ECONOMIC RELATIONS BETWEEN MALAYSIA AND JAPAN
FROM THE LOOK EAST POLICY TO THE NEW MIYAZAWA INITIATIVE

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ABSTRACT

Malaysia and Japan enjoy close economic and diplomatic relations. Japan has been Malaysia’s main trade partner as well as a major provider of foreign direct investment and economic assistance. This special relation received further impetus when the “Look East Policy” was introduced in Malaysia in the beginning of the 1980s. To reinforce relations among East Asian countries Malaysian Prime Minister Dr. Mahathir bin Mohamad proposed to form the “East Asian Economic Caucus” (EAEC) and urged Japan to play a key role in the establishing of the EAEC. At the time, the Japanese Government was reluctant to assume such a role. However, when the Asian Financial Crisis hit the region in 1997, the Japanese Government was prompt to offer help to the ailing Asian economies and came up with a rescue plan of its own, a so-called “New Miyazawa Initiative”.

Key Words: Malaysia, Japan, bilateral relations

INTRODUCTION

Since Malaysia gained independence from Britain in 1957, it has been maintaining close economic and diplomatic relations with Japan. Bilateral relations between the two countries were further reinforced through the “Look East Policy” introduced by Malaysian Prime Minister Datuk Seri Dr. Mahathir bin Mohamad in the beginning of the 1980s. Dr. Mahathir maintained that advanced countries in the West were not the only role models for Malaysia. He suggested that Malaysia could also learn from a so-called “East Asian development model” that had been shaped by economic progresses and social advancements in such East Asian countries as South Korea and Japan. Since the introduction of the “Look East Policy” two decades earlier, economic and diplomatic relations as well as cultural exchange between Malaysia and Japan have flourished. Under the “Look East Policy”, the Malaysian Government began sending young Malaysians to earn university degrees or attend training in South Korea and Japan. As a result, hundreds of Malaysians earned their degrees or diplomas from Japanese educational institutions.

In the 1990s, Dr. Mahathir voiced an idea for the establishment of a new and ambitious regional arrangement, the “East Asian Economic Caucus (EAEC)” that would reinforce economic and diplomatic ties between the countries in the region. This proposal was partly a response to a trend in other regions to form economic blocks, such as the European Union (EU) or the North American Free Trade Agreement (NAFTA). Some Asian political leaders perceived that Asian countries needed to present a united front to be able to better protect their economic interests. Japan as Asia’s biggest economy was seen an obvious choice for a leader of the proposed economic caucus. However, as the Japanese Government shunned any suggestion to become more pro-active in the international political arena it declined the offer.

When the “Asian Financial Crisis” broke out in 1997 starting in Thailand and spreading over to other East Asian countries, such as Malaysia, Indonesia and South Korea, the Japanese Government was prompt to address region’s woes and came up with its own initiatives to abate the consequences of the crisis. In order to usher economic recovery, many Asian countries, with the exception of Malaysia, began to borrow vast amounts of money from the International Monetary Fund (IMF). They also had to follow stringent IMF’s crisis-management policies. To offer an alternative to IMF’s policies, the Japanese Government presented its own rescue plan for Asia economies, the so-called “New Miyazawa Initiative”. Malaysia is one of the countries that received aid under the “New Miyazawa Initiative”.

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The aim of the paper is to critically appraise some aspects of Malaysia-Japan relations, among them:
1) the “Look East Policy”, 2) proposal to set up the East Asian Economic Caucus (EAEC), and 3) the New Miyazawa Initiative. The main focus will be put on Japan’s economic assistance policy to Malaysia in the aftermath of the financial crisis of 1997. The questions to be raised are: What are the main characteristics of Malaysia-Japan relations? What are the most important issues in Malaysia-Japan bilateral relations? Have Japan’s measures in aiding Malaysia to overcome the financial crisis been successful? What are the shortcomings of Japan’s economic assistance policy to Malaysia in the aftermath of the crisis?

Trade, Investment and Economic Assistance

Malaysia and Japan maintain robust economic relations. Japan has been one of Malaysia’s major trade partners. For Japan, Malaysia is a major provider of raw materials. Until the 1980s, the list of items that Malaysia exported to Japan consisted mainly of primary commodities, such as natural rubber, tin, palm oil and timber. In the 1980s, the liquefied natural gas (LNG) became the “rising star” of Malaysian exports to Japan as the Japanese companies had been increasingly utilizing the LNG as an alternative energy source to petroleum. For the purpose to diversify its energy sources, in 1983, a Japanese sogoshosha, Mitsubishi Corporation, initiated the Malaysia LNG Project (Satu) which was a joint-venture between Mitsubishi Corporation, Petronas, Shell and the Sarawak State Government. At present, the LNG is a major Malaysian export to Japan (Mitsubishi Corporation, 2002).

Malaysia is also an important market for Japanese manufactured goods. Japanese companies successfully penetrated the Malaysian market and established a production and sales networks in the country. However, Malaysia’s share in the bilateral trade with Japan was limited to export of primary commodities. This disparity has been noticed and commented upon by a number of economists. Thus, a prominent Malaysian economist Mohamed Ariff observed, “While Japan continues to be (Malaysia’s) major trading partner, it features more prominently as a sources of imports than as a market for Malaysian exports” (Ariff, 1991, p.57). For comparison, Malaysian exports to the USA consisted mainly of manufactured goods. As Ariff points out, “The United States has always been the largest single importer of Malaysian manufactures with a growing share, while Japan has become relatively less important as a market for Malaysia’s manufactured exports” (Ariff, 1991, pp.59-60).

A Japanese economist Takeshi Aoki described trade relations between Malaysia and Japan in the 1980s as a typical example of the “vertical trade” pattern where developed countries export manufactured goods to and import raw materials from less developed countries (Aoki, 1990, 139-140). He pointed out that primary commodities accounted for more than 80 percent of Malaysia’s total export to Japan. By contrast, manufacturing goods dominated Japan’s exports to Malaysia.

Although the basic structure of bilateral trade between Malaysia and Japan remained unchanged in the 1990s, there had been positive signs indicating that it was transforming into a more “horizontal pattern”. In other words, though Malaysia continues to be the main provider of primary commodities to Japan it has started to export some manufactured goods as well. Thus, in 2000, machinery and equipment were among top three export items from Malaysia to Japan, others being the LNG and timber. The total Malaysian exports to Japan in 2000 amounted to US$12, 827 million while its import from Japan amounted to US$ 17, 332 million (Embassy of Japan in Malaysia, 2002a).

Japan has been the main provider of Foreign Direct Investment (FDI) to Malaysia. Until the end of the 1960s, Japanese multinational corporations established their production facilities in Malaysia mainly in search of “import-substitution”. When the Malaysian Government began to promote exports by establishing “Free Trade Zones (FTZs)” in the beginning of the 1970s, Japanese multinationals adopted a new strategy for their investment -- “export-promotion”. Production of Japanese factories in FTZs was designated for foreign markets, mainly the United States and Japan. The Japanese direct investments in Malaysia reached its peak in the end of the 1980s when the Malaysian Government introduced special incentives to attract foreign investors.
At present, Japanese companies, offices and factories can be found almost in every part of Malaysia, including such relatively remote states as Kelantan, Terengganu, Perlis, Sabah and Sarawak. According to a recent research by the Embassy of Japan in Malaysia, out of 1400 Japanese companies in Malaysia, approximately 850 companies are in manufacturing sector and 200 companies are in services-related business (Embassy of Japan in Malaysia, 2002b). A number of Japanese manufacturing companies, such as Sony, Hitachi and Matsushita-Panasonic, have been operating in Malaysia for more than 20 years and created various jobs and gave training opportunities to the Malaysian employees. Besides, these companies provide venue for technology transfer.

Despite many advantages that Japanese Direct Investment (JDI) brings to Malaysia there are some contentious issues as well and those should not be overlooked. Firstly, Japan-Malaysia joint ventures are not always successful as some companies are plagued by serious financial losses or have problems with technology transfer. The fact that the end result does not always live up to the initial expectations was noticed by a prominent Harvard professor Ezra Vogel. According to Vogel’s analysis, “Mahathir needed Japanese business investments. He wanted to get a sense on how to work with Japan and how to secure the investments”. However, after two or three bad experiences dealing with Japanese businesses in Malaysia’s auto and steel sectors, Malaysian leadership grew a little wary of Japanese businesses (Vogel, 2000, p.50).

Secondly, there have been cases when Japanese multinationals were accused of the “export of dirty industries”, or “export of pollution”, to developing countries. One such case took place in Malaysia. In the end of the 1970s, a Japanese multinational corporation, Mitsubishi Chemical Corporation, set up a joint-venture company called “Asian Rare Earth (ARE)” in Bukit Merah in Perak state. ARE was engaged in extracting yttrium (a rare earth) from monazite which is a by-product of tin. The problem surfaced in the middle of the 1980s, when residents of Bukit Merah complained that ARE was dumping radioactive waste near its factory thus jeopardizing health of local residents. In 1985, the dispute was brought to court. The Ipoh High Court’s verdict was in favour of the Bukit Merah residents and ARE was asked to cease operation. Dissatisfied with the decision ARE appealed to the Supreme Court in the same year. In December 1993, the Supreme Court delivered a judgment in favour of ARE and the company was allowed to continue its operation (Lo and Furuoka, 2002, pp.280-281). The main focus during the Supreme Court trial was a weak causal relations between ARE’s operation and health condition of the Bukit Merah’s residents. The court considered that no undisputable evidence was produced to prove the causal relation between the two (Nishinippon Shimbun, December 12, 2000). At the same time, a campaign urging ARE to close its factory in Bukit Merah was mounting in Japan where “a collective group of Japanese unions and non-governmental organizations calling themselves the Japan, Asia, Africa and Latin America Solidarity Committee with over 4 million members started a signature campaign to pressure Mitsubishi to close ARE unconditionally. ARE was forced to close its operation in Bukit Merah in part due to mounting public pressure in Japan” (SAM, 2002). In January 1994, ARE finally ceased its operation. However, no formal compensation had been paid to the residents of Bukit Merah.

Let’s move to the subject of Japan’s economic assistance to Malaysia. Japan’s economic assistance program to Asian countries began in 1954 under the Colombo Plan. Japan gave economic assistance to Asian countries and received engineers and technicians for professional training. As a result, more than eight thousand Malaysians received professional training in Japan. Besides receiving trainees, since 1967, the Japanese government has been providing grant assistance to Malaysia. Grant assistance is a type of aid with no obligations of repayment. The first grant aid to Malaysia was given as a post-war reparation payment. In his memoirs, the then Japan’s envoy to Malaysia Mr. Kai, describes negotiation process for the war reparation payment between Japanese Prime Minister Sato and his Malaysian counterpart Tuanku Abdul Rahman. The negotiations were not smooth as many sensitive issues had to be discussed. However, trust and friendship between the two countries helped to overcome obstacles and a mutually satisfying agreement was reached.

As for a more recent past, from 1995 to 2000, the Japanese Government gave a total of US$1,791 million as economic assistance to Malaysia. Economic assistance can be divided into three parts. The
first part is “grant”. Grant is a more favourable type of aid to a recipient country as there is no obligation of repayment. The second type is “loan”. Loan is given on somewhat less favourable to a recipient terms as it must be reimbursed though at a lower interest rate than commercial loans. The third type of economic assistance is “technical co-operation”. Under technical co-operation, Japan dispatches specialists, i.e. engineers, teachers, etc. to developing countries and receives trainees from them.

Let us briefly review each of the three above-mentioned types of Japan’s economic assistance to Malaysia. To begin with, from 1995 to 2002, US$78 million was given to Malaysia as a bilateral grant. Among the recipients of the grant are three national universities -- UM, UKM, UNIMAS – which received audio-visual equipment. However, grant’s share in the total amount of Japan’s economic assistance to Malaysia is only 4 percent (JICA, 2002).

Regarding bilateral loans, the Japanese government provided those for large-scale infrastructure projects. From 1995 to 2000, Malaysia received from Japan bilateral loans amounting to US$627 million. Among better-known recipients of the funds are the Sabah-Sarawak Gas Pipeline project, the Port Dickson’s Power Plant project and the Temenggor Dam. The share of loans in total amount of Japan’s economic assistance to Malaysia is 35 percent (JICA, 2002).

As for technical cooperation, from 1984 to 1999, 2,389 Malaysians received training in Japan. From 1992 to 1999, Japan dispatched 2,038 specialists and 1,081 volunteers to Malaysia. Within that period, total US$1,085 million was allocated for technical cooperation to Malaysia. Technical cooperation’s share in the total amount of Japan’s economic assistance to Malaysia was 61 percent making it the dominant type of economic assistance (JICA, 2002).

The “Look East” Policy

The “Look East” policy was introduced in Malaysia in the beginning of the 1980s by Malaysian Prime Minister Mahathir Mohamad. Dr. Mahathir believed that South Korea and Japan, two East Asian countries that achieved rapid economic growth after WWII could provide a good alternative development strategy for other East Asian countries, including Malaysia, and encouraged Malaysians to learn from the “East” rather than the “West”. Especially, virtues of the Oriental society, as well as its working ethics and management style were to be promoted. To dispel any misunderstanding or misinterpretation of the new policy, Dr. Mahathir stressed, “Looking East … does not mean buying all goods from or granting all contracts to companies of the East, unless their offer is best” (Mahathir, 1988, p.1).

Under the “Look East” policy, more than eight hundred young Malaysians received their education in Japan. Albeit there have been some criticisms regarding further achievements of those graduates. Thus, the then Malaysian Entrepreneur Development Minister, Datuk Mustapa Mohamed, observed, “Only 12 out of 1200 Malaysian students sent for training to Japan under the Government’s ‘Look East’ Policy have become successful businessmen” (New Straits Times, May 5, 1997).

In Japan, the “Look East” policy received a very positive appraisal. Japanese Ambassador in Malaysia Issei Nomura commented that on the whole the “Look East” policy produced impressive results. As Nomura maintained, “The concept of the programme should be understood in the light of nation building of Malaysia. Discipline, courtesy, teamwork and corporate philosophy... All these characteristics of Japanese society were regarded as being instrumental in the nation building of Malaysia” (New Straits Times, May 19, 1997).

Indeed, until the burst of its bubble economy, Japan was a commendable “role model” for aspiring Asian economies. In the 1990s, however, Japanese development model was subjected to harsh criticism. Robert Zielinski in the article “Role Model from Hell” warned that Malaysia was headed for economic disaster because it had chosen to emulate Japan. Zielinski maintained that Malaysia adopted not only the “best of Japan”, but also more negative sides of Japan’s reality. As he put it, “(Malaysia)
imitated not only the frugal, hardworking Japan of the 1960s and ‘70s, but also the Japan of the bubble era” (Zielinski, 1998, p.29).

The East Asian Economic Caucus (EAEC)

In the beginning of the 1990s, Malaysian Prime Minister Mahathir Mohamad put forward an initiative to set up the East Asian Economic Caucus (EAEC) that would exclude from its membership “white countries”, such as the US, Canada, Australia and New Zealand. The logic was that Asia must protect its own interests without interference from the West. As Dr Mahathir asserted, “As the new world order takes shape, we in Asia must look East to find our future… The East Asian Economic Caucus, which I have proposed, is one way for Asia to look after its own interests” (New Perspective Quarterly, Winter, 1992).

Japan was encouraged to assume leadership of the EAEC. The Japanese Government, however, was most reluctant to take up this role as it assigned top priority to Japan’s relations with the US and subscribed to the US Government’s opinion regarding Japan’s role in the region. Though Japan attached big importance to friendly relations with its East Asian neighbours, it was also keen to maintain good relations with Western countries, especially the US. These considerations may offer explanation why during his tour of Southeast Asian countries in 1993, the then Japanese Prime Minister Kiichi Miyazawa maintained that “US involvement and military presence in the Asia Pacific region were still necessary” and refrained from promising Japan’s participation in the EAEC (Onozawa, 1993, p.277).

The “New Miyazawa Initiative”

Economic meltdown in Asia started in Thailand in 1997 and spread to other countries in the region, such as Malaysia, Indonesia, the Philippines and South Korea. This phenomenon was later called the “contagion effect”. To improve their economic foundations, Thailand, Indonesia and South Korea asked for, and received, rescue packages from the International Monetary Fund (IMF). The Malaysian Government decided against borrowing money from the IMF. Instead, in order to overcome financial problems that were partially caused by the “contagion effect” of the crisis, it introduced capital control.

The IMF’s policies aimed at abating the consequences of the Asian crisis were quite severe. This raised doubts among some experts regarding the validity of the IMF’s measures. Professor Jeffrey Sachs from Harvard University criticised the IMF for making a wrong diagnosis and prescribing a wrong medicine to Asian countries. According to Sachs, the IMF’s rescue packages were suitable for those countries where the problems were caused by the public sector’s debts and government’s overspending. Asian countries’ problems, on the contrary, were caused by the private sector. The IMF’s policies, such as asking the countries to further cut public spending, tighten credit and introduce emergency bank closures were too harsh for their already weakened economies. It was also argued that the IMF’s policies pushed Asian countries into a deeper recession (The Star, December 2, 1997).

Compared to the strict IMF’s policies, economic assistance from Japan came on more favourable terms as the Japanese Government did not impose strict conditions on recipient countries. To aid the recovery of the ailing Asian economies the Japanese Government announced it would provide US$4 billion to Thailand in August 1997, US$5 billion to Indonesia in November 1997 and US$10 billion to South Korea in December 1997.

In the initial stage of the crisis, the Japanese government was helping Asian economies to overcome their economic woes in cooperation with the IMF. This means that funds from Japan were used to reinforce the IMF’s methods. However, officials in Tokyo grew increasingly critical of the IMF’s policies. When, contrary to expectations, the economic situation in Asia failed to improve and Asian countries began to slide into an even deeper recession, the Japanese government came up with its own bold initiatives. For example, it proposed to establish the Asian Monetary Fund (AMF), a regional
financial institution to provide adequate funds to the Asian countries hit by the crisis to help them to usher economic recovery. However, this initiative did not materialize because it met opposition from the US Government.

As the idea to establish the AMF had to be abandoned, the Japanese Government decided to give financial assistance to East Asian countries without creating a regional monetary fund. In October 1998, it unveiled a strategy for economic recovery, a so-called “New Miyazawa Initiative” which was drafted by Finance Minister Kiichi Miyazawa. *Far Eastern Economic Review* commented on the fact that officials in Tokyo were not happy about harsh IMF’s prescriptions and mentioned, “Miyazawa obliquely criticised the IMF-led approach to recovery based on tight monetary policies” (*Far Eastern Economic Review*, December 31, 1998/ January 7, 1999, p.12).

Under the “New Miyazawa Initiative”, by March 1999, the Japanese government was to distribute US$30 billion to Asian countries to help them to recuperate from the consequences of the crisis. At the same time, calls for a greater cooperation between countries of the region came from Japanese Prime Minister Keizo Obuchi who in his speech at the Asian Leaders Summit in Hanoi in December 1998 talked about the need to foster the spirit of self-reliance. At the Summit, Japan pledged to give foreign aid worth US$1.9 billion to Thailand and US$2 billion to Malaysia.

**Japan’s Rescue Package to Malaysia**

Japan’s rescue package to Malaysia consisted of: 1) loan assistance (total US$1 billion), 2) the Export-Import bank’s loan (US$ 0.5 billion), 3) trade and investment insurance (US$ 0.5 billion).

The loan amounting to US$1 billion was to be divided between the following programs and projects: 1) the “Look East” Policy (US$ 127 million); 2) HELP II (US$ 75 million); 3) Universiti Malaysia Sarawak (US$ 168 million); 4) Beris dam (US$ 88 million); 5) Selangor raw water transfer plant (US$ 10 million); 6) Port Dickson power plant (US$445 million); 7) SMIs development fund (US$ 147 million).

Bilateral loan of US$127 million to support the “Look East” policy was given with the aim to encourage Malaysian students to enrol in Japanese universities in 1998 and 1999. Under the HELP II (Higher Education Loan Fund) program, one part of the US$75 million loan was allocated for scholarships to 440 Malaysians taking engineering or science courses in Japan and another part of the money was to be spent on educational equipment and consultation services. A loan totalling US$168 million was given for the construction of the Universiti Malaysia Sarawak’s permanent campus. As can be seen from the above figures, one-third of the US$1 billion loan, or US$ 370 million, was to be spent in the educational sector.

The remaining part of the loan was allocated to some infrastructure projects. Among them, the Selangor raw water transfer plant (US$10 million) and the Port Dickson power plant (US$445 million). Taking into consideration that the economic crisis inflicted a considerable damage on the Small and Medium Industries (SMIs) due to SMIs’ relatively weak financial base, US$147 million was given to the SMIs development fund (Embassy of Japan, 1999).

**Evaluation of Japan’s Rescue Package to Malaysia**

Apparently, the above-mentioned initiatives and measures by the Japanese government contributed to the strengthening of ties between Japan and Malaysia and were highly evaluated by the Malaysian government and people. Thus, when the “New Miyazawa Initiative” was launched, the then Malaysian Second Finance Minister, Datuk Mustapa Mohamed, commented, “The package (‘New Miyazawa Initiative’) indicates Japan’s seriousness and commitment to help countries in the region overcome the financial crisis” (*New Straits Times*, October 5, 1998). Furthermore, Malaysia’s National Economic Action Council (NEAC) was highly appreciative of low interest rates on the loans provided to important projects under the rescue package (*New Straits Times*, January 20, 1999).
A lot of positive comments came from the Malaysian mass media. The fact that Japan extended assistance to its Asian neighbours while it was undergoing a severe economic recession did not go unnoticed. As a Malaysian daily put it, “Coming at a time when Japan itself is going through difficult times, the gesture is indeed munificent” (New Straits Times, October 6, 1998). Another newspaper described Japan as a good friend in time of need. The article pointed out that instead of lecturing its harassed neighbours, the occupation that the Western powers often indulged in, Tokyo was coming out with a vast amount of funds to ease financial pain felt by the rest of the region (The Star, December 28, 1998).

However, despite all positive comments it received, Japan’s rescue package was not entirely free of shortcomings. For example, a number of problems arose in the process of disbursement of funds. This prompted a Dr. Mahathir Mohamad’s comment, “Japan’s aid package is so slow-footed that financial crisis would be over before it was spent”. Observers attributed delays in the disbursement of money to cumbersome bureaucratic procedures in Japan (New Straits Times, January 18, 1999). To fend off the criticism, the Japanese government maintained that it could not “just hand out the money without having a detailed plan on how it was to be spent” (The Star, January 18, 1999).

To a certain degree, however, the above criticism was valid as the decision-making process of economic assistance in Japan is slow, complicated and fragmented. For example, any bilateral loan has to be first officially approved by several ministries and governmental agencies before the money can be disbursed. This causes unnecessary delays in the disbursement of funds as was the case with Japan’s assistance package to Malaysia when the failure to deliver funds was noticed and criticised. It is important, that the criticism is taken positively. Instead of going into the denial mode, the Japanese policymakers might want to re-appraise the decision making-process of Japan’s aid allocation and cut excessive bureaucratic red tape.

**CONCLUSION**

Malaysia and Japan enjoy close and friendly relations. Introduction of the “Look East” policy in the beginning of the 1980s, gave new impetus to economic, diplomatic and cultural ties between Malaysia and Japan. However, more can be done to further enhance ties between the two countries. One of the issues that must be addressed is economic relations between Malaysia and Japan. The “vertical” trade pattern should give way to more balanced trade relations where not only primary commodities but also more Malaysian manufactured goods is exported to Japan. Another issue to tackle is “export of pollution” so that disputes of the type as took place in Bukit Merah do not arise in the future. Taking interest of local communities into consideration may help Japanese businesses maintain good image abroad, including Malaysia.

When Asian countries were hit by the economic crisis of 1997, the Japanese government came up with its own rescue program, the so-called “New Miyazawa Initiative”, to speed up economic recovery in the region. Japan’s prompt response did not go unnoticed and was highly appreciated in Malaysia. However, there have been some problems with the distribution of funds as money was not always distributed promptly when it was needed. This highlighted some shortcoming of Japan’s aid-giving mechanism that policymakers in Tokyo may want to address to make Japan’s ODA program more efficient.

Finally, in order to be able to assist to and promote economic development in East Asia, Japan must first solve its own economic woes. East Asia relies on Japan for more than 20 percent of its trade and investment, and 60 percent of foreign aid. Should Japan succeed in revitalizing its own economy, the whole East Asian region will benefit.
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