increase productivity of available resources and to realize a larger output and economies of scale than possible through pursuing self sufficiency or autarchy. If these outcomes are successfully achieved, the people of the nation should achieve a higher standard of living than if the nation attempts to be self-sufficient. This is assuming that there is an equitable distribution of benefits of free trade within the country. The rationale for free world trade draws from two main factors:-

1. The uneven distribution of economic resources or factor endowments between various countries; and
2. The efficient production of various goods and services requires different resource combinations and technologies.

However, reality and ideology differ. In reality the process of globalization is marred by politics and self interest. These are major concerns which affect the credibility of free trade. For globalisation to generate peace and stability around the world, the most economically and politically powerful countries should not dominate the weaker countries and regions by way of one sided trade agreements or through a host of various other political tools. Today, the functions of power and politics have affected the process of globalisation which brings it nowhere close to the perceived notion of free trade highlighted above. There is a wide disparity between the "free trade" preached and practiced today as highlighted in the recent World Trade Organisation meetings.

This article will explore the imminent U.S.-Malaysia FTA highlighting the expectations of both partner countries, the benefits versus some key criticisms, some challenges anticipated during the negotiation process and their impacts on the Malaysian people and the economy.

The Agreement

The U.S. is Malaysia's largest trading partner. In 2005, the U.S. accounted for 16.6 percent of Malaysia's total trade.¹ In the same year, trade with the U.S. increased by 8.7 percent in comparison with 2004. Malaysia has a rising trade surplus with the U.S. as highlighted in Graph 1.

In early March 2006, Malaysia and the U.S. announced the intention to negotiate a bilateral trade agreement. The first of five rounds of negotiations will take place here in Penang from 12 till 16 June. The negotiations will cover market access for goods, agriculture, cross-border services, financial services, investments, intellectual property rights, government procurement, competition policy, labour, environment, sanitary and phytosanitary measures, technical barriers to trade, trade facilitation, transparency, customs, administration and dispute settlement process. The implications of an all encompassing trade agreement of such great magnitude are enormous; and as expected, it has sparked the interest of the business community, political parties and in general, the people of Malaysia.

In this regard, the government needs to assure its people that the objectives of its involvement in this negotiation have been given serious consideration and that the potential benefits of entering into such negotiations outweigh the costs. Malaysia and the U.S. are important trade partners and benefit from a symbiotic economic relationship. In the past, these two nations have not always seen eye-to-eye in terms of political viewpoints but nevertheless have benefited from the mutual respect and pragmatic approach taken by both countries in terms of trade and business opportunities.

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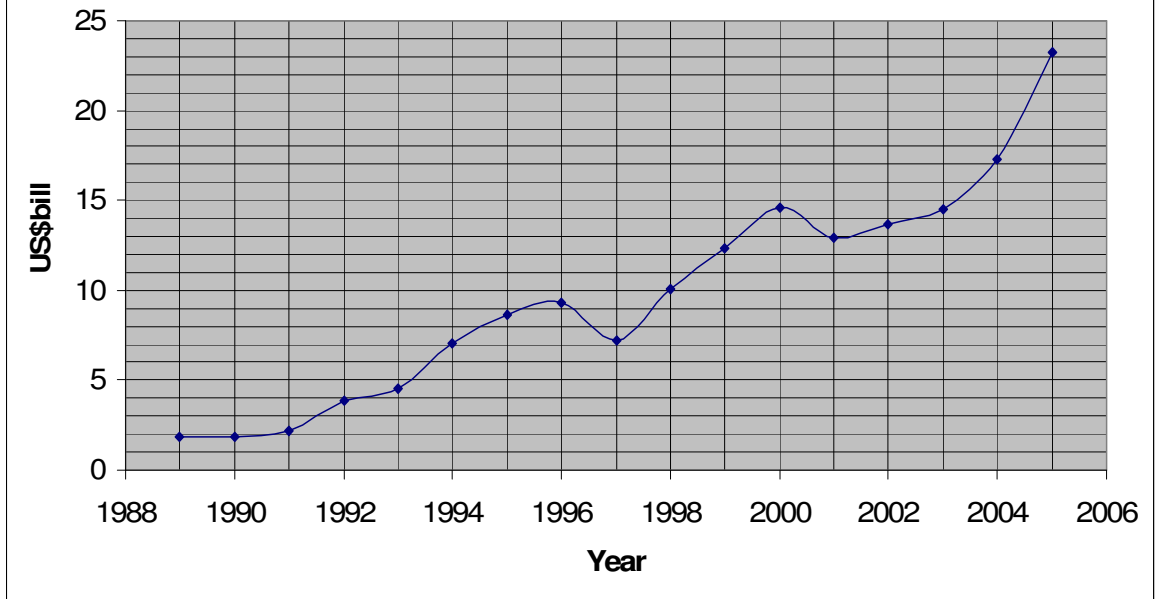
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¹ "Performance of the Manufacturing and Related Services Sectors 2005", Malaysian Industrial Development Authority, p.10

Graph 1: Malaysia's Trade Surplus with the United States



Malaysia's trade surplus with USA, without a USFTA
(US Government statistics)



Source: <http://tse.export.gov/>

Malaysia and the U.S. are important trade partners and benefit from a symbiotic economic relationship.

The TPA: How It Affects the Negotiation Process

The TPA is the U.S.' "Bipartisan Trade Promotion Authority Act of 2001". It essentially gives the American administration the authority to negotiate trade agreements with interested partner countries. Under the TPA, the American Congress sets general negotiating objectives and boundaries for the agreement, but agrees not to seek to amend any draft agreement that is sent to it for approval. Congress can vote "yes" or "no" but cannot make changes to the package. This authority is sometimes called "fast track" authority, since it limits the ability of Congress to "re-open" negotiations and establishes a fixed period for Congress to consider proposed trade agreements. The TPA will expire on 1 July 2007. The negotiating parties hope to complete negotiations by the end of 2006 in order to take advantage of the "fast track" approval as highlighted above. However, International Trade and Industry Minister Datuk Seri Rafidah Aziz has explicitly stated that "an FTA needs to benefit both countries and are not subject to deadlines", making it clear that Malaysia will not be rushed into an unsatisfactory agreement. The inability of both Malaysia and the U.S. to agree on a mutual set of terms for investment and trade by the "fast track" deadline will not render the agreement void. It merely means that the terms of the FTA will be considered under a different set of circumstances.

The Malaysian Wish List

From the Malaysian perspective, the objective of the establishing a free trade agreement with the U.S. would be to:-

- seek better market access for Malaysian goods and services;
- further facilitate and promote bilateral trade and investment flows as well as economic development;
- enhance the competitiveness of Malaysian producers and exporters through collaboration; and
- build capacity in specific targeted areas through technical cooperation.

"An FTA needs to benefit both countries and are not subject to deadlines."

The Malaysia-U.S. FTA will cover liberalisation of the goods and services sector; trade and investment promotion and facilitation activities; investment protection; economic and technical cooperation programmes; and appropriate flexibilities to cater for development objectives.²

The American Wish List

The TPA objectives include:

- Improved market access for goods, including increased agricultural access;
- Liberalisation of the services sector with particular interest in financial services, telecommunications and e-commerce;
- Non-discriminatory treatment for American investments in Malaysia and binding investor-state dispute settlements;
- Increased Intellectual Property Rights (IPR). This is expected to encompass WTO-plus obligations covering trademarks, geographic indicators, copyrights, patents and data protection with certain exceptions for public use. The U.S. would also expect enhanced enforcement in relation to the clamping down of digital and software piracy.
- Access to Government Procurement. The U.S. hopes that the FTA will create a level playing field for all prospective bidders in terms of government procurement;
- Transparency and Anti-Corruption Measures; and
- Labour and Environmental Protection.

By comparison, the American list seems more comprehensive and it states clearly what it wishes to achieve from this potential partnership. In contrast, the Malaysian list as gathered from the Ministry of International Trade and Investment (MITI) website seems to be more general in nature, with little specific information and the desired outcomes it would like to achieve from this partnership. Malaysian negotiators must be equipped with sufficient information of the domestic industries represented; including the challenges faced and their specific needs, to ensure that we are not disadvantaged in any way during the negotiation process. For example, according to current U.S. legislation, there is a specific provision which prevents the USTR from lowering its existing tariffs of 5 percent or greater by more than 50 percent in its negotiations. The Malaysian negotiation team would benefit from entering into the negotiation process with such similar and clear cut guidelines.

What's In It for Malaysia & the United States

According to the American Malaysian Chamber of Commerce (AMCHAM), this bilateral trade agreement will present a significant opportunity for both Malaysia and the U.S. to strengthen the close economic and political relationship. Broadly speaking, both nations should enjoy greater market access, the creation of more and better-paying jobs and the increased access to more goods at lower prices.

The AMCHAM website highlights the following benefits of the FTA for both countries:-

1. Increased trade flows

An FTA would increase existing trade flows between these two countries as well as the scope of goods traded. As at 2005, two-way trade between both countries exceeded RM 167 billion (USD 44 billion). More than 20 percent of Malaysia's exports are headed for the American market.

2. Significant consumer potential

The Malaysian population of 27 million people and a GDP of almost \$250 billion present a significant market for American companies. To the U.S., Malaysia is a gateway for market penetration into the developing countries of the South East Asian region. Similarly Malaysian businesses will have fewer restrictions in tapping into the third largest population in the world. The American population is estimated at approximately 297 million people.



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² Malaysia-US Free Trade Agreement, 3 May 2006; www.miti.gov.my

3. Increased awareness

Outside of the manufacturing circles (especially the Electrical and Electronics sector), American awareness of Malaysia as a nation and its achievements and progress as a leading transitional developing economy is low. An FTA is a means to raise the profile of Malaysia among the Americans, resulting in increased investments and tourist arrivals. At the same time, it will serve to educate Malaysian companies on the opportunities and possible benefits of doing business in the U.S.

4. New Opportunities

The liberalization of certain market sectors, such as services, automotive, telecommunications, if successful, will present significant business opportunities to firms in both countries. Malaysian companies will also benefit from technology transfer and may have an increased role to play in regional and global supply chains.

5. Supporting Malaysia's National Development

Liberalised trade and investment policies as a result of the FTA will allow Malaysia to build up its core competence in the newly targeted areas of growth which encompass knowledge based activities by benefiting from less stringent labour and investment laws which should facilitate technology transfer. This will enable Malaysia to diversify its economic base and to become less reliant on the manufacturing sector to generate growth as its services sector gains prominence.

6. Economic Expansion

The higher levels of foreign direct investment which may be generated are expected to translate into greater two-way trade and Malaysia's economy should experience an expansion in this regard. The U.S. should also benefit from increased export opportunities into Malaysia.

7. Jobs

Economic expansion should lead to the creation of more and better paying jobs for both countries. Economic studies have found that jobs in the export sector pay higher wages than comparable jobs in domestically focused industries.

8. Intellectual Property Rights

Malaysia is a member of the World Intellectual Property Organization (WIPO) and is a party to the Berne Convention for the Protection of Literary and Artistic Works and the Paris Convention for the Protection of Industrial Property. However, Malaysia faces problems in dealing with the piracy of copyrighted materials, especially with regards to optical media. The International Intellectual Property Association (IIPA) estimates 2005 industry losses in Malaysia due to piracy at \$147.3million.³ Malaysia has responded by tightening the laws on intellectual property protection and is seen to gain significantly from the adoption of strong IPR measures through the FTA. The stringent IPR set out in the FTA will help Malaysia's standing as an important center for IPR protections and could encourage greater investment from the software, motion picture, pharmaceutical and biotech industries.

9. Halal Products

The large Middle Eastern community in the U.S. presents a significant opportunity for Malaysian agro-based, food processing and Islamic financial services companies. An agreement on halal certification standards and procedures would facilitate two-way halal trade between the partner countries.

10. Sectoral Opportunities

A comprehensive FTA will allow American investors access to several highly protected industries in Malaysia such as automotive, express delivery services, financial services, ICT and pharmaceuticals. Nevertheless, most of these sectors, with the exception of ICT, are highly protected industries and are expected to face the most challenges during the negotiation process.



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³ USTR's 2006 National Trade Estimate Report on Foreign Trade Barriers: Malaysia, http://www.ustr.gov/Document_Library/Reports_Publications/2006/2006_NTE_Report/Section_Index.html

On the flip side, certain **concerns** with regards to the signing of the U.S.-Malaysia FTA include:-

1. The economic impact of tariff elimination

Tariffs are a form of taxes charged on imported goods in a bid to protect and raise the competitiveness of locally produced goods. More importantly, tariffs are an important source of government income. We can expect that the U.S.-Malaysia FTA will call for all tariffs on U.S. imported goods to be “zerorised”, if not significantly lowered over a course of time. The U.S. is the second largest source of imports for Malaysia, and a significant reduction or removal of these tariffs will have a huge impact on the revenue of the Malaysian government. The key concern is if these lessened income streams will affect the subsidy ability and the ability of the Malaysian government to implement various housing, education and health care schemes among others in its aim to achieve improved quality of life for its citizens and a reduction in the income inequality gap.

2. The creation of a level playing field and the impact on our domestic industries

The potential FTA will seek some form of “corporate globalization” whereby it expects a level playing field for its investing corporations. Whilst this is a good method of getting local companies to improve the overall performance and to reduce the permeating sense of complacency, it may threaten the growth and survival of domestic industries. Uncontrolled foreign investments may crowd out domestic investments and prevent infant industries from realizing their full potential as the international corporations are more likely to have the resources to out compete and outperform the local ones. Increasing corporate power and the eventual degree of influence on the host government is an important aspect to be considered.

3. Widening income gaps and the potential for domestic instability

Economic growth does not necessarily translate into equitable income generation. In most developing countries, unequal income distribution leads to widening income gaps between the rich and poor citizens which fuel dissent and eventually lead to domestic instability. In many third world countries, “free” trade as it is has further exacerbated poverty. Not long after its independence, Malaysia put in place several policies which aim to promote inter-racial harmony. These policies include certain protectionist measures where the main objective is to alleviate the status of the population who are economically compromised and also to uplift the domestic industries. To this end, Malaysia has achieved its purpose. Today, Malaysia is a peaceful and prosperous developing multi-racial nation. It has demonstrated economic resilience, political stability and racial harmony in recent times of unprecedented global volatility and turmoil. This just means that it has many aspects to consider in the negotiation of such an agreement which typically calls for the dismantling of protectionist policies and the creation of a level playing field for all parties involved.

4. Accessibility to cheaper generic medication

The most worrisome aspect of WTO-plus protection with regard to IPR is the access to and availability of generic medication. Generic drugs are a term used for prescription drugs identified by their chemical name. Generic versions of the medicine can be made if there is no patent, or if they do not infringe the patent, or the patent has expired, or under a compulsory license (see paragraph below). These are therapeutically equivalent drugs made available to the public at a more affordable price. This is because generic manufacturers of drugs have significantly less investments in research and development processes and also because prices are driven down by the increased level of competition.

In order to confront the challenges faced in fighting the HIV/AIDS disease, Malaysia became the first country to issue a compulsory license in 2003 following the adoption of the Doha Declaration on the Trade Related Aspects of Intellectual Property (TRIPS) agreement and Public Health by the 2001 Ministerial Conference of the WTO. Under this compulsory license, Malaysia through the “Government Use” or “Public non-commercial use” option, does not need to have prior negotiations with the patent holder before authorizing the import or manufacture of the subject matter of a patent. Thus for the purpose of ensuring access to medicines, a government or third party (contractor) authorized by the government can import or manufacture a generic version of a patented drug for ‘non-commercial use’. This means



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the use of those drugs in public hospitals or clinics.⁴ The government use authorization ended last November, and the Ministry of Health is now considering two options. The first is through the process of negotiations to lower the prices of patented products and the second is to apply for renewal of the government use authorization.

The impending U.S. Malaysia FTA will affect the viability of these options. Previous FTAs between the U.S. and other developing countries and Australia contain a chapter on IPR which contain expansion⁵ and protection clauses for patent holders. It restricts the grounds for compulsory licensing (but continues to permit such licensing as well as parallel imports to deal with public health emergencies) and prevents generic drug manufacturers from using the clinical test data of innovating firms to facilitate generic drug registration. These clauses will affect the manufacture of generic drugs and hinder the accessibility to cheaper generic medication by reducing its availability. When a medicine is patented, the manufacturer has monopolistic rights as no other manufacturers can manufacture the same medicine. In the absence of an appropriate watchdog, patent owners can potentially manipulate the prices of its pharmaceutical products.

The Challenges

Given the key concerns above, some of the areas which are expected to generate the most debate during the negotiation process are highlighted and summarized below.

Dismantling of Protectionist Policies

Protection refers to any artificial advantage given by governments to domestic industries to protect them from international competition.⁶ In the long run, protectionist policies do not benefit a country **economically**. The most common justification for protectionist policies is the protection of infant industries and domestic employment. The proponents of protectionist policies also argue that protectionism may also work in favour of improving a country's terms of trade and its balance of payments by making imports less attractive.

What is often overlooked however is the fact that these countries may reciprocate by importing less from the country in question. Protected infant industries seldom grow and are often incapable of penetrating global markets as they become reliant on the these policies at the expense of the government. In so far as job creation in concerned, protectionism may compromise employment in the more efficient export industries and ultimately affect the competitiveness of these industries. Local industries and firms which receive protection gain in the short term because they are able to increase prices, increase output and maintain or increase market share in a tightly controlled environment. Over time, many protected industries demonstrate inward looking traits and are usually risk averse.

One important point to note is that **protectionist policies are not imposed merely for economic purposes**. In many cases they are imposed to achieve political, social and or cultural goals. Usually, this would include the areas of government procurement and armaments as a nation seeks military self-sufficiency and sovereignty. Protectionism may also be necessary to preserve traditional ways of life. Rural communities or communities which are built around traditional industries may be destroyed by massive foreign competition. In the case of Malaysia, the non-economic objectives of its protectionist policies are clear; it is to ensure peace and promote racial harmony amongst its multi-ethnic community.

The impending FTA negotiations will provide Malaysia with the opportunity to objectively review the country's past performance under its present protectionist and non-protectionist policies. As previously highlighted, free trade in its true form should encourage and foster specialization of these areas, overcome inefficiency and increase outputs for trade exchange. However, in each country a political agenda exists which affects the optimum exchange process leaving any one country in a less advantageous position.

⁴ Chee Yoke Ling, "Malaysia's Experience in Increasing Access to Antiretroviral Drugs: Exercising the "government Use" Option", Third World Network, 2006. p6

⁵ At present the patent period is 20 years. An extension of this period will mean that manufacturers of generic medication will not be able to produce a generic equivalent for a much longer time than the current 20 year framework

⁶ Protective measures include tariffs which are taxes on imports; subsidies which are cash payments to producers; bounties which are similar to subsidies; quotas which are a quantitative restriction on imported goods; embargoes which are the complete prohibition of export or import of certain goods; local content schemes which is the requirement that a certain percentage of inputs or outputs must be manufactured within the country; technical standards; voluntary export restraints where a country agrees to limit its exports to another country and anti-dumping legislations.

Liberalisation of the Malaysian Services & Automotive Sectors

Development of the Malaysian financial sector is guided by the Financial Sector Masterplan which spans from 2001 till 2010. The Financial Sector Masterplan recognizes the need for an efficient, effective and stable financial sector to support and promote the growth of the local economy. In line with that, it has set out in three phases measures needed to assist the domestic financial institutions to evolve into more strategically focused, competitive, innovative and technology driven institutions. The first is to build up domestic capacity, the second is to increase the level of domestic competition and finally in 2007, to work towards global market integration. A lesson learnt from the 1997 Asian Financial Crisis is that premature financial and capital market liberalisation will increase a country's vulnerability to a global financial crisis. Malaysia thus views that the integration of its financial sector into the global context be approached cautiously and only when its domestic institutions are ready.

In the bid to promote the national car industry, the Malaysian automobile industry is highly protected from foreign competition by both tariff and non-tariff barriers. As part of the AFTA agreement and the WTO, Malaysia has gradually dismantled some of these protections. In October 2005, the government issued the new National Automotive Policy (NAP) which is expected to encourage and promote further automotive sector liberalization. At present the government continues to block open trade in the automotive sector through the approved permit (AP) system and the availability of tax rebates for national car manufacturers.⁷ It is stated in the new NAP that the current system of APS will be phased out by 31 December 2010. Domestic car manufacturers like Proton and Perodua, including two other locally incorporated joint ventures assembling imported kits, benefit from a 50 percent rebate on excise taxes.⁸ The NAP is expected to create more growth and expansion opportunities for national and non-national car manufacturers and is highly anticipated by the market.

Therein the challenge lies within the timeframe for liberalisation of these respective sectors. It is expected that through the proposed FTA, the U.S. will expect a concession in that it is granted a quicker pace of liberalisation of these sectors than set out in the respective domestic policies.

Government Procurement

In Malaysia, government procurement is protected for the benefit and growth opportunities of its local companies. Through the government procurement process greater bumiputera participation is encouraged. The current policy requires the involvement of minority and locally-owned companies when foreign companies compete for government contracts.

The U.S. is seeking access to Malaysian government procurement and will offer to Malaysian firms similar U.S. government procurement opportunities in return. The U.S. hopes that the FTA will create a level playing field for all prospective bidders in terms of government procurement within an environment of greater transparency. The point of contention here though is the sheer size of the contender. The market capitalization of some of these large American transnational companies is larger than the GDP of many developing countries! There is concern that this will not create a level playing field. Instead it may tip the scales in favour of these companies who have an advantage over the local indigenous firms in terms of technology and economies of scale.

The Positive List and the Negative List Approach

The Positive / Negative List Approach refers to the method used by negotiating countries to list the service industries its wishes to open or restrict access to its potential trade partner.⁹ A "negative list" approach means that a country defines and lists the service sectors that are closed to foreign participation while all other sectors which are not listed are open. A "positive list" approach means that a country defines and lists those service sectors that will be open to foreign participation while all other sectors which are not listed are closed.



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⁷ USTR's 2006 National Trade Estimate Report on Foreign Trade Barriers: Malaysia, http://www.ustr.gov/Document_Library/Reports_Publications/2006/2006_NTE_Report/Section_Index.html

⁸ Ibid.

⁹ The "positive/negative list" will also apply to the investment chapter of the Free Trade Agreement.

Malaysia, in its agreement with Japan used the “positive list” approach adopted in the General Agreement in Trade in Services (GATS) in the WTO. Malaysia has sought the similar approach in its other FTAs with Australia and New Zealand and is expected to do the same with the imminent U.S.-Malaysia FTA negotiations. Developed countries like the U.S. however, have used a negative list approach for the services chapter and it is expected to do the same in its negotiations with Malaysia.

The rationale behind a positive list approach for a developing country is easy to see. The positive list approach presents an open-ended option for the country in question. It allows the country to open the sectors which it feels is ready. By contrast, the negative list approach is a close-ended option in that the sectors listed are final at the time of the agreement. This means that in future, Malaysia could not seek to add to the negative list new emerging services related industries which would benefit from some form of protection.



Capacity Building of Local Indigenous Firms

In so far as the prospect of greater market accessibility is concerned, the possibility of tapping into the U.S. market is exciting for Malaysian companies. However, we must realize that the issue at hand is not so much market accessibility as it is the capacity of our local companies. Before Malaysian companies are able to enjoy the vast opportunities that the U.S. market can offer, efforts must be taken to first raise the profile of the local indigenous companies.

Intellectual Property Rights (IPR)

Intellectual Property Rights (IPR) is the more controversial aspect of the FTA. Under the agreement, the U.S. is seeking higher levels of patent and copyright protection than currently afforded by the WTO. Based on the experience of other countries, the viability of Malaysia's generic drug manufacturers (including government-linked companies) is likely to be severely affected by stronger intellectual property protection of the kind found in U.S. FTAs. One-third of Australia's generic medicine manufacturers had to close down when Australia accepted data exclusivity as part of the FTA (Data exclusivity is one of the provisions in all U.S. FTAs).¹⁰ The World Health Organization found that the stronger intellectual property protection in U.S. FTAs would cause the Colombian medicine manufacturers to lose 71% of their market share by 2030 and there could be a further 43% drop in their production if the scope of what is patentable is broadened.¹¹

Malaysian generic medicine manufacturers have the capability to manufacture more than 80% of the product categories in Malaysia's National Essential Drug List. There is export potential in the Malaysian pharmaceuticals industry. For the period 1995 to 1999 the industry registered an average export growth of 10.7% in which the export value totalled RM280 million.¹² The potential of the domestic pharmaceutical industry has been recognised by the Malaysian government who has identified it as a strategic industry which should be promoted. During the 1997 Asian financial crisis, the existence of local manufacturers ensured the supply of medicines when there was a foreign exchange shortage. These generic medicine manufacturers are gradually moving into research and development and some are publicly listed companies as they recognize they cannot compete on price alone. However, these industries have indicated that this would not be an opportune time for the introduction of a TRIPS plus provision under the FTA framework. They note that it took the world's largest pharmaceutical company, Pfizer, 100 years from its inception until it developed its first new chemical entity.

By **increasing** intellectual property protection too early, Malaysia risks curbing the growth potential of the generic medicine industry, nascent software development and various other industries.

Bilateral Agreements versus Multilateral Agreements

Malaysia would be the third country in ASEAN to express interest in a trade agreement with the U.S. Singapore was the first country to sign the agreement in 2003, whilst negotiations in Thailand which have been ongoing have been temporarily halted in the face of political unrest. Like Singapore, Malaysia holds an advantage over much of its ASEAN partners because of its

¹⁰ Peter Drahos (Professor of Law at the Australian National University) at Consumers International Roundtable on TRIPS and Access to Medicine at World Trade Organization Ministerial Conference, Hong Kong, 16 December 2005.

¹¹ 'The Impact of Strengthening Intellectual Property Measures as a Consequence of Free Trade Agreement Negotiations with the United States: Application of the Model to Colombia', Pan-American Health Organization, World Health Organization Regional Office, November 2005.

¹² The Malaysian Organisation of Pharmaceutical Industries; www.mopi.org.my

stage of economic and technological development as well as in terms of political stability. Given that, Malaysia is well poised to benefit from many forms of bilateral trade deals. However, unlike Singapore, due to Malaysia's size, its relatively weaker level of technology on the world stage and the characteristics of its workforce, Malaysia stands to gain more from ASEAN than Singapore. Thus Malaysia in signing the bilateral trade agreement with the U.S., should not lose focus and its determination to rally behind ASEAN, which is a scheme that has the potential, within a decade or so, to expand into the largest market entity the world has ever known, under AFTA +3. In other words, Malaysia should not forsake the key role it plays in the outcome and success of AFTA, which is to lead its members into the full implementation and future development of the scheme. The critical point to make is that any trade arrangement that Malaysia (or any other ASEAN member nation) makes unilaterally or bilaterally, it must factor in any potential impact such an arrangement will make on the progress of the AFTA and its future. Failure to do so will hinder the progress made so far. Finally, if every single member nation of AFTA were to sign an independent bilateral FTA with a major trading nation, the viability of the AFTA becomes questionable.

Finding the Middle Ground

The point of any bilateral trade agreement is to enhance the existing trade and regulatory terms between the partner countries. In this sense, Malaysia must note that the U.S. is expecting more than the current World Trade Organization standards and that it would like to benefit from certain concessions with regards to some of Malaysia's key protected markets such as government procurement, the financial services and automotive sectors which respectively are currently guided by domestic policies such as the Industrial MasterPlan, the Financial Sector Masterplan and the New Automotive Policy (NAP).

Then again, through "phase in" periods and other flexibility measures, FTAs do permit the protection of domestic industries which are in their infancy or those which are more politically sensitive. The question is if Malaysia and the U.S. cannot concur on the concessions sought after and Malaysia chooses to protect the financial, telecommunications, agriculture and automotive industry under the existing policies, would the U.S. still find the prospective FTA attractive?

Thus, both countries must find a middle ground to emerge with a fair set of rules for trade and ultimately the creation of a win-win situation for both parties.

Conclusion

The FTA is not a magic wand. What it essentially does is that it levels the playing field for all of the United States trade partners. It provides certain advantages to U.S. economic partners against countries who do not have an FTA. However, in order to realize the full potential in terms of trade, Malaysia still has to address the evergreen issues of cost competitiveness, innovation and creativity, and labour productivity as it competes with the other trade partners of the U.S. In so far as attracting new investments are concerned, Malaysia would benefit from the same amount of publicity and awareness as all these other partner countries. Again, Malaysia needs to compete on a micro level. The success of Malaysia in this regard remains with what the country is prepared to undertake and overcome in terms of internal challenges. It will not be determined by the inking of a free trade agreement alone.

The key concern with regard to the negotiation process is the unequal bargaining power between both parties. Malaysia as a developing country has much more to lose than the U.S., a global economic powerhouse, in terms of the economic and social impact of the concessions and tariff eliminations under the FTA. At the same time, Malaysia has more to gain from access to the much larger U.S. market and through the potential to increase foreign investment flows. Although it is arguable that with any agreement, one needs to "give some" in order to "win some", Malaysia must examine closely the clauses involved in order for it to "win some". In the past few years, the U.S. has concluded bilateral trade agreements with a host of other countries which include Singapore, Australia, Bahrain, Morocco, Chile, and the Central American States amongst others. The most interesting point is that these agreements do not differ very much from country to country. The clauses and expectations of each country are similar; and this brings us back to the earlier point of trade partner countries having to compete against each other in order to access the American markets and investment flows.



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Malaysia has established a track record as a strong independent country capable of making well-informed decisions without bowing to pressure. It has earned itself a reputation whether formally or informally as the leader of developing nations in the world, and has demonstrated the potential to lead most moderate Muslim nations. It is thus not difficult to see and understand why a trade agreement with Malaysia would be constructive for the U.S.

In the final analysis, major concerns which affect the credibility of free trade as it is today are politics and self-interest. In this regard, Malaysians should have faith in the elected government to put the needs of its people, both social and economic, before any political agenda in the negotiation process. Malaysia is not under any political pressure to conform nor to accept the terms of this impending agreement if it is not seen to be mutually beneficial to both parties concerned. The Ministry of International Trade and Industry (MITI) has promised that relevant business and industry associations, professional bodies, chambers of commerce, individual companies and other interested parties will be consulted for feedback, suggestions and views.

At the same time, Malaysia should review the impact its existing protectionist policies on the economy. In admitting to the complacency and underperformance of many large local companies most of which operate within the highly protected industries, Malaysia has in the course of the past few years, encouraged privatization and forced the implementation of Key Performance Indicators (KPIs) in the bid to foster a greater sense of competitiveness and higher productivity levels. At best, the outcome of these efforts remains uninteresting, with slight and minimal changes. To a certain extent, the potential competition from the entry of large American companies in the market may be what is needed to spur a shake-up of these government linked companies and non-government linked companies, irrespective of ethnicity which have become content in a secure and comfortable environment.

One very important reason behind the Malaysian government's decision to enter into these negotiations with the U.S. is the government's awareness of increasing global and regional competition and its effects on Malaysia's competitiveness on the whole. Provided that Malaysia is able to overcome its internal challenges, this FTA with the U.S. may be a means to advance its position against countries such as China and India. As such, successful negotiation of a comprehensive agreement which does not sideline community interests and suppress sovereignty of the nation will result in significant economic and business opportunities in the coming years. **§ Poh Heem Heem**

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... FTA with the U.S. may be a means to advance its position against countries such as China and India.

INTERNATIONAL HEADLINES

Korean Trade Surplus Shrinks

02 May 2006, Asian Wall Street Journal

South Korea's trade surplus had shrunk in April in comparison with the same period last year. This is due to escalating oil prices but the high crude oil prices have not fanned inflationary fears. The Korean Government is expecting the trade surplus this year to fall short of its original \$23 billion forecast because of the high oil price. Exports, driven by higher sales of petroleum products, auto parts, general machinery, ships and vessels, rose by 12.7% y-o-y in April to \$25.77 billion while imports hit \$24.23 billion, a 14% growth y-o-y, bringing the trade surplus to \$1.55 billion. Imports were up due to a rise in purchases of raw materials which included crude oil and consumer goods.

IMF Predicts Asian Growth Of 7% in 2006

03 May 2006, Asian Wall Street Journal

The International Monetary Fund has forecasted 7% growth for the Asian-Pacific region for 2006. The well-established economic expansion in Japan and Australia, and solid growth in most of emerging Asia will set the pace for the economic expansion of the region but nevertheless, high oil prices, tightening global financial conditions, global current account imbalances and potential outbreak of avian flu may slow down the growth momentum. The IMF said that 3 key challenges for Asian macroeconomic policy makers include dealing with inflationary pressures, strengthening fiscal positions and invigorating domestic demand. The IMF is expecting growth in industrial Asia (Japan, Australia and New Zealand) to hit 2.8% this year while emerging Asia (China and India) is expected to grow at 8% this year, with China expected to register GDP growth of 9.5% and India 7.3%. Growth forecast for newly industrialized economies (Hong Kong, South Korea, Singapore and Taiwan) is 5.2% while Southeast Asia (Indonesia, Thailand, the Philippines and Malaysia) is expected to expand 5.1% this year, down from its 5.2% growth in 2005.

China's Rapid Growth to Continue

10 May 2006, Asian Wall Street Journal

The State Information Center, a state-run think tank in China has forecasted China's economy to achieve growth rates of 9.8% and 10% y-o-y in the second and third quarter of this year respectively. Albeit being a slightly lower growth compare to the 10.2% increase in GDP in the first quarter, the growth levels are still relatively much faster than the targeted 8% annual growth set by the Chinese leaders early this year. China's trade surplus is also expected to grow from \$23.3 billion in the first quarter to \$29.1 billion in second quarter and rise to \$32.8 billion in the third quarter of the year. The consumer price index is also expected to rise, namely by 1.5% in the second quarter, 1.7% in the third and 1.5% for the overall year.

U.S. Trade Deficit Improves For Second Straight Month

13 May 2006, The Star

The U.S. trade deficit has improved from \$65.6 billion in February to \$62 billion in March, making it the second month in running that the deficit has recorded a decline. The narrowing gap, which is the smallest deficit in seven months, is supported by high export activities and a huge drop in the foreign oil bill. U.S. exports of goods and services hit a record \$114.7 billion and this increase was attributed to stronger overseas growth, which has boosted demand for American exports, and a weaker dollar in comparison to other currencies, which makes U.S. goods cheaper and more competitive in foreign markets. Big export gains were recorded for electric generators, industrial machinery, computers and farm products including corn and soybeans while imports of foreign cars and petroleum dropped in March. The narrowing deficit offers hope that the gap may finally be improving after 4 years of record high deficits although some private economists are expecting the deficit numbers to worsen again in the coming months.



Indonesian GDP Growth Loses Steam

15 May 2006, International Herald Tribune

Higher borrowing costs and fuel prices continued to dampen growth in Indonesia as the country's GDP grew only 4.6 percent y-o-y in the first quarter of 2006, the slowest pace in almost two years. Indonesia recorded a 4.9 percent growth y-o-y in the fourth quarter of last year. Retail sales have been sliding and the government's failure to increase spending has also affected growth. However the increase in fuel prices and interest rates actually helped lift investor confidence. The Rupiah has risen 17.1 percent since August last year and the country's key stock index has risen 65 percent in U.S. dollar terms.

Singapore GDP Surges

18 May 2006, Asian Wall Street Journal



The Singapore economy recorded an impressive 10.6% y-o-y GDP growth in the first quarter of 2006. The island republic also expanded by 6.8% in the first quarter in comparison with the preceding fourth quarter of 2005. The encouraging growth has prompted the Singapore government to upgrade its growth forecast for 2006, whereby the economy is expected to expand by 5% to 7%, faster than the previous forecast of 4%-6% growth, on a robust outlook for electronics. However, there are fears that the performance of the electronics sector will be patchy. Electronics exports rose on a slower than expected rate of 6.6% whereby shipments of disk drives and personal computers fell by 35.4% and 29.1% y-o-y respectively.

Hong Kong's Economy Races To 2.4% Growth

24 May 2006, Asian Wall Street Journal

Hong Kong's GDP expanded 2.4% in seasonally adjusted terms from the preceding fourth quarter of 2005. The country's economy grew at a rapid pace of 8.2% y-o-y in the first 3 months of 2006, beating the earlier official forecasts and market expectations. The expansion, which was much higher than the revised 7.5% y-o-y growth recorded in the fourth quarter of 2005, was given a boost by robust exports, and higher spending by consumers and companies. The expansion shows a solid growth momentum and signals that the economy is in the pink of health.

Japan's Trade Surplus with U.S. Surges 26.9%

28 May 2006, Asian Wall Street Journal

Japan's trade surplus with the U.S. reached ¥803.2 billion in April, a 26.9% hike from a year earlier and the highest level achieved in 20 years. Exports of automobiles and motorcycles to the U.S. rose 26.3% and 31.5% respectively while shipments of electronic parts have also increased by 22.7%. Nevertheless, the country's overall trade surplus had suffered a 31.8% contraction in April in comparison to the same period last year due to higher global oil prices and solid demand for foreign-made goods.