CHAPTER 5

5.1 CONCLUSION

This paper has highlighted the implications of AFTA on trade and investment in Malaysia. The ASEAN leaders agreed to establish the AFTA within 15 years, 12 years ago. Several factors has led to this decision, such as the conclusion of the Uruguay Round negotiations in 1993, the emergence of new competitors for FDIs, particularly China, India and Vietnam, and the rising trend towards globalisation and the forces of regionalism. AFTA's primary objective was to make ASEAN a production base, which will facilitate the trade and investment growth in the region. The CEPT scheme is the main mechanism used to lower intra-regional tariffs to 0-5 percent within a specified period of time for each of the ASEAN countries. Malaysia was anticipated to take on the lead and benefit the most from AFTA. Although, originally scheduled to be realised by 2008,the target for a free trade area in ASEAN has continuously moved forward since the inception of AFTA. With the exceptions of a few items, AFTA was fully implemented in January 2003.

Within a decade since AFTA was established, Malaysia has gained to experience a positive growth in terms of its intra-ASEAN trade. First of all, the proportion of Malaysia's intra-ASEAN trade to total trade had increased from US$13, 466 million in 1989 to US$37, 742 million in 1994. AFTA has contributed to the expansion of Malaysia's trade, both within and outside the region. Over the last ten years, intra-ASEAN trade grew b 93.6 percent from US$82.4 billion to US$159.5 billion between 1993 and 2002.ASEAN, as a group, is Malaysia's largest export destination. Exports to ASEAN went up by 2.3 times to RM 99 billion in 2003 from RM43 billion in 1994. In mid 2003, Malaysia was the second largest contributor to intra-ASEAN trade, after Singapore, accounting for 24.7 percent of the total intra-ASEAN trade.

AFTA strengthened Malaysia's participation in external trade with its ASEAN counterparts, providing further impetus for regional specializations. Therefore, Malaysia is certainly in the position to have accepted the challenges and to lead ASEAN into closer cooperation in AFTA. The upward trend in exports and imports in Malaysian trade with ASEAN indicates that there has been a positive trade-creation effect. Malaysia's trade with ASEAN increased from RM48 billion in 1991 to RM160.3 billion in 2002. It ranked next to Singapore in terms of its share in the intra-ASEAN trade. This is not surprising as even before the inception AFTA, the increasing trend was similar.

It is envisaged that AFTA will further boost Malaysia's share in the intra-ASEAN trade. Malaysian firms must stay ahead with the competition arising from this. They should enhance their ICT skills, set international standards in the marketing strategies, maintain efficiency and productivity by managing cost and quality of products, undertaking R&D and by establishing partnerships or strategic alliances. In addition, the Malaysian government should consider implementing an Integrated Sourcing Initiative, whereby, Malaysian companies that source components from the region, will treat these components as being of Malaysian origin. This would encourage the incoming of more FDIs and also to capture the comparative advantages of different locations in ASEAN.

The rapidly expanding regional market under AFTA, coupled with the reduction in multilateral trade barriers, is paving way for FDI opportunities in Malaysia. In particular, AFTA appears to promote further ' efficiency-seeking' investments, which takes advantage of comparative advantage in the country. The large infusion of FDI into the country has caused structural changes in the industrial base. Unlike in the past, the current influx of FDI is in the manufacturing and services sectors. Indeed, a substantial portion of FDI occurs within the industries that are subject to tariff cuts under the CEPT mechanism, namely the electrical and electronic products, transport equipment, metal, cement, chemical, paper and plastics products.

However, some cautions should be borne in mind. There are potential dangers in the shift of investment from industrial countries to ASEAN, in particularly Malaysia, as it depends largely on FDI flows. They may pose negative effects on the productivity growth and the BOP, owing to the high import content of the productions of foreign controlled companies and repatriation of profits, interests and dividends as well as equity capital and loans.

With regards to this, the government should adopt holistic approaches to lower cost of doing business, while encouraging efficiency and technological enhancement. Strategic alliances with foreign investors in key economic sectors are another possible way. At the same time, the government should recognise and forge closer links between the SMEs in the country and the large foreign owned companies.

At present, the pegging exchange rate regime has provided stability for the export-oriented business community, to engage in trade without much worry about the ringgit fluctuation against the US dollar. The benefits of a fixed exchange rates increases while costs decreases if integration, such AFTA's openness an intra-regional perspective, is large.

However, many foresee that the current pegging is not viable for a long period of time. Although it needs a necessary adjustments in one or two years time, it would not be a business friendly move, especially with the increasing trade figures between Malaysia and ASEAN, as a whole. However, the potential for such a move in the near future is still unclear.

If at all, the government decides to shift to a floating exchange rate system again, it has to manage sound macroeconomic disciplines, in order to minimise high nominal and real exchange rate variability that decrease gains. Managing a low inflation level in the country can do this. Given that Malaysia is highly trade-oriented, it is imperative that the export-oriented manufacturers place emphasis on other factors such as the cost, quality and product improvement rather than relying on the exchange rates for trade enhancement.

One development that needs careful monitoring is the labour movement within ASEAN. Over the long term, the other ASEAN nations' prosperity is the only practical answer to the problem of illegal immigrants. The Indonesia and Myanmar immigration is likely to increase in the short run. The overriding pressure to emigrate will come from the rural displacement in Indonesia and Myanmar due to land reforms and increased demands for construction and manufacturing workers in Malaysia. ASEAN should consider creating an area of free labour movement to complement the free trade and investment agreement. This will further integrate the ASEAN economies.

However, Malaysians should reconcile by speculating that in the short run, ASEAN can increase the gross number of illegal immigrants. Perhaps in the long run, AFTA should be able to create substantial prosperity in other ASEAN countries that this number will reduce, eventually.

Having said all the above, AFTA would not be without losers or gainers. It is hoped that Malaysia would certainly be the one to benefit most among all the ASEAN countries. There is much anticipation that AFTA will have a positive effect on the Malaysian economy, as a whole. Nevertheless, there are more challenges to come in the future, as more and more liberalization efforts are taking place in the region. Let us just hope that AFTA will evolve well for Malaysia in years to come.