CHAPTER 3. POLICIES FOR THE DEVELOPMENT OF THE AUTOMOTIVE PARTS INDUSTRY IN MALAYSIA

1. DEVELOPMENT POLICY FRAMEWORK

1.1 MAJOR POLICIES FOR THE DEVELOPMENT OF SMIS

1.1.1. Current Situation of SMIs in Malaysia

(1) Definition of SMIs

There is no single definition of small and medium size industries(SMIs) in Malaysia. Usually Government agencies use the terminology "SMI" based on the following criteria:

- Small Scale Industries (SSI) are those having shareholders' funds not exceeding RM500,000
- Medium Scale Industries (MSI) are those having shareholders' funds between RM500,001 and RM2,500,000.

There are various definitions for SMIs using the above criteria. In Industrial Surveys by the Department of Statistics, SMIs are defined by employment size, such that SSIs are companies employing 5 to 49 workers, and MSIs employ 50 to 99 workers. Research institutes, e.g. ISIS and ADB, adopt the definition of SMIs of employment size as employing 5 to 199 workers. In other countries, SMIs are treated as those with employment of less than 200 in Thailand, 100 in Indonesia, and 300 in Japan.

In the Annual Report of MITI in 1994, MITI defined SMIs for the purpose of the SMI census and Survey 1993/94 as "all industries with a paid-up capital or shareholders' funds of less than RM2.5 million and employing 5 to 74 full time workers." This definition uses the criteria of both shareholders' funds and employment size. These companies are exempted from manufacturing licenses under the Industrial Coordination Act, 1975.

In the case of Japan, SMIs are defined as follows, except in the case of research/study which uses

its own definition along with the purpose of analysis by researchers and of special sub-sectors ordered by the Government;

a. SMIs of the manufacturing sector are defined as companies with a paid-up capital of less than 100 million yen or employing less than 300 workers.
b. SSIs of the manufacturing sector are those employing less than 20 workers.

In the Japanese definition, SMIs are defined as companies satisfying either the paid-up-criterion or employment-criterion. The reason that using "SMIs of manufacturing subsector" in the above criteria is that the criteria are different among the sectors, i.e. SMIs of wholesalers are companies with paid-up capital of less than 30 mil. or employing less than 100 workers, SMIs of retailers and other service sectors are companies with paid-up capital of less than 10 mil. or employing less than 50 workers. These criteria are defined by the Basic Law for SMIs.

In Malaysia, on the other hand, several definitions are used not only by the researchers and/or research institutions but by government agencies. It is said the Government is now preparing a "comprehensive" SMIs' law. In this law, the definition of SMIs will be uniform. In this report, SMIs are defined as those companies having shareholders' funds not exceeding RM2.5 million. Because of the limitation of statistics, however, quantitative analysis will not always be based on the above definition.

(2) Current Situation of SMIs in Malaysia

SMIs in Malaysia comprise around 93% of total establishments in the manufacturing sector, and employ 40% of total manufacturing workers. SMIs, also, produce 20% of total value added in the manufacturing sector. (The sources of these figures are the Industrial Surveys carried out by Department of Statistics in 1988. As mentioned above, MITI are now carrying out the SMI census. Quantitative analysis of the current situation regarding SMIs awaits the results of this census.)

In Malaysia, SMI policy focussed on the nurture of SSIs after the late '70s. The SMI target policy

changed from SSIs to MSIs in recent years. Also, the basic policy for industrialisation has been emphasised to introduce foreign companies. The proportion of MSIs is relatively weak compared with foreign companies and SSIs. Many of SSIs are companies are located in residential and agricultural areas. Many of such small factory operations in these are located in ungazetted areas. Relocation of these companies to the industrial estates is an urgent issue in consideration of the following points: improvement of operating conditions and habitation circumstances, pollution control, and so forth. In order to solve these issues, both Federal and local governments have instituted counter-measures, e.g., preparation of industrial estates for SMIs. The effects of these measures, however, are not tremendous, because of the financial problems of SSIs.

In the Industrial Survey in Japan, 413,844 factories or 96.2% of total establishments, 6.154 million workers or 54.2% of total employment, and 47.305 billion or 37.7% of total value added are comprised by firms employing less than 100 workers in 1991. As statistics of the above are based on factories, the figures are not equal to SMIs. (There are cases where one company owns two or more factories.) In Japan, the percentage shares of the total manufacturing subsector in employees and value added are higher compared to those of Malaysia. Differentiations between LSIs and SMIs in Japan are very wide in terms of productivity, wages, and various welfare considerations for employees.

1.1.2. Major Problems in SMIs

SMIs in Malaysia face various problems, e.g. low level of productivity and capital intensity, shortage of financing, weak management basis, lack of technologies and difficulty of receiving technical support, weakness of management resources such as marketing knowhow, and so on. To compensate for these difficulties, the Government has introduced various measures such as managers' training, technical support, financial support, etc. Because of the lack of a integrated framework of policies and large numbers of implementation authorities to support, these supports are not always effective. The issue is to make access to existing schemes easier if SMIs really need the above supporting programmes. Major problems in SMIs are classified into the following categories.

- Management

  SMIs, especially SSIs are typically family or sole proprietorship business with one-man operations involving little managerial specialisation.

- Finance

  Levels of capitalisation are very low. Raising funds is also difficult.

- Manpower

  Low level of value added results in low wages, therefore, it is difficult to keep or secure employees.

- Technology

  Levels of technology are low. Factories are not modernised.

- Marketing

  There is a shortage of marketing know-how.

- R&D

  Around 11% of total R&D expenditure in the whole country is accounted for by the manufacturing sector (in 1988 by FMM estimation). The percentage share of the private sector of R&D expenditure is around 10%, the rest is accounted for by the public sector. This suggests R&D activities by SMIs are very low.

- Others

  Large numbers of SSIs are located and operate outside the zone approved for manufacture. Operating conditions of those areas are very bad, therefore relocation to industrial estates is an urgent issue.

1.1.3. SMIs Development Policy

(1) Introduction

In the initial stage of development (the period of the First Malaysian Plan), the Government emphasis for SMI development was placed on SSIs rather than MSIs. The strategy of SMIs, particularly SSI development, was domestic market-oriented, and for the Government to provide public support services. In line with the change of Malaysian economic structure, SMIs Development Policy has become export-oriented.

SMIs are placed as one of the highest priority industries for promoting continuous national economic growth. Direct government assistance for SMIs, however, has gradually been replaced by such private sector elements as large scale industries, banks, and financial institutions. The government will focus on infrastructure and support services (Annual Report of MITI 1994, and National Budget in 1993).

(2) Agencies involved in SMI development

There are 13 Ministries and 30 government agencies concerned with promoting SMI development. The functions and areas of responsibilities of these agencies overlap. In order to promote a more integrated approach to SMI development, the leading agency concept has already been set up setting MITI, MOSTE, MOF, and ICU leading agencies. This suggests that a single authority, similar to Japan's SME Agency or Japan's SME Corporation, is expected to be set up to ensure more effective implementation of the SMI development programme.

(3) Existing SMI Development Programme

Major existing SMI development programme factors are the following.

- Vendor Development Programme
  The main objective of this programme is to create a market for SMIs used by large-scale industries.
- Subcontract Exchange Scheme
  The main objective of this scheme is to provide a computer-based matchmaking mechanism between potential SMI vendors and LSIs.
- Umbrella Concept for Marketing
  The main objective of this concept is to assist Bumiputera vendors to gain initial market access through government procurement, and to make inroads into the open market.
- SMI Expos and Industrial Fairs
  The main objectives of these are to assist SMI manufacturers in other domestic and international markets.
- Industrial Technical Assistance Fund (ITAF)
  The objectives of this scheme are to enhance the development of SMIs into a progressive

and modern sector, capable of supporting LSIs. The scheme provides matching grants for SMIs, and is composed of four schemes with initial funding of RM50 million in July, 1990.

Table 3-1-1 Scheme and Implementation Organisations of ITAF

SCHEME	Organisation	Limit
ITAF1 Consultancy Service Scheme	BPMB	RM40,000
ITAF2 Product Development & Design Scheme	SIRIM	RM250,000
ITAF3 Quality & Productivity Improvement Scheme	SIRIM	RM250,000
ITAF4 Market Development Scheme	MATRADE	RM40,000

Source: MITI

Table 3-1-2 Performance of ITAF Schemes

Scheme	Applications Received	Applications Approved	Amount (RM Million)
ITAF1	90	66	0.83
ITAF2	204	92	5.75
ITAF3	172	59	3.34
ITAF4	127	84	1.03
Total	593	301	10.95
Year	Applications Received	Applications Approved	Amount (RM Million)
1991	229	116	4.95
1992	84	48	2.25
1993	196	137	3.76

Source: MITI

- Soft Loan Scheme

The major objectives of this scheme are to promote modernisation and automation among SMI manufacturers. Major implementation organisations and their schemes are as shown in the following Table.

Table 3-1-3 Soft Loan Scheme and Implementation Organisations

- Bank Pembangunan Malaysia Bd. (BPMB) Industrial Adjustment Fund (IAF) SMI Promotion Programme (SMIPP) New Entrepreneurs Fund (Bumiputera only) Nursery Factory Scheme (Bumiputera only) Soft Loan Scheme for SMIs Involved in the Food & Furniture Sector (Bumiputera only)
- Malaysian Industrial Development Finance Bd. (MIDF) New Entrepreneurs Fund (Bumiputera only) Industrial Adjustment Fund (IAF) SMI Promotion Programme/OECF Loan Scheme Modernisation and Automation of SMI
- MARA Scheme 1 Small/New Business Scheme 2 Medium

Source: Each Organisation

- Infrastructure Development Programme

  The main objective of this scheme is to provide affordable sites, especially standard factories, for SMI manufacturers.

- Human Resource Development Programme

  The objective of this programme is to provide human resource training for SMI in the area of management and skills upgrading. Major implementation organisations and their programmes are as follows:

Table 3-1-4 Major Human Resource Development Organisations and Programmes

- National Productivity Corporation (NPC) Quality Management Programme Productivity Management Programme Human Resource Management Programme Production Management Programme Sales and Marketing Programme SMIs and Entrepreneurship Programme
- Standard Industrial and Research Institution Malaysia (SIRIM) Quality Programme (ISO9000, ISO/IEC Guide 25) Welding Programme Ceramic Programme Plastic Programme Computer Programme Patent Information Programme

Source: Each Organisation

- Information Dissemination

  The purpose of this system is to provide a one-stop referral center for SMIs to obtain information about SMI-related development programmes and schemes. This system is operated by The Malaysian Industrial Technology Information Center (MITIC).

(4) Major Issues of SMI Development Policy

It is considered that schemes and programmes of assistance for SMIs are well prepared for the current issues of SMIs. However, the SMIs have not made use of those schemes, because of their relatively recent institution. The issue then is how to enforce their usage by SMIs. The responses to the questionnaire surveys conducted in this study indicated that evaluations of the SMI supporting programmes prepared by the Government are not high. Of course, the validity of these comments on the matter of programme efficiency is very limited because the samples are confined only to automotive parts industries, and therefore the number of samples was low. The replies of "not effective", however, are not in such small numbers as to be neglected. It is necessary that the reasons the SMIs replied "not effective" to the schemes and programmes be considered. Differentiation among regions enjoying the services provided by SMI schemes is the next issue. As for ITAF, for example, Scheme 2 and 3 are implemented by SIRIM located in Shah Alam. SMIs

located in regions where accessibility to SIRIM's offices is rather difficult naturally use the above schemes less than those located nearby. Technical services provided by SIRIM also exhibit the same tendencies. This is related to the formation of the implementation organisations for SMI programmes. In the experiences of Japan, efficiencies of SMIs programmes depend on providing "elaborate" services. In order to provide such services, implementation organisations have to be located in each region, i.e., each state. In this situation, large numbers of Government Agencies concerning SMI programmes are considered obstacles to efficiency because of the complicated information flows and the employment of needless manpower in the local bodies. It is important to implement both the integration of Government Agencies related to SMI policy and the establishment of regional implementation organisations.

SMI supporting programmes, especially technical assistance implemented by Government agencies and their related agencies, have adopted inhouse training. For the SMIs, it is difficult to dispatch employees to the Agencies because of manpower limitations. Also the contents of the programmes are not always related to the daily issues in their factories. These indicate the need to introduce a system of "visiting-advisers" for SMIs.

1.2. MAJOR POLICIES FOR THE DEVELOPMENT OF AUTOMOTIVE PARTS INDUSTRY

1.2.1. Mandatory Deletion Programme

For Malaysian local industry to acquire high level of engineering and technical skills, it is necessary that local parts and components manufacturers who can manufacture quality products at internationally competitive prices be developed. In view of this, the Malaysian Government has chosen the automobile industry as one of the priority industrial subsectors, and various programmes have been implemented focussing on the development of the automotive parts and components industry.

The Mandatory Deletion Programme (MDP) was the first of such programmes introduced in 1980. Since then, a total of 30 components have been designated as mandatory localised items, and

assemblers have to delete these items from their CKD packages so that local procurement can be done.

This policy is considered to have worked effectively in the late 1980s as shown in the industrial production index of automotive parts in Table 3-1-5.

Table 3-1-5 Indices of Industrial Production for Automotive Parts Industry

Year	Index (Base Year:1985)
1985	100.0
1986	45.6
1987	110.3
1988	235.0
1989	263.7
1990	322.8
1991	404.9
1992	328.9
1993	354.3

Source: Index of International Production, Department of Statistics, Dec., 1989, Apr., 1994

On the other hand, to extend the policy further and to develop more local parts and components manufacturers, the PROTON national car project was implemented in 1983, and production was started in 1985.

To promote further localisation of components, the Government introduced a new local content programme, Local Material Content Policy (LMCP) in January, 1992, to supplement the MDP scheme. After the introduction of this new policy, no components have been added to the MDP list, leaving the original 30 items.

One of the major problems of the MDP scheme lies in the fact that the scheme requires assemblers to use local parts and components. Although this scheme has contributed to the development of

the automotive parts industry, which was infant and needed assistance, it has caused automobile assemblers to have to procure parts and components even at high cost to assemble their cars, which subsequently increases the cost of finished automobiles. At the same time, because the number of automotive parts manufacturers is limited, automobile assemblers sometimes have to use parts and components of slightly different specifications. Actually, some assemblers have modified their own in-house engineering specifications so that local procurement of parts and components is made possible.

1.2.2. New Local Content Programme

The Local Material Content Policy (LMCP) became effective on January 1, 1992. This policy was designed to expand the use of locally manufactured parts and components in the assembly of passenger and commercial vehicles in Malaysia so that a local component manufacturing industry would develop. In this programme, each of the designated automotive parts and components, which total more than 300 items, has a certain point (%) set by the Government, and the degree of the localisation of each car model is calculated by the summation of the points of all localised parts and components used for the model.

According to this policy, automobile assemblers and franchise holders are under obligation to increase the level of local content of each category of vehicle to achieve the targets set by the Government as shown below. The thirty items which are designated as MDP items jointly represent approximately 30 points localisation for passenger cars and approximately 25 points for commercial vehicles.

Table 3-1-6 New Local Content Programme

(Unit: LMCP Points)

Achievement Date	Category I Passenger Vehicles: 1,850cc or Less	Category II Passenger Vehicles: 1,851 - 2,850 cc Coomercial Vehicles: GVW 2,500 kg or Less	Category III Passenger Vehicles: 2,851 cc or More Commercial Vehicles: GVW 2,501 kg or More
Jan. 1, 1992	0	20	MDP Items
Jan. 1, 1993	40	30	MDP Items
Jan. 1, 1994	50	35	MDP Items
Jan. 1, 1995	55	40	MDP Items
Jan. 1, 1996	60	45	MDP Items

Source: MIDA

PROTON is thought to have attained close to 90 points local content, including such parts and components as body panels and assembly of engines, while non-PROTON assembled models of passenger cars have attained relatively low figures ranging from approximately 30 to 50 points mainly because of low production volume.

In order to assist non-PROTON assemblers to increase localisation of parts and components, the Brand to Brand Complementation (BBC) scheme was agreed to between several ASEAN countries including Thailand, the Philippines, and Malaysia in 1988, and put into effect in 1989. Under the BBC scheme, imported parts and components which correspond to the same value of exported parts and components within the same brand name are considered to be localised ones and localisation points are given to assemblers. In addition, import duties are lowered by 50%.

However, to date only 6 automobile companies, including Tan Chong, ASSB, and Swedish Motor, utilise the scheme. Some of the problems pertaining to the BBC, which were learned through the interview survey by the JICA Study Team, are (i) the approval of a component takes a long time after the submission of an application to the ASEAN Secretary (often more than 2 years), (ii) MDP components cannot be targets of the BBC scheme, and (iii) it is difficult to balance imported amount with exported amount.

1.2.3. Export Credit

The Government gives automobile assemblers localisation points against the export of automotive parts. Utilizing the scheme, they can increase the level of localisation through the expansion of parts export. The maximum points to be given to assemblers is 20%, calculated based on the following formula.

(Total FOB value of automotive parts exported by the company) / (Total FOB value of CKD packs imported by the company) x 100%

1.2.4. Vendor Development Programme

The implementation of LMCP has contributed to the development of the parts and components industry in Malaysia. However, most of the products are manufactured by multinational corporations (MNCs) and a handful of large-scale Malaysian industries. Taking the importance of the development of small and medium-scale industries (SMIs) into consideration, the Government put the Vendor Development Programme (VDP) into effect where large-scale companies are requested to develop SMIs as anchor companies. In 1988 the PROTON Component Scheme as the VDP was put into effect under an arrangement whereby MITI funded technical grants through PROTON.

Among several governmental programmes designed to develop the automotive parts and components industry, including schemes such as the VDP, "Support through the ITAF Scheme", "Soft Loan Scheme for Modernisation and Automation through MIDF", and "New Principal Guarantee Scheme (New PGS)", the VDP is the most widely known and has been utilised by more automotive vendors than any other scheme.

The main objective of the VDP is that the Malaysian SMIs which have potential but lack technical, financial and managerial support will be nurtured by PROTON as an anchor company so that they can become reliable manufacturers and suppliers of automotive parts used by PROTON. Under this arrangement, PROTON manages a grant for the purpose of providing technical, managerial

and consultancy services in addition to providing relevant machinery and equipment to upgrade the vendors. In line with the VDP scheme, PROTON's technical team undertakes an evaluation of potential vendors on technical, financial and managerial aspects through factory auditing.

Although the Government plans to expand the VDP scheme by increasing the number of anchor companies, the Government is gradually phasing out direct assistance as financial assistance from the banks and financial institutions becomes available.

To date, a total of 19 SMIs have utilised the VDP scheme for PROTON, in which the amount of an average grant was approximately RM700,000. The flow of funds allocation (grants) between 1988 and 1992 is as follows:

Table 3-1-7 Funds Allocation of VDP by Year

(Unit: RM Million)

1988	1989	1990	1991	1992
3	3	1	1	3

Source: Printed material distributed by PROTON, JICA Study Team, March 1994

Meanwhile, the PERODUA, the second national car project, was set up, and its first production roll out is scheduled in the third quarter of 1994. The Government has nominated PERODUA to be an anchor company under the VDP scheme following PROTON.

The VDP scheme operated jointly between PROTON and MITI has contributed to the development of vendors, but through the interview survey by the JICA Study Team, some of the complaints against the scheme were brought out as follows:

i. the amount of the grants is too small
ii. the scheme is open to Bumiputera companies only
iii. it is difficult for sub-vendors to utilise the scheme
iv. it takes a long time (3 to 5 months) to give approval after the submission of an application
v. application conditions are too strict

2. TAX STRUCTURE FOR THE AUTOMOBILE INDUSTRY

2.1. IMPORT TARIFF SYSTEM

2.1.1. Import Tariff System to CBUs

For the sake of the protection of the domestic automobile industry, especially the national car project, the importation of CBUs (Completely Built Up) is restricted as a general rule, and high import duties are imposed. Only Bumiputera quota holders are allowed to import CBUs, but the ceiling, which is a percentage ratio over domestic production, is set by the Government, and the ratio is lowered every year.

The import tariff schedule on CBUs is shown in Table 3-2-1, while the annual ceiling is shown in Table 1-2-15.

Table 3-2-1 Import Duty on CBUs

		Passenger Vehicle	Commercial Vehicle
Import Duty		Depends on Engine Capacity	35%
Actual Engine Capacity (c.c.)	Less than 1,800 c.c.	140%	
	1,800 c.c. < 2,500 c.c.	170%	
	2,500 c.c. and Above	200%	

Source: MIDA

2.1.2. Import Tariff System to CKD Parts and Components

A very low import tariff system is applied to CKD parts used for the assembly of national cars aiming at the development of the national car projects. For parts used for PROTON, the import duty was originally 0% but was later raised to 13%. This tariff is still less than one third of that to be applied to parts used for non-national cars, which is 42%. PERODUA enjoys the special privilege of zero percentage import duty on its imported parts because the company has just begun assembly. The

reduction of tariff has contributed to the development of the less-developed Malaysian automobile industry.

Meanwhile, since November, 1989, licensing for each car model was abolished, and assemblers have been allowed to introduce any car model into the market if they satisfy the localisation programme.

Table 3-2-2 Import Tariff Schedule for CKD Parts

Passenger Car			Commercial Vehicle		
Non-national Car	PROTON	PERODUA	Truck	Van	4WD Wagon
42%	13%	0%	0%	5%	5%

Note 1: Import value is calculated based on the formula "CIF + Uplift)."
Note 2: Parts imported in the BBC scheme are exempted from one half of import duty.
Source: MIDA

2.2. DOMESTIC TAX

Both excise duty and sales tax are imposed on the sales of locally assembled motor vehicles in the domestic market. Sales tax is a uniform 10%, and excise duty for passenger vehicles is calculated on a sliding scale from 25% to 65% depending on the open market value (OMV). PROTON and PERODUA, however, receive the privilege to cut 50% of the excise duty compared with non-national cars.

Table 3-2-3 Domestic Tax on Sales of Cars

		Passenger Car	Commercial Vehicle (Truck, Van, 4WD Wagon)
Sales Tax		10%	10%
Excise Duty		(Depends on OMV)	0%
OMV (M$)	Not more than 7,000	25%	
	7,001 to 10,000	30%	
	10,001 to 13,000	35%	
	13,001 to 20,000	50%	
	20,001 to 25,000	60%	
	More than 25,000	65%	

Note: PROTON and PERODUA receive the privilege to cut 50% of the excise duty compared with non-national cars.

Source:MIDA

3. POLICIES FOR PROMOTION OF FOREIGN INVESTMENT AND TECHNICAL TIEUPS

3.1. PROMOTION OF FOREIGN INVESTMENT AND TRENDS IN FOREIGN INVESTMENT

3.1.1. First Foreign Investment Boom (1974)

Malaysia's basic policy on foreign investment is founded on the Investment Incentive Act established in 1968 which in turn is an amended version of the 1958 Pioneer Industries Ordinance. There are other factors inducing investment by foreign companies in Malaysia which cannot be ignored, that is, the protective tariffs and import quota systems set up by the government in 1966 with the aim of promoting import substitution type industries. Further, the Federal Industrial Development Authority (FIDA, the predecessor of MIDA), established in 1967 with the aim of coordinating and approving investment and development of industrial regions, played a positive role in attracting foreign investment.

The second Malaysia Plan was started in 1971 under the name of the New Economic Policy (NEP). Under the NEP, measures were taken giving priority to ethnic Malayans (Bumiputera), but stress was given in the foreign investment policy to (i) labour intensive and export industries rather than import substitution type industries, (ii) higher added value of domestic materials, and (iii) promotion of investment in under-developed regions. The government introduced "Special Investment for Electronics Industry" in 1971 for the purpose of promoting the assembly of electrical and electronic equipment. At the same time, it established the Free Trade Zone Act and in 1972 set up the first FTZ in Malaysia in Bayan Lepas in Penang. Further, it introduced the system of licensed manufacturing warehouses (LMW) in 1973 for export-oriented companies located outside the FTZs to enjoy the same facilities. These steps by the government to promote investment led to a 26.8 percent increase in foreign investment, to RM127.7 million, in 1974, around the time of the first oil crisis, and set off the first investment boom (Refer to Table 3-3-1).

In May 1975, the Industrial Co-ordination Act was established and acquisition of business licenses was made obligatory for all manufacturers. In June 1976, the FIDA announced for the first time

the amount of foreign investment by country and industry (total of called-up capital and loans) giving figures for manufacturing as of the end of 1975. This covered not only the conventional pioneering companies, but other operating companies, both receiving and not receiving incentives. As of the end of 1975, first place in the balance of foreign investment was taken by textiles at RM252 million for a total share of 19.2 percent. This was followed by food and food materials at RM202.47 million (15.4%) and electrical equipment at RM173.03 million (13.2%). Transport equipment came in at RM23.08 million - just a 1.8 percent share (Refer to Table 3-3-2).

Table 3-3-1 Inflow of Direct Foreign Investment into Pioneer Industry (end of year)

(Unit: RM Million)

Country	1971	1972	1973	1974	1975	1976	1977	1978	1979
Singapore	112.8	125.6	147.3	162.8	185.0	196.5	225.8	583.2	642.2
Japan	46.7	42.4	73.0	117.7	148.6	184.1	239.6	647.4	539.9
United Kingdom	84.5	84.4	90.0	93.4	104.9	123.3	123.7	416.0	419.9
United States	60.7	88.0	62.5	81.2	106.4	162.7	190.8	281.8	193.7
Hong Kong	36.1	36.8	45.9	61.5	104.2	93.8	166.3	278.8	281.9
West Germany	-	0.5	0.6	3.8	4.8	20.7	25.4	54.0	54.5
Australia	7.7	6.7	8.4	18.4	20.0	24.8	26.6	58.8	63.2
Canada	6.0	6.1	7.3	11.0	8.4	7.8	7.8	10.2	17.7
India	-	1.8	6.6	6.2	6.6	10.3	10.3	70.2	55.3
Others	40.7	47.4	35.0	48.2	59.4	66.3	7.9	208.2	311.4
Total	395.2	439.7	476.6	604.2	748.3	890.3	1,024.2	2,608.6	2,579.7

Note: 1971-74; Western Malaysia only

Source: FIDA Annual Report, FIDA,1971-1977 & MIDA Annual Report, MIDA1978-1979

Table 3-3-2 Direct Foreign Investment by Industry
(Manufacturing, end of 1975)

Industry	Total Foreign Investment (1,000 RM) (Shares %)	Top 3 ( ): Share of Country %		
		1	2	3
Food & Beverages	202,471(15.4)	Singapore (35.2)	India (11.5)	Hong Kong (11.4)
Textiles & Textile Products	252,050(19.2)	Japan (41.4)	Hong Kong (35.7)	Singapore (9.0)
Leather Products	964(0.1)	Singapore (100.0)		
Wood & Wood Products	103,365(7.9)	Japan (45.0)	Singapore (12.3)	Hong Kong (9.0)
Paper, Printing & Publishing	7,812(0.6)	Singapore (43.0)	Japan (23.8)	Australia (10.9)
Chemical Products	101,438(7.7)	U.K (39.5)	Hong Kong (19.9)	Singapore (17.5)
Petroleum Products	111,065(8.4)	U.S.A (68.8)	U.K. (20.3)	Singapore (10.7)
Rubber Products	60,865(4.6)	U.K (43.0)	Singapore (14.9)	Norway (8.5)
Plastic Products	10,035(0.8)	Singapore (62.2)	Japan (11.8)	U.K (8.8)
Non-Metalic Mineral Products	64,853(4.9)	Singapore (47.7)	Japan (36.6)	Australia (6.6)
Basic Metal Products	56,022(4.3)	Japan (66.2)	Hong Kong (8.7)	Singapore (6.8)
Fabricated Metal Products	52,144(4.0)	Singapore (59.6)	Japan (15.6)	Australia (8.5)
Machinery	27,524(2.1)	Japan (68.5)	Nether-lands (8.9)	U.S.A (7.8)
Electrical & Electronic Products	173,031(13.2)	Japan (27.1)	U.S.A (26.1)	Hong Kong (14.3)
Transport Equipment	23,082(1.8)	West Germany (15.2)	NewZealand (13.0)	Singapore (9.4)
Scientific & Measuring Equipment	12,984(1.0)	U.S.A (31.6)	West Germany (18.8)	Japan (15.7)
Others	55,373(4.2)			
Total	1,315,081(100.0)	Japan (25.0)	Singapore (20.5)	Hong Kong (13.9)

Note: Foreign Investment = Issued Capital + Estimated Foreign Loan
Source: FIDA

3.1.2. Second Foreign Investment Boom (1978 to 1982)

In January 1978, Mahathir Mohammed, then vice prime minister and minister of international trade and industry, became chairman of the Investment Ministerial Conference and began tackling the task of improving of the investment environment. In April of that year, the administrative process from application for investment to approval was shortened and in September of that year a "One-Stop Agency" was set up in MIDA for comprehensive processing of investment-related procedures. Further, in November 1978, a large-scale investment promotion mission was sent to Japan. Malaysia became aggressive in its approach to Japan in this way. These public and private efforts to attract foreign investment led to the balance of foreign investment breaking through the RM2.6 billion mark in 1978 - increasing 2.5-fold from the previous year.

In 1980, the government established the Heavy Industries Corporation of Malaysia (HICOM) as a body for promoting heavy industry. In July of the following year, Prime Minister Mahathir proposed a "Look East Policy" of learning from the past successes of Japan and South Korea in constructing heavy machinery and chemical industries. Foreign investment was encouraged more strongly and in 1981 the total amount of foreign investment introduced (based on proposed foreign called-up capital) reached RM495.30 million - almost double the amount of the previous year. This was primarily in large scale capital intensive HICOM programs such as ferrous metals, nonferrous metals, petrochemicals, and other material industries and machinery, papermaking, and paper products. In 1982 as well, the value of foreign investment in ferrous metals, fertilizers, electronic components, cement, etc., reached RM527.6 million. Foreign investment in HICOM programs continued to be active as in the previous year. The years 1978 to 1982, including the 1979 second oil crisis, constituted the second investment boom in Malaysia.

Public corporations, in particular HICOM, were seriously affected by the economic slump in Malaysia in the early 1980s and so were not able to perform as expected. This led to an increase in the government's fiscal deficit. Therefore, the government began privatizing its public corporations, including HICOM, in 1983.

Table 3-3-3 Total Foreign Investment by Country by Industry

(Unit: RMMillion)

Industry \ Country	Singapore	Japan	United Kingdom	United States	Hong Kong	West Germany	Australia	Nether-lands	India	Bahama	Total (Including others)
End of 1983	1,189.7	971.8	646.9	271.9	359.6	115.7	102.9	49.7	62.2	41.8	4,257.9
End of 1984	1,384.5	1,067.5	760.3	394.1	384.1	126.9	97.9	48.7	72.6	41.8	4,820.9
Industry											
Foods	269.2	67.5	148.9	15.3	35.4	7.8	0.8	1.6	42.3	40.1	709.2
Beverages & Tobaccos	161.5	-	144.3	78.0	10.8	-	0.1	0.1	-	-	409.9
Textiles & Textile Products	173.6	191.9	8.9	5.3	127.6	21.9	2.0	-	5.7	-	550.7
Leather Products	2.4	-	△	-	△	-	△	-	-	-	20.2
Wood & Wood Products	43.8	55.0	5.0	8.2	13.9	1.6	5.4	5.4	-	-	173.1
Furnitures	13.6	-	-	0.5	4.2	1.1	1.3	-	-	-	21.7
Paper, Printing & Publishing	28.2	2.1	1.7	0.4	1.6	-	△	-	-	-	35.9
Chemical Products	95.7	25.1	99.9	140.9	56.1	7.5	7.8	0.6	1.3	1.5	452.4
Petroleum Products	10.4	0.1	145.5	-	17.5	-	-	18.0	-	-	191.7
Rubber Products	36.1	15.4	21.3	7.6	0.5	8.1	11.2	-	0.4	-	121.6
Plastic Products	76.4	16.0	1.4	△	1.9	0.3	-	-	0.2	-	29.9
Non-Metalic Mineral Products	147.0	158.8	69.8	1.0	4.0	2.2	31.9	-	3.0	0.2	466.0
Basic Metal Products	79.7	88.5	15.8	6.3	0.3	4.5	6.1	-	0.2	-	227.9
Fabricated Metal Products	73.6	30.0	12.9	0.8	8.8	2.3	27.3	5.0	2.9	-	193.2
Machinery	14.7	25.2	11.9	12.2	0.2	1.5	2.5	-	0.3	-	69.1
Electrical & Electronic Products	117.1	121.8	49.7	43.3	35.0	29.1	0.6	17.1	1.3	-	458.4
Transport Equipment	49.1	230.6	18.2	3.0	5.0	7.0	0.7	-	9.1	-	381.2
Scientific & Measuring Equipment	△	2.0	0.6	8.5	1.4	25.0	-	-	△	-	47.1
Others	1.5	11.7	3.9	12.6	8.1	7.1	-	0.9	5.9	-	56.7
Hotel & Sightseeing Industry	59.5	25.6	0.6	50.1	51.6	-	△	-	-	-	204.9

Notes: 1. Foreign Investment = Issued capital + estimated foreign loan, the end of year
2. - ; Zero, △ ; Few

Source: MIDA; JETRO WHITE PAPER on Foreign Direct Investment, 1986

On the other hand, the foreign debt was increased due to the loans from other countries for large-scale public investment projects. In 1985, the cumulative foreign debt swelled to RM21.8 billion. From 1981 to 1985, the debt service ratio increased by 28.5 percent a year. At the same time, the government began more aggressively to solicit foreign investment.

3.1.3. Third Investment Boom (1988-1990)

In July 1985, the government began easing restrictions on equity ratios with the aim of promoting the export-oriented industries and high tech industries. In October, it announced preferential tax measures for the manufacturing, agricultural, and tourism sectors. In December of the same year, it eased requirements relating to business licenses under the Industrial Coordination Act by limiting the obligation for licenses to companies with capital of more than RM1 million from the old RM250,000 and with total full-time employees of 50 workers from the previous, 25. Subsequent to these amendments, the government announced major measures to promote investment in September 1986 under the Promotion of Investments Act. The objects of the 1986 amended Promotion of Investments Act were (i) the creation of job opportunities, (ii) the promotion of exports, (iii) regional development, (iv) the effective utilisation of domestic resources, and (v) technical development and development of human resources. The main amendments to the act are summarised below.

i. Easing of Restrictions on Equity Ratio of Foreign Investment

Companies applying for investment to MIDA from October 1986 to the end of 1990 were allowed to hold 100 percent equity when meeting either of the following conditions:

- Exporting over 50 percent of their products
- Employing over 350 Malays full-time

ii. Easing of Restrictions on Posts Held by Foreign Nationals

Companies with over US$2 million in called-up capital were allowed 5 expatriate posts.

iii. Easing of Restrictions on Companies Under Industrial Coordination Act (1975)

The criteria for application of the restrictions under the law were changed from the RM 1 million of called-up capital and 50 full-time employees of the amendment of December 1985 to RM 2.5 million of called-up capital and 75 full-time employees in October 1986.

iv. Expansion of Incentives

- The period of exemption on company taxes and development taxes for pioneer status companies (five years) was extended another five years under certain conditions.
- Payment of taxes on 50 percent of the income before deduction of depreciation costs.
- Introduction of a system of deduction of 5 percent from income on companies meeting the criteria of the NEP (New Economic Plan for 1971 to 1990).

These measures reflected the change in foreign investment policy to be more flexible and liberal.

In 1987, the government announced detailed rules for enforcement of the 1986 Promotion of Investments Act. It announced details on the rates of deductions in the investment tax deduction system, terms for extension of pioneer status, and additionally designated regions for encouragement of investment. The terms for extension of pioneer status were (i) investment of RM25 million in plant, machinery, and factory buildings, not including the cost of purchasing land or (ii) employment of over 500 full-time employees, within the five year period of pioneer status, in which case a further five-year extension was granted.

In the same year, efforts were made to rationalise investment procedures. The Investment Ministerial Conference ordered that all decisions relating to extension of incentives be made within two months. The Minister of International Trade and Industry sent out a directive to the effect that all administrative procedures relating to manufacturing licenses and technical tieups were to be completed within 6 weeks of the application. Further, regarding acquisition of pioneer status, the list of the industries subject to pioneer status was prepared by MIDA. In July 1988, the government came out with a policy of allowing 100 percent foreign equity, conditional on at least 20 percent exports, for just five years for even investments oriented toward the domestic market.

Foreign equity of only 30 percent had been allowed previously. In this case, 49 percent of the equity was supposed to be later transferred to the Malaysian side, including 30 percent as the Bumiputera equity.

In response to these incentives from the government, foreign investments approved in the manufacturing sector in 1988 (including increased investment) rose 2.1-fold to 470 projects worth a 2.7-fold greater RM2,010.48 million (based on proposed foreign called-up capital). The influx of foreign investment grew smoothly in 1989 as well and reached 608 projects worth RM3,412 million. The peak in foreign investment came in the following 1990, when the number of projects rose 16.6 percent and the value rose 1.8-fold.

The period from 1988 to 1990 is considered to have been the third boom in foreign investment. A look at the investment by country in the three years from 1988 to 1990 shows Taiwan first in the number of investments with 572 projects, followed by Singapore second with 431, Japan third with 343, and then Hong Kong with 133 and the U.S. with 114. In value as well, the number one spot was held by Taiwan at RM3,784.43 million, while Japan was second at RM3,404.10 million, the U.K. third at RM665.8 million, and the U.S. fourth at RM566.5 million (Refer to Table 3-3-4).

By industry, a look at the trends in the value of foreign investment approved for the three years of 1988 to 1990 shows that the biggest sector, electrical and electronic equipment, grew in investment from the RM596.5 million of 1988 to RM1,112 million in 1989, an 86 percent rise, and to a 32.7 percent share of total foreign investment received. The sector retained first position in 1990, but declined in the rate of growth to a 48.8 percent increase in value to RM1,654.8 million and thereby only accounted for a 26.6 percent share in investment.

The increase in foreign investment was particularly great in basic metal products. Investment rose 12-fold in two years from the RM127.5 million (fifth place) of 1988 to RM1,526.1 million (second place) in 1990. Transport equipment rose 8-fold in investment from the RM7.3 million of 1988 to RM61.5 million in 1989, but accounted for only a 1.8 percent share of total foreign investment. Even in 1990, it reached only RM104.5 million for a less than 1.7 percent share (Refer to Table 3-3-5).

The features of the third foreign investment boom (1988 - 1990) are summarised below.

i. There was a striking increase in investment from Taiwan. Investment from Taiwan rose from theRM 5 million and 1 percent share of 1986 to RM118.5 million, a 23-fold rise, and a 15.8 percent share in 1987, lifting Taiwan all at once to third place after Japan and Singapore. In 1988, investment rose 3.2-fold and the share reached 19.1 percent to bring Taiwan second after Japan as an investor. In 1989, further investment rose 2.6 fold to RM1,013 million to bring Taiwan ahead of Japan in share to a first place 29.8 percent. This trend continued in 1990 when investment rose 2.3-fold to RM2,353.4 million to maintain Taiwan at the number one spot with a 37.8 percent share of investment. The main reason for this surge in investment from Taiwan was the upward valuation of the New Taiwanese dollar (Yuan).

ii. Japan also increased its presence. A look at the trend in investment shows that Japan invested RM58.12 million in 1986 for an 11.1 percent share of the total, placing it second after Singapore at 17.2 percent. In 1987, however, investment rose 4-fold toRM 230.8 million to give it number one position with a 30.8 percent share of investment. Japan maintained its number one spot in 1988 as well when investment reached 561.1 million giving it a 27.9 percent share and in 1989 when investment reached RM1,065.3 million giving it a 31.3 percent share. Japan fell to number two in 1990, but maintained a high RM1,777.7 million level of investment and a 28.5 percent share. The main factor behind the increase in investment from Japan was also the appreciation of its currency.

iii. A look at the structural changes in investment by industry shows that there was an accelerated shift from investment in resource-based industries to non-resource-based industries. In terms of the shares of resource-based foreign investment, investment in oil and coal fell from a 33.6 percent share in 1986 to a 1.8 percent share in 1989. Investment in the food material sector fell from 23.4 percent in 1986 to 2.1 percent in 1990.

As opposed to this, foreign investment in the non-resource based industries, which includes electrical and electronic equipment, for example, doubled from the 21.3 percent of 1986 to 43.2 percent in 1987. In 1988, it fell somewhat to 39.6 percent, but in 1989 rose to 49.1

percent and in 1990 hit 61.6 percent. There was particularly strong growth in basic metal products. Investment in that sector rose from a 1.8 percent share in 1986 to a 24.5 percent share in 1990. On the other hand, investment in electrical and electronic equipment rose from the 10.0 percent of 1986 to a peak 35.3 percent in 1987, then declined about 30 percent in the late 1980s to hit 26.7 percent in 1990.

iv. The share of foreign investment in capital input (approval basis, including loans) rose rapidly. The share of foreign investment in capital input grew from the 16.9 percent of 1985 to 32.7 percent in 1986 and continued strong to 53.6 percent in 1988. In 1989, it hit a peak of 70.8 percent (Refer to Table 3-3-6).

v. The size of the investment per project grew as well. The average project size rose from the RM1.04 million 1986 to RM4.27 million in 1988, RM5.59million in 1989, and RM8.78 million in 1990.

Table 3-3-4 Best Ten Countries of Foreign Investment

(Unit: RMMillion)

	1980		1985		1986		1987		1988		1989		1990	
1	Singapore	53.8	Japan	81.7	Netherlands	180.3	Japan	230.8	Japan	561.1	Japan	1,065.3	Taiwan	2,353.3
2	Japan	35.7	Singapore	47.2	Singapore	90.0	Singapore	135.4	Taiwan	384.3	Taiwan	1,013.0	Japan	1,777.6
3	United States	21.8	United States	36.8	Japan	58.1	Taiwan	118.5	United States	252.6	Singapore	269.5	Singapore	321.3
4	United Kingdom	15.7	Hong Kong	18.4	Hong Kong	27.5	United States	61.3	Singapore	172.1	United Kingdom	255.5	United Kingdom	315.4
5	Canada	13.8	Taiwan	14.7	United	19.1	Australia	29.7	France	131.8	United	126.8	Indonesia	224.6
6	Switzerland	12.6	United Kingdom	10.7	United States	17.1	India	28.3	Hong Kong	129.5	Panama	117.6	Iran	202.7
7	West Germany	11.1	Korea, Rep.	10.4	Australia	16.3	Hong Kong	27.8	United Kingdom	94.8	Hong Kong	112.5	Korea, Rep.	164.2
8	Taiwan	9.9	Sweden	9.2	India	16.0	United Kingdom	26.1	India	32.2	West Germany	107.7	Hong Kong	136.1
9	Netherlands	8.2	Iran	8.7	Luxembourg	8.5	France	15.1	West Germany	25.6	Korea, Rep.	78.9	Sweden	82.8
10	France	5.1	Greece	7.5	France	6.4	Canada	11.2	Korea, Rep.	23.3	Finland	46.2	India	72.7
Total	–	247.7	–	324.9	–	524.5	–	750.0	–	2,010.5	–	3,410.1	–	6,227.9

Note: Total; Including others.
Source: MIDA

Table 3-3-5 Foreign Investment in Apporved Projects by Industry

Unit: %

Industry	Year					
	1980	1986	1987	1988	1989	1990
Food Processing	20.1	23.4	13.2	13.3	4.0	2.1
Beverages & Tobaccos	0.1	0.1	0.3	0.2	-	0.1
Textiles & Textile Products	3.0	2.8	2.9	4.4	6.8	5.0
Leather Products	0.0	-	-	0.0	0.2	0.3
Wood & Wood Products	4.3	0.7	5.0	3.7	9.8	2.9
Furnitures	0.8	0.2	0.2	1.8	1.8	1.0
Paper, Printing & Publishing	2.7	1.0	2.8	0.5	1.7	1.9
Chemical Products	7.9	3.6	15.1	13.0	13.3	10.5
Petroleum Products	0.5	33.6	-	-	1.8	8.7
Rubber Products	8.2	5.0	7.1	16.1	3.9	0.5
Plastic Products	1.6	5.8	5.5	4.8	2.9	2.8
Non-Metalic Mineral Products	15.6	1.7	3.6	2.1	3.3	1.5
Basic Metal Products	7.2	1.8	4.5	6.3	4.6	24.5
Fabricated Metal Products	2.8	2.0	0.6	2.6	6.3	2.1
Machinery	0.6	2.4	1.7	0.3	1.8	5.8
Electrical & Electronic Products	20.6	10.0	35.3	29.7	33.0	26.7
Transport Equipment	0.8	5.1	1.1	0.4	1.8	1.7
Scientific & Measuring Equipment	0.9	-	-	0.2	1.6	0.8
Others	2.4	1.0	1.0	0.7	1.5	1.1
Total	100.0	100.0	100.0	100.0	100.0	100.0
(Non-resource-based Industry)	32.9	21.3	43.2	39.6	49.1	61.6

Note: Approved amounts equal to proposed foreign called-up Capital

Source: MIDA

Table 3-3-6 Investment in Approved to Manufacturing (1980-1993)

Year	Number		Foreign Investment	Domestic Investment	Foreign Share in Total
	Total	Foreign Investment	(MR Million)	(MR Million)	Investment (%)
1980	459	97	729.5	1,373.3	34.7
1981	596	111	1,309.3	3,139.1	29.4
1982	468	63	1,626.6	3,808.2	29.9
1983	490	69	629.1	1,729.0	26.7
1984	749	85	718.0	3,083.1	18.9
1985	625	78	959.3	4,727.6	16.9
1986	447	99	1,687.9	3,475.3	32.7
1987	333	132	2,060.6	1,873.9	52.4
1988	732	301	4,878.0	4,215.9	53.6
1989	792	439	8,652.7	3,562.7	70.8
1990	906	533	17,629.1	10,539.0	62.6
1991	973	561	17,055.3	13,763.1	55.3
1992	874	425	17,772.1	10,003.0	64.0
1993	686	328	6,287.2	7,465.5	45.7
Total	9,130	3,321	81,994.1	72,758.7	-

Note: 1. Foreign Investment = 100% Foreign Equity Ownership + 51% or more Foreign Equity.
2. Foreign Investment = Foreign Equity + Estinated Foreing Loan.

Source: Malaysia International Trade and Industry Report, 1994

3.1.4. Adjustment of Foreign Investment (Early 1990s)

With the tremendous increase in foreign investment from the late 1980s to 1990, Prime Minister Mahathir announced his "Vision 2020" in February 1991. In June of that year, the government announced the "National Development Policy (NDP)" and the "Outline Perspective Plan 2 (OPP2)" as new economic plans for the period up until the year 2000. In July, it announced the "Sixth Five-Year Plan for 1991 to 1995". These plans positioned the manufacturing sector as the leading sector of Malaysian industry and called for an emphasis on private sector effort. In terms of the government policy toward foreign investment, however, the government reevaluated the preferential tax system, eliminating some incentives for investment in the draft budget for fiscal 1992 announced in November 1991. Due to this government modification in foreign investment incentives and the changing international economic environment, i.e., the global recession, the flow of foreign investment in the manufacturing sector began declining in 1991.

In 1991, the value of approved foreign investments declined 2.5 percent in value from the previous year to RM6,073.4 million and the number of projects fell by 100 to 607. In 1992 as well, the value of investments declined 3.7 percent to RM5,854.4 million. In 1993, it further fell 58.3 percent to RM2,443.3 million, but recovered to RM 4,120.3 million in 1994 (Refer to Table 3-3-7).

In terms of industries, the first place industry in 1991 was electrical and electronic equipment (RM1,139.7 million), but petroleum refining came in first in 1992 at RM2,936 million for a 50 percent share of total foreign investment. Investment in basic metal products peaked in 1990, then halved in 1991 and fell a further one-third in 1992, but began recovering in 1993.

Investment in transport equipment remained on the same level as the previous year in 1991 at RM104.6 million, but fell one-third to RM32.5 million in 1992. In 1993, it recovered to RM116.7 million, but fell to RM99 million in 1994. (Refer to Table 3-3-8).

Table 3-3-7 Foreign Investment in Approved by Country

(Unit: RM Million)

	1989		1990		1991		1992		1993		1994	
	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number
Japan	1,065.3	127	1,777.7	134	1,461.2	181	784.0	146	695.5	133	702.2	204
Singapore	269.6	150	321.4	147	403.7	148	200.7	184	194.7	150	360.9	175
United States	126.8	30	187.1	29	455.3	45	568.9	41	550.7	29	562.8	46
Hong Kong	112.5	40	136.1	43	315.2	55	44.9	38	62.6	25	297.8	38
United Kingdom	255.6	16	315.4	13	207.3	20	1,027.5	17	10.4	15	56.3	21
Rep. of Korea	78.9	29	164.2	25	466.0	43	46.2	22	50.7	13	137.2	18
Australia	15.0	6	22.3	17	176.8	20	465.4	20	31.5	12	82.7	22
Germany	107.8	10	57.9	11	56.6	19	36.9	12	22.1	10	60.2	24
Taiwan	1,013.1	191	2,353.4	270	1,606.2	216	580.4	130	343.3	87	1,017.9	100
Total (incl. others)	3,401.2	608	6,227.9	709	6,073.4	609	5,854.4	642	2,443.3	507	4,109.9	765

Note: Approved amounts equal to proposed foreign called-up capital.
Source: MIDA

Table 3-3-8 Foreign Investment in Approved by Industry and Potential Employment

(Unit: Amount; RM Million, Employment; '000 Persons)

	1989		1990		1991		1992		1993		1994 *	
	Amount	Employ-ment	Amount	Employ-ment	Amount	Employ-ment	Amount	Employ-ment	Amount	Employ-ment	Amount	Employ-ment
Food Processing	135.6	2.9	129.1	2.3	109.3	3.3	134.4	2.6	68.2	3.5	66.9	1.8
Textile	230.8	20.2	312.2	17.2	212.8	7.7	408.6	16.4	213.1	3.9	427.7	4.1
Paper, Printing	58.6	2.4	120.2	3.5	85.2	1.8	17.9	1.3	59.1	1.5	35.1	1.1
Chemical	458.6	1.9	655.6	4.6	677.5	3.4	581.8	2.5	627.0	2.4	300.3	1.6
Petroleum	64.2	0.1	540.6	3.1	539.0	1.6	2,936.0	2.6	-	-	85.0	0.2
Rubber	130.7	13.3	32.4	2.5	89.3	5.4	27.9	2.8	13.8	1.7	36.8	2.4
Non-Ferrous Metal	111.6	3.3	95.9	5.0	730.7	6.9	156.3	2.5	49.4	2.7	326.2	3.0
Basic Metal Products	154.3	3.3	1,526.1	8.1	860.6	13.5	265.6	5.3	321.6	1.7	146.1	1.3
Fabricated Metal Products	220.3	5.9	132.1	3.7	832.9	6.1	41.3	2.3	45.2	1.7	71.9	4.1
Electric and Electronic	1,112.0	64.3	1,654.8	77.1	1,139.7	80.9	426.2	31.0	630.7	34.4	1,779.5	58.3
Transport Equipment	61.5	3.6	104.5	3.3	104.6	4.1	32.5	1.8	116.7	5.3	99.0	2.9
Machinery Manufacturing	60.3	3.1	363.5	10.4	96.2	3.7	187.9	5.2	28.5	0.6	106.1	3.5
Total (Incl. others)	3,401.2	165.9	6,227.9	171.5	6,073.4	183.2	5,824.4	94.4	2,443.3	72.4	4,109.9	108.6

Notes: 1. Approved amounts equal to proposed foreign called-up capital.
2. By the revision of Industrial Coordination Act, the objective investment to be approved and with the capital of over RM250 million, or with over 75 employees after Oct. 1, 1986.
3. * Provisional figures as of May 1995.

Source: MIDA

3.2. CURRENT FOREIGN INVESTMENT POLICY

3.2.1. Incentives for Investment in Manufacturing Sector

The principal incentives for the manufacturing sector are contained in the Promotion of Investments Act of 1986, the amendment of the act of November 1991, and the announcements of the draft fiscal year budgets starting from fiscal 1992.

(1) General Incentives

The approval of Pioneer Status or the investment tax allowance is determined according to priorities termed "promoted activities" or "promoted products" as determined by the Minister of International Trade and Industry.

1) Pioneer Status

A company given Pioneer Status is granted partial exemption from the payment of income tax. It has to pay tax on 30 percent of its statutory income. The period of tax exemption is five years from the date of start of production as determined by the Minister of International Trade and Industry. No extension of the term is allowed.

The government considers on a case by case basis giving up to 100 percent exemption for projects deemed of strategic national importance. These projects are primarily those with heavy capital investment and high technology.

2) Investment Tax Allowance (ITA)

A company given the investment tax allowance is granted an allowance of 60 percent in respect of qualifying capital expenditure incurred within five years from the date of approval of the project. The allowance can be utilised to set off against 70 percent of the statutory income in the year of assessment. The remaining 30 percent is taxed at the prevailing company tax rate. Any unused allowance may be carried forward to subsequent years until the whole amount has been used up.

3) Reinvestment Allowance (RA)

The reinvestment allowance is granted to manufacturing companies which incur qualifying capital expenditure for the following objectives:

- Expansion of production capacity
- Modernisation and upgrading of production facilities
- Diversification into related products

The RA is in the form of an allowance of 50 percent of capital expenditure incurred by the companies.

(2) Incentives for Export

Discussed in detail in the next section.

(3) Incentives for Research and Development

i. Companies established for the purpose of research and development are allowed a. a tax exemption for a period of five years, and b) carry forward of accumulated losses incurred during the tax relief period to the post-tax relief period.

ii Expenses for research of a nature leading to future profit carried out by a person engaged in business or on his behalf are eligible for double deduction. Expenditure for research approved by the Minister of Finance is eligible for double deduction.

iii. Buildings used for approved research are eligible for an industrial building allowance of 10 percent for the first fiscal year and 2 percent thereafter.

iv. Plant and machinery used for purposes of approved research are eligible for depreciation.

v Double deduction is given for cash contributions made to approved research institutes.

vi. Approved companies engaged in R&D projects for companies in which they hold equity,

are related to, or are affiliated with are allowed a deduction of Investment Tax Allowance of 100 percent of qualifying capital expenditures over a 10 year period with the provision that this is limited to 70 percent of the statutory income for each year (applied since October 29, 1993).

vii. Companies engaged in R&D in-house are allowed deductions of Investment Tax Allowance of 50 percent of qualifying capital expenditures over a 10 year period with the provision that this is limited to 70 percent of the statutory income for each year (applied since October 29, 1993).

viii Buildings used by approved research institutes or companies for research purposes are eligible for the industrial building allowance (applied since October 29, 1993).

(4) Incentives for Training

i. Investment Tax Allowance of 100% for a period of 10 years is given to companies intending to undertake technical or vocational training. This allowance will be abated from the statutory income but abatement of each assessment year will be limited to 70% of the statutory income.

ii. Machinery, equipment and materials used for training are eligible for exemption from import duties, sales tax and excise duties.

iii A double deduction is given for expenditures relating to approved training. When employees receive training at approved training institutions, automatic approval is given to the double deduction for expenses. However, this is applied only to those companies which employ fewer than 50 Malaysian workers.

iv. Companies which employ 50 Malaysian workers or more can avail themselves of the assistance for training provided by the Human Resources Development Fund (HRDF). These companies, however, have to contribute to the HRDF at the rate of 1 percent of the wages of the employees.

v. The industrial building allowance (IBA) is granted to companies which have incurred expenditures on buildings used for approved industrial training. The incentive consists of an initial allowance of 10 percent and an annual allowance of 2 percent.

(5) Reduction in Company Income Tax

i. The company income tax on residential companies and nonresidential companies was 34 percent up to 1993, but was reduced to 32 percent in 1994. This rate is reduced to 30 percent effective from the year of assessment 1995.

ii. Tax incentives: The main incentives for the manufacturing sector are provided in the Promotion of Investments Act of 1986 and the Income Tax Act of 1967. Since 1986, the incentives had been considerably broadened, but starting in November 1991 the tax incentives began being reduced or scrapped.

3.2.2. Guidelines on Equity Ratio

The requirements on equity ratios of foreign investment are flexibly applied. The guidelines are as follows:

i. 100 percent foreign equity is allowed when the export ratio of products is 80 percent or more. However, in principle a joint venture is preferred for certain subcontracting industries (plastic processing, press dies, etc.)

ii. When the export ratio of products is from 50 to less than 80 percent, 100 percent foreign equity is allowed when the following conditions are met:

- The foreign investor invests RM50 million or more in fixed assets (excluding land) and the project involves an added value of at least 50 percent, and

- The products of the company do not compete with products locally produced for the domestic market.

iii. In other cases when the export ratio of products is from 51 to 79 percent, up to 51 percent in foreign equity is allowed. Further, up to 79 percent is sometimes allowed depending on the level of technology, spin-off effects, scale of investment, location of the site, value-added, and the utilisation of local content.

iv. When the export ratio of products is from 20 to 50 percent, foreign equity in the range of 30 to 51 percent is allowed depending on the level of technology, spin-off effects, scale of investment, location of the site, value-added, and the utilisation of local content.

v. When the export ratio of products is 20 percent, only a maximum foreign equity of 30 percent is allowed.

vi. When producing high tech products and products of encouraged industries for the domestic market as determined by the Government, a maximum of 100 percent foreign equity may be allowed.

3.2.3. Acquisition of Manufacturing Licenses Under the Industrial Coordination Act (ICA)

Companies which have shareholder's capital of at least RM2.5 million or at least 75 full time employees and which are engaged in manufacturing activities are obligated to obtain licenses under the 1975 Industrial Coordination act. Companies which are exempt from application for manufacturing licenses are also exempt from restrictions on equity ratios, employment, etc.

Licensed companies have to apply or sometimes just report when increasing production capacity or diversifying their product lines depending on the nature and conditions of the change.

3.2.4. Restrictions on Raising of Local Funds

i. Nonresident controlled companies (NRCC, i.e., foreign companies) are allowed to borrow up to RM10 million from domestic sources without the approval of the administrative authorities

on the condition that at least 60 percent of the credit be obtained from financial institutions established in Malaysia.

ii. Approval of the administrative authorities is required when NRCC wish to borrow RM10 million or more from domestic sources. Approval is granted in accordance with the need for the funds, the state of domestic credit, the total shareholders' capital of the company, the state of long-term overseas loans of terms of 5 years or more, etc.

3.2.5. Remittance and Reinvestment

i. All payments to non-resident for any purpose are freely permitted, subject only to the completion of a simple satistical form for remittances of more than RM50,000 each or its equivalent in foreign currency. The bank is supposed to inquire with the administrative authorities depending on the use of the funds (acquisition of foreign shares, extension of credit to nonresidents, etc.) and when accompanied by extension of credit domestically.

ii. There is no restriction on remittance of royalties so long as the technical assistance agreement was approved by the government. The rate of 1-5% of net sales can be considered.

iii. Incentives are provided for reinvestment of profits. There is no compulsory pressure such as administrative guidance applied for this.

3.2.6. Industrial Property

i. Industrial property rights are protected under the Patents Act, 1983 and the Patent Regulations, 1986. Patents expire 15 years after the date of grant.

ii. Trademarks are protected under the Trademark Act, 1976 and the Trademark Regulations, 1983. Registered trademarks may be periodically renewed and use continued. There are no limits on the term of protection for trademarks.

iii. Computer software and the like are protected under the 1987 Copyright act (enforced from December 1, 1987). The 1969 Copyright Act was abolished with the enactment of the new law. The term of protection is 50 years.

3.2.7. Employment of Foreign Nationals

i. The government's policy is for the training of Malaysians and for their employment in all jobs.

ii. Foreign companies are allowed specific "key posts" in fields where there are few Malaysians (jobs requiring specialised knowledge or abilities) where employment of foreign nationals is allowed.

iii. Foreign investment companies with at least RM2 million in called-up capital are allowed to employ five foreign nationals, including one key post. Additional expatriate posts will be given when necessary upon request.

iv. Foreign investment companies with less than RM2 million in called-up capital are allowed to employ a number of foreign nationals according to the size of the foreign paid-up capital (a key post is considered generally with RM500,000) and certain conditions (training of Malaysians, etc.).

3.3. POLICY FOR PROMOTION OF TECHNICAL TIEUPS

3.3.1. Different Types of "Technical Transfer" Agreements

(1) Joint Venture Agreements

These are basic agreements clarifying the joint-venture relationship between two or more parties. They define the name and purpose of the joint venture, the equity ownership, the composition of the Board of Directors, finance, know-how, personnel, assets, and conditions for liquidation. The financial, managerial, and other rights of the partners or formula to be used in determining such

rights are also clearly spelt out.

(2) Technical Assistance Agreements

The objective of these agreements is to obtain technical assistance for the installation and operation of the projects. Details of the technology to be transferred and terms and conditions for the transfer are also spelt out. Normally, specialised technical information and services are required so that products are competitive. These agreements also include the continued supply (during the current agreements) of scientific and technical assistance, technical services as well as training, and management assistance. The scope of technical assistance and technical services is limited to technology out of the scope of know-how and patents.

(3) Know-How Agreements

Know-how agreements bind the parties concerned for the transfer of intellectual property. These agreements usually cover specific information on formulas, processes, and industrial techniques. This type of proprietary know-how could range from a secretly held chemical formula to special manufacturing techniques which have been developed by the supplier.

Know-how holds a position somewhere between technical assistance and patents. Know-how is a package of technical information, a substantial portion of which is held in secret, which gives its possessor some technical and/or marketing advantage. Unlike the owner of a patent, the owner of know-how has no legal recourse to prevent third parties from developing and employing the substance of the unpatented know-how. Hence, a secrecy clause is fundamental to a know-how license agreement.

(4) License Agreements/Patent Agreements

1) License Agreements

These are agreements under which all rights (except legal title) are transferred to licenses for a given territory, to manufacture, use, and/or sell a product. These agreements may also include

the right (of the licensee) to sub-license to a third party. In normal license agreements, the licenser gives, sells, or leases to licensees the right to use certain industrial rights and/or technical expertise including patents, trademarks, and technical assistance.

2) Patent Agreements

These agreements usually cover the exclusive or non-exclusive rights to exploit specific technical inventions. In exchange for public disclosure of the full informational content of an invention, the state, through patent law, confers on the patent owner (patentee) certain exclusive rights for a limited period. These concern principally rights of excluding others from making, using, and selling the invented product, technique, or process in the national territory where the patent has been issued.

(5) Trademark Agreements

These agreements usually cover the exclusive or non-exclusive rights to use certain registered and well-known proprietary trademarks/names. Trademarks are distinctive visual and sometimes aural devices, words, or emblems (symbols) or a combination of them, that a firm applies to the goods it trades in or to the services it performs, to indicate to the public that they are the firm's goods or services. Trademarks play an important role in the market place since with their aid the consumer learns to distinguish between products of different manufacturers. Trademarks also serve to assure the public that the goods are consistently of a certain quality.

(6) Management Agreements

These are agreements entered into between two or more parties whereby one party is responsible for the overall management of the company and is also responsible for reporting the Board of Directors.

They may specify the powers of managing directors and their remuneration and benefits accruing to such responsibility. They may also cover other management functions such as financial, technical, administrative, and marketing functions.

(7) Sales Commission Agreements/Purchase Agreements

1) Sales Commission Agreements

These are agreements which involve the granting of rights to sell the products in a particular territory, including other sales activities such as promotion of products.

2) Purchase Agreements

These are agreements binding the producers to sell their products to the buyers either in certain quantities or at an agreed price for a certain duration.

(8) Turn-key Contracts

These are arrangements entered into between two or more parties whereby one party is responsible for setting up a plant and putting it into operation. Depending on the nature of the plant and the level of technology involved, turn-key contractors may be either technology owners or machinery suppliers or consulting engineering firms.

(9) Other Agreements

1) Service Agreements

These agreements are basically special agreements or specialised agreements which are incorporated into the above agreements.

2) Engineering Service Agreements

These agreements are short-term contracts, usually listing the technical work the supplier of engineering services is required to perform.

3) Supply Agreements

These are basically agreements to ensure the supply of raw materials or components need in finished products.

4) Franchise Agreements

These are agreements giving a right of distribution of goods or services and are often associated with high reputation trade and service marks.

3.3.2. Trends in Technology Introduction

According to MIDA and MITI, there were a total of 2,360 transfers of technology in Malaysia, on an approval basis, from 1975 to December 1994. Looking at this in five year periods, there were 313 transfers from 1975 to 1979, 589 from 1980 to 1984, 677 from 1985 to 1989, and 781 from 1990 to 1994.

By total transfers from 1975 to 1994, Japan ranked first with 940 or about 40 percent of the transfers. Second place was taken by the U.S. with 275 transfers and third place by the U.K. with 259, followed by 107 transfers for Germany, 98 for Australia, 80 for Hong Kong, 73 for Singapore, 71 for India, and 53 for South Korea (Refer to Table 3-3-9).

By industry, electrical and electronic equipment was first with 530 transfers, chemicals second with 304, and transport equipment third with 256 (Refer to Table 3-3-10).

Table 3-3-9 Technology Transfer Agreements by Country

Country	1975	1976	977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994*	Total
Japan	22	21	7	32	21	32	35	33	46	39	33	38	37	54	87	82	92	69	91	69	940
U.K.	10	6	4	13	11	20	17	6	19	11	14	21	17	17	21	8	14	12	8	10	259
U.S.A	6	4	1	9	8	11	14	10	18	12	13	12	12	22	23	10	18	10	34	28	275
Germany	-	1	4	6	11	9	11	10	2	2	3	2	5	5	6	8	5	6	3	8	107
Australia	3	2	1	-	4	10	5	6	2	5	3	9	3	16	2	7	4	5	8	3	98
Hong Kong	1	-	3	3	2	9	2	3	2	7	4	7	7	5	9	3	6	3	4	-	80
India	3	5	8	7	5	5	4	4	4	2	6	1	-	2	2	1	1	3	6	2	71
Singapore	3	2	2	1	2	4	7	5	3	8	2	3	4	4	3	6	4	1	3	6	73
Rep. of Korea	-	1	-	1	-	-	-	2	4	6	1	3	1	-	3	10	2	9	8	2	53
France	2	4	-	-	2	-	7	-	4	1	-	4	3	2	4	-	6	5	4	3	51
Swtizerland	-	-	-	2	1	-	3	1	2	2	1	1	1	3	2	1	1	3	5	-	29
Norway	-	-	-	-	1	1	-	2	1	2	5	-	2	1	-	1	1	2	-	1	20
Italy	1	1	-	1	1	2	-	-	-	-	2	1	1	-	3	3	-	1	-	-	17
Panama	-	-	3	-	1	1	-	1	-	-	-	5	1	-	-	-	-	-	-	1	13
Others	7	6	-	7	17	10	26	11	24	22	9	16	16	19	33	15	11	7	11	3	274
Total	58	53	33	82	87	114	131	94	131	119	96	123	110	150	198	155	165	140	185	136	2,360

Note: * Provisional figures as of May 1995.
Source: MITI, MIDA

Table 3-3-10 Technology Transfer Agreements by Industry

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994*	Total
Electric and Electronics	17	9	5	21	15	19	16	19	15	21	20	12	29	37	40	41	45	38	69	42	530
Fabricated Metal Products	8	3	5	7	16	6	14	7	12	3	9	22	21	17	7	4	13	6	11	5	196
Chemical	3	-	4	19	8	11	21	5	15	17	16	15	18	29	27	24	21	19	20	12	304
Transport Equipment	5	4	-	5	7	10	11	11	22	17	20	15	4	1	15	18	16	28	25	22	256
Food & Biverages	4	7	2	2	8	14	15	4	21	6	10	8	8	16	21	14	9	3	15	4	191
Textile	6	7	2	4	-	8	5	2	5	6	1	7	2	6	4	7	6	7	3	1	89
Basic Metal Products	-	5	3	3	5	7	10	13	5	5	1	1	2	-	6	4	7	2	5	4	88
Wood & Wood Products	4	1	6	5	4	-	-	4	1	6	-	4	1	-	-	5	4	-	1	-	46
Pulp, Paper, Printing	-	-	-	-	-	-	-	-	-	-	3	4	1	3	-	4	4	2	3	1	25
Rubber	6	-	1	2	5	8	14	2	7	5	4	13	8	22	18	8	10	8	5	4	150
Non-Metalic Mineral Products	1	6	1	1	7	5	4	16	9	17	7	7	12	4	10	7	7	12	5	10	148
Hotel & Tourist Complex	-	5	1	-	2	4	2	4	8	7	4	4	1	2	6	3	8	1	5	-	67
Machinery Manufacturing	-	-	-	-	-	-	-	-	-	-	-	-	-	-	7	6	6	5	2	2	28
Plastic Products	1	-	2	-	3	5	6	1	2	7	-	4	-	2	6	5	6	6	11	4	71
Others	3	6	1	13	7	17	13	6	9	2	1	7	3	11	38	11	9	8	7	25	171
Total	58	53	33	82	87	114	131	94	131	119	96	123	110	150	198	155	165	140	185	136	2,360

Note: * Provisional figures as of May 1995.
Source: MITI, MIDA

4. EXPORT PROMOTION POLICIES

4.1. BASIC POLICY REGARDING EXPORTS

4.1.1. Changes in Export Policy

The following is a brief overview of the changes in Malaysia's export policy since the 1960s.

When Malaysia first achieved independence, a very large proportion of its industry was resource-based. Natural rubber and tin accounted for about 70 percent of the value of its total exports, giving the country an extremely unbalanced structure. To correct this, the government first adopted a policy of diversifying its resource-based export products.

By the 1970s, Malaysia had made great progress in diversifying its export products in endeavouring to escape from its reliance on the above two traditional products. First, in the area of resource-based products, new items such as lumber and palm oil emerged. By the end of the 1970s, these two products accounted for over 20 percent of the country's total export value. Further, progress was made in the import substitution begun in the 1960s and export industries had started to be cultivated. Electrical and electronic products were assigned a major role in Malaysia's export industries. Many foreign companies began moving their labour intensive production processes to Malaysia in search of lower labour costs.

In the 1980s, progress was made in import substitution in the heavy industries. At the same time, the government began even more aggressively promoting foreign investment in export-oriented fields. The changes in the global economic environment wrought by the currency adjustments begun in 1985 had the effect of pushing Japanese manufacturers to move production centers overseas. Some of them went to Malaysia. As a result, Malaysia achieved higher growth in exports of electrical and electronic products.

4.1.2. Export Policy in the 1990s

The success of the export industrialisation policy resulted in exports becoming of much greater

importance in Malaysia's economic growth. The government hopes that exports will continue to drive the country's development in the future. Its basic policy toward exports may be summarised as follows:

(1) Improvement of Export Structure

Malaysia has, as mentioned earlier, made considerable efforts to diversify its export products so as to obtain greater strength in dealing with changes in the external economic environment. The specific measures adopted have changed along with the development of its export industries. At the present time, there are two objectives: The first is to raise the ratio of exports of manufactured goods. This had already reached 73 percent (value basis) in 1993. The government is aiming at raising the ratio of manufactured exports to 81 percent by the year 2000. The second is the reduction of the over-reliance on electrical and electronic products in manufactured exports.

(2) Support for and Cooperation in Maintaining and Promoting Free Trade in the World

Having made exports a major part of its economic development plans, Malaysia has declared its strong support for the maintenance and development of the free trade system and has pledged to contribute positively toward the same. For example, it supports the GATT Uruguay Round and the establishment of the WTO system and is working to build regional economic ties through the AFTA-CEPT, EAEC, etc., as a step to the realisation of full global free trade. The government has adopted the policy, further, of periodically reviewing the trade system in Malaysia itself so as to promote liberalisation.

(3) Expansion of Regional Trade and Strengthening of Trade With Developing Countries

The movement toward formation of regional economic blocks in Europe and North America, whether they will be open or closed to the outside, is expected to result in fiercer competition for Malaysian exports. In preparation for this, the government has been stressing, first, the increase of trade within Asia, that is, with the AFTA-CEPT and EAEC, and, second, the opening up of new markets, that is, the expansion of "South-South Cooperation". This is considered a step toward the achievement of global free trade and is a strategy for securing markets in the event that

other regional economic blocks end up becoming closed in nature. As such, it has double significance.

(4) Increase in Competitiveness and Higher Value Added of Export Products.

There are several requirements for stronger competitiveness. Among these, the improvement of technology is the most important. In view of this, the public and private sectors of Malaysia are both strengthening their R&D activities and promoting development of human resources. Efforts to promote standardisation of industrial products and compliance with international standards also fall under this category. On the other hand, competitiveness improvement has a close correlation with increased market size. That is, improved competitiveness brings about growth in a market. At the same time, growth in the market leads to increased production which in turn means realisation of the merits of scale and thereby further improves competitiveness.

Improved technology is essential for the achievement of another main goal of Malaysia, that is, the enhancement of the value added of its exports. Rising labour costs, shortages in the working population, and the rise of such new sites for investment such as China and Vietnam mean that Malaysia will soon lose its advantage as a site for labour intensive industries. Enhancement of the value added of products is considered to be an important means for solving this problem.

(5) Strengthening of Marketing

To open up markets and further promote exports in already opened up markets, stronger marketing is required. Toward this end, Malaysia has set up a new trade promotion organisation, MATRADE, building on the organisation and functions of the former MEXPO, and has set up an exhibition and sales promotion center in Europe.

(6) Improvement of Export Promotion System and Facilities

Malaysia offers various incentives for exports and is setting up systems and organisations for facilitating export activities. Incentives of an export subsidy nature, however, run counter to the trend toward trade liberalisation, so are being eliminated.

4.2. SYSTEMS AND POLICIES FOR PROMOTING EXPORTS

There are a large number of systems and policies for the promotion of exports under the above basic policy. Among these, "Brand to Brand Complementation Scheme" of (6)-2) and the "Export Credit System" of (7) are limited to the automotive industry. Others are applied to several industries in addition to the automotive parts industry.

4.2.1. System of Promotion Using Tax Incentives

Tax incentives given to promote exports include exemption from import duty and excise duty, tax drawback, double deduction in income tax, and tax allowances.

(1) Free Zones (FZ) and Licensed Manufacturing Warehouses (LMW)

Companies located in Free Zones and companies accredited as licensed manufacturing warehouses enjoy exemptions from Import Duty, Excise Duty, Sales Tax, and Service Tax on imports of raw materials, parts, packaging and the like. All products made in Free Zones and licensed manufacturing warehouses are supposed to be exported in principle, but in some cases domestic sale of up to 20 percent of the production is allowed. Sales to the Free Zones and licensed manufacturing warehouses are deemed exports, so fall under the scope of export incentives as well.

(2) Exemption of Import Duty and Sales Tax

It is possible to obtain an exemption on Import Duty and Sales Tax for raw materials and parts when those materials and parts cannot be procured domestically or when they can be procured but they are difficult to use due to their unacceptable quality or price. At least 80 percent of the products must be exported.

(3) Drawback of Import Duty and Excise Duty and Sales Tax

The manufacturer finally exporting a product made using imported raw materials, component parts, and packaging may obtain a drawback of Import Duty and Excise Duty and Sales Tax. Applications

for drawbacks must be made within three months after shipment. An application is supposed to be processed within two weeks of its submission.

(4) Double Deduction

Double deduction in Income Tax is allowed for premiums for export credit insurance and expenditures for business activities aimed at increasing exports.

(5) Tax Allowances

The costs for construction of warehouses for export products may be deducted from tax as tax allowance. The allowance is 10 percent for the first fiscal year and 2 percent for each succeeding year.

(6) State of Utilisation

The state of utilisation of the Tax Incentives as found by the current survey is as follows:

1) Free Zones and Licensed Manufacturing Warehouses

Table 3-4-1 The Number Factories Located in FZs

(Unit: Numbers)

Area	1991	1992
Johor	8	5
Melaka	24	25
Selangor	4	4
Wilayah Persekutuan	21	22
Perak	19	23
Others	143	134
Total	219	213

Source: Laporan Tahunan, Royal Customs & Excise Department

Table 3-4-2 The Number of LMWs

(Unit: Numbers)

Area	1991	1992
Johor	318	343
Melaka	41	50
Negeri Senbilan	35	44
Pahang	12	15
Terengganu	3	3
Selangor	167	213
Wilayah Persekutuan	101	121
Perak	77	90
Kelantan	10	10
Kedah	60	120
Perlis	6	9
Pulau Penang/S.P.	217	257
Sabah	0	1
Sarawak	0	1
Total:	1,047	1,277

Source: Laporan Tahunan, Royal Customs & Excise Department

The number of factories in Free Zones and licensed manufacturing warehouses in recent years is shown in Table 3-4-1 and 3-4-2. There has been a drop in the number of companies occupying Free Zones and the value of their shipments compared with 1991 and 1992, but the long term trend is one of an increase (101 cases in 1986). Region-wise, more than half of the Free Zones are concentrated in Penang. The number of licensed manufacturing warehouses, on the other hand, increased by 230 in just 1992 (205 in 1988). These warehouses are more spread out region-wise compared with the Free Zones, with the most, over 300, being located in Johor, but there are also over 200 in Penang and Selangor and over 100 in Kedah and Kuala Lumpur.

2) State of Utilisation of Exemptions and Drawbacks

There were 2,720 claims filed for exemptions in 1992 and 562 for drawbacks. A past survey showed there were 179 claims filed for drawbacks in the fourth quarter of 1987, so this represents a considerable increase (there has been a decrease if just comparing tax drawbacks,

but this is because the thrust of incentives was changed from drawbacks to exemptions starting in 1988 due to recommendations of the IMP. There has been an increase in tax incentives overall). The processing time for applications for drawbacks used to be within three weeks in 1987, but has now been shortened to within two weeks.

3) State of Use of Double Deductions and Tax Allowances

The current survey was not able to determine the precise number of cases of use or the value of income tax related incentives. According to an official of the Department of Inland Revenue, however, there are about 4000 companies registered for using this system and there are roughly more than 100 applications filed per month. This figure, however, includes the number of applications filed for export allowances and abatement incentives, which were abolished in 1994. The time required for processing applications is over two months due to the extremely small number of personnel in charge of them.

4.2.2. Export Financing

Malaysia has a public export financing scheme called the Export Credit Refinance (ECR). The ECR system provides both pre-shipment and post-shipment financing. The former is made available to exporters or indirect exporters (domestic suppliers of inputs or final products to direct exporters) and provides operating funds required for exports corresponding to up to 80 percent of the contract value. The financing is provided for a maximum of four months. The latter provides exports with immediate funds after shipment in the case of exports on credit or usance terms of a minimum 30 days. This offers up to 100 percent of the contract value but is limited to no more than RM50 million. The financing is provided for a maximum of six months. Note that the conditions for use of these two financing systems are that the export products not be included on the Negative List of Goods exemptions and that the local content must be at least 30 percent and value added at least 20 percent. Further, the system can not be offered for imports of raw materials. The ECR is a scheme of the Bank Negara, but is actually implemented through general commercial banks. The interest rate is determined by the Bank Negara and is set lower than commercial bank interest rates in view of the objectives

of the scheme. As of July 1994, the rate was 6.5 percent (of which 1.5% constitutes the margin for the bank handling the financing).

Figures on use of the ECR are given in Table 3-4-3.

Table 3-4-3 Bills Discounted under ECR

(Unit: RM Million)

Year	Amount
1988	1,126,916,563
1989	2,370,992,772
1990	4,049,770,905
1991	5,194,601,331
1992	3,859,888,390
1993	3,523,941,034

Source: Annual Report, Bank Negara, 1989 to 1994

In 1992, pre-shipment Foreign Input Loans(loans applied to imports of raw materials, etc.) were abolished and post-shipment loans were limited to RM50 million. Accordingly, a considerable reduction in usage was seen in the year.

4.2.3. Export Credit Insurance

Malaysia's export credit insurance system is run by Malaysian Export Credit Insurance Berhad (MECIB) under Bank Industri Malaysia Berhad. This institution offers "Comprehensive Policy" and "Bank's Export Finance Insurance Policy." The former is applied to exports and the latter to financial institutions providing export financing to exporters. Note that "exporters" include manufacturers engaged in indirect exports as well. There are no provisions stipulating minimum local content. The export product merely has to have been manufactured or processed in Malaysia. The insurance premium differs according to the degree of risk of the destination and the length of the payment period but is a maximum of 1 percent. The premium is paid by the

exporter through a financial institution. The types of risks covered by the insurance are buyer risks (insolvency of importer, default of payment by importer, refusal of importer to accept goods delivered) and country risks (blockage or delay in the transfer of payment, imposition of import restrictions, cancellation of import licenses, war, revolution, and other civil disturbances, default of payment by government (= importer), and other causes outside Malaysia beyond the control of the exporter). This provides up to 85 percent in compensation.

Table 3-4-4 Number of Policies in Force and Face Value Insured

(Unit: RM Million)

Year	Number	Value
1988	173	782
1989	192	1,117
1990	250	1,641
1991	305	2,103
1992	353	2,820

Source: Annual Report 1992, MECIB, 1992

The state of use of MECIB Policies is shown in Table 3-4-4. There are currently 19 automotive parts related deals being insured under the two Policies combined (for batteries, exhaust pipes, car audio equipment, etc.). Most cases are for exports to the Middle East.

In the sixth Malaysian plan program, use of MECIB Policies is to be doubled. The number and value of exports insured rose from the 173 worth RM7.82 million of 1988 to 353 worth RM28.2 million in 1992 (for a total number of about 2000 cases by 1994). Twenty of the 38 commercial banks participate in the schemes of MECIB. According to MECIB, however, the schemes are not used as often as it expected. MECIB gives as possible reasons for the slow growth in actual use despite promotional campaigns, first, the fact that about 70 percent of exports are conducted on a letter of credit basis and that a considerable degree of safety is already ensured for the transactions and, second, the fact that the rate of coverage of losses is not 100 percent (the 85% level, however, is not necessarily low by international standards). The scheme is used in practice mainly for transactions with regions where LC based transactions are not

possible and for highly risky destinations. Specifically, it is used often for exports to the Middle East.

4.2.4. Support in Marketing

Most of the support consists of the various export promotion activities of MATRADE, the expanded and reorganised successor to the former MEXPO. Other supporting measures are given for exports to markets in Europe and the developing countries. They are expected to play an important role in export promotion in the future.

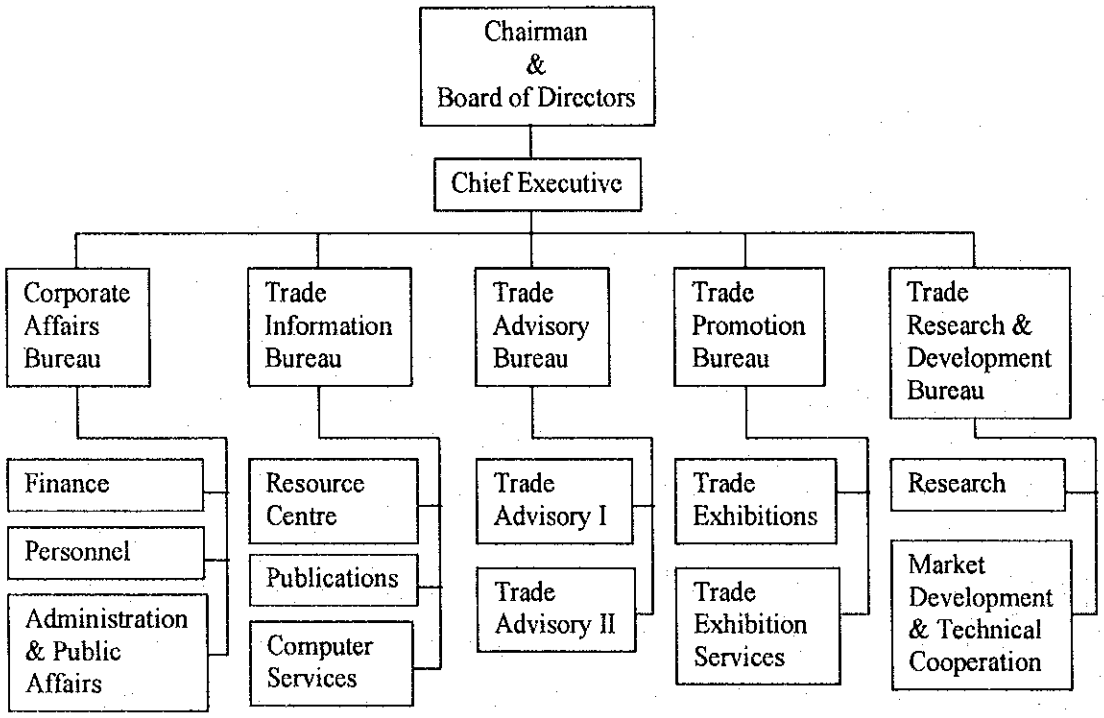
(1) Malaysia External Trade Development Corporation (MATRADE)

MATRADE is an organisation under the Ministry of International Trade and Industry (MITI). It was launched as a corporation expanded and reorganised from the old MEXPO unit of MITI. Special mention was given to it as an important part of the country's trade policy in the government speech on the 1994 budget.

1) Organisation and Budget

MATRADE is organised as shown in Fig. 3-4-1. To reinforce its functions, both its facilities and staff are being considerably expanded. Its staff has been more than doubled from the about 40 employees of MEXPO to 108 and will be increased to about 130 in the near future. The budget was RM28 million in fiscal 1993 and RM21 million in fiscal 1994. About the same level of allocations is expected in fiscal 1995 as in fiscal 1994. This represents a major increase compared with the approximately RM2 million budget of MEXPO in fiscal 1987/1988.

Fig. 3-4-1 Orgainisation Structure of MATRADE



2) Activities of Bureaus

a. Corporate Affairs Bureau

This bureau is in charge of general affairs and has no bearing on specific trade promotion activities, so will not be described any further.

b. Trade Information Bureau

This bureau is in charge of collecting and maintaining trade related information, publications, computerised trade statistics, corporate information, and information on trade fairs. The materials collected are kept in a library and made available for use by the general public. Information from computerised sources is provided in the form of hard copy. Systems are being developed to enable faster provision of information. Japan is providing assistance in facilities and know-how for this.

c. Trade Advisory Bureau

This bureau provides introductions of companies, consultations, and other services. When there is any inquiry from an overseas company, it retrieves information on the company from its computers or retrieves information from directories. The bureau also helps arrange appointments and transportation (costs of transportation borne by user). These services are in principle all free of charge. The results of past activities and target for the future are shown in Table 3-4-5.

Table 3-4-5 The Activities of Trade Advisory Bureau

(Unit: Numbers)

Item	1994		1995
	Performance (Jan. to Jun.)	Target (Jul. to Dec.)	Target
Trade inquiry	1,662	1,500	4,000
Business meeting/visitor	372	500	500
In-coming mission	5	-	15
Seminar/workshop/ briefing for other agencies	6	8	20
Company registration	225	250	500
International tender	129	50	200
Trade complaint	14	-	-
Factory visit	14	20	100

Source: MATRADE

d. Trade Promotion Bureau

This bureau is in charge of trade fairs, trade missions, standing exhibitions, and related duties. In 1994, it was scheduled to participate in 24 trade fairs. These include fairs in Asia, Europe, North America, South America and the Middle East. In addition, it was scheduled to hold "Malaysia Weeks" in Sweden, South Africa, and the UAE for

publicizing Malaysian products (already held in Sweden in April). In 1994, the bureau was scheduled to dispatch eight missions overseas. These are to visit Asia, Europe, North America, the Middle East, and Africa.

The ASEAN mission sent recently was participated in by over 50 private companies, handling marine leisure goods, building materials, food, furniture, computers, military goods, safety shoes, and other products, and over 10 states and other public organisations. A total of about 2,000 people joined in business meetings and seminars arranged by the mission. About 900 deals were discussed and about RM200 million worth of deals (potential) were arranged.

The standing exhibition hall includes 70 booths, each booth being about 1.5 meters wide and 1 meter deep. Only member companies are allowed to use these. Use of the booths is rotated every six months. During rotations, new users are given priority, but when there are still some booths left over after new users, continued use or reuse is allowed as well. The charge for use of the space for six months is RM300.

e. Trade Research and Development Bureau

This bureau is in charge of research and technical cooperation with other countries. These capabilities are particularly expected to be strengthened by the establishment of MATRADE where assistance from Japan and other countries are given now. The bureau is currently still in the preparatory stage and has not yet started functioning fully. Few overseas surveys have yet been made on the feasibility of export of specific Malaysian products. Note that this
bureau is also in charge of implementation of the ITAF4.

f. Trade Commissions

There are currently 23 trade commissions established around the world. These used to belong to MITI but were made branches of MATRADE at its establishment. Each commission is comprised of a trade commissioner from Malaysia and a locally employed marketing officer and a small supporting staff. These report on economic information, etc., in the host country monthly and yearly, and relay specific inquiries on trade with

Malaysia to the headquarters. A country profile is prepared including basic information on the host country using the yearly reports of the trade commissioner. MATRADE plans to set up more trade commissions in the developing countries in the future.

3) Company Registration System of MATRADE

General companies may register themselves at MATRADE by filling out and submitting a form about themselves and the products they handle.

The annual fee is RM250. Registered companies are given special privileges in the use of the organisation's services. They are also introduced on a priority basis to overseas companies making inquiries on trade. As of July 1994, approximately 800 companies were registered.

4) Cooperation With Other Countries

MATRADE cooperates with organisations in Japan, Germany, the Netherlands, Australia and other countries to promote its exports. Areas of cooperation include market surveys, product improvement, missions, trade seminars, and exhibitions.

5) ITAF4

The ITAF scheme was introduced by MITI to support SMIS in Malaysia. The fourth scheme provides companies with up to RM40,000 in subsidies for export promotion activities. The activities covered are manufacture of export promotion products, participation in overseas trade fairs and dispatch of export missions. The past performance of ITAF is shown in Table 3-4-6.

Table 3-4-6 Performance of ITAF 4

(Unit: RM)

	Approved (A)	Under Evaluation (B)	Total (A) + (B)	(%)
Electrical & Electronic Products	39,373.75	83,167.50	122,541.25	11.94
Foodstuff & Confectionery	55,944.17	22,618.95	79,563.12	7.75
Furniture & Component	71,529.75	148,314.57	219,844.32	21.43
Home Furnishing & Accessories	43,462.50	31,117.13	74,579.63	7.27
Medical Pharmaceutical Products	13,500.00	2,650.00	16,150.00	1.57
Metal Working Machinery - Welding	16,650.00	12,412.75	29,062.75	2.83
Metal & Ferrous Products	18,985.06	3,800.00	22,785.06	2.22
Plastic Products	26,000.00	10,908.50	36,908.50	3.60
Rubber Products	21,117.00	0.00	21,117.00	2.06
Textiles & Garments	100,424.38	57,500.00	157,924.38	15.39
Toys & Sports Items	0.00	20,000.00	20,000.00	1.95
Wooden Products	14,115.00	0.00	14,115.00	1.38
Leather Products	12,500.00	21,344.64	33,844.64	3.30
Petroleum Products	27,500.00	0.00	27,500.00	2.68
Footwear	22,194.28	104,436.38	126,630.66	12.34
Misc.	0.00	23,436.50	23,436.50	2.28
Total	484,295.89	541,706.92	1,026,002.81	100.00

Source: MATRADE

6) Premises

In September, the general affairs and research sectors and Resource Centre are scheduled to be moved temporarily to Wisma Simederby (and later to be moved to a new building). The others will remain at the current Wisma PKNS for the time being. The entire organisation is

scheduled to be moved to a single location with the completion of the new building in 1996.

7) Problems

MATRADE receives sufficient budgetary assistance not only from the government but also from other countries, so does not suffer from any particular financial problems.

MATRADE is increasing the size of its staff to strengthen its services, but is suffering from the same problem as most other organisations in Malaysia, that is, difficulty in securing the needed human resources. At the present time, it is filling its ranks mostly with staff of the former MEXPO, government and other public organisations. It is also hiring some people from the private sector. Most of the staff are not on temporary transfer, but are long term employees of MATRADE.

Activities not previously covered by MEXPO are still fairly much in the preparatory stage and it will be a while before the specific nature of those activities becomes clear. An area which will probably be boosted considerably is the newly established research division.

(2) SIRIM Library Service

SIRIM basically engages in the activities explained with reference to (5) below. However its library service is introduced here as it may be considered to be an export related information service.

1) Outline

This service was started last year by the Standard Information Unit of SIRIM. The unit has a library accommodating 200,000 pieces of information on IEC and ISO standards, 15,000 books, 3000 technical reports, 200 types of specialised journals, and CD-ROMs containing information on the industrial standards of the U.K., France, and Germany and the ISO. It also has a computer system for providing on-line information on Malaysian industrial standards (MS) and ASEAN industrial standards. Note that this service is a successor to the former

TEXPRO information service. The name of the old service was abolished and its functions improved.

Information other than that provided on-line is in principle provided free of charge, but a special form has to be submitted to request information. When existing information is insufficient for response to an inquiry, the information is sometimes obtained overseas. No special charge is levied for this.

Use of the on-line information service (SIRIM Link) requires an annual fee of RM250 and 30 sen/minute in communication costs. The unit also prepares an industry-based mailing list of about 500 companies. It uses this to notify these companies by direct mail of publication of materials relating to their specific industries.

2) State of Use

There were about 250 inquiries for information made in 1992 and about 1000 in 1993, so use is growing steadily. Along with the increase in use, however, problems are arising such as a shortage of staff (the service is currently manned by two officers and two supporting staff), insufficient training, problems in the information management system, a lack of budget for obtaining overseas information, and difficulties in translating materials due to the use of specialised terminology.

(3) Other Support

Marketing assistance provided other than by MATRADE includes the activities of the Malaysia Trade and Distribution Centre (MTDC - standing exhibitions and business facilities targeting the European market), South Investment, Trade and Technology Data Exchange Centre(SITTDEC - information service for promotion of trade and investment with the developing countries), general trading companies (GTC),etc. These will play increasingly important roles in the future.

4.2.5. Means for Strengthening Competitiveness of Manufactured Products

Promotion of improved technology and standardisation of industrial products leads to improved quality of products and in turn to higher international competitiveness and, in the end, means greater exports. Activities in this area include the research and development activities of SIRIM etc., the activities for commercialisation of new technology by MTDC, and the activities for promoting introduction of technology through foreign direct investment and technical tie-ups by MIDA. These will be discussed in detail in related chapters.

4.2.6. Cooperation within ASEAN

ASEAN began working toward free trade in the region in the 1970s. Up until the end of the 1980s, however, the countries in the region had maintained policies stressing relations outside the region rather than within it and so no sufficiently effective systems for cooperation had been set up. With the arrival of the 1990s, however, a consensus was quickly formed to liberalise trade in the region due to the common sense of crisis relative to changes in the international economic environment. Cooperation in the region is expected to be effective in increasing trade, strengthening efficiency and competitiveness in industries, maintaining foreign investment and encouraging investment in the region.

(1) ASEAN Free Trade Area (AFTA) and Common Effective Preferential Tariff (CEPT)

1) Outline

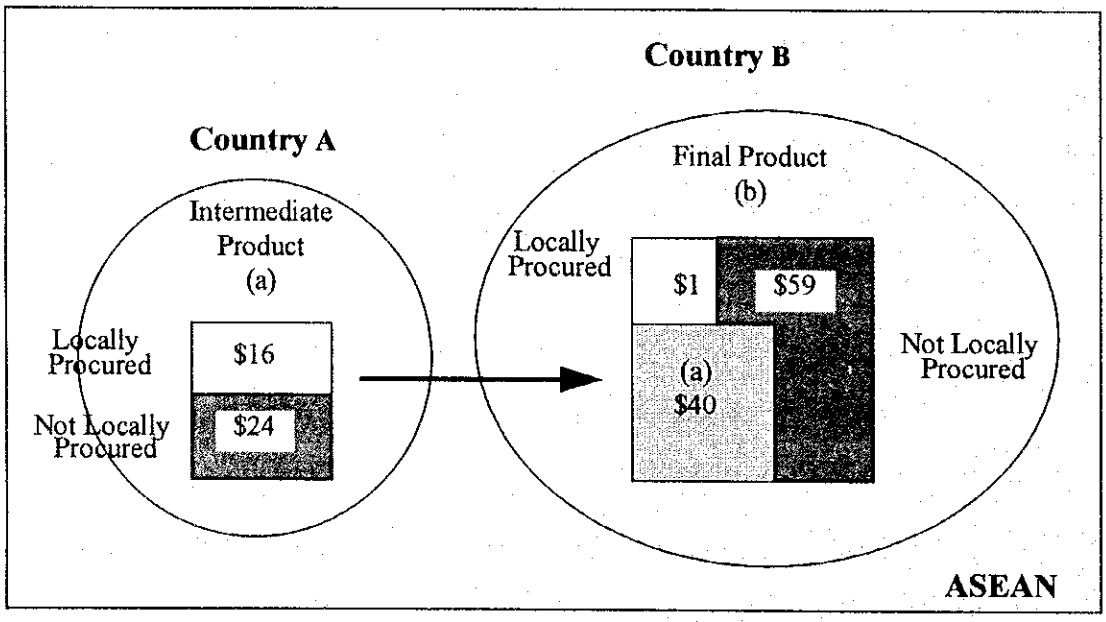
AFTA was launched in 1993 based on the formal agreement reached at the 1992 ASEAN Summit. The specific mechanism for its implementation is CEPT. CEPT calls specifically for the following:

The ASEAN countries are to lower tariffs on all manufactured products including capital goods and processed agricultural products (those falling outside the definition of agricultural products) to 0 to 5 percent over a 15 year period. Non-tariff barriers which would make the reductions

in tariffs meaningless would not be maintained or introduced. Cooperation will also be provided in harmonisation of standards, mutual recognition of test and certification of products, and so on.

The rule of origin is less severe than the ASEAN PTA and stipulates a local content of at least 40 percent and final processing performed in the region. Products imported from inside the region for use as materials are deemed 100 percent regional products even when the local content is only 40 percent. Accordingly, products given value added in two or more countries in the region are deemed to have been made in the region even when the real local content is less than 40 percent (Fig. 3-4-2).

Fig. 3-4-2 Method of Calculating ASEAN Content Rate of the Products Manufactured with Intermediate Products from ASEAN Countries



The Intermediate product (a) is considered to be a genuine ASEAN product because its local content rate is 40%. Therefore, final product (b) is also considered to be an ASEAN product with its local content rate being 41%.

2) CEPT Tariff Reduction Schedule

The schedule for the tariff reductions may be roughly divided into two tracks, that is, Fast Track where tariffs on products are to be reduced early and a Normal Track where tariffs on products are to be reduced later than Fast Track. Each Track is further divided in two categories. One is applied to the products whose tariff rates are above 20 percent at 1993. The other is applied to those whose tariff rates are 20 percent and below. Fig. 3-4-3 shows the definite schedule of each category.

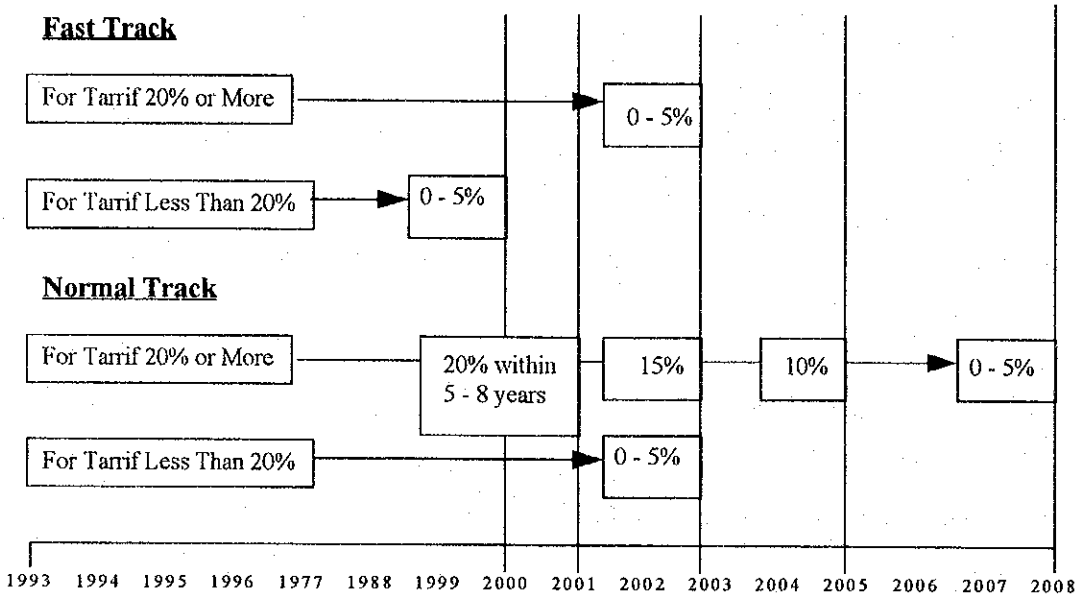
Some products for which preparations have not yet been sufficiently made are allowed to be excluded temporarily depending on the situations in the individual countries, but these are to be reviewed to participate in the reductions by December 31, 2000. Therefore, in the future, the only products excluded from the CEPT will be general exclusions such as defense, health/sanitation, and academic products and permanent exclusions such as agricultural products.

3) Problems

The CEPT allows temporary exclusions to the reductions as mentioned above. Some automotive parts are included in these (Table 3-4-7). Further, the provisions of the CEPT allow a country to refuse application of the scheduled tariff reductions on both fast track and normal track products imported from another country which has not reduced tariffs to the same extent as that country. Accordingly, it may not be until very close to 2008 that the actual effects of the tariff reductions start to appear for automotive parts.

Non-tariff barriers are supposed to be monitored to check on the state of their dismantling, but there is some apprehension over how well this will work.

Fig. 3-4-3 Tarrif Reduction Schedule under CEPT



Source: AFTA Seminar, ASEAN Center (Tokyo), May, 1993

Table 3-4-7 Outline of CEPT Schedule for Automotive Parts on HS 6-Digit Basis

HS CODE	ITEM	BRUNEI	INDONESIA	MALAYSIA	PHILIPPINES	SINGAPORE	THAILAND
401110	TYRES	E	N	E	F	F	F
401120	TYRES	E	N	E	F	F	F
401210	TYRES	E'	N	E	F	F	F
401220	TYRES	E'	N	F	F	F	F
401310	TUBES	E	N	*	*	F	F
681310	BRAKE LININGS & PADS	N	N	N	N	N	N
732010	LEAF SPRINGS	N	N	N	N	N	N
732020	HELICAL SPRINGS	N	N	N	N	N	N
840734	ENGINES OF A CYLINDER CAPACITY EXCEEDING 1,000 CC	N	N/E	N	N	N	N
840790	OTHER ENGINES	N	N'	N	N	N	N
840820	ENGINES (DIESEL)	N	N/E	N	N	N	N
840991	ENGINE PARTS	N	N	N	N	N	N
840999	ENGINE PARTS	N	N	N	N	N	N
841581	AIR CONDITIONERS	N	N	N'	N	N	N
841582	AIR CONDITIONERS	N	N	N	E	N	N
841583	AIR CONDITIONERS	N	N	N'	E	N	N
841590	PARTS FOR AIR CONDITIONERS	N	N	N	E	N	N
851110	SPARK PLUGS	F	E'	*	N	N	N
851120	IGNITION MAGNETOS	F	N	*	N	N	N
851130	DISTRIBUTORS	F	N	*	N	N	N
851140	STARTERS, STARTER-GENERATORS	F	E	*	N	N	N
851150	OTHER GENERATORS	F	E	*	N	N	N
851180	GLOW PLUGS	F	N	*	N	N	N
851190	OTHER ELECTRIC PARTS FOR ENGINES (PLUGS, DYNAMOS E	F	N	*	N	N	N
851220	LIGHTING OR VISUAL SIGNALLING EQUIPMENT	F	N	*	N	N	N
851230	SOUND SIGNALLING EQUIPMENT	F	N	*	N	N	N
851240	WIPERS, DEFROSTERS & DEMISTERS	F	N	*	N	N	N
851290	PARTS FOR LIGHTING OR SIGNALLING EQUIPMENT	E	N	*	N	N	N
852721	RADIO RECEIVERS WITH SOUND RECORDERS	F	F	F	N	F	E
852729	RADIO RECEIVERS	E	*	*	N	F	E
852731	RADIO RECEIVERS WITH SOUND RECORDERS	F	F	F	N	F	E
853910	SEALED BEAMS	F	N	F	N	N	N
853921	HALOGEN	F	N	F	N	N	N
853929	FILAMENT LAMPS	F	N	F	N	N	N
870600	CHASSIS WITH ENGINES	N	E	E	N	E	N
870710	BODIES	N	E	N	E	*	E
870810	BUMPERS	N	E	N	E	N	N'
870821	SAFETY SEAT BELTS	N	E	N	N	N	N'
870829	OTHER BODY PARTS	N	E	N	E	N	N'
870831	MOUNTED BRAKE LININGS	N	E	N	N	N	N'
870839	BRAKES & SERVO-BRAKES	N	E	N	N	N	N'
870840	GEAR BOXES	N	E	N	N	N	N'
870850	DRIVE-AXLES	N	E	N	N	N	N'
870860	NON-DRIVING AXLES	N	E	N	N	N	N'
870870	WHEELS & PARTS	N	E	N	N'	N	N'
870880	SUSPENSION SHOCK-ABSORBERS	N	E	N	N'	N	N'
870891	RADIATORS	N	E	N	E	N	N'
870892	SILENCERS & EXHAUST PIPES	N	E	N	E	N	N'
870893	CLUTCHES & PARTS	N	E	N	N	N	N'
870894	STEERING WHEELS, STEERING COLUMNS & STEERING BOXE	N	E	N	E	N	N'
870899	OTHER PARTS	N	E	N	N'	N	N'
940120	SEATS	N	N	N'	N	F	*
	NUMBERS OF F & F'	15	2	6	4	9	5
	NUMBERS OF N & N'	30	27	29	38	41	42
	NUMBERS OF N/E	0	2	0	0	0	0
	NUMBERS OF E & E'	7	20	4	9	1	4
	NUMBERS OF *	0	1	13	1	1	1

SOURCE:"PRODUCTS AND TARIFF REDUCTION UNDER THE CEPT", ASEAN SECRETARIAT, NOV. 1993

Note 1:This table shows the outline of the tariff reduction schedules by item on the HS 6-digit basis. Detailed schedules on the 9-digit basis are shown in the source material.

Note 2:"N", "F" and "E" indicates "NORMAL TRACK", "FAST TRACK" AND "EXCLUSIVE" respectively.

* indicates that the item is not classified into any category of the three in the source material

Note 3:Apostrophe (') added indicates that the item partially includes sub items belonging to other categories.

Note 4:N/E indicates that the item is mingled with "N" and "E".

(2) Brand to Brand Complementation Scheme (BBC)

The BBC system follows in the wake of the ASEAN Industrial Complementation Scheme (AIC) introduced in 1981. The AIC was aimed at establishment of a horizontal division of labour in the manufacturing sector in ASEAN and, in turn, the realisation of an economy of scale.

Actual approval was given to two projects relating to auto parts proposed by the ASEAN Automobile Federation (AAF). These projects did not succeed due to the differences in industries in the participating countries and the difficulty in allocation of products produced due to the lack of a division of labour in each brand.

Based on this experience, a brand-to-brand complementation scheme was started for auto parts in 1988.

1) Provisions

The participants in the BBC are limited to brand owners (BO) and brand-related original equipment manufacturers (B-R OEM). A brand owner means a company having its own brand, such as Toyota or Nissan, which has design rights for finished cars, subassemblies, parts, and components thereof. A brand-related original equipment manufacturer is an auto manufacturer/assembler which has a tie-up with a brand owner in capital, business, or technology.

A brand to brand parts/components manufacturer(BBPM) producing BBC products under this system may be a brand owner or brand-related original equipment manufacturer itself or may be a separate, independent manufacturer.

The product must meet the Rule of Origin set by the PTA and must be produced in accordance with standards ensuring an international level of quality. Further, it must be produced at a price lower than the market.

When the quality of the product does not meet the level required by the brand owner, the brand owner, brand related original equipment manufacturer and brand-to-brand parts/components

manufacturer must cooperate and work to improve the quality.

When introducing new products or making changes in specifications, the brand owner and brand related original equipment manufacturer are supposed to provide the specifications to the brand to brand parts/components manufacturer within 90 days of the decision.

2) Privileges

Parts imported under the BBC are deemed to be domestic products and are counted in determination of the local content. A minimum 50 percent reduction of import tariffs is available.

3) Procedures

A brand owner or brand related original equipment manufacturer must apply to the SEOM specifying the brand, vehicle type, model, sub-groups, components, or parts. The proposal must be submitted to the related countries as well.

The interested countries negotiate and agree over the source and buying countries and submit the agreed product sourcing list to the SEOM for its decision. The SEOM issues a certificate for each case.

4) State of Use

The number of approved BBC schemes as of 1992 is shown in Table 3-4-8.

Table 3-4-8 Approved BBC Schemes (As of 1992)

(Unit: Number)

Brand Owner	Number of Schemes
Toyota Motor Corp.	7
Mitsubishi Motor Corp.	6
Nissan	4
Volvo	6
Mercedes Benz	2
DAF	1
Renault	1
Total	27

Source: MITI ASEAN Division

5) Problems

The BBC scheme is conditional on establishment of a brand-to-brand complementation system. Therefore, the realisation of a BBC enables the participating countries to increase trade in parts and enlarge the scale of production. The problem, however, is that the complementation system requires equity not based on quantity, but based on value. For instance, when 10,000 sets of parts of a unit price of $10 are exported from a country A, it is only possible to export 1,000 sets of parts of a unit price of $100 made by a country B (though a margin of plus or minus 10 percent is allowed). This 10,000 to 1,000 relationship does not always match with the relationship in the number of automobiles produced in the two countries. If the country A produces 1,200 automobiles, then it would have to separately procure the slight shortage elsewhere. The efficiency of production of that shortage would be extremely low and would end up canceling out the merits of scale achieved.

(3) ASEAN Industrial Joint Venture (AIJV) Scheme

The AIJV scheme was introduced in 1983 and aims at the encouragement of establishment of joint ventures in the private sector of ASEAN so as to construct a cooperative industrial system in the region and consolidate production and thereby achieve economy of scale. This is an investment promotion scheme, but the incentives offered can be considered trade

promotion in nature due to the provisions calling for abatement of import tariffs on intra-regional trade. Besides, the objective of strengthening competitiveness of products through the economy of scale also contributes to the expansion of exports.

1) Provisions

The AIJV scheme requires the participation of companies from two or more countries in the region. Each participating country must hold at least a 5 percent share, though this may be reduced to less than 5 percent after the fourth year from the start of operations. At least 40 percent of the equity must be held by countries in ASEAN (the ASEAN equity ratio must be maintained even after the fourth year from the start of operation). A ratio of less than 40 percent, however, may be allowed:

- when at least 50 percent of the production is exported outside the region
- when the product is already being manufactured by an entity in a participating country
- when an entity has been approved to produce the products in a participating country.

Note that the provisions on equity ratios of the host country take precedence over the provisions of the AIJV scheme. Accordingly, exactly how the equity of other ASEAN participating countries is treated in a host country depends on the policies of that host country.

2) Privileges

Parts imported by an AIJV are deemed domestic parts and are counted in the determination of the local content. A 90 percent reduction of import tariffs is available.

3) Procedures

Partners wishing to establish an AIJV first basically agree on the equity ratio and other details of the venture. The partners then explain their plans to their own governments to arrange subsequent support. After that, formal nomination for AIJV designation for specific products to a Senior Officials Meeting (SEOM) is to be made through the host government or the ASEAN chambers of commerce and industry (ASEAN-CCI). If there are at least two

countries showing interest in the proposal, SEOM designates the products as AIJV products. Application for approval of production is then made in the host country. The government informs SEOM when it approves the production. SEOM then issues a certificate allowing start of business. The AIJV notifies the SEOM and the related governments when it starts actual production.

4) State of Use

As of 1992, 26 AIJV's were approved. Through this study, 8 automotive parts projects and one motorcycle project were identified. Five projects had been abandoned after approval. Among them 3 were automotive parts related.

5) Problems

The AIJV scheme is smaller in scale than the AIC scheme, gives more flexibility to approved ventures, and attempts to facilitate intra-regional cooperation by drawing out private sector initiative. It has been 20 years since the scheme was established, however, yet the number of ventures and their size are both small.

The AIJV scheme is not conditional on the establishment of a brand-to-brand complementary relationship like the BBC scheme. That is, each individual AIJV may concentrate production of its products in a single host country and the products may be exported unilaterally from the host country to other participating countries. Accordingly, when viewed from the standpoint of ASEAN as a whole, the production system is rationalised, but from the viewpoint of the individual country, there is a big difference in merit depending on whether the country becomes the host country or not. Therefore, it is quite difficult to achieve agreement on the national level.

Further, an AIJV requires new investment. Also, being a joint venture, the higher the number of participants, the harder it is to achieve a consensus.

4.2.7. Export Credit

There are Export Credit provisions in Malaysia's Local Content Program. Franchise holders/assemblers are allowed to claim a maximum 20 percent local content points for export of their parts. The points are calculated as in the following formula.

(Total FOB value of automotive component parts exported by the company) /
(Total FOB value of CKD packs imported by the company) x 100%

4.3. BASIC DIRECTION OF EXPORT PROMOTION OF AUTOMOTIVE PARTS

When considering future export policy, the first thing which has to be taken into account is the CEPT, begun in 1993. The CEPT will mean free competition for almost all export products in the region by the year 2008 at the latest. To increase exports, therefore, it will be necessary to build up enough competitiveness to survive the competition in the region.

The most direct and fast-acting means for strengthening competitiveness would be introduction of a subsidy system or tax incentives, low interest financing, or other systems with similar effects. Responses to a questionnaire survey showed strong hopes for such assistance. However, the CEPT aims at strengthening competitiveness of ASEAN with the rest of the world through the introduction of free competition. The introduction of export promotion measures of a subsidy nature would therefore run counter to the objectives of the CEPT. Further, it would invite criticism from the rest of the world as running counter to the trend toward global liberalisation of trade. The Malaysian government itself has adopted a policy of gradually eliminating this type of promotion. For example, it revised the ECR scheme in 1992 and abolished abatement and allowance incentives in 1994.

Accordingly, in promoting exports of automotive parts in the future, stress will have to be placed on assistance in strengthening marketing, primarily through MATRADE, in particular on efforts to increase markets through cooperation in ASEAN and cooperation with other developing countries. (Improved technology also leads to stronger competitiveness of, course. This will

be considered separately in relation to the technology policy.)

Here, the degree of expectations of business on marketing assistance is shown as seen from the results of the questionnaire survey (Table 3-4-9).

Table 3-4-9 Expectation for Assistance from Government for Export Promotion

(Unit: %)

Measure	Expectation		
	Very Effective	Effective	NotEffective
Organisation of trade mission to overseas market	20	56	24
Organisation of trade fairs in the overseas market	17	58	25
Overseas market information supply	7	58	35
Malaysia exporters registration system	6	59	35
Consulting service on trading business	4	43	53
Trading courses for trading business	2	42	56

Source: Questionnaire Survey, JICA Study Team, July to August, 1994

According to this, there is a high degree of expectation over the effects of export missions, overseas trade fairs, overseas market information services, and the system of registration of trading companies. There is little interest in trade consultation services and practical business training for traders. In other words, companies want to see greater measures taken to increase business chances with other countries. The results of this questionnaire can be of important reference value in considering specific export promotion measures in the future.

The BBC and AIJV are established based on private sector initiative and assume the participation of a number of countries, so would be difficult for the Malaysian government to strongly promote as a matter of national policy. Further, tariffs are being reduced under the CEPT and in the

end the schemes will be superseded by it. The ASEAN countries, however, allow temporary exemptions for some automotive parts (Table 3-4-7), so there may not be that much progress made in reducing tariffs for the time being. Accordingly, until the CEPT is fully implemented, it will be necessary to consider active use of these two schemes as a means for establishing a horizontal division of production in the region and for consolidating production.

5. R&D POLICY

The 1980s were called the age of the promotion of export-oriented industries, while the 1990s would be called the age of the promotion of R&D-based industries. The objectives of this section are to examine the technology development in Malaysia. Technology development is a very broad area, however, so the target here will focus on the manufacturing subsector, especially metal and assembly sectors and SMIs.

5.1. Outline of R&D Policy

R&D activities in Malaysia are characterised as follows: R&D expenditure has been historically concentrated in agricultural sectors, and the percentage share of public sector R&D expenditure is very high. (Public R&D expenditure accounted for 90% of total R&D expenditure and agro-related R&D expenditure 61.7% of public R&D expenditure in 1988.) The Government set targets for R&D activities as follows:

- To raise R&D expenditure of the industrial sector to 34% by the year 1994.
- To strengthen industry-oriented R&D through the R&D fund.
- To upgrade the self-financing capability of research institutions.

National R&D activities and policies are mainly undertaken by the Ministry of Science, Technology, and Environment(MOSTE) excluding agro-related activities. MOSTE is now preparing an R&D plan for the Seventh Malaysian Plan.

5.2. R&D Policy Needed by the Manufacturing Sector

Government grasps the weakness of the accumulation of factor technology in the manufacturing sector. Furthermore, these technologies have an important role in strengthening future industrial structure in Malaysia.

SIRIM under the MOSTE is one of the major implementation agencies for R&D activities. The

objectives of SIRIM are "to enhance Malaysian international competitiveness through industrial partnership in industrial technology and quality." In order to achieve the above objectives, SIRIM has the following functions;

a. To promote and undertake industrial research
   - improvement of technical processes and methods
   - discovery of new processes and methods
   - encouragement of the use of local resources
   - introduction of foreign-developed technology
   - application of the results of above research
b. To promote industrial efficiency and development
c. To provide technology transfer and consultancy services to assist industries
d. To promulgate standards and to promote standardisation and quality assurance
e. To promote public and industrial welfare, health and safety.

SIRIM is composed of 4 divisions, namely the Corporate Service Division, Standards & Quality Division, Research and Technology Development Division, and Technical Service Division. R&D activities in SIRIM are mainly implemented by the R&TD Division in 4 centres: Material Technology Centre, Advanced Manufacturing Technology Centre, Chemical & Biotechnology Centre, and Product & Machine Development Centre. R&D of manufacturing process and factor technology are implemented by AMTC and PMDC. AMTC covers the software aspect of manufacturing process systems and PMDC covers the hardware aspect. AMTC supports the technical aspect of the modernisation of SMIs through seminars and workshops for managers and engineers. PMDC implements pilot production and development such as design and production of dies and moulds. Both organisations enhance their activities by working closely with the manufacturing sector. Expansion of their activities is very difficult because of manpower and budget constraints.

SIRIM has always been actively involved in local automotive components development programme initiated by all levels of industry for the automotive market. For the prototype automotive component development, product evaluation services, metrological services, and

failure analysis services from SIRIM have been widely sought by the local industries. Components include leaf springs, coil springs, wheel nuts & studs, wheel jack, sprocket wheels, transmission chains, brake and control cables, electroplated coatings, paint coatings, aluminium alloy pistons, etc.

SIRIM possesses a wide range of electrical/electronic, mechanical/physical, metallurgical, chemical, plastics, ceramics test equipment that can be utilised by the local industries for R&D in automotive components parts development. Once a specific research project has been identified by a component manufacturers, expertise within and even outside SIRIM can be mobilised to undertake the research project. Specific research mechanisms are also available, viz:-

1. Contract Research Program (CRP)
2. Joint Research Venture Program (JVP)
3. SIRIM Tripartite Research Venture (STRIVE)

Research can also be undertaken via the IRPA mechanism.

MTDC Sdn Bhd was set up as a joint venture between the Government and 14 local corporations in 1992 (now private corporations number 17). The main objectives are to commercialise research results developed by universities and institutions and to encourage the growth of technology-based enterprises in Malaysia through venture capital. MTDC, with RM200 million of total share holders funds, has 4 subsidiary companies, namely MTDC-HQ Venture Capital Management(J/V with USA), Malaysian Technology Venture One, Malaysian Technology Development Johor, and Malaysian Technology Development Penang, and 2 associated companies, Malaysian Hi-technology Industries, and Malaysian Technology Consultants. To date, MTDC has invested in 18 companies classified into electronics, pharmaceuticals, information, dies and moulds, and metal stamping parts. Targeted types of technologies for investment are mainly the following.

- Advanced Manufacturing Technology
- Advanced Material Technology
- Biotechnology
- Electronics
- Information Technology

5.3. Incentives for R&D Activity

The Malaysian Government has introduced various incentives to enhance private sector R&D and hi-tech activities in the manufacturing sector. Available incentives now are as follows.

a. Double Deduction for expenditure related to R&D
   - Approved research projects are carried out both in-house and on a contract-basis.
   - Expenses for the use of facilities and for the services provided by approved research companies or institutions.
   - A contribution in cash for the approved research institutions
b. Income Tax Exemption to Approved Research Companies or Institutions
   - A period of 5 years
c. Exemption of import duty, excise duty and sales tax
   - Machinery/equipment, materials, raw materials and samples used for approved research projects
d. Income Tax Exemption for New Technology Based Firms
   - A period of 5 years
e. Research Allowances of the qualifying capital expenditure for a period of 10 years, limited to 70% of statutory income
   - 100% for Approved Research Companies
   - 50% for companies carrying out in-house R&D
f. Industrial Building Allowances

The Double Deduction scheme is also provided for manpower training as described in the section on human resource development in the SMI development policy.

As for R&D activities, the main issue is how to induce the R&D 'culture' within the Malaysian private sector, especially in the manufacturing sector.

5.4. Standardisation

Standardisation in Malaysia is implemented by the Standards & Quality Division of SIRIM. Up to now, SIRIM focussed primarily on spreading Malaysian Standards (MS). In recent years, they have focussed on ISO-9000. Around 350 factories have been approved as ISO-9000 factories. In order to improve Standardisation, SIRIM holds seminars, and NPC, as part of their Quality Control programmes, has one course on standardisation, "Implementation of ISO-9000".

5.5. Quality Control(QC)

Since Japanese firms started operation in Malaysia, QC activities have become familiar to Malaysian firms, especially in the related companies. Malaysian companies which have implemented QC activities were identified through the interview survey conducted by this Study. NPC under MITI implements programs of productivity and quality improvement in the manufacturing sector, and offers 25 QC courses as Quality Management Programmes in 1994.

5.6. Testing and Inspection

The technical Service Division of SIRIM implements testing and inspection for the manufacturing sector. The testing Service Section consists of a machinery & vehicle unit, civil engineering unit, material unit, electrical unit, and chemical unit, and provides testing services for manufacturers.

6. INDUSTRIAL ESTATE DEVELOPMENT

6.1. GENERAL INDUSTRIAL ESTATES

The development of industrial estates has been undertaken by government agencies such as the States Economic Development Corporations (SEDCs), Regional Development Authorities (RDAs), Port Authorities and Municipalities, and private developers. There are 26 government agencies related to IEs development, according to MIDA's information.

A total of 176 IEs had been developed in all of Malaysia as of January 1, 1994, and 103 of the total are fully occupied. Total developed area excluding housing development is around 22,800 hectares, salable and allocated areas are 13,280 and 11,540 hectares, respectively. Area still available amounts to around 2,800 hectares. Distribution of existing IEs by States is shown in the following Table. In addition to these 176 existing IEs, a total of 58 new IEs have been proposed for development, and total planned area excluding housing zones is around 9,000 hectares.

6.2. SPECIALISED INDUSTRIAL ESTATES (SIES)

Specialised Industrial Estates are classified by MIDA as follows :

- IEs prepared for specific types of industries, e.g., furniture, wood-based, foundry, ceramic, timber-based, etc.
- Technology park for R&D, High tech, etc.

According to MIDA's information, the number of existing SIEs is 18, but one of them is clarified as under planning. So this SIE is considered to be in the planning status. Therefore, there are 17 existing SIEs throughout the country, and 22 are proposed. Seven of the total existing SIEs have been fully occupied. Available area are 328.7 hectares of total 2,205 hectares. The development scale of SIEs is mainly 30-50 hectares. Large scale SMIs are targeting oil and gas industries, e.g. maximum development are a in this type is around 900 hectares, followed by wood base and furniture SIEs.

Table 3-6-1 Distribution of Existing and Proposed IEs

(Unit: ha)

		No. of I.E.	Total Area	Salable Area	Occupied Area	Available Area
1. Johor	Existing	23	3,097	2,341	1,638	616
	Proposed	3	2,141	-	-	-
2. Melaka	Existing	8	781	622	512	110
	Proposed	7	803	-	-	-
3. N. Sembilan	Existing	7	477	335	328	7
	Proposed	4	76	-	-	-
4. Selangor	Existing	22	2,732	2,036	2,036	0
	Proposed	9	-	-	-	-
5. Federal Territory	Existing	2	214	199	199	0
	Proposed	9	200	-	-	-
6. Perak	Existing	26	2,066	1,214	982	232
	Proposed	5	907	41	26	15
7. Penang	Existing	11	1,967	1,423	1,321	101
	Proposed	-	-	-	-	-
8. Kedah	Existing	15	905	750	712	39
	Proposed	2	1,644	-	-	-
9. Perlis	Existing	4	154	62	52	10
	Proposed	2	88	-	-	-
10. Pahang	Existing	13	2,448	1,033	763	914
	Proposed	5	1,118	-	-	-
11. Kelantan	Existing	7	738	366	307	159
	Proposed	-	-	-	-	-
12. Terengganu	Existing	17	2,796	1,772	1,402	509
	Proposed	4	1,458	-	-	-
13. Sabah	Existing	8	230	144	137	7
	Proposed	5	452	28	-	-
14. Sarawak	Existing	13	4,194	983	1,151	84
	Proposed	3	114	-	-	-
Total	Existing	176	22,799	13,280	11,540	2,788
	Proposed	58	9,002	69	26	-

Note: 1) Occupied area includes undeveloped land.
2) Total area excludes housing development.
3) Existing I.Es in Federal Territory are located in Labuan, and Proposed I.Es are planned in Kuala Lumpure.

Source: MIDA, 1 January, 1994

In proposed SIEs, wood-base SIEs are the largest number of the total mainly in Sarawak, followed by hi-tech and research types of SIE targeting electronics industries. The size of those proposed SIEs is around 200 hectares.

SIEs prepared for specific types of industries such as furniture, foundry, ceramic, or wood-based are considered to be tenanted by SMIs as a result. There are a few I.Es which focus on SMIs. Mukim Batu Industrial Park (MBIP) implemented by MIEL is one of the cases of specialised I.Es targeting SMIs. MIEL has rich experience in providing factory buildings to SMIs in collaboration with various SEDCs. Targets of MBIP are considered as SSIs rather than MSIs.

In the case of Japan, there is no classification of SIEs as in Malaysia. There are several classifications of IEs and research parks. "SIEs" for targeted SMIs have been developed by SMEs Corporation and Environment Corporation.

6.3. POLLUTION CONTROL AND INDUSTRIAL ESTATES

The main objectives of IEs development are as 'tools" to attract factories in order to boost the regional/national economy. The SMI IEs, however, play a role as ensuring favourable production circumstances, and at the same time, as maintaining good habitation condition through the relocation of factories from residential zones to IEs. In terms of pollution control, it is easier to control or monitor pollution from factories located in IEs than in individual locations. Pollution control is still a serious issue in Malaysia because of the tough environmental standards. On waste water treatment, for instance, each factory treats it by themselves and therefore, central treatment systems for industrial waste water are not adopted in IEs. Waste water treatment facilities prepared in IEs are mainly oxidation ponds in which SS, COD, and BOD are treated by biological processes.

The principle of individual treatment is acceptable basically. For SMIs, especially SSIs, however, it is very difficult to set up waste water treatment facilities in their own factories for financial reasons. Gathering the same types of industries, e.g., heat treatment, plating, etc., and relocating them into "SIEs" is one possible solution. The characteristics of waste water from the same types

of industries are almost same. If tenanted types of industries were known, it would be easy to treat the effluent. These suggested SIEs having waste water treatment facilities for special types of industries would play a role in pollution control for SMIs. There has been some experience in Japan, and that information will be provided in the next report.

CHAPTER 4. INVESTMENT STRATEGIES OF MAJOR AUTOMOTIVE MANUFACTURERS AND AUTOMOTIVE PARTS AND COMPONENTS ASSEMBLERS IN ASIA

1. ASIAN AREA BUSINESS STRATEGIES OF MAJOR AUTOMOTIVE MANUFACTURERS

1.1. BUSINESS ENVIRONMENT OF AUTOMOTIVE BUSINESS IN ASIA AND MAJOR AUTOMOTIVE MANUFACTURERS' RESPONSE

Major changes which the automotive industries are undergoing in the Asian area are as follows:

i. Increasing importance of the Asian market

Automobile production has been concentrated in three areas: North America, Europe and Japan. The Japanese automobile industry faces the necessity of searching for new growth opportunity due to the following:

- Restrictions on Japanese cars have been strengthened in the North American market, which has been an important market for Japan.
- The automotive market in Japan has been stagnant since the beginning of the 1990s.

The Japanese automobile industry is placing increasing emphasis on the Asian market which has been experiencing favourable economic growth. The size of the world automotive market by area is shown in Table 4-1-1. Automobile sales and production in ASEAN are shown in Fig. 4-1-1 and 4-1-2.

ii. Growth of production bases in the Asian region

The cost competitiveness of the Asian countries, largely due to their lower labour cost, has been strengthened as a result of the Yen appreciation since 1985. The technological level and industrial base which supports automobile production in the Asian region have been steadily improving.

iii. Increase in production cost of automobiles in Japan

Japanese automobile manufacturers have tended to increase overseas procurement of parts

and components as production costs rose in Japan.

iv. Pressures to increase parts and components imports as a result of Japan's trade surplus
There are strong pressures from Europe and the U.S. on Japanese automobile manufacturers to increase parts and components imports to Japan and increase local content in overseas production in order to reduce Japan's trade surplus.

v. Increasing cost of Knock-down (KD) production in the Asian region due to the Yen appreciation
The KD production cost at Japanese automobile manufacturers in Asian countries has been increasing due to the rise in import prices of KD parts reflecting the Yen appreciation. The need to reduce production cost in these countries is high among Japanese automobile manufacturers.

vi. Progress of mutual complementation of parts and components among ASEAN countries
At the ASEAN Economic Ministerial Committee Meeting in 1988, ASEAN member countries signed an agreement to establish the Brand-to-Brand Complementation Scheme for the purpose of strengthening the competitiveness of ASEAN in the world automobile market. Under this scheme, specific automotive parts and components production would be concentrated in a limited number of countries and supplied to other countries. At the ASEAN Summit Conference in 1992, the Agreement on Common Effective Preferential Tariff was signed as a step toward realising the ASEAN Free Trade Area. The step-by-step reduction of tariffs among ASEAN countries is to be carried out in 15 years based on this agreement.

Business activities of major automobile manufacturers in the Asian area are as shown in Table 4-1-2.

Automobile manufacturers have faced the necessity of re-examining business strategies toward the Asian area in order to respond to the changes in the business environment in this area. The future direction of major automobile manufacturers' business strategy toward the Asian area is as follows:

i. Entry into potential markets

Market entry into potential markets, such as China and Vietnam, is one of the most important issues for automobile manufacturers. They are making active approaches to these markets.

ii. Establishment of a mutual complementation system in the Asian area

Automobile manufacturers which have set up production bases in the Asian area have started to produce automobiles by supplying parts and components among production bases in this area instead of manufacturing all parts and components within an individual country.

iii. Manufacture of an Asian Car

Automobile manufacturers consider that the introduction of a low-priced and practical car into the Asian market is necessary in order to survive in the expanding Asian market. Japanese automobile manufacturers plan to introduce the so-called Asian car, which would be developed specifically for the Asian market and produced at production bases in the Asian area.

iv. Reduction of production cost through the enlargement of overseas procurement

Japanese automobile manufacturers are trying to reduce procurement cost by increasing purchase from a range of Asian countries instead of buying locally in each country. Taking into consideration the future of mutual complementation in the Asian area and the future market growth prospects of individual Asian countries, they are examining international procurement policies and identifying which Asian parts and components have competitiveness.

Table 4-1-1 World Automobile Sales (1993)

Area		Sales (Units)	Share
Asia	Japan	6,467,279	14%
	Korea	1,437,929	3%
	China	1,342,109	3%
	ASEAN	744,854	2%
	Others	1,317,852	3%
North America	U.S.A.	13,940,626	30%
	Canada	1,182,044	3%
Europe	Western Europe	13,302,843	29%
	Eastern Europe	2,116,585	5%
Others		4,303,213	9%
Total		46,155,334	100%

Source: *Syuyo Koku Jidosha Tokei* (Automobile Statistics of Major Countries), Japan Automobile Manufacturers Association, Inc.

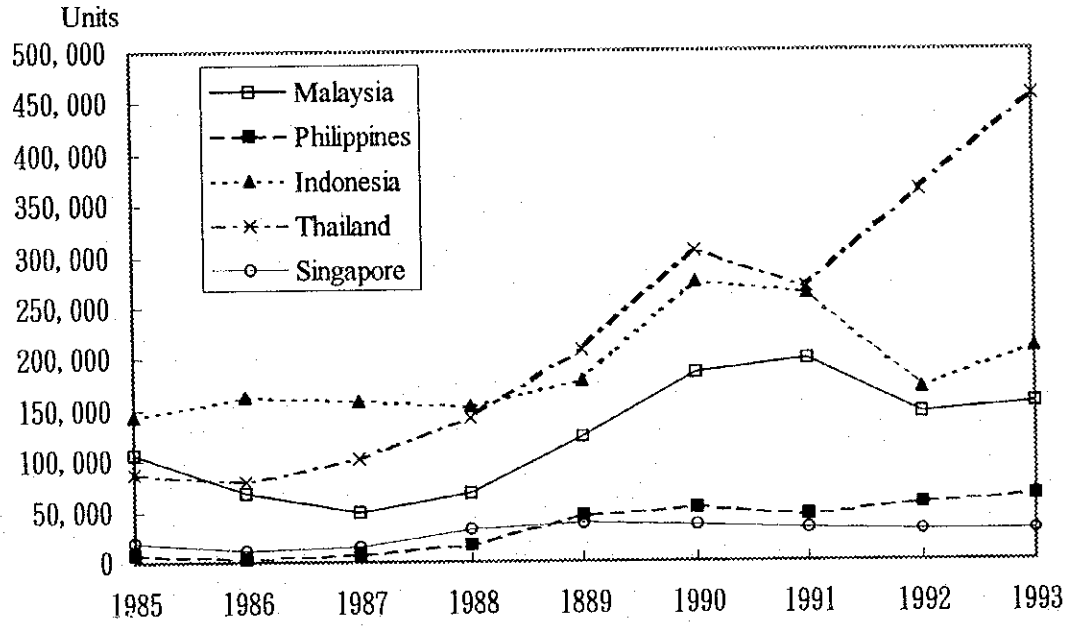
Table 4-1-2 World Automobile Production (1993)

Area		Production (Units) *1	Share
Asia	Japan	11,227,545	23%
	Korea	2,050,058	4%
	China	1,280,000	3%
	ASEAN *2	803,856	2%
	Others	818,287	2%
North America	U.S.A.	10,897,665	22%
	Canada	2,246,703	5%
Europe	Western Europe	13,949,365	28%
	Eastern Europe	2,369,672	5%
Others		3,719,674	8%
Total		49,362,825	100%

Note: *1 Figures include assembled automobiles
*2 The Philippines is not included because the data is not available.

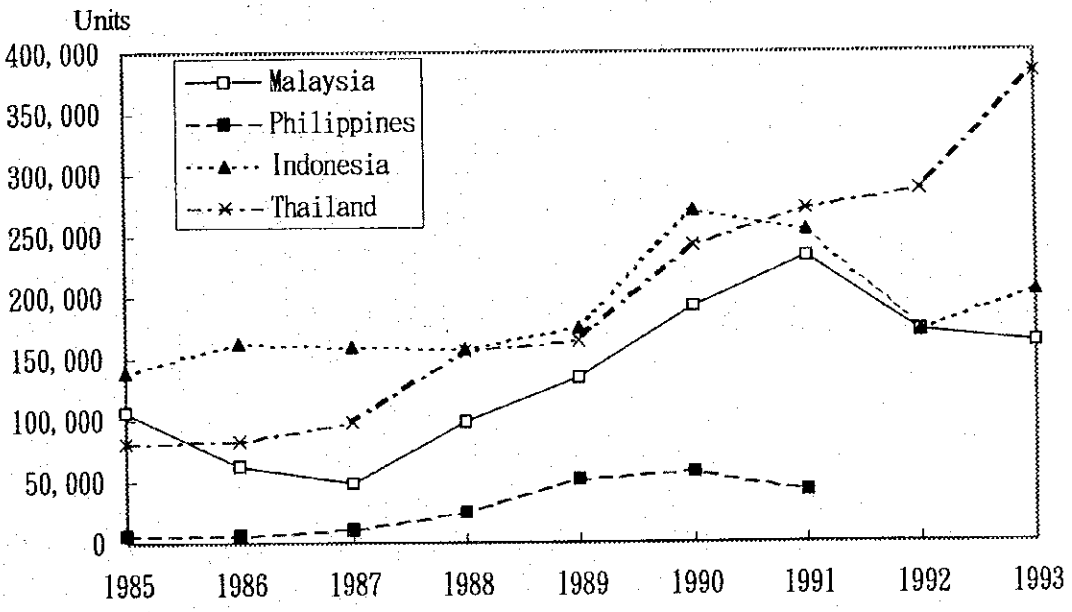
Source: *Syuyo Koku Jidosha Tokei* (Automobile Statistics of Major Countries), Japan Automobile Manufacturers Association, Inc.

Fig. 4-1-1 Automobile Sales in ASEAN Countries



Source: *Syuyo Koku Jidosha Tokei* (Automobile Statistics of Major Countries), Japan Automobile Manufacturers Association, Inc.
Jidosha Sangyo Handbook (Automotive Industry Handbook), Nikkan Jidosha Sangyo Shimbunsha

Fig. 4-1-2 Automobile Produciton in ASEAN Countries



Source: *Syuyo Koku Jidosha Tokei* (Automobile Statistics of Major Countries), Japan Automobile Manufacturers Association, Inc.
Jidosha Sangyo Handbook (Automotive Industry Handbook), Nikkan Jidosha Sangyo Shimbunsha

Table 4-1-3 Business Operations in the Asian Area by Major Automobile Manufacturers

	Toyota	Nissan	Mitsubishi	GM	Ford	VW
Thailand	◎ ● ○ Engine parts Body parts Consumer finance Technical office	◎ ● ○ Engine parts Body parts Die making	◎ ● ○ Engine parts Body parts	◎ (Consign.) ● (Consign.)	◎ (Consign.) ● (Consign.)	
Indonesia	◎ ● ○ Engine parts Body parts	◎ (Consign.) ● (Consign.)	◎ ● (Consign.) ○ Engine parts Body parts	◎ Since 1994	◎ (Consign.) ● (Consign) ○	
Malaysia	◎ ● ○ Steering gears	◎ ● ○ Body parts	◎ ● ○ Engine parts Body parts	◎ Since 1994 ●	◎ ● ○ Car audios	
Philippines	◎ ● ○ Transmission	◎ ● ○ Body parts	◎ ● ○ Engine parts Body parts	◎		
Taiwan	◎ ● ○ Body parts	◎ ● ○ Body parts	◎ ● ○ Body parts	◎ ●	◎ ● ○	◎ ●
China	◎(Tech. Assist.) ●(Consignment)	◎ (JV) ● (Consign.)	◎ (Consign.) ● ○ Negotiation with PROTON	◎ ● ○	● (Consign.) ○ JV, plastic and glass parts	◎ (Consign.,JV) ● (Consign..) ○ Engine, Transmission, Panel
Korea		◎ (Tech. Assist.)	◎ (Tech. Assist.)	○ JV	◎ ● ○	
Vietnam	◎ (Consign.)	◎ (Consign.) ● (Consign.)	◎ (JV) ● (JV) ○ (JV)	◎ (Under Nego.) ● (Consign.) ○	◎ (Under Nego.)	
Remark	Singapore office controls physical distribution in the Asian area.	Office in Thailand controls mutual complementation in the Asian area.		Hong Kong office controls operations in the Asian area.	H.Q. in Detroit controls business operations in the Asian area.	Hong Kong office controls business operations in the Asian area.

Note: ◎: Assembly ●: Sales ○: Parts production

Source: Forin

1.2. MAJOR AUTOMOBILE MANUFACTURERS' BUSINESS STRATEGIES IN THE ASIAN AREA

1.2.1 Toyota Motor Corporation

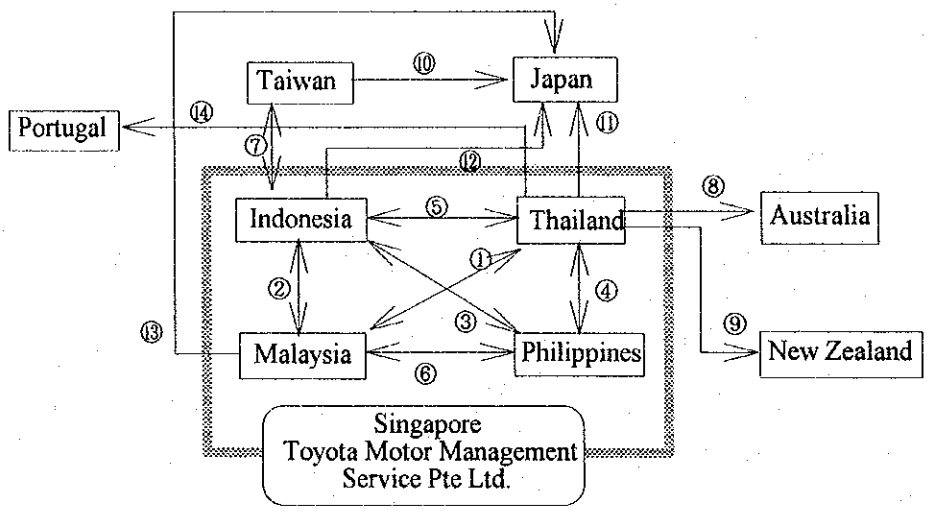
Toyota Motor Corporation (Toyota) has established a policy of expanding production and sales in areas, such as Asia and South America, where demand is expected to grow in the future. This policy was outlined in the mid-term plan released in December, 1993.

Toyota is increasing parts and components procurement from ASEAN countries for production in this region. In addition, Toyota is establishing an optimum procurement system of parts and materials from the lowest-cost sources instead of procurement only from Japan.

The existing system of parts and components mutual complementation at Toyota is shown in Fig. 4-1-3.

With the Yen appreciation, Toyota faces a serious problem of cost increase especially for passenger vehicles because imported parts and components account for more than 60% of passenger vehicle production cost. Toyota considers that the localisation of parts and components, and increase in procurement within the ASEAN region are urgent tasks. In Thailand, material expenses account for 60 - 70% of total parts and components cost. Toyota aims to reduce material expenses by shifting sources of materials from Japan to other low-cost countries. Technical evaluation by the Technical Division in Japan is required when local or ASEAN parts are newly adopted. The technical staff personnel are sent to Thailand and carry out technical the evaluation of local parts and components. Toyota plans to set up an ASEAN technical centre in Thailand in the future. This centre is expected to engage in evaluation of parts and materials and provide the technical service necessary for design modifications.

Fig. 4-1-3 Parts and Components Mutual Complementation System in the Asian Area of Toyota Motor Corp.



	From	To	
①	Thailand	Malaysia	2.0 litre diesel engine (2,300 units/year since Oct. press parts, electrical equipment
①	Malaysia	Thailand	Steering gears*, shock absorbers
②	Malaysia	Indonesia	Steering gears*
②	Indonesia	Malaysia	5K engines
③	Indonesia	Philippines	5K engines
③	Philippines	Indonesia	Transmissions**
④	Philippines	Thailand	Transmissions**
④	Thailand	Philippines	Electrical equipment
⑤	Thailand	Indonesia	Electrical equipment, moulds and dies
⑤	Indonesia	Thailand	Press parts
⑥	Philippines	Malaysia	Transmissions**
⑥	Malaysia	Philippines	Steering gears*, electrical equipment
⑦	Indonesia	Taiwan	5-piston engines, Kijang, moulds and dies
⑦	Taiwan	Indonesia	Plastic parts
⑧	Thailand	Australia	Moulds and dies, jigs, parts
⑨	Thailand	New Zealand	2 litre diesel engines (400 units/year since Nov. 1991)
⑩	Taiwan	Japan	Plastic parts
⑪	Thailand	Japan	Cylinder blocks and camshafts for diesel engines (70,000 units/year since March 1993), moulds and dies, diesel engines
⑫	Indonesia	Japan	5-piston engines (70,000 units/year since Mar. 1993)
⑬	Malaysia	Japan	Steering gears
⑭	Thailand	Portugal	2 litre diesel engines

Note: * Shipments of steering gears from Malaysia to Thailand, Indonesia, and the Philippines 120,000 units/year since

** Shipments of steering gears from the Philippines to Malaysia, Indonesia, and 150,000 units/year since

Source: Forin

Toyota plans to start the assembly of an Asian car in Thailand. Toyota intends to promote a mutual complementation system of parts and components in the ASEAN region in order to support the Asian car project. In order to achieve a low price, the key concept of the Asian car, Toyota will make the best use of its resources established in the Asian area. Toyota plans to produce an Asian car in individual ASEAN countries in the future. However, Toyota plans to procure parts and components of the Asian car mostly from Thailand. In addition, Toyota places importance on the procurement from Malaysia in its procurement policy because Toyota considers that the economies of scale of parts production in Malaysia will be achieved through National Car Projects.

An increasing number of parts and components manufacturers aim to invest in the Asian area. Toyota's basic attitude toward their intention is to respect the individual suppliers' international operation plans. At the same time, Toyota exchanges opinions with their suppliers on their investment plans in the Asian area in order to avoid problems which might be caused by the concentration of investments by parts and components suppliers.

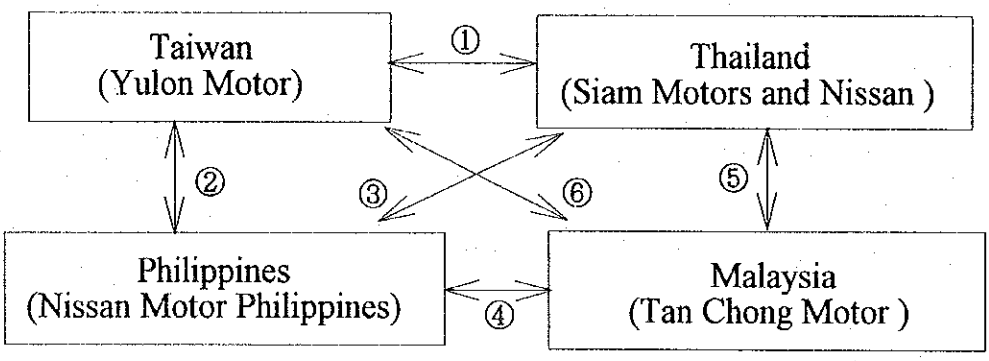
1.2.2. Nissan Motor Co., Ltd.

Nissan Motor Co., Ltd. (Nissan) announced, in 1994, their plan to establish a production capacity of 1 million units in the Asia and Pacific area by the year 2000.

In the Asian area, Nissan engages in automobile production in such countries as Taiwan, Thailand, the Philippines, Malaysia and India through joint venture companies. Nissan is promoting the establishment of a parts and components mutual complementation system to support the produciton in these countries. Fig. 4-1-4 illustrates Nissan's parts and components mutual complementation system in the Asian area.

Nissan plans to produce and sell an Asian car, which would be based on its existing model, Sunny AD Van, in Thailand, Taiwan, Malaysia, and the Philippines. Nissan has a policy of minimizing investments and reducing costs through mutual complementation of parts and components among these countries.

Fig. 4-1-4 Parts and Components Mutual Complementation System in the Asian Area of Nissan Motor Co., Ltd.



	Flow		Item
	From	To	(Parts for a new model of SUNNY)
①	Taiwan	Thailand	Electrical equipment (for 4,800 units/year)
①	Thailand	Taiwan	Fuel tanks, and front floor
②	Taiwan	Philippines	Electrical equipment (for 7,200 units/year)
②	Philippines	Taiwan	Rear front, wheel houses, etc.
③	Taiwan	Malaysia	Electrical equipment (for 4,800 units/year)
③	Malaysia	Taiwan	6 items including bonnet parts, fuel tanks, etc.
④	Philippines	Malaysia	Bonnet parts, fuel tanks, etc.
④	Malaysia	Philippines	Rear floor, wheel houses, etc.
⑤	Malaysia	Thailand	Side body parts, trim parts
⑤	Thailand	Malaysia	Fuel tanks, front floor, and diesel engines (2,400 units/year)
⑥	Philippines	Thailand	Rear floor and wheel houses
⑥	Thailand	Philippines	Fuel tanks and front floor

Source: Forin

1.2.3. Mitsubishi Motors Corporation

Mitsubishi Motors Corporation (Mitsubishi Motors) has the largest market share in the ASEAN region as of 1993. The major reason for this is that Mitsubishi Motors has been placing importance on the Asian market in its overseas business operations because Mitsubishi Motors had fallen behind its competitors in entering the US and European markets.

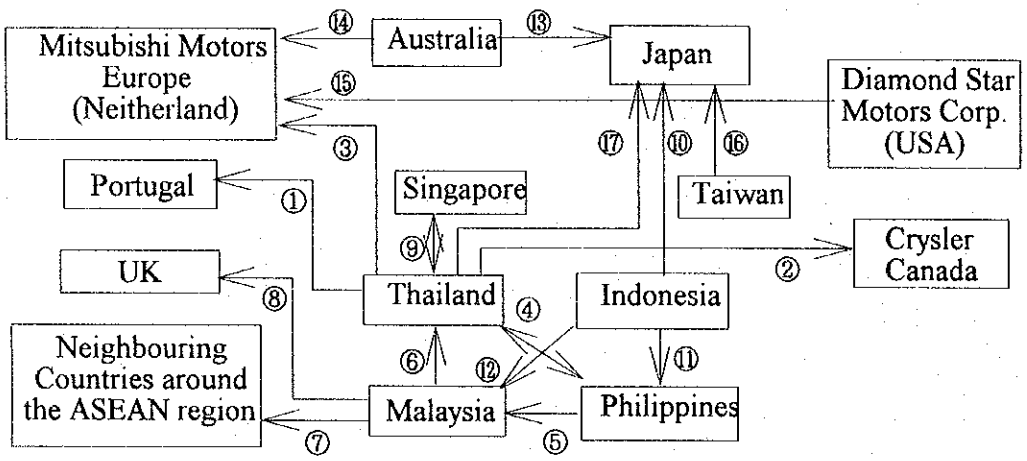
Mitsubishi Motors announced in 1994 a plan to set up a production capacity of 400 thousand units by the end of the 1990s.

Mitsubishi Motors feels the view that price competition will intensify in the Asian market because Mitsubishi Motors is decreasing its cost competitiveness due to the Yen appreciation and because American and European automobile manufacturers plan to enter the Asian market with their compact cars. To cope with this situation, Mitsubishi Motors is promoting mutual complementation of parts and components within the ASEAN region and diversifying its material sources. Fig. 4-1-5 illustrates the existing system of parts and components supply at Mitsubishi Motors.

Mitsubishi Motors plans to develop a multi-purpose type Asian car, which would be based on one of its existing models because Mitsubishi Motors considers that each individual country has specific market characteristics, customers' needs and way of use, government regulations, tariffs, etc., in the Asian area.

Mitsubishi Motors procures and supplies common parts and components of its Lancer model, e.g., door panels and plastic parts, under its parts and components mutual complementation programme. In addition, Mitsubishi Motors procures steel from Korea, plastics and paint from Malaysia, and aluminum parts from Australia.

Fig. 4-1-5 Parts and Components Mutual Complementation System in the Asian Area of Mitsubishi Motors Corporation



	Flow		Item
	From	To	
①	Thailand	Portugal	Diesel engines, bonnets, doors, and propeller shafts for pick-up trucks
②	Thailand	Chrysler Canada	CBU units of COLT model and MIRAGE model
③	Thailand	MME	1-ton pick-up trucks
④	Thailand	Philippines	Press parts including bumpers
④	Philippines	Thailand	Transmissions
⑤	Philippines	Malaysia	Transmission parts
⑥	Malaysia	Thailand	Door parts and body parts
⑦	Malaysia	Neigbouring countries	CBU units of PROTON SAGA
⑧	Malaysia	U.K.	CBU units of PROTON SAGA
⑨	Singapore	Thailand	Car radios
⑨	Thailand	Singapore	CBU units of COLT mode.
⑩	Indonesia	Japan	6-ton truck frames
⑪	Indonesia	Philippines	Moulds and dies, and jigs
⑫	Indonesia	Malaysia	Moulds and dies, and jigs
⑬	Australia	Japan	CBU units of MAGNA
⑭	Australia	MME	CBU units of MAGNA WAGON
⑮	DSMC	MME	CBU units of ECLIPSE, model based on a new GALLANT model
⑯	Taiwan	Japan	Brake drums and press trim parts
⑰	Taiwan	Japan	Small parts, hot forging, moulds for plastic parts, sheet metal parts

Source: Forin

1.2.4. General Motors Corporation

General Motors Corporation (GM) places priority on the Asian market after the North American market and the European market. In the Asian market, GM emphasises China and Japan. GM considers that such countries as Taiwan, Thailand, Indonesia, and Malaysia are also important.

GM engages in the production of automobiles and automotive parts and components in Indonesia, China, and Taiwan at its joint venture companies. In the Asian area, parts and components production has taken precedence over automobile production at GM. GM's presence in the Asian area is relatively small and its market share is generally less than 1% in most countries in this area.

GM has chosen a small-sized passenger car made by Adam Opel, which is part of GM Europe, and a small-sized truck from GM USA as strategic models for the Asian market.

1.2.5. Ford Motor Company

Ford Motor Company (Ford) has set up production bases in Japan, Australia, New Zealand, Korea, and Taiwan in the Asian and Pacific area.

Ford holds a 24.5% share of the Mazda Motor Corporation in Japan, and positions Mazda as a supplying base of parts and components. Ford also holds 10% of Kia Motors, Corporation, in Korea, and ships automobiles to the U.S. market.

Ford places strategic priority on China in the Asian area. However, Ford currently engages only in parts and components production in China. Two group companies, Mazda Motor and Kia Motors, plan to start passenger car production in China through joint venture projects with Chinese companies.

Ford promotes the commonisation of models with Mazda Motor as a measure to expand sales in the Asian area.